Tracing farmer cooperatives

An Australian example mirrors what has happened in Canada

AUSTRALIA'S WARRNAMBOOL CHEESE & Butter Factory opened its co-op doors in 1888 with six shippers. Like Dairyland, WCBF was a progressive, well-run cooperative. Both maintained and honed their edge through the 1980s.

Then, in the space of a decade, everything seemed to change. By 2001, Dairyland (see last month's column: The Dairyland Story) was picked up by Saputo for 50 cents on the dollar. In 2004, the 116-year-old Warrnambool Cheese & Butter cooperative became a publicly traded company.

In Canada – how Canadian, eh? – it all started with cheese. In the 1980s, McDonald's Restaurants sourced cheese slices locally.

One day, they announced they wanted to buy from only one Western Canada supplier. Dairy co-ops in BC, Alberta, Saskatchewan and Manitoba decided they should find a way to collaborate to keep the McDonald's market.

In the 1990s, Dairyland merged with Northern Alberta Dairy Pool, Central Alberta Dairy Pool, DPCL in Saskatchewan and Manco in Manitoba. As part of the BC-Alberta mergers, the new Dairyworld cooperative kept Dairyland's Head Office and CEO, but BC's (strong and respected) chair had to step down in favour of a (less experienced and weaker) chair from Alberta. Dairyland's requirement to go back to members for debt authorization was also dropped.

The spending spree begun several years earlier accelerated. "Deals" included Pocklington apparently getting $125 million for Alberta plants he'd reportedly picked up from Palm Dairy three years earlier for $50 million. And Ault Foods quickly accepting a "take it or leave it, one time only" offer of $18 million for the Winnipeg Silverwood fluid and ice cream plant they were about to list for $13 million. Such "deals" papered the path according to one industry observer.

It all ground to a halt under a

A warrnambool Cheese and Butter Factory building, left, and some of its products, right.

[The writer is an award-winning columnist living on Bowen Island. She encourages feedback at wendy@thehomteam.ca] mountain of debt in 2001. Members were offered no choice. Saputo walked away with the store.

In Australia, the story is a little different. Without the protection of supply management, retail milk price wars were costing dairies a lot of money, and dairies were passing this on to the farmers.

To maintain prices to its shippers, Warrnambool made a strategic decision to pursue the international market. A new cheese and WPC plant was built in 1993, a new powder plant was added in 1998, a Tokyo office was opened in 2002 and a new fluid plant constructed in 2003.

Members were told expansion needed capital, and capital meant privatization. Rejected in 2003, a resolution to privatize passed one year later; in 2004 the 116-year-old cooperative became a public company.

In the case of Dairyworld, privatization was fueled by financial crisis: sale to Saputo at 50 cents on the dollar was accepted by 90 per cent of the delegates as "either that or bankruptcy".

In the case of Warrnambool, it would appear market expansion was the privatization driver, although cooperative economist David Craig's observations at the time suggest pressure was applied:

"The board's solution was that profitable growth was necessary through demutualization. The board did not propose whether the necessary profitable growth could be achieved without demutualization. It did not, therefore, provide an alternative to demutualization. Demutualization was presented to the members as a crash through or crash option – the only viable option."

Protected from hostile takeover for seven years by a (first 10, now) 15 per cent share cap, this protection came in handy in 2009, when supporting a cheese venture with National Foods cost the company $20 million and left them holding $85 million in debt, double year earlier levels.

When Warrnambool tried to recoup by cutting prices to farmers, they quit shipping in droves. For the first time in history, Warrnambool ran in the red. Shareholder confidence plummeted and share prices dropped from $4.80 to $1.64 a share.

This vulnerability quickly attracted four takeover bids (three from Murray Goulburn Co-Operative, Australia's largest processor, and one from Saputo). All were rejected by the Warrnambool Board - without reference to shareholders - on the basis that they were "opportunistic and did not reflect the strategic value of the company".

Last June, with share cap removal a mere 12 months away, 52-year-old CEO David Lord, 14 years at the helm of Parmalat Australia, was recruited to repair the balance sheet before the next bidder knocked on the door.

Last November, Warrnambool's Board struck an alliance with Bega Cheese, selling 15 per cent of its shares for $22.6 million and raising a further $14.1 million from a new share issue. With this, Warrnambool purchased the technology needed to compete in the growing milk derivatives market. (Viewed as strategic partner, Bega is a 120-year-old Australian cooperative about to go public with a June IPO that analysts expect will peg value as high as $385 million.)

Today, Warrnambool is considered similar to Dairyland before the mergers: smaller than its rivals but a sectoral super star. Classically cooperative, its root strengths are quality shippers (over 600 farmers from Australia's prime dairy regions supply the plant with 900 million litres of milk annually), a low cost, efficient plant (sales of $480 million and anticipated net profit of $17 million this year, a doubling over last year) and a wide network of strategic alliances with international partners (95 per cent of Warrnambool's product is exported).

With share prices recovered to the $4.50- $4.70 range and debt below $20 million, Warrnambool is in good position to face the international suitors. Just in time; the share cap came off May 25th.

Close behind Bega on the bidders carpet, with an 11.4 per cent share in Warrnambool, is Murray Goulburn Co-Operative. Saputo will no doubt also be watching carefully. As will many others, including China's Bright Foods, Singapore's Olam and Australia's Fonterra.

But the real question is: who will the farmers support? As suppliers, they hold a lot of sway. While Bega appears to have the inside edge, Murray Goulburn is also seen as a fair, cooperative player that would maintain some competition in the market place. According to analysts:

To win at WCB any local or foreign buyer has to be able to show to farmers... that they can at least compete and sometimes pay better than the majors as WCB already does. If the farmers aren't convinced they could leave the company, going to another competitor even at reduced competition levels.

Fascinating. I will follow the Warrnambool story over the next few months. Keep those Dairyland stories coming. An analysis of the ins and outs of both these co-ops is in the works. Just in case there are some lessons here from which we all can profit.