How successful is your milk buyer?
The updated Company Strategy and Performance Report, now available to download from the DairyCo website, aims to give farmers new insights into how the market environment in which milk buyers operate affects their milk prices.

For most of the companies covered in this report the milk they buy from farmers is their biggest single cost, therefore how successful they are will have a major impact on the amount of milk they purchase and the milk price they can pay their producers.

In particular the report looks at the potential of milk buyers in terms of security of demand and their ability to pay a competitive milk price. It also looks at the buyers’ long term strategy which allows producers to assess how best to structure their enterprise to fit in with that strategy.

One of the key findings of the report was that while most milk buyers benefited from improved returns from dairy commodity markets during 2010, there was little improvement in farmgate milk prices. This situation resulted from a variety of conditions which were present in the GB dairy industry during the year, including intense competition for market share in the retailer own-label milk and the branded Cheddar markets.

The resulting squeeze on processor margins served to limit their ability to increase farmgate milk prices.

It was also found that there was a lack of involvement in the commodity markets, with those buyers able to divert milk supplies to commodity markets not choosing to, perhaps in an attempt to maintain long term relationships with current customers at the expense of making short-term market gains.

In context
Sometimes the only regular information a dairy farmer gets from their buyer is a notification of a price change. Understanding their buyer’s structure and business strategy, along with the market conditions in which it operates, enables producers to better understand the factors which affect the performance of their milk buyer and ultimately their ability to pay a competitive milk price.

The complete report, as well as individual company reports, can be downloaded from the DairyCo website.

UK wholesale prices continue upward trend
February saw large increases on UK wholesale markets across all commodities. Prices for butter increased by around 9.4% between January and February, to an all time high of £3,500/tonne, whilst cream went up 12.2% over the same period to £1,650/tonne. SMP increased by 7.7% in January and February to £2,850/tonne. This represents an increase of 9.6% on its February 2010 price.

These price rises have occurred in conjunction with the continued strength of EU and world markets. Demand continues to be driven by India, Russia and China, the latter of which has a struggling market for domestic products due to concerns over quality and health standards. The political disturbances in parts of North Africa and the Middle East are adding further to demand, as country leaders try to secure adequate food supplies.

At a time when competition for dairy products is high, Oceania is moving into its annual production trough, allowing the US and EU to become the main suppliers to world markets. This has had a knock on effect on UK importers, who are being impacted both by high prices and competition for product. A weak Sterling (which has not surpassed €1.20 in 2011), has made imports even less affordable, further increasing demand for UK supplies.

Welcome bonus for Ex-Dairy Farmers of Britain Producers
Ex-DFB producers who continued to supply the company after 3 June 2009, when PricewaterhouseCoopers (PWC) was appointed receiver, have been informed that they will receive an additional 2ppl on litres supplied. The additional payment has arisen because PWC was able to collect further money from Ex-DFB customers and will equate to approx £300,000 for the milk supplied during the period. This is a welcome bonus to Ex-DFB farmers, who during this period were paid between 15-16ppl for milk supplied after DFB collapsed. PWC hope that the unexpected bonus will help to offset some of the increases in input costs after the winter.

The ‘other’ important milk market - The Middle Ground
Much is said about the intense amount of competition in the middle ground markets for liquid milk, although relatively little market information exists. To shed some light and clarity on this ‘middle’ market, DairyCo is in the process of researching the structure of the middle ground retail market and how it operates in terms of milk purchasing and retailing. The ‘middle ground’ is defined by the Competition Commission as everything apart from the largest eight national multiples together with doorstep deliveries. It includes retailers (other
than the big eight), catering businesses, public sector outlets, wholesalers and business-to-business operators. The relative importance of the middle ground retail market for liquid milk is summarised in the table below.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Volume ('000 litres)</th>
<th>Volume Share</th>
<th>Value (£m)</th>
<th>Value Share</th>
<th>Average price (ppl)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large Multiples &amp; Doorstep</td>
<td>3,930,492</td>
<td>60%</td>
<td>2,669</td>
<td>62%</td>
<td>68</td>
</tr>
<tr>
<td>Middle Ground retail</td>
<td>1,184,808</td>
<td>18%</td>
<td>664</td>
<td>16%</td>
<td>56</td>
</tr>
<tr>
<td>Middle Ground other</td>
<td>1,468,390</td>
<td>22%</td>
<td>960*</td>
<td>22%</td>
<td>65</td>
</tr>
<tr>
<td>Total</td>
<td>6,583,690</td>
<td></td>
<td>4,293*</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Kantar Worldpanel for 52 weeks ending 26 December 2010

*estimated

While the majority of the volumes sold through the multiples and doorstep sector are supplied by the three large processors, Arla, Dairy Crest and Robert Wiseman Dairies (RWD), there is considerably more competition to supply the approximately 85,000 stores which make up the middle ground retail market. The main suppliers to this market segment include RWD, Dairy Crest, Medina, Paynes and Freshways.

In context

The average price for milk sold through middle ground retailers is noticeably lower than in the other sectors. For those processors heavily involved in this sector of the liquid milk market, this may have an impact on margins, and may reduce their ability to pay a high price for their milk.

Oil prices rising sharply

The price of oil has been rising quickly since the beginning of 2011 and reached $112/barrel (£69/barrel) this week according to the latest OPEC figures. This is the highest level since the boom of the summer of 2008 and is $39/barrel (53%) higher than in August 2010. Worries about the unrest in North Africa and its consequences on the supply of oil are partly to blame for the recent rally in prices. The threat of conflict spreading to other oil producing countries also explains these rises and if this were to materialise, prices could climb even further.

The DairyCo monthly fuel tracker shows the effects of this at pump-level, with the price of red diesel reaching 64ppl in February, 25% higher than at the same time last year and only 9ppl lower than its record high of July 2008.

New report adds pressure for UK food retail ‘anti-competition’ enquiry

The Global Economics Division of UBS (a leading world investment bank), published its findings of a study into consumer food price inflation vs. increases in retailers’ actual supply chain costs. According to the study, price hikes passed on to consumers by UK retailers for processed food in the last two years have risen more than 50% faster than retailers actual supply chain costs. UBS claim that this exceeds all justifiable increases in commodities, currency and wage costs over the time period.

In Germany, recent price hikes have led to an anti-competition enquiry to investigate the tactics of the four largest retailers which have an 85% share of the German market. The UBS study concludes that if the UK government feels a lack of competitive practice may be behind ‘unfair’ or ‘excessive’ consumer food price inflation, this could trigger a similar investigation of competitive practices amongst the big multiple retailers here, which have a 70% share of the grocery market according to the Institute of Grocery Distribution.