

DAIRY INDUSTRY – HISTORY

Tony Baldwin

www.tonybaldwin.co.nz

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“Know the past
if you would divine the future”

Confucius

Sources

Key sources on New Zealand's dairy history include:

- **Lind, C.** “Till the Cows Come Home – Inside the battle that built Fonterra”, Overland Publishing Ltd, Wellington, NZ, 2014
- **McLauchlan, G.** “The farming of New Zealand: The People and the Land”. Auckland: Penguin, 2006.
- **McLauchlan, G.** “The Farming of New Zealand - An Illustrated History of New Zealand Agriculture”. Australia & New Zealand Book Co, New Zealand, 1981.
- **Nightingale, T .** “White Collars and Gumboots. A History of the Ministry of Agriculture and Fisheries, 1892-1992”. New Zealand Ministry of Agriculture and Fisheries, 1973
- **Philpott, H G.** “A history of the New Zealand dairy industry, 1840-1935”, Government Printer, 1937
- **Stringleman, H and Scrimgeour, F.** “Dairying and dairy products - Beginnings of New Zealand's dairy industry”. Te Ara - The Encyclopedia of New Zealand, updated 13-Jul-12 - <http://www.TeAra.govt.nz/en/dairying-and-dairy-products/page-1>
- **Ward, A H.** “A command of cooperatives: The development of leadership, marketing and price control in the cooperative dairy industry of New Zealand”, New Zealand Dairy Board, 1975
- **Yerex, D.** “Empire of the Dairy Farmers”. New Zealand Dairy Exporter Books, 1989

Purpose

As many leading authorities highlight, the culture and values of the dairy industry's pioneering days continue to have a powerful influence in the modern era. So it is useful to understand those foundational values.

The purpose of these slides is to provide a brief overview of the industry's formative years and its structure from 1900 to the present

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Roots

The New Zealand dairy industry is deeply rooted in New Zealand's social and political history. In the 1890s, dairying was vigorously promoted by the NZ Government to attract relatively poor and unskilled workers from the UK to immigrate and settle in NZ



Roots *(cont'd)*



“Early dairy farmers all had the same ambition to achieve a decent life for their families. They all came from much the same class in Britain. All shared the same hatred of the worst features of English class society.”

David Yerex, *“Empire of the Dairy Farmers”*

Roots *(cont'd)*

As historian **Gordon McLaughlan** explains:

“Most of the small farms had been carved out of much larger blocks of land, so that there were, around the country, many areas where dozens of small farms stood cheek by jowl. Each dairy farmer was likely to have two or three other dairy farms on his boundary...

These dairy farmers were all in the same boat. They were all poor, they all had the same simple ambition to achieve a decent life for their families, they all came from much the same class in Britain, and all share the same hatred of the worst features of English society...

Because their farms were small, the distance between them was not great; the community spirit was strong and they saw a good deal of one another....

So, isolated as they were....they had learned, of necessity, to work together on their farms and they had experience the need to pull together”

“White gold” dreams

Like gold prospectors of the era, dairy farmers shared a dream that milk production would deliver independence and prosperity



“White gold” dreams *(cont'd)*

Dairy farmers' dreams were best summed up by **William Bowron**, the Government's Chief Dairy Expert, in his report to Parliament in 1894:



Government Dairy Inspectors

“White gold” dreams *(cont'd)*

“The untold enduring wealth of NZ lies upon the surface and the cow is the first factor in the way of securing it.....”



“White gold” dreams *(cont'd)*

“We have only to make the prime article in butter and cheese, then no power on earth can stay the flow of white gold in this direction“

William Bowron – ‘Chief Dairy Expert’ for the Government, 1894



“White gold” dreams *(cont'd)*

The industry’s strategy was based on the simple idea that “no industry involved in the production of food would ever fail in a hungry world” - **Arthur Ward**

Our dairy farmers’ modern era strategies have strong parallels.

“White gold” dreams *(cont'd)*

The “white gold” dream of those early days endured for 125 years, underpinning the creation of Fonterra in 2001 and the massive growth in milk production since:

- Waikato Times, 11 October 1997:
“As Waikato's white gold builds to a record flush, milk tankers work around the clock to collect it from over 6000 farmers.....”
- The Press, 14 October 2000:
“The great silver trucks glide up and down Ashburton's West Street, and then spread out to the plains of Mid Canterbury to fill their bellies with white gold”.
- NZ Dairy Board, 6 April 2001:
“Milksolids are the white gold left for export processing...and the Dairy Board sells it all” - Neville Martin
- Southland Times 21 June 2001:
White gold flows on down in Southland dairy sheds
- NZ Herald, 14 August 2014:
“A recent trip through the "white gold fields" of the South Island has proven a real eye opener for Wanganui farming commentator David Cotton”.

Government role

- The dairy industry was established by the Government with those settlers, and successive governments have remained strongly involved in shaping the industry's future.
- Early government measures included:
 - Direct financial assistance
 - Regulations on processing and standards
 - Legislation to help set up cooperatives
 - On-farm advice on how to operate a dairy farm and factory
 - Powers to enable the industry to designate milk collection zones to eliminate competition between processors at the farm gate.
 - Strong restrictions on the supply of non-dairy alternatives like margarine

Government role *(cont'd)*

- Government's 'Dairy Experts' strongly promoted the formation of cooperatives. As **Arthur Ward** notes: "The Government with its own expert dairy advisers had contributed greatly to the cooperative movement" (page 13 of Ward's text)
- Competition between dairy factories was viewed as "pernicious" (to quote Mr Cuddie, Dairy Commissioner in 1914 – in photo left)



Mr Cuddie
Dairy Commissioner, 1914

As **Tony Nightingale** notes (industry historian and former head of Ministry of Agriculture and Fisheries):

- The Dairy Industry Act 1892 established an unprecedented degree of government involvement in the industry. All cheese and butter for export to the UK had to be branded so its factory origin could be traced. The dairy instructors became inspectors and were given the task of tracing sources of unhygienic butter and cheese...The 1898 Dairy Industry Act largely completed state regulation of the industry. Under it the Government could provide cheap finance to set up dairy factories.

Government role *(cont'd)*

Tony Nightingale also notes:

- “The major problem was suspicion and competition between factory owners and dairy farmers. Factories were largely operated by private companies; farmer mistrust and price competition in pursuit of an increased share of milk supply led to bankruptcies and a lack of confidence in new ventures”.
- “The Government’s Dairy Division strongly advocated the cooperative system to provide a framework within which producers and processors could settle their differences. The Government ‘Dairy Experts’ believed that the cooperative system would not only help to solve the industry’s organisational problems but also enhance the quality of production”.

Proprietary processors' role

Proprietary dairy processors were, in fact, pivotal in the formation of the industry:

- "While admitting the force of the cooperative movement..., one should not forget that the industry owes much to the enterprise of the factory proprietors. When so-called cooperation had started the factory system and brought it to a standstill through bad management, it was the 'syndicator' who stepped in, bought up the discredited factories and built new ones, offered the public a fair price for their milk and put the industry on a sound financial basis." - 1897 report of the Department of Agriculture
- "One can scarcely overestimate the courage with which those early proprietors staked their scanty capital against a very doubtful return, well aware of the risk involved. They contracted for supply at so much a gallon of milk and it was necessary to make their offer before the season commenced. If the market prices turned out lower than anticipated, the proprietor often lost money. If, on the other hand, the rate paid to the suppliers gave him a more favourable return than he had hoped for, he was classed as a profiteer and thereby incurred the displeasure of his clients. Surely an unenviable position." H G Philpott (at page 102 of his text)

Proprietary processors' role *(cont'd)*

The risks taken and services provided by proprietary dairy processors were unfairly distrusted and under-valued by dairy farmers and, as **Arthur Ward** points out – “The risks taken by the earlier proprietary processors and their courage in supporting the industry in periods of at least doubtful future potential were steadily forgotten” (at page 11 of Ward’s text)

Farmers' attitudes

Industry historian and former leader, [Arthur Ward](#), explains that:

- "The dairy farmer was cautious of outside help from authorities or commercial interests. He was suspicious, frequently unnecessarily and ungenerously so, of approaches from or commitments to those interests".
- "He was slow to make business friends other than those with whom he had worked or of whose integrity he could be sure. He developed a suspicious of city and urban interests as not being allied to his own, and believed they were seeking more than a fair share of his hard-won livelihood. Consequently he sought through his cooperatives and district associations to secure as much of the selling price of his produce as was possible".
- "He needed this for his own meagre leaving and for his farm development. His wife and family in most cases not only shared the rigours and shortcomings of his pioneer home, but also had been active amid the harsh realities and roughness of the milking shed. They, and he, were entitled to all that could be successfully fought for in the sale of his produce and he was determined that they should get it".

Farmer attitudes *(cont'd)*

David Yerex elaborates:

- “The faith of dairy farmers in the cooperative systems was fuelled by several of the leaders rising from the ranks of the former small farmers. Among them memories were still strong of the way industrialists in Britain had exploited the lower classes. The factories, in a small way, represented "industry"; they were essential to the dairy farmers but they did not have to fall into the hands of the ‘industrialists’”
- The suspicion of ‘outside’ interests included virtually everyone beyond the farm gate: “processors, quality controllers, wholesalers, distributors, merchants, advertising agents, bureaucrats, retailers, financiers and tax gatherers”.

Clive Lind contrasts co-operatives and proprietary processors:

- “New Zealand exporters were dealing with experienced and sophisticated UK buyers. Well-organised proprietary dairy companies were usually run by professional managers with commercial links and knowledge.
- The cooperative dairy factories, on the other hand, had only local selling skills. Their knowledge and expertise on export markets were extremely limited”.

Farmer attitudes *(cont'd)*

Gordon McLaughlan highlights a contradiction that:

- “At the very time he [the dairy farmer] was building the cooperatives he was campaigning with simple fervour for the freeholding of lease-in-perpetuity land. His dripping sweat had made it grass-green. It was his, not God’s nor any other mans”.

Clive Lind also notes that co-operatives relied heavily on non-supplier capital:

- “Building early cooperative factories relied on wealthy people in the district buying ‘dry’ shares, supplementing the ‘wet’ shares issued to suppliers, but their was no guarantee of dividends and many such arrangements became virtually interest-free loans” (Lind, chapter 1, loc 206).

Clive Lind further notes that:

- Co-operatives’ exporting representatives “knew deep down that they were not able to market as effectively as they would like” as they did not have the close connection to importers that proprietary companies had.

Farmer attitudes *(cont'd)*

“Dairy farmers would congregate for hours and reinforce each other’s prejudices” - [Gordon McLaughlan](#)



Inglewood farmers were

Farmer attitudes *(cont'd)*

- “Unity among farmers emerged from their shared distrust of outsiders”
David Yerex
- “Dairy farmers developed a suspicion of city and urban interests...were seeking more than a fair share of his hard-won livelihood” - Arthur Ward
- These ‘outside’ interests included virtually everyone beyond the farm gate: “processors, quality controllers, wholesalers, distributors, merchants, advertising agents, bureaucrats, retailers, financiers and tax gatherers”

David Yerex



Chew Chong of Taranaki – an early private processor – paid cash for milk (rather than goods like many processors), but was effectively driven from the industry by suspicious farmers

Farmer attitudes *(cont'd)*

“Dairy farmers came to believe - and it was an article of faith - that they secured more of the selling price of their produce by the cooperative method”

Arthur Ward, “A Command of Co-operatives”

“After a slow start, the concept of the cooperative dairy company spread like a faith – an extension of the small-holder’s desire for as tight a mastery as possible over his destiny” - Gordon McLaughlan

The culture and values of these pioneering days remain a strong influence in the modern era

Ward, McLaughlan and Yerex

Farmer attitudes *(cont'd)*

The industry's culture is driven by a fierce determination among farmers to be 'free men'

Which makes it a paradox that the industry was created by the Government working with the early farmers...

...and that for the following 125 years, whenever problems arose, the industry turned to the Government for special treatment.

...and still does.

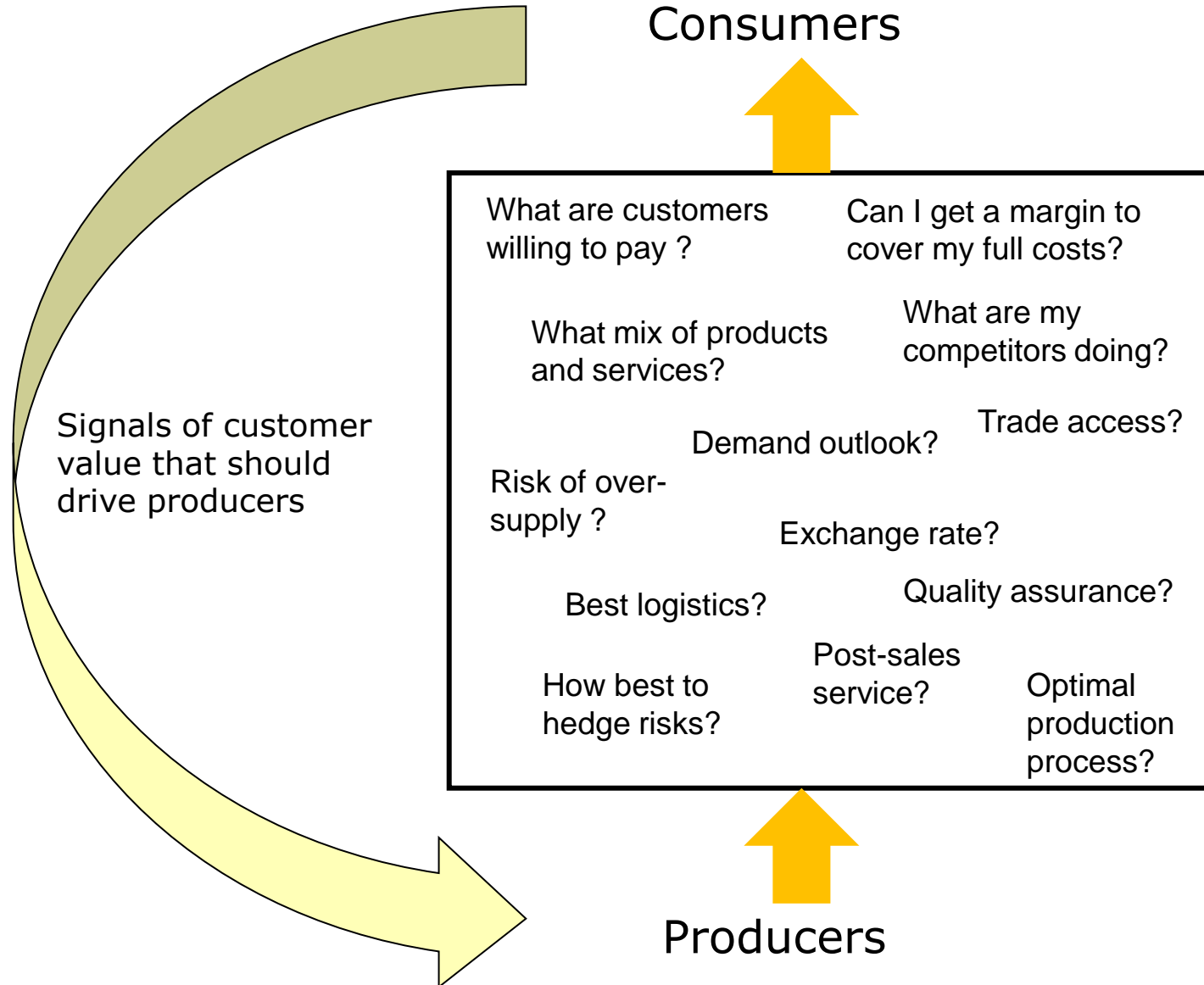
Lack of experimentation beyond farm gate

This section also looks at the first Dairy Board in 1923 – the market factors in play, the government and industry's rationale, and an economic analysis of the single-seller logic

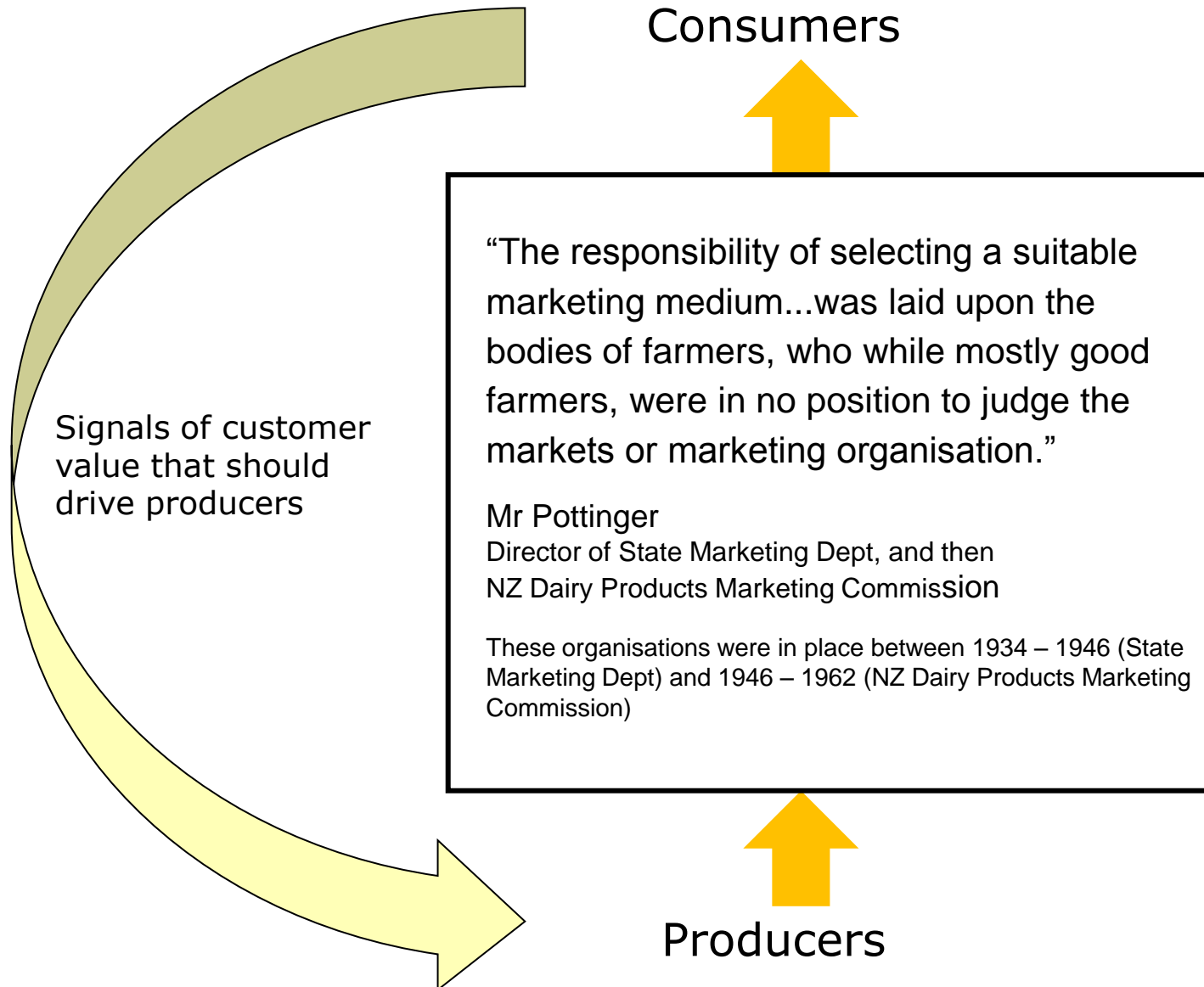
Problem

- For the last 100 years, our dairy industry it has suffered from a serious dearth of diversity and experimentation beyond the farm gate.
- While our dairy industry has been highly successful in growing milk production, since monopoly exporting started during WWI, there has been minimal trialling by different parties of alternative approaches to aggregating capital, pricing, managing risk, using global value chains, understanding customers' preferences and, most importantly, using different strategies to create wealth from the many market opportunities that a handful of decision-makers in a near-monopoly seller simply can't see, or don't have the capacity to exploit.

Beyond the farm gate – Issues for producers



Dairy's response – Centralisation



First dairy producer board

- In the years following World War I, there was a large over-supply of butter in the UK. Wholesale prices for butter crashed by about 50% (a plunge similar to the dairy price drop over the last two years – 2014 to 2016). In the early 1920s, dairy products also represented a significant proportion of total exports (22% then compared to 29% today)
- Frozen meat prices had a similar downward slide and the Government passed the Meat-export Control Act, 1921-22 with a view to controlling exports and influencing see-sawing prices.
- Dairy farmers sought similar legislation . The Dairy-produce Export Control Act was passed in 1923 (after a vote of dairy farmers approved it) and the Dairy-produce Board of Control was established.

First dairy producer board *(cont'd)*

As **Clive Lind** explains:

- “The thinking behind the [1923] legislation was reasonably straightforward. It was an attempt to give producers some combined strength when the market became difficult. The system was not designed to try to control the market – which would undoubtedly fail given milk’s widespread availability – but to enable the Board to manage the flow of products to minimise the effects of the worst declines”.
- “The Board’s powerful negotiating position resulted in huge shipping cost reductions, but market prices were still not where farmers thought they should be. This aggravated the tension between proprietary companies – with their close links to importers – and the cooperatives whose representatives, deep down, knew they were not able to market as effectively as they would like”.
- The rationale later evolved into the idea that a single dairy exporter from New Zealand could get higher prices for its products than competing exporters. This became an article of faith that determined the shape of the industry for most of last century and led to the formation of Fonterra.

Economic analysis

However, in discussing the price slump and other factors that led to the first Dairy Board in 1923, [Veronica Jacobsen](#), [Grant Scobie](#) and [Alex Duncan](#) point out in a 1995 World Bank paper that:

- “Little if any analysis was undertaken of the underlying causes, nor was any consideration given to a range of policy responses, which might have led arguably to an assessment of the alternatives. Producers, dissatisfied with the returns they were receiving, felt typically that either international prices were inequitable, or that their share of the world price was unjustly low.
- “If prices on world markets were too low, then it was argued that collective action by producers would provide countervailing market power which would allow them to extract greater returns. If on the other hand, the depressed returns to growers were a consequence of inefficiency or exploitation by those marketing or processing the products, then grower control of these functions was seen as a way to avoid the excessive costs imposed by ‘middle-men’”

Economic analysis *(cont'd)*

Veronica Jacobsen, Grant Scobie and Alex Duncan continue:

- “The effect of these [single seller] powers is to create a regulatory environment which restricts choice, limits competition, creates barriers to entry, encourages wasteful rent seeking and generates signals that distort the way scarce resources are allocated (ACIL, 1992; Finlayson, 1993).
- “Whether it is possible to duplicate the conditions required for a monopolist to exercise market power in an export market depends critically on:
 - how costly it is for new entrants, such as foreign competitors, to enter the market, given the state of technology. Other countries are not bound by restrictions imposed by New Zealand, when they trade the same type of meat or its substitutes. By controlling activities of New Zealand exporters in foreign markets, interventions may in fact deliver markets to third countries and inhibit the development of marketing expertise among New Zealand exporters; and

Economic analysis *(cont'd)*

- how readily consumers can choose cheaper substitutes. As noted above, in the telecommunications sector, even though it is costly for new entrants to set up a competing local network, there are potential substitutes such as mobile phone networks. These substitutes limit the ability of the monopoly supplier of the telephone network to exploit its position.”
- “The situation in export markets for New Zealand's agricultural products means that it is unlikely that both of the above conditions can be met for anything other than a short period of time. This severely limits the ability of single sellers to influence underlying prices, as Australian wool growers found to their cost with the collapse of their reserve price scheme”.
- Source: http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/1995/07/01/000009265_3961219102755/Rendered/PDF/multi_page.pdf
- There is a substantial body of further economic analysis critiquing the rationale and effects of an artificially created high dominant exporter.

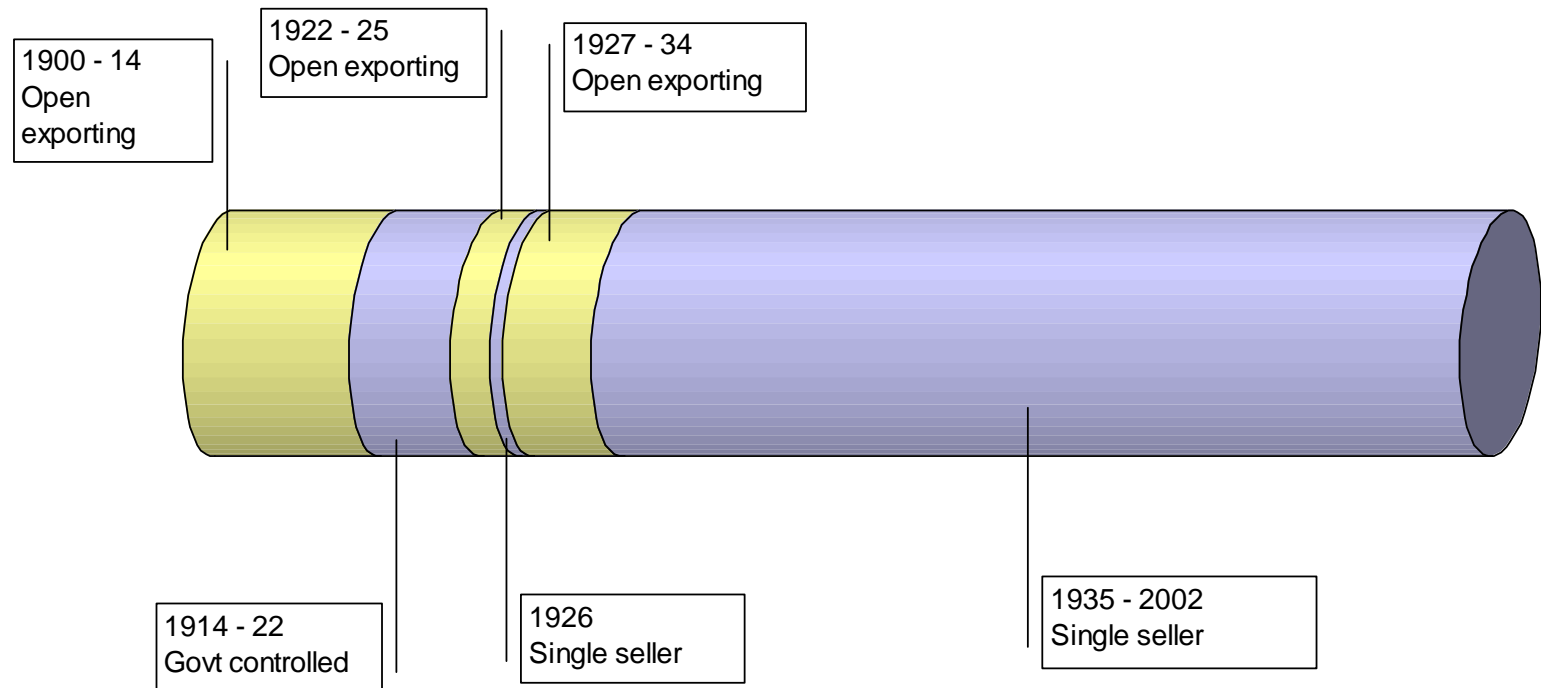
Chronology in diagrams

The following slides provide an overview of the dairy's industry's structure since 1900 and its long term reliance on a single agency – government or government-mandated – to be responsible for activities beyond the farm gate.

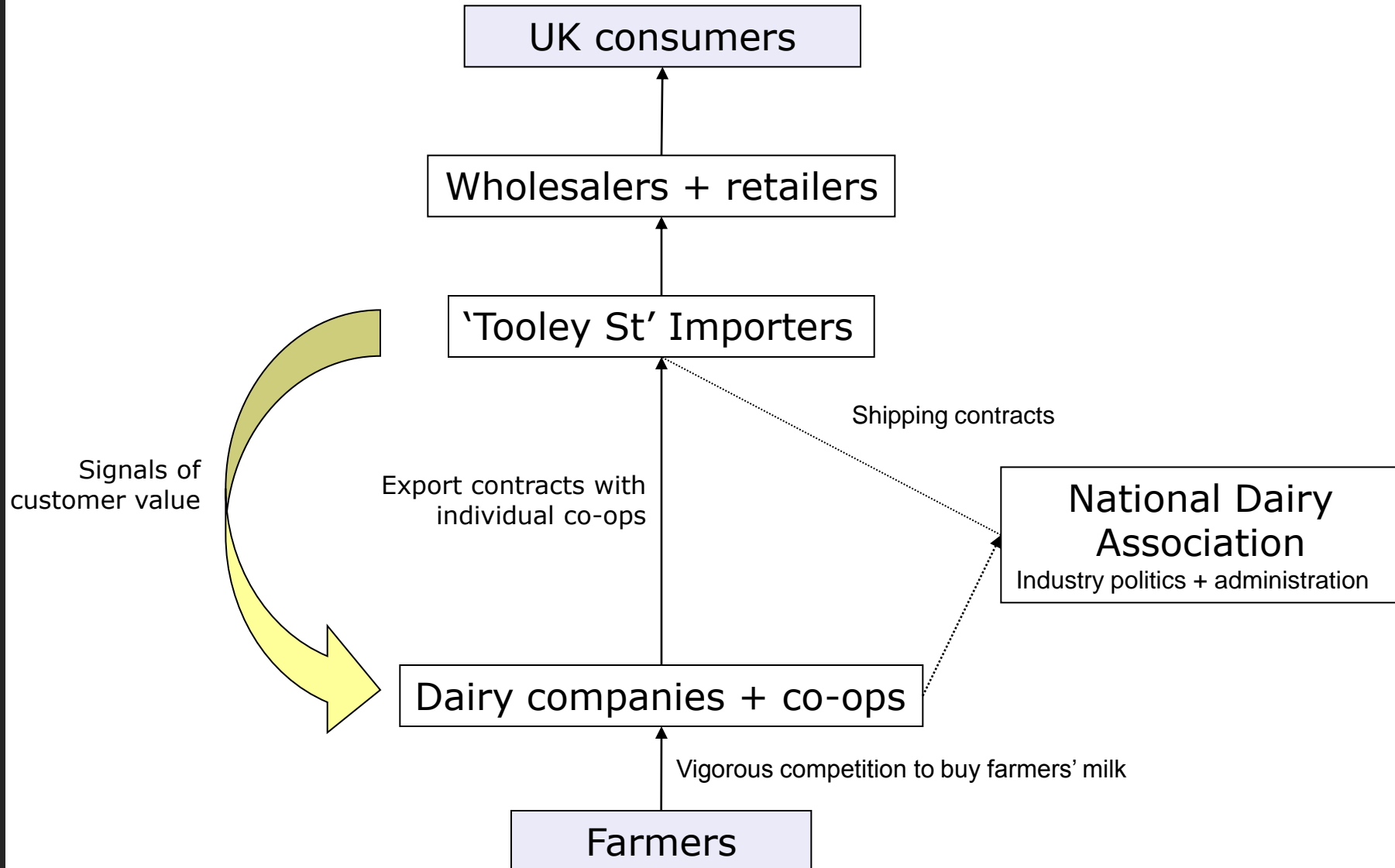
Overveiw

Over 100 years, the industry drove out competition in processing and exporting. It also drove out diversity of ideas, which any industry needs to realise its full potential. The industry's strategy is based on three misplaced myths:

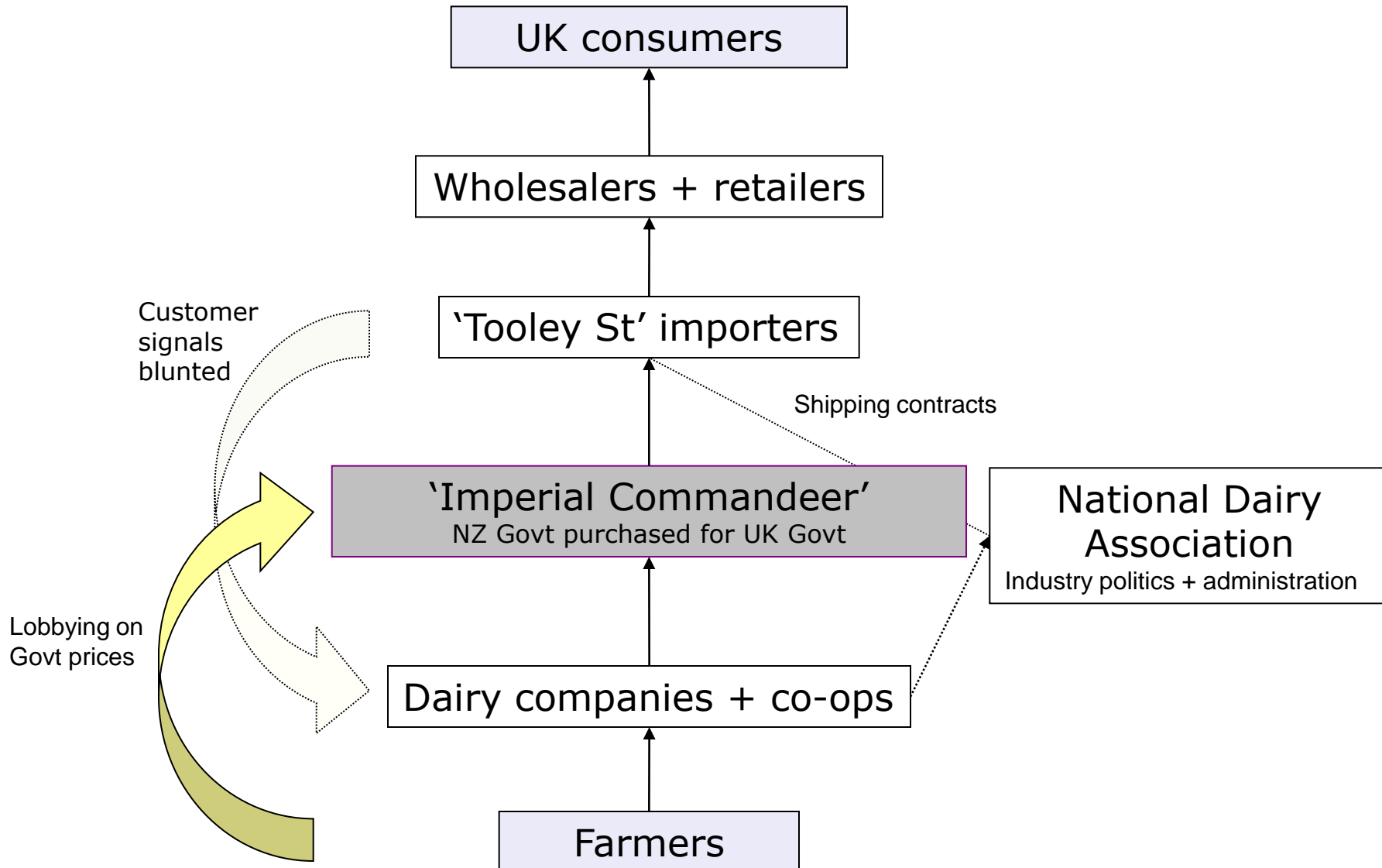
- 'Outsiders' will reduce suppliers' wealth,
- A single exporter will deliver higher prices for commodities, and
- Producers would not respond to consumer price signals, and could not manage the post farm gate business



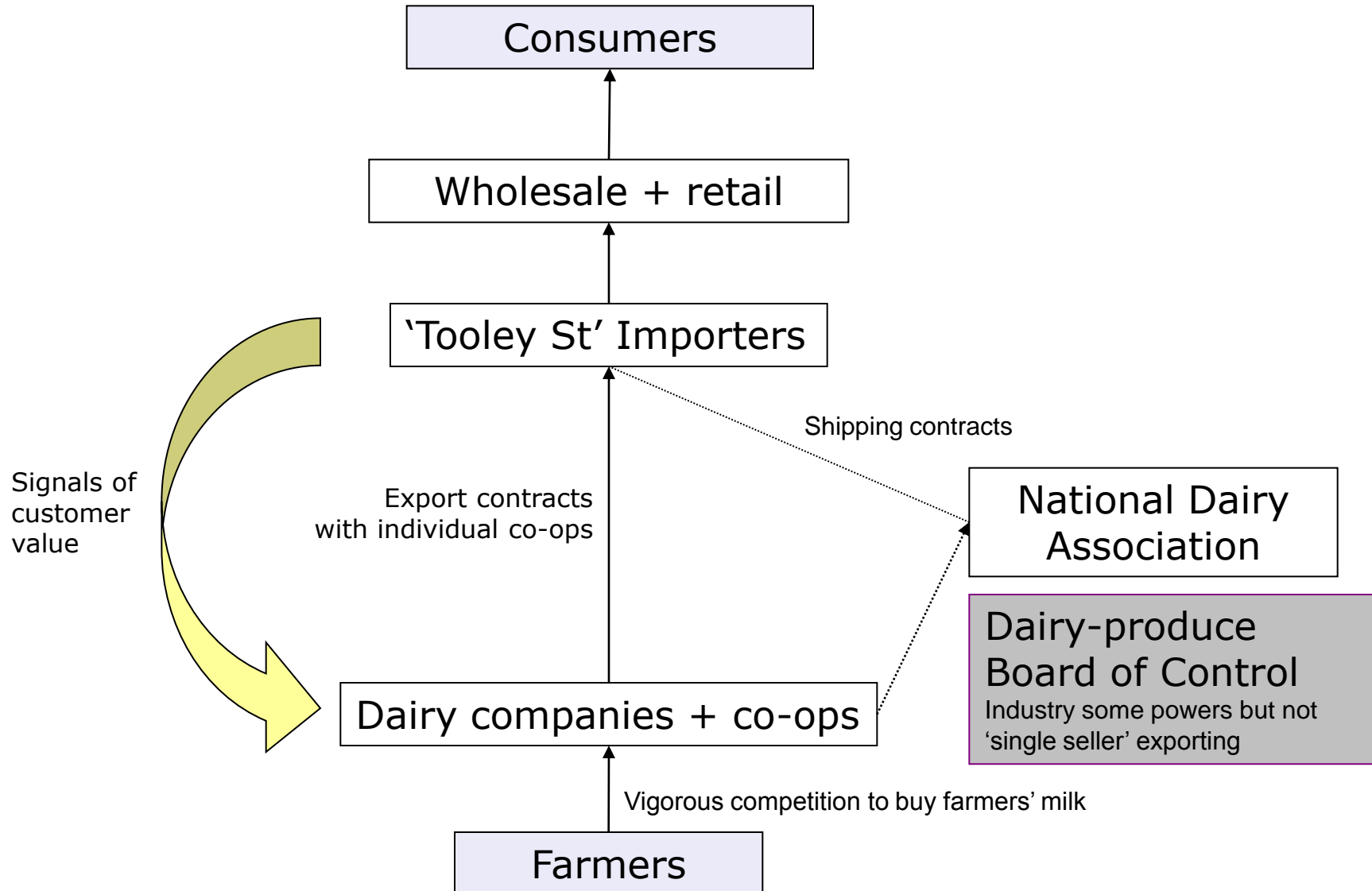
1890 – 1914: Open Exports



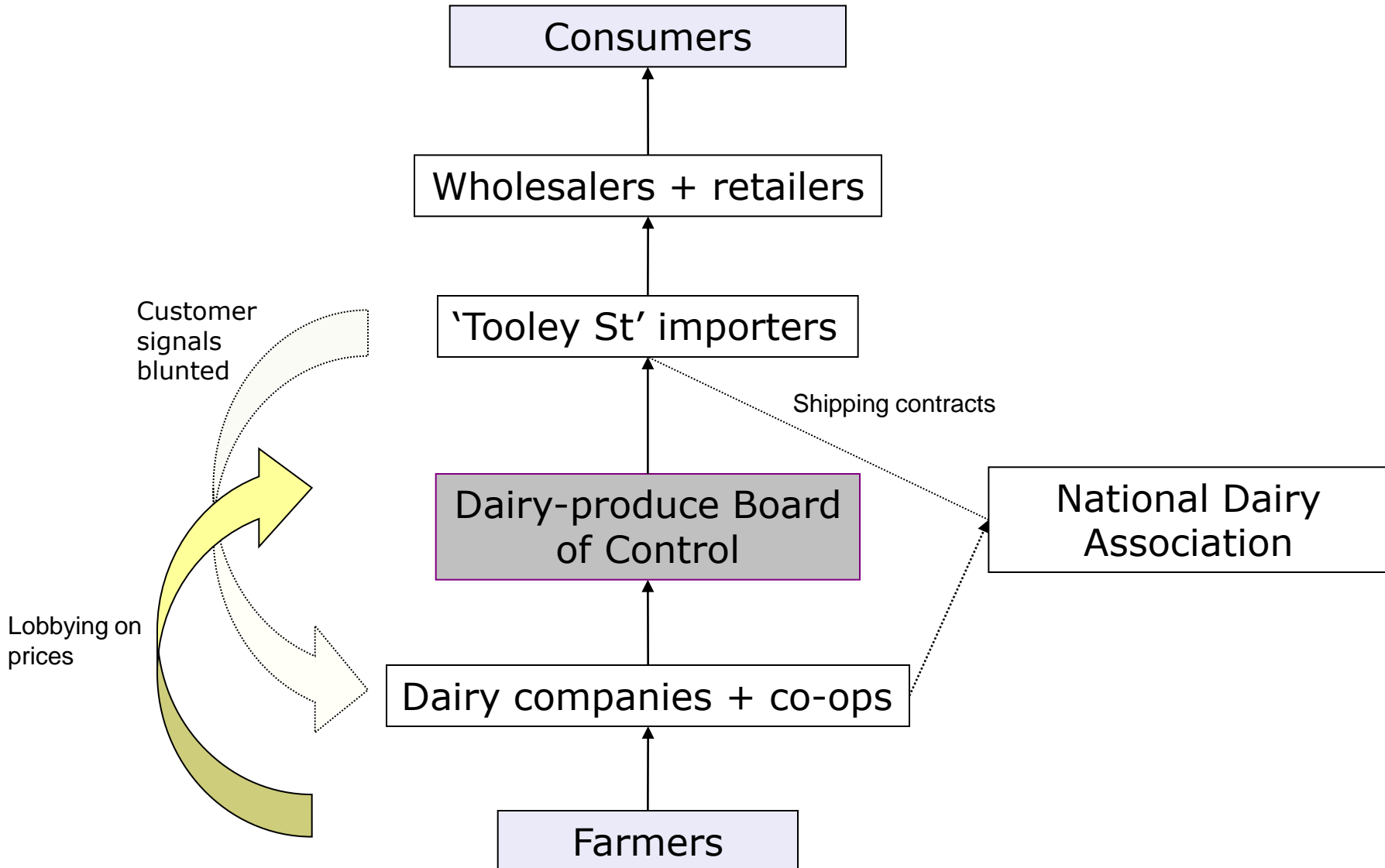
1914 - 22: Single exporter



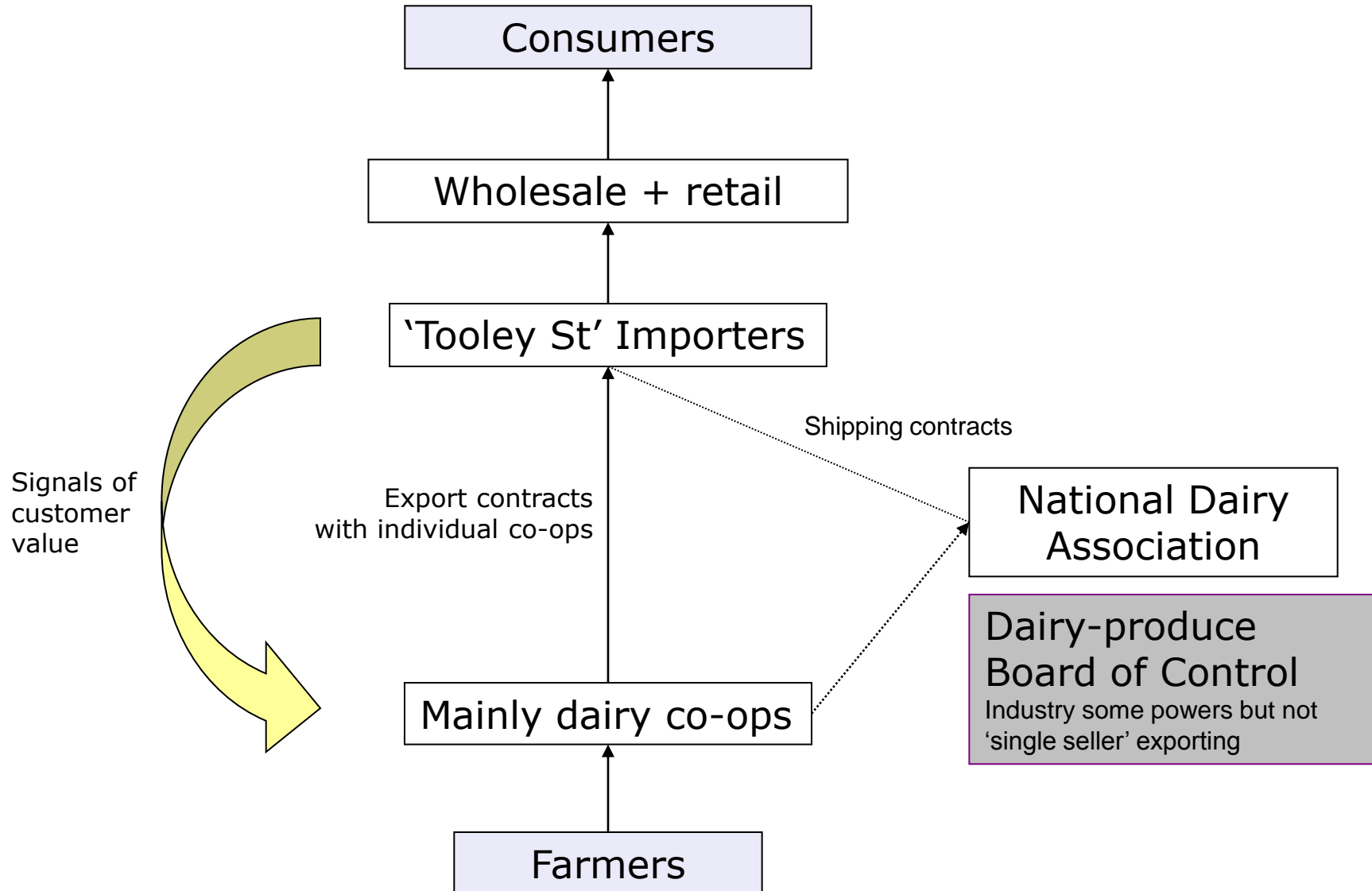
1922 – 25: Open exporting



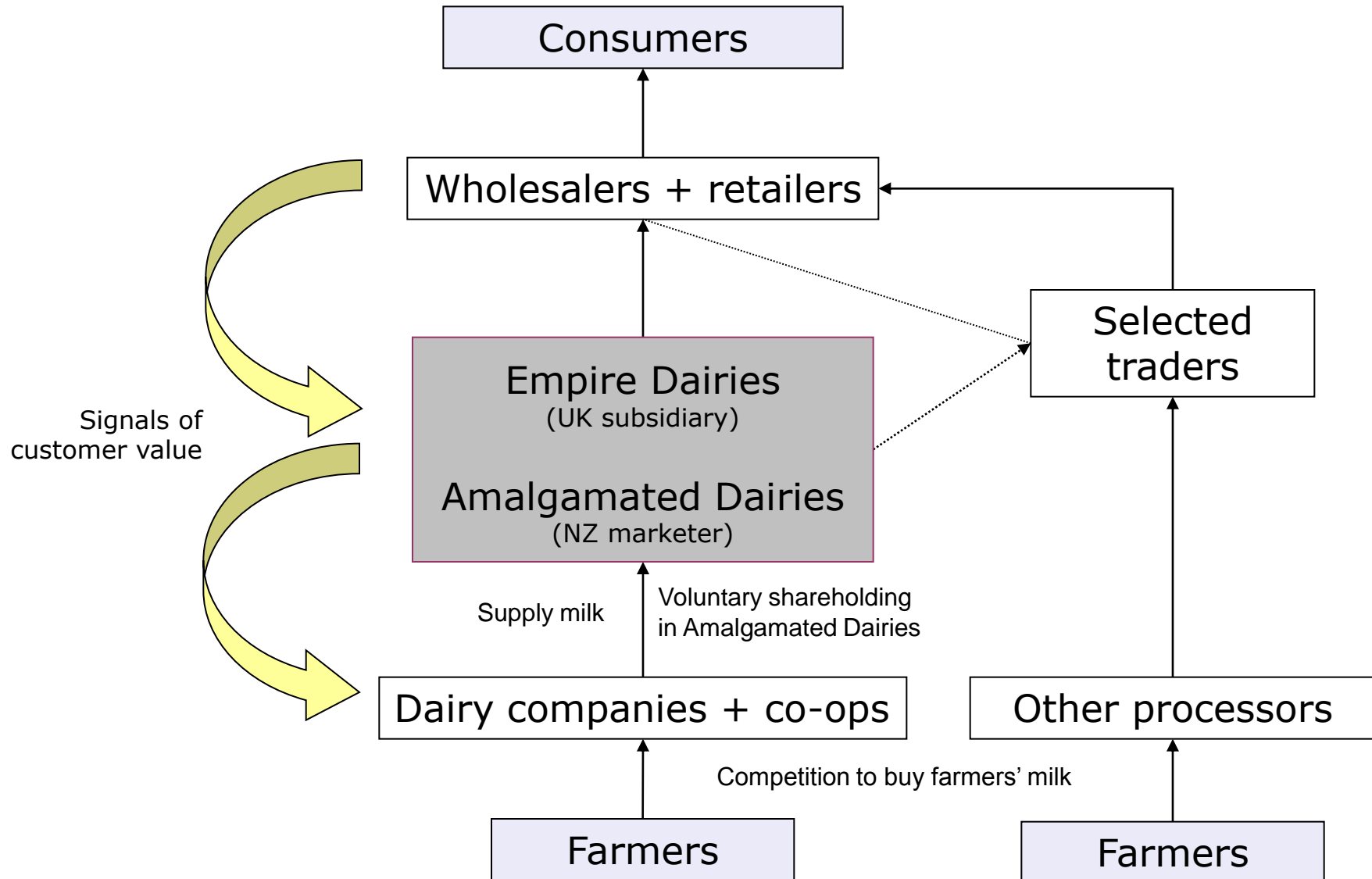
1926: Single exporter



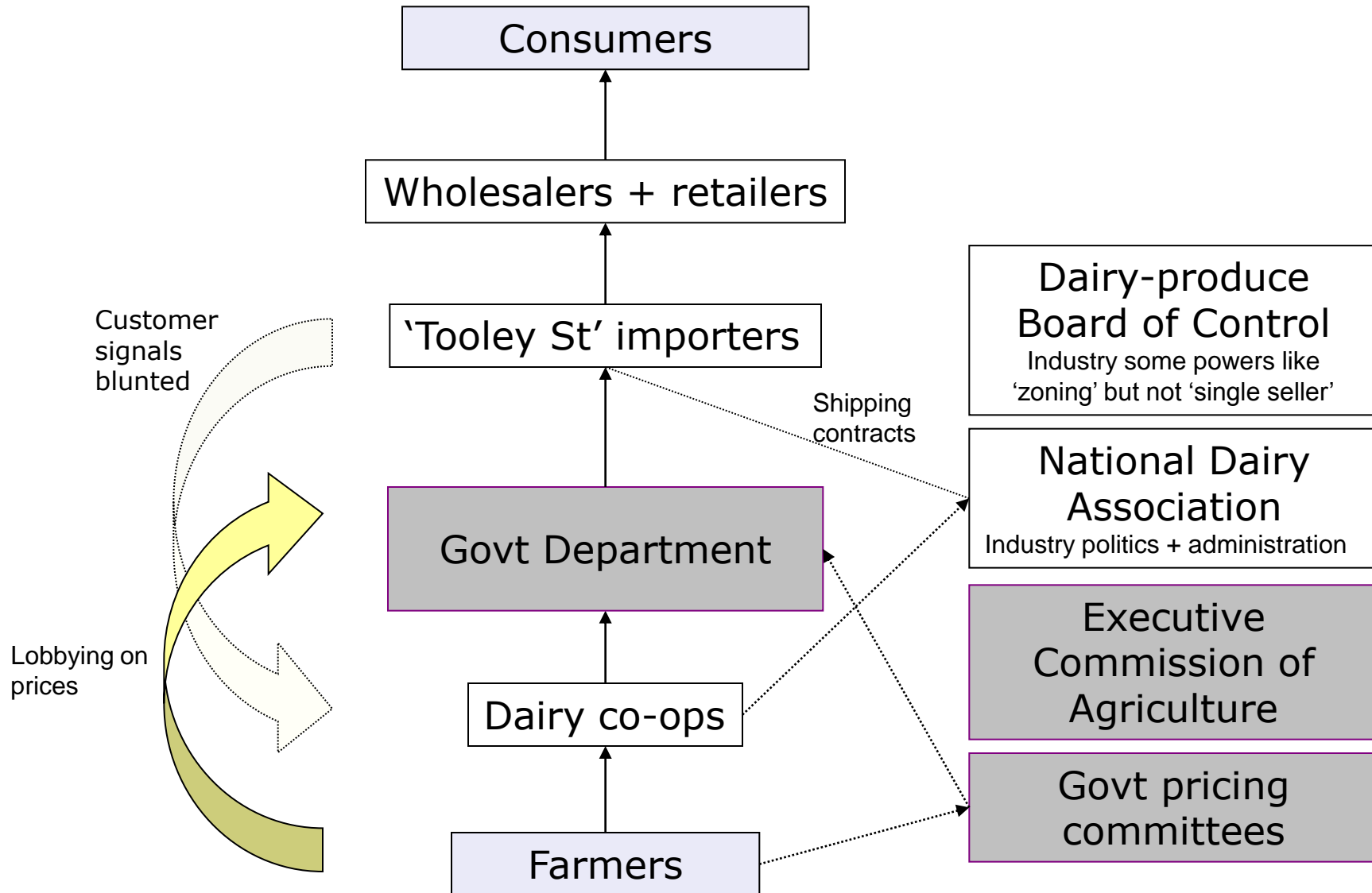
1927 – 34: Open exporting



1927: Sir W Goodfellow's proposal



1934 – 46: Single exporter

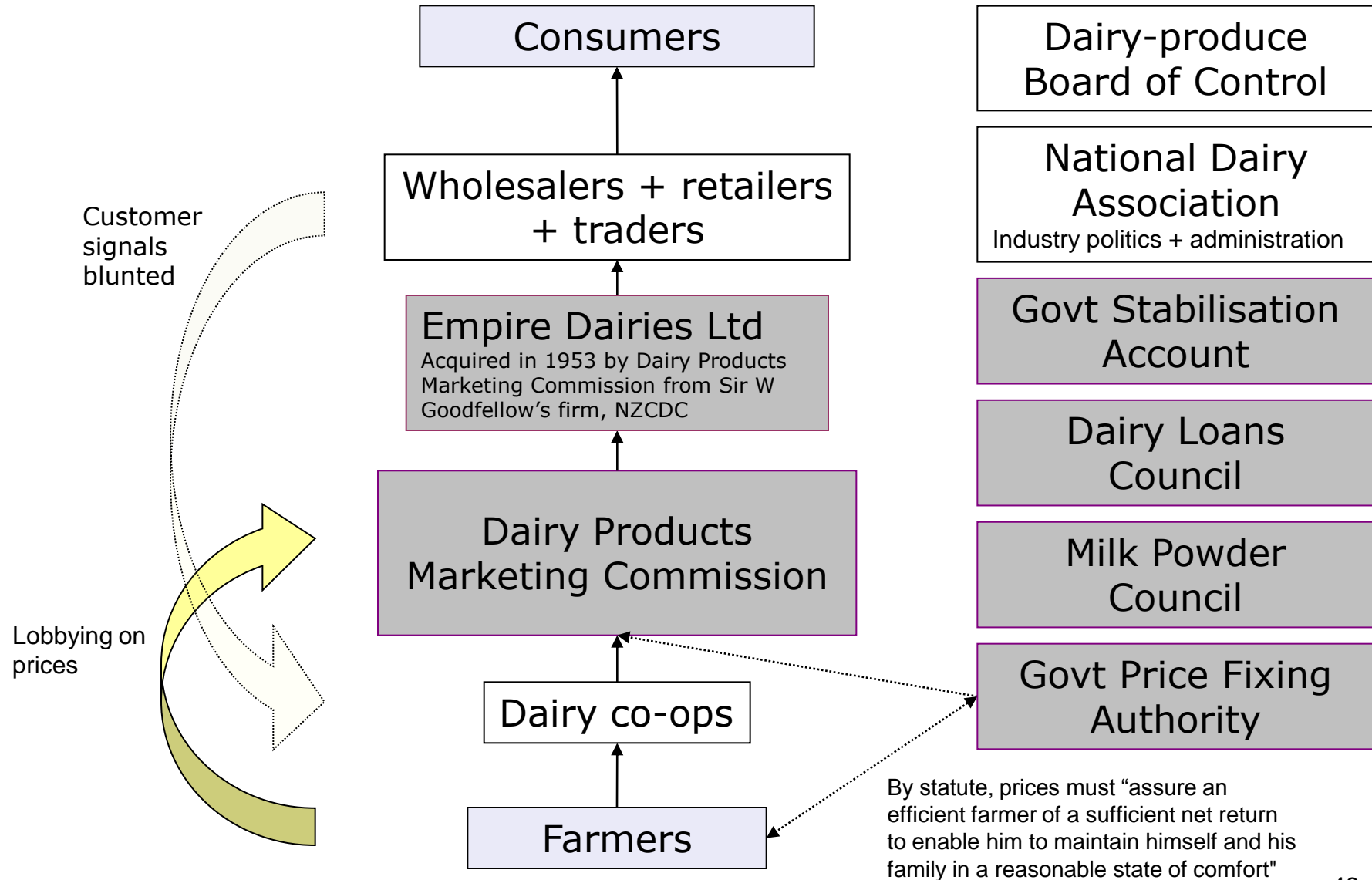


Government guaranteed price scheme

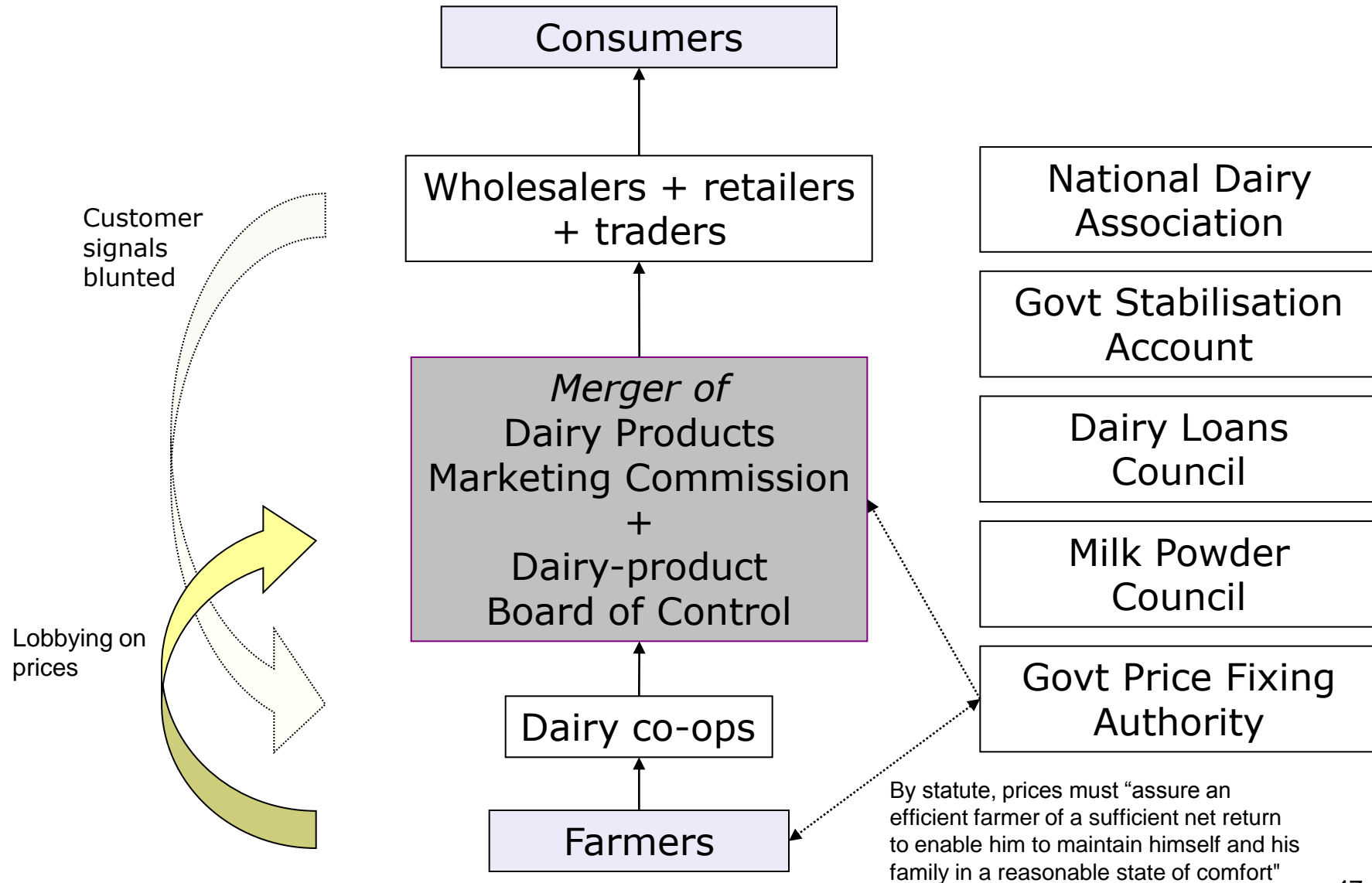
Government had to “set prices that assure an efficient farmer of a sufficient net return to enable him to maintain himself and his family in a reasonable state of comfort.”

(extract from the relevant legislation)

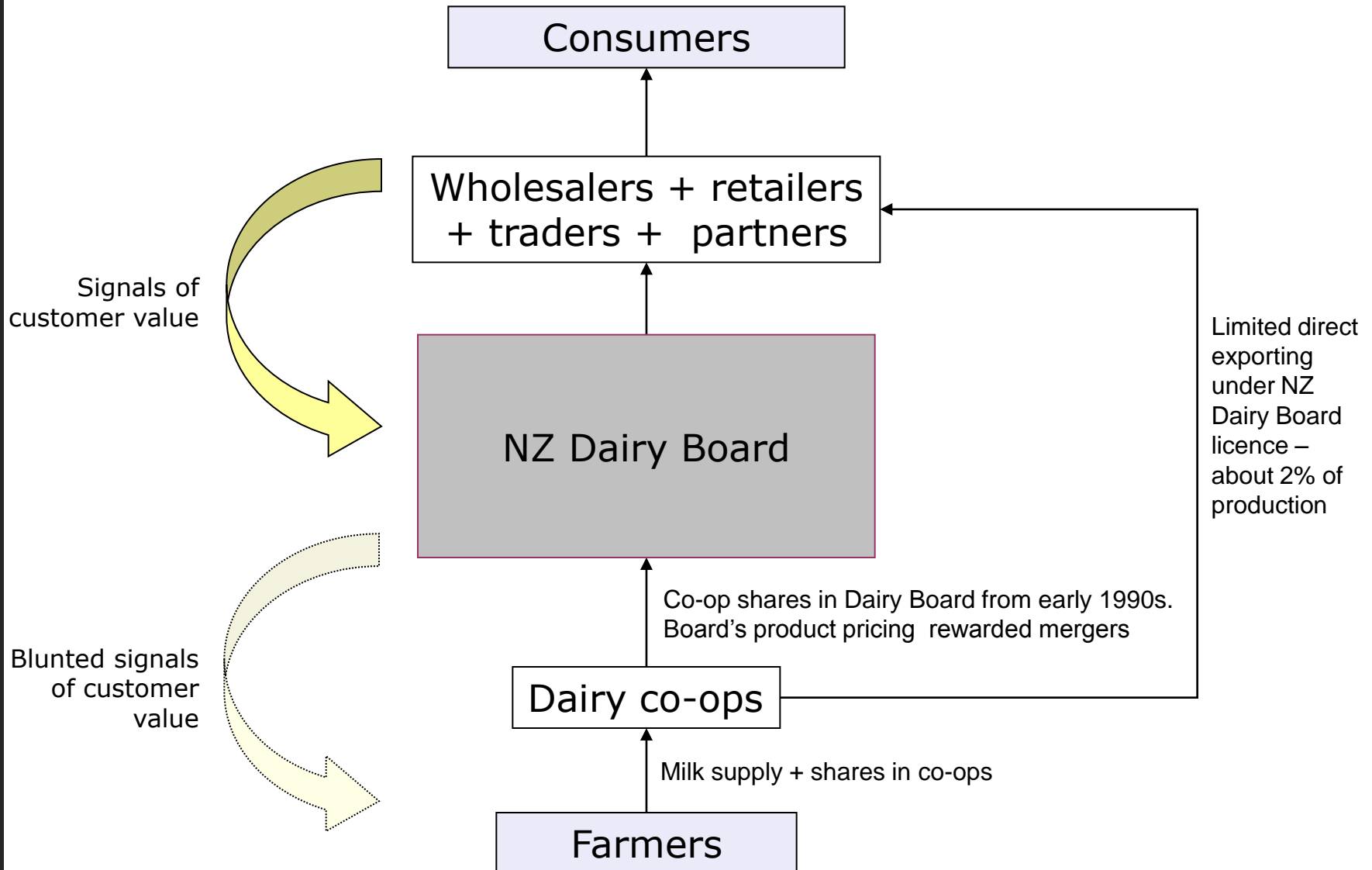
1946 – 62: Single exporter



1962 – early 80s: Single exporter



Early 1980s - 2002



2002 – present: Open exporting

