

New Zealand vs. Canada: Who does U.S. want to be?

Compiled by Sherry Bunting from producer interviews, correspondence and gov. reports

Introduction:

We keep hearing that the U.S. has an identity crisis and needs to determine “who” it wants to be: Canada or New Zealand? Truth is: It’s not that simple. U.S. can be neither New Zealand nor Canada; however, a comparison of the three systems helps U.S. dairy farmers think about future dairy policy.

Included in this summary are the observations of a retired Canadian dairy farmer who had a high production herd under the Canadian quota system. Since retiring, he has traveled thousands of miles in the U.S. for two years and then for the past year in New Zealand visiting dairy farms. His observations and the interviews I’ve had with Canadian dairy farmers and New Zealand dairy farmers, together, are illuminating. Many of the observations below are also validated by other research.

Q&A

Q: U.S. dairy farmers are at a crossroads and they are looking at other countries like Canada and New Zealand to see what they can learn from their systems and apply to their own. From your travels and experiences in all three countries, what’s your take?

A: I don't think the U.S. farmers can or want to be like Canada or NZ farmers.

Q: Why not Canada?

- **System will fail:** Canada's system will ultimately fail unless drastically altered. That is the fear of Canadian dairy farmers and the prognosis of those who have retired from dairy farming in Canada. Two reasons: 1) young people have a hard time getting into dairy because of the cost of the quota; and 2) global trade agreements put more and more pressure on Canada’s system, and longtimers fear the eventual devaluation (by imports) of their quota.
- **WTO pressure:** With the quota system operating the way it is now in Canada and world trade agreements constantly pressuring Canadian gov't to allow open access to Canadian consumer markets... how can the current system survive?
- **Quota is very expensive and Canadian farmers owe lots of money for this quota.** This debt creates vulnerability and it sure takes the ‘gravy’ out of the milk cheque.
- **Hard for young farmers:** Canada's system makes it extremely difficult for young farmers to get started. A hundred thousand dollars might get you enough quota for three or four good cows. (Current quota is valued at \$25,000 to \$30,000 per cow).

- **No impact on world prices:** Canadian farmers under their present system will never represent a threat to world export milk prices.
- **I don't know why American farmers would want this system, said the retired Canadian dairy farmer.** Quotas don't comply very well with world trade agreements and are really associated with price-fixing, which should be illegal when compared with any other industry. How much socialism do you want?

Q: From the perspective of a farmer still dairying in Canada, tell me the pro's and con's of your system:

- Families earn a good living on a small herd and dairy farmers are “satisfied.”
- Young producers can get involved as family members taking over the same herd and quota, but they need to be able to continue to make the high milk check (\$25-30/cwt) to pay off the parents’ huge investment in quota, which is sometimes partially still owed.
- Under the quota system in Canada, more than one generation can presently earn a living from under 100 cows, quite easily. There is less financial stress.
- When asked, the farmers who are dairying under Canadian quota—right now—all agree they wouldn’t want to give it up when they see what is happening to milk prices and dairy farm cash flow just over the border in the U.S. and around the world.
- They also say there are some regional battles occasionally between provinces regarding quota.
- Bottom line, Canadian farmers like the quota system because it enables a small farm to support the family comfortably. However, they do worry about the future value of their quota due to loosening of import restraints, and they worry about the ability of future generations of young people to enter the business, which simply can’t happen unless they are “born into it.”

Q: Why not New Zealand?

A: Whole nation depends on dairy: Not so in U.S.

- Many people in NZ look to the dairy industry as its saviour when it comes to exports, but **it takes a lot of guts to produce milk at world market prices.**
- Doubtful that American gov't or its farmers are ready to produce the bulk of its milk at those kinds of prices.

- Doubtful that American farmers are ready to give up their blue silos and lots of other heavy equipment for an electric fence and break feeding.
- NZ dairy farming is also unique in respect to its climate.
- NZ dairy farming is unique in the fact that it's so integrated into the income and lifestyle of most of its citizens. **It's not just the farmers that have to survive on the backs of the dairy industry here but the whole country.**

Q: How do you view the U.S. dairy market?

A: From what I've seen in the USA concerning its farms in general—and because the USA represents such a large internal consumer market (which NZ targets as its biggest export money maker)—big money constantly seems to want to control agriculture, especially the retail and processing side of things. Retail prices for milk products often do not reflect producer returns. I don't see that changing in the near future in the USA.

Q: What is different or unique about the market structure in New Zealand dairy industry?

A: The Biggest difference in New Zealand compared with ANY other country is:

- **Dairy is 25% of NZ total goods exported:** NZ milk, in one form or another, represents the biggest single export potential they have had in any sector of their economy for many years and probably will have for many years to come.
- **New Zealand is a dominant world dairy exporting country, accounting for 40% of global trade.** Largest world exporter of skim milk powder (smp), whole milk powder (wmp) and casein. These and other products are sold throughout the world in a highly sophisticated global marketing and distribution network.
- **U.S. is the most important market for NZ's dairy products,** accounting for about 20 to 25% of their total dairy exports. Fonterra announced in 2008 that it could double its revenue from U.S. joint ventures in 3 to 5 years.
- **95% of NZ milk is exported via cheese, butter, powder, proteins!** Herd is currently more than one cow per person (5 mil cows and 4 mil people) vs. U.S. herd, which is one cow per 33 people (9 mil cows and 300 mil people).
- **NZ Dairy is a source of national pride** and receives a lot of attention from the citizens and government.

- **Tremendous public and government attention:** The NZ dairy industry will always catch a lot of public and gov't attention especially if there's trouble brewing and there's always trouble brewing with the milk industry over here.
- **Dairy is integrated into income and lifestyle of NZ citizens:** NZ dairy farming is unique in the fact that it's so important to the citizens. It's not just the farmers that have to survive on the backs of the dairy industry here **but the whole country.**
- **National currency depends on it:** NZ National Currency depends on farming in general, and dairy in particular, as its chief export. Due to world market price for most commodities, NZ currency experiences tremendous volatility.
- **Government invests heavily in research not subsidies:** NZ government is not in a very good position to subsidize their farming industry to make it survive, but they do encourage research into products for any little niche market that might be available world wide: i.e. functional proteins, pharmaceuticals, organic milk products, the processing of colostrum milk products (becoming very big), etc.
- **Clean and green image:** Mistakenly or not, dairies down here carry an image of clean and green.
- **Grass to money – more of agriculture is moving into milk production as the grass to money converter:** NZ farming focus is to try to turn grass into money over here. Fruit, tobacco, wool, beef, deer, alpacas, emus, etc. have had a much harder time surviving world market prices so the one reliable resource has been milk and **everyone over here expects milk prices to go up and down like a yoyo.**
- **Seasonal milk supply:** NZ and Australia are seasonal milk supply with very few “town herds” doing winter milking for the fluid supply.
- **Small percentage of cows being milked in the winter time:** They do get a little better price for winter milk, but there's only 4 million people in the country, hence not a big consumer of domestic milk production within their own country.
- **40% of NZ farms operate sharemilking contracts,** where the sharemilkers sometimes own the herd and sometimes own a portion of the herd along with the farm owner. Sharemilking is a longstanding New Zealand arrangement that helps beginning farmers build equity and management skills while allowing retiring farmers to ease out of farming.
- **With relatively high fixed costs and low variable costs, NZ is targeting world market dairy prices, so there's no reason to restrict production** —seems like everyone is trying to utilise every blade of grass available and switching from beef and sheep to dairy to do so. One farmer told me he and wife switched from beef to dairy to develop a better asset for their children. In this example, the farmer sold

small acreage of high value land in volcanic soils to buy large acreage in swampy soils to start a dairy three years ago.

- **NZ Growth Plan is to double cow numbers and herd averages = Sheep to Cows:** NZ farmers say they plan to almost double their national herd size, adding 3 to 4 million more cows (current herd size is 5 million or about 1 cow per person). Word is that they will do this by removing 8 million sheep from pastures. They also say existing herd averages will double from 8000 lbs milk to 16,000 lbs milk via improved pasture.
- **Fonterra is investing in dairies and partial ownership of processing facilities in Chile as another milk source. They have also doubled processing capacity in portions of Australia.**
- **However, NZ farmers are having a tough go.** Sharemilkers have tougher time buying their own farms as the land values have increased dramatically in recent years.
- **NZ cost of production has very low variable costs, but fixed costs are rising:** This is because land prices in NZ are rising. Cornell economist Mark Stephenson estimates that NZ and Australia cost of production is getting about equal with U.S. because U.S. fixed costs are lower and variable costs are higher while NZ and Australia variable costs are lower and fixed costs (land) are higher.
- **Variable costs are low because** grazing model is used so feed and machinery costs are low, and also farmers confirm that they do not prep their cows. Their actual milking costs are lower because they don't use hygiene products like pre and post dips, they are also starting to use less dry treatments because of market for colostrums products. Labor cost efficiencies also gained by work ethic of seasonal Asian workers coming to NZ to man dairies during the main milking season.
- **NZ dairy farmers fear foreign interests buying up land:** There is a constant fear over here that a country like China will eventually buy up farms that become insolvent and eventually control their milk industry. Recently, the Chinese have displaced the Brits as the largest ethnic group immigrating to NZ on a yearly basis, and agriculture is becoming increasingly dependent on seasonal workers coming from Asia, who are very efficient workers and this may give agriculture over here a bit of an edge in cost efficiency.
- **Very concentrated market:** Fonterra processes over 90% of all milk produced in NZ and is a co-op owned by farmers. It carries a large debt load but keeps encouraging farmers [scares them in most cases] to buy more shares to maintain farmer ownership of their processing industry. This in turn increases farm debt, and decreases competition.

- **Farmers voted down outside investor idea:** Fonterra floated the idea of outside investors buying stock, but farmer member/owners voted it down.
- **Instead, they recently voted to raise the caps and allow farmers to hold shares for up to 120% of their production.** This is seen as a way to infuse equity into Fonterra from the farmers. Fonterra will no longer issue redemptions for those “dry” shares, but shareholders are expected to be able to trade the “dry” shares with other shareholders.
- **Shares are purchased for processing capacity per the production target of each shareholder** (10 shares per 10 kg milk solids, but recent vote means they can purchase 12 shares per 10 kg milk solids). Prior to recent restructure, if the farmer’s production was below the target (# of shares purchased), Fonterra would issue redemptions, which pulled equity out of the business. As of Nov. 2009, Fonterra will no longer issue redemptions when shareholder production is below the amount of shares they hold.
- **If the shareholder’s production is above their target, the shareholder has to purchase more shares for processing of the additional milk** (This is still the case). Now shareholders are expected to be able to trade “dry” shares with each other.

FYI on the European Union

Farmer protests have centered on the fact that EU is phasing out quota system by 2015. They were protesting to bring back stricter quotas, and they were seeking restoration of dairy subsidies.

Leaders there continue to try to push the dairy sector toward greater efficiency and sustainability in more of a free market environment by 2015.