PRESS INFORMATION from
The Dairy Group

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The Market Price Equivalent (MPE) Update June 2016

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

Dairy volatility set to become more volatile

"So Brexit it is but what does that actually mean and what are the implications for the dairy industry? Does anyone know?" asks Nick Holt-Martyn of The Dairy Group. He goes on to say "if we start with what we do know then we can try to identify the possible outcomes and see what they *MAY* hold for the dairy industry. The first thing to say is that nothing actually changes until Article 50 is formally invoked by the new Prime Minister. We remain in the EU, free trade, direct payments and market support continue and the only thing of concern is the effect on the exchange rates and stock markets.

2015/16	Production	Imports			Exports			Change in intervention stocks	Supplies	UK production as a percentage of supplies
		EU	Non-EU	Total	EU	Non-EU	Total			
Butter	158	95	3	98	45	7	52	0	204	78%
Cheese	453	491	6	497	125	29	153		796	57%
Condensed Milk	91	39	0	39	31	2	34		96	94%
Powders	165	60	0	60	103	46	149	1	75	219%
Cream	192	30	0	30	19	1	20		201	95%
TOTAL	**1058**	**715**	**8**	**724**	**322**	**85**	**407**	**1**	**1373**	**77%**

Source: The Dairy Group & Defra

As the table shows in the last milk year almost all dairy imports and 80% of exports were with EU countries. On imports cheese was dominant with only 57% of total supplies from UK production, with EU imports greater than domestic supply and a third of production exported. Whereas powders rely very heavily on exports, some imported but little Intervention. The inference that can be drawn is that we import mostly value added products and export commodities, but the balance is firmly on imports.

The trading in Milk, Grain and Meat sectors all involve significant market management measures in the EU with external tariffs, anti-dumping measures, intervention buying/storage aid, phytosanitary, veterinary and food safety at the EU border. Clearly a new relationship with the EU is going to affect the dairy industry and the wider farming economy.

The future trading options will become narrowed down this autumn when a new Prime Minister takes up office and the Brexit negotiating team gets to work. The options are: remain in the Single Market as a member of European Economic Area (EEA), become a member of European Free Trade Area (EFTA), or bilateral agreements with WTO rules as the fall back position.

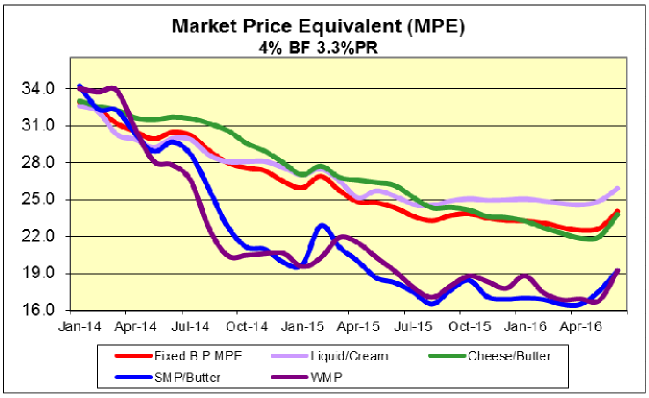
The Single Market, both within the EU or EEA, have the four pillars of the freedom of movement of goods, services, capital and labour. The required payment into the EU regional fund and the free movement of people make this option unlikely. The Swiss have a version without free movement of services and have just voted for controlled movement of people so that agreement is in jeopardy.

All EFTA members have joined up with the Single Market as outlined above so offers little other than tariff free trade. As the UK already has integration in economic cooperation and regulation this may be an option as it comes without the four freedoms required for the Single Market. Future differences in regulation may become non-tariff barriers increasing the cost of doing business thereby limiting trade.

Bilateral trade agreements with WTO fall back would mean tariffs could reappear unless subject to a free trade agreement. All EU countries come as one trading block and would be subject to a single agreement, so no special status for Ireland or Denmark for example.

There is a lot on the plate of the new Government when it is formed later this summer and the outcome will have an effect on the dairy industry given the close integration with the EU. Any tariffs are likely to affect imports more than exports so they may be beneficial to UK dairy farmers, but they would hamper the future growth opportunities for exports. In the meantime we have currency volatility to contend with which is likely to continue well into the future as the direction of negotiations are disclosed. The earliest the UK can leave the EU is probably January 2019, enough time for almost a complete turn of the dairy cycle!

Supply growth is easing off and markets are starting to lift off the floor as cool wet conditions prevail throughout northern Europe. A year of stable supply (less than 2% growth) around the globe would cause markets to firm and intervention stores to remain shut. The currency changes are helping milk prices up with sterling at €1.21 and $1.35, but there are increases in imported feed costs as well that could hold dairy margins back. For the next three years or so another layer of volatility has been added to an already volatile industry. It is to be hoped that the weather stays benign in that time so we can see some stability from that quarter at least.”

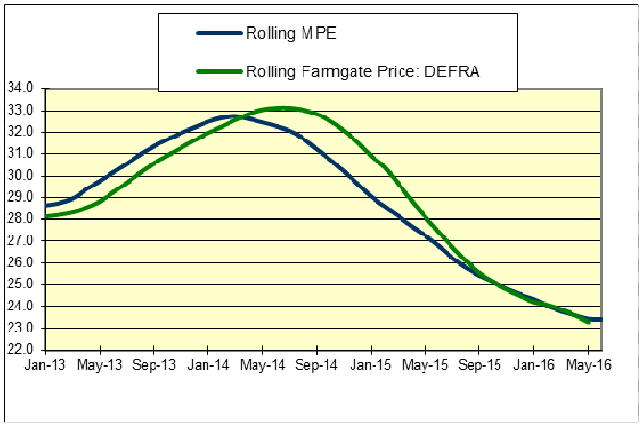


Market Prices

The Market Price Equivalent (MPE) has risen significantly (6%) by 1.38 ppl to 24.05 ppl due to further improvements across the board and the fall in exchange rate. The range across the sectors remains at 6.7 ppl from Liquid/Cream returns to WMP. SMP has lifted to £1300/t, still £80/t below a rising Intervention price and 1% below the last GDT auction, which rose 1.65% in Sterling equivalent. The GDT price equivalent (GDTPE) is up to 17.0 ppl but would be lifted by the weaker Pound to 18.3 ppl. The last GDT auction have seen a doubling of WMP tonnages back to its normal level of 44% of total auction tonnage. The MPE is down just 0.3 ppl on the year and up 0.74ppl since December 2015. United States production is running at +3.1% and New Zealand was +3.5% in May while the European Union was +1.7% in April.

Farm Gate Prices

May 2016 price falls to 20.4 ppl and a weighted average of 23.28 ppl, down 3.6 ppl and 4.8ppl on the year respectively. Still the curves are drifting down and expected to drop below 23 ppl but the MPE curve is starting to shape upwards at last. Summer has continued with the warm and wet weather which has hampered forage harvesting and pushing milk back sharply. The Brexit vote has seen Sterling drop back to end the month at €1.21 raising the SMP Intervention price £80 above the market returns and dropped against the dollar to $1.35. United Kingdom production in May was 1313 million litres, 66 below 2015 and June is forecast at 1231 M litres, 72 M litres below 2015. July is expected to be around 1200 M Litres. The milk price is forecast to stabilise as B litre prices are increased due to markets and exchange rates with rises likely from mid-late summer.



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<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. The MPE is calculated from wholesale market values, whereas IMPE (Intervention Milk Price Equivalent) accounts for just 11% of United Kingdom 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.