

## CHAPTER EIGHT

### CONCLUSIONS AND RECOMMENDATIONS

*Farmers, including dairy farmers, are price takers. Processors and retailers are price setters. The processors and retailers will 'walk all over' the dairy farmers unless there is regulation. Modern dairy farms are essentially very efficient. They just need the right economic guidelines within which to operate. That part is the Government's responsibility.<sup>1</sup>*

#### The beneficiaries of regulation

8.1 At present it could be argued that the beneficiaries of a regulated market milk industry are:

- a) farmers, through ensuring an appropriate return on their investment, both capital and labour;
- b) the consumer, by guaranteeing year round supply of quality milk at a reasonable and steady price;
- c) the regional economies which are heavily dependent on the dairy industry.

8.2 It seems certain that farmers and regional economies will suffer under deregulation and, at best, the position of the consumer will not be improved. The winners from deregulation in the short term are the two major co-operatives, other processor and manufacturing companies, if they can maintain supply and perhaps some Victorian farmers, depending on their individual circumstances. Long term beneficiaries may be the Australian dairy industry as a whole, but that will depend to a large extent on reforms at international level which will provide Australian farmers and manufacturers with a more level playing field.

8.3 An early submission to the inquiry encapsulated the views of many of the farmers and organisations appearing before the committee:

Australian dairy farmers receive no outside of industry subsidies and 60% of our product is exported against our competitors who are subsidised and protected by trade barriers particularly in the EU and USA. The playing field is not level. How good does the Australian dairy farmer have to be to export at a price to return a reasonable investment on capital? We are getting a pittance now and deregulation as it appears will decimate the

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1 Evidence, 22 July 1999, p 423

industry. The job is hard and the returns too low for the capital and labour expended.<sup>2</sup>

8.4 Concerns about industry control and the lack of competition were echoed in many submissions. They suggested that the control which regulation currently provides will shift to the processors and large retailers, who will be able to dictate terms to the industry and the marketplace. This is a matter of serious concern to the Committee.

8.5 Many of the witnesses and submissions have requested the Commonwealth Government to demonstrate some 'political courage' and take an appropriate leadership role by intervening in the deregulation process, in the interests of the dairy industry and the regional areas which are dependent on that industry:

No other country in the civilised world that I know of would treat their farmers like this. They would have said, 'No, let's work it through.' The World Trade Organisation and GATT and all of these things are staged. We were saying that we needed time. We are saying that this package buys us some time because it injects some capital. Otherwise, we should have had the time to do this in a structured way.<sup>3</sup>

8.6 The Committee considers that it is appropriate that the Commonwealth undertake such a leadership role in this matter of national importance and ensure that the transition to deregulation is managed in a structured and orderly manner..

8.7 A number of questions were posed to the committee at the commencement of its inquiry:

- *Could a case be made on national interest grounds to continue or discontinue intervention?*
- *In any event, will market forces, sooner or later, force deregulation?*
- *If they do, is a managed outcome with a soft landing preferable to a commercially driven crash;*
- *Is the proposed adjustment package, big as it is, enough?*<sup>4</sup>

8.8 The Committee concludes that sooner rather than later the market will force deregulation and that a managed outcome with a soft landing is preferable to a commercially driven crash. The Committee also concludes that the proposed adjustment package will need significant refinement – there are questions in relation to its adequacy, targeting and the extent to which it fails to address the regional implications of the deregulation of the dairy industry which require determination.

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2 Murray Bray, Submission no 2

3 RRAT, 23 July 1999, p 454

4 RRAT, 1 July 1999, p 80

## **Commercial Pressure, National Competition Policy and the Public Interest**

8.9 Commercial pressure for deregulation has emanated from the two major co-operatives, Murray Goulburn and Bonlac, which have seized the opportunity under National Competition Policy arrangements to press for deregulation.

8.10 However the Committee considers that the argument used by the Victorian industry that market milk in states other than Victoria is subsidising manufacture milk in those states is flawed. It may be that it is not a question of the market milk sector subsidising the manufacture milk sector, but that the manufacture milk price is depressed because of unfair competition at the international level.

8.11 Prices used in the manufacture of product for export are determined by the prevailing international price, which is itself determined by product produced in corrupt and subsidised economies. The international market for dairy products will never be free from corruption. Australia must significantly increase the resources it is applying to international trade negotiations to reduce the level of government subsidies enjoyed by dairy producers in corrupted economies. Ultimately, Australia, given its dependency on the export market, must ensure that it acts in accordance with WTO principles and is not subject to retaliation in the international marketplace. However, the Committee notes that, notwithstanding Australia's vulnerability in that international marketplace, there is a detrimental effect on domestic prices from the low international price, which is determined unfairly from Australia's point of view.

8.12 The Committee acknowledges that there are two drivers of deregulation – commercial pressures and the **National Competition Policy Reviews**. Despite ADIC's assertion at public hearing that the NCP reviews could be put to one side, and that commercial pressures were the primary driver behind deregulation, the Committee is of the view that, notwithstanding those commercial pressures, deregulation would not take place as precipitously as it appears it will without the justification of the NCP reviews.

8.13 However, the Committee is deeply concerned that insufficient consideration may have been afforded the 'net community benefit/public interest' and how that concept is determined. The 'flexibility' of the public interest test and the limited way in which the test has been applied in the Victorian review in particular, detracts from the findings of those reviews, notwithstanding the National Competition Council's assessment of the state reviews and its support for the rigour of the CIE's report for the Victorian Government.

8.14 The Committee is strongly of the view that the NCC's 'net community benefit' test has been ill defined and that both state review bodies and the NCC itself are taking too narrow a view of 'net community benefit'. The Committee believes that the Council Of Australian Governments [COAG] should seek to clarify the concepts of public interest, public benefit and net community benefit. It is the Committee's view that it may be problematic to continue to leave the responsibility for the public interest test solely with the states and territories.

*National inquiry/Survey of Dairy Farmers*

8.15 Many submissions and witnesses called for a national inquiry prior to deregulation, given the enormity of the consequences that course of action will have and the difficulty of reversing those consequences once deregulation takes place. The Hon Ian Robinson suggested that:

...a full national inquiry into the state of the industry and its future should be undertaken before any decision on the package is made. Notwithstanding the present attitude of certain sections of the Victorian industry and the concern of other states that interstate trade competition in milk sales would rise because of the provisions of section 92, a national inquiry with appropriate terms of reference and a responsibility to make a recommendation for the future wellbeing of the industry would be a practical course to adopt.<sup>5</sup>

8.16 A common criticism was the lack of input in relation to deregulation that the producer sector was able to have. It was generally agreed that, while farmers were advised in relation to the courses of action which had been decided by their respective representative associations, they were not party to a complete consultation process, whereby their views were sought and included in an agreed position. Witnesses from New South Wales, Victoria and Tasmania all claimed the processes had been deficient.

8.17 A national plebiscite was often suggested as a means of assessing farmer support for deregulation. The Committee considers that a simple vote on deregulation would not be helpful. However, a survey of all registered dairy farmers and share farmers, developed properly and covering a wide range of issues, may be useful for assessing the views of farmers in the different states on the future of their industry. In particular, the survey should cover the following issues:

- a) The effectiveness of industry representatives and the extent to which dairy farmers are consulted or advised about significant policy changes and other matters of importance;
- b) Views on deregulation and world trade reforms, including options to full deregulation such as a national market milk pool
- c) Investment and farm planning information, especially debt levels, investment undertaken over the last five years and plans for the future;
- d) How adjustment assistance would be used, should a re-structure package eventuate in the event of deregulation on 1 July 2000 or at any time in the future.

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5 Evidence, 6 July 1999, p 378-9

8.18 The Senate inquiry involved 12 hearings in every Australian state, attracted 116 written submissions and generated 681 pages of transcript of evidence from 99 witnesses. The Committee is of the view that this has been an exhaustive process, thoroughly exploring all key issues relating to the proposed deregulation of the Australian dairy industry.

8.19 The Committee is of the view that this body of information provides governments, both Commonwealth and state, with a sufficient basis to properly develop and implement appropriate measures to support continued change in this key rural industry.

8.20 The Committee notes, however, that some submissions have proposed a survey or plebiscite of dairy farmers to assess their views on the deregulation of the industry. The Committee considers this is a matter for individual states.

#### *Regional impacts*

8.21 The Committee also considers that both Commonwealth and state governments have sufficient understanding of regional adjustment issues to jointly develop, in consultation with local government authorities and the industry, a comprehensive and properly funded regional adjustment package to support those communities effected by the further deregulation of the dairy industry.

8.22 The Committee considers that a regional adjustment package must be finalised before 1 July 2000 and funding for it provided in the next federal and state budgets.

#### *NCP Penalties*

8.23 Given the findings of the Victorian National Competition Policy legislation review, the Committee acknowledges that if the Victorian Government maintains regulation, it may be faced with a financial penalty under the Competition Principles Agreement. However, the Committee is concerned that the parameters of the 'net community benefit' test, ie its confines to the individual state and the inability of the current process to accommodate a national community benefit perspective, renders the entire NCP legislative review process defective. The Committee considers that, before any penalty is imposed, the Government should undertake the national assessment recommended above and defer any penalty until all States and the Commonwealth have developed a national strategy for deregulation.

#### *Domestic Market Support Scheme*

8.24 There appears to be less justification now than in 1995 for the extension of the DMS Scheme, given the expansion in Australian milk production, from 6,038 million litres in 1986 to 9,440 million litres in 1998, which has negated the effect of the scheme, and required payments to be spread across a greater volume of milk. The Committee is not convinced that extending the scheme beyond 30 June 2000 would be beneficial.

### **Timing of deregulation**

8.25 There seems to be no doubt that the Australian dairy industry will become a fully deregulated industry over time. The real point at issue is the timing of deregulation – whether there should be full deregulation now, whether it should be delayed completely for several more years or whether some sort of staged deregulation is an option.

8.26 Whatever the timing of deregulation, it will be beneficial if it is co-ordinated rather than taking place on an ad hoc basis as a response to Victoria's own position. The Australian Dairy Corporation suggested that a co-ordinated transition to deregulation is desirable:

If the transition phase is characterised by uncoordinated state-by-state deregulation, the commercial activities of individual firms are likely to exert significant pressures on state-based regulations. This, in turn, will intensify the adjustment pressures on all sectors of industry. It would also maximise short-term dislocation in a number of dairy production regions. A more coordinated transition to deregulation will help smooth industry restructuring and allow participants to make more effective decisions on future resource allocation.<sup>6</sup>

8.27 The Committee considers it to be the responsibility of the Commonwealth Government, not the industry or individual state governments to coordinate the orderly transition of the dairy industry to a deregulated environment.

8.28 As this is a matter of some urgency, it is the strongly held view of the Committee that a more urgent approach is required by the Commonwealth and the States.

8.29 While the Committee notes that a staged approach to deregulation may moderate its immediate effects and allow farmers more time to restructure their businesses, a one off, properly designed, adequately resourced and fully coordinated approach to deregulation is the preferred approach, should deregulation occur on 1 July 2000.

### **Recommendation 1**

8.30 The Deputy Prime Minister and Minister for Transport and Regional Services and the Federal Minister for Agriculture, Fisheries and Forestry Government call, as a matter of urgency, a meeting of state Agriculture and Regional Development Ministers to determine a framework, and a timeframe, for the co-ordinated deregulation of the Dairy Industry.

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6 submission 93, p 9

### **Full deregulation from 1 July 2000**

8.31 The Committee recognises that the conditions required by the ADIC package may be met and that full deregulation might still occur on 1 July 2000. In this event, the Committee has several concerns in relation to the re-structure package, particularly:

- a) The quantum of the package;
- b) The taxation status of the package;
- c) Arrangements for the administration of the scheme;
- d) whether there is a need for quota holders to be compensated by individual state governments for the investment they have made in that capital asset.

8.32 Given the lengthy lead times involved in many aspects of production, the Committee is concerned at the potential that deregulation of the farmgate price has for disruption of the dairy industry as a whole, to individual farmers and to the communities where dairying is a significant contributor to the local economy. The immediate impact of deregulation will be a reduction in aggregate farm income, which in the short term will be significant, and reductions in the capital value of assets, whether they are quota or land and equipment as well as the flow on effects to the local communities, suppliers and employees.

#### *The quantum of the restructure package*

8.33 Many witnesses and submissions expressed concern about the re-structure package, particularly its adequacy, the taxation status and any restrictions on how the package may be applied. Concerns relating to the adequacy of the package extended to:

- a) Whether the amount to be received was adequate to cover the loss of income the package is intended to address;
- b) The lack of any compensation commitment by the appropriate State Governments for loss of quota entitlement. Farmers can have anything from \$200,000 to \$1 million invested in quota, the value of which has eroded considerably since full deregulation became a probability;
- c) the administrative arrangements for the assessment and dispersal of funds under the scheme;
- d) the extent to which the areas to which re-structure funds received could be applied will be defined.

8.34 The Committee notes the revised package announced by the Minister for Agriculture, Fisheries and Forestry, but is still concerned at some elements of the package, particularly that no arrangements have been made with State Governments in relation to compensation for quota losses.

8.35 The administrative arrangements for the collection, management and payment of the funds for the package are not yet finalised and the Committee is concerned that there will not be enough time before the first payments to due be made on 1 July 2000, for the finalisation of appropriate administrative and appeal arrangements.

### **Recommendation 2**

8.36 That should administrative arrangements not be in place in time to make the first payments by 1 July 2000, that appropriate compensatory arrangements are factored into the payments schedules, in order that dairy farmers do not suffer any more financial hardship than is presently envisaged.

### **Recommendation 3**

8.37 That the states of Queensland, New South Wales and Western Australia consider the issue of quota entitlement and any form of compensation that may be appropriate for the resumption of quota entitlement, including the possibility of using NCP payments as compensation.

### **Social Impacts and a Regional Adjustment Package**

8.38 The Committee is concerned that insufficient attention has been given to the social impact of deregulation of the dairy industry and especially, the impact on many of our rural and regional communities. These communities have endured considerable economic hardship in this decade and the premature deregulation of the dairy industry may exacerbate unnecessarily current difficulties.

8.39 The Committee considers that, if and when deregulation takes place, whether it is 1 July 2000 or at some later date, the impact on rural and regional areas, particularly those areas such as the Bega Valley, needs to be fully assessed. The Committee commends the study undertaken by the Bega Valley Water Management Committee.

8.40 If such assessments indicate severe impacts on communities, appropriate assistance in the form of a regional adjustment package must be developed by both state and federal governments as part of any move towards deregulation.

**Recommendation 4**

8.41 That regional adjustment packages for rural and regional communities affected negatively by deregulation be developed by both State and Commonwealth Governments.

*Retail price monitoring*

8.42 The Committee was also concerned by evidence that suggested that the costs associated with deregulation would fall on milk producers and any benefits would not flow through to consumers in the form of cheaper milk.

**Recommendation 5**

The Australian Competition and Consumer Commission in accordance with subsection 17[1] of the *Prices Surveillance Act* monitor costs and prices in the dairy industry so that dairy farmers are not unfairly burdened with the cost of the proposed levy.

**The operation of co-operatives**

8.43 Although not a central issue to the inquiry, the Committee was disturbed by the number of comments from witnesses and in submissions which were critical of the operations of the co-operatives and their lack of accountability and transparency. For this reason, the Committee considers that it may be appropriate for a review to be undertaken in relation to the operations of co-operatives and their accountability requirements and mechanisms.

**Recommendation 6**

8.44 That an inquiry into the operations and accountability mechanisms of co-operatives be undertaken.

Senator John Woodley

**Chairman**