

Rural Development Sub-Committee

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The Welsh Dairy Industry

Background

The dairy industry in Wales is an important primary production sector in terms of its impact upon the rural economy and sustainable management of the landscape, and farmers and processors alike are also integral partners with other sectors providing calves for the beef industry and winter grazing for sheep flocks.

The primary production in the Welsh dairy industry can be characterised by:

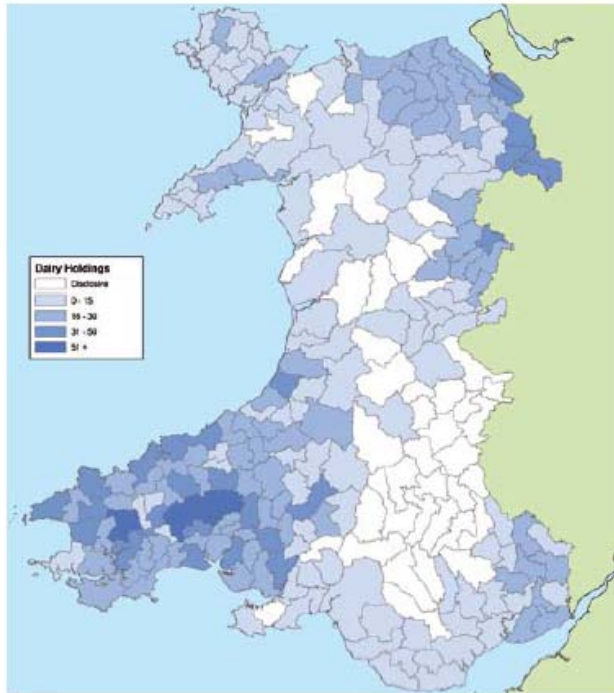
- The capacity to produce grass and conserved forage of the highest quality
- A variety of production methods e.g. seasonal / all year round calving, high/low input systems
- Mixed production units combining milk production with at least one other enterprise
- Production units vary from less than 200,000 litres wholesale quota to over 3,000,000 litres.

The gross output of Welsh milk producers is about £278 million annually, representing around 27% of total Welsh agricultural output. Approximately 75% of the 1.5 billion litres of milk produced is processed in Wales, with 80% of the milk produced used in cheese production (27% in the UK), this demonstrates the high level of dependency amongst Welsh dairy farmers on the manufacture and sales of cheese products.

Current statistics indicate that about 5,000 people are employed in milk production in Wales and 2,300 in dairy processing activities. Dairy exports in Wales amount to just over £31 million and accounts for 4% of UK exports, and accountable for 11% of overall milk production. Current value of imports to Wales is £30 million.

The dairy industry in Wales faces increasing challenges in meeting the needs and requirements of the customer and competing within an ever increasingly global marketplace, the sector faces both short and long term pressures on the farm gate price of milk and difficulty in attracting a skilled labour force.

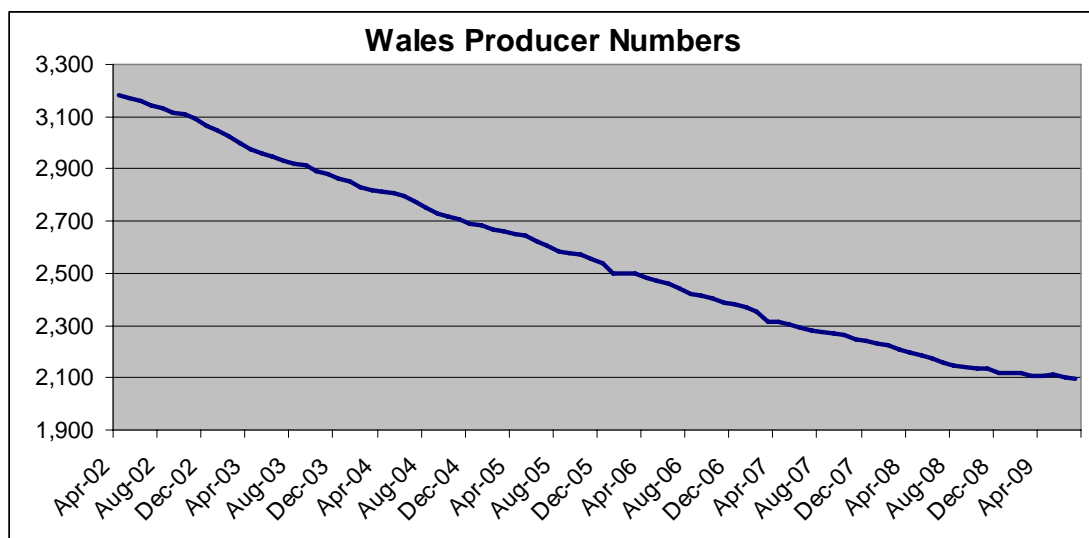
However Wales as a country presents several competitive advantages in the fact that it has a good climate and landscape for dairy production with scope to develop and maximise efficient production.



The map represents the distribution of dairy holdings in Wales by concentration, as can be noted the North East (20%) and South Western (60%) areas are the dominant milk fields in Wales with very little running through the central line of Wales in the upland and hill regions.

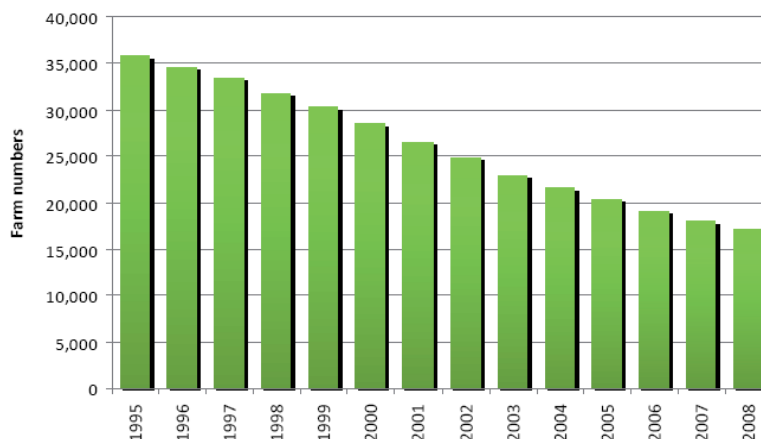
Producer Numbers

The number of producers in Wales has been decreasing for a number of years with trends indicating that the decrease has been at a rate of around 5.6% per year from 3181 in April 2002 to 2,097 in July 2009. However this rate has slowed to 2.9% in the last 12 months, the lowest relative decline of the larger milk regions in the UK. The graphs below gives a good representation of the trends occurring with milk producers over the period April 2002 to July 2009.



On a national level the number of UK dairy farmers has continued to fall year on year, in June 2008, there were 17,060 dairy farms in the UK, a 4.8% decrease too that of 2007. Over the past ten years the number of dairy farmers throughout England and has halved. The numbers of dairy producers within Scotland and Ireland have fallen by 31% and 32% respectively.

UK dairy farm numbers



Source: DHI, DARD, SEERAD

Profitability amongst farmers

Provisional figures released from DEFRA illustrate that average dairy farm business income in Wales increased by 21.6% between the 2007/08 and 2008/09 financial year although these figures include subsidy payments and exclude unpaid labour and rents.

The farm business survey demonstrates a considerable difference between the top third and average performance dairy units across Hill & Upland, and the lowland sectors as demonstrated in the tables below:

Table.1

Hill and Upland Dairy – gross margin (£ per cow)

Year	2005/06	2006/07	2007/08
Top third (£)	835	767	1007
All farms (£)	660	623	767

Table.2

Lowland Dairy Farms – gross margin (£ per cow)

Year	2005/06	2006/07	2007/08
Top third (£)	915	876	1058
All farms (£)	683	627	778

(Farm Business Survey, 2006-08)

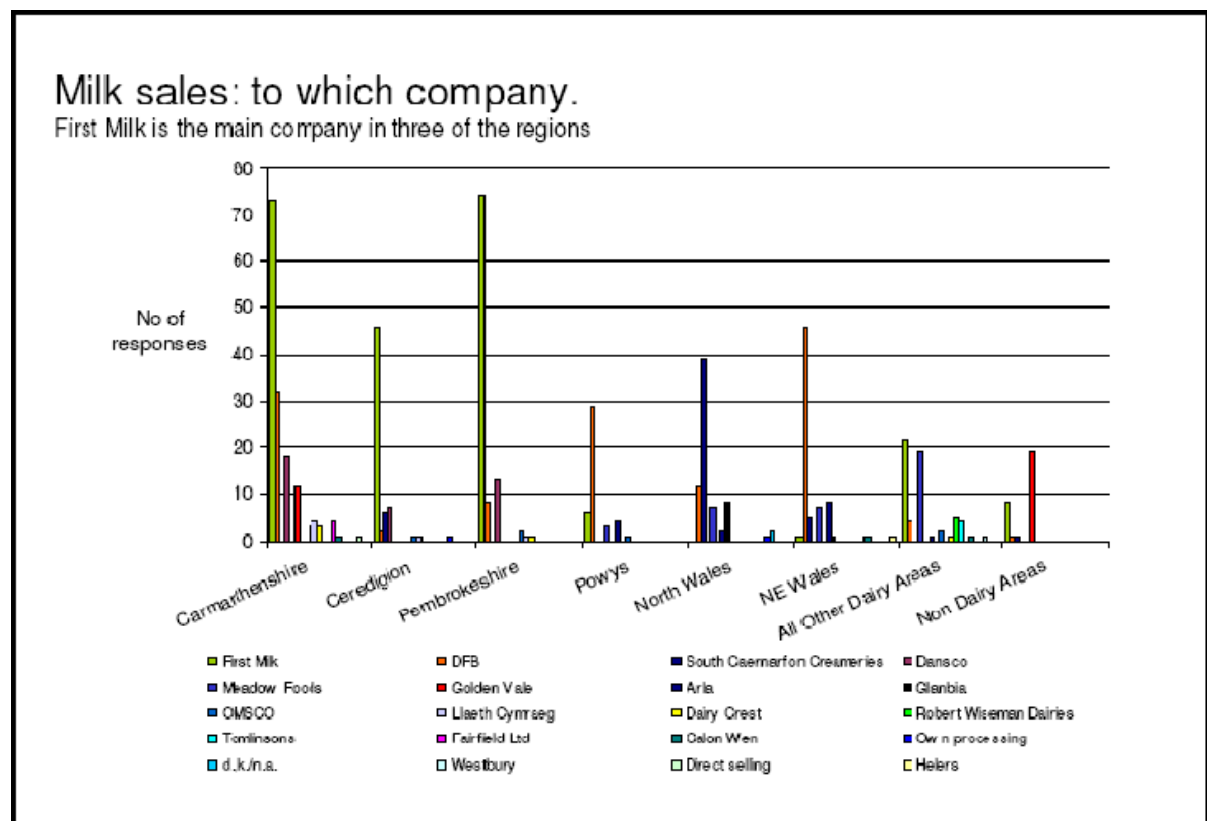
Differences of up to 30% can be found in the performance based on gross margins of hill and upland dairy farms between the top third and all farms, and up to 40% differential can be found in the lowland dairy gross margins.

Coleg Sir Gâr – Gelli Aur has been investigating and demonstrating different systems of milk production since 1999 and we have shown that the cost of production is clearly linked to the production system adopted. The choice of

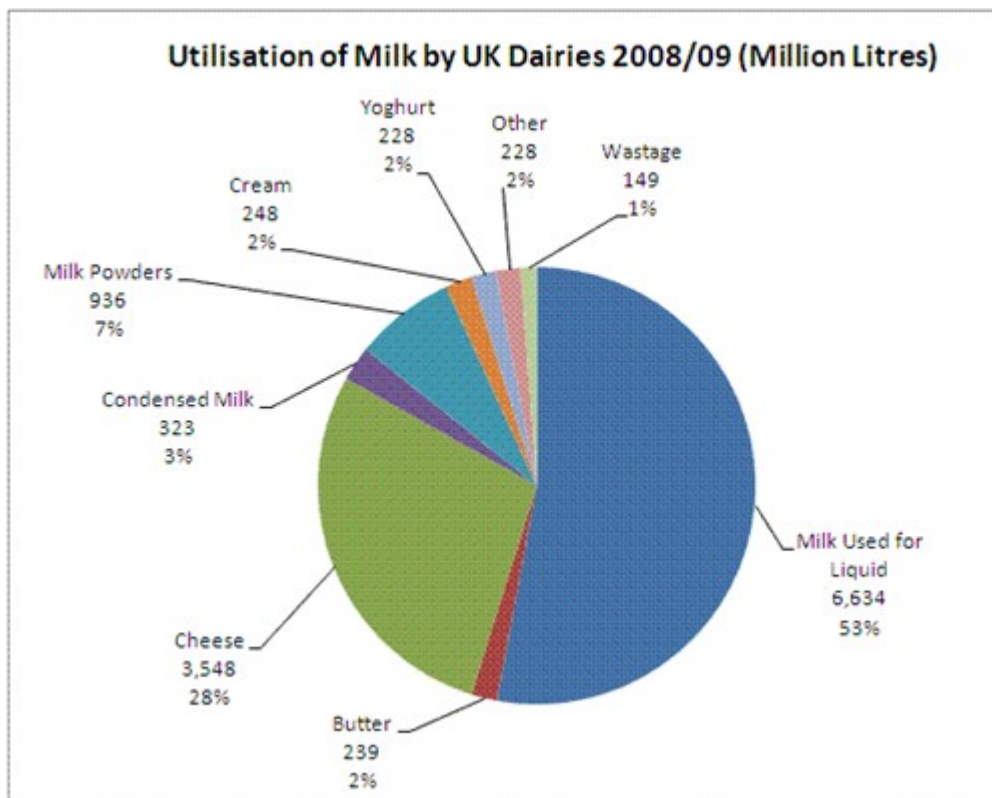
production system on many farms is influenced by numerous factors from farm layout, topography and soil type through to individual farmer preference, the nature of the supplier contract and the underlying farm business structure. However it is clear that some systems are, at face value, more financially sustainable at a lower milk price than others and there continues to be opportunity to improve efficiency of production on some farms. While some Welsh producers should consider adopting these low cost, high forage systems and indeed some countries (Ireland & New Zealand) have built their entire dairy sectors around a low cost production system it is unlikely that this would be either a practical or desirable solution for Wales.

Milk Buyers

The graph below demonstrates the milk buyers in each region and their market share. Up until recently the dominant milk buyers within Wales were the larger farmer owned co-operatives First Milk and Dairy Farmers of Britain (DFB) who together processed over 60% of the total milk produced. However, DFB went into receivership in June this year and of the 281 farmers affected by the collapse the majority have been taken on by the remaining two UK co-operatives while the remaining producers have either signed delivery contracts to other companies or retired from production. It should also be noted that the combination of smaller milk purchasers also have an important influence on the buyers market in Wales.

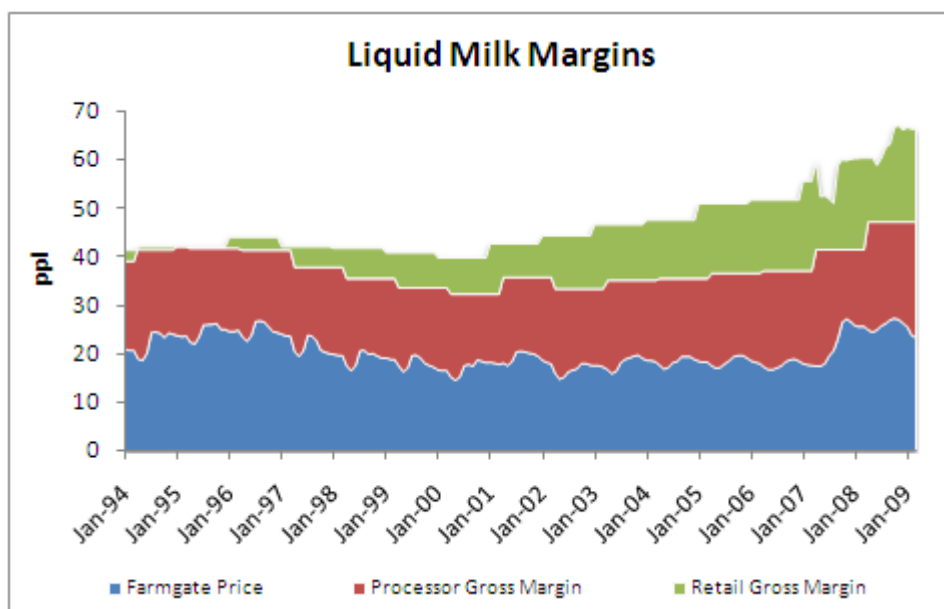


Source: WDA Dairy Strategy – Key Results. 2006.



Contrary to the UK pattern shown above, 80% of Welsh milk is processed into cheese of which, despite the developments in brand development undertaken by the co-operatives, the majority enters the commodity market. Furthermore the majority of the remaining milk enters the liquid market but again despite some positive brand relationships established by the co-operatives, their processing partners and some retailers the majority enters the commodity liquid market. As a result Welsh producers are particularly exposed to commodity trends and are not yet gaining significant benefits from the added value brands other than through the “pooling” effect associated with working through co-operatives. Unfortunately the benefits of branded sales through the co-operatives continue to somewhat diluted by the volume of commodity trading.

Dairy Co. have estimated (illustrated below) the processor gross margins of liquid milk and cheddar cheese based on the difference between the wholesale price (as estimated by Dairy Co Datum) and the DEFRA farmgate price. Analysis of the data suggests that while the farm gate prices have remained relatively constant the gross margins obtained by the processors and retailers has increased over the period analysed (94-09).



Future Interventions

It has to be recognised that the dairy sector will continue to be influenced by Global and EU markets and therefore the impact of local interventions will always be moderated by the overall economic and market environment.

However even within this context the WAG can play a significant role in delivering the mission statement – “A sustainable, profitable, efficient and innovative Welsh Dairy Sector which benefits the people of Wales” as framed by the Strategic Action Plan for the Dairy Industry in Wales. While the Action Plan is still very relevant and identifies many of the issues to be addressed the experience of the last 12 to 18 months would suggest that the priorities for the sector should be:

1. Continued interventions to assist producers to improve production and financial efficiency.
2. Targeted assistance to enable the sector to further develop its product range so that there is less dependence on and vulnerability to the commodity markets.
3. Facilitating the development of a more positive relationship across the sector enabling primary producer to get a more equitable share of the market value of the finished product.