FARMANCO PTY. LTD.

A.B.N. 24 007 191 415

Farm Management Consultants

IAN GIBB
B.Agr.Sci. CPAg, AAAC
38 Coster St.
Alexandra, 3714
Phone: (03) 5772 2709
Email: iangibb@farmanco.net.au

CAMERON SMITH
B.App.Sc(Agr). CPAg, AAAC
1214 Echuca - Nanneella Rd.
Strathallan, 3622
Phone: (03) 5484 9282
Fax: (03) 5484 9273

TOM FARRAN
B.App.Sc(Agr).
2 Collie Rd.
Byrneside, 3617
Phone: 0447 377 820
Email: tom.farran@bigpond.com

16th November 2015.

Milk Prices in 2014/15.

How did Fonterra Milk Australia (FMA) compare in terms of milk price in the four regions in which they collected milk in 2014/15?

1. Introduction.

In August 2014, Bonlac Supply Company (BSC) commissioned Ian Gibb of Farmanco Pty Ltd to undertake a study of milk prices across the four regions in which FMA collected milk in southern Australia.

A repeat of the 2013/14 study was commissioned for the 2014/15 season. As in 2013/14, the four regions were defined as north (Northern Irrigation Area), east (Gippsland, including the Macalister Irrigation Area), south (Tasmania) and west (Western District). Two milk supply patterns were selected for each of the regions, the same patterns used for the 2013/14 study; one pattern representative of a seasonal calving herd in each region and the other, a typical flat supply pattern produced by a herd with multiple calvings. Each of these production patterns was then scaled to 80,000 kg of milk solids, 160,000 kg of milk solids and 320,000 kg of milk solids to represent a small farm (around 150 cows), a medium sized farm (around 300 cows) and a large farm (around 600 cows). The end result was that for each of the four regions, milk prices were calculated for six supply patterns; small, medium and large for both seasonal and flat supply patterns.

In the 2013/14 study, BSC and FMA offered separate pricing systems (and in the case of BSC multiple pricing systems). In 2014/15, FMA offered a single, simplified pricing system in the east/west, and the north/south.

FMA prices were compared with the major dairy companies competing for milk in each region. The list of competitors for each region included:

- North
  - FMA (Fonterra Milk Australia)
  - MG (Murray Goulburn)
  - TMI (Tatura Milk Industries)
- East
  - FMA (Fonterra Milk Australia)
  - Burra (Burra Foods)
  - LFP (Longwarry Food Park)
  - MG (Murray Goulburn)
- West
  - FMA (Fonterra Milk Australia)
  - MG (Murray Goulburn)
  - WCB (Warrnambool Cheese and Butter)
- South
  - FMA (Fonterra Milk Australia)
  - TDP (Tasmanian Dairy Products)

As in 2013/14, most of these companies had multiple payment options available to their suppliers and in the case of Fonterra, also had different pricing in different regions. A total of thirteen payment options were identified (FMA 2, TMI 2, MG 2, LFP 1, Burra 2, WCB 2, TDP 2). Where multiple pricing options were available from a company, the option that produced the highest price for a particular supply pattern was chosen. Other assumptions were also required to make these calculations; for instance, that all milk supplied met the top quality payment standard, that in each case the lowest volume charge applied and that the number of tanker stops was the same in all cases.

All known step-ups, price increases, incentives, charges and deductions were applied. Growth incentives were not included. Prices were expressed before deduction of compulsory levies. In the case of Murray Goulburn price calculations, the value of shares (usually deducted at 0.65 cents per litre) were included in the final price, but not dividends paid on shares.

2. Selection of Farm Production Data.

Real farm data were used to select seasonal and flat production profiles for each region. This was done to reflect normal differences between regions in the start of calving in seasonal herds, which we know varies between regions, and also to reflect the varied impact of seasonal conditions between regions. In each case actual farm data were scaled to represent a small, a medium and a large farm.

There were unique characteristics of all of the selected production profiles which will have impacted on relative milk price both within and between regions. For example:

- The seasonal farms in each region tended to have:

- Moderately tight seasonal calving patterns (generally August but with some variation between regions).
- Usually one month with no milk.
- Lower protein:fat ratios and above average fat and protein tests than the flat farms (this is consistent with crossbred or Jersey herds).

- The flat farms on the other hand had:
  - At least two calving periods (mainly August and March).
  - Evidence of a summer production slump in the east, south and west, despite the split calving.
  - A high to low ratio (milk supplied per month) of about 2:1.
  - Generally higher protein:fat ratios than the seasonal farms.
  - Average to below average protein and fat tests.

3. Results.

The tables below show calculated milk prices by region for each of the seasonal and flat supply patterns within each region, at three different farm scales and for FMA's major competitors within each region.

3.1 North.

North	Seasonal		
Size kg MS	FMA	MG	TMI
80000	$5.69	$5.57	$5.77
160000	$5.74	$5.65	$5.86
320000	$5.87	$5.71	$5.98

North	Flat		
Size kg MS	FMA	MG	TMI
80000	$6.02	$6.07	$6.03
160000	$6.07	$6.14	$6.12
320000	$6.21	$6.22	$6.24

3.2 East.

East	Seasonal			
Size kg MS	FMA	Burra	LFP	MG
80000	$5.66	$5.47	$5.64	$5.50
160000	$5.70	$5.52	$5.73	$5.58
320000	$5.84	$5.59	$5.85	$5.64

East	Flat			
Size kg MS	FMA	Burra	LFP	MG
80000	$5.90	$5.62	$5.81	$5.95
160000	$5.95	$5.68	$5.90	$6.03
320000	$6.08	$5.81	$6.04	$6.10

3.3 South.

South Size kg MS	Seasonal FMA	TDP
80000	$5.63	$5.51
160000	$5.68	$5.59
320000	$5.81	$5.65

South Size kg MS	Flat FMA	TDP
80000	$6.02	$6.24
160000	$6.07	$6.32
320000	$6.20	$6.39

3.4 West.

West Size kg MS	Seasonal FMA	MG	WCB
80000	$5.92	$5.70	$6.07
160000	$5.97	$5.78	$6.15
320000	$6.11	$5.84	$6.26

West Size kg MS	Flat FMA	MG	WCB
80000	$6.04	$5.97	$6.16
160000	$6.09	$6.05	$6.24
320000	$6.22	$6.12	$6.35

4. Prices in 2014/15 Compared to 2013/14.

Based on these particular supply patterns, prices across the board in 2014/15 were roughly 12% below those in 2013/14 for all companies and across all four regions.

5. Outcome for FMA.

Where FMA had a reasonable claim to have been price leaders in most regions and for most supply patterns in 2013/14, this was not the case in 2014/15. For this set of production patterns FMA were price leaders in 2014/15 in the east and south for seasonal farms. In the north it was TMI and in the west, WCB who were the price leaders for seasonal supply. FMA were not price leaders for flat supply patterns in any of the four regions.

- North (seasonal) – TMI price leaders with FMA in the middle ground.
- North (flat) – no consistent price leader but FMA the lowest for each scale, although only by a small margin.
- East (seasonal) – FMA either the price leader or close to LFP.
- East (flat) – MG the price leader with FMA not far behind.
- South (seasonal) – FMA the clear price leader.
- South (flat) – TDP the clear price leader.
- West (seasonal) – WCB the clear price leader.

- West (flat) – WCB were price leaders with FMA in the middle ground.

6. Interpretation of Results (At Farmer Level).

This set of milk price data needs to be interpreted carefully if it is to be used to discuss milk price with individual farmers. While we believe the figures quoted are accurate within the limitations imposed by the underlying assumptions inherit in a study of this type, these results are quite specific to the 'farm' for which the calculations were made in each case. This means that prices are not comparable between regions as the values in these tables are based on different production profiles for each region.

The difference calculated between seasonal and flat prices within a region for any particular dairy company is likely to represent close to the full range of prices paid. What the methodology in this study does is to provide a matrix of potential price outcomes. It should be possible for individual farmers to place their own production profile within this matrix by defining their farm scale (total production) and their own supply pattern. The vast majority of farms will have received a milk price in 2014/15 that was within the range between the calculated result for the small seasonal farm and the large flat farm. However, there will be a few farms with either extreme production profiles or unusual and specific characteristics (e.g. a large number of milk quality penalties) that fall outside the price range indicated by this data.

One real danger of this type of comparative data is that it puts the focus on milk price when in fact the real issue from a farm business management perspective should be profit, not price alone. Farmers are aware that milk price is a key driver of profit. The 2014/15 season produced prices that were on average about 12% below the record prices of 2013/14. There is no doubt that lower milk prices will have had an impact on farm profit but as studies like the Dairy Farm Monitor Project consistently show, farms businesses with more flexible production systems are better equipped to adjust to changed market conditions and better able to maintain profit when prices vary.

Ian Gibb
Farmanco Pty Ltd.

Farm size and profile per region - 2014/15

Prepared to support Ian Gibb analysis of regional pricing

Source - internally prepared data sourced form Fonterra

NORTH

NORTH SEASONAL

Size kg MS	FMA	MG	TMI	% Fonterra farms in region
80,000	$ 5.69	$ 5.57	$ 5.77	**35%**
160,000	$ 5.74	$ 5.65	$ 5.86	**17%**
320,000	$ 5.87	$ 5.71	$ 5.98	**1%**

NORTH FLAT

Size kg MS	FMA	MG	TMI	
80,000	$ 6.02	$ 6.07	$ 6.03	**15%**
160,000	$ 6.07	$ 6.14	$ 6.12	**25%**
320,000	$ 6.21	$ 6.22	$ 6.24	**7%**

EAST

EAST SEASONAL

Size kg MS	FMA	BURRA	LFP	MG	% Fonterra farms in region
80,000	$ 5.66	$ 5.47	$ 5.64	$ 5.50	**34%**
160,000	$ 5.70	$ 5.52	$ 5.73	$ 5.58	**41%**
320,000	$ 5.84	$ 5.59	$ 5.85	$ 5.64	**4%**

EAST FLAT

Size kg MS	FMA	BURRA	LFP	MG	
80,000	$ 5.90	$ 5.62	$ 5.81	$ 5.95	**7%**
160,000	$ 5.95	$ 5.68	$ 5.90	$ 6.03	**13%**
320,000	$ 6.08	$ 5.81	$ 6.04	$ 6.10	**1%**

SOUTH

SOUTH SEASONAL

Size kg MS	FMA	TDP	% Fonterra farms in region
80,000	$ 5.63	$ 5.51	**29%**
160,000	$ 5.68	$ 5.59	**41%**
320,000	$ 5.81	$ 5.65	**17%**

SOUTH FLAT

Size kg MS	FMA	TDP	
80,000	$ 6.02	$ 6.24	**1%**
160,000	$ 6.07	$ 6.32	**4%**
320,000	$ 6.20	$ 6.39	**8%**

WEST

WEST SEASONAL

Size kg MS	FMA	MG	WCB	% Fonterra farms in region
80,000	$ 5.92	$ 5.70	$ 6.07	**36%**
160,000	$ 5.97	$ 5.78	$ 6.15	**30%**
320,000	$ 6.11	$ 5.84	$ 6.26	**5%**

WEST FLAT

Size kg MS	FMA	MG	WCB	
80,000	$ 6.04	$ 5.97	$ 6.16	**9%**
160,000	$ 6.09	$ 6.05	$ 6.24	**15%**
320,000	$ 6.22	$ 6.12	$ 6.35	**5%**