


BULLETIN #1



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DAIRY EXPORTS DURING THE WAR

Special information bulletin produced by Infagro analytical agency in the frame of the set of expert discussions for dairy exports support and promotion during the war

May 18, 2022

General trends

General tendencies

It is the third month since the beginning of the war, but of course, it is impossible to get used to it. However, with the first victories of the Armed Forces, after the orcs' fleeing from the forests of Kyiv and northern Ukraine, there appeared a stable optimism about the imminent victory.

After the extremely critical March, the situation in the country's dairy industry has significantly improved. Production of milk and dairy products continues to grow, trade is doing better, the personnel crisis has somewhat eased, and logistic routs are gradually recovering. Even for export it is possible to sell more products.

Despite some positive changes, there are still many unresolved issues in the industry, and also new ones are emerging. Thus, production of milk and dairy products this year will certainly decline, and imports will be lower. There have even been concerns from the government about whether there will be enough dairy products to ensure the country's food security, whether they should be removed from the category of critical imports, or whether exports are needed. The answer should be given at once: everything will suffice, export is simply necessary.

Due to the forced migration, Ukraine's population has shrunk significantly, and the solvency of Ukrainians who remain in Ukraine has declined markedly during the war. That is, the total consumption of dairy products in Ukraine in 2022 will significantly decrease. There will definitely be "excess" milk to be used for production of dairy products aimed

at export. Otherwise, dairy processors will be forced to either cut purchase of certain amounts of milk or significantly reduce milk prices. Therefore, exports are extremely important for a normal milk balance.

According to preliminary forecasts of Infagro, in 2022 in Ukraine for the needs of exports may remain about 500 thousand tons of milk, or 17% of the total supply of raw milk for industrial processing. Moreover, even if this "surplus" milk did not exist, exports would be still necessary for the proper functioning of the industry. For example, theoretically Ukraine is capable to consume the produced butter or cheese, but when they are produced, some by-products appear, and their consumption in the country is limited. These are primarily skimmed milk powder, casein and whey powder.

There are some changes seen in the recovery of dairy exports, but its indicators are still far from those of previous years. There is something to sell, but no way to do it. In early April, officials said that everything had been agreed with Europe - veterinary permits, transit of our transport through the EU and arrangement of rail transport. But a lot of problems are not solved, sales are still low. Most of the shipped goods are exported directly to the EU or neighboring Moldova. There are still big problems to transit our dairy products through Europe to traditional importing countries. Only a few logistic companies agree to supply their containers to Ukraine, because the war is going on. There are also problems with delivery of available containers to the seaports of Romania, Poland or the Baltics, starting with a week of waiting at border crossings and ending with a long queue to be able to sent goods by rail,

the "Ternopil train".

There is hope that the situation in Ukrainian dairy exports will improve in the near future both due to the development of new logistics routes and due to help of our Western partners. We remind you that the EU will soon remove all customs restrictions on imports of Ukrainian goods for a year term. The same steps were announced by Britain and most recently by Canada.

In the near future it is necessary to solve some of the most pressing problems:

- Improve the mechanism of the simplified permits for crossing the European border and transit through the EU
- Increase the capacity of container traffic through European ports
- Urgently certify Ukrainian producers for the right to supply dairy products to the EU, possibly under a simplified procedure.

Of course, the future of Ukraine depends most on Ukrainian Armed Forces, but the active work of the Ukrainian dairy industry, including exporters, is also extremely important for the imminent victory.

GLORY TO UKRAINE!!!

Key indicators

Milk balance, forecast of 2022 to 2021:

Milk supply for processing > -16%

Domestic market > -22%

Export > -22%

Inflation, Jan-Apr 2022 to Jan-Apr 2021:

Consumer (State Statistics Committee of Ukraine) **+12,7%**

Raw milk (Infagro) **+6,3%**

Commodities (Infagro) **+33%**

Fresh dairy products (Infagro) **+10%**

Self-sufficiency and foreign trade

Unlike last year, when Ukraine had balanced figures for domestic demand and supply, as well as trade parity, this year's balance has changed significantly due to the Russian aggression.

The war in Ukraine led to a general decline in both milk production and needs of the domestic market as a whole.

Consolidated opinion of dairy analysts and relevant associations is that in 2022 the supply of raw milk for processing will reduce to about UAH 2.9 mn tons (± 0.1 mn tons) in terms of baseline fat and protein, which is 16% lower than the relevant figure for 2021.

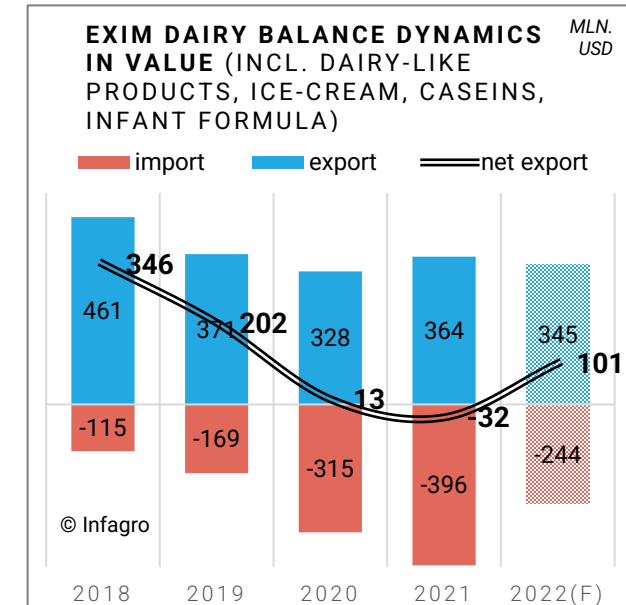
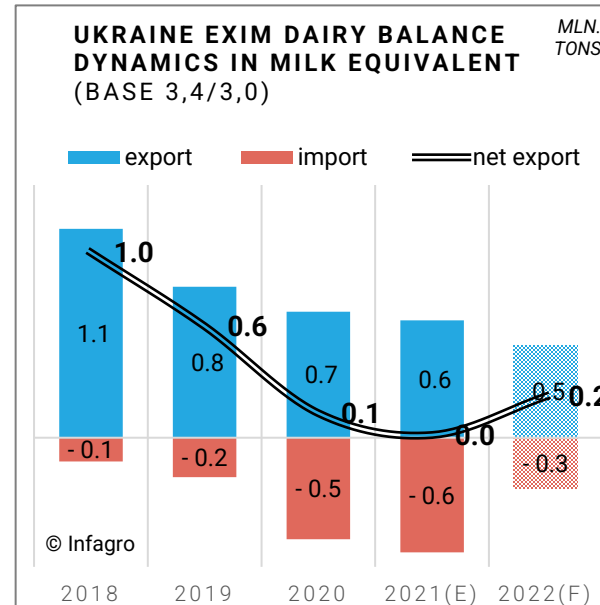
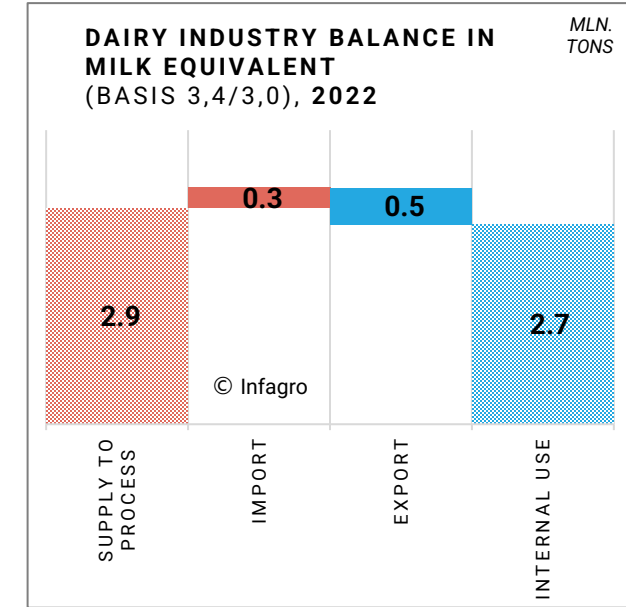
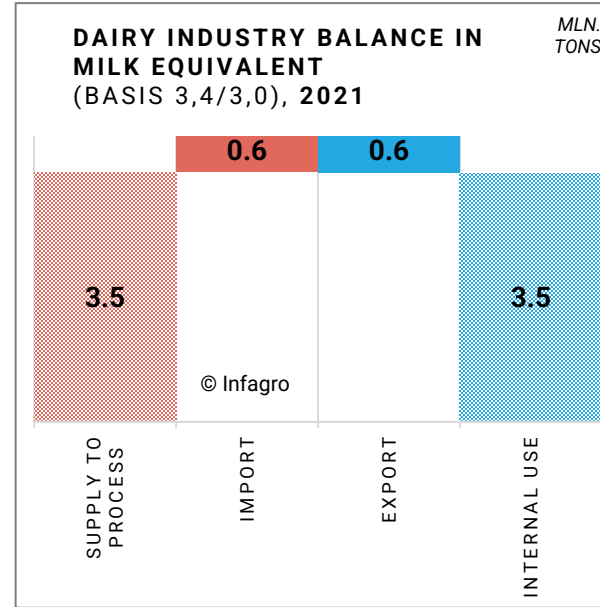
Due to the migration processes and economic downturn, the need of the domestic market (industrial consumption and/or use of milk and dairy products in raw milk equivalent) will be much lower this year. According to current Infagro forecasts, it will fall to 2.7 mn tons, which means the 22% decrease to 2021.

Thus, according to Infagro, by the end of 2022 the level of self-sufficiency of such a dairy market will be above 100% (with a peak of 115% in the second quarter), which means it is necessary to support the dairy industry by applying import restrictions and promoting exports.

The projection of dairy exports is based on actual data for two months of the calendar year, surveys and estimates of the volume and value of foreign trade in March-April, as well as on the balance sheet of dairy products surplus until the end of 2022. Of course, without unlocking export logistics in the second half of the year, the figures for foreign sales in the year may be much more modest.

The calculation of the balance sheet based on current estimates shows a net positive outlook for foreign trade in milk equivalent. Preliminary estimate of net exports for 2022 is UAH 0.2 mn tons.

Regarding the trade balance in monetary terms, there is also a forecast of the net positive statistics recovery. In case the products like technical casein, ice cream and baby food are considered in the trade balance, the net exports can amount to ≈ 100 million US dollars.



Export accents

Even in today's difficult conditions, dairy exports are able not only to support the dairy industry, but also generate support for the national economy by attracting foreign currency earnings at last year's level.

Despite the projection of a decrease in foreign trade of dairy products in raw milk equivalent, exports in monetary terms may remain at last year's level due to the global price situation and changes in share of certain goods in the overall list of Ukrainian export positions.

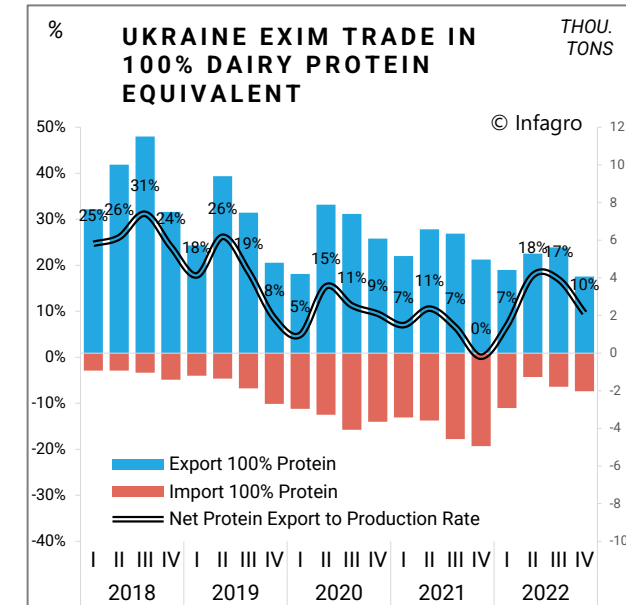
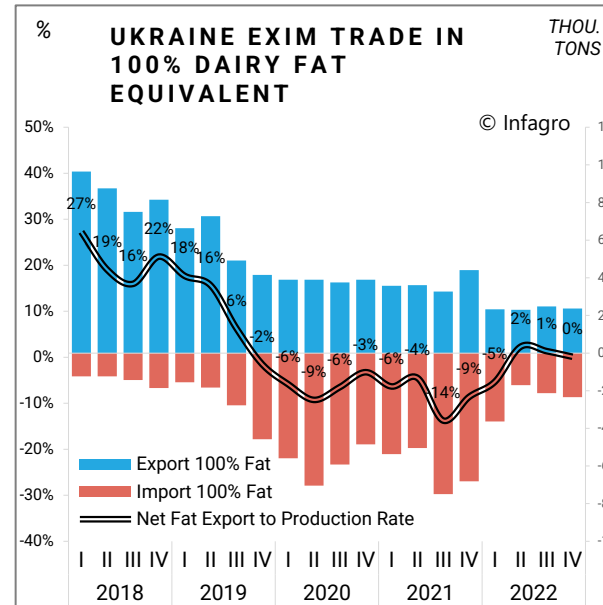
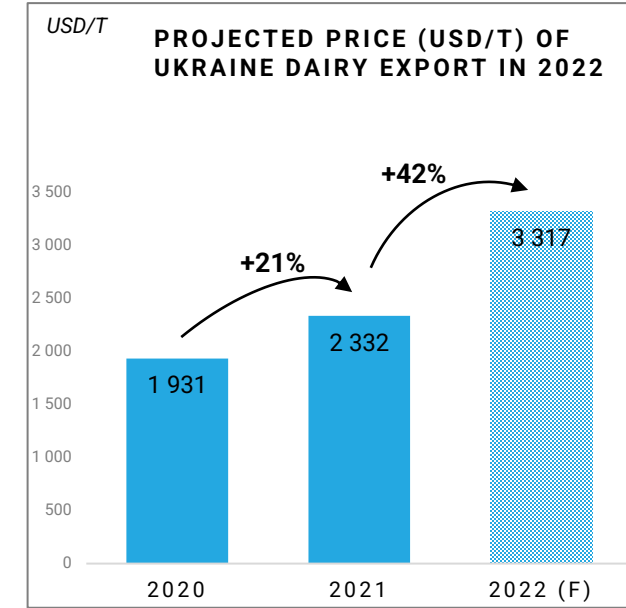
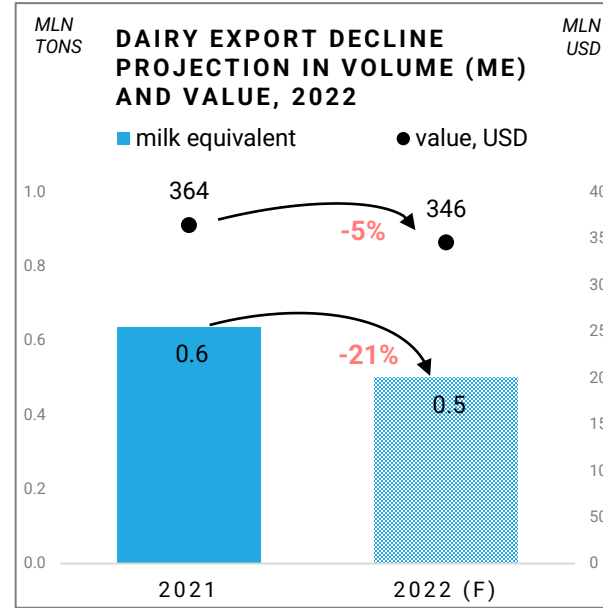
Due to the same factors, the value of a ton of conventional dairy product produced for exports in 2022 may grow by 40% compared to last year. This is due to both global inflation of dairy products and an increase in the share of value-added goods or with a direct concentration of milk in them.

It is also worth remembering that the milk balance, including the trade balance, is not homogeneous and is divided into separate balances of fat and protein. It is the deficit of fat balance in recent years that has led to an increase in imports of butter and cheese to Ukraine. The surplus of protein "supported" dairy exports mainly in the form of sales of skimmed milk powder and whey, technical casein, cheese and canned milk.

Calculations of the current year's balance sheets, with a probable increase in surplus of raw milk, show a turn to the prospects of exports of milk fats, namely butter. That is why the current rejection of critical imports of this product seems a reasonable decision.

Foreign trade and its functioning or restrictions in the second half of 2022 will be determinants for, on the one hand, operation of the Ukrainian dairy industry, and on the other hand - for curb of consumer inflation during martial law.

Therefore, the need for permanent analysis of balance sheets is a necessity for both business and government agencies.



World trends

In April, world prices for dairy commodities seem to have peaked. Following the results of the month, the FAO dairy index reached its maximum since spring 2014.

The April level was 28 percentage points higher than it was last year for the same month.

The main cause of the world milk inflation continues to be the shortage of raw milk in the EU and Oceania, which is also "heated" by restrictions on the supply of vegetable oil - palm oil from Indonesia, sunflower oil from Ukraine. At the same time, in April, world prices began to show adjustments. The main reason for this trend is the decline in China's activity due to quarantine restrictions and blockades of the ports.

The April GDT trade auction showed signs of declining of demand in the region, and the first session in May showed a significant decline in all key commodities. Not only China, but also buyers from Southeast Asia, North Africa and the Middle East have shown caution at the same time.

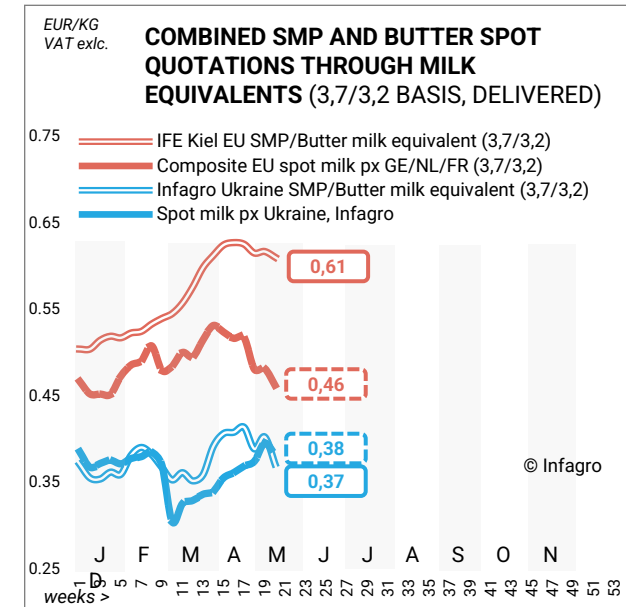
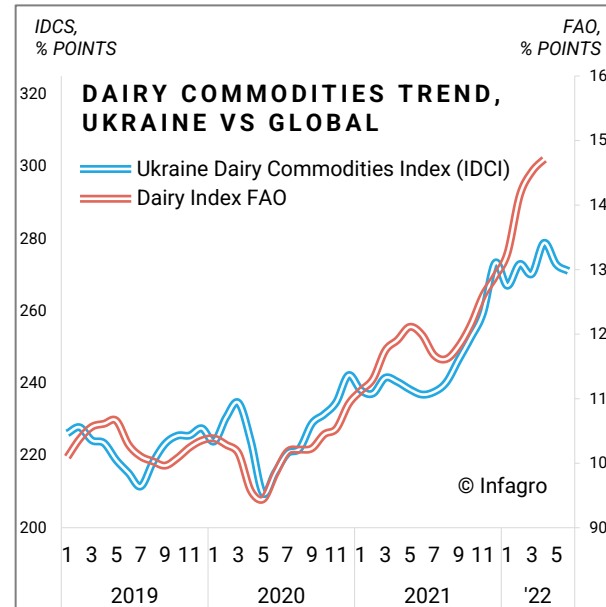
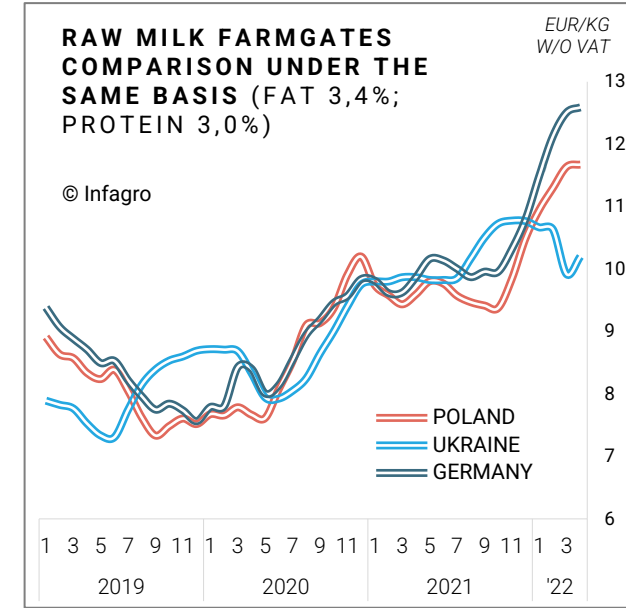
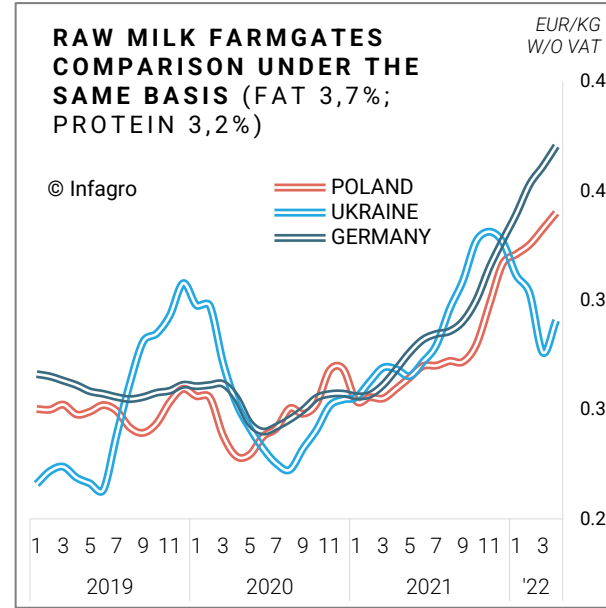
European quotations have also declined quite sharply in recent weeks. The correction was inherent in all products of the spot market, including raw milk.

Comparison of Ukraine and EU prices

Despite the adjusting spot demand in the EU, major commodity contracts continued to grow in April. The value of contracts for the last months in Germany was 0.42 EUR/kg on the basis of 3.7/3.2, the level of the average prices for Poland in the base amounted to 0.39 EUR/kg. The average value of Lithuanian raw milk was estimated at the same level in April.

Although last month in Ukraine prices changed the trend, but looked weak not only compared to EU, but also to their pre-war level: 0.34 EUR/kg on average for agricultural enterprises in the base 3.7/3.2.

The spot prices in the EU are estimated at 0.45-0.55 EUR/kg, which is clearly below the April level, but roughly correspond to the March levels. The value of the secondary market in Ukraine has been moving quite actively and now the difference with the EU is beginning to narrow, but remains significant, amounting to about 20%, as for the main contracts.



Prices of dairy commodities

This year prices of dairy products on the world markets have significantly grown and in April they reached record highs. This factor once again confirms the expediency of Ukrainian dairy exports, at least in the short term.

The war in Ukraine also affected the trend of rising world prices, albeit indirectly. In other words, Ukraine exports relatively few dairy products, but for livestock farmers in many countries around the world, it is a leading exporter of grain and oil feeds, sales of which are now almost blocked.

Thus, the world dairy market cannot but react to the war in Ukraine, but there are other factors of great influence. In May, the cost of dairy products on the world markets unexpectedly and significantly dropped. The reason was not an increase in milk production, but a significant decline in demand from China and other countries in Asia and Africa. It is difficult to predict how significant and long-lasting the fall in prices may be, because the operators did not expect such a fall.

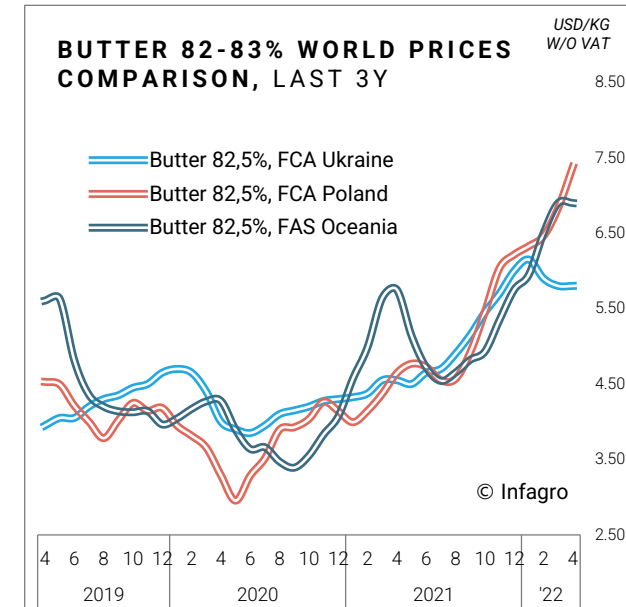
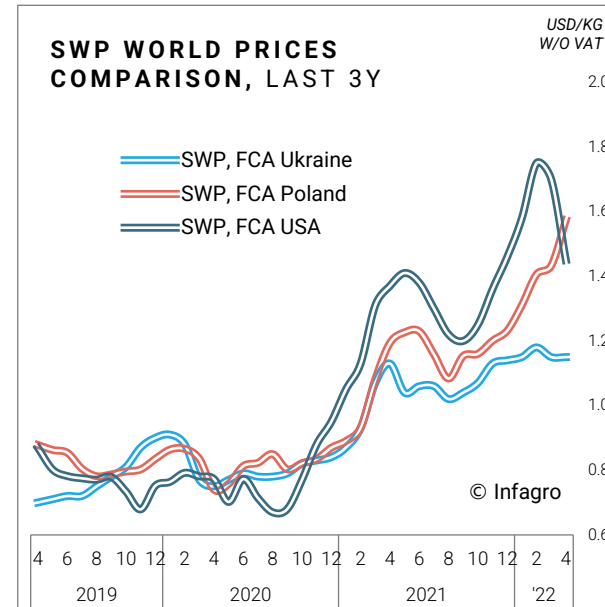
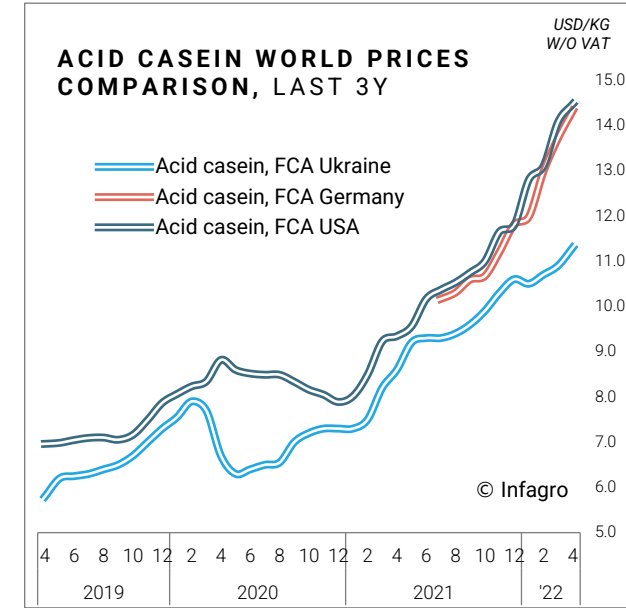
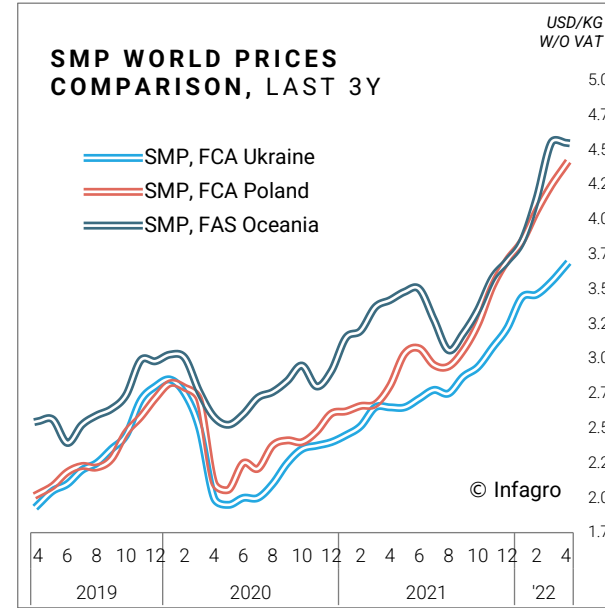
Ukrainians are now respected around the world for their indomitability, thirst for freedom and courage of their Armed Forces, but business is business. In particular, traders are in no hurry to buy Ukrainian products because of the many war related risks, mostly logistics problems. The terms of the contracts are much worse than they were before the war. The position is this: if you buy, then to buy less, cheaper and without prepayment, as it was before the war.

There used to be periods when Ukrainian export prices even exceeded the world prices. Then there was an opportunity to trade with post-Soviet countries. Now this opportunity is almost lost, most of the products are unprofitable to sell there because of the high cost and long alternative logistics.

Now dry dairy products are sold mainly only to/through Europe at prices much lower than the world ones. Often the difference in cost is unreasonably large, for example, for powdered milk it reaches 500-600 dollars, for whey 400, and for casein in general 4000 USD/t. We hope that when the new normal logistics routes are worked out, the traders will agree to reduce this unfair difference, and later, as our Victory approaches, the prepayment mechanisms will be restored.

Even at current prices, the export of dried milk products to Asia or Africa is much more profitable than domestic sales.

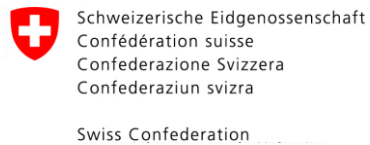
The best way out for Ukrainian exporters is to supply dairy products to EU countries. Soon there will be no quotas or duties to trade with the EU. However, it is necessary to speed up the procedures for including companies in the list of food exporters to Europe.



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These activities are carried out jointly with the state institution The Entrepreneurship and Export Promotion Office and the analytical agency Infagro within the framework of the Swiss-Ukrainian Program "Higher Value Added Trade from the Organic and Dairy Sector in Ukraine" implemented by the Research Institute of Organic Agriculture (FiBL, Switzerland) in partnership with SAFOSO AG (Switzerland), www.qftp.org.



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