HOW "REAL" IS DEMAND FOR DAIRY PRODUCTS IN EMERGING MARKETS?

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The last few months have been challenging ones for many UK dairy farmers, with cuts to the farm gate price of milk being made and the reasons for this being given not least as a slowdown in international demand from emerging markets in Asia, as well as the impact of the ban imposed by Russia on all agricultural products from the EU 28 and others.

The Fonterra auction price, often seen as a barometer of world prices based on New Zealand's pivotal position in international dairy markets, has fallen by some 45% in recent months. This is largely due to a slowdown in demand from the Chinese market and the rest of the world having excess SMP and WMP as a result of a buoyant 2013 season.

Yet for much of the last 5 years, there has been a general feeling that "this is a good time to be a dairy farmer" - a sentiment shared by other primary producers in other parts of the wider agricultural sector.

This has been based on the growing world population. We have all heard about the need to feed the 9 billion over the next 25/30 years. Allied to strong economic growth in many emerging markets and high commodity prices, this has produced a situation where for many, it generally has been a good time to be farming, although some will almost inevitably still find the going tough.

Problems still arise that are often beyond the control of individual farmers. Argentina, as an example, has had a combination of highly unpredictable weather and inflation rates running at around 25%. The Ebola outbreak in West Africa has caused uncertainty, and the ban on imports in Russia has not helped, of course.

Incidents such as these will happen again, but have all combined to make it a difficult late summer and autumn to date for UK dairy farmers. If ever we needed reminding it's what happens in the likes of China, Chile and

Chad – not just Cheshire, Cornwall and Cumbria that dictates the fortunes of the UK dairy sector, this surely has been it.

Some of the "spring in the step" felt around the UK dairy industry earlier in the year, arising from an encouraging DairyCo Intentions Survey, which saw predicted exits from the dairy farming at a low level and industry confidence at a high point in recent years seems to have ebbed away.

The more pessimistic have been quick to point out "told you so", especially with regards to the demand being experienced around the world and the opportunity it presents for UK dairy farmers and processors.

This was a fundamental plank to the "Leading the Way" document produced as a result of the ambitious plans set out before Christmas by the Defra Dairy Supply Chain Forum of reducing the UK milk deficit. This suggested an increase in UK production of around 4 billion litres over the next 10 years with the UK replacing significant volumes of imports and then making inroads to international markets.

How real then is this demand and what is the scale of the opportunity – if we want to go and grab it? Consider these facts:

- Africa has a population of some 1.1 billion, but this is growing at 2.5% per annum is a net milk importer, with all the major markets running a milk deficit. The sector is characterised by often very small farm size, high levels of wastage in the supply chain and informal distribution to processors. Per capita consumption is low per se, even in the largest import market, Nigeria, at just 8 kg per annum

- Russia is still only 80% self sufficient in dairy products and runs a milk deficit of some 6 million tonnes per annum and still has low overall milk yields of around 3,000 litres per cow per annum

- China is also only 80% self sufficient in milk production and has a consumption level of just 30 kg per annum and has a milk deficit of around 7 million tonnes per annum

- World per capita consumption of dairy products has risen from around 90 kg per annum to over 105 kg in the last 20 years and is predicted to carry on rising to over 125 kg during the next 10 years

- Global GDP is expected to hit 4% in 2015 and dairy demand is anticipated to carry on growing at an average of 2% per annum, the equivalent of an extra 20 million tonnes of milk per annum

Does this look like an industry faced with a lack of opportunity? Not to us. Yet the question of whether we are missing out in the UK on international opportunities is still an area the clients we work with ask about. Some UK farmers and companies have been highly successful in developing exports.

There is invariably talk of Asia as a potential market where UK companies should be exploiting the huge growth being seen in this part of the world. This is true and while favourable consumer demographic changes and relatively high milk prices support the argument, we will need more than "excellent grass" to make an in road into these markets.

A strong understanding of market dynamics is required and excellent business development skills and expertise. Asia is a big place – where are we talking about in particular? China is an obvious target, but there are other opportunities in India, the Pacific Rim and other ASEAN markets too.

To be successful in these markets requires a good deal of hard work. In the UK, we are not the "first cab on the rank" when it comes to doing business in Asia. We have learnt, however, never to say never, and for farmers to take advantage of the opportunities that clearly exist in Asia, they will need to align themselves to those processors who have ambitions in this part of the world and in other emerging markets too.

Competition in Asia is fierce from local suppliers to some extent, but also the established international players in the global dairy markets from NZ, Australia, the US, the Netherlands, Denmark, France, Germany and Ireland. Ireland's future plans for the development of their industry is based firmly on a clear strategy to expand production post quota by as much 50% and export it mainly to emerging markets in Africa, the Middle East and Asia. This has already started to happen.

There is also a danger maybe of getting pre occupied by the emerging markets and some UK farmers and companies will can find export opportunities in Western Europe – still home to around 500 million consumers and still relatively affluent, with well defined supply chains and routes to market. In the domestic UK market, there have never been so many ways of getting dairy food products to consumers and a sense of major players in both the processing and retail sectors looking to get closer to suppliers than ever before in order to ensure security of supply chains.

A number of things are clear:

- World dairy demand still outstrips supply over the mid to long term
- Russia will lift its ban on dairy imports eventually and trade will resume
- China will start buying powder again and is a key driver of global dairy demand
- Africa has the ability to become an increasingly important export market

- Dairy demand in India is still growing rapidly

- Brazil still has a very low average dairy cow yield, and a population of some 200 million looking to buy added value dairy products

- There are a whole range of other markets in Asia, Central America and North Africa & the Middle East all of whom will see imports increase over the next 10 years

- The EU still remains an attractive market

We believe that the fundamentals are still in place for it to be a good time to be dairy farming. Many other countries around the world seem to share this view. The general consensus from the recent International Farm Comparison Network conference in Oslo supports this. Farmers around the world need to be managing their businesses in a way which can withstand shocks to the system that will inevitably arise from time to time. Things will not always be rosy in the garden, but rarely are.

UK farmers and processors need to look beyond the last few months and set course for a brave new world that the likes of the US, New Zealand, Australia and other leading exporters seem to see. Demand is there and needs to be filled. The UK can provide some of these products. If we sit back, however, and let others take the lead, we will miss out. In effect, we will remain confined to operating in our own domestic environment and with no alternatives routes to market in order to produce a more balanced portfolio approach to business development over the next 5 -10 years.

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