Challenge Dairy Co-operative Ltd

Farmers working together….
Why it’s good for us

UWA – Institute of Agriculture Industry Forum 2009
Western Australia

2.4 million sq. km
2.0 million people

180 dairy farms
55,000 dairy cows
320 ML milk

But:
Largest herds on average in Aus
Largest farm size on average
Highest milk production per cow
Highest quality standards for milk
Largest number of non family employees
Challenge Dairy Co-op

- **Established 1999** – Began commercial operations 2001

- Under capitalised – **understaffed** - commodity products…. lack of investment in manufacturing

- Sanyuan JV – **2002/03** – the need for capital

- **October 2004** – QAF JV

- Jan 2005 – New CEO

- Nov 2005 – Benchmark study- Strategic plan
Did the WA dairy industry need a co-op?

Annual Average Milk Price - 01 - 06

Price (cpl)
The Road to Value Adding…..
COMMITMENT, VISION & INVESTMENT

• Farmers had a desire to secure their farm business long term

• They recognised the need to invest outside the farm gate in order to do it – if not… at the mercy of nameless faces in corporate offices that will affect their future

• They were/are prepared to put $$$ into that investment (whether it is cash or accept a lower milk price!! – within reason)

• They bought the commercial nous needed to develop the business plan (management)

• They ensured that the business plan would cater for the farm business (use all the milk, suit the supply, return the milk price required) – *in WA a small amount of milk therefore we need to look at specific niche/gourmet markets….*

• Be smart don’t compete with the big boys, find a small market and value add… farmers find ways of making things work

• The company looked at the opportunities and the risks (geographic location, available milk, current assets, available capital)
What next?

- Develop value added retail products (gourmet/niche/value add/export suited to lower milk supply)

- **Build front end to business** (marketing/admin/sales structure)

- Be Market driven not production driven – growth is locked step with market place opportunity – DRU system to manage value markets

- Exit commodities completely (no scale manufacturing possible in WA)

- Capital expenditure upgrading plant – spend wisely
That’s all very well… but what about growth?

Dairy processor stops taking new farmers in FNQ
Tuesday, 21/07/2009  ABC Rural

• Dairy processor National Foods has adopted a 'no new farms' policy in Far North Queensland.

• Local farmers says they've been informed the processor won't be taking on any new suppliers

• Some prices will be under pressure due to surplus milk at some times of the year. Factory closures in the regions of Queensland and NSW will add to the problem. Manufacturing capacity has been taken out of the regions.

Monday 27/7/2009  S & O Briefing Ms Jo Bills  Dairy Australia

SO HOW DO INDUSTRY / FARMERS GROW?
Confidence to Grow

- WA has cost effective supply of milk – IFCN, Red Sky data has shown dairy farming system here is cost effective and will support milk growth over and above domestic market

Annual Pasture Growth Predictable and Repeatable

Pasture Feed on Offer

- kg/ha
- month
- Jan, Feb, Mar, Apr, May, Jun, Jul, Aug, Sep, Oct, Nov, Dec
But…. 

- Value added products have been chosen to suit the size of the milk pool
- Growth needs to be matched to value markets or is problematic
- Proximity to SE Asia: Previously 7 day shipping, new technology opening up new markets for fresh milk solids. Only region in country/world capable of fresh bulk supply without refrigerated freight.
- Asia is our “domestic market” our growth
Australasia plays a crucial role in world dairy trade

Trade Flows in milk equivalents 1999 (000 tonnes)
(flows > 250,000 metric tonnes)

EU: >250,000 tons
Russia: >500,000 tons

USA 398
Mexico 331
Cuba 231
Argentina 1374
Brazil 348
Venezuela 285
Uuguay 399

Australia 359
New Zealand 350

Rabo International Agribusiness Consulting and Research Services
Speciality Cheese

- In line with retail cheese strategy - Chosen by Coles to be significant player in speciality cheese Aust wide category

- Woolworths / IGA (WA) major supply partner  Eg. Now have 30 – 40 product lines Coles WA. Would take an organisation a decade to achieve what Challenge has in 3 years:

**WE HAVE ESTABLISHED A SIGNIFICANT RETAIL BRAND IN AUSTRALIA**

Retail Milk

- After 18 month trial in South West, heading state wide with retail milk in August 09
Bulk fresh milk export

• Now have new and existing Singapore and Malaysia business and opportunity in Indonesia being developed

• Technology advances now allow us to extend to 15 days plus opening potential new markets – e.g. Indonesia / Thailand / HK / Southern China

• Successful in establishing a Dairy Australia / Curtin University grant to work further on using this technology – Concentrates.

Progressing value added butter fat project with Morinaga Japan

• Reduces exposure to commodity pricing export butter / coupled with retail butter

• R&D work done in Victoria - Only non Victorian Based Dairy Company in Australia that are members
08/09 another lesson that commodities can be a “dangerous” place when cycle is low:

The Global Dairy Market

The dairy commodity price peak of the past 2 years is now over. Prices are back to 2006 levels due to:

Prices have now stabilised and the consensus forecast is for gradual improvement through to 2010. Recent US / EU situation causing some uncertainty
So what’s changed…..?

In 07/08 Dairy commodities boomed globally prices responded

Since 02/03 price rises in WA have been driven by:

• Improvements in Challenge's capacity to pay (commodity price rise and product mix – value add ) eg: 2003 / 2004 WA was 4– 5 cents behind ESB price
  \[ \text{i.e. LAST 100M LITRES IN WA NO VALUE ADDED} \]

• 2008/9 Shortfall in supply and price competition due to declining overall volume

• Successful recruitment of farm milk by Challenge and the price premium placed on traded milk giving the value back to its members

• A significant price driver has been milk supply competition rather than an improvement in the value of the milk in final markets

\[ \text{CURRENT POSITION .....VAST IMPROVEMENT AND UNDERPINS WA GOING FORWARD} \]

\[ +5-10cpl \text{ compared to ESB} \]
Keeping wealth in the community

- We are the community
- Jobs in rural areas
- Children in schools
- Doctors in towns and hospitals
- Dairy – multiplier of value

<table>
<thead>
<tr>
<th>Primary agricultural industries</th>
<th>Type-2A multipliers *</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Output</td>
</tr>
<tr>
<td>Sheep</td>
<td>2.23</td>
</tr>
<tr>
<td>Grains</td>
<td>1.65</td>
</tr>
<tr>
<td>Beef cattle</td>
<td>2.33</td>
</tr>
<tr>
<td>Dairy cattle</td>
<td>2.07</td>
</tr>
<tr>
<td>Pigs</td>
<td>2.30</td>
</tr>
<tr>
<td>Poultry</td>
<td>2.75</td>
</tr>
<tr>
<td>Horticulture</td>
<td>2.22</td>
</tr>
<tr>
<td>Average (primary agriculture)</td>
<td>2.22</td>
</tr>
<tr>
<td>WA average (all 105 industries)</td>
<td>2.39</td>
</tr>
</tbody>
</table>

Notes:

*Type-2A multipliers demonstrate the impact of a unit increase in output, income, value-added or employment in the industries shown, on total output, income, value-added or employment in the WA economy.
THE “CHALLENGE” WAY FORWARD TO VALUE ADDING

- Develop local high quality products and use consumers parochialism to develop the market (‘cos it comes for free…) ie: Capel Brand, Farmers on milk bottles, Farmers on television ads …… builds ownership and pride in our company
• Develop Niche/value added export markets – PROTECT THEM

• Be prepared to make continuous investment in new products and management (whether its cash DRU’s or milk price – within reason)

• Hang onto the vision during tough times (when others around seem to always get the cream) - YES DIFFICULT

• End result….. a company built from low capital……a vision and excitement people own…Loyalty and ownership….. the strength of conviction and collective action………..

An integral part of community fabric
This hasn’t happened by chance...

It’s taken hard work and investment to move from a commodity process to a value added dairy ingredients business.

- Convertible grant from Govt and ongoing advice/assistance from DAFWA(WA)
- $10 M capital in 3 years
- Sales management structure WA / East Coast
- Establishment of sales support structure across Australia
- National warehousing / distribution process across Australia
- Upgrade quality systems / Admin processes
## What have we achieved?

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>No. of Members</strong></td>
<td>70</td>
<td>82</td>
</tr>
<tr>
<td><strong>Litres of milk processed</strong></td>
<td>70 million</td>
<td>120 million</td>
</tr>
<tr>
<td><strong>% of states milk under members control</strong></td>
<td>20%</td>
<td>35%</td>
</tr>
<tr>
<td><strong>Commodity Products Produced</strong></td>
<td>Bulk cheddar, Bulk Butter, Skim Milk Powder</td>
<td>Virtually none</td>
</tr>
<tr>
<td><strong>Retail Product Lines</strong></td>
<td>None</td>
<td>Retail milk, specialty cheeses, yoghurt &amp; custard, export milk, WM &amp; skim milk concentrates, 100 different lines ranged in state and national markets</td>
</tr>
<tr>
<td><strong>Dollar Turnover</strong></td>
<td>$35 million</td>
<td>$65 million</td>
</tr>
<tr>
<td><strong>Joint Venture Company</strong></td>
<td>None</td>
<td>Challenge Australian Dairy Turnover $100m</td>
</tr>
<tr>
<td><strong>Other services offered</strong></td>
<td>None</td>
<td>Farmwest – supplying breeding, herd recording, and building a portfolio of other farm services</td>
</tr>
<tr>
<td><strong>No. Staff</strong></td>
<td>80</td>
<td>90</td>
</tr>
<tr>
<td><strong>No. Trucks collecting milk</strong></td>
<td>7</td>
<td>12</td>
</tr>
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What drives everything is farmers who provide.....

VISION, COMMITMENT & INVESTMENT

.. It is this which safeguards our future and makes our community stronger
Challenge Dairy Co-operative
Proudly owned and operated by farmers

Thank you