# Cover image for the Australian Government Productivity Commission Inquiry Report titled Relative Costs of Doing Business in Australia: Dairy Product Manufacturing: 10 October 2014.Australian Government Productivity Commission Inquiry Report titled Relative Costs of Doing Business in Australia: Dairy Product Manufacturing: 10 October 2014.

Commonwealth of Australia 2014

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| The Productivity Commission |
| The Productivity Commission is the Australian Government’s independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians. Its role, expressed most simply, is to help governments make better policies, in the long term interest of the Australian community.  The Commission’s independence is underpinned by an Act of Parliament. Its processes and outputs are open to public scrutiny and are driven by concern for the wellbeing of the community as a whole.  Further information on the Productivity Commission can be obtained from the Commission’s website (www.pc.gov.au). |
|  |

# Foreword

The dairy industry is Australia’s third largest agricultural industry and had output with a wholesale value in excess of $13 billion in 2012‑13. A substantial part of the Australian dairy product manufacturing industry is firmly integrated in global markets, with about 40 per cent of output (in milk equivalent terms) exported. International competitiveness is critical for the industry’s prospects in the face of strong global competition.

The Commission was tasked by the Australian Government to undertake a study of the cost structures faced by dairy product manufacturing businesses in Australia, and, where relevant, identify areas of cost advantage or disadvantage relative to international competitors.

An issue that constantly arose during the study was the model offered by Fonterra in the New Zealand dairy market. The Commission has provided comment on the factors involved in establishing Fonterra and their relevance to Australia.

The study has found that some cost pressures on the dairy product manufacturing sector may warrant corrective action by government, but most costs are largely driven by market factors and the commercial decisions of businesses, where policy interventions are not warranted. Manufacturers and farmers will need to continue innovating and improving the efficiency of their cost structures.

The Commission is grateful to the stakeholders who participated in this study, especially those who provided written submissions.

The study was undertaken by a team in the Commission’s Melbourne office, led by Clare Sibly and including Genesis Buchanan, Imogen Curtis, Carole Gardner, Peter Garrick, Brad Griffiths, Greg Thompson and Henry Williams. Valuable advice was provided by Lisa Gropp.

**Peter Harris**

Chairman

September 2014

# Terms of reference

I, Joseph Benedict Hockey, Treasurer, pursuant to Parts 2 and 4 of the *Productivity Commission Act 1998*, hereby request that the Productivity Commission undertake a study into the cost structures of the dairy product manufacturing industry and the retail trade industry, including costs relative to international competitors, where relevant.

### Background

A sound understanding of the cost structures of Australian businesses, including costs relative to any international competitors, can provide valuable insights for considering policies to support living standards and economic growth.

### Scope of the research study

In undertaking the study, the Commission should:

1. Undertake a case study of the costs (such as costs relating to capital, labour, intermediate inputs including energy, taxation, superannuation and/or regulatory compliance) facing businesses operating in Australia in the dairy product manufacturing industry and in the retail trade industry.
2. Where relevant, identify areas of cost advantage and disadvantage for these businesses compared to international competitors.

### Process

The Commission should consult as appropriate and provide an interim report drawing on submissions and a final report.

The interim report should be published within two months of receipt of this terms of reference. The final report should contain findings and be provided to the Government within six months of receipt of this terms of reference.

The final report will be published.

**J. B. HOCKEY**Treasurer

[Received 7 April 2014]

Contents

Foreword iii

Terms of reference iv

Abbreviations and explanations vii

Glossary viii

Overview 1

Findings 23

1 About the study 27

1.1 The Commission’s task 27

1.2 The Commission’s approach 27

2 Australia’s dairy product manufacturing industry 33

2.1 Dairy product manufacturing 34

2.2 Raw milk production 46

2.3 Domestic and export markets 53

2.4 Key dairy producing countries 62

3 Costs of dairy product manufacturing 67

3.1 Cost structure of dairy product manufacturing 68

3.2 Factors underlying the cost structure of dairy product manufacturing 72

4 Raw milk production in Australia: costs, volumes and seasonality 85

4.1 Raw milk production costs 86

4.2 Raw milk volumes and seasonal variability 94

5 Opportunities and challenges for the dairy industry 109

5.1 Achieving dairy manufacturing efficiencies 110

5.2 Achieving ongoing productivity growth 124

5.3 Getting more value from raw milk 133

6 Potential policy refinements 137

6.1 Good practice policy making 138

6.2 Energy policy 141

6.3 Trade access 150

6.4 Urban and rural water supply 160

6.5 Workforce issues 164

6.6 Transport issues 170

A Conduct of the study 177

B Economics of dairy markets 179

References 185

# Abbreviations

ABARES/ABARE Australian Bureau of Agricultural and Resource Economics and Sciences (previously the Australian Bureau of Agricultural and Resource Economics)

ACCC Australian Competition and Consumer Commission

ADIC Australian Dairy Industry Council

AFGC Australian Food and Grocery Council

ASX Australian Stock Exchange

cpl cents per litre

CSIRO Commonwealth Scientific and Industrial Research Organisation

EU European Union

FIRB Foreign Investment Review Board

FSANZ Food Standards Australia New Zealand

FTA free trade agreement

GM genetically modified

kt kilotonne

LHS left hand side

LNG liquefied natural gas

MG Murray Goulburn

NFF National Farmers’ Federation

R&D research & development

RHS right hand side

SMP skim milk powder

UHT ultra heat treated (to extend shelf life)

UDV United Dairyfarmers of Victoria

VET vocational education and training

VFF Victorian Farmers Federation

WCB Warrnambool Cheese and Butter

WMP whole milk powder

# Glossary

|  |  |
| --- | --- |
| Bargaining group | A group of farmers who bargain collectively (rather than individually) with dairy product manufacturers to negotiate the terms and conditions of raw milk supply |
| Branded milk | Milk sold under the manufacturer’s brand name |
| Collective bargaining | When two or more businesses negotiate a deal for the sale or purchase of products or services with a common customer or supplier |
| Co-operative | Manufacturer jointly owned by a group of farmers |
| Dairy product manufacturers | Entities that manufacture dairy products using raw milk (includes drinking milk processors) |
| Farmgate price | Price paid by manufacturers to dairy farmers for raw milk |
| Manufactured dairy products | Fresh and long-life drinking milk products and other dairy products such as butter, cheese and milk powder |
| Private label milk | Drinking milk products sold in supermarkets under the supermarket’s brand name (also called generic or home brand milk) |
| Raw milk | Milk that has not been pasteurised |