

Demand Stands at a Crossroad

A few months ago, milk and dairy product prices were soaring as products remained scarce and milk production lagged previous-year levels. That sent autumn's CME butter prices to new highs. While cheese, nonfat dry milk (NFD), and whey prices fell



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short of all-time highs, they were significantly more expensive than in recent years. The price increases were remarkable given lackluster demand from China and decades-high inflation that slowed demand by early summer. But then as inflation moderated in late summer and early autumn, demand ramped up as consumers returned to dining out and travelling more. International demand for U.S. dairy products roared back. However, by the end of last year, signs pointed to a sputtering recovery. Consumer spending and dining out slowed at the same time milk production began to inch higher. Despite higher milk prices, dairy producers were slow to add cows and increase output, making the current situation unusual. Significantly

higher supplies didn't cause the 2023 price correction. Instead, an absence of demand has been pushing prices lower.

Last year, milk production from Oceania, the EU-27, Argentina, Brazil, and the United States fell short of 2021 by 0.8%, based on preliminary data. While 2022 got off to a plodding start, milk production from these regions began to move higher by September, with aggregate output between 0.2% and 0.5% greater than in 2021. Today, all signs suggest milk production is continuing to increase, with January milk output in New Zealand and the United States up 1.2% and 1.3%, respectively, compared to last year. Anecdotal reports indicate that the European milk supply is besting last year's by similar levels. By

most measures, these increases are modest, especially following record-high global milk prices. However, markets appear to have swung from deficit to surplus quickly, which is puzzling given the slight uptick in output. Unlike after many past price runs, milk production gains have not overwhelmed markets. Instead, fading demand has caused current supplies to exceed levels needed to

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Ken's Corner

*by Ken Meyers
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The pandemic and its aftereffects continue to dog the dairy industry. Three years after the start of Covid, global consumers continue to feel the brunt of overexuberant government spending during the worst of the pandemic as they

wait for inflation's bite to moderate.

A segment of the global population has yet to travel, and some people have still not ventured into restaurants. Nearly half (48%) of the people in China are still unwilling to travel, according to ING Research. These accumulating demand losses continue to pile up. China's drop in WMP imports last year, for instance, resulted in a phenomenal amount of excess milk. In fact, the decline in New Zealand's WMP sales to China in 2022 was the equivalent of a 15% increase in New Zealand milk production. That's a lot of milk to move.

Until the largest dairy-consuming regions of the world are confident better times lie ahead, demand will continue to falter. There are hopeful signs. EU consumer confidence recently hit a one-year high as energy prices subsided. Last week, officials in China announced the country's Covid pandemic had ended, and the U.S. labor market continues to be historically strong. If consumers are confident they'll keep their jobs, they will continue to spend. **MCT**

Markets Optimistic Despite Cracks

The market remains optimistic about dairy demand later this year, despite reports of growing milk production

and stocks. Dairy product prices rebounded from last month's lows, but the CME block-barrel price spread

remains wide. CME spot and futures butter prices continue to be the highest in the world, which could reverse trade sentiment within the next few weeks. This year's NFDM futures prices range from the low-\$1.20s to the mid-\$1.30s. A decline in the Global Dairy Trade index on Feb. 21 could indicate that Chinese buying is still a way off. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Feb	1.8875	1.5725	16.89	2.3925	18.87	0.4075	1.2625
Mar	1.8700	1.5525	16.70	2.3550	18.58	0.4100	1.2475
Apr	1.8625	1.5625	16.70	2.3075	18.29	0.4100	1.2375
May	1.9350	1.7800	18.11	2.3375	18.29	0.4100	1.2225
Jun	1.9900	1.9325	19.12	2.3925	18.78	0.4075	1.2525
Jul	2.0775	1.9375	19.59	2.4550	19.13	0.4050	1.2625

* CME prices.

**NASS prices.

...China output climbs as domestic demand slows

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satiate markets.

Last year, China increased milk production by 7% compared to 2021, and Mexico grew output by 2%, according to preliminary data. China's prolonged and widespread Covid-19 lockdowns have destroyed some demand, which along with growing internal milk production has led to more domestic output of whole milk powder (WMP) and higher stock levels. As a result, China's WMP imports dropped 17% in 2022 vs. 2021, marking the third time over the past 10 years that year-over-year imports have declined. SMP imports did not fare much better, with volumes down 21% in 2022 compared to 2021. Although China produces far less SMP internally, the country's lack of imports displaced a substantial amount of milk powder. China's combined drop in SMP and WMP imports equated to 5 billion pounds of milk equivalent that needed to find a new market last year. Unlike China, though, Mexico imported 9.8% more NFDM through November 2022 than it did in 2021, likely due to a resurgence in tourism.

That leaves dairy markets at an interesting

crossroad. Will the industry maintain current milk supply levels in the hope that demand returns by the end of the year, or will it curb output to stem further price losses, recalibrating supply to meet current demand while acknowledging that if demand returns later this year, it could take time for supplies to rebuild. Conflicting macroeconomic data has not been much help in determining where markets will go from here. Companies are issuing earnings warnings for 2023 because they expect consumers to spend less. At the same time, January's advanced consumer spending estimates jumped 3% over the previous month, a much larger gain than analysts had expected. Within that figure, estimated spending at foodservice and drinking places surged 7.2%.

For now, dairy producers and processors seem to be somewhat optimistic about demand and are thus staying the course on milk supply. If they are correct, prices could moderate this spring and recover as demand returns later this year, avoiding the pitfalls of extremely high and low prices. If they are wrong, stocks could build, and prices might need to correct significantly lower to clear markets. **MCT**



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