



DairyCo Ltd

**Three-Year Business Plan
2008/9 – 2010/11**

3 December 2007

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Introduction

This is the first business plan for DairyCo, the new dairy sector company created under the Agricultural and Horticultural Development Board (AHDB). It sets out the current issues faced by the British dairy industry, DairyCo's role and objectives in tackling these issues, and the strategies that will be used to deliver the objectives.

The dairy industry underwent deregulation over a decade ago and it has changed significantly in that period. While change has not been easy, there are signs the industry is starting to leave behind the legacy brought by the Milk Marketing Boards and political control.

The Milk Development Council, which DairyCo succeeds, was also part of the legacy; it was created to provide a home for many essential services supplied by the Boards that would not naturally have had a home elsewhere.

It is the firm intention of DairyCo that while it will continue to provide important services that help tackle the issues faced by the dairy industry, it will also do its utmost to encourage the industry to ultimately take over the provision of these services – either on a commercial or voluntary basis. It is with this ultimate goal in mind that this plan has been prepared.

A summary of the British dairy sector

The dairy sector in Great Britain is rapidly changing, and in particular consolidating; we have increasingly integrated supply chains and around 78% of milk is bought by just six organisations.

The number of British dairy farmers has fallen from 29,000 to 15,000 over the past 10 years, while milk production has remained around 14 billion litres – albeit with a more substantial and sustained decline in recent years (2007/8 production is likely to be about 4% down on the five-year average).

The UK industry is a net importer, with a trade deficit which has grown by 137% over the past 10 years to reach its current £931m. Imports of value-added products are increasing, with the volume of cheese imports increasing by 57% over the past 10 years. Meanwhile, exports of low value-added raw milk – mainly over the Northern Irish border – have increased by 260% over the same period.

Farmgate milk prices have generally fallen over the past decade due to exchange rates, world market conditions and reductions in CAP support, all leading to difficult trading conditions for UK dairy farmers. Over the same period, processors and retailers increased their gross margins on liquid milk through higher retail prices and lower farmgate prices. However, prices have been much stronger in the past six months due to favourable world market conditions which are improving the current outlook.

Consumption of dairy products is enjoying positive growth around the world. In the UK, total sales of liquid milk have been relatively stable during recent years after a thirty year decline, and have actually increased by 2.7% in the 12 months to October 2007. There has also been a 2.8% increase in cheese sales.

All these factors combine to create a rapidly changing industry, which has been analysed thoroughly by the DairyCo board in developing this plan (see section *An assessment of Britain's dairy farming sector* for more details).

A profile of DairyCo

DairyCo's board of 12 includes eight dairy farmers located across Scotland, England and Wales, who all operate very different production systems. As well as this high representation of farmers – which is appropriate considering the levy is only raised from dairy farmers – there are two independents on the board, one dairy processor, and the chairman Tim Bennett.

The MDC raised around £7 million per year from the levy over the past three years, and it is calculated that DairyCo's new plans can also be funded by this rate of levy. Hence – subject to Ministerial and AHDB approval – the levy rate for DairyCo in its first year will be 0.06 pence per litre of milk produced.

DairyCo's purpose

DairyCo will exist to:

'promote world class knowledge to British dairy farmers so they can profit from a sustainable future'

DairyCo's successful delivery of this will be demonstrated by:

'world-beating dairy farmers thriving in a vibrant industry – without levy support'

DairyCo's approach to achieving its purpose

If DairyCo is to realise this long term vision, it will need to remedy 'market failure' – ie tackle issues not currently being addressed or being addressed insufficiently to meet the needs of the industry – by encouraging the provision of key services by others on a commercial or voluntary basis.

The practicalities of achieving this are that we will need to see the following changes, implemented on a phased basis over the next three years:

- Increased funding of activities from alternative sources
- Increased uptake of commercial advisory and training services among farmers.

The stepping stones to achieving these changes include the following tactics:

- DairyCo-validation of commercial technical services
- Easier access for dairy farmers to the services and support available to them through an information hub
- Using Knowledge Transfer (KT) to promote commercial services and publicise the research programmes available through DairyCo
- Reducing each year the percentage of DairyCo's income that is levy-based.

DairyCo's role in the dairy sector

DairyCo must work effectively with public and commercial industry partners (farmers, processors, retailers, government and its agencies) to ensure levy funds are only used in the unique, unaddressed (ie market failure) areas that can generate the greatest benefit for dairy farmers.

For example, DairyCo has a significant role to play in helping to improve the key areas of business management, image management and supply chain information, which are currently not well developed in the industry.

Although various commercial services already provide support to dairy farmers in improving their competitiveness, these have a low level of uptake and are of mixed quality. Hence there is a strong case for allocating a relatively large proportion of levy funds to both providing that support and encouraging the uptake of quality commercial services.

However, it is clear that tackling the key issues facing the industry described previously is not DairyCo's sole responsibility.

In those areas where commercial organisations are rapidly increasing their activity – such as innovation and promotion of new products – the need for financial support from DairyCo will move to different areas, and so the budgets required will change according to the new predicted costs.

DairyCo's key operating principles

Given DairyCo's purpose and role, there are several key principles upon which DairyCo's operations will be based.

Facilitation

DairyCo will make the essential happen – but not necessarily by doing the work itself.

To ensure the delivery of world-class answers that address the needs of dairy farmers, DairyCo will use a process of collaboration and facilitation with our industry partners. Our staff will investigate opportunities to address issues of market failure that can be funded all or in part by third parties.

Independence

Although DairyCo will be seeking alternative sources of funding for its activities, it will never do so at the expense of independence and impartiality, and its employees will always offer the best possible unbiased advice – even when working with a commercial provider.

Alternative Markets

There is an increasing differentiation of milk supply with farmers opting for production systems based on different breeds, organic principles, varying diets etc. All of DairyCo's work will take these diverse groups into account and, where possible, bespoke information and specific activities relating directly to these groups' interests will be provided.

Quality People

The quality of DairyCo staff will be key to its success and therefore great attention will be paid to attracting and retaining the right people for all roles. This means training, recruitment and retention will be very important.

Focus

DairyCo will measure itself rigorously against the objectives set out in its business plan. However, as is appropriate for a body conducting research and servicing a wide ranging customer base in the interests of seeking the right answers, some flexibility will be built in to the system. This means that some limited resources will be made available for 'exploratory' activities which do not feature in the current business plan but which may provide key strategies for the next business plan if successful.

Attitude

For DairyCo staff to succeed in both upholding these principles and delivering the agreed strategies, they will be actively encouraged to embrace the following values:

- **Professional**
Finishing each task to the highest standard
- **Ethical**
Always remembering who we work for and what we stand for
- **Ambitious**
Daring to think that bit bigger
- **Irreverent**
Challenging the status quo

An assessment of Britain's dairy farming sector

| | |
|--|---|
| <p>Strengths</p> <ul style="list-style-type: none"> • Cool and damp climate • Large herd size (by EU standards) • Resilient family farming sector • High levels of production efficiency on some units • A wide range of market opportunities for farmers • Heritage of fresh milk consumption | <p>Opportunities</p> <ul style="list-style-type: none"> • Dedicated supply chains • Strong provenance opportunities • Growing and affluent population • Global growth in dairy consumption • New and innovative products • New routes to market • Industry consolidation • Improved business performance |
| <p>Weaknesses</p> <ul style="list-style-type: none"> • Variable production performance • Poor quality training opportunities for the development of business skills • Lack of opportunities for expansion/new entrants • Variable quality of support • Recruitment and retention of quality staff • Supply chain relationships • Poor export market • Fluctuating prices for milk | <p>Threats</p> <ul style="list-style-type: none"> • Environmental legislation • Regulatory burden • Climate change • Animal welfare and environment perceptions • Conflict within supply chains • Reduction in Government support • Pressure on land use • Increasing competition from European neighbours and rest of world • Nutritional concerns • Risk of infections and disease |

The previously agreed industry strategy for future profitability was a focus on:

- Innovation and market development
- Supply chain relationships
- Supply chain efficiency

It is possible for the industry to address, manage or exploit the SWOT elements above using these strategies, but some areas of market failure emerge.

In supply chain relationships:

- Inherently these relationships exist between commercial parties
- However, relationships are built on common understanding and the necessary information is not always available to farmers
- They also need a fair marketplace with analysis of structural issues...
- ...and the provision of information for policy formulation

This indicates a need for **Supply Chain Information**.

In supply chain efficiency:

- Processors are already addressing issues through Dairy UK...
- ...but farms still have a huge variation in efficiency (in excess of 5ppl in costs of production between top 10% and the average)
- There is a need to support improved business performance...
- ...but the quality and use of commercial consultancy services is variable
- There is a role in providing farmers with toolkits to meet regulatory and environmental requirements

This indicates a need for **Business Management**.

In innovation/market development:

- £120 million commercial funding was spent on advertising in 2006; around £140 million is likely in 2007
- Product innovation and launches are increasing...
- ...but there is possible market failure in managing the image of dairy products and dairy farming to underpin this growing commercial activity

This indicates a need for **Image Management**.

Combining these aspects with the need for DairyCo to evolve its role in the future to reduce market failure and the services dependent on levy income, DairyCo's objectives for 2008/9-2010/11 are:

- Objective 1: Supply Chain Information
 - *Provision of high quality information to help farmers and their representatives make the most of dairy markets and opportunities*
- Objective 2: Business Management
 - *Help dairy farmers increase their profits while meeting regulatory and environmental requirements – through better business management*
- Objective 3: Image Management
 - *Help promote a positive perception of dairy products and dairy farming among the general public.*
- Objective 4: Development of DairyCo
 - *Development of DairyCo towards a self-sustaining model*

DairyCo's three-year objectives and delivery strategies

Objective 1: Supply Chain Information

Provision of high quality information to help farmers and their representatives make the most of dairy markets and opportunities

Strategy: Provision of a world-class information service

Effective supply chain relationships are crucial for the success of the industry because the different parts of the chain are highly dependent on each other. Information and understanding are important for productive relationships so DairyCo will provide a world-class market information service which will be insightful, independent and impartial – yet challenging.

This means farmers and their representatives will have access to unbiased, high-quality information to assist them in business planning and improving relationships. This information will also help guide industry policy and future DairyCo strategy.

We will do this because provision of information leading to improved understanding and better relationships will support the development of the industry and allow farmers and their representatives to maximise business opportunities.

In 2008/9, the market information service will be extended to both provide the depth of information necessary to fully understand dairy markets, and to continue to develop farmer-facing economic benchmarking services.

Objective 2: Business Management

Help dairy farmers increase their profits while meeting regulatory and environmental requirements – through better business management

Strategy: Helping dairy farmers meet and manage environment needs and regulatory requirements

DairyCo will, in collaboration with industry partners, undertake research and provide tools to ensure farmers can improve sustainability and minimise environmental impact, thereby proactively managing a likely increase in regulatory burden.

We will do this because improving dairy farmers' environmental profile and ensuring regulation is realistic – while maintaining profitability – is crucial for the future of the industry.

In 2008/9 we will work with AHDB, Defra, devolved administrations and others both nationally and internationally to provide an accurate assessment about the possible climate-changing impact of milk production and how to mitigate it sustainably.

Business Management Strategies: Helping dairy farmers increase their profitability through better business management

A programme of research aligned with industry priorities will be implemented by DairyCo, as will a programme of knowledge transfer to ensure research is utilised

profitably on-farm. Genetic evaluation and other services that support or aid improved business management will also be provided and promoted.

DairyCo will work with AHDB, Defra, devolved administrations and others both nationally and internationally to provide high quality research and practical, applicable tools which can be implemented on farm through the business management strategy.

We will do this because the vast variation in performance on dairy farms means that communication of best practice can lead to very high return on investments and increased profitability.

In 2008/9, DairyCo will focus on the following five strategies:

- **Feeding** – a farm-level campaign to improve feed efficiency will be prioritised because the difference between the top 10% of farm businesses in efficiency of feed use and the average is 0.9ppl. This means that if an extension officer can assist 20 dairy farmers to improve efficiency by 0.5ppl through implementing best practice, they will more than pay for themselves in one year*
- **Labour Use** – MDC economic research has shown a significant range in the efficiency of how labour is utilised from farm to farm, and research will be carried out to develop strategies to address this variance. We will do this because the difference between the top 10% of performers and the average is 2.7ppl. This means that if an extension officer used outcomes of this research to assist as few as 10 dairy farmers to improve labour usage by 1.3ppl through implementing best practice, they would more than pay for themselves in one year.
- **Business Skills** – DairyCo will support the development of farmers' business capability through discussion groups and other tools and services. This area has been prioritised because increasing business acumen among dairy farmers has been identified as a clear industry need by several independent studies. Furthermore, the difference in costs between the top 10% and the average cost of production is in excess of 5ppl. Better business management and benchmarking will allow farmers to identify and tackle areas where they can improve business performance. If an extension officer assisted two discussion groups of 10 farmers implement best practice and improve profitability by 0.5ppl during the year, this would more than cover the costs of that extension officer.
- **Proactive Health Management** – focusing particularly on mastitis reduction in 2008/9 will deliver benefits on three levels: Improve longer term business profitability; increase levels of animal health and welfare; deliver a positive message to consumers
- **Genetic Evaluations** – the breeding+ genetic evaluation service will continue to be developed to help farmers maximise their business potential through breeding. Breeding has a considerable impact on profitability, as demonstrated by the fact that 80% of the increase in milk yield over the past 20 years can be attributed to improved breeding – giving a total annual economic benefit of well over £10m per year on all traits evaluated.

* This is calculated on 0.5ppl *800,000 litres *20 farmers = £80,000

Objective 3: Image Management

Help promote a positive perception of dairy products and dairy farming among the general public.

Strategy: Help promote the positive perception of dairy products and dairy farming with the general public.

DairyCo will work with the industry to ensure that both issues are managed and the image of dairy products and dairy farming is promoted. This means that increasing levels of commercial innovation can be securely underpinned.

In 2008/9 DairyCo will work with industry partners to agree the co-ordination of issues management and the promotion of positive consumer messages. The agreed model will be implemented during the year.

Objective 4: Development of DairyCo

Development of DairyCo towards a self-sustaining model

Strategy: Reducing dependence on levy funds

The organisation will be managed to be as efficient as possible and to increase its non-levy funding of activities. This is because any organisation tackling market failure should have an aim of fixing that market failure and reducing the number of activities requiring funding from the statutory levy.

In 2008/9 DairyCo will seek alternative third party funding for its activities which will reduce the dependency on levy funds while still addressing the market failure issues within the sector.

Strategy: Ensuring a smooth transition

In 2008/9 DairyCo will focus on making the transition from MDC to DairyCo as smooth and efficient as possible.

Strategic priorities 2008/9

| Strategy | Key Outcome | Targets 2008/9 | Key Risks | Key Controls |
|--|---|---|--|---|
| Objective 1: Supply Chain Information | | | | |
| Provision of a world-class market information service | Farmers have access to unbiased, high-quality information that assists in business planning and relationships | Annual survey of farmers shows an increase in 5% of awareness that DairyCo provides market information (MI), and an increase of 0.5 in the value placed on that service by those aware of it. ¹ | Availability of staff Perceived or actual bias Depth of analysis Depth of challenge | Appropriate recruitment, retention, and training procedures Sign off procedures Staff and time to undertake work |
| <i>Resource Requirement: £734,000</i> | | | | |
| Objective 2: Business Management | | | | |
| Sustainably mitigate the impact of dairy farming on climate change | Reduction in the amount of climate changing emissions produced per litre of milk | A detailed understanding and prioritisation of the issues for the next stage of work Sufficient knowledge to set appropriate on-farm targets | Not having the necessary detail to inform priorities | Use of robust, globally-accepted analysis and review strategies |
| Increase milk output per labour unit | More efficient labour utilisation, allowing increased time to reduce other costs | Understanding of the main issues impacting efficient use of labour Identification of solutions Sufficient knowledge and understanding to set appropriate targets | Lack of emphasis placed on people/labour management within farm businesses Poor quality research not providing solutions | Provide the right environment and evidence – in the right format – to drive change Project management of research |
| Improve feed efficiency on dairy farms | Increased milk output per kg of dry matter fed on the farms with which DairyCo is working | Feed efficiency on dairy farms with which DairyCo works improves by 5%. On a typical cost of 4ppl this equates to 0.2ppl. | Ensuring farmers have sufficient confidence in the information provided to change Training not adequate Lack of suitable staff | Develop the most effective tools and materials for targeted campaigns Peer-review tools and materials Appoint dedicated KT manager Suitable retention and progression in place for staff |
| Improved business skills to help farmers take control of the future of their dairy businesses | Farmers actively planning and taking control of their farm businesses | 100 Dairy Business Groups achieving: – 80% of attendees agreeing that it is a good use of their time – 70% say they have applied what they have learned by making changes on the farm 250 MilkBench datasets 5 What If courses successfully run | A lack of interest in planning and cost control brought about by higher milk prices Poor quality training and management of staff Lack of suitable staff | Communication of importance of cost control Delivery of proof that planning works for a more secure future Rigorous training and performance management system Suitable retention and progression in place for staff |

¹ In March 2007 42% were aware that MDC provided MI, and the value placed was 6.52 / 10; the starting point for the 2008/9 year will come from March 2008 survey.

| Strategy | Key Outcome | Targets 2008/9 | Key Risks | Key Controls |
|---|--|--|---|--|
| <i>Ingrain proactive health management into the development of business strategy</i> | An increase in the level of proactive health planning among dairy farmers Positive messages for use in image management | A decrease in mastitis levels for those farmers engaged in the DairyCo mastitis plan by 20%. On typical figures this equates to a saving of 0.2ppl. | Reliance on others to deliver the programme Industry advisors ignore information Information only taken up by small number of farmers | Work with key influencers in the industry, publicising the economic benefits to them Work with existing industry and farm advisor's representative organisations |
| <i>Effective promotion of the benefits of breeding and tools provided</i> | Farmers make informed breeding decisions that lead to the best cows for maximising their profitability | Three proof runs produced The annual survey of farmers finds that the value placed on the DairyCo's provision of genetic information increases by 10% during the year. ² | Failure to recognise the benefits of genetic services by some farmers | Careful use of targeted communication and existing attitudinal research to tailor messages appropriately |
| <i>Resource Requirement: £2,925,000</i> | | | | |
| Objective 3: Image Management | | | | |
| <i>Defend and promote the image of dairy products and dairy farming</i> | Consumers have a positive image of dairy products and dairy farming | Maintain or grow net dairy consumption intention among the public, as tracked by regular surveys | Increased pressure group activity Negative scientific outcomes Misconception of dairy farming and production Lack of industry co-operation | Close media monitoring and regular tracking of critical issues Retain high level of scientific awareness Carry out sufficient proactive and positive communication Close communication and liaison with industry |
| <i>Resource Requirement: £1,134,000</i> | | | | |
| Objective 4: Development of DairyCo | | | | |
| <i>Increase in alternative funding</i> | Non-levy monies are secured to fund DairyCo activities | Secure £250,000 of additional income or match funding, with £50,000 of that delivered within 2008/9 | Lose independence | Ensure all contracts and joint venture entered in to fit in to DairyCo objective, strategies and principles |
| <i>Ensuring a smooth transition</i> | The transition to DairyCo from the MDC is effected with minimal disruption | The annual survey of dairy farmers shows a positive reaction about the efficiency of the change for the factors within DairyCo's control | Dairy farmers perceive the change has reduced the value returned for the levy Disruption to services to levy payers | A series of 'deliverables' are scheduled after the launch of DairyCo Good communication with levy payers is carried out throughout the change Staff communication is prioritised Careful planning and risk management |
| <i>Resource Requirement: £710,000</i> | | | | |

² This question has not previously been asked but a starting point will be established from the survey conducted March 2008

Projected budget for 2008-11

| (£,000) | | Forecast | | | |
|----------------------------------|--|--------------|--------------|--------------|--------------|
| | | 2007/8 | 2008/9 | 2009/10 | 2010/11 |
| Income | | | | | |
| | Levy | 6,700 | 6,750 | 6,800 | 6,850 |
| | Non Levy | 264 | 105 | 235 | 500 |
| | Interest | 35 | 50 | 50 | 50 |
| | | <u>6,999</u> | <u>6,905</u> | <u>7,085</u> | <u>7,400</u> |
| MI | Staff | 261 | 479 | 505 | 522 |
| | Projects | 275 | 255 | 264 | 273 |
| Research | Staff | 327 | 304 | 304 | 315 |
| | Projects (inc Genetics) | 1,148 | 1,085 | 1,050 | 1,050 |
| KT | Staff | 492 | 1,009 | 1,270 | 1,685 |
| | Projects | 271 | 471 | 564 | 639 |
| Comms | Staff | 167 | 215 | 217 | 224 |
| | Projects | 424 | 435 | 342 | 354 |
| MD | Staff | 292 | 184 | 190 | 196 |
| | Projects (inc Image Management) | 2,062 | 950 | 890 | 830 |
| Central | | 861 | 916 | 833 | 860 |
| Business Development | | - | 60 | 90 | 90 |
| UK IDF | | 28 | 26 | 27 | 28 |
| IDF Conference | | - | 30 | - | - |
| DairyCo Board/MDC Council | | 156 | 226 | 235 | 240 |
| Transition | inc Tax on uplift | 175 | - | - | - |
| | | <u>6,939</u> | <u>6,645</u> | <u>6,781</u> | <u>7,307</u> |
| | Profit/Loss | 60 | 260 | 304 | 93 |
| | Reserves | 2,231 | 2,491 | 2,795 | 2,888 |
| | Headcount | 59 | 63 | 67 | 74 |