Australian Dairy Farmers

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Senator David Bushby
Chairman
Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Senator Bushby,

I am writing following the lodging of Coles' submission, dated 9 September, to the Senate Economics References Committee inquiry into the impact of supermarket price decisions on the dairy industry.

Coles continues to cite misleading and outdated statistics and provide commentary that is designed to divert attention from the key issue. In this letter ADF refutes a few of the major claims made in the Coles' submission.

An ongoing example is the fact that Coles have consistently tried to confuse this issue by quoting southern states farmgate price increases (for example Warrnambool Cheese & Butter, Murray Goulburn, Fonterra, on page 4 of its submission) when they know full well that the southern states chiefly rely on manufactured product and export markets whereas Western Australia, northern NSW and Queensland rely on the domestic drinking milk markets.

This is an important point as it highlights the regional and market differences in Australia's dairy industry.

To equate farmgate price increases in the southern states with the drinking milk states is not appropriate. The southern states are affected to a lower degree by a drop in the price of drinking milk as opposed to farmgate prices for dairy farmers in northern NSW, Western Australia, and Queensland where drinking milk is the dominant market – or as in the case of Queensland virtually the total and only market.

It is also important to emphasise that the prices seen in the southern states are based on seasonal milk production largely for manufactured or export markets and not for milk produced 365 days a year, which costs more to produce, for the fresh domestic milk market.

Coles also tries to claim that there have been "steady to rising farm gate prices by all milk processors so far for the FY12 season". This is simply untrue. ADF has cited several examples in its earlier submission dated 2 September of lower farm gate prices or farmers being asked to accept lower farm gate prices in the initial stages of negotiations that are not yet finalised. This is solely due to the unsustainable nature of drinking milk being priced at $1 per litre. The longer the marketing war initiated by Coles continues the more examples we will see.

Coles also again refuses to acknowledge large cuts to farmgate prices for dairy farmers supplying milk to the domestic drinking milk market, including for their own Coles home brand products, last year.

Coles also tries to confuse the issue when it makes reference to Parmalat's Paul's Daily Access (PDA) Scheme on page 7 of its submission. The simple fact is that the 185 affected farmers in Queensland have already lost $767,858 to the end of July 2011. This is because the Coles initiated milk price war has increased the sales of home brand milk and these farmers' milk payments are linked to the sale of branded products.

Clear evidence of these impacts is provided in our submission and further detail is provided in the submission lodged by the Queensland Dairyfarmers' Organisation (QDO) dated 31 August 2011.

Further to this on 13 September 2011 at the QDO conference a senior Coles' representative claimed they were not aware of the impact on dairy farmers supplying Parmalat. This is very surprising given the clear references to the issue in Coles' submission to the inquiry dated 9 September 2011.

Coles also selectively quotes from Dairy Farmers Milk Cooperative (DFMC) media releases but does not include the following quote which was in a media release dated 1 August 2011.

"This risk is heightened by the continuation of the $1 per litre retail price point that is being maintained by the major supermarkets, which is putting downward pressure on processor and farmer returns."

Coles makes the following statement in relation to Western Australian farmers supplying Harvey Fresh, "Coles has negotiated a higher commercial price under the terms of its new private label supply contract with Harvey Fresh in July 2011."

ADF understands that farmers supplying Harvey Fresh saw a small price increase of less than 2%, again less than inflation and increases in the cost of production on 2010/11 prices for 2011/12 from approximately 38.7 cents per litre to approximately 39.2 cents per litre.

This means that WA dairy farmers supplying this contract are effectively going backwards when inflation and costs of production are taken into account. The figures quoted above are approximate as it is difficult to be exact due to slight variations in contracts between the years and a lack of transparency between processor and retailer.

In addition, Coles has sought to blur the truth even further by claiming that it has restated its willingness to pass on higher farmgate prices in payments to milk processors. The media release that Coles includes at attachment nine does not say that at all. The closest it comes is to say it would "fund lower retail milk prices."

Hypocritically Coles calls for "increased transparency of farm gate milk pricing by milk processors". The key issue here is the price paid by retailers to the processors as they are squeezing the value chain with milk priced at $1 per litre. If Coles wishes to advocate for increased transparency then it would be beneficial for the entire industry if they showed a modicum of transparency regarding the price they pay to processors, instead of consistently claiming it is 'commercial-in-confidence.'

Coles must show the transparency it continually advocates for others and reveal the real numbers, strategy and intent behind its price cuts, if only so their customers have the full story.

It should also be noted that the report from Steve Spencer of Fresh Logic that Coles cites and supplies at attachment three has been updated and revised due to the discovery of erroneous assumptions in the analysis. The revised analysis shows the impact to processor gross product margins in Northern markets to be upwards of $6.2 million or approximately 1.34 cents per litre.

Coles also does not mention in its submission that the analysis by Fresh Logic does not include any impacts on processor margins from:

- discounting processor proprietary brand products to try and retain market share; or
- increased marketing and promotional expenditure from processors to try and retain market share.

There is now evidence of both impacts being incurred by processors since the analysis was undertaken.

On page 3 of its submission Coles mentions farmer confidence in Queensland and NSW. The quote below is from the latest Dairy Australia Situation and Outlook report (the September update) and it paints a far more accurate picture.

"Farmers in NSW, Queensland and Western Australia continue to be affected by the fall-out from supermarket private label supply contract changeovers and discounting. This is certainly impacting confidence and the short and long term production prospects in these regions. A large proportion of farmers surveyed in these domestically-focussed states cited milk price as their main challenge for the coming six months."

It is also worth noting that we are now seeing the predicted shift in milk sales from family owned corner stores and other small businesses to the major retailers. The quote below is again from the latest Dairy Australia Situation and Outlook.

"Milk sales through the grocery channel which - includes major supermarkets - have continued to rise in the last quarter - up 6 7% - as continued supermarket discounting of private label products encourage supermarket milk purchases. However sales through nongrocery channels, such as convenience stores and foodservice outlets have fallen by 3.1% - indicating a significant shift in milk sales to the supermarket channel."

Coles also quotes from the June 2011 Dairy Australia Situation and Outlook report attempting to imply there is an over-supply of milk in the key drinking milk markets. This again is simply not correct. The first table at attachment 1 shows south-east Queensland and northern NSW milk sales and farm milk supply as a % change in monthly production and sales to January 2011. It clearly shows there was no oversupply of milk in this key drinking milk region in the period before they dropped the price to unsustainable levels, which is contrary to Coles' assertions. The second table at attachment 1 shows Queensland milk production versus packaged milk sales. This again demonstrates that Coles' arguments are baseless.

Finally ADF notes that Coles' estimates that Australian consumers "have now saved approximately $175 million in grocery bills as a result of lower milk prices initiated by Coles and followed by our competitors."

Coles does not provide any evidence to back up this claim, again displaying their ongoing lack of transparency. It would be appropriate for the Committee to seek such evidence given the nature of the claim and the lack of evidence for Coles absorbing the cost of their marketing tactic in cutting the price of milk to an unsustainable $1 per litre.

ADF does not believe that Coles is absorbing the cost of this marketing tactic. It is ADF's belief that Coles' customers and dairy farmers are paying for the unsustainable drop in the price of home brand milk. Evidence is supplied in ADF's submission on pages 25 and 26 that appears to refute Coles claim to be absorbing the cost.

Coles' decision to cut retail prices for drinking milk is clearly driven by a desire to expand its market share of domestic retail food sales at the expense of retail competitors (supermarket, corner stores and home delivery suppliers). This decision was made either with a poor understanding of, or no regard for the impact on dairy farmers, milk processors, local corner stores, independent service stations or the tens of thousands of other workers who depend on milk for their livelihood.

If you require any further information or wish to discuss these matters please do not hesitate to contact me on (03) 8621 4200.

Yours sincerely,

Chris Griffin
ADF President

Attachment 1