

Summary of a hearing with the National Farmers Union

Background

1. The National Farmers Union (NFU) told us that it was the largest farming organization in England & Wales, providing professional representation and services to its farmer and grower members. Its membership comprised full-time professional farmers and growers and a smaller proportion of part-time farmers and growers.
2. The NFU had eight regional offices, one in Wales and seven in England, and 280 local branch offices. It was a democratic organization. It had extensive committees around the country, including sector boards (for example, dairy and poultry), so all its members had the opportunity to express their views. The NFU sought information from members who had experienced difficulties in the food chain; however, because its members were sometimes reluctant to talk about these issues, few members made formal complaints.

Supplier relationships

3. The most common complaints received by the NFU related to up-front payments and overrides. More cases were being reported as a result of increased general awareness. More complaints were received when supermarkets were experiencing difficulties and so were exerting pressure on NFU members.
4. There were other complaints, such as suppliers being told that if they wanted to deal with a certain retailer they had to use labelling from a specific supplier, or had to use a certain haulier. Some members had been told to use labels from companies which were more expensive than the same quality labels which they could source elsewhere. This added a cost which was totally unnecessary. Sometimes farmers were asked for money retrospectively for promotional campaigns, and might also be asked to accept a reduction in the price of the product that had already been agreed. Another complaint related to the practice whereby suppliers were asked to assist with stacking shelves. In addition, suppliers were sometimes asked to provide prizes for promotional events. Suppliers did not think this should be part of the relationship that existed for selling their products.
5. The NFU told us that food was different from the supply chains of other industries in that it had a relatively small number of very large retailers at one end, a larger but still relatively small number of quite big processors and a large and disparate farming population at the other. The top four grocery retailers (ie Tesco, Sainsbury's, Asda and Morrisons) accounted for 70 per cent of the market and had a fixed number of outlets, so farmers could only grow by being sharper in their business dealings. The UK market was imbalanced in many sectors. There were farming co-operatives in a number of sectors which were relatively small and did not have much influence. Farm shops sold direct to the public but were generally small to medium-sized businesses. The NFU was pushing hard for regional and local sourcing, the development of local farm outlets and a public procurement policy that bought locally. However, the fact remained that three-quarters of the market was controlled by the top four grocery retailers.
6. The vast majority of the farmers the NFU represented dealt with retailers through an intermediary. It was very difficult to pass on additional costs or price pressure squeezes that occurred within the supply chain. New entry had also caused a new wave of pressure for farmers. However, it was difficult to persuade these farmers to

come forward and provide details of their concerns because they feared losing business.

7. The NFU had a good relationship with the retailers. It operated in a very competitive dynamic market and understood the need to be efficient to succeed. It was anxious to ensure that the market functioned well, enabling its members to be successful suppliers to the retailers. It did not want to undermine the position of British consumers. However, its members had experienced what it considered to be poor behaviour by a number of retailers and processors, and had concerns about the long-term sustainability of some of its sectors. In the short term there was an environmental cost and potentially a cost to local infrastructure and employment. If the infrastructure was undermined, so would long-term skills and a downward spiral would result. The pig sector was a prime example, where the number of sows had almost halved in ten years and processing had been lost. It would be difficult to increase their number again.
8. The NFU was currently concerned about dairy farming as the prices paid to dairy farmers were barely sustainable; there had been a rapid decrease in the number of dairy farmers, and those leaving the industry included efficient and well managed units. Other dairy farmers had taken up the volume but the NFU was concerned about the fragility of the dairy industry and production in the long term. Dairy farmers were paid by their processors (eg Arla, Dairy Crest, Wisemans) and the price varied. There were quite complicated formulae relating to protein and fat content and the season in which product was supplied. The price paid to farmers was dictated by the retail price. Both retailers and processors had protected their margins while those of the dairy farmers had diminished and were non-existent in some cases.
9. In the short term farmers made cuts to remain in business, resulting in competitive prices for the consumer. This was, however, detrimental to producers who had to invest in long-term programmes such as farm assurance schemes and environmental standards (eg the disposal of waste). Milk production could be reduced considerably before being noticed because milk could be imported from elsewhere. About half the milk produced by UK farmers entered the liquid market and the remainder was processed. The NFU was concerned that a significant reduction in milk production would result in a reduction in processing because raw material was needed to keep the factories going. Eventually the UK might have to import milk, which would be regrettable for several reasons. First, it would be better environmentally to produce the nation's food closer to home. Second, imported milk had a reduced life span so freshness would be compromised. Third, consumer choice would be limited because the public might no longer be able to buy British milk. Fourth, there would also be knock-on effects in the meat industry because half the beef supplied came from dairy herds. If the number of cows were reduced there would be fewer calves and so less beef.
10. The supermarket multiples and the relatively large processors set their prices according to the competitive conditions they faced, and sometimes reduced prices to increase their half-yearly results. There was retrospective price cutting, promotional costs, retrospective overrides, contract prices, and retendering. Retailers asked for an up-front payment to retain the business. These requests were made mainly to the processors who passed the cost on to the farmers who received a reduction in price. Complaints were rare even though this practice was common. It happened across the board but some sectors (such as milk) were more sensitive than others. Retailers competed with one another for market share and milk was a key product. If there was a reduction in price or a retendering exercise, it was the farmers that suffered the consequences. There were only six or seven significant milk processors but they competed hard for market share and were vulnerable to pressure from retailers. If

retailers were in a difficult financial position, such as Safeway before it was acquired by Morrisons, they would ask processors and producers for cash sums or other forms of overrides without prior agreement or notification.

11. If milk processors consolidated it would increase their bargaining power vis-à-vis the retailers but it would also increase it vis-à-vis NFU members. Stability and certainty were, however, very important in the supply chain. One of the difficulties particularly in the milk sector was the instability of different tenders and contracts being moved around. The NFU asked retailers to have long-term dedicated written supply contracts so that their dealings were transparent.
12. The NFU had some members who, either individually or collectively, dealt directly with the category managers of grocery retailers who negotiated the terms of their contracts. Where the supply chain was shorter, as in the fruit and vegetable sector, there was a close relationship between the retailers, buyers or category managers, and the farmers. In the case of strawberries, the co-operatives had, due to the differences in the dynamics of supply and demand, a more balanced relationship with the retailers and so were able to command better prices. This, however, was not the case in the meat or dairy industries, where the farmers had a relationship with the processor who set the contract and the price.
13. There were, however, concerns in all sectors. There was a climate of fear which, combined with the loosely worded Supermarket Code of Practice, meant that retailers, and to some extent processors, were able to behave as they liked. Both were confident about alternative supply bases. Oversupply in the food industry meant that retailers had alternative choices, including abroad.
14. The 'buy one get one free' promotions occurred when there were seasonal surpluses but were also offered as a result of bad planning when retailers had overestimated demand and had to get rid of stocks. The NFU believed that the terms under which the product was grown (eg the amount to be grown and the growing period) should be documented in addition to financial matters because the planning arrangements at present were not good. Farmers were not told how much to produce and when, which sometimes resulted in overproduction.
15. The NFU told us that Waitrose was the best retailer in terms of having durable contracts which recognized the need for everyone in the chain to make a margin. Those dairy farmers with Waitrose contracts were doing reasonably well. Although Waitrose bought milk through Dairy Crest, the company knew the names of all their farmers and expected high environmental and safety standards. In return, Waitrose offered assurance and longer-term contracts. However, it was difficult for those dairy farmers with contracts with other retailers.
16. Other supermarkets were not as good as Waitrose at managing the supply relationship. There had been a few incidences of bad behaviour by individual buyers. One of the main concerns was that a huge amount of power and influence was given to relatively young inexperienced people who might only be in that particular supply chain for 18 months before moving on to another sector. Some of the worst practices, however, were carried out by local buying groups (the symbol stores).
17. Before Safeway was acquired by Morrisons, it had asked a number of suppliers for additional payments. An NFU member informed the NFU that he had been asked by Safeway for a substantial sum within the period of a fortnight in order to keep Safeway's business. Requests for additional payments were made by retailers irrespective of whether a farmer had a written contract. In the vegetable industry, some farmers were encouraged to make large investments which they did in the

hope of benefiting from a long-term relationship. When a supermarket asked them to raise capital it put them in a very difficult position. If the majority of a supplier's business was with one retailer it would think very carefully before complaining. Retailers could easily obtain goods from elsewhere, and suppliers could be blackballed if they did not comply. Small suppliers were able to grow volume by developing their business with the supermarket multiples and some had done very well. They had been able to innovate and expand and so were willing to hand over capital for promotional purposes or suchlike.

18. The NFU had also been informed by a supplier that it had paid one of the grocery retailers an overrider of several million pounds over the course of several years to secure the business. The retendering process, which occurred on a reasonably regular basis, was not transparent because the pricing structures did not include these extra elements. The cost of the overrides paid to grocery retailers by processors was passed down the supply chain to farmers in the form of price reductions.
19. The NFU had tried to encourage the retailers to work more closely with farmers in the livestock sector. Communication was better with Waitrose and M&S, which were working with smaller groups of producers and with a specific abattoir.
20. Farmers planned their business for the long term (over a five- to ten-year period) and short-term considerations were detrimental to sustainability of food production in the UK. A significant amount of food could be produced in the UK, and the NFU believed that a short supply chain was preferable (for retailers) in terms of fuel usage and energy efficiency. If farmers suffered in the short to medium term and exited the industry, the chances of encouraging them back were remote. The NFU was not seeking to intervene in the market but it wanted retailers to look at long-term consequences.
21. The NFU said that about ten years ago a large percentage of tomatoes were grown in the UK from spring to autumn. At that time there was a requirement for most tomato growers to category-manage their products, which necessitated the purchase of tomatoes to fulfil their contracts for the whole year round. Tomato production (with the exception of plum tomatoes) had now migrated to Spain and North Africa with the result that ordinary round tomatoes were now, by and large, not grown in the UK. This would take a long time to reverse. It would be possible to buy in the necessary skills but would be difficult to engender the trust and confidence needed for a grower to invest in the sector. Growers were prepared to deal with planning, water, labour and other issues but were discouraged by fluctuations in behaviour from purchasers.
22. The NFU and Waitrose wanted to develop the supply chain relationship. Farmers had a transparent relationship with Waitrose which was typified by sustainable production: there was a mutual understanding of the cost implications. This, however, did not mean writing blank cheques for farmers; the NFU did not want protectionism. With the Waitrose model, the infrastructure and welfare elements were reconciled; for example, it was understood that cows went outside for a certain number of days a year, and were not kept in all the time as large herds were, and that the farmer received a fair price. There was so much downward pressure, particularly in the dairy sector, that ultimately there would be a degradation of the environment and the quality of what was being produced. Consumers were demanding something extra and there was growth in the 'Finest' range. There was more added value to differentiation. If the reduction in prices continued, innovation in these areas would be curtailed.

23. The 2005 Defra report stated that net income per farmer had fallen by 11 per cent in that year. This was due in part to higher energy prices but could also be attributed to the fact that farmers were unable to pass additional costs up the supply chain. From a retail point of view, retailers could either increase their prices or negotiate lower costs, and usually did the latter. The Defra report predicted a rise in farmers' net income by 2010 but this was fairly speculative, and was a generalization across the different sectors. The NFU was not confident that the trend would suddenly return to being a balance between retailer, processor and farmer.
24. The marketplace was a tough, highly competitive place but this was what drove efficiency and good deals for the consumer. The NFU would continue to push for a good understanding in the supply chain about investment, and improving standards and assurance. Its view was that the industry needed to establish better trust in the supply chain, better expectation about what good standards were and the trend towards bad behaviour had to be turned around.

Supermarket Code of Practice

25. The NFU believed that the Supermarket Code of Practice (SCOP) had not worked for two reasons. The first was fear, because it required a party to complain about one of the leading four grocery retailers for failure to comply with the SCOP, and an investigation would then take place. Suppliers were reluctant to complain for fear of being blackballed. The second was that the SCOP was very loosely worded, and definitions of the word 'reasonable' could be debated. Equally, the NFU had been nervous about over-regulation and preferred a proactive rather than reactive approach. It wanted retailer-supplier relationships to be audited regularly by a public authority to check whether the retailers were observing the SCOP. Expected standards of behaviour should be set out and everything documented so that all the details about supply arrangements were transparent. The fact that a supplier was content with an arrangement at a particular time did not mean it was good practice, and the supplier might change its mind if something went wrong.
26. The SCOP applied only to the four leading grocery retailers. The NFU thought there was considerable merit in having a code which applied to the food chain irrespective of size. The farming community should be subject to the same set of expectations about how the supply chain worked. Overrides should be allowed provided they were transparent, agreed in advance, for a purpose, and could be audited. The NFU had attempted to obtain industry agreement to a Buyers' Charter but the retailers had not signed up to it for a variety of reasons, the fundamental one being that they did not want to be audited. The supermarkets would only agree to the charter if everyone else did and did not want to be bound by the SCOP.
27. The NFU received complaints about grocery retailers. Many of these were second-hand and many were made confidentially so the identity of the complainant could not be revealed to the retailer.