ADF response to *The Dairy Industry Crisis - the Case for Government Intervention* (the Dahlsen report)

21 May 2020

FINDING / RECOMMENDATION (Extracted from report)	RESPONSE (Support, Support in part or Do not support)	COMMENT (Justification for response)
FINDINGS		
PRODUCTION & CONSUMPTION		
85% of Australian milk production comes from Victoria.	Do not support	Victoria's share of milk production was 63.4% in 2018/19 (Dairy Australia *InFocus*). It is much lower for drinking milk.
It is acknowledged that the small drop in the per capita consumption of milk has been caused by soy, almond, oat, rice and other alternate options	Support in part	Per capita consumption of dairy milk has decreased slightly, could be due to alternatives, but also changing consumer preferences (soft drinks instead of milkshakes with burgers etc). Majority of households that buy plant-based milks also buy dairy milks, which supports the suggestion that they are substitutable.
It is clear what China would do (if Mengniu acquires Lion), starve Australians.	Do not support	This is far from clear either as an intention, or in terms of capability to follow through ('would' vs 'would try to'). Mengniu already has a presence in the Australian milk processing sector via Burra Foods and has yet to attempt to starve anyone. Lion Dairy and Drinks arguably does not have a dominant position in any region and farmers/consumers have other options. Chinese-owned dairy investments are often touted with a focus on exporting produce to China, however this is usually far more complex than they envisage, and these firms often settle into a mix of domestic/export business. In addition, Lion Dairy and Drinks is a business with very limited export exposure at present and produces very few products suitable for export.
PRICE		
The price of milk has fallen since deregulation but other dairy products like butter, cheese and yoghurt has increased considerably.	Support in part	Between 2000-2010 milk CPI was roughly in line with Food CPI (+41% for milk v +45% all Food). Since 2010 growth in all Food CPI has slowed (+13%), but cheese (+7%) and milk (-5%) Ice Cream (-3%) have fared

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		worse. Dairy is not alone - poultry, bread, cereal products, tea & coffee, jam all experienced low or negative CPI growth over last decade.
Australian milk one litre carton at $1.29 is by far the world's cheapest milk.	Do not support	The $1.29 figure is not correct. The average per litre is $1.71 (Dairy Australia). By international standards this is low but is nowhere near the lowest. For example, the US milk price is $3.45 per gallon which translates to $1.30 per litre (3.785 gallons per litre price. Their retail range is $1.00 – $1.50 per litre for the same milk in different states (USDA *Retail Milk Prices Report* 2019).
PROFITABILITY		
The industry is in a price/cost squeeze.	Support	ADF's submission to the Inquiry into the performance of Australia's dairy industry and the profitability of Australian dairy farmers since 2000 demonstrated this. It has been recognised by both sides of politics. It should be noted that this has been a feature of agricultural markets across the globe, particularly in western economies.
There is a history of steady productivity improvement.	Support in part	Despite decades of consistent productivity improvement there has been no change over the past decade (Dairy Plan *Measurement of profitability on Australian dairy farms* 2020). It is widely suggested that agricultural productivity gains (~1%pa) are less than ideal.
Many dairy farms have debt to earnings ratios that are unsustainable.	Support in part	Dairy farm equity ratios fell slowly over 1990s as people borrowed to expand farms, but the ratio now (81%) is about the same as they were over the later 1990s, early 2000s. The dairy ratio is lower than some broadacre industries (sheep-beef).
The Processors and particularly the retailers are all making money.	Support in part	Processors do not appear to be making super-profits over any sustained period. Evidence includes listed company results, high profile bankruptcies, stalling capital investment, facility closures, asset sales and exits (e.g. Lion). Retailers doing fine. For example, Coles recorded $1.3b EBIT in 2019 although this was on sales of $31b (Coles *Annual Report* 2019).

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The profit margin on unbranded milk for an independent supermarket is around 10% (but the ACCC believes it is 18%) and branded milk 20% (ACCC 50%).	Do not support	The ACCC in its Dairy Inquiry said: 1. 'The margins earned by supermarkets vary considerably across dairy products and time. In general, supermarkets make higher margins on branded dairy products than on private label products. For example, in 2015–16 supermarkets earned average gross margins of 28 per cent on branded fresh drinking milk but only 12 per cent on private label fresh drinking milk. This same observation is also true for other categories of dairy products, such as yoghurt, cream and cheese.' 2. 'Supermarkets generally sell private label milk at a gross profit but at times sell it at a loss in Tasmania and Queensland, once distribution costs are taken into account.'
INDUSTRY STRUCTURE		
The corporatisation of Processors has been a mistake for the dairy farmer and the economy. The corporatisation of Murry Goulburn (MG) has been a disaster. NZ and India have proven that in spades.	Do not support	Corporatisation of the two biggest processors (Bonlac and MG) occurred following the spectacular and dramatic collapse of each, 15 years apart under different market circumstances but both under farmer-controlled boards. Corporatisation of other processors has generated significant farmer windfalls at the time – long term impacts open for debate. India is now the largest dairy producing country in the world. They have achieved this in a relatively short period of time via subsidies and other government interventions. The issue is these have led to perverse or unintended economic effects - inefficient resource allocation, incentivising lack of farm productivity and diverting economic resources away from more productive areas of the economy. However, it is important to note that India's place is affected by inclusion of buffalo milk in its numbers. On cow's milk, they are behind US and EU (as a bloc). Also, India operates essentially as a closed shop against imports

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		(only letting product in at times of domestic shortages) and intermittent exporter of surpluses. It is not a model Australian dairy should follow.
In some dairy product sub-markets, one or more of the Processors is dominant. This exacerbates the problem.	Support	The ACCC in its Dairy Inquiry said 'The level of concentration in a market is a useful indicator of the degree of competition over time, and of the potential for firms to have market power. It measures the number of firms and the distribution of market share amongst those firms in a market. The higher the concentration, the lower the degree of competition, and the more likely it is that firms have market power.'
The fact that the dairy farmers have not been authorised by the ACCC, either by State or dairy region, to negotiate collectively with the processors tells a story in itself.	Do not support	ADF has authorisation until 30 August 2021 (from 4 August 2011) to register and administer dairy farmer collective bargaining groups (CBGs) consistent with the ACCC's determination requirements. Currently there are 18 CBGs in operation across the country. 355 dairy farmers are members of CBGs. This represents 6.8% of dairy farms based on the current total of 5,213.
MARKET FAILURE		
The market has failed and no Code of Conduct or Government jawboning will work. With drinkable milk, the problem can only be solved by price regulation. The dairy industry structure is causing market failure.	Support in part	Markets fail for various reasons. Generally, it is the result of a public good, externality, market power, risk or asymmetric information. The ACCC did identify market failure in dairy. This relates to asymmetric information between farmer and processor. Actions to address this are currently being implemented. Price regulation was not a recommendation in this or any other the other nine dairy inquiries conducted by industry and government over the past decade. To determine if there is market failure between processor and retailer in regard to discounted dairy and other products on retail shelves, the ACCC should conduct another review of the food and grocery sector (similar to its 2008 review). It is critical to the policy debate that the ACCC provide more analysis and detail surrounding the following statements in its Dairy Inquiry:

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		1. 'Supermarkets have leveraged their buying power to drive wholesale prices down and reduce the profit margins of processors. This has particularly been the case with private label drinking milk and private label cheese.' 2. 'The $1 per litre price represents a real 12 per cent decline in the retail price of private label milk since its inception in 2011. It is an arbitrary 'cap' imposed by retailers on private label milk which does not reflect the costs of production and supply.' A refresh of the 2008 review is important given the 'down down' price campaign (of which dairy has become a victim) occurred afterwards.
Adam Smith condemns oligopolies, as they interfere with and destroy the free market. Firstly, he would say that competition law is not relevant to the game	Support in part	An oligopoly is a form of market where a few very large suppliers dominate the market. Adam Smith did say in his infamous book the Wealth of Nations that 'people of same trade seldom meet together even for merriment and diversion, but conversation ends a conspiracy against the public or in some contrivance to raise prices.' However, in an oligopoly everything depends on firm strategy. The market could resemble a monopoly where there are high profits for firms, it could be stagnant, or caught up in price-cutting war. In any of these situations the ultimate winner is the firm who implements the best strategic thinking. This can be analysed via game theory. In 2008 the ACCC conducted an inquiry into competition in Australia's grocery sector. This inquiry was prompted by high rates of food price inflation across the country. It included extensive analysis of the supply chain and bargaining power of Coles, Woolworths and Metcash (the major wholesaler to the independent sector). The inquiry found 'most grocery retailers and suppliers compete to deliver value on price and quality' however barriers to entry and expansion needed to be lowered

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		in both retailing and wholesaling to attract independent supermarkets and potential new entrants, which ultimately lower prices for consumers (due to increased competition). In regards to fresh products the ACCC 'has not found any evidence to suggest that the major supermarket chains are acting in an anticompetitive way in their dealings with suppliers of fresh products. In particular, there is no across-the board evidence to suggest that retail prices for fresh products are going up by a greater percentage than farm-gate prices.'
Deregulation in 2000 has failed. Dairy farms, production, cows, employee numbers and capital have dropped dramatically to the point where Australia has an unprofitable sector, and this will continue without intervention.	Support in part	Decline in the number of dairy farms has been occurring long before and after deregulation. In 1960 there were around 50,000 dairy farms, 12,000 in 2000 and 5,213 today (ABARES Dairy Farm Statistics). The number of farmers employing labour increased by 25 per cent from 2005 to 2017, with 86 per cent of farms now employing labour (Dairy Australia 2019). The dairy industry now directly employs over 42,000 people today. Attracting people to a career in dairy continues to be a priority, with an additional 800 employees needed on Australian dairy farms by 2023. The Gross Value of Dairy Production has consistently increased before and after deregulation. In 1970 it was $425m, today it is $4.2b (ABS Value of Agriculture Commodities). The average profit at full equity for a dairy farm from 1990-2000 (pre-deregulation) was $40k, from 2000-2010 (post deregulation) it is was $63k and 2010-2019 (post deregulation) it was $106k (ABARES AgSurf data).

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		Average dairy farm equity has increased from \$1.5b in 1990 to \$4.4b in 2019 (ABARES Agsurf data). Since deregulation farm profitability has been negatively impacted by the following: 1. the move by processors to change payment systems to encourage all year-round production (rather than traditional grass based seasonal milk production system commonly practiced in southern Australia), which incurs higher production costs 2. drought and other climate linked issues including higher summer temperatures impacting grass growth and cow management, which also incurs higher production costs 3. increasing costs, for example electricity and inefficiency in the processing sector contributing to Australian dairy products, in particular bulk commodities, being uncompetitive in overseas markets 4. introduction of aggressive promotion of 'private label' or 'home brand' products by supermarkets i.e. \$1 per litre milk since 2011, which has stripped value out of the dairy supply chain. 5. significant world market price volatility caused by a range of factors including the removal of EU production quotas and EU loss of Russian market access 6. the international dairy price downturn and further price reductions late in the 2015–16 season by Australia's two largest dairy processors Murray Goulburn and Fonterra Australia 7. farmgate price growth not keeping up with the cost of production growth.

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		Over the past ten years there have been ten parliamentary and industry reviews into the dairy industry. These recommended reforms that seek to increase competition, marketing and price setting transparency, reduce trade barriers, professionalise contracting, encourage investment in RD&E and reform of industry structures. NB: ABS GVP numbers quoted are in nominal current dollar values, while the AGsurf farm profit numbers are adjusted into their 2019-20 dollar values.
The de-regulation was influenced by the Hilmer Review on competition policy where it was believed there was no public benefit in regulating dairy.	Support in part	Dairy deregulation was influenced by the Hilmer Review and several other very significant policy and trade decisions taken by state and federal governments over the past 50 years. These include relinquishing access to EU butter in the 1970s, Australia/New Zealand Closer Economic Agreement (CER) with NZ in 1980s and National Competition Policy (NCP) of the 1990s. Each state, with the exception of Victoria, found a positive public benefit to retain pricing and supply regulations. Consequently Victoria, under the terms of the NCP Agreement, was obliged to remove their fluid milk pricing and supply arrangements. With the Australian constitution allowing free trade between states, the Victorian decision meant all state fluid milk pricing and supply arrangements lapsed. Each state repealed their acts to get DSAP and DRAP funds (government structural adjustment funding over $1.6b nationally) but they did not relinquish the basic power to set prices going forward.
REGULATION		
There are several possible ways to intervene: • Voluntary or enforced codes of conduct by the ACCC giving the codes the force of the law,	Support in part	Government intervention in the dairy industry includes regulation, research and development, innovation in extension delivery, knowledge innovation systems, facilitating investment, improving market access

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• industry restructure, • price control via regulation and • authorising dairy farmers to negotiate together by State or by the market of the Processor on pricing and terms.		and enabling resilience in farms and rural communities. Given the policy debate is currently focused on price regulation ADF commissioned Dairy Australia to analyse on five different intervention options which could be considered for Australian dairy. These are: 1. Farmgate milk floor price schemes 2. Minimum retail pricing for fresh milk and/or other dairy products 3. Farmer-support levies applied at the retail level 4. Subsidized investment in processing assets in remote dairy regions 5. Regulated Two Tier pricing systems.
Codes of conduct are helpful but are limited in impact. The result is often a document that favours one of the players over the other.	Do not support	There have been numerous independent reviews of industry codes that have concluded they are of benefit to industry. Some examples: 1. The Franchising Code of Conduct was established in 1998 and has been reviewed four times. Each time the benefit of the code has been validated. In its submission to the last review the Franchise Council of Australia (peak industry body representing franchisors, franchisees, service providers and suppliers involved in franchising) supported the code as an effective part of the regulatory framework. 2. The Wheat Port Code commenced in 2014 to establish an access arrangement to ensure that exporters of bulk wheat have fair and transparent access to port terminal services. A key finding arising from the Wheat Port Code Review interim report (April 2018) was validation of the need for a mandatory code but with amendments to improve effectiveness.
We disagree with the (ADF) Report's observation that introducing any form of price control is inconsistent with	Do not support	Constitutionally, the redistribution of retail levy collections back to the farmers that supplied (or were paid for supply of) the milk subject to the

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Government initiatives and undermines Australia's international trade obligations and the Australian Constitution. In fact, ADF Report agrees with our thinking and may contradict itself on page 59 where it suggests that home brand retail fresh milk price to be fixed to $1.50 per litre with increase (50 cents per litre based on the original $1 litre milk) going back to dairy farmer via their Processors and agrees with my recommendations of short term solution to increase home brand retail milk price to stop farmers hardship and farm exit.		levy would seem to comply with Section 51 rules. A possible issue would be the basis of redistribution - market milk supply or all milk supply. A retail levy scheme would not breach Australia's WTO commitments regarding export subsidy payments. However, the pool of money that could be distributed back to dairy suppliers under any new regulated retail levy scheme would have to comply with Australia's existing domestic support commitments to the WTO (namely the total industry benefit must not exceed an AMS ceiling for all agriculture of $472 Million per annum). In recent years Australia has reported a zero AMS to the WTO. It is unclear whether the federal government would be prepared to allocate its entire AMS entitlement to just one industry (i.e. dairy). Even assuming that no other industry-level support arrangements are put in place outside of dairy: 1. Based on national milk sales of 2.48b litres p.a., a 10c per litre retail levy on all domestic milk sales would generate roughly $243m in scheme revenues. If all these revenues were paid back to farmers, the AMS obligation would essentially match this amount (as was the case with DSAP). 2. A regulated retail levy of 19 cents per litre, if applied to all domestic milk sales would raise around $460 Million per annum. Distributing these monies to farmers would essentially exhaust Australia's full AMS entitlement. 3. If the retail levy were applied more narrowly to only cover supermarket milk sales (estimated at 1.5 Billion litres per annum

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		by DA) the maximum possible AMS-compliant rate of retail levy could rise to 31 cents per litre. 4. However, the maximum gain achievable at farm gate from either a broad or narrowly focused retail levy on milk is 19 cents per litre (assuming scheme revenue is only shared across farm suppliers of drinking milk). If potential scheme revenues were to be shared across all local milk supplies (i.e. including manufacturing milk), then the maximum WTO compliant industry gain is below 6 cents / litre at current production levels. The $1.50 per litre on home brand milk is a recommended minimum for retailers to charge across the country.
The ACCC found that on investigation that 10c was not being passed on to farmers. The ACCC argues there are technical deficiencies in the Law and Coles cannot be charged for deceptive and misleading conduct both to farmers and to the general consumer.	Support	On 5 December 2019 Coles was ordered to pay Norco dairy farmers around $5.25m following an ACCC investigation into the passing on of the 10 cents per litre increase. The ACCC found that when an unrelated 6.5 cents per litre increase commenced on 1 April 2019, Coles reduced its payments to Norco under the 10 cents per litre retail price increase from 10 to 3.5 cents per litre. Mr Rod Simms, ACCC Chairman said 'we were fully prepared to take Coles to court over what we believe was an egregious breach of the Australian Consumer Law. We believe we had a strong case to allege misleading conduct by Coles.'
The reality is that Treasury controls the agenda and has many academic analysts and others to criticise the work of we mortals who concentrate on common sense not mathematical formulas.	Do not support	It is the Cabinet not an individual minister or portfolio that makes decisions for government. This is the council of senior ministers who are empowered by the government to take binding decisions on its behalf. Ministers must carry out Cabinet-determined policies with respect to their own portfolios, whether or not they agree with such policies. It is

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		the Prime Minister, on the advice of the Cabinet Secretary, to decide what matters require Cabinet consideration.
ADVOCACY		
Dairy farmer publications and information is too fragmented and too small with little reach.	Support in part	There are a number of publications - the Australian Dairyfarmer Magazine, The UDV Hotline (in Victoria), Dairy News Australia (covering northern Victoria and southern Riverina), and other publications. Of the publications mentioned, the ADF Magazine includes information on ADF's activities, Dairy Australia initiatives and other industry developments, Hotline covers information relating solely to the UDV, and Dairy News Australia covers dairy industry news and is independent of the industry. While the nature and quality of reporting and distribution varies between publication, the Australian Dairyfarmer Magazine is distributed to all registered dairy farms across the country.
The existing National Council of Dairy Farmers (ADF) with representatives from the various States has a problem, it does not have sufficient funds. Evidently its budget is $0.5 million a year and it has a 5.5 people. Without funds the prospects of this organisation being effective in looking after dairy farmer interests is too difficult.	Support in part	ADF like many of its state dairy farming organisation members are struggling financially. The traditional source of revenue, farmer membership, is declining consistent with farmer number and milk volume declines. Despite limited resources ADF has demonstrated effective policy and advocacy on several fronts. In recent years, its policy positions have been adopted by the government regarding farm trespass, workforce development, bushfire and drought response, trade and response to the ACCC Dairy Inquiry. This has been achieved by adoption of evidence-based policy, outcomes focus, employment of skilled staff and working collaboratively with Dairy Australia and other partners including the government.
RECOMMENDATIONS		
PRICE REGULATION		

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Price regulation is necessary at two levels: the price that Processors receive for their product from retailers, and the price by the Processors to the farmer.	Support in part	A range of price regulation options are discussed in Dairy Australia's recent market intervention research. As a general principle, given current industry ownership structures (and the absence of any large farmgate price setting cooperative), there is no guarantee that the value chain gains from a regulated minimum retail price for milk can, or will, pass fully back to farm suppliers. Under such a regime, there would be a strong commercial incentive for processors and retailers to expand their margins on retail sales.
The retailers, through price regulation, should increase the retail price of milk by $0.40 cents per litre to $1.70 (the world average). This should go straight to the farmer without deduction by the Processor. For the Farmer, it does not matter what the retail price is, the farmer requires a lift of $0.40.	Support in part	A price increase of 40c/L on retail liquid milk does not equate to a 40c/L increase at the farmgate. In any case, as referenced above, the pool of money that could be distributed back to dairy suppliers under any new regulated retail levy scheme would have to comply with Australia's existing domestic support commitments to the WTO (namely the total industry benefit must not exceed an AMS ceiling for all agriculture of $472 Million per annum). This equates to approximately 6c/L across all milk produced in Australia, assuming no other agricultural sectors contemplate similar schemes.
With the current state of the dairy industry, the consumer will accept a price increase, certainly 40c taking the price to $1.70 provided the Retailer and Processor do not benefit. With a 40-cent increase on farm gate price, the average household will pay only $102.96 per annum or $2 per week.	Support in part	Whilst consumer perceptions and attitudes towards a price increase are open to debate, in dairy (especially plain drinking milk) is generally regarded as a staple food. In line with this, various studies have suggested that the demand for drinking milk is not very responsive to changes in prices (being driven more by non-price factors such as health, convenience, brand loyalty). In previous reviews of dairy, the Productivity Commission estimated that the own price elasticity of demand for drinking milk (the amount by which consumption adjusts to a change in price) is -0.15. This implies that a 10% rise in retail milk prices due to regulation would lead to a 1.5% fall in direct consumption. Other Australian studies have found slightly lower (Tulpule and Powell

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		1978 found milk's own price elasticity was -0.1) or slightly higher demand elasticities for drinking milk (e.g. Ulubasoglu, 2015 estimated milk's own price elasticity as -0.23). Other international studies tend to confirm the view that price rises for milk are not likely to substantially alter local consumption levels (e.g. Huang 2025). These findings also take into account: 1. The historically low share of imports in recorded retail milk consumption, and 2. The relatively high price points of non-dairy milk substitutes. In this regard technology changes with regards to UHT and ESL milk, and trade in milk concentrates, may make these historical assumptions less iron-clad.
The increased notional price for drinkable milk should go to all dairy farmers in proportion to the litres of milk delivered by them to the Processors.	Support in part	This is one option for design of such a scheme. It would require comprehensive and timely information to be provided to the independent agency disbursing the funds, and an agreed method of disbursement including considerations for different farm ownership structures (sharefarmers etc).
An intermediary, like Dairy Australia or Australian Dairy Farmers Ltd or an accounting firm, should receive the payment from the resellers for distribution to the dairy farmers in proportion to their litres delivered to the Processors.	Do not support	A new regulated retail levy would constitute a federal (or state) tax. In the past revenue raised by such taxes has had to enter Consolidated Revenue (Commonwealth or state). A formal budget appropriation is then needed before any money raised by the levy can be transferred back to industry participants. Government usually requires external audits by an independent public body of the expenditure of all money raised by taxes and allocated by budget appropriations. This is a complex process.
The pooled amount available each month should be paid to the intermediary at the same time the Processors are	Support in part	The point of levy collection needs to be clarified, since it is not just the major retailers – route trade and food service suppliers would also have

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paid by the Resellers. The intermediary would divide the pooled amount available by the litres supplied and establish a rate per litre of milk delivered to the Processors. The intermediary with the details of litres provided by the Processor in advance of a payment being made, should mean that calculations can be made so that the dairy farmer is paid simultaneously with payments to the Processor.		to be included; alternatively, the levy would require collection at the processor level.
This could be audited, say quarterly.	Support	It is highly likely that external audit /review arrangements would be required by government for any disbursement process (e.g. ANAO reviews).
Anyone can appeal to the ACCC.	Support in part	The ACCC's powers are unclear in this context. With regards to the mandatory code of conduct, the ACCC have stated that they do not offer a dispute resolution service and excluded themselves from the process: 'The ACCC is not a dispute resolution body and does not provide legal advice...Under the Code, a milk supply agreement must provide for both an internal complaint handling procedure and a mediation process. The Code also provides both processors and farmers with a right to seek to resolve a dispute via mediation using the process set out in the Code. A milk supply agreement may also provide for an arbitration process, including by adopting the arbitration process set out in the Code. Before resorting to mediation or arbitration, parties must first try to resolve the dispute via the processor's internal complaints handling process.' Given this it would seem unlikely that the ACCC would enter this sphere under a regulated levy arrangement.
It can be implemented in weeks and the dairy farmers benefit within weeks.	Do not support	Policy change requires development of a solid business case and legislation design. It then needs to be approved by relevant ministers before they take it to Cabinet and Parliament for further approval.

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		Parliamentary approval not only requires approval of both houses it often has to pass a committee of inquiry. It then requires Royal assent before the legislation is enacted. Implementation then requires appointment of staff, governance, process and other operational functions to be designed and delivered. The quickest time this process has occurred was for the COVID-19 stimulus packages like JobKeeper which occurred in a matter of months. More contentious policies such as a levy on retailers will take at least 12 months.
DIVESTMENT		
The government is attempting to intervene and pass legislation giving the ACCC, the power to force the divestment of assets (in the electricity sector). Why will not the Government do the same in respect to the dairy market?	Support in part	The ACCC identified market power misbehaviour by state owned duopolies particularly in Queensland in its final report of the Retail Electricity Pricing Inquiry (July 2018). In response the government introduced the *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018* to implement a legislative framework consisting of new prohibitions and remedies in relation to electricity retail, contract and wholesale markets. The Bill identifies four types of relevant conduct: 1. prohibited conduct in relation to retail prices 2. prohibited conduct in relation to the electricity financial contract market 3. prohibited conduct in relation to the electricity spot market (basic) and 4. prohibited conduct in relation to the electricity spot market (aggravated). The Bill sets out a range of remedies that are to be applied in relation to the four types of prohibited conduct set out above. These include for the ACCC, in respect of any of the prohibited conduct, issuing a public

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		warning notice or issuing an infringement notice. These remedies are in addition to existing remedies in the *Competition and Consumer Act 2010* such as accepting a court-enforceable undertaking and applying to the court for an injunction. The remedies available to the Treasurer are making a contracting order—in respect of type 2 and type 4 prohibited conduct and applying for a divestiture order from the Federal Court—in respect of type 4 prohibited conduct only. There may be merit in the government replicating some aspects of the Bill for dairy retail. This will require further examination by the ACCC and Departments of Agriculture, Industry and Treasury.
TAX REFORM		
Payroll tax ought to be phased out over a five-year period for all agricultural enterprises.	Support	Payroll tax is levied by all states on businesses with payrolls above certain thresholds. It reduces the demand for labour, lowering wages to the point where the return on capital is again equal to the world level. In the short-term businesses bear the burden of this tax and in the long-term workers. Ultimately it leads to a decline in average labour productivity and national income. This is part of the rationale why payroll tax exemptions or deferrals were a key part of state economic stimulus for COVID-19 pandemic. A phase out of payroll tax should occur as part of broader taxation reform (consistent with the Henry tax review) as a national response to the emergence from COVID-19.

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15 June 2020

Hon. David Littleproud MP
Minister for Agriculture
PO Box 6022
House of Representatives
CANBERRA ACT 2600

Dear Minister,

RE: Policy response to retailing of dairy products

At last month's meeting of national and state dairy farmer advocacy bodies, which you attended, we agreed to provide you with a policy response to retailer pricing of dairy products and the use of dairy terms in labelling of plant-based alternatives. Since then, our policy committees and Board of Directors have considered these issues and determined that:

1. Our submission to the Senate Standing Committee on Rural and Regional Affairs and Transport for its *Inquiry into the Performance of Australia's dairy industry and the profitability of Australian dairy farmers since deregulation in 2000* is still valid; and
2. We will work with you to explore mechanisms, such as a retail sales levy, to provide a meaningful increase in returns to all dairy farmers.

<u>Retailer pricing of dairy products</u>

The *Independent Review of the Food and Grocery Code* and the ACCC *Dairy Inquiry* identified an imbalance of bargaining power (market failure) between retailers and dairy processors. Key statements validating this are:

- 'Supermarkets have leveraged their buying power to drive wholesale prices down and reduce the profit margins of processors. This has particularly been the case with private label drinking milk and private label cheese.'
- 'The $1 per litre price represents a real 12 per cent decline in the retail price of private label milk since its inception in 2011. It is an arbitrary 'cap' imposed by retailers on private label milk which does not reflect the costs of production and supply.'
- 'The Review received consistent complaints from suppliers in relation to the retailers' process for negotiating an increase in the price of goods.'
- 'The retailer plays a significant role in controlling prices through their acceptance or rejection of the supplier's price point. In practice, the retailer acts as the gatekeeper to pricing changes and will only purchase product at a price that has been approved or permitted by them.'
- 'With a lack of visibility of the sale transaction or access to market information, growers can find themselves vulnerable to 'price skimming' practices by traders.'
- 'Some suppliers reported instances where they have been unsuccessful in requesting a price rise for their product but later found that the retailer had increased the retail price on the shelves to capture additional profit for themselves.'
- 'Heightened retail price competition has limited suppliers from raising prices in line with their higher overheads.'
- 'The Review does not believe that the current verification process being used by retailers is leading to the best outcomes for suppliers or consumers.'
- 'Price rises were accepted by the retailer on the condition that the cost was off-set, in whole or in part, by some other means by the supplier.'

To resolve this issue, our submission to the Senate inquiry suggested that:

1. Retailers need to increase their price of home brand milk to at least $1.50 per litre. This figure was determined by analysis of market demand and supply responses following the introduction of the $1.00 per litre prices in 2010; and
2. A taskforce be appointed to insert clauses in the *Food and Grocery Code* to deter retailers from using dairy as a loss leader. It is noted that in your government response to the independent review (March 2019) you committed to expanding the good faith provision and improving the price verification process (imposition of a 30-day limit on resolving price rise notifications that do not require disclosure of all commercially sensitive information). While these amendments are welcomed it may not be enough to deal with dairy's long-standing issue.

Recently, we completed a cost/benefit analysis of various interventions a federal or state government could implement (refer attached). This covered a:

1. Farmgate Minimum Floor Price (proposed by One Nation, Katter Party and the Australian Labor Party);
2. Minimum Retail Sales prices;
3. Retail Sales Levy (proposed by John Dahlsen);
4. Two-Tier Pricing for farmgate milk; and
5. Government subsidized investment in regional processing.

While our analysis found the retail sales levy to have the strongest case, like other options, there are challenges that need to be resolved. Some of these are outlined in our response to the John Dahlsen report (refer attached). It is recommended that another taskforce be established to determine actions to resolve these issues and identify the type/s of price intervention most suitable for consideration in the retail sector.

<u>Use of dairy terms in labelling of plant-based alternatives</u>

At the November 2019 meeting of the Australia and New Zealand Ministerial Forum of Food Regulation, ADF's request for a holistic review of labelling and marketing of non-dairy alternatives, and development of additional regulations to prevent plant-based products from trading on the labelling, qualities, and values of dairy, was not supported. The meeting communiqué provided limited justification for this decision. Truth in labelling is critical to ensure there is no market failure by way of information asymmetry. Until we are provided with a clear explanation and rationale why this action is not valid there is no need for us to change our policy position.

A Dairy Australia survey found 54% of consumers purchased non-dairy alternatives because they perceived them to be healthier than dairy milk. The evidence clearly demonstrates consumer purchasing decisions on this basis cannot be substantiated. Pursuing compositional parity regulation is an option for resolving this misunderstanding. However, ADF considers it an addendum to the original policy position and only to be progressed if further research and analysis is conducted on the risks and benefits. For example, the Codex General Standard for the Use of Dairy Terms CODEX STAN 206 (GSUDT) includes significant protections for dairy terms. Australia and New Zealand supported the development of the Codex GSUDT and are WTO signatories. Compositional parity regulation has the potential to move us further from the CODEX standard.

I hope this provides the clarity you need for your parliamentary and government responses. We look forward to working with you to progress these important priorities for Australian dairy farmers.

Yours sincerely,

Terry Richardson

President
Australian Dairy Farmers