



Karikaas Natural Dairy Products Ltd
156 Whiterock Road, Loburn
RD 2 Rangiora 7472

The Registrar
Competition Branch
Commerce Commission
PO Box 2351
Wellington 6140

Commerce Commission – Submission on the Dairy competition Review Consultation Paper
12 June 2015

Contact: Diana Hawkins
Representing: Karikaas Natural Dairy Products Ltd
Contact Address: 156 Loburn Whiterock Rd, Loburn, RD2 Rangiora
Contact Email: diana@karikaas.co.nz

Karikaas is a small cheese and yoghurt manufacturer in North Canterbury. I collect milk under the 20% rule from a local Oxford farm, which also supplies Fonterra. I have been doing this since 2004. This is a seasonal farm, so during the winter months I have milk delivered to me by Fonterra, and I pay a predetermined contract price for it.

Your Questions/Consultation Document

Firstly with regard to your interpretation of sufficient and insufficient (29 – 37) “efficient operation of New Zealand dairy markets”, to quote your document, is just as vague as sufficient and insufficient. What is an efficient market? Efficient and beneficial to whom; New Zealand companies, New Zealand consumers, movement of milk from the farm to the world consumer?

Clarification of how you are measuring “efficient” is of significant interest to me.

Pg 62 page 11 – I agree with the notion that regardless of whatever the thresholds are, when reached, it should trigger a comprehensive competition analysis. At Karikaas we would prefer such analysis was more widely targeted than simply farm gate and factory gate markets. It may lead to change in regulations and/or phasing out of some and phasing in of other regulations rather than simply regulation removal.

Pg 63 – I don't know anything about competition theory except to know that it is not straight forward. 80% seems a reasonable starting point to widely assess true competition.

Karikaas Views/Comments

Generally and historically dairy companies/co-operatives do not like, and therefore contractually prohibit a farmer supplier to supple another entity. (Dual supply)

Historically there were a number of dairy co-ops in an area so farmers often had some, though limited, choice in which company they supplied. Currently the new dairy companies do not support farmers in dual supply, neither do they supply milk to other entities (factory gate). (At least my ‘local-ish’ alternative, Synlait, doesn't, I've asked!)

Phone 03 312 8708
Fax 03 312 8208
Email info@karikaas.co.nz

156 Whiterock Road
Loburn, RD 2
Rangiora 7472

Karikaas collects milk under the 20% rule and has done so since 2004. This is done for quality reasons. I have a farmer not only willing but wanting to supply me with milk, and I can collect the quantity I require, at a time which suits my production and quality demands, of a composition which meets my requirements.

Fonterra cannot deliver this to me, nor will they allow me to collect milk off farm myself milk through them. They are actually very helpful but will not deliver less than 3000 Litres at a time, and they will not contractually agree to anything else either. I do buy milk from Fonterra during the winter months, but the milk can be expensive, of poor quality, at a time which suits their changing roster not my production. This means I need to have it delivered the day before I need it, so it is an additional 24 hours older, and 48 hour pick-up is routine for Fonterra except in peak production periods.

Fonterra is forced to allow (with certain conditions attached) up to 20% farmer production to go to another entity. Fonterra is also regulated to provide milk to those who require it, also subject to various conditions. Fonterra historically and currently also supply milk at "market" price. Market price in theory is based on the current marginal return of the next best production option for Fonterra.

In reality this market price is not quite "market" price. I received a letter last week informing me that the price of regulated milk (both estimated and fixed), for the current first quarter is \$5.25/kgMS (matching the current milk price forecast) and the market price is \$5.86/kgMS. Assorted premiums and delivery charges additionally charged. The letter was dated 16th June. AgriHQ's milk price calculator, using Global Dairy Trade figures on June 16th put the current spot milk price at \$4.24/kgMS. Even allowing for significant error in the AgriHQ figures, in the current market the Fonterra "market" price for milk is very high.

Without the open entry/exit clause in DIRA there would be no choice for me, and Karikaas may not survive without being able to sell quality. In Canterbury we cannot contract the whole of a farms milk supply. We are too small, and the farms are too big.

The current DIRA controlled situation does allow choice for small entities.

Can get milk directly off farm

Can get milk from Fonterra – delivered

Without regulated milk small entities without milk collection infrastructure, or who's volume requirements are too small to contract a whole farms supply, would have no choice. No-one is required to provide milk to anyone else and there is no "factory gate" market.

The "regulations" as they stand now, are likely to reduce the "regulated milk" demand, at least in the short term, as some of the newer dairy companies will begin to supply themselves entirely. Karikaas would not like the size of the regulated milk demand to dictate the importance of the market, particularly since only about 5% of milk produced in New Zealand is used domestically.

To Quote the Commerce Commission Report: Consideration of whether to initiate a Commerce Act part 4 inquiry into milk prices, August 2011.

"160. In theory it might be relatively straightforward for an existing independent processor that already collects milk to supply raw milk to an existing town milk manufacturer or another processor. In practice, independent processors supply relatively little milk to the factory gate. Given the opportunity costs involved (see Appendix 3 paragraph 26 below), we consider independent processors will generally only supply raw milk to the factory gate at times when they have excess supply. We therefore do not consider they are likely to be a material competitive constraint on Fonterra's pricing in

this market on a consistent basis. An alternative explanation would be that the price/convenience of default milk means that it is hard for rival suppliers to get business –[].

161. Any new competitor in this market would need to contract with farmers and invest in infrastructure for the collection of milk for delivery at the “factory gate” (or direct to processors as is the case with Fonterra). We consider the only realistic candidates to supply raw milk to the factory gate are current or future processors. Any future processor seeking to enter this market also would need to overcome the conditions of entry and expansion in one or more downstream milk processing and wholesale distribution markets.

162. We consider it likely that Fonterra has little or no competition in the supply of factory gate milk in both the North Island and the South Island. We also consider it likely that there is little or no likelihood of a substantial increase in competition in these markets. This is not a surprising conclusion given the intention of the Regulations was to address this issue of limited competition by ensuring independent processors could obtain raw milk at a regulated price.”

The Karikaas view is that little has changed in the “factory gate” market since 2011.

If and when deregulation occurs/begins Karikaas would like to see the open entry/exit extended to all collecting milk companies. This has two benefits. Firstly small entities will always have the option to take small quantities of a willing farmers supply, and secondly to promote easy entry/exit from one company to another for farmers, thereby keeping companies honest – price-wise.

Also we think there needs to be an on-going reliable source of milk for domestic use. The “factory gate” market is going to be a long time coming. The current situation where 250 million litres is guaranteed to a single company, which is not necessarily a domestic company, to provide competition in a domestic market seems to have some contradictory implications.

Diana Hawkins
Karikaas Natural Dairy Products Ltd