PRESS INFORMATION from

The Dairy Group

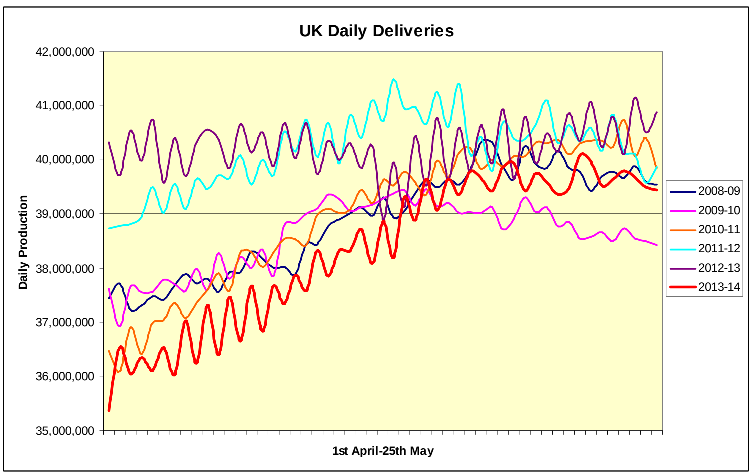
3rd June 2013

The Market Price Equivalent (MPE) Update May 2013

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

Production volatility and the danger of formula pricing

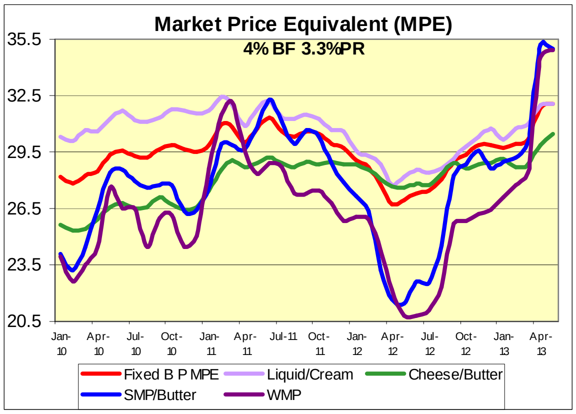
"The cold slow spring has finally given way to at least average conditions as we start summer, which should sustain production well into June," says Nick Holt-Martyn of The Dairy Group. He goes on to say "from a very low position in early April production over the last fortnight is now ahead of 2009 and on a par with 2008 and 2011, but behind 2010 and 2012. With good quality grazing and silage aftermaths not far ahead production is likely to hold on better than previous years provided the weather maintains its mix of sunshine and showers", he continues. "While daily production might be "normal" what can't be corrected is the accumulated deficit from low production in recent months, so the forecast for 2013-14 is not a recovery to the 2011/12 level (13.5 billion litres), but a resumption of the norm of 13 billion litres.



Source: The Dairy Group

As the graph shows April production is very volatile due to a combination of production coming out of winter and the spring weather. When both are good April can be as good as May, but as we have just seen, when they are bad production struggles. The effect rolls into May, but diminishes as there is usually a bit of better weather to lift production. The end of the spring flush doesn't seem to vary and by the 1st June it is all over for another year. The key weather affect is the rate of decline; too wet or too dry and production falls rapidly, whereas an average mix of rain and sun, production declines more gradually. The inability to control production in April plays havoc with production incentives at this time of year. However, now the flush has passed management becomes a greater influence on production levels.

Market volatility which stems from supply volatility outlined above is leading to more formula pricing for non-aligned producers. This is a great concern as farmers are being invited to link to an AMPE (actual market price equivalent) based farm gate price. It is worth reflecting that although today AMPE is 38.6 ppl only 12 months ago it was 22.1 ppl. In a post quota EU if a 1 billion litre swing in New Zealand production can trigger a 16 ppl rise in AMPE what will be the effect of a 2.5 billion litre rise in EU production? In whose interest are these pricing mechanisms designed to protect? It protects the processor who can say to its customers legitimately that markets have moved and prices need to change. Customers can do the same to processors and will be quick to point out that AMPE has crashed when quotas are abolished!

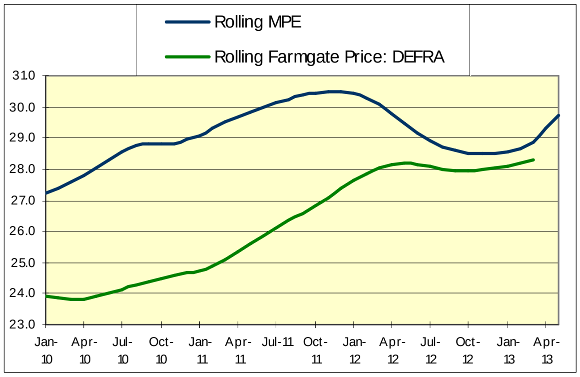


Market Prices

The Market Price Equivalent (MPE) has increased just 0.17 to 32.04 ppl due to rises in Cheese, but easing in Butter and Whey. The range across the sectors is not sustainable with a 4.5 ppl spread so prices will need to converge. Cheese should rise to be more competitive with powders, but also powders are likely to be easing due to the Fonterra auction. The change in the powder sector over the last 12 months is an alarming 15 ppl which is a warning to anyone linking their farm gate price to the AMPE. The latest Fonterra auction was down 2.1% due to autumn powders, but mostly due to short term butter values. The MPE is now up 5.1 ppl on the year and up 2.2 ppl since November 2012. New Zealand production has collapsed and is likely to end the year +3% (+600 M litres) compared to +10% (1.8 B litres) in 2012. The UK is still running 3% below last year, but rising and is likely to come close to 2012 in June.

Farm Gate Prices

The graph shows the rolling MPE continuing to rise sharply due to commodity prices with UK milk prices lagging behind, but increasing to over 30ppl from June. The rise in cheese, a major MPE component, is pushing the MPE higher, increasing the pressure on milk prices to respond. The cold late spring has slid into an average summer with positive effects on production, but confidence will remain low until feed prices start to fall and forage stocks are replenished.



- Ends -

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.