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Prepared By: Mihai Lupescu

Approved By: Evan Mangino

Report Highlights:

FAS/Canada projects flat growth for milk and cheese production in 2021, as COVID-19 restrictions on the food service sector drive significant shifts in consumption patterns. Butter production is forecast to continue growing into 2021, as industry works to rebuild stocks depleted by sustained strong consumption. FAS/Canada forecasts skim milk powder production and exports declining in 2021, as the industry reorients toward producing milk protein concentrates and isolates. Imports of cheese and butter continue to rise, in part, due to additional duty-free market access under recently concluded trade agreements, including the USMCA, which entered into force on July 1, 2020.

Executive Summary

Few sectors of the economy have been upended by COVID-19 quite like food service, where demand for some products, like fluid cream, remains well below pre-pandemic levels. Despite an increase in retail grocery consumption of some items, like fluid milk, sour cream and butter, the dairy industry scaled back milk production growth in 2020 to align overall milk supply with the pandemic market demand.¹

Cheese imports are expected to expand further in 2021, as import tariff rate quotas (TRQs) under the Comprehensive Economic and Trade Agreement (CETA) with the European Union (EU), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), and the United States-Mexico-Canada Agreement (USMCA) grow to a combined volume of just over 28,500 metric tons (MT). In addition, Canada will continue to import over 20,400 MT of cheese – predominantly from EU origins – under a TRQ established at the World Trade Organization (WTO) in 1995.

FAS/Canada expects butter stocks to remain below the industry targeted volume of 35,000 MT through 2021. By August 2020, stocks of butter had been drawn down to 28,000 MT, from over 45,000 MT during the summer of 2019, reflecting production discipline in the second half of 2019, and increased demand during the COVID-19 pandemic from both commercial manufacturers of baked goods and from individuals preparing more food at home. Butter production is expected to increase moderately through 2021, to meet steady demand and to rebuild stocks.

FAS/Canada forecasts a significant decline in the production and export of skim milk powder (SMP) in 2021, primarily as a result of USMCA provisions that would impose export surcharges on Canadian exports of SMP and milk protein concentrates in excess of 35,000 MT in year 2 of the agreement. 2021 SMP production is forecast to decline to 80,000 MT, down from an estimated 90,000 MT in 2020, and further down from 97,000 MT in 2019. SMP exports in 2021 are forecast to drop to 30,000 MT, from an estimated volume of 50,000 MT in 2020. While the overall milk protein surplus is expected to remain relatively constant into 2021, the dairy industry is expected to shift its production and export focus away from SMP and into higher-protein powders, like milk protein concentrates and milk protein isolates (this last category of protein powders being excluded from USMCA export surcharges).

¹ All years in this report are calendar years, unless otherwise noted. Canadian milk marketing year (MY) 2020/21 commences on August 1, 2020, and ends on July 31, 2021.

MILK

Production, Supply and Distribution (PS&D):

Dairy, Milk, Fluid Canada	2019		2020		2021	
	USDA Official	NEW Post Data	USDA Official	NEW Post Estimates	USDA Official	NEW Post Forecast
Cows In Milk	969	968	968	967	0	967
Cows Milk Production	9,995	9,903	10,000	9,950	0	9,980
Total Production	9,995	9,903	10,000	9,950	0	9,980
Total Imports	43	46	40	50	0	50
Total Supply	10,038	9,949	10,040	10,000	0	10,030
Total Exports	8	10	7	20	0	20
Fluid Use Dom. Consum.	2,800	2,816	2,780	2,875	0	2,910
Factory Use Consum.	6,738	6,671	6,755	6,650	0	6,645
Feed Use Dom. Consum.	492	452	498	455	0	455
Total Dom. Consumption	10,030	9,939	10,033	9,980	0	10,010
Total Distribution	10,038	9,949	10,040	10,000	0	10,030

1,000 head (cows) and 1,000 metric tons (the rest)

NOTE: "NEW Post" data reflect author's assessments and are NOT official USDA data

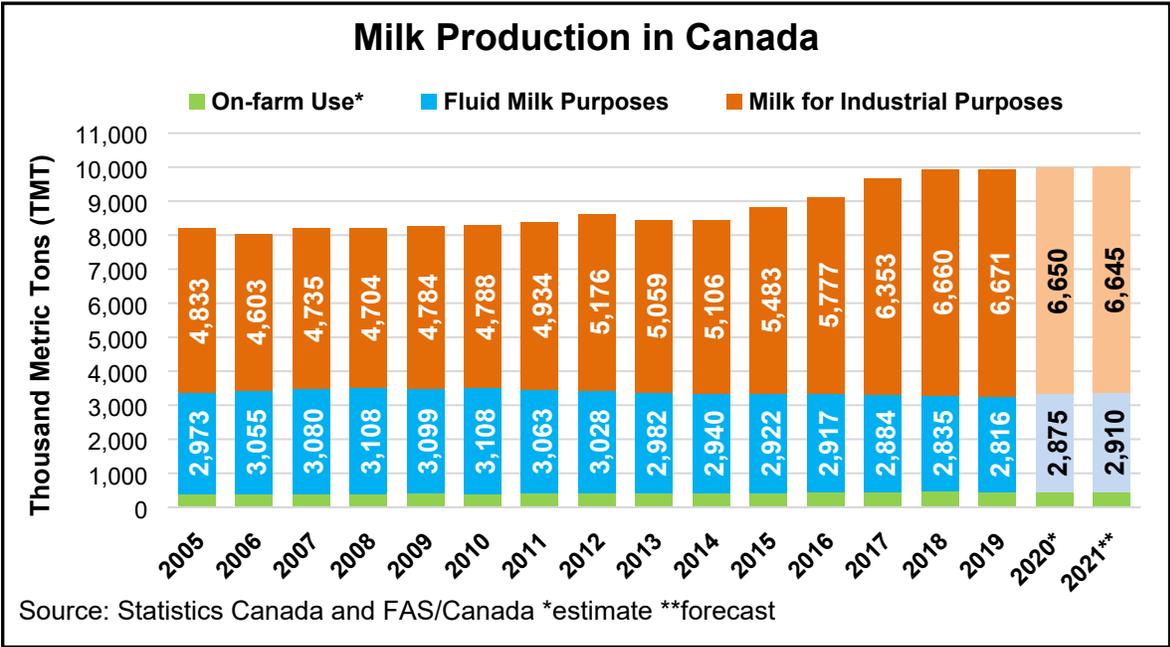
Production

Canada maintains a supply management system for milk, in which production quota is allocated on a butterfat basis such that one share of quota is equivalent to the production of 1 kilogram of butterfat per day. The national Canadian Milk Supply Management Committee (CMSMC) sets the total quota volume based on recommendations from the Canadian Dairy Commission (CDC). The CDC monitors the trends in Canadian dairy requirements and recommends milk production adjustments to reflect changes in Canadian domestic demand for milk and dairy products. The CMSMC applies the terms of the National Milk Marketing Plan (a federal-provincial agreement) to establish each province's share of the total production quota.

Until 2020, quota increases and decreases were shared among two regional pools: the Eastern Canadian Milk Pool (or P5), which includes Prince Edward Island, Nova Scotia, New Brunswick, Quebec, and Ontario; and the Western Milk Pool (WMP), which is made up of Manitoba, Saskatchewan, Alberta, and British Columbia. Each pool was then responsible for distributing shares of the quota to producers according to provincial policies and in accordance with pooling agreements. In 2020, the dairy industry decided to gradually merge, over a three-year period, the two milk pools, and to add Newfoundland and Labrador to the milk pooling system, so that by 2023 only one single national milk pool will cover all ten provinces. Milk in Canada is priced based on the end use of its major components: butterfat, protein and other solids non-fat. Milk component prices are published on the [Canadian Dairy Information Centre](#) website and on the [Milk Ingredients](#) website.

Milk produced in Canada supplies two markets: the fluid milk market, which includes fluid milk for direct consumption, creams, and flavored milks; and the industrial milk market (or milk for factory use), which is used to make dairy products such as butter, cheese, yogurt, ice cream, and milk powders. The fluid milk market consistently – even during COVID-19 – accounts for about 30 percent of total milk produced in

Canada, and milk for factory use constitutes approximately two thirds. On-farm use is estimated to account for less than five percent of total milk produced.



FAS/Canada forecasts total milk production to reach 9.980 million metric tons (MMT) in 2021, virtually unchanged from the 2020 estimate of 9.950 MMT. The onset of the COVID-19 pandemic triggered the closure of the food service sector, which resulted in significant changes in food consumption patterns. For the dairy sector, it meant an overall decline in demand for certain products, like cheese and fluid cream, for which sales through food service establishments represent a significant portion of overall sales, and a surge in demand for other products, like fluid milk, sour cream and butter, reflective of an increased number of home-cooked meals. The gradual reopening of the economy during the summer of 2020 only partially offset the overall decline in dairy consumption during the first half of the year. Dairy farmers reacted to these market changes by tightening milk production levels in order to align overall milk supply with the market demand for various dairy products.

FAS/Canada expects the COVID-19 pandemic to limit overall demand growth for dairy products in 2021, as food service establishments are projected to continue operating at reduced capacity in proportion to the local rates of COVID-19 transmission. As of writing, municipalities across Canada are tightening restrictions on food service establishments once again due to rising COVID-19 cases. Though reduced demand growth will implicitly limit milk production growth, a number of processing facilities are expected to come on-line during the second half of 2020, including a new [cheese manufacturing plant](#) in Quebec as well as an [infant formula plant](#), a [high protein milk plant](#), and a modernized [cream and milk ingredients plant](#) in Ontario. These new milk processing capacities will help maintain the 2021 overall milk production at a level comparable to the estimated 2020 production.

Between 2014 and 2018, Canada experienced a significant growth in the dairy sector, with total milk production rising by 18 percent, largely on growth in milk for factory use (also called milk for industrial purposes). Between 2014 and 2018, factory use milk production increased by over 30 percent, while milk for the fluid market declined by almost 4 percent. In 2019, when the sector saw the first signs of oversupply,

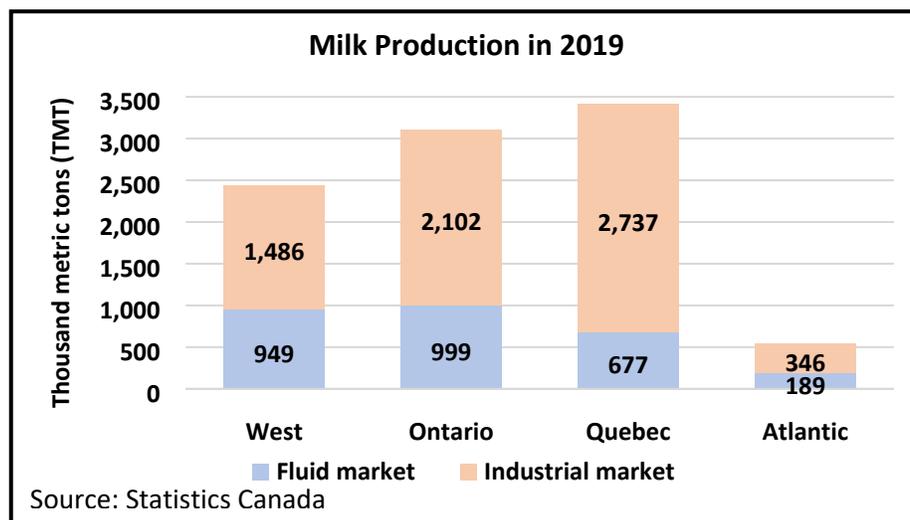
provincial milk boards sent signals to farmers to level off production. As a result, factory use milk production in 2019 remained virtually unchanged from 2018, while milk for the fluid market declined another 1 percent. With the COVID-19 pandemic, FAS/Canada expects this new pattern of stagnant growth to continue into 2020 and 2021. Factory use milk production is forecast to contract 0.3 percent in 2020, and to remain flat into 2021. Milk for the fluid market is expected to increase for the first time in a decade by an estimated 2 percent in 2020, and by another 1 percent in 2021, on increased retail sales during the pandemic response.

In general, there is no direct 1-to-1 relationship between milk board announcements related to milk production quota increases (or cuts) and the actual volume of milk produced. Production quota announcements are essentially signals sent to dairy farmers to make adjustments in order to drive production in the desired direction. The actual milk production volume is the result of numerous factors, including: the number of incentive days allowed, the number of production credit days claimed, the level of penalties applied to over-production volumes, weather conditions, and farm management practices.

Canadian dairy cow productivity has steadily increased over the past decade, primarily due to improved genetics, but also as a result of improvements in management practices, feed quality, and greater use of robotic milking parlors that increase total milkings per day. In 2008, the average volume of milk production per dairy cow was 8.0 MT annually. By 2019, this volume had grown 22 percent to 9.8 MT annually. FAS/Canada projects average dairy cow milk productivity to reach 9.9 MT annually.

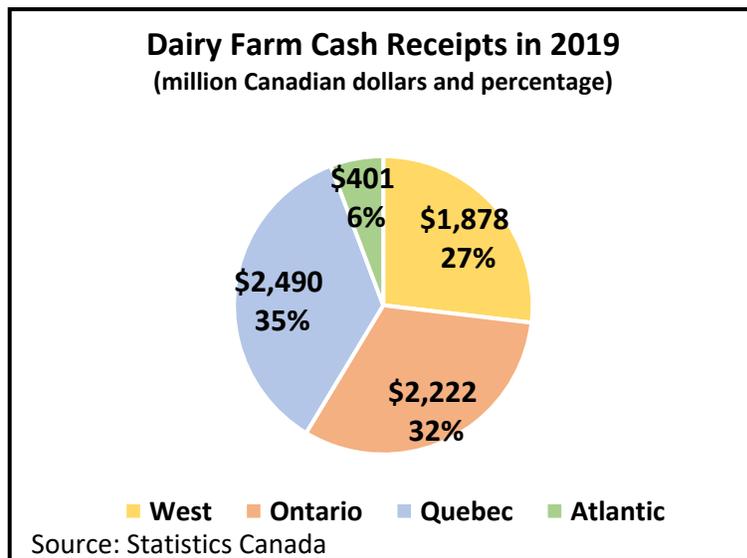
Trends in Dairy Farming²

Nearly 70 percent of Canada’s milk production is concentrated in Quebec and Ontario, with just over 25 percent in the West and roughly 5 percent in the Atlantic region. As early Canadian settlers lived primarily in Quebec and Ontario, these provinces are home to a multitude of relatively small dairy farms, often run by fifth or sixth-generation producers. By contrast, dairy farming is a relative newcomer to the Western agricultural sector, with large, modern farms still managed by first-generation producers.

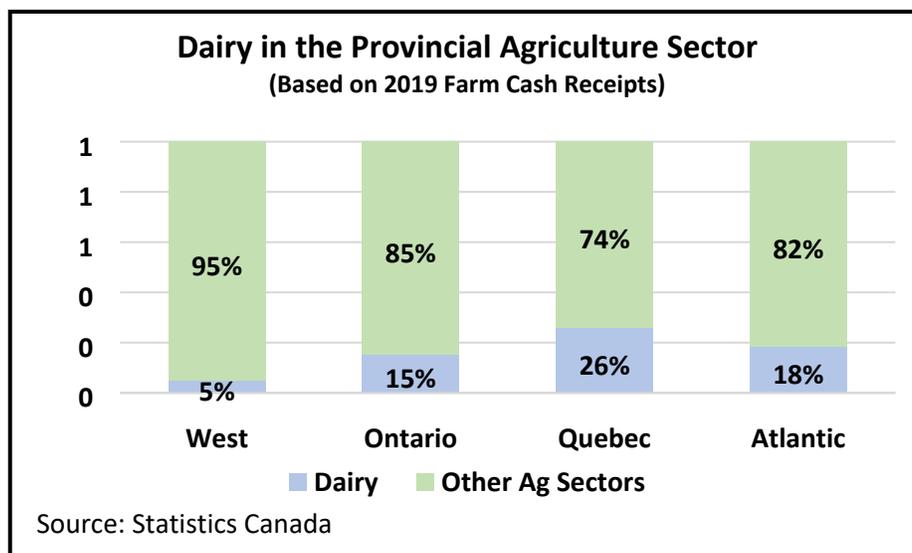


² In this section, “West” includes the provinces of British Columbia, Alberta, Saskatchewan, and Manitoba, while “Atlantic” includes New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador.

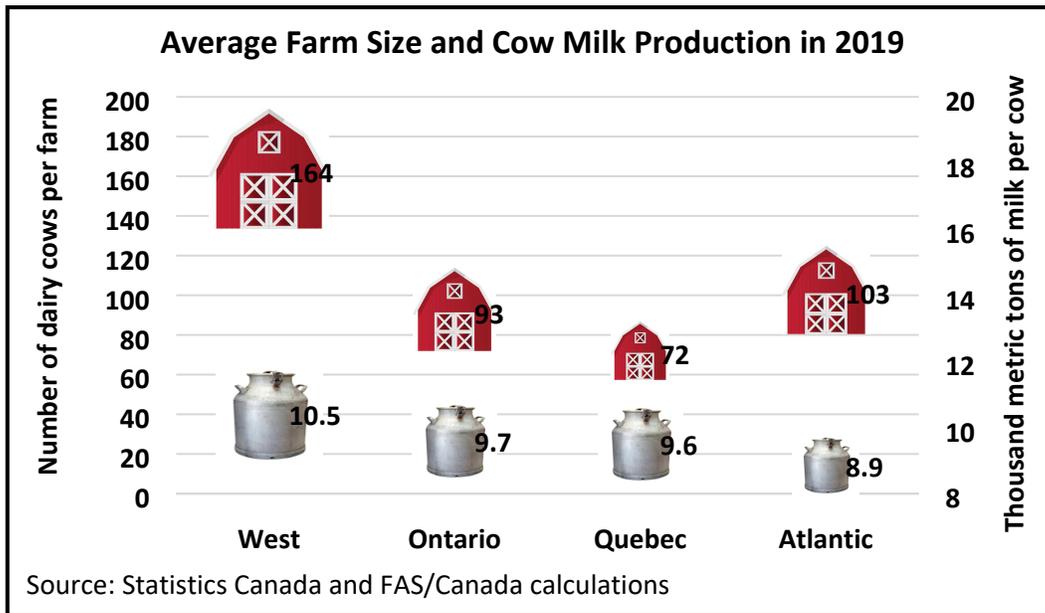
The long tradition of dairy farming in Ontario and Quebec also explains, in part, the concentration of dairy processing facilities in these two provinces. The combined share of milk for industrial use in Ontario and Quebec is close to 75 percent of total milk production in these two provinces, compared to only 60 percent in the West. As the price of milk for the fluid market is typically higher than the average price of milk used in the production of various dairy products (milk for industrial use), the larger presence of dairy processing in Eastern Canada also explains the lower blended milk price farmers receive there, compared to the blended milk price farmers receive in the West.



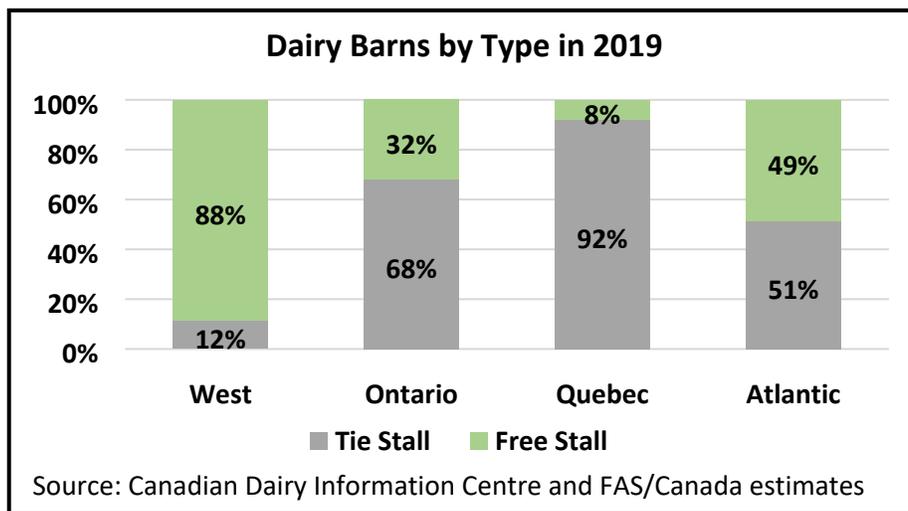
These differences in blended milk prices are reflected in the farm cash receipts generated in various regions. The West, with only 25 percent of total milk production, captures 35 percent of dairy farm cash receipts, while Ontario and Quebec generate a combined 60 percent in milk revenues, although they account for 70 percent of the national milk production volume.



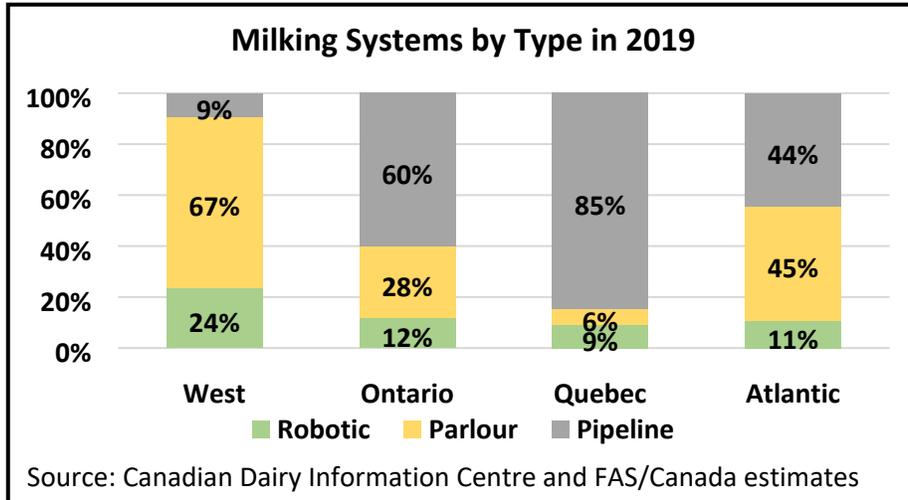
Across Canada, dairy farming cash receipts as a percentage of total agricultural sector revenue vary significantly, with Quebec generating more than one quarter of total farm cash receipts from dairy.



Despite the relatively small size of the dairy sector in the West, dairy farms in western provinces are in fact among the largest and the most technologically advanced in the country. The average farm size in the West, in terms of number of dairy cows, is about twice the size of average farms in Ontario and Quebec, supporting greater production efficiencies and yields per cow.

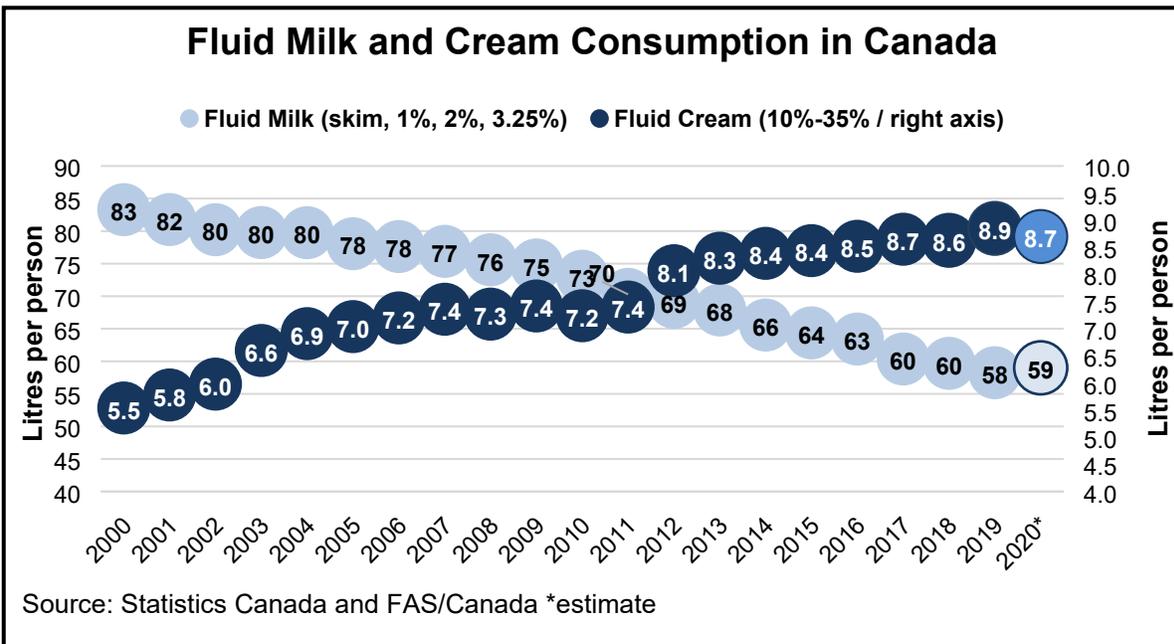


Not having inherited legacy dairy facilities, Western Province dairy farmers had greater opportunities to invest in newer barns, incorporating more modern technologies and configurations. This is evidenced by the higher adoption of the free stall dairy farming model as well as the wider utilization of modern milking technologies, including rotary parlors and robotic milking stations.

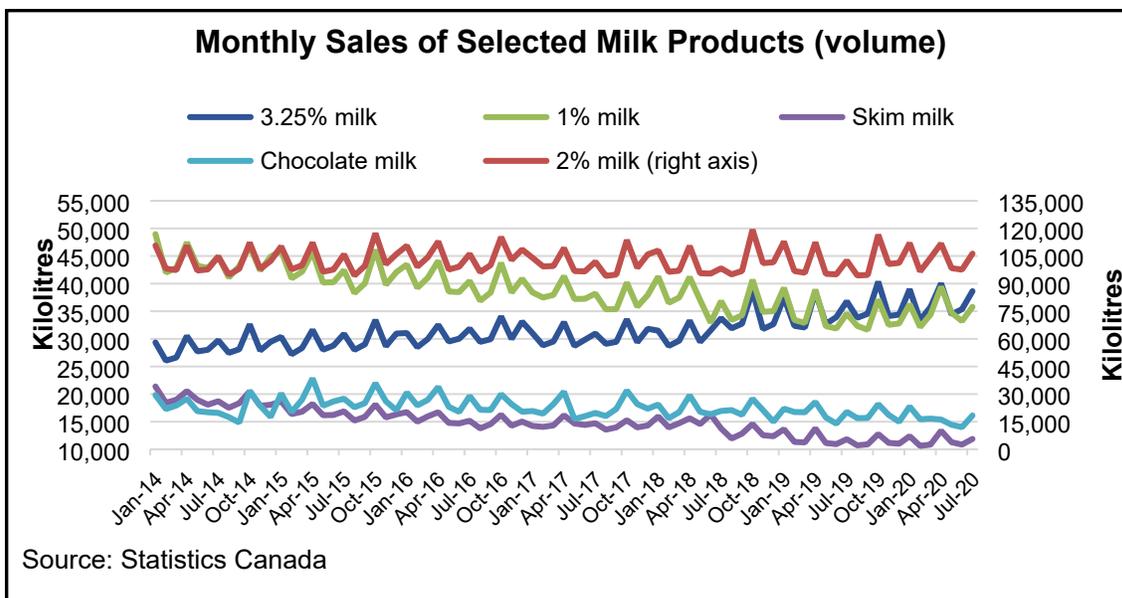


Consumption

While per capita consumption of drinking milk has been declining, the COVID-19 pandemic has reversed this trend, at least temporarily, as consumers have spent more time at home and less time at coffeeshops and other food service establishments, traditional sources of fluid cream demand.



Sales data continue to indicate that Canadians buy more whole milk (3.25 percent butterfat) and less skim milk (zero percent butterfat) and reduced-fat milk (1 percent butterfat), following the overall trend of increased fat consumption in the Canadian diet.

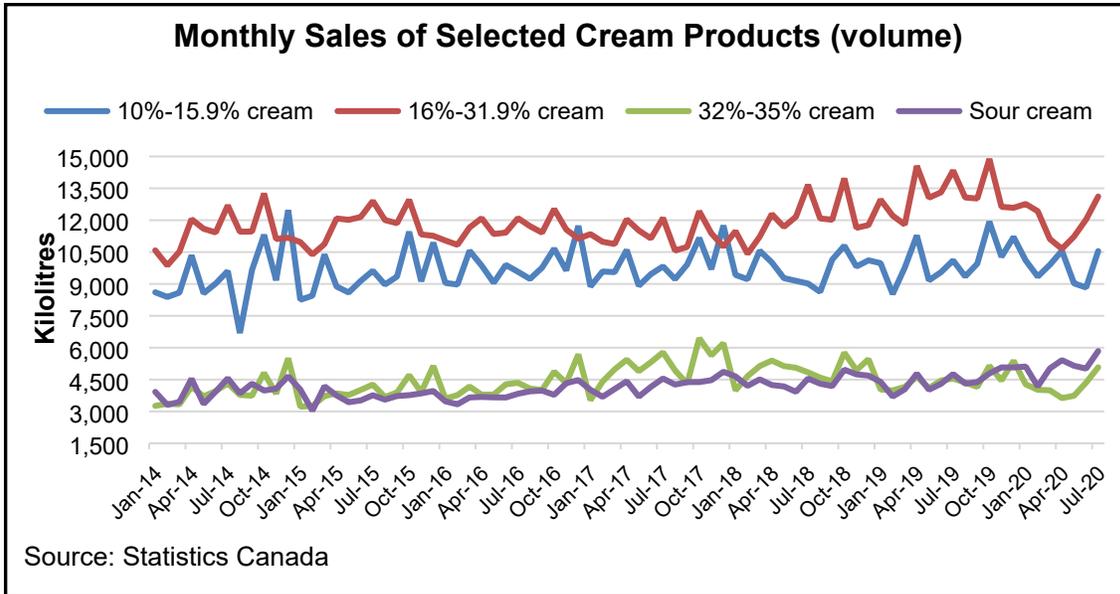


In June 2018, Coca-Cola Canada [announced](#) an \$85 million CAD investment to build a new production facility in Peterborough, Ontario to produce ultrafiltered, lactose-free milk. The new fluid milk plant is scheduled to open in late 2020 and will produce skim, 2 percent, 3.25 percent and 2 percent chocolate milk in 1.5-liter PET bottles as well as 2 percent white and chocolate milks in 240 ml PET bottles. According to the company, these ultrafiltered milk products contain 50 percent more protein and 50 percent less sugar than traditional milk.

To develop Canadian market awareness and build a customer base while the plant was under construction, Coca-Cola has been importing these ultrafiltered milk products from the United States duty free under special supplementary import permits since September 2018. When the Peterborough plant comes online, all of these products sold in Canada will be made with 100 percent Canadian milk, eliminating this temporary export sales channel for high-value U.S. dairy products.

In general, cream consumption has increased in Canada due to the popularity of coffee culture and the changing consumer preference for higher fat content products. However, restrictions on the food service sector during the COVID-19 pandemic led to a significant drop in fluid cream sales, as café and restaurant visits have ebbed and flowed in relation to COVID-19 restrictions and changing consumer behavior. Overall sales of liquid cream (10 to 35 percent butterfat content) dropped by 1 percent between marketing year (MY) 2019 (August 2018 to July 2019) and MY 2020 (August 2019 to July 2020), primarily driven by a 5 percent decline in sales of heavy cream (32 to 35 percent butterfat). As of writing, monthly sales of fluid cream have yet to return to pre-pandemic levels.

The only cream category showing consistently stronger sales performance during the pandemic has been sour cream. Sales increased by over 12 percent between MY 2019 and MY 2020, as consumers integrated this ingredient into the preparation of a greater number of meals at home.



Trade

Under WTO commitments, Canada maintains a 64,500 MT fluid milk TRQ and a 394 MT cream TRQ. Due to geographic proximity and the perishable nature of fluid milk, the United States is the primary source for Canadian imports of these products. Canadian consumers transporting fluid milk purchased in U.S. grocery stores cross the border under personal use exemptions, and the fluid milk TRQ is considered 100 percent filled by these ‘imports.’

The WTO cream TRQ is first [allocated](#) to historical importers with established distribution for sterilized cream (minimum 23 percent butterfat content) in containers not exceeding 200 ml. Any remaining volumes not allocated to the historical sterilized cream importers are subsequently allocated to new sterilized cream importers and to importers of other kinds of specialty creams (such as Devon cream, a type of clotted cream).

The [Comprehensive and Progressive Trans-Pacific Partnership](#) (CPTPP) entered into force on December 30, 2018, creating a new import [TRQ](#) for milk, providing additional market access as follows:

Quota Year (August to July)	Milk (in MT)
2018/19 (year 1)	8,333
2020/21 (year 3)	25,000
2023/24 (year 6)	50,000
2036/37 and onward	56,905

Up to 85 percent of this CPTPP milk TRQ can be allocated to bulk milk (not for retail sale) importation for processing into dairy products used as ingredients for further food processing.

Under CPTPP, Canada also agreed to a cream [TRQ](#) (minimum 6 percent butterfat content), providing additional market access as follows:

Quota Year (August to July)	Cream (in MT)
2018/19 (year 1)	500
2020/21 (year 3)	530
2023/24 (year 6)	580
2031/32 and onward	734

Based on current market conditions and the limited economic attractiveness of shipping fluid milk and cream from CPTPP countries, FAS/Canada estimates the CPTPP milk and cream TRQs will remain unfilled for the current period.

Under the [United States-Mexico-Canada Agreement](#) (USMCA), which entered into force on July 1, 2020, Canada agreed to a milk [TRQ](#), providing additional market access as follows:

Quota Year (August to July)	Milk (in MT)
July 2020 (year 1)	8,333
2020/21 (year 2)	16,667
2024/25 (year 6)	50,000
2037/38 and onward	56,905

Up to 85 percent of this TRQ can be [allocated](#) to bulk milk (not for retail sale) importation for processing into dairy products used as ingredients for further food processing.

Canada also agreed to a USMCA fluid cream TRQ (minimum 6 percent butterfat content) which provides the following market access:

Quota Year (August to July)	Cream (in MT)
July 2020 (year 1)	1,750
2020/21 (year 2)	3,500
2024/25 (year 6)	10,500
2037/38 and onward	11,950

Of the entire USMCA cream TRQ volume, 85 percent is to be [allocated](#) to the importation of cream in bulk (not for retail sale) to be processed into dairy products used as ingredients for further food processing. The cream TRQ is opened to products originating in the United States, and FAS/Canada estimates this TRQ will be fully filled.

Under the USMCA, the United States committed to an aggregated import [TRQ](#) for Canadian dairy products, including fluid cream (butterfat content between 6 and 45 percent), sour cream, ice cream and milk beverages. The combined volume under this TRQ would be 1.75 million liters in year one of implementation, rapidly growing to 10.5 million liters in year six of implementation, and then gradually increasing to the full implementation volume of 11.95 million liters in year 19.

Both fluid milk and cream are eligible under Global Affairs Canada's policy for [supplementary imports](#), which includes the [Imports for Re-Export Program](#) (IREP). A program similar to IREP, called the [Duties Relief Program](#) (DRP), is operated by the Canada Border Services Agency. Under both the IREP and DRP, Canadian food manufacturers may import milk or cream to use in processed food products, provided that such products do not enter the domestic market and are eventually exported.

Policy

On August 16, 2019, the federal government [announced](#) a support package of \$1.75 billion CAD to be distributed across eight years to dairy farmers as compensation for projected negative impacts on the Canadian dairy industry from market access concessions in the CETA and CPTPP trade agreements.

Of the total amount announced, \$345 million CAD was paid out in 2019 (the first year) as direct payments under the [Dairy Direct Payment Program](#), benefitting all dairy producers in proportion to their quota shares. To be eligible, farmers would have to own a valid dairy license, own milk quota and be registered with a provincial milk marketing board. Dairy farmers expect to receive their year 2 payments before the end of 2020.

Dairy producers also requested from the federal government additional compensation for the market access conceded under USMCA. This supplementary support package has yet to be announced.

In June 2020, Canada published milk component prices on the [Canadian Dairy Information Centre](#) website for milk classes having different prices in different provinces, and on the [Milk Ingredients](#) website for milk classes with the same price at the national level. Milk classes are defined under Canada's [Harmonized Milk Classification System](#), which, since June 2020, no longer includes milk class 7.³ [USMCA](#) requires the elimination of milk class 7 before January 1, 2021.

³ For additional information on milk class 7, please refer to the last section of this report related to skim milk powder (SMP).

CHEESE

Production, Supply and Distribution (PS&D)

Dairy, Cheese*	2019		2020		2021	
	USDA Official	NEW Post Data	USDA Official	NEW Post Estimates	USDA Official	NEW Post Forecast
Canada						
Beginning Stocks	85	85	85	85	0	85
Production	519	515	525	510	0	515
Total Imports	36	36	40	40	0	45
Total Supply	640	636	650	635	0	645
Total Exports	12	12	12	10	0	10
Total Dom. Consumption	543	539	553	540	0	550
Ending Stocks	85	85	85	85	0	85
Total Distribution	640	636	650	635	0	645

*Please note that starting with the 2018 annual report cheese data includes “cottage cheese”. Data in 1,000 metric tons. Imports include re-exports.

NOTE: "NEW Post" data reflect author's assessments and are NOT official USDA data

Production

Cheese production has been one of the driving forces behind the recent expansion in milk production in Canada, with an 18 percent increase between 2014 and 2018. However, as 2019 cheese production increased by 1 percent, production growth appeared to have leveled off as recently implemented trade agreements brought additional imported cheese volumes. Consequently, FAS/Canada estimates a 1 percent drop in cheese production in Canada in 2020, down to 510,000 MT, and forecasts a recovery in 2021, back to the pre-pandemic level of 515,000 MT.

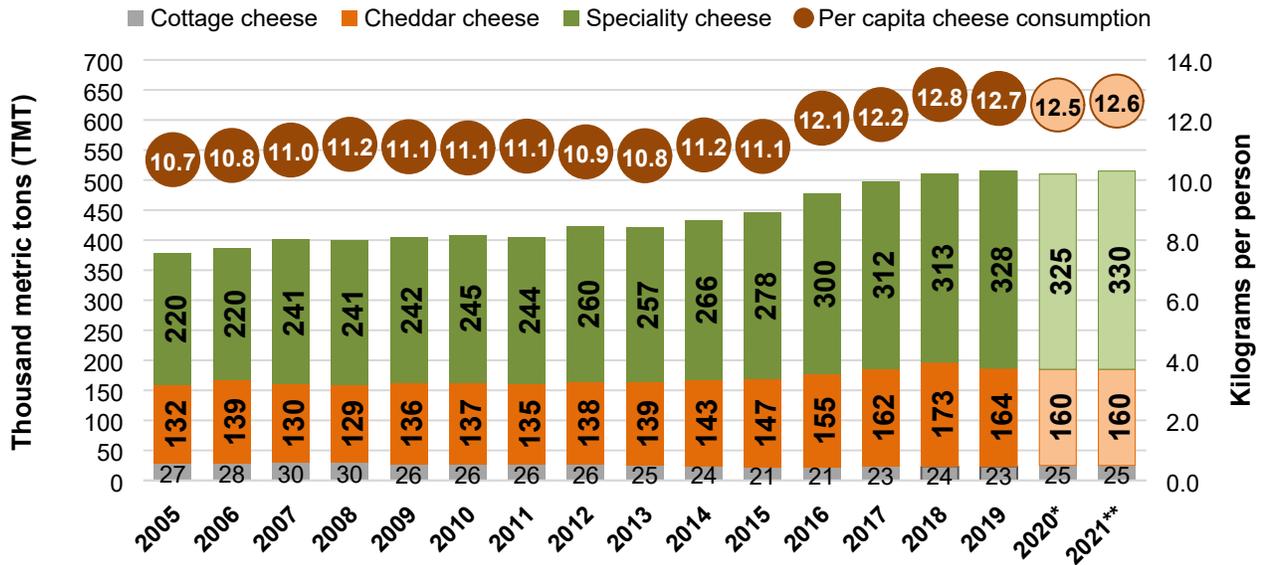
FAS/Canada estimates that cheese stocks have remained relatively stable over the past 12 months, falling to 80,000 MT in August 2020 from an estimated level of 85,500 MT in summer of 2019. Larger volumes of cheese imported from European Union and CPTPP countries, and from the United States are expected to increasingly compete with Canadian cheese and to put downward pressure on retail prices.

Consumption

The recent positive change in consumer perception towards consuming foods rich in butterfat has also had an impact on cheese consumption. After a flat or declining trend over a long period, Canadians started to increase their consumption of cheese in 2014, peaking at 12.8 kilograms per capita in 2018.

While cheese remains popular, consumption growth appears to have leveled off in 2019. Strong retail grocery demand for cheese, either directly or in processed products, has only partially offset weaker demand from the food service sector in 2020 as COVID-19 restrictions are expected to push sales down by as much as a third. For more information on the Canadian food service sector, please refer to [GAIN Report CA2020-0086](#). FAS/Canada forecasts per capita consumption at 12.5 kilograms in 2021, flat from the estimated level in 2020. In overall volume, cheese consumption is forecast to reach 550,000 MT in 2021, up from an estimated level of 540,000 MT in 2020.

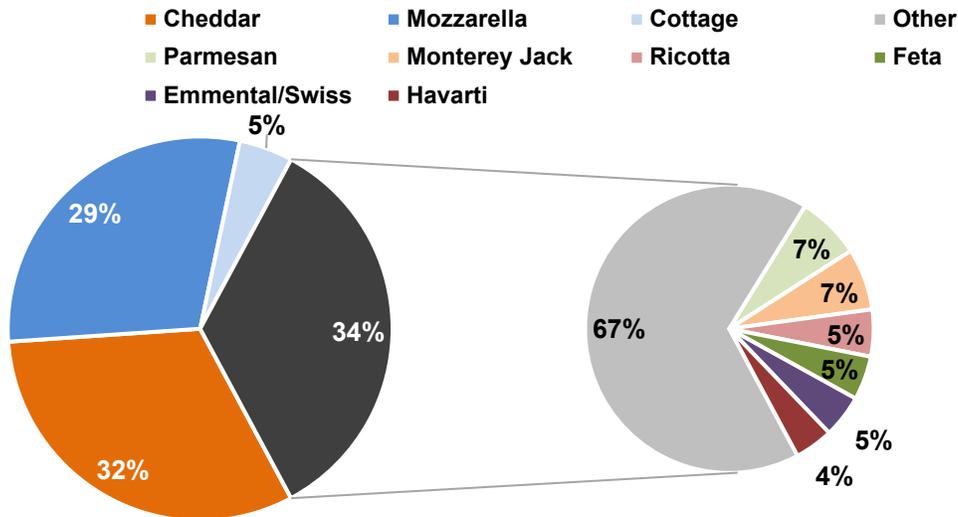
Cheese Production and Consumption in Canada



Source: Statistics Canada and FAS/Canada *estimate **forecast

Consumption of various types of cheese in Canada largely mirrors the domestic production pattern. After cheddar, which represents one third of cheese consumed in Canada, the second largest type of cheese consumed is mozzarella at about 30 percent of the total. Mozzarella is widely used in fresh and frozen pizza, but also as an ingredient in a variety of further processed food products such as lasagna and other pasta-based dishes.

Canadian Cheese Production in 2019



Source: Statistics Canada

Cottage cheese represents about 5 percent of total cheese consumed in Canada, while the remaining one third of total cheese consumed is composed of various types of specialty cheeses. Many of these specialty cheeses are used industrially as ingredients in further processed foods, while others are typically used on hamburgers, sandwiches, and subs (like Swiss, Monterey Jack, Havarti, or Provolone).

A smaller percentage of the specialty cheese consumed in Canada is the fine cheese category, which would include cheeses like Parmesan, blue cheeses, and a variety of fine hard cheeses (such as Asiago) and fine soft cheeses (like Camembert). However, industry sources indicate that the market for these fine cheeses is growing, as Canadian consumers are exposed to an increasingly wider array of choices, including via additional imports of fine cheeses under trade agreements with the European Union and, going forward, the United States. In addition, recent immigration patterns have also expanded the market for specialty cheeses from the Middle East and Latin America.

Trade

FAS/Canada forecasts cheese imports to reach 40,000 MT in 2020, before climbing to 45,000 MT in 2021, based on expanded imports from the European Union (as CETA TRQs enter the fifth year of implementation), from CPTPP countries (as those cheese TRQs enter the fourth year of implementation), and from the United States (as USMCA cheese TRQs will enter the second year of implementation).

Canadian Cheese Imports: Year-to-Date Data (January-July)

Canada Import Statistics

Commodity: HS 0406, Cheese And Curd

Year To Date: January - July

Partner Country	Unit	Quantity			% Share			% Change 2020/2019
		2018	2019	2020	2018	2019	2020	
World	T	16,355	17,152	17,867	100.00	100.00	100.00	4.17
EU28	T	10,078	10,787	11,696	61.62	62.89	65.46	8.43
United States	T	4,154	4,667	4,700	25.4	27.21	26.31	0.71
Switzerland	T	1,143	1,117	880	6.99	6.51	4.93	-21.2
Norway	T	860	308	203	5.26	1.79	1.14	-33.93
New Zealand	T	41	93	226	0.25	0.54	1.27	143.1
Australia	T	5	103	90	0.03	0.60	0.50	-13.16
Other countries	T	74	77	72	0.45	0.45	0.40	-6.49

Source: Trade Data Monitor

Under its WTO commitments, Canada maintains an annual all-cheeses [TRQ](#) of 20,412 MT. Of this total TRQ volume, 14,272 MT (70 percent) are allocated to EU members (per Canada's WTO commitment) and the balance is made available to imports from all countries. The volumes are allocated to historical [importers](#) of cheese (83 companies) and the 2019 TRQ fill rate was 97 percent.

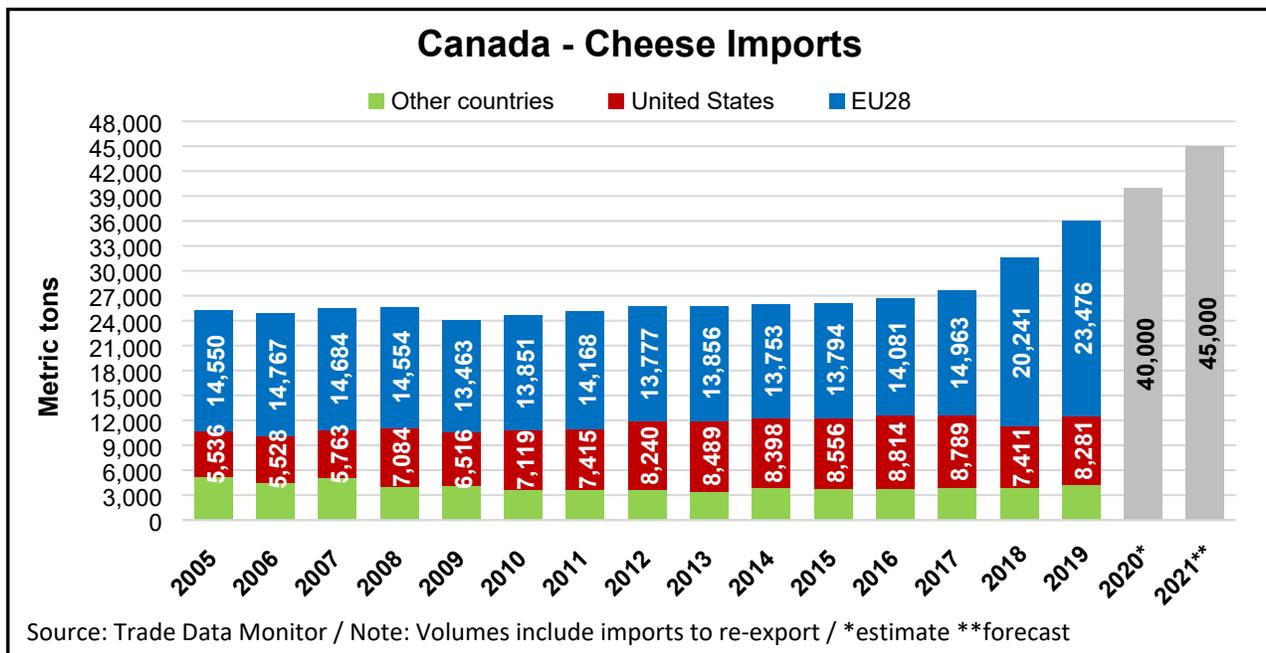
Canada provides additional access to EU members under two [CETA](#) TRQs: an industrial cheese TRQ, and an all-cheese TRQ. Both TRQs are being phased in over a six-year period.

Quota Year (January-December)	Industrial Cheese (in MT)	All Cheeses (in MT)
2017	79	745
2018	567	5,333
2019	850	8,000
2020	1,133	10,667
2021	1,417	13,333
2022 and onward	1,700	16,000

The CETA [all-cheeses TRQ](#) is allocated to two categories of [importers](#); dairy processors (about 50 companies) and distributors/retailers (about 165 companies) each receive 50 percent of the total TRQ volume. In each category, 30 percent of the total TRQ volume is allocated to small and medium-sized companies (equaling 60 percent of the total all-cheeses TRQ volume) and 20 percent of the total TRQ volume is allocated to large companies (constituting 40 percent of the total all-cheeses TRQ volume).

The CETA [industrial cheese TRQ](#) is entirely allocated to [further processors](#) (9 companies), defined as companies that use cheese as an ingredient in the production of further processed food products, other than cheese, in their own provincially-licensed or federally-registered processing facilities.

In 2019, the CETA all-cheeses TRQ fill rate reached 98 percent, while the CETA industrial cheese TRQ was 78 percent filled. Compared to the WTO cheese TRQ, both CETA cheese TRQs tend to lag behind in terms of fill rates during the quota year, and FAS/Canada estimates that in 2020 large volumes will once again be imported during the last quarter of the TRQ year (October to December).

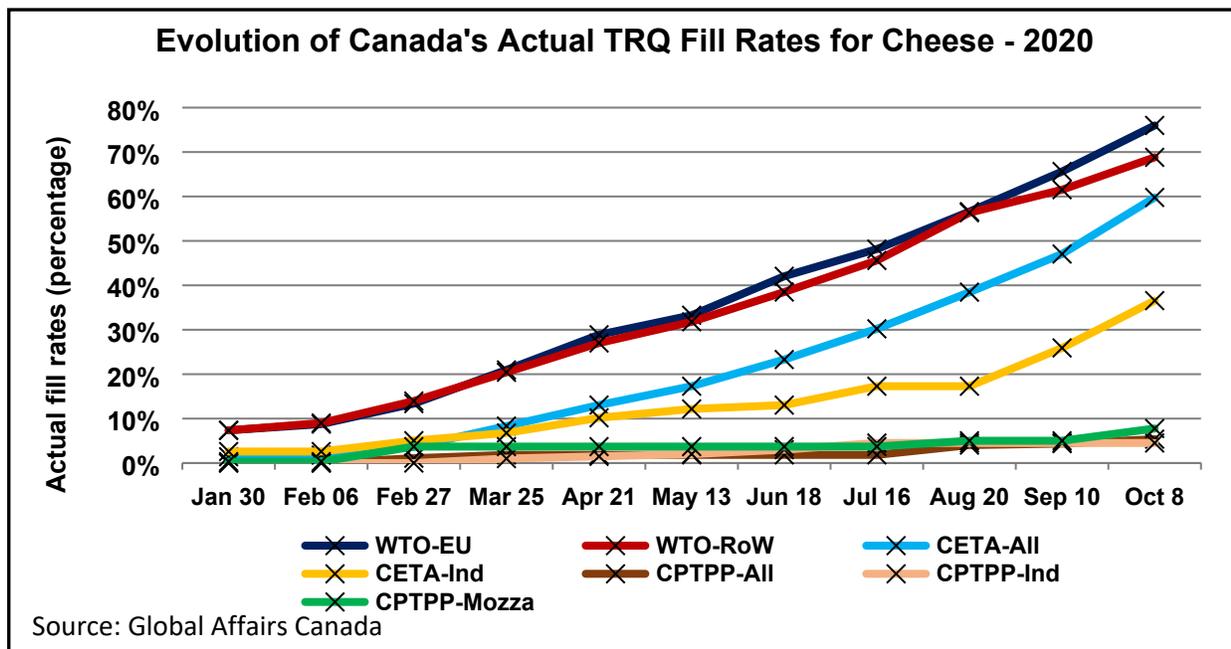


The [CPTPP](#) entered into force on December 30, 2018. Under this agreement, Canada agreed to three [TRQs](#) for cheese, which provide the following levels of market access:

Quota Year (January-December)	Industrial Cheese (in MT)	Mozzarella and Prepared Cheese (in MT)	All Cheeses
2018 (year 1)	1,329	483	604
2021 (year 4)	5,317	1,933	2,417
2023 (year 6)	7,975	2,900	3,625
2036 and onward	9,076	3,300	4,126

Similar to CETA cheese TRQ trends, the fill rates for the CPTPP cheese TRQs observed throughout 2020 lagged behind the fill rate for the WTO cheese TRQ. FAS/Canada estimates improvement in these fill rates toward the end of 2020. In 2019, the fill rates for the CPTPP TRQs were: all cheeses 57 percent, mozzarella and prepared cheeses 44 percent, and industrial cheese 12 percent.

The table below presents the evolution of the fill rates for various cheese TRQs, as observed at several points during 2020. Global Affairs Canada publishes regular reports on cheese TRQ [utilization](#) rates.



Under the [USMCA](#), Canada committed to two [TRQs](#) for cheese, which provide the following levels of market access:

Quota Year (January-December)	Industrial Cheese (in MT)	All Cheeses (in MT)
July-December 2020 (year 1)	521	521
2021 (year 2)	2,083	2,083
2025 (year 6)	6,250	6,250
2038 and onward	7,113	7,113

The USMCA cheese TRQs are available exclusively to imports from the United States. The USMCA also includes provisions to ensure the cheese TRQs volumes are allocated in commercially viable shipping quantities. FAS/Canada expects the USMCA all cheeses TRQ to fill completely, although the fill level for the industrial cheese TRQ is expected within the range of fill rates observed for other industrial cheese TRQs (CETA and CPTPP).

Under the USMCA, the United States opened a [TRQ](#) for imports of cheeses of all types from Canada. The market access available under this TRQ covers an initial 2,083 MT of cheese in year one of implementation, rapidly increasing to 12,500 MT in year six of implementation, then gradually increasing to 14,226 MT by year 19 of implementation. After that, the volume will remain constant at 14,226 MT per year.

Cheese is a product eligible under Global Affairs Canada’s policy for [supplementary imports](#), which includes the [Imports for Re-Export Program](#) (IREP). A program similar to IREP, called the [Duties Relief Program](#) (DRP), is operated by the Canada Border Services Agency. Under both the IREP and DRP, Canadian food manufacturers may import cheese to use in processed food products, provided that such products do not enter the domestic market and are eventually exported.

Policy

In response to the COVID-19 pandemic, the federal government [announced](#) a \$200 million CAD increase to the Canadian Dairy Commission’s (CDC) borrowing limit (from \$300 million CAD to \$500 million CAD) to enable the CDC to increase its temporary purchase and storage of butter and cheese to help balance market supply and demand. According to announced [program details](#), the CDC would purchase products from dairy processors under a contractual commitment that these companies buy them back at the selling price, at a later date when market conditions improve. No data is currently available on the usage of this program by dairy processors. As increasing CDC’s borrowing limit required a legislative change and parliamentary approval, this policy change is likely to remain in place beyond the COVID-19 pandemic, unless Parliament takes another legislative action to revert the borrowing limit to its pre-pandemic level.

BUTTER

Production, Supply and Distribution (PS&D):

Dairy, Butter Canada	2019		2020		2021	
	USDA Official	NEW Post Data	USDA Official	NEW Post Estimates	USDA Official	NEW Post Forecast
Beginning Stocks	33	33	37	27	0	28
Production	112	112	115	120	0	122
Total Imports	25	24	25	25	0	27
Total Supply	170	169	177	172	0	177
Total Exports	2	2	2	4	0	2
Domestic Consumption	131	140	137	140	0	142
Ending Stocks	37	27	38	28	0	33
Total Distribution	170	169	177	172	0	177

NOTE: "NEW Post" data reflect author's assessments and are NOT official USDA data

Data in 1,000 metric tons. Imports include re-exports.

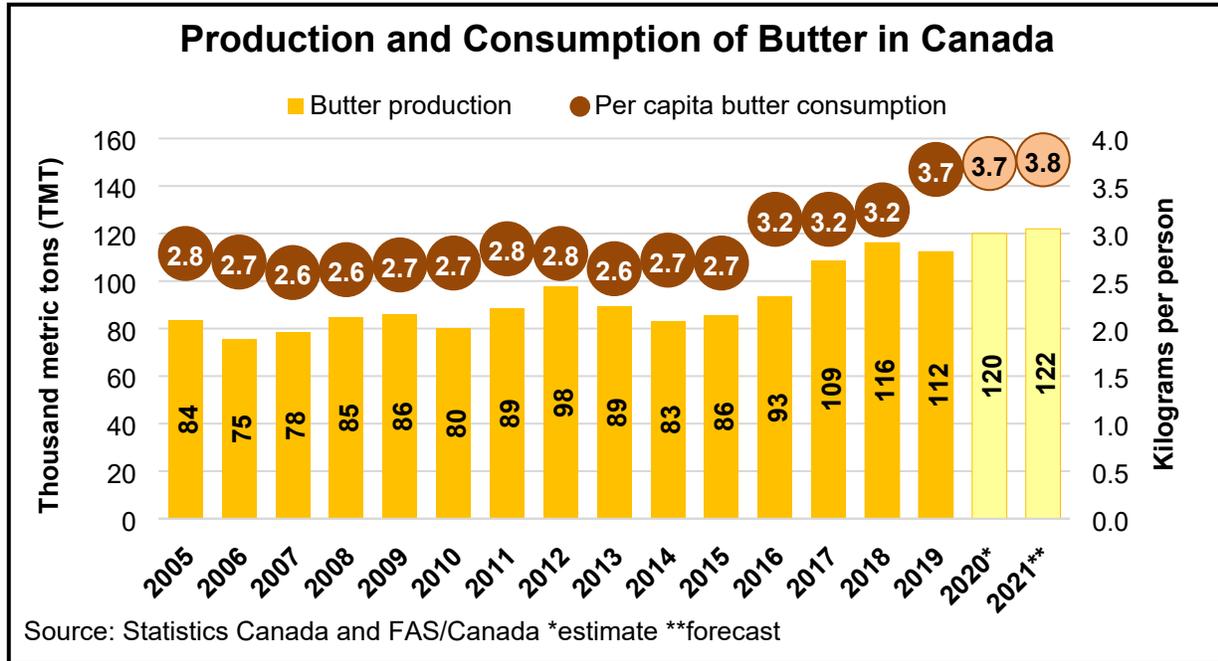
Production

FAS/Canada forecasts butter production in 2019 to increase to 120,000 MT before climbing further to 122,000 MT in 2020. The COVID-19 pandemic had a minimal impact on butter demand in Canada as the decline in consumption through the food service sector was partially offset by increased consumption at retail level and in commercial manufacturing of baked goods. Gradually declining butter stocks, which reached 28,000 MT in August 2020 (significantly below the industry target of 35,000 MT), further support the production increase forecast.

Between 2014 and 2018, butter production increased by nearly 40 percent, reflecting Canadian consumers' sudden, strong increase in demand for butterfat. Even with the unprecedented growth in production, Canada required supplemental imports in 2016 and 2017 to satisfy market demand. During summer 2019, butter stocks reached over 45,000 MT, far exceeding the industry target of 35,000 MT. This sent a market signal to processors to scale back butter production, which eventually drove 2019 butter production three percent below the 2018 production level.

Consumption

Butter consumption has expanded rapidly over the past seven years and is forecast to rise to 3.8 kilograms per capita in 2021, up from about 2.6 kilograms per capita in 2013. After highly publicized media reports on academic research, Canadian consumers' perception of the health attributes of foods rich in butterfat changed dramatically during that period, driving butter consumption up sharply. In 2020, butter consumption through the COVID-19 pandemic remained steady, as the decline in sales via the food service sector was matched by increases in the retail sector.



Trade

FAS/Canada forecasts butter imports to grow to 25,000 MT in 2020 and to rise further in 2021, reaching 27,000 MT.

Canadian Butter Imports: Year-to-Date Data (January-July)

Canada Import Statistics

Commodity: HS 0405, Butter And Other Fats And Oils Derived From Milk

Year To Date: January - July

Partner Country	Unit	Quantity			% Share			% Change 2020/2019
		2018	2019	2020	2018	2019	2020	
World	T	11,480	12,744	12,631	100	100	100	-0.89
New Zealand	T	3,526	7,404	6,467	30.72	58.1	51.2	-12.66
United States	T	7,820	4,849	4,525	68.12	38.05	35.83	-6.69
Ireland	T	0	226	659	0	1.78	5.22	191.21
United Kingdom	T	0	0	882	0	0	6.98	
Other countries	T	134	265	98	1.17	2.08	0.78	-63.02

Source: Trade Data Monitor

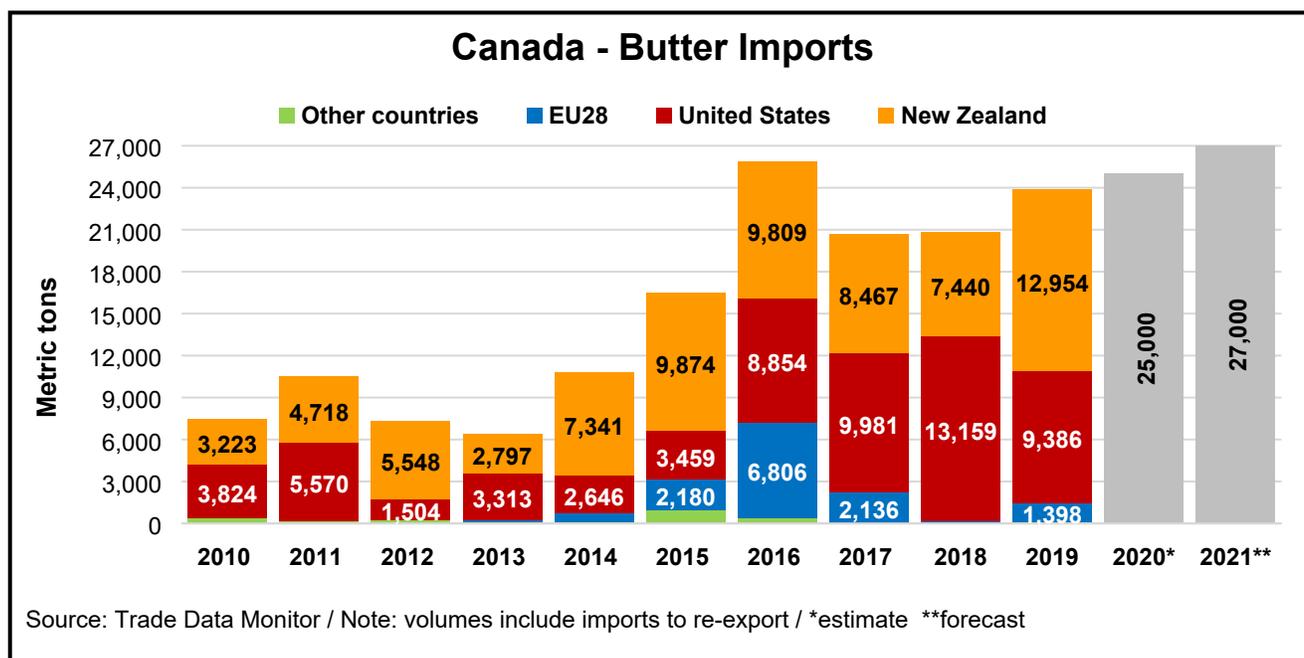
Under WTO commitments, Canada maintains a [TRQ](#) for butter, dairy spreads and fats and oils derived from milk. The total TRQ volume is 3,274 MT, of which 2,000 MT is a country-specific allocation to New Zealand. The entire TRQ volume is [allocated](#) to the Canadian Dairy Commission which imports the butter and re-sells it on the domestic market for use in food processing.

Under the [CPTPP](#) (which entered into force on December 30, 2018), Canada agreed to a [TRQ](#) for butter which would provide the following market access:

Quota Year (August to July)	Butter (in MT)
2018/19 (year 1)	750
2020/21 (year 3)	2,250
2023/24 (year 6)	4,500
2031/32 and onward	5,121

Up to 85 percent of this TRQ is to be [allocated](#) to bulk imports of butter (not for retail sale) to be used in further food processing. FAS/Canada estimates the CPTPP butter TRQ to be fully filled.

In any given year, actual imports of butter into Canada typically exceed the TRQ volumes. This is due to the fact that butter is a product eligible under Global Affairs Canada’s policy for [supplementary imports](#), which includes the [Imports for Re-Export Program](#) (IREP). A program similar to IREP, called the [Duties Relief Program](#) (DRP), is operated by the Canada Border Services Agency. Under both the IREP and DRP, Canadian food manufacturers may import butter to use in processed food products, provided that such products do not enter the domestic market and are eventually exported. Of all butter imported in excess of the WTO and CPTPP TRQs, the vast majority is imported under the IREP and DRP.



Under the [USMCA](#), Canada committed to a [TRQ](#) for butter and cream powder, which would provide market access as follows:

Quota Year (August to July)	Butter and Cream Powder (in MT)
July 2020 (year 1)	750
2020/21 (year 2)	1,500
2024/25 (year 6)	4,500
2037/38 and onward	5,121

According to USMCA commitments, up to 85 percent of the butter and cream powder TRQ volume in year 1 of implementation could be allocated for further processing (not for retail sale), with the obligation to gradually reduce this percentage so that in year 5 of implementation only 50 percent of the TRQ is allocated for further processing, with the remaining volumes being made available for any use. Based on the current [allocation](#) policy for this TRQ, for marketing year 2020/21, 80 percent of the total volume must be imported in bulk for use in further food processing. The USMCA butter and cream powder TRQ is opened exclusively to imports from the United States, and FAS/Canada expects this TRQ to fill completely.

Under the USMCA, the United States also committed to open an aggregated [TRQ](#) for Canada to cover butter, fluid cream (of minimum 45 percent butterfat content) and cream powder. The combined volume under this TRQ would be 750 MT in year one of implementation, after which the volume would rapidly increase to 4,500 MT in year six of implementation, then would gradually increase to 5,121 MT by year 19 of implementation. After that, the volume will remain constant at 5,121 MT annually.

SKIM MILK POWDER

Production, Supply and Distribution (PS&D):

Dairy, Milk, Nonfat Dry Canada	2019		2020		2021	
	USDA Official	NEW Post Data	USDA Official	NEW Post Estimates	USDA Official	NEW Post Forecast
Beginning Stocks	29	29	30	30	0	30
Production	100	97	105	90	0	80
Total Imports	4	3	4	2	0	2
Total Supply	133	129	139	122	0	112
Total Exports	47	47	60	50	0	30
Total Dom. Consumption	56	52	59	42	0	52
Ending Stocks	30	30	20	30	0	30
Total Distribution	133	129	139	122	0	112

NOTE: "NEW Post" data reflect author's assessments and are NOT official USDA data
Data in '1,000 MT

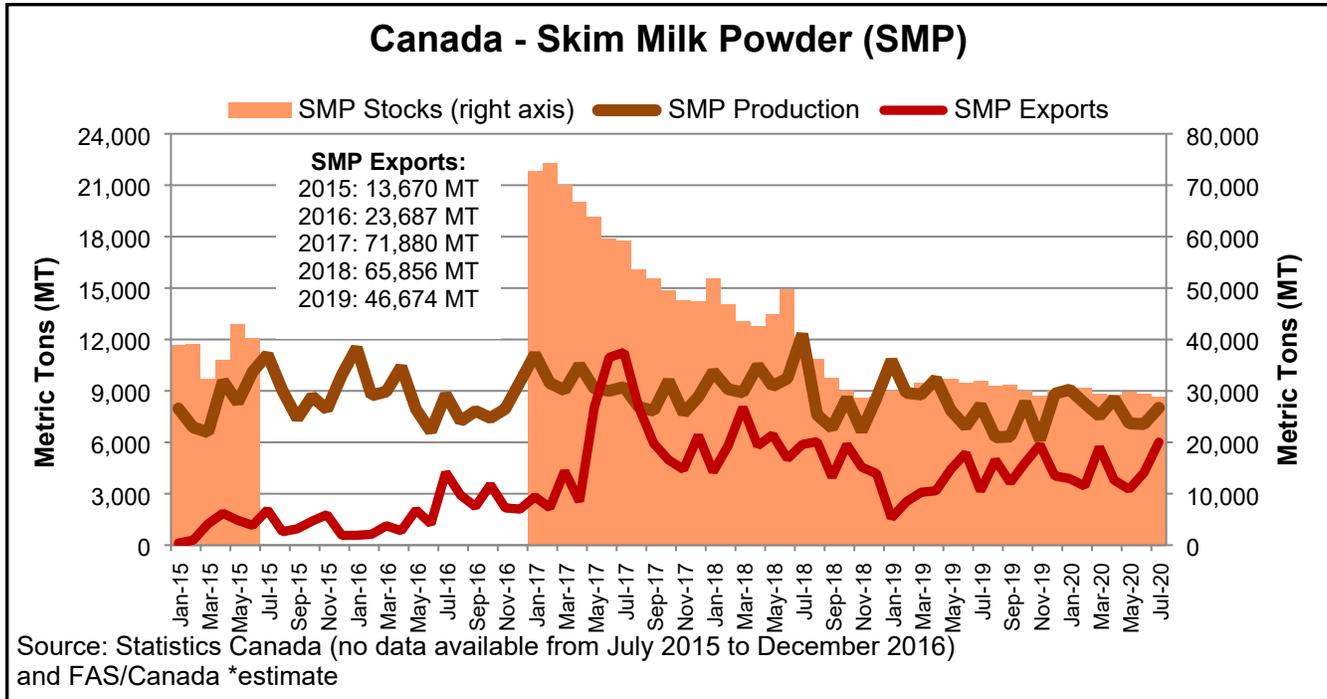
Production

FAS/Canada forecasts skim milk powder (SMP) production to drop to 80,000 MT in 2021, for a second consecutive year decline from the estimated level of 90,000 MT in 2020. While typically, SMP production follows the trends in butter production, as skim milk is largely a by-product of processing milk into butter, the anticipated decline in SMP production is rather related to the dairy industry shifting its focus toward products with a higher concentration of protein, like milk protein concentrates (MPC) and milk protein isolates (MPI).

Between 2014 and 2018, SMP production in Canada increased by 32 percent, reflecting sharply higher butter production. In addition, over the past three years, SMP production in Canada was also supported by milk price class 7. As part of Canada's "National Ingredient Strategy," milk price class 7 became effective on February 1, 2017. Class 7, also called the National Ingredient Class, included milk processed for specific ingredients, including SMP. For a further discussion of the introduction of class 7 and its effects, please see the July 2017 issue of [Dairy: World Markets and Trade](#), published by the Foreign Agricultural Service.

Following the introduction of class 7, the Canadian Dairy Commission (CDC) stopped purchasing and storing SMP under its Surplus Removal and Domestic Seasonality Programs. The CDC also stopped exporting SMP. In turn, Canadian dairy processors became responsible for managing SMP stocks. Prior to February 2017, the largest disposal market for surplus SMP was the domestic animal feed market. As SMP export prices are typically higher than domestic animal feed prices, Canadian processors began exporting increasingly large amounts of SMP to draw down SMP stocks. SMP stocks fell to nearly 29,000 MT in August 2020, declining from their February 2017 peak of 73,000 MT.

With the implementation of USMCA on July 1, 2020, Canada became subject to provisions that would apply an export surcharge on exports of SMP and MPC products in excess of 35,000 MT in marketing year 2020/21; MPI exports are not covered by these provisions. These trade commitments explain why the dairy processing sector is expected to increasingly focus on producing and exporting MPIs, products with a very high protein concentration, rather than SMP and MPCs.



Consumption

Following the introduction of milk class 7, Canadian processors have been able to access domestically produced non-fat milk solids (including SMP and MPC) at lower prices. These non-fat milk solids are used as ingredients in manufacturing various dairy products such as cheese, yogurt and ice cream. Going forward, it is expected that SMP will be in part replaced by MPC in dairy manufacturing, therefore FAS/Canada estimates Canadian utilization of SMP to remain relatively stable around 50,000 MT annually.

Trade

Exports

Following the introduction of Class 7, Canadian SMP exports grew to record high levels, reaching nearly 72,000 MT in 2017. However, as production leveled off and stocks declined, and because of USMCA provisions, FAS/Canada forecasts SMP exports to fall to 30,000 MT in 2021, from an estimated level of 50,000 MT in 2020.

The increase in SMP exports between 2019 (nearly 47,000 MT) and 2020 (estimated at 50,000 MT) can be explained by Canadian dairy processors front-loading exports of SMP ahead of USMCA and its export-limiting provisions entering into force on July 1, 2020. In addition, export data reveal a shift in focus toward exporting increasing volumes of MPC and MPI, a trend which FAS/Canada expects to continue in the coming years.

Under the [USMCA](#), Canada is subject to certain export-limiting [provisions](#), including an annual threshold for combined exports of SMP and MPC, after which an export charge of \$0.54 CAD per kilogram would apply

to volumes in excess of the threshold. These provisions apply on a marketing year (MY) basis, starting in August until the July of the following year.

With USMCA coming into force on July 1, 2020, year 1 of implementation for the export-limiting provisions was the period July 1-31. During this period, the export threshold was 55,000 MT, and Canadian exports of SMP and MPC did not exceed this volume.

For MY 2020/21 (August 1, 2020 to July 31, 2021, or year 2 of implementation), the export threshold is 35,000 MT. Going forward, for each subsequent marketing year, the export threshold will increase by 1.2 percent on an annual basis.

In addition to SMP and MPC, USMCA includes similar export-limiting provisions for infant formula. The year 1 (July 2020) threshold was 13,333 MT (which Canada did not exceed), and the year 2 threshold is 40,000 MT. The export charge for volumes exceeding the threshold is \$4.25 CAD per kilogram. After year 2, the export threshold for infant formula will also increase by 1.2 percent on an annual basis. Global Affairs Canada has a [webpage](#) dedicated to dairy export thresholds.

Canadian Exports of Skim Milk Powder: Year-to-Date Data (January-July)

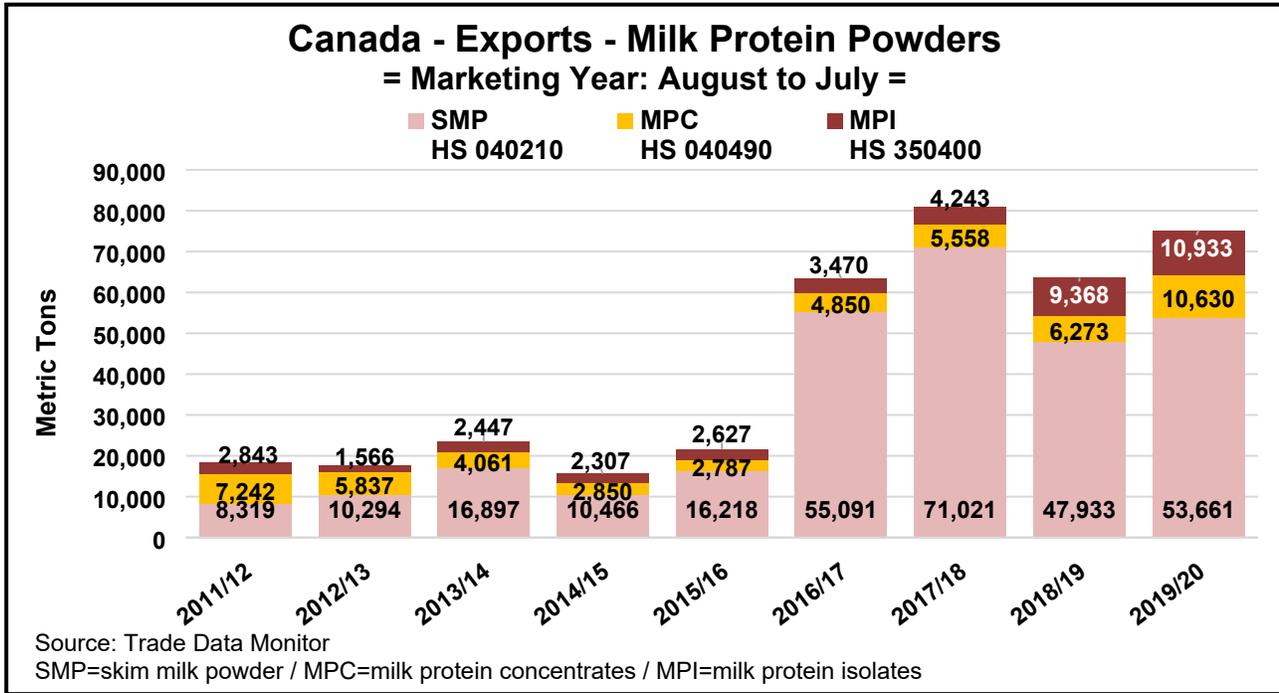
Canada Export Statistics

Commodity: HS 040210, Skim Milk Powder

Year To Date: January - July

Partner Country	Unit	Quantity			% Share			% Change
		2018	2019	2020	2018	2019	2020	2020/2019
World	T	41,270	23,348	30,335	100	100	100	29.93
Egypt	T	7,079	4,958	7,539	17.15	21.24	24.85	52.05
Algeria	T	9,123	5,353	5,997	22.11	22.93	19.77	12.04
Vietnam	T	200	250	4,741	0.49	1.07	15.63	1797.07
Indonesia	T	800	2,259	1,775	1.94	9.68	5.85	-21.42
United Arab Emirates	T	1,845	550	1,750	4.47	2.36	5.77	218.19
Saudi Arabia	T	275	175	1,325	0.67	0.75	4.37	656.87
Philippines	T	3,939	1,548	1,031	9.54	6.63	3.4	-33.41
Jamaica	T	870	737	844	2.11	3.16	2.78	14.47
Japan	T	3,025	225	794	7.33	0.96	2.62	252.77
Syria	T	3,049	475	599	7.39	2.03	1.98	26.12
Malaysia	T	1,725	1,250	500	4.18	5.35	1.65	-59.99
Jordan	T	875	25	466	2.12	0.11	1.54	1763.7
Other countries	T	8,465	5,543	2,974	20.51	23.74	9.80	-46.35

Source: Trade Data Monitor



Imports

Under the [CPTPP](#) (which entered into force on December 30, 2018), Canada agreed to a [TRQ](#) for SMP which would provide market access as follows:

Quota Year (August to July)	Skim Milk Powder (in MT)
2018/19 (year 1)	1,250
2019/20 (year 2)	2,500
2020/21 (year 3)	3,750
2023/24 (year 6)	7,500
2031/32 and onward	11,014

Given the domestic availability of protein ingredients at competitive prices, FAS/Canada does not estimate that the CPTPP SMP TRQ will fill.

Under the [USMCA](#), Canada committed to a [TRQ](#) for SMP, which provides market access as follows:

Quota Year (August to July)	Skim Milk Powder (in MT)
July 2020 (year 1)	1,250
2020/2021 (year 2)	2,500
2024/25 (year 6)	7,500
2037/38 and onward	8,536

This SMP TRQ is exclusively opened to imports from the United States, however, given the domestic availability of protein ingredients at competitive prices, FAS/Canada does not estimate that the USMCA SMP TRQ will fill.

Under the USMCA, the United States opened a [TRQ](#) for imports of Canadian SMP. The market access provided under this TRQ started at 1,250 MT in year one of implementation, after which the volume will rapidly increase to 7,500 MT in year six of implementation, before gradually increasing to 8,536 MT by year 19 of implementation. After that, the volume would remain constant at 8,536 MT annually.

Attachments:

No Attachments