



ECOVAL DAIRY TRADE

USDA Outlook Forum

Marketing Dairy Products During Price
Volatility

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Introduction

- Ecoval Dairy Trade is a global dairy trading company, with offices in Europe, North and South America and Australia
- Global strength through local presence has been the motto of Ecoval Dairy Trade since its foundation
- Our history goes back as far as 85 years, which makes us one of the very first dairy trading companies in the world – in the USA, formerly known as M.E. Franks, Inc., founded in 1948



Ecoval – key facts

- Volume: \pm 400.000 mt
- Turnover: \pm € 500 mio
- Staff: 80 (of which 25 traders)
- Core business: trade - logistics - financing
- Sales into more than 100 countries worldwide
- ISO 22000 certified



Products

- Milk powders:
 - Skimmed milk powder
 - Semi-skimmed milk powder
 - Full cream milk powder
 - Cream powder
 - Buttermilk powder
- Whey powders:
 - Whey powder
 - Whey permeate powder
 - Demineralised whey powder
 - Delactosed whey powder
 - Whey protein concentrates
 - Whey protein isolates
 - Lactose
- Milk proteins:
 - Casein (acid / rennet)
 - Caseinates
 - Milk protein concentrate
- Butter fat:
 - Butter
 - AMF
- Cheese:
 - Gouda
 - Edam
 - Cheddar
 - Mozzarella
 - Emmental
 - Cheese for processing



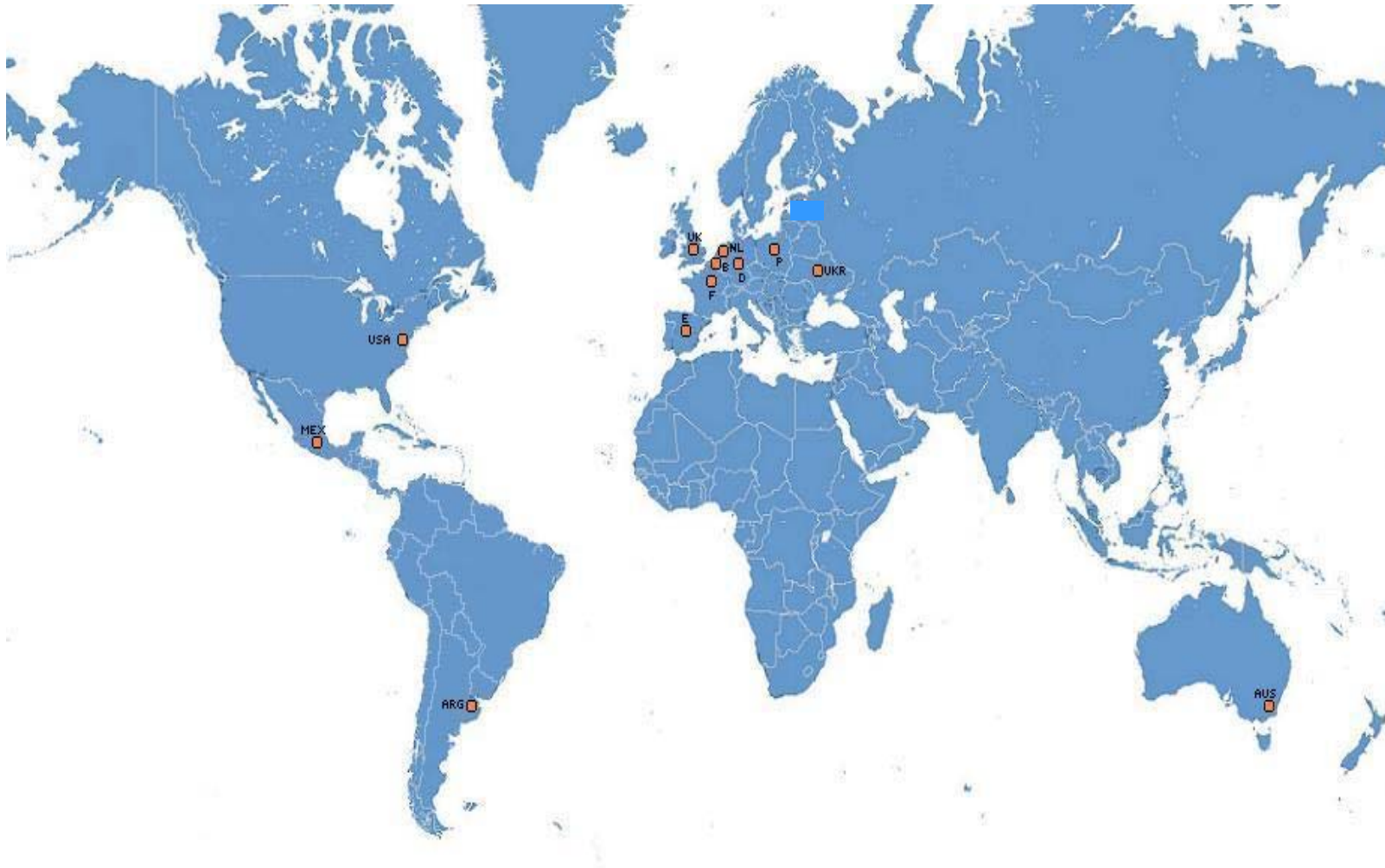
Market segments

- Infant nutrition
- Sports & dietetic nutrition
- Ice cream & dairy
- Chocolate
- Bakery & bread improvers
- Meat & sauces
- Cheese
- Animal Nutrition





Locations of Ecoval Dairy Trade





Dairy Product Buyers in the World Market

- Dairy Product Buyers - Distinct Segments
 - Multinational Companies – Nestle SA, Wyeth, Unilever, etc employ professional approach to ingredient purchasing. Diversity of origin, typically quarterly priced contracts, rigid specifications.
 - State Trading Organizations – fewer in number today, but still significant in certain markets. Mexico, Algeria.
 - Large national companies – Indomilk in Indonesia, Vinamilk in Vietnam
 - Small importers and distributors – Egypt, Philippines, Mexico. Provide service to small cheese plants, dairies, ice cream manufacturers, animal feed producers, etc.



Ability to cope with price increases

- When ingredient costs start to increase, large multinational companies with retail brands have flexibility to manage full chain
- State Trading Organizations – typically subsidize internal distribution. Frequently face budget limits.
- National Corporations – similar to multinational corporations, but less flexibility
- Small importers and distributors – follow four stages – denial, panic, fear and pain



Small Importer and Distributor Market Phases

- Denial – especially when leaving a period of prolonged low prices, this group typically rejects offers with increased prices
- Panic – after realizing that plants/customers will be without product, small importers and distributors start to accept any offer. Prices will never fall again.
- Fear – at some point, small importers and distributors realize that purchasing at such an elevated level will never make a profit in their own market. They stop buying
- Pain – contracts made in panic mode continue to arrive. Smarter competitors buy at ever lower prices. Inventories hurt.



Behavior of Market Participants

- A contract is frequently not a contract
 - Limited capital of Small Importers/Distributors – no buffer
 - A competitor with lower cost is significant problem
 - In last two years, 20% or 30% price change in a month is common
- Sometimes suppliers are part of the problem
 - Some suppliers accept position of Small Importer/Distributor
 - When offering new prices in falling market, these suppliers will adjust existing contracts
 - In extreme situations – even adjust prices on shipments
 - Suppliers who do not “follow” left at significant disadvantage



Behavior of Market Participants

- Why are contracts not rigidly enforced?
 - Structure of production market and price discovery mechanism in certain production areas.
 - World wide adoption of specifications – ADPI Extra Grade for most dry powders
 - But, no widely accepted trading rules or standard contract for dairy products
 - No NAGEA II contract or Vegetable Oil trading rules, for example
 - Expense of legal contract enforcement in many countries

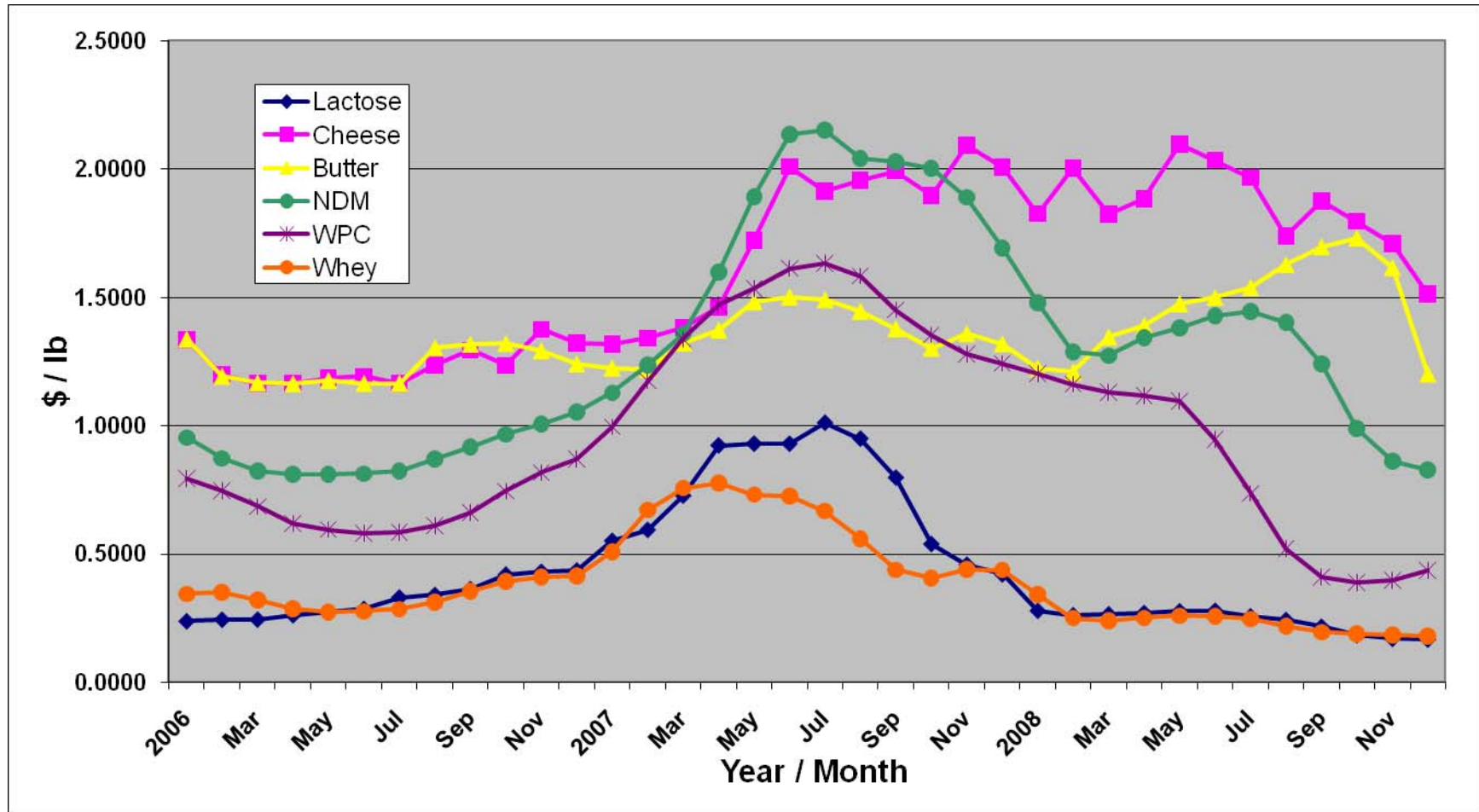


Payment Terms & Market Volatility

- No matter what terms, volatility creates stress. Even the best of customers can back out of contracts.
- The purchase and movement of goods to an export position creates risk exposure
 - Letter of credit – delayed opening, short windows to perform, buyer advantage if errors on documents
 - Cash in Advance – arrives late, if at all
 - Credit Insurance – widely adopted in recent years. But, subject to quality claims
 - Open account – good luck.

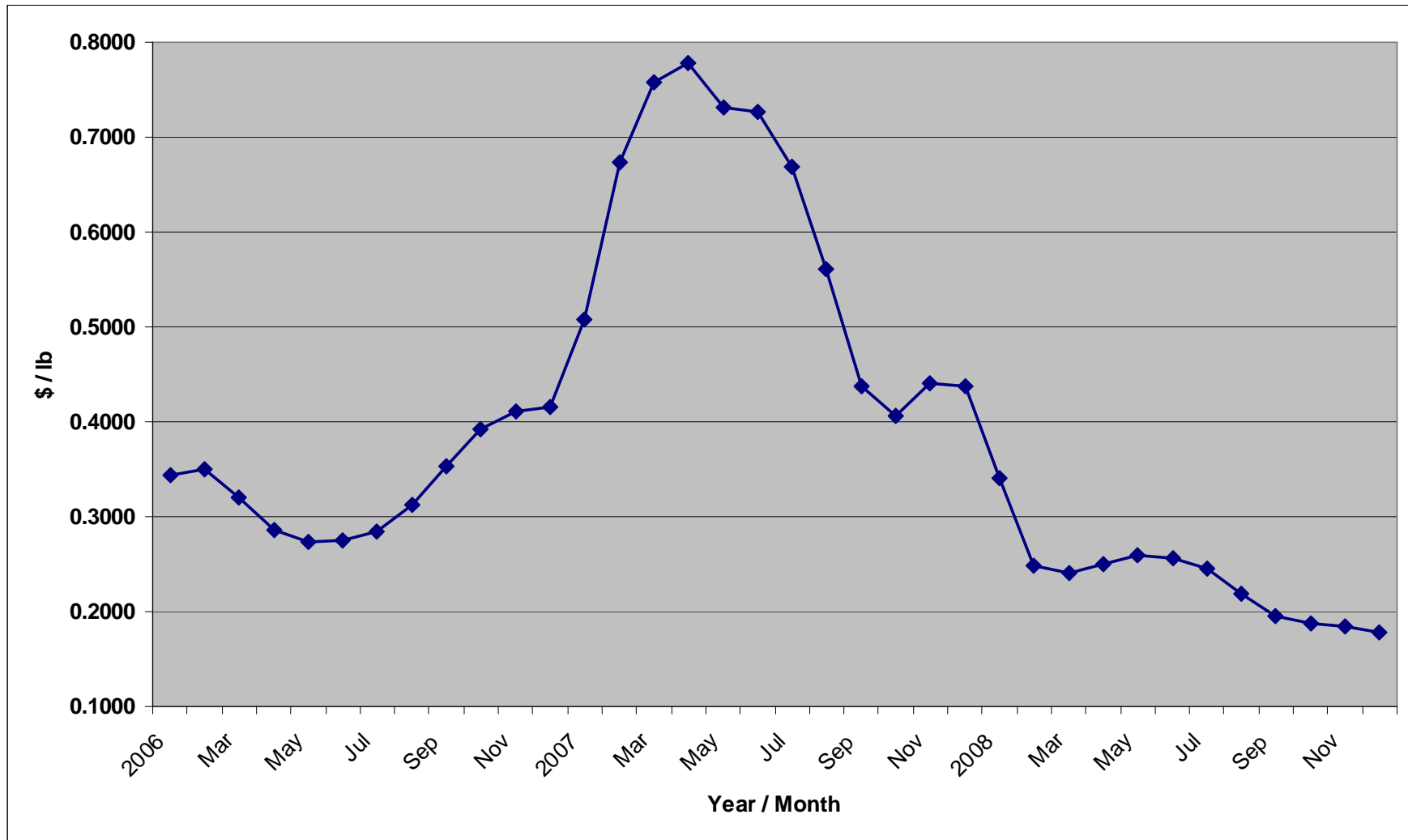


USA Market Price Summary





Central Mostly Whey Price 2006-2008



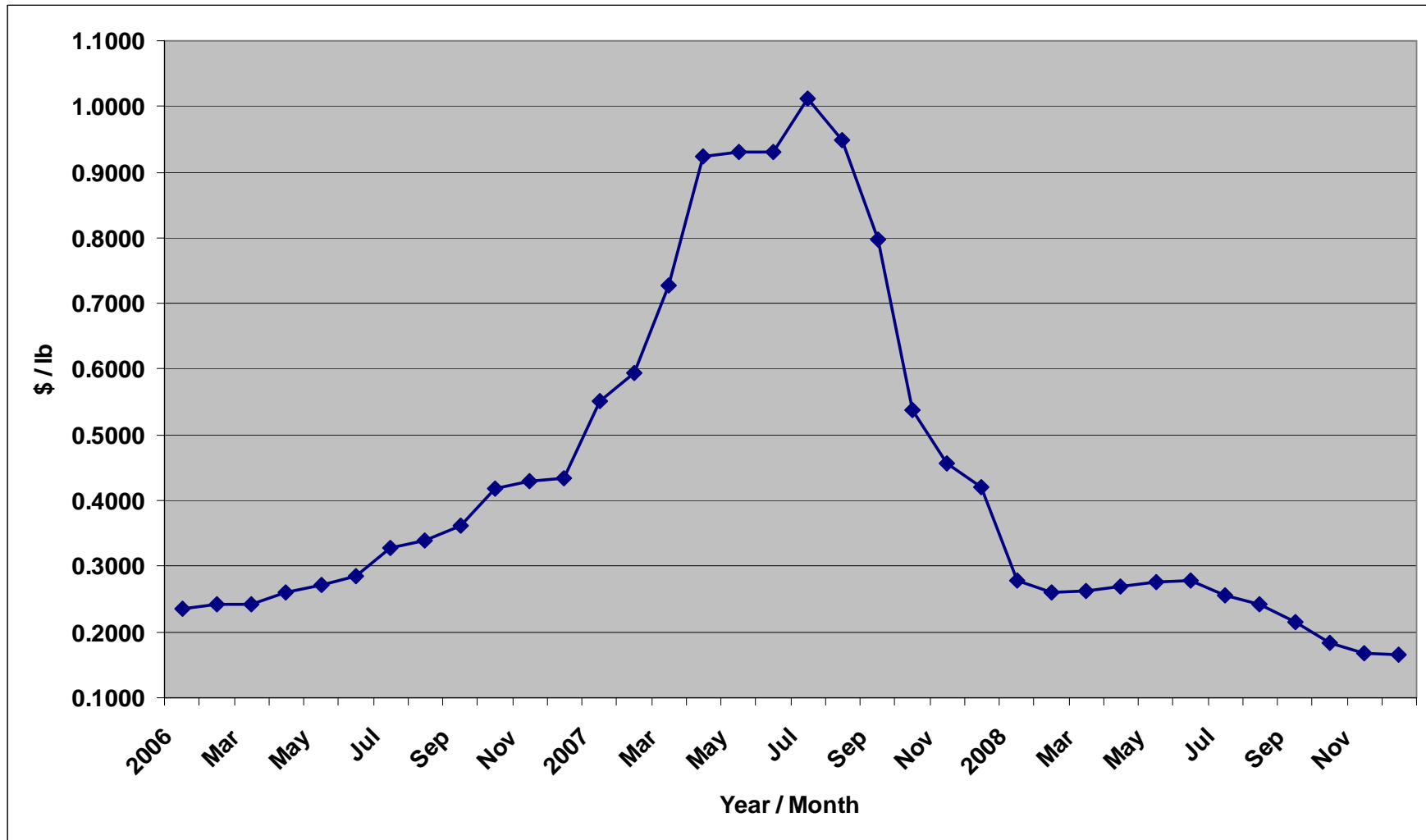


Whey Price Volatility

- 8 year mean price of 28.2 cents per pound
- Range from 13.6 cents to 82.3 cents per pound
- Standard Deviation – 14.6 cents
- 2007 price peak was 3.7 SD's above mean
- Since April 2007 – CME futures contract
 - Open interest is 1200 contracts (52.9 million pounds)
 - Monthly production is an average of 90-95 million pounds
 - To be an effective tool, market needs significantly higher open interest.
 - Most producers sell relative to AMS AOM, CME closes to NASS



Central & Western Lactose Mostly Price 2006-2008



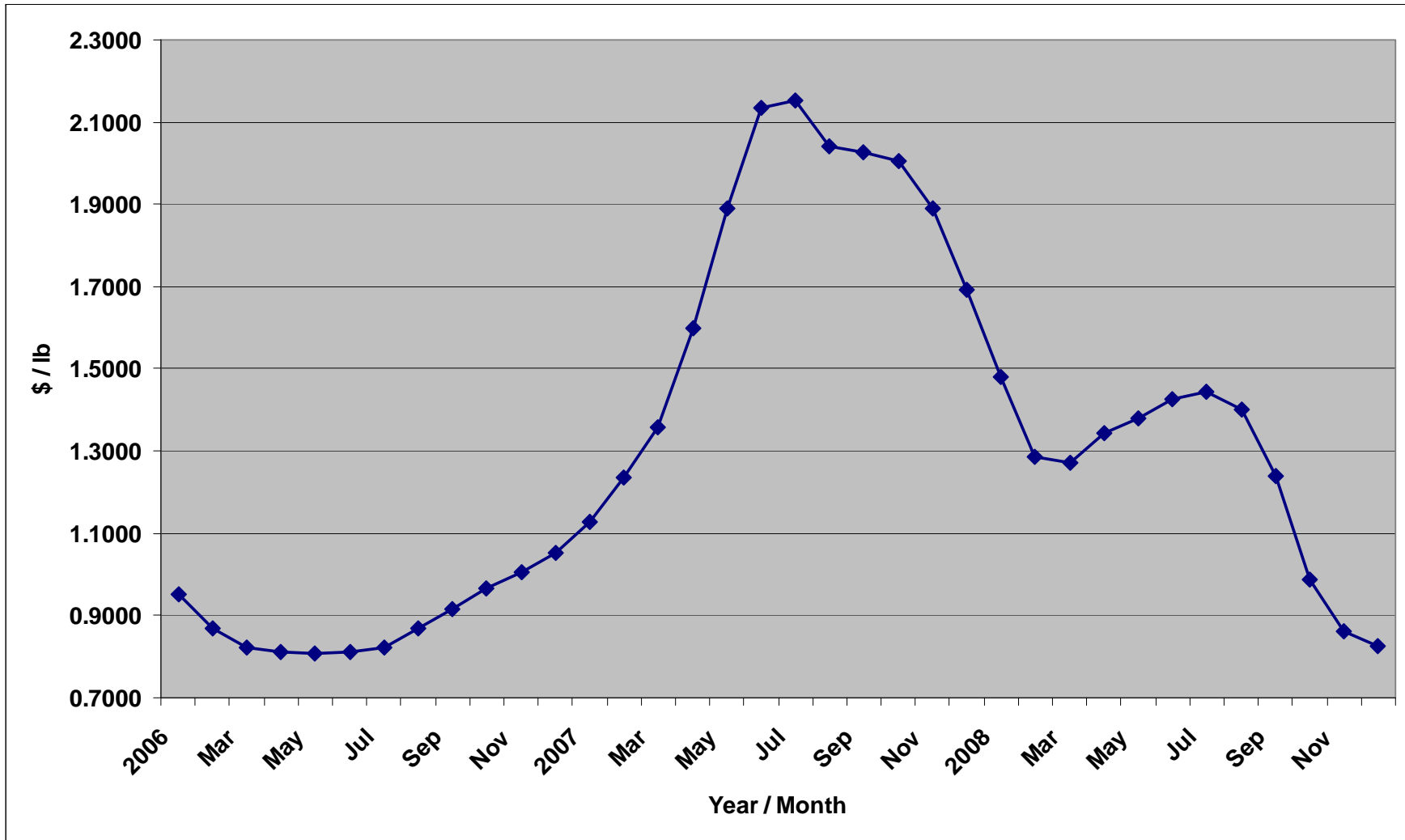


Lactose Price Volatility

- 8 year mean price of 27.7 cents per pound
- Range from 15.8 cents to 100.1 cents per pound
- Standard Deviation – 19.6 cents
- 2007 price peak was 3.7 SD's above mean
- Fixed quarterly pricing is common
- No CME futures contract
 - But, sometimes strong correlation to whey prices
 - Open interest on CME whey contract is limiting



Western Mostly Nonfat Dry Milk Price 2006-2008



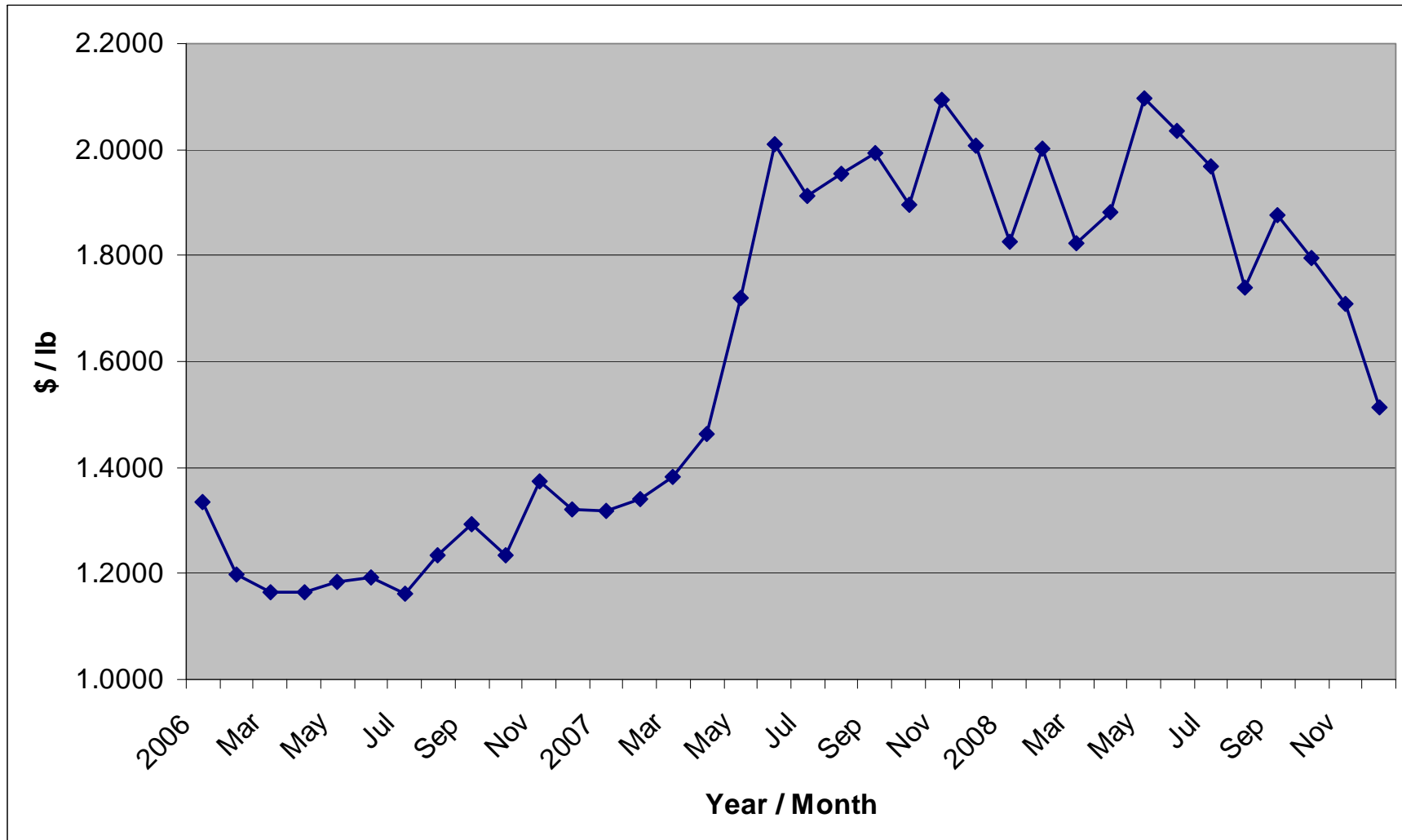


Nonfat Price Volatility

- 8 year mean price of 101.6 cents per pound
- Range from 80.1 cents to 215.3 cents per pound
- Standard Deviation – 31.7 cents
- 2007 price peak was 3.6 SD's above mean
- NASS Contracts common + AMS AOM pricing
- CME futures contract
 - Open interest is 1000 contracts (44 million pounds)
 - Monthly production is an average of 150 million pounds
 - To be an effective tool, market needs significantly higher open interest.



CME Block Cheese 2006-2008



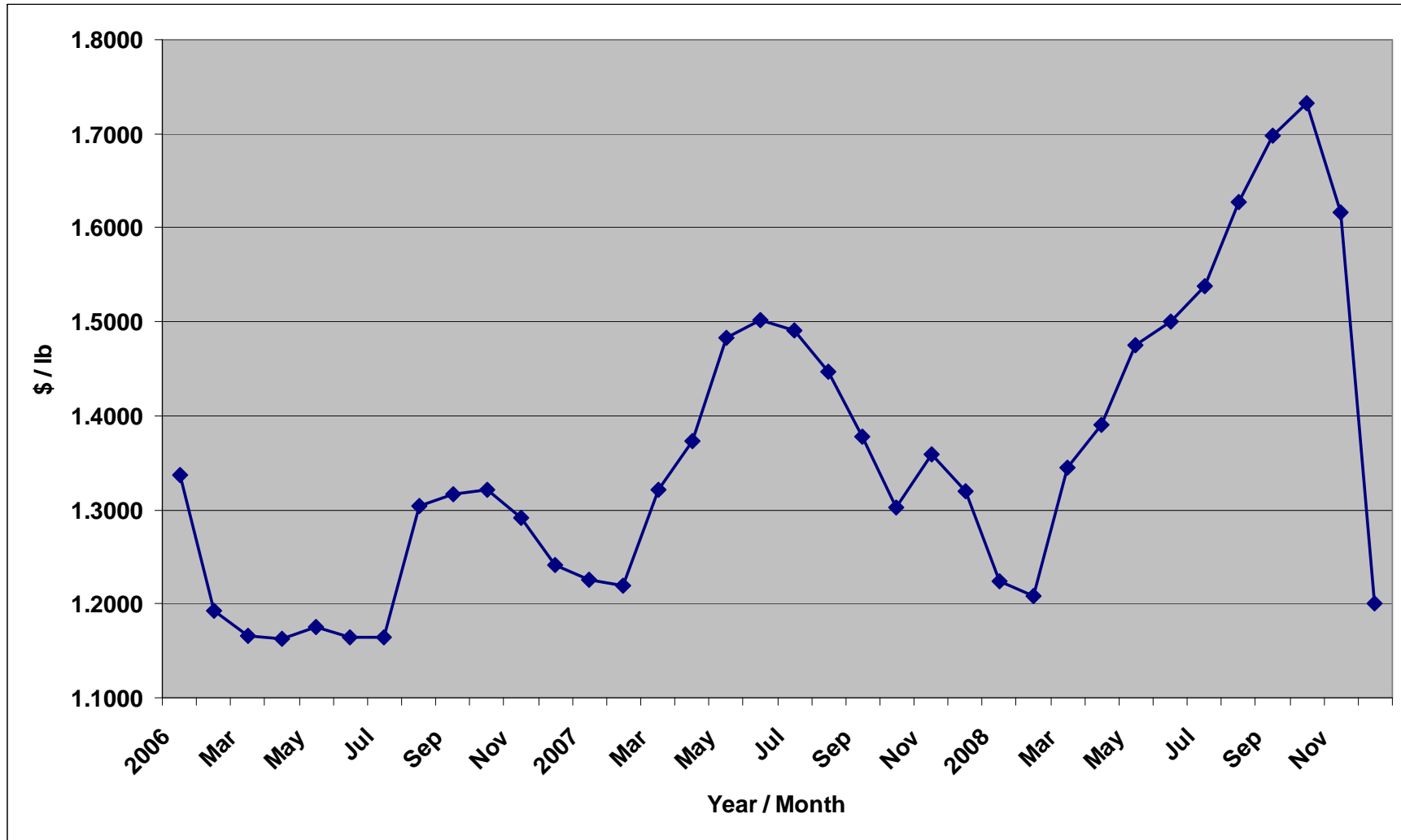


Cheese Price Volatility

- 8 year mean price of 140.3 cents per pound
- Range from 104 cents to 217 cents per pound
- Standard Deviation – 27.2 cents
- 2007 price peak was 2.8 SD's above mean
- Pricing typically formula against CME cash block price
- CME Class III futures contract
 - Open interest is 40,000 contracts = 800 million pounds of cheese and about 430 million pounds of whey
 - Monthly production is an average of 825 million pounds
 - Good liquidity for this contract



CME Grade AA Butter 2006-2008



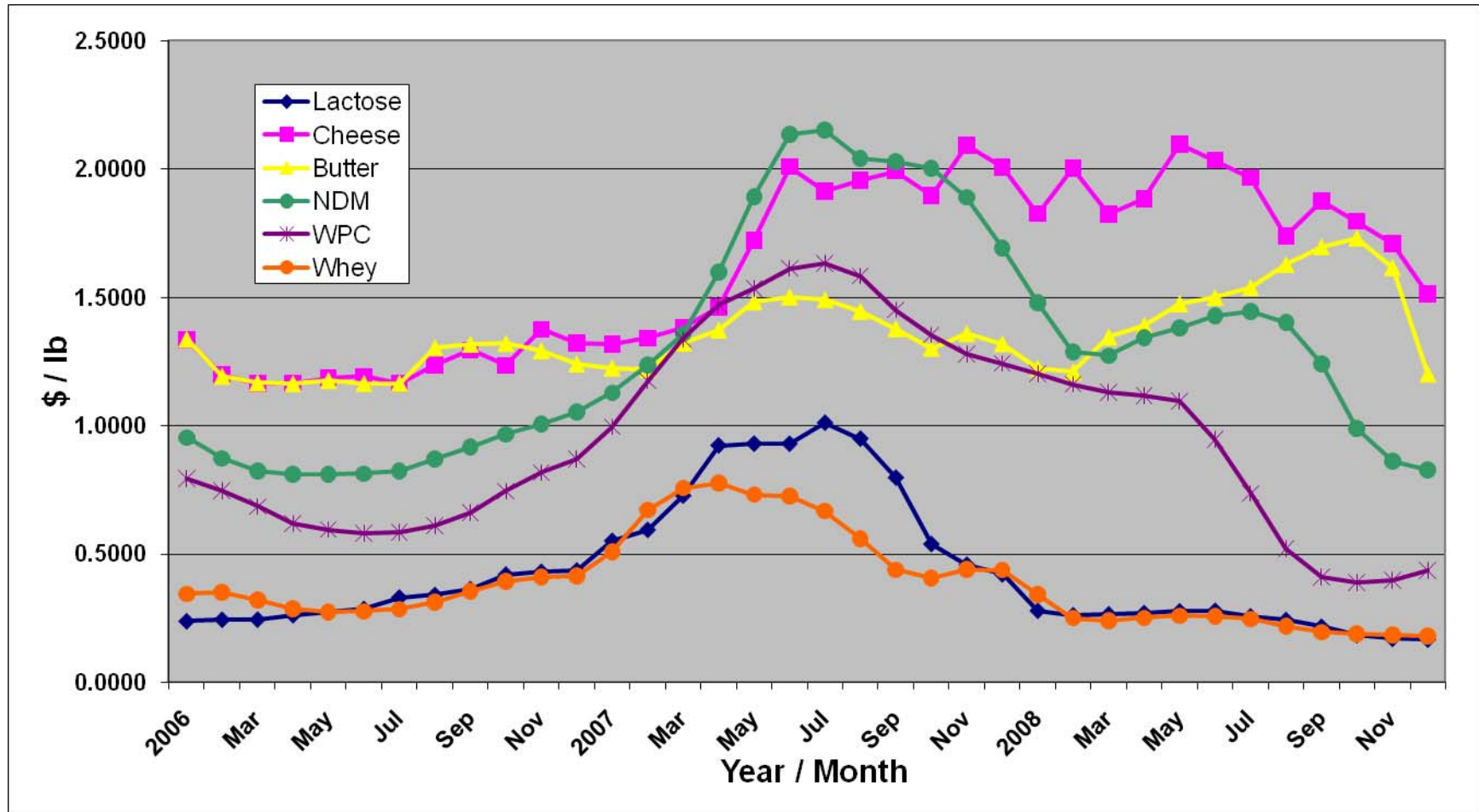


Butter Price Volatility

- 8 year mean price of 138.3 cents per pound
- Range from 91 cents to 222 cents per pound
- Standard Deviation – 30.1 cents
- 2004 price peak was 2.8 SD's above mean
- 2008 price peak was 1.15 SD's above mean
- Pricing typically CME cash price – weekly average
- CME futures contract
 - Open interest is 4500 contracts (90 million pounds)
 - Monthly production is an average of 140 million pounds



USA Market Price Summary





2009 Outlook

- Exports in 2008 were 11% of total milk solids
- NDM exports up sharply with significant volume
- Cheese exports up
- Butter exports up
- Whey derivative exports generally down in 2008



2009 Outlook - NDM

- Export success will be difficult to repeat in 2009
- For NDM – USA at or near CCC support price.
- EU has just re-started export subsidies.
- DEIP has limited tonnage – 68,000 tons (2x in 2009?)
- Australia – New Zealand can price below USA as necessary
- World demand has yet to recover with lower prices in market. In Mexico, exchange rate has more than offset price reduction.



2009 Outlook – Butter

- World Prices are below USA support prices.
- Exports will need DEIP or CWT
- Additional internal pressure from imports – license + blends
- Bottom line – minimal exports in 2009



2009 Outlook - Cheese

- Situation similar to butter
- World prices are below USA support price
- World demand is sluggish
- Bottom line – sharply lower exports of cheese in 2009



2009 Outlook – Whey + Derivatives

- USA pricing for whey, WPC and lactose almost always competitive in world market
- Otherwise, domestic stocks increase, leading to lower prices
- In 2008, export shipments for whey, lactose and WPC all declined, reflecting weak demand
- For 2009, lower prices should support small increases in volume



2009 Outlook

- Exports will be near 5% of total milk solids in 2009
- With a 1% increase in milk production, surplus in internal market is 5% to 6% of milk production.
- Allow for recovery in domestic demand of 2%, still leaves a surplus of 3% to 4%
- How will producers respond? – fewer cows, lower milk production, but how fast can the adjustment take place?
- When will world demand recover? 2010 could see demand increasing at time when production base has contracted – start of next upward price cycle.