PRESS INFORMATION from

The Dairy Group

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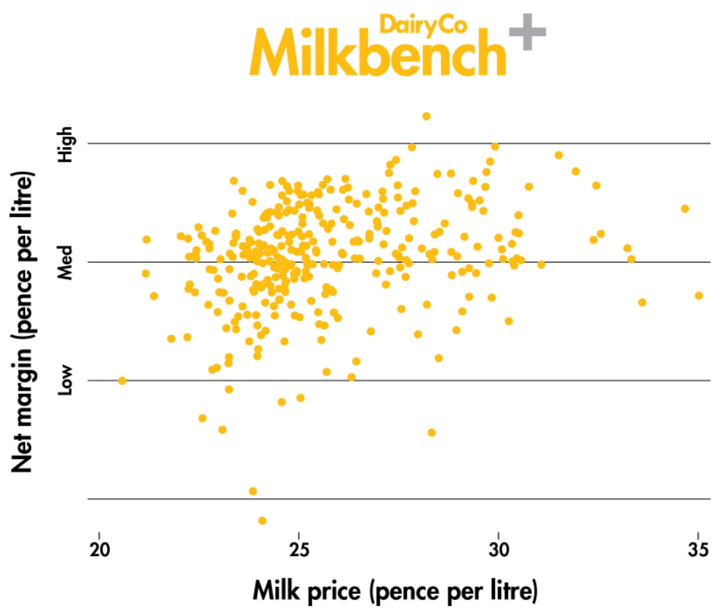
The Market Price Equivalent (MPE) January 2012

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

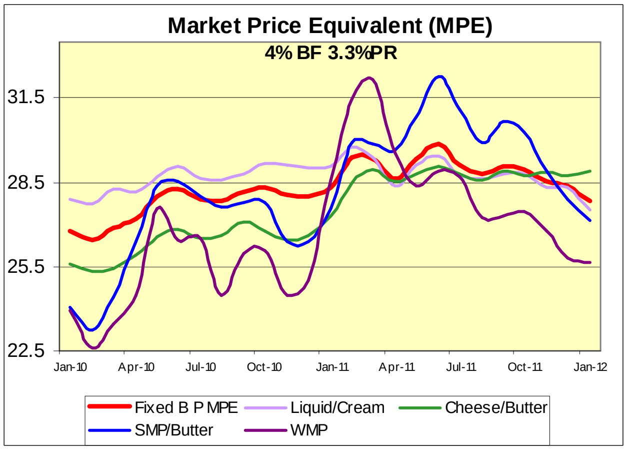
Processors: Milk Price Is Still Important

"DairyCo's first key finding in their Milkbench 2012 report is that 'The key determinant of profit is total cost of production, not milk price' while statistically correct this should not be seen as allowing milk processors to pay less for milk. With the UK just 16th in the EU milk price league, 6% below the EU average, there is still room for the UK to do much better given the UK market structure." says Nick Holt-Martyn of The Dairy Group. He goes on to say "While producing profit from milk production is possible across the milk price spectrum, changes in milk price can still have a dramatic effect on profitability.



Source: Profiting from Efficient Milk Production, Milkbench Report 2012, DairyCo

The graph above still shows a trend to higher profitability with rising milk price, although perhaps not as clear as many farmers would like. For an individual farmer a movement in milk price will affect profitability without affecting production costs. The retailer milk price premium is worth up to 3.8ppl, so the loss of a retailer contract would have a large effect on profitability without much reduction in the production costs. Some retailer contracts do incur direct additional costs, e.g. for Non GM feeds and to achieve lower saturated fatty acid content, so whilst these direct costs would be saved the remaining production costs would still be incurred. Milk price needs to reflect market returns to enable producers to be competitive. With the UK consistently below the EU average where is the export led expansion of competitively priced UK milk into the single market? UK processors fail to deliver a share of market returns comparable with other EU countries, which is why milk price will always be a key issue affecting profitability even though individually milk producers have little power to affect a change. Production cost control will remain the focus to drive higher profits and for the individual business milk price is an important component of profit."

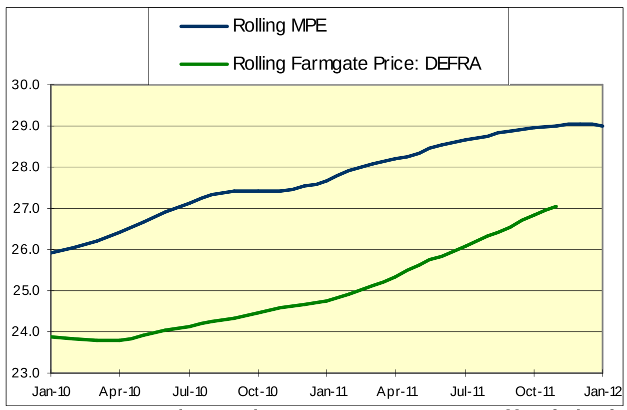


Market Prices

The Market Price Equivalent (MPE) slips again by 0.52 ppl to 27.85 ppl after further falls in SMP, Cream and Butter returns while Cheese remains stable. Whey returns are still showing some upward movement overall. Cheese returns remain higher than liquid and showing considerable stability. The Fonterra auction saw minimal movements with stability across all categories. New Zealand production is rolling +8% on last year, but easing, while both the US and EU show 1 to 2% growth. The MPE is now down 0.49 ppl on the year and 1.27 ppl lower since July 2011. The rise in the whey price remains a positive market indicator.

Farm Gate Prices

The graph shows rolling market returns have just peaked while the rolling farm gate price continues to show a new record high each month. The gap between market returns and the farm gate milk price will narrow as the normal 5 month time lag unravels. Farm gate prices will follow markets and flatten out at current levels. With market returns down 2.0 ppl since peak there will be increasing pressure for downward movement when UK milk supply picks up in the late spring. Provided New Zealand production continues to ease then the pressure on off global markets would reduce and stability could be maintained.



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For further information please contact:

- **Nick Holt-Martyn,** The Dairy Group (01823 444488/e-mail: nick.holt-martyn@thedairygroup.co.uk)
- **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.