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ALL THE KING'S HORSES AND ALL THE KING'S MEN
DEREGULATION OF THE EGG INDUSTRY IN NEW SOUTH WALES

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When the New South Wales Government deregulated the State egg industry in July, 1989, it marked the first occasion on which any regulated rural industry in Australia had been totally deregulated.

The deregulation of the egg industry in NSW has also been extremely successful by comparison with similar attempts elsewhere.

For these reasons it may be useful to identify the particular factors which were instrumental in effecting the outcome.

Why the Government deregulated the industry

It may be helpful at the outset to indicate the problems which the Government wished to overcome.

1. Consumers had to pay too much for eggs

The Government's review showed that after the industry adjusted to deregulation, the wholesale price of a dozen eggs would fall substantially.

Independent consultants found that the cost of servicing investment in egg licences alone added 13 cents to the cost of every dozen eggs produced, or \$7.3 m. annually. This simply financed the cost of participation in the quota system.

Independent consultants estimated that hen levies added a further 27 cents to every dozen eggs produced, or \$15 m. annually.

2. The regulated system was inefficient

By its very nature, the regulated system accommodated inefficiency instead of penalising it. For example, it cost private producers about 10 cents per dozen to handle eggs. This compared with a cost of 30 cents per dozen at the Corporation's Lidcombe plant. As a result, consumers had to pay 20 cents per dozen for eggs produced at Lidcombe over and above the cost of buying the same eggs from private producers.

3. The system made the Egg Corporation lose consumers' money

The system required the Corporation to buy all eggs produced in NSW at the same price, regardless of market demand. As a result, in 1988/89, about 30% of the Corporation's eggs were purchased from producers at prices higher than the price for which the Corporation could sell them.

Since the regulated system denied the Corporation commercial flexibility, the Corporation made heavy operating losses every year since its inception:

1983/84	\$24.0m loss
1984/85	\$13.5m loss
1985/86	\$9.5m loss
1986/87	\$8.7m loss
1987/88	\$20.9m loss
1988/89	\$18.0m loss

The losses of the Corporation were ultimately met by all taxpayers. Consumers had to pay 27 cents in every dozen eggs over a full year, simply to cover the Egg Corporation's operating loss for 1989.

4. The system prevented freedom of choice

The NSW Egg Corporation and its agents had a statutory monopoly on egg sales in NSW. The consumer had no choice but to buy eggs which were graded, packed and sold in the form prescribed by the Corporation. Since quality standards and prices were fixed by the old system, producers also had little capacity to cater to speciality markets such as completely free range and organic farming.

5. Regulation hurt producers

Production quotas, levies and regulated prices imposed strains on the producers they were supposed to assist. During the last 15 years, 6 producers out of every 7 left the industry. The industry concentrated into a handful of farmers who could still meet the costs associated with the system.

6. The system rewarded people who broke the law

Farmers who did not hold licences or pay hen levies enjoyed an advantage over farmers who obeyed the law. The regulated system thereby provided an incentive to break the law.

To undercut the Egg Corporation, illegal producers only needed to pass on to consumers a fraction of the savings which they made from breaking the law. Although they claimed free enterprise principles justified their actions, they had a commercial stake in the regulated system which they could not

Deregulation would remove the advantages which illegal producers derived from the regulated system and allow all producers to compete on equal terms.

7. The cost of enforcing the system was too high

In 1988/89, it cost \$1.5 m. to prosecute farmers who broke the rules. This was equivalent to \$5,800 for every egg producer in NSW, or nearly 3 cents on the price of a dozen eggs to the public for a full year.

8. Farmers should not have to hold licences to produce eggs

A medium-sized egg producer had to invest about \$800,000 simply to be allowed to produce. These costs were in addition to the costs of stock, feed, labour and land. The costs were ultimately passed on to consumers.

9. The system created artificial prices

The regulated system set prices and supply through regulation rather than through competition. As a result, it was never certain whether consumers had a right to be paying less or an obligation to be paying more.

10. Egg production is no business of Government

The system required the Government to own all eggs produced in NSW and to own and operate a major egg processing plant as a government monopoly. The Government also restricted the right to produce. It is questionable whether the Government has any legitimate right to involve itself so directly with this activity.

11. It made commercial sense to buy out of the system

It cost the taxpayer \$61 m. to buy out the licences associated with the regulated system. Since the cost of servicing levies and licences added at least \$22 m. to the price of eggs annually, consumers looked to recover the cost of compensation within three years. They would also be free of the ongoing costs.

The big issue was how to deregulate without encountering the problems which occurred in New Zealand where the egg industry lurched into major crises after deregulation.

Key elements of the deregulatory strategy

The key elements of the deregulatory strategy were as follows:

- All production and regulatory controls over the egg industry in New South Wales were lifted overnight. Only [unclear] controls remained.

- Farmers were compensated by \$15 per quota bird. They received this compensation within six months of deregulation and a total payout of about \$61 m. (an average of \$250,000 per farmer) was involved.
- The Egg Corporation continued to trade in the marketplace as a commercial business in anticipation of its sale to private enterprise.
- The Government encouraged the farmers to establish their own co-operative in order to assume more responsibility for the affairs of their industry.

Experience since deregulation

It is now evident, some six months later, that deregulation in New South Wales has gone remarkably well.

The price of eggs to consumers has fallen by between 30 to 50 cents per dozen as predicted.

The industry has remained remarkably stable without any significant reduction in producer margins or producers being driven from their farms.

Contrary to many widespread expectations, deregulation has made it possible for the Egg Corporation substantially to improve its financial position. Average prices paid for eggs consigned to manufactured products since deregulation have fallen by an astonishing 34% reducing the business' input cost by some \$3 m. annually. Deregulation has also freed the Corporation to adjust the prices of finished product sold to commercial consumers. Since deregulation, the sales price of liquid whole egg, for example, has increased by 8.3%.

As a result of these and other changes, the Corporation is now trading at cash breakeven without the assistance of levies for the first time. This represents the difference between a prospective \$8 m. loss this year and an \$18 m loss last year.

Since the regulated system was thought to be the Corporation's financial shelter, few people would have believed such a turnabout was remotely possible.

Public concerns about the egg industry also appear to have been almost totally satisfied. I do not believe that any Government needs to apologise for taking account of the popular will. During the six months prior to deregulation, the Minister for Agriculture and Rural Affairs, Ian Armstrong, received some 800 letters from the public on the subject of eggs. Since then he has received only 60 letters from all interested groups on the subject. Put simply, the Government has presided over a quiet revolution without affecting the

Why did it work?

A number of factors appear to have contributed to the success of the strategy.

Unlike deregulation in New Zealand, there was no transition period into the new system. Overnight deregulation enabled the price of eggs to fall instantly by at least the value of levies. This produced an immediate benefit to consumers without reducing producer margins. It also played an important part in persuading consumers that it was worthwhile to pay compensation to the farmers. I strongly believe that a transition period under which the old system was ostensibly in force would have created uncertainty and an opportunity for unscrupulous people in all sectors to gain an illegal head start on their peers.

Undoubtedly the most decisive factor was, however, the Government's determination to give everyone involved a stake in the change. The aim was to produce a win/win scenario for all concerned. This was certainly more important than the desire to apply deregulatory principles for their own sake.

Consumers, for their part, had to accept that compensation would be payable, but were rewarded by lower egg prices.

Farmers received compensation for their loss of quota. They could never have been expected to forego this, however indefensible the quota system itself might have been. I believe that compensation to the producers played an essential part in the success of the deregulatory process.

Nor was the industry left entirely to fend for itself. The Corporation remained in place to purchase eggs and smooth industry adjustment. The Government also helped farmers to establish their own co-operative and afforded them the chance to assume more direct responsibility for handling the industry's affairs. In so doing, the Government allowed the industry both the opportunity and the breathing space to self-regulate.

It was also necessary for the rightful beneficiaries of deregulation (producers who had obeyed the law and consumers) to be the ones who benefited. We had to make sure that unlicensed producers who were merely parasites on the regulated system were no longer able to enjoy an unfair advantage.

A number of external factors also contributed:

- The producers who were big enough to engage in predatory pricing were also the most heavily geared. This protected the system from the concentration which the opponents of deregulation most feared.

- Deregulation occurred at a time of national egg shortage. This meant that any producers who increased the size of their flocks could do so without threatening the livelihoods of other farmers. There were markets for everybody.
- Deregulation occurred at a time when all other states in Australia were still labouring under regulated systems. This meant that the interstate competitors to the newly deregulated industry in NSW were competing on disadvantageous terms from the outset. There was no threat from interstate.

In all these respects, the NSW experience has not only been unique in Australia but is a singular phenomenon internationally. The issue is, of course, whether similar strategies might succeed in other industries. The merits of deregulation aside, the lessons which are taught by NSW experience in deregulating the egg industry run counter to accepted conventional wisdom in a number of respects. Put simply, they are:

- Overnight deregulation is best for all concerned.
- Emphasis needs to be on giving all participants a stake in the change rather than implementing deregulation for its own sake. This may necessarily mean compensation for the enterprises being deregulated.
- Retention, for a transition period, of some of the institutions associated with the regulated system in order to soften the blow.
- Active encouragement to establish alternative institutions, to fill the vacuum when the regulatory authority leaves the nest. The Government's active work in encouraging the establishment of the co-operative was a case in point.
- Careful thought to timing to ensure that at the time of deregulation, sufficient demand exists to absorb the increased production which deregulation can encourage.

The overriding message is that the strategy must concentrate on benefits and reflect the likely practical ways in which those affected by the change will respond to it.