Putting the Prospectus report on the dairy processing sector into action

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It is over six months since the "Prospectus report – A Strategic Plan for the Irish Dairy Processing Sector" was launched by Minister Walsh. The report has generated a lot of discussion and supportive comment but also a number of criticisms of the Prospectus recommendations to which I would like to respond.

The report has been accused of "pulling its punches" regarding the future of quotas by only devoting two paragraphs to the issue. The scope of the terms of reference of the study related to the processing sector, milk production issues were outside the brief. We do however, recognise that there are major difficulties and challenges facing the dairy farmer and believe that the current quota management system is a major constraint to the necessary changes that have to take place if dairy farming is to remain economically viable.

The Irish industry is fragmented, highly seasonal in its milk production and is operating in an environment where costs are rising at a much higher rate than that of its competitors. A greater rate of cost increases is bad news for a sector that is mainly in the commodities business. The cost of production advantages that the industry has enjoyed for so long is being eroded. Meanwhile, Ireland's major competitors, those countries who like Ireland, are vitally dependent on export markets to take the vast bulk of their dairy output, (the Danes, the Dutch and the New Zealanders) have been very busy indeed in rationalising, achieving major processing scale, driving out inefficiencies and developing market and product strategies in response to the changing environment.

The Irish dairy industry is at a major crossroads and it needs to have a hard cold look at where it is today in terms of the number of players and the types of products it produces. Can it continue to afford, in the face of increasing competitive and market challenges, to have more than 13 processors who are very much focused on commodity production? The industry will continue to need to have smaller players to keep milk prices competitive but it needs to have smaller players who are dynamic, innovative and specialised on higher value and higher margin products. A combination of scale and efficiency issues will force out those smaller players who try and stay in commodities. Lower product prices and increased international competition will compel the industry as a whole, to address resource utilisation and processing efficiency issues or else it will face major decline. We have strongly recommended in our report that the Irish industry needs to develop a scale player (with operations both here and overseas) that can compete successfully on a global scale and meet head-on the competitive challenges from the Arla's, Fonterra's and Campina's in supplying the increasingly consolidated and global food manufacturers, food service companies and food retailers.

The industry needs to decide where it wants to get to. There are a number of potential future scenarios for the Irish dairy industry. It can try and stay more or less as it is now, with limited or no change to the way the industry is organised and the products it produces. But I don't think anyone would advocate such a strategy, as it will lead to inevitable decline.

It is argued by some, that Ireland because of its location, an island behind an island, with its cost advantages from grass based production, its seasonal milk supply, which limits product options, that it needs to be the New Zealand of the Northern Hemisphere and become extremely efficient in the production of butter cheese and powder type products. I don't believe that this is the best option for Ireland. It will still require ruthlessness in terms of cost efficiency and will necessitate major rationalisation at both producer and processor level in response to the need for scale. The industry would remain in low margin product lines with limited cash being generated to fund investments in capital and R&D. The sector would have to fight a relentless battle to stay price competitive by reducing processing and raw milk costs. Those who advocate such a strategy are being very circumspect in describing what the industry would need to look like in environment where the Irish industry is predominantly a commodity product producer, operating in a market environment where EU market supports and protections have been reduced and in some cases removed.

Another option is to look more and more to the UK and continental Europe, our doorstep markets and develop and target products, which are in demand and yield more profitable returns.

Whichever option is selected, the Irish industry needs to get more efficient as an important first step, by eliminating waste and duplication and by improving its productivity in the labour, plant and the overhead it utilises. All the cost efficiencies and painful readjustments to the changed market environment cannot only take place within the farm gate. The processing sector has to be ruthless in driving out unnecessary costs, inefficient structures and poor use of resources.

Moving more of the processed milk into higher value-added products will be difficult but it needs to be an essential component of a long-term strategy for the industry. However, this is only one element of the recommended industry strategy. A high proportion of the industry's output will still continue to be commodity based but the focus should be to move more and more into higher value areas and respond effectively to market requirements – selling what people want to buy and not simply what you can produce.

A lot of the debate and indeed criticisms of the report's recommendations has revolved around the creation of a super dairy with up 70% of the milk processed. The focus has been on the sheer size in an Irish market context of this entity and the difficulties involved in achieving this scale. The super dairy processor is a target that I believe the industry will eventually be forced to get to due to international competition. However the immediate and urgent focus needs to be on how to take costs out and improve processing efficiencies. The industry needs to start with rigorously identifying and taking actions that will have immediate impact on its cost efficiency. Industry consolidation through acquisition will absorb scare funding that needs to be deployed at improving cost efficiencies. The industry therefore, needs to be pro-active in looking at opportunities for co-operation and contracting out certain activities so as to drive out costs and make better use of resources.

The dairy industry has a long history. It has developed and adjusted to market conditions in the past. It has produced some excellent Irish companies who operate successfully on the international stage. It is also an industry that has a lot going for it but it has to quickly adjust to the very changed market conditions. There has been a lot of analysis and debate about what needs to be done but what is now required is action to achieve the dramatic reconfiguration and reorganisation of the industry to

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eliminate unnecessary duplication and improve efficiency to enable it to invest and be competitive. It is time for strong leadership and actions.