

Dairy Situation and Outlook, January 23, 2012
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Record milk prices were set in 2011. The Class III price averaged \$18.37 compared to \$14.41 in 2010. The Class IV price averaged \$19.04 compared to \$15.09 in 2010. And the U.S. All Milk price averaged \$20.14 compared to \$16.26 in 2010. But, while milk prices were a record high so were feed prices which dampened returns over feed costs.

Milk production increased just 1.8% to 196.2 billion pounds in 2011 which was positive for prices. But, domestic sales were mixed. Fluid (beverage) milk sales declined about 1.5%, the second consecutive year of declines. Both cheese and butter sales showed growth. But, a major factor contributing to record milk prices was dairy exports. The period of January through November compared to a year ago showed exports of nonfat dry milk/skim milk powder up 15%, total proteins even, cheese up 33%, butterfat up 15% and lactose up 14%. On a total milk solids basis exports were equivalent to 13.3% of U.S. milk production compared to 12.7% in 2010.

Forecasts are for lower but yet favorable milk prices in 2012. The level of milk production, domestic sales and exports will determine the final prices. January began with butter, cheese and nonfat dry milk prices all lower than averages for December. The exception has been dry whey prices which continued to show strength. NASS average prices are used to calculate federal order prices. It looks like NASS average prices per pound for January could be near \$1.59 for butter, \$1.60 for cheese, \$1.40 for nonfat dry milk and \$0.68 for dry whey. Despite lower cheese prices the strong dry whey price will hold the January Class III above \$17.00 to around \$17.05 compared to \$18.77 in December. The Class IV price will be close to what it was in December at \$16.87. Cheese and butter prices on the CME continue to weaken which will push both February Class III and IV below \$17.00. But, prices could start to strengthen by March or April, peaking out in October or November with prices for the year averaging \$1.00 to \$1.50 per hundredweight lower than 2011. But, this could easily change depending upon the actual level of milk production, domestic sales and exports.

Milk production may increase no more than 1.5% in 2012 which will be positive for milk prices. USDA forecasts a 1.3% increase. The average number of milk cows for the year may decline slightly, and while feed prices may average a little lower, prices will remain relatively high dampening increases in milk per cow. However, USDA's milk production report for the month of December shows milk production picking up rather than slowing down. Milk production for the month of December was estimated to be 2.7% higher than a year ago for the 23 reporting states and 2.5% for the U.S. as a whole. U.S. milk production for the last quarter of the year was 2.3% more than a year ago. Milk production growth above 2% will put downward pressure on milk prices.

Both more milk cows and improvement in milk per cow are contributing to the increase in milk production. Compared to the previous month cow numbers declined in October and November but increased again by 12,000 head in December. December cow numbers were 0.9% more than a year ago. Milk per cow in 2011 which averaged just 0.9% higher for the year improved to an increase of 1.6% for December. Of the 23 reporting states 16 had added cows in

December compared to a year ago. Most of the increase in cow numbers took place in the West with increases of 3.8% for Arizona, 1.7% for California, 1.2% for Idaho, 4.0% for New Mexico, 3.6% for Texas and 4.4% for Washington. In contrast, in the Northeast cow numbers were 0.2% lower for New York, 0.7% lower for Pennsylvania and unchanged for Ohio. Also in the Midwest cow numbers were 1.9% lower for Iowa, 1.1% lower for Minnesota and unchanged for Wisconsin.

Compared to December a year ago Western states had strong production increases with increases of 3.6% for Arizona, 3.8% for California, 4.9% for Colorado 3.4% for Idaho, 2.0% for New Mexico, 4.1% for Texas and 4.7% for Washington. These strong increases compare to New York up just 0.2%, Pennsylvania 0.2% lower, Ohio up 0.9%, Iowa up 2.5%, Minnesota up 0.8% and Wisconsin up 2.6%.

With milk prices lower for the first quarter of the year and feed prices still relatively high returns over feed costs will be lower. Quality hay supplies are tight and hay prices are high. This situation may result in cow numbers declining for the winter months and slowing down the increase in milk production. If cow numbers don't increase for the year, but with some improvement in milk per cow the increase in milk production for the year could still stay below 1.5% which would be positive for milk prices. But, if production increases more than this milk prices will likely not strengthen as much for the second half of the year as now forecasted depending upon domestic sales and exports.

Domestic sales may do better in 2012. Both the Consumer Confidence Index and the Restaurant Performance Index have improved which is positive for increased sales. U.S. dairy exports may be lower than 2011 but yet remain relatively strong. USDA is forecasting exports on a milk fat basis to be down 7.5% and on a skim-solids basis down 5.6%.

One factor that is positive going into 2012 for holding milk prices at more favorable levels is stocks of dairy products. In 2011 cheese production showed limited growth, domestic sales were favorable and exports higher tightening up cheese stocks. During the period of January through November of 2011 cheddar production was 3.0% lower than the year before and total cheese production was up just 1.5%. As of December 31st American cheese stocks were 4.8 % below a year ago and but still 7.4% higher than the 5-year average for this date. Butter production has been running well above year ago levels with the January through November period up 16.6%. December 31st butter stocks were 28.7% higher than a year ago but still 12% below the 5-year average for this date. Dry whey stocks are relatively tight with stocks 9% lower than a year ago. Nonfat dry milk stocks are about 141 million pounds compared to stocks of as much as 1.2 billion pounds back in 2003 and over 600 million pounds as late as 2004.

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