ABN 87 023 582 096
AMALGAMATED MILK VENDORS ASSOCIATION INC.
(Incorporated under the Associations Incorporated Act, 1984)

The Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600
economics.sen@aph.gov.au

Dear Sir,

Inquiry into the Impacts of Supermarket Price Decisions on the Dairy Industry

1. Introduction

The Amalgamated Milk Vendors Association Inc (AMVA) has been operating since 1930. It is the body recognised by all sectors of the Dairy Industry and Government in New South Wales (includes Australian Capital Territory) as the peak representative body for Milk Vendors and Dairy Distributors. It is a non-profit association run by an honorary Council of active vendors and distributors.

At the present time the AMVA has 430 members and represents distributors in New South Wales, Queensland, Victoria, Tasmania and South Australia. Milk and Dairy Distributors from Western Australia are not officially part of the AMVA at this stage although a loose affiliation does exist. Distributors are milk vendors who are either contracted or franchised to a processing company to distribute drinking milk and dairy products to major supermarkets, independent supermarkets, petrol and convenience chains, route trade, schools, factory outlets and homes.

The distribution sector of the NSW dairy industry was deregulated 1 July 1998 and at various other times in other states. Prior to deregulation most milk distribution businesses operated as a single truck model. As a result of supermarket pricing policies in relation to home branded milk since 1998 we have witnessed the demise of almost all home delivery milk businesses and the gradual demise of some parts of the route trade. In addition, many route trade milk distributors have engaged in many rationalisation schemes to takeover adjoining milk runs to remain viable. Recent trends in the industry have been moving toward a multi-truck operation which is the preferred mode of operation of all processors. We estimate that the total number of milk distributors across Australia would be around 745 and that these small businesses would employ approximately 2200 staff.

2. The Australian Dairy Industry - Overview

According to Dairy Australia, the dairy industry is the third largest rural industry in Australia. In 2009/10 it was valued at $3.4 billion at the farm gate and is a major value-added food industry. It is estimated that the industry employs a workforce of approximately 40,000 on dairy farms and processing plants. In addition, transport and distribution sector, research and development activities and those employed by regulatory bodies represent additional employment that is vital to the industry. Dairy activities provide significant economic activity and employment in metropolitan and in particular, rural areas. The Australian Bureau of Agriculture and Resource Economics (ABARE) estimate a regional economic multiplier of 2.5 from the dairy industry (Source: Australia Dairy Industry In Focus 2010).

3. Farm gate, wholesale and retail milk prices

The Australian dairy farming sector is highly regionalised. Regional factors such as climatic issues, environmental matters, land values, distance from farm to processing plant, supplementary feeding and all year round milking as opposed to seasonal milking all have bearing on the cost of production. The simple fact is that dairying in some areas has a higher cost structure than in other areas. These factors have a huge impact on prices that should be paid to dairy farmers at the farm gate to cover costs.

The economic effect on the dairy industry of reductions in prices to be paid to producers will be devastating to the industry and may see further farmer numbers being reduced as farmers are unable to receive a reasonable return (cost plus margin) to survive. Some evidence is starting to emerge that indicates that the retail price charged by the supermarkets is causing a shift in buying patterns from some wholesale customers to supermarkets. Outlets, such as coffee shops, restaurants, cafe customers and office blocks that normally purchase branded milk and dairy products through the local milk distributor are now purchasing their requirements through supermarkets. Apart from this, some retail outlets such as small independent supermarkets, petrol and convenience outlets, corner shops, milk bars and newsagents who rely on branded milk sales to get customers through their doors have also reported a drop in overall sales apart from sales of branded milk and dairy product.

The whole milk supply chain is now under threat as a result of the market strength of the supermarkets because of their enormous market share of the milk market. Coles has claimed that their “milk sales represent 5% of Australia’s milk production” – this is not the full picture as Dairy Australia statistics show that the Coles 5% share is actually 20% of the drinking milk portion of the Australian market.

The shift away from a profitable branded product for the whole supply chain to a much reduced or marginal profit home branded product has serious implications all through the supply chain and associated stakeholders in the dairy industry. This will have enormous consequences for employment for the small shop, milk distributor, processing company and finally to the dairy farm and rural communities. In addition, we are risking our national food security just because the major supermarkets have the market strength to eliminate customer choice by selling at a price that undermines the profitability of an industry. The action of Coles seems to mimic that of the English market where the supermarkets almost wiped out the dairy industry.

4. The decrease in Australian production of milk from 11 billion litres in 2004 to 9 billion litres in 2011, of which only 25 per cent drinking milk

The reduction in Australian total milk production is a direct consequence of a number of issues which include the impact of deregulation, long period of drought, volatile world markets and the price that the processor sells to the Australian market. All these issues impact upon the farm gate price and at times of low returns many farmers are forced out of the industry.

The one variable that has been badly managed by the processing sector is the sell price to the domestic market. If the domestic sell price was at a realistic level Australian dairy production may be on the increase rather than decreasing. This would obviously provide a better base for increased employment through the whole supply chain and a much needed degree of confidence for the industry. However, the market power of the major supermarket chains and the impact of their pricing policies along with the commercial realities of dealing with them have had the opposite effect.

The current action instigated by Coles will further damage the confidence of the dairy industry and may have the added effect of reducing Australia's total milk production. Already, there are indications by some dairy farmers that they are not prepared to invest further funds in their farms and will exit the industry. Reduced production has the potential to impact on Australia's future food supplies as well as having a negative impact on employment.

5. Whether such a price reduction is anti-competitive

The ACCC considers that predatory pricing is unlawful under s. 46(1) and s. 46(1AA) of the Competition and Consumer Act. Section 46(1) prohibits businesses that have substantial market power from taking advantage of that power for the purpose of eliminating or substantially damaging a competitor, preventing the entry of a person into a market or deterring or preventing a person from engaging in competitive conduct in a market. A business has substantial market power when its activities are not significantly constrained by competitors, suppliers or customers (Source: Australian Competition and Consumer Commission, 'Predatory pricing (s46(1) and s46(1AAA))'accessed at http://www.accc.gov.au/content/index.phtml/itemId/816375).

It is a concern that the action of the supermarkets has already caused a significant shift from branded milk to home branded milk (Source: ABC News, Milk price war affects sales, accessed at http://www.abc.net.au/news/stories/2011/02/15/3139703.htm) as a result of their market power. The supermarket chains are able to conduct any type of discounting to improve their position in the market because of their overall market dominance in order to eliminate competition. This usually comes at the expense of the manufacturer, supplier and other smaller competitors. In the current milk price war, the branded product has been significantly damaged which will lead to a flow-on effect through the entire supply chain which must ultimately end at the farm gate.

Coles consistently claim that their current action will not affect farmers. However, there have been numerous media reports indicating industry and other supermarket sources saying that the current milk discounting is not sustainable and that farmers will be affected. In addition, media reports have indicated that Coles is incurring substantial losses in their milk discounting (Source: Phillip Coorey, Sydney Morning Herald February 28, 2011 "Milk war heats up as Woolies sides with farmers") – is this designed to eliminate smaller competitors who are unable to respond to Coles Supermarkets?

6. The suitability of the framework contained in the Horticulture Code of Conduct to the Australian Dairy Industry

No comment.

7. The recommendations of the 2010 Economics Reference Committee report, Milking it for all it's worth – competition and pricing in the Australian dairy industry and how these have progressed

As far as we are aware the recommendations outlined in the Senate Economics Committee's report "*Milking it for all it's worth – competition and pricing in the Australian dairy industry"* May 2010 have not been acted on by government. We feel that these recommendations should be progressed.

8. The need for any legislative amendments

Statistics about the Australian grocery market in 2010 indicate that Woolworths (40%) and Coles (32%) have a combined share of the market that totals 72% (Source: IBISWorld February 2011). This scenario does not allow for effective competition in the market because of the small number of like competitors. As the two major chains increase their market share competition becomes even more diluted and the complete supply chain through to the consumer will suffer. The major chains are able to force changes on the market by promoting immediate consumer benefits through reduced prices and thus circumvent their real long term plans.

We do not advocate re-regulation of the dairy industry. However, there needs to be some mechanism introduced into either existing laws or via a National Food Security Policy to protect our food security for future generations. If Australia is to increase food production and maintain agricultural industries and associated manufacturing capabilities we must ensure that the whole supply chain remains profitable. In addition, land use and land sale policies should be developed to protect the long term interests of Australia.

9. Any other related matters.

The action of the supermarket chains also relates to many other industries because of their market dominance within the Australian market and the influence that these chains have over the total supply chain, including consumers.

10. Recommendations for consideration

- Investigate the current milk price discounting in terms of anti-competitive behaviour.
- Implement recommendations in Senate Economics Committee's report titled "*Milking it for all it's worth – competition and pricing in the Australian dairy industry"*.

- Introduce changes to Competition and Consumer laws to limit market dominance or market share allowable to ensure a better competitive environment.
- Introduce a Retail Grocery Ombudsman.
- Introduce a National Food Security Policy that ensures producers are guaranteed appropriate margins and not held to ransom by market dominate retailers or manufactures.

Yours sincerely,

Bob Paton
Secretary **4 March 2011**
11_senate_supers_lbp.docx