

## Arla Looks For Retail Price Increase

Arla Foods UK's CEO Tim Smith has announced that the company is deciding whether to increase prices to their customers following the release of Arla's financial results for the 12 months ending 30 September 2005. The company recorded pre-tax profits (after taking account of exceptional items, goodwill and discontinued operations) at £14.7million. Despite the apparently healthy pre-tax profits, return on sales was only 1.07%.

The company has identified recent oil-led price inflation as a major factor in increasing costs. It highlights the fact that further cost inflation in the final quarter of the financial year has effectively negated the benefit of the retail price initiatives earlier in the year and that fuel and packaging costs are expected to rise further in the current financial year. Mr Smith has identified the expected full year effect of further cost inflation, as 1.47ppl. As a result, Arla has already increased its doorstep price and is reportedly in talks with retail customers. In the presentation accompanying the report, the cost inflation is referred to as 'abnormal and must be recovered from customers'.

However, in its end of year report Arla notes that it will not allow itself to become disadvantaged within the marketplace due to expected downward pressure on raw milk prices in the UK. The company has also confirmed that it is under investigation by the OFT regarding recent retail price initiatives.

### In Context:

Although Arla has said that the increased costs it is facing must be recovered from consumers it has also said it they will not allow itself to become disadvantaged in the market place. Therefore if costs cannot be recovered at retail level there is the potential for farmgate milk price cuts in the future.

## Liquid Milk Sales Increase

TNS data for the 52 weeks ending 6 November 2005 continues to show that overall milk sales are increasing by 1%, to 4.8 billion litres. This growth is predominately due to increases in sales of branded and organic milk. The organic milk sector continues to show rapid growth, with volumes up 58% on last year. Industry commentators are increasingly concerned that organic milk production may struggle to meet demand over the winter period.

Despite this growth in branded milk products, Channel Island milk has seen a year on year decrease of over 20% (although this only accounts for a relatively small volume).

## Trading Begins As OTM Rule Ends

The end of the OTM rule (7 November) has prompted increased activity in livestock markets as cows can now be put through markets instead of going through the OTM scheme. As a result weekly numbers going through the OTMS has decreased slightly. With the complete end of the OTMS on the 20th January, producers have to make the decision whether to put cows through the scheme or sell them through livestock markets.

Figures from market sales conducted so far give liveweight prices that have ranged between £0.50 and £0.72/kg, compared to a November OTMS compensation rate of £0.433/kg. This gives a premium of approximately £0.07-£0.30/kg over the OTMS rate. Auctioneers have noted that only high quality cows have been put forward and therefore prices have been relatively good. Industry commentators have said that until export bans have been lifted (February 2006 at the earliest); poor quality cattle are probably not worth putting through markets; and should be sent through the OTMS instead.

### In Context:

It is important that producers should consider the quality of the animal and the cost of finishing. Once this is taken into account, as well as the labour time, it will often still make more sense to put cows through the OTMS than the open market.

## Largest Farms Expanding Fastest

The largest dairy farms in Great Britain are expanding at the fastest rate according to a MDC review of quota holdings. The work, which compares quota holdings in the 02/03 and 04/05 quota years, shows a direct correlation between the amount of quota held and the rate of increase. Individuals that held less than 0.5 million litres of quota increased their quota holding by an average of 3.9% between the two periods. This compares with individuals that held over 3 million litres of quota increasing their holdings by an average of 45.5%. Larger quota holders are potentially better able to expand as they may be able to secure volume bonuses and may

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benefit from economies of scale. However, it must be noted that a small number of quota holders in this group account for a significant proportion of the change.

Net Quota Held (million litres) based on 04/05 quota year	Average change* in litres held between 02/03 and 04/05	Total number of farmers in category
<0.5	3.91%	6,984
0.5-0.75	8.16%	3,182
0.75-1	8.73%	2,133
1-1.25	9.97%	1,444
1.25-1.5	13.31%	797
1.5-1.75	13.08%	542
1.75-2	16.28%	306
2-3	20.61%	510
>3	45.50%	175

\*Please note that average change is based on producers that retained at least 70% of their 02/03 quota in 04/05

### Further Closures In Liquid Dairies

Liquid milk processors continue to be closed, rationalised or merged as the industry sees further consolidation due to pressure on prices, especially in the middle-ground (i.e. local stores), and on margins. The most recent closure, although they will continue to trade as wholesalers, is B & M dairies who processed approximately 25 million litres of liquid milk predominantly into the doorstep and middle ground market in London and surrounding areas. This news comes soon after recent closures at Longslow Dairies and the acquisition of Scottish Milk Dairies by Grahams Dairies. Over the past year other liquid processing plants such as Midlands Co-op and Hyde Farm have been bought by Dairy Crest.

### OFT Accept DC Acquisition

The Office of Fair Trading (OFT) has accepted Dairy Crest's (DC) acquisition of Arla Foodservice in London for approximately £4 million. The acquisition fell within the OFT criteria not to be referred on to the Competition

Commission as Arla Foodservice had a turnover of less than £70 million. Also the acquisition has not resulted in a market share of greater than 25% of the defined market.

#### In context:

The important issue regarding mergers and acquisitions is how the OFT define the market. In the majority of cases the OFT will allow mergers and acquisitions to go ahead (as in the merger of Arla/Express). However, in a more recent case Wiseman's attempted acquisition of Scottish Milk Dairies (SMD) was refused. As the value of SMD was significantly below £70 million, this meant the OFT felt that Wiseman either had over 25% of the defined market or would do so after the acquisition.

### SPS Confirmed For Scotland And Wales

Both the Scottish Executive and the Welsh Assembly Government have announced their intention to pay an interim payment to farmers in December. Scottish farmers who have submitted valid applications can expect to receive 75% of their payment, while Welsh farmers will receive 80%. Farmers will not be able to receive the full payment until National Reserve entitlements have been allocated across the UK. The deadline for National Reserve applications was extended to 4 November to allow all farmers concerned to send in the relevant paperwork to the RPA. The RPA has announced that it expects to commence payment of the full single farm payment in February 2006. Please see [www.mdcdatum.org.uk/publications/cappublications.htm](http://www.mdcdatum.org.uk/publications/cappublications.htm) for more details.

### Dairy Industry Debate – Have Your Say

Do you have a 'burning issue' you would like to discuss with the 'good and the great'? And hear from key speakers where the industry is heading? Join us at one of our *Dairy Industry Debates*. Full details are available on our website <http://www.mdcdatum.org.uk/DID.htm> including venues, dates and speakers.

Quota Prices (4.00%)	Clean			Leased			Average Farmgate Milk Price: September						
Day End 02/12/05	5.11ppl			0.2ppl			2005	19.18ppl			2004	19.48ppl	
Wholesale Dairy Prices	Butter (unsalted)			Skimmed Milk Powder			Mild Cheddar			Bulk Cream			
02/12/05 £=1.730\$	Nov 05	Oct 05	Nov 04	Nov 05	Oct 05	Nov 04	Nov 05	Oct 05	Nov 04	Nov 05	Oct 05	Nov 04	
02/12/05 €=0.677£													
UK £/tonne	1,820	1,830	1,990	1,420	1,420	1,550	2,100	2,100	2,100	840	840	930	
World £/tonne	1,183	1,173	1,102	1,298	1,263	1,236	1,659	1,629	1,478	N/A	N/A	N/A	
Retail Prices	Liquid Milk (retail) 4 pint poly bottle (ppl equivalent)			Liquid Milk (doorstep) (ppl equivalent)			Butter Branded (p/250g)			Mild Cheddar Non-branded (p/kg)			
Nov' 05	81.7			52.3			83			485			
% Change vs Nov 04	+3.3			+7.7			+1.2			+8.2			