



Economics and Industry Standing Committee

THE SUSTAINABILITY OF THE DAIRY INDUSTRY IN WESTERN AUSTRALIA

Report No. 8

In the Thirty-Sixth Parliament

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THE SUSTAINABILITY OF THE DAIRY INDUSTRY IN WESTERN AUSTRALIA

Report No. 8

In the Thirty-Sixth Parliament

Presented by:

Mr A.D. McRae, MLA

Laid on the Table of the Legislative Assembly
on Thursday 4 December 2003.

COMMITTEE MEMBERS

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COMMITTEE STAFF

Principal Research Officer	Dr Ray Wills, BSc (Hons), PhD
Senior Research Officer	Dr David Windsor, BRurSc (Hons), PhD (seconded from Department of Agriculture)
Research Officer	Ms Jovita Hogan, BA (Hons) Ms Liz Kerr, BA (until July 2003)

COMMITTEE ADDRESS

Economics and Industry Standing Committee
Legislative Assembly
Parliament House
Harvest Terrace
PERTH WA 6000

Tel: (08) 9222 7494
Fax: (08) 9222 7804
Email: laeisc@parliament.wa.gov.au
Website: www.parliament.wa.gov.au

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COMMITTEE'S FUNCTIONS AND POWERS

The functions of the Committee are to review and report to the Assembly on: -

- (a) the outcomes and administration of the departments within the Committee's portfolio responsibilities;
- (b) annual reports of government departments laid on the Table of the House;
- (c) the adequacy of legislation and regulations within its jurisdiction; and
- (d) any matters referred to it by the assembly including a bill, motion, petition, vote or expenditure, other financial matter, report or paper.

At the commencement of each Parliament and as often thereafter as the Speaker considers necessary, the Speaker will determine and table a schedule showing the portfolio responsibilities for each committee. Annual reports of government departments and authorities tabled in the Assembly will stand referred to the relevant committee for any inquiry the committee may make.

Whenever a committee receives or determines for itself fresh or amended terms of reference, the committee will forward them to each standing and select committee of the Assembly and Joint Committee of the Assembly and Council. The Speaker will announce them to the Assembly at the next opportunity and arrange for them to be placed on the notice boards of the Assembly.

INQUIRY TERMS OF REFERENCE

Inquiry into the sustainability of the dairy industry in Western Australia

The Committee to inquire into the sustainability of the dairy industry in Western Australia and investigate -

1. the financial impact of deregulation on Western Australian farmers, processors, wholesalers and retailers;
2. the impact of deregulation on the supply of milk and price to consumers;
3. reforms that will enhance the sustainability of the industry including any appropriate market intervention strategies, additional industry assistance and potential for market developments;
4. the issue of equitable participation by all industry stakeholders; and
5. any other matters considered relevant by the Committee.

In accordance with Standing Order 249 (4), the member for Warren-Blackwood, (Hon Paul Omodei, MLA) and the member for Bunbury, (Mr Tony Dean, MLA) have been co-opted to participate in the Economics and Industry Standing Committee's inquiry.

CHAIRPERSON'S FOREWORD

I am pleased to present for tabling the eighth report of the Economics and Industry Standing Committee. The report is the Committee's second and final report on its inquiry into the sustainability of the dairy industry in Western Australia.

The Committee believes that the dairy industry is absolutely essential to the social and economic fabric of many districts in southwest Western Australia. The Committee notes with some pride that Western Australia's dairy farmers deliver one of the finest dairy products in the world. It is internationally regarded. We understand the quality of the product.

Before deregulation, it is fair to say that the Western Australian dairy industry had a higher level of protection than any other state in Australia. This inquiry was focused on the effects and the opportunities that are available from deregulation if the industry is to be sustainable.

This report is about taking steps that improve market opportunity and as a result enable fair pricing of produce.

There is a need for further efficiencies to be gained by this industry, and the government must be a partner delivering further support for these on-going reforms. The deregulation of an industry that had been protected for more than 30 years was implemented without sufficient consideration of the dramatic changes that would result.

The Committee's August 2003 report set out that this inquiry was looking forward to a future, sustainable industry, not backwards to a regulated and sometimes inefficient past.

Our objective was to ensure the Parliament put proposals to government to assist, and promote the industry. Western Australia must guard against losing the critical mass of this industry, not only economically, but also the historical and social structures that exist in the many communities that rely to a significant extent on the dairy industry.

Since the Assembly referred the inquiry to the Committee at the end of June 2003, the Committee has held 22 deliberative meetings, received 74 submissions, and held 41 hearings or briefings with 87 people. This includes visiting four farms in southwest Western Australia, meeting with 11 dairy farmers, the four major dairy processors and the three major grocery retail groups in Western Australia.

While many people have contributed, some people deserve a special mention. Peter Radford assisted the Committee on our visit to Bega. Peter Wilson from Dairy Australia and Steven Adams from Peters and Brownes Group have provided a steady stream of relevant data to the Committee, and this has assisted the timely delivery of this report.

This inquiry was conducted with two co-opted members, the member for Warren-Blackwood, (Hon Paul Omodei, MLA) and the member for Bunbury, (Mr Tony Dean,

MLA). Both of these members had particular knowledge of the dairy industry and have made a significant contribution to the conduct of the inquiry.

With the participation of the five regular members of this Committee and the two co-opted members representing both sides of this house, the deliberations of the Committee confirms the importance of the Parliament being able to inquire into important topical issues, to scrutinise executive government, and to deliver well-researched, reasoned findings together with practical recommendations for Government action.

It is a level of co-operation we hope becomes the norm among dairy farmers and in the dairy industry as a whole.

In addition, the work of the Committee was greatly assisted by the participation of Dr David Windsor an officer seconded to the Committee staff from the Department of Agriculture. This secondment was made possible by the agreement of the Minister for Agriculture, Forestry and Fisheries, the Hon. Kim Chance. Dr Windsor's contribution has been invaluable in allowing the Committee to report in less than six months from the time the matter was referred to the Committee by the Legislative Assembly.

The regular Committee staff has also made a substantial contribution and I acknowledge the work of Dr Ray Wills, the Principal Research Officer, Ms Jovita Hogan, Research Officer and, in the early part of this inquiry, Ms Liz Kerr. Collectively I thank all four staff for their enthusiasm and professionalism, their hard work during the conduct of this inquiry, and their dedication in the purchase of Western Australian dairy products.

While this inquiry has concluded, the Economics and Industry Standing Committee will continue its work of monitoring developments in the dairy industry. The challenge of developing and sustaining a vibrant dairy industry in Western Australia relies now on the cooperation of all stakeholders. Dairy farmers, processors, retailers, government and consumers all have a role to play in putting the industry on a sustainable footing. As with many challenges in our community, meeting these challenges with a united purpose and vision will determine our level of achievement.

The reforms proposed by my Committee do not rely on statutory enforcement of market participation, but set out the changes to behaviour and organisation necessary for our long-term success.

I commend the report to the Parliament, industry and the community.

MR A.D. McRAE, MLA
CHAIRPERSON

ABBREVIATIONS AND ACRONYMS

ABARE	Australian Bureau of Agricultural and Resource Economics
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ADC	Australian Dairy Corporation
AFFA	Department of Agriculture, Fisheries and Forestry - Australia
DAA	Dairy Adjustment Authority
DIAL	Dairy Industry Adjustment Levy
DRU	Delivery Right Unit (Challenge Dairy Co-operative)
DSAP	dairy structural adjustment payments
ESL	Extended Shelf Life milk
EU	European Union
GST	Goods and Services Tax
n.a.	Data not available
NCC	National Competition Council
NCP	National Competition Policy
UHT Milk	Milk subjected to Ultra High Temperature treatment to extend shelf life
WAFF	Western Australian Farmers' Federation

GLOSSARY

Common-user infrastructure	Assets used collaboratively by more than one business.
Deregulation	The removal of both state and federal legislation specific to the dairy industry in July 2000. For the states this meant the discontinuation of regulated sourcing and pricing of milk. Federally, support of manufactured milk prices through the Domestic Market Support scheme ceased.
Farmgate price	Price paid to dairy farmers for raw milk.
Fresh Milk	Milk processed for consumption.
Generic milk	Unbranded milk which is sold under the private labels of the retailers.
Manufacturing milk	Raw milk used as an input to non-fluid dairy products.
Market (domestic) milk	Raw milk used as an input to fluid dairy products.
Milk processors	Businesses engaged in production of dairy products.
Pasteurised milk	Milk that has been heated to enhance microbiological properties in accordance with prescribed health regulations.
Productivity	The ratio of converting business inputs into business outputs.
Route trade	Taken to mean the non-supermarket retail milk market.
Specialty milk	Milk that is marketed using an attribute other than fat reduction, flavouring or ultra heat treatment.
UHT milk	Milk subjected to Ultra High Temperature treatment to extend shelf life.
Yield	The average annual volume of milk produced per cow.

EXECUTIVE SUMMARY

The current crisis of confidence in the dairy industry reflects genuine financial difficulties faced by many farm businesses during the last two years.

Factors contributing to the decline in confidence in the dairy industry have included:

1. Continuing erosion of the price premium for market milk;
2. Lack of farmer market power and the perceived failure of the Collective Bargaining process to deliver equitable outcomes through a transparent process;
3. Ongoing adjustment issues caused by the need to rapidly adopt to an open market after decades of market milk regulation. Many businesses remain unable to compete in an unregulated marketplace;
4. Low international dairy commodity prices combined with the strengthening Australian dollar have reduced the value of Australian dairy exports by 30% since September 2001. This has rendered Challenge Co-operative unable to deliver benefits that were timely or large enough to match expectations created within industry; and
5. Drought has increased grain prices leading to a substantial increase in costs of production during the 2002/2003 financial year.

None of these issues are unique to Western Australia. Difficult economic conditions and low morale can be found in the dairy industry of every Australian state.

Deregulation of the dairy industry in July 2001 created a whole new set of rules in the domestic milk supply chain. Dairy farmers and processors suddenly found themselves in a position of weak market power compared with the giant national retail chains. The rapid market growth of generic milk made processors realise that the supermarkets were no longer merely their most important wholesale customer, but also their fiercest retail competitor. The introduction of nationwide milk tendering by Woolworths and the sale of generic milk for less than \$1 per litre created a collapse in supermarket milk prices during the final months of 2000 as competing stores and brands scrambled to maintain market share.

Falling retail prices have reduced the value of the 160 million litres of domestic milk previously supplied under quota by about 15 ¢/L. This represents a loss of income to the Western Australian dairy industry of \$24 million per year.

These losses have been partly offset by more than \$150 million in adjustment assistance provided by the State and Federal Governments. This contrasts with the estimated \$190 million loss in farm incomes projected for the eight year life of the Dairy Structural Adjustment Program (DSAP). Average DSAP payments to Western

Australian dairy farmers are the highest of any state, reflecting the high proportion of milk formerly sold through the regulated market. Western Australia was the only state government to provide complementary assistance to DSAP.

DSAP payments have created a tax burden for dairy farmers and reduced eligibility for social security payments. Governments need to structure future industry assistance schemes to avoid such unintended consequences.

More than 25% of Western Australian dairy farmers have left the industry since deregulation. Milk production has declined by about 5% and exports of Western Australian dairy products have continued to increase.

Consumers and retailers have gained short-term benefits from deregulation, but continued downward pressure on milk prices will see more dairy farmers leave the industry. Western Australia cannot afford to lose efficient but disillusioned farmers from its small production base. Declining farmer numbers have already placed financial strain on support industries that service the dairy industry.

There is still a wide range in the costs of milk production between Western Australian dairy farms. International benchmarking shows that the best Western Australian dairy farmers are among the most efficient in the world. However some businesses have not yet made the changes required for profitability in a highly competitive marketplace. Many farm businesses are struggling financially while others remain profitable.

Some farm businesses did not assess their future viability accurately at the time of deregulation. There is a need for businesses to ensure that they are structured appropriately for long term sustainability or to consider leaving the industry. There is a range of government counselling and financial assistance services available to assist that process. However, it would be valuable to establish a rural counselling service in southwest Western Australia.

Competitive participation in the domestic and international markets is the key to the sustainability of the Western Australian dairy industry. Dairy farmers must provide a competitively priced product to Western Australian processors for domestic consumption and export. Continuous improvement in farm practices and economic efficiency will be required to continue to match Western Australia's competitors.

The Senate Rural and Regional Affairs and Transport References Committee warned of the need to avoid "a commercially driven crash" in the dairy industry in its 1999 inquiry into deregulation. That crash was precipitated in September 2000 by the introduction of a national tender process for the supply of generic supermarket milk. That process unleashed fierce competition between processors for supermarket that was not matched by competition from processors for dairy farmers' milk. The supermarket tender process has expanded and continued since 2000 with scant regard for the sustainability of other participants in the supply chain.

Much of the retail margin on milk that was lost by supermarkets in the months following deregulation has been regained through increases in retail price. The benefits of increasing consumer prices have been shared by retailers and dairy processors to the exclusion of dairy farmers. At the same time, much of the market risk in the dairy supply chain has been transferred to the dairy farmer.

The Federal Government has a clear responsibility to ensure that the Australian Competition and Consumer Commission (ACCC) acts decisively and effectively to prevent abuses of market power by dominant players in the inevitable period of adjustment and uncertainty that follows deregulation of a protected industry. The ACCC must examine if market power is being used to increase retailer margins while farm gate prices are declining. The Federal Government should be concerned that the *Trade Practices Act 1974* has failed to protect vulnerable dairy farmers during a difficult period of adjustment.

Aggressive discounting of branded milk in supermarkets to below the price of generic milks has been a unique feature of the Western Australian retail sector during the past 18 months. Two litres of Pura milk sells for 20% more in Victorian than in Western Australian supermarkets. This has restricted the growth in market share of generic milks in Western Australia but has almost eliminated brand premiums. Many dairy products manufactured in the eastern states also sell at considerable discounts. Some products regularly sell for 20% less in Western Australia than in their state of manufacture.

Effective collective action will be essential for dairy farmers to improve their long-term position in the supply chain. The two options available under the existing *Trade Practices Act 1974* are collective negotiation with processors and the formation of co-operatives.

Collective Bargaining under the current ACCC authorisation has not been successful in improving returns to dairy farmers. There is an urgent need for governments to work with the ACCC and industry to develop collective bargaining arrangements that are more effective in overcoming the weak market power of dairy farmers.

The domestic milk market alone is unlikely to underpin sustainable growth by industry or individual businesses. A sustainable industry will need to be a competitive player in the international marketplace. Long term profitability in the export market is more likely to come from the development of high value products and appropriate business relationships in premium markets rather than increased participation in commodity markets distorted by European Union (EU) trade policy and dominated by the giant New Zealand and Victorian Co-operatives.

Regulation of the domestic milk industry is not a viable option to address imbalances in market power. National Competition Policy leaves little room for increased direct intervention by state governments in milk marketing. Nor would regulation serve the industry's need for increased international competitiveness if it is to continue to develop on a sustainable basis. The Western Australian Government's key role must

be to assist industry to increase its participation and competitiveness in high value markets. A stakeholder council must be convened to identify and implement priority programs for government action.

Western Australia failed to capture higher milk prices from the commodity upswing of 2000/2001. The absence of a mature farmer co-operative has been a major factor in the relatively low prices paid to Western Australian dairy farmers since deregulation. Strong export performance by a farmer-owned processing and marketing business is considered essential to create strong competition for milk supply, to stimulate price and industry growth, and through these, increase the sustainability of all participants in the industry and provide a mechanism to increase the market power of dairy farmers.

The Western Australian Government must act to make a loan facility under Section 120 (i)(c) of the *Income Tax Assessment Act 1936* available in Western Australia to assist the future development of co-operatives.

In summary, three things need to happen for the development of a sustainable dairy industry in Western Australia:

- The first is for dairy farmers to ensure that their businesses are structured to be competitive in the international and domestic marketplaces and that they have the capacity to respond to increasing competition.
- The second is for retailers to recognise that there are added costs associated with supplying fresh milk 365 days of the year and ensure that dairy farmers are adequately paid for the higher costs on a year-round basis.
- The third is for Western Australian milk processors to continue the shift away from commodity production into high value export markets. Strong performance by a farmer owned processor would be required to ensure that Western Australian dairy farmers share premiums from those markets.

FINDINGS

Page 6

Finding 1

The dairy industry across Australia faced difficult times in the 2002/2003 season due to a combination of drought, falling international commodity prices, a strengthening Australian dollar, and compounded by decreases in retail, processing and farm gate prices following deregulation in July 2000.

Page 6

Finding 2

Farmer-owned co-operative dairy companies play a major role in dairy processing in Australia. The strength of the co-operative sector is a major source of market power for many dairy farmers.

Page 11

Finding 3

Dairy is one of the highest value-adding rural industries in Western Australia.

Page 27

Finding 4

The total reduction in milk income to dairy farmers in Western Australia resulting from deregulation of the domestic milk market is estimated to be \$24 million per annum.

Page 30

Finding 5

Production costs on Western Australian dairy farms vary widely reflecting differences in climate, on-farm infrastructure, and individual farm efficiency.

Page 30

Finding 6

There are opportunities for many dairy farms to improve business performance by reducing feed and labour costs and through other strategies such as co-operative purchase of inputs.

Page 31

Finding 7

Some Western Australian dairy farm businesses are among the most efficient in the world while others are not economically sustainable in the current dairy market.

Page 32

Finding 8

The combined Federal and Western Australian Government restructure assistance totals \$150 million over 8 years compared with a reduction in income estimated at \$190 million over the same period.

Page 34

Finding 9

Average DSAP payments to Western Australian farmers are the highest per capita of any state. The only State Government to provide additional restructure assistance to complement the DSAP is Western Australia.

Page 34

Finding 10

State and Federal restructure assistance payments have created unintended barriers for farmers accessing social security payments.

Page 36

Finding 11

Current Western Australian retail prices have reduced margins for dairy farmers and processors, and will force more participants from the industry if higher returns are not achieved within the next year.

Page 37

Finding 12

More than 25% of Western Australian dairy farmers have left the industry since deregulation of the domestic market in July 2000.

Page 38

Finding 13

Milk production in Western Australia has dropped by about 5% since 1999/2000, with most of the reduction occurring in the first year following deregulation.

Page 39

Finding 14

Western Australian interstate and international dairy exports have continued to grow since deregulation.

Page 40

Finding 15

Milk supplies have been maintained and consumers have gained short-term benefits from reduced retail milk prices in Western Australia.

Page 41

Finding 16

Regular supermarket discounting has kept average prices for branded milks lower in Western Australia than the rest of Australia. This has reduced returns to farmers and processors from branded milk, but has reduced the market share of cheaper generic milk.

Page 41

Finding 17

The national tendering process for generic milk initiated by Woolworths has precipitated the “commercially driven crash” in milk prices and farm incomes that the Senate Rural and Regional Affairs and Transport References Committee warned against in 1999.

Page 41

Finding 18

Some dairy products manufactured in eastern Australia sell for lower prices in Western Australian supermarkets than in the same supermarket chain in their home state.

Page 48

Finding 19

The retail sector in Western Australia is unique and appears to be the most aggressively competitive in Australia. This has been a significant cause in Western Australian dairy farmers receiving Australia's lowest farm gate milk price.

Page 52

Finding 20

Increasing efficiencies are the key to the sustainability of the Western Australian dairy industry in both domestic and export markets.

Page 53

Finding 21

Co-operative purchasing, infrastructure development and production practices by Western Australian dairy farmers will increase farm efficiencies.

Page 55

Finding 22

In the absence of net public benefit being demonstrated, reintroduction of market milk regulation would breach Western Australia's obligations under National Competition Policy. It would also be inconsistent with the State-Commonwealth agreement establishing the basis for the \$1.94 billion Dairy Structural Adjustment Program.

Page 56

Finding 23

A united dairy industry could implement a single marketing desk now without statutory backing.

Page 57

Finding 24

State governments do not have the constitutional power to impose a tax or levy on retail milk sales as a farm income supplement.

Page 57

Finding 25

Government does not have the constitutional power to restrict trade in interstate dairy products.

Page 58

Finding 26

Demonstrating a net public benefit from the introduction of a minimum wholesale or retail price would be necessary to comply with Western Australia's obligations under National Competition Policy.

Page 58

Finding 27

The Australian domestic milk market is unlikely to grow on a per capita basis, although there appears to be opportunities for growth in domestic consumption through value-added dairy products.

Page 59

Finding 28

Low morale, a lack of unity among dairy farmers and an absence of a common vision across the industry as a whole, are fundamental challenges to the sustainability of the Western Australian dairy industry.

Page 59

Finding 29

Consistent satisfactory returns from the export dairy market are difficult to achieve from the sale of traditional dairy commodities such as butter, cheddar cheese and skim milk powder because of price distortions caused by subsidies in the EU and trade barriers in the USA.

Page 60

Finding 30

Sustaining and developing the Western Australian dairy industry will depend on the industry's capacity for export and product diversification. This will succeed if growth is focussed on high value products rather than commodity exports.

Page 61

Finding 31

Western Australian milk is recognised for its exceptional quality and is preferred in Asian markets because of its superior flavour. There is real potential to capitalise on the whiteness of WA milk.

Page 61

Finding 32

Competing in selected export markets with high value-added products will require increased investments in new product development. Western Australian producers will need to continue development of supply relationships to have sufficient market presence and power.

Page 62

Finding 33

The Federal Government has a clear responsibility to ensure that the ACCC acts effectively to prevent abuses of market power by dominant players in the period of adjustment following deregulation. The Federal Government has not adequately fulfilled this responsibility in the case of the dairy industry.

Page 62

Finding 34

The Federal Government could use some of the estimated \$400 million tax windfall generated from the DSAP package to provide additional assistance to communities adversely affected by deregulation.

Page 63

Finding 35

The most effective contribution Government can make to a sustainable dairy industry in a competitive market will be through its scientific and trade resources to increase the participation and competitiveness of Western Australian dairy exporters.

Page 65

Finding 36

Much of the market risk in the dairy supply chain has been transferred from retailers and processors to dairy farmers.

Page 67

Finding 37

The national tendering process for generic milk contracts initiated by Woolworths in 2000 continues to reduce the profitability of milk processors and dairy farmers throughout Australia.

Page 67

Finding 38

Much of the retail margin on milk that was lost by supermarkets in the months following deregulation has been regained through increases in retail price. The benefits of increasing retail prices have been shared by retailers and processors, but not by dairy farmers.

Page 67

Finding 39

It is the ACCC's responsibility to monitor the use of market power by retailers in pursuit of market share and margin. The *Trade Practices Act 1974* has failed to protect dairy farmers during the adjustment following deregulation.

Page 70

Finding 40

The Western Australian industry must retain a critical mass of efficient dairy farmers so that its small production base is not further diminished.

Page 70

Finding 41

Supermarkets have a powerful position in setting prices along the supply chain and need to temper current “loss-leader” discounting behaviour to move to long-term sustainable prices. The Federal and Western Australian Governments and the ACCC also need to develop supply chain price monitoring mechanisms that promote the long-term viability of the retail, processor and farm sectors.

Page 72

Finding 42

The ACCC has denied dairy farmers the right to withhold supply reducing the negotiating power of dairy farmers.

Page 72

Finding 43

Increased collective bargaining by dairy farmers is a key to the negotiation of higher farm gate prices.

Page 73

Finding 44

There is a widespread farmer perception that National Foods have not conducted collective negotiations in good faith. The abrupt termination of negotiations by National Foods and the short notice given for contract reductions has raised legitimate concerns about the transparency and fairness of the bargaining process.

Page 73

Finding 45

There is an urgent need for the ACCC to investigate and enable measures to increase the effectiveness of the collective bargaining process. In the absence of effective action by the ACCC, it will be desirable to develop institutional mechanisms to strengthen farmer power in collective negotiations.

Page 74

Finding 46

The Western Australian dairy industry has failed to capture benefits of peaks in international commodity prices. There is a risk that such failure will continue if structural problems throughout the dairy industry chain are not addressed.

Page 74

Finding 47

The absence of farmer co-operative structures historically has been a major factor in the relatively low prices paid to Western Australian farmers since deregulation.

Page 75

Finding 48

Strong export performance by farmer-owned processing and marketing businesses is considered essential to create strong competition for milk supply, to stimulate price and industry growth.

Page 77

Finding 49

Deregulation of the dairy industry in 2000 was supported by 58% of dairy farmers in Western Australia.

Page 78

Finding 50

DSAP payments have not always been used effectively to reduce farm debt, upgrade on-farm assets, or exit the dairy industry.

Page 78

Finding 51

Some dairy farmers did not properly assess their business viability in the lead up to industry deregulation.

Page 78

Finding 52

The most efficient dairy farmers continue to operate profitable dairy businesses in 2003.

Page 79

Finding 53

Service industries to the dairy sector have been adversely affected by decreased farm expenditure in 2003.

Page 80

Finding 54

Further reductions in the number of dairy farmers will impact adversely on the viability of local service industries to the dairy sector, other secondary businesses, and district economies generally.

Page 81

Finding 55

Some farm businesses are now in a position where they need to reassess their viability.

Page 82

Finding 56

There is a range of government services for dairy farmers to access for financial and personal counselling.

RECOMMENDATIONS

Page 34

Recommendation 1

Federal and State Governments need to frame future industry restructuring and assistance packages so that participants are not penalised through their taxation and social security entitlements.

Page 42

Recommendation 2

The Government requests the ACCC to determine whether the practice of selling dairy products in Western Australia at a substantial discount to the price in their state of manufacture constitutes dumping or anti-competitive behaviour.

Page 49

Recommendation 3

The Government ensures that dairy products eligible for promotion through the State's "Buy WA" campaign must use milk components derived exclusively from Western Australia, unless those components are not produced in the State.

Page 49

Recommendation 4

The Government ensures that food labelling requirements more adequately define the use of the word 'fresh' so that a product cannot be labelled as 'fresh' if it is made from reconstituted products.

Page 52

Recommendation 5

Government intervention in the dairy supply chain must adhere to the following principles:

1. Intervention is made on the basis of measurable industry outcomes. These must advance the industry's strategic goals, and not support the retention of inefficient or outmoded business practices; and
2. Any intervention must not weaken the competitiveness of Western Australian processors in either interstate or overseas markets.

Page 53

Recommendation 6

The Government facilitate the farm and processing sectors to develop a more collaborative approach in order to increase their efficiency.

Page 54

Recommendation 7

The Government initiate a research and development partnership with industry to assist dairy farmers to reduce their costs and develop strategies for change relevant to different dairy regions and farm business circumstances.

Page 54

Recommendation 8

The Government convene a dairy stakeholders council to improve access to and use of processing infrastructure, and to assess options to increase flexibility of product mix in response to market opportunities.

Page 54

Recommendation 9

The Government directs Western Power Corporation to cost 3-phase power projects to dairy customers on the basis of district infrastructure investment that anticipates further local power system upgrades by neighbours.

Page 55

Recommendation 10

The Government invites Dairy Western Australia and other industry stakeholders to participate in a feasibility study into development of a dairy transport services company.

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Recommendation 11

The Government facilitates exploration of a single marketing desk as a basis for improving collective bargaining practices by dairy farmers.

Page 60

Recommendation 12

The Government support institutional arrangements to stimulate Western Australian dairy exports, especially high value-added products. These arrangements must include:

1. A study to clearly define Western Australia's sustainable competitive advantages and to develop a strategy and marketing plan to maintain and exploit those advantages;
2. Using the resources of the Government, including Western Australia's trade offices, to advance business relationships in Western Australia's existing and future dairy markets;
3. Facilitating industry development of an increased range of products for new and existing markets;
4. Conducting a feasibility study of broadening the scope of the Wine Industry Centre for Excellence to include dairy and other liquid foods; and
5. Increased collaboration between Western Australian exporters to improve their efficiency in servicing key markets.

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Recommendation 13

The State Government urge the Federal Government to use part of the tax windfall created by the DSAP to provide additional assistance to rural communities adversely affected by deregulation.

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Recommendation 14

The Western Australian Government request the Federal Government to direct the ACCC to:

1. Resume monitoring of margin distribution within the supply chain for liquid milk. This will provide some much needed transparency to milk price negotiations and bring legal and public pressure to prevent exploitation of farmers;
2. Determine whether the practice of negotiating milk tenders on a national basis is an unfair restriction of trade on those processors who only trade in one state; and
3. Provide advice on possible mechanisms for raising retail prices that increase margins through the industry chain to dairy farmers that will not be subject to prosecution under the *Trade Practices Act 1974*.

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Recommendation 15

The Government request the ACCC to find ways to improve transparency in supply chain transactions and equity of participation in supply chain negotiations for market milk.

Page 71

Recommendation 16

The State Government request the Federal Government make changes to the *Trade Practices Act 1974*, particularly to make unconscionable conduct provisions more readily actionable by the ACCC.

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Recommendation 17

The Government uses provisions under a Loan Bill to enable the establishment of a Section 120(i)(c) loan facility for Western Australian co-operatives.

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Recommendation 18

The Government conducts an analysis of the roles of co-operatives and collective bargaining groups in increasing dairy farmer market power. This analysis must include recommendations to the ACCC on measures to increase the role and effectiveness of collective negotiation of market price.

Page 82

Recommendation 19

The Western Australian Government requests the Federal Government to allow dairy farmers access to Farm Help Re-establishment Grants, regardless of their DSAP entitlement, provided that they meet the standard means test.

Page 83

Recommendation 20

The Western Australian Government requests the Federal Government to allow dairy farmers to take their remaining DSAP entitlements as a lump sum exit payment. These payments should be recognised as redundancy payments for taxation purposes.

Page 83

Recommendation 21

The Western Australian Government make immediate application for a rural financial counselling service under the Federal Government's Short-Term Industry Adjustment Projects Scheme within the Rural Financial Counselling Service Project. The State and Federal Governments establish a long-term rural financial counselling service in southwest Western Australia to support adjustment decisions in dairy and other rural industries.

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Recommendation 22

The Government ensures that any unspent funds from the State Dairy Assistance Package are used to assist the further development of the dairy industry and in particular support the cost of implementing the Committee's recommendations.

MINISTERIAL RESPONSE

In accordance with Standing Order 277(1) of the Standing Orders of the Legislative Assembly, the Economics and Industry Standing Committee directs that the Parliamentary Secretary to the Minister for Agriculture, Forestry and Fisheries, the Minister for Planning and Infrastructure, the Treasurer, the Minister for Energy, and the Minister for State Development report to the Assembly as to the action, if any, proposed to be taken by the Government with respect to the recommendations of the Committee.

The Committee suggests it may be appropriate for the Parliamentary Secretary to the Minister for Agriculture, Forestry and Fisheries to coordinate the Government's response to the Assembly.

CHAPTER 1 INTRODUCTION

1.1 Background

On Wednesday 25 June 2003, the Legislative Assembly resolved to refer an inquiry into the sustainability of the dairy industry to the Economics and Industry Standing Committee.¹

The Committee tabled an interim report on 28 August 2003.²

That sector of the dairy industry supplying milk for the domestic drinking market prior to deregulation was one of the most heavily protected industries in Australia. State government legislation mandated market milk premiums worth more than \$300 million per annum across Australia. This provided the industry with an effective rate of assistance of more than 200% compared to an average of 6% for all agricultural industries.³

Deregulation in July 2000 removed all legislation maintaining market milk premiums and protecting dairy farmers from interstate competition. The Australian dairy industry is now the least regulated in the world, with market milk prices being increasingly influenced by international dairy commodity prices.

The Western Australian dairy industry probably had a higher level of protection than any other state in Australia. The overnight change from highly protected market to full exposure to market forces has seen substantial falls in milk price and exerted unprecedented adjustment pressure on the Western Australian dairy industry. This inquiry is focused on the nature and effects of that adjustment pressure, and the opportunities that must come from deregulation if the industry is to be sustainable.

It is not the purpose of this report to present a history of the events or policy changes leading up to deregulation. These are reviewed in ABARE (2001)⁴ and Edwards (2003).⁵ Neither does it recapitulate the arguments for and against deregulation.

¹ Legislative Assembly, Hansard 25 June 2003, pp. 9246-9259.

² Economics and Industry Standing Committee (2002) Report No 6. Interim report on the Sustainability of the dairy industry in Western Australia. WA Legislative Assembly.

³ Edwards, G (2003) The story of deregulation in the dairy industry. Aust. J. Agric. Res. Econ. 47, 75-98.

⁴ ABARE (2001) The Australian dairy industry - impact of an open market in fluid supply. Canberra, ACT.

⁵ Edwards, G (2003) The story of deregulation in the dairy industry. Aust. J. Agric. Res. Econ. 47, 75-98.

Much of that discussion can be found in the 1999 Report of the Senate Rural and Regional Affairs and Transport References Committee.⁶

1.2 The Global Dairy Industry

Annual global milk production is estimated to be 570 million tonnes (Mt), of which 85 % or 490 Mt is cows' milk. Production of buffalo, sheep and goats' milk is estimated to account for a further 80 Mt, with much of this centred in Asia.⁷ Milk is a raw material that has the potential to produce a diverse array of fresh and/or durable food items (Table 1.1).

Table 1.1 Products from milk.

Anhydrous milkfat (butteroil);	Milk and coffee mixtures;
Baby formula;	Milk based mixes (soft serves / thick shakes);
Butter;	Milk or cream;
Buttermilk;	Milk powder;
Casein;	Milk, condensed or evaporated;
Cheese;	Milk, processed liquid;
Cream;	Skim milk based stock feed;
Flavoured liquid whole or skim milk;	Skim milk, powder;
Health beverages;	Skim milk, liquid;
Ice cream;	Sour cream;
Lactose;	Standardised liquid milk;
Malt extract;	Whey or whey powder; and
Malted milk powder;	Yoghurt

According to International Dairy Federation (IDF) estimates, the European Union (EU) is the main producer with 24.5% of world production, and the United States holds a 15.4% share.⁸

⁶ Senate Rural and Regional Affairs and Transport References Committee. (1999) Deregulation of the Australian dairy industry. The Parliament of the Commonwealth of Australia.

⁷ Canadian Dairy Information Centre (2003) <http://www.dairyinfo.gc.ca/cdicwdf.htm>. (Accessed 18 November 2003).

⁸ Canadian Dairy Information Centre (2003) <http://www.dairyinfo.gc.ca/cdicwdf.htm>. (Accessed 18 November 2003).

Global demand trends for the major dairy product categories have varied considerably in recent years. After gradually declining since the mid 1980s, per capita consumption of butter has now stabilised in most Western countries. By contrast, commercial demand for cheese continues to increase, in both developed and developing markets. Consumption of fresh products such as yoghurt and liquid milk has not altered significantly in developed dairy markets, but there has been a shift in demand towards reduced fat varieties. However, demand for these products in Asia and Central and South America has increased rapidly in the past decade. This in turn has fuelled strong demand for dairy ingredients such as milk powders.⁹

About 8 % of global milk production is traded (mainly as butter, skim milk powder, whole milk powder and cheese) in international markets each year. The European Union (EU) remains the world's major dairy exporter accounting for 36 % of all export sales on a milk equivalent basis, (ie in terms of the total volume of raw milk required to manufacture all traded dairy products). EU export refunds exert a major influence on international dairy commodity prices. Although accounting for only 3 % of world milk output, New Zealand is the second largest supplier of manufactured products to the world market with a 31 % share. Australia accounts for around 16 % of export sales based just on a 2 % share of world milk output. The USA, while a major milk producer, accounts for only 4 % of world trade. Other significant dairy exporting nations include Canada, Argentina and Uruguay, while Poland and the Czech Republic remain important suppliers to world markets for specific products such as skim milk powder and cheese.¹⁰

World demand for dairy products is predicted to grow at 2% per year compared to a predicted growth in world supply of 1%.¹¹ Long term prospects for the size and value of dairy exports are therefore strong.

Survey data from the International Farm Comparison Network of 27 countries confirms that only farmers in Pakistan, Brazil and Argentina produced milk at lower cost than Western Australia farmers during 2001/2002 (Fig. 1.1).

EU and US trade policy create major distortions in the global market for dairy products. Trade reform is the most important policy issue affecting the long-term future of Australian dairy exporters.

⁹ Dairy Australia <http://www.dairyaustralia.com.au>. (Accessed 18 November 2003).

¹⁰ Dairy Australia <http://www.dairyaustralia.com.au>. (Accessed 18 November 2003).

¹¹ Anon. (2000) Global Focus Dairy. Primary industry Bank of Australia, Sydney.

CHAPTER 1

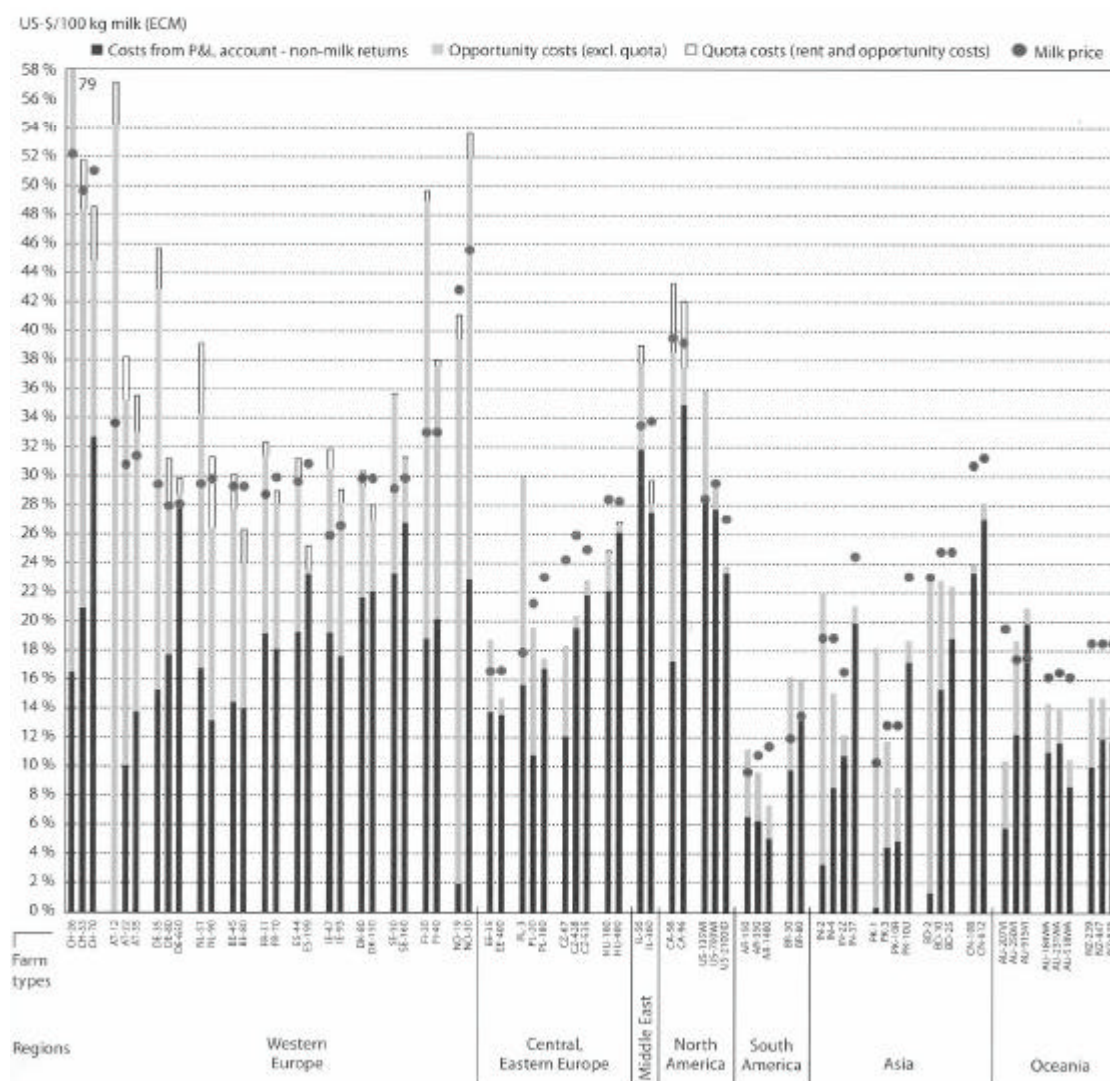


Figure 1.1 Farm gate milk prices in 27 milk producing nations participating in the International Farm Comparison Network.¹²

Internationally, the retail trade is becoming more concentrated with global retailers increasing in importance. In the United Kingdom the three largest chains have less than 45% of the market, in the USA the big three chains have less than 21%, and in Japan 17.5%. In many countries, strong private labels put pressure on proprietary

¹² Hemme T. (ed) (2003) Dairy report 2003. International Farm Comparison Network, Braunschweig, Germany.

brands - an extreme example is the UK, where private label accounts for 55% of packaged grocery expenditure.¹³

(a) The Australian Dairy industry

(i) Overview

The dairy industry is a major rural industry in Australia. Fewer than 11000 farmers managed the national herd of more than 2 million dairy cows in 2002/2003.¹⁴ Victoria is Australia's largest producer of milk (Table 1.2).

With a farm gate value of production just over \$2.8 billion dollars in 2002/2003, dairy ranks third behind the wheat and beef industries. Dairy is also one of Australia's leading rural industries in terms of adding value through further downstream processing. Much of this processing activity occurs close to farming areas, generating industry and employment in country regions. At the ex-factory level, industry output was estimated to be over \$8.5 billion dollars in 2002/2003.¹⁵

The 2002/2003 season was one of the most difficult for the Australian dairy industry that had been encountered for many years - Australia suffered the worst droughts in 100 years, compounded by falling international commodity prices and a strengthening Australian dollar. Milk production was recorded at 10.3 billion litres, a decrease of 8.4% on the record high production of the 2001/2002 season.¹⁶ Victorian dairy farmers will have lost up to \$1000 per cow during 2003/2003. Many businesses will take 6-8 years to regain their 2002 equity position.

Table 1.2 Proportion of Australian milk production by State (2002/2003).¹⁷

State	VIC	NSW	QLD	SA	WA	TAS
% Milk production	63.8%	12.6%	7.0%	7.1%	3.9%	5.7%

¹³ ACNielsen (2003) <http://asiapacific.acnielsen.com.au/industry.asp?industryID=2> (Accessed 18 November 2003).

¹⁴ ADC (2003) Australian Dairy Industry in Focus 2003. Australian Dairy Corporation, Southbank, Victoria.

¹⁵ ADC (2003) Australian Dairy Industry in Focus 2003. Australian Dairy Corporation, Southbank, Victoria.

¹⁶ ADC (2003) Australian Dairy Corporation Annual Report 2003. Southbank, Victoria.

¹⁷ ADC (2003) Australian Dairy Corporation Annual Report 2003. Southbank, Victoria.

The Committee finds that:

Finding 1

The dairy industry across Australia faced difficult times in the 2002/2003 season due to a combination of drought, falling international commodity prices, a strengthening Australian dollar, and compounded by decreases in retail, processing and farm gate prices following deregulation in July 2000.

(ii) Processors

Milk is processed by both farmer-owned co-operatives and public and private companies in Australia. Co-operatives dominate the industry, accounting for more than 70 % of all milk output.¹⁸ The three largest co-operatives - Murray Goulburn Co-operative Limited, Bonlac Foods Limited and the Dairy Farmers Group - account for over 60 % of all milk intake, and over 70 % of all milk used for manufacturing. While the largest co-operative has a milk intake of over 4 billion litres per year, there are a number of medium sized co-operatives with milk intakes of between 300 and 500 million litres (ML).

The major dairy processors are ranked among the top 2000 companies in Australia (Table 1.3).

The Committee finds that:

Finding 2

Farmer-owned co-operative dairy companies play a major role in dairy processing in Australia. The strength of the co-operative sector is a major source of market power for many dairy farmers.

(iii) Australian domestic market

In 2002, total drinking milk sales in Australia were just over 1900 ML per annum making per capita consumption of milk just over 97 litres (L) per annum. Milk sales have not kept pace with population growth, reflecting social changes, such as fewer people eating breakfast (particularly cereals), an ageing population that tends to consume less milk and migration from countries where dairy consumption is not part

¹⁸ ADC (2003) Australian Dairy Industry in Focus 2003. Australian Dairy Corporation, Southbank, Victoria.

of the culture. On the other hand, cheese consumption has been a major success for the Australian industry with consistently strong growth to reach 12 kg a head.¹⁹

Domestic yoghurt consumption continues to grow, underpinned by continued product innovation in the areas of packaging, flavours and the use of probiotic cultures, as well as new products such as drinking yoghurts. Australians continue to be among the world's leading consumers of ice cream.²⁰

The Australian retail market is dominated by two retailers - Woolworths Ltd and Coles Myer Ltd. Woolworths and Coles (including subsidiaries) have up to almost 80% market share of supermarket retail trade in Australia, the remainder of the market taken up by a range of smaller 'independent' grocers.

Coles Myer Ltd is an Australian owned public company that is ranked number 3 out of the top 2000 companies in Australia. For the 12 months to July 2003 the company generated total revenue of \$27,625,600,000 including sales and other revenue. In 2003 Coles Myer had about 165,000 employees in Australia including employees from all subsidiaries under the company's control.

¹⁹ Dairy Australian. (2003) Australian Dairy Market Reviewed.

²⁰ ADC (2003) Australian Dairy Industry in Focus 2003. Australian Dairy Corporation, Southbank, Victoria.

Table 1.3 Overview of companies operating in Australia and generating the majority of income from the Dairy Product Manufacturing (only Australian activities shown).²¹

Company	Status	Rank / 2000	Revenue (\$ million)	# employed (including all subsidiaries)
Fonterra Co-operative Group Limited.	NZ owned Co-operative	11	12,474 ^b	20,000
Murray Goulburn Co-operative Co Limited	Australian owned Co-operative	88	2,137 ^c	2,240
Australian Co-operative Foods Limited (Dairy Farmers Group)	Australian owned Co-operative	149	1,268 ^c	2,467
National Foods Limited	Australian owned Public Company	178	1,231 ^c	2,136
Bonlac Foods Limited	Australian owned Public Co-operative	197	1,105 ^c	na
Parmalat Australia Pty Limited	Foreign owned Proprietary Company	322	680 ^a	1,656
New Zealand Milk (Australasia) Pty Ltd (owned by Fonterra - above).	Foreign owned Proprietary company	342	612 ^b	232
Peters & Brownes Foods Limited (owned by NZ Milk - above)	Foreign owned proprietary Company	506	446 ^b	800 ^e
Tatura Milk Industries Limited	Australian owned Public Company	742	230 ^c	361
Bega Co-operative Society Limited (Bega Cheese).	Australian owned Co-operative	1033	223 ^c	439
Snow Brand Australia Pty Ltd	Foreign owned Proprietary company	1667	79 ^a	63
Nestle Australia Ltd ^e	Foreign owned Public Company	83	2,400 ^a	3,744
Kraft Foods (Australia) Limited ^e	Foreign owned Public Company	301	667 ^a	1,694

^a as at December 2002.^b as at May 2003.^c as at June 2003.^d as at July 2003.^e PB Foods Ltd submission: employees in Australia (600 in WA).

Woolworths Ltd is a locally Australian public company that is ranked number 5 out of the top 2000 companies in Australia. For the 12 months to June 2003 the company

²¹ IBISWorld (2003) via <http://www.seek.co.nz/if.asp?loc=ibis>, (Accessed 18 November 2003).

generated total revenue of \$26,969,200,000 including sales and other revenue. In 2003 Woolworths had about 145,000 employees in Australia including employees from all subsidiaries under the company's control.

(iv) *Australian export markets*

Australian dairy farmers now operate in a completely deregulated industry environment, where international prices are the major factor in determining the price received by farmers for their milk. At an average of less than 30 ¢/L (US 20 ¢/L as at November 2003), Australian dairy farmers receive a low price by world standards and therefore have to run very efficient production systems (see Fig. 1.1).

Nevertheless, over 55 percent of Australian milk production is exported – primarily as manufactured products – at international market prices for a value of \$3.25 billion dollars in 2001/2002. While Australia accounts for an estimated 2 % of world milk production, it is an important exporter of dairy products. Indeed, Australia ranks third in terms of world dairy trade, accounting for 16 % of all dairy product exports. Australia's top export market by value and volume in 2001/2002 was Japan (Table 1.4).²²

(b) *Western Australian Dairy*

About 300 Western Australian dairy farmers milk 68,000 dairy cows with the highest average per cow production in Australia. Western Australian dairy farms produce about 400 ML of milk annually with a gross value of more than \$100 million. Western Australia accounts for about 4% of Australian milk production (Table 1.2) and 2-3% of Western Australian gross value of agricultural production (Table 1.5).

²²

ADC (2003) Australian Dairy Corporation Annual Report 2003. Southbank, Victoria.

Table 1.4 2002/2003 Top 10 Australian dairy markets by value and volume.²³

Market	Value (A\$m)	Market	Volume ('000 tonnes)
1. Australia	\$6115	1. Australia	2273
2. Japan	\$386	2. Japan	124
3. Philippines	\$233	3. Philippines	97
4. Malaysia	\$160	4. Singapore	73
5. Saudi Arabia	\$144	5. Malaysia	57
6. Taiwan	\$136	6. Indonesia	47
7. United States	\$135	7. Taiwan	46
8. Singapore	\$134	8. China	46
9. Indonesia	\$111	9. Thailand	37
10. Thailand	\$98	10. Saudi Arabia	35

The dairy industry makes an important contribution to Western Australia through the flow on effects of its activities to the wider economy. In 1996/97 the Department of Agriculture Value-Chain Model showed the total net value added for the dairy industry in Western Australia was \$321 million, made up of \$100 million on-farm (ie gross value minus total costs) and \$221 million post-farm.²⁴ Dairy is one of the highest value-adding rural industries (adding \$2.10 in additional economic activity for each \$1.00 of farm gate value) and a significant regional employer both on dairy farms and in dairy factories. For example, every job created (or lost) in dairy processing flows on to a further 11 jobs in the wider community.²⁵

The nature of the industry requires significant inputs from a number of service industries. As well as the purchase of general farm supplies associated with farm management including soil testing, plant and animal nutrition, and the input of

²³ ADC (2003) Australian Dairy Corporation Annual Report 2003. Southbank, Victoria.

²⁴ Islam, N. (1997) Agriculture and the Western Australian Economy: value added contribution of agricultural commodities. Department of Agriculture, South Perth, WA.

²⁵ Johnson, P. L. (2001) An input-output table for the Kimberley region of Western Australia. Kimberley Development Commission.

consultants in relation to on-farm management including strategic planning, business management, production data, herd management and improvement, a range of specialist dairy suppliers are required for equipment such as liquid machine systems.

The Committee finds that:

Finding 3

Dairy is one of the highest value-adding rural industries in Western Australia.

(i) Western Australian domestic market

The Western Australian retail market turns over almost \$415 million worth of dairy products per annum (Table 1.6). Fresh white milk is the most important of these by volume and value. Western Australia's four largest dairy processors are PB Foods Ltd, National Foods Ltd, Harvey Fresh and Challenge Dairy Co-operative.

PB Foods Ltd are owned by New Zealand Milk (Australasia) Ltd who are in turn owned by Fonterra Co-operative Group Limited (all listed in Table 1.3) PB Foods, operating as Peters and Brownes Group, is the market leader for fresh milk in Western Australia under the labels Peters and Brownes. PB Foods employ almost 600 people in Western Australia, and process about 50 % of the State's milk obtained from about 50 % of dairy farmers (*ie* 155 dairy farmers) and have about 50 % of the market share of white milk.

Peters and Brownes is also a major producer and exporter of premium quality ice creams and other value-added products. Peters and Brownes has steadily grown its milk intake and production of value-added products and expects that growth to continue. Fonterra have signalled their intention to support Peters and Brownes in continuing to increase their scale and efficiency of operations and to retain product development expertise in Western Australia.

About 100 dairy farmers supply National Foods about 95 ML of milk. National Foods core business is in fresh domestic milk with almost 30% market share, but the company also produces UHT milk in Western Australia. National Foods employs over 300 people in Western Australia.

Challenge Dairy Co-operative is supplied by about 40 dairy farmers who supply all of their milk to Challenge, as well as National Foods suppliers who supply some of their milk under contract to National Foods and some of their milk to Challenge. In total, Challenge receives about 70 ML of milk from almost 50 % of dairy farmers, employs about 80 people and sells most of its milk products on the international commodity market.

Table 1.5 Gross value of agricultural production (GVAP) for Western Australia 1999/2000 to 2002/2003 (WA Dept of Agriculture 2003²⁶)

Western Australian agricultural sector	1999/00 \$M	2000/01 \$M	2001/02 (prov.) \$M	% change 2000/01- 2001/02	2002/03 (est.) \$M	% change 2001/02- 2002/03
Crops / crop products						
Wheat	1,901	1,502	2,033	35%	987	-51%
Barley	212	262	460	76%	393	-15%
Oats	50	49	102	108%	76	-25%
Lupins	214	145	212	46%	101	-52%
Other legumes	42	30	36	20%	22	-39%
Canola	289	111	171	54%	162	-5%
Sugar cane	6	7	6	-14%	9	50%
Vegetables	211	227	226	0%	232	3%
Fruit and nuts	110	118	133	13%	122	-8%
Grapes	54	102	99	-3%	115	16%
Hay	51	53	52	-2%	54	4%
Pastures	75	85	100	18%	65	-35%
Nurseries	82	108	121	12%	98	-19%
Other	26	15	25	67%	20	-20%
Total crops	3,323	2,814	3,776	34%	2,456	-35%
Livestock disposals						
Cattle slaughtered	217	262	292	11%	319	9%
Live cattle exports	141	196	204	4%	183	-10%
Sheep slaughtered	107	116	183	58%	196	7%
Live sheep exports	144	192	223	16%	259	16%
Pigs	69	76	89	17%	104	17%
Poultry	97	99	104	5%	105	1%
Other	4	4	5	25%	6	20%
Total disposals	779	945	1,100	16%	1,172	7%
Livestock products						
Wool	458	487	510	5%	548	7%
Dairy	144	103	113	10%	117	4%
Eggs	31	34	34	0%	36	6%
Other	3	3	6	100%	7	17%
Total products	635	626	663	6%	708	7%
Total Agriculture	4,737	4,385	5,539	26%	4,336	-22%

²⁶ WA DAgric (2003) WA Agri-food industry outlook August 2003. Department of Agriculture, South Perth, WA.

Table 1.6 Amount and value of supermarket retail sales for milk products in Western Australia as at 03 August 2003 (Dairy Australia).

Product	Amount	Value (\$M)
Fresh white milk	92.20 ML	\$117.7
Fresh flavoured milk	8.72 ML	\$19.77
UHT milks & creams	18.43 ML	\$38.01
Cheese	11.76 Mkg ^a	\$102.51
Yoghurt	12.00 ML	\$54.16
Dairy desserts	1.67 ML	\$10.55
Chilled cream	3.47 ML	\$12.50
Butter	1.86 Mkg ^b	\$9.06
Dairy blends	1.59 ML	\$7.67
Ice cream	14.28 ML	\$42.50
TOTAL		\$414.43

^a 1 kg of cheese contains milk solids equivalent to approx. 10 L milk.

^b 0.5 kg of butter contains milk solids equivalent to approx. 10 L milk.

Harvey Fresh is a Western Australian family company that processes 20 ML of milk supplied by about 18 dairy farmers. Harvey Fresh produces UHT milk, some of which is exported to parts of south-east Asia. Harvey Fresh pays the highest average farm gate prices for their milk.

There are also a few small boutique processors producing dairy products for niche markets (Table 1.7).

The four larger processors have indicated by word or deed to the Committee their on-going commitment to a Western Australian based dairy industry. Peters and Brownes have shown their support for the dairy industry by their continued production of manufactured products such as cheese, a process which is often loss making but ensures minimal wastage of contracted milk production. Peters and Brownes have recently announced a \$6 million expansion of their export ice cream facility in Perth.

Table 1.7 Small processors producing dairy products in Western Australia.

Processor	Processor
Benny's Gelati Pty Ltd.	Midland Icecream.
Blue Cow Cheese Company Pty Ltd.	Mundella Foods Pty Ltd.
Borrello Cheese Pty Ltd.	Normandie Foods.
Casa Dairy Products Pty Ltd.	Oggies Icecreameries.
Centra Fine Foods.	Rose Valley Cheese Company.
Harvey Cheese.	Simmo's Ice Creamery.
Heritage Country Cheese.	Swan Valley Cheese.
Kervella Cheese.	The Junction Ice Creamery.
Margaret River Dairy Co.	The Old Cheddar Cheese Company Pty Ltd.

In Western Australia, supermarket turnover is about \$5 billion, with fresh milk about \$240 million per annum, almost 5% of the total supermarket turnover. About 55 % of milk is sold in grocery stores, the remainder sold in the route trade (convenience stores, service stations etc).

As in the rest of Australia, the two retailers Coles Myer Ltd and Woolworths Ltd dominate the Western Australian retail market. Coles Myer Ltd operate over 70 Coles supermarkets in all major centres in Western Australia, employing nearly 8 000 staff, and a retail market share of milk sold in supermarkets of about 33 %. Woolworths Ltd operate 59 Woolworths supermarkets in all major centres in Western Australia, employing nearly 7 500 staff, and a retail market share of milk sold in supermarkets is about 29 %.²⁷

The Western Australian Independent Grocers' Association represents all the independent supermarket outlets and grocery retailers throughout Western Australia and has a 39% share of the retail supermarket trade. This group, including brands such as Action Supermarkets, Dewsons Supermarkets and Supa Valu Supermarkets, have a combined turnover of some \$1.2 billion per annum and employ about 15 000

²⁷ Aztec Scan Data (2003) Data for period ending 6 July 2003.

people in Western Australia²⁸ - this accounts for almost 50 % of those employed in the grocery industry.

(ii) Western Australian export markets

The two major Western Australian dairy exporters are Peters and Brownes and Challenge Dairy Co-operative.

Peters and Brownes are Western Australia's largest dairy exporter, selling products both to the east coast of Australia and internationally. They are the largest exporter of dairy products in Western Australia, and the largest exporter of ice-cream from Australia. Peters and Brownes was the first Australian company to enter the Japanese ice cream market in 1991, and now have one of the few factories in the world that has the capability to produce ice cream for Japan. The excellence of Peters and Brownes cheddar cheese, produced for domestic sale and commodity export, has been recognised in international competition.

Challenge Dairy Co-operative, established in Capel in 2001 with the assistance of a \$10 million grant from the Western Australian Government, sells most of its milk products on the international commodity market. In July 2003, Challenge Dairy Co-operative announced a \$10 million joint venture with China's Beijing Sanyuan Food Company.

The Sanyuan Challenge Australian Dairy joint venture plans to develop new processing facilities to produce value-added exports for the Chinese retail market. If this strategy succeeds in achieving a price premium over commodity exports, it should increase farm gate returns and may eventually provide leverage to arrest the decline in domestic milk prices. Completion of the joint venture saw modest improvements in milk price, but these have not been sustained or grown as predicted.

This is largely a result of a depressed export market. Low international commodity prices and the strong Australian dollar have reduced returns to farmers. All global dairy exporters have been affected. The unit value of Australian dairy commodities has declined by more than 35% since their peak in September 2001.

Nonetheless, Challenge has about a third of Western Australian farmers as members and enjoys widespread industry support.

²⁸ Cummings, J. (2003) Session 1, Transcript of evidence, 15 October 2003, and Submission, Mr J Cummings, President, Western Australian Independent Grocers' Association.

1.3 Other inquiries

(a) Australia

(i) *The Senate Rural and Regional Affairs and Transport References Committee Inquiry into Deregulation of the Australian dairy industry*²⁹

The Senate Committee concluded that market forces would inevitably force deregulation and that a managed outcome was preferable to a “commercially driven crash”. The Senate Committee raised concerns regarding the likelihood of compensation to dairy farmers for loss of quota, the likely impact on regional communities and the adequacy of the proposed DSAP package. The Senate Committee also expressed concern over the narrowness of the public interest tests applied under National Competition Policy (NCP).

The Senate Committee recommended that State and Federal Governments establish a framework and timetable for the coordinated deregulation of the dairy industry; ensure farmers are not disadvantaged by delays in DSAP payments; State governments address the issue of quota compensation; adjustment packages be developed for regional communities affected by deregulation; Australian Competition and Consumer Commission (ACCC) monitor costs and prices in the dairy industry so that dairy farmers are not unfairly burdened with the levy; and inquiry into the operations and accountability mechanisms of co-operative be undertaken (see Section (iii) below).

This Committee shares the Senate Committee’s concerns regarding the narrowness of the public interest criteria used by National Competition Council, particularly as they relate to implementation of NCP in regional communities. The Committee is concerned that NCP is limiting the ability of State governments to implement appropriate policies for regional development.

(ii) *ABARE report*

The Federal Minister for Agriculture, Forestry and Fisheries requested in 2000 that the Australian Bureau of Agricultural and Resource Economics (ABARE) report on:

1. The prices received by dairy farmers, manufacturers and retailers pre and post deregulation;
2. The value of quota entitlements held by producers pre-deregulation and any compensation paid by State governments;
3. The amount of disbursements to State governments under the National Competition Policy for dairy deregulation;

²⁹ Federal Parliament (1999) Senate Rural and Regional Affairs and Transport References Committee Inquiry into Deregulation of the Australian dairy industry. Canberra, ACT.

4. Savings to consumers following deregulation;
5. The effect of deregulation on the dairy industries in each state; and
6. The impact of cost of production and profitability of dairy farmers.

ABARE noted falling farm gate prices in all states and predicted significant drops in farm profit for Western Australian dairy farmers during 2000/2001. That prediction has been borne out by farm survey data. The report expected the shires of Harvey, Capel and Waroona to be the worst affected by deregulation in Western Australia. ABARE also predicted that milk production would be maintained or increased in all states and that consumers would benefit from lower milk prices. Total transfers from consumers to dairy farmers were predicted to decline by \$170M p.a. across Australia, equating to a 6% reduction in gross value of milk production.

(iii) *ACCC report on impact of farm gate deregulation on the Australian milk industry*³⁰

Responding to the recommendations of the Senate Rural and Regional Affairs and Transport References Committee Inquiry into Deregulation of the Australian dairy industry, Minister Hockey directed the Australian Competition and Consumer Commission (ACCC) under section 27A of the *Prices Surveillance Act 1983* to formally monitor prices, costs and profits of businesses dealing with market milk product sales.

Monitoring was to commence three months before the introduction of the 11 ¢/L Dairy Industry Adjustment Levy (DIAL) on 8 July 2000 and conclude six months later on 8 January 2001. Under the Ministerial directive, the ACCC was required to present a report of its findings to the Federal Government within three months of completing its monitoring activities.

The ACCC issued their report in April of 2001 and concluded that Australian consumers were receiving lower milk prices as a result of deregulation. Price falls were greater for milk sold in supermarkets than in convenience stores, with the result that supermarkets increased their share of the total milk market. Retail price cuts were made possible by reductions in farmer, processor and retail margins for milk. The ACCC noted that deregulation had exposed the weak market power of milk processors relative to supermarkets.

The report made a number of seminal points regarding changes in the supply chain resulting from deregulation. To quote from the report's summary:

³⁰ ACCC (2001) Impact of farm gate deregulation on the Australian milk industry: study of prices, costs and profits. Australian Competition and Consumer Commission, Canberra, ACT.

“Ultimately, as consumers are prepared to pay a premium for fresh milk, processors will have to pay farmers a sufficient return to guarantee a reliable supply if dairy farmers are not to exit into other areas of agricultural production.

A new dynamic has also emerged in the competitive relativities between processors and the retail sector. Processor bargaining power, and therefore ability to influence price, has been found to be relatively weak, partly due to pressure to lower excess processing capacity and firm up market shares in the newly deregulated environment. However, at the retail level the most complex dynamic has developed. This has been the result of supermarkets discounting generic products.

On 15 August 2000 Woolworths announced standard national milk prices for its generic-labelled milk that effectively created a new floor in the Australian price of plain milk. The new prices became effective immediately and was the first time that a retail chain had set national prices for 1, 2 and 3-litre packs of milk. These new prices followed the announcement of two-year supply contracts which were offered to tender and attracted aggressive bidding from the major milk processors. Following Woolworths’ announcement of its new milk-pricing structure, Coles, Franklins and IGA announced that they would match Woolworths’ lower milk prices for their respective private labels.

Before these announcements there had been significant state-based differences in retail milk prices. Thus the emergence of a national retail market for milk coincided with the first few months of full deregulation.

This strategy of the supermarkets, based on driving more store traffic rather than higher revenue from milk, meant that convenience and corner stores, which provide branded products as well as that intangible commodity called convenience, came under considerable competitive pressure. Accordingly, market share moved away from this part of the retail sector to the supermarkets. This illustrated the importance of basic products such as milk in shaping general consumer perceptions of pricing relativities across competing food retailers.”³¹

The Committee note that there has been no further assessment by the ACCC, and that there has been no action taken by Federal and State Governments in response to the market place shifts identified in this report.

³¹ ACCC (2001) Impact of farm gate deregulation on the Australian milk industry: study of prices, costs and profits. Australian Competition and Consumer Commission, Canberra, ACT. p xvi.

(iv) *South Australian Parliament inquiry into dairy deregulation*³²

The South Australian Joint Committee on the Impact of Dairy Deregulation in South Australia examined the management of deregulation, the impact on dairy farmers, and the prognosis and opportunities for a deregulated industry.

The Joint Committee observed that, historically, the SA dairy industry had been State based, but now faces many issues that are of national or international character. The Committee concluded there were aspects of the dairy deregulation process that were not managed in a completely fair and equitable manner, and that the Federal and South Australian Governments should take steps to address the inequities, and support initiatives for development of the dairy industry.

(b) **Western Australia**

The Dairy Industry Working Group was established as a bipartisan response to the deregulation of the Western Australian Dairy industry in 2000. The opposition Labor party provided conditional support to the passage of the *Dairy Industry and Herd Improvement Legislation Repeal Bill 2000*. Establishment of a task force to examine and report on the industry was a condition of bipartisan support for deregulation.

Following elections and a change of Government in February 2001, the Working Group's first report "A Healthy WA Dairy Industry – Let's Do It"³³ was released by the new Minister, the Hon. Kim Chance, who provided the Working Group with new terms of reference in March 2001. The Group provided the following recommendations against those terms of reference.³⁴

- Government continues to facilitate the development of a strong export-manufacturing sector in Western Australia to maintain competition for manufacturing milk.
- The Minister facilitate the conversion of loans made to Challenge Dairy Co-op to grants under the terms of the Western Australian Dairy Industry (Processing) Incentive Scheme.
- The Minister ensures the early progression of a loan facility to allow Western Australian co-operatives to take advantage of Section 120 (i) (c) of the *Income Tax Assessment Act 1936*.

³² SA Parliament (2003) Joint Committee on the Impact of Dairy Deregulation in South Australia Final Report - May 2003. Adelaide, South Australia.

³³ Dairy Industry Working Group. (2001) A healthy WA dairy industry – let's do it! WA Department of Agriculture, South Perth

³⁴ Dairy Industry Working Group. (2002) Final report. WA Department of Agriculture, South Perth.

- That Government continues its support for the implementation of the ACCC's determination on collective bargaining in the dairy industry.
- That Government continue to monitor corporate developments in the dairy processing sector and stand ready to advise the ACCC if any developments threaten to have anti-competitive effects in Western Australia.
- That Government engage the Department of Immigration and Multicultural Affairs with a view to including skilled dairy farm workers within the skilled migration program.

1.4 This inquiry

In commencing the inquiry, the Committee has carefully considered the terms of reference.

A key term in the reference of this inquiry from the Legislative Assembly is "sustainability". While it was agreed that the term sustainability encompasses all three elements of the triple bottom line (economics, environment and society), and that all elements will be considered by the Committee, economic and social aspects are considered to be of most significance in this inquiry.

The Committee also discussed the interpretation of "deregulation". The Committee considers that the deregulation process within the inquiry's terms of reference means the period from 1 July 2000 when all states repealed legislation governing sourcing and pricing of market milk, and the state milk authorities, which administered these controls, were wound up.

(a) Conduct of the inquiry

This inquiry was conducted with two co-opted members, the member for Warren-Blackwood, (Hon Paul Omodei, MLA) and the member for Bunbury, (Mr Tony Dean, MLA). Both of these members had particular knowledge of the dairy industry and have made a significant contribution to the conduct of the inquiry.

In addition, the work of the Committee was greatly assisted by the participation of Dr David Windsor an officer seconded to the Committee staff from the Department of Agriculture. This secondment was made possible by the agreement of the Minister for Agriculture, Forestry and Fisheries, the Hon. Kim Chance. Dr Windsor's contribution has been invaluable in allowing the Committee to report in less than six months from the time the matter was referred to the Committee by the Legislative Assembly.

Since the Assembly referred the inquiry to the Committee at the end of June, the Committee has held 22 deliberative meetings, received 74 submissions, and held 41 hearings or briefings with 87 people. This includes visiting four farms in southwest

Western Australia meeting with 11 dairy farmers, the four major dairy processors, and the three major grocery retail groups in Western Australia.

(i) Submissions

The Committee advertised in a range of Western Australian newspapers 12-18 July 2003 with a closing date for submissions on 26 August 2003. This date was set to ensure submissions were received in time for the tabling of the Committee's interim report on 28 August 2003.³⁵

The Committee received 74 submissions (Appendix 1). This number includes seven submissions received after the closing date - the Committee resolved to accept these and consider them in its deliberations on this important issue.

The Committee resolved not to table submissions to this inquiry to ensure full protection of "commercial, in confidence" information provided to the Committee.

The submissions revealed a diversity of opinion across and within all sectors and regions of the dairy industry.

(ii) Briefings

The Committee received 23 separate briefings from 49 people over the period of the inquiry (Appendix 2).

At the start of the inquiry, the Committee visited four dairy farms in southwest Western Australia meeting with 11 dairy farmers.

Other briefings were provided by a representatives of Peters & Brownes Group, and professional researchers and advisers in the dairy industry, including Dr Glenys Hough, Campbell Shearer and Neill Buck, and more broadly from officers from Western Australian Government agencies including the Department of Agriculture, the Office of the Minister for Agriculture, Forestry and Fisheries, and the Department of Treasury and Finance Western Australian Treasury Corporation (Appendix 2).

Further briefings were provided interstate by relevant industry bodies and government agencies in Victoria, ACT and New South Wales including representatives of the Australian Bureau of Agricultural & Resource Economics (ABARE); the Department of Agriculture, Fisheries and Forestry - Australia (AFFA), the Australian Competition and Consumer Commission (ACCC), Dairy Australia, the Dairy Adjustment Authority, the National Competition Council, and Australian Dairy Farmers. In addition, the Committee visited a dairy farm in Bega, the Bega Cheese dairy

³⁵ Economics and Industry Standing Committee (2002) Report No 6. Interim report on the Sustainability of the dairy industry in Western Australia. WA Legislative Assembly.

processing plant in New South Wales, and held discussions with New Zealand Milk (Australasia) in Melbourne (Appendix 2).

(iii) *Hearings*

The Committee heard from 38 witnesses at 18 hearings to gather information relevant to the dairy inquiry. A total of 13 hearings were held in Perth on a number of dates and five in Bunbury on Friday 19 September 2003. (Appendix 3).

The Committee agreed to a number of requests from witnesses to be heard in closed session to allow full and frank discussion including consideration of “commercial, in confidence” information.

CHAPTER 2 FINANCIAL IMPACT OF DEREGULATION ON WESTERN AUSTRALIAN FARMERS, PROCESSORS, WHOLESALERS AND RETAILERS

2.1 Introduction

The current crisis of confidence in the Western Australian dairy industry reflects genuine financial difficulties faced by many farm businesses during the 2002/2003 financial year. Contributing factors have included:

- continuing erosion of the price premium for market milk;
- low international dairy commodity prices combined with a strong Australian dollar;
- drought-initiated high grain prices leading to a substantial increase in costs of production over the 2002/2003 summer;
- failure of the Collective Bargaining process to increase farmers' market power or deliver equitable outcomes through a transparent process;
- inability of the Sanyuan Challenge Australian Dairy joint venture to deliver early benefits;
- ongoing adjustment pressures associated with deregulation and low export prices; and
- a culture of individual behaviour by Western Australian dairy farmers, compared to their counterparts in eastern states of Australia, affecting price negotiations for both purchase of inputs and sale of outputs.

2.2 Milk prices

The gross value of milk produced in Western Australia has declined by about 6 ¢/L in the three years since deregulation. Most of this decline has been attributable to the reduction in domestic milk premiums seen since July 2000. However the problem has been compounded by lower export returns as the result of poor dairy commodity prices and the rising Australian dollar.

Comparisons between farm gate milk prices before and after deregulation are made difficult by the complexity and variety of milk payment systems.

The nominal price of market milk before deregulation was 53 ¢/L. However a survey of 78 farmers in 1999/2000 shows an average net market milk price of 45 ¢/L (ranging from 22 to 52 ¢/L). This represents a premium of about 24 ¢/L over the 1999/2000 manufacturing milk price. Average net price across all milk produced in Western Australia during 1999/2000 was about 29.5 ¢/L.

Market milk price received and the proportion of milk supplied under quota were the key determinants of average milk price before deregulation (Fig. 2.1). Any dairy farmer with more than 38% quota would probably have received a higher average milk price pre-deregulation than post-deregulation. However, not all farms had access to quota sales of milk and some operations were profitably operating on less than 25 ¢/L.

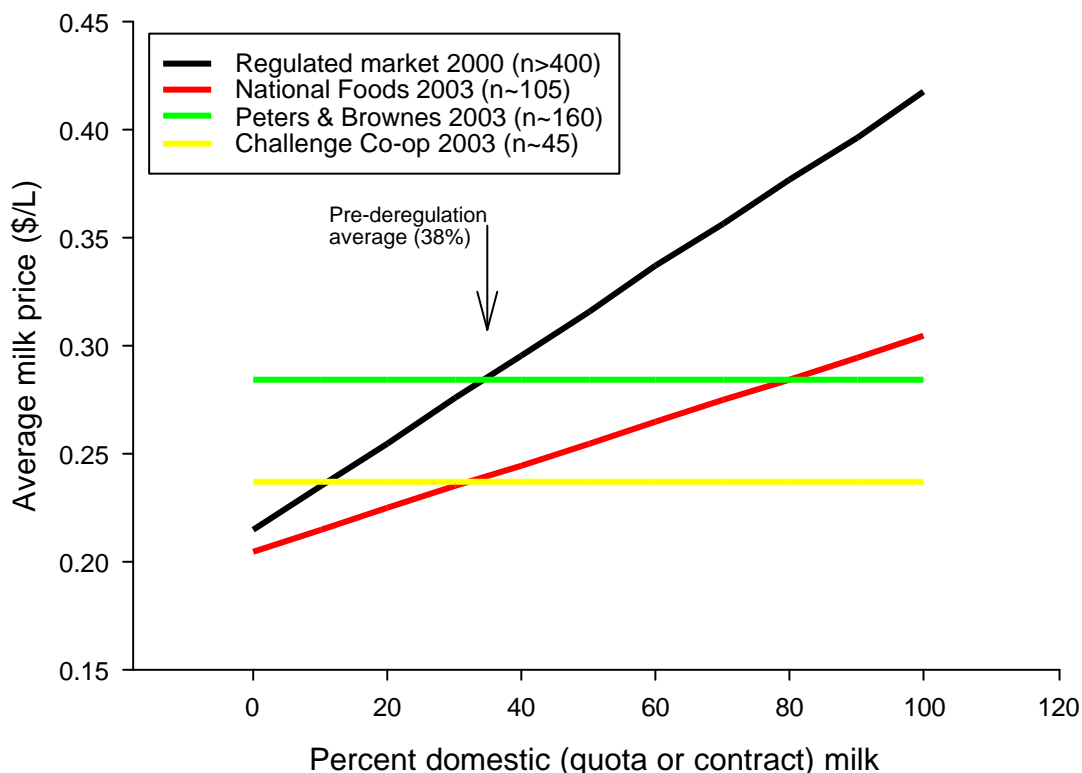


Figure 2.1 Estimates of average farm gate milk prices in Western Australia for 1999/2000 (pre-deregulation) and by three major processors for the 2003/2004 financial year.

Australian Bureau of Agricultural & Resource Economics (ABARE) Farm Survey Data³⁶ show that Western Australian dairy farmers received the second lowest price of any state in 2000/2001 and the lowest in 2001/2002 (Table 2.1).

Table 2.1 Average farm gate milk prices (¢/L) for dairy farmers in Australia 1995/96 – 2001/2002. (ABARE)

	95/96	96/97	97/98	98/99	99/00	00/01	01/02
WA	37.7	40.0	40.0	38.6	38.4	28.8	29.3
Vic	34.0	31.9	30.5	29.8	26.1	30.7	34.1
NSW	44.1	42.9	41.5	39.6	36.8	29.7	32.5
Qld	44.8	44.9	45.5	46.7	44.0	32.1	31.9
SA	33.3	34.1	33.4	33.6	30.8	28.5	32.1
Tas	33.4	28.1	27.8	28.6	25.3	25.3	33.8

Data from the International Farm Comparison Network show a lower milk price on Western Australian farms during 2001/2002 than in Victoria or New Zealand. Of the 27 countries surveyed only dairy farmers in Pakistan, Brazil and Argentina received lower prices than Western Australian dairy farmers (Fig. 1.1).

2.3 Variation in prices between processors

Prices received by farmers under the current market arrangements vary depending on the milk processor supplied, the proportion supplied under a domestic market contract, time of year and milk quality (Fig. 2.1, Fig. 2.2).

For example Peters and Brownes Foods (PBF) paid an average of 31 ¢/L in March 2003, ranging from 24 to 38.5 ¢/L depending on milk quality and volume supplied. PBF suppliers (about 150 dairy farms) expect to average about 28.5 ¢/L for all milk (before deduction of freight charges) during 2003/2004.

³⁶

ABARE (2003) <http://www.abare.gov.au> (Accessed 18 November 2003).

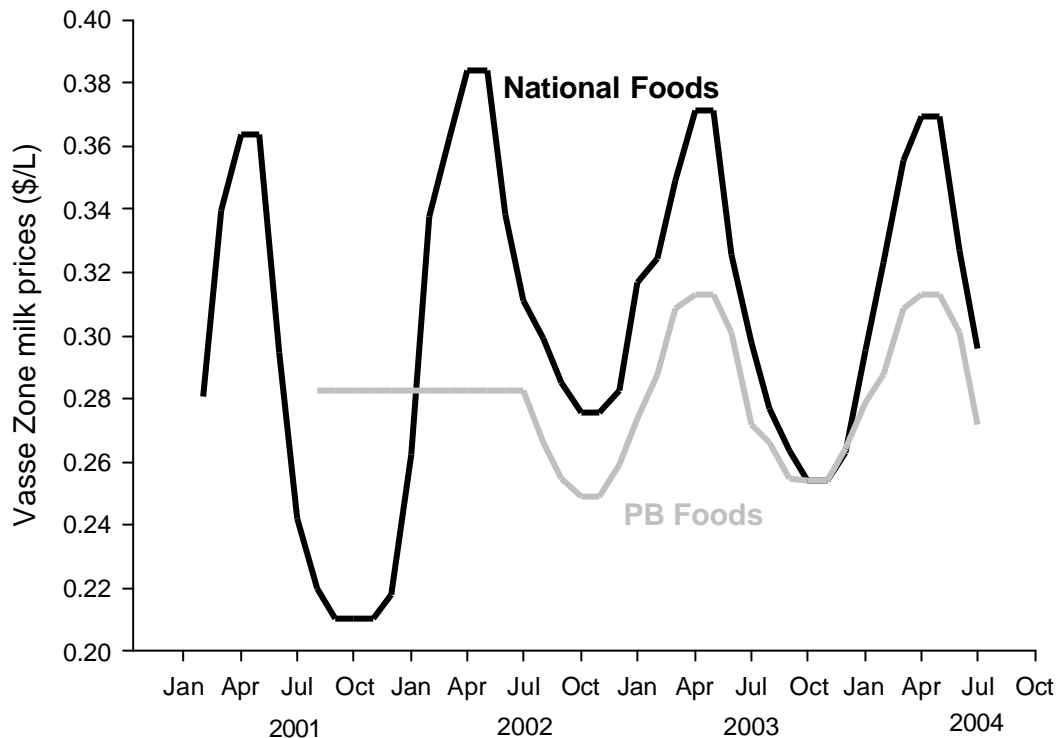


Figure 2.2 Seasonal variation in milk prices paid by the two major corporate processors (including future contract payments) in Western Australia since January 2001.

National Foods announced a reduction in the size of milk contracts (paying about 30.5 ¢/L before deducting freight costs) offered to suppliers in July 2003. Those suppliers (about 10) who signed contracts in January have had their contract volumes reduced by 5%. Suppliers who opted to participate in the collective bargaining process authorised by the ACCC (about 95) have had their winter contract volumes reduced by 40% and summer contracts reduced by 15%.

Farmers who supplied 100% of their production to National Foods under contract will have their average milk price reduced by more than 4 ¢/L over the financial year if they maintain production. National Foods suppliers have the option of sending their increased milk surplus to Challenge Dairy Co-operative, but will incur significant expense in buying delivery rights.

The National Foods contract price tends to be a benchmark price for smaller milk processors who often set their prices just higher than the National Foods level to ensure continuity of supply. Exact data on prices paid by small processors are not available.

A reduction in milk prices by Challenge Dairy Co-operative in May 2003 was a major factor precipitating the current crisis of confidence in the dairy industry. Completion of the Sanyuan Challenge Australian dairy joint venture resulted in improved prices for both contract suppliers and Delivery Right Unit (DRU) holders. However, continuing appreciation of the Australian dollar has eroded these price gains. Those farmers supplying all milk to Challenge Dairy Co-operative (about 40) are currently projected to receive a similar milk price across the financial year to their average of 23.5 ¢/L for the previous financial year.

2.4 Impact on farm businesses

An indicative average price for 2003/2004 for contract milk for the domestic market is 30 ¢/L compared to 45 ¢/L prior to deregulation. The total annual reduction in transfers from consumers to dairy farmers resulting from deregulation of the domestic white milk market can therefore be estimated as 160 ML at 15 ¢/L or \$24 million per year.

The Committee finds that:

Finding 4

The total reduction in milk income to dairy farmers in Western Australia resulting from deregulation of the domestic milk market is estimated to be \$24 million per annum.

There has also been a redistribution of market milk premium since the removal of the quota system, with the result that many farmers receive lower, and some farmers higher, milk prices than before deregulation. The effect on income and profitability has been compounded by the poor recent returns from the export market.

(a) Income

ABARE Farm Survey Data show that Western Australian dairy farmers received the second lowest milk price of any state in 2000/2001 and the lowest in 2001/2002 (Table 2.1). They also show that milk prices have fallen further in Western Australia than in New South Wales and Queensland, the two other states with a high proportion of market milk prior to deregulation.

The entry of Challenge Dairy Co-operative into the manufacturing market and increase significantly in manufacturing prices paid by Peters and Brownes saw farm incomes recover in 2001/2002 (Fig. 2.3, 2.4).

While no data are available for 2002/2003 at time of writing, it is likely that low world commodity prices and high feed costs will have combined to reduce both farm profit and family share of farm income below 2001/2002 levels. Many Western Australian dairy farms will have been unprofitable during that financial year.

Lower feed grain prices will reduce cost of production pressures during the coming summer. However all indications are that the milk price pressures caused by low commodity prices and the strong Australian dollar will continue throughout 2004.

(b) On-farm costs

Deregulation of the dairy industry highlighted the wide variation of production costs between dairy farms in Western Australia (see Table 2.2). This has meant that the price cuts associated with deregulation caused a rapid decline in the number of farmers in the State. To date this has not had an impact on the total number of cows as there has been an offsetting increase in herd sizes per farm. These data also indicate that managing production costs can be more important than milk price in determining farm profit. Total milk production costs on Western Australian farms ranged from 19 to 48 ¢/L in 1999/2000. Variations in milk quality between farms currently produce milk price differences of 15-20 ¢/L.

Data from the International Farm Comparison Network confirm that the top 50% of Western Australian dairy farms are genuinely internationally competitive with production costs comparable to Victoria and New Zealand. The best Western Australian farms are amongst the best in the world. Western Australian farms were characterised by highly efficient use of labour and capital.

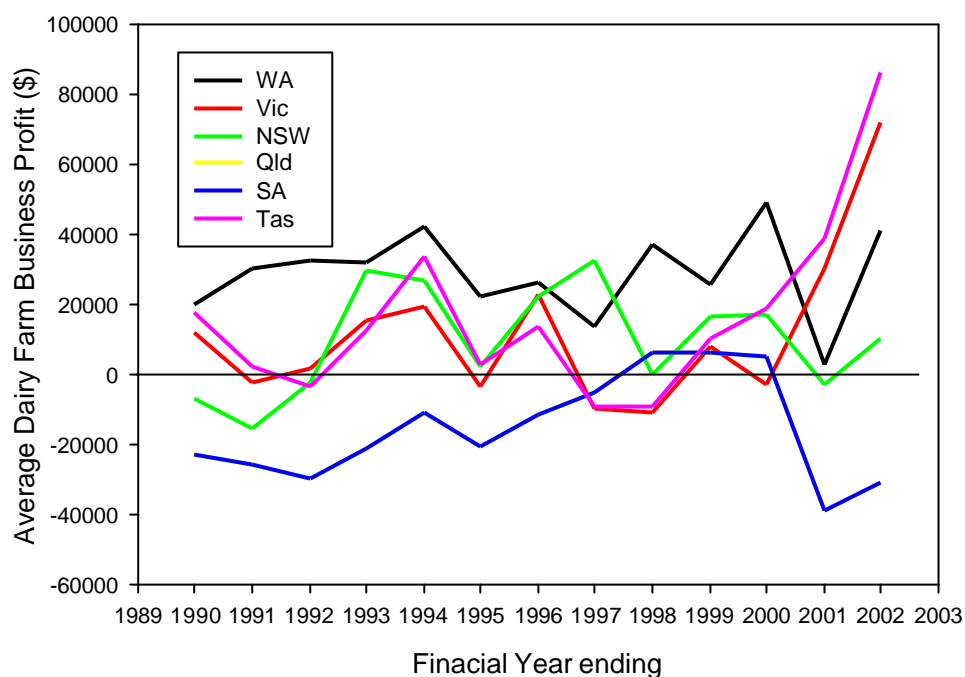


Figure 2.3 Average farm business profit on Australian dairy farms. (ABARE Farm Surveys)

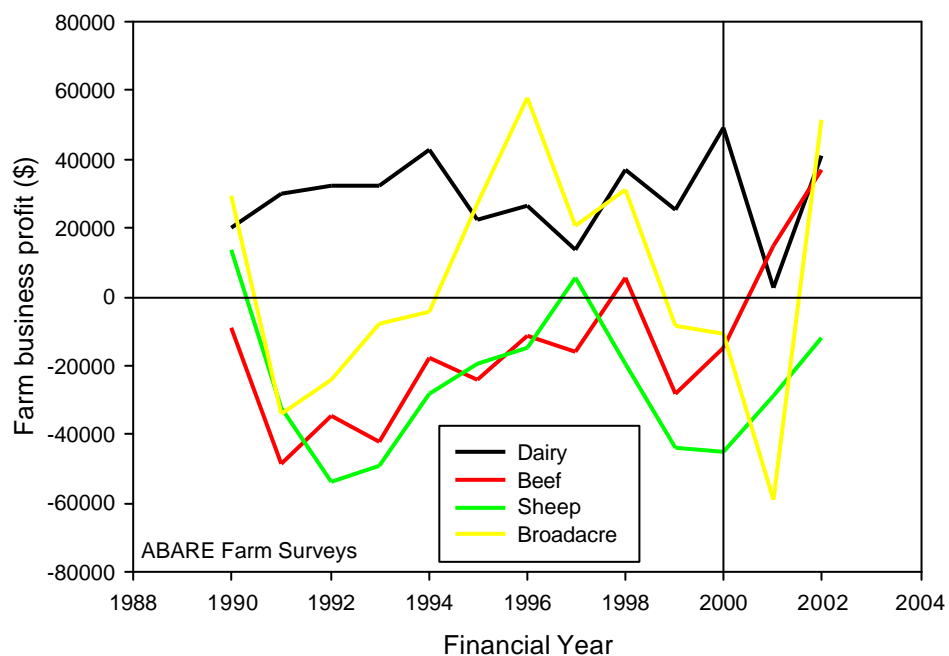


Figure 2.4 Family share of farm income on Western Australian farms. (ABARE Farm Surveys)

Table 2.2 Income and costs on Western Australian dairy farms 2000/2001 (n=39)

	Average	Low profit 25%	Hi Profit 25%
Total milk sales (ML)	1.5	1.2	1.9
Net milk sales (¢/L)	27.1	25.6	28.3
Total income (¢/L)	30.9	27.6	33.9
Herd Costs (¢/L)	1.5	1.5	1.5
Shed Costs (¢/L)	1.0	1.2	0.9
Feed costs (¢/L)	12.1	13.1	10.9
Total Variable Costs (¢/L)	14.6	15.8	13.3
Dairy Gross Margin (¢/L)	16.3	11.8	20.6
Total labour costs (¢/L) ^a	6.8	9.6	4.9
Total Operating Costs (¢/L) ^b	26.2	31.1	23.0
Operating Profit (¢/L)	4.7	-3.5	11.0
Operating profit (\$/Ha)	315	-133	793

^a Includes an allowance for the cost of family labour.

^b Includes non-cash fixed costs such as depreciation and family labour, but not debt servicing or business development, which must be funded from within operating profit

The Committee finds that:

Finding 5

Production costs on Western Australian dairy farms vary widely reflecting differences in climate, on-farm infrastructure, and individual farm efficiency.

Finding 6

There are opportunities for many dairy farms to improve business performance by reducing feed and labour costs and through other strategies such as co-operative purchase of inputs.

It is important to acknowledge that while some dairy farm businesses are profitable under current market conditions, many others are not yet capable of supplying milk at prices that will maintain the competitiveness of Western Australian processors. There is a need for individual farm businesses to understand the implications of different paths for industry development and to make strategic decisions as to whether they wish to remain in the industry. This issue is further discussed in Chapter 6.

The Committee finds that:

Finding 7

Some Western Australian dairy farm businesses are among the most efficient in the world while others are not economically sustainable in the current dairy market.

Continuing to strive for efficient and economic farming practices, equal to those of Victoria, New Zealand, and emerging competitors such as Brazil,³⁷ is essential for the provision of competitively priced raw milk to enable retention and growth of dairy processing in Western Australia.

Rates of return on assets and poor capital utilisation are perennial issues in most Australian rural industries. Existing irrigated farms need to use water more efficiently and produce pasture more optimally.³⁸ There is also the opportunity to increase milk production on low-cost pasture-based systems. Further, the Committee has heard compelling evidence that there are opportunities for dairy farms to share high value assets such as milking sheds and machinery,³⁹ and including the installation of 3-phase power, rather than duplicating under-utilised resources on neighbouring properties.⁴⁰

(c) Asset values

While it is difficult to capture an overall picture of the financial health of dairy businesses, the 2002 ABARE farm survey reported an average equity level of 87% on Western Australian dairy farms. This relatively high equity combined with the large capital base of dairy farms averaging nearly \$3 M provides a large capacity to buffer the annual ups and downs of agribusiness.

³⁷ Shearer, C. (2003) briefing to the Committee, 20 Nov 2003.

³⁸ Primary Consulting Services (2003) South West Yarragadee Economic Issues Study - Dairy. Unpublished report by to Water and Rivers Commission.

³⁹ Knott, S. (2003) Session 1, Transcript of evidence 17 October 2003

⁴⁰ Brand, A. & E. (2003) Session 2, Transcript of evidence 17 October 2003

Many dairy farm businesses will have had to increase borrowings to manage the high costs and low prices of the last 2 years. This is a normal business response to difficult trading conditions, but is unsustainable on a continuing basis. Rural consultant Dr Glenys Hough believes up to 30% of dairy farmers are at financial risk if trading conditions do not improve.⁴¹

2.5 Restructure assistance

The Western Australian dairy industry has been provided with more than \$150 million in combined Federal and State Government restructure funds to assist the transition to a deregulated market (Table 2.3). The \$1.94 billion Dairy Structural Adjustment Program is funded by the 11 ¢/L Dairy Industry Adjustment Levy on all domestic liquid milk. Average DSAP payments to Western Australian farmers are the highest of any state, reflecting the high proportion of Western Australian milk that was supplied under quota before deregulation.⁴²

Western Australia was the only State Government to provide additional restructure assistance to complement the DSAP. That assistance is a combination of direct grants to farmers, grants to dairy processors and transfer of public assets to farmer owned companies. The purpose of this scheme, which has three components (business assessment, planning and implementation, and training), was to provide support for a managed transition to deregulated market.

The \$130 million being provided as direct farmer grants over eight years is equivalent to more than five times the annual impact of the reduction in market milk price resulting from deregulation (Table 2.4).

The Committee finds that:

Finding 8

The combined Federal and Western Australian Government restructure assistance totals \$150 million over 8 years compared with a reduction in income estimated at \$190 million over the same period.

⁴¹ Hough, G. (2003) Session 3, Transcript of evidence, 17 October 2003.

⁴² ACCC (2001) Impact of farm gate deregulation on the Australian milk industry: study of prices, costs and profits. Australian Competition and Consumer Commission, Canberra, ACT.

Table 2.3 Federal and State restructure assistance to dairy industry in Western Australia.

Program	Assistance
Dairy Structural Adjustment Program (Federal) ¹	\$108,000,000
Supplementary DSAP (Federal) ¹	\$14,000,000
Dairy Farm Assistance Program (WA) ²	\$12,000,000
Dairy Processing Incentive Scheme (WA) ²	\$11,000,000
Transfer of DIA assets to Dairy Western Australia ²	\$7,000,000
TOTAL	\$152,000,000

¹ Data from Dairy Adjustment Authority.

² Data from Department of Agriculture, Western Australia.

DSAP payments will be made quarterly over eight years, however many farmers have used bank loan facilities to convert them to an up front payment. They will have received about 75% of their total DSAP entitlement as a single payment in return for transfer of their quarterly payment rights to the bank.

Data from the Western Australian State Assistance Package shows that farm infrastructure and increasing dairy and beef herds were the major areas of investment immediately before and after deregulation. DSAP has less stringent reporting requirements so there are no data available on how dairy farmers have chosen to spend DSAP payments.

The Committee believes that the most appropriate uses for DSAP payments are:

- 1 Debt reduction;
- 2 Investing in improved productive capacity to enable profitable operation in a deregulated market; or
- 3 Investment to enable inter-generation transfer or industry exit.

The Committee believes that many Western Australia dairy farmers have used DSAP in these ways. However, DSAP payments have also been used for lifestyle expenditure or to supplement business cash flow. The Committee considers the former to be inappropriate. The latter may sometimes be necessary in the short-term, but is also a likely indicator that the farm business is not structured appropriately for long term viability.

The Committee finds that:

Finding 9

Average DSAP payments to Western Australian farmers are the highest per capita of any state. The only State Government to provide additional restructure assistance to complement the DSAP is Western Australia.

Farmers and consultants have identified that the payment methods for DSAP and the State assistance package have created taxation problems for farm businesses. The payments of restructure assistance to individuals rather than businesses has meant that payments cannot be offset against business losses for tax purposes.

Farmers who used an up front facility for DSAP payments have a continuing tax burden regardless of business conditions. Farmer eligibility for a range of Government benefits through Centrelink has been reduced as a result of the higher taxable incomes created by DSAP payments.

The Committee finds that:

Finding 10

State and Federal restructure assistance payments have created unintended barriers for farmers accessing social security payments.

The Committee recommends that:

Recommendation 1

Federal and State Governments need to frame future industry restructuring and assistance packages so that participants are not penalised through their taxation and social security entitlements.

The method of payment has also provided a windfall of about \$400 million to the Federal Government through income tax revenue.

Table 2.4 Distribution of Western Australian dairy farm, production and quota (1999/2000) and exits since deregulation.

Local Government Area	Production (ML)	% Quota ¹ production	Milking July 2000 ²	Milking July 2003 ²	% Exit	Est. Reduction in turnover per annum (\$ M)	DSAP paid (\$ M) over 8 years.	Av. DSAP paid (\$ M) per annum
Serpentine – Jarrahdale	14.9	45%	21	16	24%	1.01	3.60	0.45
Murray	16.4	48%	14	7	50%	1.18	2.62	0.33
Waroona	8.8	62%	17	9	47%	0.82	8.85	1.11
Harvey	91.0	61%	107	83	22%	8.33	32.69	4.09
Dardanup	29.3	53%	43	30	30%	2.33	9.98	1.21
Bunbury			1	1	0%	0.00	NA	NA
Capel	43.3	34%	37	29	22%	2.21	10.77	1.35
Busselton	62.9	21%	59	45	24%	1.98	14.32	1.80
Augusta-Margaret River	66.9	28%	60	46	23%	2.81	16.11	2.01
Donnybrook-Balingup	0.4	50%	1	0	100%	0.03	NA	NA
Bridgetown-Greenbushes	2.6	26%	4	3	25%	0.10	0.58	0.07
Nannup	3.2	39%	7	4	43%	0.18	0.74	0.09
Manjimup	44.1	21%	41	30	27%	1.39	9.38	1.17
Denmark	8.0	27%	10	6	40%	0.32	1.26	0.16
Albany	11.3	28%	8	7	12%	0.47	3.66	0.46
Plantagenet	8.2	28%	7	4	47%	0.34	2.25	0.28
TOTAL	411.3	38	428	321	27%	23.50	116.81 ³	14.60 ³

¹ Dairy Industry Authority of WA.

² Formal statistics on dairy farm businesses are no longer collected since the demise of the Dairy Industry Authority in July 2000. Farm numbers at July 2000 and July 2003 are based on Department of Agriculture estimates.

³ Payments made in listed Local Government Areas - excludes payments outside these areas - Dairy Adjustment Authority data.

2.6 Processors, wholesalers and retailers

The ACCC found that processors and retailers both had their margins on milk sales reduced after deregulation. The ACCC also noted that profitability in the processor sector was low compared to the national retail chains who have become the dominant force in the milk market since deregulation.

This is confirmed by the Committee's observation that both dairy farmers and processors appear to have been disadvantaged by the rapid falls in milk price that occurred in the months following deregulation. This situation has been particularly pronounced in Western Australia, where retail milk prices are considerably lower than the national average (this matter is considered in more detail in Section 3.2). Current retail milk prices may be unsustainable for other participants in the supply chain as well as for dairy farmers.

The Committee believes that while farmers and processors continue to survive on reduced margins, retailers have recovered much of this lost margin as retail milk prices have moved steadily upward since 2001 (see Fig. 3.2 and Fig. 3.3).

The Western Australian retail market is characterised by aggressive discounting of branded milk as a loss leader to increase store traffic and market share. Milk processors are drawn into this process with varying degrees of willingness. Peters and Brownes have made a public commitment to support farmers by refusing to engage in deep discounting. Other milk processors have not mirrored this.

The Committee finds that:

Finding 11

Current Western Australian retail prices have reduced margins for dairy farmers and processors, and will force more participants from the industry if higher returns are not achieved within the next year.

CHAPTER 3 IMPACT OF DEREGULATION ON THE SUPPLY OF MILK AND PRICE TO CONSUMERS

3.1 Farm exits and milk supply

More than 25% of Western Australian dairy farmers have left the industry since deregulation of the domestic market in July 2000 (Table 2.4). There are no data available to indicate what proportion of dairy farmers have left the industry for reasons of financial hardship compared to those who took advantage of the retirement or family succession opportunity provided by the restructure packages. Dairy farm numbers were declining before deregulation, and indeed have been declining for the past two decades.⁴³

There have been about 100 farmer exits in the 3 years since deregulation compared to 40 exits in the three years prior to deregulation. This level of departure from the industry is similar to other Australian states where further reductions in farmer numbers are expected.

The Committee finds that:

Finding 12

More than 25% of Western Australian dairy farmers have left the industry since deregulation of the domestic market in July 2000.

The Solutions Survey conducted by the Australian Department of Agriculture, Forestry and Fisheries in September 2002 found that 24% of dairy producers surveyed expected to retire or semi-retire within 5 years. This reflected the intentions of farmers in other Western Australian rural industries (Fig. 3.1). Only 15% of dairy farmers surveyed agreed or strongly agreed with the statement “the way things are I will be forced to leave the industry”. This highlights the deterioration in industry morale that has been created by the difficult circumstances of the last 12 months.

⁴³ ADC (2003) Australian Dairy Industry in Focus 2003. Australian Dairy Corporation, Southbank, Victoria.

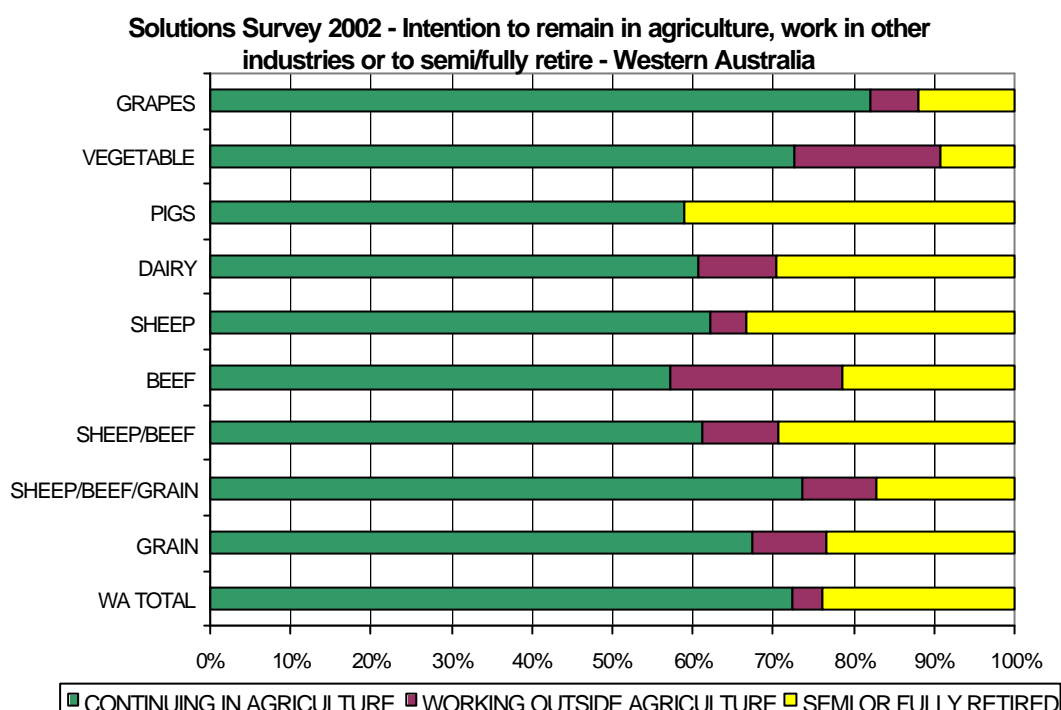


Figure 3.1 Exit and retirement plans of Western Australian farmers, Sept 2002.⁴⁴

Milk production in Western Australia has dropped by about 5% during the last three years compared to the last year before deregulation (Table 3.1). It is difficult to determine whether this is a consequence of deregulation or the difficult production conditions (high grain prices and drought in some areas) prevailing during that time. Demand has been strong for dairy cows and heifers, and prices generally higher than before deregulation. This reflects the expansion plans of many producers and the strong live export market.

The Committee finds that:

Finding 13

Milk production in Western Australia has dropped by about 5% since 1999/2000, with most of the reduction occurring in the first year following deregulation.

⁴⁴

AFFA (2003) 2002 Solutions Survey. Agriculture, Fisheries and Forestry Australia, Canberra, ACT.

Western Australian dairy exports have continued to grow since deregulation (Table 3.1); the volume of dairy products being shipped interstate has also increased. The continuing growth of exports over this tumultuous time probably reflects the fact that export market milk was already effectively operating independently of the quota system at the time of deregulation and providing viable returns to efficient export-oriented farmers.

Table 3.1 Milk production, gross value of milk production, and dairy exports from Western Australia, 1999-2003.

	99/00	00/01	01/02	02/03 ³
Milk production (ML) ¹	412	388	392	395
Gross Value (\$M) ²	144	103	113	117
Dairy Exports (\$M) ²	49	63	65	72

¹ Dairy Australia.

² WA Agri-food industry outlook August 2003.

³ Department of Agriculture Estimates.

The Committee finds that:

Finding 14

Western Australian interstate and international dairy exports have continued to grow since deregulation.

3.2 Consumer milk prices

Consumers and supermarkets have so far been the big winners from deregulation of the dairy industry, both at the national level and in Western Australia. Recent supermarket milk discounting has increased consumer benefits in Western Australia, but placed increasing financial pressure on farmers and processors. There has been no detrimental short-term effect on domestic milk supply.

Retail prices for milk and other dairy products are frequently lower in Western Australia than other Australian states. Prices for some dairy products are up to 20% cheaper in Western Australia than in their state of manufacture!

The Committee finds that:

Finding 15

Milk supplies have been maintained and consumers have gained short-term benefits from reduced retail milk prices in Western Australia.

The defining event following deregulation was the dramatic fall in the price of Woolworths Home Brand milk in spring 2000 (Fig. 3.1). Woolworths negotiated a spectacular reduction in wholesale price from NSW co-operative Dairy Farmers that saw the price of milk in 3 L packs fall below \$1.00/L. Woolworths' suppliers in other states, including National Foods in Western Australia, followed suit. Competing generic and branded milks followed Woolworths retail price down to maintain market share.

Western Australian supermarket milk prices fell by an average of about 20 ¢/L in the three months following deregulation. Price falls were larger for generic supermarket milk than for branded milk (Fig. 3.2).

Supermarkets have increased market share at the expense of other milk outlets since deregulation. There has also been a significant shift by consumers away from branded milks toward generic supermarket milk. Generic milks represented less than 25% of supermarket sales in 1999 but now command a market share of more than 70% at the national level. Market share for generic milks in Western Australia peaked at close to 60% in 2001 but then slowly declined to below 50%. Regular discounting of 2 L branded milk (Fig. 3.3) is likely to have played a major role in restricting the market share of generic milks in Western Australia. However it has also meant that average weekly supermarket milk prices in Western Australia are typically several cents per litre below the national average.

In the following three years this competitive behaviour has overridden any consideration of the longer-term sustainability of the dairy industry in Western Australia. The demand for cheap generic milk places continuing financial pressure on farmers and dairy processors. The weak market power of processors compared to retailers perpetuates this problem.

The Committee finds that:

Finding 16

Regular supermarket discounting has kept average prices for branded milks lower in Western Australia than the rest of Australia. This has reduced returns to farmers and processors from branded milk, but has reduced the market share of cheaper generic milk.

It is ironic that Roger Corbett, CEO of Woolworths, now sees the need for a national dairy summit to identify and address the industry's problems.

The Committee finds that:

Finding 17

The national tendering process for generic milk initiated by Woolworths has precipitated the "commercially driven crash" in milk prices and farm incomes that the Senate Rural and Regional Affairs and Transport References Committee warned against in 1999.

The pricing of fresh milk products in Western Australia is also reflected in the pricing of other dairy products (Table 3.2)

Data presented to the Committee indicate that many manufactured dairy products (including some manufactured in Victoria) sell for lower prices in Western Australian supermarkets than in Victorian stores belonging to the same chain. This depresses the retail price for locally produced dairy products and restricts the prices that processors can pay to Western Australian farmers.

The Committee was unable to conclude if this equated to dumping, but believes there is merit in further investigation by the ACCC to determine if this is in breach of section 46 of the *Trade Practices Act 1974*.

The Committee finds that:

Finding 18

Some dairy products manufactured in eastern Australia sell for lower prices in Western Australian supermarkets than in the same supermarket chain in their home state.

The Committee recommends that:

Recommendation 2

The Government requests the ACCC to determine whether the practice of selling dairy products in Western Australia at a substantial discount to the price in their state of manufacture constitutes dumping or anti-competitive behaviour.

Table 3.2 Comparison of pricing of dairy products from the same retailer in the same week (starting 1 September 2003) in different locations around Australia. (Bold figures highlight the lowest national price.)

Product	Qld	ACT	NSW	Vic	WA
Pura Milk 2 L	2.66	2.94	2.94	2.99	2.60
Pura Lite Start 2 L	2.97	3.54	3.54	3.49	2.97
Devondale Long Life 1 L	1.59	1.42	1.42	1.31	1.45
Bega Tasty Cheese 250 g	2.87	2.97	2.97	2.96	2.95
Pura Cream Pure 300 ml	(1.31) ¹	1.31	1.31	1.10	1.15
Ski D Lite 6 pack yoghurt	6.07	5.97	5.97	5.91	(5.65) ²
TOTAL	(17.47*)	18.15	18.15	17.76	(16.77²)

¹ Product not available at time of purchase - estimate included.

² Product out of stock at time of purchase - shelf price recorded and included here.

Qld store, Morningside - date 5 Sep 03

ACT store, Dickson - date 3 Sep 03

NSW store, Tumut - date 1 Sep 03

Vic store, Melbourne - date 2 Sep 03

WA store, - date 2 Sep 03

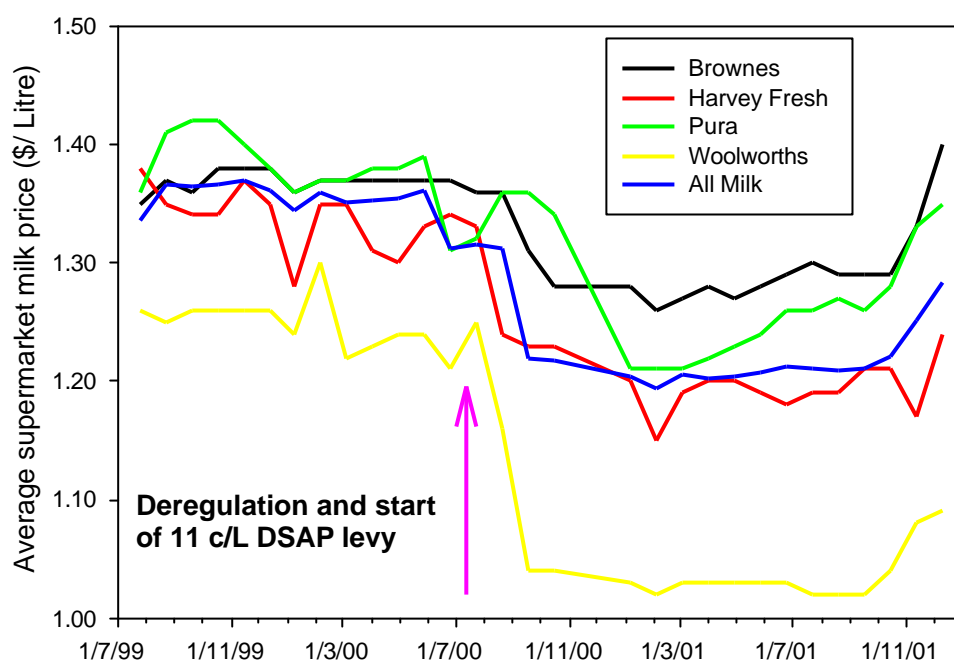


Figure 3.2 Supermarket milk prices in Western Australia: July 1999 to December 2001. (ACNeilson scan data from Dairy Western Australia)

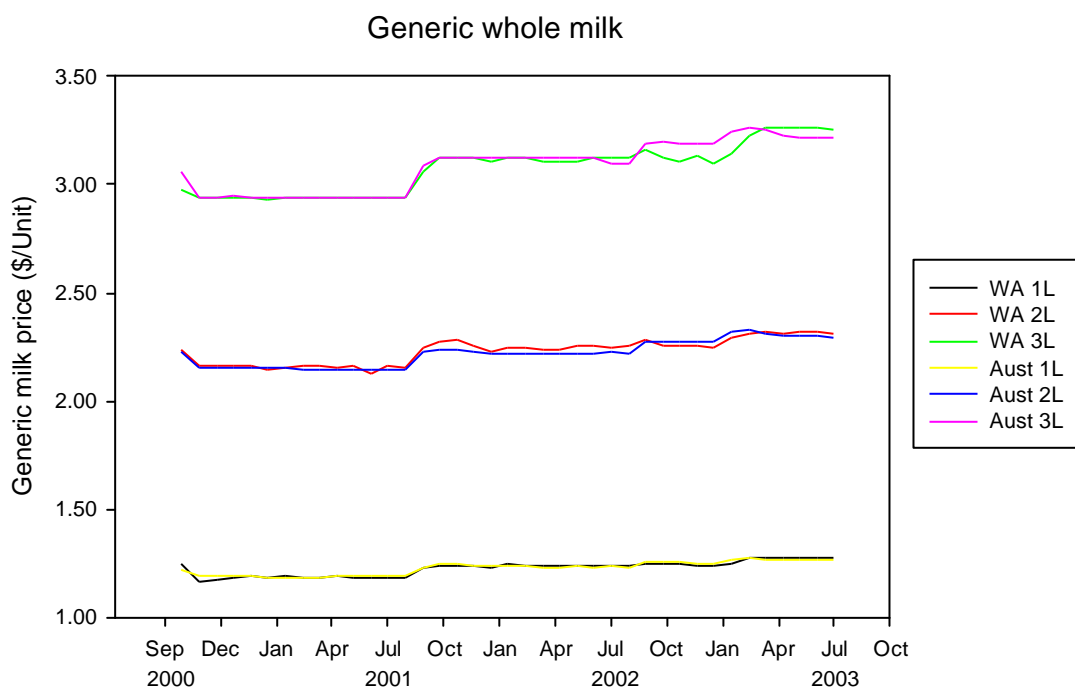


Figure 3.3 Generic milk prices September 2000 to July 2003. (Dairy Australia)

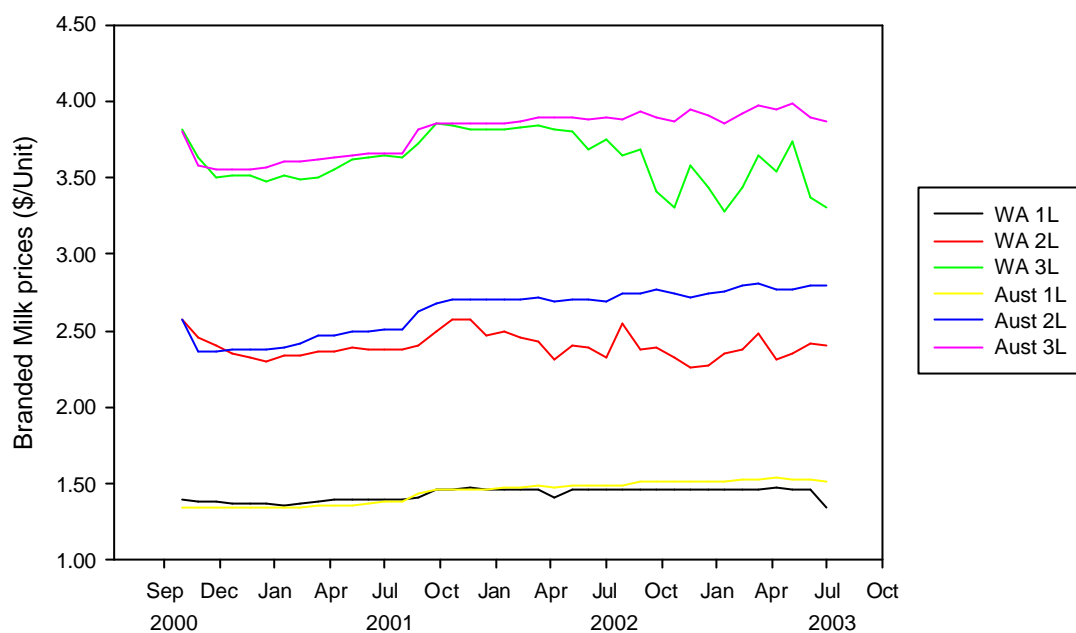


Figure 3.4 Retail prices for 1 L, 2 L and 3 L branded milk in Western Australian and Australian supermarkets. (Dairy Australia)

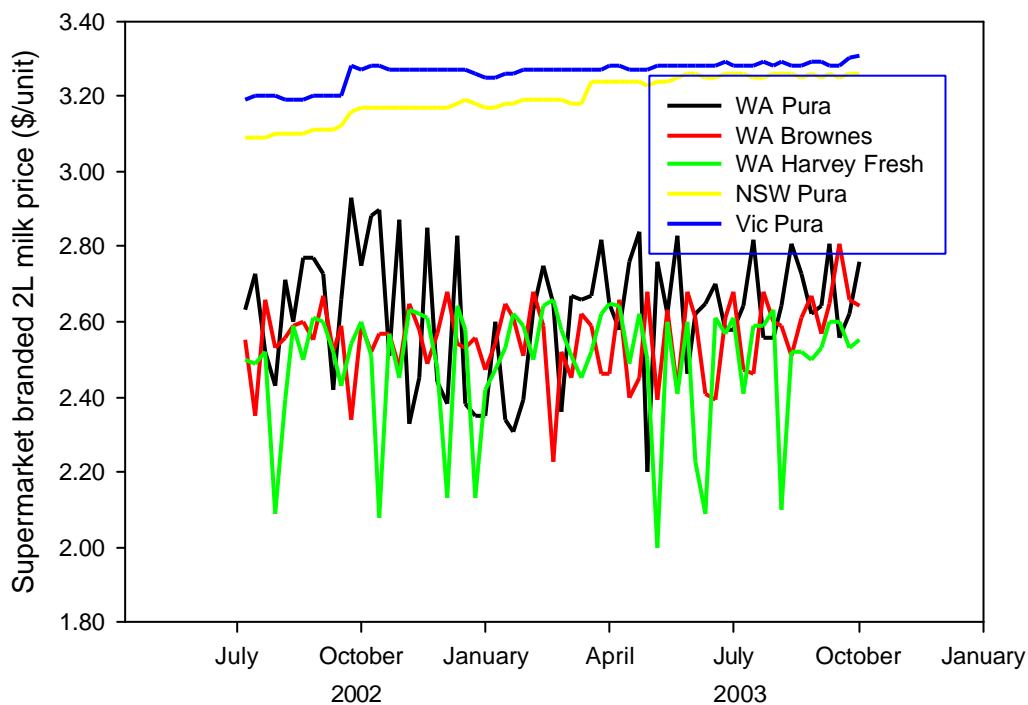


Figure 3.5 Supermarket 2 L milk prices for selected brands: July 2002 to November 2003. (Dairy Australia)

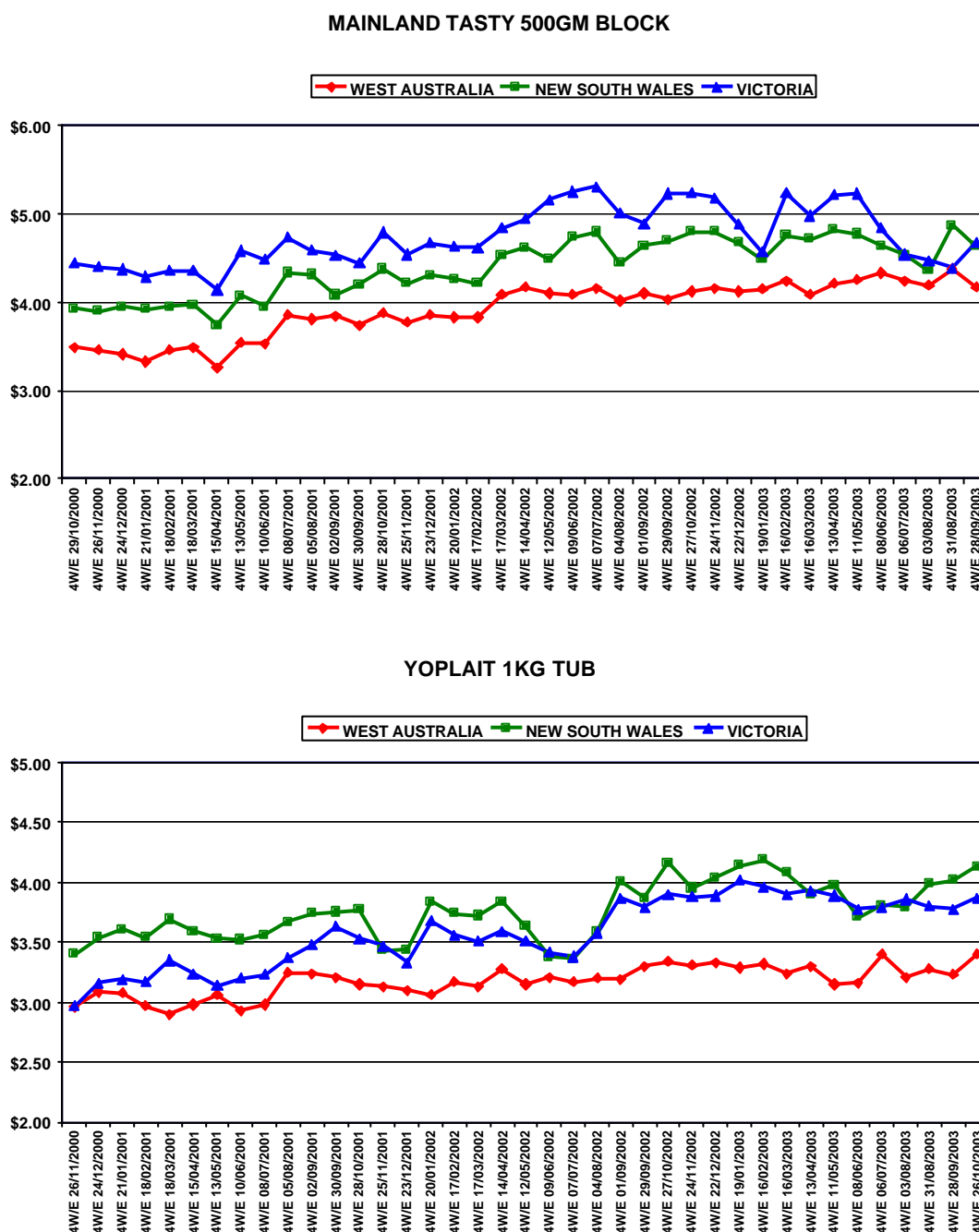


Figure 3.6 Monthly pricing of various dairy items in Western Australia, NSW and Victoria, October 2000 - September 2003.

The finding that milk is cheaper in Western Australia than in most of the country contrasts with the data presented by Australian Bureau of Statistics (ABS) in its November 2003 report on the cost-price index CPI for the September quarter.⁴⁵ The ABS reported that, based on 1 L packs, milk prices in Perth are the second most expensive of any capital city in Australia (Table 3.3). All the supermarket price data obtained by the Committee clearly show Perth milk prices to be the cheapest in Australia. While the ABS advises that figures are only approximate indicators of price levels for the items concerned, the Committee's evidence contradicts this conclusion.

The Committee considers that the use of 1 L packs by the ABS does not reflect the usual purchase by consumers. Two L units account for almost 50 % of sales by value; the 3 L unit is the next most important with almost 27 % of the market by value, with the 1 L accounting for only 22 % of sales.⁴⁶ This being the case, the Committee believes that the ABS approach should be reviewed to ensure it is including the most representative units of purchase in its assessment of the cost-price index for comparing the 'nation's shopping basket'. As stated, 2 L bottle is the most commonly acquired milk product by value, and it is using pricing of 2 L bottles that the Committee can demonstrate the reality that retail milk prices are lower in Perth.

Further, the Committee notes that if the intent of the CPI index is to provide a real indication of cost-price to consumers, and this figure influences decisions taken by a range of institutions, including the Reserve Bank when it considers the positioning of interest rates, then the variation is of some concern.

The ABS advised the Committee that the use of the 1 L milk carton in the ABS shopping basket was a historical artefact as the 1 L is the closest unit to the quart which was the original unit of pricing - it was suggested using this unit allowed a time series to be maintained

The Committee's discussions with the ABS have initiated a review of the national basket, and ABS have indicated they are considering including the 2 L and potentially the 3 L milk bottle in their CPI figures.

The Committee supports the contention made in several submissions that the retail market for milk and other dairy products is more competitive in Western Australia than in other states. Retail price data comparing the retail price of branded milks in Western Australia, Victoria and New South Wales (see Fig. 3.3). The frequent deep discounting of milk appears to be unique to Western Australia, with prices for both branded and generic milks being remarkably stable elsewhere.

⁴⁵ ABS (2003) Average retail prices of selected items - Eight Capital Cities, September Quarter, 2003. Catalogue 6403.0 [Released 5 Nov 03].

⁴⁶ Aztec Scan Data (2003) Data for period ending 6 July 2003.

Table 3.3 Average prices for selected items that are included in the Consumer Price Index (CPI) for the eight capital cities. (ABS).⁴⁷

Item	Perth WA	Syd NSW	Melb VIC	Canb ACT	Adel SA	Bris QLD	Hob TAS	Darw NT
Milk sales (1 litre)	164	155	157	144	157	159	148	182
Cheese, process, sliced, (500 g)	371	354	349	382	346	359	372	380
Butter (500 g) (a)	226	250	242	240	214	218	232	243
Biscuits, dry (250 g)	166	177	178	181	180	171	199	195
Breakfast cereal, corn (550 g)	351	326	312	336	320	337	362	328
Flour, self raising (2 kg)	398	379	390	404	352	343	270	349
Rice, long grain (1 kg)	210	187	211	195	194	192	217	212
Salmon, pink (210 g can)	266	240	231	279	234	256	296	252
Peaches (825 g can)	222	212	240	250	232	234	252	254
Pineapple, sliced (450 g can)	140	138	142	139	128	145	157	138
Peas, frozen (500 g pkt)	153	153	149	169	140	160	160	184
Sugar, white (2 kg) (e)	243	211	217	226	201	222	277	228
Jam, strawberry (500 g jar)	262	273	272	287	249	281	303	284
Teabags (180 g pkt)	367	350	373	367	340	357	445	370
Coffee, instant (150 g jar)	601	585	599	624	556	566	630	600
Tomato sauce (600 ml)	170	167	172	168	166	172	202	190
Margarine, poly-unsat'd (500 g)	232	231	236	242	222	235	248	245
Baked beans (420 g)	117	117	118	120	120	108	122	126
Baby food (120 g can)	76	73	74	78	71	72	84	77
Laundry detergent (1 kg)	529	524	497	562	505	536	573	487
Dishwashing detergent (500 ml)	339	343	345	352	331	350	359	350
Facial tissues (pkt 180) (f)	207	222	213	222	204	198	211	211
Toilet paper (4 x 250 sheet rolls)	291	290	299	299	286	282	304	302
Pet food (400 g)	104	105	107	119	99	110	118	103
Beer, full strength (24 x 375 ml bottles) (h)	3234	3206	3294	3135	3232	3054	3433	3466
Toilet soap (4 x 125 g)	251	254	252	239	277	247	274	251
Toothpaste (140 g)	229	232	230	235	232	240	237	258
TOTAL	9919	9754	9899	9994	9588	9604	10485	10265

Excludes fresh fruit, vegetables, meat and eggs. Excluded alcoholic beverages.

⁴⁷

ABS (2003) Average retail prices of selected items - Eight Capital Cities, September Quarter, 2003. Catalogue 6403.0 [Released 5 Nov 03].

The Committee considered the ABS report in detail and noted that Perth prices for a range of preserved goods that would most probably be sourced from eastern Australia are similar to Sydney and Melbourne prices. Notably, the ABS data reveal prices of selected preserved goods in Perth are similar to prices for the same goods in Melbourne or Sydney despite the burden of transport costs across the Nullarbor (Table 3.3).

In examining the Western Australian supermarket retail sector, the Committee have concluded that it appears to be the most diversified and competitive in Australia. The high proportion of independent supermarkets in Western Australia may be a consequence of a smaller rural population base in this State supports a greater opportunity for number of small independent supermarkets than may be the case in rural areas of the eastern states of Australia. In addition, retailers reputedly use milk as a ‘loss leader’ to attract customers into their stores. Industry data indicates the independent grocery sector is most likely to use milk in this way.

These conclusions appear to offer the best explanation for the fact that dairy goods imported from eastern Australia are actually cheaper in Perth supermarkets suggesting product may be being dumped into Perth’s small retail market.

The Committee finds that:

Finding 19

The retail sector in Western Australia is unique and appears to be the most aggressively competitive in Australia. This has been a significant cause in Western Australian dairy farmers receiving Australia’s lowest farm gate milk price.

Generic promotion of Western Australian milk ceased with the abolition of the Dairy Industry Authority in July 2000. Promotion of dairy products is now the responsibility of milk processors, although the State Government supports the promotion of products made in Western Australia through the Department of Industry and Resources’ “Buy WA” campaign.

The Committee is aware that one processor supplements some fresh white milk products with powder while stating on the milk container that the product is made in Western Australia, and that the product is labelled as ‘fresh’. As milk powder is not produced in WA, supplementing the product with milk powder means the milk is no longer wholly WA grown. In addition, using powder as a component of a reputedly ‘fresh’ product (when the same product can be made entirely with fresh milk) is misleading. The Committee believes that consumers make a choice in buying ‘fresh’ product (as opposed to UHT or other milk products), and would prefer to buy fresh, locally produced milk.

The Committee recommends that:

Recommendation 3

The Government ensures that dairy products eligible for promotion through the State's "Buy WA" campaign must use milk components derived exclusively from Western Australia, unless those components are not produced in the State.

Recommendation 4

The Government ensures that food labelling requirements more adequately define the use of the word 'fresh' so that a product cannot be labelled as 'fresh' if it is made from reconstituted products.

CHAPTER 4 REFORMS TO ENHANCE THE SUSTAINABILITY OF THE DAIRY INDUSTRY

4.1 Introduction

The Committee sees two possible futures for the Western Australian dairy industry.

The first is to adopt a domestic market focus that would see production contract to the 150 to 200 million L required for domestic consumption. This would inevitably bring a substantial contraction in farmer numbers. The largest 40% of Western Australian dairy farms produce more than 80% of the State's milk. It is therefore possible that movement toward a domestically focused industry could see the State's total milk requirement satisfied by fewer than 80 farms.

The attraction of a domestically focused future for the Western Australian industry is based on the price premium historically paid for domestic milk. The supermarket tender process has seen that premium reduced by more than half since deregulation. The sale of milk by Aldi supermarkets at an everyday price substantially lower than their competitors suggests that there is a risk of continuing erosion of the remaining market milk premium.

Supermarkets are likely to continue to put downward pressure on that premium in the absence of Government intervention or countervailing price pressures from other markets. The rapid progress of technologies extending the shelf life of dairy products and reductions in production and transport costs mean that local markets cannot be isolated from competition. This implies that the Western Australian Government would have difficulty in regulating a price premium to farmers for market milk.

The alternative future would build upon the State's existing dairy export capacity to enable growth by the industry and individual businesses. The Western Australian Government's vision of industry expansion and export growth was the rationale for the establishment of the \$27 million State Dairy Assistance Package in 2000.

Decisions taken by industry stakeholders and the nature and extent of government assistance to the industry over the next few years will decide the path that industry follows. Both government and industry must be certain of their vision for the industry's future when contemplating government's future role.

The Committee supports the Dairy Industry Working Group's conclusion⁴⁸ that export growth in high value markets is the preferred future for the Western Australian dairy industry. World demand for dairy products is predicted to outstrip supply so there are good long-term prospects for export growth⁴⁹. No other scenario offers the opportunity for industry and individual business growth and a milk price that exceeds base commodity levels. The Committee believes that both these things are essential for a sustainable industry.

The Committee finds that:

Finding 20

Increasing efficiencies are the key to the sustainability of the Western Australian dairy industry in both domestic and export markets.

Any intervention by Government has the potential to profoundly influence the industry toward contraction and a domestic market focus or potential growth through exports. The desired future for the industry must be a key consideration when formulating any policy of market intervention.

The Committee recommends that:

Recommendation 5

Government intervention in the dairy supply chain must adhere to the following principles:

1. Intervention is made on the basis of measurable industry outcomes. These must advance the industry's strategic goals, and not support the retention of inefficient or outmoded business practices; and
2. Any intervention must not weaken the competitiveness of Western Australian processors in either interstate or overseas markets.

⁴⁸ Dairy Industry Working Group. (2001) A healthy WA dairy industry – let's do it! WA Department of Agriculture, South Perth.

⁴⁹ Anon. (2000) Global Focus Dairy. Primary industry Bank of Australia, Sydney.

The Committee received a number of submissions suggesting that trading of milk between dairy processors undermines the ability of farmers to obtain premium prices for domestic milk. This may be the case if milk ostensibly purchased for commodity manufacturing is transferred to high value end products without sharing premiums with farmers.

However the Committee believes that there are important opportunities for the whole dairy industry in greater collaboration between dairy processors to reduce duplication of infrastructure and maximise the value of the product mix derived from the available milk. For example, Western Australia has two under utilised cheese plants rather than a single, capital efficient facility. The Committee suggests it would be more profitable to transfer milk to one of Western Australia's under utilised UHT milk production lines than to sell commodity cheese onto a depressed market. Co-operation by processors to find shared profit in export markets would benefit all, and in the Committee's view, would not contravene the provisions of the *Trade Practices Act 1974* regarding collusion in domestic markets.

The Committee has also heard evidence that there are real opportunities for farmers to increase the efficiency of capital investment by sharing dairy facilities, installation of 3-phase power,⁵⁰ or other high value capital items. There are also untapped opportunities for cost savings through co-operative purchase of inputs such as grain.⁵¹

The Committee finds that:

Finding 21

Co-operative purchasing, infrastructure development and production practices by Western Australian dairy farmers will increase farm efficiencies.

The Committee recommends that:

Recommendation 6

The Government facilitate the farm and processing sectors to develop a more collaborative approach in order to increase their efficiency.

⁵⁰ Brand, A. & E. (2003) Session 2, Transcript of evidence 17 October 2003

⁵¹ Knott, S. (2003) Session 1, Transcript of evidence 17 October 2003

Recommendation 7

The Government initiate a research and development partnership with industry to assist dairy farmers to reduce their costs and develop strategies for change relevant to different dairy regions and farm business circumstances.

Recommendation 8

The Government convene a dairy stakeholders council to improve access to and use of processing infrastructure, and to assess options to increase flexibility of product mix in response to market opportunities.

Recommendation 9

The Government directs Western Power Corporation to cost 3-phase power projects to dairy customers on the basis of district infrastructure investment that anticipates further local power system upgrades by neighbours.

The Committee recognises that Dairy Western Australia is a farmer owned company and its shareholders, not Government, are responsible for its future. However, the Committee notes Dairy Western Australia's has a unique status as an organisation able to claim the membership of all active dairy farmers in Western Australia. That, and its function as an investment company endowed with the assets of the former Dairy Industry Authority, place Dairy Western Australia in a unique position to make strategic investments that are backed by a shared industry vision.

Dairy farmers would be well advised to take advantage of the opportunities that Dairy Western Australia presents to the dairy farmers as a whole. It is the Committee's view that investment in the transport chain would provide the single best return to Dairy Western Australia shareholders.

A number of industry stakeholders have identified inefficiencies in the transport system between farm and factory as a major cost to industry. It has been suggested that a single transport company of the type operating in South Australia could save more than 1 cent per litre in costs for some companies.

The Committee recommends that:

Recommendation 10

The Government invites Dairy Western Australia and other industry stakeholders to participate in a feasibility study into development of a dairy transport services company.

The Committee received a number of submissions suggesting that the domestic milk market be re-regulated to provide income security for dairy farmers.⁵²

State government powers to vest milk in a single entity, set milk prices or otherwise intervene in the milk market ended with the repeal of the *Dairy Industry Act 1973* and *Dairy Industry Regulations 1977* in July 2000. Legal advice to the former Dairy Industry Authority (DIA) identified vesting, price control and quota barriers to market entry as contrary to National Competition Policy (NCP). Any legislation proposed to re-introduce such measures in Western Australia would be subject to NCP review. The slow pace of agricultural reform, combined with the failure to demonstrate net public benefits from continued regulation, has been reported as a factor in the decision to withhold \$40 million in annual competition payments from Western Australia.

Re-introduction of Government controls on the milk market has the potential to make Western Australia a less attractive environment for investment in milk processing. Increasing the local cost of manufacturing milk (through either direct price increases or increased transaction costs) could make the local production of cheese or yoghurt unprofitable. Food processors are national companies with the ability to relocate manufacture of nationally transported products to reduce input costs.

The Committee finds that:

Finding 22

In the absence of net public benefit being demonstrated, reintroduction of market milk regulation would breach Western Australia's obligations under National Competition Policy. It would also be inconsistent with the State-Commonwealth agreement establishing the basis for the \$1.94 billion Dairy Structural Adjustment Program.

⁵²

Various submissions. A. Green & M. Palmer; Australian Milk Producers Association W.A.; M. Papalia; and J. Tartaglia.

Several submissions were made to the Committee either supporting or opposing the establishment of a single desk milk marketing arrangement as an alternative to full market regulation.

The Committee believes that a mechanism for dairy farmers to control milk supply via a single desk already exists in the form of Challenge Dairy Co-operative or Dairy Western Australia. A dairy industry that was united in its desire for a single desk could choose to sell all milk to Challenge without the requirement for legislation.

The Committee finds that:

Finding 23

A united dairy industry could implement a single marketing desk now without statutory backing.

The Committee recommends that:

Recommendation 11

The Government facilitates exploration of a single marketing desk as a basis for improving collective bargaining practices by dairy farmers.

It has been suggested to the Committee that the Government should restrict the sale of interstate milk or dairy products to increase the consumption of locally produced goods.

The Committee understands that the Western Australian Government does not have the Constitutional power to impose either a GST on food or a retail levy on milk. To do so would breach Section 90 of the Constitution. The Federal Government has the power to collect revenue in these ways, but is unable to do so in a way that discriminates between states. Any such tax or levy would therefore have to be applied to milk produced in all states of Australia.

The Committee does not believe that the Federal Government would support a new tax or levy on milk in addition to the existing 11 ¢/L Dairy Industry Adjustment Levy. The Committee makes no recommendations regarding levy collection by the Commonwealth.

The Committee finds that:

Finding 24

State governments do not have the constitutional power to impose a tax or levy on retail milk sales as a farm income supplement.

There is currently no price incentive for processors or supermarkets to buy milk interstate. Industry sources indicate that it would cost between 8 - 10 ¢/L to transport fresh milk from the eastern states to Western Australia.⁵³ A significant increase in the cost of milk to processors could create demand from processors or supermarkets for interstate milk. The former regulated arrangements discouraged movement of milk between states by agreement between State governments supported by the “comfort clause” of the Domestic Market Support Scheme. Those mechanisms no longer exist to protect the borders of any state reintroducing milk market controls. Any legislation excluding or setting prices for interstate milk could be subject to challenge under Section 92 of the Constitution, which mandates free trade between Australian states.

The Committee finds that:

Finding 25

Government does not have the constitutional power to restrict trade in interstate dairy products.

There have also been suggestions that the Western Australian Government should impose a minimum farm gate, wholesale or retail milk price. While State governments have price setting powers under the Constitution, there is no existing legislation providing for a fixed milk price. New legislation to increase government involvement in milk price setting is unlikely to pass review by the National Competition Council.

⁵³

Submission N. Thomson, Department of Treasury and Finance.

The Committee finds that:

Finding 26

Demonstrating a net public benefit from the introduction of a minimum wholesale or retail price would be necessary to comply with Western Australia's obligations under National Competition Policy.

As discussed in Chapter 1, per capita consumption of fresh milk is declining in Australia. Growth in the domestic milk market is unlikely to provide significant growth opportunities for the Western Australian dairy industry. Government therefore needs to look beyond the domestic milk market when developing strategies for a sustainable dairy industry.

The Committee finds that:

Finding 27

The Australian domestic milk market is unlikely to grow on a per capita basis, although there appears to be opportunities for growth in domestic consumption through value-added dairy products.

Low morale in the Western Australian dairy industry reflects both ongoing structural issues associated with farmers' loss of market power following deregulation and the impact of difficult conditions during 2002/2003 on business cash flows. However the current dairy industry crisis could also be considered a crisis in confidence regarding the future of the Western Australian export market and the uncertainties of whether Western Australian producers and processors can compete in the international marketplace, and what price will farmers be paid for milk for those markets.

The Committee has observed a clear division within all sectors of Western Australian dairy industry between those who see all milk production above and beyond the immediate domestic market requirement as a liability that drags down average milk prices and those that want to see increased production as the driver for a future based on export growth. One of the greatest challenges for industry leaders and policy makers is the difficulty of articulating a clear industry vision that accommodates both of these seemingly irreconcilable views. Yet without such a clear vision it is difficult to see how industry can be effective in making its real needs, as opposed to a wish list of wants, known to Government and equally difficult for Government to respond effectively.

The Committee finds that:

Finding 28

Low morale, a lack of unity among dairy farmers and an absence of a common vision across the industry as a whole, are fundamental challenges to the sustainability of the Western Australian dairy industry.

The Committee note that experience since deregulation has shown that it is difficult to consistently achieve satisfactory returns from the export dairy market through sales of the traditional dairy commodities of butter, cheddar cheese and skim milk powder. Europe, New Zealand and Australia are the largest suppliers to these markets. The international price of all these commodities is heavily influenced by the anti-competitive behaviour of the European Union and United States. Western Australian processors also lack the economies of scale to extract the same level of profit (and hence farmer returns) from these commodities as their competitors in New Zealand and Victoria.

The reality of the global market is that commodity prices are unlikely to improve much in the short term, with the US and EU holding skim milk powder stocks equivalent to four years Australian production. In addition, with the size of EU production and the accompanying subsidies that EU dairy farmers receive, Western Australia dairy processors would be well advised to focus on products that are not influenced by international subsidy.

The Committee finds that:

Finding 29

Consistent satisfactory returns from the export dairy market are difficult to achieve from the sale of traditional dairy commodities such as butter, cheddar cheese and skim milk powder because of price distortions caused by subsidies in the EU and trade barriers in the USA.

Export success for Western Australia depends upon the identification and development of high value markets and products that build on the State's competitive advantages rather than increased exposure to commodity markets. Government needs to support research and development in partnership with dairy processors to develop new high value dairy products for export, and explore synergies between dairy and other liquid food processing and manufacturing.

The Committee finds that:

Finding 30

Sustaining and developing the Western Australian dairy industry will depend on the industry's capacity for export and product diversification. This will succeed if growth is focussed on high value products rather than commodity exports.

The Committee recommends that:

Recommendation 12

The Government support institutional arrangements to stimulate Western Australian dairy exports, especially high value-added products. These arrangements must include:

1. A study to clearly define Western Australia's sustainable competitive advantages and to develop a strategy and marketing plan to maintain and exploit those advantages;
2. Using the resources of the Government, including Western Australia's trade offices, to advance business relationships in Western Australia's existing and future dairy markets;
3. Facilitating industry development of an increased range of products for new and existing markets;
4. Conducting a feasibility study of broadening the scope of the Wine Industry Centre for Excellence to include dairy and other liquid foods; and
5. Increased collaboration between Western Australian exporters to improve their efficiency in servicing key markets.

Western Australia's diverse product range, regional position, and long standing business relationships with South-East Asian countries will continue to provide opportunities to supply Asian markets with quality dairy products. Local processors are at the leading edge of technology in the transport of fresh and extended shelf life milk products. Like other Oceanic exporters, Western Australian processors have increasingly focused on value-added milk processing and specialist dairy products for clients. Importantly the industry has a demonstrated track record in producing world-class products for this market including ice cream, cheese and yoghurt.

Western Australian milk enjoys a number of important quality advantages over milk produced elsewhere in Australia or New Zealand. Western Australian milk has the

highest microbiological quality of any Australian state. It is the milk lowest in the “oceanic” flavour or cow taint associated with grass based production systems, and is therefore preferred in some Asian markets. There is also the opportunity to exploit the relative “whiteness” of Western Australian milk in products for Asian markets.

Ultimately however, to enable sufficient scale in research and development and marketing, partnerships may be required with major Oceanic companies, such as Fonterra. Furthermore, large buyers are increasingly reluctant to maintain long term relationships with smaller companies who may not have the scale and resources to meet future market requirements.

The Committee finds that:

Finding 31

Western Australian milk is recognised for its exceptional quality and is preferred in Asian markets because of its superior flavour. There is real potential to capitalise on the whiteness of WA milk.

Competing in selected export markets with higher value-added products will involve increasing investments in new product development and producers will need to continue to invest in supply relationships to have sufficient market power. These relationships may be directly with in-country partners as in the case on the Sanyuan Challenge joint venture. In today’s global market, such processing businesses are very small and do not have the economies of scale to be competitive in base dairy products. However these direct relationships with specific end markets may enable small, ‘niche’ producers to dance between the feet of the giant dairy businesses. Milk quality and flavour are key advantages. To be successful they will need to be innovative and focus on higher value-added products, and also ensure that farmer shareholders continue to have sufficient investment in the business to command adequate end point returns.

The Committee finds that:

Finding 32

Competing in selected export markets with high value-added products will require increased investments in new product development. Western Australian producers will need to continue development of supply relationships to have sufficient market presence and power.

In summary, the Committee concludes that the State Government's obligations under National Competition Policy effectively preclude the introduction of regulation or other legislative intervention in the milk market. No legislation with the intent of increasing the level of government control over the milk market would be likely to be approved by the National Competition Council.

The Committee notes the severe limitations that National Competition Policy place upon state governments' ability to intervene in markets where acute imbalances in market power exist. This must increase the responsibility of the Federal Government to ensure that the ACCC acts decisively and effectively to prevent abuses of market power by dominant players in the inevitable period of adjustment and uncertainty that follows deregulation of a protected industry. The Committee does not believe that the Federal Government has adequately fulfilled this responsibility in the case of the dairy industry.

The Committee finds that:

Finding 33

The Federal Government has a clear responsibility to ensure that the ACCC acts effectively to prevent abuses of market power by dominant players in the period of adjustment following deregulation. The Federal Government has not adequately fulfilled this responsibility in the case of the dairy industry.

Dairy deregulation has created severe economic stress in rural communities with relatively narrow economic bases. ABARE identify the Shires of Harvey, Waroona and Capel as vulnerable communities in Western Australia. Federal Government should use some of the tax windfall generated from the DSAP package to provide additional assistance to the communities worst affected by deregulation.

There is an urgent need for the Council of Australian Governments to determine what actions can be taken to assist communities affected by deregulation within the restrictions imposed by National Competition Policy.

The Committee finds that:

Finding 34

The Federal Government could use some of the estimated \$400 million tax windfall generated from the DSAP package to provide additional assistance to communities adversely affected by deregulation.

The Committee recommends that:

Recommendation 13

The State Government urge the Federal Government to use part of the tax windfall created by the DSAP to provide additional assistance to rural communities adversely affected by deregulation.

The Committee finds that:

Finding 35

The most effective contribution Government can make to a sustainable dairy industry in a competitive market will be through its scientific and trade resources to increase the participation and competitiveness of Western Australian dairy exporters.

CHAPTER 5 EQUITABLE PARTICIPATION BY ALL INDUSTRY STAKEHOLDERS

The key issue restricting equity of participation by all dairy industry stakeholders is the enormous imbalance of market power between farmers, processors and retailers. Supermarkets have used their immense market power to increase the market share of their generic milk brands and to drive wholesale milk prices to unprecedented lows.

Dairy processors and supermarkets gained market power at deregulation. On the other hand, dairy farmers have had their power in the marketplace diminished. The competition unleashed between processors to secure high volume generic milk contracts with supermarkets has not been matched by competition between processors for farmers' milk.

Industry institutions that were adept at influencing Government and state marketing authorities to increase market milk prices have proved less successful in commercial negotiations. Supply chain relationships in the Western Australian domestic milk sector are yet to mature in a way that leads to price negotiations being conducted in a manner that protects the interests of all partners in the chain.

Deregulation has accelerated rationalisation of the Australian milk-processing sector as processors seek to gain economies of scale and expand market share. The scramble for market share has seen intense competition between dairy processors for the large volumes of milk sold through supermarket house brands. These generic milks account for nearly 50% of supermarket milk sales in Western Australia over most of the last year and more than 70% at the national level. Processors now find themselves in a dominant market position compared to farmers but vulnerable to the greater clout of the supermarket chains.

Evidence presented to the Committee suggests that much of the market risk in the supply chain has been transferred to the farm level. Milk processors have been successful in transferring increased costs to their supermarket customers and in turn to consumers. For example, National Foods have received a series of wholesale price rises from Woolworths during the last year. None of those increases in price have been passed back to farmers.

The Committee finds that:

Finding 36

Much of the market risk in the dairy supply chain has been transferred from retailers and processors to dairy farmers.

Indeed the available data show continuing downward pressure on farm gate milk prices since deregulation in July 2000. This is understandable in the case of the export market, where international commodity prices and movements in currency values exert a major influence on returns. It is less obvious why this should be the case for domestic milk.

The Committee accepts that the large falls in wholesale milk price in late 2000 were passed on to the consumer, and that retail margins as well as farm gate prices were reduced. However the Committee also believes that processor and retail margins have increased since January 2001 at the expense of continued falls in farm gate price and reduced consumer benefits from deregulation.

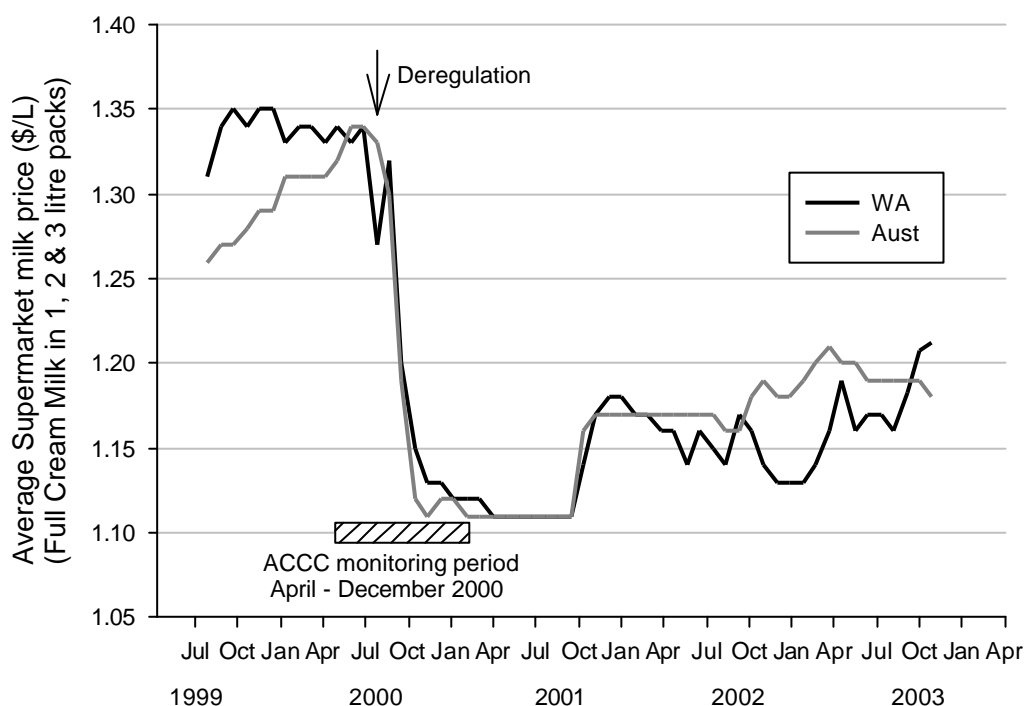


Figure 5.1 Average prices for all milk sold in Australian and WA supermarkets.

The ACCC concluded in April 2001 that farm gate, wholesale and retail margins had all fallen as a result of the dramatic fall in retail milk price that occurred in both Western Australian and national supermarkets precipitated by the Woolworths-Dairy Farmers generic milk contract (Fig. 5.1). The monitoring period on which the ACCC based its conclusion that supermarkets had not profited unduly from deregulation ended when retail prices were still declining to their lowest point during deregulation.

These data clearly show a trend of increasing milk prices at the national level following cessation of monitoring by ACCC. Farmgate prices for milk have declined rather than increased over the same period.

The Committee finds that:

Finding 37

The national tendering process for generic milk contracts initiated by Woolworths in 2000 continues to reduce the profitability of milk processors and dairy farmers throughout Australia.

The Committee concludes that much of the retail margin on milk that was lost by supermarkets in the months following deregulation has been regained through increases in retail price. The benefits of increasing consumer prices have been shared by retailers and processors to the exclusion of farmers.

The Committee believes that the ACCC should be concerned that market power is being used to increase retailer margins while farm gate prices are declining. The Federal Government should be concerned that the *Trade Practices Act 1974* has failed to protect vulnerable dairy farmers during a difficult period of adjustment.

The Committee finds that:

Finding 38

Much of the retail margin on milk that was lost by supermarkets in the months following deregulation has been regained through increases in retail price. The benefits of increasing retail prices have been shared by retailers and processors, but not by dairy farmers.

Finding 39

It is the ACCC's responsibility to monitor the use of market power by retailers in pursuit of market share and margin. The *Trade Practices Act 1974* has failed to protect dairy farmers during the adjustment following deregulation.

Western Australian dairy processors have attempted improve milk prices by reducing retail discounting of branded milk. Peters and Brownes , in particular, has spoken out

against retail milk discounting, and passed 30% of a retail price increase back to farmers. The average Western Australian supermarket price of both Brownes and Pura milk have increased in the last few months (see Fig.3.5). Intensity of discounting by Harvey Fresh has been reduced over the same period. As a result, the weighted-average price of supermarket milk in Western Australia has been higher than the national average in consecutive months for the first time in nearly two years (Fig. 5.1)

However, the rising price of branded milk has created a jump in market share for generic milk of about 10 % (Fig 5.2).

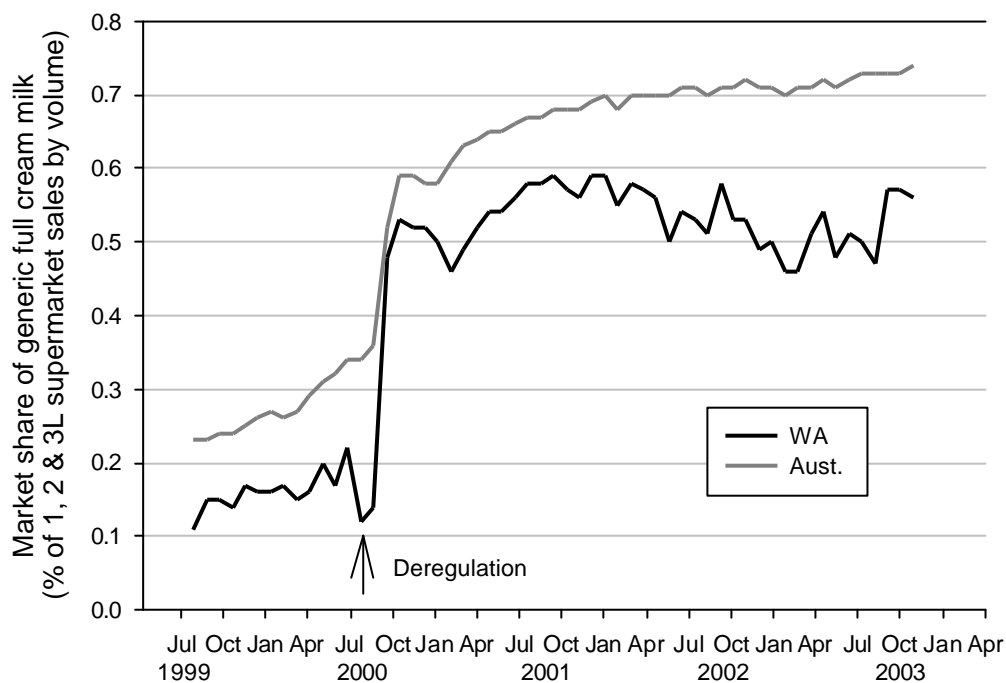


Figure 5.2 Market share of generic milk in Western Australian and Australian supermarkets.

The Federal Government should direct the ACCC to resume monitoring of margin distribution within the supply chain for liquid milk. This will provide some much needed transparency to milk price negotiations and bring legal and moral pressure to bear to prevent exploitation of farmers by their more powerful partners.

The CEO of Woolworths has identified trade practices legislation as a barrier to co-operative action by supermarkets to raise retail prices and provide an increase in milk price to farmers. Federal Government should direct the ACCC to provide advice on possible mechanisms to provide a “safety valve” mechanism that will permit milk prices to be raised to a sustainable level without risk of prosecution under the *Trade Practices Act 1974*.

The Committee recommends that:

Recommendation 14

The Western Australian Government request the Federal Government to direct the ACCC to:

1. Resume monitoring of margin distribution within the supply chain for liquid milk. This will provide some much needed transparency to milk price negotiations and bring legal and public pressure to prevent exploitation of farmers;
2. Determine whether the practice of negotiating milk tenders on a national basis is an unfair restriction of trade on those processors who only trade in one state; and
3. Provide advice on possible mechanisms for raising retail prices that increase margins through the industry chain to dairy farmers that will not be subject to prosecution under the *Trade Practices Act 1974*.

The Committee accepts that the price for milk supplied on a least cost seasonal basis is set in the international marketplace. However, the Committee also supports the contention that processors, and ultimately the consumer, should expect to pay a premium price for milk delivered on 365 days of the year. This recognises the increased production costs associated with an extra two months production at the least favourable time of the year. The Committee agrees with the findings of Dr Glenys Hough that the current level of year round supply premium is unsustainable on many Western Australian dairy farms.⁵⁴

In their 2001 report the ACCC observed that:

“Ultimately, as consumers are prepared to pay a premium for fresh milk, processors will have to pay farmers a sufficient return to guarantee a reliable supply if dairy farmers are not to exit into other areas of agricultural production.”

The Australian dairy industry has clearly reached the point where many farmers are close to making the decision to exit. This will not be confined to inefficient producers who are incapable of making the adjustment to a deregulated marketplace. Many more efficient producers are questioning whether current returns justify the long hours and 365 day per year demands of dairy farming.

⁵⁴

Hough, G (2003) Session 3, Transcript of evidence, 17 October 2003.

This has serious implications for investment in the industry's productive capacity by existing farmers or potential new entrants. Dairy farmers who have made large investments in milking sheds or other dairy specific infrastructure are likely to remain. However, those farmers whose dairies are fully depreciated or require significant reinvestment are increasingly likely to consider the options available in other industries. The Western Australian industry cannot afford to lose efficient but disillusioned farmers from its small production base.

The Committee finds that:

Finding 40

The Western Australian industry must retain a critical mass of efficient dairy farmers so that its small production base is not further diminished.

The Committee rejects the suggestion made by a national retail chain that they are price takers in the dairy market and have little market power in determining either the wholesale or farm gate price of milk. The Committee believes that supermarkets need to acknowledge that their powerful position in the supply chain brings a responsibility to ensure that their price negotiations are not conducted to the detriment of third parties. The Committee urges supermarkets to work with Government and the ACCC to develop mature supply chain price setting mechanisms that promote the long-term viability of the retail, processor and farm sectors.

The Committee finds that:

Finding 41

Supermarkets have a powerful position in setting prices along the supply chain and need to temper current "loss-leader" discounting behaviour to move to long-term sustainable prices. The Federal and Western Australian Governments and the ACCC also need to develop supply chain price monitoring mechanisms that promote the long-term viability of the retail, processor and farm sectors.

The Committee recommends that:

Recommendation 15

The Government request the ACCC to find ways to improve transparency in supply chain transactions and equity of participation in supply chain negotiations for market milk.

The Committee notes that dairy farmers differ widely in the degree of satisfaction that they obtain from their relationship with their milk processor. Milk prices vary between processors, but non-price factors are also significant. For example National Foods demands most of its milk during the summer and autumn months when production costs are highest. Peters and Brownes allow farmers to adopt whichever supply pattern best suits the needs of their business. Companies also differ in their attitude toward suppliers who want to grow their businesses by selling more milk. Companies also offer different levels of technical support to their producers.

The Committee shares industry concerns that some milk supply contracts are unfairly weighted in favour of the processor. The Committee believes that contracts offered to farmers by one processor are particularly worthy of scrutiny by the Australian Competition and Consumer Commission to ensure that none of their provisions constitute unconscionable conduct or other abuses of market power.

The Committee recommends that:

Recommendation 16

The State Government request the Federal Government make changes to the *Trade Practices Act 1974*, particularly to make unconscionable conduct provisions more readily actionable by the ACCC.

5.1 Collective negotiation

The need for effective collective action by dairy farmers to counter the market power of processors and retailers has been clearly articulated by industry organisations and governments since before deregulation. This need has been recognised by the Collective Bargaining Authorisation granted by the ACCC and in the reforms to the *Trade Practices Act 1974* recommended by the Dawson review. However, the ACCC's authorisation precludes dairy farmers from withholding supply.

It is the Committee's view that this is unreasonable and reduces the market power of dairy farmers.

The Committee is also of the view that the ACCC is being selective in the application of this aspect of competition policy as there are other sectors of the Australian economy subject to restrictions that are not in the public interest such as labour and other contracted services.

The Committee finds that:

Finding 42

The ACCC has denied dairy farmers the right to withhold supply reducing the negotiating power of dairy farmers.

Western Australian dairy farmers have formed Collective Bargaining Groups to negotiate with milk processors under the authorisation provided by the ACCC. The Peters and Brownes Collective Bargaining Group has been involved in discussions between Peters and Brownes and retailers. It has sought to increase retail milk prices with the benefits to be shared between farmers, processors and retailers.

The Committee finds that:

Finding 43

Increased collective bargaining by dairy farmers is a key to the negotiation of higher farm gate prices.

Negotiations with National Foods have resulted in some improvements in non-price contract conditions for dairy farmers. However contract volumes offered to farmers participating in the collective bargaining process have been reduced by about 27% compared to suppliers who signed contracts in January 2003. The reduced contract volumes will reduce average milk prices for affected farmers by up to 4 ¢/L.

The Committee finds that:

Finding 44

There is a widespread farmer perception that National Foods have not conducted collective negotiations in good faith. The abrupt termination of negotiations by National Foods and the short notice given for contract reductions has raised legitimate concerns about the transparency and fairness of the bargaining process.

Collective negotiation has so far failed to increase farmers' market power and may continue to fail unless retailers can be engaged in the process.

There is an urgent need for the ACCC to investigate and enable measures to increase the effectiveness of the collective bargaining process in increasing farmer market power. In the absence of effective action by the ACCC, it may be desirable for the Western Australian Government to develop institutional mechanisms to strengthen farmer power in collective negotiations.

The Committee finds that:

Finding 45

There is an urgent need for the ACCC to investigate and enable measures to increase the effectiveness of the collective bargaining process. In the absence of effective action by the ACCC, it will be desirable to develop institutional mechanisms to strengthen farmer power in collective negotiations.

5.2 The role of co-operatives

The Committee highlights that co-operatives are a major force in the worldwide dairy industry. More than 70% of Australia's milk is processed by cooperatives. Formation of co-operatives is the only form of collective action by farmers that is permitted under the *Trade Practices Act 1974* without a specific authorisation. However co-operatives had been absent from the Western Australian dairy landscape for more than two decades when Challenge Dairy Co-operative commenced operations in 2001.

The Western Australian dairy failed industry to capture the benefits of the peak in international commodity prices during 2000/2001 and 2001/2002. As a result, Western Australian farmers were paid lower milk prices than Victorian farmers who were full participants in the international commodity market.

This reflected structural issues in the Western Australian dairy processing sector and the absence of an established manufacturing co-operative in the export market rather than the effects of deregulation. Dairy farm incomes therefore fell in 2000/2001 when the incomes of farmers in the export focused Victorian and Tasmanian industries were rising (Fig. 2.3).

The Committee finds that:

Finding 46

The Western Australian dairy industry has failed to capture benefits of peaks in international commodity prices. There is a risk that such failure will continue if structural problems throughout the dairy industry chain are not addressed.

It is the actions of manufacturing co-operatives in paying their shareholder suppliers the highest possible milk price that creates a floor in the market that other processors have to match to obtain supply. The strength of local co-operatives has a major influence on the behaviour of corporate processors operating in the same regions.

The large Victorian co-operatives accept most milk from their suppliers on a seasonal basis, allowing farmers to match their production cycle to rainfall and pasture growth. The ability of co-operatives to process all available seasonal milk means that processors seeking year round milk supply must pay a significant premium above co-operative prices to obtain 365 day supply.

The Committee believes that the absence of a mature co-operative structure has been a major factor in the relatively low prices paid to Western Australian farmers since 2000/2001. The average price paid to Western Australian farmers for supply on a year round basis during 2000/2001 and 2001/2002 was lower than that paid to Victorian farmers for seasonal production. ABARE figures show that Western Australian farmers were the lowest paid of any state in 2001/2002 and the second lowest paid in 2000/2001 (see Table 2.1).

The Committee finds that:

Finding 47

The absence of farmer co-operative structures historically has been a major factor in the relatively low prices paid to Western Australian farmers since deregulation.

Challenge Dairy Co-operative sells most of its milk products on the international commodity market. That market has been depressed for most of the Co-operative's

short life and has so far delivered disappointing prices to dairy farmers. There is an urgent need for Challenge to implement its plans to move out of commodity production and to focus on higher value products.

Strong export performance by a producer owned processing and marketing business is considered essential to create strong competition for milk supply, to stimulate price and industry growth, and also to provide a mechanism to increase the market power of farmers. Cooperatives in Victoria and Tasmania were effective in returning the benefits of higher export prices to their members during 2000/2001 (see Fig. 2.4). Bega and Tatura are both good examples of small co-operatives that create a high level of value for their members through quality products and stable market relationships.

The Committee finds that:

Finding 48

Strong export performance by farmer-owned processing and marketing businesses is considered essential to create strong competition for milk supply, to stimulate price and industry growth.

One of the major issues for co-operative development is the problem that co-operatives frequently encounter in raising funds for capital investment. Co-operatives in other Australian states are able to raise funds via Western Australian Government brokered loans under Section 120 (i)(c) of the *Income Tax Assessment Act 1936*. There are also tax advantages associated with the repayments of these loans.

Early advice to the Committee suggested Western Australian co-operatives were unable to make use of such loans, and the Committee was particularly concerned that this placed co-operatives in this State at a competitive disadvantage relative to their interstate competitors in both the cost of and ease of access to investment capital.

As a consequence, the Committee, together with the Department of Agriculture, pursued discussions with the Department of Treasury and Finance, who in turn obtained the Crown Solicitor's opinion. The opinion of the Crown Solicitor is that Western Australian co-operatives are able to utilise the provisions of the *Loan Bill 2003* access a Section 120 (i)(c) loan facility. Such a loan facility is consistent with the functions and powers of the *Western Australian Treasury Corporation Act 1986*, the executive powers of the treasurer and the Minister for Agriculture and Section 120 (i)(c) of the *Income Tax Assessment Act 1936*.

The Committee recommends that:

Recommendation 17

The Government uses provisions under a Loan Bill to enable the establishment of a Section 120(i)(c) loan facility for Western Australian co-operatives.

In conclusion, the Committee's investigations find universal agreement that collective negotiation will be an important factor in rebuilding the market power of dairy farmers. Unfortunately, there are few concrete suggestions as to how that will be achieved. There is a need for a thorough investigation of the options for increasing farmer market power through collective negotiation and co-operative activity. The recommendations of that review need to be implemented with the co-operation of Federal Government and the ACCC.

The Committee notes that two reviews of the issues surrounding the supply chain for food products, including milk, are currently being conducted under the auspices of the Federal Government. The Commonwealth Office of Small Business is sponsoring a review of the Retail Grocery Industry Code of Conduct. Transparency of information in price negotiations and the market power of participants are key issues for that review. The Commonwealth Department of Agriculture, Forestry and Fisheries has commissioned a study of the supply chains associated with a variety of food products. Both of these investigations are expected to report in December 2003. The Committee urges the responsible Federal Ministers to publicly release the findings of both reviews at the earliest possible date.

Both reviews will assist the Western Australian Government in completing its own study into options for increasing farmer market power through collective negotiation and co-operative activity. This will form the basis of Western Australian Government recommendations to the ACCC and Federal Government on strategies to ensure equitable participation in the dairy supply chain by all industry stakeholders.

The Committee recommends that:

Recommendation 18

The Government conducts an analysis of the roles of co-operatives and collective bargaining groups in increasing dairy farmer market power. This analysis must include recommendations to the ACCC on measures to increase the role and effectiveness of collective negotiation of market price.

CHAPTER 6 SUSTAINABILITY AND THE SOCIAL IMPACT OF DEREGULATION

6.1 Introduction

The changes encountered by stakeholders in the dairy industry in Western Australia since deregulation has been tumultuous with approximately 2 ½ times more industry exits in the past three years than the three years previously.⁵⁵ Many in the industry have reported that that exits will continue in response to deregulation. The Committee was told by rural consultant Dr Glenys Hough that, in her opinion, up to 30 % of the industry was at financial risk.⁵⁶

Support for deregulation was not uniform. Only 58 % of the 92 % who participated in the industry plebiscite of producers, voted to proceed with deregulation.⁵⁷ However the opportunity to access the financial restructure assistance money being offered by the Federal Government, coupled with market pressures external to Western Australia, particularly because of the small size of the state industry (as 4% of the market), meant that the move to deregulation was inevitable.

The Committee finds that:

Finding 49

Deregulation of the dairy industry in 2000 was supported by 58% of dairy farmers in Western Australia.

The return on investments appears not to have been the same for producers as for others in the supply chain and, with the comfort of a regulated market removed, many farmers struggled with the associated restructuring of their businesses. The issue of business planning was critical in preparation for deregulation and those farmers who prepared for deregulation with a structured planning approach appear to have responded better to market pressures post deregulation. The Department of Agriculture in its submission has said that the dairy adjustment and assistant packages were designed to assist those who wished to exit the industry, as well as those farmers

⁵⁵ Figure extracted from submission, Department of Agriculture, p.11.

⁵⁶ Hough, G (2003) Session 3, Transcript of evidence, 17 October 2003.

⁵⁷ House, M. (2003), Second Reading speech, *Dairy Industry and Herd Improvement Legislation Repeal Bill 2000*, Legislative Assembly, Hansard 5 April 2000.

who were confident of successfully competing in a deregulated market.⁵⁸ The Committee is aware that a number of DSAP payments were used for lifestyle rather than business purposes. It was further suggested that many dairy farmers did not know how to prepare a business plan and have difficulty in adhering to one for a variety of reasons.

The Committee finds that:

Finding 50

DSAP payments have not always been used effectively to reduce farm debt, upgrade on-farm assets, or exit the dairy industry.

Finding 51

Some dairy farmers did not properly assess their business viability in the lead up to industry deregulation.

The impact of deregulation has not been evenly distributed and considerable financial risk has been transferred to the milk producers. Despite this, that not all dairy farms report a major decrease in income: in fact the Committee was advised that some medium to larger scale producers continue to operate profitably in the deregulated market. However some less efficient, less innovative, or simply less fortunate producers carrying high debt levels, have indicated that the reduction in farm income has seen them continue to re-evaluate their position in the industry while employing strategies to maintain their position.

The Committee finds that:

Finding 52

The most efficient dairy farmers continue to operate profitable dairy businesses in 2003.

⁵⁸

Submission, T. Laidler, Department of Agriculture p. 3.

6.2 Adjustment strategies

The adjustment responses made by dairy farmers are typical of some of those said to have been employed by farming families elsewhere and are related to both the domain of the household and the operation of the farm business.⁵⁹

(i) *Expenditure*

Reductions in expenditure affect not only the farmers themselves and a reduction in farm business spending is felt by the secondary industries such as suppliers of machinery, grain, fertiliser, veterinary services, farm business consultants.

This view has been substantiated to the Committee by way of submissions received and evidence gathered. For instance, Dr Donald Vass, a veterinarian who operates a practice in Harvey told the Committee that financial considerations by farmers have resulted in a drop off in call rates to farms within his area.⁶⁰ One of his great concerns was that causes of death in cows was not always being investigated which could lead to public health concerns and possible liability in some cases.⁶¹ Messrs Rose and Fry said in their joint submission that:

*“veterinary equipment is becoming a luxury....such basics as Dry Cow and Penicillins are seen as something that can be cut out and a way to save money”.*⁶²

Further, Mr Craig Carbone who operates an earthmoving and cartage business said in his submission that in the past twelve months they had done practically nothing for farmers in their area of operations.

The Committee finds that:

Finding 53

Service industries to the dairy sector have been adversely affected by decreased farm expenditure in 2003.

⁵⁹ Webb, T. *et al.* (2002) have identified 14 possible adjustment responses to ameliorate pressure on farm income - but not all involve the contracting of expenditure. *Leaving the Land: a study of Western Division grazing families in transition*, Rural Industries Research and Development Corporation. p. 13.

⁶⁰ Vass, D. (2003) Transcript of evidence, Session 1, 19 September 2003, and Submission, Dr Donald Vass, Harvey Veterinary Clinic.

⁶¹ Vass, D. (2003) Transcript of evidence, Session 1, 19 September 2003, p.3.

⁶² Submission, Mr Warwick Rose and Mr Kim Fry, p.1.

(ii) Labour

A change to labour patterns has occurred in some places; with workers formerly employed full-time now employed on a casual basis.⁶³ This strategy has immediate implications for the family unit as their own workload is increased with the corresponding decrease in leisure time, but also has long term implications for the whole of the dairy industry as it results in fewer skilled workers. Farmwest Services Ltd for instance, derives approximately 80% of its business from the dairy industry with services such as herd recording, milk harvesting and say in their submission that, should their service cease to exist, 8 long serving employees would be made redundant.⁶⁴

The Committee finds that:

Finding 54

Further reductions in the number of dairy farmers will impact adversely on the viability of local service industries to the dairy sector, other secondary businesses, and district economies generally.

In the case of farms however, and contrary to the above, Mr Mike Butler suggested that employment should not be a conditional outcome to industry recovery programs or incentives. Mr Butler made the observation that prior to deregulation, very few dairy farms employed outside labour and that case has not changed.⁶⁵

Figures support the fact that employment, or rather unemployment, has not altered significantly in the dairying areas. Harvey is undoubtedly the shire most affected by the loss of quota, and in spite of the loss of guaranteed income, unemployment has actually fallen from 5.1% in June 2000 to 4.8% in September 2003 (Table 2.4).⁶⁶ At the same time estimated resident population figures for the shire have also increased by 0.014%.⁶⁷ Figures for Augusta-Margaret River also show a similar pattern with unemployment dropping from 7.7% to 6.6% with a population increase of 0.062% for

⁶³ Tognela, D. (2003) Transcript of evidence, Session 4, 19 September 2003, p3-4.

⁶⁴ Submission, L. Giglia, Chief Executive Officer, Farmwest Services Ltd.

⁶⁵ Submission M. Butler, Real Estate Agent.

⁶⁶ The Shire of Harvey previously had 91% of quota holders with over 40% quota while 66% had over 60%.

⁶⁷ DEWRSB Small Area Labour Markets - Australia - June Quarter 2001 and June Quarter 2003. Population figures extracted from SWDC website citing original source: ABS (2003) Regional Population Growth, Australia - Catalogue No. 3218.0, 3 April 2003.

the corresponding periods.⁶⁸ These figures may indicate that farm family members have sought additional paid employment to supplement the decrease in farm income; though the Committee did not receive any direct evidence in relation to this matter.

(iii) Expansion

A number of farmers expanded their dairy businesses in preparation for deregulation.⁶⁹ This took various forms such as land holdings, increase in herd numbers, breeding programs and dairy improvements. The Committee was also advised that some diversified into beef as an adjunct to their dairy enterprises. Leaving aside those farms that embarked on an expansion program that continue to operate profitably, the Committee believes that some dairy businesses are no longer able to service current debt levels as the fall in farm gate price, post -deregulation, is now greater than was expected.

The Committee finds that:

Finding 55

Some farm businesses are now in a position where they need to reassess their viability.

(iv) Procurement of Government Assistance

As has been said in Chapter 2, Western Australian dairy farmers received direct grants of \$134 million to facilitate adjustment to the deregulated market.⁷⁰ The funding from the Commonwealth took two forms: the Dairy Structural Adjustment Program and the Dairy Exit Program. The Dairy Structural Adjustment Program did not hold farmers to their enterprises and entitlement holders were free to exit the industry and continue to receive their payment stream. The Dairy Exit Program provided payments of up to \$45, 000, tax free, for those farmers who wished to leave the industry. A further \$3500 was available as a retraining grant to undertake approved retraining. And, as noted previously in the report, about 25% of Western Australian dairy farmers have left the industry since deregulation.

Although funding under the Dairy Exit Program was only available for the first two years after deregulation, the Federal Government continues to offer assistance to farmers under the Agriculture - Advancing Australia (AAA) package provided through

⁶⁸ *Ibid.* The unemployment rate for Augusta-Margaret River has further decreased to 6.3% as at June 2003.

⁶⁹ Various Submissions - H.D Harrison, J. Tartaglia; A. & E. Brand.

⁷⁰ \$122 million from the federally funded Dairy Structural Adjustment Program and a further \$12 million from the state funded Dairy Farm Assistance Program (WA).

Centrelink. The AAA Farm Help program gives a range of assistance with up to \$51 500 and includes:

- Fortnightly income support for up to 12 months;
- Funded professional advice to assess farm viability;
- Re-establishment funding and retraining assistance;
- A case manager to provide individual support for personal and business decision making.

Apart from the above, professional advice is made available through the AAA Rural Financial Counselling Service; funded by the Commonwealth, State and local community. There are eight offices in rural Western Australia that provide independent advice, free of charge, for producers and small rural businesses (Appendix 4). There is a range of government counselling and financial assistance services available to assist that process. However, it would be valuable to establish a rural counselling service in southwest Western Australia.

The Committee finds that:

Finding 56

There is a range of government services for dairy farmers to access for financial and personal counselling.

The Committee recommends that:

Recommendation 19

The Western Australian Government requests the Federal Government to allow dairy farmers access to Farm Help Re-establishment Grants, regardless of their DSAP entitlement, provided that they meet the standard means test.

Recommendation 20

The Western Australian Government requests the Federal Government to allow dairy farmers to take their remaining DSAP entitlements as a lump sum exit payment. These payments should be recognised as redundancy payments for taxation purposes.

Recommendation 21

The Western Australian Government make immediate application for a rural financial counselling service under the Federal Government's Short-Term Industry Adjustment Projects Scheme within the Rural Financial Counselling Service Project. The State and Federal Governments establish a long-term rural financial counselling service in southwest Western Australia to support adjustment decisions in dairy and other rural industries.

CHAPTER 7 CONCLUSIONS

The dairy industry has undergone dramatic change in the last few years as a consequence of deregulation fully exposing all of the Australian dairy industry to market forces.

Three things need to happen for the development of a sustainable dairy industry in Western Australia.

1. *Dairy farmers need to ensure that their businesses are structured to be competitive in the international and domestic marketplaces and that they have the capacity to respond to increasing competition.*

World demand for dairy products is predicted to outstrip supply so there are good long-term prospects for export growth. However, it will be a competitive market and the industry must strive for efficient and economic farming practices to match their competitors. There are opportunities for many dairy farms to improve business performance by reducing feed and labour costs and through other strategies such as co-operative purchase of inputs. Continuous improvement in farm practices and economic efficiency will be required to continue to match Western Australia's competitors.

2. *Dairy processors must continue the shift away from commodity production into high value export markets.*

With only 4 % of Australian dairy production, Western Australia is a small player in the market. Western Australia must make its small size an advantage, and look for niche markets in products such as UHT and ESL, and for premium markets in products such as ice cream, cream cheese, biodynamic milk and sports drinks. In particular, processors must develop natural relationships with other food industries in Western Australia such as grain and fruit.

Western Australia is geographically close to the emerging markets of south-east Asia, China and Japan and processors must develop products tailored for the Asian market, produced from Western Australian raw materials.

To maximise export success the dairy industry needs to cooperate through the whole supply chain - local farmers working together, processors as a group pulling together, and the industry as a whole moving forward. Strong performance by a farmer-owned processor would ensure that Western Australian dairy farmers share premiums from those markets.

3. *Retailers must recognise that there are added costs associated with supplying fresh milk 365 days of the year and ensure that dairy farmers are adequately paid for the higher costs on a year-round basis.*

It is worth repeating the ACCC report on impact of farm gate deregulation on the Australian milk industry:

“Ultimately, as consumers are prepared to pay a premium for fresh milk, processors will have to pay farmers a sufficient return to guarantee a reliable supply if dairy farmers are not to exit into other areas of agricultural production.”⁷¹

It is the responsibility of the Federal Government to ensure that the ACCC acts decisively and effectively to prevent abuses of market power by dominant players in the inevitable period of adjustment and uncertainty that follows deregulation of a protected industry.

There are a number of measures that the Western Australian Government can take to assist the dairy industry to develop common-user infrastructure and technology, and in developing export markets. The most significant action the Government can take for long-term sustainability is to ensure that the Department of Agriculture has a strong, dedicated research team that examines issues from “paddock to plate” - research, which includes market research supporting new product development.

Further, Government must ensure that its funding to Western Australian educational and research establishments develop products that will bring maximum returns to local processors and to the State. These returns need not simply be measured as economic benefit, but could also be of indirect benefit such as supporting better community health outcomes, and meeting other ‘social contract’ requirements of government. For example, new product development could specifically target provision of good nutrition for children, and delivered via schools, ultimately contributing to programs of preventative medicine.

⁷¹ ACCC (2001). Impact of farm gate deregulation on the Australian milk industry: study of prices, costs and profits. Australian Competition and Consumer Commission, Canberra, ACT.

The Committee recommends that:

Recommendation 22

The Government ensures that any unspent funds from the State Dairy Assistance Package are used to assist the further development of the dairy industry and in particular support the cost of implementing the Committee's recommendations.

APPENDIX ONE

SUBMISSIONS RECEIVED

List of 70 Submissions received for the inquiry (excluding four names not for publication).

Date	Name	Position	Organisation
24/7/2003	Bryan Briney		
30/7/2003	Nick Power	General Manager	Organic Harvest
01/8/2003	Wendy Hughes		
05/8/2003	Paul Sheedy	Chief Executive Officer	Shire of Capel
06/08/2003	John Cummings	President	WA Independent Grocers' Association (INC)
10/8/2003	Craig Carbone	Production Manager	Carbone Bros Pty Ltd
12/8/2003	Mervyn Hinton		
14/8/2003	John Heugh	Managing Director	Griffon Corp
14/8/2003	Ian Noakes		
18/8/2003	Margaret Martin		
20/8/2003	John Haynes		
21/8/2003	H D Harrison		
21/8/2003	N L Gibbs		
22/8/2003	Jenny Trigwell		
22/8/2003	Donald Vass		
22/8/2003	Geoff Calder	General Manager	Harvey Water
22/8/2003	Michael Kearney	Executive Officer	Australian Milk Producers Association
22/8/2003	Leon Giglia	Chief Executive Officer	Farmwest Services Ltd

ECONOMICS AND INDUSTRY STANDING COMMITTEE

Date	Name	Position	Organisation
22/8/2003	Mike Butler		
22/8/2003	Andrew Mahaffey		
22/8/2003	Neil Thompson	Principal Policy Officer	Department of Treasury and Finance
25/8/2003	Mike Norton	Partner	H & A Norton & Sons
25/8/2003	Mark Papalia		
25/8/2003	Murray Ward		
25/8/2003	John Tartaglia		
25/8/2003	Esther Price	Executive Officer	Western Dairy
25/8/2003	Warwick Rose & Kim Fry		
25/8/2003	Shane & Jenny Birch		
25/8/2003	Don Punch	Chief Executive Officer	South West Development Commission
25/8/2003	Paul Ieraci		
25/8/2003	Bernard Ridley		
25/8/2003	Tim & Elizabeth Crimp		
25/8/2003	Tony Ieraci	Business Proprietor	Harvey Farm Service
26/8/2003	Tony Pratico	Dairy Section President	The Western Australian Farmers Federation (Inc)
26/8/2003	Colin Bosustow	Director	Lactanz
26/8/2003	Bruce Manning	Chief Executive Officer	Great Southern Development Commission
26/8/2003	Kim Franklin		
26/8/2003	Victor Rodwell and Marie Dilley	Chairman and Secretary	PB Foods Negotiating Committee

ECONOMICS AND INDUSTRY STANDING COMMITTEE

Date	Name	Position	Organisation
26/08/2003	Ted Moore	General Manager, Government & Regulatory Affairs	Coles Myer Ltd.
26/8/2003	Shelly Pike	Chief Executive Officer	Bunbury Wellington Economic Alliance
26/8/2003	Murray Tognela	Managing Director	Brunswick Agencies
26/8/2003	Dr Nigel Thomas	Chief Executive Officer	Peters & Brownes Group
26/8/2003	Margaret Palmer and Arthur Green	Secretary and President	Australian Milk Producers Association W.A.
26/8/2003	Jenny Fry	Secretary	Milk Industry Liaison Committee
26/8/2003	David Tognela		
26/8/2003	Ross Woodhouse		
26/8/2003	Gary Jenkins	Economic Development Coordinator	Shire of Augusta- Margaret River
26/8/2003	A J Gilmour	Director RSM Bird Cameron	Prepared on behalf of Ketteridge Stockfeeds, Picton
26/8/2003	Terry Laidler	Senior Policy Officer	Western Australian Department of Agriculture
26/8/2003	Leslie Chalmers	Acting Chief Executive Officer	Dairy WA
26/8/2003	Mike Norton	Chairman	Dairy Industry Working Group
26/8/2003	Leanne Ablett		
26/8/2003	David & Fiona Forrest		
26/8/2003	Jim & Marie Forrest		
26/8/2003	Ian Greenshields	Group General Manager Corporate Affairs	National Foods Ltd.

ECONOMICS AND INDUSTRY STANDING COMMITTEE

Date	Name	Position	Organisation
26/8/2003	Ian Brown	General Manager Corporate Communications	Woolworths Ltd.
26/8/2003	SW Knott	Director	Australian Business Linkages Pty Ltd
26/8/2003	Allan & Judy Daubney		
26/8/2003	Geoff Manning		
26/6/2003	D C Phillips	Business Operator	Bunbury Machinery
26/6/2003	Murray Taylor		
26/6/2003	Evelyn & Adrian Brand		
26/6/2003	Mark Furfaro		M & L Furfano & Sons
27/8/2003	Jenny & Ian Trigwell		Stenelees Pastoral Co.
27/8/2003	Mr Mark Chester	Chief Executive Officer	Shire of Dardanup
27/8/2003	Astrid Herlihy		
27/8/2003	Jim, Brett & Jo Miller		
27/8/2003	June Moran		
28/8/2003	Larry Brennen	Chair	Challenge Dairy
29/8/2003	Paul Beech	Manager Economic & Development Services	Shire of Harvey

APPENDIX TWO

BRIEFINGS HELD

List of Briefings (witnesses where Hansard is not present).

(a) Intrastate

Date	Name	Position	Organisation
20/8/2003	Neville Haddon		
20/8/2003	Elaine Haddon		
20/8/2003	David Partridge		
20/8/2003	Michael Partridge		
20/8/2003	Jacqui Biddulph		
20/8/2003	Don Fry		
20/8/2003	Laurel Fry		
20/8/2003	Peter Fry		
20/8/2003	Jenny Fry		
20/8/2003	Nola Marino		
20/8/2003	Michael MacLaughlin		
27/8/2003	Nigel Thomas	Chief Executive Officer	Peters & Brownes Group
27/8/2003	Steven Adams	Corporate Analyst	Peters & Brownes Group
27/8/2003	Bernie Plummel	General Manager, Supply Chain	Peters & Brownes Group
27/8/2003	Dean Maughan	Milk Supply Manager	Peters & Brownes Group
25/9/2003	Neill Buck	Managing Director	Neill Buck & Associates Pty Ltd

Date	Name	Position	Organisation
15/10/2003	Vince Graneri	General Manager	Western Australian Treasury Corporation
15/10/2003	Neil Thomson	Principal Policy Officer	Department of Treasury and Finance
15/10/2003	Felicity Gregory	Acting Assistant Crown Solicitor	Crown Solicitor's Office
15/10/2003	Stuart Clarke	Project Manager	Department of Agriculture
17/10/2003	Glenys Hough	Rural Consultant	Glenys Hough Consulting
29/10/2003	Andrew Weinert	Project Manager	Department of Agriculture
26/11/2003	John D'Agostino	Principal Policy Officer	Office of the Minister for Agriculture, Forestry and Fisheries

(b) Interstate briefings

Date	Name	Position	Organisation
2/9/2003	Steven Coats	Program Manager Innovation and Change Management	Dairy Australia
2/9/2003	Chris Phillips	General Manager International Trade Development	Dairy Australia
2/9/2003	Daryl Gifford	Chief Executive Officer	Dairy Adjustment Authority
3/9/2003	Vernon Topp	Research Manager Agriculture & Trade	Australian Bureau of Agricultural & Resource Economics
3/9/2003	Dale Ashton	Principal Economist	Australian Bureau of Agricultural & Resource Economics

ECONOMICS AND INDUSTRY STANDING COMMITTEE

Date	Name	Position	Organisation
3/9/2003	Peter Martin	Survey Data Manager	Australian Bureau of Agricultural & Resource Economics
3/9/2003	Greg Williamson	General Manager, Meat, Wool & Dairy	Department of Agriculture, Fisheries and Forestry - Australia
3/9/2003	Sally Standen	Manager, Industry Operations & Reform, Wool & Dairy	Department of Agriculture, Fisheries and Forestry - Australia
3/9/2003	Polly McGee	Policy Adviser, Industry Operations & Reform, Wool & Dairy	Department of Agriculture, Fisheries and Forestry - Australia
3/9/2003	Carolyn Page		Department of Agriculture, Fisheries and Forestry - Australia
3/9/2003	Tim Grimwade	General Manager, Adjudication	Australian Competition and Consumer Commission
3/9/2003	Stephanie Chenoweth	Acting Director Adjudication	Australian Competition and Consumer Commission
3/9/2003	Stefanee Lovett	Senior Project Officer	Australian Competition and Consumer Commission
3/9/2003	Tanya Mayrhofer		Australian Competition and Consumer Commission
4/9/2003	Maurice Van Ryn	Chief Executive Officer	Bega Cheese
4/9/2003	Colin Griffin	General Manager Finance Company Secretary	Bega Cheese
4/9/2003	Michael Byrnes	General Manager Operations	Bega Cheese
4/9/2003	Tom D'Arcy	Director	Bega Cheese
4/9/2003	Barry Irvin	Chairman	Bega Cheese
4/9/2003	Mathew Kimber		

ECONOMICS AND INDUSTRY STANDING COMMITTEE

Date	Name	Position	Organisation
12/11/2003	John Feil	Executive Director	National Competition Council
12/11/2003	Alan Johnston	Director	National Competition Council
12/11/2003	Michael James	Competition Policy Advisor	National Competition Council
13/11/2003	Greg Beatty	Regional Managing Director Australasia	New Zealand Milk Australasia
13/11/2003	David Mallinson	Regional Finance Director	New Zealand Milk Australasia
13/11/2003	Allan Burgess	President	Australian Dairy Farmers

APPENDIX THREE

HEARINGS HELD

List of 8 public hearings held (excluding 10 confidential hearings.)

Date	Name	Position	Organisation
19/9/2003	Dr Donald Vass	Veterinarian	Harvey Veterinary Clinic
19/9/2003	David Tognela		
15/10/2003	John Cummings	President	Western Australian Independent Grocers Association
15/10/2003	Ted Moore Chris Mara	General Manager Regulatory Affairs Advisor	Coles Myer Ltd.
17/10/2003	Stuart Knott	Company Director	Australian Business Linkages Pty Ltd.
17/10/2003	Adrian & Evelyn Brand		
22/10/2003	Antonio Pratico Andrew White	Dairy Section President Dairy Section Executive Officer	Western Australian Farmers Federation
22/10/2003	Len De Nooyer	Regional Manager	Woolworths Ltd.

APPENDIX FOUR

LEGISLATION

List of Legislation (or other relevant information) used in the inquiry.

Legislation	State (or Country)
Dairy Industry Act 1973	Western Australia
Dairy Industry Regulations 1977	Western Australia
Consumer Affairs Act 1971	Commonwealth
Fair Trading Act 1987	Commonwealth
Income Tax Assessment Act 1936	Commonwealth
Trade Practices Act 1974	Commonwealth
Dairy Industry Adjustment Act 2000	Commonwealth
Dairy Adjustment Levy (General) Act 2000	Commonwealth
Prices Surveillance Act 1983	Commonwealth
Dairy Industry and Herd Improvement Legislation repeal Bill 2000	Western Australia
Loan Bill	Western Australia
Western Australian Treasury Corporation Act 1986	Western Australia

APPENDIX FIVE

RURAL FINANCIAL COUNSELLING SERVICES IN WESTERN AUSTRALIA

Financial counsellors can help primary producers, fishing enterprises and small rural businesses in rural areas who are experiencing financial hardship and have no other source of financial assistance with:

- assessment of the enterprise's current financial position and cash flow;
- reviews of contracts and loan applications with lending institutions;
- communication and facilitation of meetings with lenders and financial institutions;
- information on government and industry assistance schemes;
- information on, and referral to, Centrelink and other relevant services
- assistance with business decision making in relation to their rural enterprise;
- assistance in considering a range of options for the future; and
- collection and provision of data on client-related activities.⁷²

⁷²

AFFA (2003) <http://www.affa.gov.au> (Accessed 18 November 2003).

Rural Financial Counselling Services in Western Australia.

<p>Albany</p> <p>Southern Agcare Inc</p> <p>Phone: 08 9842 2956</p> <p>Fax: 08 9842 2956</p> <p>Email: sagcare@iinet.net.au</p>	<p>Moora</p> <p>Central Wheatbelt Community Support Group Inc</p> <p>Phone: 08 9671 1222</p> <p>Phone: 1800 656 659</p> <p>Fax: 08 9671 1222</p> <p>Email: cwcs91@hotmail.com.au</p>
<p>Corrigin</p> <p>Central: AgCare Inc</p> <p>Phone 08 9063 2037</p> <p>Fax: 08 9063 2319</p> <p>Email: ceagcare@wn.com.au</p>	<p>Morawa</p> <p>Northern Districts Community Support Group Inc</p> <p>Phone: 08 9971 1294</p> <p>Fax: 08 9971 1084</p> <p>Email: ndcsg@wn.com.au</p>
<p>Esperance</p> <p>Esperance Districts Agcare Inc</p> <p>Phone: 08 9071 7622</p> <p>Fax: 08 9071 7655</p> <p>Email: agcare@wn.com.au</p>	<p>Nungarin</p> <p>Wheatbelt Agcare Community Support Services Inc</p> <p>Phone: 08 9046 5137</p> <p>Fax: 08 9046 5139</p> <p>Email: wheatbeltfinancial@wn.com.au</p>
<p>Katanning</p> <p>Southern Agcare</p> <p>Phone: 08 9827 1559</p> <p>Fax: 08 9827 1559</p> <p>Email: rfc.chris@westnet.com.au</p>	<p>Ravensthorpe</p> <p>Ravensthorpe & District AgCare Inc</p> <p>Phone: 08 9071 7622</p> <p>Fax: 08 9071 7655</p> <p>Email: agcare@wn.com.au</p>

AAA Farm Help can be accessed by contacting the Farmer Freecall Line at Centrelink on 1800 050 585.

APPENDIX SIX

CORRESPONDENCE TO THE COMMITTEE FROM THE MINISTER FOR AGRICULTURE, FORESTRY AND FISHERIES



MINISTER FOR AGRICULTURE, FORESTRY AND FISHERIES;
THE MIDWEST, WHEATBELT AND GREAT SOUTHERN
LEADER OF THE GOVERNMENT IN THE LEGISLATIVE COUNCIL



D. 94/03

Ref: 8-17553



Mr AD McRae MLA
Chairman
Economics and Industry Standing Committee
Parliament House
PERTH WA 6000

Dear Mr McRae

DAIRY INQUIRY

You will recall that I undertook to write to the Federal Minister Truss and the Australian Competition and Consumer Commission (ACCC) to seek their views on a range of proposals to change the marketing arrangements for milk in Western Australia. I promised to share their replies with your Committee to assist with your inquiry into the sustainability of the dairy industry.

The only reply that I have received to date has been from Minister Truss. I enclose a copy for the Committee's information.

Yours sincerely

Kim Chance MLC
MINISTER FOR AGRICULTURE, FORESTRY AND FISHERIES

27 NOV 2003



HON WARREN TRUSS MP

Minister for Agriculture, Fisheries and Forestry



- 7 NOV 2003

The Hon Kim Chance MLC
Minister for Agriculture, Forestry and Fisheries
11th Floor, Dumas House
2 Havelock Street
WEST PERTH WA 6005

Dear Minister

Thank you for your letter of 17 September 2003 regarding dairy marketing arrangement proposals in Western Australia.

I appreciate the opportunity to comment on the proposals outlined in your letter. I must emphasise from the outset, however, that it is not the Australian Government's role to determine the future direction of the dairy industry in Western Australia. The future structure of the industry is a matter for the Western Australian Government to decide consultation with your industry. To this end, the initiative of the Western Australian Legislative Assembly Economics and Industry Committee to inquire into the dairy industry in Western Australia has merit.

I met with Western Australian dairy farmers during a recent visit to the State and my frequent talks with representatives of the dairy industry have certainly identified concerns about the status of the dairy industry in many areas. I realise that a combination of adjustment to deregulation, drought and recent low world prices for dairy products have all contributed to what is a difficult time for many dairy farmers and farming communities. The difficulties associated with adjustment were not unforeseen and were the reason why the Australian Government agreed to provide such a large industry restructure support package.

However, it is my view that the Western Australian dairy industry is well placed to capitalise on rapidly changing and new and emerging markets, particularly those in China and South East Asia. A case in point is the recent success by the Challenge Dairy Co-operative in securing a \$200 million dairy contract with Chinese company Sanyuan. This is a significant and welcome development and bodes well for the future of the industry in Western Australia. Moreover, it is apparent from this success that support for similar initiatives by the State Government would serve to reinforce this trend towards greater reliance on growing export markets and thus lessen the impacts of reduced prices in the traditional drinking milk sector.

In terms of the proposal for a temporary re-regulation of the State's dairy industry, as you are aware, the Australian Government made available the Dairy Industry Adjustment Package (DIAP) specifically to respond to the States' decision to deregulate their milk marketing arrangements.

The DIAP aims to assist the dairy industry and dairy communities across Australia adjust to a deregulated environment by providing \$1.94 billion for the Dairy Structural Adjustment Program (DSAP) and Supplementary Dairy Assistance (SDA) measures. This remains the largest amount of adjustment support provided to any rural industry in Australia.


From a Commonwealth perspective as demonstrated by our actions to provide meaningful structural adjustment assistance, the alternative of an unmanaged transition to a deregulated environment, once State Governments had decided to deregulate their dairy industries would not have been in the best interests of the industry and certainly would have placed much greater pressure on dairy farmers. With this in mind, it was not contemplated at the time that any state would consider re-regulating at a later date, once funding from the package had been allocated to recipients. More than one third of the adjustment entitlements have already been paid to farmers and some producers have already cashed out their future payments through commercial arrangements. The DIAP Scheme is ongoing until 2008 and it is apparent that this funding has assisted Western Australian dairy farmers adjust to the deregulation changes.

In this context, while it is entirely a matter for the Western Australian Government to determine, I am concerned that re-regulation would not provide a sustainable solution to the industry's difficulties in Western Australia. In particular, there is now a national market for liquid milk and it would be extremely difficult to sustain artificial pricing arrangements in the face of commercial pressures from interstate suppliers. Perhaps more importantly, any moves to re-regulate the industry would likely have a negative impact on the development of an export focussed manufacturing sector through the diversion of farm milk supplies away from this growth segment of the dairy market.

In terms of the path forward, as I have previously indicated, I believe it is likely to be more productive if efforts are focussed on assisting the industry diversify into new and growth orientated export markets. As you are aware, the Australian Government has already provided further substantial assistance in this area through the provision of funding under the Dairy Regional Assistance Program. I note also that the previous Western Australia government provided assistance to the industry in the Capel region aimed primarily at market diversification. It may be preferable for the State Government to consider additional assistance measures that build on recent successes, such as that demonstrated by Challenge Dairy.

I look forward to hearing of the outcome of the Economics and Industry Committee's inquiry.

Yours sincerely



WARREN TRUSS



1. Proposed changes to current milk marketing arrangements

You have indicated that the State Government has received a number of proposals seeking change to milk marketing arrangements from individuals and groups associated with the dairy industry. You have also stated that a number of those proposals seek to overcome farmers lack of market power and increase farm incomes through collective milk marketing based on State legislation. The options as identified by Government and which you have requested the Commission's comments on include:

- (i) reconstitution of the Dairy Industry Authority and a permanent return to statutory marketing of milk;
- (ii) vesting of all WA milk in a single entity for sale by tender to dairy processors;
- (iii) collection of a retail levy on all drinking milk to provide income support to dairy farmers; and
- (iv) the development of an industry managed solution based on collaboration between different players in the supply chain.

While it would not be appropriate for the Commission to provide any formal comment on proposals that are essentially a policy decision for the WA Government, I would suggest that all these options, particularly those at (i)-(iii) are likely to have profound and significant adverse implications for the development of an efficient deregulated market and the benefits to consumers that such a market would otherwise bring. In these circumstances, I note also that in July 2000 at the time of national deregulation of market milk, the Commonwealth put in place arrangements establishing an assistance package for the dairy industry, to be funded via a retail levy of 11 cents per litre over eight years. The options as proposed may require consultation with the National Competition Council and the Competition Policy Unit within Federal Treasury.

Proposal (iv) highlights an opportunity for collaboration between participants in the dairy industry in respect of a self regulatory approach. The effectiveness of self regulatory mechanisms relies largely on the degree to which such mechanisms encapsulate the relevant market dynamics and the willingness of the participants to commit. The Commission has some experience in assisting industries to consider and develop self regulatory mechanisms and we would be happy to discuss this option further.

2. Strengthening farmers negotiating position

The Commission is aware that there is some dissatisfaction with the arrangements for collective negotiations between WA dairy farmers and National Foods Ltd, as authorised by the Commission on 12 March 2002, and subsequently amended by consent before the Australian Competition Tribunal on 16 August 2002.

I note your concerns that the current authorisation offers little leverage against a major player such as National Foods Ltd, particularly where parties are unwilling to partake in collective negotiations. I must emphasise that the terms of the authorisation do not compel parties to engage in collective negotiations, nor did the Commission require that the issue of "leverage" for a group of farmers was itself a benefit.

It is important to note that the Commission found that voluntary collective bargaining would, on a limited scale and scope, be in the net public benefit because collective bargaining:

- increases the viability of farmers supplying processors that were previously excluded from supplying due to the high cost and logistics of individually transporting relatively small volumes of milk;
- provides farmers with greater time and opportunity to gain the experience to negotiate effectively with processors thereby increasing their confidence in their dealings with processors; and enhancing their individual bargaining power;
- facilitates the adjustment to deregulation by providing dairy farmers with the opportunity to gain experience with regard to conducting contractual negotiations, thereby enhancing their ability to conduct efficient and effective negotiations when farmers resume independent responsibility in this regard;
- may result in small costs savings for farmers; and
- results in an increase in the amount of information available to both sides, allowing them to make more informed decisions about the business arrangements they enter into.

The Commission was satisfied that the public benefits resulting from the collective negotiations were likely to outweigh any anticompetitive detriments that might result and accordingly the Commission granted authorisation to this aspect of the proposed conduct, subject to conditions.

However, the Commission did not consider that conferring an ability of a supplier to withhold supply was in the public interest and thus did not authorise this aspect of the proposed conduct.

Further, the Commission saw that in the long term, a deregulated market had been agreed by all Governments as the most efficient outcome and the arrangements which it authorised were seen as facilitating a transition to deregulation.

While the Commission has received some complaints from both sides about the processes being engaged in pursuant of the authorisation, the Commission has not formally received any request to revoke the authorisation on the basis that its conditions have been breached. The Commission also understands that some progress has been made between farmers and processors regarding supply terms but not price.

As you may be aware, the Dawson Review considered at some length, the position of small business in their dealings with large business. The Commission proposed and the Committee recommended that a notification process along the lines of exclusive dealing notifications should be introduced for collective bargaining by small business, (including cooperatives that meet the definition of small business) dealing with large business. The Government accepted this recommendation and has advised that it would develop such a notification process for collective negotiations by small business.

This process may provide another opportunity for farmers to avail themselves of collective negotiation arrangements, which differ from those already authorised.

3. Use of Commission's disclosure powers

Section 155 of the Act confers a statutory power on the Commission to obtain information and documents in the course of its enforcement activity. The Commission is only able to exercise this statutory power for the purposes of Commission investigation and cannot exercise its section 155 powers to obtain evidence for third party purposes.

The Commission's previous role in monitoring the costs, prices and profits of the Australian dairy industry ceased with the publication of its report in April 2001. This role was carried out pursuant to the provisions of the *Prices Surveillance Act 1983*. Under these provisions the Commission acts according to a direction from the Treasurer, who may specify the products and time periods that are to be subject to monitoring. The Commission is not in a position to provide any data on the dairy industry beyond that published in its 2001 report.

4. Concerns of product "dumping"

I refer to your concern that there is evidence suggesting that dairy products generally sell for lower retail prices in WA than in other States. You query whether this would be an issue of concern for the Commission.

It appears you may be referring to the price discrimination provisions that were formally contained in the Act. While the specific price discrimination provisions contained in section 49 of the Act have since been abolished, price discrimination conduct may be unlawful if it satisfies the misuse of market power provisions.

In summary, section 46 of the Act provides that a business that has a substantial degree of power in a market is prohibited from taking advantage of that power for the purpose of eliminating or substantially damaging a competitor; preventing entry of a person into the market; or deterring or preventing a person from engaging in competitive conduct in any market.

The Commission would need to assess any evidence in light of the specific criteria prescribed in the Act. I welcome any additional information you are able to provide in relation to this issue, or alternatively, a meeting with staff from the Commission's Perth Regional Office may be arranged in which to discuss this matter further, or any other aspect raised in your letter.

Yours sincerely



Graeme Samuel
Chairman

REFERENCES

- ABARE (2001) The Australian dairy industry - impact of an open market in fluid supply. Canberra, ACT.
- ABARE (2003) <http://www.abare.gov.au> (Accessed 18 November 2003).
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- ABS (2003) Average retail prices of selected items - Eight Capital Cities, September Quarter, 2003. Catalogue 6403.0 [Released 5 Nov 03].
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