

IN THE AUSTRALIAN COMPETITION TRIBUNAL

of 2013

MURRAY GOULBURN CO-OPERATIVE CO LIMITED

**RE: PROPOSED ACQUISITION OF WARRNAMBOOL CHEESE
AND BUTTER FACTORY COMPANY HOLDINGS LIMITED**

Certificate identifying annexure

This is the annexure marked RAP39 now produced and shown to Robert Arthur Poole at the time of signing his statement on 28 November 2013.

Annexure RAP39

Extract from the Victorian Department of Environment and
Primary Industries website regarding United Dairy Power

Filed on behalf of Murray Goulburn Co-Operative Co Limited

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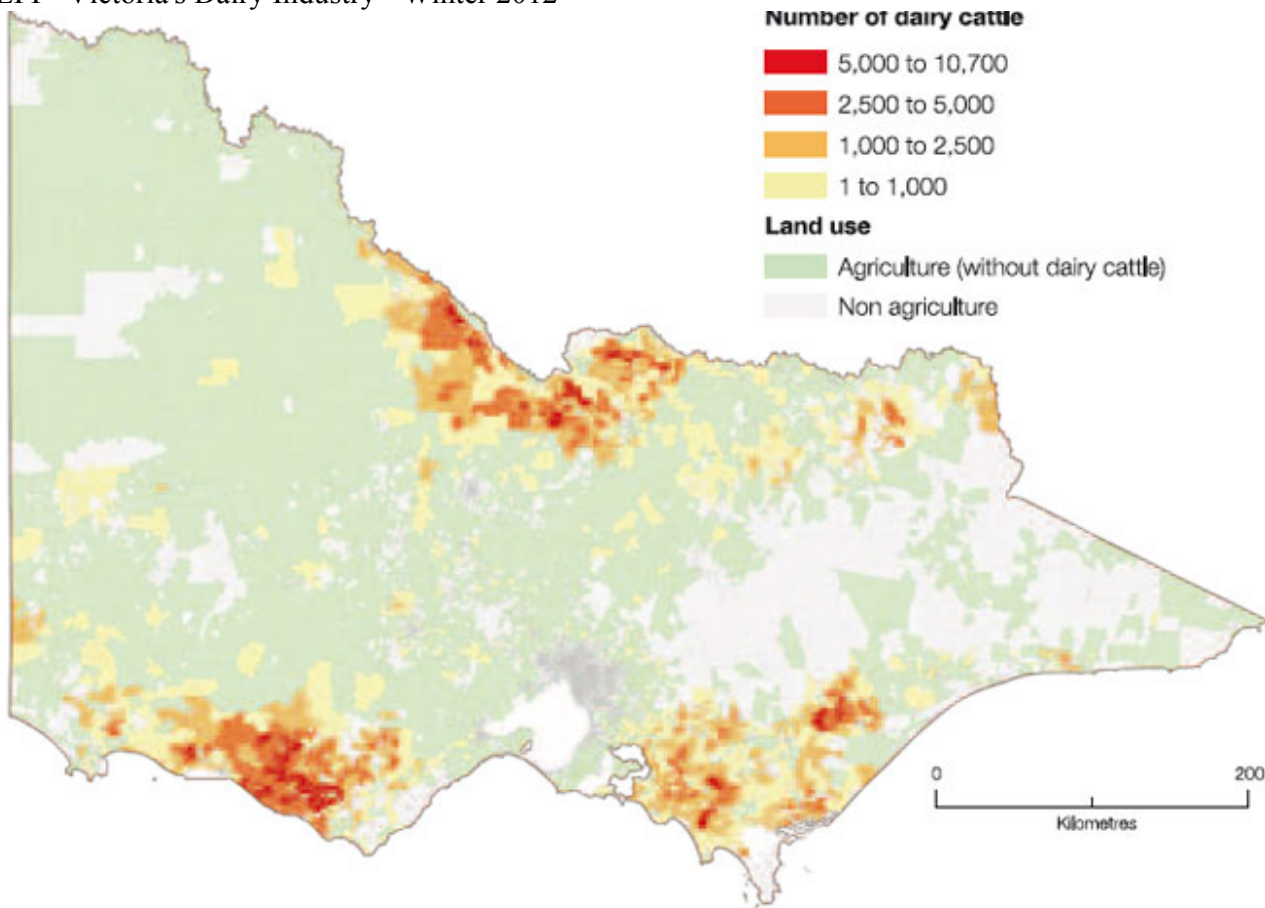
Victoria's Dairy Industry - Winter 2012



Key points

- This Dairy Industry Profile provides an overview of the location, structure and financial performance of Victoria's dairy industry.
- The dairy industry is Victoria's largest rural industry, with a gross value of raw milk production of around \$2.48 billion in 2010-11. The industry is mature, well resourced, well organised and internationally competitive.
- In 2010-11, Victoria produced 5.91 billion litres of raw milk from a dairy herd of around 1 million.
- Between 2009-10 and 2010-11, declining milk production in northern Victoria stabilised at 1.67 billion litres as seasonal conditions and water allocations improved. Early milk production figures for northern Victoria suggest milk production could increase in 2011-12 for the first time in five years.
- Milk production figures for North Victoria suggest production could increase in 2011-12 for the first time in five years, with year to date milk production 15.4 per cent higher to April 2012 than in April 2011.
- Victoria produces around 86 per cent of Australia's dairy product exports, worth around \$1.96 billion in 2010-11. As a result, returns to farmers are strongly connected to world dairy commodity and exchange rates.
- Conditions for the Victorian dairy industry have been favourable in 2011-12 with good irrigation water allocations, improved on-farm pasture/feed production, relatively low grain and hay prices and a stronger milk price. However, southern milk production regions faced slower starts to the season following heavy rainfall and flooding in early 2011.
- The high Australian dollar and recent decreases in international dairy product prices continue to present challenges to the ongoing stability of farm gate milk prices.

Figure 1: Victoria's raw milk production regions¹



Location of Victoria's dairy farms

Victoria's dairy farms are predominantly located in the North, South-West and Gippsland regions (Figure 1). The Northern region is predominantly irrigated farms, while the South-West and Gippsland are mainly dry land farms. The Macalister Irrigation District is the major irrigated dairy region in Gippsland.

Structure of Victoria's dairy industry

There are around 4,588 farms in Victoria – spread relatively evenly between the three production regions². In 2010-11 the Victorian dairy herd totalled around 1 million head.

Farm numbers have declined over time as the dairy industry has consolidated and improved economies of scale. Average dairy herd sizes more than doubled between 1980 and 2007, while farm numbers more than halved.

Dairy producers in Victoria can sell to either liquid milk or manufactured dairy product processors. Dairy product manufacturers utilise around 92 per cent of Victorian raw milk production. Manufacturing plants are generally located near or in production regions, while liquid milk processing plants are usually located near major population centres. There are more than 20 major milk processing plants in Victoria.

Table 1: Milk processors share of production (Australia)

	Milk volume supplied directly 2010-11 (billion litres)
Murray-Goulburn Cooperative	2.8
Fonterra	1.7
National Foods	1.6

Warrnambool Cheese and Butter Factory	0.8
Parmalat	0.5
Bega Group	0.5
United Dairy Power	0.2

Source: Dairy Australia – Situation and Outlook 2011

Victoria's raw milk production

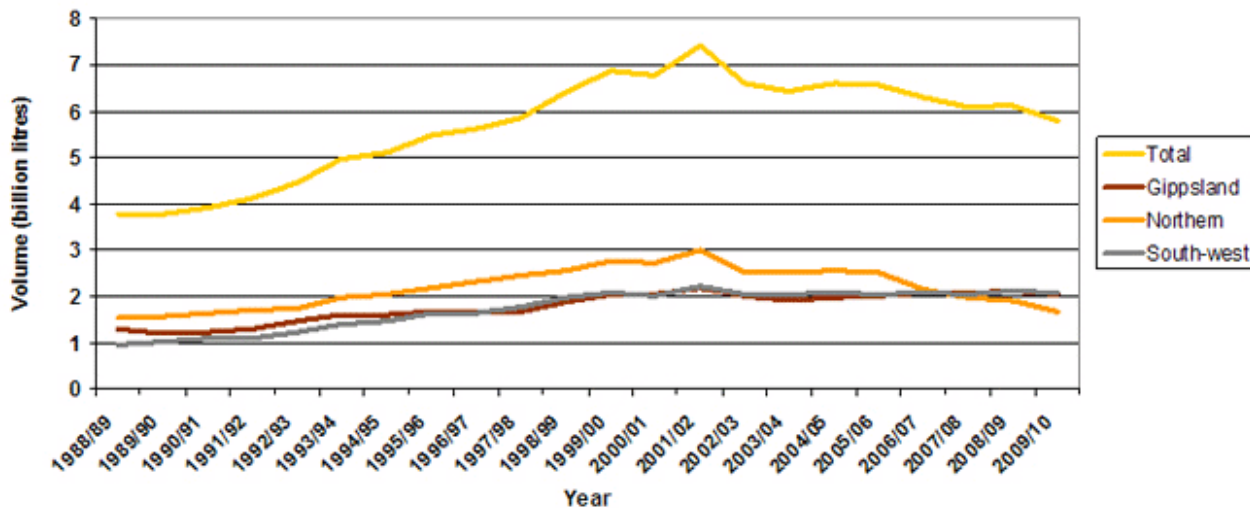
Victoria's raw milk production peaked in 2001-02 at 7.4 billion litres – more than double the 3 billion litres produced in 1980-81. Yield per cow also increased from 3,012 litres in 1979-1980 to 5,824 litres in 2010-11.³

Between 2001-02 and 2009-10, drought conditions and shortages in water allocations were the primary drivers of a 1.6 billion litre decrease in raw milk production (Figure 2). Due to its reliance on irrigation water, the North bore 1.3 billion litres of this decline, while the dairy industries in Gippsland and the South-West regions experienced less severe production declines because of more reliable water supplies and less exposure to drought conditions.

In 2010-11, Victorian milk production increased to 5.91 billion litres from 5.79 billion litres in 2009-10. This reflected a 2 million litre increase in the South-West, a 100 million litre increase in Gippsland and the stabilisation of production in the North Victorian industry.

Milk production figures for North Victoria suggest milk production could increase in 2011-12 for the first time in five years. In the first ten months of 2011-12, milk production was up 15.1 per cent on the previous year in the north, up 3.6 per cent in the South-West and down 1.2 per cent in Gippsland.

Figure 2: Victorian Raw Milk Production



Domestic and export demand for Victorian dairy products

In the last two years, around 45 per cent of Australia's total milk production has been used to manufacture dairy products for export. Australian dairy exports account for 8 per cent of products entering world trade and are worth around \$2.75 billion. The other large suppliers in the world market are New Zealand (35 per cent), the European Union (34 per cent) and the United States of America (11 per cent)⁵.

Victoria's dairy product exports in 2010-11 were worth \$1.96 billion. Victoria supplies around 86 per cent of national

In 2010-11, the main markets for Victorian dairy products, by value, were Japan (18 per cent), Singapore (9 per cent), Indonesia (8 per cent), and China (7 per cent). Greater China (which includes mainland China, Hong Kong and Macau) is the fastest growing export market for Australian dairy products⁶.

The domestic market is also an important consumer of manufactured and liquid milk products. Despite the recent instability in financial markets leading to conservatism in expenditure and a shift to cheaper eating options, domestic demand remains relatively strong – particularly in the supermarket sector.

Table 2: Victorian exports of dairy products 2010-11

	Volume (tonnes)	Value (\$AU million)
Butters, fats and oils	48,249	230
Cheese and whey products	159,275	641
Milk and cream	295,622	975
Milk extracts	7687	70
Yoghurt and Fermented drinks	13,040	42
Total	523,872	1957

Source: Department of Primary Industries Victoria, Victorian Food and Fibre Export Performance, 2010-11 Financial Year

Prices

Farm gate milk prices for liquid milk are usually higher than manufacturing prices, as farmers are required, under contract, to supply on a continuous basis across the year.

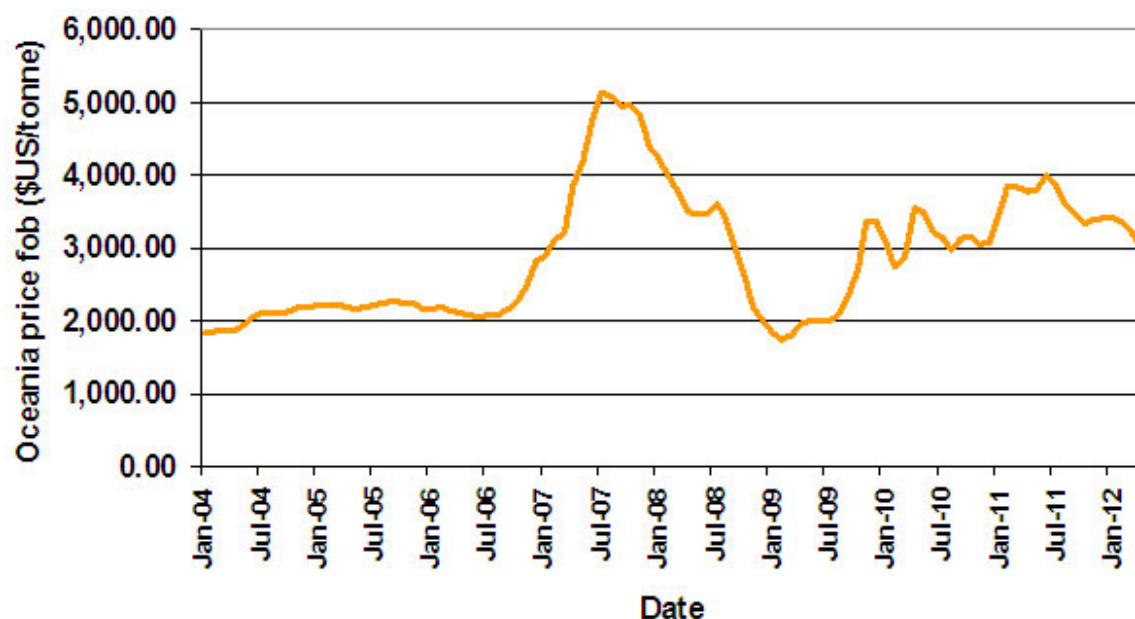
However, the liquid milk market consumes only 8 per cent of Victorian production, so the majority of farmers supply to the export reliant manufacturing sector. As such, farm gate prices in Victoria are strongly influenced by world dairy product prices and exchange rates. Historically, farm gate prices have followed world prices with only a small lag.

Farm gate milk prices have remained fairly strong since 2010-11 on the back of international demand for dairy products. 2010-11 opening farm gate prices were in the range of 34 to 36 cents per litre and closed at around 41 cents per litre. 2011-12 opening farm gate prices were around 37 cents per litre.

International dairy product prices have remained relatively strong over 2010-11 and 2011-12 with the Oceania skim milk powder price averaging over \$US3000 a tonne since September 2010 (Figure 4). However, the average Oceania skim milk powder price has decreased recently and as of April 2012 it was almost US\$800 per tonne lower than in April 2011.

Although it eased slightly in late May 2012, the strength of the Australian dollar also continues to be a challenge for Victorian dairy producers and processors.

Figure 3: Victorian farm gate milk prices

Figure 4: Skim Milk Powder Oceania Indicative Export Price⁷

Total factor productivity

Across the Australian dairy sector, productivity growth between 1979-80 and 2008-09 was reported by ABARES to be 0.5 per cent. Productivity growth across the states varied significantly in that period, with Victoria the lowest with growth of 0.2 per cent.⁸

Although ABARES estimates reflect low industry wide productivity growth, a recent study conducted by DEPI indicated that for a small sample of high performing dairy farms, productivity growth for the period 2007-08 to 2010-11 in Gippsland and South-West Victoria averaged 3 per cent. Further information on the DEPI study can be found at <http://www.dpi.vic.gov.au/about-us/publications/economics-and-policy-research/2012-research-papers>.

It is believed that productivity growth in the dairy industry was restricted due to government regulation until 2000. It is also likely that adverse climatic conditions from 2002 to 2009 limited productivity growth, particularly in the North

In 2006, around 13,232 people were employed in dairy production and around 8,042 were employed in the dairy processing sector⁹. New employment figures should become available as data from the 2011 Australian Bureau of Statistics is released.

Farm financial performance

As reported in the former Department of Primary Industries' 2011 Dairy Farm Monitor¹⁰, the profitability of dairy farmers had improved with better seasonal conditions and higher milk prices. Across Victoria, earnings before tax and interest increased from 65 cents per kilogram of milk solids in 2009-10 to \$1.73 per kilogram of milk solids in 2010-11. This growth was reflected in all three dairying regions where earnings before tax and interest increased significantly despite farmers having to manage floods and locust emergencies over 2010-11. Of particular significance, the earnings of North Victorian farmers strengthened following a decade of drought in the region.

Further detail is provided at **Table 3: Farm performance – 2010-11** & **Table 4: Purchased feed costs**.

Table 3: Farm performance – 2010-11

	Victorian			Northern			South-west			Gippsland		
	08-09	09-10	10-11	08-09	09-10	10-11	08-09	09-10	10-11	08-09	09-10	10-11
Average milk sold (kg ms/cow)	498	496	493	500	515	495	510	503	491	483	472	493.6
Average herd size	330	307	305	322	282	261	384	366	369	276	268	285
Gross farm income (\$/kg ms)	6.08	5.17	6.47	6.06	5.19	6.74	6.13	5.23	6.34	6.05	5.07	6.34
Variable costs (\$/kg ms)	3.23	2.58	2.71	3.81	3.09	3.16	2.93	2.37	2.48	3.01	2.33	2.52
Overhead costs (\$/kg ms)	1.70	1.89	2.02	1.56	1.83	2.06	1.81	1.92	2.14	1.71	1.90	1.86
Return on assets % (exc. capital appreciation)	4	2.2	6.2	3	0.8	7	4	3	5.5	4	2.6	6.1
Return on equity % (inc. capital appreciation)	5	1.1	9.3	1	-3.9	12.2	7	4.2	5.7	6	2.4	10
Average equity (%)	73	64	68	67	58	66	74	66	65	78	68	74

Source: Dairy Industry Farm Monitor Project data

Table 4: Purchased feed costs

	08-09	09-10	10-11	08-09	09-10	10-11	08-09	09-10	10-11	08-09	09-10	10-11
% of feed consumed purchased	38	34	35	54	49	42	32	29	33	29	27	31
Average price (\$/t)	321	245	264	288	214	237	332	262	268	340	256	286
Average % of costs	38.3	28.5	48.1	47.6	34.6	50.8	35.4	26.7	46.2	32.8	24.7	47.2

Source: Dairy Industry Farm Monitor Project data

Input costs

The availability of key inputs for the dairy industry has remained consistent over the last 18 months, due to better seasonal conditions and water allocations.

Allocations across all irrigation systems for the 2010-11 season were 100 per cent¹¹. For several of the smaller systems, this was the first allocation they had received for five years. Allocations for 2011-12 are also at 100 per cent in all systems.

Temporary water prices have remained low and the April 2012 water price in the Goulburn Murray region was around \$9 per mega litre.¹²

Grain and hay prices have recently increased and as of 24 May 2012, wheat and barley were valued at around \$200-215 per tonne and cereal hay at between \$155-175 per tonne in the Goulburn Murray region.¹³

Government policy/regulation influences

Dairy farmers and businesses must also comply with a range of public good policies and regulations relating to food safety, animal welfare, biosecurity and the environment.

The Australian Government Senate Economics Committee inquiry into supermarket milk price decisions reported on 3 November 2011. The report noted that the price cuts were good for consumers, but had the potential to impact on dairy producers in states such as Queensland and Western Australia. However, it found there was no evidence the major supermarkets had pushed price cuts down the supply chain.

The report also recognised that dairy farmers in Victoria would not be significantly worse off because of the supermarket milk pricing decisions, because Victoria's significant exports make international prices the main determinant in farm gate prices.

The Report made several recommendations which can be viewed here: [The impacts of supermarket price decisions on the dairy industry](#)

Notes:

¹ Australian Bureau of Statistics (ABS). Based on 2006 Mesh Block Boundaries. Number of dairy cattle sourced from the 2006 Agricultural Census. Land use based on actual activity reported in the 2006 Agricultural Census. This map

- ³ Dairy Australia, Australian Dairy Industry in Focus, 2011.
- ⁴ Dairy Australia, Industry Statistics, Victoria Milk Production 2011-12 by Region.
- ⁵ Dairy Australia, Australian Dairy Industry in Focus, 2011.
- ⁶ Department of Primary Industries Victoria, Victorian Food and Fibre Export Performance, 2010-11 Financial Year.
- ⁷ Australia and New Zealand supply 45 per cent of world dairy exports.
- ⁸ Australian Bureau of Agricultural and Resource Economics and Science. Australian Commodities, March quarter 2011.
- ⁹ ABS Census Data, 2006.
- ¹⁰ The Department of Primary Industries' Dairy Industry Farm Monitor Project. The Project analyses the performance of 71 farms across Victoria's three production regions. Note: ms=milk solids.
- ¹¹ Goulburn - Murray Water.
- ¹² Dairy Australia, Production Inputs Monitor, Issue 78, 4 November 2011.
- ¹³ Dairy Australia, Grain and Hay Report, 24 May 2012

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