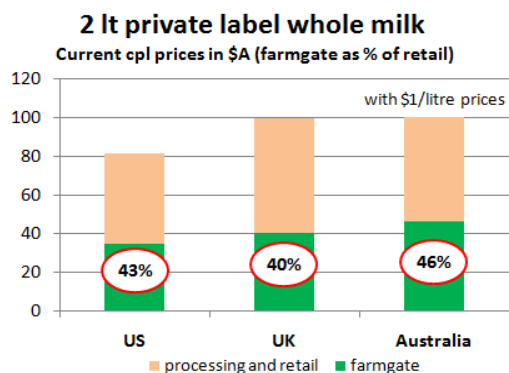


DFMC: milk war affects negotiations

War of words continues between farmers and one big retailer.

The supermarket milk price war may already be influencing negotiations between farmers and processors. Talks between National Foods and DFMC will enter mediation next month. DFMC chairman Ian Zandstra has publicly stated the concern that the impact of the rapid change in the mix of sales being experienced in grocery stores, and in the drift of milk sales away from some parts of the route trade will impact on these negotiations for the 2011-12 season.

An interesting comparison in the chart below may indicate how management of the large grocery retailers may be thinking about relative food prices between here and the rest of the developed retail world. The revised \$2/two-litre whole milk value pulls the local private label product back in line with UK milk prices for private label lines, where farmers are (unhappily as well) getting about 40% on average of the retail price of that product. In the US meantime, where private label prices are significantly lower than they are here on current currency values at least, the US dairy farmer was in February getting about 43% of the retail value.



Coles CEO Ian McLeod wrote a provocative column in the Financial Review that his company makes no apology for saving nearly \$1bn from the food bills of Australian consumers, a line which it will no doubt take when it is taken to task on its price discounts in the dairy cabinet by a Senate Review. Industry has in the past couple of weeks written about the lost revenue in milk sales – Coles quickly turns that around to argue how much they are saving the households from higher food costs.

McLeod has frequently argued that Australians pay too much for food and used the article to have a poke at dairy processors who (he infers) have been guilty of protecting profit margins.

WCB steps up

Stable, improved dairy prices drive a further step-up in farmgate prices.

WCB has announced a further step-up in farmgate milk prices for 2010/11, at 15 c/kg butterfat and 30 c/kg protein. Combined with the increase in the February to June prices announced in September and the step-up announced in November the company said it takes the current committed average price across the 12 months to approximately \$5.25/kg milk solids.

CEO David Lord said that dairy supply and demand fundamentals remain sound and in recent months the company has seen continued stability and improvement in dairy prices. WCB plans to review its milk price again in April 2011, along with considering its business performance and dairy market conditions.



Headlines

- DFMC: milk price affecting price talks
- WCB steps up
- Fonterra freezes milk prices in NZ
- GDT: high WMP the “new norm”
- Mega farm ditched by developers

Indicators	
Dairy export index	Index stronger despite \$A moving higher
World dairy prices	Prices for WMP surge after Fonterra auction
Australian cull cow prices in the US	US prices back on the rise
Grain futures	Sharp fall in US wheat prices

Coles boosts interim profits

Improved results for Coles in the middle of a food prices war.

In the thick of the milk prices war, Coles has released a vastly improved set of earnings numbers to warm a few hearts. The 2nd largest grocery retailer booked an 18% lift in EBIT in its food and liquor division for the December half, on sales that were 6.3% higher (or 6.4% on a same store basis), with price deflation for the half year of 1.7%. Earnings margins at Coles lifted from 3.6% to 4.1% in the half, but it will be interesting to see how the effects of reduced retail prices affect 2nd half margins later this year.

Milk output 1.7% down in Dec

National milk output hit by wet weather in several states.

Milk production in Australia during December 2010 fell by 1.7% compared with the same month in 2009. Year to date milk production for the first half of the season was just 0.1% ahead of the previous season. Tasmania was the only state to grow milk output in December and only trailed WA in YDT terms, while Victoria was 0.7% down in December 2010 to be less than half a percent ahead for the half year.

Lely unveils a new robot

The new robotic milking system could iron out previous barriers to use.

Lely launched the latest version of its Astronaut robotic milking system at Warrnambool's Sungold Field Days. The new robot, named the A4, is the latest in an attempt to make inroads into the Australian market. The major change to the A4 from recent models is that cows walk straight through the system, rather than entering and leaving at a 45 degree angle, which Lely believes is closer to traditional Australian milking systems. The A4 is a smaller overall unit, taking up less floor space and uses less energy, and is about 10% cheaper than current models.

DAIRY REPORTER

Weekly Dairy News for Members of DFMC

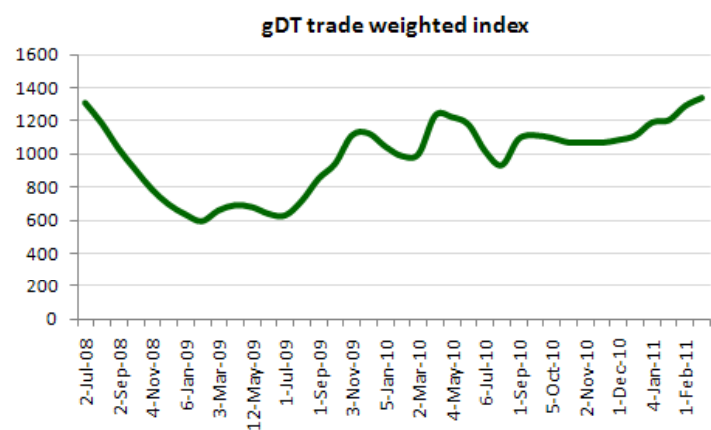
Index of export returns

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.

Dollar stays above parity as prices surge.

Spot prices were up strongly again this week, after another positive gDT auction result. WMP posted the strongest gain, but SMP and cheddar were also better. The \$A closed more than a cent higher at \$US1.0138, allowing another 2-point rise in the index to **139.4**.

Auction result: WMP prices the "new norm". Whole milk powder (WMP) made the biggest gains at this week's Fonterra globalDairyTrade online auction. Prices reached an average US\$4 320/tonne - up 7.9% on the last event two weeks ago. Prices for skimmed milk powder (SMP) steadied, as bidders pushed up average prices just 0.7% to \$3 898/t, while prices for forward orders dropped back by 1.6% to \$3 861/t for deliveries between May and July, and by 3.8% for August to October deliveries, to an average \$3 911/t. Anhydrous milk fat (AMF) also fell back after 9% gains at the last auction. The average price slumped -2.4% to \$6 324/t, with forward order bids down by as much as -3.5%.



NZX launches AMF & SMP futures - NZX has launched futures contracts for anhydrous milkfat (AMF) and skim milk powder (SMP). The new products launched late last week, will allow dairy market participants the opportunity to hedge price movements of these dairy commodities whose prices are often volatile. Since the beginning of 2011, AMF spot prices have appreciated by more than 20%, whilst skim milk powder prices have increased by 24%.

Keen bidding for EU SMP stocks - The EU has again raised the minimum selling price for skimmed milk powder (SMP), selling approximately 15,400t above the new €2500/t price threshold for tenders. The intervention saw highly competitive bids, between a range of €2401 and €2723/t for 22 104 t of SMP. Some 65 000t of SMP had been made available for this week's tenders, while the remaining 50,000t in EU stores will be offered at the next tender, running until March 1, and subject to adjudication at the March 3 management committee meeting. SMP rates rose to €2400/t at the previous management committee meeting.

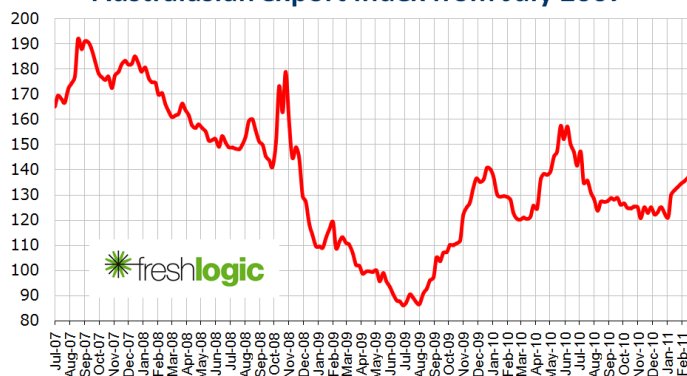
A2 Corp's first half results

Australian dairy operations give A2 its first profitable period in 11 years.

Dairy technology and brand marketing company A2 Corp says it has made its first profit since it was established 11 years ago. The Auckland-based company reported a net profit \$894,000 in the six months to December 31, compared with a previous year loss of \$717,000. Revenue for the six months was \$19.3 million (\$249,000 in the previous period), mostly from its Australian operations. Earnings across the Tasman rose 20% after switching to producing a dairy product rather than the original strategy of collecting royalties from third parties producing milk containing the A2 type of beta casein protein.



Australasian export index from July 2007



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.

Price freeze as world market climbs

Fonterra takes steps to make milk affordable for NZ families.

Fonterra has frozen its wholesale domestic milk prices in NZ for 2011, after criticism it was becoming unaffordable for many families. CEO Andrew Ferrier has stated international milk prices have risen steadily over recent months, and while these prices are good for food exports and the New Zealand economy, New Zealanders are feeling the effects. Public anger at the fast-rising milk price and other dairy products has led Agriculture minister David Carter to seek a special report from his officials on the reality of milk costs in the country.

US milk output up for 12th month straight

US continues to ride high on stronger milk flows.

According to USDA's latest "Milk Production" report, milk production in January was 2.3% higher than the same month a year earlier. The number of milk cows in the 23 states was 8.4 million, up 82,000 head from January 2010 and 14,000 head more than December 2010. Production per cow was up 29 pounds in January compared to the same month a year earlier.

61% of milk from 5% of US farms

Huge concentration in US milk production.

The US industry lost 2,500 dairy farms last year, to leave numbers at 62 500 by the end of the year. There was – as expected – growth in the number of the largest and most productive farms was higher in 2010. The farms with **more than 500 cows now make up 5.4% of farms by number and now account for 61% of all US milk production**, up 1.5% from 2009. The largest size category, farms with 2 000 head or more, grew by 10 to 750 (1.2% of farms) and accounted for 30.8% of the cow herd and 32.5% of US milk production.

Mega farm plan ditched by developers

Controversial super dairy plans gets the axe over environmental concerns.

Plans to set up the UK's largest dairy farm were abandoned because of an environmental report. Nocton said the sole reason for the decision is the response of the Environment Agency, which has maintained its objection to the proposal, on the basis of a lack of information about risks posed to the aquifer underlying the site and uncertainty about the extent of the benefits associated with the change in land use. Nocton said this precautionary stance reflect unfamiliarity with "agriculture in general" and the design of the modern dairy farm in particular. Despite its best efforts to address these concerns, lack of relevant research has made it impossible for the proponents to provide the reassurances required by the Environment Agency that livestock farming is an appropriate use of land at the proposed site.

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