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Adding Value with Mutton: Is Pricing Everything?

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This paper is an attempt at looking at the cost and benefits of the small stock value addition scheme implemented in 2004. Thus far about 146 jobs have been created through the establishment of new abattoirs, however this seem to have taken place at the expense of mutton producers as they face "losses" ranging from N$1 million to N$ 20 million due to adverse pricing on the part of local abattoirs as well as through the deduction of the value addition commitment fee of N$1.50 per kilogram from the South African reference price. This means that either we intended to create very expensive jobs or intended to reduce the income of farmers. Of equal concern is the low take-off in terms of other downstream activities traditionally link to value addition in the meat sector such as value addition to hides and skins for leather and other uses. With regards to tanning for instance, not much has happened since the scheme was implemented as skins are still exported after the basic process of pickling. The paper recommends that the Meat Board should actively monitor abattoir prices in order minimises potential income shortfalls that producers may suffer as a result of too low prices.

1. Introduction

Despite being drought-prone, Namibia hosts more than four million small livestock, and these are concentrated in the Hardap and Karas regions. These two regions accounts for 68% of the country's sheep, whereas the northern communal areas (NCA's) and Northern Kunene account for 47% of Namibia's goat population. Namibia ranks third in Southern Africa in sheep production after South Africa and Tanzania. While Namibia has several breeds of goats and sheep; for commercial trade the boergoat and doper sheep are the prime breeds. However, Damara, Van Rooy and Karakul sheep are also important breeds due to adaptability to arid conditions. With current developments in the international pelt market, the importance of Karakul may increase overtime and farmers might be well advised to move in the direction of Karakul as a way to spread risk across a wider portfolio of livestock. In fact some will argue that for long-term sustainability of grazing pastures, Karakul might be the best bet for drought-prone Namibia. However, karakul pelt production is coming off a low base and the dominant sheep breed is still the dorper, which was specifically developed for mutton production (see Table 1). The dorper sheep accounts for over 60% of all sheep bred in Namibia. This makes Namibia an excess producer of mutton and therefore a net exporter of mutton. Another small stock breed that is also developed for meat production, namely the boergoat accounts for nearly 20% of total small stock in Namibia. Jointly, the dorper and the boergoat accounts for nearly 60% of total small stock (see Table 1).

Table 1 Total production of sheep and goat: 2002 to 2005

Year	Karakul	Dorper	Other	Total sheep	% Dorper	Angora	Boergoat	Other	Total	% Boer goat
2002	236,771	1,836,731	690,751	2,764,253	66.4	4291	1,096,781	1,009,020	2,110,092	59.1
2003	222,832	1,931,566	801,056	2,955,454	65.3	4544	961,251	1,121,017	1,981,725	48.5
2004	202,542	1,675,788	741,033	2,619,363	64.0	3,683	956,801	1,036,688	1,997,172	47.9
2005	183,501	1,752,162	728,132	2,663,795	65.8	19,995	964,764	1,058,720	2,043,479	47.2

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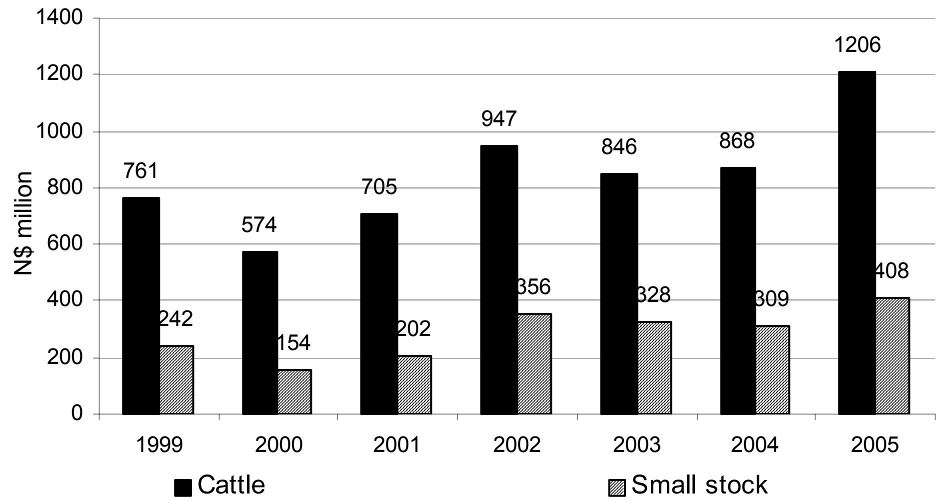
Source: Annual Reports of the Meat Board of Namibia (various issues)

For many years Namibia has been exporting on average about 960,000 live sheep per year to South Africa. The table below provides comparative figures of income generated by both large and small stock exports. In the context of the Small Stock Marketing Scheme, it is the directive that the export of small stock, especially sheep on the hoof shall significantly be reduced in the short-run and would be totally ceased in the longer-term. In addition to sheep exports, on an annual basis Namibia exports on average some 250,000 live goats to RSA.

Figure 1 Export value of cattle and small stock



Source: Meat Board of Namibia

Figure 1 shows the export value of Namibia's livestock, broken down into cattle and small stock. It is clear from this graph that the export returns of small stock have been relatively more volatile compared to cattle. In 2005, Namibia exported N$1.6 billion worth of livestock of which small stock accounted for N$ 406 million or 25%. Given the figures shown in the above-mentioned table and figure, it becomes quite possible for politicians to assume that raw materials are available in good quantities and that the issue of value addition to create and increase employment opportunities in Namibia and to support the manufacturing of leather products would be viable and should therefore be pursued. In fact the introduction of the Small Stock Marketing Scheme could be understood in this context.

2. Value Addition in Context

The introduction of the small stock marketing scheme has been underpinned by the desire of the Namibian government to jump-start industrial development and job creation by introducing value-addition to available raw materials, especially in the mining and the agricultural sectors. And this is explained by Namibia's industrial policy as set out in the White Paper on Industrial Development, which was launched in 1992.

The primary aim of Namibia's industrial policy as contained in the White Paper on Industrial Development, is to transform Namibia's economy from being the producer of primary products and exporter of raw-materials to one which is able to transform its raw-materials and exports finished manufactured goods.

The objectives identified in the White Paper were as follows:

- Increase manufacturing value added by stimulating productivity, increased exports and where efficient, import substitution

- Diversify and integrate the economy through accelerated growth of the industrial sector and the creation of better links between sub-sectors

- Generate productive employment opportunities and increase income generating opportunities for Namibians, especially for previously disadvantage groups, such as women and
- Improve the geographical distribution of industry in relation to the location of raw materials, markets, population and employment demand.[2]

Second, Namibia's industrial policy is meant to address the issue of product diversification. Currently, the country has a very narrow range of manufacturing activities, primarily based on its natural resource endowment, mainly fish and fisheries products, meat and meat products. In short, products diversification is an important element of Namibia's industrial policy – developing new products. But as yet we are far from achieving sufficient levels of product diversification for export purposes. In addition to the industrial policy, Namibia's agricultural policy is also supportive of the value addition strategy, which highlights the need for maximization of the potential value added within the country to national agricultural output.

3. The small stock marketing scheme

The Scheme has strong policy rational, as it is an instrument in the implementation of the overall value addition strategy of the country. It aims at providing producers, processors and exporters a framework to fully utilize the available slaughtering and tanning capacity in Namibia within a 4-year period, i.e. 2003 – 2007.

With its implementation it is believed that such objectives as the improvement of value addition and all its facets, i.e. employment creation, capacity utilisation, income generation and foreign exchange earnings are to be achieved.

The Scheme is underpinned by the following principles:

a. ensure that the meat production, processing and tanning industry be self-regulating within the framework of the Meat Industry Act of 1981;
b. ensure that producers will have a choice over the slaughtering facility to be used; and
c. ensure competitive prices for producers, abattoirs and tanneries.

The Scheme envisages a pro-rata increase in the local slaughtering of small stock to approximately 100% utilization of available slaughtering capacity by 1 November 2007. While most producers welcomed the Scheme, exporters of sheep on the hoof were sceptical, but were nevertheless presented with no option but to implement the government directive. Scepticism by some was hardly surprising as this is normal for any new policy initiative, with gains often being distributed unequally.

The table below illustrates the adaptability of the scheme to accommodate full utilization of local slaughter facilities at accredited abattoirs. Should new facilities be established, the percentage of intervention would increase to say 65% (Phase II) of available small stock produced which will have to be slaughtered at accredited abattoirs, locally.

Table 2 Meat industry strategy to ensure that Namibia slaughters within 4 years near to 100% of production

	Phase 1	Phase 2	Phase 3	Phase 4
Available lamb	1,000,000	1,000,000	1,000,000	1,000,000
Abattoir capacity	540,000	760,000	760,000	1,000,000
Intervention (%)	50	65	80	95
Local slaughtering	500,000	650,000	800,000	950,000

Source: Meat Board Schedule of the Small Stock Marketing Scheme (undated)

The basis of the Scheme rests upon section 10(l)(r) of the Meat Industry Act, 1981, which provides as follows: "The Board shall have power, with the approval of the Minister, to prohibit any person or any person of any category or class to sell or

[2] GRN, Review of the White Paper on Industrial Development of 1992.

export from Namibia any controlled product or any category or class thereof, except on the authority of and in accordance to the conditions contained in any permit issued by the Board". *(S. 20(b) contains a similar provision, although in that case it is the Minister who must issue the Government notice.)* The Meat Board included the following condition to the permit:" By 1 July (in terms of Gov Notice No. 129 published under the Meat Industry Act) the Meat Board started to implement the Small Stock Marketing Scheme in terms of which only 50% of sheep would have been permitted to be exported live, while 50% must have been slaughtered internally. Under the Scheme, it is only when all the abattoirs are slaughtering at full capacity, and farmers have to market animals in times of oversupply or in drought situations, that traders can apply for an export permit. In September 2006 a new quota formula was implemented allowing for exporting one sheep for 6 slaughtered (Agriforum, 2006).

4. Economic impact

4.1. Job creation

As indicated in the Cabinet resolution, 19[t]/14.03/009 of October 2003, the issue of job creation had been one of the key considerations as Cabinet assumes that the implementation of the Scheme would lead to additional jobs, for the country, which is suffering from over 30% unemployment. This optimism is based on the assumed potential of the Scheme to have downstream activities, especially, the tanning and subsequent manufacturing of leather products by established and new business entities.

Table 3 Jobs created as a result of the implementation of the Scheme

Abattoirs	Before the Scheme	After the Scheme	Net jobs
NamcoKeet	0	89	89
NamcoWindhoek	54	54	0
Farmers' Meat Market (M.tal)	93	93	0
NNMP (Aranos)	0	57	57
Total	**147**	**293**	**146**

Source: Various Abattoirs

However, the creation of additional slaughtering capacity in Aranos and Keetmanshoop, only added 146 jobs. Whereas two abattoirs that were already operational before the Scheme managed to sustain existing jobs only. NamcoWindhoek, which was Just Lamb before, maintained its employment figures even after the introduction of the Scheme. Of the total number of about 54 employees at slaughtering plant in Windhoek, about 15% are casual labourers. In the case of NamcoKeetmanshoop, employees for the now defunct ostrich abattoir have virtually been transferred to the sheep abattoir and recently about 72 employees from the ostrich section were retrench in September 2006 (The Namibian, August 2006).

4.2. Downstream value addition limited to pickling of skins

So far on the issue of downstream activities such as the tanning not much has happened since the Scheme was implemented. In fact, skins are exported after the basic process of pickling. However, at the NamcoKeetmanshoop plans are afoot to undertake production of leather from sheepskins. This is probably where most jobs are likely to be created in the future – *but when in the question*?

4.3. Utilisation of slaughter abattoir capacity

For the first 22 months since the introduction of the Scheme on 1 July 2004, an average of 67% of slaughtering capacity of all export abattoirs has been utilized. February 2005 to April 2005 has been the peak production months given the normal production cycle, when slaughtering was in excess of 73 000 sheep per month or 70% capacity utilisation. Already in the first 22 months, NamcoKeetmanshoop and NamcoWindhoek reached 80% capacity utilization implying that there is indeed the possibility to reach the set targets regarding abattoir capacity utilization. It is interesting to note that the NamCo Keetmanshoop abattoir represents 24% of the total slaughter capacity but is responsible for 32% of actual throughput. Farmer's Meat Market and the NNMP abattoir are the only abattoirs that have a throughput lower than the national average of 67%.

Table 4: Capacity utilization at export abattoirs: July 2004 to April 2006

	FMM	Namco Wdk	Namco Khp	NNMP	TOTAL
Actual slaughter	346,196	388,671	420,552	173,313	**1,328,732**
Capacity	544,800	550,800	471,600	411,600	**1,978,800**
% Of total slaughter	26%	29%	32%	13%	**100%**
% Of total capacity	28%	28%	24%	21%	**100%**
% Slaughter of own capacity	64%	71%	89%	42%	**67%**

Source: Meat Board of Namibia

4.4. Price developments

One of the core principles of the scheme was to ensure competitive prices for producers, abattoirs and tanneries. In the case of the producers, this would mean trading their stock to local abattoirs would not deprive them of higher returns elsewhere, particularly the South African market. For abattoirs, competitive prices would ensure that there is adequate capacity utilisation such that abattoirs remain profitable. To this end, a price monitoring mechanism was put in place, and following meetings (17 August 2005 and 06 March 2006) between producers and abattoirs it was agreed that the South African Red Meat Abattoirs Association (SARMAA) price minus N$1.50 would be the local reference price for the next six months (Schutz, 2006).

Table 5: Price difference: SARMAA and Namibian Abattoir Prices

Grade	2001	2002	2003	Average	Jan – April 2006
A	0.08	-0.20	0.55	**0.14**	**1.24**
AB2	0.71	0.50	1.12	**0.78**	**2.25**
B2	1.20	2.48	1.81	**1.83**	**4.49**
C2	-0.66	0.57	1.20	**0.37**	**2.85**

Source: Meat Board of Namibia

A detailed analysis of price movements' show that not all grades experienced upward movements. Apart from the A grades, all the other grades lag the SARMAA prices by a margin larger than N$1.50, with a highest deviation of N$4.49 for B2 grades (see Tables 5 and 6). This means that for an 18kg carcass a producer would be getting N$80.82 less or N$54.00 (after accounting for a difference of N$1.50 reference price) by selling locally. It is also interesting to note that price differences were lower before the onset of the scheme in mid-2004. According to Schutz (2006) this price differential could be attributed to lower marketing in the respective grades.

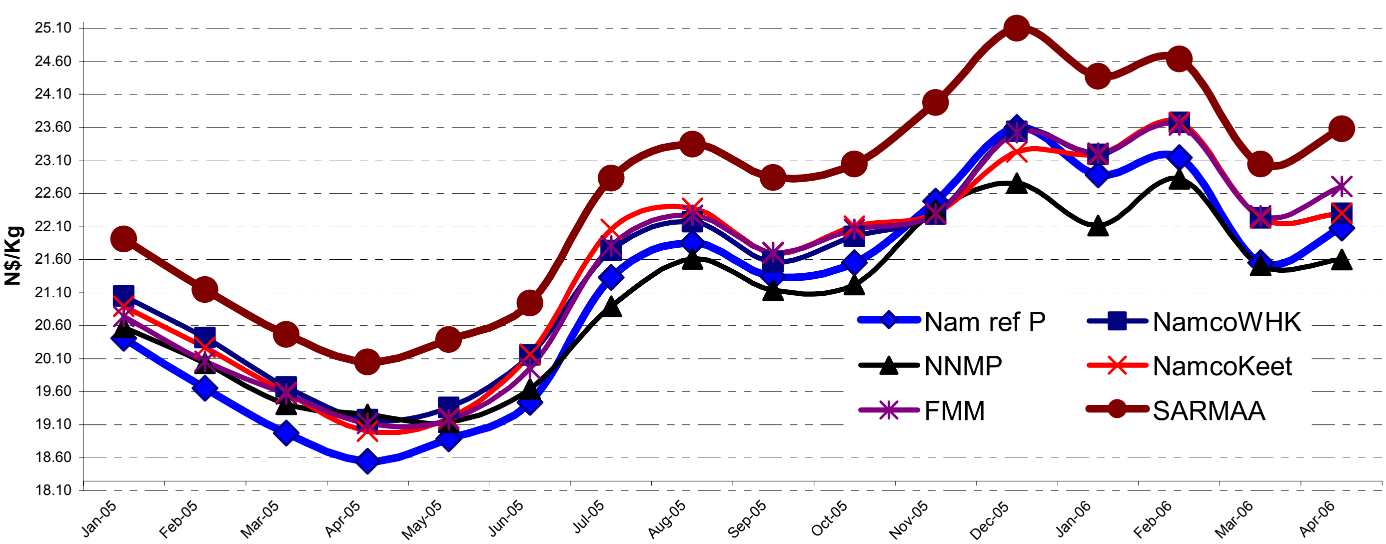
Table 6 Price difference: SARMAA, Nam ref and Namibia abattoir prices

	Nam abattoirs vs. SARMAA		Nam abattoirs vs. Nam ref price	
	Jan 05 – April 06	*Jan – April 06*	*Jan 05 – April 06*	*Jan – April 06*
NamcoWHK	1.08	1.06	-0.42	-0.44
NNMP	1.60	1.90	0.10	0.40
NamcoKeet	1.09	1.06	-0.41	-0.44
FMM	1.10	0.96	-0.40	-0.54

Source: Meat Board of Namibia

Meanwhile, the weighted A-grade price development in the respective export abattoirs is shown in the graph below (see Figure 3). In general, prices paid to producers have often trailed that of the SARMAA and for most abattoirs, prices have been above the Namibian reference price. The only exception is the Aranos (NNMP) abattoir, whose prices have been below the reference price for most of the period under review. Table 6 below summarises the difference between prices paid by the respective abattoirs compared to that of SARMAA. Clearly, prices in all with the exception of the Aranos abattoir have on average been closer to the SARMAA and higher than the Namibian reference price. Indeed, this shows that not all producers of the A-grade have been benefiting from the lower price differential as earlier pointed out. Furthermore, it does not fit in with reasoning put forward in terms of low prices in AB, B and C grades such as the low throughput for certain grades since the A-grade remains the most marketed of the all age groups. In fact the A grades represents between 80% and 90% of all slaughtered carcasses for 2003 and 2005. Altogether, this implies that some of the producers are not benefiting by selling locally as they could generate more income by selling to the South African market. We have quantified the forgone income of producers due to the scheme below (see Tables 7 and 8).

Figure 3: Price difference: weighted average producer prices for A-grade



Source: Meat Board of Namibia

5. Costs to producers – is pricing everything?

The benefits of the Scheme are centred on its potential value addition, which would have led to the development of a leather industry. But this has not taken off as yet. Also, the building of a new abattoir at Aranos and the introduction of new production lines at already existing abattoirs have made it convenient for farmers as they do not have to travel long distances to sell their stock. The fact that there has been a divergence in prices between abattoirs and

South African prices represent potential losses to sheep producers in particular. We have attempted to quantify some of these losses under two scenarios. Under the first scenario we asked the question of how much income would farmers have raised had they sold their mutton at South African reference prices. The answer to this question is found in Table 7 and shows that farmers are currently nearly N$20 million less than they would otherwise get in South Africa. Under this scenario the losses are quite pronounced for grades A (N$ 15 million) and C (N$2.66 million).

Under the second scenario we asked how much income sheep producers would earn if they were paid the Namibian Reference as discussed earlier. Currently local abattoirs are obliged by the Meat Board to pay a Namibian reference price, which is the South African reference price minus N$1.50. Under this scenario there are some improvements although not for all grades of carcasses. Notice that under this scenario we assume that the Namibian reference price is optimum. Here the loss of N$20 million recorded under the first scenario becomes a “profit” of N$1.3 million across all grades of carcasses. This suggest that on average local abattoirs are at least paying more than the Namibian reference price specifically for A grades where there is certainly competition as this grade represents over 90% of all abattoir throughput. The same cannot however be said of older grades, namely B and C. According to the calculations in Table 8 producers marketing B and C grades get N$1.5 million less than they would otherwise receive if they were paid the Namibian reference price. The question is the Namibian reference price the optimum price for all grades or only for select grades. This is an important question because without the local reference price Namibian farmers are likely realising more income from their mutton.

Table 7 Income losses suffered by farmers due to scheme in 2005

Grades	Actual Income NAM Abattoir sales	SARMAA price	Income Shortfall/Surplus (-)
All A grades	N$ 259.93 million	N$275 million	(N$15.1 million)
All AB grades	N$ 5.09 million	N$ 6.7 million	(N$1.6 million)
All B grades	N$ 1.92 million	N$ 2.2 million	(N$ 0.310 million)
C grades	N$ 12.38 million	N$15 million	(N$ 2.66 million)
TOTAL	**N$ 279.3 million**	**N$ 299 million**	**(N$ 19.67 million)**

Source: Authors’ calculations

Table 8 Adjusted Income differential due to scheme in 2005 (calculated with reference price)

Grades	Actual Income NAM Abattoir sales	Income at Adjusted SARMAA price (NAM Ref Price)	Income Shortfall/Surplus (-)
All A grades	N$ 259.93 million	N$256 million	N$3.9 million
All AB grades	N$ 5.09 million	N$ 6.2 million	(N$1.1 million)
All B grades	N$ 1.92 million	N$ 2.06 million	(N$0.140 million)
C grades	N$ 12.38 million	N$13.8 million	(N$1.4 million)
TOTAL	**N$ 279.3 million**	**N$ 278 million**	**N$1.3 million**

Source: Authors’ calculations
Notes: The adjusted SARMAA price is NAM reference price set at SARMAA price minus N$1.50/kg by the Meat Board.

6. The way forward – price monitoring critical

Given the scheme’s limited history, much cannot be said regarding the realisation of value addition in its entirety. So far, it has been observed that there has been increased utilisation of local abattoirs, which have since resulted in the retention and creation of job opportunities. On the other hand, it has been observed that the scheme has had a negative impact on price developments, particularly among AB, B and C grades of sheep. There is also evidence that not all abattoirs pay according to the Namibian reference price in the prime A-grades of lamb. This happens in the presence of price monitoring. Having said that, while the scheme has in place a price monitoring mechanism, it is not clear what actions would be taken against abattoirs whose prices are found to be below the local reference price. In this case two measures are suggested.

Going forward a penalty has to be devised that would be imposed on abattoirs found to violate the minimum set prices. We have shown that farmers are loosing between N$1 million and N$15 million on certain carcasses depending on the reference price used. While it is noble that farmers should show their commitment to economic development through receiving lower prices than they would otherwise get on the world market the scheme should not alienate producers in the long run. Therefore the Meat Board should henceforth closely monitor prices paid by abattoirs, specifically for B and C grades. Furthermore, the Meat Board should look into the optimality of the N$1.50 penalty (or commitment fee) imposed on local producers. It is clear that the Meat Board is indeed concerned about pricing as well (see for e.g. Agriform 2006, p. 59) but they have to move beyond just being concerned to active monitoring.

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List of People Interviewed

F Mouton, Managing Director. Namco Keetmanshoop

K Franken, Plant Manager. Namco Windhoek

L Swartz, General Manager, Farmers Meat Market Mariental

Smith, Secretary. Natural Namibian Meat Producers