Dear Richard,

SCOTTISH DAIRY INDUSTRY AND MILK PRICES

Committee scrutiny

Following the on-going problems facing the dairy industry in Scotland, which were highlighted recently when the producer cooperative First Milk delayed payments to its members, the Rural Affairs, Climate Change and Environment Committee held an urgent inquiry\(^1\) into the dairy industry in Scotland. The Committee’s aim was to establish a clearer picture of the challenges facing the industry from farmers through to processors and retailers, and to identify potential solutions which may improve both the current situation and prospects for the future.

Our work examined the global context to the recent problems faced by some Scottish dairy farmers; the issues at First Milk specifically; the more general situation regarding pricing, from farm, to processor to retailer; the Scottish, UK and EU policy and regulation frameworks; and what opportunities there are in the future to address the current problems and grow the dairy industry in Scotland.

The Committee received written submissions and information from a wide variety of those involved in the sector, and took oral evidence from producers, processors,

\(^1\) Scottish Parliament Rural Affairs, Climate Change and Environment Committee. All information on its dairy inquiry, including evidence and correspondence. Available at: http://www.scottish.parliament.uk/parliamentarybusiness/CurrentCommittees/85896.aspx.
industry representatives, retailers, the UK Groceries Code Adjudicator, and from you and your officials and we thank all of those who engaged with us on this urgent issue at such short notice.

The Committee was deeply disappointed that some of the major supermarkets which buy and sell Scotland’s milk and other dairy products (Tesco, Sainsbury’s, Marks and Spencer and Lidl) were reluctant to come before the Committee which was extremely frustrating for us, but, more importantly, was discourteous and unhelpful to all those working so hard across the country to produce and process Scotland’s milk. After their initial refusal to appear before us, we wrote to the Chief Executives of these four supermarkets, which account for a significant proportion of the market share in Scotland, to request their attendance before the Committee and, as a result, they all agreed to appear. However, I am sure you will agree that it is unfortunate that we had to persuade and cajole these major organisations, with threats of “empty-chairing”, before they cooperated fully with the Committee.

This is not the first time that the Committee has found it difficult to engage with some of the country’s largest retailers and calls on all of those in the retail sector, including the Scottish Retail Consortium, to engage more productively and proactively on issues of this kind.

We welcome the fact that some supermarkets appeared before the Committee at the first time of asking, and also note that those who came as a result of being written to went on to give informative and helpful evidence to us. We therefore hope that this more collaborative attitude sets the tone for a future “team Scotland” approach which can be fostered and harnessed for the good of all those involved from producers through to consumers.

Background and context

It is clear that dairy farming in Scotland is going through a period of sustained change as the number of specialist dairy farms has halved and dairy herds have decreased in number, yet production levels have remained consistent for over twenty years. Trends have moved towards keeping larger herds, with approximately the same amount of milk being produced from fewer animals.

It is also clear to the Committee that the current issues being faced in Scotland are part of global challenges in the dairy sector. The Committee heard that circumstances such as good weather in many parts of the world in 2014, and investment in the industry following high prices in previous years increased supply of milk worldwide; while the Russian import ban and the slowdown in growth in the Chinese market, have decreased demand. As one witness put it, this created a “perfect storm” in the dairy sector, as prices have been driven down by over-production and declining markets and liquid milk has flooded the market. The Committee therefore examined what could and should be done now, in the short-term, to address the current situation, and what measures could and should be put in place to put the Scottish dairy industry on a better footing in the medium to long term, which, the Committee was repeatedly told, has a very positive outlook. It was encouraging to hear you tell us that the EU Commissioner believes the current
situation to be a temporary downturn, though that may be cold comfort to some of our hardest pressed dairy farmers in Scotland.

You told us that the Scottish sector is currently too exposed to the volatility of the commodity market and this echoed what many others told us in evidence. We heard that there has always been, and is likely always to be, volatility in this market. The question therefore is how can we best protect and prepare the industry in Scotland in light of that.

The Committee was struck by several pieces of evidence it received indicating that whilst there were notable short-term difficulties being faced in the dairy sector in Scotland, the medium to long-term outlook was more positive, and also that there was always likely to be volatility in the sector and the key was to prepare and protect the industry in Scotland as much as possible from that volatility. As one stakeholder put it, the dairy sector will always be a rollercoaster, but Scotland can try and step off of the ride.

The Committee agrees that global factors are affecting the milk price and that there is likely to be continuing volatility in the sector, and we hope that the optimism expressed by many regarding the longer-term outlook for the sector is warranted. However, it was clear to the Committee that addressing the short-term pain being faced by many in the industry, particularly producers in remote and island communities, must be a top priority for the Scottish and UK Governments, alongside looking ahead to try and put policies in place to improve the situation in the medium to long term.

Current milk prices

First Milk situation
The situation with First Milk is obviously extremely regrettable and has left many of its members facing dire circumstances and having to make very difficult decisions regarding their livelihoods. The Committee recognises that by being a cooperative owned and managed entirely by its farming members, and by being able to guarantee that milk will be picked up and paid for, that First Milk provides some security to its members. However, that security is in danger of being undermined by the low prices being paid by First Milk, and, most importantly, by its recent inability to pay its members on time. We heard that the financial difficulties being experienced at First Milk are not only affecting producers’ ability to remain in business, but are also preventing it from being able to invest in infrastructure at a sufficient scale to secure and grow the businesses and therefore support the communities that rely on them.

We obtained information during our inquiry which clearly showed that farmers contracted to First Milk are more often than not, and over a sustained period, receiving the lowest price for their milk when compared to other processors or direct purchasers. However, the Committee is aware that for many farmers in places such as Gigha, Bute, Arran and Kintyre, First Milk is the only realistic option they have for selling their product. We were concerned to hear that First Milk members in such places face the same financial obligations as others in more favourable circumstances in terms of issues such as transportation costs. The example provided by those farming on an island such as Gigha, which the Committee has visited in the past, provided a stark reminder of the additional difficulties faced by
some in the dairy sector. On Gigha, we were told in written evidence, a fragile dairy sector not only has to pay for its own ferry costs to get the milk over to the mainland, but also has to pour milk away if there are problems with a particular crossing. Written evidence to us also noted that it would help if First Milk could supply a preservative to enable the milk to be collected the following day if there were collection issues. Dairy farmers in some of the most remote parts of the country are often sustaining local communities and economies and therefore providing a considerable economic and social benefit. These farmers are often not able to compete with others in terms of the opportunity to supply a range of processors and retailers due to the disadvantages of their physical location.

We are aware that the National Farmers Union Scotland (NFUS) recently wrote to the Cabinet Secretary for Infrastructure, Investment and Cities, Keith Brown MSP, to ask him to consider the commercial vehicle ferry fares for milk tankers to the Islands of Bute and Gigha, to place them on an equal footing with livestock and shellfish transporters and receive a discount on the fares.

We heard from you Cabinet Secretary that discussions are ongoing with First Milk as the Scottish Government considers what support it can provide to help stabilise the organisation in the short term, and then help it to grow it in the longer term. When you gave evidence to us, Michael Russell MSP listed eight points which he felt should be taken into account when considering how to tackle the First Milk situation, and having reflected on those, we would summarise the key points as follows—

- investment in infrastructure including the Campbeltown creamery and facilities at Cowdenbeath;
- measures to keep producers in the market;
- a dedicated in-market export resource, particularly in North America, and a marketing push on all products;
- improvement in the quality of management at First Milk;
- exploration of the potential for partnership agreements with local authorities and agencies, and also improvement of links with European cooperatives;
- examination of the pension legacy liabilities from the previous milk marketing board;
- consideration of the size of First Milk and opportunities to work with others (for example, looking at Orkney where a Producers Organisation operates a creamery owned by a public body); and
- initiating research and development for new products in Scotland to stimulate innovation as has been done in places such as Ireland.

As well as being applicable to the situation at First Milk, the Committee is of the view that several of these points are more widely relevant to the dairy industry in Scotland, and are reflected in other parts of this letter.

The Committee is extremely concerned at the situation which has developed at First Milk and was disappointed in some of the engagement it had with the organisation during this inquiry. The Committee is of the view that some of the decisions and management that have led to this situation can be criticised and it is important that lessons are learned to ensure that any support offered is not undermined in the future by poor decision making or management.
The Committee recommends that you consider the eight point strategy set out above and use this as a framework for the Scottish Government’s response to the current situation at First Milk. We ask you to report to the Committee, in your response to this letter, on exactly what action the Government will be taking regarding First Milk. We would also welcome your views on what measures can be put in place to prevent a similar situation occurring in the future, in order to protect the members of organisations such as First Milk from failures in management.

The Committee asks you to liaise with the Cabinet Secretary for Infrastructure, Investment and Cities with regard to the recent letter from the NFUS and recommends that the Scottish Government looks sympathetically at ways of reducing the burden of transportation costs for our remote and island dairy farmers.

Wider producer/processor/retailer relationships in Scotland

We looked beyond the current issues with First Milk to the wider producer/processor/retailer relationships in Scotland. The Committee was told that the cost of producing a litre of milk was in the region of 30p but that there was significant variation in what dairy farmers in Scotland were being paid, with some receiving above the cost of production prices, and some receiving below cost of production prices, with First Milk often paying the lowest price. As explored above, some farmers supplying First Milk often have no other option in selling their product and are not in a position to supply processors such as Graham’s The Family Dairy, Arla, Muller-Wiseman, or supermarkets directly.

Some supermarkets told us that the retail price they charge for milk was de-coupled from the prices they pay to producers and processors, but there was some disagreement between retailers about the extent of influence that supermarket pricing has on the prices being achieved by producers for their product. Some supermarkets are clearly working with a select group of direct suppliers, whereas others are not and are working through large processors such as Arla and Muller-Wiseman, or cooperatives such as First Milk, and this seemed to account for why some supermarkets are more successful than others in protecting farmgate prices for their liquid milk. All seemed to share the view, expressed most directly by Morrisons, who told us that they were not profiteering from milk sales and that its margins on liquid milk were actually decreasing.

We tried to obtain published data on processors and retailers margins on milk but it seems that this is no longer publically available. Several witnesses felt that the prices retailers are buying and selling milk for is not the key issue in examining how to improve the outlook for the sector in the future, as many other external pressures are brought to bear, such as supermarket price wars and consumer expectations. Supermarkets felt that whilst consumers were concerned about the ethics behind supply chains for products, price remained a key issue for them in deciding what products to buy and from where.

Some evidence also suggested that milk price was not a leading factor in whether a dairy farm was profitable or not – rather that was more linked to technical efficiency and innovation in operations which we address in more detail below.
However, it was clear from the statistics that were made available to the Committee, that retailers’ margins have increased significantly over recent years, whereas processors margins have been notably squeezed. It was also clear to us that there is a lack of transparency in the price farmers are paid for milk (and other dairy products) and the margins retailers are receiving. It is fair to say that all nine supermarkets that appeared before us painted a very healthy picture of their involvement in, and with, the dairy sector, in terms of ethics and corporate responsibility, transparency and price negotiation. However, this was not the universal impression we got from other sources, as discussed in greater detail below.

The Committee is strongly of the view that the prices paid by supermarkets for milk is a factor in the overall health and management of the dairy industry in Scotland, as evidenced by the fact that retail price margins have increased over the last 20 years from 5% to 35%, whilst processors margins have slipped from 39% to 16%.

The current lack of transparency of prices paid between processors and supermarkets, and of the price of liquid milk supplying the bulk market and hospitality sector must be addressed if trust is to be improved between producers, retailers and consumers. Customers have a right to know how much the retailers they buy their dairy products from have paid to the producers of those products and we comment further on this on the section on the voluntary UK code below.

The Committee wants everyone involved to work towards a more sustainable, equitable, and profitable dairy sector in Scotland where all producers are paid an appropriate price for the goods they produce, and where consumers can make informed decisions about what to buy, based on clear information about where produce comes from and how much it costs to produce.

*Resilience and efficiency*

As discussed above, for the industry in Scotland to cope with the volatility of the market, and improve and grow, farms need to continue to improve their resilience and efficiency. The fact that Scotland has continued to produce the same amount of liquid milk over the past 20 years with half the livestock would seem to indicate that considerable improvements in efficiency have already been made, but it was stressed to us during our inquiry that there is more that needs to be done in this area.

We heard from many of the supermarkets who gave evidence about the work they do with dairy farmers directly to help them improve efficiency, which included work on reducing carbon emissions, paying for vets to visit dairy farms, and arranging environmental visits. Sainsbury’s also told us that whilst it shares the data from this work it should be rolled out more widely.

As well as improving efficiency, it was suggested to us that consideration should be given to market-driven methods of coping better with volatility and increasing resilience, such as making use of price hedging, and also measures such as tax-smoothing over a longer period.
You told us when you gave evidence that you have asked HMRC to consider some of the tax measures which may help improve the resilience of dairy farms in Scotland. We also asked you about the ring-fencing of milk quota that still exists in some parts of Scotland and whether that should be removed or replaced with something else to support and protect dairy farming in the affected areas of the southern isles (Jura, Gigha, Arran, Bute, Great Cumbrae, Little Cumbrae, the Kintyre peninsula south of Tarbert and part of the Cowal peninsula) and Orkney (apart from the island of Stronsay). You said you would look again at this situation.

The Committee agrees that the dairy sector in Scotland needs to be as sustainably resilient and efficient as possible to enable it to compete and grow (rather than just survive) in a volatile market. We note the many projects and initiatives which the supermarkets we heard from are engaged in with Scottish dairy farmers and encourage retailers to extend that work across the sector.

The Committee recommends that the Scottish Government considers the merits of price hedging, and other such measures, in the Scottish dairy industry, and considers what advice and support may need to be provided to producers, most of whom will be inexperienced in such matters.

The Committee welcomes your comments regarding seeking to work with HMRC on tax issues for dairy farmers and notes the recent comments by the Prime Minister indicating that the UK Government would be looking at this issue. It certainly seems to the Committee that allowing tax-smoothing over a longer period (for example, up to five years) would help producers maintain stronger balance sheets and increase confidence in the sector.

Finally, we welcome your commitment to examine the issue of the ring-fencing of milk quotas still operating in some parts of Scotland and look forward to an update from you on that issue.

UK, Scottish and EU policies and regulations

Another fundamental issue the Committee considered was the current regulation and guidance which frames the operation of the dairy sector in Scotland, to determine if any changes could be beneficial to the industry and to consumers.

The UK’s Voluntary Code of Practice

The UK’s Voluntary Code of Practice on Best Practice on Contractual Relationships in The Dairy Sector, introduced in 2012 and reviewed in 2014 (led by a member of this Committee, Alex Fergusson MSP) has a very important role to play in setting the framework for best practice across the UK, including in Scotland. It was confirmed by the UK Secretary of State that 85% of UK milk production is covered by the code. The recent report by the House of Commons Environment, Food and Rural Affairs (EFRA) Committee, following its inquiry into dairy prices[^2], recommended that the code remain voluntary but that the 2015 review takes full account of the lessons

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learned from the present market conditions, and closer attention be paid to the
damage that sharp and rapid shifts in price do to the industry.

Evidence to the Committee from those dealing with the code and working within it
expressed various frustrations. Graham’s The Family Dairy felt that the code is
biased towards cooperatives over private family businesses and Muller-Wiseman
also felt that cooperatives were given favourable treatment in the code which allowed
them to tie producers to 12 month contracts whilst allowing them to change the
prices paid at very short notice. Both called for equity for all under the code. First
Milk, a cooperative, felt that the difference in terms in the code between cooperatives
and others was appropriate but also expressed some frustrations with the code in
respect of the difficulties it can cause to businesses.

The Committee acknowledges that the UK Voluntary Code of Practice has an
important role to play in setting out best practice for the sector and in
establishing a framework to guide contractual relationships. The Committee
understands that the code was reviewed recently and recommendations made
in terms of maximising its effectiveness. The Committee believes that the code
has played a positive role to date in improving trust between parties in
contractual relationships and that the recommendations made following the
recent review should be considered by the industry. The Committee therefore
recommends that the Scottish Government presses the industry in Scotland,
and encourages the UK Government to do the same in other parts of the UK, to
formally consider and respond to the recommendations which were set out.

EU milk package
The Committee explored the issue of the EU’s milk package, which gives Member
States the possibility to require compulsory contracts between milk processors and
suppliers. Twelve Member States have legislated for compulsory contracts, but, as
you know, the UK is not one of them. The general view the Committee heard was
that compulsory contracts could be counter-productive but the NFUS also told us
that there had not been sufficient impact assessments carried out by Defra to fully
explore the pros and cons of utilising compulsory contracts in the UK and Scottish
industries.

The Committee is not convinced that compulsory contracts would aid the
industry in Scotland, and is currently of the view that having flexibility in
contracts is preferable, as long as the guiding framework is effective. However, the Committee believes that there is a lack of information regarding
such contracts and therefore recommends that the Scottish Government
presses, and works with, the UK Government to examine the potential pros
and cons of compulsory contracts in the UK and Scotland in more detail, and
reports back to the Committee.

Other EU action
Under EU arrangements, Member States must intervene to buy products when they
fall to a certain level. For milk, the intervention price is currently about 17p per litre
(although exchange rate fluctuations may mean it is as low as 15p per litre). The
Committee considered whether the EU intervention price should be increased given
that many think the current level is too low and that many farmers would be out of
business before the intervention price was reached.
The EFRA Committee recommended that the intervention price be reviewed before the ending of milk quota arrangements in April 2015, and then regularly kept under review. In its written submission to the Committee the NFUS also argued increasing the intervention price could be a short-term measure that “must be deployed in order to sustain this important industry”.

However, we also heard evidence that the EU can no longer afford to intervene in the way it has done at times in the past and that other options may be more viable, such as assistance with storage. You told us that the EU had an open mind, although as the European Commissioner does not appear minded to consider this, and the UK Government is also not supportive, it does not seem likely at present.

The Committee agrees that the current level of the EU intervention price is set at such a level that many producers would be out of business before that price was ever reached. The Committee therefore agrees with the EFRA Committee’s recommendation that the intervention rate be reviewed before April 2015 and then regularly kept under review in what is a volatile market. The Committee also recommends that you press the UK Government and the EU to consider conducting an impact assessment of raising the intervention rate by different margins so that any future consideration of the matter can be evidence-based.

The supermarkets who gave evidence to us did not seem to think that extending the voluntary (dairy) code to cover them would be effective or desirable as they are already governed by another code and it was important and appropriate, to keep the two codes distinct from each other.

**UK Groceries Code Adjudicator**

The Committee took evidence from the UK Groceries Code Adjudicator (GCA), aware of the current limitations of her remit in this area, as highlighted by the House of Commons report and recent comments by the Prime Minister. The House of Commons report made several recommendations on this issue, including the need for the UK Government to urgently review the GCA remit and that the GCA be able to accept complaints from indirect suppliers, and have the power to launch investigations as well as to respond to complaints. The Prime Minister recently stated that the remit of the Adjudicator would be reviewed to enable it to cover more of the dairy industry.

We were impressed by the evidence given to us by the Adjudicator and are reassured that she is taking her role very seriously indeed, evidenced by the fact that on the morning she appeared before us, she announced her first ever investigation, telling us—

“The investigation that I launched today is into Tesco. I have acted because I have reasonable suspicion that Tesco has breached the groceries supply code of practice in the areas of delaying payments to its suppliers and asking for payments for shelf positioning.”

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The Committee heard concerning anecdotal evidence suggesting cases of supermarkets in Scotland charging for the right to tender, or for premium shelf space, and that poor prices were being paid in some cases for non-liquid milk dairy products. We are therefore delighted to hear that the Adjudicator is to investigate allegations of Tesco charging for shelf space, which will incorporate an examination of whether this included dairy products, and her intention to pursue other supermarkets if evidence of similar practices is uncovered.

However, the GCA confirmed to us that she does not have a remit to get involved in milk pricing, and also that she cannot investigate cases concerning indirect suppliers. However, she did clarify that if indirect suppliers have evidence regarding the relationship between a direct supplier and a retailer then she would be happy to consider that and discuss it with them.

The GCA would not comment on any extension of her role, which was understandable, but it was interesting to note that the GCA does have the power to recommend changes to her role.

As part of her evidence to us the Adjudicator outlined a number of other issues which she has been working on with supermarkets, which included—

- what she referred to as “drop and drive”, which, in the dairy sector, included the issue of suppliers delivering an agreed amount of milk to a supermarket, but receiving no proof of delivery, and then the supermarket claiming that the total amount was not delivered and reducing the payment accordingly;
- demand for lump sums from suppliers to fill gaps in accounts;
- the accuracy of supermarkets forecasting of orders, and penalising suppliers unreasonably;
- stipulating to suppliers who they must use for artwork/photography and then overcharging; and
- passing an inflated cost of customer complaints on to suppliers.

We were, quite frankly, horrified at this list of practices which the Adjudicator must have good reasons to investigate. It should be noted that all of the supermarkets which gave evidence to us, with the exception of Tesco who declined to comment due to the ongoing investigation, said that they did not recognise the reprehensible practices outlined by the Adjudicator.

The Committee welcomes the recent power conferred on the Groceries Code Adjudicator to be able to impose financial penalties on supermarkets, together with the other sanctions already at her disposal. The Committee was also pleased to note that indirect suppliers can raise issues with her if they relate to direct suppliers and retailers, and are evidence-based. The Committee recommends that stakeholders in the Scottish dairy industry that have evidence that supermarkets have breach the UK Groceries Code, contact the GCA with the evidence, in order to help her with her investigations. The GCA
stated in evidence that she has a duty to preserve the anonymity of those supplying evidence to her.

The Committee welcomes and endorses the recommendations made by the EFRA Committee, and the subsequent commitment made by the Prime Minister, to review the remit and powers of the Groceries Code Adjudicator to consider if more of the dairy industry can be covered by that office. In particular the Committee would like to see the Adjudicator having more flexibility to proactively launch investigations and gather evidence about relationships supermarkets have with indirect, as well as direct, suppliers.

The Committee was appalled to hear from the Adjudicator of the matters relating to supermarket practices which she is currently pursuing, some of which affect the dairy sector. All of the supermarkets which gave evidence to us, with the exception of Tesco who declined to comment due to the ongoing investigation, said they had no knowledge of such practices taking place in their businesses. However, the Committee believes this is further evidence of a breakdown in the collegiate approach that should be being followed by all those in the chain from producers to consumers. Everybody should be on the same side in seeking to produce, market, sell and consume good quality Scottish dairy products and for that to happen there needs to be a change in mind-set by many large organisations. The Committee urges all major retailers in Scotland to adopt such an approach and to work with the Adjudicator to rid Scotland of any ethically reprehensible practices.

Other measures to aid the dairy sector

As well as considering the reasons for the current problems in the sector, and what role Scottish, UK, and EU policies and regulations play, the Committee also examined what other measures could and should be considered to help the industry in Scotland.

Producer Organisations

In some Member States Producer Organisations (POs) have been formed by dairy farmers and they can have a role in negotiating milk prices for their members. The Commons report suggested that forming a PO could aid farmers and give them “greater clout in the marketplace” and the Committee examined whether POs could play a greater role in Scotland than at present. Evidence to the Committee from producers suggested that there had not been great interest in establishing POs in Scotland, perhaps because of the perceived red-tape and conditions set for recognition by the Rural Payments Agency. It was also noted, anecdotally, that countries that have POs operating do not seem to be securing better prices as a result.

We are aware that the Scottish Government has previously outlined its intention to ensure that the Scottish Agricultural Organisation Society (SAOS) is resourced to be able to support the establishment of POs and we were interested to hear from Frank Strang, who accompanied you when you gave evidence to us, that SAOS is currently working with producers in relation to First Milk at Campbeltown. You told us that the Scottish Government was supportive of producers working together and would
support POs as part of that, but that it was ultimately up to producers how they organised themselves.

The Committee believes that Producer Organisations have the potential to address some of the issues being faced by the dairy sector in Scotland at present. We were interested to hear of the role which the Scottish Agricultural Organisation Society could play in this process and in the situation with First Milk and Campbeltown in particular and ask that you provide the Committee with more detailed information on this.

The Committee believes that the potential benefits of establishing Producer Organisations in Scotland has not been fully assessed and therefore recommends that the Scottish Government works with the NFUS and any appropriate others to fully examine the potential for establishing POs in Scotland; consider what barriers may exist, including any set by the Rural Payments Agency; and consider what further support is required for the industry to assist with the process.

**Ambition 2025 and the Dairy Growth Board**

The current situation highlights the importance of the Scottish Dairy Review's report “Ambition 2025”, published back in 2013 following the review you launched at the end of 2012. That report led to the establishment of the Dairy Growth Board to help drive growth in the sector and the Committee examined what effect the board has had, now it has been established (chaired by Paul Grant) and what role it could play in the current situation. The Ambition 2025 reports also stated that the game-changer in the dairy sector would be “the development of new export markets which are now the destination for the majority of non-liquid, added value dairy products manufactured in Scotland.” James Withers of Scotland Food and Drink told us that a Scottish Dairy Hub has now been established, funded by DairyCo and the Scottish Government, and that it would provide a one-stop shop for farmers looking for advice and support.

The Committee is encouraged to hear that the Dairy Growth Board and Scottish Dairy Hub are both now up and running, and hopes that both will provide dairy farmers in Scotland with increased support, and will help the industry progress towards the growth target of 50% as set out in the Ambition 2025 report. As explored further below, the Committee believes that there is significant scope for improving the amount of Scottish dairy products sold in Scotland, particularly premium products.

The Committee would welcome further information on the work of both the Dairy Growth Board and the Scottish Dairy Hub, clearly outlining what actions both will be taking in the short-term, and plans they have for the future.

**Promotion and marketing of Scottish products home and abroad**

The Committee was particularly struck by evidence it received suggesting that much more could and should be done in Scotland to market premium Scottish dairy products, such as cheese, cream, yoghurt and butter in particular. We heard from various sources that there is huge potential to add value to the milk produced in Scotland much more effectively than is happening at the present time. We noted that that the market leaders in Scotland of these products are all currently outwith
Scotland – such as the huge market shares for Lurpak butter and Cathedral City cheese, from Denmark and England respectively. You told us that the ultimate aim should be for the vast majority of milk, butter, cheese, yoghurt and cream sold in Scotland to have been produced in Scotland and there is obviously a great deal of work required to get to us to that position. We were very interested, given all of the above, to hear about the Scottish Government’s plans to launch a new Scottish dairy brand towards the end of this year which could be the required game changer.

This issue takes us back to where our work started, with the problems we have seen at First Milk. The islands that provide liquid milk to First Milk in Scotland could have a great story to tell in terms of other added value dairy products – such as Mull of Kintyre cheddar. However, either not enough of these products are being produced in the first place, or they are not being given enough shelf space in Scottish supermarkets to give consumers more choice and more opportunity to buy Scottish products.

Supermarkets told us that they were making efforts to buy more Scottish products and market them more effectively and encouraged producers and organisations such as First Milk to meet them to discuss how to take this forward. However many of them stressed that it was important to get the right products in the right places, and also that the market would dictate to a certain extent, i.e. work needs to be done with consumers to encourage them to switch from well-established non-Scottish brands to alternative Scottish products. They also told us that Scottish products need to be branded as such but, in doing this, it was vital that products are started and finished in Scotland. Interestingly, in light of the above discussion with the Groceries Code Adjudicator, all the supermarkets said they would not charge small companies for shelf space, but Morrisons did suggest that bigger brands can put together a “package” of support for products. It was not clear to us what this “package” entailed.

We also heard that Scotland is lagging behind many other parts of the world in innovating new dairy products. Examples were given of products such as salad cheeses and bio-drinks which are growing in popularity globally but are not currently produced in Scotland. Supermarkets also told us that it is difficult to get Scottish products such as yoghurt. The Committee is aware of innovative developments in other parts of the world, from dairy muffins, to milk based puddings and trifles and “grab and go” nutritional children’s products.

It was interesting to note that the sales of organic dairy products are bucking the trend of declining sales of organic produce in Scotland, especially as you told us that organic producers can receive up to 40p per litre of milk.

It is important that we do not forget the role of others beyond the retail sector, such as public and private procurement of dairy products in Scotland. We were encouraged to see that in terms of public procurement, the vast majority of products being bought are Scottish in origin (96% of local authority procured dairy products are Scottish), but we are less clear on the situation in terms of private procurement, and the hospitality sector.

You agreed with us when you gave evidence that there was scope to do a great deal more in this area, and it was interesting to hear of the success that the food charter,
which all appointed event caterers have to sign up to, had at events such as the Ryder Cup and Commonwealth Games last year. You suggested that there was scope to extend the charter across Scotland. You also told us that the Scottish Government is keen to work with the UK Government and the EU on the Smith Commission recommendations regarding the development of “Made in Scotland” food label. We also note your commitment to refresh the Government’s food strategy, and to put children’s food policy at the heart of that.

The Committee is firmly of the view that the success of the Scottish dairy sector in the medium to long term lies not only in developing export markets, but also in shifting the pattern of sales in Scotland to home grown produce. The Committee wants to see the industry working together in Scotland to improve sales of Scottish added value dairy products such as cheese, butter, yoghurt and cream. It seems fitting that this year acts as the impetus given that 2015 is the Year of Scottish Food and Drink and we were interested to hear from you about the intention to launch a new Scottish dairy brand towards the end of this year.

The Committee would welcome further information from you on the launch of the Scottish dairy brand, and on the Scottish Government’s strategy with regard to how the industry can add value Scottish dairy products sold in Scottish supermarkets. We also call on the supermarkets to improve the marketing and promotion of Scottish products. If such products are to be given a fighting chance in such a competitive market place then retailers need to assist as much as possible.

The Committee was disappointed to learn of the lack of innovation in Scotland to develop new dairy products. With liquid milk prices currently low, and many dairy products currently sold in Scotland coming from elsewhere, there is a clear opportunity to develop new products in Scotland to sell in Scottish stores and beyond. There are also opportunities in organic dairy products given the continued growth in sales in Scotland. The Committee asks you to outline what the Scottish Government is doing, and can do, to help create the right environment to stimulate such innovation.

It is essential that the Scottish Government uses the 2015 Year of Scottish Food and Drink to ramp-up the promotion of Scottish dairy produce overseas and recommends that you update us on the Scottish Government’s strategy for growing exports of Scottish Dairy Products, having reference to all of the comments made above regarding added value and innovation.

**Increased processing capability**

If we are to try and grow the demand for Scottish dairy products home and abroad then it is vital that the infrastructure is in place to meet that demand. James Withers told us that the focus in the industry should be on: brand development; market development; export development; and investment in processing. We heard evidence that Scotland does not currently have sufficient processing capability for added value products which leads to excess milk often being channelled into low value products. We also heard evidence regarding the vital Campbeltown Creamery, operated by First Milk and which dairy farmers on Bute, Gigha and Kintyre are reliant
on. First Milk told us that further investment would be forthcoming but it was not clear to the Committee on the timescales and details of that.

If Scotland is to realise the ambitions set out for its dairy sector by the Scottish Government, as well as maintaining a viable, sustainable dairy sector in all parts of Scotland which traditionally support activity, then it is crucial that our infrastructure is fit for purpose and of sufficient scale to both sustain current activity and allow for growth.

We therefore call on all of the relevant players in the planning process, including the Scottish Government and local authorities, to work together to expedite such matters as quickly as possible and ensure that the contributions such facilities will have on a particular sector are kept to the fore.

We also hope that the launch of the new Scottish dairy brand later this year will provide fresh impetus for investment in processing facilities in Scotland and the Committee recommends that you work closely with the enterprise agencies and local authorities to capitalise on this opportunity.

Finally Cabinet Secretary, we note the Scottish Government’s intention to bring forward a milk plan in the very near future. We look forward to receiving details of that and hope that many of the issues outlined by the Committee, as a result of our inquiry, will have helped to inform that plan. The Committee’s inquiry received a great deal of press coverage, and it was heartening to see such an important issue being given the spotlight it deserves, and we hope that people are better informed as a result. We intend to seek to hold a Parliamentary debate on this very important issue next month, and we look forward to engaging with you further during that.

Yours sincerely

Rob Gibson MSP
Convener