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Senator Glenn Sterle
Chair References Committee Membership
Senate Standing Committee on Rural Regional Affairs and Transport
PO Box 6100, Parliament House, Canberra ACT 2600
Per email: rrat.sen@aph.gov.au

Dear Senator,

Re: Inquiry into the performance of Australia's dairy industry and the profitability of Australian dairy farmers since 2000

1. The South Australian Dairyfarmers' Association (SADA) thanks you for this opportunity to make a late submission to your committee with regard to its inquiry.
2. This submission is reflective of South Australia as a specific dairy producing jurisdiction.
3. We are aware that you are in receipt of the submission delivered to you in December 2019 from the Australian Dairy Farmers (ADF). This submission agrees with the conclusion of ADF but seeks to add a perspective from the position of the South Australian dairy farmer and the South Australian Dairy industry.
4. At the outset SADA wishes to make some observations about the framework of the narrative which has developed in Australia around the dairy industry and a narrative that we in South Australia believe to be both wrong and inconsistent with the best outcomes for the industry in South Australia and in Australia as a whole.
5. Over the past two years SADA has developed the South Australian Dairy Industry Action Plan 2019-2024. The plan has been adopted as policy by the South Australian Government, DairySA (A state extension of Dairy Australia), South Australian dairy farmers, DairySafe (the South Australian regulator) and the DIAA (SA) which represents processors in South Australia. A summit has been held in SA which has seen representatives from all of those sectors attend and both endorse the Action Plan and set its course. In essence the industry in South Australia has set about creating an environment of co-operation hitherto not experienced in other jurisdictions.
6. Nevertheless, the inquiry which is being conducted continues to capture the narrative which has amplified into the "us and them", narrative which has dominated the debate in Australia. The recent Senate Economics and Legislation Committee Report (March 2020) into the *Saving Australian Dairy Bill* 2019 reflects the narrative which has become dominant in Australia. This narrative has become so dominant as to see the "us and them" language metastasise in such a way as that to see in industry in any other terms is now incomprehensible to participants in the debate.

The South Australian Dairy Industry Action Plan 2019-2024

7. South Australia has a long and proud history of producing premium milk and dairy products.
8. Producing about five percent of Australia's Milk, the South Australian dairy industry has committed itself to securing a position at the premium end of the national and international marketplace. An accelerated middle class across our region offers opportunities for the intelligent positioning of the South Australian dairy industry so the highest quality products can be targeted at the new wealth which is making its economic presence increasingly felt.
9. With Asia now accounting for more than half of the world's population and its per capita wealth inexorably growing, it is becoming increasingly clear that the 21st century will be Asia's century.
10. South Australian dairy is well positioned to become part of that market by satisfying the demand for refined consumer expectations from the southern tip of India to the northern tip of Japan.
11. However, the South Australian dairy industry's ambitions aren't just for Asia alone. The South Australian dairy industry is setting its sights around the planet to be globally recognised as one of the safest and greatest places to obtain world standard dairy product.
12. The Action Plan amounts to a call to arms to all participants in the supply chain to unify in their sense of purpose and to bring their ambitions to bear to realise the best possible outcomes from this valued South Australian industry. The plan is about galvanising the mindset of all who are in the dairy chain. The chain is the producer, the processor, the wholesaler and the retailer each of which have a part to play in the process of getting milk from grass to glass or from paddock to plate. Historically it has been too easy to segregate the dairy supply chain into its component parts with each component taking an insular position.
13. In difficult times that has meant that the relationship between producers and processors for example, has been eroded at the expense of the supply product overall. The Action Plan is a vehicle by which all parts of the chain have a mind and a care about what they can do to improve the image and the performance of the dairy product in the journey from the paddock to the plate.
14. Businesses that galvanise their focus on the end result are businesses that thrive over time.
15. For those reasons the plan is the product of wide consultation and input from all sectors in the supply chain.
16. The Action Plan is a document which is owned by the industry it serves and has been a touch stone for representative organisations that seek to advocate for the industry to legislators, ministers, governments, decision makers and others who have influence in the industry. It ensures that consistent messages are coming from industry to those who can have an effect on industry then it is expected positive outcomes will be there for all to benefit. In short an industry that owns shared goals is an industry with a shared future.

Addressing the Committees Terms of Reference

17. The terms of reference for the committee may be essentially be separated into three general areas of consideration, namely, the role of Dairy Australia (DA), the role of the ACCC and the Code of Practice and alternatives for the industry. This submission attends to the terms of reference in accordance with that separation.

Dairy Australia

18. SADA welcomes an examination of the work that Dairy Australia does for its constituents. However, SADA urges Senators to approach their work with an attitude of a performance audit rather than an inquisition.
19. There is an expectation that DA take a stronger advocacy role for dairy farmers. As the levies are paid by dairy farmers this isn't unexpected, however, the advocacy work done by state dairy farming organisations (SDFOs) and ADF is by its very nature quasi-political or outright political. SADA's position, as a SDFO, is that advocacy should remain within the ambit of the SDFOs and ADF. Were DA to take such a role on there would be two risks, firstly, that it would be easy to diminish the purely researched based work as being political by anyone who didn't like the results of research work done by DA and secondly, it could amplify fractured messaging to government if different positions were taken on issues by DA and ADF and SDFOs.
20. The general and useful rule of thumb thus far has been that if it happens on farm it is the role of DA and if it happens off farm its ADF and the SDFO's. SADA sees no reason to interfere in that arrangement.
21. The first area of consideration by the committee is the ability of Dairy Australia to act independently and support the best interests of both farmers and processors. The implication in this term of reference goes directly to the issues that have been raised in the preceding paragraphs that there somehow is a competing interest between the two parties. If that is the starting position of the Committee in approaching this issue then the committee has fallen into a position of accepting the narrative and it will therefore not be able to extricate itself from creating a recommendation that is seen outside of the paradigm of those terms.
22. SADA urges the Committee to view the industry more globally than it has been tasked to look. SADA respectfully suggests that the Committee consider the reference more fully in terms of how Dairy Australia could better serve the interests of both processors and producers collectively.
23. With regard to the accuracy of statistical data collected by Dairy Australia and the Australian Bureau of Statistics, SADA has no reason to believe that the statistical information upon which DA formulates its advice is in anyway compromised, nor does SADA believe that DA does anything in its conduct to indicate that the statistical information used by DA is in anyway informed by an ulterior motive.
24. Dairy Australia is reliant of the funding it receives from levies. Like any tax such levies are generally grudgingly paid, particularly in challenging times. What the Committee is being asked is to effectively review the board's decisions as to how it spends the money collected.
25. There are two elements to the answer. Firstly, the board is obliged to follow the rules of any corporation under Australian corporation law. SADA is not in possession of any information which would suggest that the board of DA has in any way breached the law. SADA respectfully suggests that institutions such as the Auditor General and ASIC are better positioned to oversight such matters than necessarily the Senate. Nevertheless, in the unlikely event that were the Senators to become aware of something that required further investigation SADA would support a reference to the appropriate investigating authority.
26. The second element of the term of reference would then be to question the board's decision-making process and the consultation that the board conducts regarding its decision-making processes. SADA apprehends this is the motivation behind the term of reference. There are mechanisms in place where if a levy payer were unsatisfied with the board's decision-making process, they could seek election to the board through the normal channels. Indeed, at the recent DA AGM such elections were conducted regarding board positions through the normal processes available. SADA was

present at the AGM and did not observe any conduct which amounted to impropriety in that process.

27. There is no doubt that from time to time boards will make decisions that their constituent shareholders disapprove of. It does not however, automatically follow that there is any illegitimacy in a particular decision because it is not liked. SADA respectfully suggests that there is no scope for the Senate to intervene in particular decisions made by the DA board if they are nothing more than unpopular. To do so would amount to an attempt by the Senators to assume the functions of the board.

The ACCC

28. The Committee has been tasked to examine how the ACCC can regulate the price of milk per litre paid by processors to dairy farmers to ensure a viable dairy industry. The ACCC must be the overseer of the laws relating to competition and the mandatory code of conduct, but it cannot be the organ of price fixing.
29. The essence of this submission is that the ACCC is an organisation that is granted by its charter to police fairness of the commercial environment and that in a deregulated environment that role should be assertively pursued.
30. Deregulation does not mean an absence of law. What it means is that there are less laws in the commercial environment. The laws that are left are laws that have a more criminal, as opposed to civil, flavour and therefore the regulator should see their role as a policeman. If the intent of Government was to leave the commercial environment exclusively to the courts, then Government would never have enacted the Trade Practices Act back in the 1970s or subsequent Governments would have repealed such legislation.
31. This has not occurred. The Trade Practices Act has now become the Australian Consumer and Competition law which casts a wider net than the original TPA. What has occurred is the creation of the ACCC. But ACCC isn't a court, it is a police officer.
32. The inquiry being undertaken by the Committee must conclude that the ACCC is a police officer and should they discover anything that is possibly an offence the ACCC should refer it to a court for a determination as any police officer would.
33. Moreover, the legislation is crafted in many ways to be a shield in the marketplace to protect the minnows from the sharks. The ACCC should not only see its role as the bearer of that shield but as an organisation that will unsheathe its sword to protect the smaller players against breaches of regulation and breaches of the legislation in a timely fashion. A police officer is allowed to counsel or caution a person they think may be about to break the law as well as arrest them afterward should a law be broken.
34. Much of the recent activity by the Parliament and the Government in inquiring into the Dairy Industry has been driven by the poor results for farmers at the farm gate. Many farmers have reported that the cost of production has outstripped the prices being paid. Depending on who is arguing the case there are a number of reasons being given as to why this has occurred. In truth, over the past four years there has been a perfect storm in the Dairy market particularly for Australian producers.
35. The perfect storm has been an amalgam of European quotas being lifted and Russia's self-imposed trade barriers. However, commercial decisions by Murray Goulburn and Fonterra have also amplified the impact on Australian farmers, not least of which, those farmers who work in South Australia. Being able to point at European quotas or Russian sanctions however, does not absolve processors or retailers from culpability and unfair trade practices where they occur.

36. We are mindful that the ACCC is limited to the operation of Australian Consumer Law and how that law reflects on the operation of business in this country. Nevertheless, it is clear from submissions to the Senate Economics Committee inquiry into the dairy industry back in 2017 when this area was initially examined, that there is a deep concern and disillusionment harboured by many producers about the supply chain and how vulnerable producers are to the arrangements that are being made by processors and subsequent clients.
37. The relationship between Murray Goulburn and Coles at the time being the leading example. Such arrangements quickly lead many people to the belief that collusive or other anti-competitive conduct was occurring. There can be little doubt that these sorts of arrangements have had a deep impact on the confidence that many producers have in the marketplace. This sort of conduct is precisely why the ACCC exists.
38. In 2017 one of the matters that the ACCC turned its mind to was the relative bargaining positions that exist between the producers and processors. What was accepted is that relationship imbalance has existed for a long time and has been known about for many years. In good times that imbalance isn't particularly corrosive however, in times of stress that imbalance leads to pronounced public concern manifest in protests, Senate Inquiries, political noise and numerous other expressions of disquiet. From a dairy perspective, but likely in a number of other industries in the primary sector at least, the ACCC is in an excellent position to be more proactive or assertive than it historically has been.
39. Like many policing activities the ACCC often responds to complaint. Nevertheless, there are circumstances where various regulatory bodies should pre-emptively move to police a law, ostensibly becoming the beat cop on the street corner in a tough neighbourhood. Again, it is this notion of the ACCC taking up its functions as the bearer of a sword as well as a shield.
40. With the greatest of respect to the ACCC (and for that matter ASIC), if they had been more assertive in their policing roles in the industry environment four years ago, SADA suggests its presence may have made the difference between an investigation into what has already occurred and better management practices by corporations before they made potentially criminal decisions at the time.
41. Industry participants such as Murray Goulburn and Fonterra, then came under investigation for conduct already completed rather than conduct that could have been interrupted. The investigations at the time led to criminal charges being laid. It would have been better if the conduct was cautioned before there was a need for criminal charges. If the firms had been pressed by the police officer earlier in the timeline there may never have been the conduct that attracted the investigation in the first instance.
42. Simply expressed, the mere existence of a legislative instrument is often not enough to ensure compliance. There needs to be a presence that is part coercive and part cautionary.

Alternatives and the Code of Practice

43. There are two final elements of the terms of reference which are more general in nature in terms of supporting the dairy sector. The first consideration is alternative approaches to supporting a viable dairy sector. This general reference is welcome and SADA urges the Committee to take careful heed of the various recommendations made by DA and ADF in their submissions and regarding those things that could be done to improve the system.
44. From SADA's perspective we would encourage Senators to consider the elements raised in the South Australian Dairy Industry Action Plan 2019-2024 as things that can be done to improve the industry in this country. Were the Committee to reject the "us and them" premise with a report that embraced a co-operative philosophy, little harm and much good could flow from such a report.

45. SADA has been a strident supporter of the Mandatory Code of Conduct. SADA has been pleased to closely work with the ADF in drafting the Model Standard Form Contract which ADF will invite industry to contemplate for modification and use across industry. The Mandatory Code has done and will continue to do much to improve the relationship between the contracting parties and SADA hopes that the regulated requirement of “good faith” in the Code will metamorphosise over time into the embraced industry attitude.

Comments regarding imposition of artificial measures such as floor prices.

46. SADA recognises the challenges facing the dairy industry in Australia and the importance of ensuring the viability of the dairy industry. SADA notes the recent report of the Senate Economics and Legislation Committee (March 2020) into the *Saving Australian Dairy Bill 2019*, particularly the observations of the dissenting Labor Party report.

47. SADA agrees with the findings of the majority and is critical of Labor’s dissent. The anguish which has been caused in the Australian dairy industry in recent years has been the product of artificial price setting mechanisms, in particular the imposition of \$1 per litre milk.

48. SADA believes that the imposition of a floor price is just another manifestation of an artifice which is artificiality by another means.

49. The picture presented by the milk supply chain in Australia over the past five years hasn’t been a pleasant landscape.

50. It has all the coherence of a Salvador Dali painting crashing into a Picasso. How it got to that place is a history lesson that needs to be considered when thinking about a pathway forward.

51. To find the genesis of the milk crisis it is important to travel back to 2001. At that time the milk pricing mechanisms were changed to allow the markets, not regulators, to set the price.

52. For a decade, things ticked along and the market operated so that the milk price paid by the consumer was reflective of the whole supply chain, the supermarkets, the processors and the farmers.

53. Like a cannon ball in the middle of a trampoline, Murray Goulburn (MG) was a substantial organisation that sat in the middle of the industry. Everything orbited around MG. MG represented both processors and farmers interests because it was a co-operative. Therefore it was a packager and seller of bottled milk while remaining accountable to their farmer membership.

54. Like an oracle each year, MG would appear from its temple and would pronounce its price.

55. Other processors would issue a price somewhere in the range of MG’s price a few days later to maintain the polite illusion that market forces were at play. What was at play however, was a clear understanding of the national and international price pressures for milk and therefore the prices set were not the product of some arbitrary or capricious sentiment MG maintained, but rather the careful measure of the dairy commercial environment.

56. Invariably the price from other processors would be in the ballpark of MG’s price. MG’s size and broad representation meant that it was representative of the whole supply chain and as a co-operative it was mindful of both farmers and processors because it was equally concerned for both.

57. Then several events occurred almost simultaneously. Firstly, MG lost its way as it sought to become a company rather than a co-operative. As a company it failed to negotiate the reefs and shoals of the commercial world. The balance sheet became more important than the balance in the industry.

58. At about the time that MG commenced its metamorphosis, the major supermarkets, Coles then followed reluctantly by Woolworths, began their \$1 milk campaign. This campaign didn't focus on the cost of production and the supply chain, it focussed on the retail price.
59. MG played along and suddenly the power to set a milk price that reflected the cost of production shifted from MG to the supermarkets. A few years later, MG collapsed.
60. Since that time there has been no single processor big enough to challenge the supermarkets on price, leaving the major retailers in charge of prices by demanding their \$1 milk continued to be profitable for them.
61. By 2017 the distorting forces had become so pronounced that the Commonwealth Government referred the industry to the ACCC.
62. The ACCC made many important findings but basically, they laid the blame of farmer suffering at the feet of the processors.
63. All that needed to happen was that when the cost of production changed the processors would exercise their price variation clauses. These are clauses in contracts that say when the cost of production changes the price of the product changes. There is little evidence that any of the major processors have exercised their options under their price variation clauses with the supermarkets.
64. The reason for this is that processors which provide drinking milk to the supermarkets in the \$1 variety always have other branded products on the supermarket shelves next to the \$1 milk they provide to the supermarkets. If a processor moves to exercise a price variation clause on supermarket labelled milk, they run the risk of having their other products either removed or their shelf facings limited.
65. Because no processor is large enough to challenge the supermarkets they are also on the horns of a dilemma and they are forced to pass the cost onto the farmer.
66. Compare this to petrol, where the supermarkets also maintain an interest. In those instances, the suppliers of petrol are big enough to vary their prices and the supermarkets follow the lead.
67. There is no doubt that the supermarkets would become very popular if they changed the price of fuel to \$1 per litre and held it there for a decade. But they don't because they cannot threaten BP and Shell.
68. Nothing prevents a supermarket from offering \$1 petrol, but what they cannot do is bludgeon international oil company into a lower price as they do with processors and farmers.
69. The dairy industry doesn't mind if supermarkets make milk cheap, in fact the dairy industry wouldn't mind if the supermarkets gave the milk away for free if the supermarkets were still paying the processors and farmers a price that reflected the cost of production.
70. The problem is that the supermarkets artificially declare prices and then expect to be subsidised by both processors and farmers.
71. Whilst welcome at the time, the Woolworths decision that they were going to raise the price of milk from \$1 per litre to \$1.10 per litre it did nothing to address the artifice which is a milk price that is totally disconnected from the cost of production. In fact, in an important way the determination highlighted the artificiality of the pricing practices of the supermarket chains.
72. SADA, supports a free market to set a milk price. What was occurring wasn't a free market. It was supermarkets setting a course and shackling farmers and processors to it like so many slaves in the galley's bilge.

73. The supermarkets were not mindful that they were creating demands that were threatening to break the system. The casualties were real. Since the introduction of \$1 milk the number of dairy farms in South Australia had fallen from 286 to 228.
74. The supermarkets still sold water which reflected the cost of production which is why bottled water which cost more than bottled milk.
75. The risk for the supermarkets became manifest in a sharp backlash that led to calls for a regulated industry and which have invited government intrusion into the market space. If processors can't move on price it won't be long before some of them join Murray Goulburn as a memory and many farmers will go with them.
76. Recently, this truth was silently acknowledged by the Supermarkets and the milk price war which was started by Coles was called off by Woolworths. Instead of claiming victory, Coles quickly followed Woolworths off the battlefield clearly grateful that the fight had been called off.
77. Since then milk prices have settled down and now the prices being offered reflect the cost of production, processing and retailing as they should. The consumer is paying a reasonable price for the product that they buy. While that price may not always suit everyone in the supply chain it will be infinitely better than dealing with artificialities that will only decay into pain.
78. In artificial pricing environments where corrections occur, they are invariably dramatic and lead to adverse outcomes. While the free market isn't perfect, in the dairy industry at least they are reasonably gradual.
79. The Senate Economics and Legislation Committee Report (March 2020) into the *Saving Australian Dairy Bill 2019* came to the following conclusions namely:
 - a) The committee considers that setting a base farm gate milk price will not fix the power imbalance between dairy farmers and processors and will not reduce input costs such as fodder, water, labour and electricity;
 - b) Raising the price of milk paid to dairy farmers may suppress initiatives to improve productivity, reduce the competitiveness of our export market;
 - c) Make imported dairy products cheaper in comparison to domestic products and place international trade agreements at risk;
 - d) The committee considers that an insufficient case has been made for prescribing that the Grocery Code be mandatory;
 - e) The committee notes the introduction on 1 January 2020 of a mandatory Dairy Code and the government's announced additional funding for Dairy Australia to provide financial and legal advice to farmers;
 - f) The committee is confident that these existing measures will support market conditions to bring about efficient production and supply of dairy products, as recommended by the ACCC inquiry;
 - g) By comparison, this bill has significant potential to damage dairy farmers, the supply chain, international export markets and the viability of the dairy sector overall;
 - h) This bill would create a significant deterrent for processors to buy local milk from farmers in regions that would have artificially high farm gate base prices as a result of this bill. These areas would likely be those with low rainfall levels, different types of pasture and geographical influence, such as Queensland, Northern New South Wales and Western Australia;

- i) The bill would disincentivise and remove rewards for innovative farmers in regions with high farm gate prices set by the bill in competing for local processor supply;
- j) Additionally, in contravention to the stated purpose of the bill, this would not be 'Saving Australian dairy' across Australia. It would incentivise processors to purchase and transport milk from milk markets with lower input costs, typically southern milk markets to supplement higher cost markets;
- k) Further, if the price of milk was set above a competitive level with international milk supply, it may incentivise imports of fresh milk to supply the domestic market; and
- l) If introduced, this bill has the potential to weaken the domestic dairy industry – particularly the fresh milk markets in QLD, Northern NSW and WA.

80. SADA has reviewed these conclusions and for all of the reasons outlined in this submission SADA agrees with the conclusion of that committee and urges the present Committee to bring a similar mind to bear on the issues that the present Committee is considering.

Appearances

81. SADA would welcome an opportunity to present oral evidence before the Committee when it next convenes.

Yours sincerely,



John Hunt
President