

## UK Trade Deficit Increases By 20%

Latest figures for the UK show that the trade deficit in dairy products grew by 20% in 2005, to £893 million. The main reason behind the deficit has been the continuing trend of importing high value goods and the export of low value produce. The table below shows the average price per tonne of UK imports and exports.

Average £ per Tonne	2004	2005	% Diff (05 v 04)
Imports	1,568	1,604	+2.3%
Exports	914	676	-26.0%
Diff. (Imports v Exports)	654	928	

Examination of the figures shows that this has been mainly due to an increase in the volume of low value products being exported. An example would be the large exports of bulk liquid milk to Ireland, which achieve far lower returns per tonne than other products where the water has been removed i.e., cheese.

## Lactalis to Export Value-Added Cheese

Lactalis (Owner of McLelland in Stranraer and makers of the Seriously Strong product) is to start exporting a number of its value-added (mature) cheddars to Germany. The products will be sold through Metro, a national German retailer.

### In Context

This shows that there are potential markets for the export of UK value-added products. This can potentially help farmgate prices because milk is being moved from commodity to value-added markets.

## Cheese Prices Continue To Hold

Despite a rapid increase in cheese production prices continue to remain stable. Cheese production for 2005 was 12% up on the year before. The majority of this increase was in cheddar, which grew by 15%.

2005	000' tonnes	Yr on Yr % Change
Cheddar	279	+14.8%
Mozarella	56	+5.7%
Long Life Territorials	26	-3.7%
Short Life Territorials	14	+7.7%
Blue Vein	11	+10%
Other Cheese	23	+15%
Total	410	+12.3%

This increase in cheese production is primarily due to the growing differential between returns in the cheese market and the commodity (butter and SMP) market. MCVE (value of cheddar and whey powder) is now 4ppl higher than AMPE (value of butter and SMP).

This growth has continued into 2006 with January cheese

production showing an increase of 7% year-on-year, again the majority in cheddar. Despite this increase, cheese prices continue to remain firm with stocks reported as relatively balanced. A proportion of this extra cheddar manufacture will be young curd for food.

However, analysts are reporting increased price pressure in this market. There are also concerns that a stock problem could emerge in the cheddar market if production continues at its current pace. Finally, there are concerns the manufacture of cheddar is also increasing significantly in Ireland.

### In Context

In the last few weeks, price cuts have been announced by cheese makers Belton, Dairy Crest, Joseph Heler, Wensleydale and Wyke Farms. In announcing these price cuts, the companies have said it is due to a number of factors, including increasing stocks.

## Commodity Markets Round-up

Recent weeks have seen commodity markets remain relatively stable in the UK. SMP continued to creep up in March compared with February, to £1,400/tonne. Reasons include low milk production which, in turn, has meant there is less milk available for manufacture. In addition, there has been increased demand for feed SMP with prices approaching those of food quality SMP. The reason for this has been increased demand for veal on the continent, due to fears of avian flu. Recent figures suggest this market has peaked with prices weakening slightly, however, it is still expected to remain fairly firm.

The opening of intervention has helped to stabilise butter markets, and as a result, helped cream markets as well. Wholesale prices for butter had been falling but are now holding at around £1,740/tonne – just above intervention levels. In addition, exchange rate factors have aided butter and cream markets, with sterling weakening slightly against the euro.

However, there is some concern that butter intervention may be filled quickly - although initial entries were less

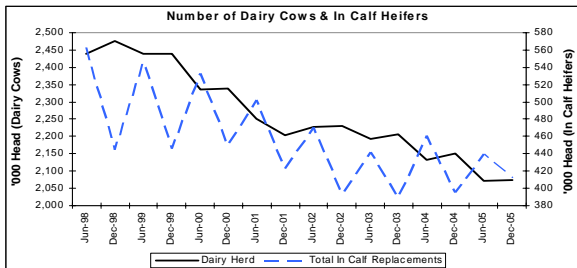
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than anticipated (approx. 12,000 tonnes has been entered). If stocks are filled, further entries would be done on a tender basis which could reduce prices further.

### Latest Census Shows Dairy Herd Down 3.6%

The size of the UK dairy herd fell by 3.6% during 2005 according to Defra census figures. The dairy herd now stands at 2,074,000 cows. This significant decrease is likely to be a significant factor behind why production is down on previous years. The UK is currently 400 million litres (2.9%) below the three-year quota profile average.

In-calf replacements for December were 412,000, up 4.3% on December 2004 and the highest December figure since 2001.



#### In Context

This reduction in cow numbers will significantly affect milk supply even if producers want to increase production. However, as less milk is available, there will be less available for the production of commodity products which could ease pressure on farmgate prices.

### First Milk and Dairy Crest Cut Prices

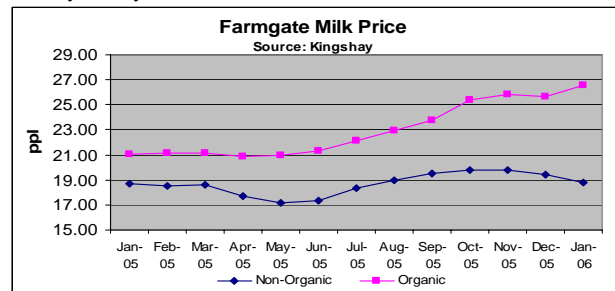
The last week has seen First Milk and Dairy Crest announce price cuts for April of 0.5ppl. First Milk stated that although it had instigated various measures to try and hold off making a cut, combined pressure from liquid

(cream) and cheese markets had forced the move.

Dairy Crest is to cut 0.5ppl from its liquid contracts (exc. M&S, Waitrose). The reduction has been attributed to weakening returns from the cream market.

### Organic Farmgate Milk Price Rises

According to Kingshay data, the organic farmgate milk price for January was 26.6ppl, 5.6ppl higher than January 2005. In comparison, the non-organic milk price for January was reported as 18.81ppl, 0.14ppl higher than January last year.



This increase in the organic price has been driven by the increase in consumer demand for organic milk and milk products. Demand for organic liquid milk increased by 59% in the year to January 2006 according to TNS data. Supply of organic milk could not keep up with the increased demand, and, in the short term, organic milk was imported from abroad.

Consumer demand for conventional liquid milk also rose slightly over the period; however, this will only have impacted on the farmgate milk price of the extra milk sold into the liquid market. This is because the price paid to farmers for conventional milk is not driven by consumer demand and supply mechanisms as in the organic market, but by the price of commodity products, which is where 30% of raw milk produced in the UK ends up.

Quota Prices (4.00%)	Clean		Leased			Average Farmgate Milk Price: January						
	4.70ppl			0.1ppl			2006	18.71ppl			2005	18.92ppl
Day End 30/03/06	Butter (unsalted)			Skimmed Milk Powder			Mild Cheddar			Bulk Cream		
30/03/06 £=\$1.735	Mar 06	Feb 06	Mar 05	Mar 06	Feb 06	Mar 05	Mar 06	Feb 06	Mar 05	Mar 06	Feb 06	Mar 05
30/03/06 €=£0.693	1,740	1,740	1,920	1,400	1,390	1,350	2,100	2,100	2,075	770	760	880
UK £/tonne	1,056	1,059	970	1,176	1,202	1,153	1,549	1,545	1,468	N/A	N/A	N/A
World £/tonne	Liquid Milk (retail) 4 pint poly bottle (ppl equivalent)			Liquid Milk (doorstep) (ppl equivalent)			Butter Branded (p/250g)			Mild Cheddar Non-branded (p/kg)		
Retail Prices	Feb 06			Feb 06			Feb 06			Feb 06		
% Change vs Feb 05	+10.4			+3.9			-7.2			+8.0		

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