

Commerce Commission Workshop: 23 May 2017

Agenda Item: Practical Feasibility

DIRA S 150A

Practical Feasibility

Purpose of workshop session:

- Identify “common ground” to:
 - Establish basis for participation of all parties
 - Strengthen the milk price model
 - Strengthen the monitoring process
- Identify follow up actions

Practical Feasibility: Principles and Guidelines

- Cost structure, risk profile, and other assumptions should reflect real-world costs and risks
- while recognising the DIRA allows the Notional Producer to assume it is able to match Fonterra scale

Straw man

- Commercial feasibility should be the test of practical feasibility
- Criteria:
 - Technical feasibility (required, but not sufficient)
 - Demonstrable feasibility (ideal)
 - “Real world” overlay “(reasonably possible to exist)”
 - Gross measures are commercially feasible
 - Unit measures are commercially feasible
- Safe harbours can displace practical feasibility
 - Discretionary
 - Transparency in application, rationale, and impact

Practical Feasibility: Principles and Guidelines

	Theoretical Feasibility	Commercial Feasibility			Safe Harbours	Drive Fonterra Efficiency?	
		Technical Feasibility	Demonstrable Feasibility (Fonterra?)	Real World Overlay			
				Gross Values			Unit Values
Toll processor; negligible margin risk							
Sales Revenue							
Sales Commissions							
Aspirational Cost Rates							
Yields/ Plant Operating Efficiency							
Changes to Product Portfolio							
USD/NZD Conversion Rate							

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				Gross Values			Unit Values
Toll processor; negligible margin risk	✓	✓ ?	✗	✗	✗	✗	

Farm gate milk market in New Zealand

88. In a workably competitive farm gate milk market, the level of the farm gate milk price would be determined through:

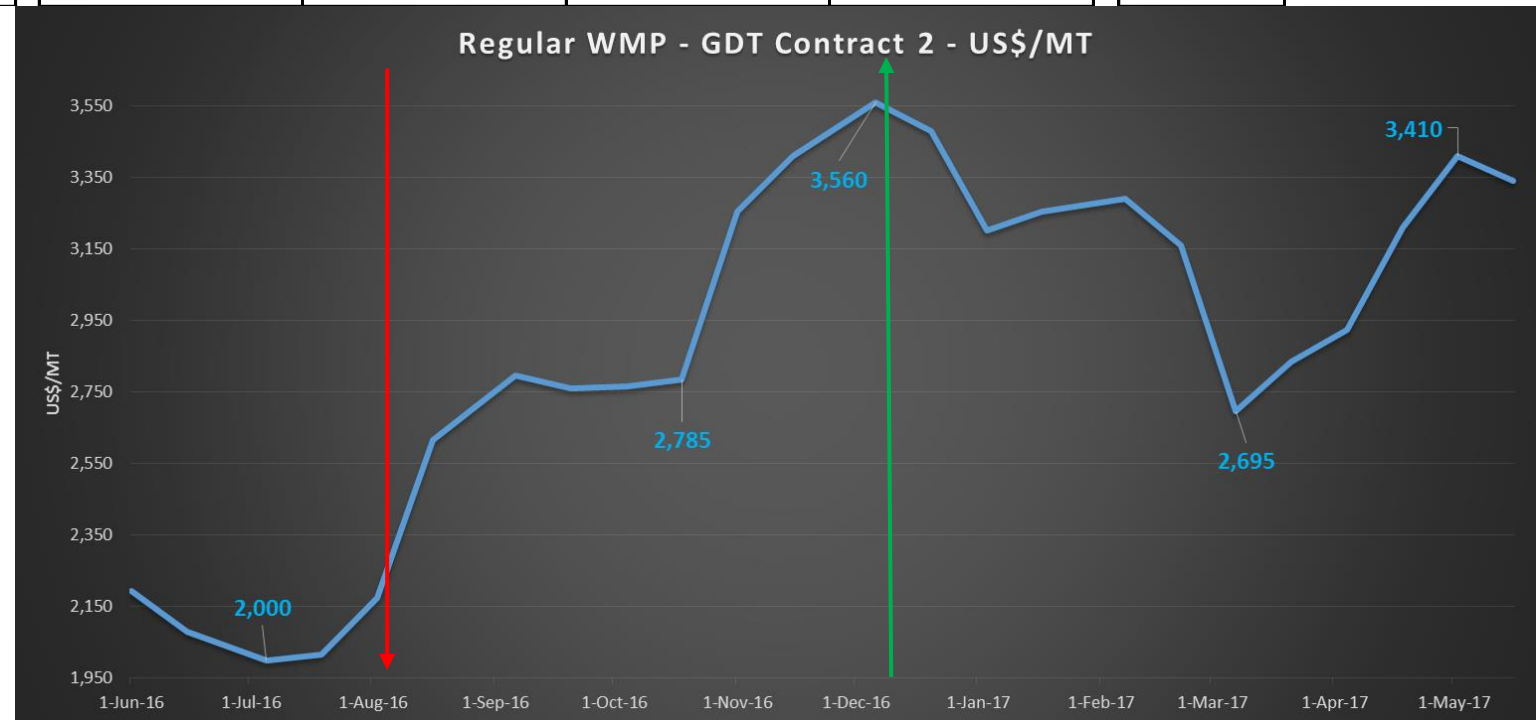
88.1 competition between suppliers of raw milk (ie, farmers) to processors; and

88.2 through those processors competing in both the purchase of raw milk and its onward sale after processing.

Commerce Commission: Our Approach to reviewing Fonterra's Milk Price Manual and base milk price calculation 15.8.16

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				Gross Values			Unit Values
Toll processor; negligible margin risk	✓	✓ ?	✗	✗	✗	✗	
Sales Revenue	✓	?	✗	✗	? ✓	✓	



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				Gross Values			Unit Values				
Toll processor; negligible margin risk	✓	✓ ?	✗	✗	✗	✗					
Sales Revenue	✓	?	✗	✗	? ✓	✓					
Sales Commissions											
									2015/16	GDT Commissions	
									MT	US\$/MT	NZ\$/MT
Notional Producer									2,693,674	6.58	9.29
Fonterra RCP Sales (1)									567,540	12.49	17.63
Next Largest Seller (ARLA) (1)			22,794	30.00	42.36						
(1) Auctions 145 to 167 (Aug 15 to July 16)											

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Toll processor; negligible margin risk	✓	✓ ?	✗	✗	✗	✗	
Sales Revenue	✓	? ✓	✗	✗	? ✓	✓	
Sales Commissions	✓	? ✓	✗	✗	✗	? ✓	

	2015/16	GDT Commissions	
	MT	US\$/MT	NZ\$/MT
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Sales Revenue	✓	? ✓	✗	✗	? ✓	✓	
Sales Commissions	✓	? ✓	✗	✗	✗	?	
Aspirational Cost Rates	✓	? ✓	✗	✗	✗	?	?
Yields/ Plant Operating Efficiency							
Changes to Product Portfolio							
USD/NZD Conversion Rate							

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Sales Commissions	✓	? ✓	✗	✗	✗	?	
Aspirational Cost Rates	✓	? ✓	✗	✗	✗	?	?
Yields/ Plant Operating Efficiency	✓	? ✓	✗	✗	✗	?	

- optimal efficiency vs normalised efficiency
- product compositions
- 85% to 90% of operating days at peak capacity (depends on product mix VOLUME not commercially feasible)
- milk consolidation costs

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Sales Revenue	✓	? ✓	✗	✗	? ✓	✓	
Sales Commissions	✓	? ✓	✗	✗	✗	?	
Aspirational Cost Rates	✓	? ✓	✗	✗	✗	?	?
Yields/ Plant Operating Efficiency	✓	? ✓	✗	✗	✗	?	
Changes to Product Portfolio	✗	✗	✗			✗	
USD/NZD Conversion Rate							

← S. 150 C (2) ?

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Sales Commissions	✓	? ✓	✗	✗	✗	?	
Aspirational Cost Rates	✓	? ✓	✗	✗	✗	?	?
Yields/ Plant Operating Efficiency	✓	? ✓	✗	✗	✗	?	
Changes to Product Portfolio	✗	✗	✗			✗	
USD/NZD Conversion Rate	✓	? ✓	✗	✗	? ✓	?	

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