

Dairy Situation and Outlook, September 21, 2009
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Dairy product prices and farm level milk prices have started to show signs of improvement. CME 40-pound cheddar blocks which were \$1.40 per pound as of August 19th dropped down to \$1.27 per pound on September 4th where it remained until September 16th. As of September 18th, cheddar blocks had improved to \$1.33 per pound. CME cheddar barrels were \$1.38 per pound as of August 24th and dropped to \$1.255 per pound on September 3rd where it remained until September 14th. As of September 18th barrels had improved to \$1.29 per pound. The current support price on blocks is \$1.31 and barrels \$1.28. CME butter was at a low of \$1.15 per pound on August 8th, was at \$1.17 per pound from August 27th through September 10th. As of September 18th butter had improved to \$1.27 per pound. The current support price on butter is \$1.05. Western dry whey has been trading in the \$0.31 to \$0.33 per pound range and nonfat dry milk in the \$0.945 to \$0.98 per pound range, which is above the current support price of \$0.92. These price improvements increased the Class III price from \$9.97 for July to \$11.20 for August, the highest for the year, and we can expect a September Class III price around \$12.10. The Class IV price was \$10.15 for July, \$10.38 for August and will be around \$11.05 for September.

We can expect continued improvement in dairy product prices and milk prices. However, existing ample stocks of cheese will slow the improvement in Class III prices. As of July 31st, American cheese stocks were 8.4% higher than a year ago and total cheese stocks 8.8% higher. While cheddar cheese production for July was just 0.7% higher than a year ago, total American cheese production was up 3% and production of all cheese up 2%. Butter production was 2.2% below a year ago, but July 31st stocks were still 7.2% higher.

With the weaker domestic and world economies slowing the growth in domestic consumption and dairy exports respectively, the recovery of dairy product and milk prices hinges on a slow down in milk production. USDA's September 18th milk production report shows this is starting to happen. Compared to a year ago, the revised USDA milk production report showed July milk production for the U.S. down slightly in July (-0.1%) and down 0.3% in August. While dairy cow slaughter was about 14% higher than a year ago January through August a good supply of dairy replacements has slowed the decline in the number of milk cows. Compared to a year ago, August U.S. cow numbers were down 171,000 head or 1.8%. Milk per cow was 1.6% higher.

Milk production continues to decline in the West and increase in the Midwest and some Northeast states. Cow numbers are down 3.5% from a year ago in California and with milk per cow 1.1% lower total milk production was 4.5% lower. Idaho had 1.3% fewer cows, 1.5% less milk per cow and 2.7% less milk production. Arizona had 7.6% fewer cows, just 0.3% more milk per cow and 7.4% less milk production. Cow numbers were down 5.0% in New Mexico, but 4.2% more milk per cow resulted in 1.1% less milk production. Washington had 3.7% fewer cows, 0.8% more milk per cow and 3.1% less milk production. Cow numbers also dropped in Texas, -1.2% but 4.7% more milk per cow resulted in 3.5% more milk production.

Wisconsin had 3.7% more milk production from 0.4% more cows and 3.3% more milk per cow. Minnesota had 0.9% more cows, 3.5% more milk per cow and 4.4% more milk production. Iowa had the no change in cow numbers but 2.4% more milk per cow. Cow numbers were up 1.4% in Michigan and 3.2% more milk per cow resulted in 4.6% more milk production. Both New York and Pennsylvania had fewer cows, -1.3% and -0.5% respectively, but more milk per cow resulted in slightly more milk production, +0.2% and +0.7%. In contrast Vermont had 3.6% fewer cows, 0.9% less milk per cow and 4.7% less milk production.

We can expect some improvement in domestic milk and dairy product sales to support the price recovery. With a major share of butter and cheese moved through restaurants and food service the downturn in restaurant traffic and a slower summer resort business has damped sales. Nevertheless, recent data indicate that cheese sales are improving and are now running above year ago levels. And some fast food service such as McDonalds has recently come out with new sandwiches that use increase amounts of cheese. At the retail level prices continue to drop which also will help sales. Compared to a year ago, the index of retail prices for all dairy products in August was 18% lower than a year, the lowest in two years. Whole milk prices were 23% lower, cheese 11% lower and butter 9% lower. Retailers are also doing more price specials on milk and dairy products. More meals eaten at home have also helped beverage milk sales. Total beverage milk sales for July were 2.2% higher than a year ago. Higher beverage milk consumption means less milk available for cheese production which gives support to cheese prices. Recent USDA purchases of cheese for food programs have also been positive for prices.

A major factor for depressed milk prices has been the loss in dairy exports. While still well below year ago levels, exports are also showing some improvement. In July, U.S. suppliers exported 28,172 tons of nonfat dry milk/skim milk power, the most since September 2008, but still down 8% from a year ago. Cheese exports in July were 9,459 tons, the most since October 2008, but still 13% lower than a year ago. DEIP activity has aided both the nonfat dry milk and cheese exports. July exports of whey protein concentrated (10,144 tons) were up 8% and whey protein isolates (1,224 tons) were up 2%. However, dry whey exports, which had been increasing, were just 13,576 tons in July, the lowest in 18 months and down 46% from a year ago. Lactose exports were 18,435 tons, up 21% from last year. But, butterfat exports were disappointing with July exports just 605 tons, down 92% from a year ago.

The world economy is showing some improvement which may help exports. But, the available supply of dairy products on the world market will also be higher, especially from New Zealand and Australia as their milk production is expected to improve, and the continued subsidized dairy product exports from the EU. Nevertheless, world prices have recently shown some improvement, particularly milk powders with some improvement in cheese and butter prices. We can expect some increase in U.S. dairy exports in 2010, particularly nonfat dry milk/skim milk powder and milk proteins, and possibly cheese.

USDA's latest price outlook shows the recovery in milk prices to be a slow process. Class III futures also show a slow recovery. However, Class III futures showed improvement last week. September 18th Class III futures for December settled at \$13.97, January 2010 at \$14.03, July at \$15.01 and December at \$15.80. I remain more optimistic than this with the possibility of Class III above \$14.00 by December, near \$16 by July 2010, and in the high \$16's by December 2010.

But, for these higher prices to occur milk production needs to continue to decline into 2010 and domestic sales needs to show improvement. History tells us that milk prices can increase rather quickly with anticipation of tightness in the market. So it is not without the possibility that prices could recover quicker and higher than this and that surely would be a great.

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