PRESS INFORMATION from
The Dairy Group

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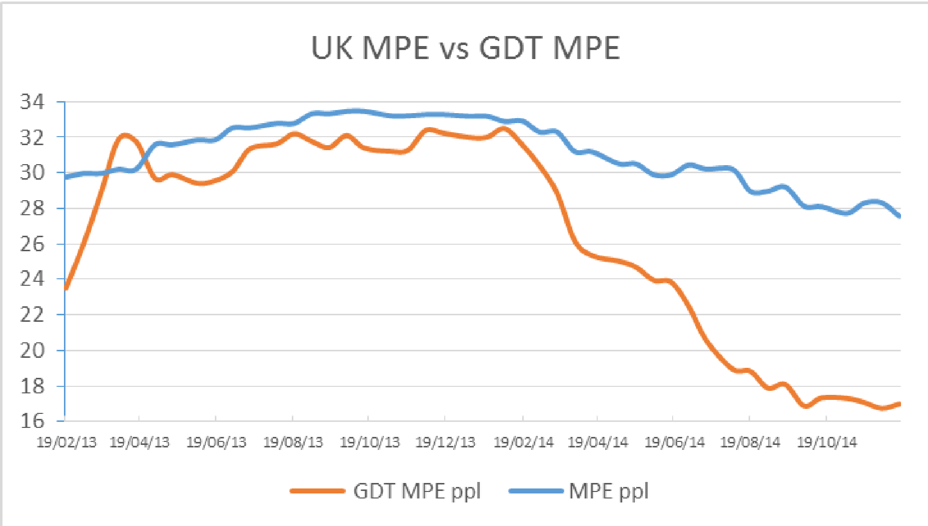
The Market Price Equivalent (MPE) Update December 2014

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

Further price falls provides a gloomy start to 2015

“Having been a portent of doom for the last year I was going to write how 2015 could be a bit better than we all fear, with low oil prices, a rising El Nino and normal market forces helping markets to stabilise as we reach the bottom of the cycle.” says Nick Holt-Martyn of The Dairy Group. He goes on to say “That was until Arla lopped 8% off their milk price for January to take their declared price to 24.19 ppl, below the 25 ppl threshold, a level I didn’t think would be reached by the big two until April 2015 and which would signal the bottom of the current cycle. With the GDT bumping along the bottom for the last 3 months at 17 ppl equivalent, we can only hope that the UK price won’t fall any lower.



Source: The Dairy Group

The graph shows how the GDT dropped away through 2014 to hit rock bottom in October just after the GDT had sold 50,000t in a single auction, the highest for a year and 10,000t more than the previous auction. While I don’t think they could have prevented the decline it does seem a bit reckless to offer so much product on a market that had lost 33% of its value in the previous 6 months!

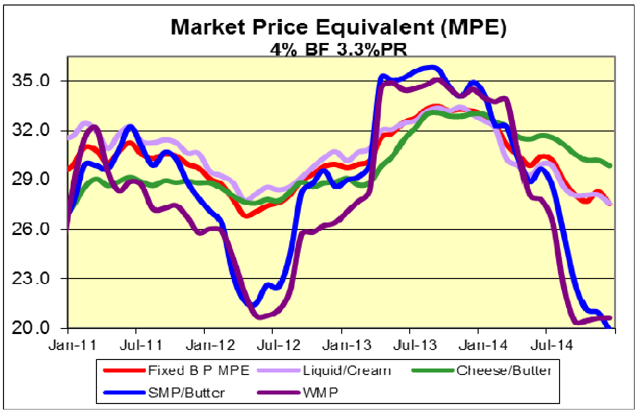
The MPE has dropped away too, but is buoyed by liquid and cheese returns which are much more stable than the commodities. Liquid and cheese returns are still around 27 to 30 ppl compared to 20 ppl for the powders and still takes around 75% of milk, albeit down from nearer 80% in December 2013 due to the growth in UK supply. The GDT is dominated by WMP and SMP (85%) with Butter and Anhydrous Milk Fat the only bright spots, although still priced 10 to 15% below the UK.

Arla is currently a weak player in terms of their UK milk price due to its pan-European price policy which doesn’t necessarily reflect on the level of UK returns. It is probable that the UK arm is helping to deliver a higher Arla price for all its members than would be otherwise achievable. While UK members might be doubting in hindsight the wisdom of the merger, a glance at First Milk’s position might reassure them that things might have been worse not better! For Arla, with its 13 billion litre northern EU milk field and broad product mix, comparisons against UK competitors may be unfair and more likely to look to Campina Melkuine which has cut its December price by 11% to 24.3 ppl, which is similar to Arla.

Based on Arla's own reporting, Arla's product mix is weighted 77% towards fresh products and cheese with 15% in spreads, leaving little exposure to powders, but has their position has weakened with the Russian import ban, supply growth and collapsing markets. The likelihood is that just as in the UK, powders have taken the lion's share of the supply growth and the milk released form formerly Russian bound product, has weakened the product mix and as a consequence their weighted returns.

No comfort for UK members who had expected a better future from the over-hyped nonsense about dairy opportunities in expanding dairy markets from those who should know better. The truth is that the future looks and behaves much like the past only with a lot more milk in it. Plans for dairy expansion post quota in Ireland for example did not appear to consider what the effect would be on milk prices if they were joined by Germany, Holland, Denmark, Poland and others in this liberated dairy world. With the Irish Dairy Board forecasting a 2015 milk price of 20 ppl and 10% growth in supply the effect is all too clear. The spectre of a greatly extended PSA and even Intervention is starting to loom on the horizon!

As always, an individual dairy farmer can do little to buck the market and external issues and they will need to focus inwards on lowering their cost of production. The point of economic optimum for a business is being shifted back with each fall in milk price and farmers will need to know what their cost of production is to adjust their system to their milk price. This will mean in the first instance targeting low yielding groups with intensive grazing and much less concentrate feeding. 2015 will be the year to make the feeder wagon redundant for the summer, join a feed buying group and feed low protein cake at grass, now that will be a challenge!

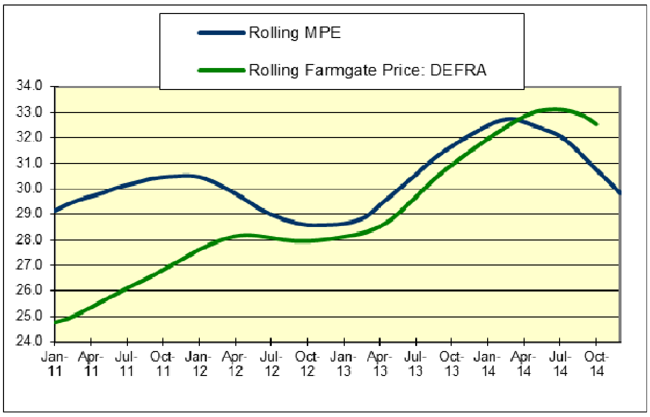


Market Prices

The Market Price Equivalent (MPE) has slipped 0.8 ppl to 27.6 ppl due to falls across the sectors as the Christmas surge passes. The range across the sectors increases to 10.0 ppl between Cheese/Butter and SMP which has now fallen to £1425/t ~ its lowest level since August 2009. The latest GDT auction was up 1.5% in Sterling equivalent, but a mix of rises and falls between sectors and contract periods, with butterfats up but powders stable to down. The GDT price equivalent (GDTPE) is up to just 17.0 ppl from a low of 16.7 ppl the previous auction. The MPE is down 5.64 ppl on the year and down 2.89 ppl since June 2014. Production globally is still rising but the rate of increase is slowing and is expected to almost stop as the EU nears the quota year end. New Zealand production is running +4.5% in October and on course to achieve +8% in 2014, the US is now running +3.4% in November while the EU is at +4.6% in September. With supply still growing at 4% markets are unlikely to improve until the autumn/winter 2015 at the earliest.

Farm Gate Prices

The graph shows the rolling MPE falling back as market returns drop away, on course for 2012 levels in the spring. The rolling farm gate price is tracking the MPE as expected, with a significant fall likely by the end of the year. The weather remains relatively benign globally, but there is a 70% chance of El Nino which should increase the chance of droughts in key dairy areas. Oil prices have fallen again helping to reduce the cost of production, but future grain prices are on the rise which will be a concern for 2015/16 feed prices. UK production is running 3% ahead of last year with December forecast at 1180 million litres and January 1200 million litres, so the UK is on track to finish the last ever quota year at 14.45 billion litres, 750 million litres below quota butterfat adjusted. The easing of the rate of increase is unlikely to be related to milk price, but just that the better feeding over the last 18 months is fully reflected in the output and further increases will now require an increase in cow numbers as well as genetic merit. The prognosis for 2015 is an increase of 1 to 2%, but subject to a reaction to low milk prices.



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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.