PRESS INFORMATION from

The Dairy Group

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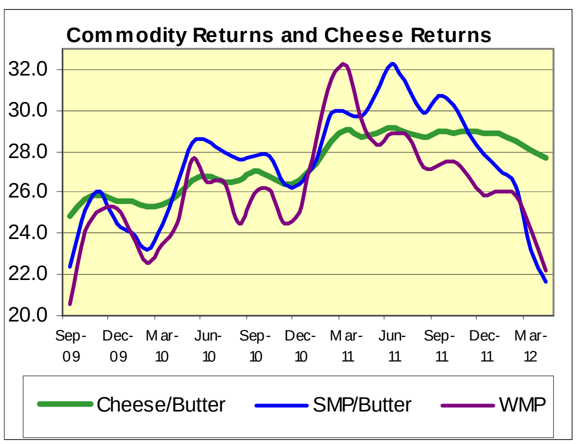
The Market Price Equivalent (MPE) April 2012

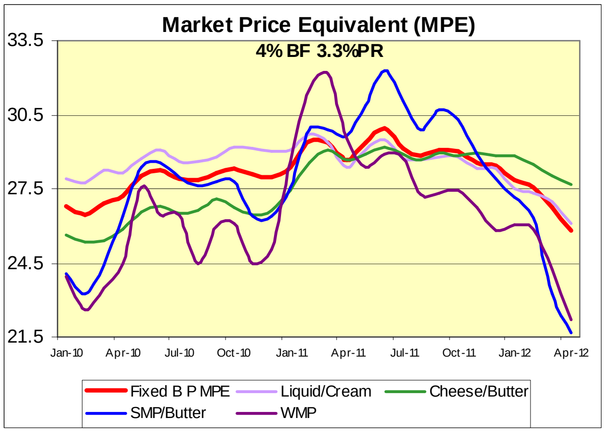
***By Nick Holt-Martyn,* The Dairy Group**

Uncertain summer for the dairy industry

“The collapse (-10%) of Fonterra’s GDT 17/04/12 auction has raised the prospect of EU Intervention for the summer of 2012, but all may not be so certain” says Nick Holt-Martyn of The Dairy Group. He goes on to say “While it is true to say that milk production around the world in on the up (EU, USA, Australia +4%, New Zealand +12%) and demand growth (GDP) has moderated to below 2% (OECD GDP growth) the market appears to be in a chronic oversupply situation. A market tone that in most circumstances heralds a decline in market returns across the world irrespective of domestic issues. However changes to the contract structure of GDT to a monthly basis at the next auction may have exacerbated the fall, although the very strong finish to the New Zealand milk season will have been the main trigger. For the UK the picture is more mixed with the worst April weather for at least 10 years stopping the spring flush in its tracks. With the weather forecast indicating a continuation into May, a flat production peak is likely, which could help to dampen the market.



The graph above shows the decline in commodity returns over the last 6 months to a level not seen since August 2009, which has not been helped by the Pound rising to its highest level since October 2008. All this only serves to heap more pressure on the cheese sector, which to date has been resilient to a price decline due to the relatively low cheese supply. The Dairy Crest cut in the non-aligned liquid price by a massive 2 ppl is further evidence of the slim margins and cut throat competition in the once premium liquid sector. The cheese sector and the retailer aligned liquid milk pools by contrast are the premium sectors now with the whole market beholden to their resilience to market pressure. High production costs mean the room for farm gate prices to fall back is limited without serious consequences for UK dairy farmers. The Dairy Group, Promar and Kite have all published production costs of around 30 ppl, with The Dairy Group projecting a small increase in 2012/13. With the UK now 13th in the EU price league the gap between production costs and market returns will begin to raise concerns about the ability of the UK to suffer large cuts in Single Farm Payments. It is little wonder that producers favour pricing mechanisms based on production costs instead of market returns, as there is little confidence or even evidence that markets can deliver sustainable milk prices.”

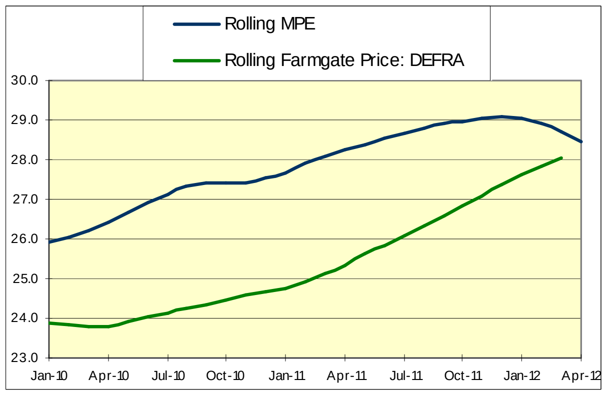


Market Prices

The Market Price Equivalent (MPE) fell by 0.92 ppl to 25.79 ppl after further large falls in SMP, Cream and Butter returns, while Cheese remains stable with only a marginal affect from Cream and Whey. The weakness in cream is also affecting liquid returns while lower butter values are lowering cheese returns. The latest Fonterra auction saw falls across all categories in mostly short and longer term contracts with changes to contract dates and strong autumn production. The MPE is now down 2.9 ppl on the year and 3.2 ppl lower since October 2011. With adverse weather affecting parts of the EU supply may be constrained, although May brought adverse weather in 2011 as well.

Farm Gate Prices

The graph shows the gap between market returns and the rolling farm gate price narrowing as rolling prices continue to climb, although the monthly price has now peaked due to seasonality. The fall in market returns is so rapid that there is the possibility of the lines crossing which will bring pressure on prices. Farm gate prices will eventually follow markets with pressure likely from mid-summer and particularly next winter. The solution to a weaker dairy market will be a tighter milk supply rather than a rise in demand which is far less elastic.



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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.