

Australian Dairy – Looking Ahead

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Australia – Current Environment

Farm

- Widespread drought conditions have had severe impacts on both income, costs, debt
- Significant group not fully recovered from increased debt
- Reduced herd
- Increased complexity of business environment
- Accelerated fall in farm numbers (below 10,000)

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Australia – Current Environment

Manufacturing

Continued rationalization/adjustment pressures

- supply constraints, through put costs
- capital requirements
- globalization pressures (investment/ customers)

Improved trade returns driving product mix decisions

- Exchange rate factors remain an issue

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Australian Supply Outlook - farm

- Milk pricing systems will stay deregulated
- Recovery from the drought will vary across production regions
- Improved grain/pasture position, but more rain needed in some areas
- Yield increases likely to lead growth - cow numbers will take time to recover
- Farmer intentions to remain in industry/ expand production

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Feed Barley price outlook



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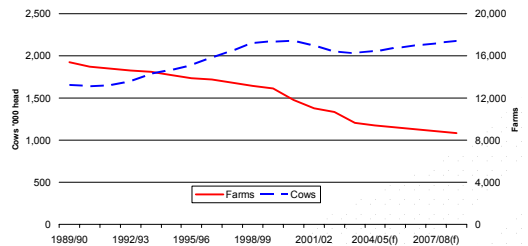
2006/07 production on my farm will be greater than 2003/04....



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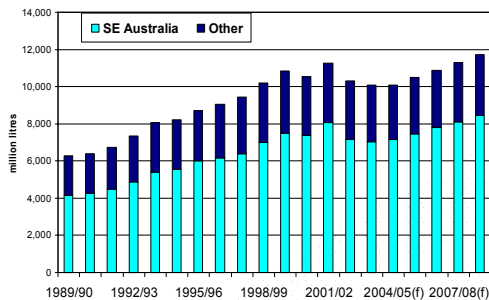
Australia - Projected Industry Trends



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Australian Milk Production Outlook



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Milk Production - wild cards

- Continued farm rationalisation – “deficit” milk production regions if loss of farms not offset by increased production/herd size in remaining farms
- Variation in performance of farms and production systems
 - Low farm profitability bottom 25% (ABARE)
 - Possible shifts in calving systems to reflect pricing
- Longer term NRM issues - access to land, water resources and pricing

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Manufacturing Outlook

- Cost Pressures
 - Low plant utilisation rates will see through put costs remain an issue
 - Drive relocation of manufacturing plant into regions with greater potential for growth
 - Greater exploration of opportunities for partnerships/facility sharing
 - Trade off between pricing strategies to flatten supply curve and investment in plant to cope with seasonal production

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Manufacturing Outlook

- Profitability
 - Value chain migration – toward higher value products to maximize opportunities, returns from limited milk pool and keep ahead of commoditization
 - Organizational restructures to continue. Increased polarisation between large players chasing economies of scale, niche players seeking specialised markets
 - Pressures from environmental, food safety, quality assurance requirements

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Domestic Market Outlook

- Australia to remain local industry's most important market
 - Some volume growth – cheeses, yoghurts
 - Significant potential for value growth
 - Sophisticated marketplace looking to value added products that are functional, healthy, convenient
 - Tension between these trends and supermarket pressure toward commoditization through broader house branding strategies

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International Market Still Key Driver

- As production expands, international market opportunities will be increasingly important drivers of industry returns, profitability
 - direct link to price settings (company and regional farm gate)
 - Continued demand for traditional products
 - Key outlet for new products, components (Japan, North America)

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International Supply Outlook

- EU expansion /CAP reform to result in more internally focussed dairy industry
 - Lower export volumes, continued reduction in subsidies
- New Zealand to increase share of world trade through production growth
- Latin American countries re-emerge as dairy exporters
- Potential Asian export rise (India)
- United States likely to remain internally focussed

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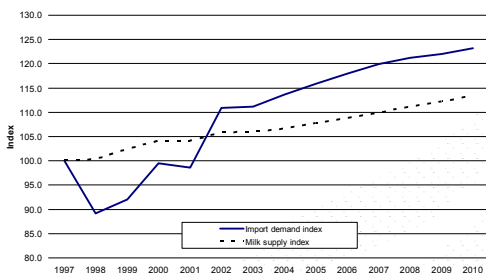
International Demand Outlook

- Steady growth in demand
 - Economic growth in Asia, Middle East, increased affordability, helping drive demand for traditional dairy products – particularly cheese, powders
 - Japan/ASEAN remain major markets for Oceania supplies
 - China to increase in importance – demand to outstrip internal production increase
 - New demand for higher value dairy components, functional foods, nutraceuticals in developed economies (but pressure from non- dairy substitutes)

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Projected supply - demand balance



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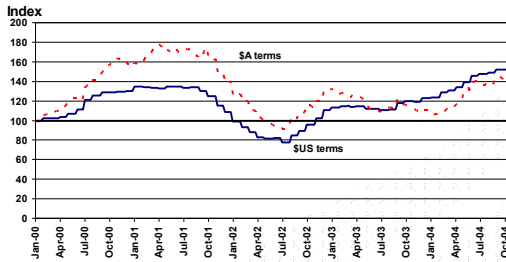
International outlook

- Near term
 - Supply balance, economic and income growth in major markets should support higher, more stable prices (US\$ terms)
 - Oil price effects, exchange rate movement major risk elements

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Australian export index



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International outlook

- Near term
 - Supply balance, economic and income growth in major markets should support higher prices (US\$ terms)
 - Oil price effects, exchange rate movement major risk elements
- Medium term
 - Policy changes should support market balance, growth provide environment for further improvement in world prices

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Dairy Policy – Potential gains

- WTO Doha Round to address export subsidy, domestic support (possibly less so market access) but gains delayed til late in decade
- Regional and bilateral FTAs offer parallel access gains.
- Market access gains important (not just price premiums). Also offer
 - Greater marketing flexibility
 - Opportunities for sophisticated, new products (reduce dependence on commodity trade)
 - Greater certainty over capital investment/ returns
 - Opportunities for joint dairy franchise development

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In summary...

	1994/95	2003/04	2008/09	2014/15
Production (mill litres)	8,206	10,075	11,718	14,602
Farm numbers	14,166	9,611	8,628	7,678
Herd size	129	214	252	318
Cow numbers ('000)	1,822	2,056	2,175	2,381
Yield (litres per head)	4,550	4,900	5,388	5,974

Assumptions: Nominal farmgate price in range 30 to 32 cents per litre, AS\$ in range 71 to 72 US cents, average seasonal conditions

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Concluding Remarks

- Expect resume profitable growth phase
 - Market fundamentals favourable, both for traditional, new dairy products
- Significant challenges as well as opportunities
 - Ongoing changes in industry structures / ownership
 - Environmental pressures/regulations
- Need for continued focus on innovation, adaptation to build, maintain momentum, gains

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THANK YOU

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