

icos DairyDigest May 2011

Cover Story

Irish versus Dutch Milk Prices

A recent analysis of the LTO/ European dairy Farmers ongoing survey of European Milk prices suggests that Irish milk prices are well below those of our European Competitors. These reports compare February Milk prices for the Dutch Milk Price (average FrieslandCampina, DOC Kaas) and for Irish Milk Price (Glanbia and Kerry Average).

Friesland Campina's recent announcement of an increase of 2c per kg in their guaranteed price, up

to 38c per kg (39.13c/litre), will serve to heighten interest in this topic. It is interesting, however, to analyse Friesland Campina's cash price, which is net of a series of deductions and bonuses, which brings the price actually received by farmers for May milk to 35.45 c/kg (36.5c/litre), at standard Co-op constituents of 4.41% fat, and 3.47% protein. Friesland's standard Butter Fat and Protein Constituents are much high than the Irish standard typically used

for its pricing purposes. So what would the FrieslandCampina price equate to if we were to pay for milk with standard Irish constituents of 3.6% fat, and 3.3% protein? This can be easily calculated using Friesland Campina's version of A+B-C, and applying all the other deductions etc. The resultant calculated Friesland Campina May milk price, for typical Irish milk is 30.81c per kg (31.72c/litre).

From a manufacturing milk perspective Irish Milk

is best compared with dairy producing countries that are of similar structure and compete with us in similar markets. Typically this assessment will result in the Irish dairy industry being compared to the Dutch, Danish, and Kiwi dairy industries. Even though each is an active player in the global ingredients market, the Irish dairy sector does face some competitive disadvantages that we need to address.

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Market insight

Dairy Markets

Commodity Prices

	Butter Index	SMP Index	May -11 Fonterra Auction WMP	Holland Milk Price per Litre**	Apr - Jan 11 Ireland Milk Deliveries
May	€4,003	€2,353	\$3,859	30.81c	12.3%
April	€4,087	€2,408	\$3,912	€0.2997	Compared with same timeframe in prev year
March	€4,180	€2,877	\$4,105	€0.2984	
	<i>Eurex*</i>	<i>Eurex*</i>	<i>GDT</i>	<i>Friesland website</i>	

* : Eurex Futures Cash Settlement Price

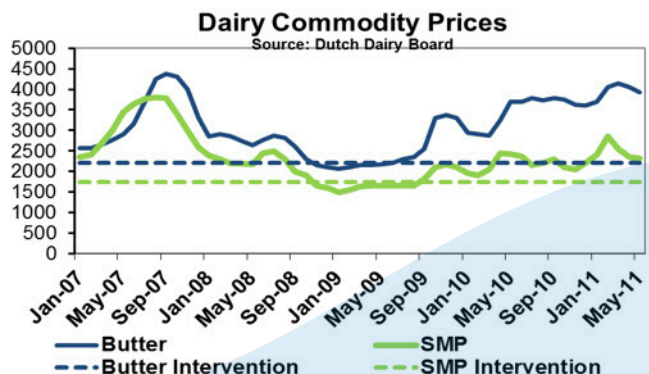
** : FrieslandCampina Price Recalculated to reflect Irish Standard Constituents of 3.6% Butterfat, 3.3% Protein.

Current indicators suggest that dairy prices should remain reasonably stable, at current, high prices. While quoted Dutch prices have shown significant slippage of late, both the Fonterra Auction, and European and World Futures markets have been steadier.

As Europe approaches its seasonal peak, production levels have been strong, with Ireland, France, Germany and the UK showing strong growth. Butter prices have fallen back by about 5% from highs in March, while SMP has fallen by closer to 20% from its high in late February. The fact that EU SMP now trades at discount of around US\$100 per tonne to Oceanic product suggests that prices have now stabilised, with supplies soon expected to decline after the seasonal peak.

European farm gate milk price are considerably higher than last year. LTO Nederland data shows the average milk price paid in March 2011 was €33.16 per 100kg milk. This price is €5.80 per 100kg (21%) higher than prices were a year ago. Many dairy processors increased their farmgate milk price during March 2011. However the average price actually decreased slightly in that

month due to changes to seasonal payments. Several European dairy processors have announced increases in milk prices which either commenced in April 2011 or will commence this month.



McLoughlin delivers Keynote speech at International Cooperative Seminar

ICOS President Pat McLoughlin gives paper at the 'Agricultural Cooperatives: Innovations and Opportunities in 21st Century' conference in Antalya, Turkey, 3rd May 2011. As Vice President of the European Cooperative organisation COGCEA, McLoughlin delivered a wide-ranging presentation on the Irish experience of Co-operative organizations and opportunities for the co-operative movement in food chain and trade affairs.

McLoughlin also used the opportunity to develop links between ICOS with the rapidly expanding Turkish Dairy industry, where growth in population, wealth and consumer demand is among the highest in Europe. Turkey has the 16th largest economy in the world, and, the 6th largest economy compared with EU countries in 2010. Turkey is expected to be the fastest growing economy of the OECD members during 2011-2017, with an expected annual average growth rate of 6.7%.



Snippets

- Armagh based **Fane Valley Co-op** show profit before tax was just over £4.8m on sales £371m (1.3% profit before tax) for the period ending September 2010
- **Kerry** reported pre-tax profits of €392.8m on sales of €4,960m for 2010 (7.9% pre tax profits)
- **Carbery** reported pre-tax profits of €6.8m on sales of €224.3m for 2010 (3% pre tax profits)
- **Arrabawn** made an operating profit of €4.24m on sales of €169.1m (2.5% operating profit)
- **Dairygold's** operating profits from its core activities were €18.9m on a turnover of €693.6m. (2.7% operating profit)
- **Donegal Creameries** reported adjusted operating profits of €3.4m on sales of €126m. (2.7% operating profit)
- **Lakeland** reports an operating profit of €4.5m on sales of €401m (1.1% operating profit)
- The **Irish Dairy Board** reports an operating surplus of €26.9m on sales of €1,900m (1.4% operating surplus)
- **Glanbia** reports operating profit €136.5 million on sales of €2.2 billion, excluding the company's joint ventures. (6.1% operating profit)

James Nicholson's report on the Milk Package Eminent

The amendments to James Nicholson's report were discussed within the European Parliament's Agriculture Committee (COM AGRI) on 2nd May 2011. Main discussions focused on contracts, status of cooperatives and PDOs regions. COM AGRI will vote on James Nicholson's report on 24th May. Until then, the rapporteur and the shadow rapporteurs will try to reach a compromise on almost 300 amendments. ICOS is heavily involved in this legislative process with its allies in likeminded member states and co-ops need to be mindful of the potential impact of this key piece of law.

ICOS welcomes increase in 2012 EU Agriculture Budget

The Commission has presented its draft 2012 budget proposal in which includes a 2.8% rise in EU agricultural spending in terms of payment appropriations compared to 2011. This brings the total for farm spending to 57.948 billion euros out of a total EU budget of €132.7 bn. Despite enormous pressure for a reduction in the Agriculture budget, ICOS has worked hard to ensure that it is maintained to support our industry and our producers.

Emissions Trading Regulations Move Forward: Dairy Industry Included

ICOS is attending a number of stakeholder workshops dealing with the functioning the new Emissions Trading System, which will soon incorporate the industrial aspects of our dairy system.

There are two regulations being formulated at present. One is a monitoring and reporting regulation, which governs definitions and procedures. The second regulation covers accreditation and verification elements of the ETS system. This essentially consolidates a number of existing laws in a single regulation. The Commission are aiming to have the regulations up and running in 2012.

ICOS warns MEPs of MERCOSUR impact

Brussel, May 1st - At a Seminar facilitated by Copa-Cogeca in European Parliament, ICOS, together with other national delegations and Primary Food Processors, warned MEPs of the impact on the EU agri-food sector of a potential agreement in the trade liberalising talks between the EU and Latin American Trade bloc MERCOSUR. The meeting came as the Commission met the MERCOSUR countries for negotiations in the trade talks this week, but offers were not exchanged. The offer is likely to be submitted by mid-June.

China's Impact on Global Dairy

Despite a very strong season end in New Zealand, leading to a 3% increase overall, as well as stabilising or a modest increase in Australia, and 2.2% annual increase in the USA (after 14 months straight of increases), there are signs that demand is keeping pace with supply, with Chinese demand particularly strong. Record levels of whole milk powder were exported from New Zealand in the first quarter of this year. China accounted for nearly 40% of the WMP shipped from New Zealand in that period. Chinese purchases of New Zealand produced WMP increased by 84% from a year ago.

Global dairy prices were down 2.4 per cent from March after seven months of steady growth, according to the latest figures from the Food and Agriculture Organisation (FAO). FAO's Global Dairy Price Index, which consists of butter, skimmed milk powder (SMP), Whole Milk powder (WMP) and casein price quotations, dropped to an average of 229 points, following an average of 234 in February. Despite the decrease, the latest figures show the dairy market is stable, according to the FAO. "WMP prices dropped by 10 per cent, but this fall represents losses of recent gains," they said.

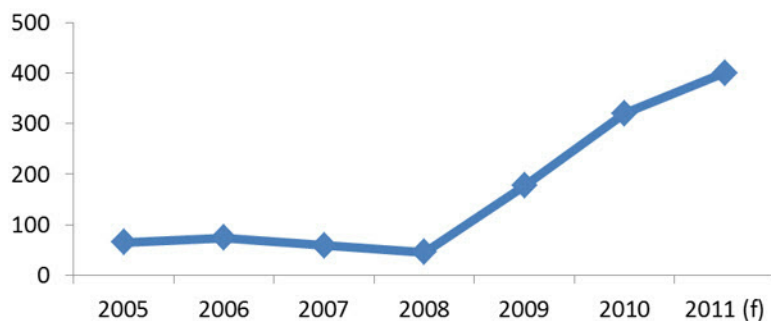
The overall Food Price Index is 36% higher than a year ago. The dairy sub index is 12% up, while the fats and oils index is 9% ahead, compared with April 2010.

Going forward, markets will remain relatively strong, according to the FAO, with a slight drop in prices and a shift between powders and fats. The FAO agree that dairy prices should remain stable, although the future depends on what China does and how the northern hemisphere season develops. "We don't know what China will do this year, and it should be closely monitored," they said.

The import surge from China in 2010 was an important element that kept world prices at high levels. The IMF is warning of an 'abrupt slowdown' in China, although economic growth is still expected to be around 10 per cent this year, according to the organisation.

'000 Tonnes - Chinese Imports of WMP Expected to Grow as Per Capita GDP Increases

Source: USDA



Seanad Elections



ICOS's nominee for the Agriculture panel in the recent Senate Elections, Senator Paddy Burke, from Castlebar, Co. Mayo, was re-elected to the 24th Seanad.

There is now intense speculation that Senator Burke will be the new Cathaoirleach.

He was first elected to the Seanad in 1993 and has retained his seat ever since. For the past two terms the 55-year-old served as Leas Cathaoirleach of the Upper House of the Oireachtas.

International News

- **FrieslandCampina** reports an operating profit €434 million on sales of €8,972m (4.8% operating profit)

- **Arla Foods** reports an operating profit 1,268m DK (€170m) on sales of 49,000b DK (€6,574m) (2.6% operating profit)

Lactalis/ Parmalat Dairy Merger Goes to Italian Courts

French private dairy Lactalis's planned bid for Parmalat SpA, Italy's biggest dairy company, is being challenged in an administrative court by Italian consumer group Codacons. They say that Lactalis shouldn't be allowed to make a tender offer because the company doesn't publicly disclose their accounts, saying it "violates the principle of transparency" and "doesn't allow those involved to make an informed choice." Lactalis on April 26 offered to pay €3.38bn in an unsolicited bid for the 71% of Parmalat they don't own to create the world's largest dairy company.

Scottish Farmers seek Transparency on Milk Pricing

The NFU Scotland has issued a proposal which is calling for the baseline price in milk contracts to be based on a market related pricing formula. After some research and analysis of historic data, a producer-working group has settled for a formula based on the market indicators of AMPE (the Actual Milk price Equivalent) and MCVE (the Milk for Cheese Equivalent), in a 20% and 80% split. This pricing mechanism "reflects real market indicators, and uses figures that are transparent and independently verifiable" according to the NFUS Vice President Allan Bowie.

The AMPE (the Actual Milk price Equivalent) is calculated using publically available market prices for butter and SMP, applying to the value of a standardised litre of milk, and deducting an assumed manufacturing margin.

The MCVE (the Milk for Cheese Equivalent) takes the value of mild cheddar, whey butter, and whey powder from public sources, removes typical processing costs and a profit margin and, by dividing all these figures by the appropriate yields, you are left with the equivalent value of the milk at the factory gate. It is calculated thus; $\text{Income} - \text{Costs} - \text{Profits} = \text{Potential value of milk}$.

While Scottish farmers have cited market failure and a general dissatisfaction with current milk pricing arrangements as the reason for such a change, they have accepted that it will leave them more exposed to price volatility, as their milk price will be directly linked to market conditions.

Continued from Page 1

For example;

- **Market Value of Milk:** comparing the average national milk solids for both Dutch and Irish milk we calculate that were the same volume of Dutch milk to be delivered for manufacturing at Irish plants its added component value would be the equivalent of ~1.5 cents per litre compared with the lower solids yielding Irish Average. Table #1 highlights the average component yield by country.
- **Routes to Market:** The aforementioned analysis of milk price assumes a similar product portfolio and route to market for Irish milk compared to our European counterparts. This is simple not the case. In order to drive debate and progress forward in a positive manner, it is necessary that we index and appreciate the true value of Irish manufacturing milk.
- **Capital Investment:** Amongst the deductions made by FrieslandCampina is a financing charge of 0.74c per kg (0.76 c/l), which should surely be a lesson to Irish farmers, pointing clearly to the willingness of our Dutch farmer competitors to see that their Co-op is adequately funded to provide for future investment and growth. FrieslandCampina's capital expenditure in 2008 alone was the equivalent of 2.3c per kg (2.37 c/l).
- **Seasonality:** FrieslandCampina ensure that the supply curve is flattened by deducting 2.3c per kg (2.37c/l) in the March to June period, thus providing the funds for a bonus of 2.45c per kg (2.52 c/l) in the August to November period.
- **Emissions:** Another issue that the Irish dairy sector needs to be aware of is the milk solids yield per cow in other countries is much higher. Graph #1 highlights the average kg milk solids (BF% and Protein) produced per cow by country. This factor may play an increasing important role on the dairy sector in years to come as Greenhouse Gases (GHG) and Carbon Trading (see page two), becomes more of an issue. This is becoming more and more a consumer driven issue. Two of our major competitors, FrieslandCampina and Arla Foods have significant plans in place to reduce their carbon emissions.

Opinion

The Irish dairy sector needs to work on providing a more objective and transparent milk pricing structure across the

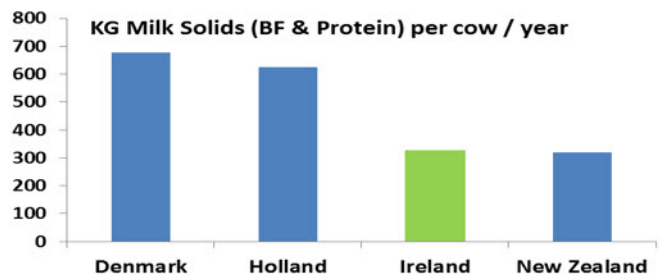
industry. Providing a fair price to the milk producer is imperative. However, we cannot let monthly pricing trends distract us from having a more necessary, albeit at times uncomfortable, discussion on the future for our industry;

- What is a fair and reasonable pricing mechanism for Irish Manufacturing Milk?
- Are we re-investing the necessary Capital Expenditure back into the system to maintain our competitiveness?
- What impact can greater co-operation and consolidation have on plant utilisation and efficiency?
- What does the Irish Dairy Sector need to do to enhance our innovation and route to market capabilities?
- What does the Irish Dairy Sector need to do to improve our weaker per hectare profitability when compared with our European counterparts?

Table 1 – Annual Average Milk Production Per Cow / Selected Countries

	Kg / year	Fat	Protein	Solids	Year
Denmark	8750	4.30%	3.45%	678	2010
Holland	7929	4.37%	3.50%	624	2008
Ireland	4562	3.83%	3.34%	327	2009
New Zealand	3759	4.82%	3.65%	318	2009

Graph 1 – Annual Average Kg Milk Solids per cow / Selected



Diary Dates:

- EP Plenary Session: May 9-12
- EU Farm Council: May 16-17
- Copa-Cogeca Environment Working Party: May 25, Brussels
- EU Veterinary Week on 18/19 May: Brussels
- ICOS AGM to be held in the Killeshin Hotel, Portlaoise, Co Laois on 30.05.2011

	Oil Price (Brent) - US\$ pbl	Carbon Spot: 1 EUA
May	\$1.438	\$16.92
April	\$1.4429	€16.18
March	\$1.3829	€15.44

Exchange rates: €1 : US\$ 1.438, 1€ : GB£ 0.877

Market Movement



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