Media Release

Australian Dairy Farmers

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ADF does not trust Coles and neither should their customers

For immediate release

ADF Vice President Adrian Drury says, 'Dairy farmers do not trust Coles and neither should their customers. There are many reasons not to. Throughout this debate Coles has knowingly used figures that are deliberately misleading. ADF is now taking the opportunity to correct them.'

Yesterday in the media Wesfarmers Managing Director Richard Goyder was quoted as saying that 'what Coles is doing is hopefully increasing demand for milk.' It is a fact that demand for drinking milk is inelastic. Consumers only buy and use a certain volume. Mr Goyder must know this.

He must also know that milk priced at $1 per litre is simply not sustainable – there is not enough money in the value chain to support farmers, processors and retailers at that price. Coles knows it. The last time milk was priced at $1 per litre was in 1992. Selling a product for what it costs (or less) to produce, transport and retail is unsustainable.

Woolworths and other retailers have stated, both publicly and privately, that these price cuts are unsustainable. The reality is that Coles' marketing tactic is sacrificing the true value of milk to use it as a tricky tool to lure customers from their competitors.

Mr Drury says 'Dairy farmers certainly do not believe that Coles is going to absorb the cost. Who will then? Their customers or those at the start of the chain – dairy farmers?'

It should also be noted that Coles has repeatedly refused to rule out dropping prices for processors and farmers in future contracts.

Associate Professor Frank Zumbo from the School of Business Law and Taxation at the University of New South Wales in an article in the Newcastle Herald on 9 March 2011 made a very pertinent statement regarding the potential impacts on Coles' customers.

'While Coles has said it has reduced the price of 5,000 products, it has been silent on what has happened to the price of the 15,000 other products sold in a supermarket. Again, consumers would lose out to the extent that the increases in the 15,000 non-milk products were greater than the reduction in the price of home brand milk.'

This aggressive discounting has happened before in the United Kingdom where the key executives behind this Coles marketing strategy are from.

An article in the Business Spectator from 7 February 2008, sums up this team of British executives and Mr McLeod's primary goal perfectly, stating it is 'creating operating environments in which to relieve customers of their disposable income.'

Mr Drury says 'We believe that the Coles' executives are here with the intent of replicating the UK model. It ultimately leads to less choice, higher prices for customers and unsustainable pressure on farmers.'

ADF has reviewed Coles' most recent media 'fact' sheet and it is full of mistruths, evasions, tricky lines and spin. In the following statement we have dispelled some of their trickiness and shown why they cannot be trusted by anyone, particularly consumers.

Coles' facts aren't facts – they are deliberately misleading

Coles' claim – "Myth One: Coles is refusing to meet with dairy farmers about its milk price cut announcement

Coles has discussed the price reductions with milk processors and has met with the peak milk industry organisation, Australian Dairy Farmers, and other farmer organisations."

The Facts:

Coles has met with the ADF twice. Even though the ADF, and other industry stakeholders, have pointed out the facts around this issue, Coles continues to peddle the same misleading statements.

We contend that although Coles have met with some industry groups, they have yet to listen and act upon the industry's concerns – and in fact seem to be outright ignoring them.

Coles know that dairy farmers in Queensland and NSW, for example, make about 2 cents a litre farm profit according to official ABARE statistics (ABARE Farm Survey Exercises for 2009-10) and have suffered severe impacts from floods and cyclones and yet they are happy to cut the price of milk by significantly more than this per litre and still try to claim that it is sustainable for dairy farmers.

The meetings could be seen as yet another part of Coles' public relations and marketing strategy. Meeting with industry stakeholders solely for the purpose of being able to say they have met with them, not with any real intention of listening or acting on dairy farmers concerns.

Coles' claim – "Myth Two: Coles' retail milk price cut will push down the farm gate price of milk.

The farm gate price dairy farmers receive is set by the world price because most Australian milk products are exported. In any case, Coles buys milk from the major milk processing companies, not direct from the farm gate and Coles paid a higher price to milk processing companies in mid-January. As such, the farm gate price should not be affected by our decision to reduce the retail price."

The Facts:

Coles has consistently claimed that over 50% of all milk production goes overseas as exports. This is just plain wrong and Mr McLeod and his overseas team of executives must be aware of this by now.

Approximately 55% of Australia's milk production is consumed domestically, significantly more in Queensland (95%), Western Australia (70%) and New South Wales (66%). In these states retail sales of drinking milk are the key regional market and farm gate price driver (see table 1).

Coles like to say that farm gate price is set by the world price because they can then absolve themselves of any responsibility for impacting the price of milk. This is poppycock for dairy farmers in Queensland, Western Australia and Northern New South Wales. Coles' actions have a big impact and it is being felt already.

Processors and dairy farmers who supply the drinking milk market rely on the margin from branded milk sales for their profitability. Competition from unsustainably priced Coles home brand milk is taking market share away from branded products.

This reduces the amount farmers receive from processors as an increased share of Coles home brand milk is being sold at little or no margin and less of the more sustainably priced branded milk is being sold.

Many Queensland farmers whose milk payments are linked to branded milk sales have already seen their milk cheques drop this month by thousands of dollars per farmer.

As Coles steals market share away from proprietary branded milk sales these farmers milk cheques go down, down, down. This is a direct result of Coles ‘cut throat’ discounting.

So it’s no wonder dairy farmers are angry when Coles promotes the spin to all Australians that they are not hurting farmers when it is simply not true. And then Coles has the hide to ask Australian consumers to trust them.

What Coles needs to do, is stop being tricky and raise its prices to what is fair and sustainable for its milk suppliers, Australian dairy farmers. We need to focus on sustaining our critically important food producing industries not devaluing their products, which ultimately leads to undermining investment, supply and choice and then ultimately to higher prices for customers.

Coles’ claim – “Myth Three: Coles’ actions are anti-competitive.

Our intent is to provide lower priced milk for our customers while not adversely affecting our suppliers. Coles increased the price it paid to milk processing companies in mid-January and is fully absorbing the cost of the lower retail price in a lower profit margin. Coles has therefore reduced its own profit margin on milk sales so that it can provide a benefit to its customers.”

The Facts:

A representative from Coles gave evidence to a Senate inquiry last year that margins were about 20 percent on the prices then of approximately $1.20 per litre. They have now reduced the price by up to 33 percent to $1 per litre, this would appear to mean that Coles cannot be making a profit on their milk sales and is using the entire category as a loss-leader.

ADF believes there is a prima facie case under section 46, including 46 (1AA) of the Trade Practices Act 1974 (now the Competition and Consumer Act 2010) that Coles’ actions constitute predatory pricing.

It is our belief that Coles’ actions are designed to steal market share away from, and damage, their competitors, such as other major retailers, corner stores, independent petrol stations and other small retailers of milk, and will lead to a substantial lessening of competition in the market place.

We also believe this action by Coles impacts the viability of branded dairy products and will lead to less product variety on supermarket shelves.

It is our view that these actions will ultimately lessen competition for consumers through increasing prices and decreasing product choice as the experience in the United Kingdom has shown.

Dairy farmers certainly do not believe that Coles is absorbing the cost of these unsustainable price cuts. Who are then – their customers or those at the start of the chain – dairy farmers?

It should also be noted that Coles has repeatedly refused to rule out dropping prices for processors and farmers in future contracts.

Coles' claim – "Myth Four: Coles funded lower milk prices through higher petrol prices at Coles Express.

Coles does not cross subsidise lower grocery prices through higher petrol prices. Pricing of these products is quite separate. Petrol prices have been rising because of higher global oil prices."

The Facts:

According to the general manager of FUELtrac (a fuel monitoring agency), Geoff Trotter, petrol prices rose by up to 15 cents per litre on the weekend of January 29 and 30, just days after Coles announced its price cut on Australia Day. "I think there is a connection between their grocery activities and their petrol activities," Mr Trotter told AAP. "If there is an opportunity for them to cross-subsidise, if they are giving away margin on bread and milk, fuel is a wonderful way to recover that margin."

Associate Professor Frank Zumbo from the School of Business Law and Taxation at the University of New South Wales in an article dated the 16th February titled "Don't be fooled, the supermarkets are milking us", stated that "The sceptical customer will ask if the major supermarket chains are listening to consumers on the price of other products. We have seen petrol prices shoot up opportunistically despite the strong Aussie dollar and the Singapore benchmark price we use to calculate local prices having remained consistent in recent weeks. Yes, international crude oil prices have jumped but local prices are instead linked to the refined price of petrol out of Singapore. So petrol prices have jumped quickly and the major retailers have been able to increase their average retail petrol profits during the past year." And "This is the old "loss leader" trick. Get customers hooked by a super special and then fleece them on other products. It's the oldest trick in the book and consumers shouldn't be fooled."

Coles' claim – "Myth Five: Lower Coles brand milk prices will result in lower branded milk prices and hurt farmers.

Coles has increased the price we pay the milk processors for Coles brand milk, so they have no reason to reduce farm gate milk prices as a result of the Coles brand retail milk price reduction. Any decision about branded milk prices is a matter for the milk processors."

The Facts:

Coles has admitted that sales of their home brand milk have increased. This alone hurts farmers as there is an immediate impact on farm income. For some dairy farmers when branded milk sales drop their milk income drops by thousands of dollars.

Processors make little or no profit on home brand milk sales. A long-term increase in the sales of home brand milk will see flow-on affects to farmers as Coles, due to its market power, dictates the price at which suppliers sell to them.

As Coles' home brand sales increase, they dominate shelf space and customers have less choice. This vicious cycle continues until in the long-term there is absolute domination by home brands with no customer choice, little product innovation and worst of all for the customer – a likely increase in the price of their home brand milk once Coles' has achieved its goal of market dominance.

Coles claim – "Myth Six: Lower Coles brand milk prices are part of a plan to replace fresh milk and with long life milk.

Coles' customers want high quality fresh milk at the lowest possible price. To achieve that, Coles' is paying milk processors more for their milk, and fully absorbing lower retail prices. That is a win for the Australian dairy industry and a win for our customers."

The Facts:

Coles plan is to use cutthroat unsustainable milk discounts to steal customers and business away from their competitors, such as other major retailers, corner stores, independent petrol stations and other small retailers of milk to gain more market share. This will ultimately lead to a substantial lessening of competition in the market place.

They also want to squeeze farmers and processors which will damage the dairy industry, particularly in Queensland, Northern NSW and Western Australia.

Coles' claim – "What drives farm gate milk prices?

The farm gate price dairy farmers receive is set by the world price because a large proportion most Australian milk products are exported. The farm gate price is rising because global demand for milk product is rising (see Dairy Australia press release 14 February 2011)."

The Facts:

Coles have consistently tried to confuse this issue by quoting Victorian price increases of 22% when they know full well that Victoria is chiefly a dairy export market, not a domestic drinking milk production market.

What Coles has repeatedly failed to mention is that milk prices to farmers in the key domestic drinking milk production markets of NSW and Queensland have dropped by more than 15% in Queensland and 10% in NSW in the last 12 months. This includes farmers who supply milk which goes into Coles' home brand milk bottles.

The share of drinking milk production in Queensland is 95%, New South Wales is 66%, Western Australia is 70% and Victoria's share is under 9% (see table 1). Yet Mr McLeod persists in quoting figures from Victoria which is clearly not affected as significantly as the key drinking milk production states of Queensland, New South Wales and Western Australia.

Coles' claim – "How much milk does Coles sell?

Coles' milk sales (including modified drinking milks) represent less than 5% of Australia's total milk production."

The Facts:

Mr McLeod also consistently tries to downplay Coles' impact on the market by saying that Coles milk sales represent less than 5% of Australia's total milk production.

What he again fails to mention is that only 25% of Australia's total milk production is used as drinking milk in the domestic market. The rest is used in manufacturing cheese, butter, milk powders and other products.

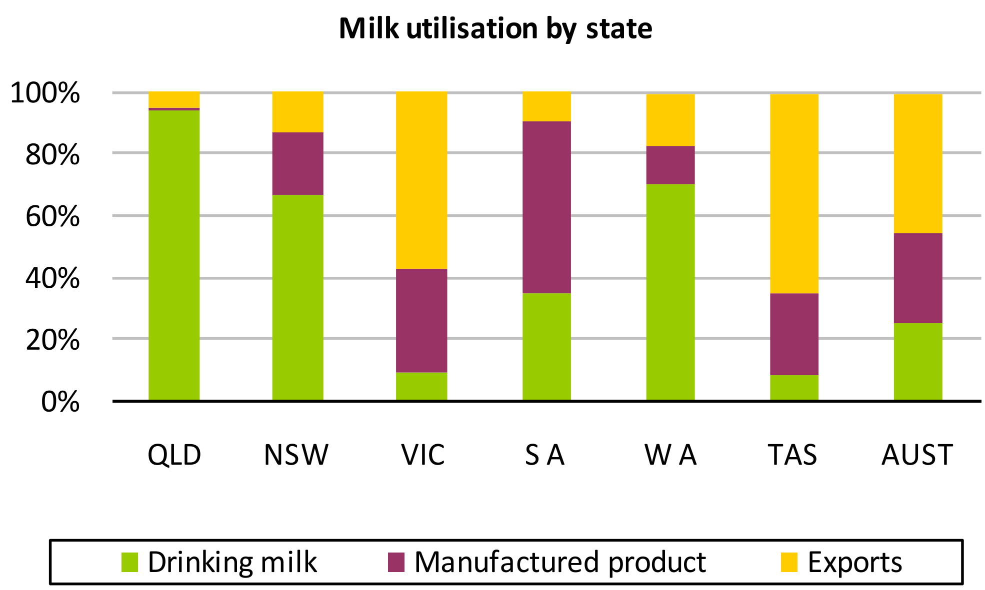
In reality Coles milk sales represent 20% of Australia's drinking milk production, which is a significant percentage in anyone's language and is made even more so by the fact that Coles' competitors have been forced to match them in these unsustainable milk prices.

When coupled with the fact that in recent times Coles has accounted for around 40% of all domestic supermarket milk sales there is a substantial impact on the drinking milk market and farmers in Queensland, Western Australia and New South Wales in particular.

More broadly Coles action cuts at the heart of all farmers since (whether they supply Coles or not) they are seeing the product they produce “devalued” in the market place.

In a tough production year, that is tough to take and another reason why farmers are so angry about Coles’ using them as pawns in its tricky marketing strategies.

Table 1



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