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MCTCOMPASS

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Will the Slumbering Dragon Stir?

What will it take for China to resume robust buying in dairy markets? For starters, China's central government is taking the most significant steps since Covid-19 lockdowns began to move the nation toward a new normal that is less restrictive than tthe last three years. Despite a very bumpy start, China recently relaxed travel quarantines and contact tracking to jumpstart the economy. That is welcome news for a global dairy industry that has been fretting about when China will resume its previous level of imports.

> *While global milk supplies have declined, falling demand from China has been even greater.*

The lingering impact of fewer imports from China makes global markets appear to be in surplus despite lagging milk supplies for much of the year. While global supplies have declined, falling demand from China has been even greater. Through October, China's whole milk powder (WMP) imports were 15.9% less than the comparable period last year. October WMP imports underperformed their five-year average as China continued to work through domestic stockpiles. Butterfat imports were 4.6% ahead of last year, the most substantial so far of all dairy product imports this year. While cheese import volumes were down 16% versus the prior year, they were still the second highest on record as demand picked up in September and October. Skim milk powder (SMP) imports through October were 25% less than last year but still the third highest behind 2021 and 2019. Whey imports lagged the previous year by 23% but have improved since August. That leaves market participants trying to guess whether the improvement is only temporary or whether China has started to resume its once buoyant buying.

While widespread lockdowns eroded demand and disrupted the supply chain earlier this year, there has been more to the story. Over the last two years, China added approximately 300 dairies and nearly 2 million dairy cows.

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Ken's Corner

by Ken Meyers
President, MCT Dairies Inc.

In many ways it's as if China is still in the beginning throes of the Covid-19 pandemic. As Americans resume their enjoyment of life by taking part in large gatherings, flying to overseas destinations, and joining friends for dinner and a night on the town, workers in China are ripping down barriers that prevent them from entering their workplaces, and protests against Covid restrictions are erupting in major cities.

With the Chinese government still trying to contain what most countries have realized is an uncontainable virus, China's goal of achieving 5.5% economic growth this year is increasingly unlikely. The country's annualized growth in gross domestic product (GDP) only hit 3.9% in the third quarter after falling 0.4% in second quarter. First quarter GDP growth was the strongest at 4.8%.

In its recent forecast, Goldman Sachs predicted that China's 2023 will accelerate from an estimated 3% this year to 4.5% next year. But the first half of 2023 could be rougher than the government has indicated. The country's eventual exit from its zero-Covid policy could lead to negative growth as cases inevitably explode. Then as people recover and finally resume much more normal lives, economic growth could rise above 5%. **MCT**

Smooth Post-Holiday Sailing

After the long Thanksgiving trading holiday, markets opened much as they had closed. Spot blocks are trending lower at a slower pace. Mid-November the block-barrel spread widened out with blocks holding a 36.2¢ spread the last full-week of trading. Butter prices remain the highest in the world with CME over $1.90/lb. Still, futures herald at least a 30-cent price correction lower between November and December. NDM markets continue a slow slide lower. Global prices converged and demand remains positive, but prices, absent China have been prone to weakness this fall. At the same time, domestic demand remains resilient and capable of keeping stocks in check. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Nov	2.1075	1.9525	20.38	2.8650	22.94	0.4750	1.5025
Dec	2.0100	1.8500	19.28	2.5750	21.08	0.4750	1.4300
Jan	1.9800	1.8325	19.05	2.5000	20.42	0.4775	1.3900
Feb	1.9400	1.8275	18.83	2.4625	20.39	0.4800	1.4050
Mar	1.9900	1.9350	19.63	2.5025	20.63	0.4850	1.4150
Apr	1.9800	1.9450	19.66	2.4400	20.62	0.4950	1.4425

** CME prices.*
***NASS prices.*

...new supplies collide with demand slowdown

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Consistent with decades of policy, China has been steadfast in its commitment to becoming self-sustaining in dairy. So far, while the nation has fallen short of its annual goals, domestic output has kept pace with rising demand, ensuring that local dairy products supply a significant portion of the country's needs. Seldom do new capacity and demand coincide to make for seamless startups, though, and that was also the case this year. As more dairies and new milk became available to the Chinese market, demand erosion resulting from the nation's zero-Covid policy collided with new supply. Rather than build massive stockpiles of dairy products, buyers slowed imports to balance the domestic market, a strategy that will have ongoing implications because China will need fewer imports until demand returns.

Reports from China suggest that the Lunar New Year and spring festival holidays could be more significant than in the last three years, which should buoy demand for dairy products. That news lifted markets after sizeable resets earlier this fall. But Covid-19 couldn't care less about government policy or people's plans. On November 22, China announced 28,000 new Covid cases, including those in Beijing, the most in a single day since April 13. Vaccination rates in China have lagged those in other nations, leaving the government to continue to rely on its strict zero-Covid policy. Recent lockdowns that encompass the capital have once again unnerved markets that were hopeful that China's recent shift away from focusing on Covid restrictions toward refocusing on its economy would help drive growth and demand. China's year-over-year import shortfalls could lessen in 2023. Since dairy producers have been tentative about expanding the milk supply, a surplus could remain modest and manageable unlike the glut of milk and dairy products that followed China's boom-and-bust import cycle of 2014 and early 2015. If the last three years are any indication, Covid-19 could relent again in summer, but lack of a vaccination policy or alternative ways to manage the spread of the virus outside of lockdowns, could mean China continues to struggle for a fourth consecutive year. Global dairy markets, meanwhile, will continue to search for other markets to backfill missing demand from China until the dragon returns. **MCT**

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