

Demand will be key to market recovery

The worst should be behind us. But be braced for a slow recovery and sustained pressure on milk prices, says AHDB Dairy's market analyst Patty Clayton.

TEXT RACHAEL PORTER

Lack of demand – literally a huge overnight drop – due to the COVID-19 pandemic and lockdown has hit farm gate milk prices hard in the UK and across the globe. Some buyers and processors lost between 70% and 80% of their business instantly as lockdown rules closed the food service and catering sectors.

Others have felt little or no impact, particularly those supplying retailers with liquid milk and some types of cheese, and some processors also acted quickly to divert milk into other routes. “So it’s been a mixed bag, in terms of the impact on producers and their milk cheques,” says AHDB Dairy’s dairy analyst Patty Clayton.

“Some felt that instant impact more severely than others. And although prices are still depressed they appear to have stabilised,” she says.

Spring glut

Ms Clayton says that the pandemic hit at a time when milk prices are typically under pressure anyway. “Just as the seasonal spring glut takes effect, so that’s exacerbated the problem. Prices are always a little tight at this time of year and the pandemic then served to take a huge chunk of demand out of the market. This ‘black swan’ event made it a double whammy.

She says that the spot market values for milk and cream are still low, but they’ve climbed through May from the bargain basement levels seen a few weeks ago – milk was selling for just 8ppl in early April. “Stabilisation is the result of two things. The first is an increase in retail demand for dairy – people are consuming more milk, butter and cheese at home due to the lockdown. “They can’t go out to eat or buy coffee, they’re working and schooling from home, and they’re also eating more meals, drinking and snacking at home. So that’s helped with demand.” And the other factor that’s helped to stabilise price is that some milk buyers, for example Muller, have asked producers to cut production by around 3% to mitigate the effect of reduced demand for milk due to the COVID-19 pandemic.

“Other processors have also encouraged producers to reduce milk output by introducing a ‘B’ pricing system. This is, in effect, forcing some producers, indirectly, to cut production as, for many, the ‘B’ price is so low that it makes sense to simply turn off the milk production tap.”

Production peak

As CowManagement went to press, the UK had just passed its annual spring milk production peak, at 37 million litres a week. This is 2% lower than production during the same week in 2019. And AHDB calculations show that April’s milk production was 23 million litres lower than expected. “And this reduction has certainly helped processors to find the capacity to handle and redirect the milk that became surplus to requirements when the food service sector was shut down.”

In terms of farm gate prices, the picture is split. There are producers who have been severely impacted because their buyer was exposed to the

Patty Clayton:

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food service sector shut down. “Few, if any, gave notice of a milk price decrease and many producers were forced to throw milk away – there were some unsavoury practices that went on, to put it mildly.” Calculations, based on information provided by a select group of producers who’ve been hardest hit, show that they lost £7 million in April and £11 million in May.

“And these producers may also be looking at losing a substantial sum during June, July and August if prices don’t recover.

“This isn’t going to resolve itself over night. Lockdown ending won’t simply see demand bounce back to where it was before – it’s not as simple as that.”

The sector may have closed overnight, but opening those restaurants and cafes and other food service outlets will be a long and drawn out process. And their customers may also be hesitant to go back.

“This business and demand will ‘trickle’ back slowly,” says Ms Clayton.

There will also be a time lag – the impact of COVID-19 has yet to really hit some processors and suppliers, and the dairy producers who fulfil their milk contracts.

Wider economy

“And don’t forget that this is also having an impact on the wider economy and could reduce consumers’ income. Milk is an essential for many households, but it doesn’t have the highest margin. So sales of cheese and other higher value dairy produce could be impacted, going forward.”

There may also be a global ‘overhang’ of dairy stocks as the pandemic has had an impact on all dairy markets – most notably on some key export markets for cheese, according to Ms Clayton.

“Cheese exports are an important outlet for UK manufacturers and, outside the EU, the US is one of our bigger customers. And they’ve been hit harder by COVID-19 than we have here in the UK. It’s devastated the country’s economy and with 65% of their cheese going into food service, compared to just 35% in the EU, there’s already a huge stockpile of cheese in the US.

“It will take a while – for some markets more than a year – to come back to previous levels. There will be more hurdles to overcome and there will be a sustained pressure on milk price,” she adds.

“Hopefully we won’t see markets drop to the low levels that we saw in April again, but it’s certainly not going to bounce back up overnight. And much will depend on the outlook for the how quickly demand recovers to support the value of cheese, butter and skim milk powder.” |