PRESS INFORMATION from

The Dairy Group

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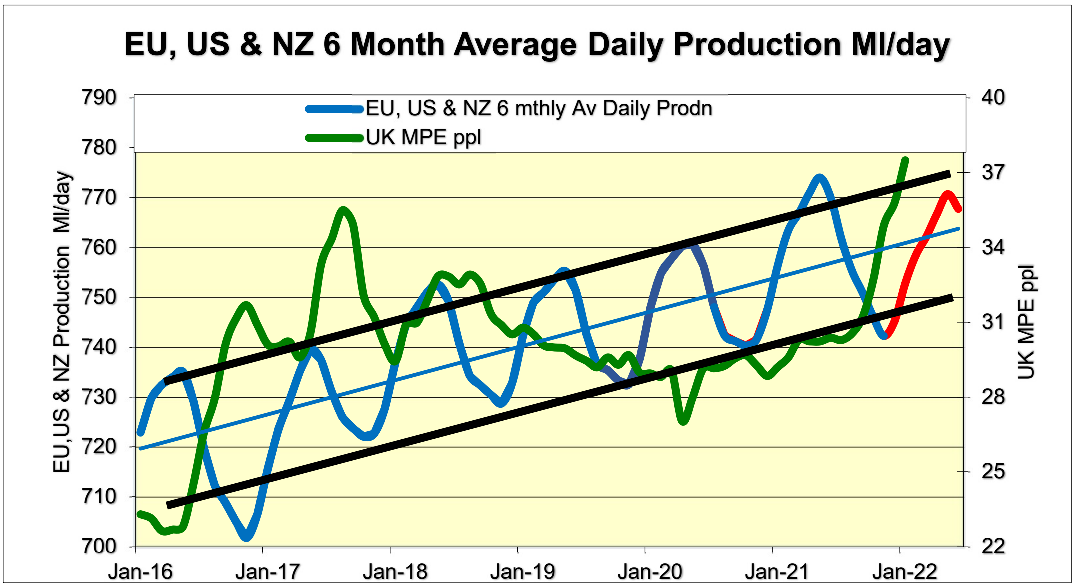
The Market Price Equivalent (MPE) Report

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

It's All About The Supply

"Dairy markets are driven by supply and demand with demand linked to global GDP and the wider economy" says Nick Holt-Martyn of The Dairy Group. He goes on to say "and supply to numerous factors including weather and dairy economics. Demand growth is fairly steady most of the time, recessions and pandemics aside, with annual growth linked to population and GDP means there is an increase in demand over time. Supply can be affected by political interventions, but these were limited to the EU during quota imposition or abolishment. It's unknown what effect a Ukraine conflict would bring other than more uncertainty.

The EU is the major milk producing global block with a significant presence in global dairy trade. The USA and India have large production, but have a much smaller presence in global trade whereas, New Zealand has much smaller production, but the vast majority of which is exported. The dominant players in exports are the EU, NZ and US and so tracking their supply gives an insight into the global supply pattern.

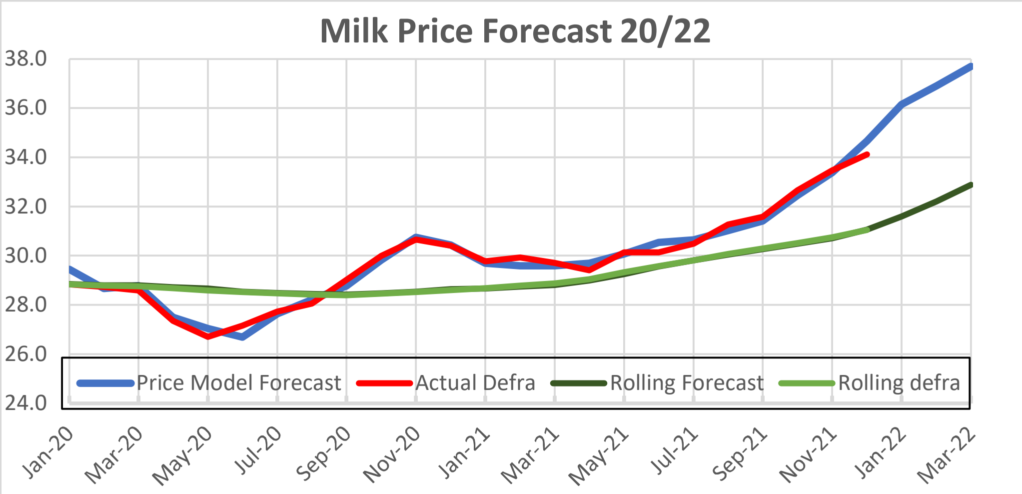


Source: The Dairy Group

The graph above shows the daily milk supply form the 3 leading exporting groups. It is averaged over 6 months to account for seasonal variations and the lag between production and product sales. The blue line shows the normal flow of milk with the dominace of the northern hemisphere producing a summer peak and an autumn trough in supply that coincides with the NZ peak supply. Against that is mapped the UK MPE which reflects the whole market returns and drives the milk price at the farmgate.

When supply stays with the trendline the MPE tends to stagnate as margin is squeezed out by the supply chain. When on the rare occasions supply falls short of the trendline the markets (as shown by the MPE) rockets with the corresponding effects on farmgate prices. As soon as supply responds to the higher prices markets resume their previous track and drift lower towards an equilibrium.

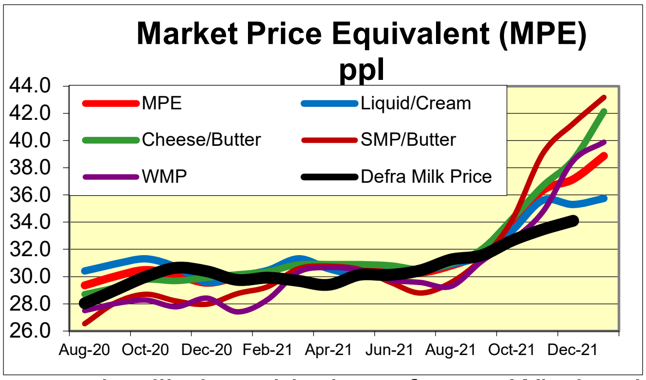
Supply remained strong through 2020/21 which held markets down until July/August when supply growth started to fall and turn into a decline from September onwards. This decline has not yet troughed, but is forecast to continue through to late spring or early summer at the very least. With higher feed and fertiliser prices globally milk supply may not recover until late 2022, subject to the northern hemisphere spring/summer weather. It is possible that the effect of 200% fertiliser price inflation is to reduce supplies of feed and forage, prolonging a fall in milk supply that stretches into 2023. The consequences for market returns are that without increased supply the current commodity price levels will consolidate and become a new base from which the normal seasonal variations will play out.



Our milk price forecast has been lifted again by January market returns towards 39ppl and there is the first hint that the Defra Farmgate price is not keeping up with markets. Our forecast for January is 36ppl, February 37ppl and March 37.5ppl. As things stand and with these prices should set the tone for the 2022/23 milk year with the farmgate milk price set to average 37ppl.

The impact of higher fertiliser prices and the expected 7.5% inflation through the wider economy is uncharted territory for agriculture so determing its effects is difficult. Higher fertiliser prices will lead to a reduction in use which in turn will reduce feed and forage supplies globally. This will almost certainly restrict milk supply in most trading blocks and prevent any recovery to previous levels. The inflation in market prices and the central banks efforts to control inflation is likely to temper demand at the same time as supply remains limited. The timing of these subtle effects are unlikely to coincide and therefore markets could rise higher before any inflation led reduction in demand occurs. Market returns could go higher early in 2022 before consolidating and potentially soften later in the year.

Farmers, processors, retailers and consumers will have to understand that for 2022 a farmgate price of 37.5ppl will be the very least that farmers will need to stay in business. Failure of the supply chain to deliver will result in fewer dairy farmers and a further decline in supply. 2022 and 2023 are going to be challenging for everyone with higher headline prices, but not higher profits. An increase in environmental regulation that restricts activities previously considered good agricultural practice and a phasing out of direct support is likely to test farmer’s resilience in the coming years. 2022 is certainly going to be a test.

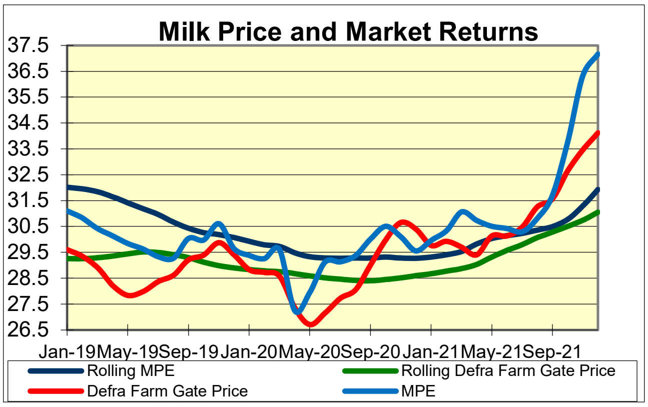


Market Prices

The Market Price Equivalent (MPE) climbs further by 1.7ppl to 38.9 ppl (+4.4%) this month, up 8.6ppl (28%) in the last 6 months and up 8.9ppl (30%) year on year. Products fared differently with Cream down -4% to +6% for Butter. The range across the sectors widens to 7ppl from SMP/Butter down to Liquid/Cream. Weaker supply still dominates the markets and there is no correction likely at this time of year. Wholesale markets are yet to find a settled level despite Cheddar, SMP, Whey and WMP at all time highs. Cream is expected to recover its post Christmas price check to resume its relationship with butter, but liquid prices are not keeping up and acting as a drag on the farmgate price.

Farm Gate Prices

December 2021 farm gate price rose by 0.65ppl to 34.12 ppl, 3.72ppl above December 2020. The rolling Farm Gate price rises to 31ppl. December milk price was 0.5ppl below our forecast, but is expected to rise further. Milk quality slipped slightly from its November record levels.



Production in October was confirmed at 1198 M litres -0.5% (-7 M litres), November at 1168 M litres -2% (-24 M litres) and December was provisionally 1225 M litres, -2.3% (-29 M litres). Based on the AHDB daily deliveries our January forecast is 1230 M litres (-1.8%), February at 1130 M litres (-1.5%) and March 1320 M litres (-1.5%).

Sterling has gained against both the Dollar and the Euro, to £/€1.197 and £/$1.344. The consumer price index reached 5.4% in December and is expected to go to 7.5% as energy price rises take fuller effect. The economic recovery is progressing with UK GDP at above pre-Covid levels despite labour shortages across the economy, border problems with exports and the sharply rising inflation.

The La Nina effects have continued with wet conditions in both Australia and New Zealand and the expected dry conditions in South America. The expectation is for 2022 to see weather move to more neutral conditions by mid-summer. Neutral weather would normally mean production would also recover to a slowly rising level of output, but with global inflation in farming inputs this seems unlikely. Production may not recover until 2023 if output and input values provide sufficient incentive for milk production."

- Ends -

For further information please contact:

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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.