PRESS INFORMATION from

The Dairy Group

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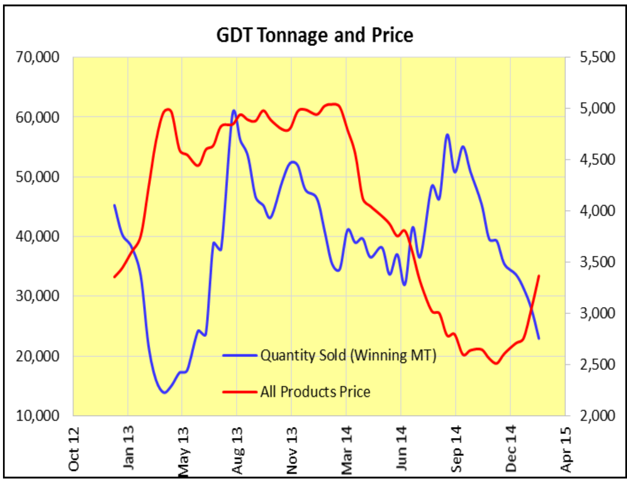
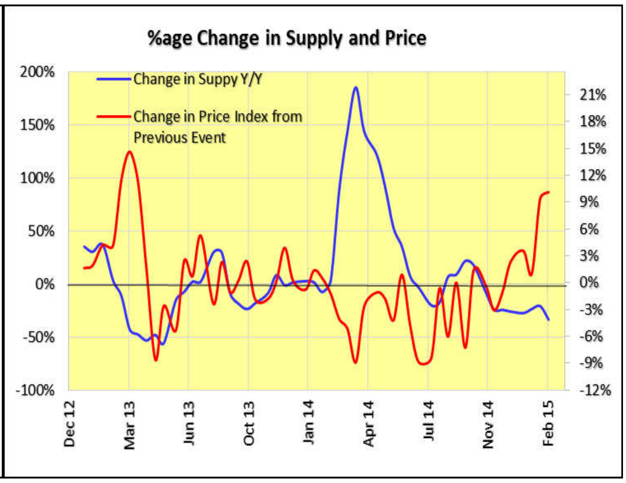
The Market Price Equivalent (MPE) Update February 2015

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

How good is the GDT as a Barometer of Dairy Commodity Prices?

The GDT was launched with lofty ambitions in 2008 to deliver the following "The goal has been to create transparency, establish market prices, reveal credible market information, and promote liquidity in dairy trade—a win-win for both buyers and sellers and a model for many other markets."(CRA's President and Chief Executive Officer *Paul Maleh July 2013, Boston (Business Wire)*, CRA is the independent trading manager of Global Dairy Trade). But what we have witnessed in the last 6 years is a roller coaster of boom and bust with 2015 starting off on another round of boom." says Nick Holt-Martyn of The Dairy Group. He goes on to say "The 33% price rise on the last 6 auctions is welcome, but with a corresponding 46% cut in tonnage offered indicates that supply to the auction appears to be driving prices and not the wider availability of product. These are familiar problems for markets with large sellers; think back to Milk Marque and Opec. When auction markets get too big instead of transparency in the setting of market prices they become market drivers themselves and their internal supply/demand dynamics increases volatility.



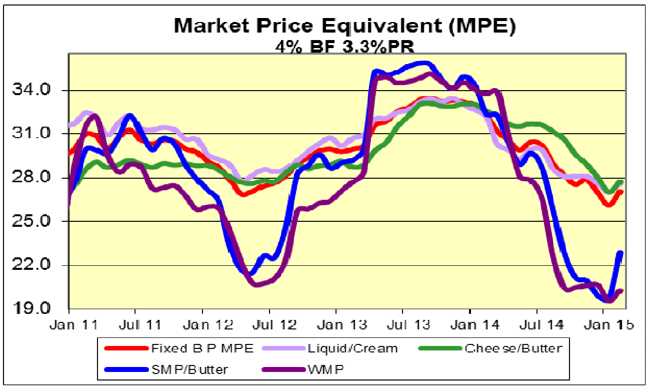


Source: http://www.globaldairytrade.info/en/product-results/
Analysis by The Dairy Group

The first graph above shows the GDT Tonnage and price achieved over the last 2 years. 2013 shows a decline in tonnage offered on the back of low global milk supply and the resulting rise in market returns. Supply recovered as the New Zealand season got under way and market returns were sustained into 2014. Supply to auction followed the normal seasonal track, but with milk production soaring all round the world more product was offered into the auction. The result was that prices started falling in March 2014 and after 3 months of falls supply to the auction was ramped up following the seasonal pattern which forced markets to fall for another 3 months. It was only when supply was cut did auctions stabilize and with successive cuts in supply we now have auctions that are rising again.

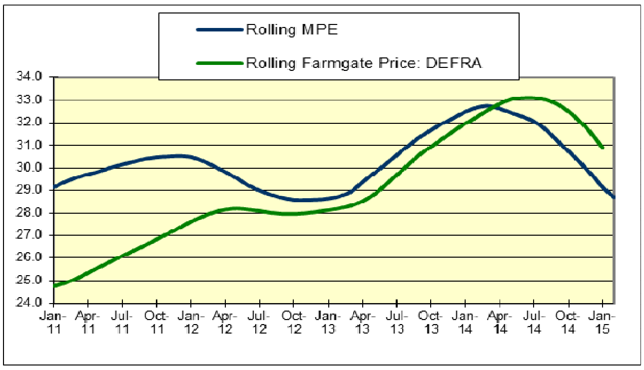
The 2nd graph shows how supply compared to the same auction the previous year and the change in price index from auction to auction. This shows the sensitivity of the index to supply. During periods when supply is stable the index is more stable, as soon as changes in supply are more marked the index reacts more violently and volatility is encouraged. The larger the market and the imbalance in the size of sellers the more likely this will occur. When prices start to fall, particularly if the supply signals are positive, sellers will increase supply to maximize sales at higher values and to reduce the quantity of stock held at lower values. Buyers do the opposite, no need to buy if next month prices will be lower. Sellers offer more product while buyers hold back and the market plummets. Eventually sellers cut supply and hold stock back and markets stabilize; if supply is cut enough markets will rise.

The GDT needs to reflect the external markets factors of supply and demand and be immune to any internal supply/demand dynamics of its own; it should not be driving global prices but informing them.



Market Prices

The Market Price Equivalent (MPE) has jumped 1.0 ppl to 27.1 ppl due to rises across the board. The range across the sectors remains at 7.4 ppl between Cheese/Butter and WMP. SMP which has increased to £1700/t and Butter at £2500/t are at or marginally below the latest GDT auction which was up 10.2% in Sterling equiv. with some rises in most commodities and contract periods. The GDT price equivalent (GDTPE) is up to 22.8 ppl after 6 successive rises. The MPE is down 5.2 ppl on the year and down 1.91 ppl since August 2014. New Zealand production is now running 0.3% ahead in January, but achieved annual growth of +8.4% in 2014, US is now running +2.1% in January with annual growth of +2.4% while the EU is at +2.3% in November and on course for annual growth of +4.3%. The New Zealand drought and lower supply to the GDT auction (-45% year on year) are driving market improvements.



Farm Gate Prices

The graph shows the familiar pattern of rolling MPE falling back as market returns drop away, down to the 2012 level. The rolling farm gate price is tracking MPE as expected with a significant fall in January as monthly prices replace the higher values 12 months ago. The weather has remained wintery for 6 weeks in the northern hemisphere and severe dry weather is impacting on New Zealand production, but Australia has seen rain. The El Nino risk has gone for another year so weather is expected to be normal. Oil prices are rising again which poses a challenge to falls in the cost of production. Sterling is rising further against the Euro making UK dairy product less competitive and dampening the upturn in farm gate pricing. UK production is running 1% behind last year with February forecast at 1080 million litres and March 1250 million litres, so the UK is still on track to finish the last ever quota year at 14.4 billion litres, 800 million litres below quota butterfat adjusted. The expectation for the new milk year is flat (at or below 2014), but subject to weather, spring calving and the numbers of out-goers. There is likely to be some expansion from existing producers, but this is unlikely to out produce the retirees. The prognosis for 2015 is a reduction in production to 14.1 billion litres, but subject to a reaction to milk prices which should begin to rise.

- Ends -

<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.