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To: Committee Secretary, Senate Standing Committees on Rural and Regional Affairs and Transport

**Re: Senate Inquiry: Performance of Australia's dairy industry and the profitability of Australian dairy farmers since deregulation in 2000**

On 17 October 2019, the following matter was referred to the Rural and Regional Affairs and Transport References Committee for inquiry and report by the third sitting day in March 2020.

The Australian Dairy Products Federation (ADPF) welcomes the opportunity to provide comment on the Terms of Reference (ToR) and the performance and profitability of the dairy industry post de-regulation in 2000.

The ADPF is the peak policy body representing commercial/ post farm-gate members of the Australian dairy industry, including processors and marketers of Australian dairy products. For the past 30 years, ADPF has worked to represent the interests of members in promoting and protect dairy products through advocating for improvements in the manufacturing, marketing and trading of dairy.

### **Background:**

The dairy industry is a vital and important contributor to the Australian economy and employment, and one of the few remaining successful manufacturing industries in Australia. It has a farmgate value of \$4.4 billion<sup>1</sup>, sitting fourth behind the beef, wheat and wool industries. The industry directly employs over 46,000 people across the country in dairy farming and manufacturing (with approximately 22,000 specifically in dairy manufacturing), and another 100,000 employed in providing services to the industry. However, the drought, and the cost of production from higher energy, water, feed and labour costs, as well as increased market volatility has put significant pressure on farm profit margins, with the costs of production outpacing the increases in milk price – particularly for those farmers who have shifted from a predominately pasture based seasonal production system to a more input intensive, flatter production system supplying milk year-round<sup>2</sup>.

There has been ongoing consolidation within both dairy farming and dairy processing. The number of farms has fallen by over half since 2000 (12,900 → 5,200), associated with a fall in milk production to below 9 billion litres in 2018-19 (8.8 billion litres) – with a 3-5% decline in full season production forecast of between 8.3 to 8.5 billion litres in 2019-20<sup>3</sup>. Processors are operating significantly underutilised plants and are unable to achieve the necessary production efficiencies. In the past 20 years, we have seen a

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<sup>1</sup> Dairy Australia (2019). Australian Dairy Industry – [In Focus 2019](#)

<sup>2</sup> Australian Dairy Plan (2019) – draft.

<sup>3</sup> Dairy Australia (2019) Situation and Outlook Report – December 2019



shift from an industry led by farmer cooperatives to one dominated by foreign-owned entities. Only one of the eight major processing firms continues to operate independently – and this is no longer a cooperative<sup>4</sup>.

A shrinking milk pool has also created opportunities for increases in dairy imports and adversely impacted the dairy industry's global trade performance. Imported dairy products now account for 22% of the market (2017/18), up from 8% in 2004/05 and the share of global trade has reduced from 16% in 2000 to only 6% in 2018<sup>5</sup>.

With all of this, it is important to note that dairy processors and farmers are inextricably linked. They are co-dependent – the success of each relies on the strength and sustainability of the other. Therefore, in this changing environment, it is even more crucial for farmers and processors (and retailers) to work collaboratively to generate greater value in the supply chain. This is because dairy production and processing does not run on short planning cycles – success depends on the continuity of supply that comes from investment in long-term relationships, built on trust.

A key part of rebuilding trust is processors' commitment to help farmers more effectively manage the risks associated with the high levels of price volatility in the dairy industry. Processors and farmers have or are currently working on a number of encouraging initiatives here, including simplified payment systems, standard form contracts, and longer-term contracts designed to improve price certainty for farmers.

The new mandatory Dairy Code of Conduct (Code) will complement this activity, playing a role in providing the foundations for fair, more transparent contracts between farmers and processors for the buying and selling of raw milk.

The next step in improving trust and transparency between farmers and processors, and generating greater understanding of farm-gate milk pricing (FMP), is through initiatives such as the Milk Price Monitor tool and information on the drivers of FMP, outlined in the new (draft) Australian Dairy Plan – refer to points 2 and 3 below for more detail<sup>6</sup>.

The Australian Dairy Plan is the industry's five-year strategy (effective July 2020) and is about the whole of the dairy supply chain working together to deliver five key commitments, to drive value and to return the industry to one of profitable growth. Economic modelling suggests a realistic scenario is for a one billion litre increase in milk production by 2024–25 (FY25), generating more than \$600 million annually in extra value at the farmgate and stimulating the growth of at least 1,000 direct new jobs, mostly in rural and regional areas. This will enable the industry to successfully contribute to the \$100 billion agri-business 2030 target. Governments support in delivering this Plan, is important.

### **The Senate Inquiry:**

The Senate Inquiry into the 'Performance of Australia's dairy industry and the profitability of Australian dairy farmers since deregulation in 2000', outlines seven ToR for assessing the 'viability' of the dairy industry.

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<sup>4</sup> Australian Dairy Plan (2019). [Australian Dairy Situation Analysis, May 2019](#)

<sup>5</sup> Australian Dairy Plan (2019) – draft [Australian Bureau of Statistics; International Dairy Federation World Dairy Situation, 2018]

<sup>6</sup> Australian Dairy Plan (2019) – draft.



The ADPF will provide specific comment on four:

1. The ability of Dairy Australia to act independently and support the best interests of **both farmers and processors**;
2. The merits of tasking the ACCC to investigate how it can **regulate the price of milk per litre paid by processors to dairy farmers to ensure a viable dairy industry**;
3. **Alternative approaches** to supporting a **viable dairy sector**;
4. The introduction of a **mandatory industry code of practice**.

Our specific comments are:

1. **The ability of Dairy Australia to act independently and support the best interests of both farmers and processors:**

The Australian Dairy Industry Council (ADIC) is the peak national representative body of the Australian dairy industry, representing the interests of Australian dairy's whole value chain through its two constituent bodies: Australian Dairy Farmers (ADF) and the ADPF. The ADIC constitution provides for the President of ADF to be President of ADIC and the President of ADPF to be Vice President of ADIC. The partnership is unique to Australian agriculture and provides a strong, unified approach to industry and government advocacy on a range of issues from trade and market access, to sustainable resourcing (including water and energy), to effective regulation and policy (Dairy Code of Conduct), and strategic leadership via participating in the development of the Australian Dairy Plan.

Dairy Australia (DA) is a farmer and government funded research and development corporation led by a dairy farmer as Chairman – with the broader dairy industry at heart. It is funded by a farmer 'all milk' levy (collected and administrated by processors), with matched payments from the Commonwealth government for eligible research and development activities. Under the ADIC umbrella, DA provides valued technical support to both ADF and the ADPF, including market insights and cost production data.

As per the 2018-19 Annual Report<sup>7</sup>, DA's purpose is to support the profitability and sustainability of dairy farming, working closely with their levy payers. It provides practical tools, services and advice to assist farming operations and the dairy supply chain. The investments in innovation are focused on increasing farm productivity and the global competitiveness of the industry.

The DA Constitution (2001 and amended in 2018)<sup>8</sup> notes the organisation is comprised of two types of members: Group A and B. Group A members are levy-paying 'dairy enterprises' (i.e. farmers) and have voting rights. Group B members are corporates representing the Australian dairy industry and do not have voting rights (currently two peak policy industry associations: ADF and ADPF).

Therefore, while DA may consider the 'whole of chain' impact, its leadership is farmer-centric and cannot offer independence.

**Request:** ADPF asks that this ToR be reworded to reflect the primary role of DA. To note, a whole of industry strategic plan is being developed branded the Australian Dairy Plan, alongside a review of

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<sup>7</sup> Dairy Australia (2019). [2018-19 Annual Report](#)

<sup>8</sup> Constitution of Dairy Australia Limited (2001, and amended in 2018)



*best-practice dairy industry structures. The outputs of these should be considered in defining the future role and accountabilities of the dairy industry, including DA – in particular the role and definition of policy and advocacy.*

**2. The merits of tasking the ACCC to investigate how it can regulate the price of milk per litre paid by processors to dairy farmers to ensure a viable dairy industry:**

Dairy processors are committed to a sustainable, viable dairy industry, with significant investments made throughout Australian in capital, people and capability, as well as local communities. It is about driving value for all dairy products, from domestic milk through to manufactured and exported dairy products, such as cheese, yoghurt and milk powders.

A number of past inquiries and reports into the efficacy of the dairy industry and fair practices have occurred, from the:

- Senate Inquiry 2009 – Competition and Pricing in the Australian Dairy Industry, September 2009;
- Report 2010: Milking it for all it's worth — competition and pricing in the Australian dairy industry, May 2011;
- Report 2011: The impacts of supermarket price decisions on the dairy industry, November 2011;
- Inquiry 2016: Inquiry into Fair/ longer term solutions to the Australian Dairy Crisis, September 2016;
- Report 2017: Australian dairy industry: rebuilding trust and a fair market for farmers, August 2017;
- ACCC Report 2018: [Dairy Inquiry Final Report](#), April 2018;

through to the current Senate Inquiry and the most recent Saving Australian Dairy Bill 2019 – referred to the Economics Legislation Committee on the 5 December 2019, for inquiry and report by 20 March 2020.

The ADPF recognises a number of recent events, largely beyond the control of current processors, have contributed to a significant loss of trust and transparency across the dairy supply chain. This is from a 'de-valuation' of dairy products secondary to the introduction of private label \$1/litre milk and other discounted dairy products, through to the 2016 farm milk price (FMP) step-down and impact on relationships between many farmers and processors.

These events have taken place against the backdrop of significant changes in the structure of the dairy industry. In just a few years, there has been a shift away from a farmer cooperative led industry to one dominated by foreign-owned entities.

Rebuilding co-dependent relationships and working with farmers (and retailers) is crucial if we are to generate more value in the supply chain and provide greater transparent pricing to improve trust.

The new mandatory Dairy Code of Conduct (Code) – a recommendation from the ACCC Report 2018<sup>9</sup> to increase fairness and transparency between farmers and processors – will play an important role

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<sup>9</sup> ACCC (2018). [Dairy Inquiry Final Report](#), April 2018.



in providing the foundations for standard form contracts between farmers and processors for the buying and selling of raw milk.

The ACCC Report called for greater transparency around FMP and the drivers, to enable better farm income forecasts.

Commitment 5 of the new (draft) Australian Dairy Plan is designed to build greater trust, transparency and confidence and provide greater disclosure and understanding about risk and the market dynamics across the whole value chain including the key drivers of FMP and the impact of their relative movement, to help farmers better understand the drivers of price volatility. The industry (with government support) will also explore the design, development and market testing for a new milk pricing and trading platform which could provide potentially greater selling options through the supply chain. It reads:

*Commitment 5: We will restore trust and transparency between farmers, processors and retailers to strengthen industry confidence*

*The industry recognises that several recent events have contributed to a significant loss of trust across the dairy supply chain. A key part of rebuilding trust is helping farmers more effectively manage the risks associated with high levels of price volatility in the dairy industry. A stronger focus on farm milk price (FMP) disclosure and supporting measures will assist here. This includes the establishment of a Milk Price Monitor that will provide transparent information on FMP, as well as steps to lay the groundwork for transitioning over time to a functioning futures market for raw milk backed by government legislation.*

The three initiatives proposed in more detail are:

- I. To establish the 'Milk Price Monitor' tool to provide greater transparency on Farm Milk Price (FMP):
  - This is a single source of verified information on FMP, collecting and integrating data from processors, across a range of parameters including region, farm size and seasons.
  - It will be led by processors through the ADPF, with support from DA and ADF.
  - It will be available through a range of channels, including a website (and possibly an app).
  - *An independent body will be engaged to undertake a review of its performance within the first three years of its operation to assure the industry of the accuracy and reliability of the FMP information.*
- II. Improve industry understanding of the drivers of Farm Milk Price (FMP):
  - Processors will publish other information to help increase the transparency of the drivers that inform FMP, including market dynamics (i.e. trends in international markets and other key signals that influence the FMP); risk and reward decisions faced by processors; and, business costs.
- III. A functioning futures market for raw milk:
  - Milk Price Monitor is the first step towards laying the groundwork for a functioning milk price market, backed by government legislation. This will be informed by the current ADF project that is looking to design, develop and market test new concepts related to milk pricing and trading.



**Other:** If government is to consider any other regulation on FMP paid by processors to farmers to ensure a viable dairy industry, a number of factors must first be considered:

- Any consideration must be underpinned by a thorough economic analysis, to understand the costs and benefits to the whole of the dairy industry.
- 'Regulation' of FMP is a very broad term and needs defining.
- The term 'viable' dairy industry also needs defining? Climatic conditions (and therefore climate change) can largely influence cost-efficient production, e.g. in the southern region of Australia.
- How would 'regulation' of FMP be executed without prejudicing competitiveness in international markets?
- Can other initiatives achieve a 'viable' dairy industry – e.g. Australian Dairy Plan/commitment 5?
- How are 'external forces' accounted for, e.g. succession, land value, alternative use (that may prompt an exit, beyond FMP)?
- In a regulated environment at what level does the regulation commence and cease, e.g. retail milk price, wholesale milk price, farm to factory milk price?
- Is it domestic liquid milk ('market milk': white/ flavoured milk) and/or manufactured and exported dairy products (e.g. yoghurt, cheese, milk powder)?
- What is the impact of import competition, e.g. the opportunity for packaged liquid milk to be imported from New Zealand?
- How would the complexities in the differences in production/consumption by state, and varying production costs by region, be managed?

**Request:** ADPF asks that the Code, along with the initiatives proposed under the Australian Dairy Plan are allowed a fair and equal opportunity to be implemented and evaluated before any other regulatory approach to FMP is considered. The term 'viable' dairy industry needs to be defined.

### **3. Alternative approaches to supporting a viable dairy sector:**

Following extensive industry wide consultation and situation analyses, dairy industry Partners – DA, ADF, ADPF and the Gardiner Foundation – have worked collaboratively to develop a whole of industry strategy called the Australian Dairy Plan (Dairy Plan).

The Dairy Plan aims to drive a more profitable, confident and united industry, over the next five years and beyond, collaboratively generating greater value in the dairy supply chain.

On the basis of modest growth projections, the Dairy Plan will support around 1 billion litres of additional national milk production annually by 2025, worth over \$600 million per annum to dairy farmers. This additional growth will stimulate the creation of at least 1,000 direct new jobs, mostly in rural and regional areas.

The draft Dairy Plan outlines key commitments and initiatives:

1. A historic reset of how farmers and processors work together to provide greater transparency and consolidated information regarding farm milk prices, as well as the establishment of a Milk Price Monitor tool.
2. New measures to drive a step change in on-farm business and risk management by ensuring by 2025, 100% of dairy farms will have completed effective business plans.



3. A renewed focus on attracting new people and investment, to build industry capacity and growth.
4. A major ramp up of industry marketing and promotion to build greater levels of trust with consumers and improve the value of dairy products.
5. A heightened focus on industry fundamentals to accelerate progress in innovation, market development, policy leadership and sustainability.
6. A more unified and strategic approach to collaborating with government on initiatives to stimulate industry growth, reduce costs and remove barriers, in line with the Federal government's 2030 goal of \$100 billion in farmgate agriculture output. This includes working with the government on dairy initiatives that can be supported by the annual \$100 million Future Drought Fund.

The Dairy Plan also focuses on initiatives to help farmers better manage the increased cost of key inputs like feed, water and energy to support the profitability of their dairy businesses.

The draft Dairy Plan was released on Friday 6 December, with the final version due in March 2020, with implementation in July 2020 – including a governance framework for implementation, monitoring and reporting. The success of this Plan is dependent on farmers and processors working in partnership – along with the support of government and other key stakeholders.

**Request:** *ADPF asks that the Australian Dairy Plan be considered as an alternative approach to driving the 'viability' of the dairy industry – its success relies on the whole of industry – farmers, processors, retailers and the government – all working in partnership to return the industry to one of profitable growth. Again, the term 'viable' dairy industry needs to be defined.*

#### **4. The introduction of a mandatory industry code of practice:**

The ADPF is committed to a sustainable, viable dairy industry based on collaborative partnerships, particularly between farmers and processors to generate more value in the supply chain – a key part of which is providing greater transparent pricing to improve trust.

Processors and farmers have or are currently working on a number of encouraging initiatives here, including simplified payment systems, standard form contracts, and longer-term contracts designed to improve price certainty for farmers.

The new mandatory Dairy Code of Conduct will complement this activity, playing a role in providing the foundations for fairer, more transparent contracts between farmers and processors for the buying and selling of raw milk.

We have been an active participant in the process to produce a fair and effective Dairy Code of Conduct for the industry.

On behalf of our members, ADPF provided a response to the Exposure Draft of the Dairy Code of Conduct on Friday 22 November 2019. We are of the view that this Code will clarify and strengthen relationships between processors and farmers across Australia, providing greater transparency on the contractual process. The ADPF supported the underlining principle of seeking to set minimum standards of dealings between processors and farmers. Overall, we had broad consensus on most of the proposed sections, however sought clarity on several key matters. With the Final Dairy Code of Conduct launched on Friday 13 December (today), we are currently working through the detail.



The ADPF is also participating in the ACCC Dairy Consultative Committee to the Code to support implementation of the Code.

**Request:** *That it be noted, the ADPF has always believed a successful processing sector requires strong, viable farmers and collaborative partnerships between farmers and processors. We have been an active participant in the process to produce a fair and effective Dairy Code of Conduct for the industry. We are currently working through the details of the Final Code and any unintended consequences there may be for both dairy farmers and processors, as well as looking to understand how to best support our members deliver on the tight deadlines as stipulated.*

In summary, the dairy industry is facing a number of significant challenges that need to be addressed, both in the short and longer term. A whole of industry approach to developing solutions is imperative, with farmers working collaboratively with processors, along with the government and retailers. Trust, transparency and confidence is integral to this. It is about driving value across the supply chain.

We believe the Dairy Code of Conduct has a role to play in building trust and transparency. The Australian Dairy Plan provides a foundation for rebuilding the dairy industry and returning it to one of profitable growth and we ask the government to consider the Dairy Plan as it assesses the viability of the dairy sector.

The ADPF welcomes the opportunity to discuss any of our responses and to work collectively with government and industry to secure a sustainable and profitable dairy industry.

We look forward to the next steps.

Yours sincerely

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