

DAIRY REPORTER

Weekly Dairy News for Members of DFMC



29 March 2011

Floods hit Bega

Milk flows curbed as Bega cops another flood

One of the worst floods in the Bega Valley in more than 30 years has caused havoc for farmers and Bega Cheese. Bega Cheese said flood waters were 3-4 feet through the company's cheese manufacturing plant.

Flooded and closed roads caused big disruptions to transport operations, with milk tankers unable to pick up milk from many farms for 48 hours. Some suppliers had to dump milk as tankers weren't able to get to them to collect it, while others who didn't have back-up power generators weren't able to milk their cows at all. Bega Cheese was forced to move all its milk out of the valley while the floods affected their plant.

Coles grilling arrives

A long-awaited day at the panel, as Coles pitches to the household

Coles senior management will face the Senate Review as this edition goes to mail, with an expected shellacking on its approach to milk pricing and food discounting. As the attention in the retail price wars has since shifted to beer and onto chickens, Coles will play the card about its savings in the overall shopping trolley for struggling households. CEO McLeod has defended Coles's price war with rival Woolworths, claiming that its customers have saved more than \$800 million on their grocery bills in the past 12 months.

Coles will stick to its party line that it paid processors more for their milk in mid-January, before the retail price cut, which was more than enough to offset any switch between branded and private labels.

Get ready for more Senate analysis

After milk, it's now time for the food processing sector to be placed under the Senate's microscope.

The Senate has established a Select Committee to investigate the competitiveness and future viability of Australia's food processing sector as well as assess constraints in the current regulatory environment, including food labelling, trade impediments and (the old chestnut) competition law, where they will again focus on the effect of supermarket pressure on manufacturers. The Senate voted 34-32 to pass a resolution seeking the review. Greens and Labor opposed the move but lost on numbers, claiming these reviews never achieve results.

Metcash case may alter few things

The ACCC has probably overstepped the mark and got more than a few things wrong in how it defines "market"

Two weeks in court may have changed a few things in the way competition law is to be interpreted in future as it applies to the food market at least, with flaws exposed in ACCC arguments and in its methods of stopping deals from going forward.

The biggest issue that Metcash has challenged in the merits of the food retailing case before the Federal Court is the narrow definition of wholesale market that the ACCC has tried to apply, attempting to exclude Coles and Woolworths from the definition of "wholesale market". The tendency for the ACCC has been to define markets narrowly, based on economics rather than commercial terms. The revealing of a Woolworths "secret meeting" to attempt to find an alternate buyer to Metcash will add to pressure on the government to find an alternative when Chairman Graeme Samuels' term ends in July.



Headlines

- Floods hit Bega
- Fonterra posts "first-ever" H1 profit
- Coles "day in court"
- Rabo sees limited impact of Japan
- Italy tries to block a raid on Parmalat

Indicators	
Dairy export index	Index curbed by stronger dollar
World dairy prices	Prices steady as anxiety on Japan lingers
Australian cull cow prices in the US	Market weaker as the \$A firms
Grain futures	Prices steady in local futures markets

Fonterra posts improved earnings

Fonterra farmers eye record payout as the dairy giant gets on track for one of its best years.

Strong international dairy markets mean 2010/11 is shaping up as one of Fonterra's best years ever in terms of returns to its farmer shareholders. Announcing the Co-operative's financial results for the half year to 31 January 2011, Fonterra confirmed its current forecast payout range for the 2010/11 season of \$7.90-\$8.00 (before retentions) and \$7.75-\$7.80 (cash: Milk Price plus dividend). This means this year's payout may surpass Fonterra's previous record in 2007/08 of \$7.90 (before retentions) and \$7.66 (cash comprising, at that time, Milk Price plus Value Return).

NZ production ahead in 2010/11

A better though still sluggish year forecasted for NZ dairy sector.

New Zealand dairy farmers are struggling to keep production ahead of last year's record milk flows, even though summer rains have rescued many regions from the drought that loomed before Christmas. The very heavy rains which arrived over the Christmas and New Year period enabled North Island dairy farmers to avoid what would have been a very early and severe drought, Rabobank said.

Milk solids production in NZ for the season to 31 January 2011 was marginally ahead of the same period last season. Assuming normal rainfall in the March-May period, overall production across the entire 2010/11 season is expected to be broadly in line with, or slightly ahead of, last season. Milk deliveries during the second quarter around 1% to 2% ahead of 2010, assuming a favourable autumn combined with Fonterra's and a near record milk price. The product mix would continue to favour whole milk powder (WMP) rather than cheese and casein.

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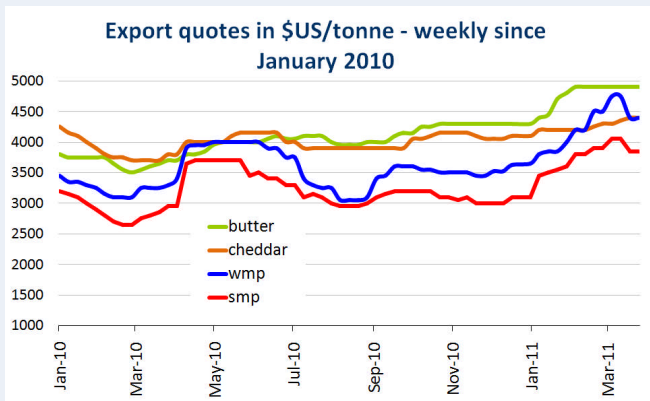
Index of export returns

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.

\$A powers through parity.

Spot prices were steady this week, but currency movements did the damage for the theoretical returns to Australian exporters. The \$A jumped 3 cents against the US dollar to close the week at **\$US1.026**, taking the export returns index down 4 points to **138.4**.

Rabo: Japan impact limited – The Japanese earthquake and tsunami should have a limited effect on global dairy sales, say Rabobank, but only if Japan avoids a nuclear meltdown (which looks more a threat as each day passes). Such an event would not only hurt local dairy consumption but the whole global economy, say the investment bankers. The effect of the disaster has rocked market sentiment, slash grains futures, and sent dairy prices downwards, it said. Rabobank expects market fundamentals to reassert themselves and to continue to sustain international prices at close to the mid-March levels through the second quarter.



Italy tries to block a bid for Parmalat

Lactalis takes stake in Parmalat to 29%, but Italy tries to block the move

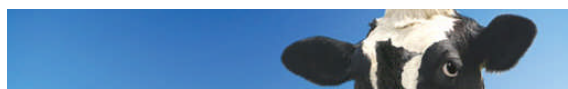
French dairy group Lactalis has lifted its stake in Italy-based rival Parmalat to 29% and said that it plans to allow the companies to offer a full range of dairy products, as both have "leading positions in product categories and geographical areas". Lactalis said its global presence could be "instrumental" for Parmalat's expansion. Lactalis will present a series of candidates for Parmalat's board of directors ahead of its AGM on 12 April.

Italy's government meanwhile declared Parmalat "strategic" to the country and said it would seek to promote an Italian shareholder group in a bid to block Lactalis from gaining management control. The Government allowed Parmalat to delay an April shareholders meeting where Lactalis, its biggest investor, would likely have gained management control. It is also reviewing further measures to prevent foreign takeovers of Italian companies. Italy's antitrust authority is also investigating whether Lactalis's control of Parmalat would violate competition rules.

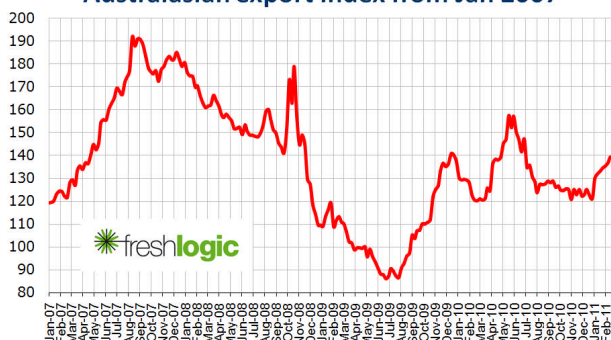
Grain markets rebound

Grain markets bounce back on weather concerns and underlying demand.

US grains prices recovered as commodity traders looked past the massive earthquake, tsunami and nuclear crisis in Japan to a slump in the US dollar and strong export sales, with corn also posting its biggest gain in nearly five months. Wheat futures have rallied back from the slump of 2 weeks ago but are still reflecting some uncertainty over the effects of the conflicts in Northern Africa. Stronger purchasing from China, coupled with weaker crop forecasts has helped push corn prices higher in the past few weeks.



Australasian export index from Jan 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.

EU Ag commissioner sees a bright future

Better conditions could mean a solid year ahead for EU dairy sector.

The lack of surplus milk in the EU in the past year has helped keep dairy markets (and commodity prices) firm for exporters to the world market. Part of the delicate balancing act within the EU is the European Commission's plan to gradually remove regulations, including a cap on production.

The EU dairy sector should continue to expand production throughout 2011 on the back of positive price trends in 2010, the European Commission told its member states. With positive weather conditions, strong demand and better milk prices, milk supply in the EU27 rose 1.23% in 2010, although milk collections are still expected to finish the quota year (ending April) about 6% below quota, a slightly lower shortfall of the overall cap on output than in 2010. This year's increased production was largely processed into value-added production such as yoghurt and cheese, rather than milk powder and butter. While the EU as a whole continues to fall short of quotas, several members will incur super levy fines for over-production this quota year, including the Netherlands, Denmark and Ireland.

These countries want a suspension of quota-overrun penalties as the EU moves towards quota phase-out, but the EC is loathed to reopen the quota debate at all. France argues against any move which could provoke an excessive upsurge in milk supply, and disturb a fragile balance that currently favoured dairy farmers. Production will likely increase in the EU in the 2011-12 quota year, with EU member states enjoying flexibility of annual 1% increases in quota limits as part of the 'soft landing' leading to the phase-out of milk quotas in 2015.

UK farmers want to build a powder plant

Farmers to look into a plan to "take control" in the milk marketplace.

UK radical farmer body Farmers for Action (FFA) wants to build a co-operative led milk drying plant in the north of England, potentially using 25% of the UK's liquid milk. FFA thinks farmers can simply move from being price-takers to price-makers by building a powder plant – taking advantage of the current strength of the global demand for milk powder. Such a strategy may work to provide farmers with improved milk prices, assuming (among other things) that powder prices remain sufficiently high for UK companies to compete on the world markets. Smaller UK plants have prevented this in the past decade.

However, raising the finance to support the venture may be difficult as suppliers need to be convinced that the project can succeed, unlike its unsuccessful predecessor run by United Milk, and be willing to accept the price volatility involved in operating in these markets.

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