DAIRY REPORTER

Weekly Dairy News for Members of DFMC

1 June 2009

WCB warns of a bigger loss

Worsening A$ and increased costs hang over 2008/09 result

Warrnambool Cheese and Butter last week announced a further possible profit downgrade as continued world dairy market volatility and decisions made earlier in the year continue to bite. A statement to the ASX said "Continuing volatility in factors affecting the Company's financial performance means that the Company's net loss is likely to exceed the $10-12m foreshadowed earlier in the year". The continuing volatility in the dairy market and the value of the $A has the company unable to pin a range on the final amount of the loss at this stage.

No early leave pass for John McLean

WCB has announced an extension of the contract of CEO John McLean. Mr McLean, the Managing Director of WCB from 1975-2007, took over in April after Neil Kearney fell on his sword after the pricing and right issue debacle. The company said he would take charge in the interim as an executive recruitment team searched for a long-term successor. Chairman Frank Davis said that the critical need for the Company in the current environment was to focus on its core business and servicing its suppliers, with McLean's continuing presence at the helm "critical to that strategy". WCB said it reclaimed 60 million litres of the lost milk after the milk price fiasco, with promises of more to come.

Fonterra releases NZ 2009/10 price outlook

The NZ co-operative forecasts that next year's milk price will be about 12.5% lower than the current year – about the same fall expected in Australia, although the exchange rate could yet play havoc with that outlook.

Depressed export prices and the worsening NZ/US exchange rate have pushed Fonterra to forecast a lower farmgate milk price next season of $4.55 per kilo of milksolids,. The price forecast comprises a "commodity" milk price of $4.10 and a "value return" of 45 cents per kg. This compares with a current year forecast price of $5.20, which includes milk of $4.75 and a value return of 45 cents.

Fonterra has a habit of topping up its forecast as the year rolls on – of course 2008/09 was an exception to that practice. Economists and analysts in NZ expect the final payout for 2009/10 similar to, or a little below, this season's forecast of $5.20 /kg of milk solids, with a range between $4.90 and $5.25. "Many of the highly-geared farmers have been struggling in the past on a NZ$5.20 payout and if it were to transpire at NZ$4.55 they'll struggle even more," said Brendan O'Donovan, chief economist at Westpac Banking Corp. in Wellington. Westpac is leaving its estimate unchanged at NZ$4.90.

The Co-operative has set its ***Fair Value Share*** (FVS) price for 2009/10 at NZ$4.52, 5 cents higher than the estimate in December but $1.05 lower than the NZ$5.57 price for 2008/09. The lower price is largely the result of the major changes in global equity and financial markets over the past year, despite no change in the added value component of its milk price.

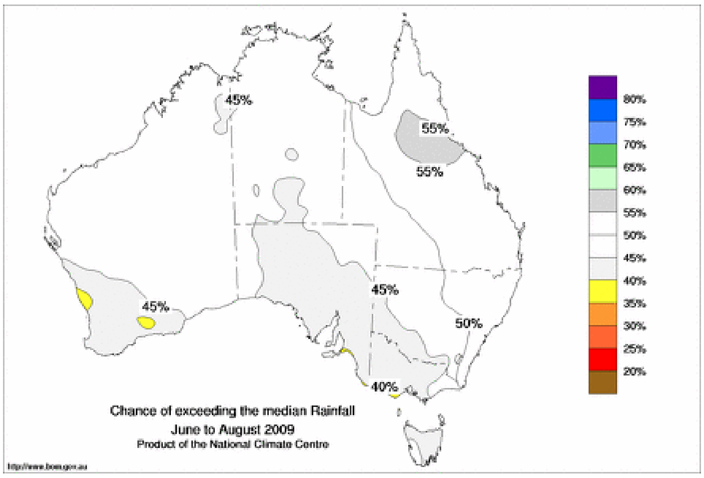
Footprint assessed

The NZ dairy industry reckons it puts out 940g of greenhouse gas emissions per litre of milk, 85% of which is on-farm. The farm assessment is very close to the assessment done for Dairy Australia in 2008. On the farm, the NZ study found that 59 percent of those emissions are methane, 17 percent are carbon dioxide, and 24 percent are nitrous oxide.

Headlines

- WCB warns its loss may be worse
- Fonterra drops prices by 12.5% in 2009/10
- Angry reaction to US export subsidies
- EU may add more to supports
- Grain markets firmer with global crop risks

Indicators	
Dairy export index	**Down by 2 points with $A past US80c**
World dairy prices	**Steady**
Grain futures	**US & local quotes up 4-7 %**
Cow prices (to US)	**Up 1% in $US but expected to weaken**



No major change in weather outlook

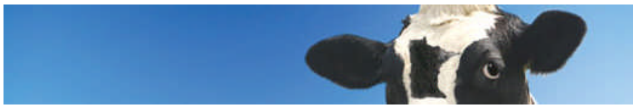
The national outlook for total rainfall over winter (June to August), shows no strong shifts in the odds favouring either wetter or drier conditions. As the map above shows, the Bureau of Met's latest outlook that came out last week suggests that much of Qld and NSW has a 50/50 chance of average rainfall in this period, which weakens over much of Victoria/ The BOM says a few small patches in WA, SA and Victoria, have a slightly weaker outlook.

Grain markets a little firmer

International feed grain prices firmed while future s prices for Australian barley and sorghum also rose last week as fears of pressures on global supply built. The strength of the hike in US prices for wheat and corn was due to concerns about the size and the quality of the US grain crop, tipped to fall in total this year, but was muted in its effects on Australian markets by the stronger dollar. There are also impacts on global grains markets of poor weather in Argentina and the southern CIS producers. Good rains across grain growing regions in Australia last week needs follow-up but will ensure a bigger crop.

DAIRY REPORTER

Weekly Dairy News for Members of DFMC



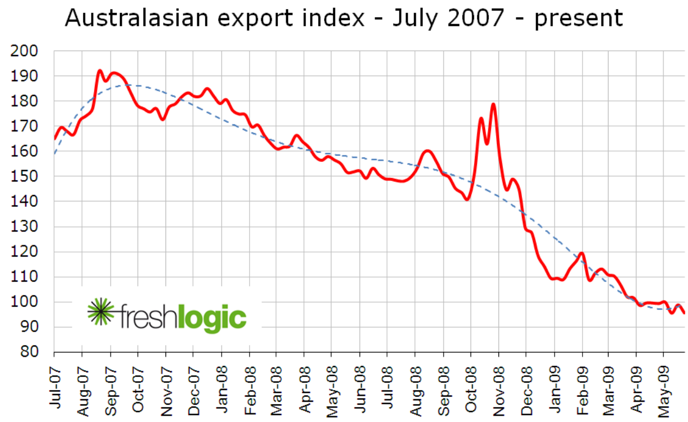
Index goes back down as $A surges

Each week, Freshlogic tracks an index of the $A value of spot returns from dairy exports as an indicator of the potential impact on southern milk prices. It's a good time to have a milk contract with a domestic market processor with the index behaving as it is.

Spot price quotes out of NZ this week stayed flat while the market took a negative view of the eventual impact of DEIP export subsidies and likely further purchases into EU's intervention stocks. The big dampener continues to be the rising value of the $A against the US dollar. The $A ended the week at **US80.1c,** leaving the export index weaker at **93.5.**

Dollar goes through the US80c barrier

This week the gloom for 2009/10 export prices continued as the $A defied "expert" forecasts and nudged through the US80c barrier. The consensus is that traders are attracted by Australia's official interest rates of 3 per cent -- far higher than most developed countries battling recession -- and by our exposure to Asian economies which are expected to come out of the global slump earlier.



Take note: The index is an indicator of spot trends in gross export returns to the industry based on quoted Australasian export prices, movements in currency and the total milk usage in exports by the Australian industry. It was set at 100 on 1 January 2004.

Anger about US DEIP export subsidies

A lot of disappointment and anger was expressed at the news that the US Government revived DEIP export subsidies - rightfully so!

The response to the announcement late last week of US initiatives to support export producers against rival subsidised production has drawn an angry response from the Australian and NZ industries. While words are one thing it will be what the US does next that matters.

The ripple effect of these supports could be significant, announcing the measure to kick in for the 2008/09 year six weeks before its end, with the plan apparently to make available a full year's skim milk powder volume before June 30. The man who runs Fonterra's powder auction said he expected the subsidies to lead to about an extra 70,000 tonnes of US product on the market before June 30 and then another 46,000 tonne tranche in the following six months.

More bad news possible out of Europe

The European Commission has flagged that the period for buying butter into EU intervention stocks (its growing butter mountain) could be stretched beyond current limits in order to aid the struggling dairy sector. The Commission said during the week that 83,000 tonnes of butter have been put into subsidised private storage, while an additional 77,000t has been bought into intervention since the market mechanisms were reactivated.

The Commission hinted that ***export refunds*** and other outlets for EU dairy produce could be further expanded. The Ag Minister for the EU took a cautious approach to the refunds issue, promising to "check" the minimum prices for refund eligibility while basing the export subsidy levels on "objective factors". The EU's farm commissioner said ***single farm payments*** are likely to be brought forward to provide liquidity for cash-strapped farmers.

While the Commission suggested "flexibility" in providing new or expanded support given "unprecedented" price problems in the sector, the Commission says it remains opposed to attempts to revisit the decision to phase out and abolish EU milk quotas by 2015.

Fonterra milk is up 7.5%

Part of the reason world markets are soft is the surge of milk from NZ in response to last year's price and this season's strong opening.

Fonterra expected 2008/09 season production to finish at 7.5% higher on 2007/08, despite earlier claims that New Zealand farmers were having a "very average" and "below average" year. Milk solids collection is likely to total 1,280 million kg compared with the previous season's 1,193 million kg.

Chief executive Andrew Ferrier indicated that Fonterra was having no difficulty selling the increased product and the inventories that built up as demand dropped off in the global recession. Fonterra predicted that international commodity prices would not rise until the EU and US cleared their stockpiles.

Milk sales still growing

Global consumption of milk and other liquid dairy products is expected to increase by a compound annual growth rate of 2.2% over the next three years, according to Tetra Pak. Tetra Pak says that in 2008, consumption of milk in all forms reached a record high of 258 billion litres, 1.6% up over 2007 or an additional four billion litres. Global consumption has grown by a CAGR of 2.4%, over four years, despite a sharp spike in prices in 2007 and 2008,

UHT is the big mover. Tipped to grow 5.2% per year between now and 2012, reaching more than 70 billion litres by 2012.

US market still weak

The reason the US has resorted to subsidising exports is because the US domestic market is in oversupply.

US domestic dairy markets consumed less milk overall in the first quarter of 2009, while US dairy farmers pumped out more. "Commercial disappearance" of all milk and dairy products was about 1.4% below the same period in 2008. Milk sales were up 1.6% in the quarter, and up 0.7% over the last year.

The use of milk in "American cheese" was up about 2.6% in the quarter. Other cheese, including mozzarella, has struggled for a year as the sales through major pizza chains stalled - milk usage down 2.0% for the quarter. It is worse for butter, despite relatively low prices, with usage in all markets including food production down 5.5% in the first quarter. SMP use is also well down about 12% during the first quarter.