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Report Highlights:

After a record jump of milk production in 2014, the increase of output is expected to decline in 2015 due to slower export demand, decrease of world market prices and high level of commercial stocks of dairy commodities. On March 31, 2015, European milk quota system was terminated. In expectation of price volatility the European Commission introduced in September 2014 and extended till September 2015 a temporary Private Storage Aid program for butter and Non Fat Dried Milk. Although the Russian ban on imports of dairy products affected EU exports in 2014, the actual effect was smaller than originally expected.

Executive Summary:

Production:

In 2015 EU-28 milk production is expected to increase by over one percent as a result of higher inventories of dairy cows, adequate supplies of feed, and termination of the milk quota system. After a record 4.6 percent increase of milk deliveries in 2014 resulting from high prices of dairy products on the world market caused by strong import demand from China and North Africa, the pace of increase of milk deliveries in 2015 is expected to slow down. Reduced imports from China, continuation of Russian ban on imports of dairy products and fluctuations of world market prices are major reasons for slower increase of milk deliveries in 2015. However, increased dairy cow inventories and high ratio of heifers ready to enter production cycle in the EU28 dairy cattle herd indicates a potential for further growth of milk deliveries later in the year and into 2016.

Very attractive milk procurement prices in the first three quarters of 2014, resulting mainly from strong export demand, boosted milk deliveries in 2014 and first quarter of 2015. The lag between market situation signals and reaction of farmers taking production decisions resulted in high milk and dairy products output towards the end of 2014 and into 2015. Some farmers from several member states will have to pay fines for exceeding the quota in 2014/2015 quota year (QY). In response to protests of farmers demanding cancelation of fines in the last quota year, the EU Commission allowed member states to pay the fines in three annual installments.

The pace of the increase of milk deliveries in 2014 exceeded the estimate presented in the annual report published on October 15, 2014 and there was a need for an upward correction of the milk production and output of dairy products estimate.

Strong demand for milk powder on the world dairy market in 2014 increased the share of Non Fat Dry Milk (NFDM) and Whole Dry Milk (WDM) in dairy processing in the EU28. The increase in milk production in 2014 was directed mostly towards NFDM, WDM, and butter production, which were in demand on the international market, as well as the higher production of cheese. However, the Russian import ban on European dairy products adversely affected the increase in cheese production because of reduced export demand.

Consumption

In 2014, higher production of milk resulted in increased domestic consumption of dairy products, however, the smallest increase was observed in consumption of fresh dairy products. The higher availability of dairy products was directed mainly to export and the remaining part was consumed domestically or used to rebuild commercial and private storage aid (PSA) stocks. It is expected that, due to increases of milk deliveries in 2015, consumption of cheese, butter, NFDM and WDM will also grow. Please note that higher consumption figures in the PSD tables also include increase of commercial stocks.

Trade

In response to spiraling import demand from Algeria, China, and Egypt, 2014 exports of NFDM increased by almost 60 percent. Although 2014 exports of fluid milk, butter, and WDM increased by 33, 17, and 4 percent, respectively, their growth of trade in comparison to 2013 has not been as

spectacular as for NFD. Decrease of world market prices for cheese and introduction of a ban on imports of dairy products by Russia on August 7, 2014, reduced EU28 exports of cheese in 2014. During the first two months of 2015, exports of cheese were 8 percent lower in comparison to the same period of 2014. Exports of cheese are expected to recover in the second half of 2015 due to increased sales to the United States, Japan, and South Korea as well as potential discontinuation of the Russian ban in August 2015. Exports of butter may continue in 2015 because of competitive prices on the world market and stocks built in 2014. Most of the increase of NFD production in 2015 is expected to be directed for exports. In the first two months of 2015 exports of WDM decreased by almost 10 percent mainly because of lower exports to Algeria and Nigeria.

Termination of milk Quota System

As of March 31, 2015, the EU system of milk quota was terminated. Predictions of impact of quota termination on milk deliveries in the EU28 estimated the potential increase of production to be up 5-6 percent in the first year of the post quota period. High procurement prices of milk in 2014/2015 QY and strong demand for export of dairy production stimulated production to the level which almost fulfilled predictions of higher milk deliveries after the end of the quota. As a result, post quota increase of milk deliveries in 2015 CY is expected to return to the pattern of a one percent increase per year. It is expected that the post quota downward adjustment of milk procurement prices and increase of commercial stocks of dairy commodities, which already happened in several member states, will help to stabilize the market and soften price volatility within the EU. The decrease of prices for dairy products in the EU28 observed in the first quarter of 2015 accompanied by a weakening of the Euro may have a positive impact on the competitiveness of the EU28 exports on the world market in 2015 and into 2016.

Impact of Russian Ban

The introduction of a Russian ban on August 7, 2014, adversely affected EU28 exports of cheese in 2014. In 2014, EU28 exports of cheese to Russia dropped by 48 percent in comparison to 2013. The Netherlands, Germany, Finland, France, Lithuania, and Poland were mostly affected by the ban. However, exporters adjusted to the situation by increasing sales to other markets like the United States, Switzerland, and South Korea. In 2014, EU28 exports of butter were not affected by the Russian ban because of increased exports to Saudi Arabia, United States, and Egypt. In the first two months of 2015 exports of butter were 7 percent higher than a year ago.

Market Intervention:

Within the new Common Agricultural Policy 2014-2020, the opening of the Private Storage Aid (PSA) requires the European Commission's (EC) decision, which depends on the current market situation. The introduction of the Russian ban on agricultural products forced the European Commission to open the PSA scheme for butter and skim milk powder and open a temporary exceptional private storage aid scheme for cheeses falling under CN codes 0406 20, 0406 30, 0406 40 and 0406 90, and frozen curd falling under CN code 0406 10. The decision was introduced for the period of September 5 to December 31, 2014. However, on September 22, 2014, the European Commission terminated the PSA for cheese to avoid the possibility of reaching the maximum volume of 155,000 MT so soon after the measure was opened on September 5, 2014. In December 2014, the EC decided to extend the period of the PSA for NFD and butter till the end of February 2015 and then extended it further till September 30, 2015. As a result of opening of the PSA program at the end of December 2014 stocks of cheese, butter and skim milk powder amounted to 32,000MT, 22,000MT and 17,000MT, respectively.

DISCLAIMER

The PS&D numbers in this report are not official USDA numbers. The numbers are the result of a group effort by the individual FAS EU offices to consolidate PS&D's from all EU-28.

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Commodities:

Dairy, Milk, Fluid

Dairy, Milk, Fluid Market Begin Year European Union	2013		2014		2015	
	Jan 2013		Jan 2014		Jan 2015	
	USDA Official	New post	USDA Official	New post	USDA Official	New post
Cows In Milk	23,193	23,193	23,500	23,481	23,700	23,574
Cows Milk Production	140,100	140,100	146,700	146,500	147,000	148,300
Other Milk Production	4,750	4,750	4,750	4,750	4,750	4,750
Total Production	144,850	144,850	151,450	151,250	151,750	153,050
Other Imports	23	23	15	10	15	16
Total Imports	23	23	15	10	15	16
Total Supply	144,873	144,873	151,465	151,260	151,765	153,066
Other Exports	420	420	465	560	465	500
Total Exports	420	420	465	560	465	500
Fluid Use Dom. Consum.	33,800	33,800	34,466	34,466	33,900	34,550
Factory Use Consum.	110,653	110,653	116,534	116,234	117,400	118,016
Feed Use Dom. Consum.	0	0	0	0	0	0
Total Dom. Consumption	144,453	144,453	151,000	150,700	151,300	152,566
Total Distribution	144,873	144,873	151,465	151,260	151,765	153,066

1000 HEAD, 1000 MT

Production:

2014

In 2014, EU-28 milk deliveries increased by 4.6 percent year-on-year. Supplies and quality of roughages were good and compound feed prices were declining. In a majority of EU member states milk procurement prices were high stimulated by strong export demand. The production estimate of milk deliveries in 2014 presented in the EU-28 Annual Dairy and Products (published in mid-October 2014) was corrected upwards in December 2014 in order to reflect higher level of milk deliveries. In several member states with favorable natural conditions for production of milk farmers started in advance to adjust to the new market situation which was created by the termination of milk quota system. In addition, there was a lag between market situation signals in the last quarter of 2014 and reaction of farmers taking production decisions that resulted in high milk and dairy products output towards the end of the year.

In 2014, EU-28 dairy cow inventories increased. This trend is expected to continue in 2015. Farmers were building cow inventories in response to favorable dairy market conditions and the dairy quota elimination coming in 2015. A high ratio of heifers ready to enter production cycle in the EU28 dairy cattle herd at the end of 2014 indicated a potential for further growth of milk deliveries in 2015.

2015

Milk deliveries in 2015 are expected to increase over one percent in comparison to 2014 because of higher cow inventories, good feed availabilities and termination of milk quota system. Dairy cow numbers are expected to grow because farmers will introduce to their herds first calved heifers in order to expand operations to generate higher overall milk production. Despite lower milk farm-gate prices many farmers are not expected to reduce milk production because they are dependent on the revenue to pay back credits taken to enlarge and modernize their farms in expectation of the approaching termination of the milk quota system and pay fines for over-quota production in 2014/2015QY. Good feed availability along with continued enhancement of genetics in national herds is expected to generate

higher per cow milk yield averages in 2015. On the basis of the aforementioned factors, the estimate of milk deliveries in 2015 was increased upwards in comparison to the “old” data..

Consumption:

In 2015, fluid milk consumption is expected to increase in response to higher output of raw milk.

Trade:

In the first two months of 2015, extra EU-28 exports of fluid milk increased by 3 percent in comparison to the same period of 2014 driven by strong demand from China for UHT milk. It is expected that towards the end of the year exports will be slower because of stable demand from China and competition for raw milk for production of cheese and milk powders.

Commodities:

Dairy, Cheese

Dairy, Cheese Market Begin Year European Union	2013		2014		2015	
	Jan 2013		Jan 2014		Jan 2015	
	USDA Official	New post	USDA Official	New post	USDA Official	New post
Beginning Stocks	0	0	0	0	100	32
Production	9,368	9,368	9,560	9,560	9,600	9,640
Other Imports	75	75	76	76	76	70
Total Imports	75	75	76	76	76	70
Total Supply	9,443	9,443	9,636	9,636	9,776	9,742
Other Exports	787	787	720	721	790	780
Total Exports	787	787	720	721	790	780
Human Dom. Consumption	8,656	8,656	8,816	8,883	8,936	8,962
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	8,656	8,656	8,816	8,883	8,936	8,962
Total Use	9,443	9,443	9,536	9,604	9,726	9,742
Ending Stocks	0	0	100	32	50	0
Total Distribution	9,443	9,443	9,636	9,636	9,776	9,742

1000 MT

Production:

In 2015, EU-28 cheese production is expected to increase by one percent due to higher availability of raw milk, recovering exports and increased domestic consumption. The world market demand for cheese remains strong, stimulating EU production and exports. Reduced world market prices for milk powders competing with cheese for raw milk supplies and potential termination of Russian ban on imports of dairy products are expected to stimulate production and exports of cheese in 2015.

Consumption:

In 2015, the increased cheese output will be directed into domestic consumption, exports and increased commercial stocks. The EU-28 domestic cheese consumption increased in parallel with the economic recovery. In 2015, growing supplies and improving economic situations in some member states are expected to stimulate cheese consumption further leading to an increase in overall consumption relative to 2014.

Trade:

It is expected that in 2015, exports of cheese will increase by an estimated 8 percent due to higher output and continuing world market demand. However, 2015 exports of cheese are expected to be lower than it was estimated in the fall of 2014 report because of Russian ban which will be in place for at least 7 months of 2015. If the Russian ban is lifted in 2015 the weaker ruble may reduce the attractiveness of the Russian market for EU28 exporters. Although the Russian ban on imports of dairy products affected EU exports in 2014, the actual effect was smaller than originally expected. For example the influence of the ban on German dairy exports was limited because previous Russian restrictions had already halved German exports of dairy products to Russia in 2013 and again in the first four months of 2014. Because of these earlier restrictions German dairy processors had already intensified their efforts to export to other markets. Germany was able to increase cheese exports to a number of countries including South Korea, USA, Japan, Switzerland, Mexico, and North African countries.

In the first two months of 2015 EU28 exports of cheese were 17 percent lower than in the same period of the previous year. It is expected that in 2015 exports of cheese will recover as domestic output gears up to meet continuing demand on the world market. Apart from Russia, major external markets for EU28 cheeses include the United States, Switzerland, Japan, and Algeria. Cheese imports are projected to remain within the established import quotas.

Stocks:

On September 4, 2014, the European Commission issued Regulation (EU) 950/2014 opening a temporary exceptional private storage aid scheme for 155,000 MT of certain cheeses and fixing in advance the amount of aid. The private storage aid scheme was opened for cheeses falling under CN codes 0406 20, 0406 30, 0406 40 and 0406 90, and frozen curd falling under CN code 0406 10. The program was closed on September 22, 2014, because according to the EC “it was disproportionately used” by certain member states. According to the Milk Market Observatory (MMO) report on September 28, 2014, the stocks built during the time when the PSA scheme for cheese has been operating amounted to 101,000MT. On December 28, 2014, PSA stocks of cheese amounted to 32,000MT and are expected to be depleted by the end of 2015. The MMO is an advisory group of experts/organizations created by the European Commission to monitor EU and world dairy market after the termination of milk quota system.

Commodities:

Dairy, Butter

Dairy, Butter	2013	2014	2015
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Market Begin Year European Union	Jan 2013		Jan 2014		Jan 2015	
	USDA Official	New post	USDA Official	New post	USDA Official	New post
Beginning Stocks	33	33	24	24	40	22
Production	2,100	2,100	2,195	2,250	2,275	2,285
Other Imports	44	44	50	53	45	46
Total Imports	44	44	50	53	45	46
Total Supply	2,177	2,177	2,269	2,327	2,360	2,353
Other Exports	122	122	135	143	150	160
Total Exports	122	122	135	143	150	160
Domestic Consumption	2,031	2,031	2,094	2,162	2,170	2,173
Total Use	2,153	2,153	2,229	2,305	2,320	2,333
Ending Stocks	24	24	40	22	40	20
Total Distribution	2,177	2,177	2,269	2,327	2,360	2,353

1000 MT

Production:

In 2015, EU-28 butter output is expected to increase in comparison to 2014 due to higher supplies of raw milk, continuing world market demand, as well as growing output of NFDM for which butter is a residual product. It is expected that, as the Russian embargo will slow down the increase in cheese production in 2015, milk that is not used for cheese will be used for butter and milk powder production. Lower exports to Russia are expected to be partly offset by growing domestic demand and partly by higher exports to other destinations.

Please note that the 2014 butter output was increased in comparison to the “old” data in order to balance overall protein-fat ratio in EU28. The imbalance of fat-protein ratio caused mainly by very high increase of NFDM production in 2014, for which butter is a residual product, was also noted in the March 2015 MMO report.

Consumption:

EU-28 domestic butter consumption is projected to increase in 2015 in response to higher output and changes in consumer preferences. Campaigns against the use of palm oil are also playing a larger role in consumer buying decisions.

Trade:

In 2015, exports of butter are expected to increase in comparison to the previous year’s level due to higher output and competitive export prices. In the first two months of 2015, EU-28 exports of butter and butter oil increased by 7 and 8 percent, respectively, in comparison to the same period of 2014.

Reduced prices make EU28 butter competitive even on the U.S. market. In the first two months of 2015 EU28 exported to the United States 2,100 MT of butter, 80 percent increase over the same period of 2014. In the first two months of 2015, imports within the EU import quota set aside for New Zealand amounted to 1,362 MT, 92 percent less than in the comparative period of 2014.

Stocks:

Introduction of the Russian ban on agricultural products forced the European Commission to re-open the PSA scheme for butter for the period September 4 till December 31, 2014. At the end of 2014 the European Commission decided to extend the PSA scheme for butter and NFDM till February 28, 2015 to avoid release of stocks accumulated in the fall of 2014 during the spring peak production period in

2015. In February the EC decided to extend the PSA program for butter and NFDM till September 30, 2015. According to the MMO report on March 14, 2015 PSA stocks of butter amounted to 38,608 MT mainly used by the Netherlands, Germany, France and Ireland. For butter, the EU aid is Euro18.93 per MT of storage for fixed storage costs, plus Euro 0.28 per MT per day of contractual storage. The storage period is 90-210 days. There is no ceiling on the volumes that can be stored.

Commodities:

Dairy, Milk, Nonfat Dry

Dairy, Milk, Nonfat Dry Market Begin Year European Union	2013		2014		2015	
	Jan 2013		Jan 2014		Jan 2015	
	USDA Official	New post	USDA Official	New post	USDA Official	New post
Beginning Stocks	0	0	0	0	30	17
Production	1,250	1,250	1,550	1,550	1,600	1,620
Other Imports	5	5	2	2	1	2
Total Imports	5	5	2	2	1	2
Total Supply	1,255	1,255	1,552	1,552	1,631	1,639
Other Exports	407	407	610	646	660	710
Total Exports	407	407	610	646	660	710
Human Dom. Consumption	848	848	912	889	951	909
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	848	848	912	889	951	909
Total Use	1,255	1,255	1,522	1,535	1,611	1,619
Ending Stocks	0	0	30	17	20	20
Total Distribution	1,255	1,255	1,552	1,552	1,631	1,639

1000 MT

Production:

After a 24 percent increase in 2014 output of NFDM is expected to continue to grow in 2015 but with a slower pace than in the previous year. Higher supplies of milk and increased drying capacity mainly in Germany and France, as well as continuing demand from export markets are expected to stimulate NFDM output in 2015.

Consumption:

Higher NFDM production in 2015 is expected to be directed mainly into export channels or commercial stocks as well as domestic consumption. Please note that the category “domestic consumption” includes commercial stocks.

Trade:

In the first two months of 2015, exports of NFDM increased by 24 percent over the same period of 2014. The increase of NFDM exports in early 2015 stems from higher imports by Egypt. The expected increase of exports in 2015 results from competitive prices and increased EU28 production.

Stocks:

As in the case of butter, opening of PSA for NFDM requires European Commission’s decision, which depends on the current market situation. Introduction of the Russian ban on agricultural products forced the European Commission to re-open the PSA scheme for NFDM from September 4 till December 31, 2014 with further extension to February 28, 2015 and continuing till September 30, 2015. According to

the MMO report of March, 2014 PSA stocks of NFDMM amounted to 15,571 MT. For NFDMM, the aid is Euro 8.86 per MT of storage for fixed storage costs, plus Euro 0.16 per MT per day of contractual storage, for 90-210 days. There is no ceiling on the volumes that can be stored.

Commodities:

Dairy, Dry Whole Milk Powder

Dairy, Dry Whole Milk Powder Market Begin Year European Union	2013		2014		2015	
	Jan 2013		Jan 2014		Jan 2015	
	USDA Official	New post	USDA Official	New post	USDA Official	New post
Beginning Stocks	0	0	0	0	0	0
Production	667	667	730	720	800	740
Other Imports	3	3	2	1	2	1
Total Imports	3	3	2	1	2	1
Total Supply	670	670	732	721	802	741
Other Exports	374	374	400	389	450	400
Total Exports	374	374	400	389	450	400
Human Dom. Consumption	296	296	332	332	352	341
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	296	296	332	332	352	341
Total Use	670	670	732	721	802	741
Ending Stocks	0	0	0	0	0	0
Total Distribution	670	670	732	721	802	741
1000 MT						

Production:

In 2015, WDM production is expected to increase due to higher milk supplies. The increase of production will be directed to domestic market and higher exports.

Consumption:

In 2015, domestic use of WDM is expected to increase in response to higher domestic demand particularly for chocolate production and growth of commercial stocks.

Trade:

It is estimated that in 2015 exports of WDM will increase compared to 2014 because of growing supplies and reduced export prices. However, the increase is expected to be less pronounced than previously expected because of slower import demand from the world market. In the first two months of 2015, EU-28 exports of WDM were 10 percent below the previous year's level, mainly due to reduced shipments to Algeria.

Policy:

EU Dairy Production Quota Regime Ends after Thirty-One Years

Launched in 1984, the EU dairy production quota system finally ended on March 31, 2015. Twelve years after the original decision to end the production quotas and after a six-year "soft landing" transitional period, European dairy farmers are operating again in a fully liberalized dairy market. After having produced completely isolated from the world market for 20 years, EU dairy farmers quickly learned to live with price volatility as they became gradually exposed to the world market in recent

years. The European Commission forecasts in its latest “[Short-term Outlook](#)” [1] report that EU milk production will only increase 1 percent in 2015 and even less in 2016. However, this comes on the heels of a 4-5 percent increase in milk production during the last quota year 2014/15, as EU farmers took advantage of high milk prices and new investments in production capacity came online ahead of the end of the quota. This big increase in production led to the largest transgression of quota since the regime was in place, with early calculations indicating that the final super-levy bill may surpass Euro 1 billion for 12 member states, compared to Euro 409 million for 8 member states in 2013/14 QY. In March 2015, the European Council agreed on a voluntary measure that would allow member states to collect this super-levy spread over three years, easing potential cash flow problems for affected farmers. The quota system was introduced to limit public expenditure on the sector, to control milk production, and to stabilize milk prices and the agricultural income of milk producers. Generous guaranteed prices for intervention storage of butter and skimmed milk powder had induced EU dairy farmers to widely expand milk production in the ‘70s leading to the infamous “milk lakes” and “butter mountains”. However, by the end of the ‘90s, in several member states the quota system was seen as stifling progress and competitiveness because of its high cost for dairy farmers, which resulted in the decision of the 2003 CAP Mid-Term Review (MTR) agreement to let the system expire in 2015. It was calculated that for [German farmers](#) [2] alone the quota regime had led to an additional cost of Euro 15 billion for super-levies, purchase of extra quota, and lease rates.

Future for Dairy Production in the EU

Most analysts agree on favorable long-term prospects for world dairy markets, with most of it to be supplied by traditional dairy exporters like Australia, New Zealand, the United States, and the European Union. However, contrary to highly optimistic sentiments, until one year ago, in member states like Ireland, Denmark, The Netherlands, and Germany, the European Commission forecast that EU milk production will only increase slowly in the next few years. Nevertheless, it has been [reported](#) [3] that EU dairy processors invested, and plan investments, up to a total of \$2.8 billion, mainly into new infant formula and powder drying capacity, in Belgium, Denmark, France, Germany, Ireland, and The Netherlands. Expectations were that the end of the quota system would lead to processors reshuffling their supply policies, which would push small and less competitive producers out of business. This would result in a significant overall productivity increase by the remaining producers in the aforementioned member states, but also in the new member states that acceded to the EU after 2004 where milk productivity is still seriously lagging.

These optimistic scenarios were thwarted by the downturn in world dairy prices towards the end of 2014. This decrease in dairy prices resulted from decreased buying by China in 2014, which was compounded by the Russian import ban as of August 2014, at a time when all major producers had increased production in response to the previous high world market prices. Droughts in Australia, the United States, and later New Zealand somewhat put a brake on the downturn in prices as they allowed smaller production increases only. Since the droughts in Australia and New Zealand have ended, production increases in these countries can be expected to speed up again. It is unclear when China will start heavier purchasing again, as well as whether the Russian import ban will cease. Therefore, the mostly stagnant EU domestic market offers only dim opportunities for short-term dairy production increases in the EU.

[1] http://ec.europa.eu/agriculture/markets-and-prices/short-term-outlook/index_en.htm

[2] <http://www.bauernverband.de/auslaufen-milchquote-maerz-2015>

[3] <http://blog.usdec.org/usdairyexporter/europe-gains-from-milk-quota-removal>

