Horizons.

Insights on Today's Global Dairy Business by Hoogwegt.

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Market Matters

Supply Chain Disruptions Continue and Worsen

The global supply chain, once taken for granted, remains in disarray. When the COVID pandemic hit in 2020, issues and challenges within the supply chain became evident and then gained prominence over time as the pandemic worsened. While these issues remain, Russia's attack on Ukraine has compounded the problem.

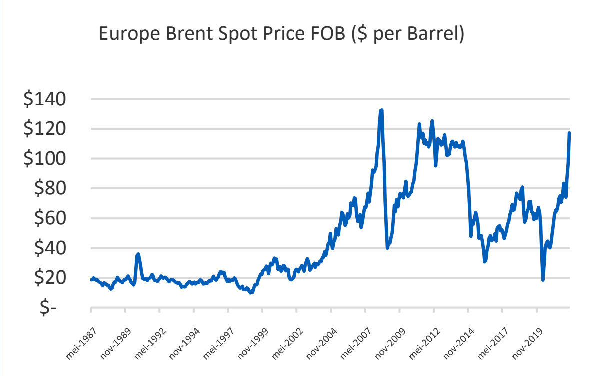
Crude oil prices have been rising since spring 2021, but Russia's war in Ukraine has sent prices spiking even higher, affecting all forms of transportation as well all sectors of the dairy industry. From the beginning to the end of 2021, the average weekly price for diesel fuel increased 37%, and price increases have accelerated. In the United States, the estimated cost for a truck to deadhead, or run empty—a common occurrence—could climb $3,000 per tractor in 2021. Shipping freights have also increased. The average weekly FBX, or global container freight index, has nearly tripled, from $3,452 at the start of 2021 to $9,488 by mid-March.

Demand for consumer goods, especially from the United States, rose sharply during the pandemic, and while these products remain in high demand, rising fuel prices are making it less economical for companies to ship empty containers back to Asia for quick reload. That has helped to work down the backload at ports, but severe labor shortages persist.

The Impact of Sanctions and COVID

Russia's ongoing attack on Ukraine is expected to worsen challenges in the supply chain. Russia produces 11% of the world's crude oil and accounts for 24% of its natural gas reserves. The combination of sanctions and/or the unwillingness of buyers to source product from Russia are expected to further support prices as well as shift flows of oil and gas, impacting every level of the global supply chain.

The West's sanctions on Russia will also put upward pressure on already lofty fertilizer prices, as the ongoing invasion prevents Ukrainian farmers from planting most of the country's spring crops and exporters from moving current supplies out of the country into world markets. This will further serve to push global grain and oilseed prices higher. For European dairies, which import feed directly from Ukraine, availability could also become an issue.



Source: U.S. Energy Information Administration

New COVID variants, such as Omicron and its subvariant BA.2, continue to pummel the already battered supply chain. Recently, the Chinese government locked down several factory cities, including Shanghai, Shenzhen, and Changchun. With a growing number of factories in China temporarily closed, more shortages and shipping delays are certain. In cities under lockdown, even getting current inventory to airports and container terminals will be nearly impossible.

Read more →

Did You Know?

A new "pop-up" site at the U.S. Port of Oakland, which can pre-cool shipping containers and provides a $125 subsidy per container, could help load empty containers with ag products before shipping them back to Asia.

To reduce reliance on Russian natural gas, Europe has discussed the feasibility of intermittently curtailing natural gas use by milk powder operations, pushing more milk into cheese vats.

Ukraine exports nearly 30% of its ag commodities to Europe and accounts for 47% of the world's exports of sunflower products, 17% of its corn, and 12% of its wheat. It also ranks eighth in soybean production.

Hoogwegt Forecast.

	U.S. Average Prices			EU Average Prices			Oceania Average Prices		
	$/ton	$/lb	Trend	$/ton	$/lb	Trend	$/ton	$/lb	Trend
SMP	3.970	1,80	Weak	4.300	1,95	Weak	4.400	2,00	Weak
FCMP/WMP	4.850	2,20	Firm	5.600	2,54	Stable	4.100	1,86	Weak
Butter	6.605	3,00	Stable	7.700	3,49	Stable	6.650	3,02	Stable
Cheddar	5.180	2,35	Firm	5.900	2,68	Firm	6.185	2,81	Weak
SWP	1590	0,72	Weak	1.700	0,77	Weak			
Lactose	970	0,44	Stable						

U.S. prices stated ex-works/including expected CWT subsidy where applicable; world prices stated FOB main port; EUR/USD: this week $1,069

World Comment

Scarcity was headlining dairy markets for quite some months but this month starts with the final sentence of our previous edition: Stocked China probably won't break their record high demand from H1 2021 and is fighting the increasing cases of Omicron with lockdowns. Omicron is a different beast that puts zero-covid policies to the test, and currently seem to cause drops in demand to significant supply chain issues. So far this led to a drop of WMP, making WMP cheaper than SMP in the latest GDT results, with AMF still at a high level. Where SMP demand is a bit more diverse, China is the biggest taker of WMP. 40% of the 2021 exported WMP went to China, compared to only 17% of the exported SMP. So, China's impact is bigger on WMP and in particular WMP from NZ. The last time that happened was very early 2015, when milk production had grown fast and Chinese WMP demand was lackluster due to their high stocks. Current WMP/SMP flip is illustrative for the symbiose between China and NZ on WMP. Milk production in Europe, NZ and US still red, including big producers like GE, NL and FR. All while the conflict between agricultural countries Ukraine and Russia remains.

→ Even before the recent lockdowns in China, manufacturers of dairy products were dealing with intermittent packaging and ingredient shortages that affected production and availability of some end products. As if that weren't enough to deal with, cyberattacks have intermittently forced some dairy companies to temporarily shut down global operations for about a week or two at a time. These hacking events have forced companies to reroute milk supplies, causing temporary local milk shortages. Then when the plants come back online, milk flows the other way, further wreaking havoc on the supply chain.

It will take time to repair the battered global supply chain, which amazingly continues to move products to those who need them despite unprecedented challenges.

Bring it Home

Dairy Supply Chain Challenges Persist

Challenges in the global supply chain have been causing major issues for dairy suppliers, especially in the United States. According to the U.S. Dairy Export Council, supply chain challenges in 2021 resulted an estimated $1.5 billion or more in direct costs, reduced value, and lost sales. If supply chain challenges continue, U.S. exporters could lose ground to competitors in highly competitive foreign markets.

Recent reports indicate that the current COVID outbreak in China is again emptying store shelves and disrupting the dairy supply chain. Reports indicate that China is currently drying more whole milk powder due to lower fluid milk demand and the inability to process milk into other products, which could influence markets later this year.

Given today's numerous transportation delays and back-ups combined with inflationary pressures, costs throughout the supply chain are expected to remain elevated or work their way higher. At the farm level, it appears record or near-record milk prices have not yet been high enough to offset soaring costs. In fact, the global slowdown in milk production worsened in January as input costs increased. Together, the United States, Europe, Australia, New Zealand, and Argentina produced 1.8% less milk in January than a year earlier.

Burdened with high raw milk prices and rapidly increasing energy and ingredient costs, manufacturers are now faced with the choice of formulating end-products with less expensive ingredients, raising consumer prices, or shrinking package sizes, known as shrinkflation, when companies hold prices steady but decrease the amount of product consumers get for that price. For instance, less cheese may go into a frozen pizza or packages of shredded cheese could shrink.

In addition, depending on whether the situation deteriorates, fewer choices might be available to consumers and some markets might not be serviced or able to afford more costly dairy products, leading to changes in total demand.

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