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Mark Allen

Conference report-Future of the dairy industry

1 Background

The dairy sector continues to be one of the key elements of the local agricultural industry, but it is a sector which is likely to experience significant changes in the coming years, not least as a result of the proposed abolition of the milk quota system in 2015.

Against this background the Ulster Farmers Union, in conjunction with DARD and key stakeholders from the dairy industry, organised a conference to consider the future of the dairy industry which took place in the Armagh City Hotel on the 8th of July 2011.

2 Speakers and key points.

All of the speakers were introduced by Clarke Black, the Chief Executive of the Ulster Farmers Union, who also acted in the role of chair and moderator for questions posed by conference delegates.

2.1 **Richard Wright – BBC agriculture correspondent**

In his presentation Richard Wright provided a broad brush overview of many of the issues affecting the dairy industry in Northern Ireland and further afield, covering issues such as the CAP, on-going CAP reform, milk quota introduction and abolition, food security, the growing world population and associated demand for food, and climate change.

2.1 Bill Mustoe – Chairman, First Milk.

Mr Mustoe provided an overview of First Milk which is GB's leading farmer owned dairy business. At present the co-operative has a membership of over 3000 farmers who supply 15% of GB's milk. Over the last 2 years the company has restructured and refocused in an effort to become more efficient, more profitable and in order to reduce company debts.

One of the key moves that the company has made is in the development of a more diverse range of products. Historically liquid milk was viewed as the gold standard but Mr Mustoe highlighted the fact that there is now more money to be made in cheese. Given this circumstance First Milk has developed a number of cheese brands including Lake District and Pembroke. Lake District cheese alone has now become a £50m brand with 1 pack being sold every 3 seconds within the UK.

The key messages from the First Milk model were that developing a range of products enabled margin and profitability and that the UK dairy industry needs to drop the island mentality and realise that there is a global market for dairy products that could be better exploited by local producers.

2.2 Key note speaker - Sir Henry van der Heyden – Chairman, Fonterra Dairy Co-operative.

Sir Henry has been the chairman of the Fonterra dairy co-op based in New Zealand since 2002. Fonterra is recognised as being the world's largest exporter of dairy produce (2 million metric tonnes annually) and is currently responsible for a 1/3 of world dairy trade.

Fonterra accounts for 10,500 dairy farmers across New Zealand and 90% of New Zealand's milk production. Any farmers wishing to join the co-op need to bring around £250k capital on entry to the business as a condition of membership. The company also has an integrated strategy for the distribution of its product which could be summarised as 75% commodity and 25% consumer.

In addition the average herd size of 350 cattle is significantly higher than the average herd size found across the UK on average and Northern Ireland specifically. New Zealand currently produces 15 billion litres of milk annually which is about 8 times the production capacity of the dairy industry in Northern Ireland.

Sir Henry revealed that New Zealand's milk production capacity is currently growing at 3% per year and this growth is projected to continue over the next 20 years and perhaps even accelerate. As a result the dairy industry forms a major part of the New Zealand economy – 3-4% of GDP (NZ\$10 billion).

In Sir Henry's opinion the development and success of the dairy industry within New Zealand has been due to a number of factors. Firstly, the mind-set of dairy farmers in New Zealand has been galvanised by the realisation that if the industry is to compete on a global market then it needs to achieve a critical mass (i.e. be large), and this realisation has created the conditions for unity and collective working. Secondly the desire for change and reform within the dairy industry in New Zealand has been driven by the farmers themselves who have a strong wish to control their own destiny. As a result of this drive Fonterra's chairman and the majority of directors must be dairy farmers, and must be elected by the dairy farmers who are co-op members.

With regard to future changes in the demand for dairy products Sir Henry highlighted the projected growth within the Asian market due to factors such as growing prosperity and a growing focus on the health and wellbeing benefits of dairy products. In India alone this demand is projected to be 45 billion litres by 2019. Fonterra's research is also pointing to the fact that the developing Asian market is likely to be willing to pay more for dairy products than the developed western world.

Fonterra's position is that this rising demand for dairy products cannot be met by the industry in New Zealand and this circumstance does present opportunities for producers in other nations and regions. By way of example for this situation Sir Henry drew attention to the fact that Fonterra is now buying 6 billion litres of milk annually from producers in countries like Australia, Chile and Brazil to meet the demand for dairy products.

In looking to the future of the dairy industry in both New Zealand and wider world terms Sir Henry outlined some of the key challenges that need to be addressed as follows:

Volatility

Market volatility continues to be a problem and is likely to be one that will not go away. Variations in the cost of inputs such as oil and fertiliser, the impacts of climate change and the actual price paid for the finished products mean that the dairy industry either needs to accept market volatility or develop and adopt mechanisms which reduce its impact.

In terms of mechanisms that can have the potential to reduce the impact of market volatility Sir Henry made reference to Global Dairy Trade (GDT) which Fonterra founded in 2008. In simple terms GDT is an auction platform for internationally traded commodity dairy products. As things currently stand GDT has become the leading price reference indicator for dairy products traded, with more than 300 bidders from over 50 countries registered to bid.

Whilst milk prices had initially fallen following the introduction of GDT, Sir Henry emphasised the benefits that the mechanism had brought to farmers in New Zealand. GDT had made the market more transparent and in requiring customers to bid and set the price for products was also effectively operating as a risk management tool for producers by reducing market volatility.

Sustainability

Customers and consumers alike are increasingly demanding and expecting sustainable production models. The dairy industry is not immune from these pressures and more needs to be done to both reduce negative environmental impacts, better manage finite resources such as water and adapt to opportunities and threats presented by factors such as peak oil and climate change.

Despite these undoubted challenges Sir Henry concluded his presentation by stating that the future for the global dairy industry was bright given the growing demand for dairy products.

2.3 Jim Nicholson MEP

Mr Nicholson gave conference delegates an update on his work in the European Parliament relating to the future of the dairy industry. As the rapporteur for the recent report into contractual relations in the milk and milk products sector Mr Nicholson outlined some of the likely changes and challenges facing the sector over the coming years and post the abolition of milk quotas in 2015.

A key consideration according to Mr Nicholson was the need to resolve the mechanics of the milk quota situation before the CAP reform proposals appeared this Autumn. In addition there is an on-going need to ensure that any proposals emerging from Europe on dairy contracts need to deal effectively and practically with the issue of producer-retailer relations, which Mr Nicholson felt were currently too heavily weighted in favour of the retailers, a situation which was to the detriment of producers and the long term sustainability of the industry within Europe.

In contrast with the earlier speakers Mr Nicholson also cautioned delegates on the risks posed to the local dairy sector by an open market for dairy products given the small scale of the local industry which could make it hard to compete on a global level.

2.4 Vincent Gilhawley – Chief Executive, Town of Monaghan Co-operative

In his presentation Mr Gilhawley provided an insight into the operation of the Town of Monaghan Co-op established in 1901 which has a current turnover of €175 million. The business which has 651 milk suppliers in Northern Ireland and 400 within the Republic of Ireland is effectively gearing up for the abolition of milk quotas in 2015, which have severely restricted milk production within the Republic of Ireland.

The issue of market volatility was highlighted by Mr Gilhawley as a challenge that the dairy industry faced and he was able to illustrate the issue by referring to the milk price variation found in the United Action in Northern Ireland. In April 2006 milk was achieving 16.22p per litre whilst just over a year later in August 2007 the price was 37.49p per litre.

Looking to the future for the industry Mr Gilhawley made reference to the Irish Government's Harvest 2020 report which calls for a 50% increase in Irish milk production by 2020. In highlighting this opportunity for growth he raised the question as to how this might impact on Northern Ireland in terms of the need to increase processing capacity.

Mr Gilhawley also drew attention to the findings of a Teagasc study into the international competitiveness of the Irish dairy sector at farm level. This study revealed that on a cash costs basis the Irish dairy sector is amongst the most competitive within the EU. However on a full economic costs basis this advantage deteriorates, whilst productivity on a per hectare and per labour unit basis is low relative to the EU 15.

Overall Mr Gilhawley struck a positive and optimistic note for the future of the Irish dairy sector within the caveats that 90% of production will need to be exported, that the industry will predominantly be in the commodity market and that commodity markets are cyclical.

2.5 John Moloney – Group Managing Director, Glanbia

Glanbia is an international nutritional solutions and cheese group headquartered in Ireland with over 4,300 employees worldwide. In 2010 the business generated revenue of €2.5 billion and is currently the largest cheese producer within the British Isles and Europe's number one supplier of pizza cheese.

Mr Moloney revealed that Glanbia is currently actively engaged in planning for the market post milk quota abolition in 2015. Key issues being looked at by the company include milk supplier intentions post 2015, market demand and dynamics, products mix options, plant and processing requirements and funding requirements and options.

In terms of market development Glanbia were undoubtedly looking towards a strategy based on both the domestic and export markets with the majority of the volume growth in demand for dairy products likely to be outside the EU, with Asia providing the particular focus.