

A structural change is underway in global dairy markets. A perfect storm has emerged through a coincidence of events, technology, and policy changes across the major dairy producing nations, including Australia, which will result in a long term significant reset of dairy economics across the globe.

Cooperatives Murray Goulburn and Fonterra have both dramatically reduced the prices they offer dairy farmers for milk, [sparking a backlash from farmers](#), who say they will be pushed into the red and out of dairy.

It is only due to the strength of the two cooperatives in absorbing the costs of high milk prices in a changing market that these reductions did not occur earlier. The cooperatives have shown an inadequate understanding of global dairy economics by over-paying farmers and by seeking to [claw back over-paid advances](#).

The low prices have been blamed on a short-term [oversupply coinciding with a reduction in demand](#) from China and Russia. Some of this demand is now being met by Chinese investment in both Australia and New Zealand which also contributes to the changes underway. But the debate thus far has focused on problems with demand while ignoring the bigger issue of increasing global over-supply.

The preoccupation with the belief that global demand will solve emerging on-farm production cost difficulties and that a [“substantial improvement in prices was still expected by mid-2016”](#); was naïve and failed to recognise how quickly, and irreversibly global dairy supply can change.

Since the mid-2000s a strong increase in demand for milk products across Asia, largely on the back of rising middle-income wealth led to the complete depletion of surplus dairy stocks in the European Union and the US. This change to the supply-demand equilibrium resulted in a temporary sea-change in dairy markets because growth in [demand simply outpaced growth](#) in supply by between 50% and 100% in some markets on an annual basis.

To a large extent this imbalance had been driven by regulation of the global supply market in which only a few export nations competed – Australia and New Zealand included. It resulted in higher than historical average dairy prices in global markets, but considerably more short-term volatility due to global GDP shocks and [short-term supply-demand imbalances](#) .

Regrettably a critical assumption that appears to have emerged among producers during this period, as evidenced by continued investment and expansion, was that the real price for global dairy commodities was increasing, a trend they expected to continue in the long term.

The current dairy price scenario, which would historically have been short-lived, is in fact masking underlying structural changes to supply-side dynamics that are now underway. Only approximately [7% of globally produced milk is traded](#) (65 billion milk-equivalent litres). Therefore, a small change in supply globally has a profound effect on the global dairy market equilibrium.

The EU is the world's largest milk producer, [with approximately 160 billion litres produced annually](#) . The [removal of milk production quotas](#) in March 2015 presented an opportunity for dairy expansion and, even more importantly, one that is no longer confined to the traditional dairy exporters of Ireland, France, Belgium, and the Netherlands.

Under quota, [EU exports doubled](#) between 2000 and 2013 to 9.5 billion litres and are anticipated to increase again this coming season. Quota removal has freed dairy farmers in central and Eastern Europe to increase in scale considerably, availing themselves of technologies denied during the Cold War years. Coupled with the removal of regulations concerning the transportation of liquid milk across borders, producers and processors now find themselves with opportunities for growth not experienced since the second world war.

Political policies in the world's third largest dairy producer, the USA, are also likely to influence global dairy supply in the future. Current dairy production is being stimulated by low feed prices, which were [driven by record yield seasons](#) in 2013 and 2014, similar levels in 2015 and new [projected highs](#) this year.

Milk price cuts reflect the reality of sweeping changes in global dairy market

Written by The Conversation USA

Eighty percent of US dairy farm costs are feed. The reduction in feed costs from US\$29.26 per 100kg milk in August 2012 to US\$18.04 per 100 kg milk in June 2015 has greatly increased the value of marginal production.

The advent of large-scale fracking, which has resulted in a significant reduction in the price of oil, will likely maintain lower corn prices, at least in the short-term. This comes as the reduced value of biofuels re-focus the use of corn back to a feedstuffs for farmed livestock. The net result is that 75% of every new tonne of production across the USA is expected to be sold on the global surplus market.

Farmers have fought for free trade and open access for decades on both sides of the Tasman. Now that it is emerging, profitable returns will be caught first by the lowest cost global producer.

We are fools to think that that will be either Australia or New Zealand. Therefore, possibly with the exception of the US market, a downward reset is in store for global dairy prices.

The authors do not work for, consult, own shares in or receive funding from any company or organization that would benefit from this article, and has disclosed no relevant affiliations beyond the academic appointment above.

Read more <http://theconversation.com/milk-price-cuts-reflect-the-reality-of-sweeping-changes-in-global-dairy-market-59251>