

EU Dairy Markets, Situation and Outlook

January-April 2012

by Erhard Richarts, Dairy Market Consultant, Chairman of IFE (Informations- und Forschungszentrum für Ernährungswirtschaft e. V., Kiel)

Special report produced for CLAL

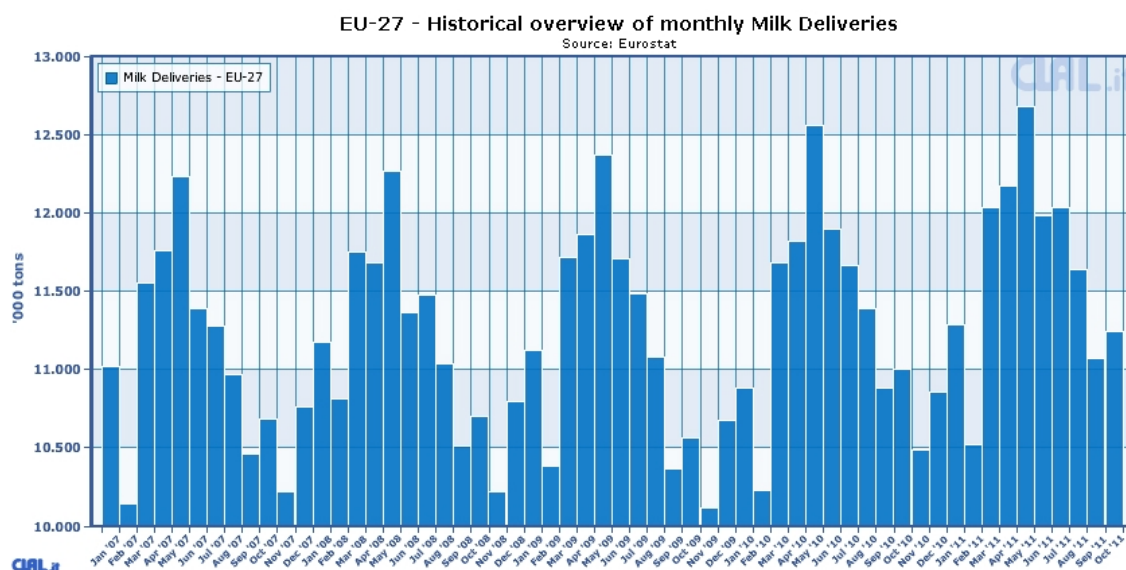
Highlights:

- Milk and dairy markets are still characterized by prices at high levels and growing production.
- EU milk supplies will go up seasonally until May. But the growth is likely to slow down, compared to 2011.
- Like in past years most of all additional milk supplies in the EU will be used for additional cheese production, therefore output of butter and skim milk powder will not grow in line with the extra milk volumes
- Outside EU milk production will continue to grow, but also at a slower pace than 2011.
- Domestic demand in the EU might partly be affected by economic problems of many consumers as result of the debt crisis. But the reaction will be modest.
- Again demand for exports will clear the European market from temporary surpluses.
- Prices of nonfat dairy commodities, mainly skim milk powder, dairy protein products and lactose on the international market and in the EU will continue to be very close to each other.
- The EU will hardly be in the position to export similar volumes of skim milk powder as in 2011.
- Butter and milk fat supplies will not be as tight in relation to demand as they were last year. Nevertheless, prices of butter and other milk products with high fat contents will continue to stay at still high levels, when compared to many years prior to 2011.
- Butter and whole milk powder export opportunities could improve temporarily as result of seasonally lower domestic prices and favorable currency rates.
- The weakness of the Euro vs. the US-Dollar is favorable for international competitiveness. However the question is how long the uncertainty resulting from the debt crisis impacts will keep the exchange rate favorable.

Milk Production slowing down

EU milk supplies are expected to reduce their growth in the first trimester of 2012, but to be ahead of 2011 for the remainder of the year. The growth had started already in May 2010 and had reached the high rate of 3% just in the first four months of 2011. In the period from May 2011 until December, it was 1,7% on average. For some member countries the space to continue with the expansion is narrow because they risk to exceed their quotas unless they reduce milk supplies in the first trimester, according to recent information from ZMB. Notably dairy farmers in Ireland, Belgium, Germany, Austria, the Netherlands and Denmark will be faced with that problem.

But after March 31, the quota year's deadline, new space for expansion is given by the next increase of national quotas by 1% (based on 2008/09 quotas) except for Italy. Moreover, the higher milk prices might give incentives to take advantage of this additional space, even if a slight decline of the milk prices from 2011 levels for most of the EU cannot be ruled out. In Bulgaria and Romania, more time has been given to the dairy farmers to comply with EU hygiene and quality requirements. Initially the transition time allowing to sell milk below EU standards should have been ended by December 31, 2011. In view of the difficulties to achieve sufficient milk supplies this deadline has been delayed. But all milk which does not meet the standards is only eligible to the respective domestic market.



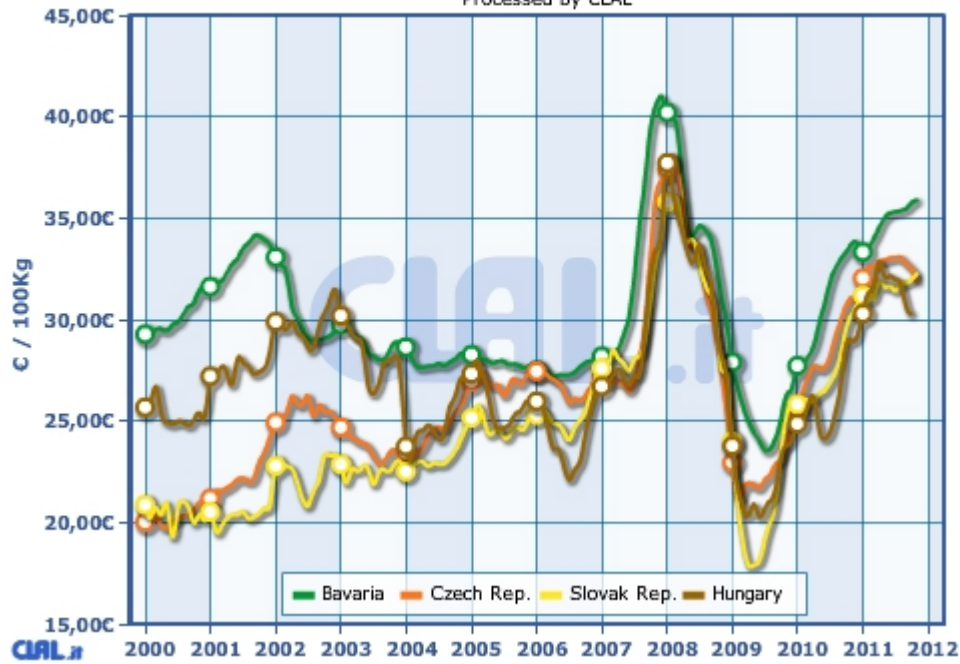
On the world level also a slowing down of the expansion of milk supplies can be expected. This assumption is based on the expectation of an only average growth not only in the EU, but also in New Zealand and Argentina, where outstanding increase rates had been observed and which are hard to repeat within a time span of two years. The world's cow milk production had increased by 11 million to 611 million metric tons in 2011. It seems to be difficult to go on in that speed, although sales have followed and prices are still high. All milk production is estimated to be significantly above 700 million t in 2011, with an estimated growth of 15 million t. However, this has to be set in relation to an average growth of world milk production by 16 million t per annum in the years from 1999 to 2007, a period which ended in the clearing of all stocks and high prices on national and international levels. How things go on now depends much on the economic situation. But the debt crisis in the EU is still far from driving the whole world economy into a recession, which had stopped the bullish situation of dairy commodity markets in 2008.

European milk prices relatively stable

Milk prices in Europe had continued to go up in 2011. But as far as the farmgate milk prices are highly linked to the situation of the key commodities butter and skim milk powder, a slight decline cannot be ruled out, since a weaker situation in particular from the butter market seems to be possible. But the year 2012 has started with firm prices of milk powder and only slight weaknesses in the bulk butter market. Butter and skim milk powder prices are quoted below the levels of early 2011, but they are still high in relation to earlier years. The returns for milk from cheese making have soared and are higher than a year ago, boosted by higher prices of cheese and whey products as well. But it will be hard for dairy companies with the focus in the sector of liquid products to keep pace in the payout performance of the others, in particular in Germany. However, under normal conditions it can be expected that in the first half of the year average farmgate prices of milk with fat contents between 3,7% and 4,0% are moving closely to the levels of 2011.

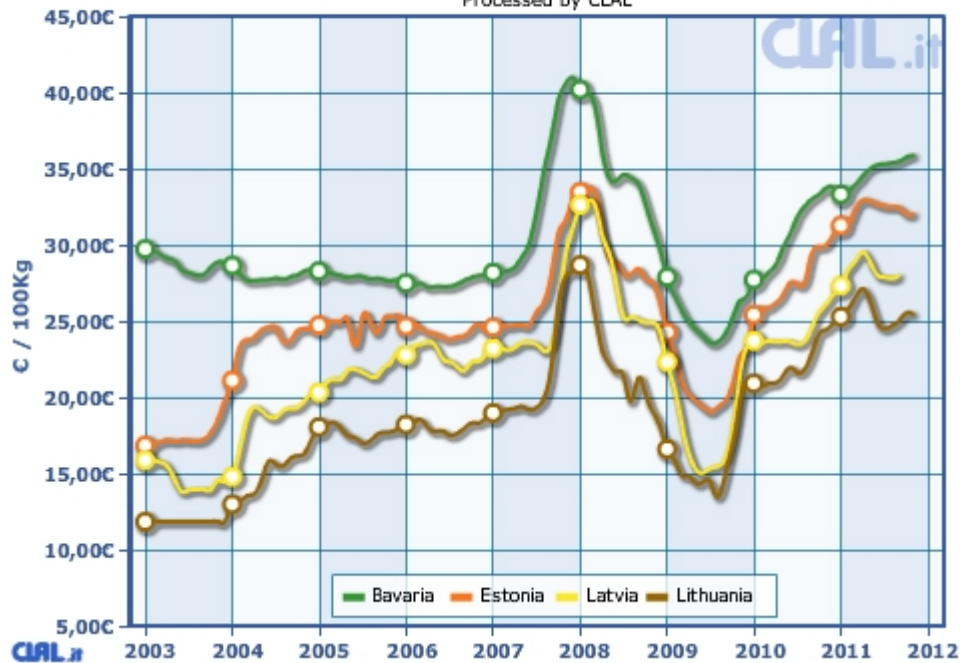
Bavaria, Czech Republic, Slovak Republic, Hungary Historical comparative overview of farm-gate raw milk prices

Processed by CLAL



Bavaria, Estonia, Latvia, Lithuania Historical comparative overview of farm-gate raw milk

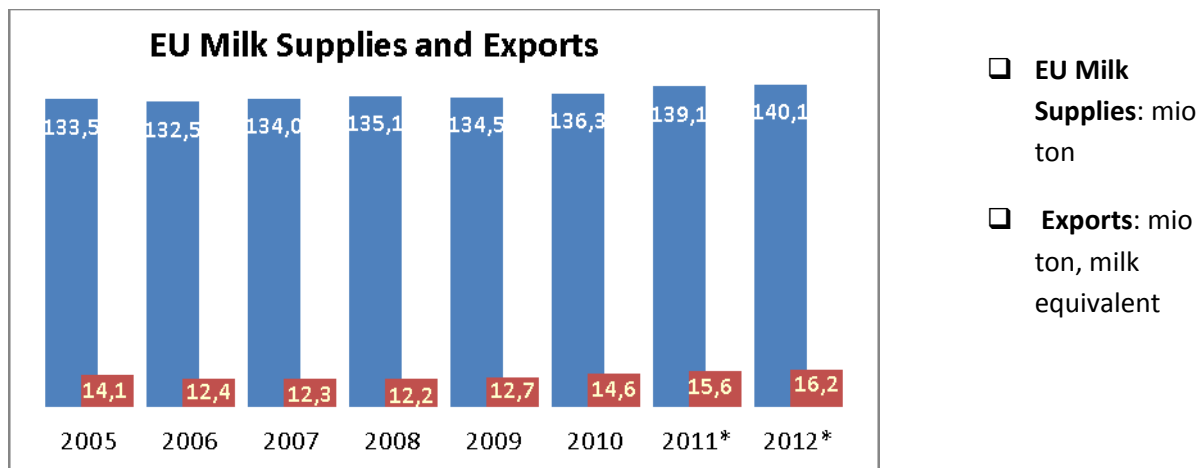
Processed by CLAL



Milk utilisation: Cheese will absorb most of all milk

As already happened in recent years, cheese manufacturing will absorb most of all milk which is delivered to dairy companies. And with the ongoing growth of cheese demand from both domestic and foreign markets also the major part of the expected additional supplies (+ 1 million t) will be used for cheese, leaving only small volumes to produce more butter and skim milk powder.

In view of the rather smaller growth of world milk production, export demand from emerging markets will continue to clear again all potential surpluses; consequently an almost stable market development is likely, but with the usual seasonal movements with possibly some weaknesses in spring in the butter sector.



*)Provisional/ Forecast

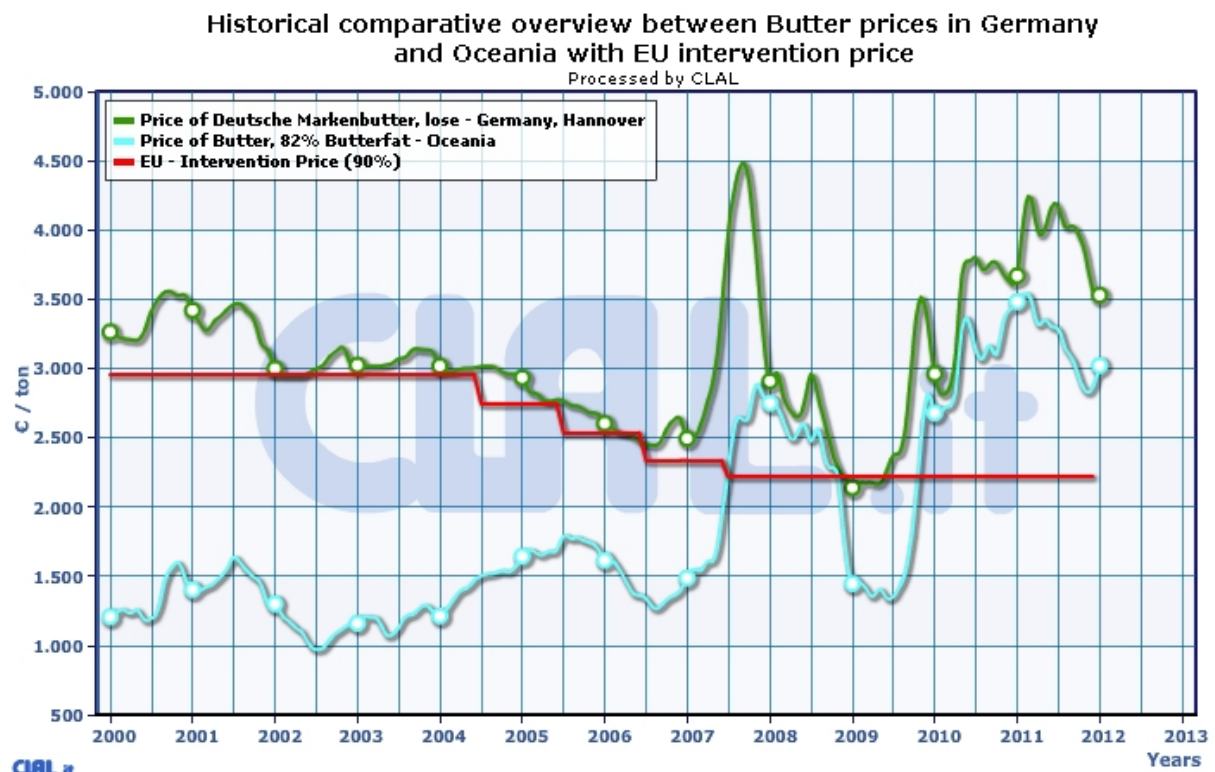
Stable butter market

As result of increased milk supplies also butter production is expected to grow slightly. Temporarily butter prices will be above the levels of the international market, which might attract also more imports into the EU, notably from New Zealand. But also depending on the market situation in particular in spring and early summer the price difference to the international market can be small, which might enable the EU to export more butter to foreign markets than in 2011. Domestic consumption will not be subject to major changes: Slight declines in the sector of private households might be compensated in the sector of caterers etc. and in the food industry. All this can end up in a modest increase of stocks and a price evolution below 2011 levels, but still elevated when compared to the long term development. Anyway, the average prices in 2011

were only slightly below 4€/kg, which was for instance in Germany the highest average since the early Eighties!

The Oceania butter prices have gone down since the mid of 2011. But if they are transformed into Euro terms they have recovered towards the end of the year and moved closer to the EU prices. With the actual rate from time to time the window for increased exports could be opened.

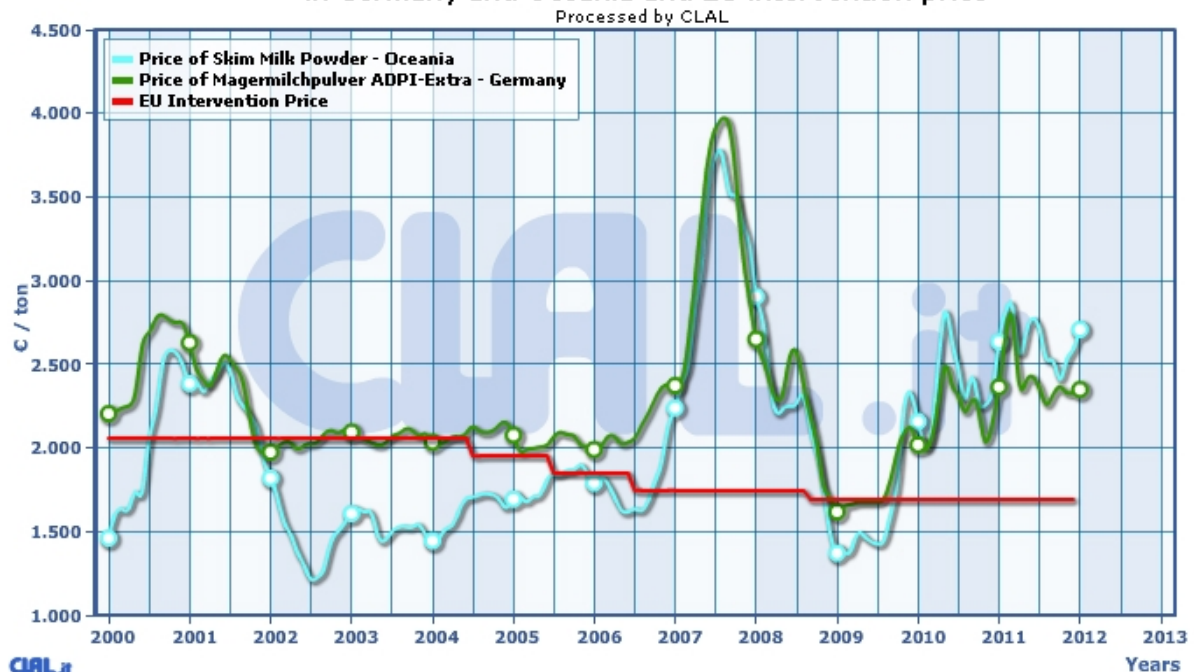
The scenario could be somewhat different if milk supplies would grow faster than has been assumed for this market assessment: It would probably end in more exports or higher stocks and lower prices.



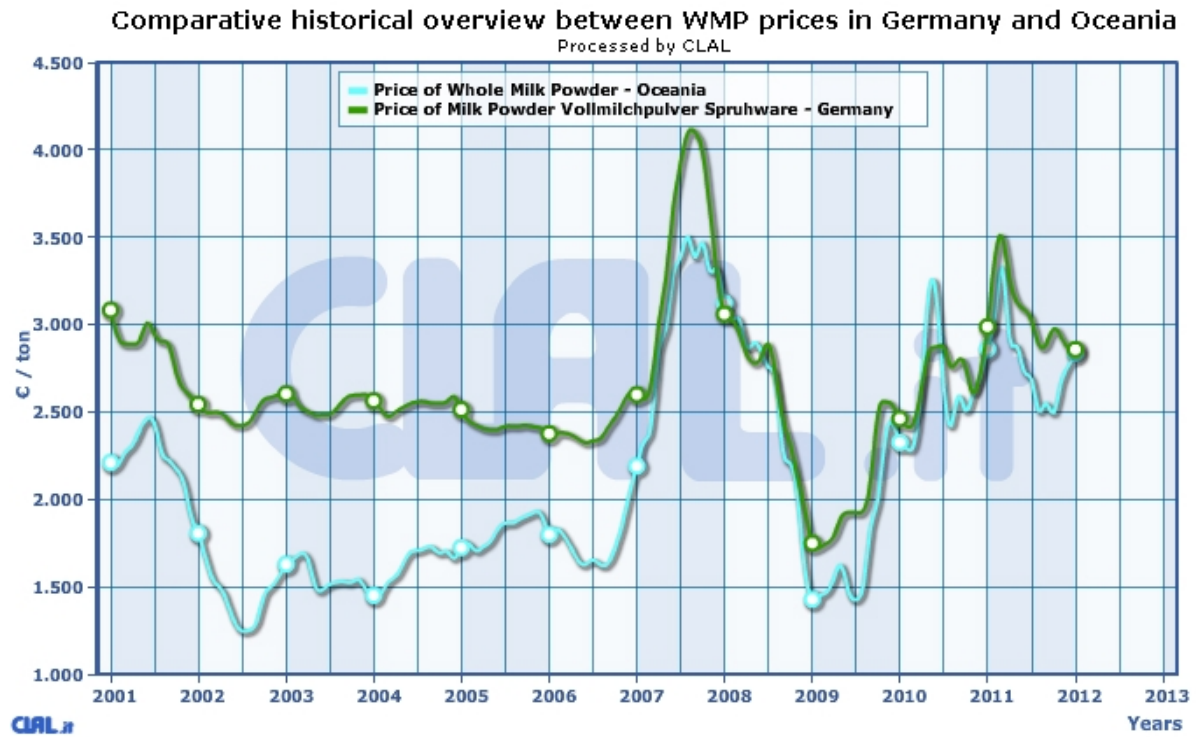
EU milk powder markets will remain highly interlaced with the international market

Although the second quotation held in Germany this year displayed increased prices for milk powders it seems to be premature to predict a similar development as in early 2011 with fast increasing prices of skim and whole milk powders in the first months of the year. The recent strength of the domestic prices has resulted from the weakness of the Euro vs. the US-Dollar. But as no solution of the financial problems of the Euro-zone is in sight yet, a recovery of the currency rate is unlikely, and the relatively comfortable situation for European exporters will continue.

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



Therefore also a slight recovery of whole milk powder exports, and consequently of the European production is expected, notably because the price gap to the international market has been bridged recently.



As cheese and whole milk powder production are likely to go up, only small increases of skim milk powder production can be expected. Therefore the market will remain shortly supplied in the EU, also because stocks will be reduced further, though not in the same speed as it happened in 2011. And as in particular over the next months the Euro rate is likely to remain weak, the strong production in spring might find its market very quickly both within and outside of the EU market. Therefore a further easing of the prices cannot be expected. It will also be difficult to keep export volumes on the record level of 2011. The domestic market will require at least similar volumes for the food and the feed industries as in 2011, because prices of whey powders, whey derivatives, casein and lactose are still high and have started the new year also with firmer prices. In the case of skim milk powder the situation would not be much different if milk supplies were higher than the 140,1 million t which are assumed in the annex table 1 .

Annex

Table1

EU- Dairy Market 2007 - 2011 and Forecast 2012

in 1.000 t	2007	2008	2009	2010	2011**	2012**
Milk deliveries *	133.969	135.103	134.525	136.273	139.080	140.100
Liquid Products	45.818	45.577	45.200	45.791	46.000	46.200
Butter						
Production	2.110	2.100	2.050	2.010	2.070	2.090
Consumption	1.994	1.968	1.984	1.970	1.960	1.965
Cheese						
Production	8.983	9.084	9.083	9.220	9.300	9.380
Consumption	8.728	8.863	8.869	8.891	8.945	9.020
Skim Milk Powder						
Production	1.090	1.040	1.160	1.080	1.200	1.210
Consumption	870	775	800	800	810	810
Whole Milk Powder						
Production	773	835	735	755	725	740
Population m. head	496	498	500	501	503	504
*) Revised time series **)Provisional/forecast.						Updated Jan. 2012

Source: ife, Kiel; ZMB, Berlin.

Table 2

EU Butter Balance Sheet

1.000 t	2007	2008	2009	2010	2011*	2012*
Total production	2.110	2.100	2.050	2.010	2.070	2.080
Imports	85	65	62	40	40	65
Exports	211	147	143	155	120	170
Final stocks	100	150	135	60	90	100
- in intervention	0	0	80	2	0	0
Consumption	1.994	1.968	1.984	1.970	1.960	1.965
*) Estimated.					ife January 2012	

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

Table 3

EU Cheese Balance Sheet

1.000 t	2007	2008	2009	2010	2011*	2012*
Production	8.983	9.084	9.083	9.220	9.300	9.380
Imports	94	89	84	82	75	70
Processed cheese impact	265	255	250	260	245	250
Exports	594	555	578	676	670	680
Stock change	+20	+10	-30	-5	+5	+0
Consumption	8.728	8.863	8.869	8.891	8.945	9.020
-per capita (kg)	17,6	17,8	17,7	17,7	17,8	17,9
*) Estimated.					ife January 2012	

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

Table 4

EU WMP Balance Sheet

1.000 t	2007	2008	2009	2010	2011*	2012*
Production	773	835	735	755	725	740
Imports	2	2	2	2	0	0
Exports	366	485	463	444	390	410
Stock change	20	15	-55	-20	10	0
Consumption	389	337	329	333	325	330
*) Estimated.					ife January 2012	

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

Table 5

EU SMP Balance Sheet

1.000 t	2007	2008	2009	2010	2011*	2012*
Production	1.090	1.040	1.160	1.080	1.200	1.210
Imports	10	8	6	4	6	6
Consumption	870	775	800	800	810	810
- as Feed	245	150	160	165	190	190
Exports	201	179	227	378	500	450
Ending stocks	124	217	357	263	159	115
- in intervention	-	-	260	195	54	0
*) Estimated.					ife January 2012	

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