

**Submission
No 81**

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

Name: Professor Greg Patmore

Date Received: 20 October 2020

19.10.2020

Re Inquiry into the long-term sustainability of the dairy industry in New South Wales
(Legislative Council of NSW – Portfolio Committee No. 4 – Industry)

Dear Committee,

I welcome the opportunity to make a submission to the Inquiry by highlighting the benefits and history of the co-operative model for the dairy industry. Co-operatives being member-owned and controlled ensure that farmers participate in and fully benefit from value added by their co-operatives. Co-operatives also have benefits for their local communities by earnings being retained at the local level.

The Co-operative Business Model

The modern principles of the co-operative business model have their origins in the ideas underpinning the Rochdale consumer co-operative that was established in the UK in 1844. Since 1995 the International Co-operative Alliance, the co-operatives' international organisation, has set forward several fundamental co-operative principles: voluntary and open membership; democratic

member control; member economic participation; autonomy and independence; education, training and information; co-operation among co-operatives; and concern for community.¹

The co-operative model took on a variety of forms with different challenges including consumer co-operatives, worker co-operatives, financial co-operatives and agricultural co-operatives. Farmers formed agricultural co-operatives to provide crucial supplies for farmers such as seeds and fertilizers through bulk purchases that reduce costs. They may also allow farmers to vertically integrate by marketing and distributing their goods. Early examples of these types of agricultural co-operatives can be seen in the US, where farmers had to sell stock in distant markets, with co-operative pig marketing beginning in Granville, New York, in 1820. Farmers can also vertically integrate through co-operatives by establishing facilities to allow the processing of their products so that they are fit for human consumption. Early examples of these types of agricultural co-operatives can be found in cheese factories and creameries in countries such as Canada, Denmark, Ireland and the USA. Other forms of agricultural co-operatives include irrigation co-operatives and fishing co-operatives.²

There are a variety of reasons why farmers would form an agricultural co-operative. They can be a protest against the present economic and political system, especially during economic downturns. Agricultural co-operatives may specifically arise from market failures or contract failure, where suppliers, processors and marketers cannot be controlled through traditional contracts. Farmers desire to cut out the ‘middle-man’ and gain direct control over supply, marketing and production. They wish to obtain a fair price for their produce and to reduce production costs through economies of scale, greater co-ordination and avoiding intermediaries who may charge large fees for their services. They also desired to create new markets for their produce and protect existing markets. Agricultural co-operatives also allow farmers to pool risk in what can be a volatile industry in terms of market demand, weather and pests and capture profits from others involved in the food supply chain. Greater stability in income allows farmers to

¹ Birchall (1997), 57-65; Patmore and Balnave (2018), 3-4.

² Barton (1989), 12; Birchall (1997), 14-16; MacPherson, (1979), 10-11.

exercise greater quality control and achieve greater productivity through crop variety and herd improvements. The governance costs of co-operatives are also lower if members are homogenous with similar objectives such as producing a similar crop. Overall by combining together farmers increase their market power.³

There have been claims that agricultural co-operatives, including dairy co-operatives, inevitably fail or demutualise. Agricultural economists have argued that agricultural co-operative failures, including demutualization, may arise from systemic problems with the co-operative business model. They claim that agricultural co-operatives tend to be less flexible than Investor Owned Businesses (IOB) in shifting their economic focus as markets change due to their democratic governance and their attachment to the original objectives that underlay their formation. As they grow there tend to be more competing interest groups which leads to conflict and a tendency for those with goals relating to organizational gain rather than co-operative ideals to take over. One competing interest group are ‘dry’ or non- trading shareholders, such as retired farmers, who may be interested in getting the best return for their shares rather than getting the best price or service from the co-operative. The co-operative increasingly behaves like an IOB with corporate-orientated aspirations such as profitability and financial stability taking priority over member centred goals such as the level of service and economic democracy.⁴ Cook and Bures have noted that the life cycle of agricultural co-operatives consists of five phases: economic justification; organizational design; growth, glory and heterogeneity; recognition and introspection; choice, whether to ‘tinker, reinvent, spawn’ or set up a ‘separate entrepreneurial venture’ or exit.⁵

While this ‘life cycle’ approach can be criticized for determinism, the long lifespan of some co-operatives indicates that co-operative demise is not inevitable. Co-operative members and managers have choice and can adapt their organizations and objectives without compromising

³ Barton (1989), 12; Hansmann (1980), 845; Hansmann (1996), 125, 137; Lewis (2006), xviii.

⁴ Cheong (2006), 226; Cook (1995); Hansmann (1980), 845; Hansmann (1996), 125, 137; Helmberger (1996); Hind (1999).

⁵ Cook and Bures (2009).

the essential democratic nature of co-operative enterprises, even shifting forms as is the case of transformational co-operatives, where the form of the co-operative shifts over time to match changes in local conditions, such as where dairying co-operatives become retail co-operatives as local milk production declines.⁶ Even where dairy co-operatives have demutualised, such as with Murray Goulburn in Victoria, former dairy farmer members continued to value the co-operative business model, with the formation of the Mountain Milk Co-operative in 2017. One example of a NSW dairy co-operatives that has survived the fluctuations of the business cycle in NSW is NORCO, founded in 1893.⁷

The agricultural co-operative literature also generally overlooks the idea that co-operatives are not just businesses, they are also a movement with regional, national and international organizations such as the ICA, which promotes the co-operative movement worldwide and provides a forum for international co-operative collaboration. There is an ideology and culture built around collective self-help, economic democracy and community obligation enshrined in co-operative principles. There are important cultural artefacts associated with the co-operative movement such as International Co-operative Day, co-operative halls of fame and museums. Co-operatives may also be concentrated in geographical clusters, such as the Emilia Romagna region of Italy or the Basque region of Spain, which reinforce co-operative culture through economic transactions and collaboration as part of a local or regional network. Co-operative values and culture provide a source of resistance to demutualization, which relies on appealing to members' personal financial interests. While some dairy co-operatives have demutualised, some dairy co-operatives with a strong co-operative culture have successfully resisted demutualisation.⁸

Dairy Co-operatives in NSW

Dairy co-operatives began in NSW during the 1880s. There was awareness of the Rochdale co-operative model among dairy farmers and rural press coverage of the success of dairying co-

⁶ Cook and Burrell (2009), 14-15; Patmore (2020), 19; Patmore and Balnave (2018), 12.

⁷ NORCO, 29 June 1893, 03 July 1893. A003 V475, Minutes 1892-4, University of New England Archives, Armidale, Australia,

⁸ Birchall (2011), 174; Gurney (1996), 61-87; Hilson (2017), 47-48.

operatives in Denmark.⁹ The Illawarra district on the NSW south coast, with its closely knit dairy communities provided the initial interest in co-operation, with farmers increasingly dissatisfied with the network of agents and merchants selling their products in Sydney and looking at the possibilities of co-operation with better transport links and refrigeration. The cream separator was introduced into NSW from Denmark in 1881, encouraging farmers to come together to build factories, with Illawarra farmers sending a representative to study co-operative production in Denmark in 1884. The first co-operative for the distribution of farm and dairy products was the South Coast and West Camden Co-operative Company at Kiama in 1880 and the first known co-operative butter factory was at Kiama in 1884. Co-operative dairies spread to Northern NSW, through the immigration of Illawarra dairy farmers and local initiatives. A successful attempt to rationalize the various co-operative creameries occurred in the Richmond River Region of NSW, when the North Coast Fresh Food and Cold Storage Limited (later NORCO) opened a central creamery at Byron Bay in 1893.¹⁰

There is aggregate data available that highlights the trends over time for dairying in NSW. The Visual Atlas of Australian Co-operative History, a joint project of Macquarie University, the University of Sydney and University of Technology Sydney,¹¹ which currently has data for 4,324 co-operatives in Australia and 1,639 in NSW co-operatives from the late 1820s to the present. As more co-operatives are added to the Atlas the quality of data improves. The Atlas classifies dairy co-operatives as agricultural production co-operatives. While this category primarily consists of dairying co-operatives, it also includes co-operatives that process for example rice, poultry and meat. The NSW data indicates that agricultural production co-operatives are sustainable business organisations with an average life span of 44.74 years for the 204 agricultural production co-operatives in the current sample. As Figure 1 below indicates since 1868 there have been peaks of interest in agricultural production co-operatives in NSW in 1922-23 and 1950.

⁹ *The Richmond River Herald and Northern Districts Advertiser* (Coraki, NSW, Australia), 12 April 1889, p. 3.

¹⁰ Patmore and Balnave (2018), 101-102.

¹¹ The chief investigators for project, which is funded by Australian Research Council DP170100573, are Associate Professor Nikola Balnave, Professor Greg Patmore and Professor Olivera Marjanovic

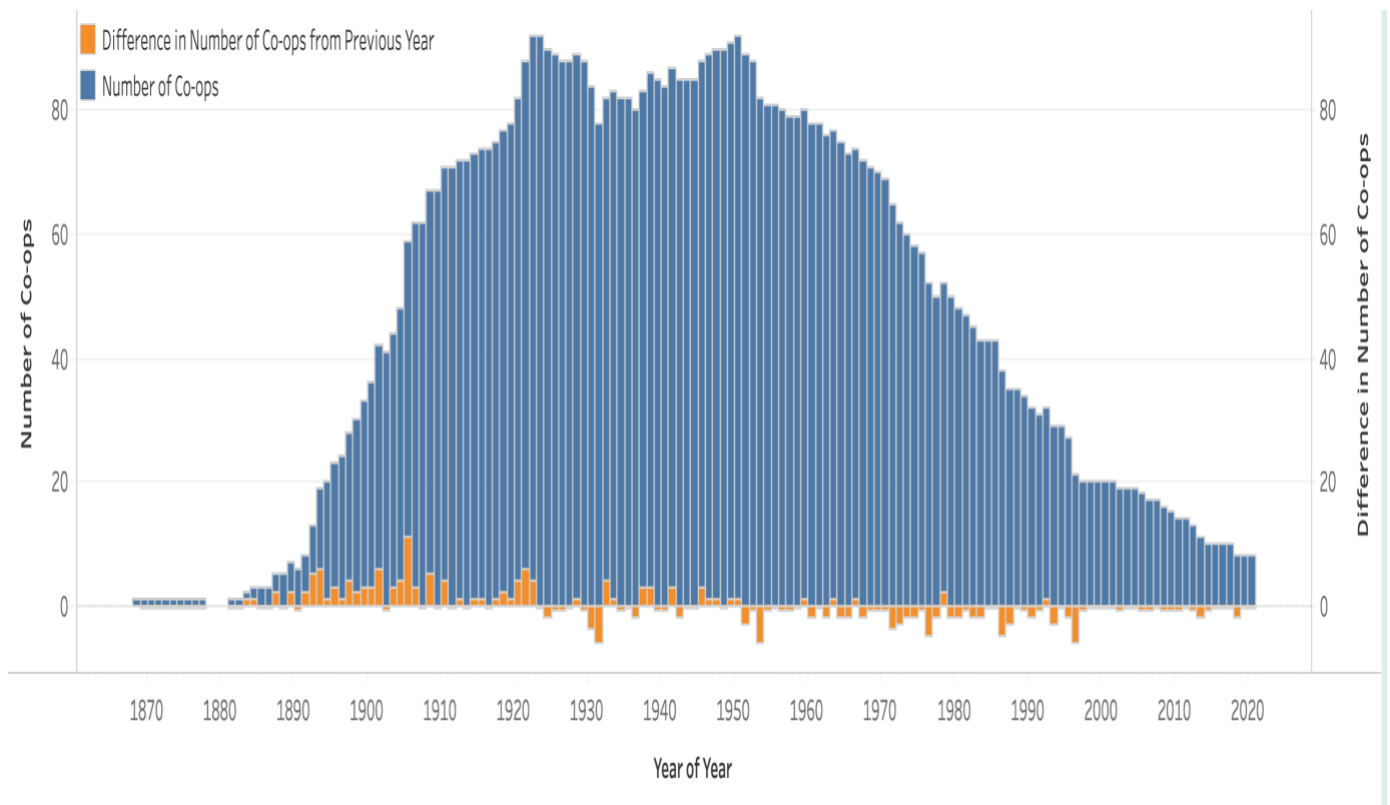


Figure 1 – Agricultural Production Co-operatives in NSW 1868-2020

Source – Visual Historical Atlas of Australian Co-operatives (Version 20 – September 2020)

While there has been a decline in agricultural production co-operatives such as dairy co-operatives since 1950, dairy co-operatives amalgamated as dairy farmers faced declining milk yields in particular areas or the need for economies of scale to reduce costs in the face of increased competition and deregulation of the dairying industry. Dairy Farmers Co-operative merged with dairying co-operatives at Dungog and Taree during the 1980s before merging with the Shoalhaven and Hunter Valley dairy co-operatives to form Australian Co-operative Foods in 1990.¹² There are examples of ‘transformational co-operatives’ in the NSW dairy industry with a recent example being the Hastings Co-operative, which sold its dairy factory in 2011 and now focuses on retailing.

¹² Todd (1994), 219, 230; Todd (2001), 36.

There were dairy co-operative demutualisations. Australian Co-operative Foods undertook a partial demutualisation in 2006 with Dairy Farmers Milk Co-operative Ltd. continuing as a co-operative directly supplying milk. The Bega Co-operative Society deregistered in June 2009 after voting to change its capital structure into an unlisted public company and subsequently becoming publicly listed on the ASX in August 2011. While Bega Cheese placed a cap on the number of shares a shareholder could own to protect it against a corporate takeover, the proportion of shares held by local dairy farmers has declined and corporate shareholders such as NZ Dairy Giant Fonterra have purchased shares. A vote to remove the cap was narrowly defeated at the 2015 AGM reflecting growing tensions between farmer members and corporate shareholders and highlighting a risk that demutualisation may lead to the loss of local control and Australian ownership.¹³

One successful example of dairy co-operative is NORCO. It has strong commitment to the co-operative business model and is part of a co-operative geographical cluster in the Richmond River Valley, which the Visual Atlas highlights is a major region for co-operative activity in Australia both in the past and present. NORCO's dairy processing activities include milk and ice cream, but it also operates a chain of 30 rural supply stores that strengthen the retail profiles of communities ranging from Dungog in NSW to Bundaberg in Queensland. The co-operative's success is highlighted by its economic performance in 2019-2020 despite drought, bushfires and the COVID-19 pandemic. It paid a record price of 70.63 cents per litre to its 302 members and recorded a profit of \$5.4 million, an increase of \$4.2 million from the previous year. NORCO's revenues are retained by the co-operative's members and their communities.¹⁴

Conclusion

Co-operatives are an essential element for ensuring the long-term sustainability of the NSW dairy industry. The co-operative business model allows dairy farmers a direct voice in the supply and

¹³ Lewis (2006), 352-3; <https://www.abc.net.au/news/rural/2015-10-29/close-run-bega-cheese-agm-voting-pits-farmers-against-corporate/6896568> accessed 19.10.2020

¹⁴ Thompson (2020)

processing of their product. They allow dairy farmers to pool risk and reduce governance costs by cutting out agents for processing and marketing. The Visual Atlas project finds that agriculture production co-operatives such as dairying co-operatives are sustainable with an average life span in NSW of 44.74 years. While there have been claims that large agricultural co-operatives eventually either fail or demutualise, co-operative managers and members make strategic choices about their business and there are long established dairy co-operatives that continue to survive and thrive such as NORCO. Demutualisation also increases the risk that ownership may pass from local communities to ultimately overseas ownership. Any changes to government policy in regard to the dairy industry should recognise the valuable role played by co-operatives and ensure that are given equal treatment to other business models such as IOBs.

Yours Sincerely,

Greg Patmore,

Emeritus Professor of Business and Labour History,

University of Sydney Business School

References

Barton, David. 1989. "What is a Co-operative?" In *Co-operatives in Agriculture* edited by David Cobia. Englewood Cliffs (USA), Prentice Hall.

Birchall, Johnston. 1997. *The international co-operative movement*. Manchester: University of Manchester Press.

Birchall, Johnston. 2011. *People-Centered Businesses. Co-operatives, Mutuals and the Idea of Membership*. Houndsmills (UK): Palgrave Macmillan.

- Cheong, Elizabeth. 2006. "The Agricultural Co-operative Business Structure in Context: A Western Australian Study." Available at <http://ro.ecu.edu.au/theses/56>
- Cook, Michael, 1995. "The Future of US Agricultural Co-operatives: A Neo-Institutional Approach." *American Journal of Agricultural Economics*, 77 (5): 1153-1159.
- Cook, Michael and Molly Burress. 2009. "A Co-operative Life Cycle Framework." Available at <http://departments.agri.huji.ac.il/economics/en/events/p-cook.pdf>.
- Gurney, Peter. 1996. *Co-operative Culture and the Politics of Consumption in England, 1870-1930*. Manchester: Manchester University Press.
- Hansmann, Henry. 1980. "The Role of the Non-Profit Enterprise." *The Yale Law Journal*, 89 (5): 835-901.
- Hansmann, Henry. 1996. *The Ownership of the Enterprise*. Cambridge (MA), Harvard University Press.
- Helmberger, Peter. 1966. "Future Roles for Agricultural Co-operatives." *Journal of Farm Economics*, 48 (5): 1427-1435.
- Hilson, Mary. 2017. "Co-operative History: Movements and Businesses." In *A Global History of Consumer Co-operation since 1850: Movements and Businesses*, edited by Mary Hilson, Silke Neunsinger and Greg Patmore. Leiden: Brill.
- Hind, Abigail. 1999. "Co-operative Life Cycles and Goals." *Journal of Agricultural Economics*, 50 (3): 536-548.
- Lewis, Gary. 2006. *The Democracy Principle. Farmer Co-operatives in Twentieth Century Australia*. Wambion (Australia): author
- MacPherson, Ian. 1979. *Each for All: A History of the Co-operative Movement in English Canada, 1900-1945*. Toronto, Macmillan.
- Patmore, Greg. 2020. *Innovative Consumer Co-operatives: The Rise and Fall of Berkeley*. New York: Routledge.

Patmore, Greg and Nikola Balnave. 2018. *A Global History of Co-operative Business*. New York: Routledge.

Thompson, Brad. 2020. "Dairy co-op delivers record price to farmers and big jump in profit."

Available at <https://todayspaper.smedia.com.au/afr/default.aspx>

Todd, Jan. 1994. *Milk for the Metropolis. A Century of Co-operative Milk Supply in New South Wales*. Sydney: Hale & Iremonger.

Todd, Jan. 2001. *More than Milk. Dairy Farmers and the Co-operative Response to Industry Deregulation*. Sydney: Hale and Iremonger.