THE CASE FOR THE RETENTION AND STRENGTHENING OF THE NATIONAL MILK AGENCY

IFA NATIONAL LIQUID MILK COMMITTEE

Executive Summary

- The National Milk Agency (NMA) was established in 1995 under the Milk (Regulation of Supply) Act to replace the Dublin and Cork District Milk Board in regulating liquid milk supplies in Ireland.
- It is entirely financed by farmers and industry.
- A review of state agencies as part of the Public Service Reform Plan has identified it for either abolition or merger with Bord Bia.
- IFA rejects both options out of hand.
- This is because:
    - The NMA **registers and monitors contracts** between suppliers and dairies and insists that they provide **"adequate compensation" for the significantly higher production costs** incurred by specialised liquid milk producers;
    - It provides **market transparency** for liquid milk producers by ensuring dairies' milk sales match up with milk volumes purchased under contract;
    - The Dublin and Cork Milk Boards, in their day, and the NMA in the last 17 years have been **instrumental in securing supplies** of high quality, locally produced fresh milk for Irish consumers year-round;
    - In the context of major, mostly seasonal, dairy expansion after 2015, and the extreme retail discounting by multiples and dairies, the **continued necessity for provisions securing year-round quality milk supplies** from specialist producers will get even more pressing;
    - The NMA is financed by industry and farmers and **costs the State nothing**. Abolishing it, on the other hand, would create staff related liabilities for the State;
    - Its **functions are not duplicated** by any other state or industry agency.
- Failing to continue regulating liquid milk supplies will endanger the livelihoods of just under 2,000 specialised producers, and displace an ever rising share of their supplies with imports.
- This will also have serious consequences for up to 2,000 jobs in the Republic of Ireland dairies.
- Allowing the destruction of our self-sufficiency in drinking milk would seriously challenge our credibility as a world class dairy nation with major export expansion ambitions.
- IFA wants to see the NMA strengthened, to make it fitter for purpose in the new context of dairy expansion post quota, and better able to deal with the increasingly aggressive retail discounting activities of both dairies and retailers.

Background

In 1994, the Milk (Regulation of Supply) Act was introduced, to abolish the Dublin and Cork District Milk Boards and replace them to regulate Ireland's liquid milk supplies.

The Act created The National Milk Agency (NMA). Primary producers, dairies (milk processors), consumers and distributors are represented on its board, and its main mission is to secure adequate supplies of fresh milk for the consumer market in the Republic of Ireland.

The NMA does this by registering and monitoring contracts between dairies and milk producers, and by satisfying itself that (as per the Act) the contracts *"provide adequate compensation to the producer for raw milk supplied under the contract throughout the year, taking into account, in particular, in relation to the winter months, the economic cost of production of raw milk of suitable quality for heat treatment for liquid consumption all the year round".*

The NMA further monitors sales of liquid milk by registered Republic of Ireland dairies to ensure that the volumes of milk sold by dairies into the consumer market match up with the volume of milk purchased from farmers under registered liquid milk contracts.

The NMA employs a small staff of 5, is financed in equal part by farmers and dairies, and is run without any contribution from the National Exchequer. There is no duplication between the functions of the NMA and those of any other agency in the State.

Late last year, the Government published its Public Service Reform Plan, which included the proposed rationalisation of state agencies and "quangos". In Annex 11b of this document, a proposal has been made to either abolish the National Milk Agency, or to merge it with Bord Bia.

IFA rejects both options out of hand.

We believe that neither approaches are warranted, and believe the NMA must not only be allowed continue to play its crucial part in sustaining domestic liquid milk supplies for Irish consumers, but must be strengthened to improve its ability to do so.

Why do we need specialist liquid milk producers?

Ireland's liquid milk producers are a group of around 2000 farmers who, in order to supply a set amount of milk from freshly calved cows every day of the year, have specialised their production system with split herds which are partly calved in spring, and partly in autumn.

Years ago, this specialisation was absolutely necessary to ensure that, when most milk was produced seasonally and was unsuitable for the drinking market, the consumer could rely on the high quality milk from freshly calved cows they expected all year round.

Also, many liquid milk producers have specialised because it was the best way for them to maximise output from a limited land base.

In the current context, with a 50% production increase target in Food Harvest 2020, some may want to believe that there will be more than enough milk all year round to supply the consumer market.

However, even allowing for a degree of peak management by co-ops, most of the additional milk will be produced at the lowest cost time of the year, and will remain heavily seasonal.

This will leave a big quantitative and qualitative gap over the winter months, which can only be catered for by specialist producers capable of delivering milk from freshly calved cows.

A higher cost production system receiving an ever decreasing premium

This system of farming has much higher costs, especially in terms of feed, labour and energy, than spring-calving, grass-based creamery milk production.

In 2011, IFA joined forces with Teagasc's liquid milk expert Joe Patton to identify and isolate the actual cost of producing liquid milk, separating it from the manufacturing milk element that every liquid milk producer supplies.

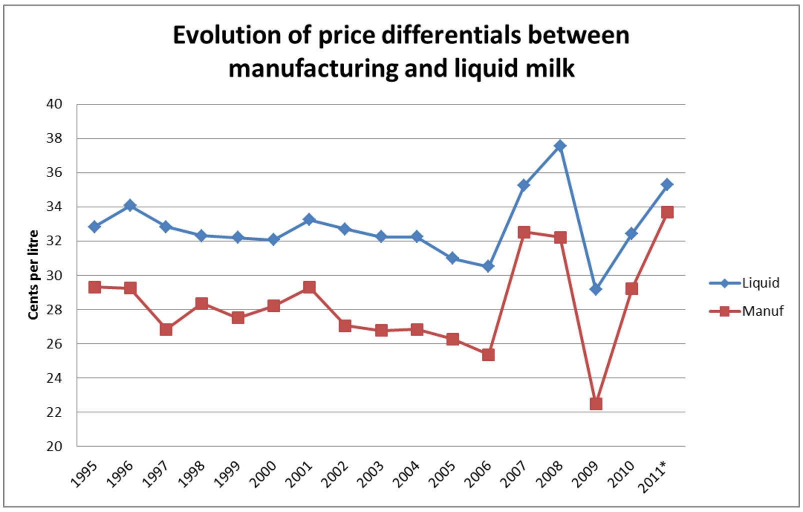
Our study was based on the results of the 2010 Winter Profit Monitor, filtered in order to most closely match the typical liquid milk production profile. Each line of cost was then critically analysed so that it would reflect liquid milk production rather than winter production.

Our study concluded that the total cost per litre of contracted liquid milk, including 7c/l for the remuneration of the farmer's own labour and 1c/l for "ticking over" re-investment on farm, was 36c/l in 2010, rising to 39c/l in 2011 due to fast rising feed, fuel and energy costs in particular.

In the past, farmers used to receive price premiums which allowed them to cover production costs reasonably comfortably especially over the winter months. In fact, the liquid milk price often cross-subsidised relatively low manufacturing prices in dealing with overall on-farm costs.

In the last few years, margins on liquid milk farms have been squeezed to unsustainable levels, due to unprecedented discounting by both dairies and retailers, and farmers have found it impossible to recoup fast rising cost increases.

To cover the bare difference in production costs, the annualised differential between the price paid for liquid milk and that for manufacturing milk needs to be between 5 and 6c/l. In the last couple of years, it has been decimated (see graph) falling to an estimated 1.6c/l in 2011. Many farmers only keep their heads above water because of relatively high manufacturing milk prices.



Source of data: National Milk Agency
*2011 NMA's preliminary estimate

However, the new volatility of both manufacturing milk prices and input costs means that a time will soon come when the lack of profitability of liquid milk will force many farmers out of the business.

Unless supply contracts reinstate appropriate levels of differentials, strengthening significantly producer prices, the Republic of Ireland's long term self-sufficiency in liquid milk will be in doubt.

Why do we need the National Milk Agency?

In the context of unsustainable discounting of milk by dairies and retailers, most dairies have downgraded the contractual arrangements they have with their liquid milk suppliers.

They have moved away from flat, liquid milk specific pricing towards prices based on premiums over manufacturing milk prices. They have removed summer premiums almost entirely, and many have reduced the number of winter months for which they pay a premium.

Their purpose in so doing is to reduce the raw material cost of milk in the context of tighter margins from the retail trade.

Eliminating the NMA would remove the last bastion against this trend, and leave liquid milk producers totally exposed to low standards of supply contracts which will not be adequate to justify their continued involvement in this costly specialised production system.

While the NMA has limited powers when it comes to enforcing a level of price guaranteeing "adequate compensation" for higher production prices, this provision in the Milk Supply Act nonetheless strengthens the hand of producer groups when they negotiate prices with their dairies.

Producer groups also benefit from the transparency provided by the NMA with regards to milk supplies purchased under contracts and retail sales. Without the pressure exercised by the NMA on dairies, producer groups would not be in a position to assess whether the volumes they are contracted for actually match up to their dairies' retail sales.

The National Milk Agency provides an invaluable forum for representatives of all stakeholders in the sector - producers, dairies, distributors, retailers and consumers - to come together.

It also makes available to its stakeholders a wealth of statistics on compared liquid milk pricing systems, differentials between liquid and manufacturing milk prices, bulk and bottled import trends and other market data.

In the absence of the NMA, the trend towards weaker contracts would in turn reduce domestic liquid supplies and leave the Republic of Ireland's consumer milk market even more dependent on imports.

This would have obvious serious consequences for up to 2,000 people employed in the year-round processing and marketing of liquid milk in Ireland.

What would it say about the world class export ambitions of our dairy industry if we let our domestic liquid milk market become totally or substantially dependent on imported milk?

Domestic liquid milk supplies add up to around 500 m litres, just under 10% of our national milk production. Liquid milk forms a vitally important part of the Irish dairy industry sector, delivering steady, valuable sales of high quality product to the consumer market.

Liquid milk sales have historically contributed a strong, steady cash flow into our dairy co-operatives, even when dairy market returns were poor.

If even a fraction of our liquid milk pool were to be displaced by lack of profitability into the creamery milk pool, the pressure this could create for our processing industry investment plans, even before 2015, would be extremely damaging to the entire sector.

Why give away a lucrative, domestic market, and reduce our expansion potential?

Neither abolition nor merger with Bord Bia make any sense

The purpose of the current proposed rationalisation of state agencies is clearly to make savings for the hard pressed tax payer.

While the National Milk Agency is a statutory body, it is actually financed equally by liquid milk producers and dairies. It does not cost the National Exchequer or the tax payer anything.

Indeed, abolishing the NMA would create National Exchequer obligations with regards to redundancies, pensions and other staff related costs.

There is therefore no advantage to the taxpayer in abolishing the NMA.

The National Milk Agency has no common area of responsibility with Bord Bia, nor does its functions overlap with those of any other state or industry agency. Therefore, there is no scope for savings for farmers and industry, in merging the NMA with Bord Bia.

IFA would also be extremely concerned at the ability of ring-fencing NMA's industry and farmer financed resources in a merger situation. IFA will not accept that the NMA could be subsumed into Bord Bia as little more than a new income stream.

Conclusion

It is very clear that the National Milk Agency continues to fulfil a most important role in the regulation of fresh, quality, locally produced liquid milk all the year round.

It is even clearer that this role is severely challenged by the rising pressure from retail discounting on the industry as a whole, and producer prices, contractual conditions and volumes.

However, the National Milk Agency is not without its issues, and every organisation benefits from regular reviews.

IFA is willing to engage actively with the Minister in a root and branch review of the National Milk Agency, not to abolish it, merge it with another agency or otherwise downgrade it, but to critically reassess its structures and workings with a view to improving them.

Our ambition for the NMA is that it would be put on a stronger statutory footing so that it can help secure volumes of milk purchased from registered, specialist liquid milk suppliers, and a fair, sustainable share of retail returns allowing farmers to recoup costs and generate a reasonable income.

We believe this is totally coherent with the Government's assurances, reiterated at the 2012 IFA AGM by Minister for Agriculture Simon Coveney, with regards to forthcoming legislation on the regulation of the retail trade.

CL/NLMC/IFA 25th January 2012