

EU Dairy Markets, Situation and Outlook May-August 2010

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Special report produced for CLAL

Highlights:

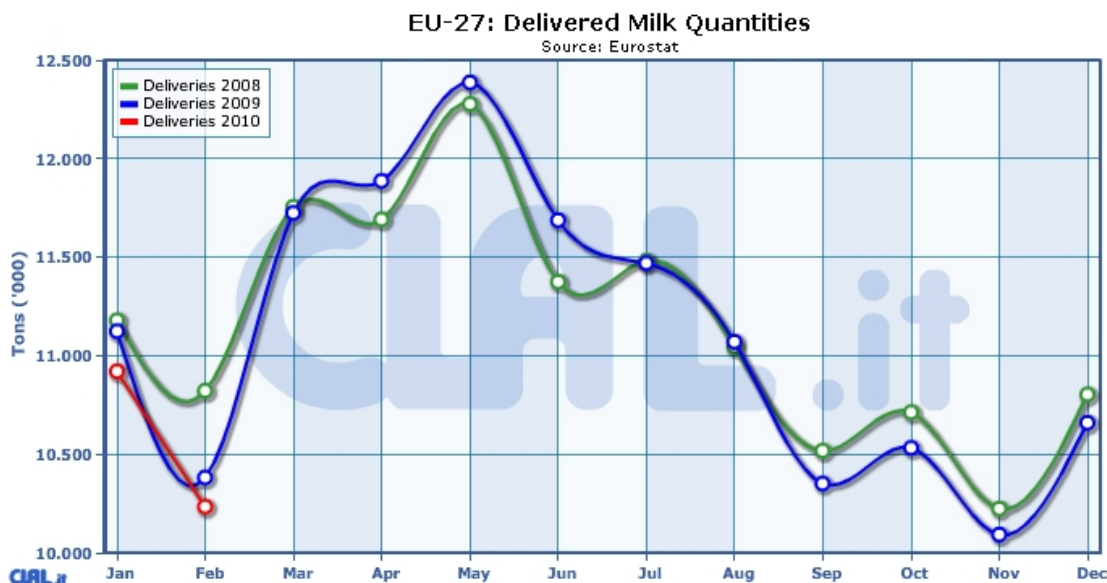
- Milk supplies going down seasonally, gap to quotas widening
- Milk prices for farmers rising and ahead of last year
- Production of butter and SMP significantly reduced, which results from lower milk production and more milk being used for cheese manufacturing
- Demand from international markets boosted by reduced prospects of global milk production and weakness of the Euro
- Butter supplies are tight and will already be short in relation to demand in June 2010.
- Also SMP supplies will be reduced and intervention stocks will be needed to cover demand.
- Milk prices in major EU countries will be driven upward by increasing world market prices when expressed in Euro terms.

Milk Production

EU milk production has reached its seasonal peak by the mid of May, with some countries being ahead (France) and others being later (Poland, the Baltic). When compared to the year before milk production was reduced in the period from September 2009 until now and the recent data which are available from the Netherlands i.e., where production had been expanding until the end of 2009, now also reveal stagnation. Only in Germany and Austria recent data show a modest expansion now again. In the first trimester of 2010, milk deliveries to EU dairies are estimated to be reduced by more than 1%, which means at least

0,4 million tones less than the year before. This reduction has mainly to do with reduced expectations of dairy farmers as result of low milk prices. Unfavorable weather conditions which prevail until now have a minor impact (their influence almost used to be overestimated). Differently from earlier years there was no country where farmers had to reduce milk deliveries in the first trimester to avoid super levy payments, therefore no quick recovery to expanding milk supplies after the deadline of March 31, when the quota year 2009/10 ended, could be observed. In this projection, it is assumed that milk supplies in the EU will be reduced by 0,5 million tons. Since this has already happened in the first four months, it seems to be optimistic to assume that supplies might be on 2009 levels for the rest of the year. Should that optimistic view of the milk deliveries not come true, markets will be more tight on the supply side than discussed in the following.

On the world level, after the year 2009 with only poor expansion of milk production also no quick return to earlier growth rates is likely. In Oceania it is now the low season with ending of the dairy year in New Zealand as of May 31 and in Australia as of June 30. In Australia milk production is reduced, and in the North island of New Zealand the last months were unfavorable due to weather which lead to earlier reducing of milk production. In Latin America growth expectations are also only moderate, whereas in the United States recent figures show expanding milk production again. No expansion is likely in Russia, and in Ukraine no recovery from the last year's decline is in sight.



Demand boosted by Cheese and International Markets

Long term projections of the worldwide demand for milk and dairy products calculated the annual increase of demand at 12 to 14 million tons in milk equivalent. Times of economic crisis are the exemption. But now many signs in the markets give scope for again rising demand, whereas now the second subsequent year with only small or no increases on the supply side is going on. As most of the world market suppliers are sold out, demand is now focussing the EU market as potential source, which is supported by the weakness of the Euro as result of the state debt crisis risk of several EU countries. Also demand from the EU domestic market is rising again now, but with modest rates and in particular mostly in the cheese sector.

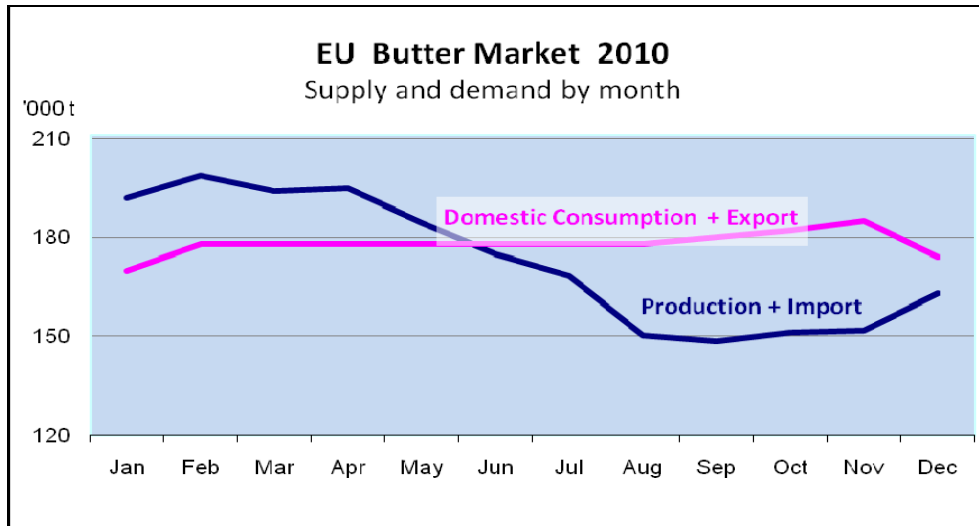
Exports of butter, cheese and SMP were higher in the first months of 2010 than the year before. SMP exports were almost doubled, whereas whole milk powder exports were slightly reduced. But WMP production was expanded in the Netherlands and France, which is likely to result from stronger demand for exports, which, however, was not yet visible in the EU export data for the first months but might appear in figures which are published later.

Combined with reduced milk supplies and stable demand in the other sectors significantly less milk is left for the manufacturing of butter and SMP, whereas more volumes of both products are required from international markets and in particular more butter should be stored in private stocks to balance the domestic market in Europe after the peak production season of spring and early summer.

The Butter Market

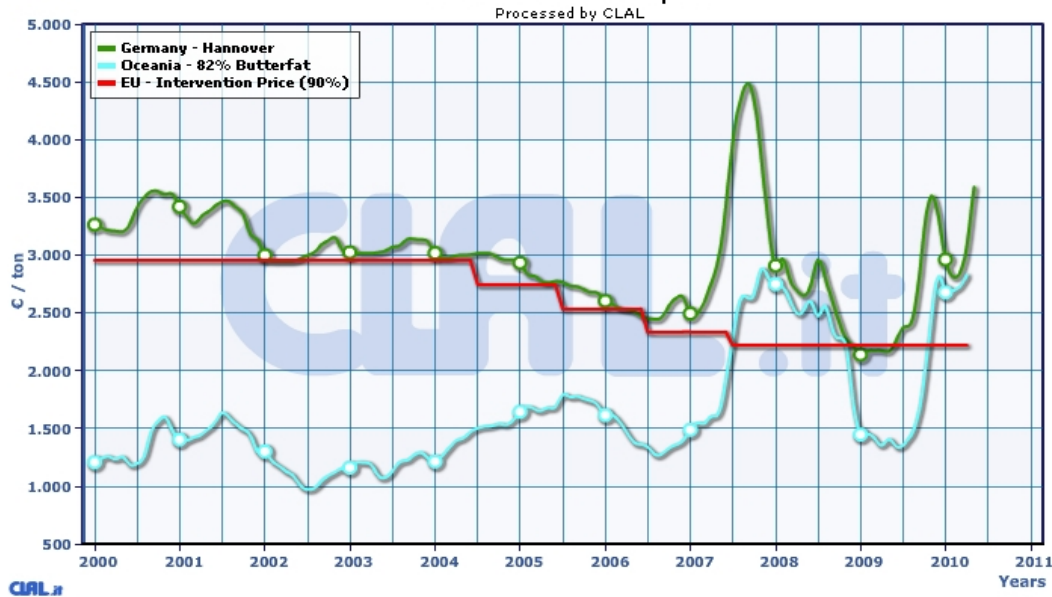
With a declining butter production, unchanged domestic consumption in the EU and growing exports, the butter stocks of the EU will be reduced. So far no butter was sold to intervention agencies and, as prices are significantly over intervention levels, it will not happen this year. Parts of the stocks in intervention are cleared by the scheme of butter donations. Concerns that this would disturb the retail market have not been confirmed. Inventories in private stocks which are needed to fill supply gaps later in the year are significantly lower than last year, therefore it seems to be necessary to take more butter in the period until the end of August, but the market is short. If present developments

regarding milk supply and export demand continue, it will be hard to build up enough private stocks, because already in July production will be short of domestic and export demand.



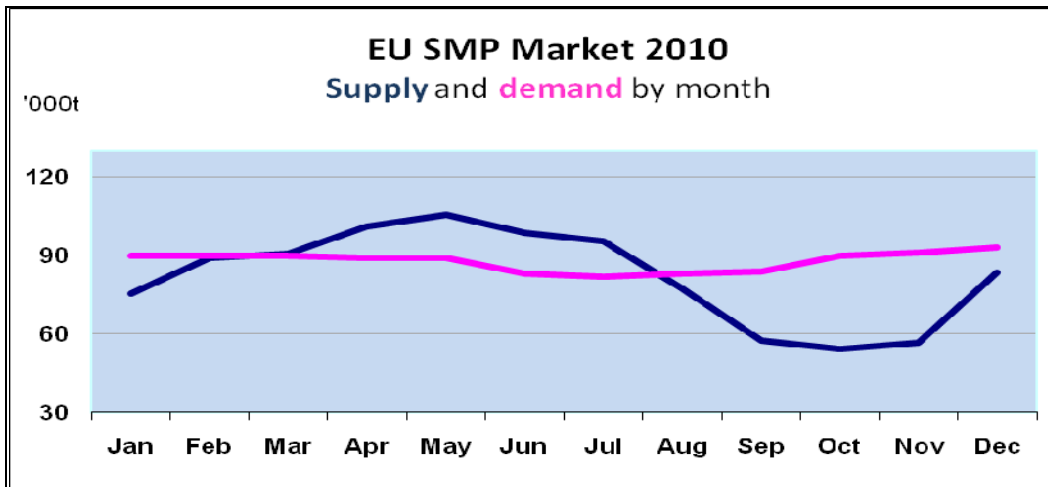
Also differently from last year is that no export refunds are necessary, since EU and World market prices are almost identical. After the slump of the Euro rate in May even domestic prices of bulk butter are below the world market level which means that international process would be reduced or EU domestic prices go up further, with the latter being more likely. According to the butter quotations held weekly in Hannover, also the prices of packaged butter for the retail trade are significantly lower, and an upward adjustment seems to be inevitable. Also the sale of intervention stocks cannot moderate the price development because the available stocks are low with 25.000 tons at the end of April.

BUTTER: Comparison between market price in Germany and Oceania and EU intervention price



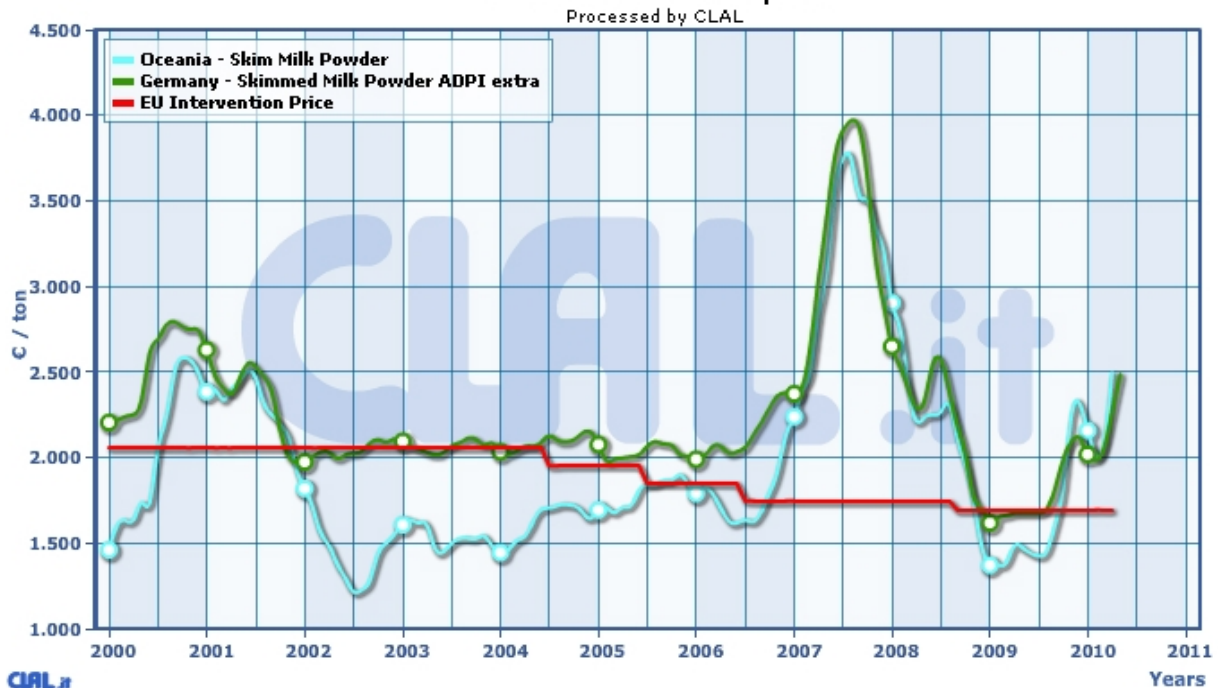
The Market of Skim Milk Powder

In the February projection the buying in of skim milk powder into intervention was not completely ruled out but regarded as not very relevant for the market situation. It is now clear that it will not happen anyway this year. Moreover, a strong reduction of stocks is likely. With the still available stock of 192.000 tons of SMP in intervention at the end of April, the market can well be balanced to some extent if production goes down as expected and export demand continues to be high. In the January and February exports had more than doubled to 63.000 tons. In the balance sheet embedded in the Annex, exports of 280.000 tons are assumed, which will not lead to a significant higher reduction of stocks than that which is intended in the scheme of donation to most deprived persons. But if production is constantly below the figure in that projection balance sheet much more will be needed to balance the market. Anyway, also here the supply from current production is expected to fall short of domestic and export demand already in July, provided present tendencies continue.



The question is when the EU Commission will start to sell from intervention stocks. They can start at any time, but they are expected when farm milk prices are higher than at the beginning of 2010, which might be soon the case. The volume of stocks is sufficient to stabilize price levels for a longer time, which is very different from the butter market situation.

SMP: Comparison between market price in Germany and Oceania and EU intervention price



Annex

Table 1

EU Dairy Market: Overview 2007 - 2009 and Forecast 2010				
	2007	2008	2009	2010 F-cast
Milk Deliveries	133.767	135.508	135.225	134.800
Liquid Products	46.370	46.600	46.600	46.800
Butter				
Production	2.065	2.075	2.040	1.990
Consumption	1.966	1.933	1.950	1.950
Cheese				
Production¹⁾	9.241	9.285	9.280	9.340
Consumption	9.909	9.919	9.974	10.030
Skim Milk Powder				
Production	1.090	1.040	1.100	980
Consumption	874	770	770	770
Whole Milk Powder				
Production	775	850	800	800
Consumption	362	481	420	425
Population (m. head)	496	498	500	501

1) Including processed cheese impact.

Source: ife Kiel, according figures collected from ZMP, ZMB and EU Commission publications.

Table 2

EU Butter Balance Sheet

1.000 t	2007	2008	2009	2010*
Total production	2.065	2.075	2.040	1.990
	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>
Imports	92	65	62	70
Exports	211	147	143	180
Final stocks	90	150	160	100
- in intervention	0	0	80	20
Consumption	1.966	1.933	1.950	1.950
*) <i>Estimated.</i>		<i>ife May 2010</i>		

Sources: ife, Kiel; ZMB, Berlin; EU Commission

Table 3

EU Cheese Balance Sheet

1.000 t	2007	2008	2009	2010*
Production	8.976	9.030	9.030	9.090
Imports	94	89	84	90
Processed cheese impact	265	255	250	250
Exports	594	555	570	600
Stock Change	+20	+10	-40	0
Consumption	9.909	9.919	9.974	10.030
- per capita (kg)	17,6	17,7	17,7	17,7
*) <i>Estimated.</i>			<i>ife May 2010</i>	

Sources: ife, Kiel; ZMB, Berlin; EU Commission

Table 4

EU WMP Balance Sheet

'000 t	2007	2008	2009	2010*
Production	775	850	800	800
Imports	2	2	1	0
Exports	362	481	420	425
Change in stocks	0	-20	0	0
Consumption	415	391	379	400
*) <i>Estimated.</i>			<i>ife May 2010</i>	

Sources: ife, Kiel; ZMB, Berlin; EU Commission

Table 5

EU SMP Balance Sheet

1.000 t	2007	2008	2009	2010
Production	1.090	1.040	1.100	980
Imports	6	8	6	5
Consumption	874	770	770	770
Exports	196	179	227	280
Ending stocks	121	220	330	265
- in intervention	-	-	260	200
*) <i>Estimated.</i>			<i>ife May 2010</i>	

Sources: ife, Kiel; ZMB, Berlin; EU Commission