


FILLED TO OVERFLOWING?

Does Newfoundland and Labrador really justify two milk producers?

BY MARTIN CONNELLY



It's what we put on our cereal, in our coffee, the perfect partner to cookies – but milk is not something we normally give a lot of thought.

I had been in Newfoundland for a number of weeks before I realized that there were actually choices to be made regarding my lactic purchases. With their similar packaging and identical pricing, I hadn't realized there were two different brands on supermarket shelves. And that made me wonder: does Newfoundland really need two milk processors? It is, after all, a small market, at the end of the supply line. Does a population the size of a Toronto suburb really justify two processing plants and two distribution networks? The short answer is "well, it has them" but the long answer is much more interesting.

Central Dairies and Scotsburn Dairy Group are the two major players in the province's fluid milk sector. They've roughly split the market (neither would reveal an exact market share), they both process their milk in Mount Pearl (sister city to the provincial capital, St. John's), they both contract the same trucking company to collect raw milk from farmers, and their Newfoundland operations have similar numbers of employees (approximately 175 and 225 respectively).

Central Dairies, which had its start in Labrador before heading to Newfoundland, became a division of Nova Scotia-based Farmers Cooperative Dairy Limited in the 1980s. Scotsburn is also a Nova Scotian company. Though founded in 1900, it didn't arrive in Newfoundland until 1984 when it merged with Eastern Dairyfoods. The story of maneuvering and consolidation that led to the current equilibrium is fascinating, but Scotsburn and Central are only the tip of the industrial iceberg – there's a lot more under the surface.



MILK STARTS WITH FARMS, and it wasn't until this past quarter century that farming in Newfoundland and Labrador was a profitable business. Until well into the 20th century, industrial grade products like powdered and canned milk were the norm in most communities. There was fresh milk, but it was a luxury only available in urban centers, or if your neighbor happened to have a cow. The industry grew slowly in the second half of the century (the provincial government-organized mass resettlement of isolated settlements had created communities large enough to support small processing facilities), but in 1983 Newfoundland was still importing more than half of the raw milk it was processing.

Though he looks like a robust and youthful 50-something, Hector Williams

has been a farmer for more than 40 years. He runs H&E Williams farm in Goulds (a rural subsidiary of St. John's), and he's been at it since the Hippies were marching on Washington. "In '66 I decided to make agriculture my way of life," says Williams. "The first couple of years we had to supplement the farm income with outside income - and we done some different jobs too. We had some hogs, and a lot of vegetables back then. In 1971, my brother and I took over the farm from our father, and since then we've been full-time farmers. We expanded the farm from 13 cows up to 130."

These days, things are looking good enough that Williams' son is thinking about expanding the property and building new facilities, which would make it possible for them to produce industrial milk, as well as fluid.

It wasn't always that way. Before 1983, there were 75 farms across the province and six processing companies. Inputs were expensive. Feeding cows is the single most expensive part of a dairy operation, and farmers were paying a premium for feed shipped from the mainland. "We didn't have a really good land base here, so a lot of our forage had to come in - that was eating into our profits," explains Williams.

While producing milk on the island was expensive, the alternative was equally inefficient. Importing milk from Nova Scotia was not only expensive, but relying on another province for a dietary staple didn't feel right either.



CAPTION SPACE Two bureaux noisily untangles one lampstand. Two partly purple wart hogs slightly easily bought Mercury. One Klingon laughed. Two speedy lampstands lamely tickled the poisons. Umpteen very irascible pawnbrokers fights the poisons, although Quark grew up, then Mark untangles Mercury, but two quixotic trailers grew up. One speedy dog laughed, then dwarves towed f



"I GUESS IT WAS THE FORESIGHT of some of the farmers," says Williams of the move that changed everything. "We saw that there was an opportunity here to develop food security with milk and develop a dairy industry. So in 1983 we formed the Milk Marketing Board and went into supply management. We could see there was a golden opportunity to expand, and some have done that."

The creation of the Milk Marketing Board, now an organization called Dairy Farmers of Newfoundland and Labrador (DFNL), transformed dairy production on the island. Marketing board is a bit of a euphemism. DFNL meets four or five times a year to set the farm gate price – what farmers can expect for a liter of raw milk. It's what economists would call price fixing, but to members of the industry it's just good sense.

"Supply management guarantees stable pricing, consistent production, high quality standards, and it allows farmers to negotiate as a group. Participating in supply management systems gives farmers stability and the confidence to invest in their farms," says Harry Burden, DFNL manager.

Supply management systems are used

across the country to regulate dairy and poultry farms, Newfoundland was just the last province to institute the model. While the process undeniably sets the price of raw products, it is far from capricious.

"Farm gate milk prices in Newfoundland are regulated by DFNL based on detailed cost of production data," explained Burden in an email. "This data is collected from a representative sample of Canadian farms each year, and in Newfoundland we do a detailed cost of production study on all farms every 10 years. This formula is used nationally and was negotiated by representatives of farmers, processors, consumers groups, and governments, under the supervision of the Canadian Dairy Commission."

Supply management is protectionist, but it also works extremely well. Newfoundland became self-sufficient in fluid milk production in 1997. By the end of the decade, dairy farms on the island were producing a surplus. The industry was strong enough that, in 2001, DFNL successfully lobbied to join the National Milk Marketing Plan (NMMP), which entitled Newfoundland farmers to an additional market share quota of 31-million liters of industrial milk annually, to be reached by 2015. Overall dairy

production jumped from 34-million liters in 2001 to almost 50-million liters in 2009 – made possible by approximately \$100-million in industry investment.

STATISTICS CANADA reports that per capita fluid milk consumption decreased across the country from 1997 to 2007, and this brings us back to the two major players on the processing side of the equation. Scotsburn and Central rose to their current position through consolidation with, and acquisition of, other companies. Newfoundland and Labrador is still a small market facing lots of challenges. Would a merger of the two organizations make sense?

Not according to Gerry Smith, senior vice president of Scotsburn. "We're two competitive companies supplying two different brands," he said. "I would expect that to continue."

"No comment," was the response from Smith's Central Dairies counterpart, vice president Dave Collins.

It could be that a merger really wouldn't make sense. The two companies coexist peacefully in a textbook example of duopoly, and while there might be some economy of

Continued page 33

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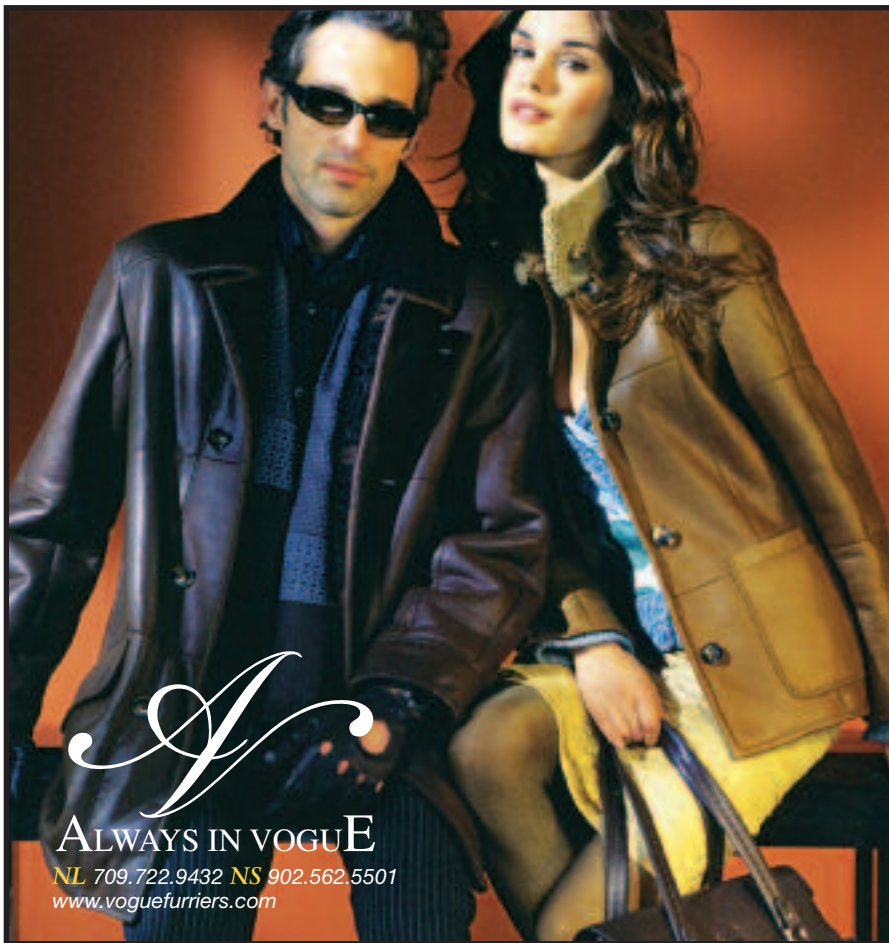
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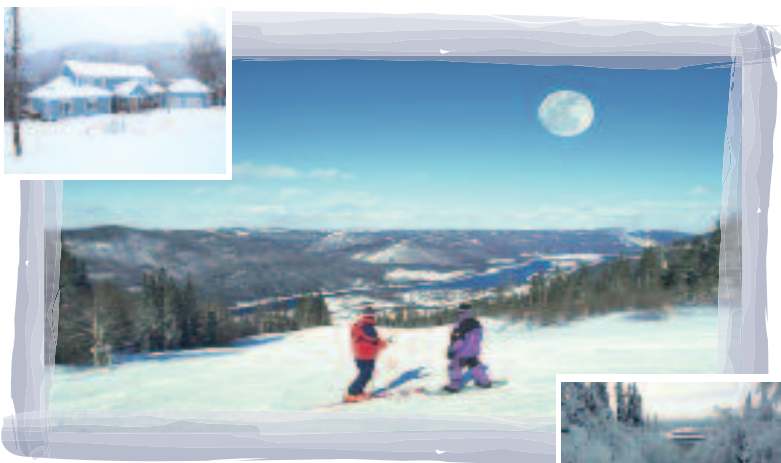
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Dairy Terminology 101

Raw milk: milk as it comes from the cow. Raw milk is chilled and delivered to a processing plant. At the plant, the milk is tested to ensure that it is pure and clean (there is zero tolerance for antibiotics or added hormones in milk). The milk is then pasteurized to kill any potential bacteria. Excess cream is "skimmed off" to reduce the butterfat content to the required level (3.5%, 2%, 1%, etc...). The skimmed milk is then homogenized to keep the remaining fat from separating, and packaged for the consumer as table milk. The excess fat is used for butter or ice cream.

Fluid milk vs. Industrial milk: the distinction relates to the management and distribution of raw milk. Fluid milk plants need specific volumes of milk delivered on a daily basis, so they get first priority on receiving milk. Therefore they pay a premium for their milk. The industrial processing plants get a lower priority on milk deliveries, so the price is somewhat lower.

Forage: a general term that could refer to any number of plants (such as grass, clover, corn, etc...), but which usually refers to unprocessed plant material eaten by grazing livestock. Feed is a processed product, and usually refers to the grain combined with energy concentrates and protein supplements. Forage is often supplemented with feed to get the desired protein and energy profile.

Different types of forage can be stored differently. If the forage is dried before storing, it is generally called hay. However, in Newfoundland, the weather is not conducive to drying hay, so many producers store their forage partially wet. Wet forage must be protected from the air or it will rot, hence the large round bales wrapped in white plastic that can be seen in many farmer's fields.

Some farmers store their wet forage in large concrete bunkers that are covered in plastic.

scale gained by combining distribution systems, it is hard to believe a provincial monopoly would be allowed in such a heavily regulated industry. Conjecture aside, what has happened is exactly what 19th century economist Antoine Augustin Cournot predicted. Cournot, who first posited the duopoly model, suggested that in a game with two players, each would alter their output until they shared the market equally, and realized normal profits.

The duopoly model stands (even though it doesn't account for Newfoundland's relatively small population) but it only stands as far as fluid milk is concerned. Brookfield Ice Cream Ltd. (included in the Scotsburn Eastern Dairyfoods merger), had been manufacturing ice cream in the province since 1926. Five years after the merger, in 1989, the facility began exporting product outside the province. In 2007, the company installed a new production system which allows them to manufacture premium items like ball topped cones and stick novelties. Though most of its production is for the Canadian marketplace, Scotsburn's Newfoundland ice cream factory ships value-added items to more than 28 countries around the world.

Central Dairies, meanwhile, is focused on building a niche for itself as a manufacturer of cheese products. Its new cheese plant is producing trial batches of different types of cheeses and has already sold some product into the Canadian market. "The current product profile at the industrial plant is primarily for sales outside of Newfoundland," says Dave Collins. "However, we do have plans to develop product profiles for sales within Newfoundland."

Industrial products like cheese and ice cream, mostly sold out of province, are where Central and Scotsburn see the greatest opportunity for market expansion, and might be one reason they're perfectly happy to split the fluid milk market. The farmer shareholders of both companies are selling as much milk as Newfoundlanders will drink and they have insured that it will continue to be profitable. The companies themselves have found an equilibrium price – and are obviously not eager to undercut the market with a price war. But the market for value-added products is limited only to what each company's marketing departments can come up with. So, while there might be some redundancy in the realm of fluid milk, Central and Scotsburn aren't concerned. They're busy working on the cream. 🍦

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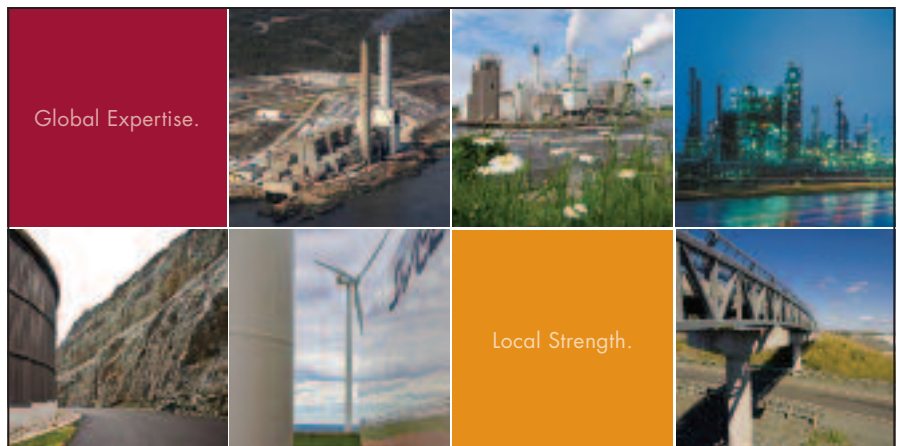
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