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WILL **CHINA**'S THIRST FOR INFANT **MILK** POWDER REVIVE AUSTRALIA'S STRUGGLING **DAIRY** INDUSTRY?

Chinese are buying up infant **milk** powder everywhere they can get it, outside of **China**. And that has led to shortages in at least a half-dozen countries ...

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The New York Times, July 25, 2013

A man was arrested at the Lok Ma Chau border [between **Hong Kong** and **China**] on Monday and accused of attempting to smuggle \$HK24,940 worth of **milk** powder into the **Chinese** mainland ...

South **China** Morning Post, February 26, 2013

Randy Cowan recalls the day his town got its first taste of the **Chinese** mania for Australian infant **milk** powder. It was late 2011 and Cowan was working as a caretaker of the abandoned **dairy** that had once been the main employer in Toora, a community of roughly 600 people on the windswept coastal plains of southeast Victoria. As a younger man Cowan had worked at the factory in the 1970s, bagging **milk** powder, just as his father had worked there in the 1950s when its towering white tin-and-timber buildings and brick smokestack were first built. The plant's closure in 2002 gutted Toora, and ever since it has loomed over the town like a ghostly reminder of the **dairy** industry's heyday. Then Dajian Li turned up from Melbourne with a grand plan.

The 45-year-old **Chinese**-Australian took a tour of the **dairy**'s 0.8ha **site**, with its cracked windows and rattling corrugated-**iron** storage sheds, and asked Cowan how much it might cost to get it back up and running. "I said, 'If you've got a spare \$100 **million** it'd be easy,'" recalls Cowan, a grizzled 64-year-old with an asthmatic chuckle. "His response was: 'No problem'."

By October 2012, Li had bought the **dairy** and was having his photo taken with Victoria's deputy premier Peter Ryan and local shire officials. Busloads of would-be **Chinese** investors began turning up to tour the **site** as Li talked about spending \$76 **million** to bring back Toora's glory days, when truckloads of **cheese**, yoghurt and bottled **milk** left the town each day. This time, though, there'd be no **coal**-fired drying plant belching smoke and dust; this would be an environmentally friendly, 21st-century production line churning out tonnes of infant formula, the white powder that's become so popular in **China** it's now akin to contraband.

"He said there was good demand in **China**," recalls Cowan, who went on to help Li's **company** find tradesmen to refit the factory. One local councillor almost wept while talking about the **dairy**'s reopening, for even here in Gippsland - the richest **dairy** region in Australia - the previous decade has been a hard grind for farmers. Suddenly, **China** is being touted as their saviour and **milk** is being touted as "white **gold**" in the **business** pages. Sixty kilometres up the road from Toora, the Burra Foods factory has spent \$70 **million** installing a new **milk** powder processing operation, which last week produced its first consignment of infant formula for **Chinese** babies. In nearby Poowong, United **Dairy** Power has been

bought by **Hong Kong** businessman William Hui for \$70 **million**. In Tasmania, a new \$75 **million** plant on the **site** of an abandoned timber mill is processing 150 **million** litres of **milk** a year into powder for export. In NSW, the **dairy** industry is talking up plans for \$200 **million** of **Chinese** investment.

Everyone is chasing the same dream: cashing in on the rocketing demand for **milk** and infant powder among the middle-class of Asia, particularly **China**, where 16 **million** babies are born annually and parents are paying up to \$70 for a tin of "clean and green" imported baby formula that costs \$20 in Australia.

It's a stampede that could hit some potholes, if Toora's experience is a guide. For while Dajian Li's new **company**, Viplus **Dairy**, has started shipping pallet-loads of formula to **China** from the town, the operation has some curious aspects. The website paints a seductive picture of Toora's entire population happily toiling in the **dairy** while fat Gippsland cows laze around waiting to be milked, but on a recent March afternoon there were just a handful of workers inside the largely abandoned factory and not a cow in sight. Instead, **milk** powder from New Zealand was being mixed with nutrients to make baby formula packaged in tins with an "Australian made" certification. Dajian Li had suddenly become unavailable for interviews and it was difficult to determine who was running the **company**. "Mr Li is behind the scenes in many ways," explained the administration manager, Marion Hannon, in her office in the draughty and half-finished administration building. Viplus is "wholly and solely" an Australian **company**, she emphasised as she offered a guided tour of the factory, although who finances the operation is unclear. "I can't really comment on that," she said. "But there's a lot of money being spent on the project."

Down the road, **dairy** farmer Ray Argento is one of many locals watching the rebirth of the Toora **dairy** with a mixture of hope and bemusement. Like most of his peers, the 46-year-old has struggled to make a living as the price he was paid for **milk** waxed and waned over the past decade. He's heard the stories about how Asian demand could spark a renaissance in Australian farming to rival the **mining** boom; he's watched the share price of Australian **dairy** companies rising; he's spoken to local farmers who are buying up neighbouring properties in anticipation of the good days to come. Still, he doesn't sound convinced. "You look over the fence and you wonder: Do they know something I don't?"

The spark that lit **China**'s wildfire demand for Western **milk** powder came in July 2008, when 59 babies in northwestern Gansu province were diagnosed with kidney stones. The babies had fallen ill, it turned out, after drinking locally made infant formula made from **milk** adulterated with melamine, a toxic chemical which artificially boosted the **milk**'s protein count. By year's end **Chinese** authorities were admitting that at least 22 **dairy** companies had perpetrated the heinous deception. One of the biggest food-tainting scandals in **Chinese** history, it caused six children to die and nearly 300,000 to fall ill.

Those poisonings and a series of subsequent food-tainting scandals led to skyrocketing sales of imported baby formula as alarmed **Chinese** parents abandoned local **dairy** products. Infant formula has been the preferred food for infants in **China** for several decades, with fewer than 16 per cent of urban mothers breastfeeding. Dr Mu Li, associate professor in international public health at Sydney University, attributes that to rapid urbanisation and a cultural resistance to breastfeeding in public. "Family income has increased significantly, which has made formula more affordable, and many women have moved from rural areas to major cities seeking work, leaving their infants behind to be cared for by grandparents," she says. "Using imported brands also symbolises 'privilege', due to the high prices, or the fact that someone brought them from overseas." Corruption has also played a role: health workers in scores of **Chinese** hospitals have accepted bribes from baby-powder manufacturers to encourage mothers to use formula, investigators revealed last year.

By 2012, demand for imported infant formula was running so hot that **Chinese** tourists travelling in the West were stripping supermarket shelves bare, buying tins by the dozen to pack into their luggage and distribute as prized gifts or sell at outrageous mark-ups. Shortages in Australia became so acute that the Safeway supermarket chain last year imposed a four-can limit on its customers, similar to restrictions imposed in New Zealand, Europe and the US. In March 2013, the **Hong Kong** government announced that outbound travellers would be limited to carrying 1.8kg of formula, a law that has kept border guards busy - in the first month alone they busted 879 people and seized nearly 9000kg of contraband infant powder. Last December a persistent smuggler was jailed for the first time; the 37-year-old woman had been caught with four tins of baby formula, her fourth offence following a suspended jail sentence handed down only a month earlier.

Behind these nutty tales of international baby-powder smuggling looms a question that could not be more serious for Australian **dairy** farmers: could this all herald a revival in their fortunes? The past decade has been a chastening one for the Australian **dairy** industry, which saw its global market share decline dramatically and thousands of **dairy** farmers move off the land. The shift began as overseas **dairy** companies merged into large conglomerates - Fonterra in New Zealand, Arla in Europe, **Dairy Farmers of America** in the US - with enormous economies of scale. The Australian **dairy** industry found itself facing tough international competition at a time of persistent drought and a high Australian dollar, along with

depressed **milk** prices caused by the global financial crisis and the bargaining power of Coles and Woolworths, which control a massive share of domestic **milk** sales.

The result was that the Australian **dairy** industry shrank at a time when global demand for **milk** was rising. From 2000 to 2013, according to **Dairy Australia**, herd numbers dropped from 2.2 **million** to 1.6 **million** cows, **milk** production fell from 10.8 to 9.2 **million** tonnes and the number of **dairy** farms more than halved to 6398. Other countries stepped in to fill Asian demand, notably New Zealand, which signed a free trade agreement with **China** in 2008 and now accounts for nearly one-third of international **dairy** sales, producing 19 **million** tonnes of **milk** last year. New Zealand's **dairy** exports to **China** have leapt from \$520 **million** in the year of the melamine scare to \$4.57 **billion** today; by contrast, Australia's went from \$337 **million** to \$523 **million**. Last year, at a time when the global price for **milk** powder jumped 65 per cent, Australian production fell because of a drought-induced fall in **milk** supplies. "We have a very robust and efficient competitor across the ditch, and they're leading the world," comments Grant Crothers, CEO of the Victorian **dairy company** Burra Foods. "We are never going to be as **dairy**-centric as New Zealand, but they are showing us what can be done."

Crothers has done better than most in the past decade; he and his brother William launched Burra Foods in 1991 with five employees in a converted **butter** factory in Korumburra, 118km southeast of Melbourne. In 2009 Japan's Itochu Corporation bought a 45 per cent share of the **business**, helping to finance a \$50 **million milk** powder factory and a \$20 **million** infant formula facility, which went into production this month. Burra Foods now has 140 employees and hopes to export 15,000 tonnes of infant formula to **China** annually, but asked whether getting enough **milk** supplies might be a challenge, Crothers replies simply: "Yes."

Theoretically this is all good for farmers, given that they are supplying a relatively scarce commodity to an increasingly competitive industry. Burra isn't the only **company** investing heavily in **milk**. Last March, Tasmanian **Dairy Products** officially opened its \$75 **million milk** powder facility in northwest Tasmania, a joint venture with Mitsubishi. Tasmania's biggest **dairy** farm operation, the Van Diemen's Land **Company**, is seeking \$180 **million** from investors to expand, and even smaller infant formula **operations** such as Bellamy's Organic in Launceston now has an office in Shanghai and sales approaching \$50 **million**. In January the Canadian **company** Saputo paid \$530 **million** for a controlling **stake** in the 120-year-old Victorian **dairy firm** Warrnambool **Cheese & Butter**.

The selling point for all these companies is Australia's international reputation as a place that's free of pollution and stringently regulated. Since 2008 several new businesses have appeared in Australia, selling baby formula to Asia via websites that lean heavily on our "clean and green" image, replete with photos of rolling verdant paddocks and coastal backdrops. These aren't **dairy** companies, strictly speaking; they are more like canning facilities that turn powdered **milk** into formula. **Milk** powder is expensive to make - drying plants cost \$50 **million** and upwards, which is why there are only a handful in Australia - but making infant formula is a straightforward task of mixing nutrients and **milk** powder, albeit in sterile conditions to local and international health regulations.

Dajian Li's **company** Viplus launched its website, milkformula.com.au, last year. "Blue sky and clean water is the most attractive feature in Toora," reads the spiel. "Cows lying on the ground, enjoying the sun, eating natural grass with relax [sic] lifestyle. Toora produced the best quality cow **milk** in the world. Only 600 local residents live in this small town who are all working for the factory." The website goes on to promise that "only the best local quality ingredients will be used into [sic] our infant formula".

The reality, as the **company** freely admits, is that only a handful of Toora's residents work at Viplus and no local farmers sell their **milk** to the **dairy**, for the simple reason that **milk** isn't processed there yet. The **company's** sales manager, Jenny Fang, says the website is referring to future plans, when **milk**-drying and powder production begins. As for the claim about the 600 townsfolk, it was meant to convey that the **dairy** "directly or indirectly" supports the whole town. Fang acknowledges that Viplus has primarily been using New Zealand **milk** powder in its formula, but says the **company** complies with its 'Australian Made' logo because 50 per cent of manufacturing costs are Australian.

Viplus is now shifting to Australian **milk** powder, according to Fang, but the website isn't the only aspect of Viplus's **operations** that has raised eyebrows in Gippsland. Randy Cowan fell out with the **company** early on, after Dajian Li enlisted him in mid-2012 to find contractors to clean up the old **dairy site** and begin the fit-out. Things got off to a strange start, Cowan recalls, when Li said his **company** didn't yet have an Australian **Business** Number and needed to pay employees and contractors through Cowan's bank account. By December 2012, Cowan and many other employees were owed thousands of dollars, and after leaving Viplus that month he won a case against the **company** in the Victorian Civil and Administrative Tribunal for \$7740 in unpaid wages. In October, another **group** of employees and contractors accused the **company** of failing to pay them.

Cowan still hasn't been paid, but Fang says the **company** is in the process of resolving all those disputes, which were a result of language difficulties and early management problems. Viplus now has new **Chinese** and Australian investors, she says, and Li is no longer the owner of the **business**. "Overseas investors coming to a small town in Australia, working in a different language and different culture, you can imagine there were difficulties," she says. The cultural differences do seem acute: a photographer from this magazine was shooting pictures of the factory when a Viplus employee demanded he leave or he would be "thrown to the pigs".

Some established **dairy** industry figures privately worry about the effect of inexperienced operators cashing in on the white-powder boom. "There are a number of **Chinese** companies setting up here," says one, "and I don't know how to say this politely, but how do we ensure they comply with our regulations and standards?"

Just how important quality control can be was shown last year when New Zealand giant Fonterra mistakenly announced botulism-causing bacteria had been found in **milk** powder ingredients it supplied to companies in seven countries. A massive recall of several brands of infant formula was ordered, until Fonterra discovered that the bacteria was in fact a different and harmless strain. The incident rocked New Zealand's **dairy** industry - **China** suspended imports and Fonterra's **milk** division head, Gary Romano, resigned. One customer, the French **company** Danone, says it is planning to sue the **company** for 350 **million** euros in lost sales.

But Grant Crothers of Burra Foods plays down the dangers of new operators in Australia sully our green image in the rush to supply **China**. "I don't agree that we are seeing infant formula companies pop up everywhere," he says. "We've got four sites where formula or nutritional powder are made, Burra being the latest. Then you've got 10 to 15 canners, who are a bit more entrepreneurial, but they are subject to rigorous food safety and audit regimes."

If anything, the "white **gold**" fever is likely to ratchet up in coming years, given that financial analysts are predicting **China's** annual baby formula consumption could reach \$25 **billion** by 2016, double what it was in 2012. Last December, the National People's Congress announced a loosening of **China's** one-child policy, which will allow couples to have a second child if either parent has no siblings - a change that could result in 1-2 **million** additional births per year.

The Australian **dairy** industry, meanwhile, is hanging on a promise that Tony Abbott made before he became prime minister - a free trade agreement with **China** in his first term. Such a deal would put Australian **dairy** operators on an equal footing with New Zealand, although the prospect of international investors swooping on Australia to "**buy** the farm" is one that sends a shiver through many a rural community. State-owned **Chinese** businesses currently cannot invest in Australia without approval from the Foreign Investment Review **Board** and private **Chinese** companies require approval before acquiring a substantial or controlling interest in a **business** worth more than \$248 **million**. In theory, any loosening of those rules under a free trade agreement would allow the **Chinese** to **acquire** large chunks of Australia's **dairy** industry.

Last year the state-owned **China** Investment Corporation was reported to be considering a buyout of the Van Diemen's Land **Company** in Tasmania, which did not eventuate. More recently, **Chinese** investors toured several **dairy** regions in NSW to assess plans for \$200 **million** in **milk**-powder facilities in the state. But David Williams, a Melbourne investment banker who has advised **dairy** companies during recent takeovers, says fears of a **Chinese** takeover are a furphy. "The **Chinese** have been making noises about companies they are going to **buy**, but they're too late to the party, and they're typically not well advised," says Williams. "Mostly what they are doing is buying broken-down dairies no one else wants."

China will have a significant influence on the **dairy** industry, says Williams, but indirectly through its demand for powder, along with the rest of modernising Asia. He points to Tasmania, where new **milk**-processing projects have fuelled a resurgence in **dairy** farming and where the government is aiming to lift **milk** production by 40 per cent. "If you wanted to **buy** a farm, the thing to do right now would be to **buy** a **dairy** farm in Tasmania," he says.

This month, the farm-gate price for **milk** leapt to 50 cents a litre, a rise of nearly 50 per cent on last year. The dollar has dropped and, according to one survey, 52 per cent of **dairy** farmers feel optimistic about the future - the equivalent of an outbreak of wild jubilation in any other industry. In Toora, the old **dairy** still looks dilapidated, with its empty car **park** and abandoned guard-house, but Viplus is sticking to its talk of revitalising the plant, and the town.

"We've come through a difficult period as a new **company** trying to resurrect an old beast," insists Marion Hannon. "Mr Li and his associates are the only ones who've put their hands up to do anything down here

for 10 years." The **milk**-drying plant should be built by the end of the year, says Jenny Fang, and the **company** is already talking to farmers to secure supplies.

On his farm a little way down the road, Ray Argento says ruefully that he's not sure if he'd sell his **milk** to Viplus, should the **dairy** start processing **milk**. All those stories about people not being paid have made the locals wary, and Argento is a hardened sceptic after 30 years in **dairy** farming. He got his start as a teenager on the farm his Italian-immigrant father owned in Gippsland, but the 20 years he's lived on his own 110ha in Toora have been hard. Right now he's getting 43 cents a litre for his **milk**, a nice step up from the 30 cents he was getting at the bottom of the financial crisis, but not much of a living for a 46-year-old with three kids.

"All of a sudden **dairy** is flavour of the month," he says. "But for us at ground level, well, I like to say I'm not sure whether my **milk** glass is half-full or half-empty. People in the industry paint an optimistic picture of us becoming the food-bowl of Asia but we're just not seeing it in our returns." Back in 2010 a sustained revival was predicted, he recalls, only for drought to send supplies tumbling.

Argento's 16-year-old son recently started a boilermaker's apprenticeship. "He wanted to come home and work on the farm but at this point it's just not financially viable for him," says Argento. "I look at the hardships we've gone through and I don't want that for my son. He might earn enough to own a farm through his trade one day, but in the current circumstances it's hard to see how he could save any money farming."

Still, he says, if the Asian boom continues, maybe his son will come back to the land. In the meantime, Argento has one eye on the old **dairy** up the road. "I really hope that they can double or triple production and in 10 years' time there'll be a hundred people working there." He smiles wryly. "Once again, we live in hope."

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