

Brexit Delay Releases Stocks

European cheese markets have been trading well below their world counterparts. In fact, European Cheddar and Gouda prices have been lower than they were in the summer months of the past few years. Unlike in the United States, where better demand prospects and moderating stocks levels are translating into higher prices, some EU cheese prices have been steadily declining since spring.



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According to news reports, companies have stockpiled cheese spurred by concerns over a “no-deal” Brexit. Last November, the *Guardian* reported that Irish cheese makers were storing Cheddar in the United Kingdom to avoid a potential 42% tariff in the event of a no-deal scenario. When the Brexit target date was pushed to Oct. 31, those holding cheese needed to deplete their stockpiles, which likely displaced some fresh cheese for immediate needs. That coincided with the decline in EU cheese prices. The buildup and subsequent depletion of stocks along with what appears to be softer demand could

provide some insight into why EU-28 Cheddar and Gouda prices have been on the decline since early spring.

Between February 2017 and March 2019, weekly European Cheddar cheese prices, on a currency-adjusted basis, maintained a premium to CME Cheddar block prices, likely providing U.S. exporters with an advantage in world markets. For the week ending Aug. 18, EU-28 Cheddar prices were \$1.53/lb., or 9.9% less than the same week in 2018 and 13.8% lower than in 2017. By comparison, the CME block price averaged \$1.88 for the same week, or 35 cents higher than EU prices. The significant price gap was the result of swelling inventories caused by both slower demand and the release of stocks

after the Brexit target date was delayed.

In its July short-term outlook, the European Commission forecast that EU-28 cheese production this year would exceed the prior year by 1%. Through midyear, cheese output was tracking near that level at 0.7% higher than the equivalent period a year earlier. The same report expected exports to better last year by 3%. Through

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Ken's Corner

*by Ken Meyers
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Markets are certainly never stagnant. Just when the EU-28 is close to eliminating its once humongous stockpile of skim milk powder, the pending withdrawal of the United Kingdom from the European Union has convinced some European cheese makers to

stockpile cheese rather than pay large tariffs on future sales if a no-deal Brexit were to occur. Manufacturers fear—and rightfully so—that retail sales could plummet if the additional costs were to be passed on to consumers.

This week, after opposition Members of Parliament began devising legislative strategies to prevent a no-deal Brexit from occurring, UK Prime Minister Boris Johnson sought and received permission from Queen Elizabeth to suspend Parliament. This type of wrangling over whether Brexit will or will not occur—with or without a deal—will continue to impact markets, including dairy. For now, EU cheese prices will likely continue to be weak until overall inventories decline and Brexit is settled.

These types of quirks, or market hiccups, occur from time to time, and often spread to international markets. The rapid devaluing of EU cheese, particularly Cheddar, these past several months could become a bit of a weight on U.S. cheese prices. **MCT**

Cheese and Butter Prices Diverge

This summer, cheese prices in the United States, as opposed to those in Europe, have reached multi-year highs driven by low stocks and healthy

demand. While CME block prices have retreated from the highs set in early August, they are still 35 cents more than EU-28 Cheddar prices. U.S. cheese holdings

in July fell 3.5% below prior-year levels, marking the largest decline between June and July on record. Strong internal demand could make it more challenging for U.S. exporters in second-half 2019 and well into 2020. Expanding butter stocks, meanwhile, sent CME spot butter prices to their lowest levels of the year in late August. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Aug	1.8725	1.7100	17.60	2.3175	16.55	0.3675	1.0350
Sep	1.9275	1.7300	17.88	2.3525	16.77	0.3625	1.0450
Oct	1.8700	1.7025	17.87	2.3375	16.91	0.3600	1.0675
Nov	1.8425	1.6925	17.53	2.3125	16.97	0.3600	1.0875
Dec	1.7975	1.6975	17.35	2.2900	16.98	0.3575	1.1000
Jan	1.7425	1.6200	16.92	2.2625	16.95	0.3650	1.1100

* CME prices.

**NASS prices.

...EU cheese market pretty much in balance

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June, EU-28 exports fell short of these expectations, only bettering the prior year by 1.1%. Exports that were less than expected likely resulted from first-quarter 2019 EU cheese prices that were higher than equivalent U.S. prices.

However, given the price downturn since spring and summer, European cheese exporters could make up lost sales in the second half of this year. But cheese imports are also expected to be higher. Through midyear, EU-28 cheese imports were 3% greater than the same period last year, when they were expected to be unchanged, but imports reflect only 0.5% of the European Union's annual domestic use. Based on this information, production and trade data suggest that European cheese markets are close to being in balance and thus an imbalance does not explain the current devaluation in the region's cheese markets.

Stocks, and ultimately sluggish internal demand, provide a glimpse into why EU-28 cheese prices are lower than last year and showing few, if any, signs

of a significant price increase anytime soon. While the short-term outlook predicts EU-28 cheese stocks could decrease by 40,000 metric tons (MT) compared to last year, early data show that a decline that large could be an insurmountable feat this year. The June 2019 Milk Observatory reported EU cheese stocks above 400,000 MT at the end of April—about 5-7% more than the same period a year earlier—confirmation that some companies could be holding more inventory due to Brexit fears. In most years, EU-28 stocks build in the summer. Given the European Commission expects internal EU consumption to expand by only 0.5% this year, exports or regional demand would need to exceed current expectations to keep stocks from building further.

The Oct. 31 Brexit deadline has companies, once again, accumulating surpluses to avoid disruption should a no-deal scenario occur. In early August, Fox Business reported that companies like Domino's were increasing inventories ahead of this fall's Brexit deadline. While a no-deal Brexit would have a severe impact on global markets, postponing Brexit would continue to plague EU-28 cheese markets this winter. **MCT**



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