PRESS INFORMATION from
The Dairy Group

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The Market Price Equivalent (MPE)

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

The Tightening Vice of Inflation

“Inflation is everywhere you look in the Global economy despite having been allegedly consigned to the dustbin 40 years ago” says Nick Holt-Martyn of The Dairy Group. He goes on to say “as always it hinges on supply, whether that is gas, oil, fertiliser, wheat or milk. When supply is interrupted market prices always respond. A heady combination of Brexit, Covid Pandemic and now the Russian invasion of Ukraine have disrupted the finely balanced supply/demand relationships in the key commodities. When there is such widespread inflation, returning to some kind of “normality” seems unlikely due to the fine balance on connectivity throughout the market and devaluation of currencies, 40ppl becomes the new 30ppl. For example, with production costs climbing over 40ppl milk supply will not stabilise unless milk prices rise to ensure a similar level of profitability to what has gone before. It also suggests that prices cannot fall back in isolation without a further period of destabilisation.

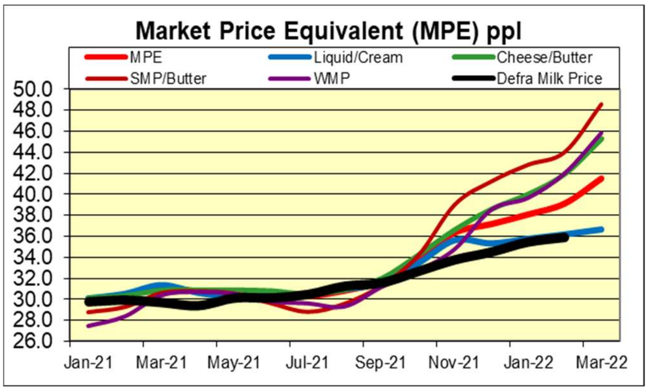
The table below shows the trend in Cost of Production over the last 2 years with a tentative projection for the 2022/23 year.

The Dairy Group: Cost of Production Analysis				The Dairy Group Proj.	
	2020/21	2021/22	Yr on Yr Change	2022/23	Yr on Yr Change
Defra Farmgate	28.83	32.8	13.6%	39.4	20.1%
Milk Sales	29.2	33.1	13.4%	39.4	19.0%
Total Output	32.3	36.4	13%	43.1	18%
Total Variable Costs	15.5	18.4	19%	22.9	24%
Total Overhead Costs	15.6	16.5	6%	17.9	8%
Profit after Unpaid Labour	-1.2	-1.0		-0.3	
Total Costs	33.5	37.4	12%	43.4	16%
Non Dairy Income	3.0	2.9	-3%	2.7	-7%

Source: The Dairy Group

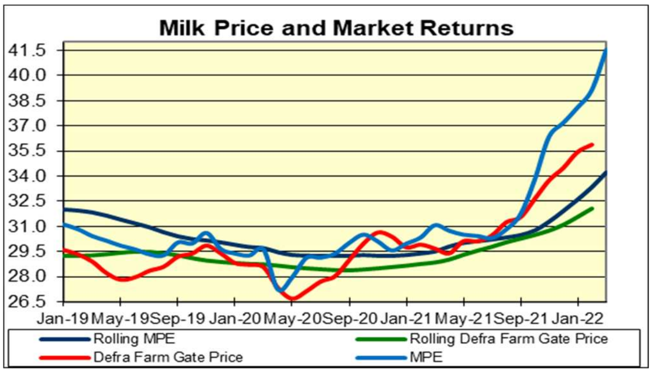
The table shows the effects of inflation on producton costs in the year ending **March 2022** to be +12% with Variable Costs, not surprisingly showing the biggest rise of 19%. Total Output has risen to leave Profit after Unpaid Labour higher by 0.2ppl, better than **March 2021**, but still below breakeven point. The projection for year ending **March 2023** shows cost of production up by 16% to **43.4**ppl with Variable Costs up 24% alone. Within the Variable Costs Forage Costs are estimated to rise by 50% and Purchased Feed by 25%. Total Output is up 18% despite a 19% rise in Milk Sales to 39.4ppl. The net effect however, is an improvement in Profit after Unpaid Labour to -0.3ppl, 0.9pl above **March 2021**. Over the two years Variable Costs will have risen by 48% and the Cost of Production by 30%.

The effects of input cost inflation will be progressive and unique to each business as previously bought feed and fertiliser stocks and contracts are used up and get replaced by new supplies at 2022’s inflated prices. With many milk processors looking to have prices above 40ppl in place for May some farmers may enjoy a temporary boost to cashflows, before the effects of the inflation vice squeezes the cash out of their businesses. By the end of the summer the effects of inflation on feed, fuel and fertiliser prices will be having a big impact on business cashflows. In all likelihood, milk prices will have to keep up with market returns and rise beyond 40ppl for the economics of milk production to add up. If processors have got their sums right dairy farmers will have been encouraged to soldier on and keep up milk supplies, if not milk supply will fall further. As we have seen falling supplies equals price rises! Global milk supplies remain in the red and falling in all the key exporting nations around the world, with the expectation that will continue throughout 2022. Northern hemisphere will be hit with input inflation while the southern hemisphere has yet to see the back of La Nina that has hampered their milk supply. At some point stability may occur but it’s impossible to say how it will look.



Market Prices

The Market Price Equivalent (MPE) climbs yet again by 2.4ppl to 41.5 ppl (+5.7%) this month, up 9.8ppl (31%) in the last 6 months and up 10.4ppl (34%) year on year. Products were up across the board, from Cream (+3.9%) to Butter (+9.7%). The range across the sectors widens to 11.6ppl from SMP/Butter down to Liquid/Cream. Supply continues to remain weak around the world which is dominating markets and a correction seems less likely this year. Wholesale markets are driven higher by demand with all time highs being achieved monthly. Whilst consumer liquid prices have not shown a response retailers and liquid processors are now playing catch up with the commodity market with 40ppl prices for the summer.



Farm Gate Prices

The February 2022 farm gate price rose by 0.4ppl to 35.9 ppl, 6.0ppl above February 2021. The rolling Farm Gate price rises to 32.0ppl. February milk price was 0.7ppl below our forecast, but will rise further with a flush of increases announced for May.

Our latest milk price forecast, based on current prices and market returns, suggests the Defra milk price will hit 37.3ppl in March, rising to 38.5ppl by the summer and before rising to 40.1ppl in the autumn.

Production in January was confirmed at 1230 M litres -1.9% (-24 M litres) and February was provisionally 1226 M litres, -2.0% (-24 M litres). Based on the AHDB daily deliveries our March forecast is 1300 M litres (-3.0%), April at 1315 M litres (-2.9%) and May 1375 M litres (-2.6%). 2021/22 production looks set to finish the year -0.7% at 14.90B litres and our forecast for 2022/23 is 14.74b litres (-1.1%).

Sterling eased down against both the Dollar and the Euro, to £/€1.187 and £/$1.314. The consumer price index reached 6.2% in February and is expected to go to 7.5% as energy prices rise 20% since the invasion of Ukraine.

The shift from La Nina to neutral conditions is much slower than expected and is likely to affect the Northern Hemisphere growing season, particularly North America where summer is expected to be hotter and drier. All things considered a recovery in supply is unlikely in 2022 and pressure is on to support producers to prevent further declines."

- Ends -

<u>For further information please contact:</u>

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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 United Kingdom market utilisation of milk. AMPE (Actual Milk Price Equivalent) also only accounts for 14% of United Kingdom milk production. The MPE provides a far superior indicator of the wholesale value of milk and therefore the likely market returns available to the dairy farmer.