

NZIAHS Forum

“Where do we want our dairy industry to be in 20 years time?”

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The issues for dairy farmers in 20 years

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New Zealand's farm export story is straightforward. We have some dirt and water and we grow some grass. We convert these into protein that we sell around the world, earning export dollars and paying our bills back here at home. The dairy industry contributes significantly to this and is on a growth path.

Farming viability is one of two important areas of focus for Federated Farmers when it considers how to improve our farm exports. Essentially, this focuses on anything that affects income and expenses and tries to ensure the former is greater than the latter. Issues around input costs, compliance, rates, employment, farm gate returns, the supply chain, trade access, market structures and the impact of government monetary and fiscal policies (locally or globally) will always have an impact and will matter 20 years hence, as they did 20 years ago. Profit will still matter.

The second area of focus can be summed up as “our ability to farm for generations” and embraces strategic issues we must get right so we can continue to farm for another century, whether viably or not.

Environmental sustainability is critical. As custodians of the land and water we need to leave it better than we found it. We have set up and support the Landcare Trust and the QE2 Trust to do practical stuff, and farmers contribute millions of dollars to DairyNZ to work on practical solutions in the field. We also celebrate environmental success through our support of the Balance Farm Environment Awards Trust and of Janette Fitzsimmons and her www.goodfarmingstories.co.nz website.

Water is critical for dairying and for the country. Its ownership, allocation, management, quality and storage are in play right now and the decisions made in the next few years will have consequences that are felt for the next 50 years. If we get them wrong, our success as a nation will be constrained. If we get the balances right, then our ability to harvest and benefit from one of our critical comparative advantages will be enhanced. Water needs not be an issue in 20 years.

We have been running a campaign for the last two years on water storage. If it is successful, in 20 years we will have secured some economic and environmental resilience for the country. Around 30 projects up the eastern seaboard of New Zealand could be developed. We know from Opuha dam experience that for every 1000 hectares irrigated, about \$7.5 million extra cash is pumped into the economy every year and 29 new jobs created. We get more fish, less drought and increased

recreational opportunities for the wider community.

We need to build resilience over the next 20 years – both environmentally and economically, and water storage does that. We have just been through the worst recession we've experienced in three quarters of a century, but it wasn't started by the global financial crisis. It was started by the 2008 drought that, according to MAF, cost \$2.8 billion.

Urban rural understanding and perceptions of agriculture generally and dairy in particular will become more critical because the decision-makers increasingly are becoming more distant from the practicalities of farming and farmer numbers are declining in a proportional representation system of government. With Farm Day and other programmes the federation is trying to address that.

Agriculture needs good infrastructure - roads to cart inputs on to and produce away from our farms and transports links with global markets. Critically, we need rural broadband to enable us to connect with people and markets and to information to enhance productivity and production.

Our concerns about research are not only about investment levels, but also about the incentives on the players in the innovation supply chain. We need to be obsessive about innovation. The risk is that we become complacent.

The world is a competitive place and will become even more competitive over the next 20 years. The New Zealand dairy industry needs to keep ahead of its competitors, some of whom haven't yet been identified, and to be relentless in this pursuit. Genetic and other research around our farming systems needs to remain at the forefront.

That brings me to our agricultural intellectual capital and the importance of capturing cash flows from our genetics, from our farming systems and other agricultural intellectual property. We must develop models to monetise our weightless exports. Concerns around foreign investment in farms to some extent reflect our lack of a successful Intellectual Property (IP) strategy and business model.

The shallowness of our **capital markets is tied in with this**. The demand channel for protein is strong but the supply channel for credit is weak, resulting in our Government being challenged over the amount of foreign investment intended in farmland and particularly dairy land. Our lack of savings and shallow capital markets are among the country's greatest challenges over the next 20 years and part of the problem retaining our IP. We need to fix it.

The current dairy model is characterised by the aggregation of smaller units into larger ones, more intensely managed, with changing ownership structures. The traditional owner operator family farm is under some pressure, but perhaps the constraints on capital and the removal of gift duty will see a resurgence of that model over the next 20 years.

Succession is a big issue. The farmer in 20 years will be the young man or woman who now will be making decisions about moving into farm ownership. Our share milking structure, which Federated Farmers oversees, has been a huge success but is

coming under pressure. After we lobbied to get death duties and stamp duties removed, we began working on gift duty. Its removal should enhance inter-generational transfers.

New models will evolve. More use will be made of leases and equity partnerships, as is starting to happen now.

We've seen from Fonterra's experience in China that consumers want food they can eat that does not harm them. Increasingly they want to eat for better health, rather than just sustenance. New Zealand has an excellent track record and reputation. Enhancing that reputation will become even more important over the next 20 years.

We need skilled people on our farms. Farming is a complex business needing good people to run them and their management systems. We need skilled and motivated people, too, in our science and rural professional communities. Striking the right balance between education and immigration over the next 20 years will be important.

Something that wasn't predicted just a few years ago was the global financial crisis. According to an item on the Bloomberg website on 25 August, it is likely to impact the next 20 years through inflation, deflation, reduced demand, civil unrest, disrupted capital markets and so on. The Bloomberg report quoted a *Morgan Stanley executive director, Arnaud Mares, who said investors face defaults on government bonds, given the burden of aging populations and the difficulty of increasing tax revenue.*

"The question is not whether they will renege on their promises, but rather upon which of their promises they will renege, and what form this default will take."

"While the US government's debt is 53 per cent of GDP, one of the lowest ratios among developed nations, its debt as a percentage of revenue is 358 percent, one of the highest..."

"Italy has one of the highest debt-to-GDP ratios, at 116 per cent, yet has a debt-to-revenue ratio of 188," Mares said.

If things turn out as Mares predicts, the greenback is likely to tank and our NZD would appreciate significantly. If our strategy in the dairy sector – and in the wider agriculture sector - is to wait to be saved by a falling dollar, then we are taking a very big risk.

The global financial crisis has seen unprecedented volatility. So farmers have to deal not only with the weather and off farm regulatory risk, but with volatile commodity, interest and exchange rate values. Fonterra's new payment system and capital structure will see more volatility, which farmers and their banks will need to get used to. The costs of capital will rise and risk management will become more critical.

Also, as a result of the global response, economies that have over-indulged in debt

will have to take drops in standards of living and those that haven't are growing. We are seeing a massive shift from West to East as one empire declines and another rises. China is taking back the pre-eminent global position it gave up a century or two ago.

It is being followed by India, which is place today where China was about 10 years ago. This is good news for New Zealand. With a large emerging middle class, we have an increasing number of increasingly affluent consumers who are not as price sensitive who will pay premiums for safe high quality foods and protein. There is a big shift from starch to protein, so the protein demand channel is very strong.

There will be massive demographic changes, too. These are driven by two key issues – lots more people and more people living much longer. The metrics are phenomenal.

And then we have ethnic and family structure changes. This impacts on both the demand and supply side of agriculture.

Along with a geopolitical and demographic change, perhaps we are seeing an emerging ideological change. We are moving from a global division on the basis of democracy vs. communism to one based more around religion. That raises questions about our markets - the products we produce, how we produce them, and the location of our markets all may change as has happened over the last 20 years.

A key message is that over the next 20 years, as an agricultural sector, we need to focus on solutions, not just the problems. The longer anyone focuses on a problem and not the solution, the worse it gets.

Many of the issues we are concerned about now will still be concerning us in 20 years. Our ability to have what it takes to farm profitability in New Zealand will still be critical. But we live in an increasingly volatile, unpredictable world where change happens quickly.

The demographic and geopolitical changes that are happening are phenomenal. Technology advances and research endeavours provide an exciting catalyst for change on an ever-shrinking globe. We need to look over the horizon, look to manage increasing risk and volatility. We need to build resilience now. We need to aggressively seize the opportunity, or someone else will. We need to do all this and take the rest of New Zealand with us if we are to have successful agricultural businesses and happy lives.