

**Dairy Situation and Outlook**  
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A continued building of the dairy herd and good milk per cow keeps milk production well above year ago levels. For the 23 reporting states, October milk cow numbers were 1.2% higher than a year ago and milk per cow was 2.8% higher resulting in 4.1% more milk production. Cow numbers have been higher than the month before each month beginning with May. Cow expansion is very evident in the West and Southwest with cow numbers up 5.1% in Arizona, 5.0% in Idaho, 2.7% in California and 2.4% in Texas. The exception is New Mexico where cow numbers were 6.7% lower. But, cow numbers are also up in the Midwest with Wisconsin up 0.4%, Minnesota 2.9% and Iowa 3.4%. Cow numbers are down in the South, Southeast and Northeast. Cow numbers were down 5.2% in Missouri, 8.4% in Kentucky, 2.3% in Florida, 0.6% in New York and 0.2% in Pennsylvania. Increases in milk per cow were relatively high in several states with increases of 7.6% in Arizona, 3.0% in California, 8.7% in New Mexico, 3.0% in Texas, 3.9% in Wisconsin, and 5.2% in New York, for examples. The combination of more cows and good production per cow resulted in strong increases in milk production for most West, Southwest and Midwest states. Production was up 13.0% in Arizona, 5.8% in California, 6.2% in Idaho, 5.5% in Texas, 4.3% in Wisconsin, 3.5% in Minnesota and 2.6% in Iowa. The same was not true in the South, Southeast and Northeast. Production was down 1.3% in Florida, 9.1% in Missouri and 5.0% in Kentucky. Increases in milk per cow did offset fewer cows in New York and Pennsylvania netting 4.4% and 0.5% more milk production respectively.

The production data clearly show that dairy producers have responded to very favorable milk prices by increasing milk cow numbers. The increase in cow numbers are the result of keeping lower producing cows that normally would be slaughtered in the herd longer and bringing in more replacements. Cow slaughter, which was running 10 to 15% higher for the first half of the year, fell below or only slightly higher since then. In recent weeks slaughter numbers have increased some running about 5% higher. High feed costs and tighter winter supplies of quality hay may keep slaughter numbers higher this winter. The July 1<sup>st</sup> cattle inventory showed that dairy herd expansion is possible with replacement numbers 2.6% higher than a year ago.

Despite milk cow numbers increasing month to month beginning with May and total milk production running more than 3% higher than a year earlier since July, milk prices have not only held at high levels but have increased. The Class III price was \$18.70 for October, down from the \$20.70 the month before, but will be back to about \$19.20 for November. While dry whey prices have dropped from almost \$0.80 per pound this summer to now about \$0.44 per pound, cheddar cheese prices, somewhat surprising, have strengthened, resulting in these favorable Class III prices. Cheese prices strengthened despite reports that cheese buyers may be reluctant to carry any extra inventory with fear that prices could fall and that orders for the holidays are close to being filled. CME cheddar barrels in early October were \$1.8575 per pound and 40-pound cheddar blocks \$1.84 per pound. But, by early November barrels had increased to \$1.98 per pound and 40-pound blocks to \$2.045 per pound. As of November 16<sup>th</sup>, barrels were \$2.03 per pound and 40-pound blocks \$2.15. This strength in cheese prices may be attributed to the fact

that production has been below a year ago. Compared to a year ago, September production of cheddar cheese was 8.4% lower and year-to-date production 2.6% lower. Production of all American cheese was 5.3% lower for September and 1.5% lower year-to-date. September production of Italian cheese was up slightly, +0.9% and up 1.4% year-to date. For all cheese, September production was down 1.4% and year-to-date up just 1.4%. Less cheese production and favorable sales has reduced cheese stocks. September 30<sup>th</sup> stocks of American cheese were 3.4% lower than a year ago and stocks of all cheese down 2.7%.

Even butter prices, which were as low as \$1.29 per pound towards the end of October, increased to \$1.37 per pound by early November. This was even higher than the \$1.31 per pound butter price a year ago. While retail butter prices are higher than a year ago, butter sales through August were about 6% higher. Further increases in butter prices are unlikely and will likely decline as Christmas orders are filled. Butter supplies are more than ample with September production up 7.3% from a year ago and year-to-date production up 5.2%. September 30<sup>th</sup> butter stocks were 27.4% higher than a year ago.

With cheese plants operating at capacity in the West more of the increased milk production is going into the production of nonfat dry milk. While the production of nonfat dry milk was below year ago levels for the first six months, production picked up in July and September production was 42.7% higher than a year ago. Exports of nonfat dry milk for the first nine months of the year were down 17.8%. Stocks of nonfat dry milk are building and prices have weakened. Nonfat dry milk prices which were \$2.00 per pound or higher this summer are now around \$1.85 per pound. Nonfat dry milk prices and butter prices resulted in a \$20.45 September Class IV price and \$20.07 in October. Some strengthening in November butter prices will yield a November Class IV price around \$20.40. The advanced Class IV price continues to be the mover of Class I prices. The November Class I mover was announced at \$21.45.

With milk production running well above a year ago and increasing seasonally, along with orders of additional cheese and butter for the holidays coming to a close, we can expect cheese and butter prices to decline by December and into 2008. But, the questions are, how sharp and how far of a price decline can we expect? Recent history shows, such as what occurred when cheddar cheese was above \$2.00 per pound in 2004, those prices can fall sharply and far. But, the current situation may be different. High feed prices, high prices for dairy replacements and dairy producers still recovering from low milk prices and high feed costs that existed in 2006 all may dampen increases in 2008 milk production. High retail milk and dairy product prices have dampened demand some, but over-all sales remain favorable, plus continued exports of nonfat dry milk and dry whey, as well as some increase in cheese and butter exports, will help to support milk and dairy product prices. So at this time sharp declines in cheese prices and milk prices are not anticipated. However, Class III prices could well be below \$17.00 by January and in the low \$15.00s by May before showing some seasonal strength. There are now opportunities for producers to protect favorable milk prices for all of 2008 since Class III futures are still more optimistic than this.

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