

PRESS INFORMATION from *The Dairy Group*

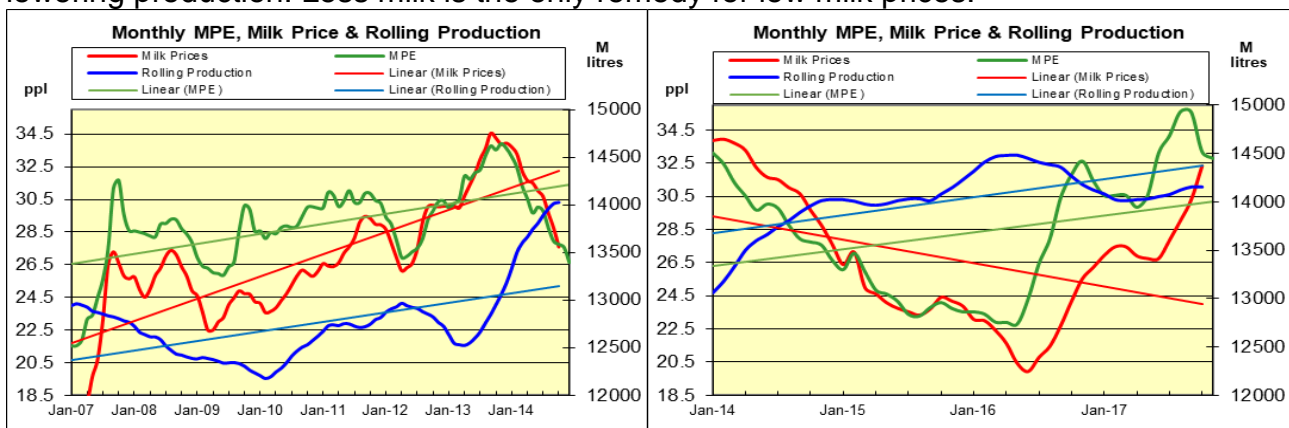
1st December 2017

The Market Price Equivalent (MPE) Update November 2017 By Nick Holt-Martyn, The Dairy Group

Speculation on Scale of Volatility as Dairy Cycle Tips Down Again

“With milk prices already falling in January concern abounds regarding how bad things might get given the depth of the last milk price disaster of only 2 years ago” says Nick Holt-Martyn of The Dairy Group. He goes on to say “unfortunately as with the weather, while market patterns might look familiar they are rarely if ever repeated. The recent peak was solely due to EU cream/butter prices setting new records (UK £2850/6150), with even the current values £2100/4500 above levels achieved at previous peaks before May 2017 and 14% above the latest GDT. Coupled with the EU Commissions failure to shift any of their 400,000t stock of SMP, despite the opportunity to use the record butterfat values to compensate for low SMP returns. The prospect looms of SMP intervention in 2018 being unavailable or at values that undermines farm gate prices.

The next phase of the dairy cycle will not see another quota abolition, but will encompass the Brexit/transitional period which could be anything from free trade to WTO tariffs and any point in between. Although quota abolition is history it is not yet known whether EU milk producers will respond quickly to falling prices by reducing feeding and thereby lowering production. Less milk is the only remedy for low milk prices.



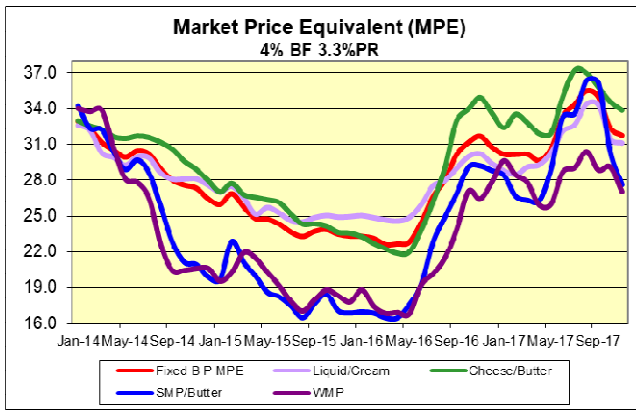
Source: The Dairy Group

The left-hand graph covers the period up to quota abolition which shows that a gentle rise in production was matched by markets and farm gate prices. Low prices in 2012 was followed by poor weather in 2012-13 which produced a sharp drop in production and a recovery in markets. This fuelled the production rise in the run up to quota abolition which then sent markets into a tail spin. The 2007 to 2013-14 period might be considered normal with little political activity, empty Intervention stores and the start of the GDT.

The right hand graph picks up the story from 2014-2017 and shows that whilst production has continued to grow overall, as have market returns, farm gate prices have not. Indeed there is a suggestion in the graph that farm gate prices dropped away from the market in spring 2016 and are only just getting back there now in late 2017. It is worth noting that a relatively small drop in supply is all it takes to lift markets back up to a more sustainable level. Going forward, the faster producers respond to market signals the faster markets will recover.

The key to milk pricing in 2019 will be the supply pattern of 2018, with New Zealand experiencing a drought it is the EU that controls the outcome with average supply growth

of 1.6% per annum in the last three years compared to New Zealand -0.6%. EU production has averaged +2.6% growth since June 2017, the highest of the main dairy exporters and close to 2 billion litres or 10% of New Zealand annual output. The question remains will EU dairy farmers freed from the restraint of quotas respond to falling milk prices by cutting production? Unless they do, the downside of the cycle will be deeper, longer and ultimately more destructive than it needs to be.



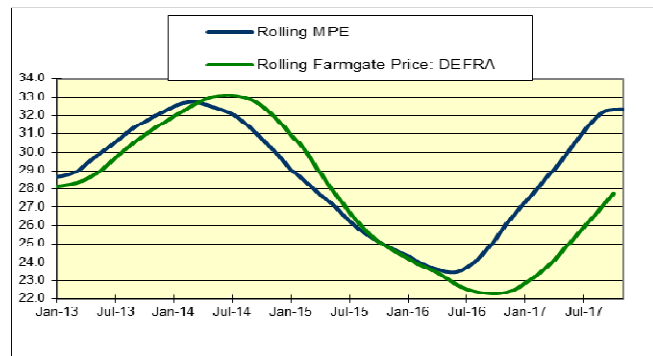
Market Prices

The Market Price Equivalent (MPE) has slipped again, by 0.6 ppl (2%) to 31.8 ppl with all sectors dropping back, due to their butterfat exposure and powders. Butter dropped 10.9% and cream 3.7%, but are still 5 to 18% above levels 6 and 12 months ago. SMP dropped 5.9% to £1270, 16% below Intervention. The range across the sectors widens to 6.8 ppl from cheese returns to WMP. The GDT price equivalent

(GDTPE) has eased to 24.3 ppl and rolling at 27.1 ppl. The GDTMPE fell 6.3% in the month and is flat at 13% in the last 6 months compared to the MPE which fell 2% in the month, but is up 4% in the last 6 months. UK SMP has dropped to £15/t below the last GDT auction and is £245/t below Intervention. Global supply is growing strongly with the US at +2%, New Zealand +2.7% in October and the EU +3.7% in September. New Zealand has experienced drought in November which is extending into December, but EU production is the main driver. With farm gate prices falling in the EU from December 2017, EU production growth may be curtailed by the spring.

Farm Gate Prices

The October 2017 farm gate price soars to 32.3 ppl, the highest since April 2014, is up 8.1 ppl on October 2016 and 5.4 ppl (+20%) since April 2016. The rolling milk price curve will continue to improve into the winter, tracking the MPE curve which is now peaking. November weather has been drier but with most cows housed on full winter rations milk production has taken off. There is a big discrepancy between the daily production figures with the Defra monthly October litres and our calculation of average UK milk price compared with the Defra reported price. They can't both be right and it is the Defra data which is questionable.



Sterling has firmed since the budget to around \$1.35 to the Dollar, but is stable against the Euro at €1.135 as the 1st Bank of England base rate change for more than 10 years materialised. The production for September was 1110 million litres +2.9% and 1109 million litres in October, up 0 million litres on 2016. The forecast for November is thrown in disarray by these figures, but is expected to be 1100 million litres and 1184 million litres for December. Milk prices have moved up rapidly in the last quarter to close the gap to wholesale returns, but with MPE falling are likely to peak in the next 2 months around 32 ppl. Production is rising rapidly in the EU and market returns have fallen, so farm gate prices are likely to fall in 2018, with Muller cutting by 1.5ppl from 1st January 2018. Thereafter with EU production rising the prognosis for 2018 milk price is not good even with a New Zealand drought affecting their production in the short term.

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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.