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Dairy

Dairy Report

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Report Highlights:

The slowdown of Brazil's economy in 1998 is reflected in the dairy industry which faces weakening demand, notably for some dairy products such as yogurts and milk drinks. However, fluid milk production will likely increase by 5 percent in 1998 due to higher productivity, but the rate of growth will decline in 1999. Production of other dairy products will follow the same trend. Producer efforts to restrict imports may cause import growth of dairy products to decline in 1999. A producer effort to raise the duty on imported whey powder from third countries directly threatens an important U.S. export item to this market.

Includes PSD changes: Yes

Includes Trade Matrix: Yes

Annual Report

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Executive Summary

Milk production in 1998 has been influenced by conflicting factors: Weather problems, particularly prolonged dryness in the Center-West; lower domestic demand for dairy products, reflected in lower milk prices; higher than expected dairy product imports. These were offset by higher productivity and increased production from non-traditional areas. We estimate fluid milk production in 1998 to show about 5 percent growth. Four percent is our current forecast for 1999 milk production growth.

Production of dairy products (cheese, powdered milk) will also increase in 1998 and 1999, but at slower rates because of slowing domestic demand for these products.

Imports of dairy products during Jan.-Aug. 1998 were higher than expected by most analysts, particularly in

view of measures taken by the government to restrict dairy product imports. Total volume imported was 22 percent above that in 1997's comparable period. Value was up by 12 percent. Volume of powdered milk and whey powder were up 24 and 193 percent, respectively. Cheese imports were down 25 percent.

The spread of the global financial and economic crisis to Latin America and Brazil has changed business expectations, and affected the dairy sector, particularly imports. The federal government is seeking new ways to restrict imports of food and agricultural products. The Brazilian economy has begun to slow, and economic growth is now projected to be around one percent (or less) in 1999, against perhaps 1.5 percent or less in 1998. Most economists forecast a recession next year. To attack the budget deficit, the government is implementing a new fiscal squeeze, aimed at increasing tax collections, and reducing government expenditure. This will clearly be de-stimulative to growth. The government is also carefully (to avoid loss of domestic competitiveness) applying non-tariff barriers to imports, while attempting to stimulate exports, to address the current account deficit. Both the fiscal and trade measures are essential to qualify for contingency support lines the government is negotiating with the IMF and other lenders. Such support is aimed at avoiding a devaluation and stemming the outflow of the borrowed dollars/foreign reserves used to underpin the domestic currency, the "real", which markets perceive to be overvalued.

Commodity Outlook for Fluid Milk

Production

Fluid milk production's growth in 1998 is expected to be about 5 percent, slower than the average of 8 to 10 percent in recent years. The slowing is attributed primarily to weaker domestic demand for dairy products, reflecting slowing economic, rising unemployment, and consumer purchasing power relatively stagnant.

The following factors continue to support Brazil's increasing fluid milk production:

a) Increased productivity. The major factor contributing to increased milk production in Brazil is the increase in productivity. It is estimated that productivity increases an average 5 to 8 percent a year because of the large investments made in dairy genetics. The United States is a major genetics supplier to Brazilian breeders, competing with Canada and the European Union. In 1997, imports of dairy semen increased by 25 percent, and since 1990 imports of dairy semen have increased by over 120 percent. OAC is working with average annual milk production of 1,280 liters/cow for 1998, which is 6 percent higher than last year.

The use of BST (Bovine Somatotropin) to increase milk yields is still very small in Brazil, and is not a major factor in the increase in milk productivity. Brazilian dairy breeders can more than double productivity by just investing in genetics, management practices and nutrition.

b) Mixed weather patterns. Milk production in Brazil is still highly seasonal because practically all cows are grass fed. Thus favorable pasture conditions are critical to yields. In 1998, pasture conditions were reported poor in the Center-West regions due to the prolonged dry weather. Pastures were excellent in the South and Southeast regions, which had above average rainfall.

c) Investments in the dairy sector. Milk production in Brazil has also increased due to investments production and processing in non-traditional milk producing areas, such as the state of Goiás, now believed to be Brazil's second leading milk producing state (after Minas Gerais). Investments in the Center-West region are primarily

aimed at reducing production costs, using cheaper land and labor, and feed available at lower cost in this region to supplement cattle during the dry season. The development of UHT (ultra high temperature) long-shelf-life milk packaging facilities in this area, and consumers' acceptance of this product also supported an increase in milk production in these areas because it enabled milk from these areas, more remote from consumers, to be transported economically over longer distances to market.

d) Price. Although the price of milk dropped nearly 13 percent during Jan. - August 1998, relative to the same period in 1997, this level still provides good returns to specialized dairy producers with higher productivity. The problem with producer prices in Brazil is the extra quota price, which dropped significantly last year.

Consumption

Higher unemployment and the financial squeeze most Brazilians are now facing will likely keep expansion of dairy product consumption at more moderate levels than in the past 4 years. Demand for fluid milk will continue to increase for UHT (ultra high temperature) milk because of several factors, including greater convenience to consumers; carton packaging, not glass; refrigeration is unnecessary; the milk has a longer shelf-life; and competitive pricing. In fact, the price premium for UHT milk over milk type "C" is down from an average of 40 percent 3 years ago to an estimated 5 percent.

"C" type milk remains the most widely consumed, with its standard 3 percent butterfat content. However, C milk's consumer image has declined as other grades' packaging has improved, and because it is often sold in soft plastic bags, (sealed at the dairy) and may not always meet normal sanitation requirements established by the Ministry of Agriculture. C milk is highly perishable, which in a tropical country such as Brazil, becomes a major negative for consumers.

Trade

Brazil imports small amounts of fluid milk (most is packaged UHT type) from Argentina and Uruguay. Most of this milk comes from Argentine companies with commercial interests in Brazil. There are no reliable trade data for imports of UHT milk.

Policy

There is no specific federal program to increase milk production in Brazil, but there are funds within the rural credit program for major dairy cooperatives and large dairy companies to foster members' milk production. Although these company programs are aimed at improving quality and reducing costs, they contribute to increase milk production because they encourage technology improving investments. Large multinational dairy companies can borrow large amounts of money, an average US\$40,000 per producer, under the subsidized rural credit system and lend to their milk suppliers (6 to 8 percent per annum, compared to 20 percent interest rates available to other dairies.) Most of the investments go for improving pastures, dairy genetics and coolers.

Commodity Outlook for Cheese

Production

Cheese production is up 4 percent reflecting demand from the fast food industry, the lower price of fluid milk, and less competition from cheese imports. Import competition declined because the government raised the import tariff from 19 to 33 percent for cheese imported from sources outside the MERCOSUL. In addition, the government has tighten the sanitary control on imported milk.

Consumption

The growth of the fast food industry in Brazil continues to boost demand for cheese, mostly mozzarella type, but also cheddar. However, domestic consumption of cheeses will likely increase at a more modest pace than over the past several years because of the bleak economic outlook.

The current average Sao Paulo wholesale price of domestic cheese by major type are:

Type	US\$/Kilogram
Minas (fresh)	4.24
Mozzarella	3.65
Provolone	5.25
Parmesan	5.40

Trade

Brazil's cheese imports are declining in 1998 for the third consecutive year, and continue to shrink in 1999. Lower imports are due in part to the hike in the import tariff from 19 to 33 percent for 1998. During 1996 and 1997, the government changed the import tariff for cheese more than five times, and tighten sanitary and inspection controls on imported cheese. The import duty for cheese from third countries (others than MERCOSUL) is scheduled to drop to 30 percent in 1999. However, the government has recently reduced the maximum import payment period for imported cheeses from 365 to 30 days maximum to avoid financial gains on import transactions due to internal high interest rates in Brazil.

For a special report on changes in the import tariffs for dairy products, including cheese, please see BR8606, dated 2/20/1998.

Although small, U.S. market share of imported cheeses is expected to double in 1998 from 6 to nearly 12 percent. This is mainly attributed to higher demand for cream cheese, cheddar and mozzarella.

Commodity Outlook for Butter

Production

Butter production in 1998 is expected to decline by nearly 3 percent, reflecting strong competition from margarine and lower industrial use for rehydrated milk.

Continued replacement of butter by margarine reflects price competition among margarine producers. Margarine production will likely increase by 5 percent in 1998, and reach 685,000 metric tons.

Wholesale prices in Sao Paulo by butter are:

Type	US\$/Kilogram
Salted	3.60
Unsalted	3.40

Trade

Butter imports are expected to increase by 3 percent in 1998, mostly due to higher imports from Uruguay, which benefits from MERCOSUL zero import tariff.

Commodity Outlook for Powdered Milk

Production

There are no official statistics on production of powdered milk in Brazil. OAC estimates for powdered milk production are based on interviews with trade contacts.

Brazil's powdered milk production is expected to increase by about 4.2 percent in 1998, and to reach 298,000 metric tons, of which 240,000 mt is expected to be whole milk powder (WMP), and 58,000 mt would be nonfat dry milk powder (NDM). The increase in WMP production (up from 231,000 mt in 1997) reflects higher use of whole milk in social programs, mostly by some state governments, since the federal government has not included WMP in its "basic food basket" for donations to the poor and drought affected people in the Northeast. Production of NDM is expected to increase by 5 percent, the higher growth rate reflecting higher use of NDM by the food industry.

The outlook for 1999 calls for a modest increase in production of powder milk at a lower average rate of 3 percent reflecting the slower economy, and likely weaker food-industry demand. It is not clear yet whether the federal government's 1999 social programs will include powder milk under the "basic food basket" because of the fiscal squeeze and budget cuts. If powder is included, the 1999 production and imports of powder milk could turn out higher than currently estimated.

Trade

Powdered milk imports are up a surprising 24 percent in volume in Jan. - Aug. of 1998, over the same period last year, despite the policy measures implemented early in 1988 to restrict imports of subsidized dairy products in general. For the entire year, however, OAC estimates imports will be up by only 16 percent, in view of an expected decline in the pace of imports during 1998's final quarter.

For a complete report on the changes in import tariffs for dairy products please see report BR8606, dated 2/20/1998. The import tariff for powder milk (both WMP and NDM) was raised in 1998 from 27 to 33 percent,

but it is to be reduced as of January 1, 1999 to 30 percent. The federal government has restricted the maximum import payment period for imports of powdered milk from 365 days to 30 days maximum.

Note: Brazil has become a major importer of whey powder. During Jan. - Aug. 1998, imports of whey powder increased by 193 percent, over the same period last year. The increase in imports of whey powder reflects the large increase in demand for flavored milk drinks in Brazil, and the fact that Brazilian and multinational dairy companies need to diversify their product lines in order to compete more efficiently. The continuation of increases in imports is clouded by domestic Dairymen's pressure on the government to raise import duties for whey (currently 17 percent) to 33 percent. Under current conditions, the United States is expected to increase its market share from 30 to 40 percent of Brazil's whey powder imports in 1998.

Policy

The focus of the Brazilian domestic dairy industry in 1998 has been on gaining import restrictions to address alleged disruption by imports of subsidized products, mostly powder milk. The first result of this pressure was tariff increases, reported under BR8606, dated 2/20/98. Import tariffs for most dairy products were raised.

The sharp tariff increases, aimed at restricting imports, may have simply encouraged higher internal prices, providing greater draw for duty free imports from MERCOSUL partners. Brazilian producers, surprised that imports continue to increase in 1998, are now pressuring the government for new actions, among which are the increase in the MEROSUR Common External Tariff (CXT), currently around 19 percent to 33 percent for most dairy products. However, this increase depends on negotiations with other MERCOSUL partners, primarily Argentina. Brazilian producers complain that Brazilian importers use so-called "triangle operations," importing subsidized powder milk from the European Union into Argentina and reselling to Brazil. One new measure already in force is the reduction in the maximum import payment period for imports of dairy products from 365 to 30 days.

The purpose of this measure is cut the financing benefit to importers of powder milk, whose external payment terms at 8 percent or less provided arbitrage gains by demanding prompt payment from internal dairy purchasers, and then investing the externally borrowed funds in the internal market at internal rates above 20 percent per annum.

Another objective of Brazilian dairy producers is to gain application of non-tariff barriers to imports of dairy products. Measures envisaged include pre-inspection of plants in the country of origin, certificate of origin, laboratory quality test of the product, and label registration of the product according to the Brazilian consumer law. Another non-tariff measure proposed would require the importer of powdered milk to register with the Ministry of Agriculture and meet sanitary measures. Several importers in Brazil are basically repackers of imported powder milk with no sanitary control by the government.

Brazilian producers are also requesting the Federal Government shift to use of UHT milk in social programs. This would further reduce the demand for imported powdered milk.

Tables

PSD: Dairy, Milk, Fluid

PSD Table						
Country:	Brazil					
Commodity:	Dairy, Milk, Fluid					
		1997		1998		1999
	Old	New	Old	New	Old	New
Calendar Year Begin		01/1997		01/1998		01/1999
Cows In Milk	17220	17067	17300	16900	0	16750
Cows Milk Production	20600	20600	21800	21630	0	22495
Other Milk Production	0	0	0	0	0	0
TOTAL Production	20600	20600	21800	21630	0	22495
Intra EC Imports	0	0	0	0	0	0
Other Imports	0	0	0	0	0	0
TOTAL Imports	0	0	0	0	0	0
TOTAL SUPPLY	20600	20600	21800	21630	0	22495
Intra EC Exports	0	0	0	0	0	0
Other Exports	0	0	0	0	0	0
TOTAL Exports	0	0	0	0	0	0
Fluid Use Dom. Consum.	12100	12100	12800	12826	0	13467
Factory Use Consum.	8300	8300	8800	8632	0	8890
Feed Use Dom. Consum.	200	200	200	172	0	138
TOTAL Dom. Consumption	20600	20600	21800	21630	0	22495
TOTAL DISTRIBUTION	20600	20600	21800	21630	0	22495
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Price Table: Dairy, Milk, Fluid

Prices Table					
Country:					
Commodity:					
Year:	1997				
Prices in (currency)	US\$	per (uom)	Liter		
Year	1996	1997	% Change		
Jan	0.25	0.22	-12.0%		
Feb	0.24	0.23	-4.2%		
Mar	0.24	0.23	-4.2%		
Apr	0.25	0.23	-8.0%		
May	0.29	0.23	-20.7%		
Jun	0.29	0.23	-20.7%		
Jul	0.29	0.23	-20.7%		
Aug	0.27	0.24	-11.1%		
Sep	0.25	0.22	-12.0%		
Oct	0.23	0.22	-4.3%		
Nov	0.24	0.21	-12.5%		
Dec	0.22	0.2	-9.1%		

PSD: Dairy, Cheese

PSD Table						
Country:	Brazil					
Commodity:	Dairy, Cheese					
		1997		1998		1999
	Old	New	Old	New	Old	New
Calendar Year Begin		01/1997		01/1998		01/1999
Beginning Stocks	0	0	0	0	0	0
Production	405	405	425	421	0	434
Intra EC Imports	0	0	0	0	0	18
Other Imports	25	29	17	21	0	0
TOTAL Imports	25	29	17	21	0	18
TOTAL SUPPLY	430	434	442	442	0	452
Intra EC Exports	0	0	0	0	0	0
Other Exports	0	0	0	0	0	0
TOTAL Exports	0	0	0	0	0	0
Human Dom. Consumption	430	434	442	442	0	452
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	430	434	442	442	0	452
TOTAL Use	430	434	442	442	0	452
Ending Stocks	0	0	0	0	0	0
TOTAL DISTRIBUTION	430	434	442	442	0	452
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Import Trade Matrix: Dairy, Cheese

Import Trade Matrix			
Country:		Units:	Metric Tons
Commodity:			
Time period:	Jan-Dec		
Imports for	1997		1998
U.S.	1750	U.S.	2100
Others		Others	
Argentina	11207		8405
Canada	573		540
European Union	3887		2820
New Zealand	1465		900
Uruguay	8074		6080
Total for Others	25206		18745
Others not listed	1748		683
Grand Total	28704		21528

PSD: Dairy, Butter

PSD Table						
Country:	Brazil					
Commodity:	Dairy, Butter					
		1997		1998		1999
	Old	New	Old	New	Old	New
Calendar Year Begin		01/1997		01/1998		01/1999
Beginning Stocks	0	0	0	0	0	0
Production	72	72	74	70	0	70
Intra EC Imports	0	0	0	0	0	0
Other Imports	8	6	7	6	0	5
TOTAL Imports	8	6	7	6	0	5
TOTAL SUPPLY	80	78	81	76	0	75
Intra EC Exports	0	0	0	0	0	0
Other Exports	0	0	0	0	0	0
TOTAL Exports	0	0	0	0	0	0
Domestic Consumption	80	78	81	76	0	75
TOTAL Use	80	78	81	76	0	75
Ending Stocks	0	0	0	0	0	0
TOTAL DISTRIBUTION	80	78	81	76	0	75
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Import Trade Matrix: Dairy, Butter

Import Trade Matrix			
Country:		Units:	Metric Tons
Commodity:			
Time period:	Jan-Dec		
Imports for	1997		1998
U.S.	37	U.S.	30
Others		Others	
Argentina	654		890
Australia	100		30
Canada	0		0
European Union	120		30
New Zealand	285		120
Uruguay	4344		4900
Total for Others	5503		5970
Others not listed	646		372
Grand Total	6186		6372

PSD: Dairy, Dry Whole Milk Powder

PSD Table						
Country:	Brazil					
Commodity:	Dairy, Dry Whole Milk Powder					
		1997		1998		1999
	Old	New	Old	New	Old	New
Calendar Year Begin		01/1997		01/1998		01/1999
Beginning Stocks	31	31	27	27	0	39
Production	231	231	242	240	0	247
Intra EC Imports	0	0	0	0	0	0
Other Imports	100	105	100	122	0	95
TOTAL Imports	100	105	100	122	0	95
TOTAL SUPPLY	362	367	369	389	0	381
Intra EC Exports	0	0	0	0	0	0
Other Exports	0	0	0	0	0	0
TOTAL Exports	0	0	0	0	0	0
Human Dom. Consumption	335	340	355	350	0	357
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	335	340	355	350	0	357
TOTAL Use	335	340	355	350	0	357
Ending Stocks	27	27	14	39	0	24
TOTAL DISTRIBUTION	362	367	369	389	0	381
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Import Trade Matrix: Dairy, Dry Whole Milk Powder

Import Trade Matrix			
Country:		Units:	Metric Tons
Commodity:			
Time period:	Jan-Dec		
Imports for	1997		1998
U.S.	246	U.S.	250
Others		Others	
Argentina	44411		55520
Canada	546		590
Australia	2773		3100
European Union	24190		29028
New Zealand	4611		5400
Switzerland	18115		21300
Uruguay	4669		5600
Total for Others	99315		120538
Others not listed	5693		1766
Grand Total	105254		122554

PSD: Dairy, Milk, Nonfat Dry

PSD Table						
Country:	Brazil					
Commodity:	Dairy, Milk, Nonfat Dry					
		1997		1998		1999
	Old	New	Old	New	Old	New
Calendar Year Begin		01/1997		01/1998		01/1999
Beginning Stocks	12	12	2	8	0	10
Production	55	55	61	58	0	60
Intra EC Imports	0	0	0	0	0	0
Other Imports	75	41	87	47	0	42
TOTAL Imports	75	41	87	47	0	42
TOTAL SUPPLY	142	108	150	113	0	112
Intra EC Exports	0	0	0	0	0	0
Other Exports	0	0	0	0	0	0
TOTAL Exports	0	0	0	0	0	0
Human Dom. Consumption	140	100	150	103	0	105
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	140	100	150	103	0	105
TOTAL Use	140	100	150	103	0	105
Ending Stocks	2	8	0	10	0	7
TOTAL DISTRIBUTION	142	108	150	113	0	112
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0
Calendar Yr. Exp. to U.S.	0	0	0	0	0	0

Import Trade Matrix: Dairy, Milk, Nonfat Dry

Import Trade Matrix			
Country:		Units:	Metric Tons
Commodity:			
Time period:	Jan-Dec		
Imports for	1997		1998
U.S.	822	U.S.	930
Others		Others	
Argentina	13961		16060
Australia	5883		6780
Canada	112		125
Czechoslovakia	96		100
European Union	2401		2640
New Zealand	6969		8014
Poland	0		20
Switzerland	2349		2700
Uruguay	7672		8850
Total for Others	39443		45289
Others not listed	501		671
Grand Total	40766		46890