

EU Dairy Markets, Situation and Outlook, January 2014

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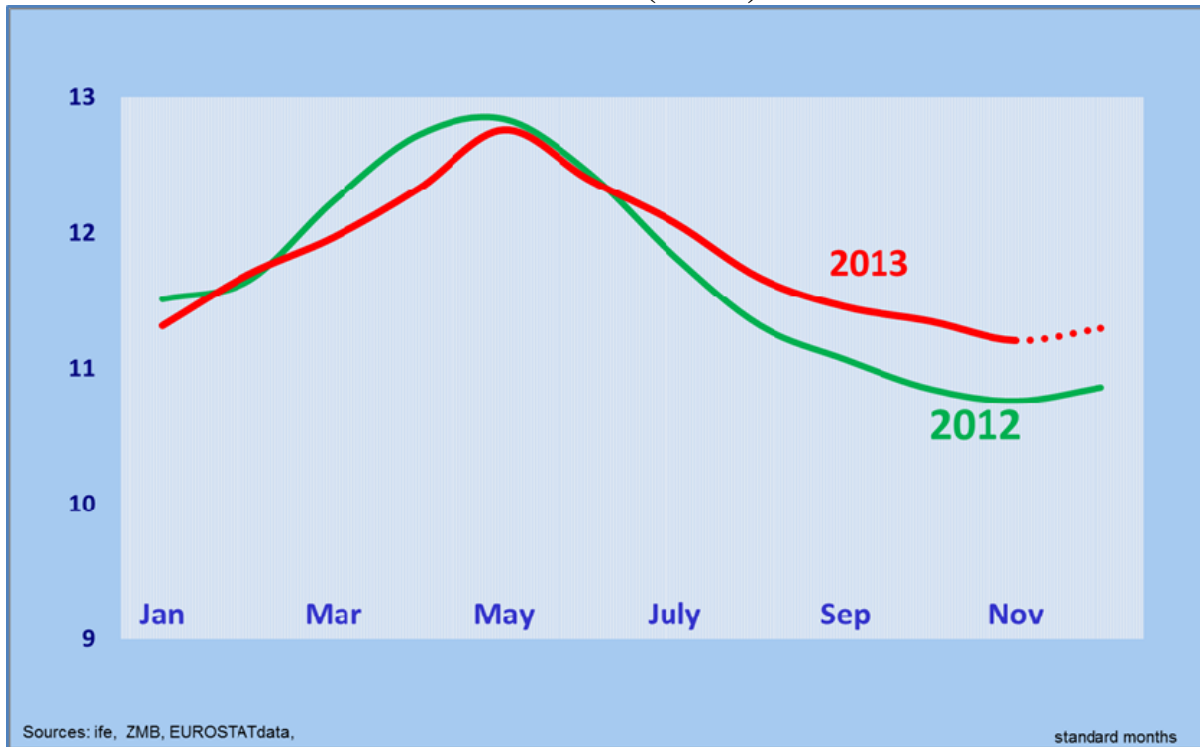
Highlights:

- In the period up to May, 2014 EU milk production will grow seasonally and cyclically at the same time. This growth might be reduced on the short term towards the end of the quota year 2013/14.
- Also in other major production areas of the world milk production continues to grow, but so far this growth trailed behind demand from international markets.
- The returns in the different sectors of milk processing have come closer to each other and will stay relatively stable over the next months.
- With the expanding milk collection in the EU, production of butter, cheese and milk powders will grow.
- The prices of cheeses and milk powders will stay at high levels in the period until May. More easing of butter prices, however, seems to be possible, but also here high levels will prevail.

Ongoing expansion of EU milk production

European milk production has started to grow according the usual seasonal pattern in December, after expanding on a year to year basis already since the mid of 2013. Favourable conditions have resulted in increasing expansion rates in autumn: milk prices have followed the development of the dairy commodity prices which have boosted the returns of dairy processors. Basic feed supplies for dairy cows had improved in the third trimester and in most countries winter feed supplies seem to be sufficient. Moreover, supplementary feeding of concentrates became attractive also by falling prices of grain and also slightly reduced prices of soy bean crushing.

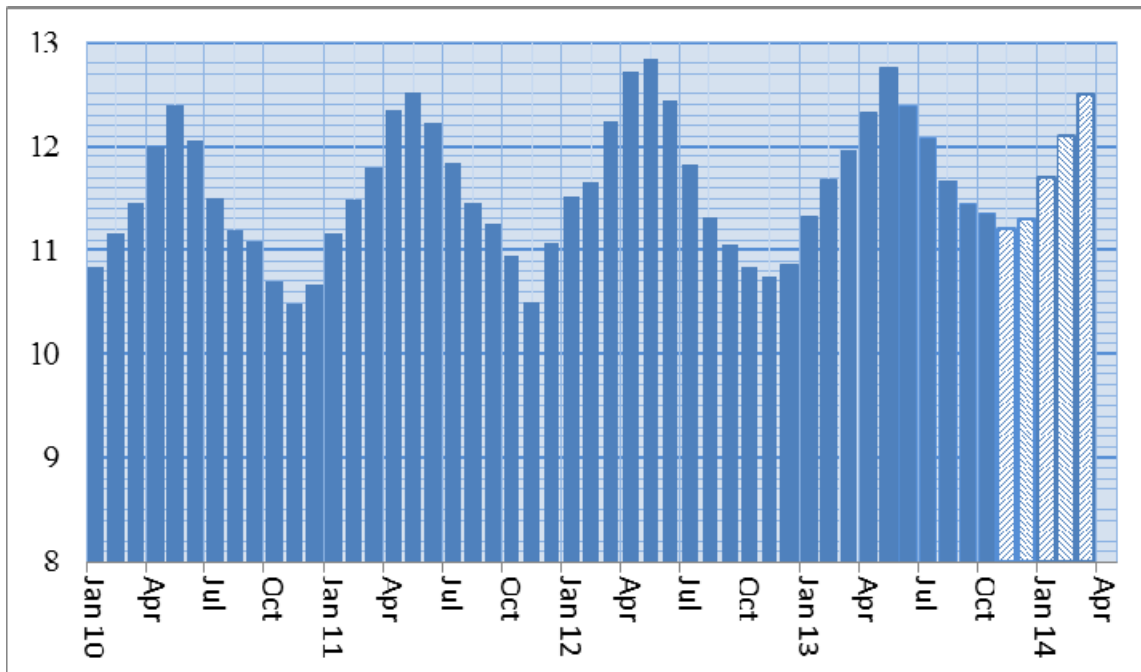
Biennial overview of EU milk deliveries (mio. t)



Not yet clear is the situation in terms of figures for the month of December and later. An easing of the expansion rates from over 4% to 3% is still a substantial increase. In view of the good market conditions and improved scale economies by better usage of processing facilities this development is highly welcomed by the dairy industry. The expansion rates peaked above 4% in October and November, which are the months of the seasonal bottom of milk production on the Northern hemisphere. Strong expansion rates could be observed just in those countries where milk supplies had been severely depressed the year ago, notably in Ireland, the U.K. and France. Also the Netherlands, Germany and Poland reported significant expansion both in percentage and in volume terms.

Most of these additional volumes of milk have been and will be used to produce more cheese, butter and milk powders. In particular the EU domestic cheese market is good for a moderate growth. On top, some parts of the larger productions will be disposed of to replenish stocks which are short in all categories. Thus also more products are needed just to bring pipeline stocks to levels which are regarded as normal. If the international market continues to demand more and more dairy products, the EU will be in a good position to export all the extra production of butter and milk powders. The question is only how long prices can be maintained at present levels and how far downward adjustments will go. This will be subject of the following considerations.

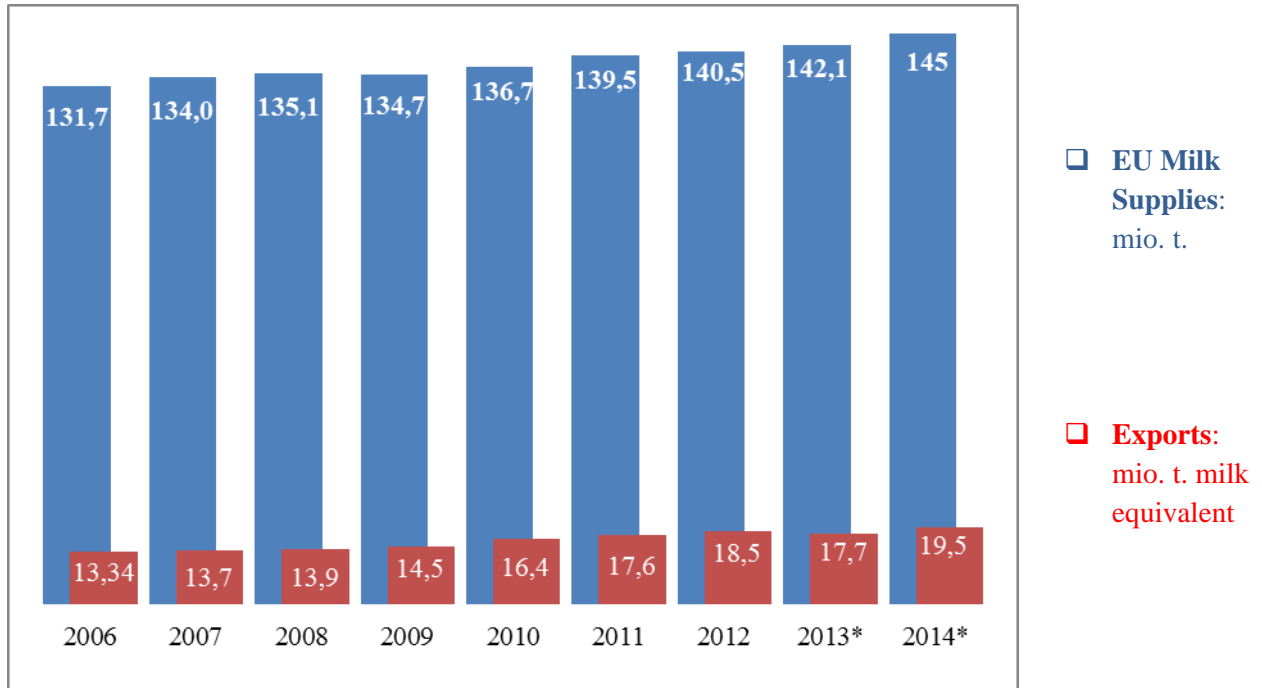
EU-27 Milk Deliveries, January 2010/November 2013 and estimate December 2013/ March 2014, adjusted for average length of months, mio t.



For the outlook period until May 2014 the situation seems to be clear: Large contracts have been made in advance which will keep the returns for most of the milk which will be processed at present high levels. And with the payout strategies of most dairies which are characterized by a certain time lag in which farm milk prices trail behind the market returns, regardless whether they go up or go down farmers can expect favourable price for most of this year. The expectation of a relatively stable situation at high levels is nurtured mainly by the strong impacts of world market developments on the EU market. Also the prospects for the EU economy have improved and an easing of the crisis affecting consumer incomes is forecast by many observers.

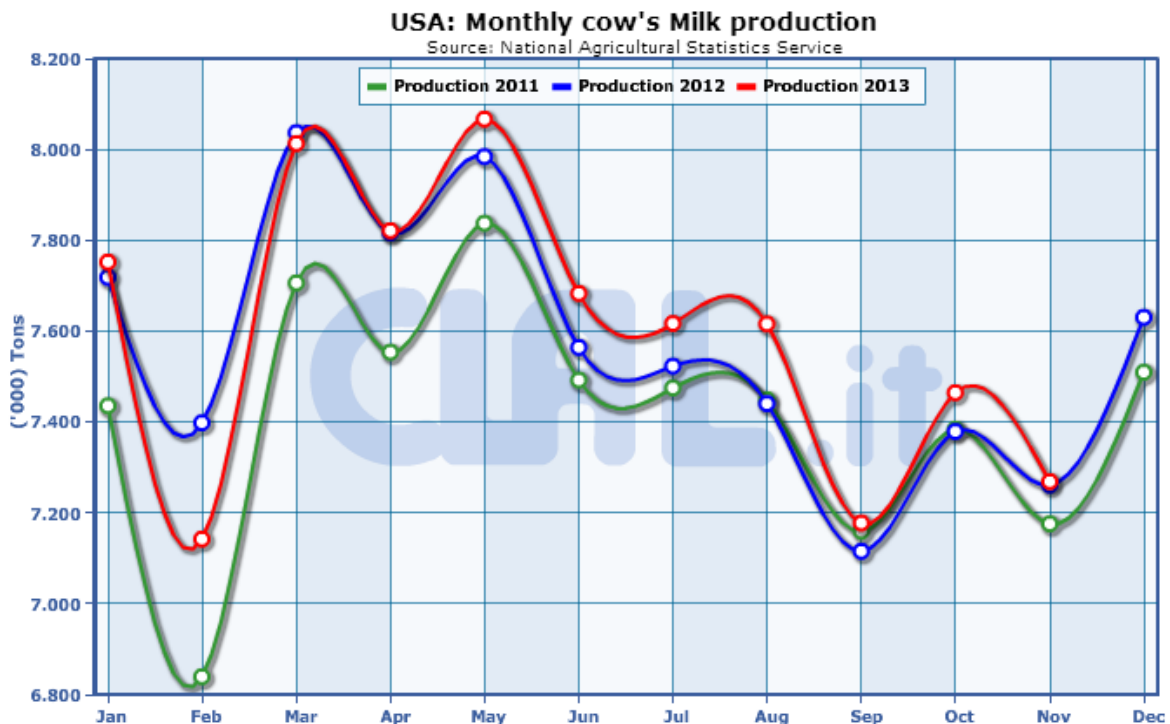
Anyway, the combined exports, (expressed in milk equivalents based on the solids content of the dairy products) will reach a new historical high.

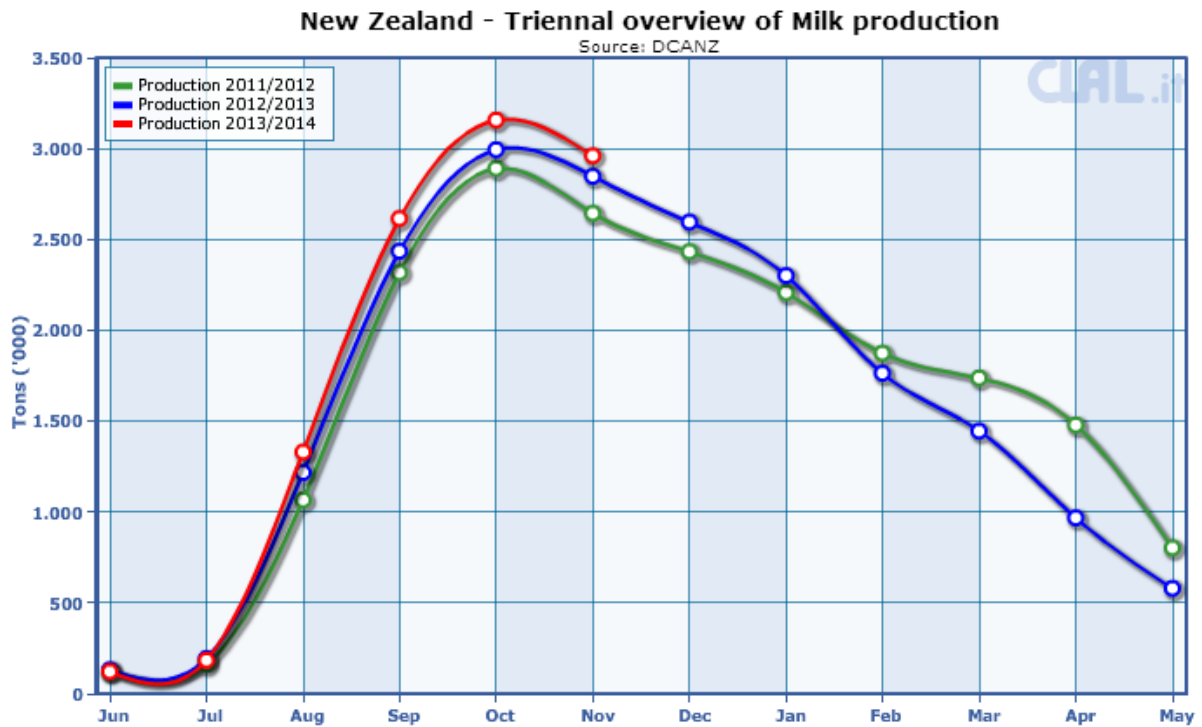
EU milk supplies and dairy exports



Only moderate expansion in other parts of the world

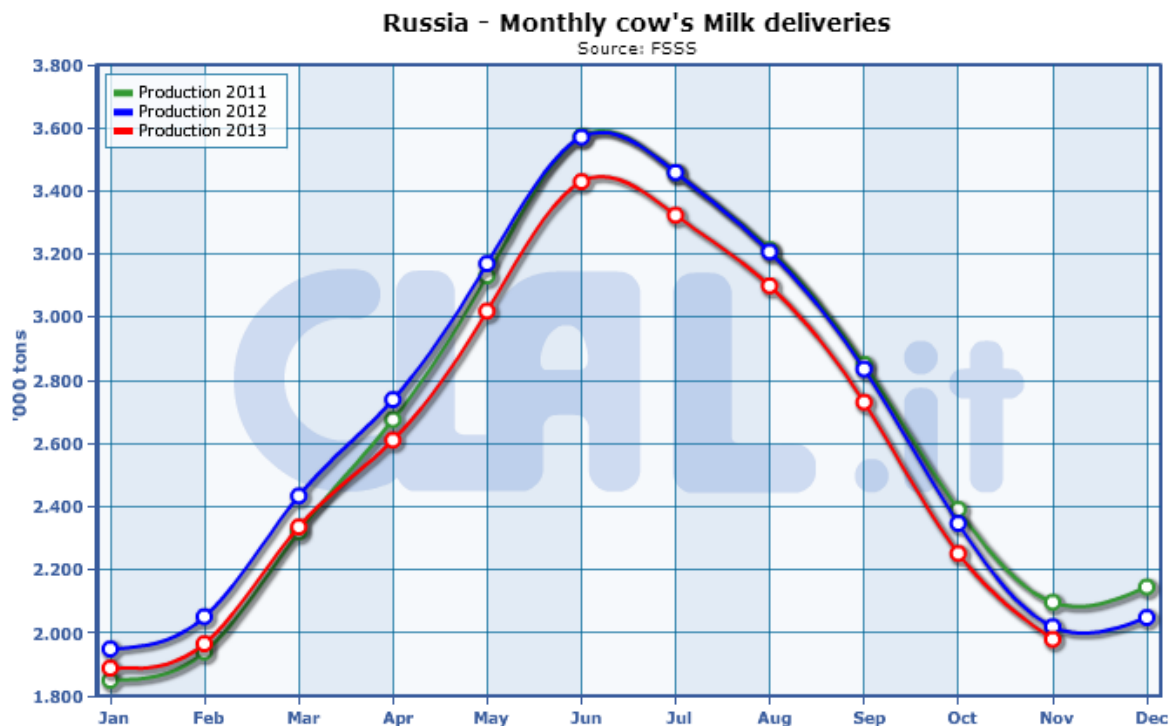
More milk can be expected from other major exporting countries, notably the U.S. (despite a temporary slowing down at the end of 2013) and New Zealand.





Other exporting countries like **Australia** and **Argentina** produce less milk. A recovery might be possible in the second half of 2014.

In **major importing countries** like **Russia** and **Japan** production is stagnating.



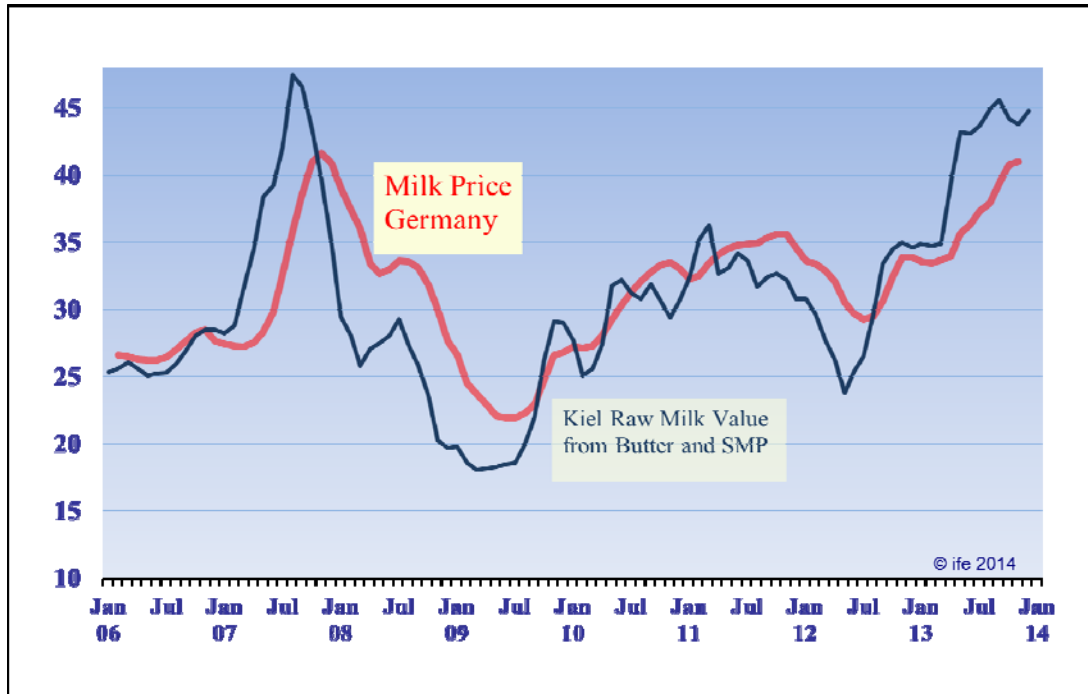
China continues to buy large quantities of dairy products including liquid products and baby food. Imports are driven by a growing demand which is largely outpacing domestic milk production, regardless whether it is stagnating or increasing. Later in the year, a stronger expansion of milk production all over the world is possible, which might bring production growth closer to the development of demand. But after May, milk supplies will go down seasonally. Therefore a fundamental change of the international market situation in the current year 2014 is not in sight yet, and in particular not in the time span of this outlook report until May, 2014.

Ongoing high prices on major markets

After the turn of the year no major modification in the price quotations occurred, apart from a few modest fluctuations. The interest of international buyers is focussing more to the increasing supplies from the EU, since Oceania and U.S. supplies are almost committed. Already large forward contracts have been reported, despite the firmer rate of the Euro versus the US-Dollar. The slight reduction of bulk butter prices within the EU domestic market in January is no surprise. The situation of milk powders is stable. In general, the return from both commodities as given in the Kiel raw milk value which is calculated by *ife-Institut* will stay significantly above the levels of the first half of 2013. Most of the other dairy products, for which this indicator is a reference will also stay at high levels. They react with a time lag to changes of the key commodities butter and skim milk powder, if it should go down or up. Therefore the also the perspective for higher farm milk prices is good.

Market return from butter and skim milk powder in Germany

(Ct/kg, 3,7% fat until 2009, afterwards 4,0% fat, 3,4% protein)



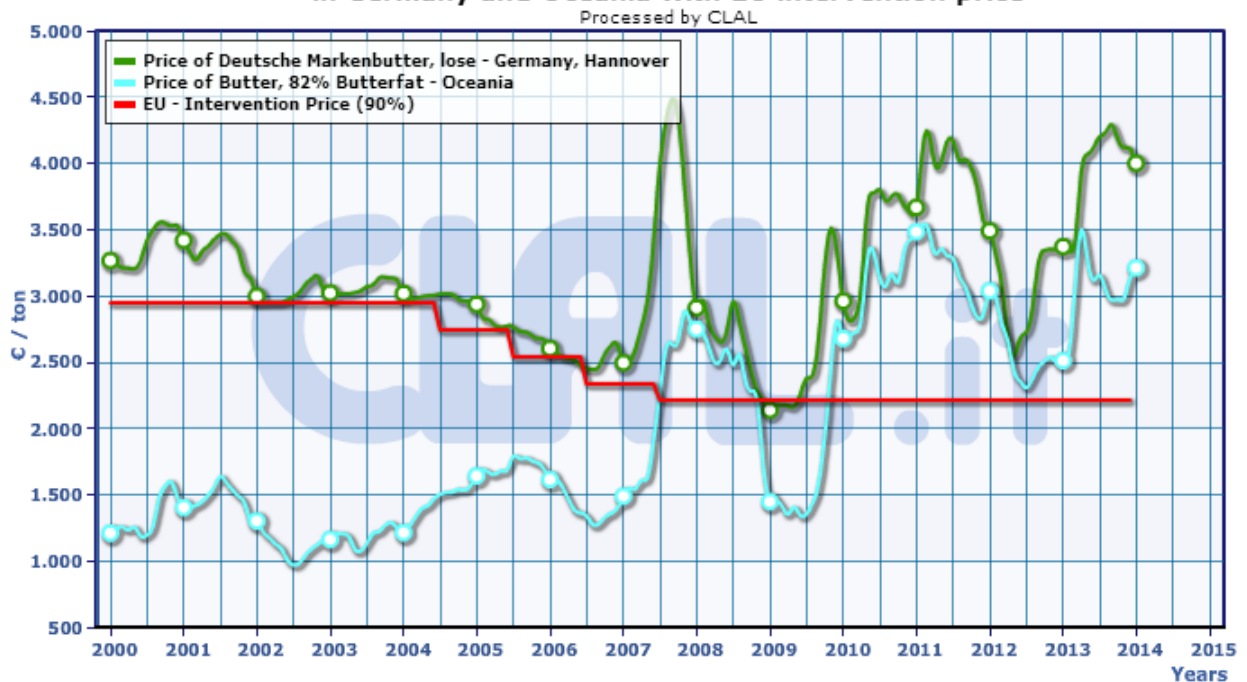
More milk powders, butter and cheese

With growing milk supplies in the EU more butter, cheese and milk powders will be produced, whereas the market of liquid milk and other fresh products can only absorb a small share of the additional milk supplies. But more UHT products are exported to China and other destinations.

Slight weakening of bulk butter prices

In the first weeks of January bulk butter prices were quoted a bit lower than in November and December. This is not unexpected, as butter production has been increased on a year to year basis already since the mid of 2013, thus responding to attractive market prices. Thus the relative shortage situation has eased. At first, the greater volumes filled the gap of low stocks in the period of seasonally low production. After the turn of the year, more butter will be available to rebuild stocks and production will very soon exceed temporarily EU consumption. Part of these surpluses will be taken into stores as supplementary market supply in autumn and winter, but also exports might play a more important role than they did so far. The level of world market prices will form the bottom line if prices should go down further. Lower market prices in spring are also in favour of taking butter into cold storages under the PSA scheme.

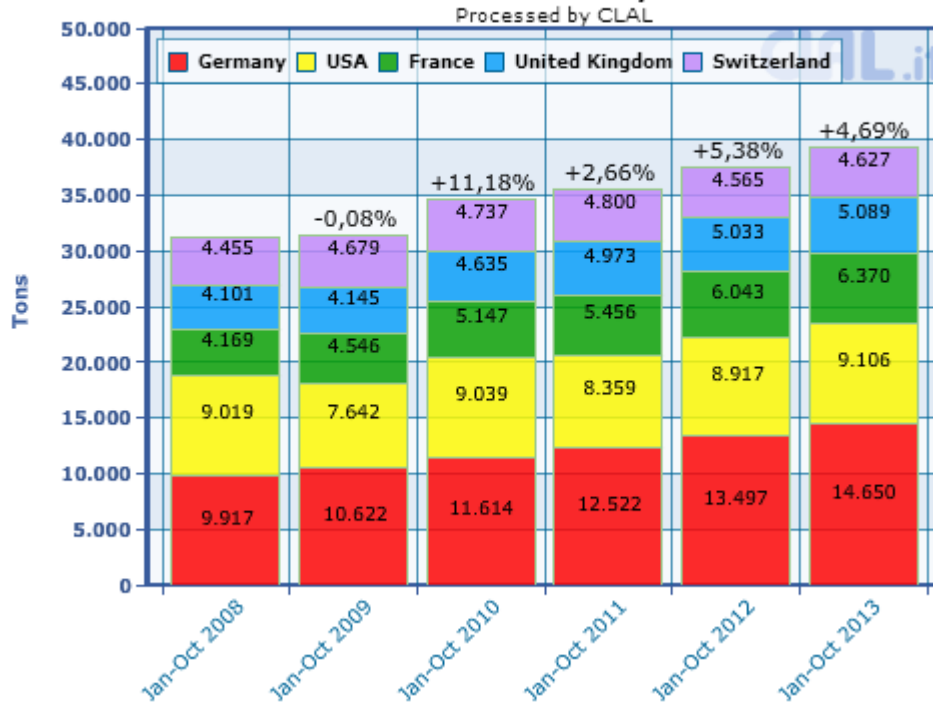
Historical comparative overview between Butter prices in Germany and Oceania with EU intervention price



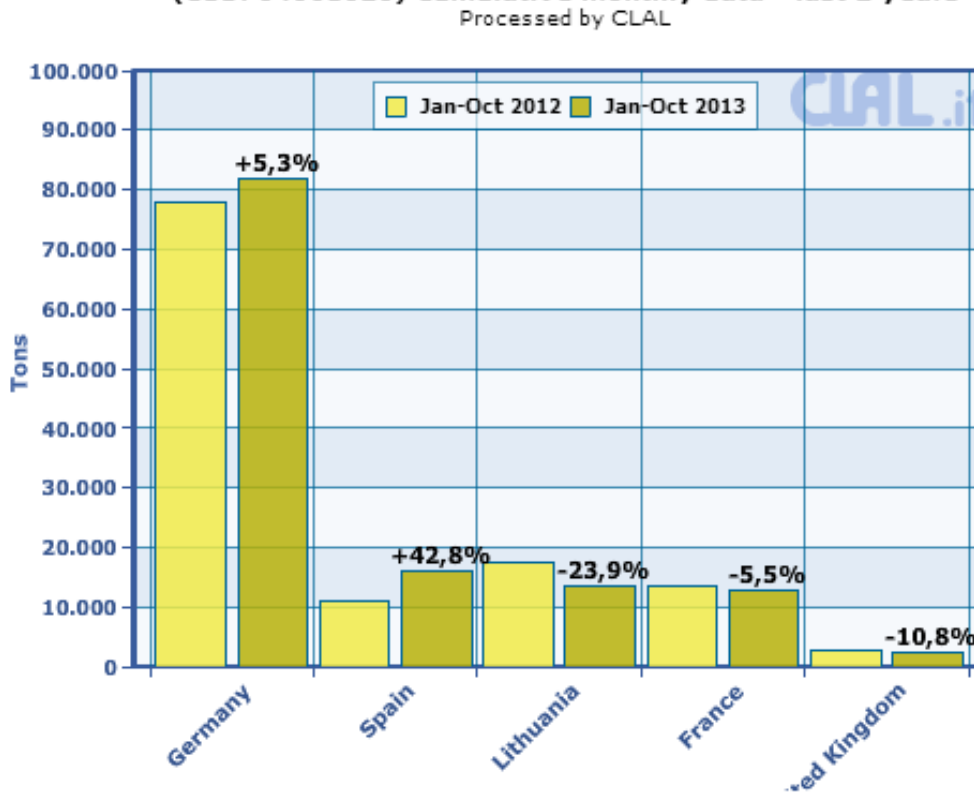
Stable commodity cheese prices at high levels

Commodity cheese prices have continued to follow rising prices of bulk butter and milk powders and stay also at high levels. The EU cheese market is still characterized by a modest growth, despite some contrary views which might be nourished by the economic crisis in some member countries. More internal consumption is the main explanation for the growth of production and low stocks, whereas increasing exports take the second place if the balance sheet for recent years is considered (Annex table 3). Partly this gain in consumption volumes can be explained by the shift of consumer demand from high value specialty cheeses to commodity cheeses. This hypothesis is supported by Italian import/ export figures: More cheese was imported from Germany, whereas more specialty cheese was exported to Germany. Semi-hard block cheese produced in Germany took advantage of the general market situation by increasing prices, which, however, are still far below the specialty prices. And the Italian specialties gained some competitiveness by reduced prices. Although they are still much more expensive than the Gouda/ Edam blocks they found good opportunities in Germany where consumer confidence has improved in 2013.

Italy - Main Purchasing Countries of Grana Padano PDO and Parmigiano Reggiano PDO (04069061) Cumulative monthly data

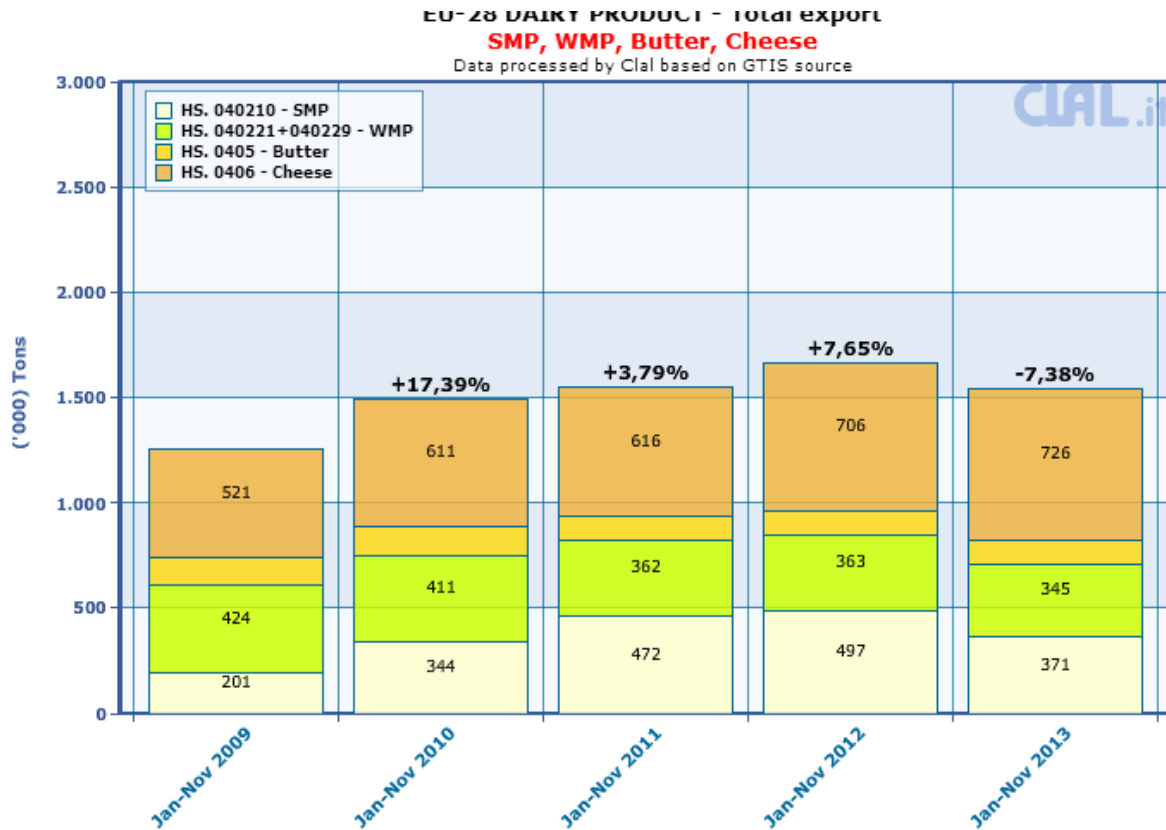


Italy - Main Supplying Countries of FRESH CHEESE (COD. 04061020) Cumulative monthly data - last 2 years

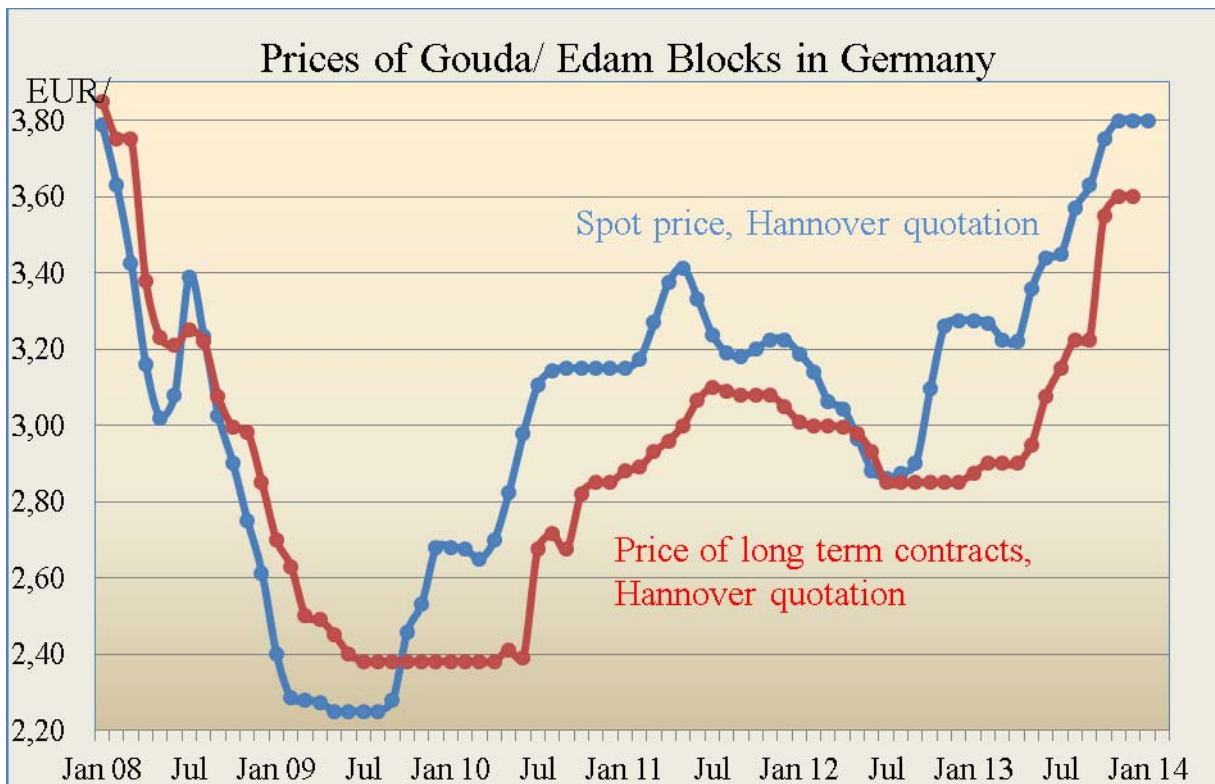


Exports to destinations outside the EU have been increased again, despite the difficulties in exporting to the Russian market. These problems have created

different affects among cheese producers depending on being licenced or not to supply cheese to the Russian market.



Nevertheless, more other destinations are in focus and together with the difficulties of the Russian dairy chain to supply sufficient volumes to the domestic market the prospects for rising exports are positive. And a moderate growth rate of EU domestic consumption can be more in volumes than a much stronger rate in exports. On top of this the necessity to replenish low stocks in ripening storage houses creates a good space to continue in producing more cheese. The returns from cheese making, however, have to be competitive to milk powder and butter production in view of several new capacities for milk drying. All this might keep the commodity cheese prices at present high levels for the time until May which is under consideration here.

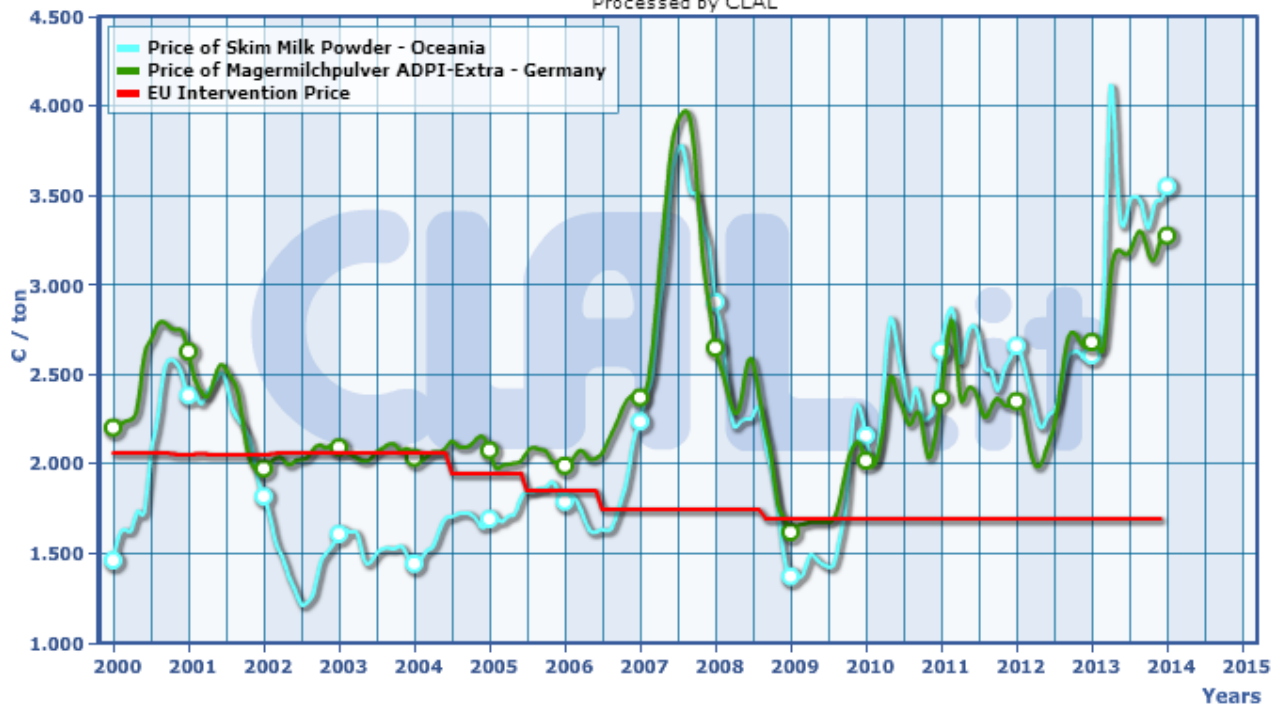


Milk powder prices: Poor prospects for lower prices

The perspective for high milk powder prices close to present high levels in the near future is good. Against the normal situation around the turn of the year prices for food qualities remained stable in the first weeks of January. This stability is mainly supported by the export demand. As most of the exportable volumes from Oceania and the U.S. are already committed, **more exports from EU countries are expected**, also because of the expanding production: More whole milk powder than the year ago has been produced since the mid of 2013 and more skim milk powder since autumn, and this trend will continue when milk supplies continue to grow. In general, the expansion of skim milk powder will be stronger than that of whole milk powder production, because competition with other international suppliers is easier with skim milk products. The raw material costs of whole milk powder depend also on butter and cream prices, which are mostly higher within the EU than outside. The possibility of butter price reductions, however, can lead also to some slight weaknesses in the whole milk powder market.

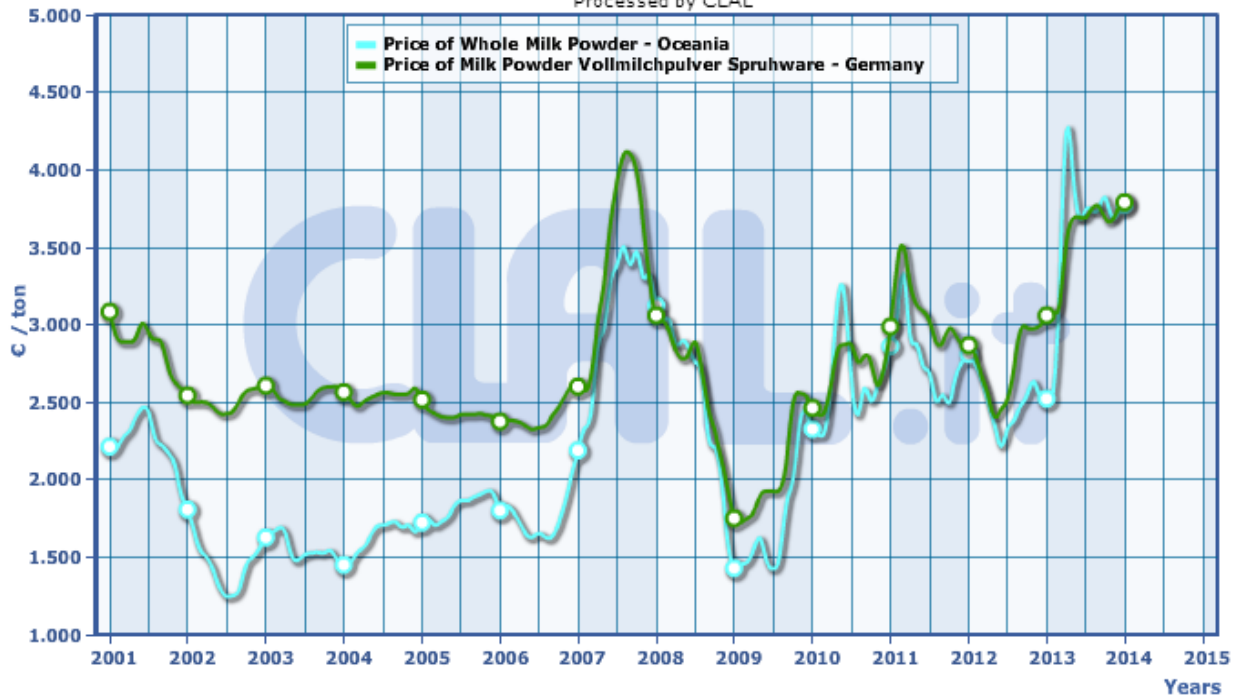
Comparative historical overview between SMP market prices in Germany and Oceania and EU intervention price

Processed by CLAL



Comparative historical overview between WMP prices in Germany and Oceania

Processed by CLAL



Annex

Table 1

EU- Dairy Market 2007 - 2013 and Forecast 2014

1.000 t	2007	2008	2009	2010	2011	2012	2013*	2013**	2014**
	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 28	EU 28
Milk deliveries	134.047	135.108	134.702	136.666	139.526	140.510	141.600	142.100	145.000
Liquid Products	44.242	43.772	44.157	44.440	44.555	44.850	44.860	44.960	45.000
Butter									
Production	2.110	2.100	2.050	2.010	2.080	2.105	2.115	2.119	2.180
Consumption	1.994	1.968	1.984	1.974	1.966	2.013	2.025	2.031	2.045
Cheese									
Production	9.248	9.339	9.333	9.497	9.611	9.700	9.798	9.830	9.940
Consumption	8.728	8.868	8.840	8.908	8.993	9.006	9.068	9.110	9.165
Skim Milk Powder									
Production	1.090	1.040	1.160	1.080	1.220	1.230	1.190	1.190	1.320
Consumption	870	770	800	805	810	810	790	793	790
Whole Milk Powder									
Production	773	835	735	760	750	715	710	710	760
Population m. head	495	498	500	501	502	504	505	510	511
*) Provisional. **) Forecast.								<i>ife Jan 14</i>	

Sources: ife, Kiel; ZMB, Berlin.

Table 2

EU Butter Balance Sheet

1.000 t	2007	2008	2009	2010	2011	2012*	2013**	2013**	2014**
	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 28	EU 28
Production	2.110	2.100	2.050	2.010	2.080	2.105	2.115	2.119	2.180
Imports	85	65	62	40	47	56	45	45	45
Exports	211	147	143	161	132	128	135	133	150
Final stocks	100	150	135	50	80	100	100	100	130
- in intervention	0	0	79	2	0	0	0	0	0
Consumption	1.994	1.968	1.984	1.974	1.966	2.013	2.025	2.031	2.045
*)Provisional. **)Estimated								<i>ife Jan 2014</i>	

Table 3

EU Cheese Balance Sheet

1.000 t	2007	2008	2009	2010	2011	2012*	2013**	2013**	2014**
	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 28	EU 28
Production	8.983	9.084	9.083	9.237	9.366	9.465	9.558	9.590	9.700
Imports	94	89	85	82	74	77	75	75	75
Processed cheese impact	265	255	250	260	245	235	240	240	240
Exports	594	555	578	676	682	776	810	800	840
Stock change	+20	+10	+0	-5	+10	-5	-5	-5	10
Consumption	8.728	8.868	8.840	8.908	8.993	9.006	9.068	9.110	9.165
-per capita (kg)	17,6	17,8	17,7	17,8	17,9	17,9	17,9	17,9	17,9

*)Provisional. **)Estimated ife Jan 2014

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

Table 4

EU SMP Balance Sheet

1.000 t	2007	2008	2009	2010	2011	2012*	2013**	2013**	2014**
	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 28	EU 28
Production	1.090	1.040	1.160	1.080	1.220	1.230	1.190	1190	1320
Imports	6	8	6	4	0	2	5	5	5
Exports	199	179	227	378	518	523	410	407	530
Final stocks	121	220	359	260	152	50	45	45	50
- in intervention	-	-	260	195	54	0	0	0	0
Consumption	870	770	800	805	810	810	790	793	790
- as Feed	245	150	160	165	175	160	120	120	120

*)Provisional. **)Estimated ife Jan 2014

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

Table 5

EU WMP Balance Sheet

1.000 t	2007	2008	2009	2010	2011	2012*	2013**	2013**	2014**
	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 27	EU 28	EU 28
Production	773	835	735	760	750	715	710	710	760
Imports	2	2	2	2	2	2	3	3	3
Exports	366	485	463	447	390	387	380	378	430
Stock change	20	15	-55	-20	10	0	0	0	0
Consumption	389	337	329	335	352	330	333	335	333

*)Provisional. **)Estimated ife Jan 2014

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