

Got Milk? It's Good for You – Unless It's Contaminated

Don Lizhong bet that being a dairy farmer was his golden ticket out of a factory job in China. Unfortunately, a contamination crisis in 2008 shattered his dairy business when babies mysteriously started developing kidney stones from contaminated baby formula. A chemical called melamine, an additive used to make plastic, was discovered in the milk supply of one of China's third-largest dairy producers. Four infants died from the contamination and at least 53,000 fell ill. According to the official Xinhua news agency, officials knew about problems with the milk for months before informing the public.

China's four largest dairy organizations, accounting for nearly half the country's milk market, pulled their goods off shelves. More than 20 countries, including France, India, and South Korea, banned not only dairy products from China, but also candies, cookies, and chocolates. "This is a disastrous setback. I estimate that it will take one or two years to rebuild confidence in dairy products," says Luo Yunbo, dean of the College of Food Science & Nutritional Engineering at China Agricultural University.

The local milk-collection station in Dong Lizhong's village discontinued purchasing milk. Farmers continued to milk their cows, but they drank the milk themselves or poured the milk into their cabbage fields.

Cutting Corners

Chinese do not traditionally drink milk. However, as the country has grown more affluent over the past few decades, the domestic dairy industry has skyrocketed. China's two largest dairy companies have greatly benefited from this new trend: China Mengniu Dairy and Inner Mongolia Yili Industrial Group. Simultaneously, numerous entrepreneurs – from dairy farmers to milk-collection station owners to milk distributors – have jumped into the supply chain of dairy products to make their fortunes. Due to the fierce competition within China's dairy industry, a few companies decided to cut corners to reduce costs, regardless of the consequences.

As Mengniu and Yili expanded at breathtaking speed, they found themselves in the unique position where supply could not keep up with demand. According to KPMG, China consumes 25 million tons of milk yearly, putting its dairy market ahead of France and Germany. In their quest for more raw milk, Mengniu and Yili have expanded outside their base in the northern province of Inner Mongolia and set up production facilities in other parts of China. Most of the quality problems in milk were found in dairy farms in Hebei and Inner Mongolia provinces, where the competition for raw milk supplies has been the fiercest.

Most dairy farmers in Hebei province traditionally sold their milk to milk-collection stations established by local heavyweight Sanlu. In recent years, new privately owned milk-collection stations to buy raw milk for Mengniu and Yili started popping up next to existing stations. These new entrants captured raw milk supplies by offering dairy farmers slightly higher prices. "This competition broke the rules. As milk buyers fought over milk supplies, their standards for quality fell," says Roger Liu, vice chairman of American Dairy Inc., a Heilongjiang province-based powdered milk company.

Additives to Boost Protein

Many of the milking stations do not have the equipment to test milk for additives. At the Nanxincheng station, 16 households bring their dairy cows in the area to be milked in the red brick farmhouse. The farmers hook up the cows to a milking machine, which pumps the milk directly into a big vat. "They didn't test the milk here. They sent it to Sanly for testing," says Du Yanjun, a government inspector who was posted to monitor the Nanxincheng station after the contamination crisis broke.

The milk is collected from the stations and shipped by middlemen to big dairy companies such as Sanlu, which would do their own testing and grading. It now appears that unscrupulous middle-men added melamine to the raw milk to increase protein levels in their milk samples, so their milk would be graded higher. However, ingesting melamine can also cause kidney stones or kidney failure, especially in infants.

Matthew Estes, president and CEO of BabyCare, had looked into switching from Australian and New Zealand sources of milk for the company's infant-formula business in China. BabyCare tested possible Chinese suppliers and realized it could not locate a suitable supplier in China. "We couldn't find the quality that met our standards. We chose to not sell in China rather than take the risk," he says.

Stiff Sentences

A Chinese court sentenced two of the middlemen to death and a dairy boss to life in prison for their roles in the milk contamination scandal. The swift trial and harsh sentences show Beijing's resolve in tackling the country's stubborn food safety problems and an eagerness by the communist leadership to move past the embarrassing scandal.

Questions:

1. List 10 products that could possibly be affected by a problem in the U.S. milk supply chain. What would be the damages to an ice cream business that used contaminated milk in its manufacturing process? Who do you think should be held liable for such an issue?
2. Do you think a CRM system could have helped communicate issues in the milk production supply chain? How could a company use a CRM system to perform damage control after finding out about contaminated milk in the supply chain?
3. Do you agree with the Chinese court in sentencing of the middlemen to death and a dairy boss to life in prison for their roles in the milk contamination scandal? Do you think the United States should implement similar laws for unethical corporate behavior?
4. Many companies in the United States use Chinese suppliers in the sourcing of raw materials and manufacturing of products. Research the Internet and find three examples of recent issues for U.S. companies because of Chinese products. What will happen in the long run as companies use Chinese suppliers?