Competition Policy

What's that got to do with the price of milk?

Discussion Paper

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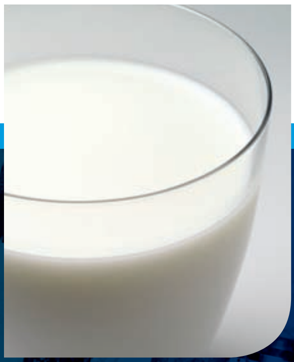

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This paper is the first of a planned series of five case studies that test the dominant paradigm of microeconomic "reform" in Australia. The aim of this paper is to enhance discussion on what I believe has been one of the most substantial policy changes in this nation's history, with almost no depth of public debate.

Dee Margetts

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Introduction

Whilst National Competition Policy (NCP) is arguably the biggest policy change ever adopted within Australia[1], public debate has been limited to the margins. But despite the enormous implications, mention of the term "National Competition Policy" is likely to be met with a blank stare from most Australians. There has, however, been a level of public debate around the social impacts of NCP-driven deregulation of the Australian dairy industry. One element of that debate has been whether the way dairy farmgate deregulation took place in Australia was 'inevitable'[2], and whether, by extension, that means it does not need to be reassessed.

One reason for the level of public interest controversy over dairy market deregulation is that, milk and dairy products are considered a dietary staple, which makes demand for market milk quite inelastic. Almost half of Australia's milk and dairy produce is still consumed domestically (Spencer 2004a: 9). Whilst there are other options such as long life milk or powdered milk, Australian consumers generally continue to prefer the fresh product.[3]

The origins of dairy industry deregulation began when Australia experienced a shift in economic policy with the coming to power of the Hawke Labor Government in March 1983. The signing of the Australia-NZ (CER), an agreement which had been negotiated by former Liberal Prime Minister Malcolm Frazer (Department of Foreign Affairs and Trade 2007), one of the Hawke Government's first official acts, put extra pressure on the Australian dairy export sector to find ways to reduce costs in order to compete more effectively with New Zealand. Economic policy began shifting even further with the introduction of financial deregulation and preparations for further trade and free-market reforms (PC 2003: 46).

Prior to the implementation of NCP, deregulation of the Australian dairy industry had occurred in stages. Before 1986, pooling arrangements existed for both domestic and export milk produced in Australia (Senate Rural and Regional Affairs and Transport References Committee [SRRATRC] 1999: 20). In 1986, during the time of the Hawke Labor Government, the Minister for Primary Industry, John Kerin, introduced a new market support scheme with the intention of making the dairy industry more market oriented. Between 1986 and 1992, export support was wound down from 44.2% to 22% above world parity prices. (Ibid: 21) This was followed by the Crean plan, (prompted by findings from Industry Commission inquiries into rural marketing arrangements and the dairy industry in particular

[1] Whilst previous steps in the Hawke/Keating Labor Government's microeconomic reform agenda, such as financial deregulation and tariff reductions affected parts of the economy, the impacts of National Competition Policy spread throughout Australian economy and society.

[2] See Cocklin and Dibden 2002

[3] Dairy Australia reports that the share of Australian milk production used in exports increased from 44% in the early 1990s to almost 60% in 2002/03 but fell back to 50% in 2004/05 as a result of the decline in total industry output. (Dairy Australia, 2006:11) This means that some milk production which would normally be directed to manufactured product for export was diverted to the fresh milk market.

in 1991, both of which will be considered later in this paper in some detail) which saw the extension, but gradual reduction in export assistance from July 1992.

This reduction in export assistance coincided with a range of export tariff reduction schemes in Australia associated with the April 1994 signing of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). Australia's commitments to the World Trade Organization (WTO) under this agreement required the termination of export subsidies (domestic industry assistance was still permitted but it was required to be totally unconnected to export sales).

The Crean Plan for market assistance for dairy exports was subsequently stopped on 30 June 1995 to be replaced by a Domestic Market Support Scheme (DMSS) which supported the domestic manufactured milk sector (Ibid: 21). The DMSS was designed to wind down and to be abolished by 2000. Its planned abolition is recognised by the industry as the first stage in the Federal Government's implementation of the NCP reforms into the Australian dairy industry (Dairy Australia 2003a: 8). It should be noted that the DMSS was industry funded. Levies were charged per litre to milk manufacturers and to market milk producers to assist the producers of milk for use in Australia's domestic value-adding sector.

The 1992 submission to the Hilmer Inquiry by the Australian Dairy Industry Council, which included the United Dairy Farmers of Victoria, had opposed dairy deregulation on public interest grounds (ADIC 1992). However Victorian dairy farmers had been by far the greatest beneficiaries of the DMSS (Ibid: 23), and therefore the greatest losers from its abolition and Dairy Australia identifies the winding down of the support for producers of domestic manufacturing milk and the pressures to implement the next stages of NCP change as the major reasons why commercial dairy interests and manufacturing milk producers in states like Victoria, began to push for farmgate deregulation (Dairy Australia 2003a: 8). As shall be shown later in this paper, just prior to deregulation, Victorian dairy farmers were receiving farmgate prices even lower than that paid to New Zealand dairy producers. With the removal of the DMSS looming, dairy producers in the large Victorian dairy cooperatives saw an option to use further NCP–driven changes to secure, or regain, a market advantage over the other states by the removal of the market milk premium (Cocklin & Dibden 2002).

Prior to farmgate deregulation in mid 2000, each state had regulatory arrangements for market milk quota or pooling arrangements and the setting of farmgate prices for market milk to help ensure year-round, reliable and adequate supplies of fresh milk. Market milk pooling provided an equitable sharing of the higher farmgate prices which market milk attracted compared to milk used in manufacturing. In non-pooling states, such as Western Australia, the dairy industry operated under a tradeable quota and market regulatory system administered by the Dairy Industry Authority of Western Australia (SRRATRC: 31). A more detailed description of each state's pre-deregulation dairy market arrangements are provided later in this paper.

The DMSS, as it applied only to domestic value-added production, was designed to comply with Australia's WTO obligations (Ibid: 22), but as shall be seen, the Industry Commission had not just pushed for the removal of export assistance[4], they also argued for domestic

[4] Originally the Tariff Board's role was to advise on taxes and assistance for internationally traded commodities. Its successor, the Industries Assistance Commission, whose role in the early 80s (after the election of the Hawke Labor Government) turned to approaches to reducing s industry protection, and then by 1989, renamed the Industry Commission, under the *Industry Commission Act 1989* which spelt out the government's desire to reduce industry regulation. (PC 2003: 2/3)

market deregulation arguing that domestic market milk prices would fall as a result. Cocklin and Dibden identify three main components of dairy deregulation; the removal of the DMSS, the removal of state based price and supply management systems and the offer to pay compensation packages to farmers (Cocklin & Dibden 2002: 32).

The changes leading to dairy market deregulation were pushed by the Industry Commission, as part of the Government's free trade agenda, but the arguments supporting National Competition Policy were that it would bring about domestic benefits which are greater than any associated social costs.

The targeted or measurable 'public benefits' of National Competition Policy, are unclear although terms such as 'greater efficiency' 'improved productivity' and 'improved international competitiveness' have been used alongside terms such as 'increased community welfare' (Hilmer et al 1992). This paper will argue that predictions of the outcomes in relation to dairy industry deregulation were largely based on untested assumptions. This paper will also argue that the assumptions of the benefits of the implementation of National Competition Policy, including the dairy industry, were not tested by systematic monitoring or assessment, nor were there systematic assessments of the social impacts of deregulation in the targeted sector, or the impacts on regional development. The abstract goals of NCP do not include regional social impacts. This paper will assess the strength of their original argued case for NCP-driven deregulation against currently available data on outcomes in the dairy sector.

This case study will critique a number of official reports and reviews prior to and after Australia-wide farmgate deregulation was implemented in mid 2000, and in the process, seek to find answers to the following questions:

- Who are the main beneficiaries of NCP- driven deregulation of the Australian Dairy industry?
- Has dairy market deregulation resulted in a more efficient resource use in the Australian dairy industry?
- What are the outcomes for Australian dairy consumers?
- Is there more or less competition in the Australian dairy market after NCP – based deregulation?

Along with these specific questions are the inevitable value judgements of whether the basis for policy making in this area has been sound and if not, what remedies should be sought?

This paper argues that NCP-driven dairy market deregulation was enabled by the ideological preferences in some parts of Government for the "free"-trade and "free" market agenda and driven by the potential "winners", not the public interest. [5] It has

[5] *"… the current economic policy mix that has given birth to Competition Policy is a version of neo-classical economic theory which, having rejected Keynesian demand management, also tends to ignore the warnings of Galbraith. The free market assumptions of Friedman-style economics (minus the money supply intervention) appear again in deregulation and microeconomic reform. The goal of reducing costs to industry is paramount in the quest for international competitiveness and this has been largely focussed on attaining economies of scale as well as reducing costs of labour, taxes and regulation (including those which inhibit access to markets). The combined push for deregulated markets at a global and domestic level is widely referred to as 'economic rationalism'. Economic rationalism gave birth to National Competition Policy".* (Margetts 2001: 23)

contributed to reduced dairy farmer bargaining power and increased regional social (and environmental) costs. The market power shift has also enabled economic cost and risk shifting from the ever more concentrated retail and dairy manufacturing sector onto dairy farmers, contributing, by 2006, to a reduction in average dairy farm total factor productivity growth, a loss of Australian dairy manufacturing capacity to overseas interests, a growing shortage of domestic fresh milk supplies and higher average domestic retail milk prices.

As well as the 1993 publication, *National Competition Policy, Report of the Independent Committee of Inquiry*, which is generally referred to as the “Hilmer Report”, this paper will assess the official predictions in some detail from influential publications which called for dairy market deregulation; the main Industry Commission reports referred to earlier in this paper and, in order to help assess outcomes against these assumptions or predictions, this paper will also critique two of the major post-deregulation assessments produced for or on behalf of Government bodies on the impacts of dairy market deregulation.

Policy Context

In searching for the theoretical basis of NCP, it is most significant that, two years after the publication of the Hilmer Report, Fred Hilmer wrote that:

“*Many of the areas of competition policy are not amenable to simple answers based on proven principles. The economic logic on which competition policy is based is still being formulated*.” (Hilmer 1995: 24)

As was argued in Margetts, 2001, so-called “economic rationalism” gave birth to NCP and both were linked to corporate globalisation. This view appears to be supported by the former federal Labor Member for Adelaide, Bob Catley, in his 1996 publication, “*Globalising Australian Capitalism*”:

“*During the 1980s, the **national political elite** reached a broad consensus that Australia would need to open or internationalise its economy in order to meet the **unavoidable challenge of globalisation**…this eventually produced **economic rationalist policies of deregulation and privatisation** with a view to making Australia more competitive*.” (Catley 1996: 2) (Emphasis added)

Catley (1996: 62) wrote that, having taken over from Jim Cairns, in August 1975 the new Federal Labor Treasurer in the Whitlam Government, Bill Hayden, produced a budget, influenced by the visit in April of that same year by well-known ‘Chicago School’ monetarist, Milton Friedman, “…*under the rubric of ‘economic rationalism’”* Prior to that, the new Whitlam Government had also cut tariff protection by 25% in a range of Australian Industries, a move which proved to be unpopular with voters as well as causing schisms within the Labor Party (National Archives 2007a). The Hayden 1975/76 budget was, of course, never implemented but the Friedman influence was evident even after the 1975 dismissal. [6] The National Archives of Australia report that the Fraser Liberal Government which followed, began reducing government expenditure and streamlining the public service but they point out that:

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[6] The way Friedman influenced economic policy in 1970s/80s Australia is examined in “*How Milton Friedman came to Australia: A Case Study of Class-based Political Business Cycles*” Courvisanos and Millmow (2005).

"*In the macro-economic arena, Fraser modified rather than led, the reform push. Within the Liberal Party in the late 1970s, the 'new right' emerged – followers of the economic rationalist theories of Milton Friedman and known as 'economic rationalism'. Within the party, economic rationalists were known more familiarly as 'the dries'. Anyone on either side of the House wanting to prioritise social development or welfare measures were dubbed 'wet' and, by comparison, irrational*." (National Archives 2007b)

Catley attempts to explain and justify how and why senior bureaucrats and the Cabinet of the Hawke/Keating Labor Governments picked up and ran so hard with the economic rationalist theme (introduced during the Whitlam era) after coming to Government in 1983, but near the end of the book, without ever referring specifically to National Competition Policy, he admits that the outcomes of deregulating the internal economy were likely to lead to greater inequalities, regional population drains, a less broadly based economy and less self sufficiency (Catley 1996: 208) stating also that:

"*Many of these policy directions will be seen, and some have already been described as contrary to the Australian tradition and, more particularly, as betraying ALP principles*," (Catley 1996: 221)

However, Catley's final justification is that there was no alternative:

"*The globalising of Australia's capitalism described in this book has become unavoidable, necessary and desirable*" (Catley 1996: 222).

However, the terms, "unavoidable "necessary" and "desirable", appear to be at odds with Catley's own stated concerns regarding the ideological choices and the driving forces of such changes.

"*Treasurer, John Dawkins (1991-93) moved the Industry Commission to Melbourne in the hope of relating it to the real world of commerce. Seized by economic rationalist thinking during the 1980s, these Ministries drove the reorganisation of the national economy and its internationalisation. Dawkins was being somewhat disingenuous when he later ascribed Labor Government strategy to the Business Council of Australia, though there was some congruence.*" (Catley 1996: 101)

The view that 'there is no alternative' is also questioned by Quiggin, who emphasised the need to assess microeconomic reform, rather than just surrender to corporate pressures:

"*A careful assessment of the gains and losses of microeconomic reform and of the areas in which reform has succeeded and failed may help to guide the path of reform and to identify policies that would yield greater benefits to ordinary Australians than have been adopted in past.*" (Quiggin 1996: 22).

Even supporters of the basic economic tenets of NCP, such as Law Professor, Bronwen Morgan, acknowledge its impact on Australia's most vulnerable groups. However, Morgan describes NCP as a 'meta regulatory system' of unprecedented scale, scope and comprehensiveness (Morgan 2003:10) with powers akin to that of a constitution, which can place 'extra-political constraints' on legislation and lawmaking by way of 'economic adjudication' (Ibid: 27) and powerful enough to enforce economic rationality (Ibid: 72). However, whilst Morgan acknowledges that NCP was sponsored and promoted by a coalition of business interests and technocratic officials (Ibid: 50) and driven politically by the Right faction of Labor (Ibid: 64), she uses terms such as ‘objective’ and ‘neutral’ to describe NCP’s economic rationalist power structures, appearing to support their overriding of democratic processes:

The economic rationality of cost-benefit analysis which dominates meta-regulatory regimes lays claim to an objectivity and neutrality which will temper the arbitrary exercise of political power (Ibid: 31).

The globalisation of Australia’s internal economy tended to focus on “international competitiveness” by means of economies of scale (that is, upsizing and amalgamations) and reducing costs to industry by way of reducing labour costs, taxes and regulation (Margetts 2001: 23).

Paul Keating, a free trade enthusiast, also saw NCP as a means of Australia taking a lead role in global free trade negotiations. Keating made the links between trade policy and NCP quite clear when he announced in his press release relating to an earlier pivotal Industries Assistance Commission inquiry which produced the, “*Government, (Non-Tax) Charges*” report that it was specifically designed to assist the Australian Government in negotiations surrounding the Uruguay Round of GATT. [7] In order to help in the implementation of this major policy change, as shall be seen, even the Productivity Commission admit that the Government chose to make powerful allies of the corporate sector to line up against the likely “losers” from the implementation of such policies. [8] [9] This introduces what appears to be a major inconsistency in the policy directions of the time – if major parts of the agricultural sector were identified as potential “losers” from Competition Policy, and the rationale for Australia’s targeting the agricultural sectors for deregulation was to try to influence the rest of the world sufficiently that they would to agree to agricultural free trade, on the assumptions that that would to improve the outlook for those same sectors.

Ironically, Kenyon and Lee (Kenyon & Lee 2006: 42) report that:

“*Australia consistently argued* (up to 1986) *that the lack of benefits it had received on agriculture justified its maintenance of an industrial tariff that was not subject to GATT bindings.*”

The “benefits” to which they refer presumably relate to the assumed benefits of agricultural free trade. This statement indicates that up to that time, Australia’s position had been to try to use the manufacturing sector as a bargaining chip to achieve what they wanted in other

[7] In 1986 Australia inaugurated a meeting of 14 agricultural exporting nations in Cairns, Northern Queensland, to push for agricultural free trade leading into the Uruguay Round of GATT. This group became known as the Cairns Group (The Cairns Group 2005) By July 1988, the Cairns Group had submitted a proposal on agricultural trade liberalisation calling for the elimination of all production or consumption subsidies affecting agricultural trade (Congress of the United States Congressional Budget Office 1988: 1). A further explanation of the links between trade and competition policy is provided in Margetts 2001: 23-30)

[8] PC 2003: 58)

[9] Catley’s explanation of this close big business association was that, after a decade in office, Labor Ministers devised a strategy of getting big business onside, including:
“Going to business meetings, dinners and conferences, and exhorting business leaders and managers, some of whom have been less than enthusiastic about the program, to pursue globalisation and competitiveness...”, adding that *“...Leaders of the modern Labor Party must co-ordinate their program with business, although, as we have seen, it is not business that designed them.*” (Catley 1996: 105)

sectors, such as agriculture, in trade negotiations. That indicates that they knew Australian manufacturing would be harmed by "free"-trade.

As well as being seen to take a leading role in economic deregulation to somehow impress the rest of the world during the negotiations for the Uruguay round of GATT, reducing the regulatory or other non-tax government costs for big business via competition policy in Australia was also seen as a means of helping corporations operating in Australia "compete" internationally with the assumption that this would benefit the entire economy. And as shall be seen from the dairy example, opening up more of the internal economy to deregulated market forces also opened up many more trans-national corporation takeover targets.

In the Report of the Independent Committee of Inquiry (more commonly referred to as the "Hilmer Report"), there are links between trade and market deregulation and whilst there are no clearly stated consumer outcomes there are references to the combined impacts of the reduction of trade barriers and the relaxation links to the relaxation of restrictions in competition within Australia:

"*…in sectors as diverse as telecommunications, aviation, egg marketing and conveyancing. Consumers are already obtaining substantial benefits through these reforms*." (Hilmer et al: xvi)

And furthermore when discussing **competition** itself:

"Competition offers the promise of **lower prices** and improved choice for consumers and greater **efficiency**, higher economic growth and increased **employment opportunities** for the economy as a whole." (Ibid: 1) (emphasis added)

But the report also qualifies that:

"*Competition policy is not about the pursuit of competition per se. Rather, it seeks to facilitate effective competition to promote* ***efficiency*** *and economic growth while accommodating situations where* ***competition does not achieve efficiency or conflicts with other social objectives***." (Ibid: xvi). (emphasis added)

It will be shown later in this paper that the then Labor Treasurer, Paul Keating, and the Industries Assistance Commission (IAC) made a point of targeting agricultural marketing arrangements. The views and preferences of Paul Keating, the (renamed) Industry Commission, and other free trade enthusiasts clearly influenced the Hilmer Inquiry, as did their assumptions that rural marketing arrangements were detrimental to the price, efficiency and quality of Australia's agricultural product. A section of the report specifically dealing with agricultural marketing also presented the view that they impeded the development of value-added manufacturing capacity within Australia:[10]

[10] As shall be seen, these were simplistic assumptions. They may have been driven more by a fear that any such arrangements for price, quality and quantity are (or would appear to be) an export subsidy, than by any realistic modelling. In the light of the very strong Cairns Group views on agricultural assistance there was likely to have been a concern amongst Australian trade negotiators that other countries would **perceive** such agricultural marketing arrangements as an export subsidy, making free trade negotiations more difficult, i.e. it may have had little, if anything to do with the international price of milk, so to speak!

"*As well as the impact on **consumer prices, price** and **quality** effects of these arrangements flow on to **Australia's food processing industry**, and can impede the development of internationally-competitive value-added industries in Australia*." (Hilmer et al, 1993: 141) (emphasis added)

Dairy Market Deregulation in Australia

As we have seen, the Hilmer Inquiry arose from the recommendations of a number of previous inquiries undertaken by the IAC[11] (which became the Industry Commission in 1990, and still later, in 1998, the Productivity Commission). Most notably, the model for NCP came from the recommendations from an IAC inquiry into Government (Non-Tax) Charges, commissioned by then Federal Treasurer, Paul Keating in June 1988, and following the release of his May 1988 Economic Statement. The Terms of Reference referred to "*…the impact of significant government charges (other than taxation) on the international competitiveness of Australian industries…*" (IAC 1998: 101) and even though it did not specify which type of industries were being targeted, the submissions were strongly representative of the corporate sector, particularly mining (IAC 1998: 106-144). It thus became an inquiry largely focussed on ways to reduce the regulatory or other (non-tax) government costs for big business[12] in order to help these corporations "compete" internationally[13] and to open up more of the Australian economy to overseas investment. The IAC's report was published in September 1989.

Along with Keating's May 1988 Economic Statement, the IAC report thus played a major role in the development of NCP. To quote from the Productivity Commission:

"*The report, in identifying inefficiencies and their impact on business competitiveness, had a long term impact. The Government used it in developing its microeconomic reform*." (PC 2003: 54)

From the IAC's inception 1974, there had been a range of reports relating to statutory marketing arrangements.[14] Looking at their major findings, at a point in the early 1980s [15] the

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[11] In 1989 the IAC became the Industry Commission, with a more specific focus on industry deregulation, and still later, in 1995, the Productivity Commission.

[12] This view is supported by the then Leader of the Opposition in the Senate in 1989, Senator Fred Chaney, who noted the IAC's support for the introduction of corporate investment in the form of "foreign competition" and emphasised that by far the biggest winner from the IAC's microeconomic reform agenda would be the mining sector (Senate Hansard 1989: 2878-9). John Quiggin's submission to the 1993 Industry Commission Inquiry also backs this up. He states that the ORANI model, upon which the IC's theoretical framework has been based, favours the mining sector at the expense of manufacturing, and capital at the expense of labour (Quiggin 1993:22).

[13] In effect, as shall be seen from the dairy example, it also left such corporations open to take-over by trans national corporations.

[14] See "*IAC Reports Considering Statutory Marketing Arrangements*"(IC 1991: 137-148)

[15] This coincided with the 1983 election of the Hawke Labor Government which saw a significant shift in government policy and followed the 1981 publication of *Australian Financial System: Final Report of Inquiry into the Australian Financial System* (the "Campbell Inquiry"). The Hawke/Keating Labor Government's first major policy reform involved the floating of the Australian dollar and the abolition of exchange controls in December 1983. The Productivity Commission quotes free trade, free market enthusiast, Professor Ross Garnaut:
"*The floating currency and removal of exchange controls, the dismantling of most protection in a series of decisions from 1983, and a wide range of other reforms to remove structural rigidities, raise productivity and strengthen the educational base, marked a sharp break from earlier Australian policy.*" (PC 2003: 46)

recommendations of these inquiries generally changed from recommendations to assist industry to recommendations to remove industry assistance and regulatory control. The Productivity Commission have acknowledged this change:

"…*as a harbinger of things to come, the IAC reported to the Government on approaches to general reductions in protection (1982) and on harmonising the customs tariff (1986*)" (PC 2003: 2)

The Government clearly recognised there would be winners and losers from such a major departure from past policies and approaches and found ways to give the whole process a big business investor focus:

"*The Government harnessed the support of the industries and interests that stood to gain from the reforms by enhancing their political power through its 'recognition' of 'peak' interest groups; it sought to lower the resistance of potential 'losers' by structural adjustment assistance and 'compensation'*" (PC 2003: 58)

Given, as we have seen, that the Government's role in initiating the Cairns group of agricultural nations in relation to the negotiations leading to Uruguay round of GATT negotiations, and the Cairns Group's 1988 call for the elimination of all agricultural subsidies, it is not surprising that in May 1990, Treasurer Paul Keating commissioned the IAC's successor, the Industry Commission (IC), to conduct a targeted inquiry into Statutory Marketing Arrangements for Primary Products despite that fact that none of the submissions to the IAC's inquiry into Government (Non-Tax) Charges argued for their abolition (IAC 1989).

The IC's low regard for the efficiency of those primary industries subject to statutory marketing arrangements at that time and their positive assumptions for domestic dairy consumers and (mostly negative) projected effects for dairy farmers and manufacturers of the removal of statutory marketing arrangements for milk can be summarised as follows:

- price distorting effects of statutory marketing arrangements would be relatively small;
- domestic prices would be lower;
- output for manufacturing milk would decline by 10 percent;
- exports of processed foods would decline;
- the dairy industry would become a marginal exporter, its exports having; being simulated to decline by around 80 percent;
- a decline in output and employment is predicted of around 10 percent for manufacturing milk; and
- consumption of market milk would rise leading to a slight expansion in output and employment in that sector

(IC 1991a: 230)

Later in this paper, we shall return to these projections, along with others the Industry Commission used as justification for the scope and nature of NCP changes in the Australian dairy industry, to test their accuracy. As shall be seen, there is a very strong case for an independent review of these assumed outcomes, given the influence that these reports had on the National Competition Policy legislative and regulatory review process, and ongoing policy positions by Government and those bodies advising on or enforcing National Competition Policy.

In December 1990, Paul Keating also commissioned the Industry Commission to conduct a specific inquiry into the Australian Dairy Industry, the terms of reference specified that:

"*…in reporting on market milk and manufactured dairy products, the Commission identify institutional, regulatory or other arrangements subject to influence by Governments in Australia which lead to **inefficient** resource use and advise on courses of action to **reduce or remove such inefficiencies**…*" (IC, 1991b: 1) (emphasis added)

This would appear to be saying that the Treasurer also assumed dairy market regulatory authorities helped make dairy producers inefficient and that their removal would benefit the wider Australian economy.

This report included the following recommendations, which they said:

"*…must be considered as an integrated package, are aimed at increasing the welfare of the Australian community through;*

- *removing price distortions, particularly the artificial distinction between market and manufacturing milk, and the unnecessary costs they impose on society;*
- *ensuring that milk is produced in the least-cost location relative to market outlets;*
- *reducing the extent of unnecessary government intervention in the industry; and*
- *ensuring that the industry has the flexibility to adjust to changing circumstances and to capitalise on market opportunities.*"

(Ibid: xiv)

Given the weight these recommendations carried, based on assumptions about the outcomes and the implications for the "welfare of the Australian community", it is worthwhile looking at each of these recommendations in more detail.

1 – "**removing price distortions, particularly the artificial distinction between market and manufacturing milk, and the unnecessary costs they impose on society**"

The Industry Commission itself admitted that, on average, the "price distortions" of statutory marketing arrangements were relatively small (IC, 1991a: 230). It is acknowledged, however, that the farmgate prices for manufacturing milk were much lower than that of market milk, however, it may also have been partly a function of the fact that the farmgate prices for Australian manufacturing milk were low and considerably less than the international "average". In 2000, whilst our Victorian manufacturing milk producers were being paid around AUD $0.22 c a litre, the average European farmgate price for milk was 30.67c Euro (AUD $0.49) and even New Zealand milk prices were higher than in Australia at 16.64c Euro (AUD 0.26) (LTO, 2002: 4).

In relation to the "artificial distinction" between market and manufacturing milk prices even the supervisors of National Competition Policy legislative change, the National Competition Council, in attempting to justify their position on dairy deregulation post-facto have since admitted that there **are** increased costs and risks attached to producers of year round fresh milk;

"*Processing of* (market) *milk requires a reliable flow of milk on a year round basis as there is little if any seasonality to milk demand…*

"*…Farmgate prices in these regions tend to be higher to reflect the higher cost of producing a year-round supply of milk to processing plants. This is due to the need to provide supplementary feeding of grains, concentrates and stored fodder, which has a higher cost than pasture grazing*." (Spencer 2004b: 14)

And a similar case was put, post deregulation, by the Australian Bureau of Agricultural and Resource Economics (ABARE) on behalf of the (statutory dairy levy funded) industry body, Dairy Australia:

"*In year round milk production, calving of cows is spread throughout the year to enable milk production to be maintained during the year. Year round calving was traditionally used to provide a constant supply of drinking milk. It remains the dominant production system in most of Queensland, Western Australia and northern New South Wales, areas that historically had a larger proportion of their production used for drinking milk.*

Historically, average production costs for year round producers have been higher than other systems, reflecting the costs of feeding cows when seasonal pasture production is below requirements." (ABARE 2005a: 4)

They go on to explain that whilst year round producers have been forced by reduced farmgate prices for market milk, to cut their production costs, increasing irrigation costs, particularly in the Goulburn and Murray Valleys have meant that the production costs of seasonal producers are rising and getting closer to those of year round producers.

Milk is a commodity which, worldwide, is generally produced for local consumption. It is estimated that in 2004 only about 7% of the world's dairy output was traded (Spencer 2004b: 11).

The same author, earlier that year, this time on behalf of "Dairy Moving Forward"[16], admitted that there is no set "world price" for dairy commodities:

"*There is no such thing as an exchange-traded "world price" for dairy commodities. The world market in dairy does not operate as other tradeable commodities such as grain, sugar and cotton, in that there is no single recognised trading exchange that sets prevailing "world prices*"" (Spencer, 2004a: 11).

This paper argues that, with a product such as milk, which has such an inelastic demand curve, in times such as drought when the costs of water and supplementary feed are higher, it is not "efficient" to attach domestic fresh milk production artificially to a mythical international milk price. If the domestic farmgate price is not linked sufficiently to local supply circumstances, such as the need to pay more for water or supplementary feed in times of drought, there will be insufficient fresh milk supply and many milk suppliers will have insufficient margins to remain in the industry, leading to longer term fresh milk shortages and unused processing capacity.

[16] Dairy Moving Forward formed in early 2004 as a collaborative dairy industry initiative, in conjunction with Dairy Australia, in a period of widespread drought and lower than average milk prices. Its activities include research and publications, farm business plan development, meetings, events and advisory support for dairy farmers (Dairy Moving Forward 2006)

In other words, where milk production was primarily for the fresh milk market, in the past, dairy farmers have been able to make sure they have sufficient supply by planning to produce a little more than the market demands for fresh milk on the understanding that any overproduction can be sold at a lower price (because that is what they were being offered in line with lower international milk prices). Fresh milk quotas and regulation were there to ensure production efficiency and market balance, something that may be found to be lacking in the current system if supply fails to meet domestic demand.

As this paper will show, one outcome of forcing the Australian fresh milk market to accept the lower farmgate prices is that many dairy farmers have already left the industry. In WA, for instance, milk production figures published on Dairy Australia's website shows milk production in 2004/05 totalled 395.8 million litres, in 2005/06 380.0 million litres and in 2006/07 it had dropped to 349.4 million litres (Dairy Australia 2005, 2006, 2007). On the 28th of February 2007, the West Australian Newspaper reported that, due to poor farmgate prices and farm departures, National Foods were bringing tankers across the Nullarbor, in this case to fill export contracts (Thomson 2007a: 7) and again on the 2nd of March where dairy farmer representatives warned that WA's milk shortage would worsen unless the farmers were paid more (Thomson 2007b: 14).

Any system of milk marketing in Australia which fails to factor in changing climate, the real costs of irrigation at a time of growing water shortages and increasing petroleum prices cannot be fully resource efficient. [17]

As we shall see, the prices for manufacturing milk just prior to deregulation were already low by world standards but even in predominantly market milk producing states such as Queensland and Western Australia (where the average costs of milk production were likely to be higher because they were producing year round) dairy manufacturing provided a market for any excess production of a product which in its unprocessed form had a limited shelf life. A well-run farmgate price and milk quota system provided the double benefit of ensuring consumers of sufficient production for the local fresh milk market and limited excess production.

The projected outcomes on Australian society of removing the difference in price between market and manufactured milk were part of the package of largely unproved assumptions pushed on the Government by the Industry Commission on behalf of the likely "winners", the corporate sector.

If nothing is done to reconsider the deregulated market environment, many more dairy farmers, having reached the limits of sustainability, will leave the industry, leading to a shortage of production capacity and fresh milk in those markets, to the detriment of consumers.

2- **"ensuring that milk is produced in the least-cost location relative to market outlets**"

Dairy market deregulation is a blunt instrument. The statement above assumes that those who survive the removal of statutory market arrangements and industry regulation will be the

[17] See Appendix A

lowest cost or most efficient producers.[18] However, a comparison of measured efficiency (prior to deregulation), average loss of gross incomes and dairy farm departures by state indicate that this assumption is an over-simplification. It is true that the largely market milk producers of Sub-Tropical Queensland had the lowest average technical efficiency levels (over 6 inputs) prior to deregulation and Queensland and has suffered the highest levels of farm departures in the post-deregulation period but whilst Victorian dairy producers were assumed to be Australia's most efficient producers because they were being paid lower farmgate prices, it was WA market milk producers who were found to have the highest average technical efficiency (over 6 inputs) than any other milk producing region, (Fraser & Graham 2005: 6). WA producers experienced the second highest percentage income loss of any of the states (-22.1%) (Spencer 2004: 26) but, so far, the second lowest percentage of farm departures (23.3% compared to an Australian average of 28.5%) from 2000 to 2005 ABS 1992-1995, 1996a, 1997a, 1998-2005, 2006a). However, from 2000 to 2004 WA suffered the highest percentage of regional employment loss of any of the milk regions post deregulation, meaning they had to find cost savings in other ways than simply producing more milk.[19] A survey by Dairy Australia indicates that, in the next few years, 34% of the remaining Western Australian dairy farmers are considering leaving the industry, second only to Far North Queensland (40%) (Dairy Australia 2006: 25).

Dairy Australia expresses the ongoing pressure on market milk producers as follows:

"*Due to the transparency of world market prices,* ***and the structure and practices of the retail grocery sector****, there is no effective sustainable premium over time for sales into the domestic market compared to domestic returns, when all cost are considered*." (Dairy Australia 2006: 11) (emphasis added)

"There has been a decline in milk production in northern dairy regions in recent years due to the combined effects of continuing drought on the costs of year-round milk production, and the commercial pricing of milk at the farmgate." (Dairy Australia 2006: 36).

And as has been mentioned above, whereas the market outlets for manufactured milk can be quite dispersed, it is different for market milk. By removing much of the premium for market milk and pushing more fresh milk producers out of business, the costs of transport and storage take on greater significance, especially in a time of rapidly increasing fuel costs.[20] These kinds of medium to long term "efficiency" issues were rarely, if ever, taken into consideration in the lead up to the removal of statutory marketing arrangements and other dairy market regulation.

There are also wider resource use "efficiency" issues which surround irrigated dairy feedlots, (especially in times of drought). The costs of irrigated dairy feedlots must include consideration of the water required per litre of milk produced and the comparative fertiliser, fuel and salinity costs of dairy production, especially where seasonal milk producers are being asked to convert to year-round production to help reduce any unused capacity of dairy

[18] Joseph Schumpeter would have called this "creative destruction" (Schumpeter, 1975: 82-85).
[19] See discussions later in the paper comparing pre-deregulation efficiency, loss of gross incomes state by state and farm departures.
[20] Reasons for this are, as shall be seen, is that fewer and more dispersed fresh milk producers and greater cost pressures placed on the milk processing sector by the retail sector have led to amalgamations and rationalisation of processing facilities. There is also the increased transport of fresh milk across state boundaries, made possible by dairy deregulation, to fill production gaps and keep farmgate prices to a minimum.

manufacturing. This may increase the "efficiency" of dairy manufacturing at the expense of the total factor productivity, social and environmental costs to the dairy farming sector, the sector with the greatest percentage capital risk. Such issues were not part of the IAC reports and recommendations. As will be discussed later in this paper, the multi-faceted nature of deregulation can cause cost shifting and factor inefficiencies in the medium to long-term which were not considered in the narrow "public interest" assessments. There is a strong argument that the scarcity of water in Australia and rapidly rising fuel costs will mean that use of those factors changes the "efficiency" balance of dairy production and should be reconsidered.

Greater retail consolidation (related to NCP) means greater market buying power. This puts extra pressure on processors to rationalise and reduce capacity wastage. Fewer, and larger, dairy processors can then put extra pressure on dairy producers to flatten their production curves. This type of cost shifting at the farm level can generally only be achieved by sacrificing some degree of total factor productivity and increasing purchased inputs such as water and stock feed. A 2005 Dairy Australia survey showed that only 37% of respondents across Australia were operating on a seasonal calving system, compared to 50% in the previous year (Dairy Australia 2005b: 25). Nevertheless, Dairy Australia report that, despite the significant increase in split calving systems in Southern Australia, in a largely manufacturing milk state such as Victoria, there was little difference in seasonality of milk production between 2004/05 and 2005/06 (Dairy Australia 2006: 43).

3- reducing the extent of unnecessary government intervention in the industry

The test of "necessary" versus "unnecessary" comes down to a value judgement, depending on whose interests are being represented. The interests of the big players in the industry (the large supermarket chains and national/international manufacturing giants) have been served by getting rid of further "unnecessary" regulation. The way NCP changes have been implemented means that if they were based on wrong or untested assumptions, it is only after the new market power changes have had their most profound effects that an argument can be remounted as to whether those changes were beneficial or harmful, not only for regional Australia but for the long term interests of the consumer and wider community. This type of re-assessment was never incorporated into NCP.

4- ensuring that the industry has the flexibility to adjust to changing circumstances and to capitalise on market opportunities

This can only be measured over time. The concept of "flexibility" is used frequently as a positive but can also mean finding ways of coping with less sustainable market conditions. It can also refer to the ability, or inability of existing economic structures to cope with the profit maximising strategies of large corproations once their market buying power has been enhanced by deregulation.

Once again, it is necessary to remember that a blunt instrument such as deregulation and the removal of statutory marketing arrangements ensures nothing in particular (except extra survival pressure for much of the industry). In fact, Western Australia, after more than a century of local, or at least, Australian-owned production, the vast majority of local dairy processing industry had been taken over by foreign capital within three years of deregulation.[21] This might suggest that it was the big players who have been "flexible" enough to capitalised on the "market opportunities" created by the cost/price squeeze associated with the major policy changes.

The Industry Commission made the following predictions of the outcomes of their recommendations for the Australian dairy industry based on their assumptions and modelling:

- the farm gate price of manufactured milk would decline between 5 and 9 percent, or 2 to 3 cents per litre;
- prices of manufactured dairy products would fall by around 12 percent as market support payments are reduced;
- the farm gate price of market milk would decline by more than one third, or around 12 to 15 cents per litre;
- the reduction of the farm gate price would allow a similar reduction in the retail price of fresh milk;
- total milk output would likely contract by around 5 percent; and
- Australia would remain a net exporter of dairy products."

(IC 1991b: xv)

They added; "*…it is not possible to predict with certainty the overall effect on retail prices in the medium term. However, **it is certain** that implementing the Commission's recommendations (for industry market deregulation) would result, in the long term, in **considerable downward pressure on retail prices** and in an industry structure conducive to lower retail prices*." (Ibid: xv) (emphasis added)

And; "*In the absence of regulation, there would not be separate prices for market and manufacturing milk. Rather, higher prices would apply for milk produced out of season compared with milk produced in season, reflecting the additional costs of production in times of low pasture growth. The Commission considers that the seasonal price differential would be in the range of 10 to 20 percent*." (Ibid: xvii)[22]

Six years after farmgate deregulation could be considered medium term. These predictions, alongside those of the Industry Commission's previous Report No 10 *Statutory Marketing Arrangements for Primary Products,* 29 March 1991, should be part any NCC or ACCC assessment of whether the policy changes or any related decisions ought to be reassessed for their public interest outcomes.

Since 1995, the Productivity Commission (PC) has published two major reviews on National Competition Policy but in neither have they assessed their own former models and predictions

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[21] See Appendix C

[22] As it turns out, price differentials have been offered mostly in Victoria and Tasmania- those areas where manufacturers are endeavouring to convince dairy farmers to change from a seasonal calving system (possibly to fill the gaps left by departing fresh milk producers) (Dairy Australia, 2006 p 49) But the incentives to move from seasonal production to year round calving systems appears to have just maintained the overall seasonality of milk production:

"*There has been little overall change in the seasonality of milk production in southern Australia despite a significant increased incidence of split calving in herds*". " (Dairy Australia 2006: 43).

against measurable outcomes in those sectors that have been subject to NCP reform. (PC 1999, 2005) In the absence of such Government bodies being willing or able to act in the public interest, rather than as proponents with a vested interest, this paper challenges a number of those original highly influential Industries Assistance Commission (IAC) assumptions. These predictions will be revisited later in this paper, along with the Industry Commission predictions behind their recommendations to end statutory marketing arrangements for milk.

The analysis so far of the role of the IAC/IC has sought to show how parts of the Hawke/Keating Labor Government, with an eye to the negotiations for the Uruguay Round of GATT, along with powerful corporate allies, set the parameters for the Hilmer inquiry of 1992/93.

Jones (2000:1) has pointed out the role played by both the Industry Commission and its predecessor, the Industries Assistance Commission to eliminate industry protection, regardless of it consequences. He also pointed out an even earlier influence, the 1981 Campbell report which:

"*…heralded the merits of competition without comprehending its character. It promised more banks; we got less. It promised an era of the rational allocation of financial resources. We got an orgy of irrational lending practices, $28 bn in bad debts on bank balance sheets, and an asset-inflation boom in turn badly managed with adverse consequences in an ensuing recession…"*

"...Nobody thought officially about the gap between the promises and outcomes before a Labor Government unleashed the 1993 Hilmer report on the public" (Jones 2000: 2)

The Hilmer Inquiry

National Competition Policy did not just appear by public demand. It was driven not only by a wish list from the powerful corporate sector, the Industry Commission and Labor elites such as Paul Keating but also by other influential sections within the Australian Government bureaucracy of the time, including Treasury[23] and the Department of Foreign Affairs and Trade.[24]

Treasury's position is clear from their 1993 submission to the National Competition Policy Review (the Hilmer Inquiry):

"*Treasury considers that the best outcome for the National Competition Policy Review would be for the Heads of Government to commit their respective Governments to progressively implementing structural reform and extending coverage of the TP Act to, in particular,*

[23] It should be noted that Treasury, under Paul Keating, had taken over the responsibility for oversight of the Industries Assistance Commission in 1987, from the Department of Industry and Commerce. (PC 2003: p 27)
[24] A/Prof Evan Jones pointed out that after John Dawkins was appointed Trade Minister in 1985, the Cairns group of 'non-subsidising' agricultural exporters was formed in 1986 under Australian leadership and a "mega-Department of Foreign Affairs and Trade" resourced for trade policy making. He goes on to highlight how Australia positioned itself to "punch beyond it weight" in international trade negotiations. (Jones 2002, p2/3) This could explain the desire to lead the way with National Competition Policy, that is, assuming that other countries would follow suit and that this would assist in meeting the stated goals of the Cairns group for agricultural free trade and the removal of export subsidies in the negotiations for the Uruguay Round of GATT.

unincorporated bodies (such as the professions), State government business enterprises (GBEs) and statutory marketing authorities, in order to achieve lasting pro-competitive outcomes in the sectors where these entities participate." (Department of the Treasury, 1993: ii)

A range of influences, including "*a strong body of elite opinion from academic economists and the Industries Assistance Commission*" had reportedly influenced the formulation of Treasurer Paul Keating's May 1988 Economic Statement which signalled a some major policy direction changes, including substantial tariff cuts and a number of domestic economic reforms and reduction in rural industry support (Goldfinch 1999: 11). The terms of Reference of the 1988/89 Government (Non-Tax) Charges inquiry, required the IAC to have regard for the May 1988 Economic Statement, so, in effect, the IAC helped put together their own terms of reference which then led to the recommendations used to put together the basis of the Hilmer inquiry. From the early 1980s, the IAC had seen "microeconomic reform" as part of the overall push for trade and market deregulation.[25] As has been mentioned, the Hawke/Keating Labor Government, recognising that there would be "winners" and "losers" in such a major policy change, enhanced the political power of the "peak interest groups" (PC 2003: 58). (And this paper suggests that support at the highest levels of Government for the "free-trade" free-market" position made the IAC an effective vehicle to give this corporate power maximum affect.)

Keating's commissioning and directing further IC reports in particular areas including statutory marketing arrangements and specific industries such as dairy, then made sure that the findings and recommendations from those inquiries were taken forward to the next stage of the Governments reform agenda, as part of their planned preparations for Australia's future role on the international free trade negotiations.

The National Competition Policy Review itself was commissioned by then Prime Minister, Paul Keating in October 1992. The Independent Committee of Inquiry, which produced the National Competition Policy model, consisted of three members, the Chair, Professor Frederick Hilmer, Dean and Director of the Australian Graduate School of Management, and Members, Mr Mark Rayner, Director and Group Executive of CRA Ltd, and Mr Geoffrey Taperell, International Partner, Baker and McKenzie.) (Margetts 2001: 29)

Taking the many unproven Industry Commission predictions and assumptions as given, the report of the Hilmer Inquiry incorporated both the IC agenda for rural marketing reform as part of the Government's preparation for the next round of free–trade negotiations and much of the corporate wish list as expressed in the Industry Assistance recommendations. The result was the targeting of specific sectors of the economy:

"*While trade policy reforms have increased the exposure of the internationally traded goods sector to competition, many goods and services provided by **government businesses**, some areas of **agriculture**, the **professions** and other important sectors are sheltered from international competition. Increasing **competition** and **efficiency** in these sectors requires more sustained attention to **domestic constraints on competition***." (emphasis added) (Hilmer et al, 1993: 11)

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[25]See – *From Industry to Productivity: 30 years of 'The Commission'* "Themes from IAC annual report from the 1980s" (PC, 2003: 61)

Given that NCP was part of such a major policy change, transferring major aspects of Government into the competitive environment and subject to the *Trade Practices Act*, and, at the same time deregulating many sectors of the economy, the checks and balances against market power abuse should normally have been at least maintained, if not strengthened. Amongst the assumptions, in the setting up of this inquiry, such concepts as "constraints on competition", "unnecessary barriers to competition" and what is meant by "competition" itself were not clearly defined nor what it meant for "competition" if the outcome of policy changes was to leave far fewer and much more powerful players than before. Chapter 4 of the Hilmer Report addresses "Misuse of Market Power, Mergers & Other Rules" and even cites the kinds of prohibited practices used in other jurisdictions such as Canada, such as:

- Use of fighting brands introduced selectively on a temporary basis to discipline or eliminate a competitor;
- Requiring or inducing a supplier to sell only or primarily to certain customers, or to refrain from selling to a competitor, with the object of preventing a competitor's entry into, or to eliminate him from the market;
- Acquisition by a supplier of a customer who would otherwise be available to a competitor of the supplier or acquisition by a customer of a supplier who would otherwise be available to a competition of the customer, for the purpose of impeding or preventing the competitor's entry into, or eliminating the competitor from the market; or
- Selling articles at a price lower than the acquisition cost for the purpose of disciplining or eliminating a competitor (Hilmer et al 1993: 67)

As an indication of the Hilmer Report's stance on the meaning of "competition", in relation to the misuse of market power they chose to "*…strike a balance between deterring unilateral conduct, encouraging business certainty and minimising regulatory interference in daily business decisions*" so as not to "*deter vigorous competitive activity* " (Hilmer et al 1993: 74). Despite recognising what other countries, like Canada, were doing to prevent market power abuse, the Hilmer report recommended removing Section 49 (which dealt with the prohibition against price discrimination) from the *Trade Practices Act* (Hilmer: 1993:74-80). In other words, they chose to recommend to weaken an important part of the existing Trade Practices provisions for the prevention of market power abuse. This parallels the previously described strategy of the Hawke/Keating Government of siding with the potential "winners" of the process of market deregulation (PC 2003: 58).

Concerns about the possible abuse of market buying power by large food processors and corporate supermarkets was very much in the minds of many dairy producers prior to the introduction of NCP. In their submissions to the Hilmer Inquiry from the Australian Dairy Industry Council (a peak body whose functions include representing the industry's views to the Commonwealth), the Australian Dairy Farmers Federation and the United Dairyfarmers of Victoria, who together represented the vast majority of Australia's dairy producers, all called for state-based dairy regulatory bodies to be retained, in the consumers' and the public interest.[26] [27] [28]

The Report of the Independent Committee of Inquiry on National Competition Policy was published in August 1993. The report was signed, not only by the Committee members, but

[26] Australian Dairy Industry Council, 1992, Submission to NCP Review,
[27] Australian Dairy Farmers Federation, 1992, Submission to NCP Review
[28] United Dairyfarmers of Victoria, 1992, Submission to NCP Review

also by Paul Keating and all State and Territory Premiers and Chief Ministers. Having each State and Territory sign such a report makes it awkward for them to disagree with its directions and findings at a later date.

The Hilmer Report was discussed at the February 1994 Council of Australian Governments meeting and the Heads of Government at that meeting requested two pieces of further work before proceeding, a report on the implications for state government businesses and draft legislation and intergovernmental agreements.

The agreements were drafted by a group of Commonwealth, State and Territory senior officials, known as the COAG Microeconomic Reform Group (MRG) (Churchman 1996: 97), but it was the Commonwealth officials who appeared to have the controlling hand on the content. Susan Churchman, who was a Senior Executive of South Australia's Competition Policy division of South Australia's Department of Premier and Cabinet at the time, describes some of the difficulties state officials experienced during the process as they were limited in both time, expertise and resources. At the negotiation meetings, each state's one or two representatives were confronted by a "phalanx" of Commonwealth officials, some of whom were working full time for the project (Ibid: 98). The state representatives were generally having to cope with a range of other responsibilities and the time available to properly consider each draft appears to have been very limited:

"*Great wads of newly drafted or redrafted material would hit the fax machines a couple of days before the meeting and we would have to analyse it for possible issues and get any necessary legal advice before the meeting. Usually this would have to be done in conjunction with a number of unrelated responsibilities, all with their own deadlines and political imperatives. This could lead to a certain imbalance in the degree of preparedness at the meetings*." (Ibid: 98)

A number of concerns were raised by the states and territories but by February 2005 the only issues where all states and territories agreed were the issue of their voting rights and their share of commonwealth revenue support for the costs of implementation of compensation for revenue loss as a result of some aspects of the agreements. However, the Commonwealth came out unexpectedly with a new intergovernmental agreement which made the payment of that Commonwealth revenue subject to the states and territories being adjudged to be meeting their obligations under the agreements.

"*The new National Competition Council (NCC) has been given the job of deciding whether the states have met these conditions of payment. The former Assistant Treasurer described the NCC as policeman, making sure states do not backslide on their commitments. Many states and territories found such a view offensive as a description of the implementation of a policy which was meant to work through intergovernmental cooperation* (Ibid: 99).

The response of the Federal Government was to adjust their offer of compensation or "tranche payments" until the states and territories agreed to sign the agreement. The finally agreed tranche payment package was to start at $200 million in 1997/98 and rise to annual cost of $2.4 billion a year by 2005/06 (COAG 1995: 1). Effectively, the Federal Government had bought the agreement of the States and Territories.

Government Implementation of Hilmer

The Hilmer package had recommended a range of changes to the *Trade Practices Act* as well as a series of Agreements between the Commonwealth and the States and Territories. Despite the corporate investor focus of the inquiry and the ensuing economic model, nevertheless, Senator Crowley's Second Reading Speech of the *Competition Policy Reform Bill* on behalf of the Government, emphasised **consumer** and **employment** benefits, as well as the perceived need that a "*…more national approach is needed for business regulation*." (Senate Hansard 1995a: 2434) (emphasis added).

"*The payoff from this bill for ordinary Australians is very real. It paves the way for* ***cheaper prices****, more growth and more* ***jobs***." (Ibid: 2434). (emphasis added)

And emphasised that the Government was "*…not interested in reform or competition for its own sake. The package recognises that economic* ***efficiency*** *is one element of a broader public policy context* ***which also includes social considerations****. Explicit recognition is given to these broader elements of the* ***public interest*** *in the bill and the Competition Principles Agreement*." (Ibid: 2436) (emphasis added)

The long term test of the Keating Government's representation of the NCP package is not only whether the assumed benefits such as cheaper prices, more jobs and greater economic efficiency were the medium to long term result from each of the targeted changes but whether those "social considerations" have been properly recognised in the way the states, the NCC and the Federal Treasurer assessed the public interest process. The deregulation of the Australian dairy industry provides a good basis to test these assumptions.

As we have seen, the mostly state-based regulatory arrangements for the Australian dairy industry was just one of the areas targeted by the Industry Commission and the subsequent Hilmer Report. The major means of forcing changes to these targeted areas was the National Competition Policy Legislative Review Process.

The NCP Legislative Review Process

One of the most important (but probably least understood) recommendations from the Hilmer report was the review and "reform" of all Government legislation and regulations at all levels, unless a successful case for public interest could be mounted.

"*The Committee believes that the time has come to progress regulatory reform more broadly, and to do so by reversing the onus of proof in considering the desirability of reforming particular regulation. Consistent with the principles already agreed between governments, in relation to market conduct, the Committee considers there should be no regulatory restriction on competition unless clearly demonstrated to be in the public interest*." (Hilmer et al, 1993: 190)

This recommendation became a core part of the 1995 National Competition Policy agreements between the Commonwealth and the States and Territories and was tied in to the Commonwealth providing progress or "tranche" payments to the states and territories. This process saw the National Competition Council, supervise whilst roughly 2000 pieces of legislation were pulled out for review. It was then up to State and Territory Governments to conduct legislative review processes for their own legislation. This required industry and community groups to know enough about what was going on to mount the case of public interest at their own expense if they wished to retain regulations.

How was "public interest" defined under this process? When the Competition Policy reform Bill was debated in the Federal Senate in 1995, the author questioned the Trade Minister over the meaning, uses and implementation of the term "public interest".

"*I note that the Assistant Treasurer, (Mr Gear) said in a press release two weeks ago that all governments – presumably state and federal - will publish by June 1996 their agenda on implementing the competition principles agreement.* ***A vital part****, according to the press release, '****will be the way each government intends to protect the public interest, and to deliver community service obligations****. Equally important is the role each state sees for local government in the reform process.' In other words, there are currently no guidelines, statements or strategies about how the public interest will be protected. This information will not be available until next year, but we are being asked to pass the bill now…*" (Senate Hansard 1995b: 1757) (Emphasis added)

The response from Senator Cook, from this and other criticisms and questions at the end of the second reading debate included:

*"…(*opposition to the Competition Policy Reform Bill*)… reflects baseless fears about what the bill might do. It does not attack, as has been suggested in this debate, our humanity, for example, or community service obligations, as has also been inferred and suggested.* ***That is a matter that governments will decide individually, as they do now. So this bill does not seek to change those arrangements. It was for each of the state governments as well as this government to decide what the right balance of community service obligations might be and for the democratic process to inform their decision making****.*" (Senate Hansard 1995c: 1884) Emphasis added

The Competition Policy Reform Bill was therefore passed without a definition of public interest, but Part 1(3) of the Competition Principles Agreement lists matters that **can** be taken into account in assessing whether to enforce or exempt a particular arrangement from the principles of NCP. They are:

- *"Government legislation and policies relating to ecologically sustainable development;*
- *Social welfare and equity considerations, including community service obligations;*
- *Government legislation and policies relating to matters such as occupational health and safety, industrial relations, and access and equity;*
- *Economic and regional development, including employment and investment growth;*
- *The interests of consumers generally or of a class of consumers*
- *The competitiveness of Australian businesses; and*
- *The efficient allocation of resources."* (NCC 1998)

As can be seen, there was already a substantial market focus in the "public interest" provisions but, in addition, the legislative review was somewhat circular because of the built in assumption that competition was in the public interest and that even if the public interest of a particular regulatory arrangement could be proven, a non-legislative (e.g. market or industry self-regulatory) approach would be preferable. Clause 5 (9) of the Competition Principles Agreement required those carrying out the public interest assessment to:

a) Clarify the objectives of the legislation;
b) Identify the nature of restrictions on competition;
c) Analyse the likely effect of the restriction on competition and on the economy generally;
d) Assess and balance the costs and benefits of the restriction; and
e) Consider alternative means for achieving the same result, including non-legislative approaches. (NCC 1998)[29]

Theoretically, the power was allocated to the states and territories to make their public interest own judgements, but if the outcomes of any review were not what the National Competition Council decided ahead of time was their nationally preferred approach (in line with the Industry Commission/Hilmer position) they would find fault with the review process and, using the threat of recommending to withhold commonwealth tranche payments to get their way or punish the states until they acquiesced (Margetts, 2001: 89-90). Bronwen Morgan (Morgan, 2003: 202) quotes the Queensland Treasurer as saying in 1999:

"*The NCC has fundamentally exceeded its legitimate role and responsibilities, as provided for under the COAG Agreements. Inappropriately, the Council has sought to question the validity of Community Service Obligations (CSOs) and the 'second guess' the outcomes of public benefits tests. Effectively, the NCC is an umpire which is seeking to determine the outcome of the game, rather than enforcing the rules*."

Morgan, also acknowledges:

"*On the one hand, the NCC made strong attempts to cast its recommendations for penalties, where it made them, in procedural terms, usually by focussing on the fact that a government had failed to follow the pro-competitive recommendations of an independent review. On the other hand, the NCC also objected to reviews on the basis of weak and unreasonable evidence and conclusions*." (Ibid: 202).

Indeed, Morgan refers to the NCC's "blunt hostility" to the public interest clause of the Competition Policy Agreements, and she reinforces this with the following quote from leaked correspondence from the NCC:

The rationale underlying the competition policy agreements is the presumption that enhancing competition is generally in the public interest. As a consequence, the Council does not see a requirement for a government to formally examine the matters in clause 1(3) of the Competition Principles Agreement on every occasion that it implements reform (Morgan 2003: 124), [30]

The NCP legislative review process, driven by the NCC and overseen by Federal Treasury, has placed far more emphasis on theoretical market and free trade/investment outcomes, (based, as this paper argues, on untested and often faulty assumptions) and a nationally

[29] A more detailed discussion of the NCP public interest test and its implications for the NCP legislative review process can be found in Margetts, 2001 pp 55-61 and 87-107)

[30] Morgan sourced this quote from a union submission to the 1995 House of Representatives Standing Committee on Banking, Finance and Public Administration *Inquiry into Aspects of the National Competition Policy Reform Package*, Volume 6: 817)

consistent approach as desired by the potential "winners", than on the actual arguments of state or regional public interest.

Box 1 - Judging the public interest

The multi-party Senate Select Committee on the Socio-economic consequences of National Competition Policy (of which this author was a member until the end of June 1999) was very critical of the NCP public interest test processes for a range of reasons including the predominance of narrow economic interpretation of the policy, the lack of transparency of reviews and the lack of appeal mechanisms. (SSCSCNCP, 1999: 101) This paper argues that these serious criticisms have never been adequately addressed.

This paper argues that even if though the Senate Select Committee reported considerable community criticism of the public interest tests themselves, the table below of adjudged "non-compliance" of the legislative reviews by the National Competition Council indicates they took a much narrower economic interpretation of "public interest", than those who conducted the public interest tests, overseen by the states.

The National Competition Council explains the process as follows:

"*Clause 5 of the Competition Policy Agreement obliges governments to review and, where appropriate, reform all existing legislation…that restricts competition. It requires governments to remove restrictions on competition unless they can demonstrate that the restrictions are warranted - that is, that restricting competition benefits the community overall (being in the public interest) and that the restriction is necessary*." (NCC 2003: 4.2)

However, in response to a Senate Question Without Notice lodged on 11 May 2006 of the roughly 2000 pieces of Commonwealth, State and Territory legislation pulled out for review under the National Competition Policy legislative review process, how many public interest requests for exemption (from reform) or partial exemption, had been received by the National Competition Council, Senator Minchin, representing the Treasurer replied:

"The legislative review process under National Competition Policy (NCP) does not involve states and territories or relevant stakeholders lodging public interest requests for exemption to the National Competition Council." (Senate Hansard 2006)

The National Competition Council refers to such cases as "*failure to comply with the CPA requirements*" although it is the National Competition council themselves who made these assessments and then recommended to the Federal Treasurer what punitive action should be taken and they admitted themselves that compliance failure was a "judgement call" (NCC 2003: 4.13).

"Failure to comply with the CPA requirements can arise for a range of reasons. In some instances, the Council assessed that outcomes are not consistent with the obligations under the CPA clause 5(1). In other cases, non-compliance was the result of a timing failure – that is, a government did not meet the (extended) deadline of 30 June 2003." (NCC 2003:4.11)

It is difficult to quantify how many NCP legislative changes were reluctantly made by the States, Territories and even the Federal Government contrary to the findings of their public interest review processes, however, Table 1 shows examples of disagreement or "compliance failure" as documented by the NCC in 2003.

Table 1

Jurisdiction	Areas of non-compliance with priority legislation	Incomplete activity and no commitment to reform
Commonwealth	22 (66%)	11
New South Wales	28 (31%)	9
Victoria	10 (22%)	6
Queensland	24 (39%)	11
Western Australia	49 (69%)	31
South Australia	34 (43%)	25
Tasmania	14 (23%)	9
ACT	11 (41%)	8
Northern Territory	16 (53%)	14
Total	180 (44%)	115

(Source NCC 2003: 4.14 – 4.21)

The NCC identified "priority legislation" areas as water, primary industries, communications, fair trading and consumer legislation, insurance and superannuation services, health and pharmaceutical sector, legal services and other professions, planning, construction and development services, retail regulation, social regulation and transport services

As Table 1 shows, apart from Western Australia, the next worst complying jurisdiction with the NCC's judgements of priority legislative change was the Commonwealth Government itself, (as the NCC could not require the Federal Government to place financial penalties on themselves!)

The NCP Legislative Review process effectively started in 1995 when the states agreed to publish their agenda for implementation of the NCP agreements by mid 1996. The preparation for the legislative review process was meant to start straight away and the whole review and reform process was meant to be complete by 2001, with tranche payments to continue to 2006, as demonstrated by the following quote from the Compendium of National Competition Policy Agreements:

"*Under the Implementation Agreement, the Commonwealth Government undertook to make on-going National Competition Policy payments (NCP payments) to each State and Territory over a period 1997-98 to 2005-06, subject to that State or Territory making satisfactory progress against their NCP and related reform obligations. NCP payments are to be made in three tranches: prior to July 1997, July 1999 and July 2001, the NCC accesses whether each State or Territory has met the conditions for the payments to commence*." (NCC 1998: 5)

However, this somewhat painful process began slowly and was still continuing in 2006 when the last of the NCP tranche payments were made.[31]
The implementation of the NCP legislative review process has had serious consequences for many manufacturers, small businesses and rural producers, but the theory of community benefit has never been systematically tested in relation to the medium to long-term impacts of such legislative and regulatory changes.

Whilst, as has been stated, each state and territory is supposed to have been given the power to make their own decisions, based on properly constituted public interest review processes, there is little evidence that the NCC have ever recognised or accepted a public interest request for exemption in those areas designated by Hilmer and the NCC as "priority legislation". This "priority legislation" covers a very broad impact area and can be summarised as primary industries, planning, construction and development, fair trading and consumer legislation, finance, insurance and superannuation, retail regulation, communications, professions and occupations, social regulation, transport services, and water. (PC 2005 p 18) In other words, the desire for market deregulation and legislative uniformity in those areas has frequently overridden any public interest arguments, however valid. The figures of "non-compliance" provided by the National Competition Council give no idea of how many of the legislative changes that were enacted were done reluctantly by those state governments but as we have seen from the "non-compliance" figures and discussion in the Box above ("Judging the Public Interest") the NCP legislative review process has provided little, if any, acceptance of the different circumstances of different states and territories or regions.

Having so far critiqued the process of developing and implementing National Competition Policy, this paper will now focus on how this has impacted on the Australian dairy sector. The following section gives some background to the situation Australia-wide and in each state jurisdiction prior to deregulation. In the case of milk market deregulation, a broad summary of the driving assumptions seems to have been that:

1) The domestic milk premium constituted an export subsidy;[32]

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[31] Since then, the National Competition Council has been relieved of its legislative review functions and a new body formed in 2007, to oversee COAG reforms, the COAG Reform Council (COAG 2007).

[32] In 2000,(the year milk deregulation took place), the published average international farmgate milk price was 30.67 Euros per 100 kgs, (which translates to around AUD 0.49c per litre). The same source put the price of NZ milk in that year at 16.64 Euros (around AUD 26.45c per litre). (LTO 2000, Ozforex, 2007)

2) Australian dairy farmers, especially those producing for the fresh milk market, were inefficient producers;
3) Removing state-based regulatory systems and market milk premiums ("the artificial distinction between market and manufacturing milk") and reducing farmers' ability to jointly market their product, will make them more efficient producers
4) Consumers will benefit by cheaper milk and dairy products;
5) Those who leave the industry will be inefficient dairy farmers, leaving a more innovative and efficient primary industry; and
6) Even if deregulation causes some temporary pain to sections of the Australian dairy industry, dairy deregulation will be to the overall benefit of the Australian community.

The Australian dairy market situation prior to deregulation

Before 1986, the Australian dairy industry operated under pooling arrangements for milk produced for either domestic or export production. Producers received an average pool price for their product, irrespective of quality or product destination. (Senate Regional and Rural Affairs Committee 1999: 20) However, in 1986, a new national market support scheme was introduced under Minister John Kerin. [33] The Kerin Plan for dairy market support, funded by a national levy of 2 cents/litre on all Australia milk produced, was used to support an export support payment for all Australian dairy exports. From 1986 to 1992, this export support was reduced from 44.2% to 22% above world parity prices [34], that is, export subsidies were reduced by half.

Prompted by the Industry Commission Inquiries (into Statutory Marketing Arrangements and the Dairy Industry) the Kerin Plan was replaced, in 1992 by the Crean Plan, which saw the continuation but gradual phasing down of the support of the dairy industry. However, commitments made to the WTO as part of the Uruguay Round of GATT saw a requirement that any domestic support be provided independent of export sales. Export market support payments terminated by June 1995, to be replaced by the Domestic Market Support Scheme. (DMSS) (SRRATRC 1999: 21).

The DMSS commenced on 1 July 1995. This provided for payments for farmers for milk used in the manufacturing sector (for products consumed domestically) (Ibid: 21). This support for value-adding in the dairy industry was funded by a levy on all market milk production and by the dairy manufacturing sector. The Federal export assistance having already been removed, the focus shifted to the variety of state regulatory arrangements. The DMSS ended on 30 June 2000, by which time it had been wound down to 10% above world parity prices (Ibid: 22). Its removal could be described as the first stage leading up to of the implementation of the Federal Government's NCP package for the dairy industry.

The variety of state regulatory arrangements leading up to nationwide farmgate deregulation are described below.

[33] The 1986 changes to Australia's domestic dairy marketing arrangements coincided with Australia hosting the inaugural meeting of the Cairns Group of agricultural trading nations in Queensland in the lead up to the GATT meeting in Uruguay (Cairns Group 2006).

[34] It was during this time that Treasury took over the administration of the Industries Assistance Commission from the Department of Industry and Commerce (PC 2003: 27).

State regulatory arrangements for market milk

Post farmgate dairy market deregulation had already been adopted by each dairy producing state, the last being Queensland on January 1999. (Ibid: 25) That is, regulation governing wholesale and retail prices for packaged milk was removed by Victoria in 1995, in NSW in 1998, and the remaining states by June 1999. (Spencer, 2004b: 18) The states continued to regulate the farmgate price and supply of market milk in order to ensure the quality and all year round supply for drinking purposes. Typically, this type of regulation included the vesting of milk in a statutory body, farmgate price setting for market milk, supply management arrangements, food and safety standards and compulsory funded industry levies (Ibid: 26).

The following summarises the systems used by each state for market milk support, prior to June 2000.

Victoria

A quota system operated in Victoria from the 1970s until the *Dairy Industry Act* 1977 oversaw the managed buyout of quota over a ten year period at a cost of $39 million.

The *Dairy Industry Act* 1992 vested regulatory control of the Victoria dairy industry to the Victorian Dairy Industry Authority. Parts 5, 6 and 7 of the Act regulated milk supply and payments to producers by processors.

Milk was the property of the VDIA and if insufficient milk was produced to meet market milk requirements, the VDIA could request a processor to deliver milk as market milk. The VDIA determined the farmgate price which were reviewed and published every six months. The VDIA deducted their own costs and then distributed the surplus to all licensed dairy farmers in proportion to their total deliveries of acceptable quality that month.

All dairy farmers shared in the premium from market milk, whether or not their milk was used in that way (Ibid, p 27). It is therefore not surprising that most Victorian dairy producers chose to produce their milk for manufacturing because it could be produced seasonally. [35]

New South Wales

The NSW Dairy Corporation was established by the *Dairy Industry Act* 1979 to regulate the supply, treatment and price of milk and dairy products. All milk produced in NSW was vested in the NSW Dairy Corporation (which later became Safe Foods). All farmers were registered to supply designated milk factories, which acted as agents for the Corporation for purposes of processing and selling. The Dairy Corporation issued milk quotas to ensure sufficient milk supply to meet demand, and issued tradeable contract to farmers. NSW dairy farmers were able to trade such contracts through a four weekly “quota exchange” (Ibid: 27).

Queensland

Queensland, until 1999, had several different systems operating regionally.

[35] In April 1999, over 90% of Victoria’s milk production went to manufacturing, and over 50 % of that was exported. Market milk accounted for 6-7% of their total production. (SRRATRC 1999: 14)

In SE Queensland a statutory market milk entitlement attached to a producer. Allocations were based on entitlements issued in April 1986, and each allocation was "grown" as required. Entitlements were tradeable and also transferable from one processor group to another.

Within the SE Queensland dairy region, the Queensland Dairy Authority determined market milk access to two access schemes, the Brisbane Market Milk Access Scheme and the Suncoast Market Milk Access Scheme. The schemes allowed processors in the larger population areas to access raw milk from other processors.

In Central Queensland a factory quota system was operated by a subsidiary of Paul's Ltd, the area's only franchised processor. The quotas gave dairy producers the authorisation to supply a specifics quantity of market milk, but these did not constitute a statutory right to supply market milk. Prices were negotiated between buyer and seller. New entrants to the area required the approval of the company to purchase quota.

North Queensland used a pooling system operated a subsidiary of Dairy farmers group, the only franchised processor in North Queensland. Like Central Queensland, the pooling system did not give the dairy producer a statutory right of supply market milk. All milk produced was pooled and market milk was supplied from the pool. Farmers were paid a market milk price according to the relative proportion of the milk they delivered to the pool (Ibid: 28/29).

From 1999, the system changed as a result of the National Competition Policy legislative review of their *Dairy Industry Act 1993*, to an interim state-wide statutory supply management arrangement consistent with the recommendations of the NCP review, to remain in place for the same period as regulated farmgate milk prices (Ibid: 29).

Tasmania

The Tasmanian Dairy Industry Authority was established under the *Dairy Industry Act* 1976 to regulate and control the industry by setting standards and licensing all sectors of the industry. As part of its functions to rationalise the market milk sector, in 1977, the authority changed the arrangements for fresh milk and cream from a quota system to a pool system, to enable a more equitable sharing of the higher farmer returns from that sector. From 1978 to 1985, they purchased quota contracts from quota holding dairy farms. From that time, a notional 10% of each farmer's production was designated as market milk and farmers received the percentage premium that provided.

The *Dairy Industry Act* of 1996 replaced the previous legislation. It provided for the setting of a milk price which the milk packagers must pay producers. The TDIA were responsible for administering milk pooling and marketing arrangements, promoting Tasmanian market milk and dairy produce, managing the supply of milk for the Tasmanian market milk and cream trade, helping to administer quality assurance programs in conjunction with Government and industry bodies and consulting with the Tasmanian dairy industry (Ibid: 30).

South Australia

The *Dairy Industry Act* 1992 established the Dairy Authority of South Australia, as an independent statutory authority fully funded by the dairy industry. DASA's functions under

Section 12 of the Act included advising on the imposition, variation or removal of price control in respect of dairy produce covered under the Act, determining fees and conditions for licenses under the Act and monitoring the extent of compliance with dairy industry standards and codes of practice.

The South Australian Market Milk Equalisation Committee Ltd (a representative body of producers and processors) managed access to the market milk premium by every dairy farmer on a pro-rata basis, and ensured that dairy farmers were paid correctly and fairly for the types of milk they produced (Ibid: 31/32).

Western Australia

The Dairy Industry Authority of Western Australia was established under the *Dairy Industry Act* 1974 to regulate the production of milk so as to ensure as far as possible, the continuous availability of milk, oversee the payments and sale of milk and ensure the quality, production and treatment of milk at dairies.

The Authority administered a system of market milk quotas and a licensing system and determined the market milk price, administered various production, promotion and transport allowances, and financed the Distribution Adjustment Assistance Scheme. The Authority also maintained industry statistics and conducted research into policies and market conditions as well as operating a technical and quality program for farm milk and monitoring the standards of Western Australian manufactured dairy products.

The market milk quota system had operated in WA since the 1940s. WADIA would hold three quota auctions per year on the industry's behalf. WA dairy farmers, through this authority had the opportunity for input into pricing based on the costs of their production. (Ibid: 31)

Industry Snapshot

In a submission the Minister for Agriculture, Forestry and Fisheries, 20 April 1999. the Australian Dairy Industry Corporation (ADIC) provided an industry snapshot, as of April 1999:

- *Has export earnings of $2 billion in 1998/99*
- *Supplies 12% of world dairy trade (third largest dairy trader after the EU and NZ)*
- *Is Australia's third largest rural industry in value at the farmgate (behind beef and wheat)*
- *Is the largest rural industry valued at the wholesale level ($7 billion)*
- *Has efficient milk production costs by world standards*
- *Exports over 50% of total milk production*
- *Produces 10 billion litres of milk – a 55% increase since 1986, and 6% average annual increase during the 1990s*
- *Has 13,500 dairy farmers – a 30% reduction since 1985 (19,342) – with approximately 98% of dairy farms in family ownership*
- *Average farm size (now 180 hectares) and average herd size (now 149 cows) have doubled since the 1980s*
- *Has seen dairy companies invest $1.5 billion to expand manufacturing capabilities in the five years to 1998*

- *Is an important regional employer (60,000 direct jobs at farm and manufacturing level)*
- *Has 75% of Australia's milk production processed by dairy farmer owned cooperatives*
- *Has 45% of all milk intake and 50% of all milk used for manufacturing controlled by the two major dairy co-operatives (Bonlac Foods and Murray Goulburn, both Victorian based)*[36]

(SRRATRC 1999: 5)

As this snapshot indicates, the Australian dairy industry was not a static industry leading up to the 2000 deregulation. Milk production per farm and per cow had been rising steadily and it would seem that the ability of producers to have some input into the regular review of farmgate prices did not prevent Australian dairy producers from being competitive within their own ranks or constantly looking to innovate and improve efficiency.

Federal Political response to dairy deregulation proposals

In the absence of widespread and informed political debate on these issues, the political responses to competition policy have also often displayed both a lack of deep understanding of what was actually happening and relative powerlessness to stand in the way of corporate-driven change. This is illustrated in the Report from the 1999 Senate Rural and Regional Affairs Committee (composed of Labor, Liberal and Democrat Senators) *Deregulation of the Australian Dairy Industry* which did not so much applaud deregulation but considered that the pressures for market change as inevitable and argued for a harm minimising approach:

"*The Committee concludes that sooner rather than later the market will force deregulation and that a managed outcome with a soft landing is preferable to a commercially driven crash*." (SRRATRC 1999: xiv)

The Senate Inquiry report identified the main "market forces", or "drivers of deregulation", as the large export oriented Victorian Co-operatives, which, in turn, were under market pressure as a result of the eminent removal of the Domestic Market Support Scheme (Ibid: xiii). The committee identified Australia's two largest dairy processors, Murray Goulburn and Bonlac as arguing that the Australian dairy industry would gain from freer trade and that the gains from trade would be greater with the abolition of the DMSS (Ibid: 25). Cocklin and Dibden (2002: 35) report Victorian farmers as suggesting that as well as international and domestic commercial pressures, the major supermarkets were exerting pressure for farmgate deregulation.

The Senate Committee also noted that such deregulation would make the Australian dairy industry the only one in the world, at that point, without Government legislative support (SRRATRC 1999: xiii).

The NCP Legislative Review of Dairy Legislation

Under National Competition Policy, all Commonwealth, State and Local Government legislation was reviewed to identify and assess legislation for compliance with the NCP

[36] Both Australian-owned at the time, but Bonlac was later taken over by New Zealand milk giant, Fonterra.

agreements and principles. As has been discussed, rural marketing arrangements were one of the prime targets of the Industry Commission, then the Hilmer Inquiry.

The irony in relation to dairy farmgate deregulation is that of the five states which undertook the whole public interest review processes in 1998, the public interest reviews from the majority of those States (New South Wales, Queensland, Western Australia and Tasmania) recommended that there was a public benefit in retaining farmgate regulations (Joint Committee on the Impact of Dairy Deregulation in South Australia 2003: 10-11). Not surprisingly, Victoria, which had already undergone a degree of dairy market deregulation and whose dairy sector was mostly geared to the manufactured milk market, concluded that there was no public benefit in retaining farmgate regulations (See below). Victoria dairy producers were already producing the majority of Australia's milk and were hoping for an increase in their farmgate prices as a result (Ibid: 11).

Summary of the NCP State Reviews of Dairy Regulation

NSW November 1997

The NSW Dairy Legislative Review Group prepared an Issues Paper in May 1997. The review Group conducted public consultations in eight different regional centres and over 450 submissions were received (SRRATRC 1999: 77).

The review found that the process of price setting provided quota holder a competitive advantage over other milk producers but that, even if competition was effected, the effect was negligible compared to the increased manufacturing efficiencies. (Ibid: 78)

The submission s provided a range of reasons for retaining the existing price setting and supply arrangements. The Senate Committee Report cited the following;

a) "*To meet consumer preferences for stable prices;*
b) *To guarantee adequate year round supply of market milk;*
c) *To provide producers with countervailing market power;*
d) *To offset corrupt world prices for dairy products;*
e) *To encourage stable dairy industry development; and*
f) *To provide equitable opportunity of access to the entire NSW fresh milk market and subsequent regional development.*"

The NSW Review group concluded that the first two reasons did not justify Government intervention but were divided on the others (Ibid: 79). The majority (Chairman, Industry and Dairy Corporation members) recommended that the current pricing and supply arrangements remain in place until 2003 when they should be reviewed again (Ibid: 80).

Queensland July 1998

The report of the Queensland Dairy legislative review found:

" a) *Irrespective of the NCP process, commercial pressures existed which would continue to force greater restructuring of the dairy industry;*

b) The review committee's vision of the dairy industry essentially involved a sustainable, competitive and profitable industry operating in a commercially flexible manner with a minimum of justifiable government intervention" (Ibid: 80-81)

Independent consultants were commissioned to undertake a public benefit test and they found:

"*Economic analysis suggested that in most scenarios, deregulation was likely to have little* ***overall*** *impact on the Queensland economy, but that regional impacts from deregulation were likely to be very significant;*

i) *Producers with low equity and high indebtedness and/or located I marginal dairying areas distant from processing plants would be at greatest risk;*

ii) *Attendant consequences for regional communities in terms of job losses and a reduction of business activity would be substantial.*" (Ibid: 81)

They did, however, also conclude that ultimate deregulation of the farmgate prices was inevitable because of the commercial strength of the Victorian industry.

They nevertheless did not recommend deregulation.

Western Australia February 1999

The Western Australian Review concluded that there was a net public benefit from:

" a*) The regulated farmgate price for market milk and that in this context a quota system was an appropriate ongoing mechanism to distribute a regulated farmgate premium;*
b) Vesting of milk in so far as it provides funds for the Dairy Industry Authority to provide services to the industry;
c) Licensing by the Dairy Industry Authority of processors and dairy farmers with respect to food safety standards." (Ibid: 84)

The review report thus recommended that the status quo be maintained.

Tasmania May 1999

In Tasmania an Issues Paper was release in October 1998. Major stakeholders were contacted and public meetings were held in Hobart, Scottsdale, Deloraine, King Island and Smithton. 21 submissions were received (Ibid: 85-86).

Having taken into consideration the range of likely social and adjustment costs, the Review Group concluded that these costs would be considerable. They also concluded that the possible quantifiable and non-quantifiable costs and benefits were quite evenly balanced. However, they also concluded that in the longer term there were potential efficiency benefits to be gained from deregulation. (Ibid: 87) They therefore recommended against immediate deregulation in favour of reform over 5 years. Their recommendation was made subject to the outcome of the Victorian dairy review and the details and conditions attached to the proposed structural adjustment package. They also recommended that the TDIA continue to regulate milk quality standards until a national food safety scheme was implemented (Spencer 2004a: 8.16).

Victoria July 1999

The Kennett Victorian Government commissioned the Centre for International Economics, a private consulting company (whose publications list show a clear history of support for the global free-trade, free market agenda), to undertake their review of dairy legislative arrangements in February 1999. The National Competition Council supported this review because it was an "arms-length" review without a multidisciplinary committee as was the case with most of the other reviews (SRRATRC 1999: 69).

An issues paper was prepared and 25 submissions were received.

Cocklin and Dibden give some perspective on the Victorian situation in their paper, *Taking Stock* (Cocklin & Dibden 2002) where the authors reveal that, despite over 80% of Victorian farmers voting in favour of deregulation, their interviews revealed that Victorian dairy farmers' opinions were divided between those who saw deregulation as a good thing, those who grudgingly saw it as inevitable but were worried about the Commonwealth's threat to withhold compensation if they voted NO, and those who did not agree that farmgate deregulation was the right answer. They claim that, the case that farmers were presented at forums and discussions was that deregulation was a given and so the debate largely centred on the nature and timing of the compensation packages.

"*The view that deregulation was the inevitable result of commercial pressures was disputed. Some people argued that if dairy farmers in Victoria opposed deregulation, as farmers had in other states, that the Federal government would not proceed...*" (IBIB: 37)

Cocklin & Dibden also report that their interviews showed that even amongst supporters of deregulation, there were a number who would have preferred a five year delay (Ibid: 33).

In relation to the regulations allowing for sharing of market milk premiums the views of the big players in Victorian dairy appeared to differ from a number of smaller groups and individuals:

"a) *The United Dairyfarmers of Victoria, the Victorian based co-operatives, processors and manufacturers considered the pooling system harmful for the further development of markets for Victorian milk and dairy products.*

b) A number of individual dairy farmers and groups of farmers, which included the Simpson Branch of UDV, and the New South Wales based Dairy Farmers, strongly supported regulated farm gate milk pricing and pooling of returns." (SRRATRC, 1999: 70)

There was also apparently, general support for the retention of the role of the Victorian Dairy Industry Association for maintaining and developing milk markets (Ibid: 70.

The report of the public interest tests concluded:

"*a) The gains to consumers from access to cheaper milk more than offset the losses to producers; there was therefore a net public benefit from the removal of price and supply controls on market milk;*

b) The higher the market milk premium which remains after deregulation, the smaller the reduction in dairy farmer income and the smaller the improvement in processing efficiency required to avoid farm sector income loss from deregulation;

c) There was no demonstrable net public benefit from retaining a statutory requirement to maximise the opportunity for the sale of market milk produced in Victoria." (Ibid: 72)

The multi-party Senate Rural and Regional Affairs and Transport Committee pointed to what they saw as a number of defects in Victoria's dairy industry NCP assessment including the view that the public interest test as test was too narrowly applied, and lacking in transparency (Ibid: 75).
It is also significant that Pat Rowley from the Australian Dairy Industry Council pointed out that, having received this negative NCP public interest assessment from CIE, the Victorian Government (now a Labor Government, under the leadership of Steve Bracks) was threatened with the loss of Commonwealth NCP tranche payments if they did not dismantle dairy regulation (Ibid: 40). This type of political pressure, using the market dominance of Victoria as a potential weapon against the other states, puts a different light on the perceptions of "market forces" and "inevitability" of the way dairy deregulation occurred in Australia.

South Australia September 1999

It appears that South Australian Liberal Government, given its proximity to parts of the Victorian dairy industry, was watching to see what Victoria would do.

The way the Final Report from the Joint Committee on the Impact of Dairy Market Deregulation in South Australia, describes it, despite the conclusions from the other states, there is a tone of inevitability that once Victoria had decided that they would deregulate, South Australia would too.

"*During 1998, New South Wales, Queensland, Western Australia, Victoria and Tasmania had undertaken competition policy reviews of their market milk legislation.*

New South Wales, Queensland, Western Australia and Tasmania all concluded from their reviews that there was a public benefit to continue with those regulations. The Victorian competition policy review concluded that there was no public benefit for the continuation of those Victorian milk regulations and a removal of regulations in Victoria would have meant that commercial deregulation would take place much more rapidly. Victoria was delivering 63% of all milk production in Australia.

South Australia supported the policy change and on 1 June 2000 the South Australian Parliament passed the Dairy Industry Deregulation of prices) Amendment Bill." (Joint Committee on the Impact of Dairy Deregulation in South Australia 2003: 11)

It should be noted that, whilst Victoria represented the majority of Australia's dairy producers, the states whose public interest assessments claimed that retention of dairy statutory marketing arrangements was in the public interest, represented the interests of the majority of Australians.

It appears that the National Competition Council, like the Industry Commission and the Hilmer Report were always determined to deregulate rural market arrangements such as dairy, so the public interest reviews of the majority of states on this occasion appear to have fallen on deaf ears. Even though, theoretically, the States had the decision making powers in relation to the NCP public interest reviews, the National Competition Council refused to accept any of the public interest arguments opposing farmgate deregulation. The SRRATRC reported that the National Competition Council concerns included the following:

"*a) the Council was not satisfied that the (state) reviews clearly demonstrated a net community benefit in support of the retention of market milk arrangements;*

b) the robustness of the cost-benefit analysis undertaken in reviews;

c) the independence of some of the panels." (SRRATRC 1999: 91).

So regardless of views of the other states and the different implications for dairy regions outside Victoria, the National Competition Council recommended that the Federal Treasurer threaten to punish the states by holding back a portion of their NCP tranche payments until or unless they deregulated to the NCC's satisfaction (Ibid: 91).

Political response in Western Australia

Some impression of the kinds of pressure which the National Competition Council and Federal Treasury put on states like Western Australia can be gained from scanning the Hansards for the *Dairy Industry and Herd Improvement Legislation Repeal Bill* 2000.

Leading up to the final vote on the repeal of the *Dairy Industry and Herd Improvement* legislation, Murray Criddle, representing the Minister for Primary Industry, tabled a letter signed by the President of the WA Farmers Federation dairy section, formally requesting the removal of the *Dairy Industry Act* 1973.

Much of the debate and Ministerial questions around that time related to what the dairy farm sector itself wanted. It was reported that the Labor Party Members of the WA Legislative Assembly, despite stating that they opposed deregulation, felt they had no choice but to support the repeal bill. Some clues as to why they may have felt this can be picked up from Murray Criddle's explanation of the farmgate deregulation in Victoria. He explained that Victorian milk processors and United Dairy Farmers of Victoria had been lobbying for farmgate deregulation (which was later supported in a plebiscite from Victorian dairy farmers) and that because of the dominance by that state of the Australian milk production, if they deregulated, it would put considerable pressure on the milk markets of the other states.

Given that the existing dairy market support scheme was due to expire on the 30th of June 2000, the Commonwealth Government offered a $1.8 billion structural adjustment package to help dairy farmers through the change to deregulation. The deal was that if the states agreed to deregulation their dairy farmers would receive assistance. If states chose not to repeal their existing dairy market regulation, their farmers would be denied assistance to help them through the market changes which would permeate through the system from deregulation in Victoria (LC Hansard 2000a: 6618).

On the 21st of June 2000, in his role as Shadow Minister for Agriculture, Kim Chance reported that the results of a ballot conducted by the Australian Electoral Commission of Western Australia dairy producers indicated that 65% of WA dairy producers opposed

farmgate deregulation (LC Hansard 2000b: 7918). Later in this animated debate, Kim Chance explained that, within the industry, the push to support NCP dairy market deregulation "*…began in Victoria, principally with the Murray Goulburn Co-operative, but once it made a decision, Bonlac Foods was bound to go along. That influence flowed to the farmers' organization in Victoria and, by necessity, to the national organization…(…)…corruption exists in this process, as it exists in most processes*." (LC Hansard 2000b: 7924) [37] [38]
And later "*To suggest that this process of dairy deregulation has happened naturally and in accordance with the normal laws of commerce and that it does not involve greed and corruption is wrong. Greed and corruption are at the core of this issue*." (LC Hansard 2000b: 7924)

Nevertheless, the repeal legislation passed the Legislative Council with the support of the Labor Opposition.

2000 - Australia-wide farmgate deregulation

Legislation to deregulate dairy farmgate arrangements, one way or the other, was passed by all dairy-producing states by 30 June 2000.

The effects of deregulation of a number of existing rural marketing arrangements has been made all the more acute on many parts of Australia's dairy farming sector because it has coincided with many aspects of NCP related retail trading deregulation. This has enhanced the dominance of the major retail chains at the expense of independent traders and diminished even further any effective bargaining power for individual primary producers, who are also struggling against the market power of the large processors.

Has this resulted in more efficient use of resources or, improved manufacturing opportunities or benefits to Australian consumers? The National Competition Policy agreements did not set any specific consumer goals, when they were introduced in 1995. However, the largely untested, assumption has generally been put forward by the supporters of NCP that the consumer is the main beneficiary, as expressed in Federal Treasury's (late) submission to the Senate Select Committee's Inquiry into the Socio-Economic Consequences of NCP:

"The NCP reform package is designed to improve the efficiency of the Australian economy, leading to lower prices for consumers and raised living standards." (Department of the Treasury 1998: 1)

It is worth noting that, at the same time, Treasury also cited some of the items mentioned in the public interest test check-list as other "goals" of NCP:

[37] Leading up to deregulation, Murray Goulburn Co-operative and Bonlac Foods were the largest Victorian dairy co-operatives and could influence the farmgate price of Victorian milk, and by extension, milk within the potential market reach of Victoria, especially as the removal of state based farmgate regulation allowed for the potential movement of milk across state borders. Farmer members of those co-operatives stood to gain from increased farmgate prices for their milk as it was mostly manufacturing milk. For further information on dairy processing in Australia, see Appendix B and in Western Australia, Appendix C

[38] This reference to "greed" may not have been simply referring to the Victorian co-operatives wishing to extend their market dominance. With the termination of dairy export market support in 1995 and the pending loss of the Domestic Market Support Scheme in June 2000, for milk used in manufacturing, the potential flood of New Zealand dairy imports may have increased the feeling of vulnerability of even the major Victorian milk co-operatives to the market power of their New Zealand rivals.

"However, the package clearly acknowledges that economic efficiency arising from increased competition is not the only goal, and must be balanced against socio-economic factors, such as the protection of the environment, employment and regional development. (Department of the Treasury 1998: 1).

The most commonly cited reasons for many of the market-based changes associated with the push for global free trade/ free markets was to help make Australian business more "internationally competitive" (that is, reduce business costs) and make more sectors of the Australian economy international investor-friendly. Neither of these major goals actually specifically relate to the Australian consumer.

Some years after the introduction of National Competition Policy, the Senate agreed to begin to investigate what they had helped to create. The Federal Treasury made a late submission (too late to be considered in the text) to the *Senate Select Committee on the Socio-Economic Consequences of the National Competition Policy*. In it, Treasury claimed that:

"*The overall aim of competition reform is to improve the efficiency of resource use and hence maximise the community benefits of economic activity*." (Department of the Treasury 1998: 5)

The Federal Government had responded to lobbying by industry representatives prior to nationwide deregulation, and announced on 28 September 1999 an agreement to implement a levy scheme to assist drinking milk sector adjust to the new deregulated environment. The levy was to fund a Dairy Industry Adjustment Program (DIAP) (Dairy Australia 2003a).

The Dairy Industry Adjustment Program included four schemes for assistance to farmers:

- The Dairy Structural Adjustment Program (with an available fund of $1.63 billion for payments to eligible dairy farmers and administered by the Dairy Adjustment Authority
- The Dairy Exit Program, with an available fund of $30 million, offering tax-free exit payments to a limit of $45,000, and administered by Centrelink
- The Dairy Regional Assistance Program, with available funds of $65 million to provide assistance to regional communities to assist with the impacts of dairy deregulation, and administered by the Department of Transport and Regional Services; and
- Supplementary Dairy Assistance, from a fund of $139 million for payments to eligible dairy farmers, administered by the Dairy Adjustment Authority as well as a further $20 million for discretionary payments. (Dairy Adjustment Authority 2002: 6)

The levy on domestic drinking milk and drinking milk or milk used as an ingredient for beverages was imposed at the point of delivery to the retailer at the rate of 11c per litre for a period of 8 years. The levy fund was used to provide payments to farmers under a range of schemes, including covering the expenses of the Dairy Adjustment Authority, costs to the Commonwealth related to the adjustment package, interest on borrowings and even the costs of ACCC price monitoring exercises. (Dairy Adjustment Authority, 2002: 4) [39]

[39] Given (as shall be shown) the substantial falls in the farmgate prices for drinking milk following nationwide deregulation, in effect, it was the producers of market milk themselves who paid this levy to assist themselves as well as paying for many aspects of their own industry deregulation. The actual net effect of the levy on the drop in farmgate prices compared to the value of any assistance packages, including packages to help farmers leave the industry, deserves further scrutiny.

The ACCC Review

In April 2000, just prior to nationwide farmgate dairy deregulation, the Federal Minister for Financial Services and Regulations, Joe Hockey, had commissioned the ACCC to monitor prices, costs and profits in the Australian milk industry for three months prior to and 6 months following the implementation of the 11 cents per litre dairy adjustment levy (ACCC 2001: xv).

In their report summary the ACCC gave an explanation for the commissioning of their review:

"There were concerns that milk processors and retailers would be the main beneficiaries of deregulation and that reductions in farmgate prices would result in only marginal savings to Australian milk consumers.

Consequently to help Government and the community better understand the impact of dairy deregulation the ACCC was asked to monitor prices, costs and profits in the milk industry." (ACCC 2001: xv-xvi)

This paper argues the monitoring was over too short a period to fully assess the impacts pacts of such a major change in this industry to dairy farms, the dairy processing sector, dairy retailers and to dairy consumers.

Even the authors of this report admit that;

"*Six months would normally be considered a relatively short period to fully assess the impact of such a substantial change in the regulatory environment. However and the dynamics of the industry have undoubtedly altered, although further changes can be expected.*"

To note some of the main findings from the ACCC report:

1) Before dairy deregulation the on 1 July 2000, the Australian average farmgate price for market milk was around 47 cents per litre and manufactured milk around 21 cents per litre. (p xv)

2) Not all dairy farmers bargaining power was lost with deregulation. (p xvi)

3) "*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*" – (p xvi)

4) "*Processor bargaining power (and their ability to influence price) has been found to be relatively weak*" (p xvi)

5) "*The report broadly concludes that Australian milk consumers are better off*" (p xvi)

6) "*Australian processors and retailers, therefore, have not captured the benefits of deregulation to the exclusion of consumers*" (p xvi).

7) "*Many dairy farmers in Western Australia, Queensland and New South Wales have been badly affected by the removal of farmgate price controls for drinking milk*." (p xvi)

8) "*…farmers in the other states that have traditionally had a high reliance on milk directed to the manufactured dairy products have seen market milk premiums largely offset by recent increases in prices for internationally traded dairy commodities*." (p xvi-xvii)

9) Over the monitoring period, supermarket prices for plain, reduced fat and low-fat milk had, on average, dropped by 22 cents, 6 cents and 9 cents per litre respectively. (p xv11)

10) Supermarket prices for UHT, flavoured and specialty milk increased in price by 10 cents, 14 cents and 3 cents per litre respectively. (p xvii)

11) Supermarket gross margins on milk declined by 19 percent (with retail prices falling at a greater rate than the wholesale prices). Despite a six percent increase in sales volumes, overall aggregate milk revenue decreased during this monitoring period. (This sales volume increase was matched by a 24 percent decline in convenience stores milk sales over the same period) (pp xvii- xviii)

12) Net profit margins for milk processors decreased by 12 percent and 18 percent for the September and December quarters respectively relative to the June 2000 quarter. (p xviii)

13) After deregulation, despite the changes in the mix and volume of sales, the total volume of milk sold in Australia was largely unchanged. (p xviii)

14) The drop in aggregate revenue losses translated to a savings to consumers which they projected to be worth more than $118 over a full year. (p xviii)

15) Supermarkets reported to the ACCC that their lower prices for generic labelled milk (introduced in August 2000) would apply indefinitely. (p xix)

To deal with each of these points in turn:

1) **Before dairy deregulation the on 1 July 2000, the Australian average farmgate price for market milk was around 47 cents per litre and manufactured milk around 21 cents per litre**.

This is a statement of fact, designed to justify removing the "artificial" price distinction between market and manufactured milk. But as noted earlier in this paper, to put this in perspective, at the time of Australian dairy deregulation, European Dairy Farmers LTO Nederlands website's published average international farmgate milk prices for 2000 were 30.67 Euros per 100 kgs (which translates to around AUD 0.49c per litre at the average 2000 Euro conversion rate of 0.629077). (LTO 2002, OzForex 2007) in the same year, the average farmgate prices for New Zealand milk was quoted as Euro 16.64 per 100 kgs litre (around AUD 26.45 a litre) and as New Zealand is considered to be the world's lowest cost dairy exporter, the question arises as to why Australian dairy farmers were being paid such low prices for manufactured milk.[40]

The push to remove the price premium for market milk assumed that somehow, the extra input costs of producing milk at times when supplementary feed and water were required would be met by higher farmgate spot prices during those seasons, but this option is not necessarily available to those producers of market milk on set price contracts, such as the dairy producers currently supplying Dairy Farmers and National Foods. (Dairy Australia 2006: 49)

Also, the fact that post deregulation the farmgate milk price is now linked to **the** international milk market assumes that there is **an** international milk price, which there is not. Milk is a commodity mostly produced for local or regional consumption. Australia is one of the lowest cost milk producers in the world. However, by linking all Australian milk production to the export milk market and an artificial international milk price, (which is still lower than that obtained by most European producers [41]), we have seen a loss of ability of the Australian milk market to respond adequately to major impacts on local and regional milk supply, such as drought. [42]

This begs the question – who is ultimately making the decisions about what price is paid at the farmgate in Australia?

2) **Not all dairy farmers bargaining power was lost with deregulation**.

In effect this is a statement which admits that farmgate deregulation has, on balance, reduced dairy farmers market position by pointing out the exception to the general rule. The dairy farmers who did not appear to have lost bargaining power were from regions producing milk mostly for the manufactured milk market **and** who already belonged to a strong cooperative, like Murray Goulburn or Dairy Farmers. These dairy farmers received some marginal farmgate price improvements, at least in the short term.

Farmgate price setting by the states prior to deregulation included consultation with producers and their representative organizations. Based on the cost of year round production, the farmgate price for market milk was usually much higher than the manufacturing milk price. States have also had legislation that milk sold interstate for drinking is sold at the regulated farmgate price prevailing in the source state (Dairy Australia, 2003).

By removing the role of states in price setting, farmers without strong cooperatives who produced mostly market milk were hit hardest in terms of lost revenue. As shall be discussed later in the paper, this is why milk producers in states likes Western Australia have been struggling to gain the right for some form of collective bargaining with the multinational manufacturing sector or corporate supermarkets.

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[40] A further perspective of pre-deregulation farmgate milk prices can be gained from UWA agricultural economist, Henry Schapper's, 1956 paper "A Survey of whole milk producers for the Perth Metropolitan Area of Western Australia, which included farmgate prices from 1948 to 1956. Translated to cents and indexed to 2006 prices, they range from 86.28 to 93.6 cents per litre (Schapper 1956)

[41] LTO –Nederland published an International Milk Price Review for August 2006 ranging from 34.87 Euro cents per kilo in Finland down to 15.12 Euro cents per kg in New Zealand, the average on their list being 28.47 Euro cents per kg. (LTO 2006)

[42] A more responsive domestic milk price may mean an increase in milk imports in such times of difficult domestic production conditions.

It must be remembered, however that the deregulation at the farmgate was not the only influence on dairy farmers bargaining power. The loss of milk quotas and the removal of the distinction between market milk and manufactured milk occurred at the same time as the milk processing sector was concentrating even further and NCP driven changes to retail trading laws and creeping acquisitions have given the major supermarket chains even greater market power, impacting on both the milk processing and the dairy farm sector.

The changes to dairy farmers bargaining power has parallels within the industrial relations debate in relation to Australian Workplace Agreements. The following are excerpts from the December 2005 Journal of Australian Political Economy, introductory article by John King and Frank Stilwell:

"*Before 1993 almost all Australians were covered by awards, handed down by state and federal arbitration tribunals and regulating the conditions of their employment in considerable detail…* (King & Stilwell 2005: 1) – similarity with state-based regulatory arrangements for market milk.

"*…It is (…) likely that there will be an increase in the incidence of non-union CAs (certified agreements) both where there is no union involvement at all and where the employer takes part in token 'negotiations' on what is actually a take-it or leave-it offer…*" (King and Stilwell 2005: 9) – echoes of the loss of the negotiation process between state regulatory authorities and dairy industry representatives for milk prices and market conditions and the subsequent impact that has had on many individual dairy farmers attempting to 'negotiate' with a multinational dairy manufacturer or a major supermarket chain.

"*…What the 2005 industrial relations 'reforms' signal is an attempt to shift the balance of power between employees and employers.*" (King & Stilwell 2005: 12) – this echoes the general shift in market power to the corporate supermarkets and multinational dairy processors, under NCP.

The debate on market power takes on particular relevance when it comes to some of the more recent decisions made by the ACCC relating to the ability of dairy farmers to bargain collectively. This will be discussed in greater detail later in this paper in relation to the ACCC and Dairy WA.

3) *"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"*

This assumes that the post-deregulation farmgate market for fresh milk will be responsive to domestic supply conditions. It also assumes that any price premium which results from the consumer preference for fresh milk, post deregulation, will be passed on by milk retailers to the processors and by those processors to ensure supply from dairy farmers. In reality, these presumptions depend on the situation of the farming sector and the bargaining power of both the processors and the farming sector. [43] As the graph of Australia-wide farm exits later in

[43] There is some evidence that seasonal milk producers in states such as Victoria and Tasmania are being offered higher prices for off-season milk supply to entice them to change to a split calving system (Dairy Australia 2006: 49) but it is the primarily fresh milk producing regions such as parts of Queensland, where processors are facing

this paper suggest, accelerated dairy farm departures throughout Australia post-deregulation do not indicate that the bargaining power of dairy processors against the corporate retail sector or of dairy farmers against the rationalised processing sector has been sufficient to ensure farmgate prices which would prevent mass exits, either to other areas of production or out of farming altogether. [44]

4) *"Processor bargaining power (and their ability to influence price) has been found to be relatively weak"*

For a time after deregulation, whilst the ACCC were still monitoring the industry average farmgate prices improved, albeit in a very uneven fashion across Australian dairy regions (See Table 2). [45] This largely coincided with a reduction in the retail price of milk (especially for plain milk) and appeared to leave local processors struggling and vulnerable to takeover by interstate and overseas interests. [46]

The fact that milk is a dietary staple with a relatively inelastic demand enabled it to be used as part of aggressive corporate retail strategies to reduce their competitors' market share. The ACCC report indicates that farmgate deregulation has allowed the major supermarket sector to use milk as a means of bringing more customers into the stores to conduct their weekly shopping:

"*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. This has been the result of supermarkets discounting generic products.*

"On August 15 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 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.*" (ACCC 2001: xvi) (emphasis added)

This was happening at the same time as the states were being pushed by the NCC (as part of the National Competition Policy legislative review process) to further deregulate retail trading hours and the major supermarket chains taking the opportunity to pick off flagging

severe shortfalls in supply (Dairy Australia, 2006: 5) and Western Australia where only 38% of farmers felt their business was sustainable at current profit levels (Dairy Australia 2006: 83).

[44] See also Appendix D - Summary of social costs and benefits of dairy deregulation

[45] This price drop is illustrated in a graph of "*Supermarket prices for 2 litre milk 1998 to 2003*" in Spencer, (2004b: 23).

[46] See Table3 in Appendix B, below summarising the dairy processing ownership changes pre and post deregulation and Appendix C on the history of the Western Australian dairy processing.

competitors through creeping acquisitions. It was part of a multi-faceted process of grabbing more retail market share from convenience stores and independent supermarkets:

"*This strategy from 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*." (ACCC 2001: xvi)

This indicates that it was not so much the world market price for manufactured milk which was influencing such low farmgate prices for market milk as the corporate strategies to use milk as a "loss leader" made possible by the buying power of those same major supermarket chains (and the ability to access or threaten to access milk across state borders).

This begs the question as to what happened after many of the major supermarkets competitors had been taken over or knocked out of the market (and the ACCC ceased their monitoring 6 months after deregulation). How much of the retail milk price increase was passed on to the processors and then to dairy farmers? (See Graph 12 of retail and farmgate milk price indexes 1989/90 to 2004/5). The relative bargaining power of processors would still have been vulnerable to the tendering policies of the major supermarkets as the retail prices climbed towards and beyond their previous levels.

5) "*The report broadly concludes that Australian milk consumers are better off*"

The consumer benefits turned out to be short lived, in fact, not much longer than the time taken by the ACCC to monitor the industry! (See Graph 12)

6) "*Australian processors and retailers, therefore, have not captured the benefits of deregulation to the exclusion of consumers*"

The data on retailer and processor margins obtained by the ACCC in their April 2001 Report was made possible by their use of the special powers afforded them by the *Prices Surveillance Act 1983*. The retail and farmgate price indexes (Graph 12) show that retail milk prices and farmgate milk prices were not closely linked prior to deregulation, but after deregulation, farmgate prices became far more volatile, with little if any connection to retail market milk prices.

Hence there is a very strong argument that the ACCC should be required to undertake a follow-up study of dairy farmer, processor and retailer margins on milk and dairy products. Six months was not sufficient time for any firm conclusions to be drawn and the evidence of divergent farmgate and retail prices with an ever powerful and concentrated retail sector strongly suggests that the retail margin has increased not only at the expense of dairy farmers but at the expense of the Australian dairy processing sector as well.

7) "*Many dairy farmers in Western Australia, Queensland and New South Wales have been badly affected by the removal of farmgate price controls for drinking milk.*"

In terms of price and income drops, this statement is certainly true. According to the NCC report, it was Queensland (-25.6%), Western Australian (-22.1%) and New South Wales (-

14.1%) dairy farmers who suffered the greatest in loss of average gross income from 2000 to 2004 (Spencer 2004b: 26).

If your measure is farm departures, from 2000 to 2005, Queensland leads the way with 48.3%, followed somewhat surprisingly by South Australia (47.9%) and less surprisingly by Western Australia at 33.5%. The greatest number of farm departures over the period 1999 to 2005 were from Victoria (1867) but they had by far the highest number of dairy farms to start with and this number constitutes the lowest percentage (23.1%) of state farm departures over that period (ABS 1992-1995, 1996a, 1997a, 1998-2005, 2006a). The wider range of social impacts of deregulation are discussed in Appendix D.

It should be noted that in Western Australia, there is a growing fresh milk shortage (Dairy Western Australia: 7) and the northern NSW and Queensland dairy producing regions milk processors are facing the prospect of lower production levels. Dairy Australia reports that the northern (sub-tropical) processors:

"…face the prospect of severe shortfalls in local supplies. Farm gate values have been adjusted upwards, reflecting the value placed on year round supplies close to growing regional markets." (Dairy Australia, 2006: 5)

8) **"*…farmers in the other states that have traditionally had a high reliance on milk directed to the manufactured dairy products have seen market milk premiums largely offset by recent increases in prices for internationally traded dairy commodities*."**

This refers to such regions as Western Victoria, south-east South Australia and Tasmania. Not surprisingly, South Australia, Victoria and Tasmania recorded average gross income increases after farmgate deregulation, as opposed to the average income losses recorded in those states and regions which produced milk mostly for the fresh milk market. Between 2000 and 2004, the percentage changes in gross income have been calculated as Victoria (+ 15.1%), Tasmania (+19.7%), South Australia (+3%), New South Wales (–14.1%), Western Australia (-22.1%) and Queensland (–25.6%) (Spencer, 2004b: 26).

9) **Over the monitoring period, supermarket prices for plain, reduced fat and low-fat milk had, on average, dropped by 22 cents, 6 cents and 9 cents per litre respectively.**

As has been mentioned, although the six month monitoring period saw a drop in retail prices for plain[47] and some fat reduced varieties of white milk, a six month period without periodical reviews was not sufficient to be certain of such trends, as shall be seen in Graph 10 below. The reality was that the drop in average milk prices was not permanent.

10) **Supermarket prices for UHT, flavoured and specialty milk increased in price by 10 cents, 14 cents and 3 cents per litre respectively.**

And even as plain and lower fat white milk dipped in price, albeit temporarily, other varieties of milk increased in price, perhaps partly because of the increase in farmgate prices for manufactured milk, but also because it was necessary for the survival of the processing

[47] Particularly generic brand milk, where supermarkets could play off one supplier against the other.

sector.[48] It is understood that the ABS milk price indexes takes into consideration the relative prices and market shares of the retail milk product range. (Perscomm Steve Whennan ABS Canberra 2006)

11) Supermarket gross margins on milk declined by 19 percent (with retail prices falling at a greater rate than the wholesale prices). Despite a six percent increase in sales volumes, overall aggregate milk revenue decreased during this monitoring period. (This sales volume increase was matched by a 24 percent decline in convenience stores milk sales over the same period)

The ACCC must be commissioned to follow up this short period of monitoring to be sure what the trend in gross margins has been in reality and who have been the real winners and losers of dairy farmgate deregulation and to what extent.

12) Net profit margins for milk processors decreased by 12 percent and 18 percent for the September and December quarters respectively relative to the June 2000 quarter.

They go on to say that even as the price discounting of branded milk "fell away" (in the December 2000 quarter) net profit margins remained considerably lower than for periods before deregulation. (ACCC 2001: xviii)

The sharp (albeit impermanent) retail price drop and associated (but longer-lasting) wholesale price squeeze may well have broken the camel's back for a number of remaining local dairy processors. For instance in Western Australia, in 2000, Manassan foods, a NSW based food company took over the Margaret River Dairy company and in the same year, Kiwi Co-operative holdings (who later became Fonterra) acquired a 54% stake in PB Foods (Peters and Brownes). [49]

13) After deregulation, despite the changes in the mix and volume of sales, the total volume of milk sold in Australia was largely unchanged.

This is hardly surprising as the demand for milk is fairly inelastic, but it is at odds with the predictions of the Industry Commission Report on Statutory Marketing Arrangements in 1991, which predicted an increase in overall milk demand in Australia due to their prediction of lower post-deregulation prices. (IC 1991a: 230) Other non-dairy options such as soy milk and variations in market conditions such as an ageing population may be contributing to a slight per capita decline in milk consumption (see Graph 14).

14) The drop in aggregate revenue losses translated to a savings to consumers which they projected to be worth more than $118 over a full year.

The ACCC must be required to revisit these findings.

15) Supermarkets reported to the ACCC that their lower prices for generic labelled milk (introduced in August 2000) would apply indefinitely.

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[48] And because flavoured and specialty milk were not considered staples, like white milk, to be used as "loss leaders" by the major retail chains?

[49] This is particularly significant as Fonterra are based on a large New Zealand dairy producers' cooperative and New Zealand is Australian's main international competitor on the dairy export market.

Generic branded milk may well be generally sold at a lower price than most branded milk (Harvey Fresh has been an exception in WA), but that does not mean that even the index of those prices have not now climbed at a rate greater than the CPI index (See Graph 10), contributing to the rise in the average milk price index.

Dairy: Now and Then - The NCC defends dairy deregulation

In April 2004, The Federal Treasurer, Peter Costello, commissioned the Productivity Commission to conduct a review of National Competition Policy. Given that a review by the Productivity Commission (in their former role as the Industry Commission) were some of the major proponents of National Competition Policy, having enlisted the potential corporate "winners" as political allies, such a review could hardly be seen to be "independent". As part of this "review" process, the National Competition Council chose to contribute by commissioning three projects; a wish list for the next round of deregulation, and reviews of the impacts of grain industry and dairy industry market deregulation. (NCC: 2004: 1)

Ridge Partners, Consultants and Advisors, were selected by the NCC to produce a report into dairy market deregulation but, at the same time the author of this report, Ridge Partners' director, Steve Spencer, was working for Dairy Australia on "*Dairy 2004: Situation & Outlook*", a paper on behalf of "Dairy Moving Forward". "Dairy Moving Forward", as its name suggests, was a collaboration seeking a positive future for the Australian Dairy Industry.[50]

It is argued that *Dairy 2004: Situation & Outlook* takes a "Don't mention the WAR" approach (the "war" being dairy market deregulation) and, in its efforts to be positive about the dairy industry, displays some serious problems of methodology. Indeed, the author of the NCC-commissioned *Dairy: Now and then report* has included many sections which have simply been cut and pasted from the "Dairy Moving Forward" document!

It is therefore not surprising that *Dairy: Now and then* provides few sources for its data and findings, has no reference list and no bibliography attached.

One of the more serious problems of methodology relates to the fact that the reported producer attitudes and future projections in *Dairy 2004: Situation & outlook* are based on survey data of the Australian Dairy Industry. They rely primarily on the results of a phone survey which is premised on the multiple positive (and arguably unrealistic) positive assumptions that "weather patterns and feed prices are favourable over the next 12 months…" and "thinking ahead to the 2006-2007 season and assuming favourable weather, if prices increased by 2-3 cents a litre…" (Spencer 2004a: 66).

It is also mentioned of a total of 33% of farmers refusing to participate in the National Dairy Farmer phone survey, 20% of contacted farmers refused to be involved because "they don't like to get involved", another 4% refused because they were feeling too negative about the industry and a further 4%, did not participate because they were planning to leave the dairy

[50] Dairy Moving Forward was a collaboration between sections of the Australian dairy industry and funded by Dairy Australia. Dairy Australia, in turn, is Government and producer levy funded.

industry. [51] By interviewing the others, the authors themselves admit that the phone survey may be biased away from people negative about the industry (Spencer, 2004a: 59)!

They also distributed a less-detailed mail survey (which did not include that multiple positive premise). They admit that the results of both were quite different, both in the level of optimism/pessimism and the explanation of the reasons for the current market difficulties. The mail survey outlooks were far more pessimistic but they were considered less statistically reliable because they were self selected rather than randomly selected like the phone survey. It would hardly be surprising that a mail survey, which could be submitted with a degree of anonymity, would produce a higher number of respondents prepared to blame the buying policies of the major supermarkets for the farmgate prices during the drought.

Another example of different responses is that 77% of participants in the phone survey indicated they intended to be in dairying in 3 years time, as opposed to only 60 % of the mail survey participants. There were 1079 phone surveys conducted but, significantly, 2,579 dairy farmers returned mail surveys. (National Dairy Farmers Survey, 2004 p 5) (except for WA farmers who were not sent mail surveys and were asked had some slightly different phone survey questions).

Apart from the methodological problems in the 2004 farmer survey, as shall be shown, later in this paper, there are also serious and acknowledged data gaps in the NCC *Dairy Now and then* including in the social impacts of dairy market deregulation. To quote from the submission:

"*There is little data available from within the dairy industry and wider government resources to measure important flow-on effects of the change in the industry over the last 5 years since the inevitability of removal of regulation became apparent.*

These gaps include:

- *Readily available current information on dairy industry employment at a regional and sub-regional level in farming and factory occupations*."
- *Changes in farm performance and productivity across dairying regions across different production systems and different farm sizes(…)"*
- *An analysis in the changes in farming practices and the uptake of technology in regions most affected by change.*
- *A comprehensive understanding of the use of DSAP* (Dairy Structural Adjustment Package) *and SDA* (Supplementary Drought Assistance) *in the years since their availability, including the impact that drought had on their application in dairy enterprises.* (Spencer 2004b: 8) [52]

In other places in the submission, analysis and conclusions appear either contradictory or to be at odds with their own data. For instance, in relation to farmgate milk prices, on page 10:

[51] This last 8% were probably the ones whose views may have been most important.

[52] In the last point, there is no acknowledgement of the need to understand not only the impact of drought on the uptake of structural adjustment funds, but the need to know how deregulation had impacted on the ability of dairy farmers to survive serious supply challenges such as drought.

"*…farmgate milk pricing for **all producers across Australia** will be shown to be inextricably linked to world market conditions*."[53]

Then on page 13:

"In simplistic terms, farmgate prices are derived by major cooperatives based on the following equation which sees the milk return derived as a residual value:

Gross income
- *The returns from sales into a mix of export and domestic markets*

Less:
- *Costs of milk collection and cartage to factory;*
- *Costs of processing and manufacturing;*
- *Costs of marketing and distribution;*
- *A retention for business profit, working capital and capital investment*." (Spencer 2004b: 13) (emphasis added)

It should be remembered that Australia's major milk cooperatives were producing mainly manufacturing milk, so it is unclear where this method of calculation was being applied. There is no reference to the source of the date of this information, and as it appears to be describing the situation as existed when milk prices for manufactured milk and market milk were being pooled and prices were negotiated by these cooperatives and others in the industry in conjunction with the state-based statutory dairy marketing authorities, this reference information is all the more important.

It may be the case that the major cooperatives have played a major role in setting a minimum standard for farmgate pricing, and since the artificial linking of fresh milk to the international milk market:

"*Processors no longer have regard to the end use of milk in products, using a uniform pricing approach in each region*." (Spencer 2004b: 35)

And, of course, the major changes to farmgate prices created by the national tendering systems by the corporate supermarket chains in a post-deregulation environment:

"*Removal of farmgate regulation however allowed the creation of a meaningful national retail supply market at wholesale:*

- *retailers could then have access to cheaper quotes based on a transparent Victorian benchmark milk supply price which was based on the lower farmgate supply price given the low-cost production conditions – even on a year round basis*
- *they could then ask dairy companies to bid for business on a national basis, without the restrictions on farmgate pricing across state borders*." (Spencer, 2004b: 36)

But, there is also recognition of the way that the inelastic nature of milk demand is being used by the big retail players in a deregulated (post NCP) environment:

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[53] Which, as we have seen earlier in the paper is misleading in itself because the average "world" price for milk works out to be about twice the Australian farmgate price.

"*With the increased market share sought by major chain retailers, independent food stores and specialist retailers (such as Aldi) have discounted milk lines taking their price per litre consistently under $1 per litre) as part of their strategies to* ***loss lead*** *the customer into the store*." (Spencer 2004b: 22 (Emphasis added)

This is another reason why it would be important for the ACCC to be asked to use their powers under the *Prices Surveillance Act* to investigate just how many of those occasions were actually "loss leading" and by how much, to gain increased retail market share, and how frequently extra pressure was placed on milk suppliers to accept lower wholesale prices:

"*It can be argued that the removal of farmgate regulation created the opportunity for retailers to take greater control of the supply chain through the exertion of competitive pressure. Again no measurement of the effect of these changes has been undertaken at a regional level*." (Spencer 2004b: 42)

Their conclusion - blame the drought and the world market [54]:

"*To conclude that the significant changes that have been seen in farm numbers, farm incomes and employment in the industry are the direct product of deregulation would be a gross simplification, as…* (world market changes and drought)*… have worked to create considerable change in the level and structure of farmgate returns in the industry since June 2000*." (Spencer 2004: 6)

This example leads to the question: Was *Dairy: Now and then*, a fully objective assessment of the outcomes for the Australian dairy industry, or the result of a recognition of the public controversy surrounding dairy farmgate deregulation and an example of the NCC carrying out their admitted "*…central role in promoting NCP reforms*"? (Spencer 2004a: 1)

To help to answer this question and put some perspective to a number of the Industry Commission's original assumptions, this paper critiques in some detail the main arguments, data and conclusions in *Dairy: Now and then*.

Firstly, it should be noted that, in the forward to the NCC submission, the executive of the National Competition Council is quoted as saying that he saw this submission as a means of making a positive contribution to the Productivity Commission's 2004 review of National Competition Policy as part of its role in "*…promoting NCP reforms*" in response to "*…claims of adverse results from reform*" for that sector, in other words, controversy. (Spencer 2004b: 1)

The submission repeated some of the main claims of the 2001 ACCC report:[55]

- *Savings to consumers were estimated at over $118M from supermarket sales alone;*
- *Farmgate prices fell by around 19 cents per litre in respect of the supply of milk for market milk usage;*
- *Retail prices fell by 22 cents per litre, taking account of the 11 cents per litre levy to fund the DSAP; and*

[54]Even though deregulation has, arguably, made dairy farmers far more vulnerable to both.
[55] The submission claims that the ACCC findings were "*…in the first year after deregulation of fresh milk supply*" but its oversight stopped only six months after farmgate deregulation (Spencer 2004: 5).

- *Supermarket margins fell 18% in the first six months and processors by 19%.* (Spencer 2004b: 5)

As we have seen, even the ACCC acknowledged that six months into deregulation was an unusually short period for such a monitoring exercise. Therefore the NCC submission claimed, (amongst other things) that it would:

1. *"Assess the longer term outcomes from the deregulation of the dairy industry, including the national impacts of the reforms on the sector as a whole on **output, scale, employment, productivity** and **efficiency**"*. and

2. "*Assess the distributional impacts of the reforms on **farmgate, processor** and **retailer margins**.*" (Spencer 2004: 5) (emphasis added)

The report also provided a summary of the impacts of farmgate deregulation on three dairying regions (Subtropical, that is, SE Queensland and Northern NSW, Western Victoria and Western Australia), commented on the relative contribution of international market forces and deregulation to the "structure and competitiveness" of the dairy industry and discussed the impacts of the adjustment package linked to the NCP driven changes (Spencer 2004b: 5).

The NCC submission discussed its main findings under the following headings;

- **The key impacts at farm level are blurred;**
- **The change in incomes;**
- **Consumer is the winner;**
- **Major changes in the industry;**
- **Changes in practices;**
- **Theory v outcome**
- **Future challenges for the industry; and**
- **Where further work may be required.**

(Spencer 2004b: 8)

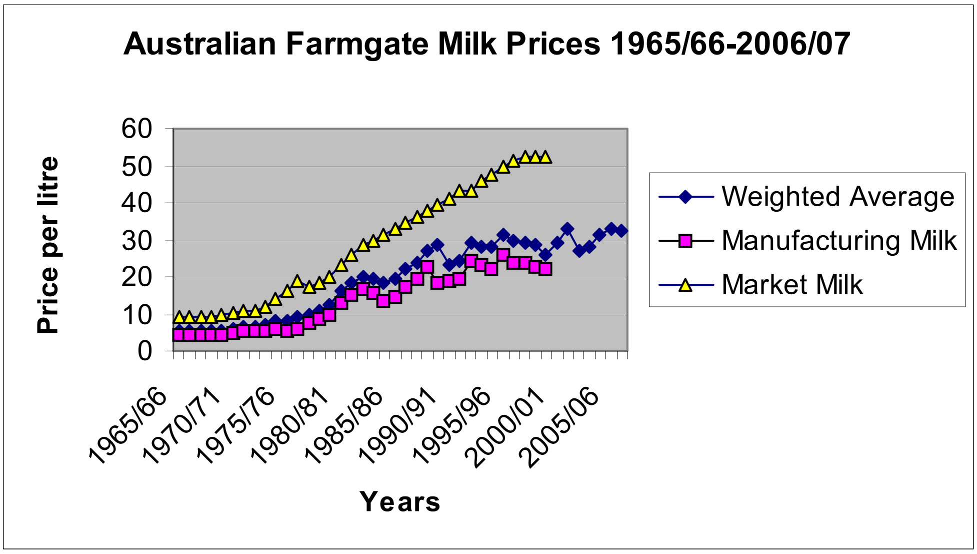
Taking each of their headings in order:

<u>"The key impacts at farm level are blurred"</u>

It is true to say that the impacts at the farm level have not been uniform across all dairy producing regions in Australia. Averages don't tell the whole story. As can be seen from Graph 1, following deregulation, whilst the prices paid to producers of market milk plunged, the weighted average farmgate price for milk rose to 33.9 c/l in 2001/02 but then fell back to 27.1 c/l in 2002/03 before a mild recovery (ABARE 2005d, 2006b, 2007).[56]

[56] This graph also shows how farmgate prices for manufacturing milk had been edging down prior to deregulation (at the same time the industry-funded assistance for domestically consumed manufacturing milk was being wound down by the Federal Government.)

Graph 1



Data Sources: ABARE 2005d, 2006b, 2007

The key point is that biggest price impact has been on the farmgate price of market milk which has experienced substantial falls while farmgate prices for manufactured milk, following farmgate deregulation increased a few cents per litre. The actual farm impacts in each region depends on the percentage of market milk and manufacturing milk which each region produces.

The loss of market milk premiums may have affected the end use of Australia's milk production to some extent but the change in end use is also a function of the relatively inelastic nature of fresh milk demand which tends to expand in line with population, meaning that any additional increase in milk production can only be directed to manufactured or export markets.[57]

The least vulnerable dairy states to the drop in market milk prices post deregulation were those whose percentage of market milk to manufactured milk was lowest, (Victoria, Tasmania and South Australia), and the more vulnerable were those with rising percentages (in NSW, WA and Queensland).

The figures from the NCC report for market milk show the following price changes from 2000 to 2004:

[57] Production data anomaly - Dairy 2004 reported that the percentage of milk exported grew from 44% in 1992/93 to 59% in 2002/03 Dairy 2006 reported that this fell back to 50% in 2004/05, due to the decline in total industry output and the need to redirect some of the manufactured and export component back into market milk. (Dairy 2006: 11) However, the same author (Steven Spencer) in Dairy: Now and then said the 1992/93 figure was 38%.

Table 2 - Farmgate milk prices changes 2000-2004

Pre-deregulation				Post Deregulation	
Dairy Region	Market milk	MFG milk	Average Price	2003-4 prices	Av change
Far North QLD	54.9	21.9	36.7	29-31	-5.7 to –7.7
Central QLD	54.9	21.9	36.7	38-41	+1.3 to +4.3
S E QLD	54.9	21.9	36.7	29-31	-5.7 to –7.7
N Central & S NSW	47.7	21.8	32.6	29-34	-3.6 to +1.4
Victoria	42.7	22.2	22.2	25-30	+2.8 to +7.8
South Australia	44.6	22.2	28.0	25-30	-3.0 to +2.0
Tasmania	44.6	18.8	20.9	25-27	+4.1 to +6.1
Western Australia	45.5	24.6*	34.3*	24-27	-7.3 to –10.3

Data Source – Dairy: Now & then, 2004: 20

* These figures from the NCC commissioned report appear to be at odds with those from a 2003 Report to the WA Parliament which puts the average pre-deregulatory manufacturing milk price in WA as 21c/l and the average net price at 29 c/l (Economics and Industry Standing Committee 2003: 24).

A clear pattern emerges. The average percentage gross income changes from 2000 to 2004 are recorded as Queensland -25.6%, WA –22.1%, NSW –14.1%, SA + 3%, Victoria + 15.1% and Tasmania + 19.7% (Spencer, 2004b: 26).[58]

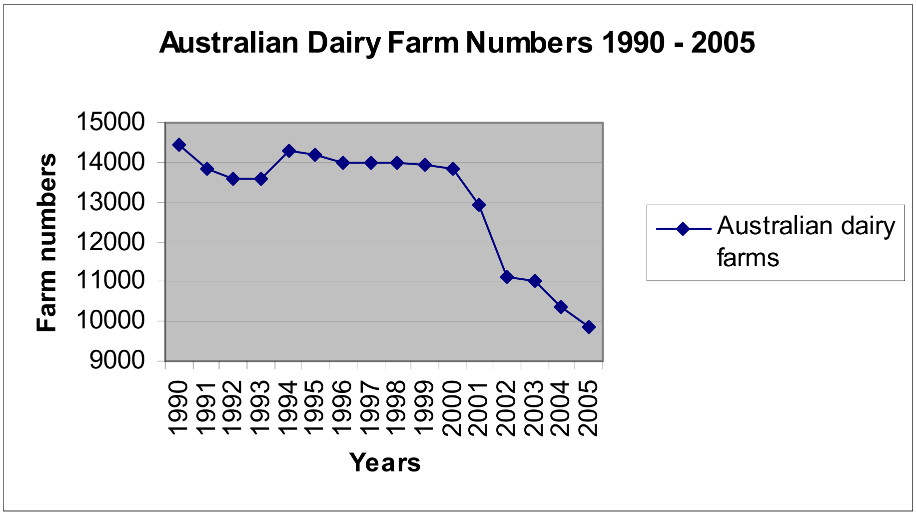
ABARE shows in its Dairy Industry Reports (03.1, 04.1 and 05.1) that Australian dairy farms have been profitable slightly more than one year in every two prior to deregulation in 2000. However, because there are greater numbers of dairy farmers in the areas whose incomes increased, Australia wide, the figures will show that there has been a slight average increase in farm incomes.

What the ABARE graphs do show is that post deregulation profitability has become highly unstable. That is, tying all farmgate prices to a mythical world price means that in years of poor production conditions in Australia, there may be low international prices and vice versa. The outcomes have therefore become even less stable than before.

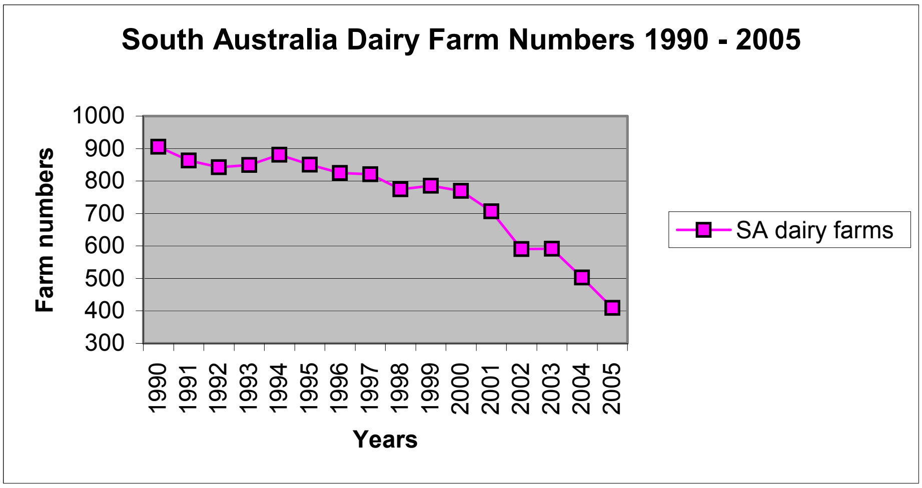
One measure of the impact of this increased profit risk and instability is the level of farm departures, Australia-wide and state by state. There is little doubt that, Australia-wide dairy farm exits have accelerated since deregulation, as can be seen from the graphs of dairy farm departures below.

[58] Not surprisingly, the impact tens to be inversely proportional to the proportion of drinking milk produced by each dairy region.

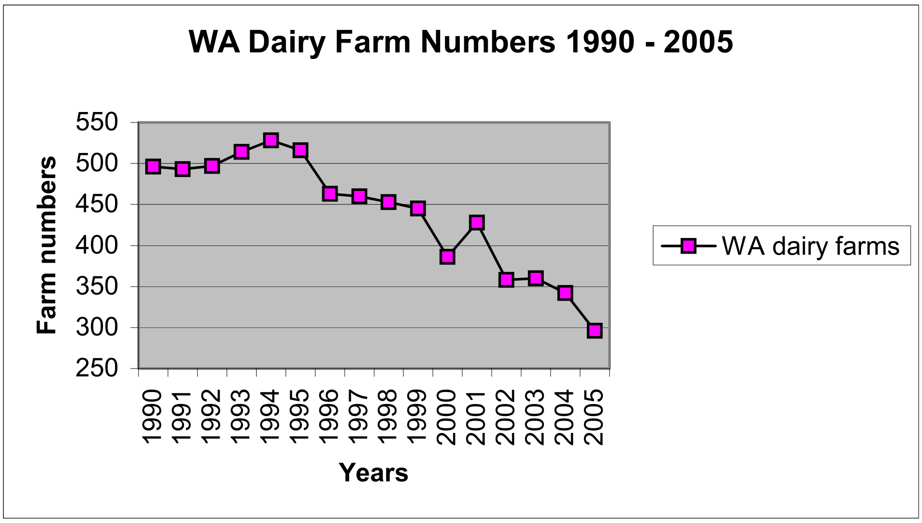
Graph 2



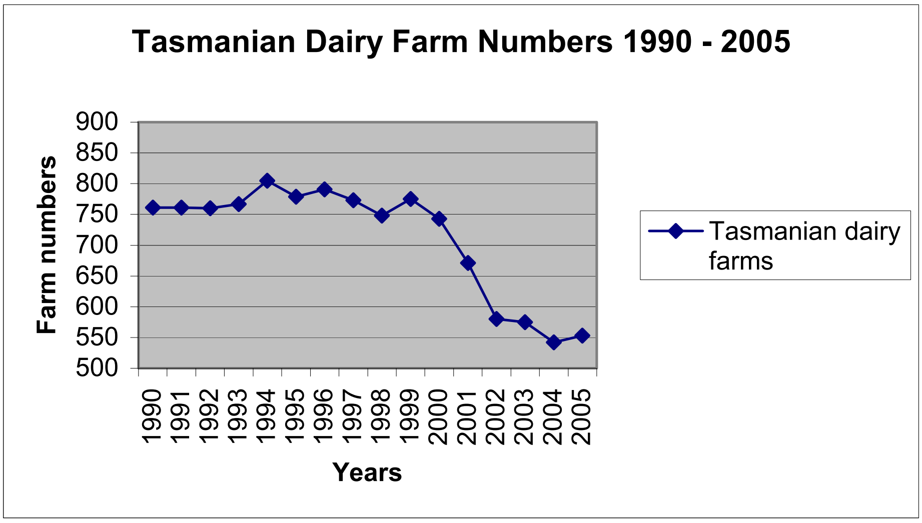
Graph 3



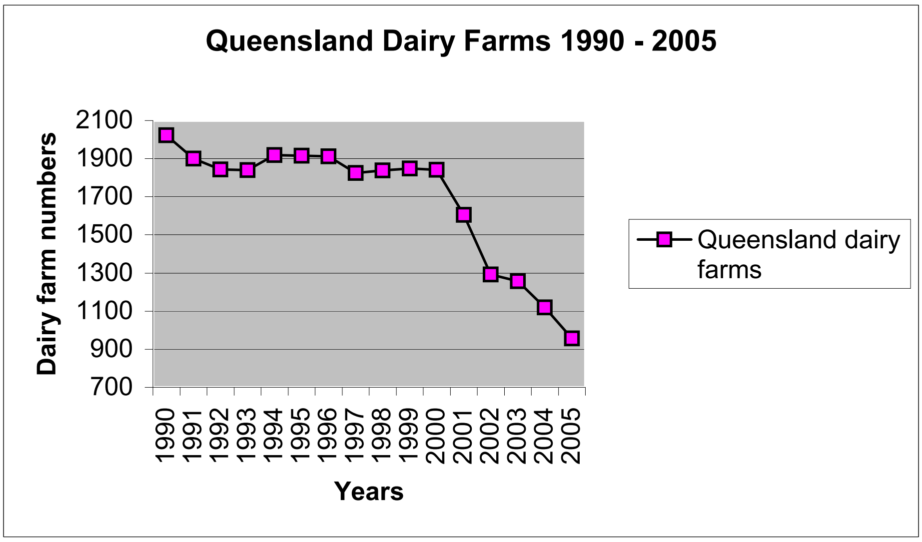
Graph 4



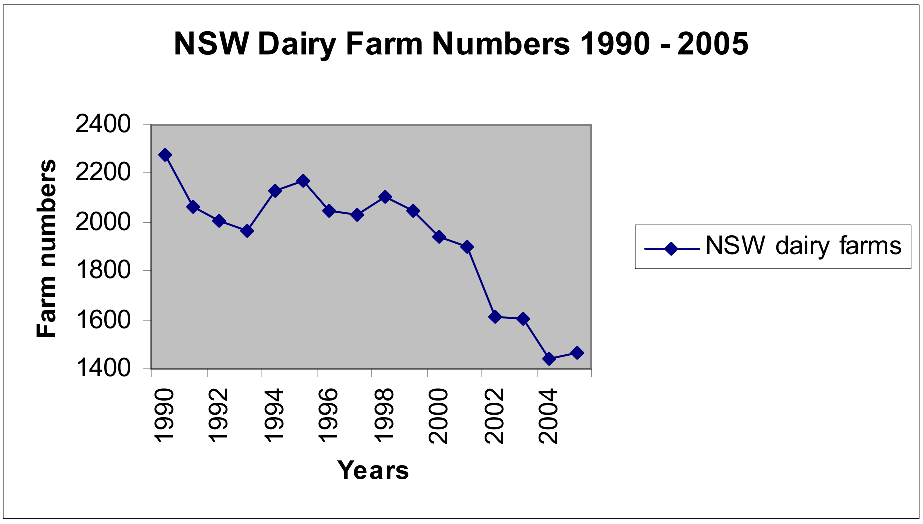
Graph 5



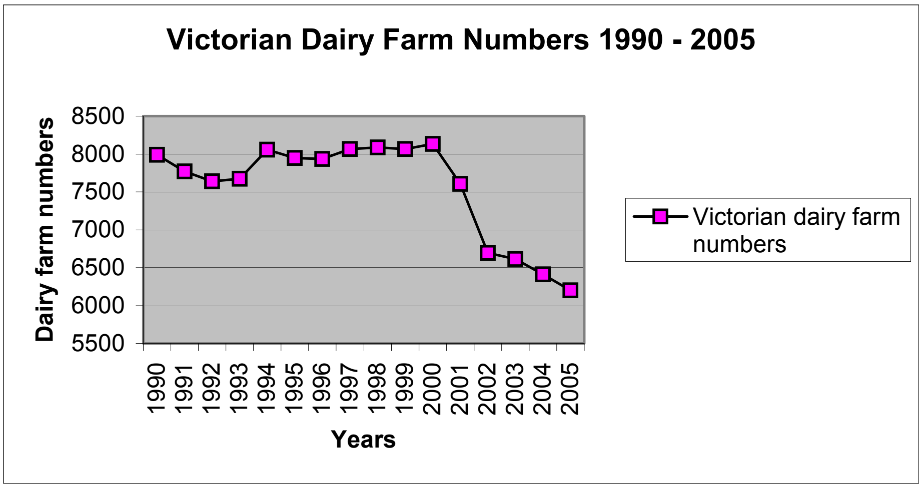
Graph 6



Graph 7



Graph 8



Data Sources Graphs 2-8: ABS 1992-1995, 1996a, 1997a, 1998-2005, 2006a) and ABS 2006d 1997/98 – 2004/05

The graphs of farms departures show that, across Australia the greatest number of farm departures occurred between 2000 and 2002, but farm departures have continued, especially in those market milk focussed states like Queensland. Perhaps the most telling story this tells is that post 2000 dairy farming, even in Victoria, has been unsustainable for many dairy producers (See Box 2 'The Kiwi Invasion').

Box 2 - 'The Kiwi Invasion'

Graphs of farm numbers may not give the full picture of Australian dairy farm departures. In recent years, in a number of Australian dairy regions, dairy corporations have sought to attract more dairy farmer immigrants, mainly from New Zealand but also from European countries such as the Netherlands and the UK. To quote from an industry publication:

"*With the 'invasion' of New Zealand dairyfarmers to Victoria showing no signs of abating, WCB* (Warrnambool Cheese & Butter) *considered the time was right to launch a promotion in Kiwi land to make farmers fully aware of what was on offer in south-west Victoria, particularly with Warrnambool Cheese & Butter."* (Warrnambool Cheese & Butter Newsletter April 2006: 2)

A Victorian regional newspaper also refers to the recent trend:
"*More New Zealand dairy farmers have set up operations in Victoria in recent years because of high land costs and a restrictive milk supply structure back home.*" (Matilda Abey, The Weekly Times, March 21 2007: 96)

This dairy farmer immigration trend appears to be wider than just Victoria. A March 2007 Australian Dairy Conference program included a presentation entitled 'the Kiwi Invasion' (http//australiadairyconference.com.au/program.htm – accessed 19/4/07). Also, the Tasmanian 'IntoDairy' website promotion of dairy business immigration includes transcripts of interviews from ten couples explaining why they have moved to Tasmania in recent years from other countries, mostly from New Zealand, citing the relatively cheap dairy farmland, the offer of sharefarming (from dairy corporations) and the lack of dairy regulations compared to their home countries as amongst their reasons for moving (http;//www.intodairy.com.au/migration/ - accessed 19/4/07)

Dairy: Now & then admits that the on-farm impacts of deregulation are "discernable", but qualifies them be saying they are "blurred by:

- *Significant changes in the world market for dairy products which have seen major cyclical change since June 2000*, and
- *The impact of drought which has severely affected most dairying regions directly or indirectly overt he period from late 2001 through to the present time.*

(Spencer 2004b: 6)

The ABS figures show that Australia-wide from 2000 to 2005 we have lost around 3939 dairy farm businesses (an average 28.5% reduction), that is, nearly one third of dairy farm businesses have been lost in only 5 years after deregulation and as the farm exits have not levelled out, this figure will get worse.

Breaking down these figures, from 2000 to 2005 WA lost 90 dairy farms (23.3%), Victoria lost 1934 farms (23.8%), NSW 475 (24.4%), Tasmania lost 190 (25.6%), SA lost 361 (46.9%) and Queensland lost 886 (48.1%) %) (ABS 1992-1995, 1996a, 1997a, 1998-2005, 2006a). On these figures, so far, Queensland dairy farmers appear to have responded most negatively, suffering the multiple whammy of a substantial cut in farmgate income, drought and cyclones!

Dairy Australia reports that, according to their survey respondents, there is worse to come, especially for the mainly market milk production regions:

"*…the highest exit rates over the next three years are likely to be in Far North Queensland (40% saying they are unlikely to remain in industry in response to direst question, 30 % suggesting this will be the case in relation to production) and WA (34% and 24%).* (Dairy Australia 2006: 25)

And on these farm departure figures, whilst Western Australian dairy farmers appeared to have coped better than states like Queensland or South Australia, in terms of percentage of farm losses, their relative pre-deregulation efficiency may have helped (See below) it needs to be factored in that WA did not experience the drought in the early 90s from which many of the eastern states dairy producers struggled to recover. 2007 could be the maker or breaker for the Western Australian dairy industry, given the record low autumn rainfall and low winter rainfall conditions experienced. It should also be noted that, given the size of Western Australia, the relatively small number of remaining dairy farms and the very high level of producer discontent, (Ibid: 26), we could soon see the recent drop in milk production translate to a mass exodus of many of the remaining dairy farmers if their concerns are not addressed.

A 2006 Dairy Australia farmer survey showed that WA Dairy farmers were by far the most negative about their future. Whilst better rainfall in most dairy regions in the last two seasons in the other states has seen positive feelings to the industry improve (61% positive about the industry as opposed to 53% in 2005 and 34% in 2004, Dairy Australia report that in 2006 only 29% of Western Australian dairy farmers are feeling positive about their industry, compared to 53% negative (Ibid: 26).

This paper argues that farmgate deregulation has made all Australian dairy producers more vulnerable to local supply problems such as drought conditions because it has effectively disconnected the normal supply and demand signals from local market conditions. [59] In times of drought and other supply problems, producers of fresh market milk have considerably more expenses involved to supply the market (such as supplementary feed and water), given the relatively inelastic demand for milk and the contradictory obligations of fresh milk suppliers. The international milk market cannot respond to local conditions effectively, and if local

[59] Drought is of growing concern because climate research indicates that in the eastern states of Australia, drought occurs when the Southern Oscillation Index (SOI) is strongly negative. A graph of the SOI shows that these events are occurring more frequently and with greater intensity in recent decades. A graph of the SOI since 1886 is included in Appendix E

processors fail to adequately increase their prices in recognition of extra production costs during periods of drought etc, this will leave dairy producers even more out of pocket, accelerating farm departures.

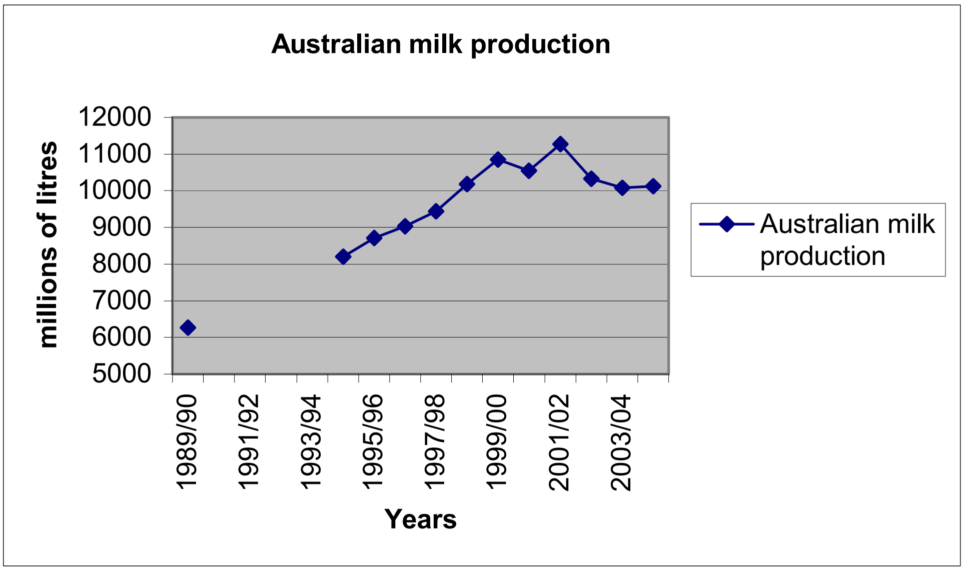
The low producer margins, increased exposure to international market volatility and the disconnection of market returns to local supply conditions is beginning to create shortages in the fresh milk sector, something which was not predicted by the Industry Commission, who suggested that there would be increased demand for retail domestic milk and a slightly expanded production that sector!

Recalling one of the Industry Commission's earlier projections on dairy production outcomes, i.e. that exports production would decline by around by around 80%, what does the current data show?

ABARE publications show that Australian dairy farm numbers declined from the mid 1970s until the late 1980s, levelling out until 2000, at which point dairy farm numbers again began to decline rapidly, (coinciding with farmgate deregulation). These publications also show that milk production began to increase in the late 1980s and continued to grow until 2000, dropping briefly then peaking in 2001/02 before a combination of drought and accelerated farm departures began to have an impact on Australia's total milk production. (ABARE 2003a, 2004, 2005a)

Graph 9 below shows Australian dairy production from 1994/95 to 2004/05 with the figures for 1989/90 included as an indication of the movement of production from the early 1990s.

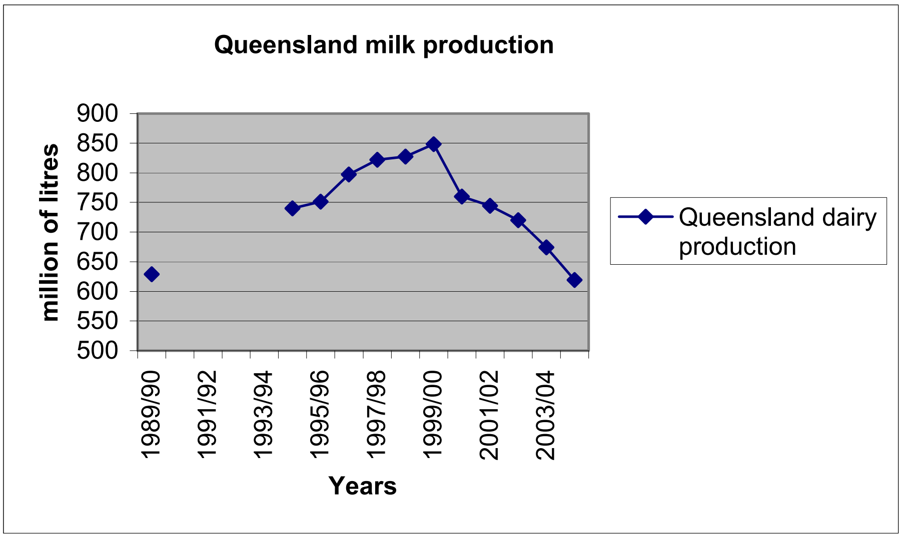
Graph 9



Data source: Dairy Australia 2005a: 15

The effects on production vary across Australia with the greatest impact evident in Queensland.

Graph 10

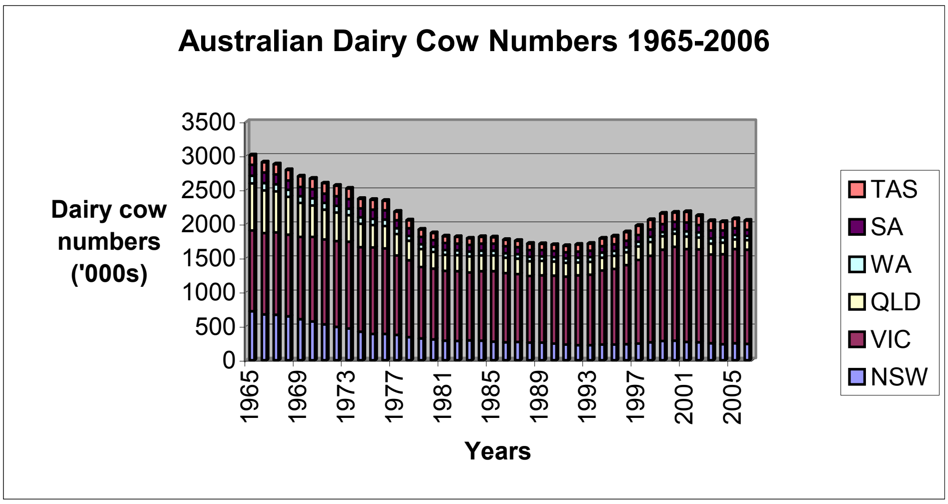


Data source: Dairy Australia 2005a: 15

It should be noted that that farm departures do not necessarily mean a drop in production capacity if the land and other production assets, including dairy cattle are consolidated into larger holdings. However, if stock is sold off and dairy farms are converted to other farming, or dairy land is sold for other uses, that production capacity may be difficult to replace.

Graph 11, below, shows what has happened to dairy cow numbers from 1965. The rise in dairy cow numbers from the early 1990s until 2000 roughly coincides with an increase in Australia's dairy export volumes.[60] If the majority of farm departures were from market milk producers, those regions with the greatest losses will need higher farmgate prices and incentives for sufficient numbers of seasonal milk producers to switch to year-round production if ongoing domestic market milk shortages are to be avoided even after the drought has broken.

Graph 11



Source: ABARE 2006b: 78

[60] See Graph 13

Dairy Australia reports:

"*The production sector has benefited from a second year of relatively high farmgate returns and low grain prices, offering favourable production margins in most regions. Nevertheless, production has not grown, as farmers have focussed on consolidating their businesses, while others continue to take the opportunity to exit*." (Dairy Australia 2006: 5)

And while Dairy Australia reports a growth of positive sentiment in those regions which have benefited from increased returns, "…*in northern fresh milk regions supply and demand curves are converging, and processors face the prospect of severe shortfalls in local supplies*." (Dairy Australia 2006: 5) [61]

In Western Australia, production dipped in 2001 but from then has been fairly steady until recently, despite farm departures (Ibid: 82). But Dairy WA report that the situation amongst their members is changing:

"*At the time of deregulation it was estimated that based on milk production there was approximately 70,000 dairy cattle in Western Australia.*

Initially volumes of raw milk produced did not decrease, as remaining dairy farmers purchased the herds of farmers exiting the industry. This changed in the current financial year, herds are now being exported and/or slaughtered and the volume of raw milk produced started to decline in March 2004. Grower reports indicate that twelve (12) months ago 100% of dairy stock sold in the market place were actively purchased by dairy farmers currently this has been reduced to approximately 50%, with the remaining stock sold for export or slaughter.

It is anticipated that there will be a further reduction in March 2005 when it is anticipated further dairy farmers will exit the industry." (Dairy WA 2005: 7)

Western Australian raw milk production prior to deregulation (1999/00):
Milk production 412 million litres
Market milk 190 million litres

<u>The volume of raw milk produced in 2003/04:</u>

Milk production 403 million litres
Market milk 204 million litres

<u>Rolling yearly raw milk production to the end of January 2005</u>:

392.3 million litres

(Dairy WA 2005: 7)

[61] In the Far North Queensland dairy regions, they didn't only have to contend with drought but also Cyclone Larry!

Since then, Dairy Australia's figures for WA milk production are:

2004/05 395.8 million litres
2005/06 377.2 million litres
2006/07 349.4 million litres.

(Dairy Australia 2007)

Whilst the dry conditions and the increased costs of supplementary feed will have contributed to this decrease in production levels, the removal of statutory marketing arrangements and subsequent severe reduction in dairy producers bargaining power has clearly kept the farmgate prices below the level where such increased costs could be adequately covered.

Given, as we have seen, that the current and expected exit rates for largely market milk producing regions like Far North Queensland (40% saying they are unlikely to remain in industry in response to direct question, 30% suggesting this will be the case in questions relating to production) and WA (34% and 24%) (Dairy 2006: 25), it would appear that there are going to be looming serious supply problems in the near future in these regions. This is significant in light of the Australian Dairy Farmers' Federation original submission to the Hilmer inquiry in 1992 which stated that, one of the two primary functions of State Statutory Marketing authorities was:

> "*To ensure a supply of fresh milk to consumers 365 days a year…*" a function which they also expressed as "*…an essential role of Government*." (Australian Dairy Farmers' Federation 1992: 1)

Efficiency and productivity assumptions and outcomes

The assumptions that statutory marketing arrangements result in inefficient production were simplistic in that they make no distinction for regional circumstances or outcomes of deregulation. They were clearly based on the assumption that the price for market milk was simply an export subsidy to inefficient dairy producers. If that was the basis for the assumption, those dairy regions with the highest market milk prices prior to deregulation should be the least efficient. However, In their 2005 paper for Australasian Agribusiness Review, Efficiency Measurement of Australian Dairy Farms: National and Regional Performance, Iain Fraser and Mary Graham found Western Dairy (WA) to be, on average, the most efficient prior to deregulation. Calculated the average using 6 inputs, the results were as follows[62]:

[62] Dairy Regions indicated:

- Western – south-west Western Australia
- Dairy SA – South Australia
- Gippsland – eastern Victoria
- WesVic – Includes south-west Victoria and south-east South Australia
- Murray – the River Murray region of Victoria and NSW
- DIDCO – the Central coastal area of NSW
- Sub-Tropical – eastern Queensland

Table 3

Region	No Farms Assessed	Mean	Minimum	Maximum
Western	94	0.625	0.253	1
Dairy SA	130	0.622	0.252	1
Gippsland	295	0.614	0.221	1
WestVic	280	0.614	0.215	1
Tasmania	179	0.603	0.252	1
Murray	308	0.578	0.131	1
DIDCO	191	0.573	0.228	1
Sub-Tropical	265	0.265	0.148	1
Australia	1742	0.589	0.131	1

Source: Fraser and Graham, 2005: 6 [63]

Across the Australian Dairy Industry, the data from Dairy Australia and the published ABARE papers indicates that total factor productivity began to drop off after deregulation. It is noticeable, however, that both Dairy Australia and ABARE seem to have difficulty admitting this in so many words. Instead of talking of the reasons for the drop off in productivity from 2000, as can be seen from the quote below, ABARE talk of the slowing of average (total factor) productivity growth over the decade from 1993/94 to 2003/04:

> "*Although dairy farmers achieved average growth in output of 5.3 percent a year over the decade to 2003-04, they obtained this by increasing their use of inputs, on average, by 4.4 per cent a year. As a result, the average rate of growth in total factor productivity slowed to 1.0 per cent a year*". (ABARE 2005a: 3)

That is, the measured index of the volume of total outputs divided by the index of total outputs declined as a result of changed management practices post-deregulation until 2003/04 (ABARE 2005a: 3) then levelled off in 2004/05 in response to improved terms of trade (ABARE 2006a: 3). Australian dairy producers, on average, have struggled to regain their pre-deregulation levels of efficiency, measured as total factor productivity. This decline is likely to be associated with cost and risk shifting from the retail and manufacturing sectors to producers post-deregulation, especially when trying to cope with drought conditions.

Dairy employment is certainly considerably reduced from its pre-deregulation levels. In a submission to the Minister for Agriculture, Forestry and Fisheries, the Australian Dairy Industry Council provided an "industry snapshot", which included in its points that the dairy industry "*…is an important regional employer (60,000 direct jobs at farm and manufacturing level*)"

Dairy Australia advise that these employment figures were sourced from the annual Government publication "*Food Statistics*", which is an annual publication from ABARE, produced on behalf the Federal Department of Agriculture, Fisheries and Forestry - An update

[63] Fraser and Graham used Data Envelopment Analysis (DEA) to estimate technical efficiency over a sample of 1742 Australian dairy farms. DEA use a linear programming specification to estimate a production frontier in order to measure the efficiency of an economic unit, from observed data. (Fraser & Graham 2005: 1-2)

tells us that the most current published figures are 37,450, comprising 21,550 employed in dairy cattle farming and 15,900 in dairy manufacturing (ABARE 2005c). [64]

To summarise, whilst not all dairy regions are yet in the same position, it has been established that all have been affected, some far worse than others[65]. And whilst it is true to say that there are gaps in information (such as the lack of detailed historical employment statistics within the industry for many years), some clear patterns are emerging pointing to a degree of market failure in the fresh milk industry. These patterns, it is argued, require both immediate attention and further research but it is not helpful for an arm of Government such as the NCC to conclude simply that the results are "blurred".

"The change in incomes"

"*The continuing concern with the powers and role of the supermarkets in affecting returns – especially to farmers in regions that chiefly supply domestic markets – remains a vocal issue in the industry…*" (Spencer 2004a: 66)

The issue of the relative changes in incomes for the producer, manufacturing and retailing sector for milk is central to the critique of the use of the blunt instrument of dairy market deregulation. Incomes, of course, do not give the full picture of profit margins unless we have data on the corresponding costs for the particular sector. Post deregulation, far more is known about the farm sector than either the manufacturer or the retail sector in relation to milk, and what we know about the dairy farm sector is that costs have tended to rise at a rate which exceeds that of commodity prices.[66]

The following quote is sourced from a report prepared by Whitehall Associates for the Australian Government Department of Agriculture and Forestry in the same year as Spencer's 2004 submission on behalf of the NCC:

"*As expected, with the loss of regulated arrangements, there was sharp fall in the farmgate price (*of packaged milk*). Since that time, **farmgate prices have fallen** (commensurate with a fall in world market prices for dairy products) and **average retail prices have risen**.*

*The **gap between farmgate and retail has widened** now that world market return effectively set the benchmark for prices for packaged milk processing*." (Emphasis added) (Spencer, S 2004c: 23)

The irony of the particular quote is that the author of the Whitehall Associates report is the same as the author of the NCC submission, so he appears to be disagreeing with his own earlier position, and the official and central argument of the NCC submission that the consumer being the "big" winner (See Comments under "**Consumer is the winner**" below). [67]

[64] For further discussion on employment impacts see Appendix D on social impacts of dairy deregulation

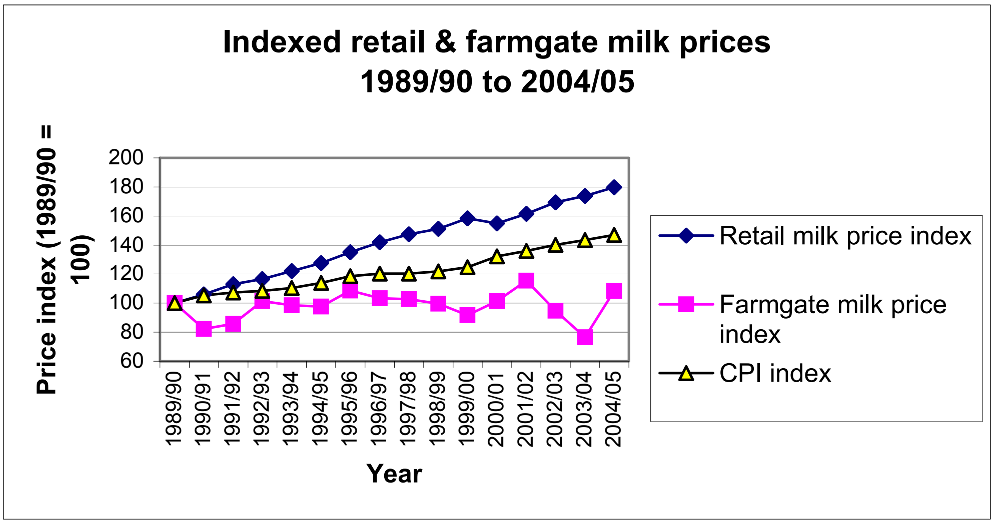
[65] And as we have seen, even Victorian farmers left the industry after farmgate deregulation in greater numbers than any other state.

[66] ABARE shows that the terms of trade, being the difference between percentage changes in prices received and prices paid for inputs continues to decline, from an average of –1.1% 1984/85 to 2003/04 to –2.3 from 1994/05 to 2003/04.(ABARE,2005 Australian Dairy 05.1, p 4)

[67] This begs the very important question as to whether this was the real finding of the RidgePartners report when it was found that the data failed to back up the assumptions or was it inserted later, in which case, whose ultimate decision within the National Competition Council was it to include or reinstate that line as a major finding?

As can be seen from Graph 12 below, after years where the retail price of milk had been rising steadily, whilst farmgate prices varied slightly with seasonal conditions [68], the drop in average retail prices following farmgate deregulation appears as a temporary phenomenon, which lasted for about as long as the ACCC were monitoring retail milk prices (until April 2001). After that, retail milk prices continued to rise at a rate exceeding CPI. The index also shows although there was a post-deregulation farmgate price increase, this situation changed in 2001/02 and farmgate prices, post deregulation display a much greater level of volatility, not surprisingly as they were more closely linked to the "international" market for milk. The graph also shows that during the time of the most recent drought impacting much of the eastern states of Australia's dairy producing regions, (from 2002) then later in Western Australia, the average farmgate price for milk dropped and then rose again just as climatic conditions in some states appeared to be easing a little!

Graph 12



Data sources: ABS, ABARE 2005d [69]

What this graph does not show is what was happening to wholesale milk prices during this period. The ACCC report that gross margins on aggregate milk sales fell by 19 percent over the period from June to December 2000, that is, despite increasing milk sales during the period immediately following deregulation, the use of lower (plain) milk retail prices to attract increased custom resulted in a overall drop in milk revenue for supermarkets during that period (ACCC 2001 p 95).

There has been considerable pressure and effort by the dairy manufacturing sector to rationalise and reduce costs in recent years and clearly, some have succeeded better than others. The NCC's *Dairy: Now and then* claims that the manufacturing sector has been impacted the most by the deregulation in the fresh milk production chain, especially since the introduction of private (supermarket) milk labels and the accompanying lower wholesale

[68] For instance an increase in farmgate prices can be seen around 1992, most likely associated with low rainfall conditions in much of eastern and northern Australia at that time.
[69] The ABS prices for milk, as of other retail items on their list represents weighted average prices for volumes, brand names and generic milk and includes specialty and flavoured milk as well as plain white milk (Perscomm Steve Whennan ABS Canberra 2006).

prices offered by the supermarkets to supply their generic labels (Spencer 2004b: 21). But the report goes on to explain that the processors:

"*…passed this loss onto farmers in the net milk prices offered…In aggregate terms in the 2003-4 year, processors are paying slightly less for milk at the farmgate, by at least the amount of the loss in wholesale number – by as much as $315m per annum…*" (Spencer 2004b: 22)

As Appendix B will show, a number of major dairy processors were taken over by overseas interests in the period following farmgate deregulation. Now that the retail sector is can potentially trade (or threaten to trade) for milk across state borders, it has opened its tendering system to national bidders and has used its generic brands and buying power to change the wholesale milk environment.

It is not sufficient for the NCC to rely on data obtained by the ACCC over such a limited monitoring period. The ACCC must be asked to go back and find out definitively what has happened since then to the relative milk margins in the farm, manufacturing and retail sectors to find out who have been the main beneficiaries of farmgate deregulation.

"Consumer is the winner"

Graph 12 (above) should also be seen in light of the statement by the ACCC after just 6 months of monitoring following dairy deregulation:

"*Supermarket chains have indicated that these lower prices will apply indefinitely*." (ACCC, 2001 p 88)

Given the rationale the majority of Australian states arguing that it was in the public interest to **keep** farmgate regulations (involving price, quotas or fresh milk market access via pooling), it makes it all the more important for the proponents of deregulation to win the argument that the milk consumer is not only better off, but the "big winner". (NCC p 6)

As we have seen above, the quote from a report prepared on behalf of the Federal Department of Agriculture, Fisheries and Forestry, by the **same** author of both the National Competition Council Report and the Dairy Moving Forward Report all published in 2004, is inconsistent with the conclusions within the NCC submission regarding price outcomes for the consumer!

The consumer did see lower milk prices immediately following farmgate deregulation but Graph 12 (above) shows that that level of aggressive milk price discounting was temporary. The use of generic brands has continued and expanded but even generic milk prices have risen to the point where the average price mix according to price statistics published by the ABS is now above its pre-deregulation levels and is climbing at a rate which exceeds CPI.

What do modern consumers want? – Is it simply lowest priced commodities or do buyers want the choice to buy local or choose products produced in more sustainable manner? The recent support for labels on Western Australian fruit and vegetables signifying whether they are local, interstate of from overseas would indicate that consumers want to support fresh local product, and local producers where possible.[70]

The debates on country of origin and GMO labelling and the growing demand for "dolphin-safe" or "GMO-free" products also indicate that not only the source of products but the mode of production is increasingly important to the Australian consumer. It therefore follows that if staple foods like milk or other dairy products were found to have been produced or procured in less sustainable fashion – such as replacing fresh locally produced milk with milk from interstate irrigated dairy feedlots and transported ever increasing distances in energy guzzling refrigerated trucks (or un-refrigerated tankers)[71], many consumers would be less than happy, whatever the price.

At the time of writing, there is already a growing long distance trade in milk as major supermarkets in Western Australia are offering shelves of UHT varieties from Victoria and New Zealand. As is already happening in the interstate fresh milk markets (such as from South Australia into Victoria and NSW, from northern NSW into southern Queensland and from northern Victoria into NSW – Source: *Dairy Now and then*, p 33), the change may also be coming for the WA fresh milk market as well as the fresh milk shortfall becomes more acute as a result of what the WA Dairy industry is describing as "*…an escalating reduction in raw milk volumes…*" stemming from farm gate prices below costs of production (Dairy WA 2005: 7).

"<u>Major changes in the industry</u>"

Dairy Now and then summarises the major industry effects of changes of farmgate deregulation in the domestic market as:

1) Encouraging greater competition in the packaged milk sector at the retail and wholesale level to create a "truly national milk supply market", which they concluded has "*…contained prices to the consumer*" (NCC p 6) (See comments on consumer outcomes above)
2) "*Enhanced the **scope** for better performance of the product category for major retailers*". (scope equalling potential, not actual performance)
3) "*Significantly reduced the income from the packaged milk category to processors and dairy farmers*". – clearly, especially for dairy farmers.
4) "*Created strong incentive for innovation in product development and marketing across the dairy cabinet by dairy companies*" This may be part of the general trend towards more healthy living and designing dairy products to meet that demand, along with the incentive of the higher prices which can be charged for such products.

[70] On the 31st of January 2006, The West Australian Newspaper published the results of Westpoll survey conducted by Patterson Market Research. 68% of respondents believed it is "very important" that fresh produce on sale in WA shops be labelled with the state of origin and further 23% believed that it is "quite important" – a total of 91%. Over 85% of respondents answered that the State Government should introduce compulsory state of origin labelling for fruit and vegetables and other fresh produce for sale in WA shops (*The West Australian* 31 January 2006: 14).

[71] See article on Dairyinfo website "*Milk tankers crossing the Nullarbor*" at **http://www.dairyinfo.biz/index.cfm?MenuID=101&NewsID=1100** - accessed 12/5/07

5) "*Created strong incentive for better processing and manufacturing efficiencies – especially in regions where there is a higher than average end-use of milk in packaged milk products*" – i.e. cost cutting and amalgamations of processing facilities.
6) "*Created greater incentive for dairy companies to manage and value their milk flow requirements according to market requirement*" – Given that the milk flow had been managed by state regulatory authorities, this obviously has fallen to dairy companies, but the extent to which they have successfully managed this may have been limited by their wholesale margins imposed on them by the supermarkets. The success of this process in the medium to long term may be judged by farm departures and fresh milk shortages.
7) "*Increased the awareness (to the farm sector) of the relative value of the milk components and attributes of milk supply*" – The irony of this somewhat unclear statement is that some dairy farmers may have taken on this attribute to the extreme, having realised that their dairy margins are so low that rather than increasing their herd sizes, they get better returns from exporting their heifers or selling their land for other purposes! (Dairy Australia, 2006:4)

At the export level, the main effect they cite is the greater exposure of dairy farmers across the nation to "*the complexity of international market conditions*" without the potential access to higher market milk prices as an alternative (Spencer 2004b: 6)

Some major summary points missed by the NCC submission at this point are the obvious ones that by 2006 the domestic milk market, having been artificially attached to a mythical international milk market by the actions of supermarkets and major processors, is now less able to effectively respond to local market supply conditions. The effects of that are a drop in total milk production, far fewer dairy farmers, a considerably "rationalised" major processing sector, employing fewer people with fewer major processors still owned and fewer controlled by Australian interests, and, along with an ever more concentrated and powerful retail sector, significantly less competitors rather than more all down the chain.

"Changes in practices"

The NCC submission acknowledges that substantial changes have taken place in the industry. They claim that these changes have moved it from a "totally production driven sector" to one which "now feels significant influence from the marketplace". (Spencer 2004b: 7) It could, however, be argued that rather than being totally production driven, the pre-deregulation situation saw statutory bodies regulating the market with an eye on both supply and demand conditions. Whilst dairy farming bodies were able to participate in that process, it is unlikely that dairy producers would agree that they were totally controlling their income and production outcomes.

It has also been argued in this paper that the situation, especially for those dairy regions producing mainly for the domestic milk market that their "markets" are domestic consumers and their supply conditions are as much a factor of climate, water and input costs as anything happening on the international market. This paper further argues that these local supply and demand signals have been largely drowned out by the use or abuse of the market power of large retail chains and large processors. If large processors or retailers are using their market buying power to keep off-season spot prices too low to cover the costs of supply, it is likely that fewer milk producers will bother keeping up their levels of production when the price of supply is high, more producers will become unviable, more will continue to leave the industry, and supply will inevitably drop.

"Theory v outcome"

This is arguably one of the most ironic parts on the NCC submission. The NCC submission quotes five predictions, mostly without ascription, leaving out all of the incorrect assumptions used by the Industry Commission to justify their push for dairy market deregulation in the first place. However, even their five chosen predictions and outcomes require further qualification.

"*Milk would flood across state borders from Victoria and attack the Sydney milk market*". Questions have been asked in both the Federal and WA State Parliaments to find out exactly what the current situation is relating to milk moving across state borders and the result shows that neither Federal nor state Agriculture ministers know what the situation is. Labels on generic branded milk are unclear in this regard, perhaps deliberately so. However, it is clear from the rapid downward pressure on market milk prices after deregulation that NSW dairy producers were affected in a similar way, whether or not Victorian milk physically travelled across state borders. We also know that there are interstate milk transfers going on already, as has been mentioned previously. What is uncertain are the actual volumes involved.

"Milk prices at the farmgate in NSW and QLD would be cut by an average 4-6 cents". Averages hide some harsh realities, especially for some in those regions within NSW of QLD holding quotas for the fresh milk market, the price drops were more like 20c per litre, similar to WA.

"*Farm exits in QLD and NSW would exceed 25% in 5 years*." This prediction was very close for NSW (24.4%) but far exceeded in Queensland (48.1%)!

"*There would be rapid consolidation of the processing sector*" This has certainly occurred, but what is significant is that the NCC paper claims that further consolidation of ownership has yet to develop – they forgot to mention corporate takeovers such as the almost total loss of WA manufacturing capacity to overseas interests!

"*The retail sector will benefit from the reduction in farmgate prices*" – They claim that the consumers have benefited, and that prices have remained "broadly at or lower than pre-deregulation levels" – considering the widespread use of averages in the NCC submission, this position is highly questionable. Certainly 2 years on from the submission, Graph 12 above shows that it is incorrect.

As has been argued previously in this paper, for a definitive answer on just who has benefited most and by how much from dairy deregulation, it is necessary for the ACCC to be asked to use their legislative powers to follow-up their previous research.

If nothing else, it can be argued that the retail sector has benefited by being able to conduct temporary milk price wars to lure extra custom to their stores, to the detriment not only of their smaller independent retail rivals but of Australian dairy processors and dairy farmers.

Given that even the NCC submission, in this section admit that most of the feared ("purported") outcomes from within the industry in terms of social cost had come true and worse, it is now useful to return to the Industry Commission's own "purported outcomes".

Revisiting the Industry Commission's assumptions

Returning to the major Industry Commission assumptions in the push for dairy deregulation as part of the development of National Competition Policy:

1) **price distorting effects of statutory marketing arrangements would be relatively small**

Response – This statement was more likely to be associated with assumptions for agricultural commodities other than milk. The IC estimated that removing statutory marketing arrangements would lead to a small boost to GDP of 0.03% but assumed that deregulation would remove what the IC termed a "30% price distortion" for market milk which would translate to a similar farmgate and retail price reduction (IC 1991a, 1991b).

It may, however, be an admission that abolishing statutory marketing arrangements in some agricultural commodities was never really expected by the Industry Commission to bring substantial benefits to consumers.

2) **domestic prices would be lower;**

Response – Immediately following dairy deregulation, retail prices of market milk in supermarkets generally dropped, especially in the newly emerging homebrands, whilst prices for flavoured and specialty milk continued to rise. The ACCC was commissioned to monitor farmgate, retail and wholesale prices and profit margins from April to December 2000, just 6 months after dairy deregulation. (ACCC, 2001: xv). Average domestic retail prices, having dropped temporarily, then began climbing again at a rate which exceeds CPI, as can be seen from Graph 12.

Graph 12 also shows that what has happened to prices at the farmgate has not been directly reflected in retail prices. That is, the assumption that dismantling state-based regulatory bodies that control the price quantity of market milk will automatically result in the reduction of retail milk prices is called into question.

It has been argued that the price of homebrand milk This issue is recognised by the ACCC and the NCC as having great significance for the public interest assessment of dairy deregulation.

3) **output for manufacturing milk would decline by 10 percent;**

Response – As Graph 13 shows, output for manufacturing milk has declined since 2001/02. Given that this drop did not begin immediately after dairy deregulation this could have been the combined result of farm departures and drought conditions in many parts of Australia (both of which mean that output which would normally be used in the manufactured product has been redirected to meet the needs of the fresh milk market). It won't be clear how much of the drop is climate related until rainfall is the major dairy regions returns to near normal levels.

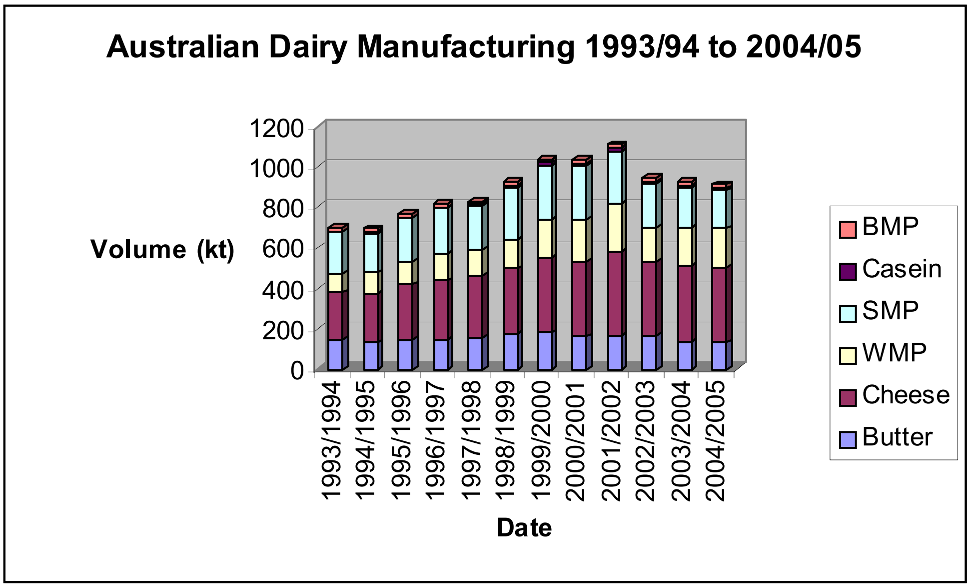
Ironically, even though the Industry Commission's assumed that output (and employment) in dairy manufacturing would decline as a direct result of dairy deregulation (dairy being one of Australia's most valuable agricultural commodity), the Hilmer Report promotes the potential of National Competition Policy for enhancing the value-adding of primary produce in Australia:

"*The continuing exemption of some agricultural marketing arrangements (...) effects efficiency, and runs counter to efforts to increase our export income through further processing of primary products in Australia*." (Hilmer et al 1993: 15)

And in its executive summary, the Hilmer report cites Prime Minister Paul Keating's promotion of "*free and open competition*" from his 1992 '*One Nation'* speech and adds:

"*…Competition is also a positive force that assists economic growth and job creation. It has triggered initiative and discovery in fields ranging from the invention of the telephone to the opening of new retail stores and small manufacturing operations. In fact, it is these developments in smaller firms, prompted by the belief in these firms in their ability to compete, that are the main source of both new jobs and value-added exports*." (Hilmer et al 1993: xv)

Graph 13



Data source: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c

4) exports of processed (dairy) foods would decline; and

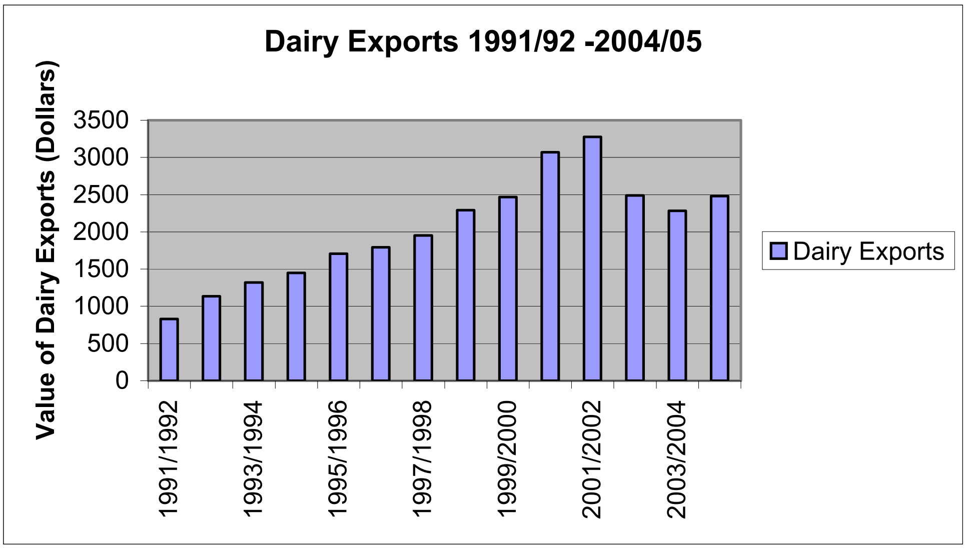
5) the dairy industry would become a marginal exporter, its exports having; being simulated to decline by around 80 percent

Response – Not surprisingly, most of Australia's dairy exports are processed rather than fresh milk products. In value, *Australian Food Statistics* report that of the $2.291 billion worth of dairy exports in the year before deregulation (1999/2000), 96.72 percent was processed dairy products and in 2004/2005, of $2.486 billion, of which processed dairy exports represented an increase to 97.75 precent of the total. (ABARE 2005c: 74)

Dairy exports as a proportion of total production expanded from 44% in the early 1990s to almost 60% in 2002/03 and back to 50% in 2004/05. (As total production has reduced in recent years, and some milk has been redirected from manufacturing/export production to market milk). (Dairy 2006: 11)

The graph below shows how the value of Australian dairy exports since 1991/1992. It shows that directly following dairy deregulation in 2000, the value of dairy exports rose, reaching a peak in 2001/02 and then dropped off following the 2001/02 season when the most recent drought began to have an impact. The most recently published export figures are similar to the dollar value of exports prior to deregulation. (1999/00 $2,467 million, 2004/2005 $2,482 million –ABARE 2005c: 71)

Graph 14

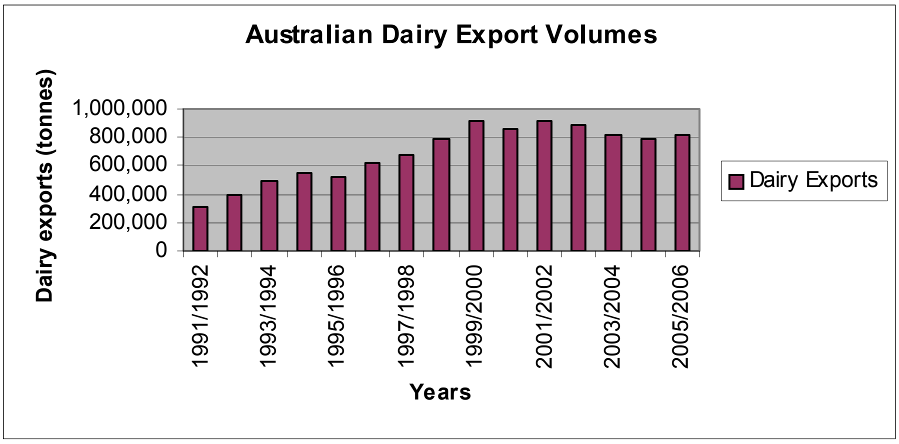


Data Sources: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c

The prediction of an 80% decline in dairy exports was clearly based on the assumption that the state based statutory marketing arrangement for market milk constituted an export subsidy. But Victoria is by far the largest milk producing state in Australia and in 1999/2000 Victoria produced 6,870 out of a total of 10,847 million litres- over 63% (Dairy Australia 2003b: 9), of which only 440 million litres was sold as drinking milk - 6.4% (Ibid: 17). It was also the state whose market milk price prior to deregulation were the lowest in Australia (Spencer, 2004b: 20). Victorian dairy producers, on average, thus gained the least from market milk premiums whilst exporting the most.

The Graph below provides a picture of dairy export **volumes** over a similar period, which indicates a plateau in export volumes coinciding with dairy deregulation, i.e. a flattening out, rather than the predicted massive drop in dairy export volumes following deregulation. Dairy export volumes are reported to have risen to 911,494 tonnes in 1999/2000 (reaching a peak of 917,392 in 2001/2002) and dropped around ten percent from its pre-deregulation levels to 820,075 tonnes in 2005/2006.

Graph 15



Data Sources: Australian Dairy Corporation, 1999- 2002, Dairy Australia 2003-2006

This outcome is significant as the IC prediction of an 80% decline in dairy exports was clearly linked to the dual assumptions that deregulation would bring about a drop in farmgate prices for manufactured milk and that the State based statutory marketing arrangements for market milk constituted a substantial export subsidy. Other domestic or international trading conditions may well have affected the export volumes but it would have required an extraordinarily *positive* set of market circumstances to negate a prediction of such a large export loss. That prediction of a massive decline in exports appears to ignore the fact that the dairy regions likely to have been least impacted by a post-deregulation drop in market milk farmgate prices are those generally with highest percentage of exports.

6) **a decline in (…) employment is predicted of around 10 percent for manufacturing milk**

Response - The latest available figures do show a drop in employment in dairy processing in Australia. Australia Foods Statistics show dairy manufacturing employment just prior to deregulation at 17,000, peaking in 2002/03 at 19,050 and then dropping to 15,900 in 2004/05. This represents a drop of 6.5% from pre-deregulation employment levels and a drop of 16.5% from its 2003/04 peak. (ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c)

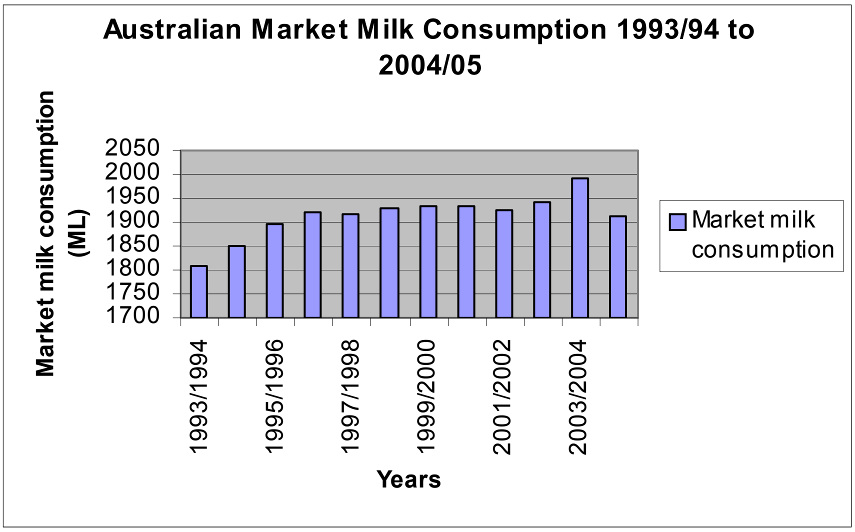
There is insufficient data so far to determine what will happen to manufacturing employment after the drought.

7) **consumption of market milk would rise leading to a slight expansion in output and employment in that sector**

Response – Demand for milk is relatively inelastic, to the extent that consumption of market milk, which had been steadily growing with population in the years leading up to deregulation, levelled out in 1999-2001 rising in 2003/2004 before dropping again in

2004/2005, as can be seen from Graph 4 of total Australian market milk consumption from 1993/94 to 2004/05. A sudden drop off in fresh milk consumption is more likely to be related to the availability of fresh milk (and promotion of its alternatives such as long-life options or soy) than a direct response to price.

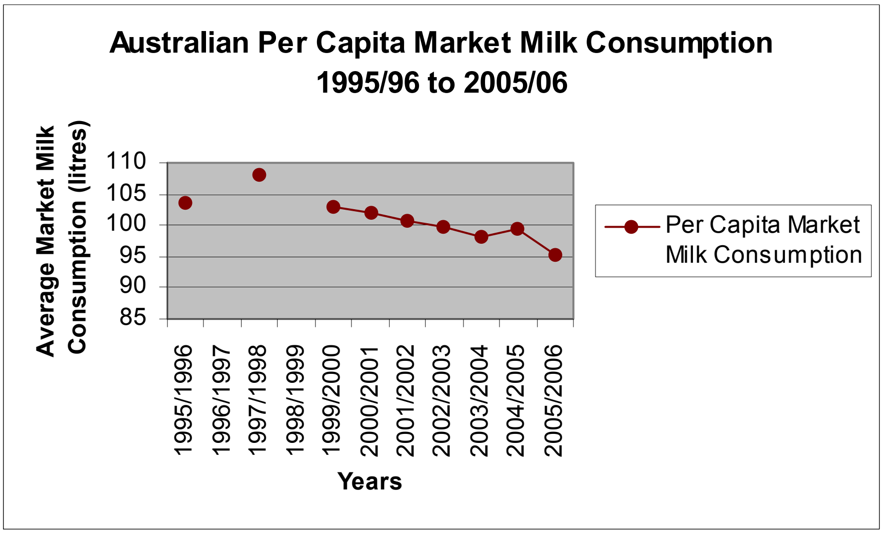
Graph 16



Data Source: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c

Graph 17 below, however, indicates that per capita milk consumption has been trending down in the years following deregulation.

Graph 17



Data Sources: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c, ABS
Note: No data available for milk consumption 1996/97 and 1998/99

In dollar terms, *Australian Food Statistics 2005* reports that average weekly household expenditure on dairy products rose slightly from \$10.50 in 1998/99 to \$11.26 in 2003/04 but for combined fresh milk and cream over that same time period dropped from \$5.89 to \$5.64. As the consumption of milk had remained relatively steady, despite a brief increase in

2003/04, this would indicate that consumption of cream has dropped since deregulation. (ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c)

There are no specific employment figures available for market milk but dairy farm employment has dropped at a much greater rate than dairy manufacturing. Dairy farm employment is reported to have dropped from 33,736 in 1999/2000 to 21,550 in 2004/2005 – a drop of over 36%. This does not count indirect regional employment losses.

Entire federal elections have been lost over potential direct job losses in the native woodchipping industry of far less than this.

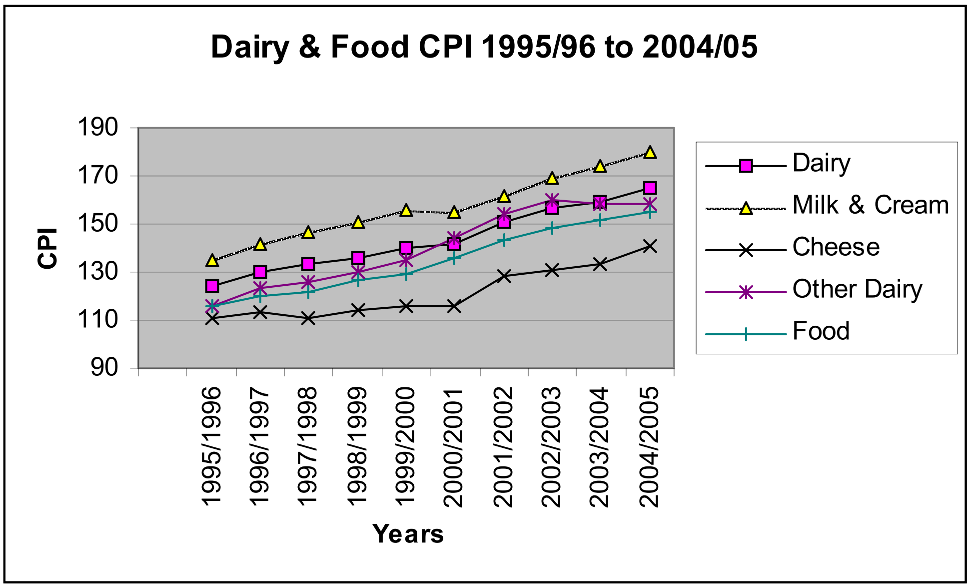
8) **The farm gate price of manufactured milk would decline between 5 and 9 percent, or 2 to 3 cents per litre;**

Response - On average, the farmgate price for manufactured milk rose after deregulation, but the actual amount varies from region to region, as has been seen from Chart 1 above.

9) **prices of manufactured dairy products would fall by around 12 percent as market support payments are reduced;**

Response: There is no evidence of any sustained fall in the prices of manufactured dairy products post deregulation. In fact, as can be seen from Graph 18 below, the prices for processed dairy foods such as cheese that had been rising at a rate less than CPI prior to deregulation, stabilised, then rose 12 percentage points from 2000/01 to 2001/02. (ABARE 2005c: 66)

Graph 18



Data sources: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c

10) **the farm gate price of market milk would decline by more than one third, or around 12 to 15 cents per litre;**

Response: - As can be seen from Chart 1 above, this prediction would appear to be an underestimate. In some cases, the farmgate price fall for market milk was over 25c per litre – a drop of over 40%.

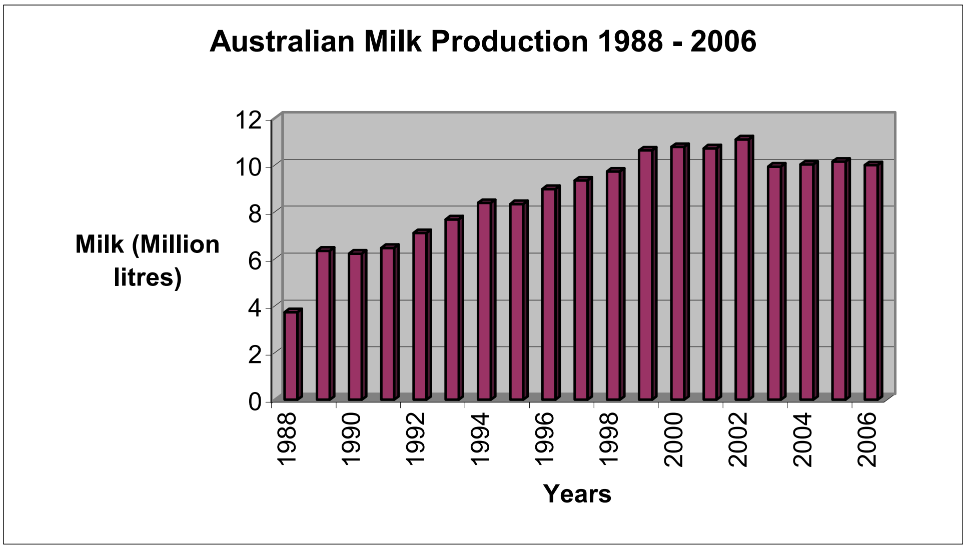
11) the reduction of the farm gate price would allow a similar reduction in the retail price of fresh milk;

Response: As we have seen above, the fact that the blunt instrument of deregulation "allows" a retail price reduction is no guarantee that it will happen, (or continue). There was a temporary drop in average milk prices up until the ACCC ceased monitoring dairy wholesale margins.

12) total milk output would likely contract by around 5 percent

Response: As can be seen from Graph 19 below, total milk production steadied after deregulation, peaked in 2002 and dropped again from 2003. Production in 2006 is around 10 % lower than 2003 levels and over 6% below pre-deregulation levels. Farm departures appear to have halted the levels of pre-deregulation production growth, but the recent drop in production may also be related to drought.

Graph 19



Source: ABARE 2001a, 2001b, 2002, 2003b, 2005b, 2005c

13) Australia would remain a net exporter of dairy products.

Response: This prediction is true so far, and, as we have seen, as Australia was already internationally competitive prior to deregulation, this prediction is likely to continue as long as we retain a dairy industry in Australia.

The IC's original dairy industry assumptions and modelling were generally open-ended and lacked qualification but this paper is not claiming that all of the post-deregulation experience of the dairy industry can be attributed to NCP.[72] ABARE identify the combined effects of deregulation, drought, reduced water allocations and fluctuating world market prices as causing major restructuring in both dairy production and manufacturing since 2000 (ABARE 2005a: 1). It is argued, however, that deregulation has made domestic market milk producers much more vulnerable to conditions which formerly would only have affected the dairy export sector, such as a rising dollar, and less able to survive domestic market conditions such as drought.

IC assumptions, such as the loss of most of Australia's dairy exports and the benefits for domestic dairy consumers once the premium prices for market milk were abolished, have yet to be proven. Such assumptions, especially relating to consumer outcomes, appear to have given little regard to the impact of the changes to the market bargaining powers of the production, corporate retail or manufacturing sectors once the statutory marketing arrangements were removed or the retail sector's potential to take more profits from the dairy sector at the expense of the dairy manufacturing, dairy production sectors and of dairy consumers in a post-regulatory environment.

"Future challenges for the industry"

The NCC submission admits that there remain a range of unsolved problems or "future challenges". They include in such "challenges" the ability (or inability) to recover from drought. As droughts have become a more common feature of the Australian agricultural landscape (along with observed increased frequency and severity of low values in the Southern Oscillation Index), the inability for large numbers of farmers to recover from drought must be considered to be part of the deregulation problem, a situation made worse by farmgate deregulation, not a mitigating argument or justification.

There was discussion of the slow adjustment in those regions which have been hit hardest by the substantial drop in the prices of market milk. It might more truly be said that for many dairy producers in these regions, the "slow" adjustments may be a euphemism for slow death, if they have been left in an unsustainable position. If that is the case, just who and how does the blunt instrument of deregulation respond?

The NCC submission predicts further farm losses and production losses, "*threatening volumes of milk used in dairy product manufacture*" – why do they not recognise and mention the threat to the volumes of fresh milk available especially in states like Western Australia?

Along with this rather limited discussion of future challenges can be added the challenge of continuing increases to fuel prices as the world demand outstrips new sources of supply and the climate-related changes to the availability and price of water for irrigation.

There is also the potential for overseas takeover of the already very powerful supermarket chains, with potential buyers attracted to the potential to squeeze even greater margins from

[72] Some would say that Australia's free-trade agreements, especially with New Zealand, made the removal of state-based statutory marketing arrangements inevitable but the 1992 submission to the Hilmer Inquiry by the Australian Dairy Industry Council, which included the United Dairy Farmers of Victoria, opposed dairy deregulation on public interest grounds (ADIC 1992). Pressure from the powerful export-based Victorian dairy cooperatives to deregulate coincided with the phasing out of market support for domestically consumed manufacturing milk and the scrutiny put on the States via NCP after 1995. (Spencer et al 2007: 8).

their supply chains, to the further detriment of local suppliers and any remaining local food manufacturing capacity

Any future debate on resource efficiency within the Australia dairy industry should include a full assessment of the energy use efficiency (especially in light of the increased or potentially increased transportation of fresh milk within and between states), water use efficiency, landcare, including water table implications, salinity and other such issues associated with environmental debt, not just a narrow financial bottom line to producers, processors or retailers.

In 2005 the Western Australian Department of Agriculture, estimated that the cost of transporting market milk from South Australia to Western Australia would be 18.6 cents per litre by tanker or 56.4 cents per litre packaged. With recent increases in petrol prices and the potential future prices as demand for world petroleum continues to outstrip new discoveries, this would appear to be a considerable underestimate (Dairy Western Australia 2005: 7/8).

Another major future assessment of resource efficiency or inefficiency must take into consideration that states like Western Australia currently have a much smaller proportion of their dairy production under irrigation (in 2006, only 9% of WA was under irrigated feedlots) as opposed to 28% in Central South Australia and as much as 72% in Northern Victoria and Riverina! (Dairy Australia 2006: 82). Any serious discussion of Australia's water future must consider how the current marketing arrangements of Australia's milk production are affecting our water use efficiency. Most dairy farmers in the Murray Darling system already have water allocations, so if water trading rights have increased the price of water for irrigation, it will mostly affect these producers by providing them with a water trading option.

"Where further work may be required".

"*There is little data available from within the industry and wider government resources to measure important flow-on effects of the change in the industry over the past 5 years since the inevitability of removal of regulation became apparent*" (Spencer 2004b: 8)

Having said just 3 pages earlier that the paper had been "…*prepared to assess the longer term outcomes from the deregulation on the dairy industry, including on employment, productivity and efficiency*" this section of the NCC paper is an admission that they did not do what they said they were going to do, especially when it comes to the awkward issues of industry social costs.

Studies on dairy industry employment have been thin on the ground. However, a number of published Government sources do give figures for dairy farm and dairy manufacturing employment for the general period covered in *Dairy: Now and then*. Given that the author of the NCC report produced papers for at least one of the Departments which has published such data since 1990, it is hard to see why this employment data was not cited. As we have seen, the 2004/5 industry snapshot compared to 1999 shows a marked drop in combined dairy farm and dairy manufacturing employment levels over that period.

There is also information available from ABARE's annual dairy industry reports on total factor productivity for dairy farming, but these figures were not cited in the NCC paper. As has been mentioned, these figures show that in recent years, annual average total factor productivity has dropped. It will be necessary to see the post drought figures show to get the full picture.

Dairy W.A.'s Application to the ACCC

This paper has discussed the loss of bargaining power of dairy farmers as a result of both the farmgate deregulation process and the increased buying power of the major supermarket chains through increased market share. In 2001, the Australian Dairy Farmers Federation Ltd (ADFF) lodged a request for authorisation in relation to collective negotiation by dairy farmers of contractual terms and conditions with dairy processing companies.

The ACCC granted authorisation for the parties to engage in collective negotiation subject to 11 conditions on 12 March 2002 expiring on 1 July 2005. The matter was appealed at the Tribunal by National Foods and was finalised on 16 August 2002 with one other condition added.[73] The Australian Competition Tribunal issued a determination which replaced the Commission's previous determination. (Australian Competition Tribunal 2002)

In the lead-up to the expiry date of the original authorisation, a number of applications were made to the ACCC for new collective bargaining approvals. In January 2005, the Western Australian dairy industry, through Dairy WA, applied to the ACCC to ask if WA dairy farmers could appoint Dairy WA to act on their behalf in negotiations for supply of raw for contract with National Foods, PB Foods, Challenge Dairy, Harvey Fresh, and other Australian or international dairy processors or retail suppliers of milk in Australia.

The application requested that Dairy WA be able to make and enter contracts directly with processors or retailers on behalf of WA Dairy farmers who have appointed Dairy WA as their negotiating agents. The difficulty for Western Australian dairy producers is that that the numbers and concentrations of dairy producers are much smaller than for states like Victoria. Given their low or negative profitability, it would be difficult, if not impossible for producers to fund local negotiating bodies and the condition limiting negotiating bodies to include only producers "*…within a distance in which milk can economically be delivered to that processor's plant.* This condition is open to interpretation and is arguably relative to the size of the dairy regions themselves but if strictly administered would make post-deregulation collective bargaining virtually impossible in Western Australia.[74]

Their initial application included a request for WA dairy farmers who had appointed Dairy WA as their negotiating agent to be able to collectively boycott any processor or retailer who attempted to contract without consent with WA dairy farmers who are using Dairy WA as their contracting agent. This part of the application was later withdrawn. In her evidence to the ACCC, Dairy WA representative, Nola Marino, explained that it was an ACCC official who strongly advised them to include such a provision in their application. (Dairy Western Australia 2005: 7/8)

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[73] The final 12 conditions included the fact that the Australian Dairy Farmers Federation were not permitted to be involved in any price and supply negotiations between dairy farmers and dairy processors, and that all farmers involved in collective bargaining groups have similar supply patters (i.e. seasonal or year round supply) and all be located "*…within a distance in which milk can economically be delivered to that processor's plant*". (Australasian Legal Information Institute 2007)

[74] One means of improve collective bargaining opportunities could be for many more Western Australian dairy producers to join an existing co-operative, but there appears to be a reluctance by WA Dairy producers to take that step at present.

The application also included the provision of the ability for those WA Dairy Farmers who had appointed Dairy WA as their agent to refuse to supply processors where there is no current contract in place or where there the price offered to the producers that have not been agreed by Dairy WA. (That is, if the processor seeks to undermine contracted terms and price).

Normal market conditions would be such that the willingness of farmers to supply the market diminishes as the offered farmgate price is reduced. This paper argues that changes to the milk marketing arrangements, the application was one of the few means available to WA dairy farmers to make sure that market signals could be effectively sent and received, to avoid longer term supply problems if the producers were being treated unreasonably or unfairly by the supermarkets and big buying groups, like National Foods.

The response from the ACCC was to refuse the application, on the basis that the "…*potential public benefits likely to arise from the proposed agency (to enable collective bargaining) would be unlikely to outweigh the potential anti-competitive effects likely to be generated by the arrangements*" (ACCC Letter 20 February 2006). There are parallels here to one-way enforceable industrial relations contracts.

There were approvals for some limited negotiation power for some eastern states co-operatives but, as mentioned, they each were required to meet a range of conditions applying to those negotiating powers. As mentioned, the Western Australian dairy sector is far smaller than most of its eastern states counterparts and the producers far more geographically dispersed. Each sub-region is not resourced to be able to support its own negotiating body.
It could also be argued that there may be a public interest case for revisiting the rejection of the ability of dairy producers to collectively bargain and, if necessary, to refuse to supply milk if the price offered is unreasonable. From a dairy producer's point of view, this may mean that no matter what is offered by processors and corporate retailers, their only choices are to supply at that rate (even if that rate fails to cover their costs) or get out of the business. It should be investigated as to whether the level of departures (and shortfall in milk supply in some regions) has been made worse by the inability, even under strictly controlled circumstances, to withhold supply if the offer is unfair or unsustainable, especially in times of higher costs, such as drought.

In light of all of the above arguments presented in this paper about the mistakes in official predictions, about the social costs and the necessity for official bodies such as the ACCC to be required to go back and reassess the margins within the industry, it is argued that the ACCC should reconsider their position in such cases.

Conclusions

Having looked in some detail at a number of the main publications by Government bodies leading up to and following Australia-wide dairy farmgate deregulation, we should now return to the original questions to which this paper has been seeking answers:

Who are the main beneficiaries of NCP- driven deregulation of the Australian Dairy industry?

This paper was not able to obtain a definitive answer to this question is by way of access to retail and wholesale costs and margins data which is generally impossible to obtain in the absence of the kinds of legislative powers available to the ACCC under the *Prices Surveillance Act 1983.* However, the information available on trends in retail prices and farmgate prices clearly reinforce the conclusion that dairy farmers have not been the beneficiaries and refute the arguments by the Industry Commission and the National Competition Council that the main winners are Australian milk consumers.

It is clear that major retailers have gained sufficient market control of the retail milk market that they can, where required, discount generic brand milk as a loss leader to increase general custom. It is also clear that after the dust of deregulation cleared and the subsequent changes in ownership of a number of dairy processors, the most successful of the remaining owners of the processing sector have been those who have found ways to amalgamate and otherwise reduce their overhead and production costs. So whilst it is expected that the main financial beneficiaries of dairy deregulation will turn out to be the corporate retail sector, extra work is recommended to find out what has happened to these margins since 2000.

It is also clear from states like Western Australia that other countries, most especially producers other from Australia's main export competition, New Zealand, now have much greater influence on Australia's farmgate outcomes than prior to deregulation. And whilst it is also not clear exactly what the situation would have been if this form of farmgate deregulation had not taken place, it should not be assumed that such major policy changes should be blindly accepted on an all or nothing basis, because NCP-driven deregulation is a very blunt instrument.

Some sectors, and some individuals within sectors, have benefited, some have been relatively unscathed but for some others the outcomes have been devastating. If the states, in effect, had been pushed into this kind of major policy direction, and a number of their public interest assessments overridden, more than a decade later, efforts should made to openly assess the actual outcomes, sector by sector, especially for communities, small business and regional Australia. These assessments should be made independent of proponents of NCP such as the Productivity Commission.

Has dairy market deregulation resulted in a more efficient resource use in the Australian dairy industry?

It is useful to remember here that the whole push for the removal of all state based farmgate milk market regulation was justified by the assumption that state-based farmgate milk market regulatory arrangements had held back efficiency improvements in dairy production. However, these assumptions are not supported by the available facts. Both Dairy Australia and ABARE data show that Australia milk production levels and production efficiencies had been steadily improving for some years leading up to nationwide farmgate deregulation.

The paper argued that Australian dairy producers at the time of deregulation were some of the most cost-efficient dairy producers in the world, second only to our major export competitor, New Zealand. It is however, quite likely that on a regional basis, efficiency and viability issues have impacted on the decisions of many producers to leave the industry, post deregulation, including producers in states such as Victoria.

However, data from ABARE indicates that in recent years, dairy total factor productivity growth has fallen. This is made worse by drought and the decline in the terms of trade for dairy production and the outlook for future input costs, including those associated with the water and fuel.

In particular, farmgate deregulation has affected the industry's ability (or inability) to survive the likelihood of more frequent and severe climatic events such as drought, floods and damaging storms associated with climate change and we see a strong case emerging for a reassessment of the whole "efficiency" debate relating to the Australian dairy industry.

What are the outcomes for Australian dairy consumers?

It is true that farmgate deregulation has enabled the development and widespread use of the generic milk brands by major supermarket chains, so in that sense there has been some consumer choice. But, following the brief post-deregulation period of milk price wars which damaged Australian-owned milk manufacturing capacity, and taking all milk products into consideration over time, average milk prices in Australia continue to climb at a rate which exceeds CPI, whilst farmgate prices have fluctuated but generally remained low.
So, the most currently available date on price does not support the claim that the consumer has been the main winner from farmgate deregulation.

Of growing concern is the recent drop in production, which may lead to a shortage in market milk, a greater use of (costly and environmentally unsustainable) long distance transport of fresh milk or a greater reliance on UHT varieties, against consumers' preferences.

Is there more or less competition in the Australian dairy market after NCP – based deregulation?

Lower farmgate prices do not, of themselves, prove more or better competition if the cause is the abuse of market power.

There are demonstrably fewer dairy producers now than in 2000 and in states like Western Australia, in the absence of any total industry approach, this situation could be about to get far worse. In the past in states like Western Australia, those leaving the industry, or planning to leave the industry could sell their stock to other dairy producers. Dairy Australia report that local market is such that many are now choosing to go into cattle farming or leave the industry altogether and heifer sales overseas are now becoming more common to the detriment of local herd development.

Despite the proliferation of tiny "boutique" dairies targeting speciality markets or the tourist trade, the vast majority of production is still directed to a small number of major processors, albeit with some changes in ownership. There has been considerable consolidation in the dairy processing sector, with the closure of many regional processing facilities and the takeover of a number of Australian manufacturing facilities. Some dairy cooperatives, like Bonlac have already been taken over by overseas interests, whilst others remain in Australian ownership and control but Dairy Australia reports that others, like Dairy Farmers, at this time, in the process of changing their structure to a more corporate form (which may make them more of an overseas takeover target in the future). Deregulation meant dairy farmers lost their place on the negotiating table with statutory authorities to negotiate prices and production levels, at the same time as both the manufacturing and retail sectors were becoming far more concentrated. It is argued that only the continued existence of some strong surviving cooperatives have stopped the farmgate outcomes from being totally disconnected to local producers costs and conditions.

On the retail level, there is no question that the sector is more concentrated than ever before, and it is argued that the oligopsonistic power that this provides has been to the detriment of Australian dairy producers who, it appears, don't even get left with a "take it or leave it" option as it is now virtually impossible for dairy farmers to collectively refuse to supply those offering poor or unsustainable prices. Apart from Victoria, the proportion of Australian milk collected by traditional cooperative structures is falling (Spencer, S et al, 2007: 51) and as strong co-operatives appear to be necessary to retain a reasonably healthy bottom line in farmgate prices, their future loss in the face of increased retail dominance is likely to be significant.

By the time both Federal and State Governments publicly recognise and acknowledge the signs of market failure, it may well be too late to easily rebuild capacity and repair the damage such reduced "competition" has wreaked to some sectors of our economy and community.

Was the basis for policy making in this area sound and if not, what remedies should be sought?

This paper has shown that the predictions of the Industry Commission and the subsequent Hilmer Report which lead to Australia-wide dairy farmgate deregulation were mostly based on untested, inaccurate or misleading assumptions.

Given this, along with the fact that the majority of states submitted public interest arguments to retain some their statutory marketing arrangements, there is a clear indication that the National Competition Council process of assessing and making recommendations to the Federal Treasurer on the basis of these public interest cases was flawed.

At least one State Minister for Agriculture is on record as stating that if market failure could be proven, he may be prepared to take action of some sort. This is a positive sign but change also needs to take place on a national basis. Unfortunately, this paper (and the author's previous thesis) concludes that the way COAG has operated so far in relation to NCP leaves much to be desired as busy Premiers and Chief Ministers generally are briefed by enthusiasts (Senior COAG Officials, who have a stake in retaining their current power base). The push for change must therefore come from a much broader base and this requires a much greater level of public understanding.[75]

States should not have to face punishment by the Federal Government for taking action to correct such mistakes, or even legal action by the body which has taken many of the functions of the NCC, the COAG Reform Council (or the ACCC) for doing so if those very bodies have not looked carefully enough at the actual outcomes to admit that they themselves may have been wrong in their actions and decisions.

The Australian dairy industry is not the only Australian industry or community sector to have been impacted severely by the enforcement of National Competition Policy "principles" but it

[75] This process is explained further in Margetts, *National Competition Policy and the Theft of Democracy*, 2003

provides a strong case for revisiting the whole process of the National Competition Policy legislative review and many of the associated enforced changes in order to properly question the public interest justification for past and ongoing actions and the future direction of both the COAG Reform Council and the ACCC. There is also a strong case for questioning those parts of Government pushing for further competition policy related outcomes which may see not only more destruction of primary industry and regional communities but further damage to community services and Australia's remaining manufacturing capacity.

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APPENDICES

Appendix A

Water as a resource in the in the dairy industry

Agriculture is the major water consumer in Australia, accounting, in 2000-01 for 67% of Australia's total water consumption. (ABS 2006c: vi) Dairy Moving Forward reports that the dairy industry is "significantly dependent on irrigated water" and is, in fact the largest rural user of water (Spencer, 2004a: 88). ABARE's published irrigation water use per dairy cow against average yield per cow, indicate that the average irrigation water use per litre of milk between 2001/02 to 2003/04 ranged from just over 200 litres to over 500 litres, depending on the year's conditions and the type of calving pattern. It should be remembered that these averages include both irrigated and non-irrigated dairy production, so water use in irrigated dairy regions would be substantially higher. (ABARE 2005a: 5)

A 2001 Dairying for Tomorrow survey found that 57% dairy farmers irrigate their pasture and crops. (Mostly for farms with larger herds) and that farms with more than 20% of their land under irrigation represent 43% of national production. The amounts of water used in irrigated dairy farming would be considerably higher than the averages cited above.

Dairy 2004: Situation & Outlook, shows that dairy represents approximately 40% of Australia's total rural water use – the next largest user in 2004 was cotton at approximately 15% (Spencer 2004a: 88). Based on the ABS figures for total rural irrigation water use in that year, that would amount to over 4,000 gigalitres. (ABS 2006c: 4) Dairy 2006: Situation & Outlook reports that the dairy industry accounts for 25% of the total surface irrigation water use in Australia. (Dairy Australia 2006: 61)

Dairy Australia report that nationally in 2006, 52% of milk production came from farms with irrigation (compared to 59% in 2005). They also report that in 2006, 36% of milk production came from farms with more than 20% of their land irrigated, compared to 38% in 2005 and 43% in 2004). This is insufficient data to identify a trend independent of drought conditions, but enough to indicate that more research is required in this area.

Percentage of dairy farms with > 20% under irrigation in 2004, by region

Table 4

Region	2004
Far North Qld	25%
SE Qld	40%
Central & S NSW	55%
N Victoria & Riverina	90%
Gippsland	30%
W Victoria & SE S Australia	13%
Central & N S Australia	22%
Tasmania	60%
WA	15%
Total	43%

Source: : Dairy Australia 2006: 66-83

Percentage of dairy farms irrigated, by region 2006

Table 5

Region	Farms Irrigated	Percentage of dairy land irrigated
Far North Qld	17%	13%
Northern NSW & S Qld	26%	15%
Central & Southern NSW	39%	22%
N Victoria & Riverina	95%	72%
Gippsland	N/a	3%
W Victoria & SE S Australia	N/a	4%
Central South Australia	48%	28%
Tasmania	64%	30%
WA	N/a	9%
Nationally		23%

Source: Dairy Australia 2006: 66-83

Clearly from these tables, the Northern Victorian dairy region is by far the most intensive water user in the industry. The significance Victoria's dairy water use is further discussed in the case study below.

As can be seen from the tables above, with the exception of dairy producing regions such as Western Victoria and Western Australia, the Australian dairy industry is very dependent on irrigation – and the cost per unit volume is increasing as water becomes more scarce and water trading is applied in more regions. However, Dairy Moving Forward report from their farmer survey that within the industry there is a relatively low level of recognition of future challenges associated with water, however they do report that issues associated with water cost, availability and climate risk rated highly in the northern Victorian irrigated dairy region, mainly because of price and market reasons. (Spencer 2004a: 90)

They also report that generally, there is little data available on more efficient water use in the industry and add that…"*Published pilot studies of efficiency programs have shown low rates of improvement, and best practice studies show that the returns per megalitre in top 10% would increase the returns per megalitre to double that…* (of current returns). (Spencer, 2004a: 88) i.e. there is considerable potential for water efficiency improvement in the dairy industry.

"*The risk for the industry in total is that whilst there is an apparent "holding pattern" preventing forward movement for many producers until a price horizon becomes more positive, progress in enhancing water use efficiency will remain a low priority*" (Ibid: 90)

In some areas, the potential for water trading is seen as part of an exit strategy, along with land sales for other uses, including residential land and the sale of stock.

However, the use-it or lose-it approach adopted by some states relating to National Competition Policy water reforms may prevent some dairy farmers from taking action yet to use less than their current allocations. Or, given the apparent lack of general water efficiency pressure within the industry, producers may be waiting to see what happens with their own futures and/or until the trading price for water is so high that it is worthwhile for them to sell their water entitlements (and get out of dairy production).

It could be argued that if statutory authorities still had a level of control over Australia's dairy production, access to dairy quotas could be linked to world's best practise in water use efficiency (as dairy market deregulation per se does not appear to have lead to more efficient water use).

Dairy 2006 reports that Australian Dairy Farmers and Dairy Australia are working with CSIRO to develop an irrigation policy blueprint for the dairy industry. (Dairy Australia 2006: 61) At the very least, the blunt instrument of the water market would seem to require considerable further investigation in relation to dairy water use efficiency.

The Victorian example

As has been mentioned, the dairy industry is far the largest user of rural irrigation water in this country and Victoria is by far the largest dairy producing state.

The Victorian Parliamentary Inquiry into the allocation of water resources reports that the average precipitation in the form of rain or snow in Victoria is 150 gigalitres. Of that water, approximately 1% (1.5 gigs) reaches the groundwater, discharging around 15% (22.5 gigs) as stream flow. That makes a total of approximately 24 gigalitres (Environment and Natural Resources Committee 2001: 7).

The significance of this figure is that in 2000/01 the annual consumptive water use in Victoria was reported as 5,788 gigs, with a further 814 gigs diverted to NSW from the Snowy River through the Murray River system. (Ibid: 38).

Information sourced from the Victorian Department of Water Resources indicates that 77% of Victoria's consumptive surface water use goes to irrigation and approximately 70% of Victoria's consumptive groundwater use goes to irrigation. . (Ibid: 38-39).

In relation to landcare they also report that:

"*Salinity and water logging affect much of the irrigated land in Victoria, as well as in other parts of Australia. It is an issue of particular concern in the Murray-Darling Basin*" (Ibid: 14)

They further report from the Victorian Auditor General's report of 2001, that 74% of Victoria's irrigated land is at risk of salinity and that the costs of salinity are estimated at $68 million per year (Ibid: 15).

They cite figures from the Victorian Department of Natural Resources and Environment that the annual farmgate value of irrigated production was $1.5 billion, of which $1,206 was from the Goulburn-Murray water district, and of that, 46 percent came from dairying. (Ibid: 52) In 1999, the Senate Rural and Regional Affairs and Transport References Committee reported that the irrigated northern Victorian dairy region produced 40% of the state's milk output while the mainly rain fed pastures of western and eastern Victoria accounted for about 30% each (SRRATRC 1999: 14)

This means that the biggest portion of the dairy income from Victoria is produced with water which does not fall as rain in Victoria and improvements in the water use efficiency of the Victorian irrigated dairy production has potential benefits for other states and the river ecosystems which support them.

Appendix B

Changes to Australian dairy processing ownership and control

A number of reports have made mention of the challenges which have faced the Australian dairy processing sector in recent years. The ACCC explains the weakened post deregulation market power of Australian dairy processors against the major supermarket chains:

"*…the concentration in the supermarket sector combined with the excess capacity within the dairy processing sector and the importance of supermarket contracts to processor turnover imposes demand conditions on the processor sector which limit their capacity to influence pricing outcomes.*

"As milk is essentially a homogenous product and milk labels are only weakly differentiated, retailers can switch demand to a different processor without risking a consumer backlash. Milk processors would appear to have limited capacity to protect sales of branded milk from aggressive price discounting of supermarket generic labelled milk. Consequently processor bargaining power and therefore ability to influence price is weak. The aggressive tendering by processors for supermarket contract flowing deregulation showed the competition within the industry as processors sought to build market share and reduce excess processing capacity in the deregulated market. Also by tendering for generic milk contracts, supermarkets are provided with knowledge of processor cost structures and the associated value of proprietary brands. This information is likely to be useful to supermarkets in contract negotiations." (ACCC 2001: 42)

This market pressure from retailers has forced dairy processors to find ways to reduce their operating costs. The uneven loss of Australian dairy farm numbers has presented some challenges to dairy processors:

"*In northern fresh milk regions supply and demand curves are converging, and processors face the prospect of severe shortfalls in local supplies*." (Dairy Australia 2006: 5)

But more particularly, the fact that dairy processors generally have far greater market power than individual dairy farmers, means that they can use price incentives and market buying power to "encourage" seasonal milk producers to flatten their production curves to help reduce unused processing capacity.[76] The other implication of these combined pressures is the closing down of those regional processing facilities which are less profi6

A number of official reports have recognised this and cited, that alongside the loss in dairy farm numbers, the Australian dairy industry is undergoing a process of amalgamation or "rationalization" of dairy processors in Australia in recent years, especially since deregulation. (Refs: ACCC 2001 p 45 etc) [77] Few, however, make mention of the fact that

[76] This may make the processors more cost "efficient", but it shifts costs to dairy farms and reduces dairy farm efficiency, as flattened production curves require extra feed and water in the off-season.

[77] Ironically, the section of Dairy Australia's website "**Who makes what**" lists 354 dairy companies in Australia in 2006. Some of these are traders rather than processors but it would appear that the increased number is largely due to a proliferation of micro-processors of specialty and/or tourism related value-added dairy products springing up. This seems to happening especially within those dairy regions like Western Australia which are primarily fresh milk producing regions and have been hit hardest by farmgate price reduction – see Appendix C which outlines the History of Western Australian Dairy Processors)

along with "consolidation" of manufacturing and processing capacity and mergers, we are seeing a growing number of major Australian dairy processing companies falling to overseas ownership and control.

This paper argues that the aggressive milk tendering process for supermarket share following deregulation weakened the financial position of a number of dairy processors, making them much more vulnerable to overseas takeover bids.

In their 2000 report on the impact of farmgate deregulation, the ACCC listed Australia's 15 major milk processors (of a total of 53 milk receival companies) which received over 97% of Australia's total milk production (Source ACCC, 2001, p 38) were listed along with their percentage of their milk intake for the 1999-2000. The table below lists those companies and indicates their ownership prior to farmgate deregulation and ownership in 2006:

Table 6

Changes to Major Dairy Processor Ownership 1999-2000 to 2006

Company	% Milk intake 1999-2000	Ownership in 2000	Ownership in 2006
Murray Goulburn[78]	29	Co-operative	Co-operative
Bonlac Foods	21.4	Co-operative	Fonterra (NZ)
Dairy Farmers Group	13.4	Co-operative	"hybrid" Co-operative
Nestle Australia	5.8	Nestle Int'l (Switzerland)	Nestle Int'l (Switzerland)
National Dairies	5.4	Australian Public Company	San Miguel (Philippines)
Warrrnambool Cheese & Butter	4.8	Co-operative	Listed Company
Tatura Milk Industries	3.9	Co-operative	Co-operative
Parmalat Australia	3.9	Parmalat (Italy)	Parmalat (Italy)
Kraft Foods Ltd	2.7	Kraft (USA)	Kraft (USA)
Norco Co-operative	1.7	Co-operative	Co-operative
Bega Co-operative	1.6	Co-operative	Co-operative*
Peters & Brownes Foods Ltd	1.5	Australian **	Fonterra (NZ)
Lactos	0.9	Bongrain (France)	National Foods/San Miguel (Philippines)
Capel (Wesmilk)	0.6	Wesmilk (WA)	Challenge Dairy (WA)
Cadbury Schweppes	0.6	US/ International	US/ International

Source: Company list and market share – ACCC 2001, 2006 Ownership – Company websites.
* Bega has retained its ownership as an Australian-owned cooperative, but has developed a close commercial relationship with Fonterra.
** PB Foods was a company rather than a cooperative business structure

[78] It should be noted that MG's share of milk intake rose to 35% (at Bonlac's expense) by 2006 (UTS Business Centre 2007), which indicates the possible benefits of retaining a strong cooperative structure.

Of greater concern is that Dairy Farmers, is changing from a co-operative structure into a "hybrid" structure "…*as a transitionary step towards a further ownership restructure*…". Dairy Australia suggest three reasons behind the pressure to change from co-operative to other business structures:

1) the capital requirements of manufacturing and marketing operations;
2) the financial pressure on farmers to "unlock" investments in co-operatives; and
3) the background farmgate market (and emerging fresh milk shortage) which sees some non-co-operative processors offering incentives to gain access to new suppliers (including members of dairy co-operatives).

(Dairy Australia 2006: 38)

Considering that Warrnambool Cheese and Butter has become a listed company and if Dairy Farmers becomes a publicly listed company, (as two of the remaining strong dairy co-operatives), they could also be lost to overseas ownership and control in the not too distant future. This is particularly significant in the light of the clear and arguably naïve assumption within the Hilmer report that removing agricultural marketing arrangements would increase **Australian** export income via the further processing of our raw products:

"*The continuing exemption of some agricultural marketing arrangements also affects efficiency and runs counter to efforts to increase our export income through further processing of primary products in Australia*."

As can be seen in Appendix C, some states, like Western Australia, have already lost most of their dairy processing sector to overseas interests since deregulation.

Australia's general manufacturing capacity has been considerably depleted in recent decades (give figures). Losing ownership and control of our existing value-adding capacity makes us much more vulnerable as an economy and much more dependant again on services and mining.

The loss of any more remaining strong dairy co-operatives is also significant because it is acknowledged that the co-operatives are a way of addressing the weak bargaining power of dairy farmers, setting benchmark farmgate prices, which private companies are challenged to match (ACCC 2001: 33). As a greater percentage of our processing sector is controlled by overseas and particularly New Zealand interests, it is argued that it is far easier for local market signals to be ignored. We are likely to experience serious major market failures, as the combination of corporate retail oligopsonies and our main trading rivals interests overshadow the interests of the producers and the Australian consumer.

Appendix C

Western Australian Dairy Processors – Historical Summary

In April 2001, the ACCC reported that there were 53 milk receival companies in Australia, collecting an estimated 10,846 million litres of milk from dairy farms in the 1999/2000 year. The top 15 companies accounted for over 97% of the total milk intake, with many of the remaining dairy companies operating in specialty cheese markets. (ACCC "*Impact of farmgate deregulation on the Australian milk industry: study of prices, costs and profits*." April 2001)

Which were the major milk brands of the mid 20th Century in Western Australia? **Brownes** and **Masters**. Major dairy brands **Peters** Icecream, **Watsonia** butter and cheese and **Kraft** cheese. (**Kraft** is a subsidiary of **Kraft Foods, USA**).

The following is a brief historical summary of the major changes to the dairy processing industry in WA starting at the end of the 19th Century:

Brownes - Edward Browne, an Irish farm boy came to Western Australia in 1886, soon establishing a dairy farm in Perth. In the wake of the gold rush, business expanded rapidly and in 1915, Browne bought up a farmers' dairy co-operative, renaming the business **Brownes Dairy**. **Brownes Dairy** bought milk from farmers, cooled it in brine and sold it to milk retailers. (Source: www1.pbfoods.com.au/history.asp 5/7/06)

By the 1920s, as a result of a population increase fuelled by returned servicemen and immigrants, Edward Browne expanded his business into the South West and by 1926 had built a new milk depot at Brunswick. He died shortly after the depot came into operation. The depot and the Perth dairy were taken over by his sons, Robert and Walter, and the next year consolidated the dairy and depot into a new company – **Brownes Limited**. (Source: www1.pbfoods.com.au/history.asp 5/7/06)

Watsonia - Watson's Luncheon Rooms opened in Fremantle in 1895, soon expanding to 11 outlets in the Perth metropolitan area. As part of the development of his smallgoods operation, in the Depression, William Watson purchased a product known as "farm butter" and with special processing equipment produced "Table Quality" butter. By the end of WWII, **Watsons** supplied much of the entire meat and dairy needs to Singapore until Europe recovered. (Source: georgewestonfoods.com.au 30/6/06)

Masters – In 1926 **Westralian Farmers Co-operative** (**Wesfarmers**) took over the operations of **Dairy Farmers Co-op Co**. (Modern milk processing began after Wesfarmers introduced pasteurisation under the brand "Pascomi")

Peters - 1927 E L Neville, from the **Western Ice Company** (Perth) travelled to Sydney to negotiate a deal to market ice cream produced by **F A B Peters**, an American who had been building up an ice cream business in Sydney since 1910. (Source: www1.pbfoods.com.au/history.asp 5/7/06)

1928 **Peter's Western Ice Cream** launched in WA. It was so successful that it was decided to manufacture ice cream in Western Australia.

1929 the **Peters American Delicacy Company (WA)** was incorporated, acquiring all of the shares and assets of the **Western Ice Company**. F A B Peters became the first Chairman and E L Neville the first Managing Director.

The US stock market crash and the associated Depression meant that ice cream production was carried out at the **Western Ice** factory and it was not until 1937 that a new 2 storey ice cream factory was completed next to the ice factory.

After WWII, **Wesfarmers** bought out several dairies in the metropolitan area including the Hollywood dairy run by the **Masters** family and **Dreyers** dairy in Claremont. **Wesfarmers** centralised their operations in Claremont and installed new machinery. They then began trading as **Masters Dairy Pty Ltd**. (Source: Sunday Times 1963 p 74)

1948 the **Peters American Delicacy Company (WA)** changed its name to **Peters Ice Cream (WA)**.

1949 **Peters and Brownes** joined together as partners in the Brunswick milk depot, a move initiated by **Peters** to ensure a steady supply of condensed milk for ice cream. (Source: www1.pbfoods.com.au/history.asp 5/7/06)

1962 **Peters** bought **Brownes Dairy Limited**. Changes included the expansion of their SW creamery.

George Weston Foods (Australia) formed in 1949 and began acquiring Australian food interests. In 1965 George Westons acquired **Watson Foods** in WA. (**George Weston Foods** is a wholly owned subsidiary of **Associated British Foods Plc**, one of the world's leading food companies. (Source: georgewestonfoods.com.au 30/6/06)

1966 **Fonti Farm Cheese** pioneered a range of mainly Italian style cheeses in Perth.
(Source: margaretriverdairy.com)

1981 **Peters**, now trading as **Peters (WA) Ltd** increased its ice cream market share by taking over rival company, **Pauls**.

1983 **Pura HiLo** launched as **Masters HiLo** (Source: pura.com.au 29/6/06)

1986 **Harvey Fresh** established in Harvey

1990 **Fonti Farm Cheese** relocated to Margaret River.

1991 **Pura Dairy** (based in Victoria) combined with other food related brands to form **National Foods** Limited. (Source: pura.com.au 29/6/06)

1993/1994 **National Foods** acquired **Masters Dairy** from **Wesfarmers**.

1994 Owners of **Fonti Farm** acquired **The Margaret River Cheese Company**, merging their operations (Source: margaretriverdairy.com)

Feb 2000, **The Margaret River Cheese Company** purchased by NSW based **Manassen Foods** and formed **The Margaret River Dairy Company**

At 2000, **Capel Dairies (Wesmilk**) had 80 local producers

DAIRY MARKET DEREGULATION

In August 2000, **Kiwi Co-operative Dairies Ltd** acquired a 54% stakeholding in **PB Foods Ltd (Peters and Brownes**)

In December 2000, The Agwest Trade and Development Report on the Dairy Industry Working Group spoke of WA's 3 main processors, **National Foods Ltd** (including the **Masters** and **Pura** brands), **PB Foods** (**Peters and Brownes**,) and **George Weston Foods**. (**Watsonia** etc). They state that WA had more minor processors than other states, the largest of which they identify as **Harvey Fresh**, with 3% of the packaged liquid milk market and under utilised modern UHT processing facilities to handle additional milk.

In 2001, the ACCC also reported that the major milk producers in Western Australia were **National Foods** with the bulk of the additional fresh milk produced through **Peters/Brownes** (**PB Foods)** although at that time **Capel (Wesmilk**) was also reported as one of the country's 15 major dairy producers (albeit on the bottom of the list at 0.6 % of the nation's production)

In mid 2001, **George Weston Foods (GWF)** sold its **Capel Dairy** business to **Challenge Dairy Co-operative Ltd**, whilst maintaining ownership of **Capel River, Mt Barker** and **Watsonia** dairy brands. GWF maintained a supply arrangement with **Challenge Dairy Co-op** for butter and cheese products

Kiwi Co-operative Dairies (owned by more than 12,000 NZ dairy farmers) and its subsidiaries (including **PB Foods Ltd**) forms **Fonterra** in October 2001.

(**National Foods** acquired by **San Miguel Corporation** based in the Philippines, 2003/4)

Therefore, it would appear three years post deregulation, by far the majority of Western Australian milk was being processed by companies owned and controlled by overseas interests, with the exception of **Harvey Fresh**, **Challenge Dairy Co-operative** and a number of specialty dairy producers and tiny boutique dairies.

WA producers as at 2006 – Source: Dairy Australia website 'Who makes what"

Alphabetical 29 dairy companies, 4 of which are goat milk dairies and 2 sheep milk dairy processors.

Agri-Best Australia Pty Ltd

Suite 9/ 8 Clive Street West Perth, WA 6005
Ph: 08 9226 3833 Fax: 08 9226 3988
Web address: www.agri-best.com
Products: butter and milk powders
Company links to Netherlands, USA, Australia and China

Azzura Gelati

7 Zeta Crescent O'Connor WA 6163
Ph: 08 9314 1656
Products: Gelati

Borello Cheese

59 Rice Road Oakford WA 6121
PH: 08 9525 1232 Fax: 08 9256 2449
Products: Italian style cheeses

Brownes Dairy Pty Ltd

Part of PB Foods Ltd

Web address : www.pbfoods.com.au
Email address: pbflinfo@pbfoods.com.au

Company Info – PB Foods now owned by Fonterra

Cambray Sheep Cheese Factory

RMB 470 Vasse Hwy, Nannup WA 6275
Ph: 08 9756 2037
Web Address: www.cambraycottages.com
Email address: cambray@westnet.com.au

Casa Dairy Products Pty Ltd

1/27 Carrington Street, Nedlands WA 6009
Ph: 08 9386 6196, fax: 08 9389 1347
Web address: www.casadairy.com.au
Email Address: sales@casadairy.com.au
Products: cottage cheese, feta, labneh, yoghurt, mascapone, quark, ricotta

Centra Fine Foods

6 Granite Place, Welshpool WA 6101
Ph: 08 9350 6766
We Address: www.centrafinefoods.com.au
Email address: info@centrafinefoods.com.au

Challenge Dairy Co-operative Ltd

60 Roe Road Capel WA 6271
Ph 08 9727 0000 Fax: 08 9727 2634
Web address : www.challengedairy.com.au

Products: Australian, Capel River, Challenge, Capel

Company info- Challenge purchased Capel Dairies (Wesmilk) from George Weston Foods in mid 2001. Has supply agreements with George Weston Foods and joint supply arrangements with other major Australian dairy co-operatives such as Tatura, Murray-Goulburn etc.

Chrystal & Co Pty Ltd

10 Bell Street, Canning Vale WA 6155
Products: Cheeses, Including cheddar, edam, feta and gouda.

Cloverdene Farm

RMB 200A Karridale WA 6288
Ph: 08 9758 5579 Fax: 08 9758 5333
Web address: www.cloverdene.com.au
Email address: cloverdene@bigpond.com
Products: Yogurt (cow's milk), feta and other sheep's milk cheese

Coffee Holdings Pty Ltd

48 Barbery Way, Bibra Lake WA 6163
Ph: 08 9418 7000 Fax:
Products: specialty butters e.g. garlic, chilli, herb etc

Fonti Foods

27 Howe St Osborne Park WA 6017
Ph: 08 9446 3666 Fax: 9446 7171
Products: Yogurts- various, Feta varieties, cottage cheese, Ricotta, baked Ricotta

Company info: Connected to Manassen Foods Australia Pty Ltd, based in NSW

Harvey Fresh Dairies

Third Ave Harvey WA 6220
Ph: 08 9729 2199 Fax: 08 9729 2298
Web address: www.harveyfresh.com.au
Email address: info@harveyfresh.com.au
Products: milk, flavoured, specialty, low fats, UHT, lactose free etc.
Custard, yogurt- various varieties, cream

Company info: Still family owned, based in WA

Heritage Country Cheese

Balingup-Nannup Road, Balingup WA 6253
Ph: 08 7641 1016 Fax: 08 9417 7230
Web address: www.heritagecc.iinet.net.au
Email address: heritagecc@iinet.com.au

Products: Cheeses- Cheddar, Edam, Feta varieties, Gouda

Jalong Goat Dairy

Lot 19 Bailup Road, Gidgegannup WA 6083
Ph: 08 9574 7169 Fax: 08 9574 7017
Products: goat milk yogurt

Kervella Cheese

52 Clenton Road, Gidgegannup WA 6083
Ph: 08 9574 7160 Fax: 08 9574 7160
Products: Affine (a goat's cheese) fresh goat curd

Kytren Fine Quality Goat Cheese

McKnoe Drive, Morangup WA 6083
Ph: 9574 7147
Products: Goats milk, curd and cheese varieties

Masters Dairy

Owned and controlled by **National Foods**
Products: market milk, flavoured milk, icecream, cheddar, cream

Company info: **National Foods** also own **Pura Milk** which is understood to produce its fresh market milk in WA.

Moondyne Goat Dairy

19 Bailup Road, Gidgegannup WA 6083
Ph: 08 9572 9257
Products: Plain goats yogurt and goats milk

Mundella Dairy

46 Randell Road, Mundijong WA 6123
Ph: 08 9525 5754 Fax: 08 9525 5764
Web address: www.mundellafoods.com.au
Products: Yogurt – multiple varieties, feta varieties, cream cheese, custard, ricotta

Company info- medium size family business

Normandie Foods

15 Drake Street, Osborne Park WA 6017
Ph: 9242 3511
Products: cream cheese

Organic Harvest

No address given
Ph: 08 9729 3949 Fax: 9729 3999
Products: Feta, organic milk

Rose Valley Cheese Factory

2 Wungong Road, Armadale WA 6112
Ph: 08 9399 2238 Fax: 08 9497 2760
Products: No product details given

Sanav (Aust) Pty Ltd

69 Dalkeith Road, Nedlands WA 6009
Ph: 08 6389 1602 Fax: 08 6389 1603
No product details given

Serpentine Cheese Products

Lot 500 Hall Road, Serpentine WA 6205
Products: Ricotta cheese

Swan Valley Cheese Company

640 Great Northern Hwy, Herne Hill WA 6056
Ph: 08 9256 0600 Fax: 08 9296 0699
Products: Bocconcini, feta, mozzarella, ricotta, stracchino-crescenza

The Margaret River Dairy Company

Lot 2535 Bussell Hwy, Cowaramup WA 6284
Ph: 08 9755 7588 Fax: 08 9755 7582
Web address: www.margaretriverdairy.com.au
Products: Yogurt 11 varieties, brie, feta 11 varieties, havarti, butter, camembert, cheddar 10 varieties, cream cheese 6 varieties, ricotta 4 varieties

Company info: Originally **Fonti Farm Cheese**, which relocated to Margaret River, acquired and merged operations with **The Margaret River Cheese Company** and were acquired themselves by **Manassen Foods Australia** (Australian owned, NSW based) in 2000.

The Old Cheddar Cheese Company

Lot 2 Yalyalup Busselton Road, Busselton WA 6280
Ph: 08 9751 1264 Fax: 08 9751 1524
Products: 6 varieties of cheddar

Watsons Foods (WA)

174 Hamilton Road, Spearwood WA 6163
Ph: 08 9418 0777 Fax 08 9418 5836
Brands: Capel Valley, Mount Barker, Watsonia
Products: Cheddar, Colby, butter, butter blends,

Company info – Fremantle origin, purchased by British based food company **George Weston Foods** in 1965.

Appendix D

Summary of social costs and benefits of dairy market deregulation

This may be more a list of what we need to know than what is currently publicly available.

1- Changes to farmgate prices

2- Changes to dairy farm incomes

3- Loss of family farm businesses

4- Changes to levels of unemployment in dairy regions

5- Pressures on land and water resources

6- Loss of local dairy processors to overseas interests

7- Changes to the demographics in Australian dairy

8- Personal costs

9- Positives – e.g. proliferation of new micro dairies etc in states like Western Australia

1) Changes to farmgate prices

As we saw from Graph 10 above, average dairy farmgate prices have not kept pace with inflation, and are losing ground in relation to the rising average retail price for milk. We also saw from Table 2 (Farmgate milk prices changes 2000-2004) that the impact of farmgate prices is uneven across Australia depending on the proportion of market milk that was being produced in each region.

On average, it is reported that manufactured milk prices have increased, meaning that Victorian dairy farmers, on average would be the major beneficiaries of any manufactured milk price rises given their high percentage of manufactured milk whereas dairy regions like the South West of Western Australia have experienced the most dramatic drops as their production had been largely market milk.

2) Changes to dairy farm incomes and profits

Graph A of ABARE's December 2005 publication on behalf of dairy Australia, "*Australian Dairy 05.1*" shows that dairy farm profits rose briefly and sharply, on average for a period around the year 2000 and then dived even further into negative territory (to an average negative profit of $40,000 per year (ABARE 2005a: 1) before returning to a zero profit level for 2004. The impacts on profitability of attaching market milk to an "international" milk price would not have been uniform, as it depended on the percentage of market milk produced in each region. What appears clear, however, is that deregulation has introduced a much greater level of profit volatility in the Australian dairy industry.

One reason for the increased profit volatility is that the price for market milk is no longer to be negotiated according to the domestic demand or supply conditions. The prices negotiated by the former State and Territory milk regulatory authorities would have been able to adjust to overproduction in good seasons, or to drought and other low production events – a means of evening out milk producer's revenue streams to some extent.

ABARE's Graph B from the same report also show that the terms of trade in the Australian dairy industry, which had been declining steadily from the early 1990s to 2000, rose briefly then dropped sharply following deregulation, as input costs became more disconnected to farmgate prices. (ABARE 2005a: 2)

3) Loss of family farm businesses

The loss of dairy farms over the past 2 decades indicates that there were issues of sustainability prior to deregulation however, graph E from Australian Dairy 05.1 shows that there had been a period of relative stability from the late 1980s until 2000. ABS figures on dairy farm numbers show the loss in dairy farm numbers has accelerated from 2000, the year of nationwide farmgate deregulation. (See Graph 1 above)

Graph B in ABARE's 2003 Australian Dairy Industry "*Productivity and Product"* Report (ABARE 2003a: 2) shows that Australian dairy farm numbers have been declining for decades, but also shows that farm numbers had steadied in the decade immediately preceding farmgate deregulation. Their 2005 report, however, tends to skip over the impacts of farmgate deregulation by referring to the average loss in dairy farms over 20 years:

"*The number of dairy farms in Australia has declined by over half in the past two decades to around 9600 farms registered in 2003-04*." (ABARE 2005a: 3).

As Graph 1 (above) has shown, there was a sharp dive in dairy farm numbers after 1999. ABS figures show that from 2000 to 2005 Australia lost around 3939 dairy farm businesses (average 28.5% reduction). The levels of post-deregulation farm losses varied across Australia; from 2000 to 2005 WA lost 90 dairy farms (23.3%), Victoria lost 1934 farms (23.8%), NSW 475 (24.4%), Tasmania lost 190 (25.6%), SA lost 361 (46.9%) and Queensland lost 886 (48.1%).

4) Changes to levels of employment/unemployment in dairy regions

The Australian Government Rural Industries Research and Development Corporation published a report in 2004, "*Social Profile of Australian Dairy regions*"(Herreria, Magpantay & Aslin 2004: vii) which shows that declines in levels of employment in the dairy industry have occurred in all dairy regions since 1996. Declines were highest in Western Dairy (from 19.4% to 14.6%), DIDCO (from 18.8% to 14.8%), Sub Tropical Dairy (from 14% to 11.4%) and DairyTas (from 29.5% to 27.1%) and smallest in GippsDairy, WestVic Dairy, and Murray Dairy (down around 1% respectively. (Herreria, Magpantay & Aslin 2004: vii).

In April 1999, the Australian Dairy Industry Council, in their submission to the Federal Minister for Agriculture, regarding proposed dairy market deregulation, provided an industry snapshot, which included the point that the Australian dairy industry was an important regional employer (60,000 direct jobs at farm and manufacturing level). (SRRATRC 1999: 4)

Six years later, the direct employment figure has been reduced to 37,450, (a reduction of around 38%) consisting of 21,550 in dairy cattle farming and 15,900 in dairy processing. (ABARE 2005c: 48 & 55)

Details on dairy employment have been difficult to obtain. On ABARE's interactive data website (Agsurf), it is possible to obtain a time series from 1990 to 2004 of average expenditure per dairy farm on **paid** labour (as opposed to risk/profit sharing between family members or business partners). The amounts involved are not large but they are tending to increase. With the general demise of the family dairy farm for larger establishments and at the same time an increase in tiny tourist oriented value-adding dairy establishments this trend is not surprising). It is also possible that the increased pressure on seasonal producers to produce all-year round may impact on this trend.

4) **Extra pressure on dairy farm land and water resources (due to loss of bargaining power of farm sector)**

A survey carried out on behalf of Dairy Australia in February and March 2006 showed that in the largely non-irrigated dairy regions of Western Australia, as few as 29% of dairy farmers were feeling positive about their future (Dairy Australia 2006: 45). Dairy Australia also report that in the 12 months before 2006, 42% of Western Australian dairy farmers sold heifers on the export market, compared to a national average of 12% (Dairy Australia 2006: 44). This would indicate that a number of these farmers are planning to leave the market.

"*…National milk production has not grown. The key limiting factor has been the number of cows milked. Farmers have generally considered their businesses, and focussed on improving their financial position rather than producing more milk.*

"*Demand for water, cows, heifers and land are providing people with more options for entry or exit from the market.* (Dairy Australia 2006: 4)

Some departing dairy farmers in states like Western Australia, may be selling, or considering selling their farms for other farming purposes, or for totally different uses, such as residential development. As more farmers leave and production capacity decreases, this means that the remaining dairy properties are under greater production pressure. Where there is a growing shortage of market milk, there is likely to be a greater use of UHT or milk powder coming in from other states, which are more likely to be produced from irrigation.

As was discussed in Appendix A, in some other regions, dairy irrigators have been waiting for water trading to be fully implemented in their states before exiting the industry. Under a "use-it-or-lose-it" quota system, widespread voluntary reductions in water use is unlikely to be achieved until trading of excess water is available. However, during drought years, across Australia, overall water used for dairy irrigation has dropped because there has been less to use.[79] In April 2007, Prime Minister, John Howard, announced that irrigation water will be cut off if there was no significant rainfall by mid July. (ABC 2007) One impact of the reduced river flows is the likely increased use of groundwater, which impacts further on river flows.

[79] See Appendix A

7) Loss of local dairy processors to overseas interests.

The issue of ownership and control of dairy processing is particularly significant in relation to the impacts on farmgate milk prices. Dairy Australia acknowledges that dairy farmer owned cooperatives have tended to play an important role in the establishment of farmgate prices:

"*The traditional cooperative model plays a critical role in generally setting the farmgate value of milk in the Australian industry"* (Dairy Australia 2006: 39)

They also acknowledge that the market share of collected by such cooperatives has been "reduced in recent years (dropping from 55% in 2002 to 41% in 2005 (Dairy Australia 2006: 39)

As can be seen from Appendices B and C, the situation of ownership and control of dairy processing facilities has undergone considerable change since deregulation, especially in relation to growing number of processors which have been bought up by overseas interests.

In a state like Western Australia, without a strong cooperative structure, the prices paid by the large corporate milk producers, such as Fonterra, is still influenced to some extent by the prices paid by smaller cooperatives such as Challenge. That is, in order for smaller producers to obtain the required returns compete in the deregulated market environment against the market buying and selling power of the larger corporate producers, the small cooperative producers have kept their farmgate prices lower, and that has left the big players with the ability to keep their prices just a little higher than the only other option;

"*A commitment to a higher milk price by Fonterra in 2006/07 will influence prices paid by other companies, however ongoing returns will be influenced by the achievements of Challenge*." (Dairy Australia 2006: 51)

This situation has, no doubt, contributed to the level of negativity of Western Australian dairy producers.

Appendix E

Climate Change and the Southern Oscillation Index (SOI)

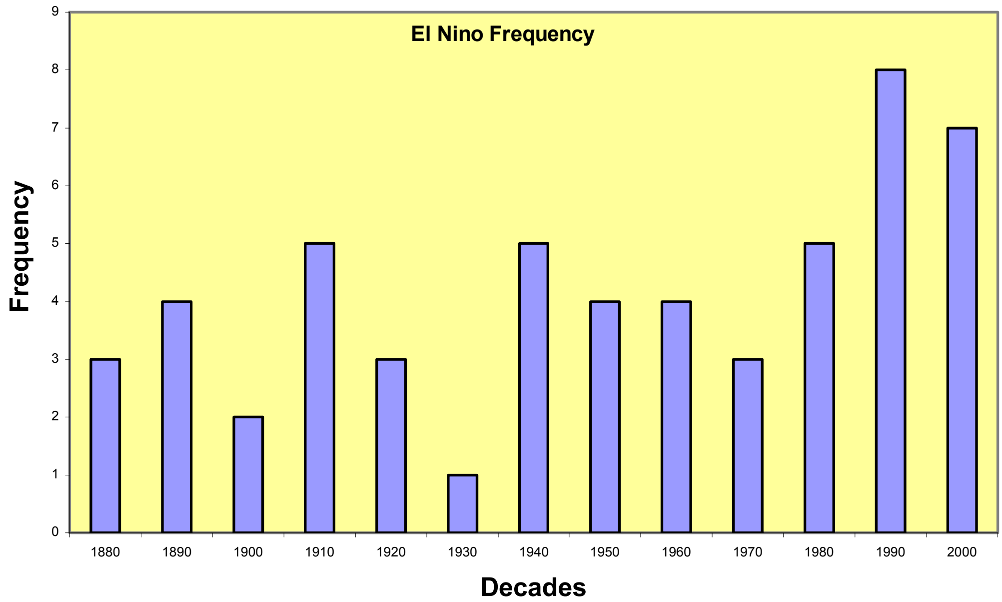
Drought has had a significant impact on Australian agricultural production over our history since European settlement. The following information from the Australian Bureau of Meteorology (BoM) traces not only Australia's drought history but points to the likelihood that such events will become more frequent and more severe with climate change.

The causes of climate fluctuations in Australia in recent decades are described as being:

"...connected with the climate phenomenon called the Southern Oscillation, a major air pressure shift between the Asian and east Pacific regions whose best known extremes are El Nino events." (BoM 2006c: 1)

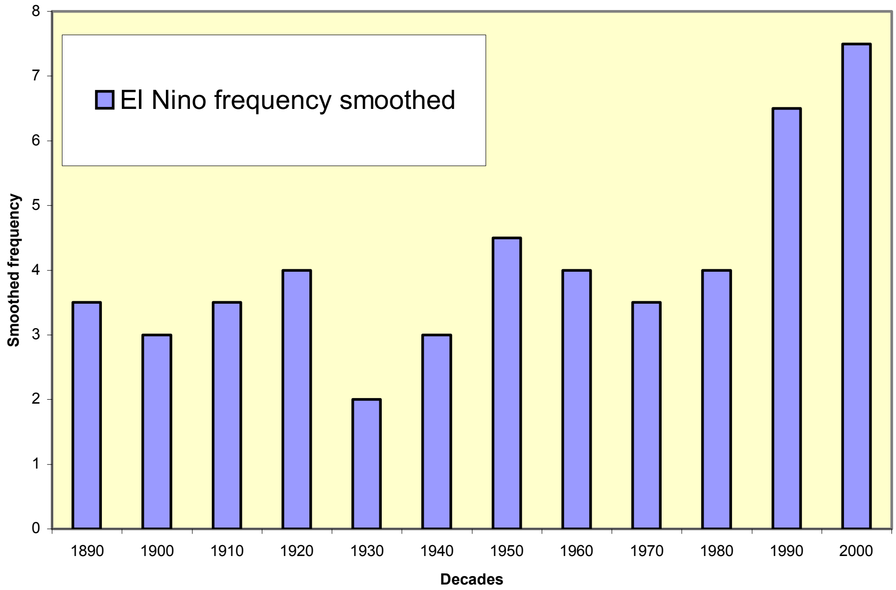
"*…During El Nino episodes (...) seas around Australia cool, and slackened trade winds feed less moisture into the Australian/Asian region. There is then a high probability that eastern and northern Australia will be drier than normal*." (BoM 2006c: 4)

The graph below illustrates the frequency of El Nino events in Australia since 1880.



Data source: Australian Government Bureau of Meteorology 2006b

The graph below represents a smoothed frequency (calculated by averaging each decade of El Nino frequencies with the next). These graphs of SOI over more than a century, would appear to indicate that the destructive weather events such as drought and damaging storms associated with El Nino are likely to become more frequent.



Data Source: Australian Government Bureau of Meteorology 2006b

The significance of this scientific data for the dairy industry is that the supply conditions are likely to continue to be difficult, affecting the costs of production.

Any pricing/marketing system which fails to take these impacts into account, in relation to the domestic milk supply is likely to experience growing supply shortages, especially of fresh market milk.

About the author

Born in Fremantle in 1955, Dee Margetts left full time study at UWA in 1974 to commence work as Qantas ground staff, continuing at UWA part-time before leaving Australia in 1979 to undertake further studies in England. Dee was awarded an Honours Degree in Development Studies from the University of East Anglia in 1982, returned to Australia and completed a Diploma of Education from UWA in 1983. After working as a high school teacher and as state Coordinator for People for Nuclear Disarmament, Dee commenced work towards a Masters of Philosophy in Economics at Murdoch University until her election to the Federal Senate in 1993 where she served for 6 years.

As the Greens parliamentary spokesperson in a wide range of areas, including economics, Dee witnessed the Federal Government positioning Australia prior to the signing of the Uruguay Round of GATT and then the introduction of National Competition Policy, nearing the end of the Keating Government's term in office. After the election of the Coalition Government in 1996, Dee lobbied for two years for the Senate to set up a select committee to investigate the socio-economic impacts of National Competition Policy, a committee on which she served until the end of her Senate term in mid 1999.

Soon after leaving Federal Parliament, Dee began research for a Masters of Philosophy in Political Economy, successfully completing her thesis entitled "Competition Policy, State Agreement Acts and the Public Interest" at Murdoch University in 2001, the year she was elected to the WA Legislative Council as a Member for the Agricultural Region.

As a WA Parliamentarian, Dee worked with many community and business sectors concerned about the impacts of forced reforms under National Competition Policy. Dee witnessed the way regional WA struggled to cope with many aspects of National Competition Policy and the manner in which States like WA responded to threats of the loss of Competition Policy payments for non-compliance with National Competition Council rulings. Dee finished her WA Parliamentary term in mid 2005 and is currently undertaking research for a PhD on the outcomes of National Competition Policy at UWA as part of the new Australian Global Studies Research Centre.