

## Where will SMP prices land in 2023?

In a global dairy market that has been short of milk for some 16 months now, the key question going forward is where SMP prices will find their new price range when milk production starts to grow again. Will we return to the average price range of the pre-pandemic years or have some of the price and cost drivers in supply trade and demand changed in a fundamental way. Just to mention a few of these fundamental price drivers:

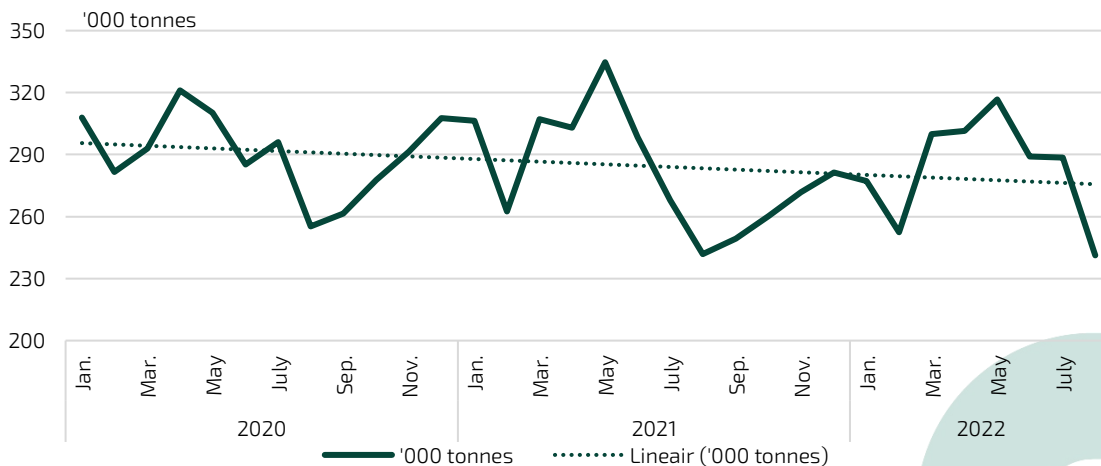
- some of the key SMP production regions are facing sustainability limitations
- to some extent the surplus role of SMP/butter may be shared with Mozzarella
- has China's import demand portfolio changed in 2022?
- will the cost of drying milk and transportation return to a new normal?

In this article Dairyntel will be looking at some of the longer term trends in the SMP market and how these might translate into a new balanced price level going forward.

### Downward trend in production and trade

There has been a downward trend in the production of SMP for some time (figure 1.). Due to the still lagging global milk supply, this is not expected to change in the short term. The only supply region that may have more SMP on offer despite weak milk production is New Zealand. This country does not publish SMP production data but because of the recent weak Chinese demand for its key product WMP, it seems safe to assume that more New Zealand milk will be available for SMP and butter in the upcoming peak months.

Figure 1. Production of SMP by selected countries \*)

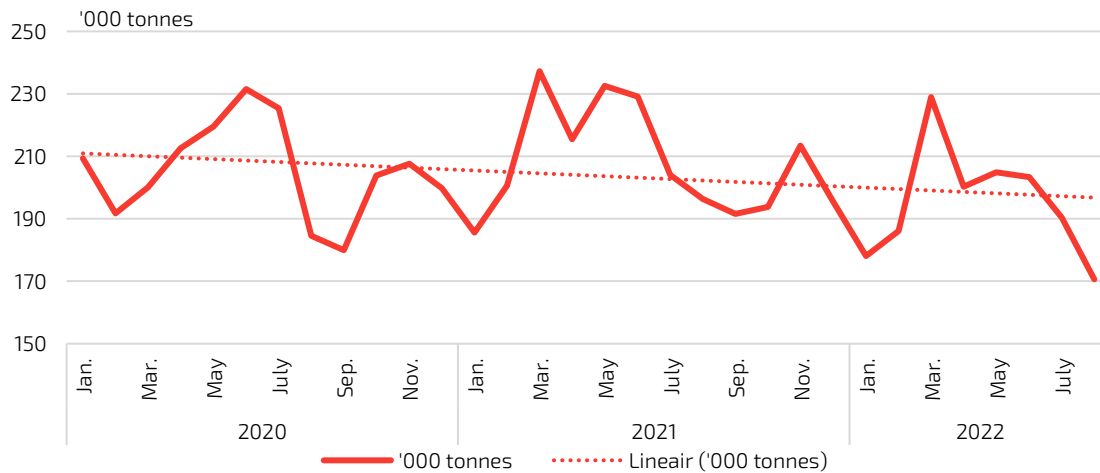


Source: National statistics

\*) Argentina, Australia, Canada, EU-27, New-Zealand (estimates), Switzerland, United States.

At the same time we also see falling volumes in the world trade of SMP (figure 2.). In the recent past, this can partly be explained by uncertainties in the market caused by COVID-19 and the war in the Ukraine. The high price levels also play an important role. As a result of all this, buyers often purchase smaller quantities to cover their needs for the short term.

**Figure 2. World trade in SMP**



Source: Dairyntel trade database

### Impact Mozzarella production in the EU

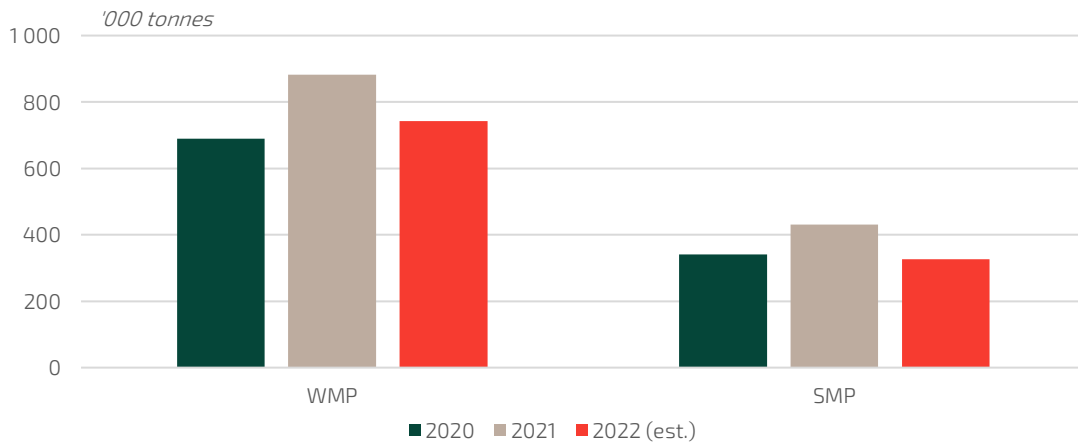
Between 2018 and 2021 some 400 – 450 thousand tonnes of new Mozzarella capacity was built in the EU. Due to the disappointing milk production growth in the EU since 2018 it seems safe to assume that capacity utilisation has not developed according to the investment projections.

Now that we see the initial signs that milk production growth accelerates again in the EU it will be interesting to observe how the new milk volumes will be prioritised in 2023. A better capacity utilisation strongly improves the profitability of the new Mozzarella processing lines. Therefore it cannot be ruled out that Mozzarella will pull some milk away from the SMP dryers. Not in the least because Mozzarella can also function as a temporary milk surplus destination. This could have an upward impact on EU SMP prices going forward as well as EU SMP availability for exports.

### China import portfolio projection 2022 versus 2021

The imports of China have a major – and growing - impact on global trade and the availability of milk powders in particular. China's very strong 2021 import performance more or less swept the dairy market clean towards the end of that year and by doing that initiated the strong surge in prices in 2022. This year – based on import volumes the first 9 months of the year – we may expect import volumes of both WPM and SMP to almost fall back to 2020 levels again (figure 3.). This decrease is partly due to the economic impact of the country's many lockdowns as a result of COVID-19. But this decrease may also be a result of the strong growth in imports that took place in 2021 (which resulted in the build-up of stocks). The question is, is 2022 the new normal or will we see a return to growing import volumes of WMP being required to balance the local Chinese market. One way or another China's import preferences will also become a major factor in the future price levels of SMP, especially if WMP's dominant role in the portfolio will diminish and the preference for SMP continues to strengthen.

Figure 3. China (Hong Kong included) imports of WMP and SMP

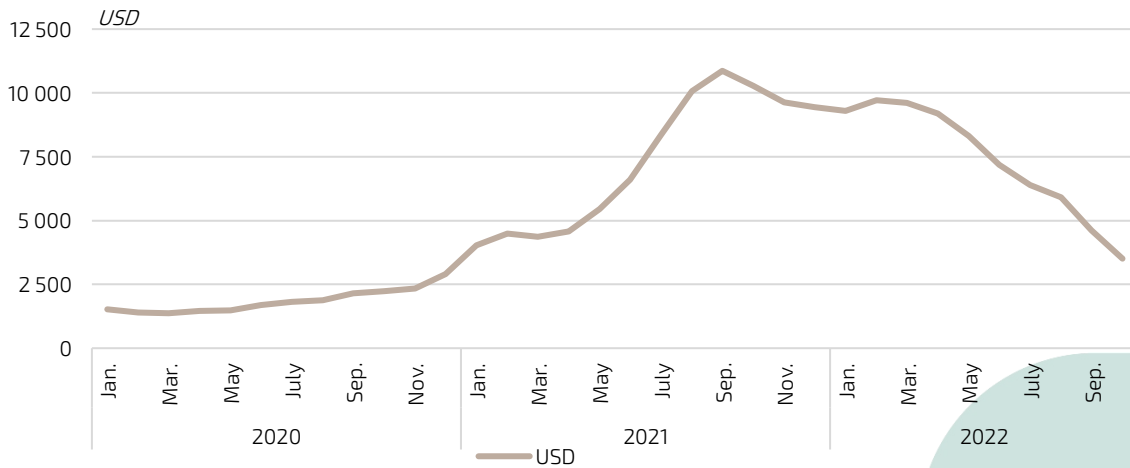


Source: Dairyntel trade database

### Extraordinary price development for energy and freight

Since April 2022 the overall global container volumes declines. This also reduces the costs for overseas transport (figure 4.). It is expected that traders will pass on these lower costs to buyers to some extent.

Figure 4. Price development of global container freight (40 ft sea containers)

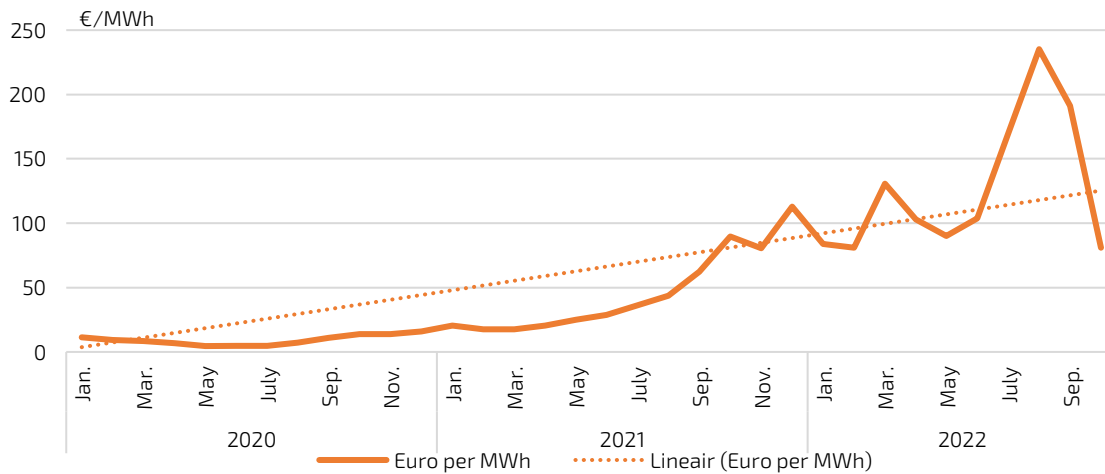


Source: Freight Rate Index / Freightos Baltic Container Index

On the other hand, the continuing uncertainty in the market about the availability of energy in the coming winter (particularly in Europe) could still lead to high gas prices (figure 5.) and therefore high processing costs.

In the United States, this energy problem plays a more limited role. This creates a competitive advantage for US manufacturers on the world market, assuming sufficient milk supply and stock levels and absence of logistical problems.

Figure 5. Gas price development (Dutch TTF)



Source: Dutch TTF (Dutch (virtual) trading place for gas)

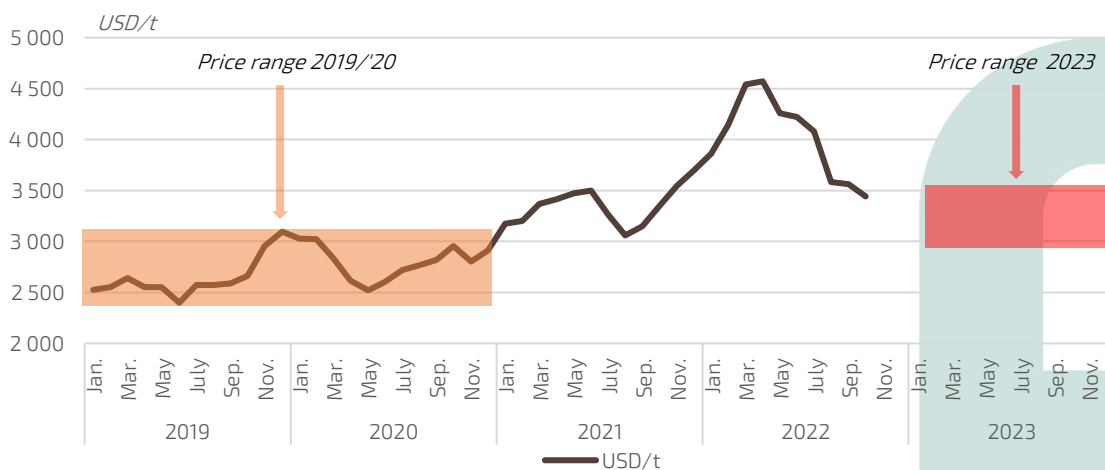
### SMP prices remain above historical average

Since the second half of 2020 SMP prices have appreciated consistently (figure 6). The high prices are therefore not only the result of the war in Ukraine that started in February 2022, but were already driven upwards by a combination of minimal stock levels in the EU, rising energy/freight costs and other uncertainties related to lockdowns during the pandemic.

Recent market developments suggest that we have come to the end of these high price levels for SMP. The reasons for this are gradual return to growth for worldwide milk supply, a serious drop in demand in major export destinations in Africa and Asia due to growing resistance to the increased prices and negative economic developments.

A further downward correction can most likely not be avoided in early 2023. Negative market sentiment could lead to overshooting the target range on the downside, but it is likely that this will be followed by a positive market correction and ultimately a development above the historical average for a longer period of time.

Figure 6. SMP prices (Oceania, USD/t)



Source: Dairy World, ZMB

*If you are interested in our in-depth market insights or data underlying this analysis, please feel free to [contact us](#).*