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The Market for Dairy Products

Situation and Outlook -- Second Quarter 1994

A. International Market Developments

The general developments in world prices for the major dairy products since the third quarter of 1993 are shown below. Prices reported to the GATT International Dairy Arrangement have declined to varying degrees, according to the individual product. During the second quarter some signs of price stability returned to the market for milk powders.

Export prices reported to the GATT International Dairy Arrangement
(dollars per tonne, f.o.b.)

<table>
<thead>
<tr>
<th>Product</th>
<th>4th Qtr. 1993</th>
<th>1st Qtr. 1994</th>
<th>2nd Qtr. 1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Skim milk powder</td>
<td>1 500 - 1 750</td>
<td>1 450 - 1 600</td>
<td>1 425 - 1 620</td>
</tr>
<tr>
<td>Whole milk powder</td>
<td>1 400 - 1 600</td>
<td>1 380 - 1 560</td>
<td>1 425 - 1 600</td>
</tr>
<tr>
<td>Butter</td>
<td>1 350 - 1 500</td>
<td>1 350 - 1 480</td>
<td>1 100 - 1 500</td>
</tr>
<tr>
<td>Butteroil</td>
<td>1 625 - 1 750</td>
<td>1 625 - 1 780</td>
<td>1 400 - 1 800</td>
</tr>
<tr>
<td>Cheese (Cheddar)</td>
<td>1 800 - 1 950</td>
<td>1 650 - 2 000</td>
<td>1 750 - 1 900</td>
</tr>
</tbody>
</table>

1. Butter – depressed market, suspension of minimum price

In general, the world butter market has remained in a depressed state for the most of the past twelve months. This has been in response to generally lower demand for butterfat in OECD countries, in the CIS, in Africa and the Middle East, as well as in Japan due to a rise in domestic Japanese stocks. The countries of the CIS (in particular the Russian Federation) remain the largest importer of butter; and, according to the FAO, these countries accounted for over 50 per cent of world butter imports in 1993, much of it in the form of food aid or purchases made on concessional terms. The combined effect of the above factors has been continued downward pressure on world prices. Prior to the suspension of the GATT minimum price for butter in May 1994 (see following paragraphs), during the previous three quarters most sales (excluding the derogation sales to the CIS) were at or slightly below the GATT minimum price of $1 350/tonne.

In an effort to stimulate the depressed butterfat market, the International Dairy Arrangement of the GATT adopted a derogation from the minimum price requirements in June 1993. In December 1993 and in March 1994, extensions to the deadline were granted, and the maximum allowable quantity shipped per participating IDA country was raised. During the first quarter of 1994 the pace of these sales continued to be rather slow, and the structural imbalance on this market continued. In an additional effort to encourage butter sales, the IDA at its meeting of May 1994 agreed to suspend the minimum price for butter and butteroil, for a period of 12 months. It was further agreed that the price/market situation would reviewed periodically, and that the suspension could be terminated at any time, should the market situation significantly change.
As regards shipments and commitments to ship butter under the special derogation to the CIS (which were made prior to the suspension of the GATT minimum price), about 86 000 tonnes had been notified to the IDA as of 6 June 1994. About 64 000 tonnes traded at a price between $1 100 - $1 200 per tonne. The major shippers and the total tonnages involved were: New Zealand – 50 000; Australia – 16 500; and, the EU – 14 000.

2. Cheese – continued demand growth, but at a slower pace

Unlike the butter market, the world market for cheese (primarily cheddar and other hard cheeses) has been relatively steady over the past 12 months on the strength of continued strong world demand, and this has been reflected in cheese prices. The demand for cheese is expected to continue to outpace the rate of production, which is likely to provide support for cheese prices throughout 1994. The demand for softer cheeses has not been as strong, thus prices for these cheeses declined slightly during the first half of 1994. The USDA forecasts an increase of 3 per cent in world cheese exports in 1994 (to 889 000 tonnes), compared with an increase of 10 per cent in 1993. The EU, Australia, New Zealand and Switzerland continue to account for over 80 per cent of the volume of exports. Ending stocks of cheese in 1994 are expected to be little changed from their level of 1.7 million tonnes in 1993.

3. Skim milk powder – lower production and consumption

World skim milk powder production declined by about 5 per cent in 1993, while export volumes declined by about 10 per cent. According to the USDA, total output in 1994 is expected to remain virtually unchanged, but consumption is expected to decline further to about 2.2 million tonnes – a decline of about 10 per cent since 1990. Exports are expected to rise by about 10 per cent over the 1993 level, to 1.23 million tonnes. The less-than-buoyant export market in 1993 and during the first half of 1994 was reflected in the range of world prices, which was generally below the level of the fourth quarter of 1993. Reflecting the higher volume of exports forecast for 1994, ending stocks of SMP in 1994 are expected to decline by about 12 per cent to around 850 000 tonnes.

4. Short term market prospects – potentially higher prices and lower subsidised exports

In spite of the less-than-buoyant level of world dairy product prices in mid-1994, the potential for higher prices for lower subsidised exports can be considered bullish for these prices during the remainder of 1994. For example, the general weakness of the US dollar which began in mid-1994 should be a bullish factor, since this is the currency in which contracts are negotiated. Another potentially bullish factor is the fact that the volume of exports permissible under the US Dairy Export Incentive Program is considerably lower than in the past. Thus, if the volume of US exports actually shipped under the DEIP remains at a percentage of about 60-80 per cent of the allowable tonnage (as was the case in 1992 and 1993, respectively), the total tonnage of subsidised exports by the US could decline substantially.
5. Stocks – continued declines, reaching historically low levels

As the data below illustrate, the level of intervention stocks continues downward in the EU and the US, as a result of both countries’ efforts to export butter and SMP, while the level of production has also declined. Combined intervention stocks of butter in these countries were about 450 000 tonnes as of end-1993, and had declined to about 225 000 tonnes by mid-1994. The corresponding volume of SMP stocks declined from about 110 000 tonnes to about 85 000 tonnes. At the same time, the volume of "market" stocks in Australia and New Zealand has declined substantially, as exports have risen. Thus, the combined stock levels (especially the level of intervention stocks) of these four major exporters is substantially below the levels of the past few years.

<table>
<thead>
<tr>
<th>Commodity</th>
<th>Country</th>
<th>end-1993 (000 t.)</th>
<th>mid-1994 (000 t.)</th>
<th>type of stock</th>
</tr>
</thead>
<tbody>
<tr>
<td>Butter</td>
<td>E. Union</td>
<td>240</td>
<td>132</td>
<td>intervention</td>
</tr>
<tr>
<td></td>
<td>United States</td>
<td>206</td>
<td>89</td>
<td>intervention</td>
</tr>
<tr>
<td></td>
<td>Australia</td>
<td>27</td>
<td>25</td>
<td>&quot;market&quot;</td>
</tr>
<tr>
<td></td>
<td>New Zealand</td>
<td>60</td>
<td>30</td>
<td>&quot;market&quot;</td>
</tr>
<tr>
<td>Skim</td>
<td>E. Union</td>
<td>65</td>
<td>47</td>
<td>intervention</td>
</tr>
<tr>
<td>Milk</td>
<td>United States</td>
<td>52</td>
<td>37</td>
<td>intervention</td>
</tr>
<tr>
<td>Powder</td>
<td>Australia</td>
<td>74</td>
<td>25</td>
<td>&quot;market&quot;</td>
</tr>
<tr>
<td></td>
<td>New Zealand</td>
<td>70</td>
<td>40</td>
<td>&quot;market&quot;</td>
</tr>
</tbody>
</table>

Source: OECD dairy questionnaire AGR/CA/APM/MD(94)2.

B. Developments in National Markets and Policies

Australia

- Market developments and related factors

Federal marketing arrangements for manufactured dairy products were reviewed during 1990/1991. As a result of this, the Commonwealth Government enacted legislation aimed at providing a framework to enable a more productive, internationally competitive and export focussed sector to develop. Detailed information was provided in Quarterly Report No. 31. Market support rates have slightly increased since last revisions (fourth quarter 1993). As of 1 July 1994 market support rates were as follows:

Market Support Rates ($A/per tonne): Selected products

<table>
<thead>
<tr>
<th>Product</th>
<th>Support rate 27/9/93-2/12/93</th>
<th>Support rate as of 3/12/93</th>
<th>Support rate as of 1/7/94</th>
</tr>
</thead>
<tbody>
<tr>
<td>Butter</td>
<td>$301</td>
<td>$295</td>
<td>$296</td>
</tr>
<tr>
<td>Cheddar</td>
<td>$360</td>
<td>$352</td>
<td>$355</td>
</tr>
<tr>
<td>SMP</td>
<td>$288</td>
<td>$282</td>
<td>$285</td>
</tr>
<tr>
<td>WMP</td>
<td>$305</td>
<td>$298</td>
<td>$301</td>
</tr>
</tbody>
</table>
- Adjustment measures and policy developments in the dairy sector

The very favourable seasonal conditions experience over most of 1993/94 have resulted in significant milk production increases.

With some recovery in the domestic economy, demand for dairy products has increased slightly. For example, demand for cheese products has increased by around three per cent compared with only around 1-2 per cent in 1992/93. In line with a general trend towards lower fat/health lines, demand for yogurts and dairy desserts continues to grow.

Consumer preference for convenience lines of cheese is sliced and shredded, has resulted in these lines now accounting for over 30 per cent of total supermarket sales of cheese.

In line with some easing in international market prices, farm gate prices have fallen. Opening 1994/95 farm gate prices are likely to be around 5-10 per cent lower than the opening prices of 1993/94.

New Zealand

- Market developments and related factors

For the dairy season ended 30 May 1994 New Zealand milk production was 9.3 million tonne, the largest quantity ever produced in New Zealand in one season, an increase of 12 per cent over the previous season and 18 per cent above the decade average. Milk used for the manufacture of dairy products was 8.8 million tonne in 1993/94, 7.9 million tonne in 1992/93, 7.7 million tonne in 1991/92 and 7.3 million tonne in 1990/91. Three consecutive years of favourable climate for New Zealand dairy farming, that entailed dry mild winters, warm wet springs and moist summers have been attributed to an El Nino climate event that now appears to have abated.

While the processing capacity has been expanded over recent years, the unexpected level of increase in volume of milk produced during 1993/94 strained the existing processing capacity during the peak of the season. To cope with peak milk flows, milk was diverted from the Waikato region to other areas where companies still had excess capacity. Further expansion of cheese and wholemilk powder manufacturing plants is under way or being planned. A new powder plant, capable of processing up to 3 million litres of milk a day, will be commissioned in the Waikato, in time for the 1994/95 season. A further increase in the region’s processing capacity will occur with the commissioning, in time for the 1995/96 season of a cheese manufacturing plant, with an initial production of around 45,000 tonnes.

As well as the 1993/94 increases in cheese and whole milk powder production of 33 per cent and 10 per cent respectively (provisional), butter and skim milk powder production also grew by about 10 per cent. In future seasons there can be expected to be a significant drop in butter manufactured as a consequence of an expected decline in milk production closer to the long term average as the weather situation returns to normal.
The estimated number of dairy cows at the beginning of 1993/94 has been revised upwards to 2.9 million (provisional), an increase of 3 per cent over the previous season. Fluctuations in this range are usual as farmers either defer or advance culling of old or less productive cows depending on the amount of feed available in each season.

- Adjustment measures and policy developments in the dairy sector

The average farmgate price for milk in 1993/94 is expected to be 15 per cent lower than that in the previous season at NZ$3.16 per kg milk solids or NZ$0.26 or US$0.15 per litre of milk. Milk revenues per farm declined only by about 3 per cent as the increased milk volume offset the price fall. Returns from livestock sales were less and average gross farm income is expected to be 3 per cent down on the last season.

Canada

- Adjustment measures and policy developments in the dairy sector

Industrial milk and cream production in the 1993/94 dairy year (August-July) is expected to reach totalled 43.3 mHL at 3.6 kg of butterfat per hectolitre, up from 41.89 mHL in the previous dairy year. Total milk deliveries should increase slightly to 73.8 mHL at 3.6 kg of butterfat per HL.

Butter production is expected to decline in this current dairy year, but at a slower rate than recent years mainly because of the butter utilization program administered by the Canadian Dairy Commission. The objective of this program is to increase the domestic utilization of butter in specific baking goods.

Cheddar cheese production is forecast to increase to 114 Mkg and consumption to 109 Mkg. This would be the same level as in 1990/91. Specialty cheese production and consumption are still expected to increase to 160 Mkg and 173 Mkg respectively.

United States

- Market developments and related factors

Milk production increases will keep farm prices well below a year earlier during the rest of 1994. Production increases are expected to surpass the increases in commercial use.

April-June milk production per cow received the expected lift from new forage, heavier concentrate feeding, and use of bovine somatotropin (BST), and rose more than 2 per cent from a year earlier. However, May-June gains in output were not as large as in April, when very favorable weather in southern regions gave an extra boost to the normal seasonal peaks. Increases in milk yields per cow are projected to rise slightly during the rest of 1994.
Although down substantially from a year earlier, spring milk cow numbers showed a slight rise over the past few months. Cow numbers rose in the western and southern States, where expansion in herds continues, while some Midwestern States are stabilizing after sharp declines in cow numbers in 1993. Relatively high milk prices in the first-half of 1993 contributed to more stable cow numbers, but longer-run structural pressures remained dominant. Second-half declines in milk cow numbers are projected to be slightly smaller than the almost 1 per cent drop in April-June.

The projected 2 per cent increase in second-half milk production and large late spring stocks should keep skim solids markets amply supplied. Growth in skim solids use is expected to be modest. Government purchases of nonfat dry milk are expected to continue into autumn because subsidized export sales of SMP show no signs of picking up.

MILK & DAIRY PRODUCTS - Second Quarter Statistics

<table>
<thead>
<tr>
<th></th>
<th>Jun-93</th>
<th>Apr-94</th>
<th>May-94</th>
<th>Jun-94</th>
</tr>
</thead>
<tbody>
<tr>
<td>Milk production</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Production - 21 States, 000 t.</td>
<td>4 962</td>
<td>5 395</td>
<td>5 196</td>
<td>4 990</td>
</tr>
<tr>
<td>Milk cow numbers - 21 States, 000s</td>
<td>8 130</td>
<td>8 014</td>
<td>8 021</td>
<td>8 037</td>
</tr>
<tr>
<td>Milk per cow - 21 States, kg.</td>
<td>611</td>
<td>624</td>
<td>648</td>
<td>669</td>
</tr>
<tr>
<td>Production - U.S., Mil. t.</td>
<td>5 877</td>
<td>5 974</td>
<td>6 671</td>
<td>5 955</td>
</tr>
<tr>
<td>Milk prices: Dol./hundredweight</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>All milk</td>
<td>13.00</td>
<td>13.50</td>
<td>12.90</td>
<td>12.80</td>
</tr>
<tr>
<td>Milk for fluid use</td>
<td>13.10</td>
<td>13.60</td>
<td>13.00</td>
<td>12.80</td>
</tr>
<tr>
<td>Manufacturing grade milk</td>
<td>11.90</td>
<td>12.60</td>
<td>11.50</td>
<td>11.20</td>
</tr>
<tr>
<td>Minnesota-Wisc. price (3.5% fat)</td>
<td>12.03</td>
<td>12.99</td>
<td>11.51</td>
<td>11.25</td>
</tr>
</tbody>
</table>

The European Union

- Market developments and related factors

Milk deliveries for the first four months of 1994 were 1 per cent down on the same period in 1993. This was chiefly due to poor weather which kept livestock inside, hence a lower milk fat content in some Member states.

Since 1989 producer prices have fallen by 4 per cent at current prices. In 1994 they fell more sharply, except in Spain and Greece where they were much higher. These are countries with a deficit in such products and price trends have run counter to those in other Member states.

The amount of butter in public storage continues to fall, while private stocks reflect a seasonal rise that is not as sharp as in previous years. Cheese stocks are still declining.

Public stocks of skimmed milk powder (SMP), however, are showing a seasonal increase. As soon as intervention opened on 1 March, large amounts of SMP were put onto the market. So far, 50 165 tonnes have been offered for
sale, of which 41,682 tonnes from Ireland. This is because the Irish currency has appreciated against other currencies, including the country's traditional markets, and this has raised problems for Irish sales, especially to the United Kingdom.

- **Adjustment measures and policy developments in the dairy sector**

In April 1994, export restitutions of dairy products were reduced by an average of 5 per cent (except for butter and skim milk powder), and subsidies for private cheese stocks were reduced by between 9 and 22 per cent depending on the type of cheese.

The abolition of the co-responsibility levy as from 1 April 1993 made it necessary to introduce a new scheme (1) for promoting dairy products, since the previous system was funded from the levy. However, resources available for the new scheme amounted to only Ecu 10 million, whereas expenditure in 1992/1993 and 1993/1994 totalled Ecu 55 million. In a Communication (2) to the Council on 7 April 1993, the Commission set out a programme of measures for promoting consumption in the Community and expanding the milk markets in 1994/95. Given the limited availability of funds, the Commission opted to focus on a single product, namely liquid milk, with a view to increasing the consumption of whole milk, which is steadily declining, the trend being particularly noticeable in the case of pasteurised whole milk.

The following decisions concerning dairy policies for the 1994/95 dairy year were taken at the June 1994 meeting of Ministers of Agriculture:

- the suggested one per cent reduction in reference quantities for national quotas was not adopted;
- the temporary quota increase of 1993 (900,000 tonnes) for Italy was made definite;
- the 1993 quota increase for Greece "will be assessed";
- the extension of the provisional attribution of quotas to the new German States was extended;
- the intervention price for butter was reduced by 3 per cent for 1994/95.

As was the case in 1993, due to the relatively low price level of skim milk powder, intervention buying was again initiated in 1994. Intervention buying at the full intervention price was available during 1/3/94 until 31/8/94, up to a total of 106,000 tonnes. At mid-year, about one-half of this quantity had been accepted. Stocks of SMP were about 65,000 tonnes at mid-year, compared with ending stocks in 1993 of about 40,000 tonnes.

Following negotiations for the prospective new member States, quotas were granted in the following quantities for 1994/95 (million tonnes): Sweden - 3.303; Finland - 2.552 (including an allowance of 200,000 tonnes to cover the producers who are currently "opting out"); Austria - 2.752, of which 2.205 is for deliveries to dairies, with 240,000 tonnes in direct sales plus a SLOM-style reserve of 180,000 tonnes; and, Norway - 2.017.
United Kingdom

- Market developments and related factors

There were no cuts in national milk quota for the year 1993/94. There are currently no plans for an outgoers’ scheme or any other form of inducement for farmers to leave dairying.

- Adjustment measures and policy developments in the dairy sector

As a result of poor weather conditions in early May first cut silage quality is likely to be variable.

That cut early has the potential to be wet with a butyric fermentation. That cut later in good weather conditions is likely to be dry and well fermented but of below average energy content.

There is little forward buying of straights for next winter as milk producers anticipate low autumn cereal prices.

As a result of the Minister’s announcement accepting the proposals for the scheme of reorganisation Dairy Companies are expected to announce milk prices and those producers, who have not already done so, will over the next few weeks be making the decision on where to sell their milk.

Quota leasing and purchase prices are high compared to this time last year reflecting both:

1. concern that the potential quota threshold will be low
2. confidence in the industry.

There is concern with regard to the risks of increased diseases as a result of the importation of live cattle.

There is some ‘bad’ feeling with the regard to the ‘none’ allocation of SLOM III quota and the effect that this is predicted to have on final threshold for the 1993/94 quota year, i.e. higher than expected meaning that some may have cut back production unnecessarily.
Trade liberalisation among the PIT countries, is to be accelerated, under a supplementary protocol to the CEFTA, which was signed in Budapest on 29 April 1994. Under this agreement, duties on agricultural trade between Hungary and Poland were cut by 50 per cent in 1/7/94. This compares to the original agreement which called for these duties to fall by 20 per cent over two years, and by 50 per cent in five years. Hungary has also agreed with the Czech and Slovak Republics to reduce duties on farm goods by 50 per cent (instead of 20 per cent) by 1 January 1997. These agreements are likely to stimulate trade in all agricultural products, including dairy products.

**The Czech Republic**

- Adjustment measures and policy developments in the dairy sector

The dairy sector continues to react to privatisation and restructuring under the current economic conditions. A further decline in dairy production is forecast for 1994. In May, the Ministry of Agriculture indicated that milk deliveries could decline by about 17 per cent in 1994, to 3.2 billion litres, primarily due to the continued decline in the dairy cow herd. This will lead to a decline in the surplus of milk production over consumption, which is currently estimated at 237 million litres. The major reason for such a surplus is the decrease in purchasing power of consumers, which has led to an overall decline in per capita consumption of dairy products.

**Poland**

- Adjustment measures and policy developments in the dairy sector

The National Association of Dairy Co-operatives has prepared a five-point strategic development programme for the Polish dairy sector. Its recommendations are:

1. Concentration of milk production by supporting producers in their efforts to expand dairy herds and to improve milk quality;
2. The integration of dairy co-operatives with specialisation of production;
3. More efficient promotion of dairy products to increase consumption, as well as the expansion of specialised dairy shops;
4. Financial support to modernise dairy technology;
5. Market coordination of exports/imports and intervention buying of butter, SMP and cheese.

The Association estimates that 700 billion zlotys (about $33 million) are needed to support milk producers, primarily farmers with larger herds. Most of the support, according to the Association should be spent on modernisation of equipment and purchasing high-quality heifers, thus stimulating long term herd improvement.
Argentina

- Market developments and related factors

The annual average producer price for milk varies between 15 - 20 cents (US) per liter, depending on the volume and quality delivered. Also, the price is higher in the proximity of population centers. The price system was liberalised completely in 1991. Essentially due to this liberalisation, the price to producers in 1994 (in real terms) is between 10 per cent and 50 per cent below the average of the 1980s. According to the Farmers Association of Argentina, producers are currently in the process of trying to lower their costs of production, since they are faced with rapidly rising input costs. They are concentrating on lowering the cost of labor and services, and are intensifying their usage of machinery and equipment.
NOTES

(1) Council Regulation (EEC) No. 2073/92 on promoting consumption in the Community and expanding the markets for milk and milk products; and Commission Regulation 3582/93 on detailed rules for its application.

(2) COM(94)113 FINAL: Programme of measures for promoting consumption in the Community and expanding the markets for milk and milk products in 1993/94.
Table I
Table II
Table III
Table IV
Table V
Table VI
Table VII
Table VIII