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Report Highlights:

Despite continuing government and industry efforts to increase dairy production, Philippine milk production remains at less than one percent of total dairy requirements with import filling most of the supply. Imports of milk and milk products declined significantly last year due mainly to tight supply and rising milk prices in the world market. Imports of NFDM are expected to remain sluggish this year while WMP imports are forecast to recover driven mainly by rising re-exports to the region.

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Annual Report
Manila [RP1]
[RP]

Executive Summary

Despite continuing government and industry efforts to increase dairy production, Philippine milk production remains at less than one percent of total dairy requirements with import filling most of the supply. Imports of milk and milk products declined significantly last year due mainly to tight supply and high milk prices in the world market. Imports of NFDM are expected to remain sluggish this year while WMP imports are forecast to recover driven mainly by rising re-exports to the region.

Production

Data from the Philippine National Dairy Authority (NDA) shows that in terms of volume, domestic milk production grew 6.33 percent from 11,610 metric tons in 2004 to 12,340 metric tons last year. Value of dairy production in 2005 amounted to P337.13 million (\$6.74 million at current exchange rate¹). Currently, the country produces less than one percent of its total annual dairy requirement and imports the balance.

As of January 1, 2006, there were estimated 25,746 dairy animals, an increase of about 5.6 percent from the previous year, comprised of cattle (11,261), water buffalo (13,380) and goats (1,105). Dairy cattle numbers, in particular, increased by more than 12 percent due mainly to the on going herd build-up programs of the NDA. Dairy animal numbers are expected to continue increasing by 500-1,000 annually, due to this government program as well as increasing farmgate prices for milk.

DAIRY ANIMAL NUMBERS (as of January 1, 2004-06)			
	2004	2005	2006
Cattle	8,514	10,043	11,261
Carabao	13,062	13,140	13,380
Goats	1,285	1,209	1,105
TOTAL	22,861	24,392	25,746

Source: Bureau of Agricultural Statistics

Female breeders or dams accounted for about 42 percent and 50 percent of total cattle and carabao (water buffalo) population, respectively. The rest were bulls, heifers, yearling and calves. On the other hand, goat female breeders comprised 55 percent of total dairy goat inventory, and the rest classified under kids and bucks.

Despite an increase in the number of dairy animals, the average milking capacity per animal remains low due mainly to inadequate feeding and poor animal management practices. For the NDA-assisted dairy projects in 2005, the total daily milk production was estimated at 21,670² liters, coming from a dairy herd of 12,974 animals.

The average farmgate price of cow's milk rose by 5.61 percent to P16/liter in 2005 from P15.15/liter in the previous year, while the price of carabao's milk increased by 18.42 percent from P38/liter in 2004 to P45.00/liter. Goat's milk increased 9.38 percent from P32/liter in 2004 to P35/liter last year. Average composite price of milk (farmgate) was P27.32/liter in 2005, up 14.26 percent from the previous year.

¹ \$1=P50, Source: Bangko Sentral ng Pilipinas as of October 16, 2006

² Milk production per day = total milk production/number of days from the corresponding reporting period

According to NDA, a total of 16,280 on-farm jobs and 339 off-farm dairy jobs were sustained and created in 2005, realizing an income of P230 million. About 8,781 hectares of land was utilized by the dairy sector in 2005.

Consumption

Philippine GDP grew 5.1 percent in 2005, slower than its projected target of 5.3 to 6.3 percent. The slower growth has been attributed to weaker farm output and slow export demand. Philippine GNP, however, rose by 5.7 percent last year, buoyed by remittances from overseas workers, although still lower than the 6.2 percent GNP growth in 2004. Surprisingly, the significant increase in overseas remittances (which have fueled personal consumption in recent years) did not boost personal consumption to expected levels.

Many analysts have attributed the weak growth in consumption spending to the prevailing political uncertainty in the country. Average inflation was in the 7.7 to 7.9 percent range in 2005, and is projected at 8.0 to 8.5 percent this year. This year's GDP growth target is between 5.7 to 6.3 percent, lower than the previous GRP estimate of 6.3 to 7.3 percent. Some private analysts, however, predict that the 2006 Philippine GDP growth rate will be similar to last year's level. Rising consumer prices, as well as the imposition of new and additional taxes, are expected to produce shifts in the consumption pattern of the average Filipino.

The Philippines, with an estimated population of 84 million, growing annually at 2.36 percent, is a large market for milk and milk products. Dairy products are the country's second largest agricultural import after wheat. The country's dairy industry, which sources 99 percent of its inputs from abroad, is estimated to generate sales of up to \$1 billion annually. The Philippines is the largest Southeast Asian market for U.S. dairy products. The top US exports to the Philippines in 2005 were: nonfat dry milk powder (\$43.1 million), whey (\$10 million) and cheese (\$2.5 million).

In 2005, NDA estimated total domestic dairy requirements to be about 2.53 MMT per year, growing at about 2 percent annually. According to the Food and Nutrition Research Institute (FNRI), per capita milk consumption increased from 16 kg/year in 1993 to 19 kg/year in 2003.

Over the last few years, numerous dairy cooperatives have sprung up in various regions of the country. About half of local milk production, according to NDA, is absorbed in the local communities where it is produced. The other half goes to school and community milk feeding programs co-funded by local government units. With dairy production in the country being more community-based, maintaining the quality of fresh milk becomes a major concern due to the lack of dairy processing facilities and milk delivery vehicles.

Trade

Imports of milk and milk products in 2005 declined by 24 percent in liquid milk equivalent (LME), from 2,110,820 MT down to 1,604,610 MT, due in part to tight supply and rising milk prices in the world market. The major country suppliers by volume were New Zealand with 41 percent share of the total imports; Australia, 22 percent; the United States, 15 percent and France, 5 percent. Imports of NFDM are forecast to increase only marginally in 2006 due to continued weak demand for dairy and dairy products. Imports of whole milk powder (WMP) on the other hand are expected to recover due to a rise in WMP re-exports projected for this year. Imports of fluid milk are expected to rise, despite continuing local fresh milk production, due to growing demand for this product.

In 2005, fluid milk imports on the other hand increased by 5 percent in volume. In terms of value, liquid milk at \$34 million is the second largest dairy product import after non-fat dry milk (NFDM). NFDM and WMP imports stand at about 60 percent of total milk imports. NFDM imports declined by 27 percent while WMP imports are down by 31 percent from the previous year's levels. Imports of whey powder, curd and cheese also decreased in volume.

VOLUME OF DAIRY IMPORTS 2004-05 ('000 MT, in LME)³			
1. Milk and Cream	2004	2005	% Change
o Skimmilk Powder	935.77	685.12	- 27%
o Wholemilk Powder	389.14	267.99	- 31%
o Buttermilk Powder	134.34	148.43	10%
o Whey Powder	371.99	284.04	- 24%
o Liquid (RTD) Milk	43.42	45.71	5%
o Evaporated Milk	16.27	14.69	- 10%
o Cream	34.57	9.91	- 71%
o Condensed Milk	4.56	3.7	- 19%
o Others	8.31	5.13	- 38%
Total Milk and Cream	1,938.37	1,464.72	- 24 %
2. Butter & Butterfat & Dairy Spreads	93.4	85.5	- 8%
3. Cheese	27.78	24.34	- 12%
4. Curd	51.27	30.05	- 41%
Total Imports	2,110.82	1,604.61	- 24 %

Source: National Dairy Authority

Large imports of WMP in 2004, adjusted by Post to 51,000 MT from 45,000 MT, led to higher beginning stocks in 2005, which augmented low levels of imports of milk powder in 2005. Likewise, higher dairy product prices in 2004 led to a lower demand for NFDM, adjusted by Post from 104,000 MT to 94,000 MT, resulting in higher beginning stocks for 2005.

Ice cream and ice drop exports rose significantly during the year resulting in a higher level of exports. The largest re-export item is still whole milk powder.

VOLUME OF PHILIPPINE MILK & MILK EXPORTS (In MT, LME)				
	2003	2004	2005	% Change 04 / 05
Liquid (RTD) Milk	1.34	8.59	6.64	- 23%
Skimmilk powder		404.53	2,329.87	476%
Wholemilk powder	204,322.64	255,195.68	239,311.35	- 6%
Evaporated milk	1810.08	247.33	149.26	- 40%
Cream	63.86	66.12	97.47	47%
Condensed milk	22.02		2.34	0%
Ice cream/mixes	1,273.74	1,571.06	1,669.12	6%
Ice drop	35.84	65.12	5,807.28	8818%

³ To get the LME, NDA uses a conversion factor of 8.02 liters per 1 kg of whole and non-fat dry milk powder and 5.51 liters per kg of cheese

Whey	164.56	18.94	266.68	1308%
Others	1.44	0.51	7.93	1455%
MILK AND CREAM	207,695.52	257,577.88	249,647.94	- 3%
Butter/Butterfat	30.22	66.44	32.18	-52%
Cheese	867.13	1,043.62	1541.11	48%
TOTAL	208,532.87	258,687.94	251,221.23	- 3%

Source: National Dairy Authority

Policy

The Philippine DA continues to prioritize the development of the Philippine dairy industry, recognizing the growing demand for fresh milk by the specialty coffee shops, hotels and restaurants as well as by the local government units for their milk feeding programs. While the DA accepts that Philippines cannot compete in the powdered milk market, it believes that it can focus on supplying fresh milk to the market.

The National Dairy Authority, an attached agency of the Philippine Department of Agriculture, is mandated to ensure the accelerated development of the Philippine dairy industry through policy and program implementation. The NDA aims to accelerate dairy herd build-up and milk production, enhance dairy business through the delivery of technical services at farm and enterprise levels, increase the coverage of milk feeding programs to reduce malnutrition and mobilize broad support for local milk consumption. The NDA implements the following four main programs:

1. Dairy Business Enhancement – inculcates enterprise orientation along the supply chain from farm to market. Includes training programs to establish effective business models to assist participants to think business and profits and not merely productivity
2. Herd Build-up Program– increase local dairy stocks and ensure good animal performance. Supervises animal infusion from importation, compliance with quarantine procedures, distribution and provision of technical services, as well as strengthening of the animal loan program of Quedancor.

In 2005, the NDA implemented a one-month quarantine in Cagayan de Oro for the 646 dairy animals imported from New Zealand under the “Expanded Dairy Program for Rural Enhancement.” Collectively known as “Batch 8”, the animal shipment included 630 pregnant Holstein-Sahiwal heifers, 16 bulls and 5,000 semen straws.

After the quarantine period, the pregnant heifers valued at about P85,000/head (\$1,700/head) were distributed through the NDA-Quedancor animal loan program to qualified farmers. Under the NDA animal loan payment scheme, 50 percent of the value of the animal will be paid under QUEDANCOR financing at 8 percent interest rate per annum and the remaining 50 percent shall be paid-in-kind through NDA. Repayment period for the loaned animals is five years.

The pregnant dairy heifers are expected to calve starting November this year to January 2007. While, the four bulls comprising of two (2) pure Holstein Friesians and two (2) Holstein-Sahiwal will be turned over to the National Artificial Breeding Center in Dalwangan, Malaybalay City that will be used for semen collection and processing.

3. Milk Feeding Program – the NDA Milk Feeding Program (MFP) provides a steady flow of income to local dairy farmers and cooperatives as well as used to address the problem of malnutrition in children. In 2005, the number of MFP beneficiaries

increased by 73 percent from 55,607 to 96,167 children, with Mindanao having the highest number of beneficiaries at 24,796 children, followed by Luzon with 32,692 children and Visayas with 28,678 children.

In 2005, dairy farmers/producers supplied a total of 1.8 million liters of milk to the MFP valued at about P84 million (\$1.68 million), including recombined milk for the NDA's Milk Feeding Program funded by the USDA Section 416(b) grant.

4. Milk Quality – in June 2005, the NDA's Central Milk Testing Laboratory was accredited the Bureau of Food and Drug (BFAD) to conduct testing for milk quality and animal health. Following accreditation, the NDA began charging fees for its laboratory services and milk quality assistance and milk formulation standardization for milk feeding programs.

The NDA Quality Assurance department was also created to disseminate quality standards and closely monitor quality procedures at the milk collection centers, milk plants and distribution points.

Tariffs: In 2004, tariff rates for raw materials such as NFDM and whey were lowered to 1 percent, while the duty for butter, dairy spreads, processed cheeses, yogurt, etc. were either raised or maintained at the 2003 levels. The 2006 MFN tariff rates for dairy and dairy products remain unchanged from previous year.

TARIFF SCHEDULE 2006			
H.S. Code	Description	Rate of Duty	
		MFN	CEPT
0401	Milk and cream, not concentrated nor containing added sugar or other sweetening matter		
0401.10.00	Of a fat content, by weight, not exceeding 1 percent	3	3
0401.20.00	Of a fat content, by weight, exceeding 1 percent but not exceeding 6 percent	3	3
0401.30.00	Of a fat content, by weight, exceeding 6 percent	3	3
0402	Milk and cream, concentrated or containing added sugar or other sweetening matter		
0402.10.00	In powder, granules or other solid forms, of a fat content, by weight, not exceeding 1.5 percent	1	3-5
0402.21.00	In powder, granules or other solid forms, of a fat content, by weight, exceeding 1.5 percent		
	Not containing added sugar or other sweetening matter	1	3-5
0402.29.00	Other	1	3-5
0402.91.00	Other		
	Not containing added sugar or other sweetening matter	5	5
0402.99.00	Other	5	5

0403	Buttermilk, curdled milk and cream, yogurt, kefir and other fermented or acidified milk and cream, whether or not concentrated or containing added sugar or other sweetening matter or flavored or containing added fruit, nuts or cocoa		
0403.10	Yogurt		
0403.10.10	Containing fruits, nuts, cocoa or flavoring matter; liquid yogurt	7	5
0403.10.10	Other	7	5
0403.90	Other		
0403.90.10	Buttermilk	3	3
0403.90.90	Other	7	5
0404	Whey, whether or not concentrated or containing added sugar or other sweetening matter; products consisting of natural milk constituents, whether or not containing added sugar or other sweetening matter, not elsewhere specified or included		
0404.10.00	Whey or modified whey, whether or not concentrated or containing added sugar or other sweetening matter	1	3
0404.90.00	Other	3	3
0405	Butter or other fats and oils derived from milk; dairy spreads		
0405.10.00	Butter	7	5
0405.20.00	Dairy spreads	7	5
0405.90.00	Other	1	0
0406	Cheese or curd		
0406.10.00	Fresh (unripened or uncured) cheese, including whey cheese, and curd	3	0
0406.20	Grated or powdered cheese, of all kinds:		
0406.20.10	In containers of gross weight exceeding 20 kgs.	3	0
0406.20.90	Others	7	5
0406.30.00	Processed cheese, not grated or powdered	7	5
0406.40.00	Blue-veined cheese	3	0
0406.90.00	Other cheese	7	5

Source: Tariff and Customs Code 2004

USDA Food For Progress FY 2006 Project: In 2006, Land O' Lakes, Inc. received a Food For Progress grant to conduct a dairy development project in the Philippines. Land O' Lakes Foundation Philippines will implement this project in the country in partnership with NDA and other local NGO partners to establish four new dairy zones. The projects will include dairy animal infusion, installation of processing facilities and technical support, as well as the establishment of a Milk Quality Center.

Milk Code: In May 2006, the Philippine Department of Health issued the Revised Implementing Rules and Regulations of Executive Order No. 51 or the Philippine Milk Code, which promotes and supports breastfeeding. The revised IRRs seek to regulate marketing and advertising and promotional activities of breastmilk substitutes or milk formula for infants and young children up to 24 months of age. Industry representative have aired concerns that the IRRs may pose significant restrictions on the sale and marketing of infant formula. The complete text of the revised IRRs is available at:

<http://home.doh.gov.ph/ao/ao2006-0012.pdf>

Marketing

It is reported that Nestle plans to invest P10 billion (\$200 million) in the Philippines over the next five years. In 2005, the company invested P2.2 billion (\$44 million) in new production facilities in Cabuyao, Laguna, Cagayan de Oro and in Lipa City comprising the Nestle Group's ASEAN Supply Center for infant nutrition, filled milk powder and breakfast cereals.

In 2005, new brands of milk that became prominent in supermarkets include UHT Pura Milk in tetrapaks from National Foods of Australia, which was acquired by San Miguel Corporation, the largest Philippine food and agribusiness company, and the Amul brand of UHT milk from India. Likewise, Dairygold Milk from the United States in gable top cartons is also sold in supermarkets at premium prices of about P120/liter.

A new UHT processing plant started operation in Trece Martirez, Cavite in August 2005. Additionally, four fresh milk processing plants were established during the year in Negros Occidental, Zamboanga del Norte and Siquijor under the auspices of the National Dairy Authority. Three private sector processors also started the installation of fresh milk processing plants in the following areas: Zambales, Camarines Sur and Lanao del Norte.

PSD Table									
Country	Philippines								
Commodity	Dairy, Milk, Nonfat Dry⁴						(1000 MT)		
	2005	Revised	New	2006	Estimate	New	2007	Forecast	New
	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate
Market Year Begin		01/2005	01/2005		01/2006	01/2006		01/2007	01/2007
Beginning Stocks	2	2	12	2	2	7	2	2	3
Production	0	0	0	0	0	0	0	0	0
Other Imports	130	130	87	135	135	90	0	0	98
Total Imports	130	130	87	135	135	90	0	0	98
Total Supply	132	132	99	137	137	97	2	2	101
Other Exports	18	18	18	20	20	18	0	0	20
Total Exports	18	18	18	20	20	18	0	0	20
Human Dom. Consumption	112	112	74	115	115	76	0	0	79
Other Use, Losses	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	112	112	74	115	115	76	0	0	79
Total Use	130	130	92	135	135	94	0	0	99
Ending Stocks	2	2	7	2	2	3	0	0	2
Total Distribution	132	132	99	137	137	97	0	0	101
CY Imp. from U.S.	22	22	22	22	22	20	0	0	20
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0

⁴ Beginning stocks in 2005 were adjusted upwards to reflect lower consumption of NFDM estimated at 94,000 MT in 2004 as a result of lower domestic demand for dairy products.

PSD Table									
Country	Philippines								
Commodity	Dairy, Dry Whole Milk Powder⁵								
	2005	Revised	New	2006	Estimate	New	2007	Forecast	
	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		01/2005	01/2005		01/2006	01/2006		01/2007	01/2007
Beginning Stocks	0	0	6	0	0	0	0	0	0
Production	0	0	0	0	0	0	0	0	0
Other Imports	48	48	35	52	52	45	0	0	50
Total Imports	48	48	35	52	52	45	0	0	50
Total Supply	48	48	41	52	52	45	0	0	50
Other Exports	30	30	26	34	34	29	0	0	32
Total Exports	30	30	26	34	34	29	0	0	32
Human Dom. Consumption	18	18	15	18	18	16	0	0	18
Other Use, Losses	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	18	18	15	18	18	16	0	0	18
Total Use	48	48	41	52	52	45	0	0	50
Ending Stocks	0	0	0	0	0	0	0	0	0
Total Distribution	48	48	41	52	52	45	0	0	50
CY Imp. from U.S.	1	1	1	1	1	1	0	0	1
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0

⁵ Higher beginning stock in 2005 is a result of an adjustment in 2004 WMP imports from 45,000 MT to 51,000 MT.

PSD Table									
Country	Philippines								
Commodity	Dairy, Milk, Fluid						(1000 HEAD) (1000 MT)		
	2005	Revised	New	2006	Estimate	New	2007	Forecast	
	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		01/2005	01/2005		01/2006	01/2006		01/2007	01/2007
Cows In Milk	12	11	12	12	0	12	0	0	0
Cows Milk Production	13	13	13	15	15	14	0	0	15
Other Milk Production	3	3	3	3	3	3	0	0	3
Total Production	16	16	16	18	18	17	0	0	18
Other Imports	45	45	49	45	45	51	0	0	53
Total Imports	45	45	49	45	45	51	0	0	53
Total Supply	61	61	65	63	63	68	0	0	71
Other Exports	0	0	0	0	0	0	0	0	0
Total Exports	0	0	0	0	0	0	0	0	0
Fluid Use Dom. Consum.	56	56	60	58	58	63	0	0	66
Factory Use Consum.	5	5	5	5	5	5	0	0	5
Feed Use Dom. Consum.	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	61	61	65	63	63	68	0	0	71
Total Distribution	61	61	65	63	63	68	0	0	71
CY Imp. from U.S.	0	0	0	0	0	0	0	0	0
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0

PSD Table									
Country	Philippines								
Commodity	Dairy, Cheese								
	2005	Revised	New	2006	Estimate	New	(1000 MT)		
	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		01/2005	01/2005		01/2006	01/2006		01/2007	01/2007
Beginning Stocks	0	0	0	0	0	0	0	0	0
Production	2	2	2	2	2	2	0	0	2
Other Imports	7	7	5	9	9	6	0	0	7
Total Imports	7	7	5	9	9	6	0	0	7
Total Supply	9	9	7	11	11	8	0	0	9
Other Exports	0	0	0	0	0	0	0	0	0
Total Exports	0	0	0	0	0	0	0	0	0
Human Dom. Consumption	9	9	7	11	11	8	0	0	9
Other Use, Losses	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	9	9	7	11	11	8	0	0	9
Total Use	9	9	7	11	11	8	0	0	9
Ending Stocks	0	0	0	0	0	0	0	0	0
Total Distribution	9	9	7	11	11	8	0	0	9
CY Imp. from U.S.	0	0	0	0	0	0	0	0	0
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0