THE ULSTER FARMERS UNION CASE FOR A REVIEW OF DAIRY INTERVENTION REFERENCE THRESHOLDS

Background to the UFU call for a review of Dairy Intervention Reference Thresholds

Current Milk Price Situation and Short Term Prospects

The milk price cycle illustrates the classic “peak and trough” pattern, with farmgate prices as a rule going back down as quickly as they went up. This has been accepted as a consequence of the growing volatility in milk prices. However, what is facing dairying at present is different, with the industry enduring a prolonged period of low prices (possibly sub 20ppl) which could continue for at least another 6 months.

This pessimistic view is backed by the June 2015 report from Rabobank, which stated that any recovery would be unlikely until early 2016 at the earliest. However, the report also contained a stark warning for the short term prospects for Dairying. Since the Melamine scandal in China (along with the urbanisation of large sections of their rural population) demand for dairy imports has soared. This, in turn boosted the fortunes for dairying, bringing about recovery from the previous instances of falling prices in the cycle.

It has been recognised that that overproduction has contributed to the current fall in prices and for the last 12 months, the dairy world has been looking to China to once again contribute to rising prices. This was seen in 2009, 2012 and 2013. However, Rabobank do not believe that Chinese buyers are likely to return to the market any time soon.

There will only be a sustained recovery in prices when milk supply and demand reach equilibrium. The days of China shoring up demand could be gone as they address their own economic problems.

NI Farmgate Milk Price

From the peak of December 2013, the farmgate milk price has fallen by 50%, with a record number of consecutive monthly falls. Table One below illustrates the fact that Northern Ireland faces different pricing patterns to not only GB, but also EU.

Table One - NI Farmgate Milk Prices v GB v EU

Pence/litre	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
EU	28.78	24.65	27.19	30.37	27.31	31.91	30.91
NI	22.93	19.79	25.09	27.37	26.11	31.51	29.11
GB	26.47	24.66	26.62	27.36	28.52	31.60	32.04

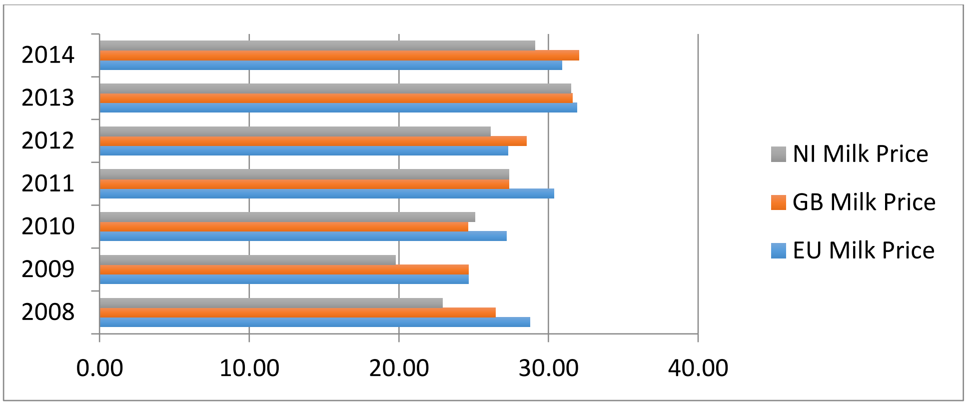
Source – DARD/Dairy Co/DG Agri

NI – GB Farmgate Prices – Northern Ireland exports 85% of the milk we produce and the GB market has a more significant domestic liquid sector. The UFU would stress that when the Commission consider the UK milk price, closer investigation would point to a 2ppl price differential over the 7 year period, which exists despite NI having access to more lucrative commodity markets. The difference between GB and NI data is now accounted for in our submission to the Milk Market Observatory, with NI-specific prices available.

NI – EU Farmgate Price – EU farmgate milk prices over the last 7 years have been 2.75ppl higher than those in Northern Ireland.

Graph One illustrates the start differences between NI, GB and the EU.

Graph One - NI Farmgate Milk Price v GB v EU - 2008 to 2014



The UFU Policy Request

In light of the unprecedented sustained low prices, the UFU have been and are continuing to formally call upon the Dairy Intervention Reference Thresholds to be at the very least reviewed and then revised upwards to ensure that this already concerning situation does not get any worse. This has increased urgency following confirmation that the Russian ban has been extended for a further 12 months.

Intervention Reference Thresholds were last reviewed as part of the 2008 CAP "Health Check" and the UFU wish to make the case that production costs have increased significantly on farms throughout the EU since then and a review of reference thresholds is long overdue and it is upon this basis that we will make our case

Background to Dairy Intervention

The "reference thresholds" for intervention for SMP and butter are detailed in Article 7. 1. (e) of Parliament and Council Regulation 1308/2013 as outlined below:

- SMP = €1698.0/t £1221.58/tonne
- Butter= €2463.90/t £1771.94/tonne

At an exchange rate of €1 = £0.71.

Public misconception of Intervention and the most recent use of Dairy Intervention

When Intervention is mentioned to the general public it summons images of milk lakes and butter mountains, and this view is not accurate. Market measures were used in the dairy crisis of 2009, with Intervention being used from January 2009 to beginning of 2010 to limit the drop in EU prices. At the time, UFU consistently called for the release of store product to be managed so as not to put any further downward pressure on price. As it happens, the purchase of public stocks provided a buffer to mitigate the downward path of prices at that time and the stocks were sold eventually for a significant profit without any stockpiling of product.

CAP Reform

Throughout the negotiations for the current Common Agriculture Policy, reference was made to intervention providing a “safety net”. During the negotiations, there was support among some EU Member States and MEPs to strengthen the intervention system in view of the likelihood of increased price volatility. The Parliament’s negotiating mandate included the following amendments to the Commission’s intervention proposals:

- Public intervention to be available throughout the year with no calendar limits:
- Raise the volume limit for public intervention for butter from 30,000t to 70,000t.

In the final agreement, the Commission did cede on three modifications: the public intervention period for butter and SMP was extended by one month; the volume limit for public intervention for butter was increased to 50,000 tonnes; and the possibility of private storage aid is restored to PDO/PGI cheeses.

This fell short of any formal review of the intervention thresholds and the UFU are now once again calling upon the Commission to take action to address this.

European Commission Mandate

Article 7.2 of Parliament and Council Regulation 1308/2013 does state that “the reference thresholds provided for in paragraph 1 shall be kept under review by the Commission, taking account of objective criteria, notably developments in production, costs of production, (particularly inputs), and market trends. When necessary, the reference thresholds shall be updated in accordance with the ordinary legislative procedure in the light of developments in production and markets”

Dairy Production costs in Northern Ireland

Northern Ireland dairy farm production costs have increased very substantially since intervention was last reviewed. This is illustrated below incorporating fixed and variable components for production costs.

- **On-Farm Fixed Dairy Costs (Northern Ireland)**

As shown in Table Two below, fixed costs on Northern Ireland Dairy Farms have increased by 32%.

Table Two - Fixed Costs Dairy Farms

Fixed Costs (exc labour)	**2008/2009 (£ per farmed hectare)**	**2013/2014 (£ per farmed hectare)**
Conacre Rent	62	68
Depreciation (fixed capital expenditure)	162	184
Depreciation (plant and machinery)	128	176
Upkeep and running of machinery	147	222
Fuel	39	50
Rates	15	17
Building Repairs	48	75
Miscellaneous	40	54
Total Fixed Costs (exc labour)	642	846

Source - DARD Northern Ireland Farm Performance Indicators 2013/14

- **On-Farm Variable Dairy Costs (Northern Ireland)**

Table Three below illustrates a 66% increase in on-farm variable costs for NI dairy farmers over the same period.

Table Three – On-Farm Variable Dairy Production Costs

Variable Costs	**2008/2009**	**2011/2012**	**2013/2014**
Concentrates	386	535	675
Silage	140	163	204
Vet/Medicines	87	124	141
Total Variable Costs	613	822	1020

Source - DARD Northern Ireland Farm Performance Indicators 2013/14

The rising use and cost of concentrates in Northern Ireland Dairying is particularly evident. The quantity of concentrate feed fed to cows is now in excess of 1 tonne, and the subsequent expenditure on feed has increased substantially. This is illustrated below in tables 4 and 5 over the last number of years.

Table Four - Concentrate feed per cow – DARD Northern Ireland Farm Performance Indicators 2013/14

	2008/2009	**2011/2012**	**2013/2014**
Concentrates per litre (kg)	0.31	0.33	0.37
Concentrates price per tonne (£)	206	232	266

Source - DARD Northern Ireland Farm Performance Indicators 2013/14

In terms of cost per litre figures, Table Five below clearly illustrates the increased cost of concentrates impacts on NI dairy farms.

Table Five – Concentrate Price per litre of milk produced

	2008/2009	**2011/2012**	**2013/2014**
Yield per cow (litres)	6025	6676	6710
Pence per litre	6.38	8.01	10.38

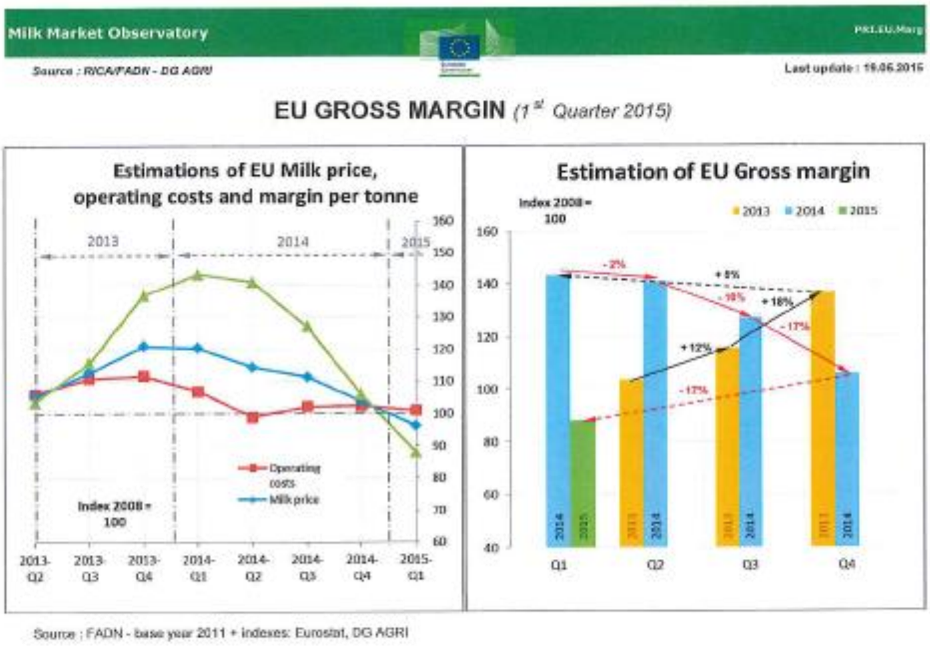
Source – Ulster Farmers' Union

The combination of all these costs equates to is an average cost of production for many NI Dairy farmers **in the region of 26.5p per litre**. There are however many farmers closer to 30ppl, those who are more heavily borrowed for example, and those who have housed herds with no access to cheaper forage. So, with a base price of 20.02ppl and Rabobank talking about no recovery until early 2016 at the earliest, the Northern Ireland Dairy Industry is an extremely difficult situation with the viability of many dairy farms genuinely in doubt.

Dairy production costs in the rest of Europe

Whilst NI has been feeling the pain for longer, we are aware that our EU-counterparts are under pressure too.

On a quarterly basis, monitoring of average EU dairy farm margins is carried out by the EU Milk Market Observatory and their analysis clearly illustrates that since the last quarter of 2014, European dairy farmers have, on average, been producing milk at a loss.



Volatility in Dairying

On page one, we mentioning the peaks and troughs associated with dairying and this is illustrated below in Table Six.

Table Six – Indices of average cash income in real terms 2009/10 to 2014/15

	09/10	10/11	11/12	12/13	13/14	14/15
Dairy	67	126	131	88	142	102

Source - DARD Statistical review of Northern Ireland Agriculture 2014

Commission Review of Intervention Reference Threshold

As stated previously, the CMO EP and Council Regulation 1308/2013, under article 7.2 specifically states that the EU Commission shall keep the "reference thresholds" under review, taking account of objective criteria, including production and input costs, and market trends. Based on the UFU's analysis, now is the time that the update process, which the Commission is mandated to undertake, must be actioned.

The UFU does understand that this review and any resulting threshold increases could take some time to implement, but this review is considered to be an essential element in ensuring that we are not in this position in the future due to the impact of increasingly market volatility.

UFU Policy Position

The current "reference thresholds" are inadequate to provide a realistic safety net. The current base price (average of what was paid by local processors was 20.02ppl) and this is only c. 1.2ppl above the threshold shown in Page 1 (at current £/€ exchange rates), meaning we are already very close to Intervention prices.

The UFU wish to make it clear that whilst we fully accept and understand that the intervention system is not intended to provide an alternative to real market forces, however it should provide a genuine safety net. In its very basic form, Intervention Reference Thresholds based on a formulaic production cost mechanism should be introduced to allow farmers to cover a substantial portion of their basic production costs (both fixed and variable).

The UFU accept that the current intervention threshold level should be set below the floor for production costs.