

Summary and recommendations

Australia has a large and efficient dairy industry which acts as a major regional employer. While the bulk of milk production occurs in the south-east regions of Australia, dairying continues to be a geographically widespread economic activity with dairy farms operating in each state.

The industry has experienced much consolidation, rationalisation and adjustment, particularly since deregulation in 2000. At times, dairying can be an uncertain and challenging occupation. As with other agricultural industries, phenomena such as drought and flooding can make the occupation difficult, and for some farmers, no longer viable. International prices have a significant influence on farm gate prices (although the extent of this influence varies between dairy regions depending on the volume of exports). Negative external shocks to these international prices, such as those following the global financial crisis, can significantly reduce the value of the supply chain, sometimes leading to tense contract renegotiations and eventually impacting farmers' incomes. The structure of the supply chain and domestic market trends, issues which are directly relevant for this report, can also have various short and longer-term implications.

This committee was tasked by the Senate with examining the impacts of the decision in January 2011 by the major supermarket chain Coles (followed by its competitors including Woolworths, ALDI and Franklins) to heavily discount the price of its 'private label' or 'home brand' milk and other dairy products. In particular, the price cuts mean that milk can now be purchased by consumers for \$1 a litre—a price many argue does not reflect the significant effort put into producing and distributing milk, as it is lower than the price of many other food and drink products which are not perishable and are less costly to produce.

The circumstances which gave rise to this inquiry appear unusual in many respects. In recent years, public debate about the competitiveness of the supermarket sector has been focused on concerns about food price inflation and grocery prices being too high. In conducting this inquiry, the committee has been troubled that the benefits gained by consumers have not received sufficient attention in the debate about milk prices. In general, price discounting is likely to be pro-competitive and of benefit to consumers. Provided it does not constitute predatory pricing, a retail price cut should not be discouraged. The January 2011 price cuts in a staple product is undoubtedly good news for consumers in the short-term. Attempting to predict with any certainty any longer-term impact on overall consumer welfare is difficult, if not impossible.

Along with the impact on consumers, the committee focused on any impacts, or likely impacts, on the other end of the supply chain. When the inquiry commenced, the committee had strong concerns about the effect the price cuts could have on dairy farmers' incomes. The committee is grateful to the large number of individuals and organisations involved in the dairy supply chain who were willing to provide detailed

evidence and material for this inquiry. Much of this information, however, concentrated on concerns about shifts in sales away from the processors' branded milk products to the discounted supermarket private label milk. As a matter of overall principle, these types of free market outcomes should not be a matter for government. Many private label grocery products have grown in share in recent years, fulfilling the demand of those consumers who are happy to purchase them—particularly when there are little distinguishable characteristics between the branded products and their lower priced private label equivalents.

Milk is one such product; it is apparent that there are very little quality and specification differences between many of the processors' branded milks and the private label alternatives. It should not be a matter for public policy to protect brands that consumers no longer value. It also does appear that the steadily increasing sales of private label milk—which have more than doubled their share of sales in supermarkets over the past decade—is a trend that is unlikely to be reversed.

Impact on dairy farmers

It is apparent that when looking at the dairy industry at a national level, most dairy farmers will not be significantly worse off because of the price cuts. This is because the vast majority of milk production occurs in states such as Victoria where a number of processors operate and drinking milk represents a relatively small share of production, compared to the production of manufactured dairy goods. Due to significant export opportunities, international prices are a key determinant of the income farmers in those areas receive.

However, it is clear that in states which do not have these characteristics, such as Queensland and Western Australia, the impact is potentially greater. In these states, there are few processors operating and milk production is primarily for drinking milk. The emphasis on drinking milk means any pressure on retail prices could potentially be pushed back down the chain, although at this stage there is no evidence the major supermarkets have done this. Additionally, in some areas it is also difficult to distinguish between the consequences of natural disasters, such as the Queensland floods, and the impacts of the discounting.

One key area of concern for the committee, however, was the speed and ease with which a certain group of farmers in Queensland contracted to Parmalat were affected by the cuts in the retail price of private label milk led by Coles. Under these arrangements, it appears the risk of any retail price movements or other shocks that affect the sales of branded products are in large part being passed immediately onto the farmers. It is not clear why this should be the case when the processor has chosen to supply both products to the supermarket. Whether a consumer chooses to buy a bottle of processor-brand milk or the supermarkets' private label should not (again, as a matter of principle) be a concern for farmers. Although processors are undoubtedly in a challenging position, the management of their branded products and the terms on which they supply private label milk to the supermarkets is a matter for them.

Recommendation 1

5.43 The committee urges processors to make their pricing structures for sourcing drinking milk:

- **reflect the volume they estimate they require to meet their total commitments;**
- **offer more stability in prices rather than changing frequently; and**
- **not be dependent on the final retail sales of branded versus private label milk.**

Recommendation 2

5.45 The committee recommends that contracts with dairy farmers should offer a clear, consistent formula for milk pricing with unambiguous conditions.

The committee received evidence about the current deficit in drinking milk production in Queensland and, given present market signals, the likely ability of the dairy industry in the drinking milk-focused states to meet future demand.

If it is the case that it is more economically viable for processors to transport milk from other states where it is cheaper to produce, this is also not necessarily a matter for public policy. Such a result can be argued to be an outcome dictated by realities in the market, as well as similar to the interstate trade which occurs for other agricultural produce. However, the committee believes these issues need further examination to allow an informed discussion about the future of the industry in those states.

Recommendation 3

5.47 The committee recommends that the Government commission a study of the dairy industries in Queensland, New South Wales and Western Australia. The study should focus on the future sustainability of the dairy industry in each of these states and their capacity to meet future local consumer demand. The report of the study should also examine possible policy options and be tabled in the Senate.

Competition law

A number of organisations that participated in this inquiry called for an investigation of Coles' conduct by the Australian Competition and Consumer Commission (ACCC) and for aspects of Australia's competition laws to be amended.

The ACCC undertook an examination of Coles' conduct against the current competition law, and concluded that there was no evidence that Coles was engaging in predatory pricing in contravention of the *Competition and Consumer Act 2010*. The committee discussed the details of this investigation extensively with the ACCC, and also passed on other issues to the ACCC regarding the milk discounts, such as certain statements made in Coles' initial advertisements relating to its 'Down Down' campaign.

The committee is not of the view that the specific price discounts by Coles which were the subject of this inquiry warrant legislative amendments. Care needs to be taken when suggesting amendments to the Competition and Consumer Act based on the experience of one industry (or part of one industry, as is the case with the milk discounts) as they would apply to the entire economy. Even if amendments to Australia's competition law were needed, it is not clear that the amendments proposed during the inquiry would actually provide a 'remedy' to the milk pricing issue.

The committee, however, notes the recent comments by the new chairman of the ACCC that some aspects of section 46 of the Competition and Consumer Act, which deals with misuses of market power, are 'worth debating'.¹ The effectiveness of Australia's competition laws has been raised in the context of various sectors and has been considered by this committee on numerous occasions. It has also been some time since the Dawson Review in 2003, which was the last independent review of the Act undertaken. The inquiry before that was the Hilmer Review, which was finalised in 1993.

Since the report of the Dawson Review, a number of amendments have been made to section 46 of the Competition and Consumer Act. The committee urges the ACCC to identify and litigate appropriate matters that will enable these recent amendments to be tested in the courts. However, questions remain about the operation of certain provisions. Additionally, in recent years a number of other competition issues including price signalling, creeping acquisitions and geographic price discrimination have been raised. It appears appropriate that, rather than recommending piecemeal amendments, an independent inquiry be formed to fully address any perceived gaps in, or issues with, Australia's competition law.

Recommendation 5

7.100 The committee recommends that the Government initiate an independent review of the competition provisions of the *Competition and Consumer Act 2010*.

It is clear that Coles and Woolworths have a very strong position in Australia's grocery market. While the recent signs of Coles and Woolworths more fervently seeking to attract consumers to their respective stores are encouraging for competition, the effects need to be closely monitored. Other possible developments, such as implications for the major supermarkets' dealings with their suppliers due to the growth in private label products generally, need to be monitored for any signs of anti-competitive conduct. The committee expects the Government and the ACCC to keep a watching brief on these issues and the grocery sector in general.

Transparency of ACCC investigations

An issue which the committee considered was the transparency of the investigations the ACCC undertakes. Whether or not the ACCC was undertaking an active

¹ Mr Rod Sims, Chairman, Australian Competition and Consumer Commission, *Committee Hansard*, 6 October 2011, p. 41.

investigation into Coles' milk price cuts was a question that frequently arose during the early stages of this inquiry. More broadly, there can be significant concern within certain sectors and the wider community regarding the effectiveness of the ACCC in enforcing the legislation for which it is responsible.

In most cases there will be little public information available as to whether or not the ACCC is investigating or has investigated a particular matter; however, substantial public interest appears to pressure the ACCC to provide some insight into its investigative activities. The committee is pleased that the ACCC was, on this occasion, willing to publish a statement that provided a high-level summary of the findings of its investigation. Such public statements on key matters help inform the broader public debate.

It is important to keep in mind that the ACCC is a law enforcement agency, and accordingly there are certain principles and practices it should be expected to adhere to. While increased transparency of what the ACCC is investigating at any point in time may be desirable in terms of ensuring public confidence in the ACCC, there are important consequences to consider. Overall, while the majority of investigations would still require confidentiality, there may be some scope for increased transparency or improved communication of the ACCC's enforcement activities.

Recommendation 4

6.58 The committee recommends that the Australian Competition and Consumer Commission (ACCC) review its approach to publicly releasing information about its investigations, with a view to providing greater general information about its current enforcement activities and relevant issues of particular public concern.

6.59 This recommendation is subject to the proviso that such action would not deny procedural fairness to the parties involved or threaten the integrity of the ACCC's investigations.

Imbalances of bargaining power and use of collective bargaining

More so than raising questions about the effectiveness of Australia's competition laws, the milk pricing issue is fundamentally a matter that reflects imbalances of bargaining power at various points in the dairy industry supply chain. These imbalances can be more pronounced in some regions than others.

The dairy industry makes use of allowances contained in legislation for some collective bargaining arrangements. However, the ability for processors to 'walk away' from negotiations with collective bargaining groups (as highlighted during the committee's 2010 inquiry), market realities such as the number of drinking milk processors in some areas and the fact that the processors must deal with the two major supermarket chains that dominate the grocery sector, can mitigate the benefits of collective bargaining arrangements.

Evidence was given, however, that although the dairy industry is utilising collective bargaining arrangements to some extent, they could be used more in situations where

there is a choice of processor. While imbalances of bargaining power issues are difficult to resolve and are always going to be present in some form, the committee considers this is an area that warrants attention.

Recommendation 6

8.9 The committee recommends that the Government review the effectiveness of collective bargaining laws and arrangements for agricultural industries, with a view to strengthening that framework to create a more equitable balance of power between the negotiating parties and to otherwise improve their operation.

Industry codes of conduct

The terms of reference for this inquiry required the examination of the suitability of the framework contained in the Horticulture Code of Conduct for the Australian dairy industry. No significant support was given to extending this type of arrangement to the dairy industry, largely because the issues dealt with by the Horticulture Code did not appear relevant.

The Produce and Grocery Industry Code of Conduct was also examined by the committee. It is a voluntary code created after the report of a joint parliamentary committee in August 1999. A government-funded ombudsman is in place to assist in dispute resolution.

This Code was put forward as a mechanism that is already in place for resolving disputes between suppliers and the major supermarkets. However, it is apparent that there are a low number of enquiries received by the Produce and Grocery Industry Ombudsman, and many representative organisations for dairy farmers were either unaware of the Code, or did not consider it relevant. Based on the evidence received during this inquiry, the committee considers that the effectiveness of the Produce and Grocery Industry Code should be reviewed.

A number of submitters also called for a mandatory code of conduct and an ombudsman or commissioner to be created, either for the drinking milk industry or covering the grocery sector more broadly. There may be merit in some form of office to act as a point of focus for grocery sector issues, particularly for responding to matters which are outside of the remit of the ACCC. However, the committee is aware that it has been asked to focus on one sector that supplies the major supermarkets—namely the dairy industry. Certain issues which are relevant to dairy farmers may not be relevant to other producers. Others would need to have input into any grocery sector-wide proposals. This consultation and debate could take place as part of the review of the Produce and Grocery Industry Code, which the committee also recommends.

Recommendation 7

8.43 The committee recommends that the Government initiate the following:

- **A review of the effectiveness of Produce and Grocery Industry Code of Conduct and mediation process undertaken through the Produce and Grocery Code Ombudsman. The review should include a consultation process regarding options to strengthen the Code, including that it captures entire supply chain relationships, and whether a revised Code should be made a prescribed mandatory industry code under the *Competition and Consumer Act 2010*.**
- **A consultation process on the need for a new statutory office to address issues regarding supply relationships in the grocery sector, and the role, powers, coverage and governance regarding such an office.**

