

The history of the dairy cooperative Murray Goulburn and its farmer suppliers shows how a close relationship of trust has developed and been broken with the collapse of the farmgate milk price. Roots of the current crisis can be traced all the way back to the deregulation of the dairy industry at the start of the century.

Murray Goulburn was founded in Victoria in 1950 and grew steadily over the next two decades to become the nation's largest dairy company by 1973. In its [2015 annual report](#) it recorded total assets of over A\$1.84 billion and total revenues of A\$2.88 billion. It holds a large portion of the dairy market, in 2016 it was estimated by [IBISWorld](#) to have just over 42% of the national market for milk powder and 31% of the national market for milk and cream.

Over half its revenue comes from exports, primarily into Asia. It's also the nation's [largest buyer of raw milk](#), employing around 2,400 people and with approximately 2,500 members.

Deregulation and the “keystone” role of cooperatives

The deregulation of the Australian dairy sector started in 1999 and rolled out over the following year. It saw the repeal of existing state legislation regulating the supply and pricing of milk.

The impact of this deregulation was mixed across Australia but it led to the decline in the total number of dairy farmers, from around 10,000 in 2000 to about 6,061 in 2016. It is likely to fall even more over coming years.

Despite increases in the overall size of dairy farms, most remain small-scale, family owned businesses. Dairy farming requires higher levels of capital investment than most other agricultural sectors, with major expenses being automated milking machines.

Milk is now essentially a global commodity and dairy farmers are price takers. With the need to invest more into capital equipment, fuel and stock feed, profit margins in the sector have been

squeezed.

Over the past five years the average profit margin for dairy farms has fallen. Any decline in the farmgate milk price will only put many producers into unsustainable losses unless they can increase economies of scale by having larger herds or lower input costs.

Another consequence of the deregulation of the dairy industry has been the decline in cooperatives. The Dairy Farmers Cooperative was sold to National Foods (now Lion) in 2008, and Bega Cheese demutualised in 2011 and listed on the ASX. Today there are about nine dairy cooperatives active in Australia, the largest of these are Murray Goulburn and Norco Ltd from northern NSW.

Cooperatives like Murray Goulburn are different from other businesses. The cooperative should be focused primarily on its members' welfare and as such it is unusual for them to be able to satisfy the often competing interests of members as patrons and outside investors from the ASX.

A well-run cooperative can be sustainable and profitable. It can serve as a "keystone" business that helps sustain its members. Keystone businesses are those firms that serve as a major buyer or supplier for many smaller "niche" firms, helping to keep the smaller firms more sustainable for an entire industry.

The approach taken in terms of milk supply and pricing is an example. Since the deregulation of the dairy industry Murray Goulburn has effectively set the farmgate milk price across most of the Australian dairy sector. It also takes all the milk its members wish to supply.

This stabilising and coordinating or "keystone" role within the dairy industry has been a feature of Murray Goulburn since market deregulation. Given the size of the cooperative anything that might affect its long term operations will have significant impact on the Australian dairy industry.

The issue of trust in a cooperative

Cooperative enterprises are owned by their members who also have a trading or patronage relationship with them. What differentiates them from other businesses is the democratic governance of the business, with member-owners having a say in major strategic decisions.

Management of a cooperative is therefore more complex and the board and executive leadership team must maintain the trust and loyalty of the members to keep the business strong. They also need to balance the member's interests as suppliers (patrons) and as investors, while encouraging them to see themselves as owners of the cooperative and members of a [community of purpose](#).

The financial strength of the cooperative is only as important as the financial strength of its members. To survive the cooperative must maintain a clear social and economic purpose with the members' interests first and foremost.

Gary Helou, then CEO, was part of a new management team brought into Murray Goulburn in 2011 to modernise and strengthen the cooperative's leadership. However, his management style appears to have been more in keeping with that of a regular firm.

Recent [revelations by Fairfax Media](#) suggest that Helou and the senior management of Murray Goulburn had evidence of declining export sales as early as July last year. However, they continued to promise farmers a "guaranteed" high farmgate milk price and share price.

Although a capital restructure at Murray Goulburn was endorsed by the board it raised some concerns in the financial press and among [former directors](#). The financial crisis that the cooperative has found itself in is something of a self-inflicted wound.

It has sought to "[walk both sides of the street](#)" with its ASX listing and overconfident pronouncements of keeping the farmgate milk price at around \$6 per kg/MS.

Dairy farmers who are or once were members and shareholders have lost money. Many retired farmers who had their preference shares converted to the ASX listed ordinary shares have seen the value of their stock collapse. For their younger active counterparts the loss of share value is

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Written by The Conversation USA

compounded by the lower milk price with many facing debts of A\$100,000 to A\$120,000.

Former CEO Gary Helou and former CFO Brad Hingle have departed Murray Goulburn leaving the cooperative's board and Chairman Philip Tracy to face down angry farmers and shareholders, plus a class action led by legal firm Slater and Gordon.

Murray Goulburn's members have been essentially turned from owners and members of a democratic community of purpose, into suppliers and investors whose share value is linked to the price of a litre of milk. That's where the problem lies.

This is not necessarily the end of Murray Goulburn, however, they will need to regain the trust of their members and demonstrate that as a cooperative their primary focus is on the well-being of their farmer members.

As a business it must be frugal and focused on delivering its members the best prices at the lowest costs it can. Any investment and growth should be designed to provide its members with the best long term returns to their businesses at suppliers or buyers, not just to see the value of its share capital appreciate.

Of equal importance is the cooperative's ability to keep its members loyal not just through the prices or dividends that it offers, but because they feel a sense of ownership and being part of a community of purpose that would be lost if the cooperative disappeared.

Tim Mazzarol receives funding from the Australian Research Council (ARC), Co-operative Bulk Handling Ltd and the Business Council of Co-operatives and Mutuals (BCCM). He is also the Director of the Co-operative Enterprise Research Unit (CERU) at the University of Western Australia.

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