# PRESS INFORMATION from

# *The* Dairy Group

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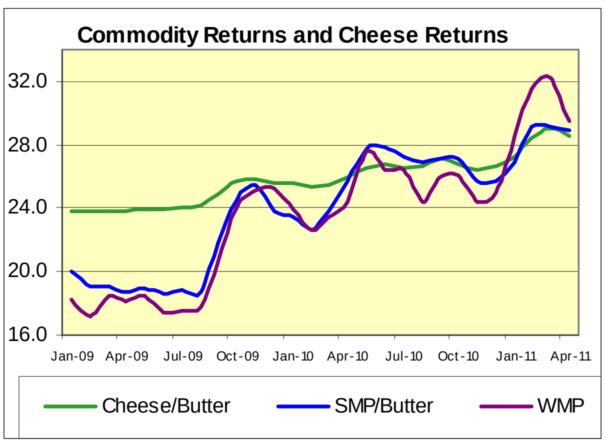
## The Market Price Equivalent (MPE) April 2011

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

### *Formula Pricing Has to Work in All Market Conditions*

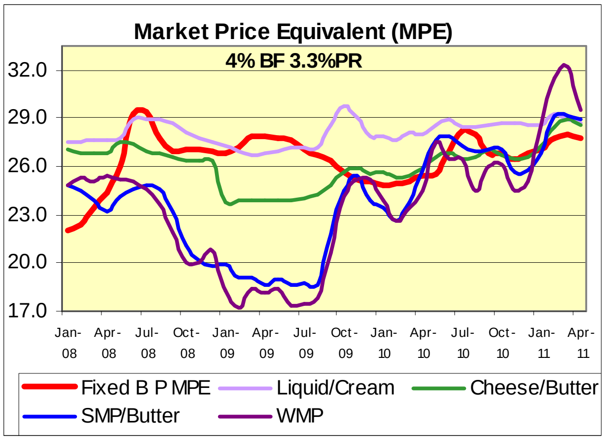
“The suggestion that formula pricing as the answer to reducing the gap between market returns and farm gate prices comes around every 4 years when the UK market fails to deliver price increases to farmers. Some of the retailer contracts have an element of formula pricing, although they tend to weight towards production costs rather than market returns as the main driver of milk price. There is no doubt that a formula price based on commodity returns would have delivered a decent milk price over the last 6 months, but that was in a good market. The question is, how would it have fared in 2009 when milk prices across the EU collapsed” says Nick Holt-Martyn, The Dairy Group. He goes on to say “In April 2009 milk prices in Ireland, Germany and The Netherlands fell to around 22 cents per litre (less than 20 ppl), whereas the UK average price was 23.6 ppl. This led to the emergency dairy package from the EU and the large level of intervention buying that still has a disposable stock of SMP of 50,000 tonnes. Those exposing themselves to the full force of commodity pricing need to understand the global market cycle and the requirement to take the “rough with the smooth”.




As the graph shows cheese returns are much less volatile than commodity returns and underpin the UK farm gate price, with liquid tending to follow a lead from cheese and production costs. It is only 2 years since the last slump when commodity returns dropped below 20 ppl which put significant pressure on UK companies more exposed to the commodity sector. Mild cheddar really falls into the commodity category, but thankfully the UK market is dominated by mature cheddar which accounts for around 75% of cheddar sales. MCVE only reflects the commodity cheese and associated commodity products, rather than the whole cheese sector and will tend to be more volatile than a measure of the whole cheese sector as shown above.

The easing of world markets looks like being tempered by dry conditions across the EU and adverse weather in the US, which is reducing expectations of an expansion in northern hemisphere production this year. The prognosis is for settled markets through most of 2011 until the next southern hemisphere production season is well underway. This should mean there will still be room for more farm gate price increases as the higher market returns feed back to the farm gate."

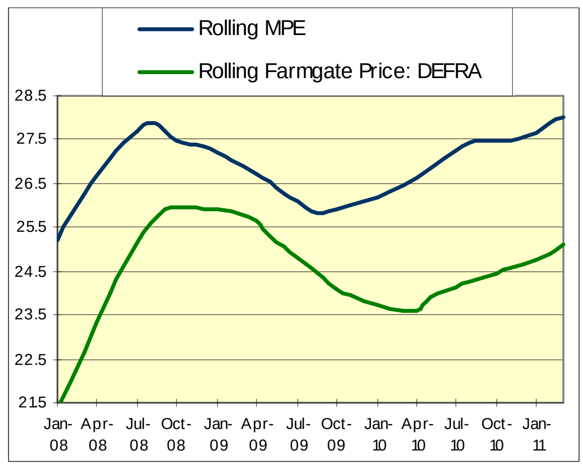
***Market Prices***




The mild cheddar price has eased along with most commodities, except SMP, to lower the Market Price Equivalent (MPE) by 0.25 ppl to 28.7 ppl. The Northern Ireland auction price slipped again to 25.85 ppl with lower commodity returns. The Fonterra auction saw prices largely unchanged. The (MPE) is up 0.7 ppl since October 2010 and up 1.6 ppl on last year. The market fundamentals are still sound, with dry weather starting to limit the spring flush in the EU. Globally demand is stable, so the market is largely driven by supply side sentiment which is currently stable.

***Farm-gate Prices***

Milk price rises are coming through thick and fast with most producers seeing increases this spring. The largest increases have come in the cheese sector with the rise last month in mature cheddar prices. As these prices feed into the rolling milk price the gap with market returns will start to narrow. The UK is still languishing in the lower levels of the EU price league and seems destined to remain there until commodity prices fall some time in the future. With stable market returns in 2011 the UK position will reflect the ability of the UK market to deliver returns to the farm gate.

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