PRESS INFORMATION from

The Dairy Group

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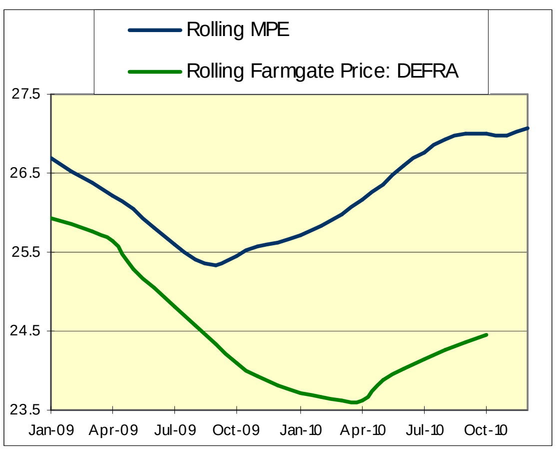
The Market Price Equivalent (MPE) December 2010

***By Nick-Holt Martyn, Director,* The Dairy Group**

UK milk price 23rd in the EU price league

"With the UK now languishing at **23rd** in the EU price league, 10% behind our nearest western European neighbour, the UK market is failing its primary producers", says Nick Holt-Martyn, Director of The Dairy Group. He goes on to say "In a year that has seen the rise in global GDP lift market returns across the world should be good news for UK farmers, but unfortunately not. Despite the UK being an island dairy nation with a high value internal market focussed on liquid milk and quality cheese, the market is dominated by retailers prepared to sacrifice their suppliers for market share. Just when the supply chain needs to counter production cost inflation throughout the supply chain there is a round of undercutting that undermines the viability of both processors and primary producers."

He goes on to say "As the graph shows market returns have been on an upward trend since September 2009, while it took until April 2010 before rolling milk price started to increase. Whilst the 6 month time lag is not unusual, the gap between market returns and



farm gate price at 2.5 ppl is now 50% wider than the average of the last 10 years, which indicates that milk price should continue to increase. Failure to ensure UK farmers receive the market returns when markets are good does not bode well, when the next inevitable downturn takes place at some point in the future.

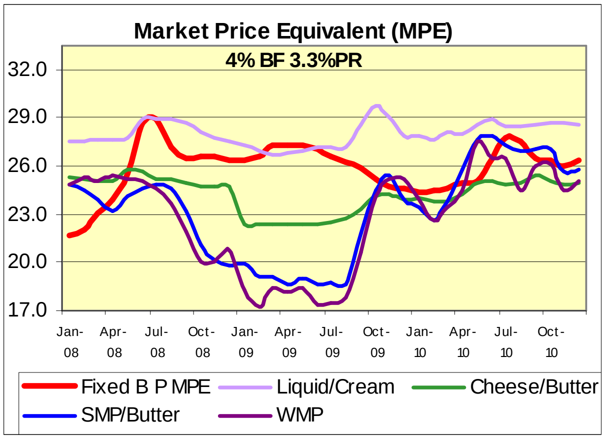
The prospects for 2011 are mixed with indicators pointing in many directions at the same time. Global consumption is rising as world GDP continues to recover, however both the OECD and IMF indicate a weakening in GDP growth by 10 to 20% in 2011 due to fiscal tightening in advanced economies. Meanwhile global production is rising and looks set to continue, although drought and excess rain in New Zealand and Australia looks likely to restrict their production growth to around 1%, while both the US and EU are also showing continued growth.

Markets are reflecting the current stable outlook with Fonterra auction prices for powders showing rises of 2 to 3% suggesting the markets are expecting a tightening of supply in 2011. So globally 2011 looks favourable for production and prices.

Domestically, as the graph shows, there is still a period of catch up while market returns are transferred down the supply chain. For the last 10 years at least market returns have driven milk prices and there is no reason to suppose that will change despite the influence of the retailers and the width of the gap ~ *rising markets will lead to rising milk prices*.

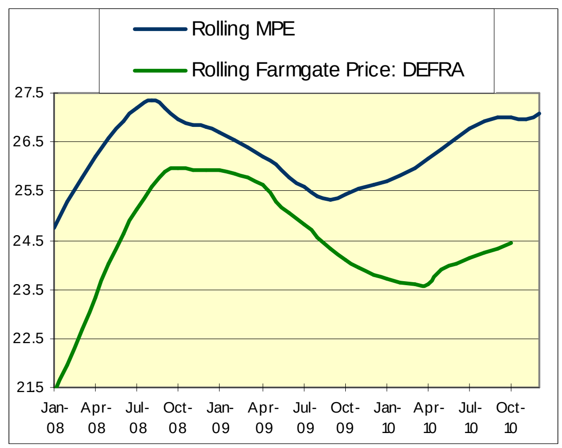
On the downside there is cost inflation, driven by high crude oil prices, currently over $90/barrel which will feed into feed, fertilizers and fuel costs which has not been factored into the forecast for GDP and which cannot be controlled by interest rate rises. Production cost inflation through high feed prices will limit production in the northern hemisphere and will also damage profitability. On balance 2011 is likely to be a difficult year with production cost inflation preceding milk price rises.”

Market Prices



UK commodity markets have firmed as the influence of world commodity prices trickles through to the UK market. The manufacturing sector is returning similar returns with cheese starting to lag behind, encouraging a switch to powders and butter. The Northern Ireland auction price firmed slightly to 26.98 ppl which suggests stability, although there is likely to have been some disruption of supply during the cold snap. The Market Price Equivalent (MPE) slips to 27.29 ppl, down 0.1 ppl on November, down 0.22 ppl since June 2010, but up 0.86 ppl on last year. The easing of production forecasts in the southern hemisphere due to dry conditions or floods is lifting price expectations for 2011 in advance of the Northern Hemisphere production peak. The prognosis for 2011 looks more favourable provided growth in global GDP can be sustained. A dip due to oil price inflation could weaken the current upward price movement.

Farm-gate Prices



The lack of milk price rises continue to be the issue as the gap between market returns shows no sign of narrowing, indicating that further farm gate price rises are overdue. Rises in the retailer aligned sector are helpful, but it is in the wider market that movement is needed. With the UK now languishing at **23rd** in the EU price league, 10% behind our nearest western European neighbour the UK market is failing its primary producers. Production costs are rising and dairy margins will come under increased pressure in 2011. Despite the delay in response, 2011 should see improvements in farm gate prices driven by the market. With many farmers relying on the Single Farm Payment for profitability the direction of CAP reform is causing concern.

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- **Visit www.thedairygroup.co.uk**
- The MPE is calculated from the weighted actual wholesale prices for liquid milk, cheese, butter and powders after the normal processing costs. The MPE accounts for 90% of the UK market utilisation of milk. The MPE is calculated from wholesale market values, whereas IMPE (Intervention Milk Price Equivalent) accounts for just 11% of UK milk production and is effectively determined by the Council of Ministers and the prevailing exchange rate. The MPE provides a far superior indicator of the wholesale value of milk and therefore the likely market returns available to the dairy farmer.