

**INQUIRY INTO SUSTAINABILITY OF THE DAIRY
INDUSTRY IN NEW SOUTH WALES**

Organisation: Dairy Connect Limited

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13 November 2018

The Hon Robert Brown MLC
Chair
Portfolio Committee No. 5 – Industry and Transport
Legislative Council
Parliament of NSW
Macquarie Street
SYDNEY NSW 2000

By email

Dear Mr Brown,

Re: Inquiry into the Sustainability of the Dairy Industry in New South Wales

By way of background, Dairy Connect is an industry body representing the value chain of the Australian dairy industry, including but not limited to dairy farmers, processors, vendors and other industry stakeholders. We also work cooperatively and collaboratively with other agricultural and dairy bodies to ensure that the best outcome is obtained for the dairy industry in NSW specifically and in Australia generally.

Terms of Reference 1(a)

“The nature of, and relationship within, the value chain between farmers, processors, logistics companies and retailers and their respective influence on price”

One of the major issues confronting the sustainability of New South Wales’ dairy industry is the relationships between dairy farmers, processors and supermarkets. The influence of the relationship between farmers and

processors on farmgate price is particularly of concern. At the root of the problem is the fact that currently the farmgate price received by farmers by selling their milk supply to processors does not, generally, cover the costs of production in the operations of a dairy farming enterprise.

This is due in part because of a bargaining power imbalance which exists between the two parties, an imbalance which the Australian Competition and Consumer Commission (ACCC) has specifically noted as an issue in the release of its interim report in November 2017 and in its final report released in April 2018. These reports may be found at <https://www.accc.gov.au/focus-areas/inquiries/dairy-inquiry-0>.

Dairy Connect has indicated to the ACCC our strong support of the 8 recommendations that the ACCC have put forward to the Federal Government to address, in part, the inequities that are being encountered by producers in providing fresh nutritious produce, on a daily basis, to their contracted processor. A copy of the submission from Dairy Connect to the ACCC by letter dated 31 January 2018 may be viewed at <https://www.accc.gov.au/system/files/D18-13587%20Dairy%20Inquiry%20-%20Submission%20-%20Dairy%20Connect%20-%20paper%20only%20-%2031%20January%202018%203.pdf>.

The mandatory code will provide for dairy farmers to be able to go from being 'price takers' to 'price negotiators'.

This provides information as to the difficulties that are encountered by producers where milk supply agreements contain clauses that may be considered unconscionable. While the introduction of a federal mandatory code, overseen by the ACCC, will not be a panacea to all the issues confronting the relationship between the producer and processor, it will provide a platform that is transparent, balanced and fair thus ensuring robust discussion to agree on contents of a milk supply agreement. This may provide a mechanism for an improved farm-gate price for the producer above the cost of production.

Hence, the monetary leverage that processors have over farmers has been reflected in 'one-sided' contracts which then dictates the low farmgate price that producers receive. It is important to note that this has come most likely as a trickle-down effect of the bargaining power that supermarkets have over these same processors. This is also reflected in the low wholesale prices that are negotiated and the passing of risk onto processors. Clearly there is a problem with this system. However, this is a matter that should be addressed once the mandatory code has been implemented between the producer and processor as recommended by the ACCC and endorsed by Dairy Connect.

In some cases, farmers have a direct trading relationship with supermarkets. For instance, in the United Kingdom, the supermarket Tesco has formed a Tesco Sustainable Dairy Group (TSDG) which aims to directly support their farmers by guaranteeing a market leading price. Importantly, this price is given irrespective of the price at which the milk is sold to the consumer and therefore provides a stable source of income.

This is a solution involving a direct relationship between farmers and supermarkets which has shown to be affective. While this is not accepted practice in Australia, a small number of dairy farmers have provided milk directly to the supermarket. An example of this is the Woolworths 'Farmers Own' brand.

As is stated on the Woolworths website:

"We have direct relationships with our Farmers and not via a processor or a Co-op to ensure they are getting a good deal every time. Our goal is to pay our Farmers a good price for their milk that allows them to continue to produce quality milk. We pick up milk from their farms and transport directly to be processed so we know exactly where the milk comes from that goes into Farmers' Own milk. Our farmers are engaged in the branding and feel a sense of belonging to the brand because it is their milk that goes into each bottle."

<https://www.woolworths.com.au/shop/discover/our-brands/farmers-own-milk>

Dairy farmers in NSW are feeling disenfranchised and disempowered by the lack of market transparency within the value chain. They are often provided with milk supply agreements that are overly complex, in both the clauses contained therein but also as to the length and number of contractual documents to which they are provided. They are provided with a price letter, a

milk supply agreement and a supply handbook. The length and type of the milk supply agreements needs to be amended and independent advice provided to the producer in a timely fashion by a third party.

An example may be referred to milk sampling, testing and calibration of milk testing equipment in NSW. Given the technical nature of the testing and the necessity to have appropriate oversight so as to ensure a consistent approach by the differing processors in NSW, Dairy Connect believes that the NSW Government through either the Department of Primary Industries or the NSW Food Authority should ensure that standards for milk sampling, testing and calibration of testing equipment should be standardised.

For instance, in relation to the calibration of milk testing sampling, Dairy Connect has not been able to find standards that would be used across industry, even though such calibration of equipment has a direct impact upon the price obtained by farmers at the farm-gate. Hence, there appears to no consistent methodology for the truck driver to sample the milk.

Further, Dairy Connect has been informed that there is no cross-checking between laboratories to ensure consistency. Hence, the farmers have reported inconsistencies after changing to a new processor.

Terms of Reference 1(b)

“The impact of external influences on the dairy industry, including but not limited to drought, water, energy, and price-setting”

Input costs for a dairy farmer has continued to increase without any corresponding increase in the farm-gate price of their produce. This has ranged from the increasing costs and availability of fodder (due to the onset of the drought), increasing energy costs, lack of water availability and reduced funding for dairy research & development.

Drought

The devastating ‘1 in 100’ year drought (of which agriculture has endured over the past decades on more than one occasion) has taken its toll on agriculture

and on the economies of rural and regional NSW and is financially crippling the dairy and livestock sectors. The long-term impact of the drought must not be underestimated at a time when dairy farmers are already receiving low farm-gate prices for their fresh produce.

At the current time, many dairy farmers are desperately attempting to source feed and fodder to keep precious livestock alive as the drought has entered its second year. Paddocks in New South Wales have lost moisture for continued growth and access to water has become difficult in areas such as the Murray and elsewhere.

Livestock producers and dairy farmers all need fodder supplies and short supply and demand are forcing prices up. Dairy Connect has been informed that producers are paying approximately \$450 and more for a tonne for grain

Dairy Connect acknowledges that the NSW Government has provided assistance for drought affected farmers. In July 2018, the NSW Government announced a \$500 million NSW Emergency Drought Relief Package to help farmers manage the effects of lingering drought.

Major elements of the \$500 million NSW Emergency Drought Relief Package include: \$190 million for Drought Transport Subsidies; \$100 million for cutting the cost of farming fees and charges – by waiving Local Land Services rates, waiving fixed water charges in rural and regional areas, and waiving class one agricultural vehicle registration costs

The package also includes \$150 million to bolster the Farm Innovation Fund infrastructure program; counselling and mental health; critical services in regional communities, including transporting water and drought related road upgrades and repairs; and animal welfare and stock disposal.

One way to ensure that producers are able to grow their dairy farming enterprises would be for the waivers and other fees set aside be continued for the foreseeable future by the NSW Government.

Energy Costs

Based upon data provided by Dairy Australia, and information obtained from them, a significant influencing factor on the sustainability of the dairy industry is the high cost of energy to processors and farmers. Energy costs were set to rise 50 – 70% for processors in 2017/18 which was projected to have a flow on effect on farmers and cost them \$89 million on farmgate prices. The energy increase meant that there was the prospect for processors to pay farmers 1c/L less, equating to approximately \$15,340 less paid per farm. Moreover, the energy price rise could also mean dairy farmers pay up to 20% more on their own power bills for dairy sheds, which is approximately up to \$4,840 on top of the current \$24,200 average. The increase in energy price has therefore acted on farmers directly and indirectly through processors.

The increase in energy price and shortage in gas supply in Australia is a deterrent for investors in Australian dairy. In recent years there has been a steep increase in gas production in Australia. However, there is a shortage of domestic gas supply which is due to market failure - the increase in exports of gas as a proportion of production, that is the free market's inability to account for Australia's national gas needs. Due to the shortage of domestic gas supply for use, higher prices are offered for gas supply which results in less favourable contracts arrangements.

The closure of coal-fired power stations despite the lack of an action plan to replace the baseload energy they currently provide is another deterrent for investment. For example, the closure of Hazelwood coal fire power station has made Victoria a higher importer than exporter for the first time in many years. The risk of energy supply disruptions is also particularly costly for farmers due to the risk of milk spoilage and failing to meet contract requirements since milk is a perishable good. These issues are contributing simultaneously to make Australian farmers less competitive.

The drivers of high gas and electricity prices include factors such as changing demand for energy, retail market manipulation which has maintained high prices and energy policy uncertainty which has led to low investment in new renewable energy generation technology. In a situation where market

mechanism such as a Clean Energy Target are utilised it would be expected that there would be a reduction in emissions which incentivises investment in new energy generation, new energy generation at a price lower than that of gas and an overall increased supply of energy from these new technologies such as through solar farms.

Thus, sky-rocketing electricity costs have meant that Australia was losing international competitiveness for agricultural products and this had hit dairy and irrigation farmers hardest. This impact is particularly severe on irrigated dairying that needs to pump water to grow fodder crops as well as keeping fresh nutritious milk cool. In reality, this appears to be market failure.

The ACCC report into the Australian Energy Market found that dairy farmers were paying twice for energy cost hikes. It was concluded that they pay once at the dairy shed and again at the farm gate in the form of price cuts for their fresh nutritious milk.

As can be seen, energy comprising electricity and gas accounted for a significant proportion of costs of dairy production and Dairy Australia has estimated that the total cost of energy for dairy processors was about \$160 million a year.

Dairy Connect has been cooperating with a renewable energy provider, Solar Bay, to assist dairy farmers in unravelling complex commercial transactions between producers and energy retailers.

Cameron Quin, National Business Director of Solar Bay has indicated to Dairy Connect that often debts claimed for energy consumption are just plain wrong and dramatically overblown. Solar Bay has provided information to Dairy Connect that indicated that dairy farmers who had not received an energy bill for months at a time were sent several bills at once with late payment fee's, incorrect energy tariff's and network tariff's that could be up to three times contracted charges.

A further example was provided that showed that one producer paid an incorrect network tariff fee over several months totalling \$7000, an amount that still hasn't been repaid.

As with milk supply agreements, energy retailers make it difficult with complex invoice and anti-competitive clauses. Producers are, more often than not, far too busy to take the time to try to analyse and understand indecipherable and incorrect invoices and anti-competitive contracts.”

One way to overcome this is to provide assistance to producers via a revamped milk marketing board.

Terms of Reference 1(c)

“The impact of previous policies, in particular, the deregulation of the dairy industry”

The deregulation the Australian dairy industry in 2000 has resulted in the number of dairy farming enterprises in Australia decreasing and Dairy Connect makes the following observations:

- Since deregulation the farmgate price of milk has not kept pace with CPI or inflation, and hence is falling behind significant input price increases such as energy, feed, labour etc.
- Milk production has stagnated processing and manufacturing capacity in NSW has declined. There has been less investment in the industry impacting on the growth and development of the industry and the opportunities for job creation, especially in rural and regional communities.
- There is market failure that needs to be addressed. We are not advocating for re-regulation in the former method but some form of regulatory intervention is needed to address the imbalance in market power between farmers and processors and between processors and supermarkets.

- Since deregulation there has been no state based generic promotion of the important role of dairy consumption in health and nutrition which can positively influence increased demand.

Terms of Reference 1(d)

“The role of government in addressing key economic challenges to the industry”

Given these challenges which are facing farmers, it is the responsibility of the government to help address the economic challenges which cannot otherwise be solved naturally in the dairy market. The following recommendations may provide a platform for the NSW Parliamentary Committee to consider:

Primary Recommendations for further review:

NSW Commissioner for Dairy & NSW Milk Marketing Board

It has become apparent that the producers require external support. This could come through the creation of a NSW Commissioner for Dairy. This position would be conduit to the relevant Minister and Parliament on issues that continue to be raised by the dairy industry in a regular and on-going basis.

Such reports could, for instance, an annual ‘state of the NSW Dairy Industry’ where information is provided to the Parliament as to the current position of the dairy industry in NSW.

The Commissioner, who would also be available to meet with producers within the regions, could be supported by a small secretariat based within the NSW Department of Primary Industries or alternatively, a small Milk Marketing Board could be re-establishment. It is not suggested that the Board would have any mandatory powers but rather be a point of contact for producers in NSW with issues that may arise with, for instance, their milk supply agreement.

Consistent regulations and reduction of red tape in the collection, transport and delivery of milk

The dairy industry, like other commodity areas, is subject to 'red tape' in the orderly operations of their dairy farming enterprises. However, unlike other commodity groups, dairy is also subject to testing that may be considered inadequate in some instances and without standards being implemented consistently. It would be opportune for the NSW Government through the NSW Commissioner for Dairy or other bodies such as the NSW Food Authority to standardise the current testing of milk samples and calibration of testing equipment in NSW.

Introduction of State based levy for RDE & infrastructure improvement for dairy farming enterprises

A State based levy could be imposed on the sales of all drinking milk sold and/or produced within NSW. These funds could be quarantined within, for instance, NSW DPI or a newly established NSW Milk Marketing Board with the purpose of providing assistance to producers for further research, development and extension services within the dairy industry. This fund could also be extended to assist producers seeking external assistance, infrastructure projects and similar projects. This could be a project that a NSW Dairy Commissioner could project manage.

A NSW 'Fair Milk Logo' campaign

This would be a mechanism to enable the consumer to identify milk sold that it is produced locally by placing appropriate 'logos' on containers of milk sold within NSW. This could extend to, for example, logos showing the nutritional value of milk as against plant-based drinks. This would be a voluntary campaign to highlight the importance of 'buy local' and/or 'buy nutritious milk'

Restoration of the availability of milk to schools for distribution to students

Dairy Connect has been advocating, with Foodbank NSW/ACT, for the restoration of the 'schools' milk' program to all schools in NSW. This would provide nutritious milk to children but also be a further source for sales of locally produce milk. It is noted that the International Dairy Federation (IDF) at the World Dairy Summit in October 2018 has strongly supported the

availability of nutritious through a school's program in member countries.

More recently, the NSW Legislative Council Committee Inquiry into fresh food pricing, chaired by the Revd the Hon Fred Nile, recommended:

“That the NSW Department of Education and NSW Ministry of Health, in liaison with Foodbank NSW and ACT and other non government stakeholders, introduce an evidence based school breakfast program across New South Wales that targets schools with a high proportion of children from socially disadvantaged families, by the end of 2019.” (recommendation 11)

IDF President Dr Judith Bryans told the IDF World Dairy Summit that school milk programmes provide children around the world with the nutrients they need to help them grow and develop healthily.

Milk sampling, testing and calibration of testing equipment

The NSW Government through either the Department of Primary Industries or the NSW Food Authority should ensure that standards for milk sampling, testing and calibration of testing equipment should be standardised.

Concluding Remarks

In conclusion, there have been many dairy reviews since deregulation in 2000 but still there has been a continued reduction in the number of dairy farms in NSW, from over 3000 at the time of deregulation to under 700 in 2018. This number is continuing to diminish.

The recommendations that evolve from this Inquiry will provide a benchmark for the dairy industry within NSW and without the support of Government and Parliament it is likely that NSW will, one day, import its milk from outside of the State, if not from outside of Australia. This may sound dire but the industry is at crossroads and has a 'once in a generation' opportunity to ensure its sustainability within NSW.

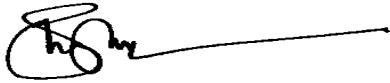
Failure to do so may result in the decline of the dairy industry's importance to the economic vitality within Australia and elsewhere throughout the world where Australian dairy produce provides sustenance to growing nations

Dairy Connect compliments the NSW Parliament and in particular the Committee and its Chair, the Hon Robert Brown MLC for the holding of this Inquiry. It is apparent that NSW, as a fresh milk State, has many differences to

other parts of the Australian Dairy landscape.

The question that needs to be asked now for a NSW dairy industry is not will it be sustainable and how best to ensure that outcome but rather will a NSW dairy industry survive past the current generation of dairy farmers within the State.

Yours Faithfully,

A handwritten signature in black ink, appearing to read 'Shaughn Morgan', followed by a long horizontal line extending to the right.

Shaughn Morgan
Chief Executive Officer