

# STATES OF JERSEY

## Economic Affairs - Dairy Review Sub-Panel

WEDNESDAY, 13th DECEMBER 2006

**Panel:**

Deputy A. Breckon of St. Saviour (Chairman)

Deputy A.E. Pryke of Trinity

Deputy K.C. Lewis of St. Saviour

Deputy R.G. Le Hérisier of St. Saviour

Deputy S.C. Ferguson of St. Brelade

**Witnesses:**

Dr. D. McQueen

**Deputy A. Breckon:**

Thank you. It is 2.00 p.m. We are back in session. Jane, could you just confirm the sound system is working? Thank you. Welcome, Dr. McQueen. I will come to you in a moment or two. I will just go through the procedures of where we are, some of which will be known to you but I will just give you a general outline. This is a scrutiny sub-panel hearing which was set up to review the dairy industry in Jersey. It is a joint review with the Chief Minister because the Economic Development Minister is conflicted because of a family interest in the dairy industry and as a result of that joint terms of reference were agreed and given to Promar who are international consultants advising us. They have produced a report of which the final version has appeared in the last few days. The Minister for Treasury and Resources had two propositions before the States of Jersey. One was to move the existing dairy to Howard Davis Farm and the other one was to changes to a covenant at Howard Davis Farm and those proposals have subsequently been withdrawn. The States, the Ministers and this panel are deliberating about how we best would proceed and hopefully you will be able to inform and advise us on that, bearing in mind your experience and I will come to you in a moment. If you would outline first your relationship with Jersey and your previous history, if you will, just in brief to set the scene. First of all, could I remind you on the desk in front of you there should be a copy of the oath for witnesses who are not members of the States of Jersey and I will just read this. It is important that you fully understand the conditions in which you are appearing at this hearing. "The proceedings of the panel are covered by parliamentary privilege under Article 34 of the States of Jersey Law 2005 and the States of Jersey (Powers Privileges and Immunities) (Scrutiny Panels, PAC and PPC) (Jersey) Regulations 2006. Witnesses are protected from being sued or prosecuted for anything said during hearings unless they say something that they know to be untrue. This protection is given to witnesses to ensure that they can

speaking freely and openly to the panel when giving evidence without the fear of legal action although the immunity should obviously not be abused by making unsubstantiated statements about third parties who have no right of reply. The panel would like you to bear this in mind when answering questions and the proceedings are being recorded and transcriptions will be made available on the Scrutiny website.” I should just like to add to that, Dr. McQueen, that you will be given a copy of the transcripts. If there is anything you say which you then subsequently discover is factually incorrect you will be given the opportunity to correct that and we will take out the “ums” and “ahs” not for your benefit more for mine, really. So, that will happen within, hopefully, within the next 48 hours and then after 7 days if you have not commented they will become a matter of public record. We have apologies from Deputy Anne Pryke who will be joining us. She has another commitment. That is Deputy Sarah Ferguson, Deputy Roy Le Hérisier and Deputy Kevin Lewis. My name is Alan Breckon and I am the Chairman of this panel and I will hand over to you. First of all, if you could tell us who you are and a little bit about yourself?

**Dr. D. McQueen:**

Yes. Well, thank you very much, Chairman, and these look like quite sophisticated microphones. Is this tone of voice correct or is it too soft? Is it all right for everybody?

**Deputy A. Breckon:**

It is okay.

**Dr. D. McQueen:**

Thank you very much. Well, I have spent my entire working life either in the dairy industry or closely associated with the dairy industry. Having first of all done my PhD at the University of Glasgow on the evolution of the dairy industry, I moved into the milk marketing board system, initially with the Milk Marketing Board of England and Wales and latterly with the Scottish Milk Marketing Board where I was Marketing Director and then Deputy Chief Executive. I left the Scottish Milk Marketing Board in 1989 to take up the position of Chief Executive of the Scottish Dairy Trade Federation, which was the milk processors’ organisation in Scotland. That appointment effectively came to an end with the dissolution of the milk marketing boards in 1994 because the Federation no longer had the role it previously had under the statutory arrangements. It was shortly after then that I set up my own business providing consulting services in the dairy sector (and other associated activities that are not relevant to this meeting) and I have been doing that ever since. I was engaged by the Jersey Department of Agriculture, or the Agriculture and Fisheries Committee as it was at that time, in 2002 to undertake a fundamental review of the dairy sector in Jersey. This was completed and submitted in February 2003 and was accepted by the States. It involved about 20 recommendations for economic recovery in the industry, mostly, but not solely, addressed to the Milk Marketing Board. The Milk Marketing Board has been going through these recommendations systematically ever since and most of the key ones have

been put in place. Until we reached the particular set of circumstances that have led to the present enquiry the recovery programme was , in my judgment, moving forward satisfactorily.

**Deputy A. Breckon:**

Can you confirm that you have also been advising on a regular basis to that report?

**Dr. D. McQueen:**

Yes. I was asked to continue in an advisory capacity after the report was submitted to oversee the developments in the industry in the light of the recommendations in the report and I have been submitting routine monthly reports ever since. I have in fact just completed my 44th monthly report. It seems an awful lot, but all these reports taken together will provide a historical record of what the board and others have been doing by way of reforming the industry and putting it on to a more sound financial footing.

**Deputy A. Breckon:**

Thank you for that. I take it you were given written questions of some of the subjects?

**Dr. D. McQueen:**

I was indeed. Thank you, yes.

**Deputy A. Breckon:**

I would just add to that there could be supplementaries so we may bury you a little bit. That was for guidance and depending on what develops we will obviously work from that. Could I ask you, then, the first question that is listed there? Have you had any involvement with the terms of reference in production of the *Promar Report*?

**Dr. D. McQueen:**

I had no involvement at all with the terms of reference that I can recall. There might have been some brief exchange at some point but no substantial involvement and when I eventually saw the terms they were new to me and much wider than I had expected. So far as the Promar investigation itself is concerned, there was an expression of desire in the Department of Agriculture that I might be involved significantly with Promar. I think the phrase was “in a guidance capacity”. It was recognised that there were certain aspects of the industry where I had, by virtue of my experience in Jersey, an expertise which the Promar team could not reasonably be expected to have and there was a hope that a measure of guidance would take place. In fact this did not happen to any material extent. I had, of course, and thanks for that, pre-notice of this question and was able to check on the facts. At an early stage in the enquiry I had one substantial meeting with two of the Promar team at a location between our two offices. I spent, I suppose, more than half a day with them but that was really entirely about sketching

the background to the industry; giving them a framework within which they might start to think about the problems. The meeting was not concerned in any way with solutions to problems or about what they thought might be in the report. It was entirely background information. I did express a willingness to help further in any way I could including, if required, visits to their office in Cheshire. That never materialised. I did, however, receive two telephone enquiries after that. The first was to ask what I knew about the product costings arrangements in Jersey Dairy because that had been a weakness I had identified in my earlier report – that the dairy did not have proper costings data – and they asked if I knew whether the situation had been improved. As a matter of record I told them that it had been substantially improved but that they should speak to Mr. Eamon Fenlon, the present finance director at the dairy, who had all the records they might want to see. That was one exchange, and of course we talked about some of the facts underlying the question. Then quite near the end of the inquiry – I am not sure but it might have been after the first draft appeared, near the end of the inquiry anyway – they came back to me and asked about what happened in the United Kingdom when the milk marketing schemes were revoked and a system of voluntary co-operatives were put in place. That is, of course, a complicated subject but I was able to give them some factual material, copies of old records and that sort of stuff, which I see they have in fact used to some extent in their final report. That was the extent of my involvement.

**Deputy A. Breckon:**

Could you comment on the *Promar Report* and how, if anything, it mirrors or builds upon your own recommendations from years earlier?

**Dr. D. McQueen:**

Yes. Well, I have to be careful here. Can I start with the second part of that question? It does not in any sense build upon my recommendations. It is, in fact, flatly contradictory to my recommendations. The recovery programme I recommended, and which has been accepted up until now, was based on the Milk Marketing Board being at the heart of the industry in Jersey. There was discussion in my report about the role of the Board, and also about some ways in which its operations could be improved – that is on the record for people to look at – but the essence of the board, its essential nature, was not in my mind open to question. I built my case on the Milk Board being fundamental to economic recovery. The *Promar Report* deviates in a major way from that and, from my perspective, insofar as it deals with that aspect (ignoring for the moment aspects like semen importation and other things that are not central to the marketing function) I think it is an unfortunate distraction from the recovery of the industry. That is at the very best. At worst it is a recipe for a total disintegration of the industry and obviously you would want me to elaborate on that, but at your pace, please, Chairman.

**Deputy A. Breckon:**

Please, if you feel --

**Dr. D. McQueen:**

Do you want me to go into the mechanics of that situation? Let me tell you the essence of this. This was not spelt out in my report, but it could easily have been so, because it seemed to me so transparently obvious that the Milk Marketing Board system in Jersey is the right system for the market in this Island that I did not even begin to make a case for retaining it. I did make a case for changing it in some fashion but not for removing it. Now, the essence of this is that if you look at the matter historically milk marketing boards were put in place in the United Kingdom, and indeed elsewhere in the world, where certain very specific circumstances applied. These circumstances were that the markets in which they were to operate had a high dependence on liquid milk sales. If you look at the European dairy industry you will find that in every other country apart from the United Kingdom and these Islands the dairy industry is based on milk products. Liquid milk is a very small part of the industry. They are based on cheese and butter production and on condensed milk production or other products. When you get a dairy industry based on the liquid milk market you have a naturally higher priced market because liquid markets are inherently immune from foreign competition, basically. You cannot shift liquid milk over huge distances as you can butter and cheese, for example. Now in the United Kingdom what happened was that back in the 1930s –and this is ancient history but it is all very relevant – the market began to be undermined by cheap imports of dairy products from the Commonwealth. In those days it was most notably cheddar cheese from Canada which came in, and also butter from New Zealand. It all came in very cheaply and given the free market conditions of these times those low-priced products undermined the entire dairy market. The high price which the farmers previously got for their liquid milk was no longer sustainable because those farmers who found themselves getting low prices by selling milk to cheese and butter manufacturers quite naturally diverted their milk supplies to liquid milk processors at lower prices to get a cut of that market. The entire market collapsed. Now, there were various attempts made in the United Kingdom to set up voluntary farmers co-operatives to solve this problem. Some were reasonably successful for a short time. The most outstanding one was something called The Scottish Milk Agency which survived for about 3 years and then it too collapsed. It collapsed because farmers on the edges saw the opportunities to cream off money from the market by going straight to the processors. It was when that happened that the Government in the United Kingdom brought in statutory control of milk marketing to protect the market, to keep prices at a reasonable level for farmers. Now if you leap forward in time, 70-odd years or so to the situation here in Jersey, you have basically the same situation. You have it, I would suggest, even more obviously than in those early days in the United Kingdom. You have a market here in Jersey which is highly dependent on a protected liquid milk market. I see various reports in some of these documents about the Milk Marketing Board being a monopoly. I think that is a rather misleading concept. The Milk Marketing Board is a monopoly of milk produced in Jersey, that is true, but it is certainly not a monopoly when it comes to trading in products in the shops with its butter and its yoghurt and its ice cream and everything else. There it has to compete with people who can send these products into Jersey from all over the

world. All over Europe anyway. It has to accept the prices it can get in competition with these imported products. As a consequence the value of the milk going into these products is much less than it is for milk going into the liquid milk market. To give you a rough idea - and this is where I had difficulty with the detail in my own report, because the Board in those days did not have good costings – the net return to the Milk Board for selling milk into the liquid milk market, after all the costs are taken into account is something in the region of 55 pence a litre. It is in that kind of area. It retails in the shops at around 90 pence. Take off the packaging costs and so on and they get about 50-odd pence. Mr. Fenlon would give you a more precise figure but it is in that area. This must then be compared with the return the Board gets from milk products. The net return available to the farmer from butter and powder, and you must look at these 2 together because they are joint products, it is something in the region of 7p a litre. The net return for other products is usually in between this and the return from the liquid market. They are probably on average around 20p a litre or something like that. It is difficult to be precise but you are talking of a vast gap in returns. That is what has to be protected because immediately you remove the disciplines which the Milk Board can put in place for the benefit of all the farmers in the Island you allow people to exploit that available liquid milk premium to the disadvantage of everybody else. That is the reason why, if you take away the disciplines which the Milk Board have in place then you invite people to exploit the opportunity, and they will do. You can see it already in the Classic Herd initiative and in Mr. Binet's recent suggestion for a joint liquid milk operation . These are both examples of people who see an opportunity to get more out of the market at the end of the day at the expense of everybody else. If that is allowed to continue the entire market will collapse.

**Deputy A. Breckon:**

Would you like to comment on how you see a milk marketing scheme that is over 50 years old against a competition law in a competitive environment?

**Dr. D. McQueen:**

Yes. I see no fundamental conflict there. I know so far as the Competition Law is concerned there is a legal conflict. I know you have just had Bill Brown speaking to you and no doubt he would explain this in fine detail. The problem is one about the way in which the Milk Marketing Scheme is written in Jersey and there is an unfortunate turn of phrase used in it that is quite different from that used in the United Kingdom where this legal conflict never arose for that reason. This is something that can be cured at the stroke of a pen. It can be cured by altering the wording of the Milk Marketing Scheme in a very small way or by giving a public policy exemption to over-ride the conflict. But it does seem to me almost a Gilbert and Sullivan situation that you have two important pieces of legislation in place in Jersey, admittedly 50 years apart, which are in conflict. Now, somebody should have spotted that when the Competition Law was drafted. That is something that maybe needs to be looked at. How was it possible to put in place a piece of legislation that was in conflict with another piece of legislation? But that conflict can be resolved. Now when you come to ask about the practicalities of this I take you again

back to what happened in the United Kingdom. First of all there was no conflict between the milk marketing schemes and competition law because of the way in which they were framed. The boards were given the powers to do things and they were required to do them under law. What is more, the milk marketing schemes in the United Kingdom were endorsed by European law. There was a set of European regulations, which are available for anyone to consult, put in place specifically to authorise the existence and continuation of the milk marketing boards in the context of European law. You have asked the question. I say there is no necessary conflict between milk marketing board systems and modern competitive environments.

**Deputy A. Breckon:**

I would just like to ask a supplementary on that. How you would see from a milk marketing scheme a move to a non-statutory co-operative to set up a workable alternative?

**Dr. D. McQueen:**

I think it is a dangerous alternative, for a number of reasons. The board is in place to regulate the market. That means to keep competition under control. When you remove that control you remove the glue that holds the entire system together and that is why it will collapse. Now, you ask what will happen if you put a voluntary co-operative in place and I would suggest that you simply need look at what has happened in the United Kingdom. A voluntary co-operative could be put in place. It would require a lot of assistance from the Government because if you just end the milk marketing scheme and do nothing else you have to disburse the monies to the farmers and then you have total chaos. You have to create some kind of machinery for transferring the assets of the Board to the new voluntary co-operative. That is not an easy thing to do, but it can be done. But in the middle of all of that you have to recognise that you cannot deny individual farmers their right. A voluntary co-operative is exactly that – it is voluntary and therefore you have to allow individual farmers who do not want to be part of it to be out of it and we know already that there are some. We could all name some of them in this room, those who would not want to be part of it. These people have rights too and their rights are to a share of the assets. You have to find some way of allowing them access to the assets. Now I could go further because what will then happen will be that immediately you put in place a voluntary co-operative where there is freedom for individuals to act outside the co-operative, as there would have to be, the incentive of the high liquid milk price as an inducement to do it alone would become immediately very obvious. It is already obvious. We have two people, one person doing it and another person thinking of doing it. That will become an irresistible force and what will happen will be what has happened in the United Kingdom – the voluntary co-operative, which might well start off with the majority of farmers in membership will progressively find itself handling the milk that nobody else wants. If you look at the United Kingdom that is exactly what has happened. Look at all the dairy companies in the UK and look at the big co-operatives. There are 4 very big ones. See what they are paying the farmers. They are all paying farmers the lowest prices. Why are they paying them the lowest prices? Because they are

dealing with the milk that the dairy companies do not want. They are dealing with the weekend milk and with the high seasonal surpluses at the end of May and beginning of June. It is a high cost operation, they pay low prices and they always will pay low prices. That is what will happen in Jersey, because the co-operative will be up against it from day one and it will find itself progressively under attack from independents.

**Deputy R.G. Le Hérissier:**

Dr. McQueen, you said earlier that your recommendations were progressing satisfactorily. But yet here we are looking at yet another consultant's report and the dairy industry, certainly the Members feel they are on the brink of a possible blood bath. Quite bluntly. Why do you think, from your analysis of your industry and your long acquaintance with it over the last 10 or 15 years, we have reached this situation yet again where the industry appears to be in crisis?

*(Marginal note re. above statement: my involvement has actually only been since 2002 – say 4 or 5 years)*

**Dr. D. McQueen:**

Well, I think it is in a kind of crisis now because of the *Promar Report* and all of the issues arising from that, but before we go on to that stage I think “crisis” is much too strong a word. The key recommendation in my report was to get a huge amount of cost out of the processing sector. This was partly to overcome some of the excesses of the past but mostly to compensate for the increased weight of overheads due to the planned reduction in the total herd size in 2001/2002. The Board have had substantially new management in the period following my report – a new managing Director and a new Finance Director and other key people have changed as well – and they have done extremely well in removing costs from the industry. In fact, they have removed about 50 per cent more cost from the business than I recommended. I recommended a 20 per cent cut in the running costs of the dairy, which sounds a bit high, does it not? I think, and again the dairy can tell you the exact figure, the reduction in cost is now approaching 30 per cent. But they have gone about as far as they can for there is a limit to what can be done at Five Oaks. So the next step is, of course, to get the new dairy. Everybody recognises that. Promar recognise that. That will be a step change. What is happening now is, you see, that they have reached a position where they cannot reduce their costs significantly more until they have a fundamental change in their dairy. Naturally, if you cannot reduce your costs inflationary pressures will catch up with you. So what you are finding at the moment is that the board is experiencing a squeeze. It cannot any longer reduce its costs structurally to a major extent but its elemental costs are increasing all the time – wage costs and everything else. So it is finding itself squeezed. It needs to get out of that dairy. When that happens there will be a step change and they will be back on course. That is the problem.

**Deputy R.G. Le Hérissier:**

The allegation has been made that within the industry there are inefficient operators and that a co-



operative is in a sense a way of disguising inefficient operations and sustaining them beyond economic common sense. Do you agree with this?

**Dr. D. McQueen:**

Well, there are two aspects of that question. Are there inefficient operators and is a co-operative the best way of dealing with this? It is a feature of the dairy sector in every country in the world, when compared with other types of farming – cereal farming, beef farming, whatever – that the range of net profitability is greater. This is because dairy farming is a relatively high-tech kind of business. It is a more difficult thing to get right than growing crops. Because of that, you are going to get some people who do not do it very well and others who do it extremely well. So, this big range of ability is inevitable in the dairy sector. Promar make the point that the range is greater in Jersey than it is in the United Kingdom. I do not have evidence to counter that but I do question that statement. I question it statistically, apart from anything else, because you are only looking at 33 herds in Jersey and statistically it is very difficult to draw a robust conclusion from that small number. It only takes one rogue case to upset all your figures, so I do question whether Jersey in that regard is any different from anywhere else, but I have to confess I cannot readily prove that statement. As for a co-operative protecting things, the important thing is that the industry maintains a revenue stream for the farmers in Jersey which is sufficient to maintain a significant industry. Throughout all the commentary I have seen it does seem to me to be a kind of absolute that the Island requires to have a significant dairy industry based on Jersey cows. Now that is a political view, a philosophical point almost, and one which, not being a Jerseyman, I do not have any particular feeling for. But if that is what is required, then you do require to maintain a reasonable level of income to sustain that kind of industry. If you let it collapse, which is what will happen if you take the Milk Board away, you will end up with a situation where that type of unique industry structure could not possibly survive and you will then end up with pressure to have other breeds of cattle on the Island. I can see the industry comprising half a dozen Friesian herds, for example, if the milk price comes down materially from its present level. That may, of course, be a solution that some people would regard as acceptable. That is debateable, but it is not what people tell me is wanted and I would conclude that you have to maintain a reasonably high milk price. That will always sustain people some people who are better operators than others and some who are poorer operators than others. That is the inevitability of the case.

**Deputy S.C. Ferguson:**

It has been said by Promar in their report that one of the problems with the co-operatives in the UK was that they did not own their processing facilities. Is that a valid comment on this being the reason why the co-ops did not work? They made further comments that for a co-op to work in Jersey it must own its own processing facilities.

**Dr. D. McQueen:**

Well, that is a very profound question really and it requires a slightly profound answer. First of all the contribution which processing can make to farmers' incomes is not huge. There is a misconception around in the UK that the milk processors are making a huge amount of money at the farmer's expense. Typically the margin a processing operation will make, that is net margin after costs, is somewhere between one penny and 2.5 pence per litre, and that is what is up for grabs if a co-operative runs its own dairy business. I would have to say that it is better running your own dairy business successfully than not, but I do not think that is the reason for the relative lack of success of the dairy co-operatives in the UK. The reason is that they have to take all the milk from their members that the members give them. That is the nature of a co-operative, whereas a dairy company can buy milk as it requires to meet its requirements. I believe that is more important than the fact that they may or may not own processing businesses. Take Northern Ireland for example. I was looking at this just yesterday. The main dairy farmers co-operative in Northern Ireland is called United Dairy Farmers. That is the co-operative which took over, unusually in the UK, the old processing factories of the MMB and it is the one co-operative in the UK which has had, from the start, a substantial involvement in milk processing. Today it has probably the lowest milk price in the UK. It is now paying 17.5 p a litre when the UK average is about 19 p. Whether they would be even worse off if they did not have their own dairies is another question, but I do not think that dairy ownership is the key to the entire situation.

**Deputy K.C. Lewis:**

Dr. McQueen, Promar International I believe somewhere here describes the Jersey dairy industry as an industry in crisis. Obviously by your previous remark you disagree with that. If not in crisis how would you pitch the level there?

**Dr. D. McQueen:**

I would say the industry is in a state of anxiety. There is no doubt about that. "Crisis" is a very emotive word. The industry is not in crisis in the sense that it is going to collapse next week or something of that nature.. It is not that. But there is undoubtedly a growing anxiety. I have been watching this month-by-month, as I explained, and there has undoubtedly in the last year or so been a growing unease among farmers, because they have not seen their milk price increase. The milk prices which the Board are paying have not increased in, I think, the last two years, certainly in the last year they have not increased. They shot up initially by about two to three pence a litre when the Board at first successfully cut costs out of the system, but then other costs began to creep up on them and the milk price has not been able to be increased again. So, there is a growing unease and there is a fear among farmers that they are not going to get any more for their milk in the future. This will be solved when the new dairy is put in place.

**Deputy K. Lewis:**

Do you agree with Promar that the situation has changed since the production of your report?

**Dr. D. McQueen:**

I do not believe that the situation has changed in a way that requires a dramatic departure from the course of action that was put in place following my report. I do not accept that at all. Obviously the situation has changed. It has changed in the sense that the dairy is more efficient than it was when I did my report. Prices are higher than they were when I did my report. The dairy industry is a bit smaller. A few people have dropped out. Yes, there have been changes but I do not think they are changes that require a fundamental change of direction in how the industry is to recover. That has not been demonstrated by Promar

**Deputy A. Breckon:**

Can I ask you to comment on something which you touched on earlier, asset protection? Could I combine that with possible asset stripping and how you see that that is maybe a period where things are ring-fenced so that a strategy and a plan could be put in place? Would you like to comment?

**Dr. D. McQueen:**

Yes. I think you are referring again to the mechanics of switching from a statutory system to a voluntary co-operative. First of all, I think the term ring-fencing is an unfortunate one. It has all the wrong connotations and I think it should be dropped from discussion on this particular issue, for a reason that I will explain. The concept of ring-fencing is that you protect a particular set of assets for use by an organisation and do not allow anyone else access to them. Now, as I explained earlier, that is impossible under a voluntary system. All the milk boards in the UK, when they converted to co-operatives, were required to make provision for those who did not want to be part of the new arrangements to get access to the assets. So in that sense the assets were never ring-fenced. What you can do is you can facilitate the transfer of the assets to a new organisation but you cannot protect them. You cannot ring-fence them in that sense. I say to you that there will undoubtedly be people who will see an opportunity here to get their share of the assets out of the organisation. They may have to do that by taking shares in the organisation and there may be trading rules that restrict early access to the cash which these shares represent, but you cannot deny people who have been part of the construction of the present industry access to their share of the assets in a situation where the system has been disbanded. So, ring-fencing is not in the narrow sense a total possibility.

**Deputy A. Breckon:**

In your opinion then would something like that need to be confined with an orderly exit strategy for those who, for age or circumstances, wish to leave the industry?

**Dr. D. McQueen:**

I think that is a political matter. I would not necessarily have thought that followed. I do not think you

necessarily have to provide an easy access for people to get out of the industry. The people who are not joining the co-operative are people who will hope to do better than being in the co-operative. That is the situation.

**Deputy A. Breckon:**

The reason I say that, Dr. McQueen is perhaps there are people who are still in the industry waiting for an outcome and then will decide what to do and exiting could be part of that.

**Dr. D. McQueen:**

Yes. I have not thought too deeply about that question, I have to confess, but my feeling is that the natural course of events should be allowed to happen. I certainly do not see any case for government money being put into that.

**Deputy A. Breckon:**

Is it, in your experience in the UK, a practice that there is in fact a type of ring-fencing which protects the assets for a given time so that too many people do not leave at the same time? Did that happen in the UK?

**Dr. D. McQueen:**

Yes. That certainly happened but they had to be paid out eventually.

**Deputy A. Breckon:**

It was done in an orderly way?

**Dr. D. McQueen:**

It was done in a fashion which allowed the assets to carry on under new ownership. Yes.

**Deputy A. Breckon:**

Can I touch on something else regarding the export market, and I think we have a buffer which use is made of, and you said earlier about butter, but in your experience how achievable is the export market to the Jersey Dairy? I should say we were told by the consultants earlier in the week that the UK dairy market was about £3 billion and it would be achievable if Jersey, I think it was described as: "Come up with a jackpot and hit a niche that was acceptable with a suitable outlet" be it a supermarket or something else. Would you comment on how tough that market is and what is your experience of it?

**Dr. D. McQueen:**

Yes. My experience of that market, and we are talking here essentially about the market for fresh milk products, not cheese and bulk butter though possibly packet butter but yoghurt particularly. That is what

we are talking about – fresh products.

**Deputy A. Breckon:**

Value added. Yes.

**Dr. D. McQueen:**

So-called value added. That is an extremely tough market. Every dairy company in the UK, almost, is looking for an opportunity to get into that market, because it is potentially rewarding. But it is also a market area which is very tightly controlled by a number of very big players. It is extremely tough. I am not saying that Jersey Dairy should not try to get into it but I do not think that you should necessarily build a case on getting into it. It was never part of my solution for the industry. I think people should persevere but it should not be the plank on which success or failure is measured. What is important to the industry is that the processing sector generates a high enough return on average to sustain a sensible size of industry. I think it is quite capable of doing that without major involvement in export markets if it has to be that way. The liquid milk market will generate its own high return and while the other things, which at present are basically butter and skim milk powder but in future are likely to be cheese, will make a lower return they should, in a modern custom-built dairy, make a high enough return which, when taken together with the liquid return, will give a decent enough average producer price to sustain a healthy industry.

**Deputy A. Breckon:**

Can I ask how that view you have just expressed squares with the current quota of in excess of 14 million and an average liquid milk of 9? Where is this buffer going?

**Dr. D. McQueen:**

Right. Well, that was looked at in my report and the figures were very similar to the ones you have just quoted. I came to the view that there was no case for engineering a change in the size of the industry from the present level. This is basically because the liquid milk market requires significantly more milk than the sales total of about 9 million litres to sustain. This because the milk which is being sold is largely fat-reduced whereas the milk coming into the dairy is full cream milk and the two do not match up. For this reason alone you need more milk coming from the farms than the total you are selling. You also have to cope with seasonal fluctuations and with weekly fluctuations as you cannot have a situation where you run temporarily out of milk. So, you are talking really of a minimum requirement in the region of maybe 11 million litres. This is a difficult calculation. Promar have attempted it but did not come to a very clear conclusion. If 11 million litres is right that only leaves you with about 3 million litres for the other products and it does not seem to me that the difference between, say, 11 million and 14.3 million, the current annual licensed volume, is particularly material in the context of what we are talking about here. 14.3 million litres represents a significant dairy industry here in Jersey and I have

always felt that is what the over-riding objective is, to maintain a healthy, significant dairy industry. I say, and I say again, that a 14.3 million litre industry can be sustained in future on the basis of liquid milk, cheese and fresh products mostly for the local market, all based at a new efficient dairy. I see no problem with that provided the Milk Marketing Board system is in place to regulate the market.

**Deputy A. Breckon:**

You earlier said that butter and powder would have a price of about 7 pence a litre and the dairy were paying 33 pence per litre so there is an element of loss and risk already there. So, can you explain the economics of that?

**Dr. D. McQueen:**

I think that is a very important concept you raise. There has been great confusion over this. The *Promar Report* never really got to grips with the difference between the net return to milk producers from processing milk and the profitability of a commercial milk processing operation. If you take the example you have just given of milk being purchased at 33 pence from the farmers and generating a return of 7 pence you might say: "Well, that is a total loss-making operation" but every co-operative in the world operates this way because they are all selling milk at different net returns and what they pay the farmer is an average after their costs are met. Quite clearly some of their products will be below the average and others will be above. So it does not make any sense to cut out the ones that are below the average because you then have to start all over again. The key thing is what is the average return to the industry? What can be done? What sort of system can produce a reasonable return for the industry? That is the question. So it does not follow to my mind at all that because the return is only, in the example I have given, and subject to checking by the accountants, 7 p per litre that production should be discontinued. Where it should be discontinued is if the actual cost of converting the milk is greater than the return from the market. If, for example, you make a tonne of butter and you get, let us say, £1,200 for selling that tonne of butter and it costs more than £1,200 in the factory to make the butter then that is a nonsense. In that situation the milk should be poured down the drain. But that never happens. Not in my experience. There is always a bit left over to pay the farmers and that is all that is required, provided the overall net return from all sales is considered satisfactory

**The Deputy of Trinity:**

Good afternoon, and I apologise for being late. I had another appointment. Just looking to the future, what do you see are the main issues that the new co-operative, well before that the board, have to face immediately?

**Dr. D. McQueen:**

Immediately?

**The Deputy of Trinity:**

Yes.

**Dr. D. McQueen:**

Do you really mean immediately? Before the new dairy is in place? The new dairy is the key issue here. That has to be the principal objective, but only if the Board has a clear vision of the way ahead, which it does not have at the moment because there is a great blanket of uncertainty over the industry. There is particular uncertainty about whether the board is going to retain its regulatory powers or not, and this is likely stop everything in its track. I am not party to what the Board are discussing privately but I would be surprised if there is any clear intention to proceed with re-investing at Trinity at the moment, given the uncertainty in the industry. I would go so far as to say that such a major investment commitment could be irresponsible because the Board do not know at the moment whether they will be able to retain their powers and if they do not how many farmers are going to be with them. How can they commit an unknown number of farmers to a heavy investment? This is a difficult area. But if the Board's powers are kept intact, and they are able again to see the way ahead, that is their prime objective - to get a new processing facility to replace the current one.

**Deputy K.C. Lewis:**

Dr. McQueen, following on from Anne's question, and apologies in advance if I am misquoting you, but I got the impression that you are against a co-operative as such and that the present Milk Marketing Scheme could work with some tweaking or restructuring. Could you outline that a bit more, please?

**Dr. D. McQueen:**

Well, I think it can work without any tweaking or restructuring to be honest with you. I mean I do not think you have to touch anything at all. But if you want to make it a bit better than it is at the moment I think there are certain things that you certainly could do to it. Some of these things are in my report, incidentally. I think the entire internal governance of the Board could be looked at. They have a curious way in which they delegate much of the responsibilities to an executive committee, which is a sub-set of the Board. I am not convinced that is a necessary part of the system but it is a matter for debate. It is in the Scheme. More fundamentally, I think that the whole nature of the dairy in relation to the Board should be looked at. The dairy is essentially a commercial operation and the Board is a milk management operation. These two in Jersey are inter-woven to a degree where it is very difficult to disentangle them. I think there would be benefits in having the dairy as a more clearly separate entity. Now, I am not saying that it should be a totally separately-owned entity. I still see it as being owned by the Milk Board or owned by the farmers, but to be separately accountable to a greater degree than it is at the present time I think would be a benefit. These are matters which need discussion in points of detail.

**Deputy A. Breckon:**

Is that one of the conclusions of your report, that the dairy should be more commercial and pro-active?

**Dr. D. McQueen:**

More separate, yes. It is because of the confusion that can arise between the two operations. You have seen this in the present debate about the Competition Law. With the emergence of other dairies like Classic Herd, for example, it is important that they should all be trading on the same milk supply terms as each other, and this would include Jersey Dairy. That at the moment is not terribly clear. There are ways in which it could be clarified. The old milk schemes in the UK were subject to an EU legal requirement that their commercial operations should be subject to a separate system of accounting and administration. This was to clarify the difference between the two operations, not for other reasons. These are areas that could be looked at. They are not essential but I think they are desirable.

**Deputy A. Breckon:**

In your opinion in the time that you have been involved in looking at the local situation would you say that there is a dramatic improvement in the governance and reporting structure of the dairy in generally accepted accounting practices, FSR17, and the pensions thing? Is there more transparency and clarity than, say, 5 years ago?

**Dr. D. McQueen:**

Absolutely. I mean, it is night and day, frankly. I am not equipped to go through every area here but certainly in general this is true. Milk price accounting, in particular, is hugely more transparent now than it was. When I was doing my report it was almost opaque. It was very difficult to see through what was going on at the dairy and it was very difficult to write that part of the report. That has changed quite fundamentally. They have made great strides in that area.

**Deputy R.G. Le Hérisier:**

Dr. McQueen, you have spoken very robustly of the need for the current scheme to continue, which is essentially a monopoly, but of course there is a ghost at the back which is a lifting of the import ban. If that were to occur, do you think there is enough robustness built into the system to withstand --

**Dr. D. McQueen:**

I think that is a very pertinent question and a good one. Obviously, if the import ban is lifted, and let us say it was lifted next month, there would be an immediate problem. There would potentially be stiff competition from imports from the United Kingdom. My answer is that the Milk Board is by far the best arrangement to counter that situation, better than any other one you could imagine. At the most elementary level you have a situation where the Board is a vehicle through which the Government can exercise its influence and control. The government can go straight to the Milk Board and know it is speaking to the entire industry and discuss issues and come to solutions with their assistance.



Immediately you remove that and you are dealing with 5, 6, 7, who knows what number of individuals, you have a different problem. When you come to imports I would say to you that if you have, let us just postulate, 5 businesses packaging and selling liquid milk in Jersey independently and imported milk comes in at a cheap price there is going to be greater price competition among these 5 to get an edge in the market against imports than there would be with the Milk Board operating as a single local supplier. So I say again that the Milk Board arrangement is the best defence against imports. It would be difficult, but it is the best way of dealing with this situation were it to arise..

**Deputy R.G. Le Hérissier:**

One of the comments, Dr. McQueen, made about the *Promar Report*, by the people who have supported it perhaps, is that it might be a little short on detail in regard to the export strategy section. Now, you have spoken of the need for an export strategy, in not the same breath but in an accompanying breath, you have spoken of likely intense competition in places like the yoghurt market and here we are going into the jungle, so to speak. I mean, what steps should be in place to make sure we can really operate well in that export market?

**Dr. D. McQueen:**

Sorry, you say: "Going into the jungle." What jungle are we referring to here?

**Deputy R.G. Le Hérissier:**

Well, it is one of my colourful phrases. The jungle of exports. The intense competition within the supermarket sector of getting our product on their shelves, albeit in only relatively small quantities.

**Dr. D. McQueen:**

Yes. Well, I cannot really add a great deal to what Jersey Dairy are already doing. They have experts in this area. Dairy staff have been constantly speaking to all the major multiples for the last two years at least. They know what is required of them. It is a question of getting a degree of interest. I do not think there is anything I could add to help their marketing strategy. I will just say again it is a very difficult area.

**Deputy R.G. Le Hérissier:**

Well, you have been very candid with us and we do appreciate that and this is your chance to be even more candid. The government and the industry are locked in an embrace, and I am not sure both parties quite like the embrace, but we are locked in this embrace for good and for bad and you have observed the politics of this situation over several years. Have you got any advice to the politicians? On the one hand clearly our money is needed and certain programmes are needed but on the other we are seen as very sort of over-interfering and so forth and we do not let the managers manage. What is your view?

**Dr. D. McQueen:**

This is a very wide question. I presume it is meant to be in a narrow context within the milk industry and I hesitate to go into areas outside of the milk industry. My clear view, and I will say it again at the risk of repeating it unnecessarily. Let the Milk Board get on with the job. When this whole issue of the apparent conflict between the Competition Law and the Board's regulations first arose I could not understand why the Government did not leap in to defend the Milk Board. The Milk Marketing Scheme is an important part of the legal framework of this Island. I wondered, and still wonder, why the Government did not just say: "Wait a minute. There is something wrong here. Let us sort this out." Instead of that we have a huge area of damaging uncertainty, obfuscation and difficulty and I think, if you ask for advice, that is the advice I would give. Let the experts get on with it. The Milk Board is full of experts and they have a lot of relevant experience. They know how to run the industry, but need to be given a chance to do it.

**Deputy A. Breckon:**

I would just like to bring this session to a close but before I do that, Dr. McQueen, I would like to thank you for the time and trouble you have taken and, as Roy has said, the candid views and opinions you have expressed. Before I close I would like to give you the opportunity to say anything that we may have missed or anything you would like to say in conclusion.

**Dr. D. McQueen:**

Yes, well, I think we have covered a great deal of ground and the questioning has been very good, to the point and varied. I do not want to extend the process any more. I would only say that as regards the *Promar Report* specifically I would draw the panel's attention to the fact that virtually all of the main conclusions, particularly about marketing structures, are without substantiating evidence. I would suggest that you have only to look quickly at the report see that. The evidence is lacking because the evidence is not there. That is the first thing I would say. Apart from that my only concern is that the Government will have a sufficiently wide view of the situation to know how best to support the dairy sector and to ease quickly the present atmosphere of dreadful uncertainty. In my view, this threatens to lead to the ending of the industry as we know it. I think that is all I would say, Chairman.

**Deputy A. Breckon:**

Thank you very much. Again, I conclude by thanking you, Dr. McQueen, and we now adjourn until 3.15 p.m.

**ADJOURNMENT**