

Co-ops are the right answer for dairy farmers

Amidst the discussion about how farmers can best participate in the dairy market in future, it's important to remember that dairy co-ops, First Milk and Milk Link, already fulfil the roles proposed for POs and do much more besides. That's why we believe that dairy co-ops offer the best long term position and prospects for farmers, and it's why we suggest that joining a co-op should be farmers' default first choice.

The objective for POs (Producer Organisations) is to replace individual farmer negotiation and contracts for the sale of raw milk with collective negotiation and collective contracts held by a PO. This represents a considerable step forward from the position of non-co-op farmers currently. POs will be able to negotiate from a position of market significance with a substantial volume of milk. This should enable more price transparency and open up new capabilities in supply and quality programming, joint planning with customers and shared market intelligence. In the longer term, as trust and track record build, new collaborative opportunities should arise to pursue win-win strategies for all businesses in a supply chain that will release extra value, perhaps through innovation in products, processes and marketing.

However, POs will still be selling raw milk, the most perishable of farm products, without any ability to store or convert to a stored form. They will continue to have to sell to the restricted range of processors within a reasonable geographic distance, and they will have minimal influence on the strategies that those processors will pursue in maximising returns to their shareholders, which may include limiting the transparency and flow of information along the chain.

Dairy co-ops go further and address these restrictions in exchange for farmers investing to own the next stage of their supply chain – processing, brands and distribution. This enables them to determine the products, markets and degree of risk they wish to incur. It also means that the profit margin that is generated in processing, marketing and distribution is available to co-op members to either support the milk price, reward their capital investment or invest further in the co-op – it's up to them to decide. Co-op membership involves greater responsibility and off-farm investment, but gives farmers much greater control over their destiny than other routes to market. Just ask dairy farmers in New Zealand, Netherlands, Denmark or the USA.



How to decide - dairy co-op or Producer Organisation?

Co-ops and POs offer quite different propositions to UK dairy farmers and for that reason there is a legitimate place for both – co-ops for those seeking long-term security and a share of value-added with willingness to invest off-farm, POs for those with a shorter term horizon and less willing to invest off-farm. However, it's always important to remember that no business model provides absolute shelter from commodity market volatility. SAOS is in discussion with our members, NFU Scotland and the Scottish Government about how POs might be most advantageously established in Scotland, and SAOS is available to assist any formative groups.

On the next page we take a closer look at the some of the features that distinguish co-ops from POs.

Keep the date!

31 Jan 2013 - SAOS Annual Conference & Dinner (plus optional morning workshops)

We've now set the time and place for our conference, which will be held at Creiff Hydro Hotel. More details to follow in due course but please note the date for now.

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Dairy co-ops

The main advantages of farmers investing on a large scale are:

- Farmers own more of the marketing chain, so capture for themselves the value that is otherwise lost to PLC shareholders.
- Real extra value can be added in processing, by creating brands and owning distribution.
- Through their co-op, farmers develop a range of markets to avoid over-dependence on any single product or product group. They decide for themselves the optimal market mix and marketing strategy for risk management.
- Market intelligence and emerging opportunities can transmit back to farmers more quickly and farmers can get involved early in premium value and growth opportunities.
- A truly global perspective on market development can be adopted.
- Co-ops create absolute long term security for dairy farmers and their family successors.
- Scale provides other opportunities such as joint purchasing of inputs, power, advice, etc.

However, the following points must also be considered:

- A significant amount of capital is required from members, and this has an opportunity cost to each farmer as it might have been invested elsewhere (possibly on farm). Based on latest accessible accounts, investment in Arla is £123,255/member, Fonterra is £261,000/member, Campina is £120,902/member and First Milk is £30,888/member.
- The demand for capital in any ambitious globally competitive business is unceasing, although beyond a certain scale extra capital is likely to be generated by co-op operations and borrowing rather than by continuing member investment.
- Given their long term nature, co-ops require a long term perspective from farmers. They are not suitable for farmers who require freedom to transfer their milk sales amongst alternative buyers. A co-op becomes the permanent marketing arm of a dairy farming business through both ups and downs.
- Success requires excellence in co-op governance and management, with members, directors and managers all understanding their roles in this regard and discharging them effectively. Once this is established, a co-op becomes extraordinarily resilient.

Dairy POs

Some advantages from collectivising farmer milk sales are:

- Buyers are obligated to adhere to a single negotiated contract with the PO, rather than separate contracts with each farmer. This should provide farmers with a stronger organised negotiation.
- The introduction of contract negotiations will be from a position of market significance with a substantial volume of milk and the ability to respond to chain requirements.
- It will be possible to increase price transparency and negotiate an acceptable basis for milk pricing.
- Opportunities will arise in collaboration with contract partners in supply programming, joint planning and shared market intelligence.
- New opportunities will become available to identify, evaluate and pursue win-win strategies (for businesses in a supply chain) to release extra value that is not accessible in current farmer selling. This could be through innovation in products, processes and marketing.
- POs will adopt risk management strategies that identify and manage key marketing risks.
- Members are not required to invest large sums of capital.

These points must also be considered however:

- There are no established dairy POs in the UK, so the risks entailed in a new start-up must be borne. Although POs should prove to be a low risk route to market, they may be perceived as high risk in the start-up phase, which will deter farmers from joining at the outset and could moderate initial levels of success.
- The fact that there are no POs means there are no proven successful commercial strategies from which to learn. However, this also means that there could be 'low hanging fruit' awaiting the first POs that get into position. A PO (or POs in collaboration) will have to prove they can avoid becoming weak sellers of raw milk.
- The ownership and priorities of supply chain businesses may change, and some will prove not to be resilient and long term commercial partners.
- Producers will not have access to the profit generated in processing and marketing that is distributed to shareholders of PLC processors.
- Success will require excellence in governance, with directors of the PO understanding their role with respect to the maintenance of the contract, adhering to its terms and developing useful and meaningful working relationships with their customers. These will need to be established.

First Milk On Recruitment Drive

"It's time to get out of the stands and on to the pitch. The more producers come with us, the greater the opportunity to develop a broad range of markets and customers and the greater the influence on returns". That was the message from Kate Allum, Chief Executive of First Milk to hundreds of dairy farmers who attended First Milk road shows as the co-op embarked on a determined recruitment drive.



Pig co-ops respond to rising feed costs and Vion announcement

With high cereal costs and rocketing protein prices, many pig producers are failing to cover production costs. Andrew Peddie, Scotlean Pigs director and SAOS chairman, explained how serious the situation is when he hosted a visit to his farm by Scottish Secretary Michael Moore MP on 31 August. Working hard to help improve members' position, Scotlean Pigs state that "major processors are aware that they cannot continue to buy pig meat below the cost of production" and they reported an increase in processor prices in late August, following price increases across Europe.

The announcement that Vion had entered a 90 day consultation with its employees at Broxburn regarding the future of the site was most unwelcome news earlier in the summer.

North east based Scottish Pig Producers is the largest supplier of pigs to Broxburn and quickly communicated a "business as usual" message to its members and others while its directors and management identified and evaluated a range of possible outcomes and solutions to ensure that north east pig farmers will continue to have viable outlets for their pigs whatever the future of Broxburn.

Gordon McKen, (pictured above, left) SPP's Managing Director, says "It's obviously a sensitive time, but our confidence in maintaining high quality viable markets for our members' production is not in any doubt. In fact we are more determined and clear than ever in pursuing our strategies for maximising value through service, high quality, high health pigs, and building strong provenance credentials. We are optimistic about the future of Scottish pork in the growing global market and the opportunities for SPP members".



Jim McLaren, (pictured above, right) Chairman of Quality Meat Scotland commented: "Our pig sector has repeatedly shown its resilience and ability to adapt to a range of challenges in recent years and this flexibility is a great strength. Our producers are highly efficient and now very much focused on long-term sustainability. Indeed, during the past 12 months farmers have invested £millions in improvements on Scottish pig units."

Meanwhile, Quality Meat Scotland and SAOS are commencing work to review and update the Pig Industry Strategy, which was formulated in 2008. This will take into account changes at farm level, in the processing sector, and in consumer markets. It will make strategy recommendations to the industry and Government.

SSMG doubles processing capacity

The Scottish Shellfish Marketing Group – the UK's premier producer of farmed mussels and oysters – officially opened its new processing facility at Bellshill in late August. More than 60 guests enjoyed a special seafood buffet showcasing the very best of Scottish shellfish, and heard of the co-op's exciting development plans for the future at the opening event.

The new facility is double the size of the previous processing site and will enable the company to innovate and develop its product portfolio to meet growing consumer demand for premium Scottish shellfish and was opened by SSMG's two longest serving employees, Beth Fraser Khan and Isobel Smith (pictured centre left and right).

Chairman Michael Laurensen (pictured far right) said the new processing facility has placed the co-op in an excellent position for future growth: "In particular, it will give us the opportunity to expand our shellfish range to meet the requirements of a dynamic consumer market. We will achieve this through product innovation and by diversifying our operation to include other shellfish species."

Managing director Stephen Cameron (pictured far left) praised the dedication of the co-op's workforce, which had played a key role in the success of recent years: "Our employees have been fantastic and their hard work and enthusiasm has enabled the smooth transfer of operations to our new processing site," he said. "We believe the Scottish shellfish industry has a great future because of growing consumer demand and widespread recognition of the range and quality of seafood found around our coasts."

Environment Minister Stewart Stevenson said: "The clear, clean waters around Scotland produce some of the most delicious and highly sought after shellfish anywhere in the world. I welcome the opening of the Scottish Shellfish Marketing Group's new processing facility in Motherwell, backed by £132,500 support from the Scottish Government."

CO-OP FACTFILE - SSMG

A group of mussel and oyster farmers in the Highlands & Islands and Shetland formed the Scottish Shellfish Marketing Group in 1992 to develop UK sales and introduce added value products. Turnover has grown consistently to £11 million in 2010/11, and their product range is available in leading supermarkets.

SSMG sources its mussels and oysters from member farms on the west coast of Scotland and Shetland, which have been independently certified by the Marine Stewardship Council and Friend of the Sea for their sustainable and environmentally responsible manner of cultivation.

They are then transported to the plant at Bellshill, where they are cleaned, graded and some are cooked in sauce. The co-op delivers to UK customers as well as developing export opportunities. SSMG products are of the highest standards - provenance and quality are guaranteed and feature in all marketing messages.

The success of the co-op has enabled farmer members to increase their scale of production through collective and professional marketing and product development. The result is additional income generation in fragile areas of Scotland, overcoming the disadvantages of remoteness from market and securing livelihoods for present and future family producers.

What does co-operation mean to SSMG? "Co-operation is very important within the rural communities and fundamental to the local culture where our members choose to live and work. Whilst many businesses are focused purely on profit, our members exist to provide long-term, sustainable employment within a friendly, local environment. Moral values, integrity and building communities are important to us."

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Director remuneration survey

Attracting and retaining good people onto the board is vital for a co-op's success. Directors carry legal responsibilities and should be compensated for their time and costs incurred. There are concerns that the remuneration levels for farmer directors in co-ops is too low, however, this needs balanced with ability to pay. For example, many smaller co-ops do not pay any remuneration at all.

Non-executive directors have a crucial role to play in ensuring the co-ops they represent are successful. For farmer directors in particular, the increased time needed by the Coop is often matched by increased pressure to manage their core farming business and so it is now more important than ever to ensure they are rewarded properly for their efforts.

The 'Combined Code on Corporate Governance' states, "levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose."

SAOS in partnership with EFPF has just completed the third Director Remuneration Survey of nearly 170 co-ops in England and Scotland. The survey highlights include:

- The average board size is 8 comprising on average 1 Executive Director, 7 Non Executive Directors (NED) with 1 if those NEDs being a non-farmer
- Larger and more complicated co-ops tend to have larger boards
- The average fees paid to Chairman are approximately £20,444
- The average fees paid to Vice Chairman are approximately £7,460
- The average fees paid to Farmer Directors are approximately £6,448
- In the sample, 25% of co-ops paid nothing to any of their directors
- On average Chairman spend 30 hours per month on their duties
- On average Non-executive directors spend 10 hrs/month on their duties
- Over 76% of co-ops have at least six board meetings per annum.

Fees paid to Director by co-op throughput

Co-op Throughput	£ per Annum		
	Average	Highest	Lowest
£5m - £50m			
Chairman	£11,433	£30,000	£500
Vice-chairman	£3,123	£8,500	£600
Farmer Director	£1,828	£5,665	£200
Independent Director	£2,640	£7,000	£200
£1M - £5M			
Chairman	£5,140	£8,200	£500
Vice-chairman	£2,966	£4,500	£2,000
Farmer Director	£1,300	£2,000	£800
Independent Director	£5,000	£5,000	£5,000
< £1M			
Chairman	£2,254	£6,000	£500
Vice-chairman	£965	£1,260	£300
Farmer Director	£567	£900	£200
Independent Director	£600	£900	£800

All those co-ops who contributed to the survey will each receive a full copy of the report. As always, if you need further advice with regard to director remuneration please contact us.

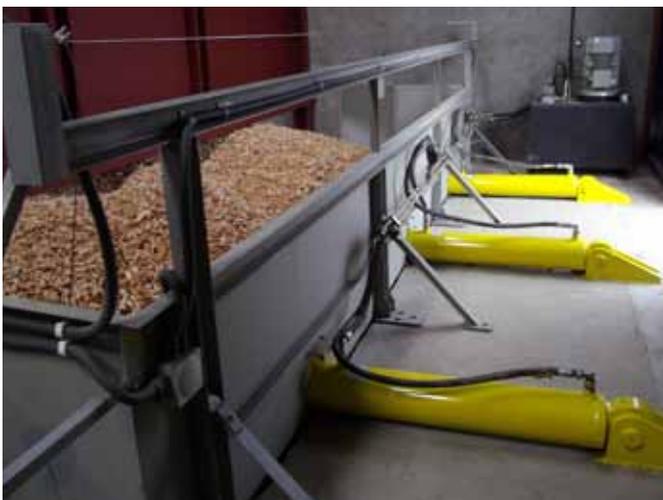
Biomass - the way forward for drying crops?

There is growing interest within the farming community in biomass as an alternative fuel source for drying combinable crops. Traditionally, farmers use gas oil (red diesel) or propane to dry their crops at harvest, however, due to the rising cost of fossil fuels and concerns over future supplies many are now actively looking for alternatives.

Aberdeenshire Council and the Forestry Commission recently commissioned a study to assess the potential for biomass grain drying, including the potential demand and supply, in the north-east. Although seen mainly as a livestock region, the north-east actually accounts for over 30% of Scotland's cropping area and grows 39% of our spring barley. The region's annual fuel bill for combinable crop drying is estimated to be > £5.5 million. With the introduction of the 'Renewable Heat Incentive' (RHI) in November 2011, eligible schemes can now receive a financial subsidy which makes the commercial case for switching to biomass for drying grain even more attractive.

The potential uptake of biomass crop drying largely depends on its commercial viability. The issue is complex and will vary with each situation. Factors include: the current system, the capital cost to change, the scale of operations, operating costs and any practical considerations. Any investment in renewable heat will invariably mean higher capital costs, however, the benefit is usually lower operating costs – lower fuel costs per tonne.

If the use of biomass for crop drying is to be encouraged, it is important there are sufficient supplies of locally sourced biomass to support any future development. The study has shown that farm woodland in the region, which is largely unmanaged, has the potential to supply 43,600m³ per year, providing enough energy to dry over 670,000t of cereals. In addition, farmers also have access to surplus straw which can be used as a biomass fuel source. In particular, there are significant supplies of OSR straw (32,664t) which has little value and the potential to dry 1 million tonnes of cereals – all of the region's production.



The key conclusion from the report is that biomass crop drying can be commercially viable and has real benefits for both individual growers and the north-east region as a whole. Although biomass crop drying is at an early stage, drying costs are greatly reduced making the case to switch. The eligibility of biomass crop drying for RHI will only strengthen the case.

Biomass driers also provide an opportunity to future proof a farm business against the shock of rising energy costs in the future. Those arable farmers with existing farm woodland or easy access to biomass are likely to show the most interest in biomass crop drying.

Jim Booth comments "Biomass crop drying represents a great opportunity for any grower looking to cut their drying costs. There could also be a role for co-ops with arable farmer members with respect to information, demonstration visits, biomass supply, development support and independent advice."

For further details or a copy of the report please contact jim.booth@saos.coop

Savouring success in Dumfries & Galloway



Back for its third year, Dumfries & Galloway's region-wide celebration of delicious local food and drink, Flavour Fortnight, ran from 25th August to 9th September. On the menu was a diverse range of events and opportunities for people to engage with the people behind Dumfries & Galloway's food and drink industry. Existing events like farmers' markets incorporated additional activities such as demos, family entertainment and extra tasting sessions into their markets during the fortnight, hospitality businesses held one-off dining events or created special menus and producers came up with a whole host of ways in which people were invited to 'do something delicious', from wild food forages to fine chocolate making.

Flavour Fortnight is just one of the many ways that Savour the Flavours, Dumfries & Galloway's organisation for local food and drink, has very successfully been promoting 'delicious

Dumfries & Galloway' over the summer. This year they sponsored the Scotland Food & Drink Cookery Theatre at the Royal Highland Show where the region's food, producers, chefs and food events were all on show in the Food Hall, and where the programme for Flavour Fortnight was launched.

Liz Ramsay, Project Manager and main point of contact for Savour the Flavours, says: "The Royal Highland Show was a perfect platform for us to showcase Dumfries & Galloway's exceptional food and drink and visitors to the Royal Highland Show were in absolutely no doubt that Dumfries & Galloway provides a delicious and naturally inspiring holiday experience."

In the Cookery Theatre, several notable chefs working in the area demonstrated some of their favourite dishes made with local produce. And a Dumfries & Galloway stand in the Food hall invited visitors to buy speciality produce direct from the producer, to hear the stories behind the products and to discover exactly what makes artisan food and drink so special. The stand, organised by the South of Scotland Business Competitive Project, included A Taste of Galloway, Clash Farm, Sulwath Brewers, Cream o' Galloway, Galloway Lodge Preserves, Galloway Fudge and Ruthy's Scones, and also included a collaborative area hosted by the region's farmers' and community markets, full of delicious produce from some of our region's micro food and drink businesses.

Liz continues: "Local food and drink continues

to soar in popularity across the UK and Dumfries & Galloway is seeing a surge in the numbers of people turning their love of quality food and drink into small businesses. Discovering and sampling the fare of these micro businesses is a real joy in a region like Dumfries & Galloway and visitors to the area now see sampling our local produce as an essential part of their holiday experience. Our farmers' markets in particular make a wide range of local produce easily accessible to large number of people. While many of our 'experience' events during Flavour Fortnight sold out well in advance, the markets can be relied upon to provide people with a highly enjoyable day out and an opportunity to try and buy a tremendous variety of locally produced food and drink."

Douglas Watson of SAOS tells us "Savour the Flavours is a leading example in Scotland of how a regional organisation can bring together the various food and drink interests under one banner where everybody benefits. The content of this year's Flavour Fortnight clearly shows the level of activity and collaboration that Savours has stimulated. SAOS is pleased to have worked with the Savours team on a number of developments over the last few years and delighted to see the progress and impact they are having."

www.flavourfortnight.co.uk



MBE for Karen Tait of HI Health*

On our recent visit to catch up with our Orkney co-ops, we heard from Karen Tait about a rather unusual year for her involving a sojourn to Buckingham Palace to collect an MBE for her services to the local farming industry. She was also interviewed for a recent edition of STV's Countrywise programme which was set on Orkney.

Karen explains how she got involved with OLA (the Orkney Livestock Association) and how this led to her award: "A group of Orkney farmers got together in the late 1990s to try to improve the depressed livestock farming market following the BSE crisis. Together with the late Sandy Clarke from SAC, they launched a BVD eradication programme, as the disease was very prevalent in the islands, causing a lot of health problems and losses. When the efforts of founders Alistair Foubister, Michael Cursiter, George Rouse and vet Iain McCulloch came to fruition and enough farmers saw the benefits, it became evident that their idea would become reality, and I was asked to administer the scheme in 2000".

Around the same time, HI Health Ltd was launched in the Highlands and Islands to improve the health of cattle there, so OLA became a sub-group and adopted most of their protocols for disease eradication. The hard work was first recognised in 2007 when HI Health was awarded 'Animal Health Provider of the Year' at the Scottish Farmer Agricultural Supplier Awards at the Highland Show. "That was a real boost to us all," says Karen.

Having had so much success with the BVD eradication scheme, OLA decided to extend its work to investigate another prevalent cattle ailment in Orkney, Johne's disease. In 2009, OLA applied for, and successfully won funding from Orkney Islands Council to pay the laboratory fees to test for Johne's which is very different to BVD. Testing is carried out to identify infected animals before they show the clinical signs of profuse diarrhoea and wastage, and to prevent further spread of the bacteria that causes it. Many breed societies have introduced compulsory herd testing for Johne's disease if pedigree animals are to be sold at society sales.

Karen is convinced that OLA's ground-breaking work has had a knock-on effect across the whole country. "Both the Orkney BVD and Johne's eradication schemes have led the way and have inspired others to follow suit. OLA met with the Chief Veterinary Officer for Scotland on several occasions to discuss the BVD eradication scheme in Orkney. Our experiences no doubt inspired the Scottish Government to make BVD eradication within Scotland compulsory. From December 1st, 2011 all farmers with breeding cattle must screen for BVD and eradicate the disease. The sale of infected animals will be an offence from December 1st, 2012.

Karen says of the Buckingham Palace investiture ceremony, "There is never going to be a day like that again and when I look back it now, I just feel like I was in the middle of a fairy tale. It was just fantastic"

(*Hi Health Ltd and Biobest Herdcare have merged to create Hi Health Herdcare.)



PROFILE - RONA SUTHERLAND

In this issue, we are quizzing SAOS' Supply Chain Development Manager, Rona Sutherland. Rona joined SAOS in 2007 after spending ten years working with Scottish Enterprise.



Tell us a bit about your role.

I work on the supply chain development side and have the opportunity to work with everyone from farmers to multiple retailers to encourage greater collaboration. Through our Cultivating Collaboration (C2) programme, we've assisted over 300 businesses in looking at how they can collaborate to access new markets, develop new products and make their supply chains operate more efficiently and effectively. I've worked on a huge variety of projects within that, ranging from events linking farmers to processors, enabling each to understand more about each other's role in the supply chain; to programmes designed to help groups of companies learn techniques for developing new products and services as quickly and cheaply as possible; to projects demonstrating the value to be had from sharing business resources.

What is the most enjoyable part of your job?

The variety of work and being part of a small, close-knit team. I get to meet people from all parts of the industry, find out more about what they do, what they hope to achieve and work with them to help find ways of achieving their goals. I used to work for Scottish Enterprise and knew some of the SAOS team from the outside. I always thought it would be a great place to work - and it is.

What's next for the C2 project?

We've had great support from Scottish Government over the last four years with our C2 project and we've made significant progress. The surveys we did showed that there has been a real change in attitudes and willingness to collaborate over the last few years. However, we feel there is still a long way to go if we want to truly embed collaboration as part of our culture of doing business and so, as C2 winds up, the big challenge now is how to keep that work going.

We're working closely with Scotland Food & Drink and the Government to find ways to take forward some key pieces of work that will help to maximise existing resources within the industry and really build supply chain capacity and effectiveness. Watch this space!

If you could change one thing about Scotland's food and drink industry, what would it be?

I'd like to see it become the norm for businesses to think about collaboration as one of the ways to help them grow. It's not always appropriate, but in so many cases if a business can concentrate on its own core skills and work strategically with a partner to provide the knowledge and expertise it doesn't have, it helps to minimise risks and costs, maximise investment return and speed up the whole process.

What would you be doing if you didn't work for SAOS?

I used to renovate houses as a hobby and still do a lot of DIY, but it works best if it's combined with something that keeps your brain active and involves you working with other people, otherwise it can be a bit lonely. We let out part of our house as a holiday cottage and have other holiday cottages in the family, so possibly something in the tourism line.

How do you like to spend your free time?

Outdoors. I spend a lot of time sitting indoors and so any free time I have, I like to be outside - pottering in the garden, walking with the dogs, out on the hills, or doing anything more active than sitting.

What's your ideal holiday?

We've spent quite a bit of time in Africa and love the African bush, walking with guides while trying not to get eaten or trampled. We also love going to remote cottages, where we can spend time hill walking. Last year we started camping, or, more accurately, 'glamping', as I have been told that carpets, wardrobes, goose down mattress toppers, etc. are not part of standard camping equipment. It's a great way to have a short break with the dogs in tow.

We're recruiting - could you be our new Project Manager?

SAOS is currently seeking a new Project Manager to join the team. The full job ad can be viewed on [S1jobs.com](https://www.s1jobs.com). If you, or someone you know fits the bill, please send an application by e-mail to jennifer.grant@saos.coop by 1st October 2012.