AgWest FARM CREDIT

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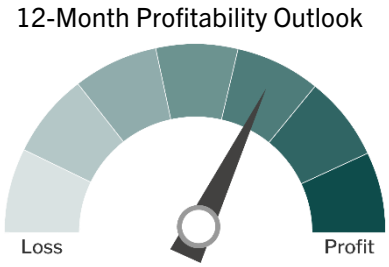
MARKET SNAPSHOT

Dairy

Dec. 31, 2022

Executive summary



AgWest Farm Credit's 12-month dairy profitability outlook suggests slightly profitable returns. Demand will soften as economic uncertainties hinders domestic consumer spending and less international trade places downward pressure on global prices. Dairy margins will be squeezed tighter by weakening milk prices and volatile production expenses.

Industry drivers

Inflated grocery bills shifts US dairy demand

Retail prices increases have impacted demand for dairy products. Prices for dairy and related products rose 15.5% year over year, more than double the average food price increase. Dairy will remain a staple for most American consumers but worsening economic outlooks, dairy supply chain challenges, and tighter grocery budgets will create headwinds for premium dairy products (i.e., branded items or more expensive dairy categories like butter). Consumer have already started to substitute branded dairy products for generic versions. A major grocery retailer survey found that generic brand cream cheese was one of their fastest-growing brands of 2022. Holiday butter sales were down impacted by higher prices as consumers cutback on butter in their holiday dishes. Consumer demand will focus on foods that stretch their dollar the furthest, cost-effective dairy products will fair better in 2023.

Feed costs and expenses uncertainties

Feed costs have been volatile. Each month, the USDA Dairy Margin Coverage program calculates a national feed cost per cwt which peaked at 16.22 per cwt in August and then softening by more than $1 in October. This feed cost number is a national estimate based on a ratio mix including corn, premium alfalfa, and soybean meal. While corn and soybean meal prices have weakened, alfalfa prices have steadily risen each month to a record $348 per ton. For Northwest dairies, hay expenses have eased following drought improvements in 2022, but projected reductions in national hay and grass production due to drought and lower on-farm inventory supports strong hay prices throughout 2023. Production expenses across nearly every category have increased for dairies.

Record milk components

Milk fat has increased throughout 2022 to a record 4.04% monthly milk fat. For the Pacific Northwest Federal Milk Marketing Order, average butterfat tested at 4.59% in November 2022, up 0.4% from a year ago. Increases in milk fat could indicate changes in rations because of higher feed costs or shift in dairy breeds that specialize in higher components. As some Northwest producers do receive bonuses for components which could also be driving a focus on higher milk components.

Chinese dairy demand soften

Chinese dairy demand was a driving force sustaining record dairy prices throughout the summer, but Chinese demand is weakening attributing to softening dairy prices. China is the largest dairy importer in the world, purchasing nearly 4 million tons of dairy products in 2021. While October 2022 exports set a monthly record at 525 million lbs. of dairy products, exports to China were down 18.6% year over year.

Significant headwinds from continued COVID lockdowns, economic challenges, and increased domestic production will hinder Chinese import demand. New Zealand (the largest Chinese trade partner accounting for 70% of WMP imports) saw demand for whole milk powder (WMP) decreased in the summer of 2022 (due to stockpiles being replenished). In turn, New Zealand had less demand for WMP instead using their cream to make butter, addressing some of the country's production deficits and lowering regional prices. The US dairy industry will be hurt by lower imports (specifically fluid milk, WMP, skim milk, butter and cheese which have weaker economic outlooks) and global downward price pressure on dairy products.

Profitability

Strong dairy profits in 2022 enabled dairies to pay down their lines of credit. Producers were concerned with the significant increase in production costs in all expense categories, but high prices offset rises in operating costs. This year, the all-milk price is projected at $22.70, down $2.95 per cwt from the 2022 price. The USDA Class III and Class IV milk are both forecasted lower at $19.80 and $20.10 per cwt, respectively. Milk prices are softening faster than input costs, dairy margins will be squeezed through the year as milk price likely continue to soften.

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Milk Producers Council
www.milkproducerscouncil.org

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