PRESS INFORMATION from

The Dairy Group

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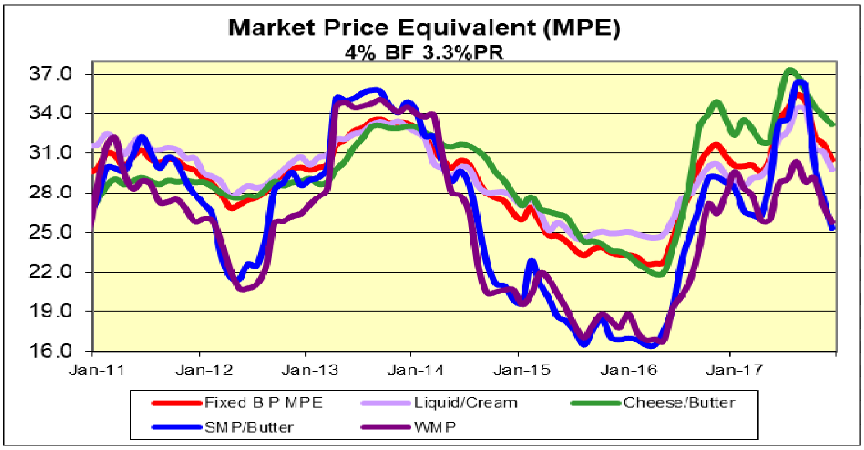
The Market Price Equivalent (MPE) Update December 2017

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

Dairy market outlook for 2018

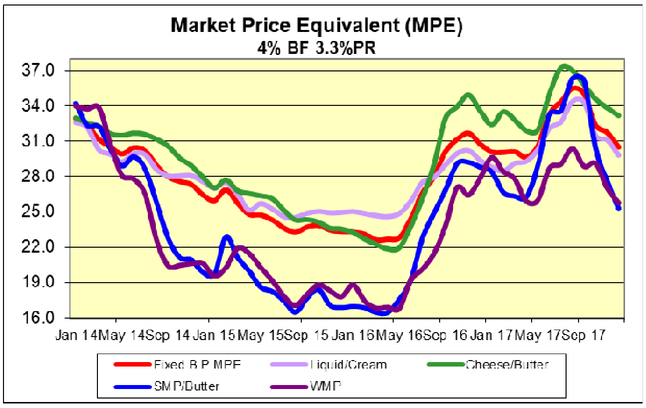
"As this time of the year we look forward to what the New Year might mean for markets and farm gate prices, excluding any dynamic weather effects of course. 2017 turned out as expected, with low milk supply stimulating markets, which in turn has stimulated milk supply to a level that is now stifling markets" says Nick Holt-Martyn of The Dairy Group. He goes on to say "nothing new there except the much promoted butterfat spike in late summer which pushed markets much higher, opening up a massive value gap, with milk powder returns still anchored to the 400,000t EU stock of SMP. The returning of butterfat values to "normal" levels in December leaves MPE values back where the year started, around 31ppl.



Source: The Dairy Group

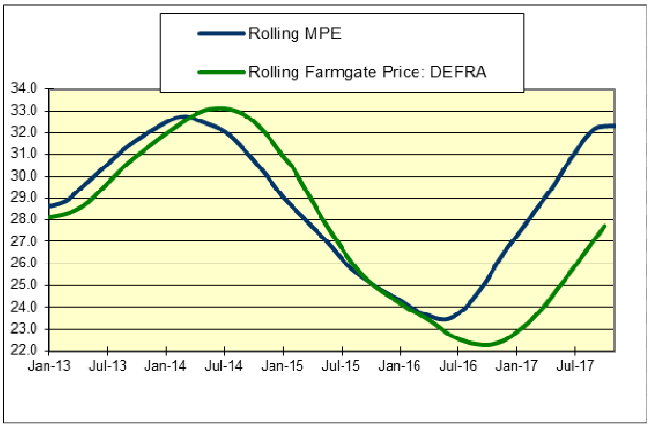
As the chart shows, we have seen three market peaks in the last 7 years, with each peak surpassing the previous. The quota abolition period shows how an unresponsive supply can cause sustained damage to market returns. The faster the supply responds to market signals the quicker markets can stabilise. These patterns in market returns all depend on the milk supply. A more subdued supply growth would limit the market downside. Volatility is not inevitable provided supply remains relatively stable and responsive to market signals.

In the past EU Milk Quota and Intervention have acted as the supply brake for global dairy markets by preventing supply rising too fast and by intervening when markets were low. Arguably, this coupled with a low cost of production and a focused export outlook has enabled New Zealand dairy to grow at twice the rate of the EU (+35% compared to +15% in the EU) in the last 10 years. Market volatility only kicked in from 2007 once the EU intervention stocks had been depleted, also coinciding with the start of the GDT. Volatility is not a given but a result of supply fundamentals. Unfortunately 2018 starts with a large intervention stock (400,000t), September to December milk supply rising (+3%), market returns falling since August (-14%) and farm gate price cuts already signalled by some milk buyers for January 2018. The prognosis for milk prices over the next 3 to 6 months is therefore poor unless supply growth is severely curtailed. Thereafter it all depends on how supply responds to poor market signals and the weather through the EU spring and summer. 2018 may be another year that EU dairy farmers feel the icy blast of market realities, so soon after 2015/16. So it's business as usual and all about milk supply.



Market Prices

The Market Price Equivalent (MPE) has drifted down again, by 1.2 ppl (3.9%) to 30.5 ppl due to all sectors dropping back due to their butterfat exposure and powders. Butter dropped another 11% and Cream 14% and are now only 0 to 8% above levels 12 months ago and down 23% in the last 6 months. SMP dropped 3% to £1230, 18% below Intervention. The range across the sectors widens to 7.9 ppl from Cheese returns to SMP/Butter. The GDT price equivalent (GDTPE) has slipped to 23.2 ppl and rolling at 26.6 ppl. The GDTMPE fell 4% in the month and is down 17% in the last 6 months, compared to the MPE which fell 4% in the month and is down 8% in the last 6 months. UK SMP has dropped to £22/t below the last GDT auction and is £267/t below Intervention. Global supply is growing strongly with the US at +1%, New Zealand +4% in November and the EU +5% in October. New Zealand is experiencing drought although production was up in November. However, EU production remains the main global supply driver. With farm gate prices falling in the EU from December 2017, EU production growth may be curtailed by the spring.



Farm Gate Prices

Defra have corrected the October data on both supply and price to more realistic values. The October 2017 farm gate price at 31.6 ppl, the highest since June 2014, was up 7.4 ppl on October 2016 and up 4.7 ppl since April 2016. The rolling milk price curve will continue to improve into the winter tracking the MPE curve which is starting to ease. Recent weather has been seasonal with some losses due to snow but with cows on full winter rations milk production was running at +4% through November. Sterling slipped through December but has recovered to $1.35 to the Dollar, but has eased against the Euro at €1.125. Milk production for October was 1155 million litres (+4.1% on last year) and 1125 million litres in November (+4.4%). The forecast for December is 1174 million litres (+1.8%) and 1200 million litres (+1.4%) for January. Milk price cuts have been signalled for January by some milk buyers in a response to falling market returns. Production is rising rapidly in the EU and market returns have fallen, so farm gate prices are likely to fall further in 2018. Thereafter with EU production rising the prognosis for 2018 farm gate pricing is not good even if the New Zealand drought affects their production later in the milk season. Unless EU production is curtailed before the spring prices are likely to fall further.

- Ends -

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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.