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Sent: Friday, 2 December 2016 4:43 PM
To: DIT
Cc: Craig Perkins; Tom Black (tomblacktas@gmail.com)
Subject: Legislative Council Select Committee - Dairy Industry in Tasmania Legislative Council SUBMISSION
Attachments: Dairy Tasmania Critical Issues Paper 2016 FINAL.pdf

To the Secretary, Legislative Council Select Committee - Dairy Industry in Tasmania Legislative Council, Parliament House,

Please find attached the RDA Tasmania Critical Issues Paper written in response to the impact on the Tasmanian dairy industry of the processor price cuts in May this year.

The purpose of the paper was to objectively summarise the issues and provide comment on the role of that government in supporting industry. It was widely distributed at the time of publication in July 2016. RDA Tasmania's role is not to be the expert in every issue or industry. As a neutral organisation, our value is being able to provide objective data and comment and facilitate communication across a range of government, industry and community stakeholders. As such, the value of our submission is more this summary document than specific recommendations.

However, in relation to the Terms of Reference of the Legislative Council Select Committee, we can provide the following response:

1. Marketing opportunities for the Tasmanian Brand

We are not the organisation to provide recommendations on marketing and branding.

2. Processing opportunities in Tasmania

This issue is specifically addressed in our paper (Page 18). The information provided includes the following suggestion:

In order to develop the processor market and protect farmers' interests, the following could be considered:

- o Encouraging additional capital investment into existing farms (expansion and upgrade)*
- o Government consider ways to invest in support infrastructure (energy, roads and irrigation) to aid expansion to improve productivity and logistics*
- o Identification of greenfield sites for high value processing plants*
- o Future processing focused on Tasmanian brand and higher value*

3. The role of the Tasmanian government

The Conclusion of our paper includes the following:

Government and public reaction to the milk price drop has been positive and commendable...Dairy in Tasmania has demonstrated that the underlying support mechanism to help the industry through crisis is strong. The actions of milk processors, industry organisations and government have provided assistance to farmers and could be used as a model for other industries.

The question is which support mechanisms are required in the longer term – a question which RDA Tasmania is not the most appropriate organisation to answer.

I trust that you may find the paper of assistance and we look forward to hearing the outcomes of the Select Committee inquiry.

Yours sincerely,

Jen Newman

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Critical Issues Paper

Dairy Industry in Tasmania

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Stanley farm animals courtesy of Tourism Tasmania Visual Library



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Premise

The dairy industry in Tasmania is a significant contributor to the state's economy with 440 working farms contributing over \$425 million per annum. The May 2016 drop in milk prices came at the end of a dry year with high costs and has been compounded by record-breaking floods in June 2016, resulting in loss of livestock, equipment, roads, bridges and houses. The combined impact of these events has become a critical issue for Tasmania.

At the time of writing, (5 July 2016) the scale of the longer term impact on the Tasmania dairy industry is uncertain. For some businesses already struggling to break even, the compounding factors of dry conditions, the drop in milk price and recent destructive flooding may be insurmountable.

This document has been prepared to provide an overview of the issue as it effects Tasmania; consider how these current circumstances eventuated; and summarise what options are available to assist farmers back to prosperity for the long term.

Acknowledgment

RDA Tasmania wishes to acknowledge the input from the Tasmanian Farmers and Graziers Association, Dairy Tasmania, Rural Business Tasmania and AgriGrowth Tasmania.



Background

Dairy industry since deregulation

The deregulation of the Australian dairy sector started in 1999 and included the repeal of existing state legislation regulating the supply and pricing of milk. The impact of deregulation was mixed across Australia, but the total number of dairy farmers declined from around 10,000 in 2000 to about 6,061 in 2016. Despite increases in the overall size of dairy farms, most remain small-scale, family owned businesses. The picture is changing slightly in Tasmania whereby more large scale dairy farms are evident with larger herd sizes (of around 380 head). Since deregulation, milk production in Tasmania has more than doubled, while nationally production has reduced.

Dairy farming requires higher levels of capital investment than most other agricultural sectors. Milk is essentially a global commodity and most dairy farmers are price takers.

Murray Goulburn

Murray Goulburn sources milk from about 21 per cent of Tasmanian dairy farmers.

Murray Goulburn Co-operative Co Limited is a public company that was formed as a cooperative in Victoria in 1950, and become the nation's largest dairy company by 1973. In its 2015 annual report it recorded total assets of over A\$1.84 billion and total revenues of A\$2.88 billion¹. It was estimated in (early) 2016 to hold over 42 per cent of the national market for milk powder and 31 per cent of the national market for milk and cream². Over half Murray Goulburn's revenue comes from exports, primarily into Asia and the company is the nation's largest buyer of raw milk³.

Cooperative enterprises are owned by their customers in a democratic membership; however, the Murray Goulburn Unit Trust (MGC) partially listed on the Australian Securities Exchange (ASX) on July 3 2015 and is now a listed cooperative. Non-voting shares were issued (209 million), with the balance of shares still held by more than 2600 farmers who own the cooperative and supply it with 3.5 billion litres of milk annually⁴. Return to farmers is now linked to the share price. Contracts with the company for raw milk supply include the potential for retrospective price variation at the end of the financial year.

Milk Prices

Murray Goulburn (MG) has had a goal of keeping the farmgate milk price at around \$6 per kg/MS (milk solids) and reported in the 2015 Annual Report⁵ that:

While the final price was lower than the 2013/14 record closing price, it was very pleasing to be able to hold to a final price of \$6.02 per kgms, the third highest MG farmgate price on record.

It appears that the anger over the recent announcement is heightened because of continued assurances by Murray Goulburn that the price would not drop despite a global downturn. Murray

¹ <http://www.mgc.com.au/media/28754/MG-Annual-Report-2015.pdf>

² <http://www.ibisworld.com.au/industry/industryreports.aspx?indtid=87&indpid=2086>

³ <http://www.ibisworld.com.au/car/default.aspx?entid=1103>

⁴ <http://markets.theaustralian.com.au/shares/MGC/mg-unit-trust>

⁵ <http://www.mgc.com.au/media/28754/MG-Annual-Report-2015.pdf>



Goulburn (former) CEO, Mr Gary Helou announced at the Global Food Forum in Melbourne as recently as 21 April 2016 that Murray Goulburn⁶:

expected to maintain its price at \$5.602 per kilogram in 2016, at the bottom end of the previous guidance provided of \$5.60-\$5.90.

Six days later, on 27 April 2016, Murray Goulburn announced it will cut its milk price for suppliers to between \$4.75-\$5.00 (retrospective across the 2015-2016 financial year), with chief executive Gary Helou and chief financial officer Brad Hingle also announcing their departure⁷. Three directors have since announced their resignation from the board and the share price fell from \$2.14 on 27 April 2016 to \$1.00 as at 30 May 2016.

Class Action

On 16 May 2016, a class action was filed against Murray Goulburn Co-operative Co. Limited (MG) and MG Responsible Entity Limited, as responsible entity of the MG Unit Trust, and a number of current and former directors in the Supreme Court of Victoria. The statement of claim alleges contraventions of the Corporations Act through allegedly misleading or deceptive statements made in a Product Disclosure Statement (PDS) issued on 29 May 2015, and in subsequent market announcements. The proceeding purports to be brought by the lead plaintiff on behalf of unit holders who purchased units pursuant to the PDS and/or in the period “on or after 3 July 2015 and prior to the commencement of trading on 29 February 2016” and who held any of those units at the commencement of trading on 27 April 2016. The companies strongly deny there is a proper basis for this claim, and will vigorously defend the proceedings⁸. The impact of this class action on the Tasmanian dairy industry is unknown.

Flow on pricing effect

The drop in price from Murray Goulburn has flowed through to the rest of the market with Fonterra and to a lesser extent with Lion Dairy and Cadbury announcing subsequent price drops. Murray Goulburn and Fonterra are estimated to make up approximately 21 per cent and 55 per cent of the Tasmanian raw milk market respectively⁹.

Fast Facts on Dairy in Tasmania

Industry Profile

Over the past 10 years, milk production in the Tasmanian Dairy Industry has continued to grow at an average rate of close to 5 per cent per annum. There has been a 43 per cent increase in production over the last 10 years compared to a national decrease of 4 per cent. Tasmania is the only state of Australia to show growth. Growth is based around sustainable farm management practices, efficient on farm production systems and a relatively favourable climate for pasture based dairy farming.

⁶ [Link to resource](#)

⁷ <http://www.abc.net.au/news/2016-04-27/murray-goulburn-price-drop-helou-departure/7361654>

⁸ <http://www.aspecthunting.com.au/asxdata/20160517/pdf/01741355.pdf>

⁹ Estimations from State Government

The Tasmanian dairy industry produced a record 891 million litres of milk off 440 dairy farms in 2014/15. 2015/16 has been a challenging season with exceptionally dry and warmer conditions. Tasmania now produces over 9 per cent of the nation's milk¹⁰ (year to date production is up 1.3 per cent on 2014/2015). Dairy farming in Tasmania occurs throughout the state but mainly across the north and the average age of dairy farmers is 53 years of age¹¹.

The Southern Hemisphere's largest dairy farming operation, VDL Company was recently sold to Chinese investors for \$280 million¹² with the investors keen to expand the farming operation both domestically and internationally.

The majority of milk produced in Tasmania goes to further processing of milk powders, cheeses, yogurt and other products.

Milk Processors in Tasmania¹³

Processor	Proportion of state milk
Fonterra	55%
Murray Goulburn	21%
Lion Dairy & Drinks	14%
Cadbury (Mondelez)	8%
Other	2%

Tasmania's main fresh milk producers are Betta Milk and Pura Milk. Smaller scale, niche producers such as Ashgrove Farm Milk are also gaining traction but on a much smaller scale.

Betta Milk is a Tasmanian owned and operated cooperative established in 1956. While Betta Milk only produces 12 million litres (plus) of liquid milk (approximately 1 per cent of local production), the business makes up about 40 per cent of branded fresh milk sales in Tasmania¹⁴.

Pura Milk, another significant brand of fresh milk in the state, is owned by Lion Dairy & Drinks (formally National Foods) which is owned by the Japanese company Kirin Holdings Co. Ltd.

2015/2016 Season

In the Dairy Australia survey data in February/March 2016, before price cuts and flooding, almost all Tasmanian respondents (93 per cent) had realised an operating profit in 2014/2015. Only 60 per cent expected to do so in 2015/2016 which will impact on the proportion investing on-farm. Dry conditions had resulted in 4 in 10 respondents planning to invest in irrigation. The average milking herd size in Tasmania continues to be the largest nationally and average production levels in respondent herds had been reasonably stable¹⁵.

¹⁰ <http://www.intodairy.com.au/index.php/tasmanian-dairy-industry>

¹¹ <http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/S%20and%20O/2016-06%20S%20and%20O/2016-06%20Situation%20and%20Outlook.pdf>

¹² <http://www.theaustralian.com.au/business/companies/sale-of-tasmanias-van-diemens-land-company-to-chinese-approved-by-government/news-story/3ab349972d094cdc411763124217196f>

¹³ Tasmanian Government Tasmania's dairy regions A guide for investors April 2016 – figures are an estimate and indicative only.

¹⁴ <http://bettamilk.com.au/betta-milk-history/> and pers. comm.

¹⁵ <http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/S%20and%20O/2016-06%20S%20and%20O/2016-06%20Situation%20and%20Outlook.pdf>

Tasmania saw milk production hit by a hot, dry season that has caused ongoing tightness in feed supplies and affected farmer profitability, despite good rainfall in February. Production rebounded in March, up 4.1 per cent¹⁶, but recent floods will have a significant impact on production for June and into the next financial year.

Table 1: Farm and cow numbers by region, April 2016¹⁷ (pre: price drop)

Region	Number of dairy farms	Number of cows	Average herd size
Far North West	149	68 741	460
North West	100	28 659	286
Central North	89	36 383	409
North East	67	24 383	364
South	14	5 625	401
King Island	13	3 585	275

Table 2: Financial performance, Tasmania dairy industry, 2013-2014 to 2015-16, average per farm¹⁸

Performance indicator	units	2013-14	2014-15p	RSE	2015-16y
Total cash receipts	\$	1 115 710	1 162 600	(6)	1 107 000
Total cash costs	\$	877 580	940 800	(7)	975 000
Farm cash income	\$	238 130	221 800	(10)	132 000
Farms with negative farm cash income	%	0	6	(83)	17
Farm business profit	\$	123 100	112 700	(24)	- 5 000
Profit at full equity - excluding capital appreciation	\$	258 530	256 900	(14)	146 000
Farm capital at 30 June a	\$	5 684 980	6 403 300	(9)	na
Farm debt at 30 June b	\$	1 740 440	1 728 600	(14)	1 851 000
Equity ratio b	%	69	73	(4)	na
Rate of return - excluding capital appreciation c	%	4.7	4.1	(14)	2.2
Off-farm income of owner manager and spouse b	\$	6 730	35 700	(81)	na

Note: a Excludes leased plant and equipment. b Average per responding farm. c Rate of return to farm capital at 1 July. p ABARES preliminary estimates. y ABARES provisional estimates. na Not available. RSE Relative standard errors, expressed as a percentage of the estimate provided.
Source: ABARES Australian Dairy Survey

2016/2017 Milk Prices

New milk prices for the 2016/2017 financial year have been announced.


Murray Goulburn has an opening price for 2016/2017 of \$4.31 per kilogram of milk solids, the lowest it has been since 2009, with a \$4.80 finishing price. Fonterra has set an opening price of \$4.75, 44 cents higher than Murray Goulburn, with a \$5.00 finishing price expected. The cost of production for most Tasmanian farmers is estimated to be about \$5 per kilogram¹⁹.

¹⁶ http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/S%20and%20O/2016-06%20S%20and%20O/SandO_June16_WEB.pdf

¹⁷ http://www.intodairy.com.au/images/stories/pdf/DTAS15019_Tasmanias_Dairy_Regions_En_20160406_Web.pdf

¹⁸ Australian Bureau of Agricultural and Resource Economics and Sciences; Agriculture, Fisheries and Forestry in Tasmania, April 2016 – pre the price drop announcement

¹⁹ <http://www.abc.net.au/news/2016-06-28/murray-goulburn-makes-major-price-announcement/7535602>



Lion Dairy & Drinks (Lion) has announced an opening variable milk price of \$5 a kilogram milk solids for its direct milk suppliers in Victoria, Tasmania and South Australia. Since 2013, Lion has offered its suppliers the option to lock in all or part of their price on 50 per cent of the milk produced. The majority of Lion's suppliers have opted to secure all, or part of their pricing for up to three years and contracts from previous years have been carried over. As a result, the majority of direct suppliers in the southern region can expect an average price of \$5.67 per kilogram of milk solids²⁰.

National Market and Forecast²¹

Dairy Australia provides an overview of the national market in their publication 'Dairy Situation and Outlook, June 2016'. Confidence amongst farmers as measured by the National Dairy Farmer Survey (NDFS), fell significantly from 2015 to 2016. The annual survey, conducted in February and March, showed a decline in the proportion of farmers feeling positive about the future of the industry from 74 per cent to 67 per cent. More recently, late season cuts to farmgate prices have caused a significant decline in sentiment across most regions, which are currently being quantified through follow up research.

A global market turnaround remains some way off, though the Australian market remains stable. Australian milk production has continued to track below prior-year levels since early spring 2015, with most regions experiencing difficult seasonal conditions in addition to challenging margins. March data shows a 1.1 per cent drop over the nine months since June 2015, with intakes for the month of March down 4.6 per cent compared to last year. A late autumn break, persistently high feed costs, and other issues such as pasture pests and herd health problems have also contributed²².

An already challenging season became significantly more difficult during April and May, as late-season farmgate price cuts were announced for most farmers in the southern, export-focused regions. The impact of these developments continues to unfold, and the process of revising budgets and strategies to accommodate sharply lower late season incomes has begun.

The latest Dairy Australia update suggests:

- Overall, margins have been significantly tighter through 2015/16; squeezed by both higher costs and lower income.
- Income for many farmers will fall below the previously assumed base case of a farmgate price around the 2015/16 opening level for the final months of the season.
- Although some easing of costs during the 2016/17 season is likely, a weak milk price suggests that margin pressure will intensify – at least through the first half of the year.
- An earlier than expected commodity price recovery may provide relief in the second half of the season, but either way, cash flow challenges through spring will present a significant hurdle for many farms.

Global Market

Globally, the volume of dairy products traded grew by 5.8 per cent over the past twelve months, with a recovery in demand from Greater China accounting for much of this growth. Exports to Greater

²⁰ <http://adf.farmonline.com.au/news/magazine/industry-news/general/lion-announces-opening-price-of-5kg/2753099.aspx>

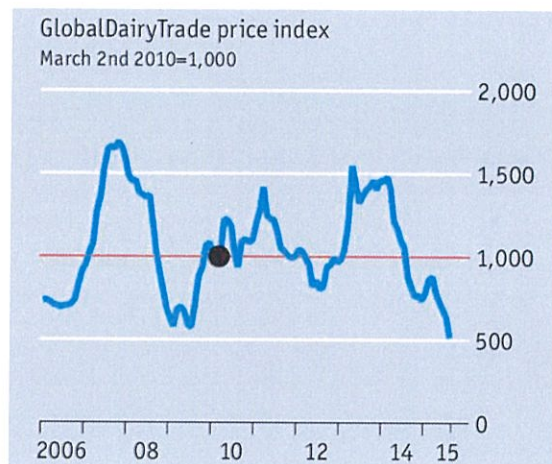
²¹ http://www.dairyaustralia.com.au/~/_media/Documents/Stats%20and%20markets/5%20and%20Q/2016-06%20S%20and%20Q/2016-06%20Situation%20and%20Outlook.pdf

²² http://www.dairyaustralia.com.au/~/_media/Documents/Stats%20and%20markets/5%20and%20Q/2016-06%20S%20and%20Q/SandO_June16_WEB.pdf

China (PRC, Macau and Hong Kong) grew by 16 per cent in volume terms over the twelve months to February 2016. Australian export volumes to Greater China grew by 21 per cent, while the value of Australian exports increased by 29 per cent year-on-year, with strong growth in high value categories such as liquid milk and infant formula.

Higher production costs for Chinese dairy farmers, combined with low international prices for dairy commodities have constrained local production and led to a recovery in demand for dairy imports. Within China, the government has encouraged continued improvements in the national herd genetics through the import of live dairy cows (of which Australia is the largest supplier)²³.

Overall volumes to Southeast Asian countries continued to grow, with strong growth in milk powder categories, while exports volumes to the Middle East and Japan have eased slightly. Despite the increase in volume, value of global exports fell by 9 per cent, with falls across all major markets. Demand from Russia, previously the world's second largest single country dairy market, has collapsed following the embargo on western exporters. Mexico has since assumed this title, with strong growth in (mainly US) import volumes²⁴. The global price index has fallen to its lowest point in ten years (see graph²⁵).



In New Zealand, dairy farmers are facing the lowest milk prices in almost a decade after major processor Fonterra announced the forecast farm gate milk price for the 2015/16 season has dropped from NZD\$4.15 per kg to NZD\$3.90 per kg²⁶. Fonterra is expecting global dairy pricing to gradually improve over the season and an opening price of \$4.25 kgMS has been announced for 2016/17.²⁷

²³ http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/S%20and%20O/2016-06%20S%20and%20O/SandO_June16_WEB.pdf

²⁴ <http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/S%20and%20O/2016-06%20S%20and%20O/2016-06%20S%20and%20O/2016-06%20Situation%20and%20Outlook.pdf>

²⁵ <http://www.economist.com/news/business/21660995-boom-turns-bust-global-milk-prices-slump-turning-sour>

²⁶ <http://www.abc.net.au/news/2016-03-10/tas-country-hour-tuesday-8-march-2016/7230434>

²⁷ <https://www.fonterra.com/au/en/hub/sites/news+and+media/media+releases/fonterra+announces+forecast+farmgate+milk+price+for+201617+season/fonterra+announces+forecast+farmgate+milk+price+for+201617+season>



Social Impact

At a regional level, an economic or environmental crisis can have long-term social implications seen in the regression of development indicators like population, employment and asset values²⁸, but it is at the personal level that Australians often witness the magnitude of a crisis.

Health and Wellbeing

Environmental challenges as well as changes in the economy and commodity pricing in agriculture particularly affect people in rural and remote communities. Bankruptcy, unemployment and financial difficulties can lead to depression and hopelessness and are all known risk factors for suicide. Other factors such as relationship conflict or breakdown, gambling or substance abuse also increase.²⁹

Coinciding with the drop in milk price, Rural Alive and Well (Tasmania)'s outreach program reports a 28 per cent increase in clients in the month of April, 2016. Record dry conditions in the 12 months since May 2015, have contributed to an increase in total case load of 46 per cent. Rural Business Tasmania, which delivers the Rural Financial Counselling Service in Tasmania, has also seen a 47 per cent rise in demand from farmers for support and assistance.³⁰ Dairy farms in the north west and north account for nearly all of the rise in demand.

Given the recent floods, this demand can only be expected to increase.

Community Implications

Dairy farms are pillars of the community in many parts of Tasmania. A contraction in the profitability or even the number of dairy farms will extend social pressures on communities as they experience a decrease in expenditure and employment.

Regional Tasmania is characterised by low labour force participation, low educational attainment, lower wages and a dispersed population which complicates the challenge of growing the economy.³¹

The compounding factors of dry weather, floods and the cut in milk price have hit communities where dairy has been a profitable, growth industry. The opportunity of investing in dairying has been attractive because of increased access to irrigation, increased demand for product and slow growth in some other sectors of the Tasmanian economy. The more efficient and effective the recovery of the dairy industry proves, the better the prospects for those businesses, communities and individuals affected.

Loss of labour will be an issue. In recent years the dairy industry re-skilled and employed Tasmania forestry workers, but as dairy farms release these workers they are returning to a resurgent forestry industry.

Social Impact Mitigation

Many people from rural and remote communities prefer to focus on finding solutions, rather than dwelling on problems and difficulties.³² Rural Alive and Well (Tasmania) and Rural Business Tasmania


²⁸ Otker-Robe and Podpiera; The Social Impact of Financial Crises: Evidence from the Global Financial Crises; The World Bank; November 2013

²⁹ <http://livingisforeveryone.com.au/uploads/docs/LIFE-Fact%20sheet%202018.pdf>

³⁰ Roger Hanson, The Mercury, Tuesday 24 May 2016

³¹ RDA Tasmania, Regional Plan 2015-16, August 2015

³² <http://livingisforeveryone.com.au/uploads/docs/LIFE-Fact%20sheet%202018.pdf>



provide support to farmers and rural communities that help build resilience such as financial planning, coping techniques and by directing individuals to available support programs.

The Tasmanian community has become engaged with the issue of the retrospective price cuts and there has been a rise in support for Tasmanian brand dairy products³³ and donations to the Rural Relief Fund.

Additional funding commitments made by the Tasmanian and Australian Government to support services are welcomed and are summarised below.

State Government: The Tasmanian Government will provide \$569,000 in 2016-17 to Rural Alive and Well (an extra \$100,000 to Rural Alive and Well outreach services in addition to their existing \$1 million funding commitment) and an increase in funding to the Rural Financial Counselling Service from \$40,000 to \$85,000 over the next three years.³⁴

Australian Government³⁵: An additional 9 Rural Financial Counsellors will be deployed in Tasmania, Victoria, South Australia and New South Wales with \$900,000 of additional funding. Tasmania has received 1.5 FTE in additional Counsellors.

The Department of Human Services Farm Household Allowance scheme will fast track applications with 18 more staff made available to process claims, and the department has appointed a Dairy Industry Liaison Officer. Two Department of Human Services Mobile Service Centres have been redirected to dairy regions. They are currently travelling through Victoria and South Australia and it is unclear at this stage if they will come to Tasmania.

Business: Coles supermarkets has announced a consumer-driven milk fund that will pay 20 cents a litre to an independent fund aimed at supporting the 2,600 Murray Goulburn farmers in Victoria, NSW and Tasmania effected by the May 2016 price cut. However, it is expected to take two or three months to get the new brand on sale³⁶.

Community³⁷: The Rural Relief Fund provided by Rural Business Tasmania offers grants of up to \$2500 for crisis relief gifted to eligible farming families. Family and animal welfare is a priority and funds can cover everything from basic household goods including food to utility bills to the repair of damaged fences. Public donations are invited to support the grants that were originally established by Rural Business Tasmania and the state government in response to the prolonged dry season. Approximately \$100,000 in grants have been approved mainly for electricity, grain feed, fencing, food vouchers and veterinary expenses. Recipients are predominantly in the north west.

A rural stakeholder forum of 21 key organisations was initiated following the milk price cuts and is chaired by Rural Business Tasmania. They help mitigate the impact by collaborating on priorities, sharing information and combining resources.

³³ <http://www.examiner.com.au/story/3922931/ashgrove-milk-walks-off-shelves-in-support/?cs=95>

³⁴ http://www.premier.tas.gov.au/releases/additional_funding_to_help_support_our_farmers, 24 May 2016

³⁵ <http://www.ericthutchinson.com.au/news/news/support-for-dairy-farmers/>

³⁶ <http://www.abc.net.au/news/2016-05-17/new-coles-milk-brand-to-raise-20-cents-a-litre-for-farmer-fund/7420320>

³⁷ <http://www.ruralbusiness Tasmania.org.au/Relief-Fund>

Support for farmers requiring financial assistance

Murray Goulburn customers are now in the position of either paying back income received over the year; foregoing income for a period to compensate for the debt now owed; or continuing to receive income that will need to be repaid over a 3-4 year period. Following is a summary of support offered:

Murray Goulburn³⁸

Murray Goulburn reduced its farm-gate price from an average of \$5.60 to \$4.75-\$5.00 (retrospective over the 2015/2016 year) after it said it would struggle to meet even half of the profit forecast outlined in its prospectus for its partial float on the ASX in July 2015. Murray Goulburn has offered a "milk supply support package" with a supported price for the season of \$5.49 a kilogram of milk solids. This supported price would be funded by Murray Goulburn and is expected to cost between \$100 million and \$170 million.

Suppliers in Tasmania would be required to pay back this support package which will cost \$0.18-\$0.24 a kilogram of milk solids for the next three financial years. Alternatively, suppliers have the opportunity to repay this loan by June 17 2016, with no deductions from milk cheques for the next three financial years.

Fonterra³⁹

Fonterra has an agreement to meet Murray Goulburn's prices under its supply agreement and cut its price from an average of \$5.60 to \$5.00 after the Murray Goulburn announcement. Additionally, it has reduced the price for May and June milk supplied.

Fonterra will offer farmers the Fonterra Australia Support Loan, of up to 60 cents a kilogram to maintain its \$5.60 average price. Farmers will have until the start of the 2018 financial year to start repaying the Fonterra loans, which will also accrue interest.

Dairy Recovery Concessional Loans⁴⁰


\$555 million in concessional loans have been announced, funded by the Australian Government and administered through State Government. These loans were made available while the federal government was in caretaker through the agreement of the Labour Party and an extension of the Droughts Concessional Loans Scheme to 1 November 2016. This scheme will be expanded to help dairy farmers who have had their incomes retrospectively cut by dairy processors Murray-Goulburn and Fonterra in South Australia, Victoria and Tasmania.

It is understood that Victoria has been offered \$30 million, New South Wales \$10 million, Tasmania \$10 million and South Australia \$5 million in the first round of federal dairy support loans. The remaining \$500 million loan fund is money already allocated to the Droughts Concessional Loan Scheme to June 2018.

³⁸ <http://www.mgc.com.au/media/34552/MSSP-Opt-out-Letter-to-Suppliers-FINAL.pdf>

³⁹ <https://www.fonterra.com/au/en/hub/sites/news+and+media/media+releases/fonterra+australia+revises+milk+price+for+may+and+june+2016+and+introduces+support+loan/fonterra+australia+revises+milk+price+for+may+and+june+2016+and+introduces+support+loan>

⁴⁰ <http://www.malcolmturbull.com.au/media/the-coalition-will-guarantee-support-for-australian-dairy-farmers> and Department of State Growth



Dairy farmers will be able to apply for loans of up to \$1 million, or half what they owe, whichever is less. Although the loans are concessional, they are not interest free. From August 1, the interest rate on the loans will be 2.66 per cent and offered over a 10-year term⁴¹.

While the announcement has been welcomed, there is concern that already overstretched farmers may not benefit from further debt. Loans will still require assets and security with appropriate asset to debt ratios. With dairy industry prices falling, asset values are down and highly leveraged producers may not qualify for further debt, or have the capacity to service debt if it is approved. This risk will need to be managed by administrators when considering applications for loan relief.

Dairy Australia's 'Tactics for Tight Times' programme⁴²

\$900,000 has been provided for the Dairy Australia / DairyTas programme offering financial advice and management support to dairy farmers. The main component of this is the "Taking Stock" program which provides individual farm advice around business and financial management looking at the performance of the business and planning for the coming season. This and other relevant programs will continue into 2017 and be supported by the reallocation of \$140,000 of Tasmanian Government IntoDairy funds. In addition, DairyTas has conducted information sessions across the state on managing people, pasture management and surviving a low milk price season. DairyTas and the Tasmanian Government is working with the TIA Dairy Centre and other providers to deliver these services.

The Milk Price Levy debate⁴³

Some political and community response to the recent processor price cuts has been to propose a consumer levy of 50 cents a litre on milk sold in Australian supermarkets to help farmers. While the intention is positive, in practice it is difficult for government to re-regulate the industry and impose a levy on consumers to pay for an industry exposed to global commodity prices.

The Tasmanian Farmers and Graziers Association (TFGA) made the following comments:

From the TFGA Dairy Council's point of view a tax on milk makes no sense, particularly in Tasmania where only a small amount of the State's dairy production is consumed as milk. There is no purpose to punishing consumers in this way.

Better recognition of the value of our products may give us more leverage with the major retailers and processors in future.

Better that we continue to encourage consumers simply to buy more Australian dairy products, particularly branded products that put more money into the supply chain and into the state's economy.

Re-regulation of the dairy industry would set us back 20 years – to a time when our industry agreed that path was not our future. Not only would this further punish consumers, but it would also likely breach Australia's international trade obligations.

⁴¹ <http://www.abc.net.au/news/2016-06-01/dairy-concessional-loans-victoria-commonwealth/7465396>

⁴² <http://tftt.dairyaustralia.com.au/> and <http://www.dairytas.com.au/events/>

⁴³ <http://www.tfga.com.au/in-the-news/> - Andrew Lester

Supporting farmers wanting to grow their business

While it is important to recognise and support farmers who are already financially stretched and for whom this price decrease after a difficult, dry year may be too much to manage; thought should also be given to farmers who have managed their business well and who remain in a strong position. There is support available to assist farmers to improve efficiency, productivity and to focus on longer term investment.

State Government: The Tasmanian Government has available the AgriGrowth Loan to provide low interest loans for projects that advance the Government's agri-growth agenda as part of the Government's AgriVision 2050 plan to grow the value of the agriculture and agri-food sectors in Tasmania. Low interest loans ranging from \$30,000 and up to a \$1 million are available to Tasmanian farm or agri-food businesses who wish to invest in growing production and adding value to their product⁴⁴.

AgriVision 2050 initiatives will include the development individual and relevant strategic plans for each sector (for example, horticulture, red meat, dairy, viticulture, aquaculture, protected cropping, fibre and agri-tourism) and the integration of workforce needs/skills with vocational education/training⁴⁵.

Programs and activities under the State, Federal and industry-funded Into Dairy Project will continue to support and encourage growth in the dairy sector in response to long term demand for product.

Australian Government: has committed \$2 million to establish a commodity milk price index, although no detail is available at this stage.

NRM: Dairy Cares for the Derwent is a collaborative initiative from local farmers, Dairy Tasmania, Derwent Catchment NRM Committee, NRM South, Tas Water and both State and Federal Governments to ensure environmental sustainability underpins expansion of the southern Tasmanian dairy industry. A Fert\$mart nutrient management plan will be created as part of property management planning and will be regularly reviewed and actioned. All dairy farms will have best practice effluent management as part of their Fert\$mart approach⁴⁶.

⁴⁴ <http://dpiptwe.tas.gov.au/agriculture/government-and-community-programs/agrigrowth-concessional-loan-scheme>

⁴⁵ <https://www.tas.liberal.org.au/sites/default/files/policy/Cultivating%20prosperity%20in%20agriculture.pdf>

⁴⁶ <http://www.nrmsouth.org.au/wp-content/uploads/2015/11/Case-Study-Dairy-Cares-for-the-Derwent-2015.pdf>



Lessons learnt from the current crisis

Understanding the contributors to what has occurred

Within the context of agriculture's cyclical trends,⁴⁷ the current crisis owes much to the “glut” of milk in international markets including Europe – partially due to the Malaysian Airlines flight MH17 crash in the Ukraine which caused Russia to block European and Australian exports⁴⁸. Additionally, the removal of European Union (EU) milk quotas⁴⁹ has many farmers fearful of price falls as production increases in competition to Australian exporters. This comes after a period of high global prices.

While demand for Australian exports to Asia has increased, prices have decreased, which in turn has had an effect on domestic prices.

Locally, dairy farmers have been encouraged to invest in increased herds and new infrastructure to meet the projected increase in demand for dairy products.⁵⁰ This leaves many farm operations highly debt leveraged with falling margins and income. The average farm debt of Rural Financial Counsellor Service users is from \$800,000 to \$1 million. Banks have an interest in keeping farms operational because an increase in farms for sale could reduce land values and make the debt unserviceable. New entrants to the dairy industry have high establishment costs and take time to comprehend the challenges and fluctuations that determine their success.

Climatic and seasonal variations have surprised dairy farmers in the North West where dry conditions are unusual.

This downturn will not last indefinitely; however, milk prices are forecast to remain low in the short to medium term. The recent record-breaking flood event has come at just the wrong time, on top of a dry, expensive year and the retrospective price drop in milk prices. There may be a portion of farmers who choose to exit the industry rather than rebuild but it is believed these are farmers who were considering this before the milk price cut. Exiting isn't being encouraged because the market is predicted to be more certain by early 2017.

Contractual arrangements

Contracts for milk supply vary across farm suppliers and processors. Typical contracts include fixed term (three year) and single year supply contracts with a range of variable and fixed pricing. While the application of retrospective pricing in contracts has been criticised, it is not the only option available to farmers and in recent years has provided end of year bonuses.

There appears to be mixed opinion about the fairness of these contracts. While there has been calls for the retrospective element to be abandoned, this has been a source of additional 'bonus' income in recent years. If more of the market risk is moved from suppliers to processors, it could be expected to come with a price cut to reflect this shift in risk. For those farmers who have managed this risk effectively, a price cut imposed in this way may be a negative outcome.

⁴⁷ Productivity Commission, Trends In Australian Agriculture, 2005

⁴⁸ <http://www.theaustralian.com.au/news/inquirer/full-cream-crisis-for-the-dairy-industry/news-story/5c8ccb4ec73626aae7b1c9b5d7f28af8>

⁴⁹ <http://www.bbc.com/news/uk-32136218>

⁵⁰ <http://www.dairytas.com.au/plan/>



The following is a summary of contractual arrangements for the two largest raw milk purchasers in the state.

*Murray Goulburn*⁵¹

Murray Goulburn cooperative members have had a high (over \$6.00 per kilogram of milk solids) farmgate price for the last two years in addition to company dividends. In 2016, despite assurances, the price has been revised late in the contract period and is retrospective back to 1 July 2015.

All suppliers must be shareholders of the cooperative. A single base price for each month of the year is announced at the start of the financial year. The monthly milk solid price is available to all suppliers in the southern milk region. Monthly values may vary throughout the season as a result of price increases, including back-pays and step-ups or, in rare instances, price decreases. The aim is to provide a clear market signal to suppliers about the value of milk relative to when it is supplied. These varying monthly payments are built into the base price. In establishing these prices, returns to suppliers, as well as the costs associated with milk production across the year, had been taken into account.

*Fonterra*⁵²

Fonterra's Australian forecast monthly prices per kilogram of milk solids at the beginning of each financial year. Fonterra operates three sets of prices in Australia: one that is available to Victorian and Tasmanian suppliers and different prices for farmers in WA and NSW. The prices vary each month in line with the seasonal milk production curve.

In Tasmania, dairy farmers generally have the low milk production costs and the high productivity in spring, while the on-farm costs of producing milk are highest in autumn and winter. Fonterra offers higher prices outside of the spring months to provide a production incentive to suppliers. For Tasmanian farmers, the opening price at the beginning of the financial year has historically been a conservative estimate, then prices have usually increased incrementally across the season with what is known in the industry as 'step-ups' (farmgate milk price increases backdated to the beginning of the financial year). Fonterra's WA and NSW suppliers generally do not receive step-ups, although their set prices are traditionally higher.

While the step-up process generally provides price increases, a mid-season price drop occurred in 2008-09 due to the global financial crisis; and this retrospective downward adjustment has been repeated in the 2016 financial year. In 2015/2016 the Fonterra contract price was decreased from an average of \$5.60 per kilogram of milk solids to under \$5.00 and the 2016/2017 price is set at \$4.75 with an anticipated closing price of \$5.00 per kilogram of milk solids.

*Lion Dairy & Drinks (Lion)*⁵³

Lion offered three year contracts in 2014 that allowed farmers to choose from three options including a variable pricing model with a guaranteed safety net; a one year fixed price offer; and a three-year fixed price offer applied to up to 50 per cent of a supplier's total volume. Total contract terms of up to five years were available. The three year fixed price contract was available for up to 50 per cent of a supplier's total volume at \$6.14/kg milk solids.

⁵¹ <http://www.mgc.com.au/media/24629/Supplier-Handbook-Southern-Milk-Region.pdf>

⁵² <file:///C:/Users/Jen.RDA/Downloads/sub10a.pdf>

⁵³ <https://www.lionco.com/media-centre/lion-announces-competitive-new-milk-pricing-model>



According to Lion Agricultural Procurement Director, Murray Jeffrey:

"Managing Farm gate price volatility is a major concern for our suppliers and not knowing prices from year to year makes it very hard to invest and secure capital in an ever-changing environment. Lion's three year fixed pricing program will deliver a huge benefit to suppliers to mitigate world commodity risk and enhance decision making knowing that 50 per cent of their volume has a fixed price."

Domestic retail pricing

Whilst the processor market will continue to be influenced by the larger players, the two large supermarket chains have significant retail influence, particularly since introducing low priced supermarket brand milk. However, it appears that this has not caused the expected drop in retail milk value and overall sales of fresh milk have continued to rise. There was concern over the market power of these large players, however, the data shows that overall fresh milk sales are up, due in part to this low price structure and the long term (five by five year) supply contracts give a degree of certainty to processors and suppliers⁵⁴.

*Impacts of \$1.00 per litre supermarket milk five years on*⁵⁵

On 26 January 2011, Coles supermarkets announced that it was making significant and permanent reductions to the retail price of its private label lines of drinking milk. Other major supermarket competitors followed suite, although the majority believed the new margins would be unsustainable. Analysis at the time concluded that the overall retail value of drinking milk sales would decline substantially.

Total drinking milk consumption growth averaged 1.7 per cent per annum over the ten years to 2010, so it was assumed that there would be no extra growth overall in milk sales volumes. In reality, volumes grew by 2.8 per cent and 3.3 per cent over the first two years, and have since steadied before slowing slightly over the last two years.

It was also assumed that there would be a strong shift (10 per cent) to buying supermarket milk; however, by the end of 2015, the move to supermarket milk at the expense of other suppliers such as corner shops was only 1.4 per cent. The data suggests that over the five years to the end of 2015, the total fresh milk market in Australia has increased by an estimated \$325 million in retail value to nearly \$4.6 billion.

⁵⁴ http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/5%20and%20Q/2016-06%20S%20and%20Q/SandO_June16_WEB.pdf
⁵⁵ http://www.dairyaustralia.com.au/~media/Documents/Stats%20and%20markets/5%20and%20Q/2016-06%20S%20and%20Q/SandO_June16_WEB.pdf

Attracting competition into the processor market

Ensuring long term market viability

The number of milk processing companies in the Tasmanian market is reasonable but not excessive with the main participants including Murray Goulburn, Fonterra, Lion and Cadbury's. There is a predominance of foreign ownership in these processors with less local choice for farmers as these larger processors dominate the market and continue to grow market share.

Niche processors including Ashgrove, Pyengana and Red Cow Dairy have entered the market at a minor boutique level supplying fresh milk, cream, butter and cheese products to Tasmanian markets. Whilst these processors remain locally owned, their respective influence on the overall market is limited.

In order to develop the processor market and protect farmers' interests, the following could be considered:

- Encouraging additional capital investment into existing farms (expansion and upgrade)
- Government consider ways to invest in support infrastructure (energy, roads and irrigation) to aid expansion to improve productivity and logistics
- Identification of greenfield sites for high value processing plants
- Future processing focused on Tasmanian brand and higher value



Richmond Farm courtesy of the Tourism Tasmania Visual Library



Conclusion

The Tasmanian dairy industry has had a challenging year. From a dry 2015 winter to a hot, dry summer, an unexpected retrospective price drop in farmgate milk prices from the larger processors and most recently record-breaking floods. These direct impacts come on top of significant fires in Tasmania's North West, low dam levels and a break in the Basslink cable causing an energy shortage across the state.

In the last decade, the Tasmanian Dairy Industry has experienced strong investment and growth, bucking the national trend. However, there are concerns that this investment and expansion, coupled with these recent shocks may result in some farmers who are already financially stretched being challenged to remain viable.

Government and public reaction to the milk price drop has been positive and commendable. However, the offer of increased debt (albeit concessional), may not be a solution for those already in financial hardship.

Dairy in Tasmania has demonstrated that the underlying support mechanism to help the industry through crisis is strong. The actions of milk processors, industry organisations and government have provided daily assistance to farmers and could be used as a model for other industries.

It is difficult to find facts to quantify the extent of those who may leave the industry as a result of these recent events. ABARES reports estimate 17 farms (approximately 4 per cent of dairy farms) already had negative cash income prior to the price drop so as a result of the crisis this number could have grown. The reasons for exiting the industry are complex and it is too early to know, it can take up to five years after a crisis to see structural adjustment. Leaving the industry at a point of low confidence and reduced market prices will produce low returns for those forced to sell, an issue for banks who don't want land prices to decrease.

Focus should also be given to the 85-95 per cent of the industry who will work through this impact and continue to grow and thrive. Those farmers who have been prudent, maintained comprehensive insurance and foreseen and managed price and margin fluctuations should be supported and rewarded for their diligence.

There has been commentary about the industry's contractual arrangements, commodity price indexing and the role of key market forces such as the supermarkets and the large processing companies, but there has been no consensus that intervention is required. Representative bodies such as the Tasmanian Farmers and Graziers Association (TFGA) and Dairy Tasmania have warned against moving back to industry price regulation or decreasing market competition.

2014/15 Tasmanian Dairy Region Breakdown

		TOTAL SA
Dairy farms ¹	No.	440
Cows in milk & dry ²	000	170
People employed on farm ³	No.	1,000
People employed in processing	No.	900
People directly working in dairy	No.	1,900
Volume of milk produced ⁴	Million Lts	891
Share of National milk production		9.2%
Value of milk leaving farms ⁵	\$M.	\$442
Ex-factory value of domestic sales ⁶	\$M.	\$589
Value of dairy products exported ⁷	\$M.	\$243
Share of National exports - value		8%
Volume of dairy products exported	000 tonnes	62
Share of National exports - volume		8%
Gross Regional Product Multipliers ⁸	Regional output generated from every \$1 of direct dairy output	0.75
Employment Multipliers	FTE per \$1mill of direct dairy output	6.44

¹ Dairy farm no.s by State from InFocus - & estimated by RDP from LMR data.

² Cow no.s by State from InFocus - & estimated by RDP from ABS Farm Census data.

³ derived from state level figures from DAFF Australian Food Statistics publications: split on the basis of milk production.

⁴ DA milk production database

⁵ region milk flow multiplied by State average milk prices

⁶ DA estimates

⁷ ABS export data

⁸ Econsearch 2016, *Economic Impact of the Australian Dairy Industry*, Report prepared on behalf of DA

Processor Location Summary



- TASMANIA**
- 1 Lion Dairy & Drinks, Hobart
 - 2 Wicked Cheese Co, Richmond
 - 3 Bruny Island Cheese, Bruny Island
 - 4 Pyengana Dairy, Pyengana
 - 5 Fonterra Australia, Tamar Valley
 - 6 Westhaven Dairy, Invermay
 - 7 Meander Valley Dairy, Hillwood
 - 8 Lion Dairy & Drinks, King Island
 - 9 Ashgrove Cheese, Elizabeth Town
 - 10 Elgaar Farm, Mollema
 - 11 Fonterra Australia, Spreyton
 - 12 Lion Dairy & Drinks, Burnie
 - 13 Betta Milk Co-op, Burnie
 - 14 Mondelez, Burnie
 - 15 Fonterra Australia, Wynyard
 - 16 Red Cow Dairies, Oldina
 - 17 Murray Goulburn, Edith Creek
 - 18 Tasmanian Dairy Products, Smithton

Milk	Cheese	Butter/AMF	Fresh Dairy	Whey/Powders	Ice Cream
✓					
	✓				
	✓				
	✓				
			✓		
	✓		✓		
	✓				
	✓				
✓	✓	✓			
	✓				
	✓	✓		✓	
✓				✓	
✓					
	✓			✓	
	✓				
				✓	
				✓	

2014/15 Tasmanian Dairy Region Breakdown and Processor Location Summary Information kindly provided by Dairy Tasmania 2016 ⁵⁶