The South Island Kiwifruit Market - Should we Cooperate?

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Table of Contents

Introduction

There are three main factors influencing Kiwifruit Growers profitability, productive yield, cost of production and the return they receive for the crop they produce.

When a kiwifruit crop is put through a packhouse, it is separated by size and quality into four grades. Class 1 and 2 are usually exported, class 3 is usually sold on the New Zealand domestic market, and class 4 is usually sent for processing or used as stock feed.

The major factor influencing a kiwifruit growers total return is the return they receive for the fruit that is exported (normally 85-98%). But the return from class 3 fruit sold on the New Zealand domestic market also has an important impact on a growers total return, and hence overall orchard profitability.

The purpose of this report is to look at the South Island domestic kiwifruit market, and consider if there is a potential benefit to South Island kiwifruit growers from cooperating in their sales and marketing efforts.

The Current Situation

Kiwifruit in The South Island is harvested between mid April and early June. New Zealand kiwifruit is supplied to the market from the beginning of the harvest season until early in the new year. Kiwifruit will then be imported from the Northern Hemisphere until New Zealand fruit is back in supply.

There are five parties in the sale of kiwifruit on the domestic market. Kiwifruit growers send their fruit to a packhouse, who after grading, packing and cooling will send it to a wholesaler. The wholesaler will then sell it to a retailer, and charge a commission for doing so. The retailer will then add their mark up and sell it to the consumer.

The return to the grower is driven by the sale price between the wholesaler and the retailer. The wholesaler, after charging their commission, will then return the remaining funds to the packhouse's grower pool.

The majority of fruit sold on the South Island Market is fruit grown and packed in the South Island. This is due to the proximity to market, compared to the prohibitive cost of shipping from the North Island. As well as North Island Packhouses tending to have a more flexible grade standard for class 2 product that they supply into Australia, and subsequently having a lower volume of class 3 which can mostly be consumed by the North Island Market.

There are 10 kiwifruit packhouses in the South Island, and no collaboration, either formal or informal, currently exists between them when supplying fruit to the market.

There are 4 major wholesalers in the South Island. The majority of kiwifruit in the market is sold by these wholesalers to the retailers, the largest of which are the 2 supermarket chains, Progressive Enterprises and Foodstuffs.

With 4 different wholesalers and only 2 different supermarket chains, the wholesalers must compete with one another to supply the major buyers.

Domestic kiwifruit is a commodity product. There is no discernable difference between kiwifruit being supplied by different packhouses. The standard way for wholesalers to compete for the retail buyer is to have a lower price than their competitors, allowing retailers to either lower the

retail price to increase throughput, or to have a higher markup percentage. Either way this increases the margin for the retailer, while decreasing the return to the grower.

Cost of Production

If we assume that class 3 kiwifruit is a by-product of the production of class 1 kiwifruit, then we can also assume that it incurs no cost until the time of grading in the packhouse.

The cost of production of class 3 kiwifruit is therefore made up of the cost of packing, coolstorage and freight to market.

Packing and coolstorage charges are highly confidential, but as I believe that charges are similar throughout South Island Packhouses, I will use the charges supplied by Thomas Bros Ltd as the base for the cost of production for South Island class 3 kiwifruit.

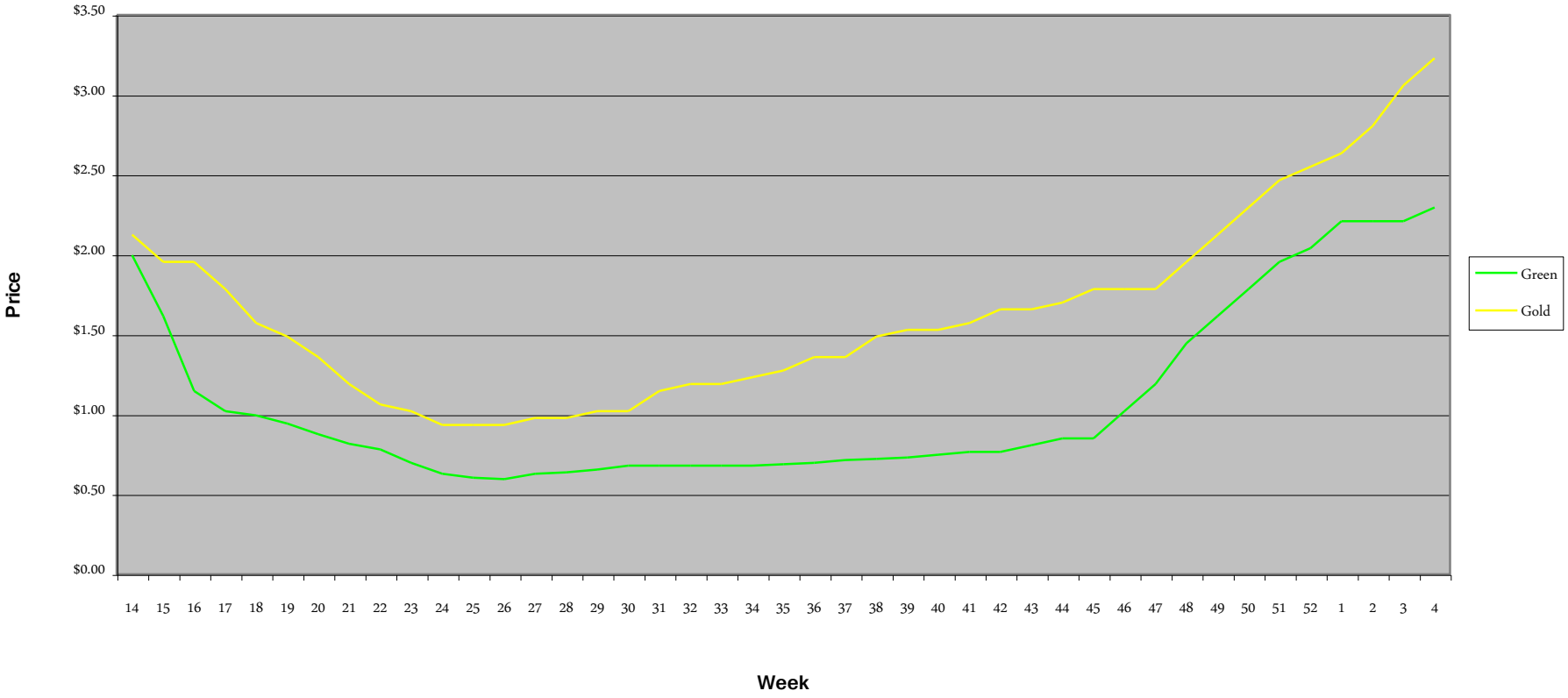
This would put the cost of production of class 3 kiwifruit at $0.68/kg.

Wholesale Price Patterns

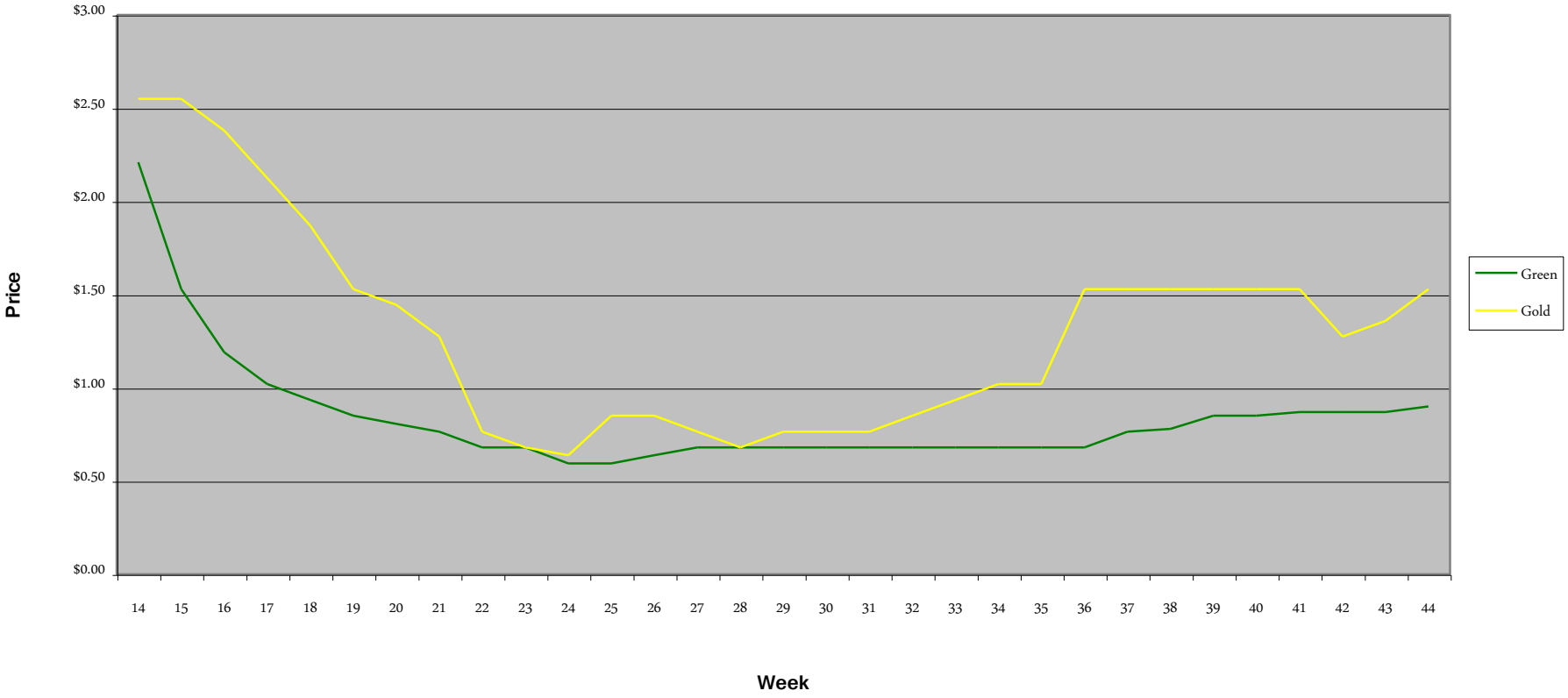
Imported kiwifruit is sold at a high wholesale price due to the cost of shipping and supply. As the New Zealand harvest begins wholesale prices decrease over an 8-10 week period. Prices then usually stay depressed for several months, until slowly climbing back up towards the end of the New Zealand season to meet with the imported supply.

As is shown in the diagrams below, the wholesale market price has reached its lowest point between weeks 24 and 26. This is within a couple of weeks of the completion of kiwifruit packing, and when packhouses stock of kiwifruit is at its highest point.

2012 Wholesale Market



2013 Wholesale Market Prices



Supply and Demand

As shown in the graphs above the market price reaches its lowest point between weeks 24 and 26. The question here is what determines the level at which the lowest price is reached, and more importantly can it be manipulated?

By the beginning of May (week 18) packhouses have enough stock on hand to supply the market completely with all sizes and varieties, yet it is typically another 6 to 8 weeks later when the market price reaches its lowest point.

Over the 2012 and 2013 selling seasons the market price has reduced from its preseason high to just below the cost of production, where it has stayed for several weeks before lifting back over. Over this whole period packhouses have had a full range of stock on hand, and it has only been the rate of supply to the markets, and a willingness to accept the sales price from the wholesalers that has led to such a steep fall in market returns.

Can The Market be Manipulated? - Case Study

Thomas Bros Ltd supply kiwifruit to Wholesalers throughout The South Island. They usually supply 2 different wholesalers in the main South Island market of Christchurch. During August this year they were approached by the other 2 major wholesalers based in Christchurch, who were looking to increase their supply base. With Thomas Bros holding a large volume of class 3 fruit in store, it was decided to supply the 2 new wholesalers under strict price conditions.

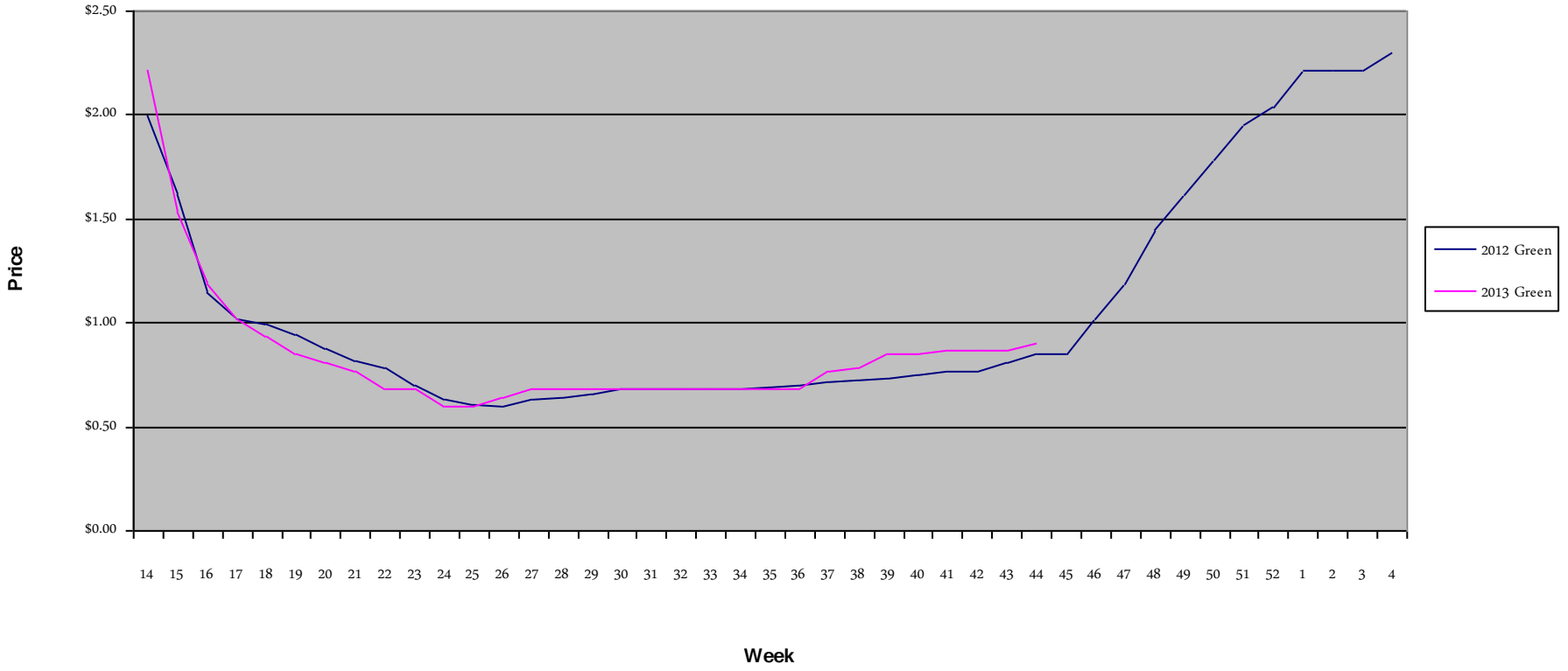
During late August the average market sales price was $0.80/kg. This provided an after commission return back to the grower pool of $0.68/kg, only just covering the cost of production.

At the end of week 36 Thomas Bros sent fruit to all 4 Christchurch wholesalers for sale during week 37. Each wholesaler was told that we needed a minimum sales price of $0.90/kg. The first couple of sales that were made at the beginning of week 37 were just below $0.90/kg, but the average price came up to $0.90/kg by midweek.

At the beginning of week 38 average sales prices were holding firm at $0.90/kg. Each wholesaler was told that as our stock on hand was getting lower we needed to have a minimum sales price of $1.00/kg from the beginning of week 39 and for the rest of our selling season. In week 39 all four Christchurch wholesalers had a minimum sales price of $1.00/kg.

Over the next few weeks sales prices held steady, before continuing to climb slowly.

Green Prices 2012 vs 2013



Proposal

Mainland Kiwi Growers Entity is a kiwifruit supply group to Zespri. All South Island Kiwifruit Growers supply Zespri through Mainland Kiwi. Mainland Kiwi's current roles include managing coolstore inventory, allocating orders and organising freight of product required by Zespri. As well as managing grower pools for all funds received from Zespri for fruit supplied to them.

Mainland Kiwi charges an administration fee on all fruit received into its inventory to cover its costs for the year, and at the end of the financial year any left over earnings are returned to growers through a rebate.

If Mainland Kiwi became a supplier to the domestic market, it could manage the inventories of all South Island Packhouses. Mainland Kiwi could receive orders from the different wholesalers and allocate the orders to packhouses to dispatch.

With Mainland Kiwi controlling the supply to market, it can also have much more of an influence on price. By setting a base price and providing clear direction to wholesalers that supply is solely linked to sales returns, Mainland can limit the ability of wholesalers to undercut each other.

With a much larger inventory than any one packhouse would have, opportunities would arise for providing value added lines to customers for a full season across a large range of sizes and varieties. Providing an added value pack can increase revenue for retailers as well as returns for growers and often comes with good price stability throughout the selling season.

Although the cost of production would increase for growers due to Mainland Kiwi charging an administration fee (approximately $0.04/kg if set the same as for other products), the higher sales returns should more than compensate.

Equal drawdown between packhouses would be required to give equal opportunity to each packhouse pool to receive the highest sales returns. At times though it may be best for exceptions to be made. With kiwifruit being a perishable product there may be occasions where one packhouse has a line that is deteriorating faster than others. It would be prudent then for that particular line to be dispatched to market as quickly as possible so as not to spoil. Mainland Kiwi could prioritise the ordering of this product

ahead of product form other packhouses. This would help reduce fruitloss over the season, and help to keep in market quality as high as possible for as long as possible.

Conclusion

For South Island Kiwifruit Growers to realise the greatest return for their class 3 product packhouses need be strict in their supply of fruit to wholesalers. If all packhouses supplied fruit with the same price expectations from wholesalers there would be no price undercutting of one packhouse's fruit by anothers.

The vehicle for cooperation between packhouses already exists in the form of Mainland Kiwi Growers Entity.

By Mainland Kiwi overseeing supply to the South Island Markets, sales prices can be positively influenced and returns to growers can be maximised.

References and Acknowledgements

The list below contains people companies and websites used to gather information for the development of this report.

www.zespricanopy.com

Paul Gnad of Freshmax NZ Ltd

Nick Bright of Turners and Growers Ltd

Thomas Bros Ltd

Mainland Kiwi Growers Entity Ltd

Appendix

The wholesale market prices below for 2012 and 2013 have been collated using information from Buyer Created Tax Invoices received by Thomas Bros Ltd from Turners and Growers Ltd, Freshmax NZ Ltd, MG Marketing Ltd, Fresh Direct Ltd, as well as the Daily Sales price sheet provided to Thomas Bros Ltd by Turners and Growers Ltd. Sales prices after commission are shown.

2013	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28
Green	$2.21	$1.53	$1.19	$1.02	$0.94	$0.85	$0.81	$0.77	$0.68	$0.68	$0.60	$0.64	$0.68	$0.68	$0.68
Gold	$2.55	$2.55	$2.38	$2.13	$1.87	$1.53	$1.45	$1.28	$0.77	$0.68	$0.64	$0.85	$0.85	$0.77	$0.68

2013	29	30	31	32	33	34	35	36	37	38	39	40	41	42	43
Green	$0.68	$0.68	$0.68	$0.68	$0.68	$0.68	$0.68	$0.68	$0.77	$0.78	$0.85	$0.85	$0.87	$0.87	$0.87
Gold	$0.77	$0.77	$0.77	$0.85	$0.94	$1.02	$1.02	$1.53	$1.53	$1.53	$1.53	$1.53	$1.53	$1.28	$1.36

2012	14	15	16	17	18	19	20	21	22	23	24	25	26	27
Green	$2.00	$1.62	$1.15	$1.02	$0.99	$0.94	$0.88	$0.82	$0.78	$0.70	$0.63	$0.60	$0.60	$0.63
Gold	$2.13	$1.96	$1.96	$1.79	$1.57	$1.49	$1.36	$1.19	$1.06	$1.02	$0.94	$0.94	$0.94	$0.98

2012	28	29	30	31	32	33	34	35	36	37	38	39	40	41
Green	$0.64	$0.65	$0.68	$0.68	$0.68	$0.68	$0.68	$0.69	$0.70	$0.71	$0.72	$0.73	$0.75	$0.77
Gold	$0.98	$1.02	$1.02	$1.15	$1.19	$1.19	$1.23	$1.28	$1.36	$1.36	$1.49	$1.53	$1.53	$1.57

2012	42	43	44	45	46	47	48	49	50	51	52	1	2	3
Green	$0.81	$0.85	$0.85	$1.02	$1.19	$1.45	$1.62	$1.79	$1.96	$2.04	$2.21	$2.21	$2.21	$2.21
Gold	$1.66	$1.66	$1.70	$1.79	$1.79	$1.79	$1.96	$2.13	$2.30	$2.47	$2.55	$2.64	$2.81	$3.06