

MILK PRODUCERS MANAGING MARKET RISKS IN A DEREGULATED ENVIRONMENT*

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Changes within the supply chain as a result of deregulation have resulted in substantial new risks for milk producers. To grow in this dynamic and transitory environment, milk producers will become more responsive players in the supply chain. The strategic goal will be an effective leverage of the internal resources, buyers, suppliers and competitors to appropriate and accumulate optimal value from the supply chain. It will require effective internal and external assets management, relational competence management and superior operational performance.

Deregulation of dairy industry in Australia in mid-2000 has been the catalyst for substantial restructuring of the industry. With the withdrawal of Government from setting milk prices and supply arrangements, the relationships between the players within the industry, both new and old, are being renegotiated.

The emerging market configuration has a profound impact on the milk producers, especially in the former 'market milk' States of Queensland, New South Wales and Western Australia, as they bear the considerable brunt of the changing market scenario. There are substantial additional risks, as market milk prices fall and the differential in the farmgate prices for market milk and manufactured milk reduces substantially. Total income from milk production has been reduced in the order of 25%.

Some evident trends in the supply chain are:

- Acceleration of the long-term trend of declining farm numbers and increase in average herd size,
- Sweeping rationalisation of farm milk production as it becomes more concentrated on larger farms and in low cost production areas within Australia,

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- Rationalisation of the co-operative structure,
- Consolidation of fluid milk processors on Australia's eastern seaboard,
- The historical producer-dominated corporatism being challenged by the retailer-led regulation through the supply chain.

These trends in the supply chain inevitably impact on the supply relationships. The current indicators are pointing in the direction of:

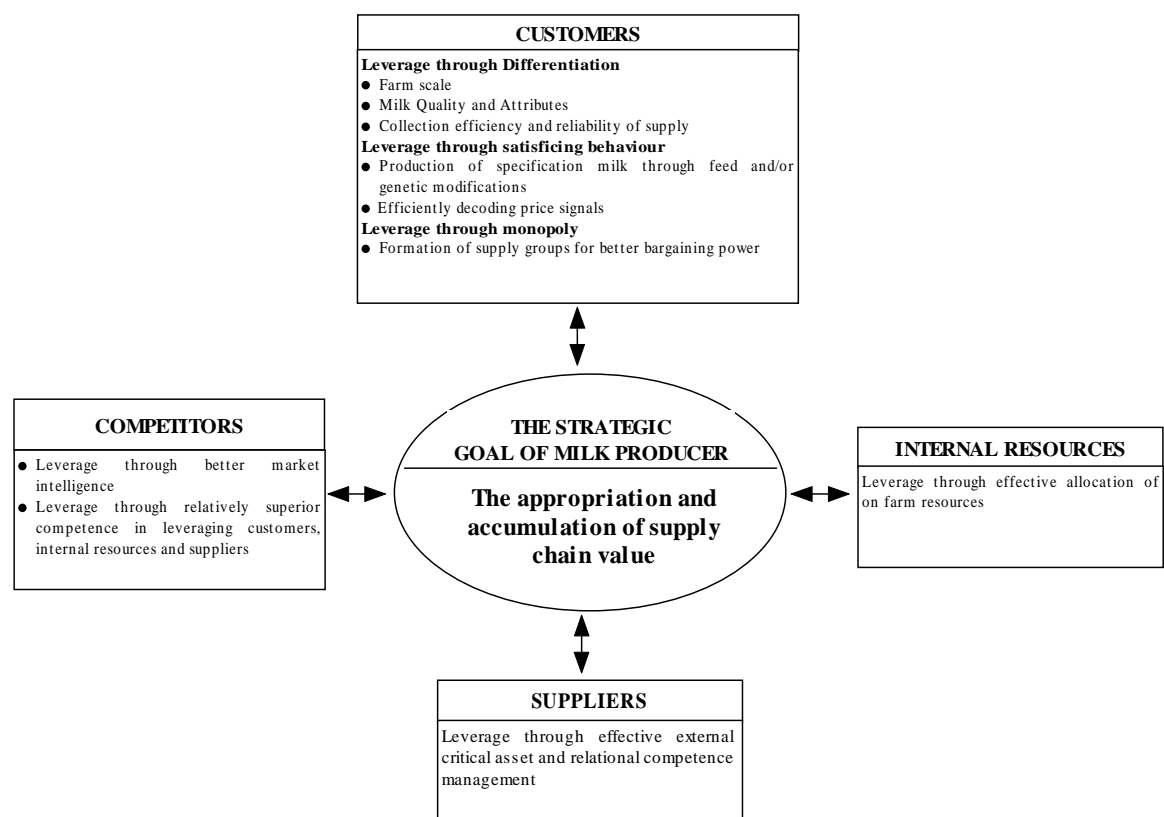
- Individual contracts with the large milk producers,
- Formation of milk producer supply groups to “collectively bargain” with the processor,
- Milk producer groups wanting more input to the price negotiations between processor and super-markets,
- There is also expected to be increasing differentiation of milk prices based on farm scale, milk quality and attributes, collection efficiency and reliability of supply, as well as product mix of the processor.

To grow in a dynamic and transitory dairy industry, the milk producer will not only have to improve operational efficiencies through better farm management, but also be a more responsive player in the supply chain. A passive involvement as “seller” of milk will have to give way to a more involved role in the exchange relationship through:

- Better market intelligence,
- Efficiently decoding price signals,
- Seeking a niche through product differentiation, such as milk production to specification.

The key is an effective leveraging of the internal resources, buyers, suppliers and competitors to appropriate and accumulate optimal value from the supply chain. It will require a better awareness of one's position in the supply chain and what strategies and/or critical resources lead to appropriation of more value from the supply chain (Figure 1).

Figure 1: The four principles of effective leverage



Source: Adapted from Cox, A. 1997: *Business Success*, Earslgate Press, Boston, UK

An effective leverage could be obtained through:

- Effective internal and external assets management,
- Relational competence management, and
- Superior operational performance.

Milk producers are already trying to adjust to the changing environment with a more efficient allocation of on-farm resources, production of specification milk through feed and/or genetic modifications, formation of supply groups for better bargaining power and a more business like approach to dairy farming.

The sustainable growth for milk producers will not be contingent on doing any one particular thing, but on an understanding of what it is that should be done to appropriate value from the supply chain under changing circumstances.

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