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# THE ROLE OF INTERNATIONAL TRADE IN THE RISE OF THE NEW ZEALAND DAIRY INDUSTRY FROM ITS BEGINNINGS TO THE FONTERRA ERA

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## ABOUT THE AUTHOR



Bruce Muirhead is professor of history and associate vice president, external research, at the University of Waterloo, and recipient of a CIGI Collaborative Research Award. He has written extensively on post-World War II Canadian agricultural political, diplomatic, financial, international and trade history, and has published five books with university presses and numerous refereed chapters in books and journal articles on these topics. His ongoing work relates to dairy supply management in Canada and competing systems in Australia, the European Union, New Zealand and the United States. His current research focuses on the financialization of farmland in Canada's West.

## ABOUT THE PROJECT

This project, funded by a CIGI Collaborative Research Award, undertakes a comprehensive, comparative analysis of a number of dairy management systems, including those of the European Union (a hybrid system containing subsidies, tariffs and quotas), New Zealand (neo-cooperativization and free market), Australia (a recently deregulated system), the United States (subsidization and tariffs) and the unique Canadian dairy supply management system. The research examines the advantages and disadvantages of these paradigms, addressing, among other elements, the cultural, financial, political and social costs and benefits to dairy stakeholders and consumers. Moreover, the ability of each system to provide food security and agricultural resilience in an international context of rising food prices, environmental degradation and climate change is assessed. Research findings will be disseminated in a series of CIGI papers and policy briefs.

## ACRONYMS

ADC	Australian Dairy Cooperation
BRICS	Brazil, Russia, India, China and South Africa
CER	Closer Economic Relationship
EC	European Community
EEC	European Economic Community
GATT	General Agreement on Tariffs and Trade
OECD	Organisation for Economic Co-operation and Development
NAUK	National Archives of the United Kingdom
NZ	New Zealand
NZDB	New Zealand Dairy Board
NZNA	New Zealand National Archives
RCEP	Regional Comprehensive Economic Partnership
TPP	Trans Pacific Partnership
WTO	World Trade Organization

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## INTRODUCTION

Since its widespread settlement by Europeans in the 1840s, New Zealand (NZ) has been an agricultural economy. As has been pointed out “there [has been] no serious challenge to the fundamental precept that the country’s economy rested on an agricultural foundation” (Macdonald and Thomson 1987, 231), and dairy has been a significant focus of that base. Dairy production was introduced to New Zealand with the clear intent to establish New Zealand as an adjunct to the economic needs of Britain (Hawke 1985). Indeed, the closeness of the relationship between “the Britain of the south” and the metropolitan centre is one of the fundamental characteristics of any environmental history of NZ agriculture (Pawson 2008). This would persist in a material sense for more than a century, until the United Kingdom joined the European Community (EC) in 1973.

Uniquely among the developed countries of the world, New Zealand came to rely heavily on dairy exports to support its way of life. Ensuring that adequate supplies of milk powder, butter and cheese found their way to the British market was the end point of much of its policy development. When that ended for the reason noted above, the NZ federal government in Wellington was forced to cast about for something to take its place. Slipping in global rankings of prosperity by the early 1980s, there were few obvious methods to change course. The newly-elected Labour government of David Lange hit upon probably the only policy that would work in the NZ context — to remove all subsidies from dairy and let it sink or swim on its own. That it swam mightily is a testament to its leadership, its perseverance and its particular situation. New Zealand’s system could also not be replicated elsewhere; it is, above all, a product of NZ geography and circumstance.

The advantage that accrued to New Zealand did not occur because of the adopted neoliberal policies that had become popular with the election of British Prime Minister Margaret Thatcher and US President Ronald Reagan — quite the opposite. As will be seen below, with the establishment of the New Zealand Dairy Board (NZDB) in 1961 as a single desk exporter, the removal of public policies designed to shield the dairy industry from external competition in the later 1980s and the creation in 2001 of Fonterra, the mega-cooperative, out of the amalgamation of the NZDB and two smaller cooperatives, the NZ Cooperative Dairy Company and Kiwi Cooperative Dairies, the country’s dairy industry sustained its position because of its steadfast focus on markets expressed through a single agency. It adopted what could be called neo-cooperativism, which ultimately led Fonterra to control about 92 percent of the country’s dairy production and 34 percent of global cross-border trade in the commodity. And that set the Fonterra cat among the multilateral trade negotiation pigeons in the early twenty-first century.

As will be seen below, all countries with pretensions to a dairy industry, including the European Union and the United States, have balked at undertaking serious trade liberalization negotiations in the sector with New Zealand. The latter is perceived to be too efficient, surely an irony given, for example, American rhetoric about the virtues of competition. Both the Doha Round of the World Trade Organization (WTO) and the negotiations undertaken through the Trans Pacific Partnership (TPP), a 12-member group working to complete a free trade area of certain Pacific Rim countries, have demonstrated that fact. NZ dairy is excluded from polite conversation while Americans, in the case of the TPP and both Americans and Europeans through the Doha Round of the WTO, continue to support their dairy industries.

## NZ DAIRY HISTORY — THE COLONIAL FARM IN THE SOUTH PACIFIC

Most colonial farms had small dairy herds to supply family needs and to provide useful preserved products like butter and cheese for sale. Quickly, specialist dairy production emerged with the rapid establishment of a myriad of farmer cooperatives to support the development of local and regional infrastructure. As a result, from the outset, New Zealand’s dairy industry was dominated by family farms and the cooperative organization of regional industry infrastructure and governance (Muirhead and Campbell 2012).<sup>1</sup> Significant opportunity for these smallholders was provided with the introduction of refrigeration in 1882.<sup>2</sup> For the first time dairy (among other commodities) could be shipped over long distances, making dairy exports to Britain a possibility just as the imperial centre found feeding itself to be increasingly difficult. This created a new large market for perishable foodstuffs “and created ‘a whole new reason for New Zealand to exist’” (Steel 2005, 182). As a dairy inspector concluded in 1883, “We have only to make the prime article in butter and cheese, then no power on earth can stay the flow of gold in this direction. The untold enduring wealth of New Zealand lies upon the surface and the cow is the first factor in the way of securing it” (ibid.).

This intense and growing market connection also fed New Zealander’s belief in the British Empire as the repository of all that was good and moral. When mixed with a bit of self-interested NZ intent to maximize market share, it

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1 Of course, Fonterra continues that tradition today.

2 This was critical to NZ’s economic progress: “Without refrigeration New Zealand would be a poor country in the South Pacific. Refrigeration gave New Zealand the opportunity to develop an extensive export economy, which has made possible a high standard of living for the population and the opportunity to be a world leader in social development. Refrigeration was, and continues to be, of utmost importance to the New Zealand economy and to the New Zealand people. It turned the blessing of a good climate for pastoral farming into a major economic resource” (R.L. Earle quoted in Cleland 2009, 1).

was all that was required to make the United Kingdom the preferred and only market for its produce. As noted by Waterson (1969, 50), “The area was an economic frontier of London, one of the large ‘Dairy Farms of the Empire’ relying on cheap capital, advanced agricultural technology, skilled management and labour, and a European value system. The whole *raison d’être* of the district rested on the assumption that the British urban market would require ever-increasing quantities of marginal foodstuffs produced from cow’s milk. This tremendous act of faith was originated by Anglo-Saxon colonists holding a series of socio-political beliefs in the family farm as the key unit of both production and society.”

And that worked, more or less, as NZ butter and cheese travelled in increasing volumes to the United Kingdom, along with lamb and wool. The passage of the Dairy Industry Act (1908) synthesized all dairy legislation into one act, and dairy farming became more scientific in terms of breeding, feeding and milking. As well, it established the rules governing the formation, registration and shareholding etiquette of dairy cooperatives that were so important. The legislation also represented a significant step along the path of dairy “professionalization” in New Zealand, as did the cooperative movement more generally, which became a strong focus in the industry. By 1900, co-ops accounted for 42 percent of all dairy factories, and the push toward a national marketing organization originated mainly through this movement (Nayga and Rae 1993, 95). As well, the government took a more active role in supporting dairy during the First World War with official control of buying and selling and purchase schemes. As did other governments during those four years, Wellington generally took a much greater interest in the functioning of the national economy, subsidizing some consumption, regulating other areas and legislating what citizens could eat, drink and do. In a time of global crisis, voters approved of government intervention in a way that would not have been possible in pre-war years.

Increased government activity, regulation and economic surveillance, however, did not extend to buying and selling land, and speculation became a national sport during the period from 1915 to 1921. It had an impact on dairy farmers as people gambled with their land and “bought and sold rural properties with amazing rapidity” (Waterson 1969, 45). The crash, when it came in 1921–1922, was swift and merciless, leaving dairy farmers with huge interest bills and dwindling amounts of milk with which to meet that debt. It represented the classic economic downturn and result.

Partly in reaction to that, in 1923 the NZ Dairy Export Control Board was established by statute. It would control marketing but not prices, as its main purpose was to regulate the flow of supplies to the British market and, as far as possible, avoid successive gluts and shortages, which were the bane of the dairy trade. The board was

the result of a search by producers for a way back to the days of high milk returns, before their speculative gamble with land came back to earth. The board reduced the cost of preparation, storage, shipment and disposal of their product overseas so that the benefit of economies of scale and efficiency would accrue to farmers (Smith 1943, 171). As has been pointed out, “apart from marketing and actual production, the history of the dairy industry was henceforth largely the history of the operations of the Board” (Evans 1969, 162). Given the hype, producers expected increasing returns. When that did not happen for various reasons, the board was met with increasing opposition. By 1926, it had abandoned its control of marketing because of producer pressure — it was as if “all the lessons of the past were suddenly forgotten” (ibid., 182). It was only with the Great Depression and increasing farmer bankruptcy that the board regained the power to become more active in dairy producer affairs, and only then because producers were staring disaster in the face.

### INTO THE DIRTY ‘30s

As noted, in the later 1920s the board beat a retreat, the result of opposition from a hostile prime minister, resurgent processors and a bad situation for dairy in the United Kingdom. In 1926, large unsold stocks of butter were held in Britain, making New Zealand’s control of the market difficult. Prices fell and the experiment was abandoned the following year. Returns were reasonably favourable for the next few years, which seemed to confirm the superiority of private sector processors in marketing NZ butter and cheese in Britain, at least until the global economic collapse in October 1929. By 1934, the price of all primary products had dropped by so much and for so long that the government finally agreed to the request by the dairy industry that it establish a Royal Commission to examine farm conditions. One of its findings, to the surprise of no one, was that “at least 50 percent of the dairy farmers of the Dominion are, in varying degree, unable at the present time to meet their commitments” (Smith 1943, 171). The Commission recommended a plan for the more effective control of marketing via a “single central body, acting in the national interest and having due regard to the requirements of all branches of production” (ibid.), a not dissimilar creature to that set up in 1923. The NZDB, as an effective agent acting on behalf of farmers, was solidified and it was provided with strengthened government representation.

Almost as that legislation was being made into law, the Labour party won power for the first time, vowing “to give

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Boards their running shoes" (ibid., 172)<sup>3</sup> and dairy farmers a stable, guaranteed price for their product. That proved to be popular among rural people. The government also passed the Primary Products Marketing Act (1936), giving it control over the marketing of any such product abroad, as well as locally. In the NZ context, that meant dairy.<sup>4</sup> The latter was a distinct change in practice as prior to the act, local production had been in the hands of local processors and merchants. In the estimation of the new government, it was necessary that the wholesale market for butter should be stabilized in relation to the price for export butter so that dairy companies received the same price, regardless of where their butter was headed. As for the guaranteed price calculation, "prices were to be such 'that any efficient producer engaged in the dairy industry under usual conditions and normal circumstances, should be assured of a sufficient net return from his business to enable him to maintain himself and his family in a reasonable state of comfort'" (Rosenberg 1959, 245). This legislation remained on the books well into the post-Second World War period. It also brought with it economic stability for the dairy industry, as well as establishing a system of smooth-running marketing machinery that was soon to be adapted to the marketing requirements of the Second World War.

New Zealand participated in the discussions that led to the Ottawa Agreements, held in the Canadian capital in July and August 1932. These were 12 bilateral trade agreements providing for mutual tariff concessions and a number of other commitments among Empire countries and colonies. As a contemporary analysis pointed out, the agreements "became definitely necessary, particularly as an outlet for exports of farm products, on account of the fading of foreign markets in the last half of the last decade" (Lattimer 1934, 567).<sup>5</sup> Of some importance for New Zealand was that the United Kingdom had raised duties and imposed quotas on non-Empire foodstuffs, including dairy. It basically extended the effects of the Import Duties Act (1932), which had allowed for a direct duty of 10 percent to be levied on a broad range of non-Empire imports (Jacks 2011, 10). That would also apply to Empire products after November 1932, if nothing were agreed upon at the Imperial conference. However, sufficient progress was made so these provisions

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3 W. Nash added, "The victory of the Labor Party...was partly due to their election promise 'to ensure the payment to the farmer of a price for his production that would cover all his working expenses and secure to the farmer an income in accordance with the time, skill, energy and experience used by him in producing the commodity'" (quoted in Rosenberg 1959, 243).

4 The full name of the Primary Products Marketing Act is "An Act to make better provision for the marketing of dairy Produce and other primary products so as to ensure for Producers an adequate remuneration for the services rendered by them to the community."

5 This did not mean, however, that farmers were always satisfied. By 1938, the government was basing the price paid more on market conditions, much to the chagrin, rising anger and disappointment of farmers.

did not apply. Indeed, British Preference remained, largely because of the activities of farmer groups from the United Kingdom and the dominions. At the Ottawa conference, Sir Thomas Baxter of the National Farmers' Union of England and Wales, an unofficial member of the UK delegation, had been instructed "to immediately get in touch with our brother farmers from the Dominions, to appeal to them to present to our Ministers a united case...to get the greatest possible preference over the Foreigner...and to get this one acknowledgement: The Home producer is entitled to the first place in his own market for all he produces; that the Dominion farmer should be entitled to second place, and the foreigner to third place" (National Archives of the United Kingdom [NAUK] 1933b).

That did happen and New Zealanders, in particular, were elated, given their economic dependence on agricultural exports to Britain. The duty on foreign butter was raised from 10 percent *ad valorem* to a fixed amount of 15/- per hundredweight, and the duty on cheese from foreign sources was raised from 10 to 15 percent. The dominions were also guaranteed a free market in the United Kingdom for three years. However, by October 1932 (a mere two months after the conclusion of the Ottawa negotiations), the price of butter and cheese in Britain collapsed, the result of unregulated imports from Empire countries of which New Zealand was a particular offender. As a result, London wanted a quick revision of that section of the Ottawa Agreements, demanding the dominions accept a quota that they could not exceed in terms of exports of dairy products to the United Kingdom. Britain itself had established a Milk Marketing Board for England and Wales in September 1933, approved by almost 100 percent of affected dairy farmers, designed to increase dairy farmer incomes by raising prices. It became a monopoly seller and did increase prices, much to the consternation of consumer representatives.<sup>6</sup> Its purpose was to help English and Welsh dairy farmers make ends meet through fluid milk sales in their own market.

And that is where they ran afoul of the Ottawa Agreements, at least in NZ dairy farmers' eyes. Sir Thomas Baxter's trip to New Zealand in October 1933 was to convince the latter of the necessity of reining in their exports to the United Kingdom. As he told a radio audience on the North Island, the British government was compelled "to regulate the supply of dairy produce from all sources by giving each supplying country a quota" (NAUK 1933d). Baxter was asking New Zealanders to cooperate, especially given the agreed upon wording of the summer of 1932 — that the home producer was entitled to first place in his own market. However, the envoy failed in his mission; as he told the UK minister of agriculture and fisheries, Walter Stewart, "there was little hope of New Zealand agreeing to reduce her exports of cheese to the United Kingdom" (ibid.; Steel

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6 For an interesting discussion of this, see Whetham 1978, 251–253.

2005, 186).<sup>7</sup> Nor did they. The NZ high commissioner in London told the UK's minister of agriculture and fisheries just that: It would be "highly unfair to New Zealand as the main supplier of cheese to the United Kingdom to be thus subjected to special treatment ...the New Zealand government is unable, in fairness to the Dominion, to assent to quantitative regulation of cheese alone" (NAUK 1933c). While some in the country began to talk up the potential lucrative markets for dairy that surrounded them in Asia in face of this British obstinacy, the inertia of NZ processors and middlemen was startling (NAUK 1933a).<sup>8</sup> These potential export destinations would only begin to be tapped by the early 1980s.

## WORLD WAR II AND ITS AFTERMATH — FOREVER ONWARD INTO THE UK MARKET

The Second World War put an end to NZ dairy issues. As their soldiers travelled overseas, so too did the country's agricultural products in ever-increasing volumes, supplying British consumers with food. The United Kingdom, so reluctant a few years earlier to leave New Zealanders with an open market, wanted everything the dominion could send by 1941. Indeed, the government entered into bulk purchase contracts with New Zealand for cheese and butter that were in effect from 1939 until 1955.<sup>9</sup> Wellington restricted New Zealanders' intake of dairy products through rationing in 1942, which remained in place until 1950. The stark and unalterable fact Britain confronted was that its reliance on imported calories accounted for about 70 percent of its food. Broken down by sector, that translated into approximately one-half of the meat citizens consumed, 70 percent of its cheese and 91 percent of the butter spread on bread in the United Kingdom. Of those totals, significant percentages were provided by New Zealand. Provision would have to be made for the continued flow of those vital commodities. Indeed, as the UK's minister for food, Frederick Marquis,

7 By 1935, butter and cheese were contributing 71 percent of New Zealand's total export earnings, all of it generated by sales to Britain. Little wonder the government was not anxious to reduce its access to the UK market.

8 Alex Tetzner, a member of the NZ Farmers' Union, told Baxter that "The slogan of the day is: *New Zealand has no alternative markets but Britain*, and the leaders of our dairy industry have spared no efforts, time and money to try to prove that only Great Britain can buy our dairy produce, the rest of the world, apparently, never knowing what butter and cheese are...I can assure you that good, free and open markets for dairy produce *do* exist in the Far East. These enormous markets are the nearest to us, and the easiest to exploit [all emphasis added]" (NAUK 1933b). An example of this commitment to Britain was seen in the headline from the February 13, 1979 edition of the *Financial Times*, "NZ Dairy Industry — UK the only outlet for butter sales" (NAUK 1979). See also Smith (2005, 347).

9 In the post-war era, Anglo-NZ negotiations resulted in a commitment by the British that prices would not vary by more than 7.5 percent from prices paid in the preceding season. This stipulation helped to keep the dairy industry on a more even keel for the decade following 1945.

Lord Woolton, noted in 1941, the Second World War was "a food war" as much as it was a fighting war.<sup>10</sup> New Zealanders could not have agreed more as London purchased every calorie they could export.

The post-war period did not bring much change to dairy producers as government guarantees remained in place. In 1947, the NZ government agreed to important changes in marketing and the method of fixing the guaranteed dairy price. This came about in part because of differences of opinion with respect to pricing that developed between farmers and government. First, a new tribunal was established to undertake the task, comprised of two industry and two dairy farmer representatives and an independent chairman. The second change was that the prime minister, Peter Fraser, wanted dairymen to participate directly in marketing. This represented wholesale change to what had gone on since 1936 — instead of sole responsibility for marketing and fixing the dairy price remaining with the government, an independent tribunal would now take on that role. In support of this objective, it passed the Dairy Products Marketing Commission Act (1947), which empowered the Marketing Commission to purchase all NZ butter and cheese for export and to regulate the local price for those two commodities as well. Despite this, Wellington still agreed to underwrite the price, which was quite an achievement by the dairy sector; in a sense, it was a case of "heads I win, tails you lose." At the same time, on-farm refrigeration was introduced, which made dairy products more secure, long-lasting and accessible.

This act was modified in the 1956 Dairy Products Marketing Commission Amendment Act. In fixing the actual payout to producers, certain principles were to be observed, including:

- The necessity in the public interest of maintaining the stability and efficiency of the dairy industry.
- The cost of the production of butter.
- The amount which butter and cheese acquired by the Commission realized.
- The ruling level of prices for farm produce other than dairy produce.
- The estimated cost to the Commission of marketing the butter or cheese concerned and the cost of administration.
- Any recommendation made by the Dairy Board.
- Any other matters deemed to be relevant. (Rosenberg 1959, 248)

10 A wartime ditty reflecting this sentiment went:

"Those who have the will to win  
Cook potatoes in their skin  
Knowing that the sight of peelings  
Deeply hurts Lord Woolton's feelings." (Sitwell 2012, 565)

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This act was passed just as dairy produce experienced a rapid fall in price, and the government blew through £25 million of NZDB reserves, as well as another £12 million that was borrowed from the Reserve Bank as a subsidy. The important part for the dairy industry was that government, even in such dire circumstances, was not prepared to let farmers fall upon the vagaries of “the market.” Regulation remained the guiding principle. As it happened, the price of butter rose dramatically in 1959, which paid off the 1957–58 deficit as well as providing a 1960 surplus that was distributed to farmers.

Further, Wellington passed the Dairy Board Act in 1961, conferring enormous power on its creation to the NZDB. As one critic has suggested, “it could do anything it liked as long as it wasn’t illegal” (Fox 2013, paragraph 4). Consisting of a board of 13 members, including two appointed by government, eight selected by NZ cooperatives and three by the NZ Cooperative Dairy Company, the NZDB was to cover all dairy products designated for export.<sup>11</sup> If a producer were to export from the country, that export would be done through the NZDB as it would purchase the milk from the producer before export, being a single desk seller of dairy products. Further, the act enabled it to work on the development of dairy in New Zealand, exhorting farmers to produce ever-larger amounts of dairy to supply the UK market.

## THE FAILURE OF THE GATT TO DEAL WITH AGRICULTURE

The role of the General Agreement on Tariffs and Trade (GATT), the organization that was established in 1947–1948 and which devoted itself to overseeing the orderly reduction of tariffs and other impediments to trade that had, or so popular wisdom believed, made the Great Depression that much worse, was to help facilitate the export of agricultural products. However, as events transpired, this seemed less likely. While it was intended that agriculture be covered in negotiations, it quickly became apparent that certain countries, the United States chief among them, did not wish it to be so. The United States had a heavily subsidized agricultural sector, made so by the exigencies of that same depression, and passed into law through the Agricultural Adjustment Act (1933), which paid farmers not to grow crops, and its sister legislation, the Agricultural Adjustment Act (1938), which provided price support to certain commodities. Following this, any international commitment entered into by the United States had to conform with Section 33 of these laws and the GATT agreements did not. Accordingly, the United States demanded and received a waiver of its agricultural obligations under the GATT in 1955. Given this toxic environment, New Zealand chose not to join in the commitments to cut manufacturing tariffs,

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<sup>11</sup> For the act itself, see New Zealand 1961.

“out of frustration with the unwillingness of other GATT contracting parties to commit to lowering their agricultural protection rates” (Anderson et al. 2007, 9). Agricultural trade to small, isolated and remote New Zealand was its lifeline.

In terms of overseas custom, that pretty much left the United Kingdom. Wellington pursued that market with great vigour and passion throughout the 1950s, rationalizing its effort in a 1959 Anglo–NZ trade agreement. That came about partly because of NZ imperatives; as a British note pointed out, “we are frequently reminded by the New Zealanders that the pattern of farming in that country was developed to serve the British market... Britain has a duty to safeguard the New Zealand dairy industry” (NAUK n.d.). Indeed, R. H. Wade, the deputy NZ high commissioner in London, noted on more than one occasion that, “United Kingdom production trends and British agricultural policy were a matter of considerable importance to NZ” (NAUK 1968). That was largely the result of the history of the two countries going back to 1882; the 1959 trade treaty merely made formal what had been practice. The agreement was renewed in 1965 and was to be extended until 1972, whereupon the United Kingdom was moving into the closing stages of its membership negotiations with the EC. The two also began a series of meetings that were convened under Article 10 of the 1959 agreement, which provided for full discussion between them on “their agricultural production and marketing policies, the food import policy of the UK government and other related matters” (NAUK 1970a). These gatherings were important, in particular to the NZ side, as exports of their butter and cheese to the United Kingdom accounted for 60 percent of total export earnings, even into the 1970s (NZDB 1971; NAUK 1970b; New Zealand National Archives [NZNA] 1965).<sup>12</sup> Given this situation, it was clear that New Zealand would react bitterly to Britain’s May 1967 application to join the European Economic Community (EEC). It had settled all its butter and cheese in that one market basket and was loathe to watch it melt away.

However, London did proceed with membership, while also working to keep NZ dairy on the EC agenda. Protocol 18 was the result, where NZ butter and cheese were granted privileged access to the British market for a period of five years, ending on December 31, 1977. It also stipulated the maximum quantities of those two products that New Zealand could export to the United Kingdom at a fixed price, which was calculated using the average of

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<sup>12</sup> As the NAUK 1970b document notes, “approximately 90% of all New Zealand butter exports come to this market and approximately 80% of her cheese exports. New Zealand has tried hard to develop new markets but there are very great problems in this.” New Zealand tried to cultivate markets in both Canada and the United States. With respect to the former, “there remained a basic objection to a [Canadian] protectionist policy which virtually excluded imported dairy products from the Canadian market” (NZNA 1965) to which the New Zealanders vigorously objected.

prices over the years from 1969 to 1972. Protocol 18 was eventually extended to 1980 for butter, but not for cheese; the situation was clearly untenable and NZ exporters worked diligently to find alternative prospects.<sup>13</sup> In this, they were at least partially successful: in 1960, Britain had taken about 53 percent of NZ's exports; by 1976, that figure had fallen to 19 percent (Lodge 1978, 303).<sup>14</sup>

## CLOSER ECONOMIC RELATIONS AND RESTRUCTURING THE NZ ECONOMY

But without the UK market, Wellington was left floundering. There was some talk of New Zealand "taking on for two or three years the EEC 'at their own game' and out-competing [them] (with export subsidies as necessary) in third country markets" (NAUK 1969). That resulted in a producer support estimate, the measure of government subsidy to farmers, by 1983 that approached the EC level (Harris and Rae 2004, 3). The general context in which this downward spiral had occurred also led to the signing of the Closer Economic Relationship (CER) with Australia in 1983.<sup>15</sup> That process had begun in 1978, following on from the 1965 NZ–Australia Free Trade Agreement, when the NZ deputy prime minister, Brian Talboys, met with the Australian prime minister, Malcolm Fraser.<sup>16</sup> They agreed that the Tokyo Round of GATT negotiations was not yielding results commensurate with their effort in the area of agriculture. "Australia and New Zealand," they noted, "regard improved world trading conditions for agriculture as an essential ingredient of a satisfactory outcome to the Multilateral Trade Negotiations...there is a pressing need for substantially improved access for agricultural products into the markets of the major industrial countries" (Australia 1978). That did not happen as the Tokyo Round discussions wound down, and agriculture was still not a part of the agenda, but would be almost a decade later as the Uruguay Round, the last held under the auspices of the GATT, was convened in 1986.

However, Australian dairy farmers were not entirely keen to get involved with their NZ counterparts through a CER agreement, fearing that they could not compete. The executive director of the Australian Dairy Farmer's Association noted:

The Government, through yourself, the Prime Minister and the Minister for Primary Industry, has given the dairy industry an unequivocal commitment that:

- Consultations will take place between the industry and the Government before any agreement on dairy products as part of the Closer Economic Relationship with New Zealand.
- No arrangement will be entered into that will result in disruption to Australia's domestic marketing arrangements for dairy products.
- The Australian dairy industry will not be disadvantaged by unfair competition from New Zealand. (Australia 1982a)

That seeming hostility arose in part because of the different natures of the Australian Dairy Farmers' Federation and the NZDB. Australians found competing with New Zealanders difficult because of the evolutionary track of the two countries' industries. The former's was not as homogeneous as the latter's, being split geographically and plagued by problems that arose out of federal/state relationships. As well, the Australian Dairy Corporation (ADC) was a regulatory body and had changed considerably over the 1970s and 1980s. Prior to that, it had been producer-dominated, so the NZDB and the ADC had often adopted common approaches to issues, but by the early 1980s, the ADC was dominated by the non-producer element.

Further, the NZDB had a plan that it hoped to realize through the CER — to remove Australian dairy from the export scene. As was happily pointed out in a meeting between Charles Patrick, an architect of the Dairy Board's international trading policies and its network of markets and several NZ officials, the Australians were now "virtually out of the butter market internationally and were phasing out of the casein market" (Australia 1981). Patrick also did not want to push the Australians on the dairy front in the CER — while it was a matter of political judgment, he thought his industry "would get further just working in with the Australian industry." The NZ side should not push things but should "wait for the plum to fall" (ibid). It took longer than anticipated for that plum to become available as the "Memorandum of Understanding on Dairy Products" placed constraints on NZ's ability to flood the Australian market with milk: "Special circumstances apply to the institutional arrangements of the dairy industries in the two countries that would result in *unfair and unreasonable disruption to the Australian dairy industry* [emphasis added] in the event of any relaxation of the formal and informal arrangements that now control trade in dairy products. Because of the serious disruption that would inevitably result from greater New Zealand access to the Australian domestic market, the current agreements between the two dairy industries should be

13 That sentiment was echoed during a European Parliament debate in March 1977 on butter surpluses and their disposal. As was then pointed out, "the maintenance of dairy imports from third countries, in particular New Zealand, was creating 'an untenable situation'" (Lodge 1978, 308).

14 This said, Britain still took 80 percent of New Zealand's butter exports.

15 An excellent archival record of the talks that led to the CER are available online, posted by the Australian government. They can be found at [www.dfat.gov.au/publications/historical/volume-21/](http://www.dfat.gov.au/publications/historical/volume-21/).

16 For an account of the evolution and effect of the NZ–Australia free trade agreement, see Hoadley 1999.

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formalized at government level” (Australia 1982b). In the end, dairy was placed on the deferral list, which pushed off the rigours of competition between the two sides until 1995.

However, the CER could not right the dislocation experienced by New Zealand with the loss of the UK market, nor could it help in terms of allowing Wellington to continue to subsidize dairy. By 1984, with nothing left in the budget and the country spiralling downward in economic rankings, the newly elected Labour government of David Lange undertook draconian change, embarking on a free trade policy for agriculture among other areas. The new government was responding to a number of macroeconomic problems that had become acute, as well as “heavy selling of the New Zealand dollar, which threatened to exhaust the country’s foreign reserves” (Harris and Rae 2004). The Labour government’s major reform program helped in terms of realigning agriculture with its primary base of support in the cities — farmers were left outside of the consultation process. It was so successful in its declared objective that, by 1993, the producer support estimate had fallen below three percent of gross farm receipts from the 35 percent it had reached in 1983 (ibid.).<sup>17</sup>

Nothing was left untouched by the Lange government. The NZDB was stripped of its subsidies, although the new Labour administration left in place the NZDB’s authority to serve as the country’s single desk exporter of manufactured dairy products which, as events transpired, was critical to the rise of New Zealand as a dairy superpower. That power had been conferred in 1961 by an act of the NZ Parliament, and had evolved from serving as an exporter for about 180 cooperatives in 1961 into the exporter for 14 co-ops by 1996 (Dobson 1997, 1). In 2001, Fonterra, the mega-cooperative, was established to market NZ dairy through the merger of two co-ops, the NZ Dairy Group and Kiwi Cooperative Dairies, with the NZDB. In the meantime, however, the NZDB’s strategy was to increase exports of specialized, value-added products, increase sales through foreign subsidiaries and diversify across products and countries (Dobson 1990, 547). A new era in NZ dairy had been launched, just in time for the announcement of the Uruguay Round, the last of the freer trade rounds under GATT.

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17 Reform was also visited on other sectors, including “a 20 percent devaluation of the NZ dollar, and removal of financial and exchange market controls in 1984 and the floating of the dollar in 1985. Export assistance was removed, tariffs were progressively lowered across the board and import controls dismantled, all with the objective of increasing international competitiveness...the labour market was deregulated in 1991. The public sector was downsized, and commercial activities of government were corporatized or privatized (including agricultural extension)” (Harris and Rae 2004, 3).

## THE URUGUAY ROUND, 1986–1994

The year 1986 was “one of the worst in the history of the New Zealand dairy industry” (NZDB 1987, 5). That was caused by “a bleak market outlook, a dollar which was continuing to drain the life blood from exporters, high inflation and competitive interest rates,” which meant that farmers were in for “severe difficulties and, at worst, financial disaster”(ibid.). The GATT negotiations could not have come at a better time, at least from the NZ perspective. Dependent on dairy exports and working through their own major reform process, Wellington was anxious. As the government well knew, prices on the international dairy market were not set by the flow of market forces or by supply and demand factors. In large part, they were determined by government-financed export subsidies and from protected and segregated dairy markets located largely in the northern hemisphere. As the NZDB lamented, “Northern hemisphere over-production and the inelasticity of markets had the inevitable consequence of collapsing international prices and creating surpluses which stood in the way of the Board’s every effort to sell” (NZDB 1989, 4).<sup>18</sup> Tightly restricted market access and the willing use of export subsidies were the basic features of the international dairy trade.

New Zealanders hoped that an improved international mechanism to control the level and frequency of export subsidies would emerge from the Uruguay Round. Indeed, the limitation of subsidies on agricultural exports, along with improved market access, were the two fundamental aims of the Round’s discussions in the agricultural sector, placed on the agenda by the major exporters of those commodities. Wellington believed that what was achieved in the GATT Round in those two areas could have a major impact on the country’s prosperity over the coming years. This intent also led to the establishment of the Cairns Group in 1986, comprised initially of 14 countries including Australia, Canada and New Zealand, but not those of the European Community or the United States. The purpose of the Cairns Group was to take on the wildly excessive subsidies that had smoothed the road along which the European Community and the United States pushed their agricultural goods out into global markets. By 1992, there was some evidence that “the world [was] inching away from the use of agricultural subsidies,” or so the NZDB believed (NZDB 1991, 3).

However, the results of the Round did not promise new markets. As was pointed out, “The overall level of trade in milk and milk products is not expected to be affected by the Uruguay Round,” although there was the belief that there “would be some redistribution in terms of region of origin and destination” (UN 1995, 46). New Zealand, the

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18 Following six dismal years for NZ dairy farmers, 1989 was the first where prices firmed and northern hemisphere surpluses dried up.

UN Food and Agricultural Organization believed, would be better off: “Output [in that country] is particularly sensitive to changes in international conditions, as over 80 percent of milk production is exported” (ibid.). While the country may have benefited somewhat, it did not change the context in which dairy exports occurred. Indeed, the dynamics of the Uruguay Round differed little from those prevailing during previous GATT rounds — they reflected the economic power imbalance in the world, and involved dialogue (and disagreement) primarily between the European Union and the United States. Little attention was paid to those that were agriculture-exporting smaller powers, such as Argentina, Australia, Brazil, Canada, Indonesia, New Zealand and Thailand, which mirrored past practice. Indeed, as one critic has noted, “it is obvious that real liberalization was not achieved” (Meyers 1996, 2). Any talk of eliminating trade distorting practices had dried up by the time the Dunkel Draft was submitted in December 1991, and these watered-down resolutions were further diluted by the Blair House Agreement of December 1992 (DeRosa 1992, 756).<sup>19</sup> By the time the Uruguay Round Final Act was agreed to a year later, any hope of a significant agreement in terms of mitigating the effects of trade distorting practices was “reduced to grudging concessions four years later” (ibid.).

By 1997, New Zealand was aware of the unrequited hopes of the Uruguay Round. Still, the country’s Dairy Board embraced what it called a new era: “In the past, the state of the international market and the business environment in which the Board operates has been governed — more or less exclusively — by the size of the European surpluses of butter and milk powder and by the volumes of butter the central planners of the old Soviet Union might, or might not, choose to buy” (NZDB 1997, 8). In this new world, EU surpluses were much reduced and their stockpiles did not hang “menacingly over the market” (ibid.). The USSR no longer existed, having imploded in 1991, but other markets did, and NZ milk was pouring into regions such as the Middle East and Latin America. Wellington also placed some emphasis on the new trade rules as established by the recent GATT round, of tackling the old bogey of the international dairy business — the use of export subsidies to dispose of surpluses generated by the protection and support policies of the major producers. This optimism, however, did not blind New Zealanders to the continuing practices of the European Union and the United States of manoeuvring “to avoid their [Uruguay] commitments”

<sup>19</sup> The Dunkel Draft, named after the managing director of the GATT, presented “a comprehensive draft of the final Uruguay Round agreement to the negotiating parties in December 1991. The draft attempted to forge a consensus around the elements agreed to in other areas of the negotiations, plus several elements proposed by the GATT Secretariat for concluding the hapless negotiations on agricultural trade” (DeRosa 1992, 756). For the Blair House Agreement, see Meunier 1998, 201–203. It provided for a 20 percent reduction in internal EU price support over six years, while also promising a reduction in export subsidies by 21 percent, among other results.

(ibid.). Protectionism, or so the NZDB believed, was not “an easy addiction to break.” And so it proved to be.

## THE BIRTH OF FONTERRA

The Dairy Board’s musings on a new era were also germane for another reason — Fonterra, the mega-cooperative born from the merger of Waikato’s NZ Dairy Group, Taranaki’s Kiwi Dairies and the Dairy Board, came into existence in October 2001. It was in some ways “a miracle,” given the distrust that characterized relations among the various entities, including the ousting of the NZ Dairy Group’s chair, John Storey, in a dairy farmer vote taken in 1999, which resulted in the concomitant loss of his Dairy Board chairship (Lind 2013). A part of the act that established Fonterra provided for, “the transition of the NZDB to a wholly-owned subsidiary of the new co-op and its conversion into a company 12 months after the commencement of this Part” (New Zealand 2001, section 1.4(b)). The momentum for this particular development had come several years earlier with Dairy Board Amendment Act (1996) having transferred ownership of all Dairy Board assets to what were then New Zealand’s 12 cooperatives.

It was also a time of upheaval for the industry, following closely on the heels of the Uruguay Round. Indeed, the Dairy Board, now on cooperative books, lost its statutory support, in theory opening up the export trade. John Storey, then the chairman of the NZ Dairy Group, quite correctly noted that, “we can no longer sit back — as we have sometimes done in the past — and leave the Board to carry the responsibility of its performance” (quoted in Ferrier 2004, 23). These pressures, at least according to Andrew Ferrier, Fonterra’s CEO from 2003 to 2011, were “the pivotal point in the development of the modern dairy cooperative” (ibid.).

And develop it did, despite an initial flirtation with the United States in terms of negotiating a free trade agreement. Then prime minister, Jennifer Shipley, suggested that she would have a “serious engagement concerning the Dairy Board in the context of FTA [free trade area] negotiations” (US Congress 1999).<sup>20</sup> She told the board “it should step out of this framework” and that if a free trade agreement with the US was forthcoming, she would “deal with legislation forthwith concerning the agriculture boards” (ibid.). Both sides could also agree on the European Union’s “abuse of the [global trading] system” and its “regionalism” (ibid.). But that romance fizzled; as the NZ trade minister, Lockwood Smith, noted to visiting Americans, “if an agreement is not concluded in 1999, it would be difficult to move even in New Zealand because of its own elections” (ibid.). And so it was. The National Party government fell

<sup>20</sup> Later in the meetings, John Luxton, the minister for food, fibre, biosecurity and border control, stated that if a free trade area was negotiated, “New Zealand would eliminate the Dairy Board very quickly” (US Congress 1999).

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in the December 1999 election giving Labour, under Helen Clark, control of the legislature. NZ-US free trade died because of changed NZ priorities and the US inability to secure trade promotion authority from Congress. However, it is clear that the Americans recognized the dangers posed to their dairy industry of the single desk exporting system employed by New Zealand. The latter acknowledged that to sign an agreement with the United States, it would have to move away from that system, the issue that was to plague the two in TPP negotiation a decade later.

## **DOHA ROUND OF THE WTO, NOVEMBER 2001**

The Doha Round of the new WTO was agreed upon to deal with issues surrounding the rather lacklustre observance by the European Union and the United States of rules relating to agriculture implemented during the previous Uruguay Round. As well, it focused on trade relating to the Global South, those countries that had, in times past, been called “developing” but which were now of sufficient size and influence so as to exert influence on the process. These included what became known as the BRICS – Brazil, Russia, India, China and South Africa, a term coined by the economist Jim O’Neill in his book *Building Better Global Economic BRICS*. This focus on trade with the Global South was the reason why it was colloquially named the development round. For New Zealand, the critical objective was a “rules-based, open and non-distorted world market [for agricultural goods] — the reduction of market access barriers and trade-distorting domestic support, and the elimination of export subsidies” (Armstrong 2003, 121). That targeted primarily the European Union and the United States, as they accounted for 60 percent of the dollar value of Organization for Economic Cooperation and Development agricultural support, as well as 80 percent of subsidies (Elliot 2006, 31).

Ultimately, the challenges presented by Doha proved to be too onerous to be appropriately addressed. The European Union and the United States would not agree to lower their support of agricultural products, while the other track, international development, had largely dropped off the agenda following the Cancun meeting in Mexico in September 2003. However, that negotiation is more (in)famous because of the complete breakdown of the Doha Round over the issue of EU and US domestic support for agriculture. By 2005, in Hong Kong for continuing Doha negotiations, the Labour government’s trade negotiations minister, James Sutton, claimed that “the international trading system is facing one of the most severe crises in its almost 60-year history,” while the US trade representative, Robert Portman suggested that Hong Kong represented “a once-in-a-generation opportunity” (Sutton 2005). Michael Moore, New Zealand’s ambassador to the United States and soon-to-be managing director of the WTO, noted,

“We just can’t seem to get the political stars to align at the moment” with respect to Doha (Moore 2011, 1).

Hong Kong became synonymous with failure. The Indian minister of commerce, Kamal Nath, remarked some months later that, because of the meeting, Doha “was between intensive care and the crematorium” (Wilkinson and Lee 2007, 4). However, it did initially seem poised for some success; as has been pointed out, the run-up was “qualitatively different from that which has preceded Seattle and Cancun. [There was] a willingness to keep moving forward with negotiations, ‘despite the persistence of significant differences was in evidence’” (ibid., 7). Agriculture was the straw that broke the proverbial camel’s back, and it turned out to be key in the discussions, especially in terms of the European Union and United States making commitments to phase out export subsidies. The former was not keen to do so unless countries from the Global South opened their market for services and eased the way for EU industrial products to be permitted free entry into those countries. France, in particular, “would not allow the negotiation round to come down to a ‘Yalta of agricultural markets’” (Meunier 2006, 1).

Further, the European Union and the United States continued to express their distaste for single desk exporters, whether in the private or public sectors. The Australian and Canadian wheat boards were highlighted, as was Fonterra. Indeed, so seriously did Europe view this issue that the European Union’s agricultural commissioner, Mariann Fischer Boel, visited Australia and New Zealand in March 2006. While in the latter, she criticized the country’s dairy arrangements as being counterproductive, and that it should end Fonterra’s monopoly over access to export quotas (Wilkinson and Lee 2007, 179). At the same time, Europe maintained high tariffs in favour of dairy producers, perhaps a reflection of its structural milk surplus and the economic marginalization of its dairy farmers.

As for the United States, prior to Hong Kong it had tabled a two-step proposal that claimed to provide a path forward in terms of eliminating agricultural trade barriers, in particular tariffs and export subsidies, over a five-year period. This would be followed by a five-year hiatus, to be followed by a second stage, during which all tariffs and subsidies would be eliminated. This did not happen, but an agreement to end all dairy export subsidies by 2013 did. This was also a substantial concession on the part of the European Union, as about 90 percent of all export subsidies used by WTO countries originated there (Jesse and Dobson 2006, 13). In the end, however, it was much ado about little; the Hong Kong ministerial meeting broke up with little accomplished.

## NZ BILATERALISM, AS ALL ELSE FAILS

This brief account of Cancun and Hong Kong are necessary in order to contextualize New Zealand's way forward — to negotiate free trade agreements with willing partners in the Asia-Pacific region. Most importantly, this involved China, with which discussions began in December 2004, leading to an agreement in April 2008. As the then minister of trade, Philip Goff, noted, “the Free Trade Agreement with China [was] one of [his] most important achievements for New Zealand” (Goff 2013). Trade did increase substantially between the two following 2008, from NZ\$2.2 billion in 2002 to NZ\$8.6 billion by 2012, and dairy was an important part of that increase, accounting for NZ\$2.8 billion of the export total (Barber 2014).

This activity also led into other areas — primarily, but not exclusively, an expanded TPP. It had started off as the Trans Pacific Strategic Economic Partnership Agreement, signed in the summer of 2005 among Brunei, Chile, New Zealand and Singapore. On November 14, 2009, the United States announced its intention to enter into negotiations with the so-called Pacific 4, and the number of countries involved increased dramatically, as did the combined GDP represented by the potential agreement. The TPP has been touted as a twenty-first century “living agreement” in that it will be subject to constant revision and will dive deeply into each participants' more cherished sectors to open them up to competition. As the University of Auckland's Jane Kelsey (2011) has pointed out, “a lot of attention has centred on agriculture, and it is a crucial issue in the negotiations, but it is not the centerpiece of the TPP. This is no ordinary ‘free trade’ deal...[and] negotiators meet in 21 working groups that range across business mobility, customs, competition, cooperation, e-commerce, environment, financial services, horizontal issues, government procurement, investment, intellectual property, labour legal issues, market access, rules of origin, sanitary and phytosanitary measures, technical barriers to trade, telecommunications and trade remedies.” Finally, of some importance to the potential success of the TPP, Kelsey has suggested, with the weight of history on her side, that “Congress will never approve a TPP agreement if it requires any significant new liberalization from the US and if it does not contain major new concessions from its negotiating partners” (ibid.) And the Americans seem to have targeted the revision and breakup of Fonterra as one such major new concession.

New Zealand helped to set the agenda early on, given its prominent position from the outset. Of primary interest to Wellington was the removal of impediments to trade in dairy products, particularly in the United States whose dairy farmers resisted. As other, more protectionist minded countries such as Japan have entered the TPP negotiation process, this became even more problematic. Fonterra went on record as insisting that it would not support an agreement that did not eliminate tariffs and restrictions

on agricultural and particularly on dairy products (“Food Producers Take TPP Tariff Stand” 2014). Similarly, the NZ prime minister, John Key, emphasized in late 2012 that his country would not “sign up to the Trans-Pacific Partnership free trade deal unless it includes an agreement to progressively abolish tariffs on agricultural products exported to North America” (“No TPP Deal” 2012).<sup>21</sup>

For their part, US dairy producers took direct aim at Fonterra and its degree of market control, especially given New Zealand's precisely articulated demand to obtain greater access for its dairy products in the United States. A letter from the American National Milk Producers Federation to the Secretary of Agriculture, Tom Vilsack, and the US Trade Representative, Michael Froman, laid out the case. Strong concerns remained among American dairy farming and manufacturing constituents about the impact of expanded NZ-US dairy trade on the country's dairy sector if major reforms were not undertaken by New Zealand. The letter noted that:

It is our understanding that New Zealand has resisted considering meaningful reforms to its dairy sector policies. Those policies include special legislation to permit exorbitant market concentration by one company and exclusive access for that same company to the country's export licenses that lasted for several years. Taken together, these government policies have yielded the concentration of roughly 90 percent of New Zealand's milk supply into the hands of one company which in turn dominates over one third of global dairy trade. Dairy producers and processors in our states are deeply concerned that this government policy provides New Zealand with a tremendous advantage in global markets and believe strongly that it must be effectively addressed as a precursor to any expansion of U.S.-New Zealand dairy trade in TPP. (US Congress 2013)<sup>22</sup>

US dairy farmers would be “crushed by unfair trade deals that threaten their ability to recover their costs of production,” or so offered Ben Burkett, a Mississippi farmer (Lawson 2013). One American commentator has correctly

21 Later in the interview, Key mentioned that he believed New Zealand could “get dairy in there in a phased way over the next ten years” (“No TPP Deal” 2012). That brought the swift rejoinder from commentator Bernard Hickey that that would be “a problem because the longer time we take to get dairy in there, the greater chance that the corporate lobbyist in America, who are very closely aligned with the US government on this, to block Fonterra from getting into America” (Hickey 2012).

22 On the other hand, Tom Suber, the president of the US Dairy Export Council, pointed out that his industry “sees real value in the TPP negotiations if we are able to open new markets like Japan and Canada, use the TPP process to strengthen global trading rules and secure meaningful competition policy changes in New Zealand's dairy sector” (National Milk Producers Federation 2013).

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observed that, “there are a lot of areas where the US wants everyone else to change, but doesn’t want to change much itself” (Pilling and Donnan 2013).<sup>23</sup> In short, the United States is seeking protection from New Zealand’s much more nimble, low-cost, grass-fed, concentrated and flexible dairy sector even as it goes after international markets that take market share away from Fonterra. US dairy is surging in international markets while DairyAmerica, a large marketing cooperative based in the country, has ended its 13-year relationship with the NZ company to export skim milk powder, in order to do so itself. US dairy exports were worth almost US\$7 billion in 2013, up 31 percent from the previous year. On a volume basis, in terms of kilograms of milk solids, the increase was 19 percent (Foreman 2014). As well, China is anxious to diversify its sources at Fonterra’s expense. Indeed, while the company has put the best face on it, the trend can only be alarming as Americans and Europeans are gearing up to access the East Asian country’s market for whole milk powder, digging directly into Fonterra’s market (Jourdan and Tajitsu 2013). American farmers are desperate to continue to exploit this possibility behind their protective walls of tariffs and tariff rate quotas.

New Zealand persists in the TPP negotiations with the increasingly forlorn hope of greater access to the US dairy market, despite the obvious fact that that will not happen. The United States is an intense competitor in overseas markets, and likely to become more so. However, New Zealand has not put all its cheese in one basket, as was so clearly the case in times past with the United Kingdom. In 2007, for example, Wellington began investigating with India the feasibility of a free trade agreement between the two, while in 2009 it undertook negotiations with South Korea designed to lead to a free trade agreement, although those discussions have run up against Seoul’s unwillingness to fundamentally alter its agricultural protectionism (New Zealand 2013). As well, in early 2009, New Zealand, along with Australia, signed a free trade agreement with the ASEAN block of 10 countries, while in March 2010, Wellington inked the NZ–Hong Kong, China Closer Economic Partnership Agreement, the first that Hong Kong has signed with any country other than mainland China. This was followed in July by an agreement with Taiwan, which the New Zealanders carefully call Chinese Taipei. Finally, in terms of Asian agreements, since November 2012, New Zealand has been involved with 15 other countries in discussions that will give shape to the Regional Comprehensive Economic Partnership (RCEP), with an agreement to be signed by the end of 2015. This includes the regional economic heavyweights, China and India.

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23 The quote is from Jeff Schotte of the Peterson Institute in Washington, DC.

This short list demonstrates NZ’s rapidly increasing economic engagement in the Asia–Pacific region and its growing distance from the countries with which it used to be intimately connected, those of Western Europe, the United Kingdom and the United States. While ties of history, culture and language tend to bind countries closely together, increasingly tight market relationships perhaps do the same, but more intensely. So, does New Zealand require the US market for its dairy business to remain viable or growing? As analyst Bernard Hickey suggests, the answer to that is “no.” He noted on New Zealand’s *RadioLive* that the country should not “spend so much time and effort building this Trans Pacific Partnership when our real effort should be in Asia” (Hickey 2012).<sup>24</sup> Increasingly, focused effort is in that region; New Zealand is not able to increase its shipments of dairy products to the United States because of commitments elsewhere in Asia, resulting in a lack of capacity. As well, it is highly unlikely that the United States will liberalize its agricultural markets to the satisfaction of its negotiating partners, hewing to a position not dissimilar to that of Japan, even as it vastly increases production for export, largely of whole milk powder to China. Washington has publicly mused on somehow expelling Japan from the discussions, or signing an agreement without it because of its refusal to open its five “sacred” commodities to international trade.<sup>25</sup> However, as Dan Ikenson, the director of the Centre for Trade Policy Studies at the right-wing Cato Institute, tweeted in February 2014, “given the US logic about closed markets, it would make more sense that the US should sit out the TPP” (Kelsey 2014).

Should the TPP negotiations collapse, which seems more and more likely given its dysfunctional internal dynamics made worse by the fact that the Obama administration has not secured trade promotion authority, New Zealand would not necessarily notice any adverse effect in its dairy products trade, the country’s most important export sector. The much vaunted US policy shift, its so-called “pivot to Asia” has already been accomplished by New Zealand in a relatively short time. As the trade negotiations minister, Tim Groser, noted in a speech in October 2013, “We prospered between 1880 and 1970 in an Anglo-Saxon dominated world. This is a very different world we are entering” (Smellie 2013). He could just as easily have said “entered.” Arguably, RCEP, despite its limited reach as compared with the TPP, is more important to New Zealand’s future well-being. While Groser insists that a TPP failure or a NZ withdrawal from negotiations

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24 The focus of New Zealand’s TPP effort is on the United States and accessing its dairy market.

25 The five areas include dairy, wheat, rice, beef and pork and sugar. There is no consensus in the government of Japanese Prime Minister Shinzo Abe that the country should acquiesce to US demands. See (“At odds with US” 2014).

would be a folly of “historic proportions,” the evidence would suggest otherwise.

## CONCLUSION

NZ dairy, at one time or other, has covered almost every possible model of dairy industry organization over the past century. That it has now determined the best way for it to move forward through Fonterra is unquestionable. Dividend payouts dwarf milk receipts and, as global prices look set to remain in the NZ\$6–7 per kilogram of milk solid range with the odd foray into the heights of NZ\$8, the former will continue to yield significant returns to dairy farmers. Undoubtedly, they have capitalized on their low-cost regime, with which more expensive northern hemisphere venues cannot compete. Blessed with ample grasslands and a temperate climate, cows remain outside the year-round with no necessity for expensive barns or feed stocks that cows need over a harsh winter. It is the perfect system for NZ farmers. However, it would not work elsewhere; New Zealand has not so much a comparative advantage as a geographic one.

Further, Fonterra was created from unique circumstances, emerging from the amalgamation of two large dairy cooperatives and the NZDB, which itself had been given monopoly powers as a single desk exporter in 1961. And while the country remains primarily a dairy exporter, along with some lamb, wool, kiwifruit and forest products, its markets have diversified from necessity, from the United Kingdom, which used to take up to 80 percent of all NZ exports of agricultural produce, to a number of customers in East Asia and the Middle East. Indeed, the United Kingdom now absorbs a negligible percentage of NZ exports of dairy, while China has become the overwhelming source of Kiwi prosperity. In short, New Zealand remains true to its origins as a farm-based economy in the South Pacific determined to maximize its comparative advantage with states in the Asia–Pacific region.

In a way, New Zealand has become a victim of its own success, with the most efficient dairy industry in the world. As noted, other countries are unable to compete based on their climate, feed availability or their lack of dominance in the global dairy economy. If they have a viable industry of their own that can satisfy the requirements of their citizens, they are unwilling to consider competition with Fonterra because they cannot do so effectively without the use of government programs involving subsidies or tariff rate quotas, which block much of a national market through the use of very high tariffs once a certain threshold of imports has been reached. They are right to be frightened of that scenario. Dairy is an industry where about 50 percent of consumption is done locally in the form of fluid milk, which makes measures to support it justifiable. The spillover protectionist effect is into milk powder, which has a longer shelf life and is more easily transported. This is the fact that Fonterra and the NZ government, oddly

enough, do not seem to understand, focused as they are on battering down all resistance to the spread of their dairy gospel in selected markets. However, neither the European Union nor the United States will liberalize their milk markets to a competitor such as New Zealand. As well, the TPP is bound for failure, the result of American arrogance and exceptionalism and Japanese resistance, which will leave Wellington’s policy in tatters. It will be left to the likes of DairyAmerica and its increasingly focused export crusade to East Asia to put dents into Fonterra’s ambitions, presumably with the help of the US government, as conditions warrant.

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