

A political perspective from New Zealand

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Kia Ora or a special Hello from New Zealand.

Background

It is just 200 years since the Rev Samuel Marsden bought the first two cows and a bull to New Zealand, from Sydney, for the Church Missionary Society. 152 years ago, my great-great grandfather, John Windsor Luxton, his wife and first three children arrived in Christchurch. They came from Northlew, in the heart of Devon: some of your best dairy country. My great grandfather was born in New Zealand later that year. My direct ancestors have all been dairy farmers. Today my son and daughter, both university graduates, are sixth generation New Zealand dairy farmers.

Coming to New Zealand, settlers found a country with a mild temperate climate which quickly could be transformed to pastoral farming. Initially the focus was on wool and some grains, being products with shelf life to travel the vast distance to the world marketplace. The food demands of New Zealand's small population were quickly met. The introduction of refrigeration into shipping in the 1880's allowed expansion into the export of meat, butter and cheese. We became largely a supplier to the UK market of these products. As a consequence our farming shared the pain of each economic cycle in the UK and ultimately world market.

Comment [MTS1]: ups and downs?

As a result of Britain joining the EU in the early 1970's, our dairy industry was forced to focus on other markets. Over 60% of our dairy produce was coming to the UK at that time. Ten years later the UK was still our biggest market with around one quarter (23%) of our dairy exports, as we rapidly diversified both our product range of long life dairy products and our markets. Last year, I understand that just £12m (0.2%) out of £7,100m of New Zealand dairy exports, mainly cheese, came to the UK.

World Dairy Production and Trade

World dairy production has been traditionally domestically focused, because of the perishable nature of milk. Hence, it has evolved into one of the most regulated and protected industries in most milk consuming countries. Only around 5 to 7% of world dairy production is traded internationally. The rising wealth of a middle class in Asia and the Middle East has allowed new markets to grow in the last decade. New Zealand is also fortunate to have a free trade agreement with China, which is now our largest dairy market. China is followed by the US and Japan, and New Zealand dairy produce is sold to nearly every country in the world. The New Zealand dairy industry's ability to distribute dairy products across the world is an important asset of our farmers. Over 80% of our production is still sold as commodity ingredients so there is continuing scope to increase our "value add" products, to get a greater brand presence and to continue to seek freer trade rules. All of this needs capital.

Comment [MTS2]: Useful to add in percentage of exports that go to China here.

New Zealand dairy products still face major trade barriers, particularly in developed northern hemisphere economies. However the gradual improvement in international trade rules against dumping surpluses, tighter environmental rules, and free trade agreements have opened up new market opportunities for New Zealand dairy produce. As well as China, New Zealand now has free

trade agreements with much of South East Asia, the Middle East, Australia and Chile and currently hopes to see the Trans Pacific Partnership include many more countries around the Pacific Rim in a large free trade market for our dairy produce. We were disappointed the WTO's Doha Round was not completed. So we still rely on our politicians and upon Government to improve trade access. It is a major focus of New Zealand Foreign policy.

That said, international trade barriers are gradually reducing, meaning that there is an enormous pressure for dairy industries to be able to compete, although there are still calls from some, for trade barriers to protect 'food security'. The majority of the liquid or fresh milk part of domestic dairy markets is always likely to remain local around the world. There is also an increasing confluence of milk prices around the world as subsidies become politically less acceptable.

New Zealand Dairying

The New Zealand dairy industry is now around one third larger (19.1 billion litres of milk last season) than your UK dairy industry. New Zealand has 11,800 dairy farms (herd average of 393 cows). New Zealand is the eighth largest dairy producing country but produces just 2.6% of world milk production. New Zealand's big difference is that around 95% of that milk is exported. By comparison approximately 90% of your market is domestic. In New Zealand this has meant, a totally different processing focus onto products which have shelf life. Our revenue line is dependent upon world commodity markets. These are generally buffeted by variable surpluses from the EU (139.3 billion litres) and the US (89 billion litres), our major international competitors in recent years, resulting in volatile pricing. The impact of volatile pricing from operating on the world market without subsidies has created the driver to continue to improve our farming systems. I feel sympathy for EU farmers who have been constrained from growth for 25 years by quota systems. You don't get to see change within your farm systems on an annual basis.

The relative returns for dairy farming over other land uses in New Zealand, has also seen continuing growth and innovation in our industry. Faster milking systems such as the herringbone and rotary dairy have spun out of this drive for lower cost dairying. The farming system is still largely focused around the seasonal pasture growth pattern with most dairy herds calving in spring and drying off in winter. This has led to a relatively high level of fertility in the New Zealand dairy cow (average of 4.5 lactations) and an increasing focus on crossbred Kiwicross (Friesian x Jersey) herds.

The other significant change in recent times has been the growth in dairying in our South Island from 600 million litres in 1990 to 7.5 billion litres this year, partly as a result of irrigation. This has had a very significant economic benefit to the economy, which sees our industry now producing, but when meat is included, around 30% of our country's traded export income.

Whilst New Zealand dairy farming is becoming more corporate in its model, a majority of our farms are still owner operated, which I believe still gives us a significant advantage. At the same time younger professional managers are finding dairy farming a great way to accumulate personal wealth, although high land prices and larger herds have created a barrier to farm ownership for the next generation. However, contract milking, leasing, sharemilking and equity positions still allow career progression for motivated young farmers.

The conversion of sheep, beef and arable farms to dairying is revitalising some regions of our country with increased employment, support for schooling, health and social services being retained and expanded. Such economic activity creates new employment opportunities and helps to grow rural servicing sectors.

Politics and New Zealand Dairying

The old New Zealand Dairy Board was a creature of statute, governed largely by farmers with a single seller monopsony over all dairy exports and operating a price smoothing mechanism, but always without Government subsidies. Its head office was down the road from our Parliament and it was a strong lobbyist to retain its powers of regulating dairy exports. It had had some of these powers since the 1930's, which prevented other processors from investing in New Zealand dairying. In 2001 it lost these powers and became part of Fonterra.

A decade after deregulation of New Zealand's single dairy seller, another seven dairy companies (including two co-operatives) now compete for farmer's milk. Fonterra Co-operative, our largest dairy company, currently processes around 89% of New Zealand's milk. New Zealand dairy farmers opposed deregulation at the time and now regularly complain about any form of industry regulation. New Zealand competition law still impacts on Fonterra inside New Zealand, given its dominance in the sector. Since deregulation the industry has had a significant growth spurt and its focus and head office are now in Auckland, our commercial capital. Its lobbying in Wellington is more limited, although as New Zealand's largest company, governments do listen to it.

The rural sector is now more disconnected from urban New Zealand and represents a small electoral vote. A generation ago most New Zealanders had relatives farming and better understood the rural sector. Animal welfare, health and safety, and the environment have become politically more important to the electorate than farming and export earnings.

Government has been more heavily impacted by NGO lobbying in recent years and an active Green movement. The environment is a key area of public policy and dairy growth is seen as an easy target. For example, the expansion of dairying into some of our freer draining soils with new irrigation projects has led to significant concerns around nitrogen leaching in some catchments and Government regulations have instructed Regional Authorities to maintain and enhance water quality. At the same time Government has been promoting new irrigation projects to allow intensification of land use. We are one of the richest countries for renewable water per capita in the world. We have fifty times, as much renewable water per person as China. This creates our export opportunity. New Zealand's land area is slightly larger than the UK but with only around 4.5m people compared with 60m over here and as many milking cows as people.

Another challenge is that dairying produces about 38% of New Zealand's greenhouse gas emissions, whereas for most countries it would not register as significant. Even so our system still has one of the lowest carbon footprints of any dairy industry. So utilising our resources more efficiently is a continuing drive for New Zealand dairying. The increasing concern around the environmental impact has the potential to slow growth in our dairy industry. Farmers are responding as guardians of the land by fencing off and planting riparian strips alongside waterways and investing in more sophisticated effluent disposal systems. Farmers actually do more to protect the environment than do their urban counterparts.

Maintaining the relationship with Government is also important in the area of biosecurity which still poses our biggest external risk, particularly with the increasing connectivity of our world.

In addition with land prices similar those in the UK, our industry could be seen as overpriced as New Zealand farmers have capitalised increases in production into farm prices. With the recent listing of a Fonterra unit share this may change. Our farmers tend to be asset rich but not always cash flow positive for some farmers with high debt levels. New Zealand is short of capital yet also has a difficult regime restricting Foreign Direct Investment into our farming sector. Concern about foreign ownership of land is often driven by urban groups.

Comment [MTS3]: Need to start this sentence with something to make sense of it.

Keeping New Zealand Dairying Competitive - DairyNZ

Following the removal of the New Zealand Dairy Board single seller legislation in 2001, 'industry good activities', became separated out from the commercial sector. DairyNZ is the farmer owned 'Industry Good Organisation'. Every five years all dairy farmers can vote as to whether to continue to pay a levy to fund it. Currently the levy is around £2,500 per farm, so DairyNZ is our equivalent to your 'DairyCo'. Our Dairy Farming Strategy is for 'Sustainable Dairy Farming' focusing on New Zealand dairy farming remaining competitive and being responsible. Our biggest spend is on research and development to improve our competitiveness, some of this through our own 'farm systems' research capability and some of it jointly with Government Research Institutes. Considerable research also goes into the long term sustainability issues of our industry.

DairyNZ's second largest area of spend is in education and extension. With larger and more complex farming businesses and an increasingly complex regulatory environment, the skill level of our managers has had to improve rapidly, like the systems which we operate. Unfortunately New Zealand went through a period where farming was not seen as an occupation of choice, but that is changing slowly.

Our farming systems have become more diversified in recent times ranging from all pasture through to a few farms looking at housed systems, and everything in between. An element of standoff from pasture assists with the environmental issues and an element of supplementary feeding protects the industry from animal welfare issues during dry periods of the year. However New Zealand dairying must always realise that its income is based upon international dairy prices and needs to be flexible to accommodate that volatility. It is easier to do this if capital costs are constrained and supplementary feeds are just that; supplementary to a pasture based system.

Dairy farmers like to be appreciated and recognised as doing society a service by providing exports and jobs while improving their environmental performance. However there is more we must do in this space to be ahead of our regulators.

Future Opportunities

The dairy sector is changing around the world. Half of the US's dairy farms have disappeared over the last decade as they have in many countries. To an outsider it still seems strange that 50,000 US dairy farmers as a lobby can restrict the US Congress's ability to negotiate free trade arrangements around dairying when US dairying is a large exporter in its own right. The recent IDF Conference raised questions around high intensity farming systems in the US with world grain prices moving up faster than milk prices.

Large beverage brands are moving into the milk space. Brands have enormous value in the marketplace. Pfizer's baby food business was last year, purchased for £6.8 billion, being well over twice New Zealand farmers' net asset value in Fonterra, the world's largest milk processor. (Yet a large proportion of that product is sourced from Fonterra.) The majority of New Zealand's milk is still sold as bulk commodities and the country needs capital to significantly change that. But that is not all bad. Whilst the western world may not be consuming as much milk per capita, with world dairy consumption growing by about New Zealand's total production each year, there would seem to be plenty of opportunity in the dairy industry around the world. So I am very optimistic about the future of dairying particularly from a New Zealand perspective.

We have largely got our politicians out of our dairy industry and I believe we are the better for it. We need them for trade access and in the environmental space to prevent extreme positions. They generally recognise that the dairy industry is New Zealand's most internationally competitive industry.

Comment [MTS4]: US?