Chapter 3

Private label milk in Australia

3.1 The major supermarket chains sell milk in two formats: private label milk (also variously known as 'home brand', 'store brand' or 'generic') which usually carries the name of the supermarket selling it and 'branded' milk which usually carries the name of the processor.[1] The price cuts that are the subject of this inquiry were for private label milk.

3.2 It is estimated that private label products currently account for almost 25 per cent of all grocery sales, including 20 per cent of those through Coles and Woolworths.[2] A 2010 report released by IBIS World, a market research company, noted that certain categories of products are particularly suitable for successful competition from private label products:

> … due to the common perception that branded products are not necessarily of higher quality within specific segments of the supermarket, particularly the dairy aisle. The same applies to other staples such as eggs, flour and sugar, all of which have enjoyed solid private label growth, reaching more than 25% of sales.[3]

3.3 Dairy Australia notes:

> Private labels tend to gain significant share in what are termed 'low involvement' product categories—or those where the product offerings are very similar across the range on the market and the consumer decision-making process is relatively simple and straightforward.[4]

3.4 IBIS World also consider that the 'only way is up' for sales of private label grocery products, noting that they count for about one third of sales in the United States and more than half of those in the United Kingdom.[5]

Growth in private label milk post-deregulation

3.5 The growth in private label milk can be traced back to the deregulation of the Australian dairy industry in 2000, when excess capacity in the industry provided an impetus for growth. The Australian Competition and Consumer Commission's (ACCC) 2008 inquiry into the competitiveness of retail prices for standard groceries received evidence from a major processor on the dynamics of the industry at that time:

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1 Examples include Pura, Pauls, Harvey Fresh and Canberra Milk.

2 IBIS World, *Australia's appetite for private labels set to grow*, August 2010, p. 1.

3 IBIS World, *Australia's appetite for private labels set to grow*, August 2010, p. 1.

4 Dairy Australia, *Dairy 2011: Situation & Outlook,* May 2011, p. 31.

5 IBIS World, *Australia's appetite for private labels set to grow*, August 2010, p. 2.

> Parmalat contended that this provided a strong competitive tension to the point where the processors were prepared to tender for private label business at very low prices in order to utilise capacity. Parmalat considered that wholesale prices were driven down by this excess capacity, creating a gap between wholesale prices for branded and private label product which then expanded over time.[6]

3.6 The first national contract for supermarket private label milk was given to National Foods by Woolworths in 2002 (Dairy Farmers held a number of contracts at a sub-national level with Coles).[7] The ACCC, in evidence to the committee, remarked that the change in tendering arrangements by Woolworths had a clear impact on the returns farmers received, although they were not of the view that this experience is applicable to the current pricing decisions:

> Senator XENOPHON—You referred to the history—that is, that the dairy farmers have been at the wrong end of history on this in terms of the impact they have had in the past. Is that correct?
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> Mr Cassidy—Yes … I go back to 2000, when Woolworths changed the arrangements for purchasing home brand milk. They moved to a national tender, which drove down the price that they were paying for their home brand milk, and that flowed straight through the chain and ended up with the farmer. That is the sort of history I refer to, but that is not happening at the present time.[8]

3.7 Since 2000, the market share of the supermarkets' private label milk has steadily increased. Sales of private label milk have increased from about 22 per cent in 1999–2000, to approximately 50 per cent in 2009–10. Further, in the plain fresh white milk category, the supermarkets have increased their private label market share from 27 per cent to the current level of approximately 70 per cent.[9]

3.8 In some areas of Australia, however, the supermarkets' private label milk is a relatively new phenomenon. For example, Woolworths only began selling private label milk in their Western Australian stores in 2010.[10]

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6 Australian Competition and Consumer Commission, *Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries*, July 2008, pp. 235–6 (footnotes omitted).

7 National Foods, *Submission 97*, p. 16.

8 Mr Brian Cassidy, Chief Executive Officer, Australian Competition and Consumer Commission, *Committee Hansard*, 9 March 2011, p. 31.

9 Australian Dairy Farmers, answer to question on notice, 8 March 2011 (received 28 March 2011), p. 1.

10 Mr Pat McEntee, General Manager, Fresh Foods, Woolworths, *Committee Hansard*, 29 March 2011, p. 24.

3.9 At its appearance before the committee, the Dairy Farmers Milk Co-operative (DFMC) provided some interesting insights into how private label milk came about and grew in market share:

> Obviously for many years private label was absolutely loss making. I was on the Dairy Farmers board when it first started to occur. It was not done on the margin line; it was done at the request of retailers wanting some consumer shop choice. We are not against that. The more there the more buy, you might say. The shelf is about choice. Nobody can control the retail price of this product and, as we can see now with Coles, that absolutely happened 10 years ago. It was a pretty keen and loss-making wholesale price. The sales just boomed. Nobody expected the retail price point to be dropped that much compared to brand. I know when Dairy Farmers got the contract we just kept losing and losing money because much more was sold than was ever anticipated in the contract. But you had to meet the contract.[11]

3.10 The increasing divergence between the retail price of branded milk and the supermarkets' private label milk over the past decade, and its effects on the dairy supply chain, was also discussed:

> … if you go back to 2000, the differential between the two pools of milk, proprietary brands versus supermarket brands, was roughly 18c a litre. The differential across all sales through the supermarket was about $44 million. Ten years later at the end of last financial year, that difference has blown out by about 71c a litre or across the value chain about $414 million. That is a big chunk of money in terms of the domestic dairy industry value chain. That is money that is not going back into the value chain. This latest discount by Coles has actually pushed that differential out even further. That gives them an absolute price advantage in terms of growing their own brand market share and it puts greater pressure on the proprietary brands and that is going to put greater pressure back through the value chain on, obviously, the farm gate.[12]

3.11 One point that needs to be considered regarding the January 2011 price cuts is that since about December 2009, at least some private label milk products have been available at near $1 a litre. Prior to the January 2011 price cuts, Coles offered two private label milk brands with different pricing structures (Smart Buy and Coles brand). Coles have now discontinued the Smart Buy brand. The January 2011 price cuts means that while the price of the full cream product Coles retained has been significantly reduced (from $2.47), the price reduction only amounts to about 4.5 per cent for the now discontinued product (which sold for $2.09 for two litres). The price cut was more significant for the low fat product, which was reduced from $2.99 to $2.

11 Mr Ian Zandstra, Chairman, Dairy Farmers Milk Co-operative, *Committee Hansard*, 8 March 2011, p. 71.

12 Mr Adrian Peake, Chief Executive Officer, Queensland Dairyfarmers' Organisation, *Committee Hansard*, 8 March 2011, p. 83.

3.12 The committee received evidence from Coles that the majority of private label milk sold prior to the brands being consolidated was the Smart Buy product.[13] The committee is concerned that, given this evidence, certain advertisements which focused on the larger price drop may have caused the consumers of the full cream Smart Buy product to believe they were receiving a bigger discount than they actually were. These issues were discussed with the ACCC at the last hearing conducted for this inquiry in October 2011, with the ACCC indicating that it will examine them.[14]

3.13 Perhaps countering arguments related to the majority of the price cuts being less than five per cent, it could be argued that the January 2011 pricing decisions have continued the trend in declining retail milk prices, and reinforced any negative impacts associated with the earlier price reductions. Coles pointed out that in December 2009 its competitors reduced the retail price for two litres of private label full cream milk by eight cents from $2.17 to $2.09.[15] Coupled with the January 2011 price cuts, this represents a total decrease of over eight per cent in just over a year.

Table 3.1: Supermarket private label milk prices (per litre)

	2007–08	*2008–09*	*2009–10*	*February 2011*
Regular whole	$1.16	$1.18	$1.12	$1.00
Reduced fat	$1.34	$1.35	$1.30	$1.00

Note: In February 2011 the 11 cent Federal Government milk levy was removed.

Source: Dairy Australia, *Australian Dairy Industry in Focus 2010*, p. 44; originally sourced from Synovate Aztec.

Current private label contractual arrangements

3.14 Although Woolworths moved to a national contract in 2002, it has since reverted to state/regional contracts. After the merger of National Foods and Dairy Farmers in 2008, virtually all supermarket private label milk was provided by National Foods.[16] Since then other processors have gained or regained contracts for particular regions.

3.15 The duration of the contracts the processors enter into with the major supermarkets differ; Woolworths advised that their contracts are for either 12 or 24 months, whereas Coles informed the committee that the majority of their contracts end in January 2014.[17]

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13 Mr Ian McLeod, Managing Director, Coles, *Committee Hansard*, 29 March 2011, pp. 51–52.

14 *Committee Hansard*, 6 October 2011, p. 33.

15 Coles, *Submission 131*, p. 16.

16 National Foods, *Submission 97*, p. 16.

17 Mr Pat McEntee, General Manager, Fresh Foods, Woolworths, *Committee Hansard*, 29 March 2011, p. 3; Mr John Durkan, Merchandise Director, Coles, *Committee Hansard*, 29 March 2011, p. 43.

3.16 There have been a number of recent changes to private label contract arrangements. From September 2010, Parmalat began supplying Woolworths' stores in north Queensland after being awarded the contract previously held by National Foods. Woolworths' most recent tender process (conducted between December 2010 and June 2011) resulted in:

- National Foods continuing to supply stores in Victoria, South Australia, Western Australia and the Northern Territory;
- Murray Goulburn Co-operative continuing to supply stores in southern New South Wales, the Australian Capital Territory and now also stores in northern Victoria; and
- Parmalat gaining the contract previously held by National Foods to supply stores in New South Wales.

3.17 National Foods holds most of the contracts to supply Coles' private label milk.[18] These contracts were reviewed in January 2011. An additional development this year related to Coles' contracts in Western Australia, where National Foods does not supply Coles. In July it was announced that Harvey Fresh had gained Coles' private label contract for that state from Brownes Dairy.[19]

Differences between private label and branded milk

3.18 In its evidence to the committee, Coles responded to claims it had received that it 'has watered down its private label milk to save money', and that there are significant quality differences between its private label milk and other branded products in the same category:

> This is simply not true. Coles abides by standard milk formulation practices and, in accordance with federal government requirements, labels the key ingredients in all of its products, including the private label milk.[20]

3.19 Coles provided a document that compared the levels of energy, protein, fat and other specifications between the major supermarkets' private label milk and selected brands. It indicated that its private label brand has the same levels of energy, protein, fat, saturated fat, carbohydrates, sugars, sodium and calcium as one of the processor branded products, and shared similar specifications to a product offered by another processor.[21]

18 Dairy Australia, *Dairy 2011: Situation & Outlook*, May 2011, p. 32.

19 Coles, 'Harvey Fresh awarded Coles Western Australian milk contract', *Media release,* 28 July 2011.

20 Mr Ian McLeod, Managing Director, Coles, *Committee Hansard*, 29 March 2011, p. 37.

21 The comparisons were based on milk sold in Victoria. See Coles, document tabled at 29 March 2011 hearing, appendix VII.

3.20 Coles' position was supported by the Australian Dairy Farmers, which noted the Food Standards Australia New Zealand's (FSANZ) minimum regulatory requirements for drinking milk:

> In accordance with *FSANZ Standard 2.5.1 – Milk*, all packaged cows' milk for retail sale in Australia must meet minimum composition requirements for milk fat and protein. The standard also allows for milk composition to be adjusted to comply with the compositional requirements by the addition of and/or withdrawal of milk components, provided the adjustment does not alter the whey protein to casein ratio of the milk being adjusted.[22]

3.21 The high degree of similarity between private label and branded products may be a recent occurrence. Previously, when Coles offered two private label brands of milk—'Smart Buy' and 'You'll Love Coles'—there were slight quality differences between the two products.[23] Now that Coles' Smart Buy product has been discontinued, the higher quality private label product—that is, the product whose specifications are further away from the minimum standards set by FSANZ—is being sold. However, prior to the elimination of the lower grade private label brand, a 2009 CHOICE study concluded:

> - Almost all milk is highly processed.
> - Generic brands are much the same quality as the major branded versions – and a lot cheaper.
> - Most people will get no real benefit from the more expensive "milk" products with added extras.
> - All milk qualifies for the description "good source of calcium". There's between 115mg and 120mg of calcium per 100mL, regardless of brand.[24]

3.22 Nevertheless, whether the specifications of this product will significantly change in the future is something that may need to be monitored so consumers stay informed as to what they buying.

Why do processors continue to supply private label milk?

3.23 The profit margin processors currently have on private label milk was raised throughout this inquiry, with a number of assertions made. Coles' submission argues

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22 Australian Dairy Farmers, answer to question on notice, 8 March 2011 (received 28 March 2011), p. 16.

23 Mr Ian McLeod, Managing Director, Coles, *Committee Hansard*, 29 March 2011, p. 53.

24 CHOICE, *Milk products review*, 10 September 2009, www.choice.com.au/reviews-and-tests/food-and-health/food-and-drink/beverages/milk-products-compared.aspx (accessed 2 March 2011). This study was also noted by the South Australian Dairyfarmers' Association in their response to a written question on notice related to differences in specifications.

that National Foods, Fonterra and Parmalat have each announced profit margins higher than Coles.[25] Coles also suggested:

> In terms of their overall margins, there is an assumption made that lowering the retail price automatically means that the farm-gate price will be put under pressure. Our view on that is that there are higher levels of profitability within those companies overall and they can look for alternatives to improve their overall efficiency, improve their innovation, improve their product development and look to other ways to make savings should they wish to protect the margin, or invest some of it in the dairy industry here. There are a number of different ways in which they can take action through their broader level of economic strength, rather than just simply taking the easy route of squeezing the dairy farmers.[26]

3.24 Early in the inquiry, National Foods advised that their margin on Coles' and Woolworths' private label milk was close to zero, with their overall profitability on milk sales (generic milk plus National Foods' branded milk) being approximately two per cent.[27] National Foods also advised that they were making a loss on their private label contract with Coles prior to the wholesale price increase paid by Coles in January 2011.[28] National Foods (now Lion Dairy & Drinks) has since advised that for the year ending 30 September 2011, its projected full-year white milk earnings before interest and taxes (EBIT) margin 'is now expected to be negative'.[29]

3.25 Fonterra also objected to statements about the comparative profitability of milk processors:

> It has been suggested that the processors who sit between the farmers and retailers are the ones who are making unreasonably high margins and taking value out of the system. Nothing could be further from the truth. Dairy processing is a capital intensive exercise and those in the industry struggle with seasonal conditions, price volatility, higher input and energy costs, higher safety and quality costs, and erosion of margin. Further, developing market leading dairy brands with consumer propositions around health, wellbeing, superior nutrition, taste and convenience, requires significant investment in research and development. Dairy processors in Australia make only a modest return on their invested capital and this may be a

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25 Coles, *Submission 131*, p. 11.

26 Mr Ian McLeod, Managing Director, Coles, *Committee Hansard*, 29 March 2011, p. 49.

27 National Foods noted that at the time of their hearing it was too early to update these figures to reflect shifts from branded milk to generic as a result of the retail price discounts: Mr Duncan Makeig, Group Sustainability Director and General Counsel, National Foods, *Committee Hansard*, 9 March 2011, p. 63.

28 Mr Duncan Makeig, Group Sustainability Director and General Counsel, National Foods, *Committee Hansard*, 9 March 2011, p. 67.

29 Lion Dairy & Drinks, *Submission 159*, p. 4.

> reason why Australian interests have sold dairy assets to foreign entities in recent years.[30]

3.26 If there is little difference in specification between branded milk and private label milk (and thus processors risk eroding the market share of their branded product by supplying it), and the profits for processors historically associated with private label milk have been low or negative, the question naturally arises: why do processors continue to supply it? When asked at a public hearing why they supply it, National Foods' initial response was 'that is a very good question'. They elaborated:

> Since farm gate deregulation in 2000, house brand milk has become more and more of a reality … [T]he volume of milk is pretty inelastic. Consumers in Australia drink 102 litres per head per year or thereabouts. As more and more milk has transferred to house branded over time, we have large manufacturing facilities which need scale and volume. We also have contractual arrangements … longer term contractual arrangements with farmers … it is a volume management issue and it is a cost issue for us as well.[31]

3.27 The ACCC's 2008 report of its grocery inquiry also discussed why processors tender to supply supermarkets' private label brands:

> In confidential evidence provided to the ACCC, processors indicated that the main reasons they pursued private label contracts were:
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> - overhead recovery—generating revenue through private label sales to contribute to fixed costs of running the business
> - supply relationships with retailers—supplying private label product provides a stronger relationship and possibly improves processors bargaining position in relation to branded products
> - volume—the volume of milk supplied through private label contracts provides some stability to the business.[32]

Implications for influence of the major supermarkets on the dairy industry

3.28 A number of arguments were put forward about how the major supermarkets can impact the dairy industry by affecting the overall value of the supply chain, the value of milk as a product and the incomes of farmers. These issues, in the context of the specific price cuts led by Coles, are explored in more detail in chapters 4 and 5.

3.29 There is limited direct evidence available regarding how the major supermarket chains can affect farm gate prices. To complicate matters, a number of

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30 Fonterra Australia, *Submission 81*, p. 1.

31 Mr Keith Mentiplay, Director, Technical and Business Development, National Foods, *Committee Hansard*, 9 March 2011, p. 73.

32 Australian Competition and Consumer Commission, *Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries*, July 2008, pp. 234–5.

seemingly conflicting statements have been made about how the major supermarket chains can directly and indirectly impact farm gate prices.

3.30 Coles has stated on a number of occasions that it is committed to absorbing the costs resulting from its milk price reductions, and that it does not have a 'direct influence over farm gate prices because Coles buys milk from processing companies, not from dairy farmers'.[33] ALDI also submitted that it:

> … has not, and is not considering passing on the costs associated with this price reduction onto our suppliers.[34]

3.31 Coles also noted that because its generic milk accounts for approximately four per cent of total Australian milk production, 'this suggests that Coles, by itself, does not have a material influence over Australian milk prices'.[35]

3.32 However, Coles' share of the drinking milk market is significantly higher, at about 17 per cent.[36] While it may be the case that the influence the major supermarkets have in the manufacturing milk states is restricted by the nature of that market, the major supermarkets appear to have a greater influence on the value of the supply chain in the drinking milk production focused regions of Australia. Also, the observation that Coles' competitors seemingly had no choice but to immediately match Coles' price cuts, while perhaps supporting arguments of robust competition existing in the grocery market, demonstrates Coles' influence on suppliers, such as in the drinking milk market.

3.33 Woolworths made similar statements about its contractual arrangements:

> Woolworths has no contractual arrangements with Australian dairy producers. Woolworths does not have any insight into, or control over, the contractual arrangements, such as price, that dairy processors enter into with dairy farmers. That is, Woolworths has little or no ability to directly influence the farm-gate price paid to dairy farmers by processors. To the greatest extent possible, however, Woolworths does look to support farm-gate price through ensuring that it does not enter into a Private Label milk contracts that would, based on Woolworths' estimates, result in a dairy farmers receiving less than an economic return for their milk.[37]

3.34 Revealingly, however, Woolworths did not share Coles' view on the cost of the retail price cut being absorbed. Woolworths has made a number of public statements, including in its submission to this inquiry, which raised concerns that the

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33 See Coles, *Submission 131*, p. 10; Coles, 'Coles Milk Pricing Fact Sheet', www.coles.com.au (accessed 25 February 2011).

34 ALDI Stores, *Submission 61*, p. 2.

35 Coles, *Submission 131*, p. 12.

36 Coles, answer to question on notice, 29 March 2011 (received 19 April 2011), p. 6.

37 Woolworths, *Submission 98*, p. 2.

price cuts are unsustainable for the Australian dairy industry. Woolworths explained in its submission:

> … we are specifically referring to the fact that this price move has effectively re-based the price of white of milk across Australia overnight, and for an unknown period into the future, which also potentially devalues the whole milk category in the eyes of the consumer. In effect, the consumer baseline for price is now at 1990s levels, but with 2011 input costs for all parts of the supply chain.[38]

The tender process for private label contracts

3.35 The supply of private label milk, and the tender process associated with the contracts to supply it, raises questions about the degree of direct and indirect influence the major supermarket chains may have on the prices paid to farmers. Some instances of indirect influence are clear—the shift in demand from branded milk to private label products as a result of the price cuts particularly affects farmers on contracts that are structured to balance these prices. This will be discussed in more detail in chapter 5.

3.36 Woolworths' described its tender process to the committee:

> The information that we provide to the processors when we are establishing the tender for milk is the volume of milk that we sell. We provide that information on a national basis, on a state basis and on a regional basis, to all of those suppliers. So we are actually providing the volume of white milk that we sell for a private label product. We are not communicating to the processing partners the price of what we sell product for. It is a volume based tender process.[39]

3.37 Given the limited number of private label contracts available, and the volumes associated with them, it is clear that there is a strong incentive for processors to win a contract to avoid uncertainty in their business and significant adjustment of their operations. Accordingly, one dairy farmer described the tender process as 'a race to the bottom':

> The processors are just putting in a price, as low as they think they possibly can go.[40]

3.38 When it was suggested that the processors are not compelled to supply milk to the major supermarkets at such a low price, the same witness argued:

> Who is their other market? We have National Foods with a billion litres, if they do not supply Coles and they do not supply Woolworths, who are they

38 Woolworths, *Submission 98*, p. 2.

39 Mr Pat McEntee, General Manager, Fresh Foods, Woolworths, *Committee Hansard*, 29 March 2011, p. 4.

40 Mrs Lynne Strong, Co-owner/operator, Clover Hill Dairies, *Committee Hansard*, 10 March 2011, pp. 66–7.

going to sell that billion litres to? You do not turn round overnight and become an exporter. That takes major capital investment.[41]

3.39 Paragraph 3.34 noted Woolworths' view that the recent price cuts put the consumer baseline for retail milk prices at 1990 levels. Perhaps in a further admission of the direct influence on farm gate prices that the supermarkets can have through the tender process, Woolworths' submission also included a warning about future contract negotiations and outcomes:

> Ultimately, these prices set a new benchmark, and can be expected to flow back to processors and farmers as new supply and pricing agreements are negotiated over the coming months and years.[42]

3.40 The meaning and intent behind this statement was pursued at Woolworths' appearance before the committee:

> Senator O'BRIEN—… Is it not fair that I take that to mean that Woolworths—and your competition as well, I expect—will be forced to seek lower prices to retain a reasonable margin on the product that you sell in your supermarket?
>
> Mr McEntee—I think the context in which our submission was written was in relation to the concerns we have with the changing mix of private label milk at retail and the flow-on effects back through the supply chain. Woolworths will always negotiate vigorously on behalf of our customer to offer best value, but our concerns within—
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> Senator O'BRIEN—Is your submission right or not? Do I understand wrongly? Can you explain it to me in any different way? It seems to be saying very clearly that you are going to have to negotiate a lower price. I just want you to be clear with us. Is that what you are saying or not?
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> Mr McEntee—What I am saying is that I believe the context in which the submission was written is agreeing with our concerns about the flow-on effect back through the supply chain in milk.
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> Senator O'BRIEN—The flow-on will go back through the supply chain, so prices will go down in the supply chain.
>
> Mr McEntee—Will flow right through the supply chain.
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> Senator O'BRIEN—So prices will go down in the supply chain. That is what you are saying, isn't it?
>
> Mr McEntee—Potentially it will.
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> Senator O'BRIEN—Potentially? So the alternative is that they will stay the same, is it, or will they go up? Is there potential for them to rise?

41 Mrs Lynne Strong, Co-owner/operator, Clover Hill Dairies, *Committee Hansard*, 10 March 2011, p. 68.

42 Woolworths, *Submission 98*, p. 3.

> Mr McEntee—As previously discussed, the way in which the processor will submit pricing to Woolworths will be based on their costs and the cost of production back to us.
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> Senator O'BRIEN—So if the prices to the processors were to go up and the processors' price to you, by that necessity, had to go up, does that mean that the price of milk in the supermarket would have to rise?
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> Mr McEntee—The price at the supermarket is dictated by the market price. So, clearly, there are two differences here: there is the cost of product and there is the sell price of the product. Sell prices are dictated by the market. We have a central manner in which we check competition prices on a regular basis. Our commitment to our customers is to provide the best value Therefore, where the market price is on key value items is where the retail sales will be. It is a separate discussion from negotiating the cost price of goods.
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> Senator O'BRIEN—So you could be selling at a loss?
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> Mr McEntee—We would not sell at a loss.
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> Senator O'BRIEN—So if the price goes up, you will have to put your price up at some point? They are contradictory positions that you are putting to us, in a sense, and I am trying to tie you down to a response. Clearly, you have to have flexibility in the market, but if your position is that you have to make a profit on the product and the price has to go up, at some stage the price has to go up, doesn't it?
>
> Mr McEntee—As you would appreciate, I do not think I can predict pricing in a public forum. There are laws that stop me from doing that.[43]

3.41 On the other hand, there are clear restrictions on any influence the major supermarkets may have. A strong consumer preference for fresh milk will likely mean that the supermarkets will have to continue providing it. An official from Treasury noted:

> … it would be an interesting strategy for a supermarket to attempt to steer things in a direction where they are not supplying that milk while others continue to do so. They could be taking themselves out of a market which continues to reflect customer demand.[44]

3.42 Further, given the perishable nature of the product, supermarkets cannot realistically import fresh milk:

> … the milk has to come from somewhere. The only place that the milk can come from is from dairy farmers in Australia.[45]

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43 Mr Pat McEntee, General Manager, Fresh Foods, Woolworths, *Committee Hansard*, 29 March 2011, pp. 11–2.

44 Mr Brad Archer, Department of the Treasury, *Committee Hansard*, 10 March 2011, p. 5.

45 Professor Stephen King, *Committee Hansard*, 10 March 2011, p. 43.

Other factors

3.43 Some of Coles' statements and actions, however, suggest that it can *directly* influence farm gate prices:

> In an effort to ensure retail milk price reductions would not adversely impact farmers and to demonstrate our commitment to sustainable dairy farming, we increased the contract price paid to milk processors shortly before the "Down Down" price reductions on Coles brand milk.[46]

3.44 In February 2011, Coles announced that they had increased the price paid to WA milk processor Brownes Dairy (owned by Fonterra) by five cents a litre 'to ensure WA dairy farmers are not impacted by Coles' recent cuts to its retail milk prices'.[47] Coles explained this action in their submission:

> In mid-January 2011, Fonterra offered Coles a lower price as part of the competitive tender in Western Australia. In February 2011, Coles subsequently offered to pay Fonterra an additional five cents per litre if it passed that money direct to their dairy farmer suppliers in WA. Initially, Fonterra decided not to pass on this increase to WA dairy farmers but has now agreed to do so.[48]

3.45 In perhaps another acknowledgement of its ability to directly influence farm gate prices, in a letter to the committee chair the Managing Director of Coles remarked:

> In a theoretical worst case scenario, milk processors [sic] margins would be affected by no more than a few cents per litre. Given Coles has just paid them an equivalent price increase there is absolutely no excuse for processors to squeeze farm gate prices. Processors [sic] profit margins are already higher than our own in any event.[49]

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46 Coles, *Submission 131*, p. 14.

47 Coles, 'Coles Milk Pricing Fact Sheet', www.coles.com.au (accessed 25 February 2011).

48 Coles, *Submission 131*, p. 10.

49 Mr Ian McLeod, Managing Director, Coles, letter to Senator Alan Eggleston dated 18 February 2011, *Additional information 1* [p. 2].