

DAIRY REPORTER



Weekly Dairy News for Members of DFMC

9 August 2011

NatFoods reports better first half

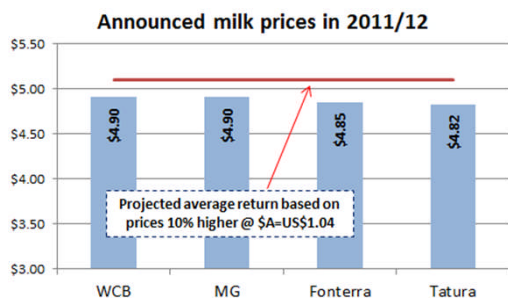
NatFoods trims full-year forecast, despite reporting a better first half.

Kirin Holdings has revised earnings expectations for its Australian subsidiary Lion in a 2nd quarter profit announcement released last week. The dairy and non-alcoholic drinks division of Lion (formerly NatFoods) reported operating income before goodwill write-offs for the 6 months to the end of March 2011 of \$62 million, up 44% on the same period in the prior year, with sales volumes down 13% on the comparative period. Kirin has however revised downwards the division's full-year forecast (for the year to September 2011) from \$98m to \$91m as the full effects of the discounting of milk products and lower volumes kick-in. Lower raw milk costs have helped keep the full year result closer to last year, but the effect of lower volumes is having the biggest impact on the outlook for the diversified group in 2011.

Market decline threatens strong step-ups

How global market prices could affect farmgate price step-ups in 2011/12.

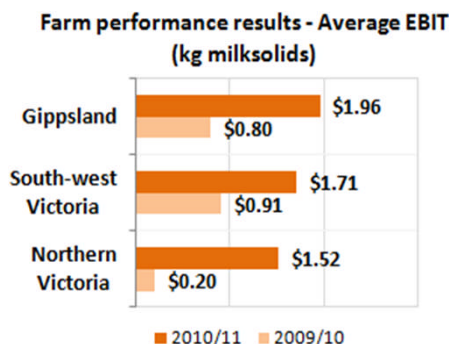
Weaker world market prices may mean farmgate milk price step-ups for the rest of the 2011/12 season could be limited. The opening price period has now passed with opening price averages that appear to now provide limited room for improvement – if world prices improve on current levels. Our full-year price matrix – using US-dollar export prices 10% better than current levels and an exchange rate of A\$1 = US\$1.05 shows some room above announced prices. Dairy farmers will be hoping that the world market bottoms at current levels after its recent “correction” and puts on some gains over the rest of the season.



Farm performance results

Average incomes boosted for Victoria's three major dairying regions.

According to the annual DPI farm monitoring project report, Victorian farmgate milk price was up 25% in the 2010/11 season, averaging \$5.64/kg milk solids, compared to \$4.46/kg milk solids in 2009/10. Average EBIT was \$1.73/kg milk solids, up 166% on the previous period. The biggest profitability movement was recorded in Northern Victoria, with a big rise to \$1.52/kg milk solids in 2010/11 from \$0.20/kg milk solids in the previous season. EBIT averages in south-west Victoria rose 88% to \$1.71/kg milk solids. However, the highest profitability was recorded in Gippsland with a rise of 145% to \$1.96/kg milk solids, from \$0.80/kg milk solids in 2009/10.



Headlines

- NatFoods reports better first half
- Farm performance results 2010/11
- No inquiry into Fonterra's milk pricing
- Dairy prices ease at latest auction
- Kraft lifts forecasts and wants to split

Indicators	
Dairy export index	Index rises, as dollar falls
World dairy prices	Prices firm, with small lift in SMP
US cull cow prices	Market improving
Grain futures	Increase in wheat and local grain prices

Australian full-year production

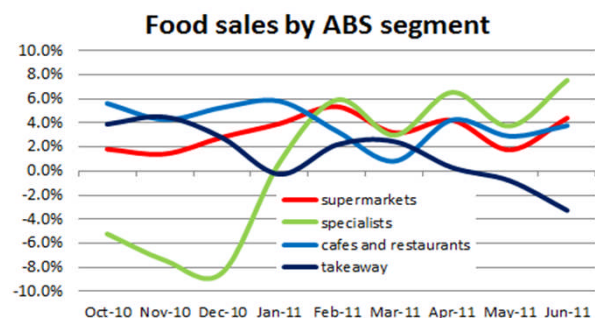
Significant lift in milk powder output, as others declined in 2010/11.

Dairy Australia has reported that milk powders remained the focus of manufacturers, with SMP and WMP recording significant growth in production in the 2010/11 season compared to the 2009/10. Total year-to-date WMP and SMP production were up 20% and 17% at 151,269 and 222,483 tonnes, respectively. In contrast, production of all other major dairy commodities was lower than the last season.

Retail sales show gains for grocery

Food retailing escapes the brunt of an Australian tough retail climate.

Retail sales data released by the Australian Bureau of Statistics (ABS) showed that Australian retail spending fell in June contrary to economists' expectations, after a drop of 0.6% in May. In trend terms, retail sales rose 0.1% in June 2011 compared with June 2010. Data on food sales shows that food retailing (mostly grocery) recorded an increase over the same time last year of 4.7%. In contrast, cafes, restaurants, and takeaway food lifted marginally by 0.5%.



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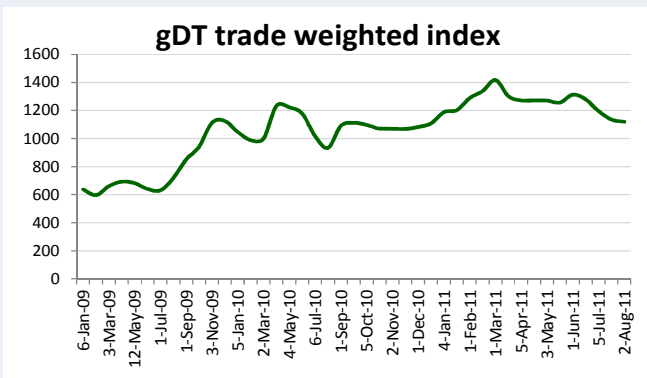
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Index of export returns

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.

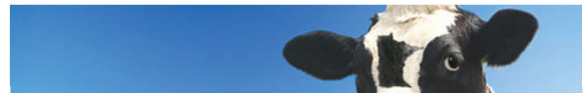
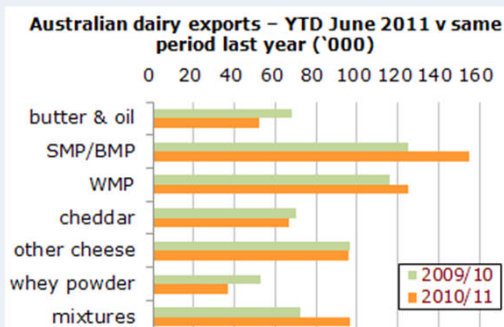
Index rebounds on financial market turmoil. The slump in the value of the \$A late last week as stock markets went into meltdown over the risks associated with deeper EU financial uncertainty has pushed up the index of export returns this week. There were minimal changes in export quotes with a small lift in SMP prices the only action. The \$A closed the week more than 5 cents lower at **\$US1.044**, and the index of spot returns rebounded from last week's 22-month low to **122.3**.

Prices ease at latest auction. Average dairy product prices posted their fourth consecutive decline at Fonterra's online auction last week, lowest since the December sale, tracking a broader decline in global commodity prices. The latest *globalDairyTrade* weighted index fell 1.3%, compared to the previous auction held a fortnight ago on July 19. The biggest movement came again in AMF, which led the decline at an average of \$4,297/t, down 7.2% compared to the previous auction. It was followed by rennet casein which dropped by 4.6% to \$9,498/t. In comparison, SMP fell 1.4% to \$3,479/t and WMP by 0.3% to \$3,474/t. In contrast, butter milk powder rose 3.3% to \$3,319/t and milk protein concentrate 1.7% to \$5,632/t

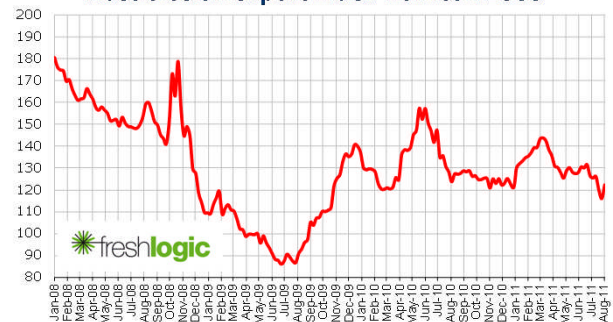


More online trading platforms to follow GDT. Following the lead of Fonterra in launching online trading in dairy commodities, more online trading platforms will be launched soon. Dairy Auctions Online - a platform for trading European sourced dairy products - will commence weekly auctions in October or November 2011. The company's trading scheme is backed by Rabobank and already has one supplier signed up for the first event.

Meanwhile, Argentina has announced plans of commencing a monthly online auction soon, in a bid to stimulate exports and tackle an ongoing spike in production. Government officials have backed this proposal and have met with the dairy industry association CIL to work out the specifics of the proposal. The association of small and mid-sized dairies APYMEL and the dairy boards of Córdoba, Santa Fe, La Pampa and Santiago del Estero have also been involved in the proposal planning



Australasian export index from Jan 2008



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.

Commission upholds Fonterra's pricing

Competition watchdog: There is nothing wrong with co-op's milk pricing.

After a three-month preliminary investigation, the Commerce Commission has announced that it will not be undertaking a formal inquiry into Fonterra's milk pricing, as it found no valid basis for a full inquiry under Part 4 of the Commerce Act - which regulates markets where there is little competition and little likelihood of an increase in competition. The Commission interviewed 32 players at four levels of the domestic milk market, including farm gate supply, factory gate supply, wholesale supply and retail supply.

However, Fonterra still faces several other probes, including the issue of the alleged abuse of market powers. The Commission has said that it would be working with officials from the three government departments investigating "farmgate price" and intended to make a submission to the Agriculture Ministry's current consultation on potential changes to the raw milk regulations governing Fonterra and domestic markets

Dean Foods profits slide

Law suit costs slashes first-year profits at Dean Foods.

The largest US fresh dairy company Dean Foods suffered a loss in first-half profits, affected by the cost of its out-of-court settlement with dairy farmers in the south-east of the US. Net profits plummeted 40.8% to US\$57.1 million for the six months to the end of June 2011, while operating profit dropped 13.9% to US\$221 million. The company has also struggled under soft sales of dairy products, tied in part to the weak US economy, as its costs for raw products from dairy farmers have climbed steadily.

Kraft lifts forecast, as it plans to split

Kraft moves to break in two, as its earnings rise 4%.

Kraft Foods has lifted its full year guidance, on the back of "strong" second-quarter results. The company now forecasts revenue growth by at least 5% in 2011, up from a previous forecast of growth of 4%. For the three months ending June 30, the company saw a net income increase by 3.9% to US\$976 million, operating income by 6.2%, and net revenues by 13.3%.

At the same time, Kraft Foods announced plans to split into two separately trading business - a North American grocery business and a global snacks marker business - by the end of 2012, in order to enable each segment to focus on its distinct strategic priorities. The new global snacks business will consist of the current European and Developing Markets units, and the North American snacks and confectionery businesses will have key brands like Oreo, Cadbury, and Trident gum.



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