DECODING DAIRY DISRUPTION

WHY UK RETAILERS MUST RE-THINK DAIRY PROCUREMENT STRATEGY NOW

September 2025

Kite

EXECUTIVE SUMMARY

2025 has been a year of surprises in the UK dairy market. Despite tight global supply, UK milk production surged – reaching record highs in the spring – while farmgate prices lagged behind those on the continent. This report explores the factors driving that anomaly, the structural dynamics shaping the sector, and the implications for farmers, processors and retailers across the UK dairy value chain.

The May 2025 milk glut was not a structural issue, but a warning sign. UK farmers responded quickly to favourable margins, good weather and fewer production restrictions than seen in the EU or New Zealand. Meanwhile, whilst investment in processing capacity is happening, capacity lagged production, creating bottlenecks that exposed inefficiencies in supply management and raised environmental and reputational concerns.

At the heart of the issue lies a market in transition. For decades, the UK dairy sector has been focused on domestic retail, shaped by the logistics and pricing of liquid milk. But with processors like Arla and Müller investing heavily in export capabilities – mozzarella, powders, whey – UK milk is increasingly tied to global markets where premium-added products command higher returns.

This shift is reshaping power in the value chain. What was once, for most of the time, a buyer's market is now becoming a seller's market. Farmers are beginning to question the value of traditional cost of production (COP) models, which cap upside in buoyant markets. With global prices often outperforming domestic benchmarks, producers are seeking more flexible, reward-driven pricing.

At the same time, UK retailers ask for higher standards than some global commodity markets. Sustainability, carbon metrics and animal welfare are now expected farm-level deliverables. But in a seller's market, customers asking for more requires paying for more – consistently and at a premium. Otherwise, local customers may be out-competed by better-paying global customers, with less demands.

KEY CHOICES NOW FACE EACH PLAYER IN THE CHAIN

- **Retailers** have a short-term opportunity to guarantee security of supply of milk produced under their specific standards. Export opportunities and policy threats in the UK could put their supply at risk. That means revisiting pool contract terms, improving milk pricing structures, and offering meaningful incentives for sustainability, biodiversity and supply consistency.
- All **processors** need a strategy to secure future milk supplies and avoid being out competed for milk by ambitious peers.
- **Farmers** – the rules of the game have changed. Farmers need to look at the market signals and ask what their processor requires in the way of milk quality, welfare standards and seasonality. The advantage first movers had on seasonal milk production has gone as nearly all processors will manage seasonality by using financial penalties. Farmers need to work out what works financially for their business model.

The takeaway is clear: the UK dairy market is becoming more global, more competitive, and more supplier led. The current surplus is temporary. The shift in power, pricing dynamics and expectations is here to stay. Those who move fastest to adapt will be best positioned to thrive.

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2025: A YEAR OF ANOMALIES

Over the last six months, there have been some unexpected trends in the UK dairy market. Milk production has significantly increased, and raw milk prices in the UK remain relatively weak compared to those seen across Europe. At a time when global milk supplies are tight, the UK seems to have plenty, so what's going on?

To help clarify this unusual situation and, more importantly, to explore what the wider context means for the future, this paper reviews the factors at play in the UK milk market, how recent activity by farmers and processors is playing out and discusses the implications for the future stability of milk supply.

While UK-wide data is used, the analysis focuses on Great Britain due to its more integrated, retail-driven market. Including Northern Ireland, which primarily serves B2B and international markets, would introduce complexities beyond the scope of this report.

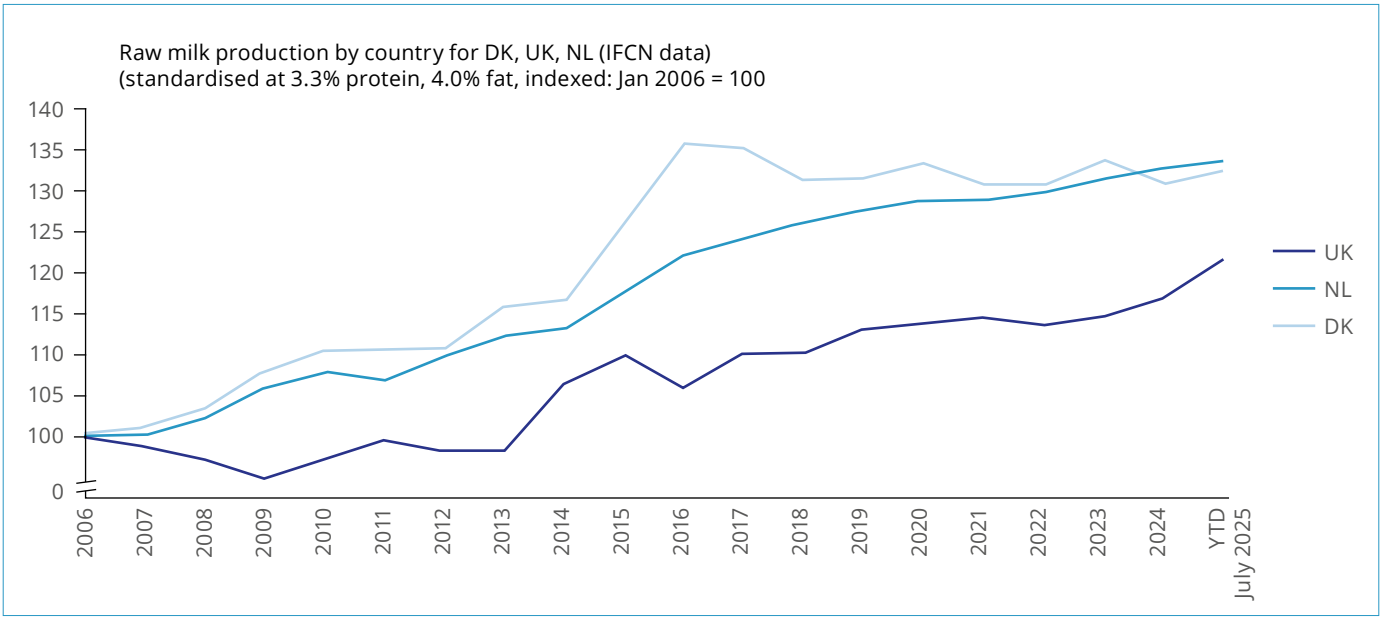
STRONG PRODUCTION GROWTH IN 2025

As of July 2025, UK milk production is up nearly 5% year-on-year, marking the fastest growth since 2014. That year was notable for record-high global dairy prices and preparations for the EU's quota removal in April 2015, which opened the door to greater production across the continent.

This surge puts the UK in contrast with two major European dairy exporters – Denmark and the Netherlands.

As shown in Figure 1, since 2006, milk production in these countries has grown considerably, while UK output growth has lagged behind. Now, however, the UK is catching up, and the pace is accelerating. This is in contrast to The Netherlands, where growth has been stagnant since 2015, and slower growth in Denmark, which is expected to stall due to anticipated restrictive agricultural legislation.

Figure 1: Raw milk production by country



> "With changing market dynamics and increasing interest in products like cheese for export, the UK dairy sector is beginning to pivot.

There are key structural differences at play, however. The Netherlands and Denmark produce more than double what they consume, making them strong export players. The United Kingdom, on the other hand, remains close to 95% self-sufficient. Great Britain has traditionally focused on domestic retail markets, particularly in liquid milk.

This inward focus, combined with historical challenges like overcapacity, fragmented industry structures, and policy tensions, has limited UK dairy's growth – until recently. With changing market dynamics and increasing interest in products like cheese for export, the UK dairy sector is beginning to pivot.

The data suggests substantial growth potential for the UK, but this won't be uniformly achievable. Factors such as regional planning restrictions, land availability and environmental pressures will shape where and how this growth can occur. What's more, some of the growth potential will be limited by retailer corporate responsibility activity.

Inevitably, legislation will become more restrictive here too. But it is worth considering that by comparison, the intensity of dairy farming in the UK – measured by output per square kilometre – is around one-seventh that of The Netherlands (see Figure 2).

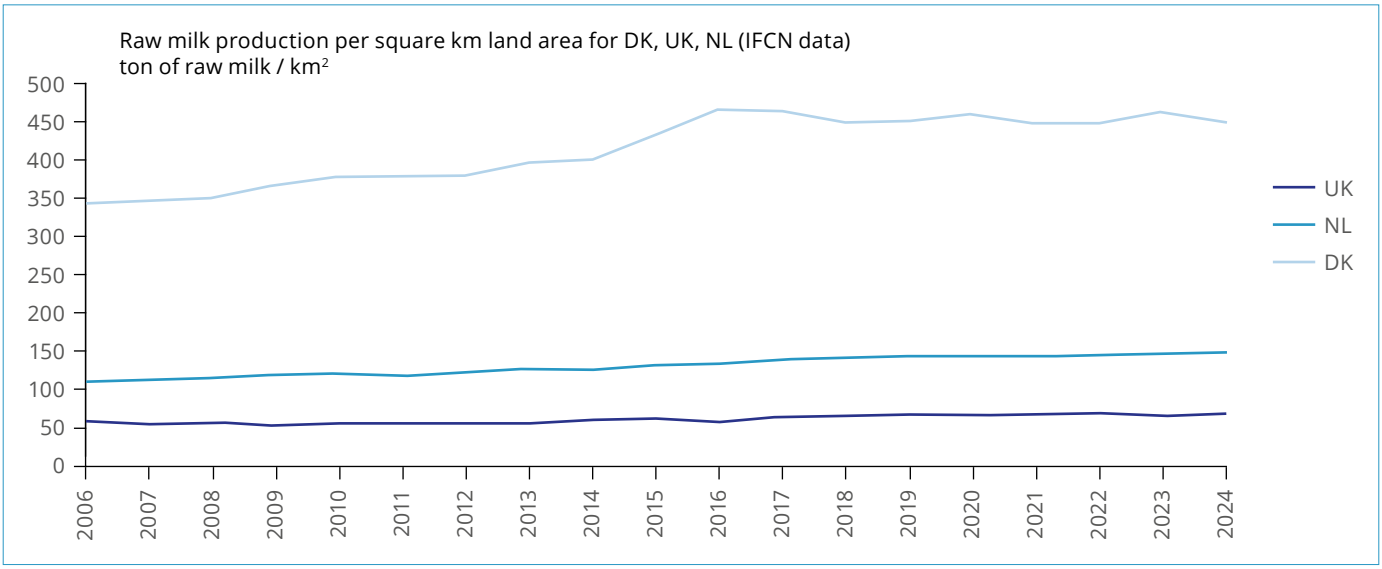
This suggests room to scale, particularly as some of the environmental issues that now limit Dutch production (like eutrophication) are not as severe across most of GB.

Another structural factor that has limited growth in the UK has been the traditional reliance on daily fresh milk deliveries to retail, creating the so-called 'liquid premium'. This model prioritised consistent supply over expansion or international competitiveness and drove behaviour from farm to processor.

However, as new export opportunities emerge, the dairy sector is beginning to evolve. This raises important questions about how competitive UK milk prices are, especially compared to those in more export-oriented markets, and what role pricing will play alongside volume going forward.

What does seem clear is that the structure of the UK dairy industry is shifting, and this shift carries commercial implications for processors and retailers alike.

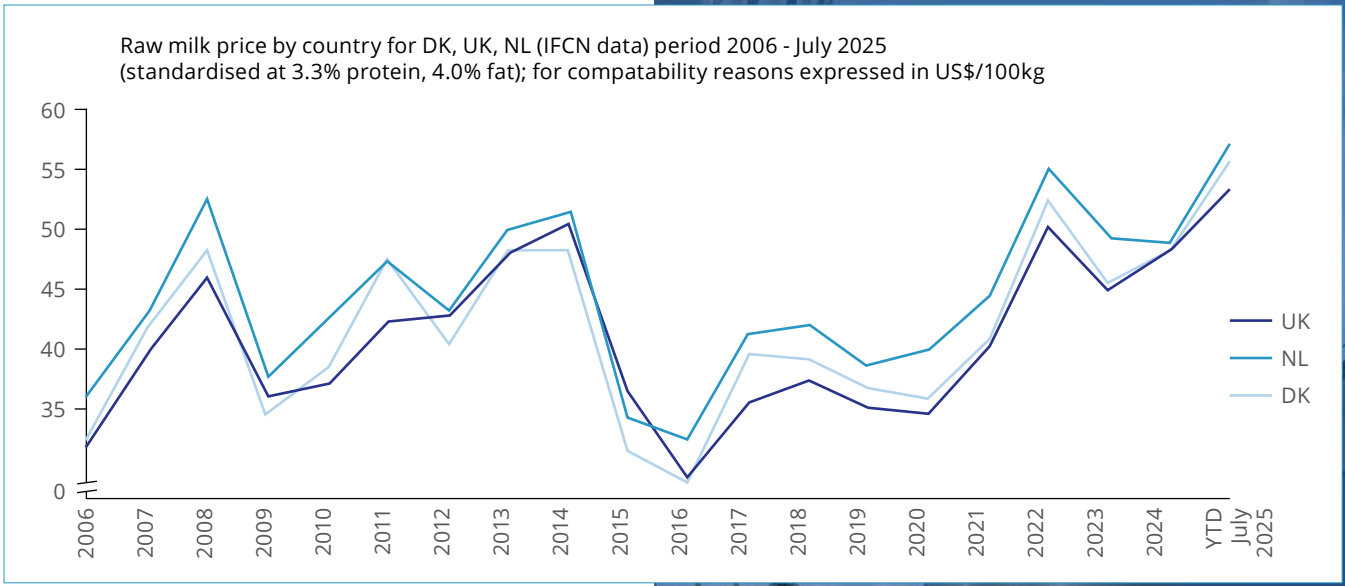
Figure 2: Raw milk production per square km of land area



WHY UK MILK PRICES LAG BEHIND

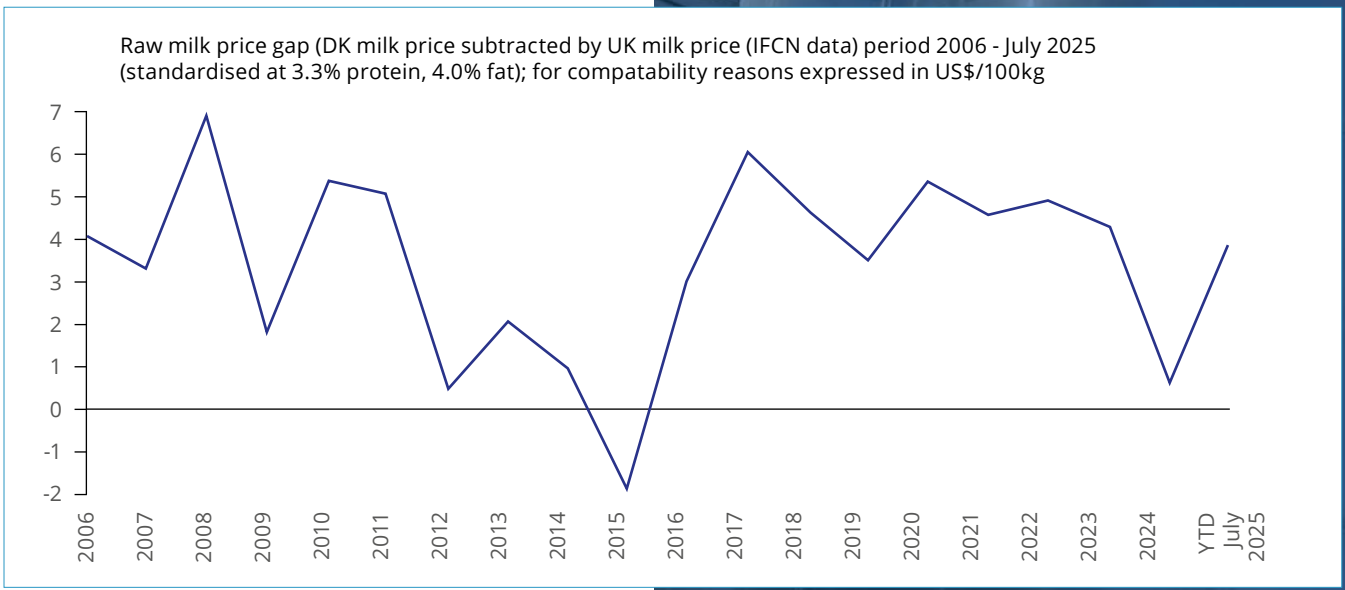
Despite recent gains, UK raw milk prices continue to trail those seen in comparable European countries. Figure 3 compares farmgate milk prices in the UK, Denmark, and the Netherlands, all standardised to 3.3% protein and 4.0% fat, and converted into US dollars per 100 kg for cross-country comparison (source: IFCN).

Figure 3: Raw milk price by country



When UK prices are compared to Denmark over time, the difference is stark, as shown in Figure 4.

Figure 4: Raw milk price gap – UK and Denmark



"Over a 19-year period, Danish milk prices averaged $3.50/100 kg higher than UK equivalents. Using a long-run exchange rate, that's equivalent to around 2.3 pence per litre.

So, what does this tell us?

- **Interconnected markets:** While GB milk isn't shipped abroad due to high logistics costs, UK prices are still influenced by trends on the continent. The market may be insular in geography, but not in pricing dynamics.
- **Structural underperformance:** Historically, UK prices have consistently underperformed, especially when compared with Danish prices. In 2024, price levels were nearly aligned, but in 2025, continental prices rose more sharply than those in the UK.
- **Persistent price gap:** Over a 19-year period, Danish milk prices averaged $3.50/100 kg higher than UK equivalents. Using a long-run exchange rate, that's equivalent to around **2.3 pence per litre** – an important differential in a margin-sensitive industry.

Why does this gap exist?

There are several underlying structural reasons why UK milk prices remain lower:

- **Ownership structures and scale matter:** In much of continental Europe, large farmer-owned cooperatives like Arla, Friesland Campina and Valio dominate processing. These businesses prioritise high farmgate prices over company profit, reinvesting into the business rather than paying out dividends. They also access global markets, spreading risk. By contrast, the UK dairy market is influenced by smaller processors, many of whom are focused on domestic markets, with a large number of privately-owned processors who naturally make different commercial decisions.
- **A legacy of fragmentation:** Historically, the UK's cooperative movement was weakened by political reform. After the dissolution of the Milk Marketing Board monopoly, the sector was left with underpowered cooperatives unable to invest in higher-value processing capabilities. This lack of scale held back price growth for many years. Only recently has the UK market begun to emerge from this structural lag.

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VOLATILITY VS VALUE

The UK dairy sector remains heavily weighted toward domestic retail markets; especially liquid milk sold via major supermarkets. These retail-focused contracts tend to be less volatile – but also less lucrative over time – than export-oriented supply chains focused on high-value products like cheese and specialised whey ingredients. However, globally, the highest returns in dairy now come from premium-added products like whey protein isolate and mature cheeses. These markets offer better long-term value than fresh milk supply.

Ultimately, the ability to access both stable domestic demand and premium export markets correlates with stronger, more consistent farmer pay-outs. The UK has been slower to develop this dual-channel capability, hence the historic price gap with continental Europe, but that dynamic is now beginning to change.

WHY UK DAIRY SUPPLY HAS SURGED IN 2025

Over the past 30 years, the UK dairy sector has undergone major consolidation. Indeed, 70% of farms have closed since the early 1990s. While closures have slowed in recent years, about one dairy farm still exits the industry every working day. This is part of a wider European trend; Denmark and the Netherlands also saw closures of 84% and 62% of farms, respectively, over a similar period.

But what matters more than the number of farms lost is the structure of those that remain. UK farms now rank among the largest in Europe in terms of herd size and, increasingly, efficiency. While output per cow still trails countries like the Netherlands (by about 14%), the trend suggests room for improvement and scalability.

Historically lower milk prices in the UK may also have forced farms to become leaner and more competitive. However, competition for land is intensifying. In the south west of England, for instance, high demand for bioenergy crops like maize has made it more profitable to grow feedstock for digesters than for cows, whilst elsewhere renewable energy investments such as wind turbines are shifting farmer focus away from dairy.

Ultimately, these longer-term structural influences came together with short-term market dynamics to create a surge in UK milk production in early 2025:

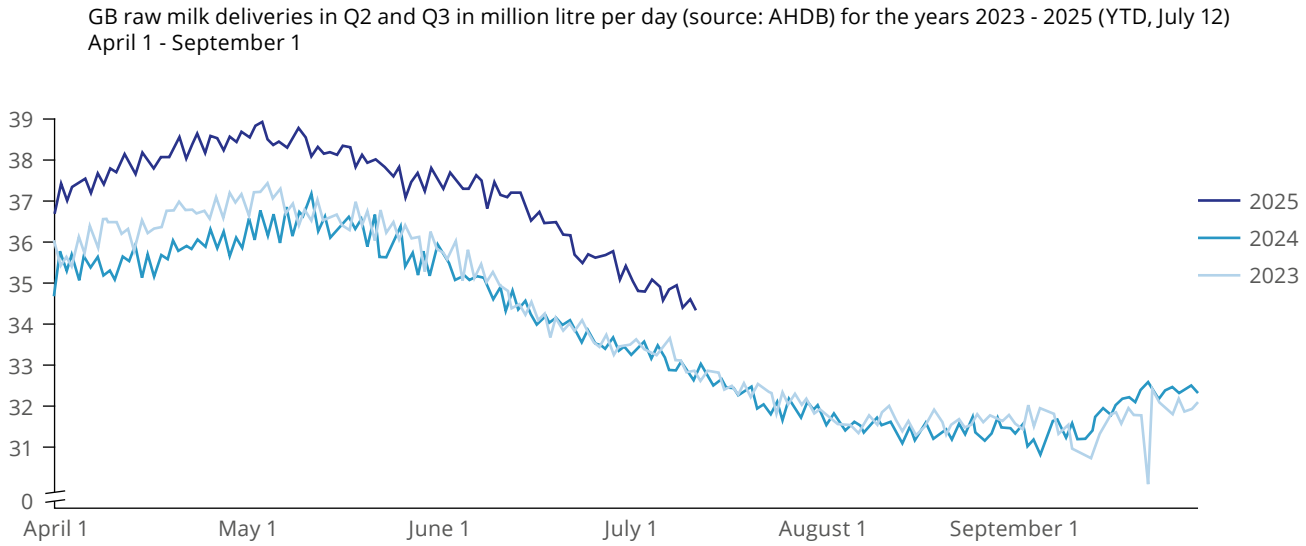
- **Improved margins:** For the first time since 2006, the indexed cost of feed dropped below that of the milk price. With feed costs falling and global dairy prices rising (driven by demand for premium whey and cheese), margins for UK dairy farmers improved significantly.
- **Lack of UK growth limits:** Unlike farmers in the EU or New Zealand, UK producers aren't facing strict output caps or environmental quotas – enabling them to respond more freely to market signals.
- **Favourable weather:** A good early season further boosted output.

The result? A rapid and substantial supply surge, even as global markets remain tight. This favourable mix – relatively high milk prices, relatively low feed costs, and room to grow – has contributed to higher UK milk supply, which may continue for the coming months. However, it may be temporary. Feed and energy prices are closely tied through land use, and global energy markets are volatile. Any shift in energy or policy (as seen in Europe post-2022) could quickly change the margin landscape. Recent policy shifts on IHT and access to labour will also be factors affecting the confidence to invest in long term capacity at farm level.

THERE'S A SHORT-TERM CHALLENGE AROUND SEASONALITY

In spring 2025, the UK dairy market hit a record high: daily milk deliveries peaked at nearly 39 million litres in May, up 4.2% from the previous year. This wasn't just more milk – it was more milk delivered all at once, as shown in Figure 5.

Figure 5: GB raw milk deliveries



While autumn milk volumes also rose (up 4.4% in Nov 2024 vs. Nov 2023), they remain about 15% lower than spring peaks and currently manageable from a processing standpoint. However, shifts in calving patterns – including modest growth in autumn block calving – could indirectly amplify future spring peaks.

Indeed, data suggests UK milk seasonality (measured as the May peak vs. annual monthly average) increased from **109.2% to 111.8%** year-on-year. This is notable, but not unprecedented.

In fact, seasonality remains within historical norms and below extreme models like New Zealand and Ireland (see Fig 6), although it still exceeds levels seen in Denmark, the US or The Netherlands.

However, this increase in spring production caused a processing bottleneck in GB in 2025. Some milk was only partially processed (e.g. skimmed with cream retained), skimmed milk was diverted to feed or AD plants and, in some cases, milk wasn't collected at all due to cost constraints. Such situations are unsustainable – they pose reputational and environmental risks and are not compatible with the UK dairy industry's stated environmental goals.

This creates a 'watch out' for spring 2026 if milk production remains high for the rest of 2025 and into 2026 – we could face an even larger glut of milk next year.

But this is unlikely to be a long-term issue. Historically, there would have been two ways to solve seasonality – either adjust seasonality payments to discourage spring milk production or build additional processing capacity to deal with larger peaks.

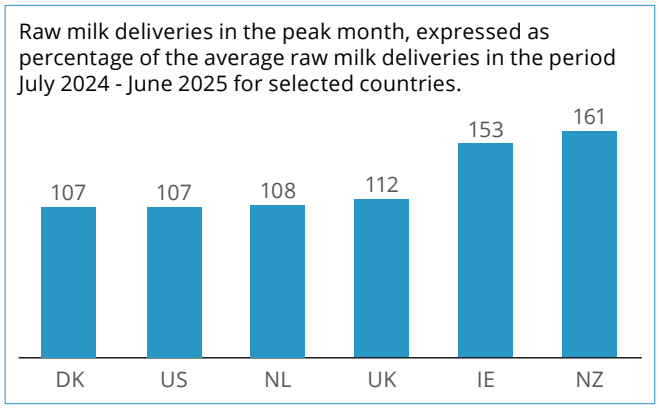
The first is now impacted by the Fair Dealing Obligations (Milk) Regulations 2024 (FDOM), which limit how processors can agree milk pricing. This has happened through the introduction of A/B pricing, where a price is agreed based on an agreed monthly volume, with a market-related price paid for any litres produced over that level. Whilst the new contract regulations give producers more flexibility in how they sell their milk, the practicalities of selling excess litres in a saturated seasonal market do not look attractive, which is likely to limit further seasonality extremes.

Because the latter option – investment in additional processing capacity to deal with larger spring peaks doesn't look attractive. Three commercial realities limit a processor's appetite to handle growing seasonality:

1. Idle assets: spring-only capacity sits unused the rest of the year delivering a poor return on capital, especially with higher interest rates
2. Flat demand: in the main, dairy consumption is stable year around. Seasonal supply creates inefficiencies that someone must absorb, and processors are unlikely to make investments simply to drive down overall efficiency.
3. Working capital: cheesemakers, who traditionally enjoyed cheap spring milk to improve margins, now avoid surplus spring milk that exceeds their order books, due to increasingly high cheese storage and maturation costs.

Analysis comparing The Netherlands (flat supply) and New Zealand (seasonal supply) shows that while commodity returns per litre (AMPE price) are similar wherever milk is processed, farmgate prices are significantly lower in seasonal systems – by nearly **4 pence per litre** over 19 years. The difference? Capital inefficiency which must be absorbed by farmers through lower milk prices. In a GB setting, the mismatch of seasonal supply and market demand is particularly striking.

Figure 6: Raw milk deliveries in peak months by country



In short, Great Britain would do well to avoid drifting toward a high-seasonality model. A flatter, more consistent supply not only supports processing efficiency, but also underpins stronger, more sustainable milk prices overall. More importantly, whilst this short-term supply dynamic may cause market uncertainty, buyers must not be distracted by this and ignore the underlying market trends if they wish to secure long-term stability.

AN ATTRACTIVE PLACE TO PROCESS MILK

Despite the short-term seasonality pressure seen in GB in 2025, unlike highly seasonal producers like Ireland or New Zealand, the UK still offers relatively stable year-round milk supply – a key advantage for processors aiming to maximise return on capital-intensive assets.

Moreover, the UK's lower dairy farm density further enhances its appeal as a processing hub. These conditions have drawn significant investment:

- Arla Foods is investing £179 million into its Taw Valley facility to produce mozzarella for export markets.
- Müller is channelling £45 million into the Skelmersdale (Yew Tree Dairy) site, on top of the undisclosed acquisition cost, to ramp up milk powder and ingredient exports.

What we have seen in the short term is simply that British farmers have been able to respond quickly to global price signals, ramping up milk production in a matter of months, whilst in contrast, processors need years to bring new capacity online. This mismatch explains the current processing bottlenecks and reinforces the logic behind strong farmgate milk price mechanisms to help manage oversupply and discourage volatile seasonal production surges.

However, whilst we have seen (and may see in 2026) a short-term glut of milk in the spring, once Arla's and Müller's new facilities are operational, GB processors may well welcome more consistent but growing supply to fill their expanded capacity. As such, the current over supply is merely a short-term imbalance, not a structural problem for the UK dairy sector.

Indeed, global demand continues to outpace stable milk supply globally. IFCN reports that over the past decade, world dairy fat prices have consistently outstripped global inflation, driven by a rising demand from emerging and mid-income economies. In that environment, milk flows to the highest bidder, and UK-produced milk has a growing global audience.

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RE-THINKING MILK PRICING IN A SELLER'S MARKET

Global dairy dynamics are shifting. With demand outpacing supply, the power in the value chain is moving from buyers to farmers. What was once, for most of the time, a buyer's market is now becoming a seller's market, and this opens new opportunities for British dairy farmers, particularly as investments by Müller and Arla unlock access to global export channels.

This evolving landscape raises important questions about the long-term relevance of existing milk pricing approaches, particularly COP pricing models. While COP agreements offer security during downturns – ensuring costs are covered – they limit upside potential during price peaks, as has been seen in recent months. COP contracts have provided great stability during difficult market conditions and today, many of the farmers that have benefited from them are among the UK's most efficient, sustainable units. However, in a market where prices are more likely to rise than fall, many farmers may begin to see COP as outdated, particularly when based on a small number of macro factors such as feed, fuel, fertiliser and labour. Protection against rare troughs may no longer justify missed profit during most of the cycle.

However, connecting to global value is not automatic. Farmers will only benefit from high world prices if processors have the capacity and product portfolio – such as mozzarella, premium whey, and speciality milk powders – to compete in these markets, and if relevant processor contracts are available.

Serving international markets also means meeting diverse product and quality requirements (e.g Nestlé, Danone and Mondelez). Milk is no longer just 'white', global buyers now demand assurances on sustainability, hygiene, and animal welfare.

But herein lies another dimension that needs to be considered in British milk pricing going forward. UK retailers have led on sustainability, and many global buyers don't yet require the same standards. This creates a commercial dilemma: if domestic buyers want to retain high-quality British milk, they'll need to at least match, if not exceed, global prices and compensate producers for meeting higher environmental and welfare expectations.

"If domestic buyers want to retain high-quality British milk, they'll need to match or exceed global prices.

CHOICES AHEAD

FOR RETAILERS:
Don't be distracted by short-term market dynamics – act now to secure supply for the long term

Retailers may no longer be able to rely on abundant, low-cost British milk. As processors scale their export capabilities, milk will flow to those who value it most. There's no doubt that British retail will have access to both raw milk and processing capacity. The real question is whether retailers are acting fast enough to recognise – and adapt to – the structural changes reshaping the dairy market. The reality retailers face is that they should anticipate structural dairy price increases above inflation and, whilst short-term market dynamics over the coming months may cause 'fuzziness' if milk supply continues ahead of domestic processing capacity, the underlying longer-term trend is clear and requires action. To secure long-term domestic supply at more predictable prices, retailers must act now to:

- Revisit aligned pool contracts
- Adequately reward farmers for sustainability investments and reliable supply

Reform can't wait. Changing contract terms can take as long as building a factory but delaying action now risks higher costs and volatile supply tomorrow.

FOR UK PROCESSORS:
Step up or be left behind

Processors have made strategic decisions about which markets they want to service. Arla and Müller have taken clear positions: invest in both domestic and export-oriented capacity to reduce dependence on UK retail. Their investments in mozzarella, powders and whey derivatives open new global routes for British milk – and will increase their pay-out potential.

Other processors must now assess their competitiveness. Those without strong export pipelines risk falling behind if they can't match the rising prices that global buyers – and leading UK processors – are prepared to pay.

Processors need to explore the opportunity of twin-track pricing in order to drive milk supply to the requirements (sustainability standards, welfare standards and seasonality) of the marketplace.

FOR DAIRY FARMERS:
Local loyalty or global opportunity?

UK dairy farmers face two strategic paths:

1. Align with British retailers, via specific processor contracts: this route involves investing in higher sustainability standards, consistent year-round supply, and enhanced animal welfare – standards increasingly demanded by retailers. While this strengthens local supply chains, it comes with higher on-farm costs and uncertain reward. Tensions have already emerged in 2024–25, as farmers seek fair compensation for the investments made under retailer-aligned schemes.
2. Position for export markets: alternatively, farmers can orient toward export growth. Global markets may demand less in terms of farm-level sustainability upgrades but offer higher price potential in a seller's market. With global supply constrained, this option carries lower risk than in past cycles – and may require less capital to access.

As market power shifts to producers, farmers will also re-evaluate their pricing agreements. Models need to change to reflect the new world.

- Is a COP model still worth it? It protects during downturns but limits upside during high-price periods. Farmer attitude will depend on how a COP contract would align with their businesses vulnerabilities and risk.
- Is there an opportunity for twin-track pricing? Are processors offering a stable price and supply requirement for part of milk volume, in exchange for access to the risk and reward potential of export market access for a proportion of the contract.
- What A/B pricing structures are available? Understanding thresholds and penalties (e.g., for overproduction or seasonality) can shape decisions on calving and feed strategies.
- Are premiums for sustainability investment worthwhile? What are the costs, expected returns, and payback timelines for meeting higher environmental and welfare standards?
- Is level supply rewarded? Some processors may be willing to guarantee volume growth for farms delivering consistent, forecastable supply. This could become a competitive advantage.
- Models need to evolve to reflect the new world.

SUMMARY

There is a short-term window of opportunity opening up to reshape a future, stable relationship with processors and farmers.

The UK milk market is pivoting. May 2025's milk glut was temporary – but telling. The oversupply seen this spring was not structural, but the UK market is now more tightly linked to global dairy markets, where returns are increasingly in line with or above those available in domestic retail. To secure reliable supply, British retailers will need to at least match, if not exceed, world market prices going forward.

What's more, typically British retailers demand more on sustainability, quality and welfare than most global buyers. Asking farmers to deliver to these standards requires investment and that investment only makes sense if the price premiums are substantial, consistent and long-term. Competing with the global market means not just maintaining parity but offering a clear incentive to stay local.

Finally, this year taught farmers two hard lessons – oversupply in the spring offers poor returns and uncontracted volumes may not be collected at all. Expect forecasting and supply discipline to sharpen as processors adjust to protect their margins and avoid overproduction. The days of unmanaged volume growth are over.


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