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Argentina

Dairy and Products

Annual

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Report Highlights:

Argentine milk output for 2005 is projected to recover to 10 billion liters, very close to 1999's record. The combination of a drop in production costs after the 2002 devaluation and strong world demand with very good prices is driving local farmgate prices to very profitable levels. Record exports are forecast in 2005, accounting for 25 percent of the country's total milk output. Whole dry milk powder shipments are expected to account for 70 percent, followed by cheese. Algeria, Venezuela and Mexico are expected to be the main destinations. As long as profitability in the export business continues over the next 3-4 years, local production will grow 3-5 percent annually. There is still processing capacity to increase exports further.

Includes PSD Changes: Yes
Includes Trade Matrix: No
Annual Report
Buenos Aires [AR1]
[AR]

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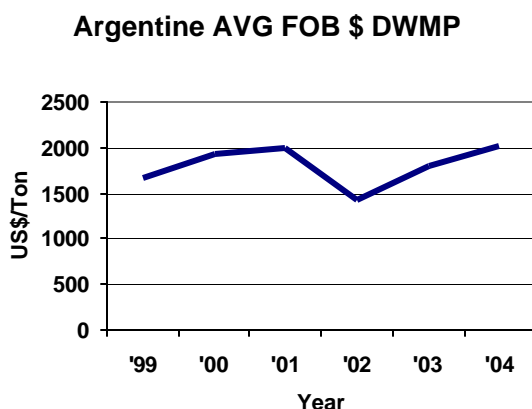
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SECTION I. SITUATION AND OUTLOOK

Argentine dairy exports for 2005 are projected to continue increasing and, for the second year in a row, to finish at record levels. The equivalent of 2.5 billion liters of milk are forecast to be exported to more than 100 markets in 2005, accounting for 25 percent of the country's expected total milk output. This would be the highest share of exports in history. The strong devaluation of 2002, and very firm world prices, is driving the incredibly strong recovery of the Argentine dairy sector. The domestic market continues to struggle with weak demand due to the economic crisis of 2001-02, which increased unemployment and eroded the purchasing power of the population.

Dry whole milk powder is the main dairy product Argentina produces for export. Exports for 2005 are forecast at 210,000 tons, a historic record, and account for more than 70 percent of Argentine total dairy exports (in liter equivalent). Although Argentina has a large cheese industry, most of it is not produced for export. During the 1990s, in order to get rid of the surplus milk, large dairy processors invested heavily in expanding the spraying capacity to dry milk. After the devaluation, and with good competitive costs of farmgate milk prices, milk powder processors are enjoying very profitable returns. The total spraying capacity until 2003 was roughly 13.5 million liters a day. With the investment of three medium/large local processors it will grow to 15 million liter per day in 2005. Milk powder processors work at full capacity during spring, the peak of production, and have unused capacity during the rest of the year. However, if international prices continue to be firm and profitable, more milk will be dried throughout the whole year. Most contacts state that it is unlikely that the drying capacity will grow further in the next few years as most companies have already invested in expanding capacity. Additionally, the two largest processors are not expected to further expand capacity as they have recently renegotiated large debts.

Apart from Argentina being a low-cost milk producer, the strong recovery of world dry milk prices have made the export business very profitable. The firm demand and the Euro/dollar relationship have encouraged local processors to increase shipments. Although traders believe world dairy prices are high, they do not expect great fluctuations in 2005. The following table shows Argentina's annual average FOB price for dry whole milk powder:



The main markets for Argentine dry whole milk powder in 2005 are expected to be Algeria (primarily instant, in 500 grams boxes), Venezuela (regular with vitamins), Brazil, Mexico

(fortified), and other west coast African countries. Local traders expect good demand, as most buyers are oil-producing countries that are currently enjoying high oil prices. Exported product can be regular or instant dry milk and, depending on the customer, it can be fortified or added with vitamins. Argentina normally sells to private companies but has also participated in governmental bids. Exports are either large bags of 25 kilos or small boxes for retail use.

Cheese will be the second most exported product in 2005, accounting for less than 15 percent of Argentina's total dairy exports (in liter equivalent). The U.S. is expected to continue to be the main market, taking about 6,000 tons of Italian-type cheese under a tariff rate quota. Mexico, Chile, and Russia are also good markets. Mexico and Russia buy primarily semi-soft cheese, while Chile imports different types of cheese. About 35 percent of the country's total milk output is used in cheese production. Although most of the large/medium processors make good quality cheese, there are hundreds of small and medium manufacturers which produce cheese. Almost the entire cheese industry is focused on the domestic market. Last year a large Canadian cheese company purchased a large/medium dairy processor with a strong focus on cheese. This company is incorporating technology to produce frozen mozzarella for export. Argentina is expected slowly, but steadily, to increase its cheese exports in the future. Several medium cheese companies are planning to explore the possibility of exporting cheese, especially to neighboring countries.

Nonfat dry milk is the third most important dairy product exported, accounting for about 10 percent of Argentina's total dairy exports (in liter equivalent). Exports in 2005 are projected to increase to 18,000 tons. The main markets are expected to be Mexico, Brazil, and Southeast Asia.

Other exported dairy products are butter, UHT milk, and dulce de leche. A growing business with good profitability is the export of butter oil, whey protein concentrate, milk protein concentrate, and whey powder. Several companies produce these products and some new, minor investments are expected in the near future.

As result of an unexpected large increase in milk production in 2004, exports will be higher than earlier estimated. Most of the extra 1.5 billion liters produced in 2004 were directed to the export market.

Imports of dairy products for 2005 are expected to remain negligible. Total dairy imports through August 2004 were US\$9 million, of which half was fluid milk imported from Uruguay. The balance was cheese from Brazil (processed), Uruguay, and France; fermented dairy drinks from Brazil; and whey and modified whey from the U.S. and Denmark. Although Argentina, with its milk production recovery, does not need to import fluid milk from neighbor Uruguay, especially with very similar prices, a couple of companies will continue to do so as a strategic decision. These companies signed agreements when there was a supply shortfall in Argentina and they want to keep Uruguayan suppliers as an alternative. However, the volume will drop somewhat as a third company will stop buying from Uruguay. Total fluid milk imports represents less than 0.5 percent of Argentina's milk output.

The following table shows 2004 import duties, export rebates, and export taxes for Argentine dairy products (in %):

Product	Import Duty	Export Tax	Export Rebate
UHT Milk	14.0	5.0	3.4
WDM	16.0	5.0	3.4
NFDM	16.0	5.0	3.4
Cheese	16.0	5.0	4.5

Argentine milk production for 2005 is projected at 10 billion liters, the second highest volume in history. Very good farm level returns, weaker competition from other agricultural alternatives, and the fact that the best cows and the more efficient producers remained after the dairy crisis of 2000-02, are expected to push production up one more step.

Dairymen are expected to continue improving cows' nutrition, use better genetics, and devote more land to dairy. The fact that soybean prices fell significantly over the past few months will lessen competition for dairy. Weaker returns to field crops will force land rental prices to drop. Very high soybean prices in 2003 drove rental prices up significantly. Many milk producers in Santa Fe and Cordoba were unable to afford the high prices.

Although it is very difficult to reach an average cost of production of milk, due to the diversity of operations, sources estimate that the cost for efficient medium and large producers ranges roughly between US\$0.11-0.12 per liter. The average farmgate milk price in 2004 was close to US\$0.15 per liter. Prices for 2005 are expected to remain at similar 2004 levels.

Milk farmgate prices vary between the different provinces, the purchasing company, and the final product. Milk prices in the area near Buenos Aires city for fresh products (fluid milk, yogurt, fresh cheese, etc.) are higher than those paid in the "cheese area" which is far removed from the country's capital city and demand somewhat lower quality milk. Most sources indicate that a large portion of the price paid to producers is due to firm export demand. Farmgate prices would be significantly lower if production was solely for the domestic market.

Larger concentration in the dairy sector is expected in the near future as the number of dairy operations continues to fall. Unofficial sources estimate that there are currently approximately 12-13,000 dairy producers, roughly 6-7,000 less than 6 years ago. The average age of dairymen is relatively high, with the younger generations looking to other occupations. Very few new operations are being installed. Although there is no official, accurate dairy cowherd number, it is expected to grow somewhat in 2005 as result of good returns.

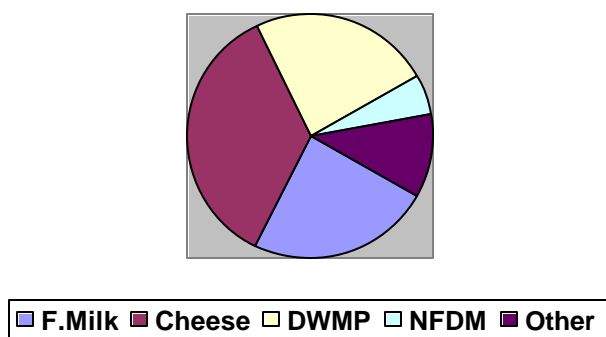
As result of large investment in technology and modern management, milk production in Argentina in the 1990s grew 60 percent. This growth was geared by strong domestic demand. However, from 2000 onwards, the economic recession and the following economic crisis in 2002, hit the dairy sector very hard. Production bottomed out in 2003 at 7.95 billion liters, equal to production 10 years before. In October 2003 most dairy contacts (producers, industry, traders) were not very optimistic about production in 2004. However, several factors were underestimated at that time. After negative returns in 2002 and part of 2003, milk prices by mid-2003 were well above production costs, providing producers with very good profitability. Improved world dairy prices made large processors with drying capacity want to increase production. In order to do so, they were forced to pay more to encourage

producers to deliver their production to them. As a result, dairymen began to increase (in volume and quality) the supply of feed and the condition of the cows improved significantly. Under this situation and with excellent weather throughout 2004, production “exploded”, with most sources projecting an increase of about 18 percent.

The largest 15 dairy processors account for more than 60 percent of the total milk output. The local industry can be divided into three categories. The first, large companies, which are two, have recently renegotiated the payment of their large debts. These companies invested strongly in the 1990s to expand capacity and become more efficient, but with the country’s default and devaluation in 2002, they could no longer pay. They are multi-product companies and have in-country distribution. Today they are profitable companies, mainly supported by very good returns in the export business. Both of them have strategic alliances with large dairy multinationals. The second groups, medium/large companies, are also mainly multi-product (except for two which focus primarily in cheese and one in dry milk) but have smaller distribution networks. They are in general either international companies or family-owned and are in very good shape. The final group consists of hundreds of medium and small cheese producers, of which many operate in the informal market. Most of these are in a complicated situation because they have to pay high milk prices to compete with the large exporting processors, sell at low prices in the domestic market (which is oversupplied with cheese) and cannot export and therefore, do not receive the benefit of excellent returns.

The following table shows the share of dairy products manufactured in Argentina (estimated 2004 – liter equivalent):

Product Manufacturing in % Liters



Driven primarily by anticipated low prices of products manufactured by processors which do not export (roughly 35 percent of the total milk output), domestic consumption for 2005 is forecast to improve somewhat. The local economy is also expected to expand, encouraging some more demand. In addition, some leading companies are in the process of creating a larger demand for fresh products, supported by marketing campaigns and lower prices. Dry whole milk powder, which is widely consumed in the interior of the country, far from the large dairy processors, is projected to increase slightly as national/provincial/county governments are expected to continue with social programs which distribute food to the needy. Argentine consumption reached a record of 230 liters-equivalent in 1999, and then it began a decreasing trend, bottoming out in 2003 at 175 liters per capita. Consumption recovered in 2004 and it is expected to reach about 185 liters per capita in 2005.

Apart from the few cases of investment mentioned in the first part of the report, post does not foresee great expansion in capacity or modernization. The capacity for cheese and fresh products is currently underutilized. The local industry in the late 1990s was prepared to handle much more milk for the domestic market than what it does currently.

Argentine FOB prices in 2004 were very good and traders expect them to stay at somewhat similar levels in 2005. However, due to the low production cost, Argentina still has room for world prices to drop and still be profitable. If world prices fall significantly and the domestic market does not react, there would still be room for a reduction in farmgate prices.

The quality of local milk is very good and is improving. Although processors during the dairy crisis did not increase pressure for better quality (as they had done throughout the 1990s), under this new situation, which is profitable for almost all in the supply chain, they will demand tighter sanitary controls. Transportation and industrialization is modern and efficient.

Most local traders indicate that the Argentine dairy sector will depend on the exchange rate of the peso against the dollar and the Euro against the dollar. The Argentine Government said it would try to maintain a weak peso to encourage local production and exports. The exchange rate, which is expected by the end of 2004 to be 3 pesos to a dollar, is expected in 2005 to closely follow inflation and Brazilian currency. Regarding the Euro/dollar exchange rate, a stronger Euro benefits local dairy exports. The local dairy sector will continue to recover and even surpass the record production levels as long as the export market continues to be profitable.

In early 2004, a Congressman from a rural origin, passed a bill to create a Promotional Institute for Argentine Dairy Products. The goal of this entity is to promote the dairy industry and to solve the historic problems which affect the dairy supply chain. The industry would pay a very small percentage based on the milk marketed domestically. It is doubtful this entity will be created any time soon, especially after the example of the National Beef Institute, a local check-off program with similar goals, which is struggling in its first years of activities.

SECTION II. STATISTICAL TABLES

PSD Table

Country Commodity	Argentina Dairy, Milk, Fluid					
	(1000 HEAD)(1000 M					
	2003	Revised	2004	Estimate	2005	Forecast
	USDA Official [	Estimate [DA	Official [	Estimate [DA	Official [	Estimate [I
Market Year Begin	01/2003			01/2004		01/2005
Cows In Milk	2000	2000	2000	2000	0	2100
Cows Milk Production	7900	7950	8100	9400	0	10000
Other Milk Production	0	0	0	0	0	0
TOTAL Production	7900	7950	8100	9400	0	10000
Intra EC Imports	0	0	0	0	0	0
Total Imports	32	34	30	40	0	30
TOTAL Imports	32	34	30	40	0	30
TOTAL SUPPLY	7932	7984	8130	9440	0	10030
Intra EC Exports	0	0	0	0	0	0
Total Exports	1	2	1	12	0	14
TOTAL Exports	1	2	1	12	0	14
Fluid Use Dom. Consum.	2000	2050	2100	2250	0	2400
Factory Use Consum.	5931	5932	6029	7178	0	7616
Feed Use Dom. Consum.	0	0	0	0	0	0
TOTAL Dom. Consumptic	7931	7982	8129	9428	0	10016
TOTAL DISTRIBUTION	7932	7984	8130	9440	0	10030
Calendar Yr. Imp. from U.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

PSD Table

Country Commodity	Argentina Dairy, Cheese					
	(1000 MT)					
	2003	Revised	2004	Estimate	2005	Forecast
	USDA Official [	Estimate [	DA Official [	Estimate [	DA Official [	Estimate [
Market Year Begin	01/2003		01/2004		01/2005	
Beginning Stocks	29	29	27	22	20	30
Production	350	325	360	345	0	360
Intra EC Imports	0	0	0	0	0	0
Total Imports	1	1	1	1	0	1
TOTAL Imports	1	1	1	1	0	1
TOTAL SUPPLY	380	355	388	368	20	391
Intra EC Exports	0	0	0	0	0	0
Total Exports	23	23	23	28	0	30
TOTAL Exports	23	23	23	28	0	30
Human Dom. Consumpti	330	310	345	310	0	330
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	330	310	345	310	0	330
TOTAL Use	353	333	368	338	0	360
Ending Stocks	27	22	20	30	0	31
TOTAL DISTRIBUTION	380	355	388	368	0	391
Calendar Yr. Imp. from U.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

PSD Table

Country	Argentina					
Commodity	Dairy, Dry Whole Milk Powder (1000 MT)					
	2003	Revised	2004	Estimate	2005	Forecast
	USDA Official [	Estimate [	DA Official [	Estimate [	DA Official [	Estimate [
Market Year Begin	01/2003		01/2004		01/2005	
Beginning Stocks	12	12	13	27	13	33
Production	165	198	165	280	0	310
Intra EC Imports	0	0	0	0	0	0
Total Imports	1	1	0	1	0	1
TOTAL Imports	1	1	0	1	0	1
TOTAL SUPPLY	178	211	178	308	13	344
Intra EC Exports	0	0	0	0	0	0
Total Exports	75	100	70	180	0	210
TOTAL Exports	75	100	70	180	0	210
Human Dom. Consumption	90	84	95	95	0	100
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	90	84	95	95	0	100
TOTAL Use	165	184	165	275	0	310
Ending Stocks	13	27	13	33	0	34
TOTAL DISTRIBUTION	178	211	178	308	0	344
Calendar Yr. Imp. from U.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

PSD Table

Country Commodity	Argentina Dairy, Milk, Nonfat Dry (1000 MT)					
	2003 USDA Official	Revised Estimate [1]	2004 USDA Official	Estimate [1]	2005 USDA Official	Forecast Estimate [1]
Market Year Begin	01/2003		01/2004		01/2005	
Beginning Stocks	6	6	5	6	4	5
Production	24	31	26	35	0	40
Intra EC Imports	0	0	0	0	0	0
Total Imports	1	1	0	0	0	0
TOTAL Imports	1	1	0	0	0	0
TOTAL SUPPLY	31	38	31	41	4	45
Intra EC Exports	0	0	0	0	0	0
Total Exports	12	14	12	16	0	18
TOTAL Exports	12	14	12	16	0	18
Human Dom. Consumpti	14	18	15	20	0	21
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	14	18	15	20	0	21
TOTAL Use	26	32	27	36	0	39
Ending Stocks	5	6	4	5	0	6
TOTAL DISTRIBUTION	31	38	31	41	0	45
Calendar Yr. Imp. from U.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Prices Table

Country Argentina

Commodity Dairy, Milk, Fluid

Prices in per uom

Year	<input type="text" value="2003"/>	2004	% Change
Jan	<input type="text" value="0.35"/>	<input type="text" value="0.48"/>	37%
Feb	<input type="text" value="0.4"/>	<input type="text" value="0.48"/>	20%
Mar	<input type="text" value="0.41"/>	<input type="text" value="0.48"/>	17%
Apr	<input type="text" value="0.42"/>	<input type="text" value="0.48"/>	14%
May	<input type="text" value="0.48"/>	<input type="text" value="0.47"/>	-2%
Jun	<input type="text" value="0.52"/>	<input type="text" value="0.46"/>	-12%
Jul	<input type="text" value="0.51"/>	<input type="text" value="0.45"/>	-12%
Aug	<input type="text" value="0.5"/>	<input type="text" value="0.45"/>	-10%
Sep	<input type="text" value="0.47"/>	<input type="text" value="0.45"/>	-4%
Oct	<input type="text" value="0.47"/>		-100%
Nov	<input type="text" value="0.47"/>		-100%
Dec	<input type="text" value="0.47"/>		-100%

Exchange Rate Local Currency/US \$

Date of Quote MM/DD/YYYY