

The Milkweed

Dairy's best marketing info and insight

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U.S. Milk Powder Supply Very Tight; Prices Rising

by Pete Hardin

Current demised prices for Cheddar cheese do not reflect honest market conditions. Surprisingly, a more honest picture of dairy supply-demand is found in nonfat dry milk:

- Nonfat milk supplies are tight and prices are rising. Increasing complaints are coming from brokers and users who cannot obtain current product for their needs. Last summer, DairyAmerica, the U.S. co-op marketing agency for nonfat dry milk, advised buyers to lock in monthly commitments for purchases.
- U.S. production in recent months is way down. October-December 2004 saw a 20% decline in U.S. milk powder output, compared to 2003's fourth quarter. For all of 2004, U.S. nonfat dry milk production was 1.411 billion lbs—down 11.2% from 2003.
- Declines in U.S. milk powder production were dramatic in the January-May and September-December segments of 2004. Basically in 2004, milk powder production became the alternative of last choice when cheese prices were high, because processor returns were higher for milk made into cheese. Manufacturing nonfat dry milk is far more energy-intensive than cheese manufacturing.
- Global milk powder supplies are very tight. During 2004, U.S. exports of nonfat dry milk surged as the global dairy protein picture tightened dramatically. During January-November 2004, U.S. nonfat dry milk exports totaled 194,988 metric tons. That's an increase of 89%!
- The Commodity Credit Corporation of USDA has purchased no surplus nonfat dry milk since November 2004. Surplus purchases of nonfat dry milk by USDA during the second half of 2004 were miniscule, compared to 2003's second half. Meanwhile, CCC's remaining 300+ million lbs. of (very old) nonfat dry milk is unavailable. CCC officials are telling interested parties that all its holdings are committed.
- USDA estimates that by the end of the current federal fiscal year on September 30, 2005, the CCC will have about 100 million lbs. of "surplus" nonfat dry milk. That figure is way down from recent amounts. On September 30, 2003, CCC had 1.138 billion lbs. of surplus nonfat powder in storage.

• Imports of nonfat dry milk during the second half of 2004 shriveled, compared to July-December 2003.

• Imports of other dairy proteins (such as Milk Protein Concentrate) are both scarce and expensive. Global supplies of dry dairy proteins are scarce and expensive. Milk production has been hit hard by weather in many parts of the globe in the past couple years. And global demand for dairy protein powders is strong—especially in Asia.

Cash prices for Grade A nonfat dry milk at the Chicago Mercantile Exchange hit the \$1.00/lb. mark on Tuesday, February 8. Prices for nonfat powder have climbed steadily since November, gaining 15 cents per pound. Dairy and food processors have become accustomed to low-priced, abundant nonfat dry milk for so long that they missed many of the building signals that nonfat dry milk was tight.

Big exports reducing U.S. supplies

An unfortunate squeeze is developing for domestic users of nonfat dry milk: exports are drawing offshore products they need for food processing. The global price for nonfat dry milk is generally higher than U.S. prices. Domestic needs for nonfat dry milk are, in some instances, begging ... as product leaves the country.

Fonterra, New Zealand's dairy marketing monolith, has an exclusive arrangement with DairyAmerica to control all U.S. milk powder exports. Fonterra officials recently stated that they intend to use supplies from the U.S. to compensate for their shortfalls of milk powder in Oceania. What domestic users of U.S. nonfat dry milk can't appreciate: the weak value of the U.S. dollar means U.S.-sourced exports are very lucrative when bought on the basis of the U.S. dollar and sold internationally on the basis of a stronger currency.

Export data show that 79,600 metric tons of nonfat milk powder left the U.S. in December 2004—an increase of just under 400% compared to December 2003 export totals.

In contrast to forecasts by USDA and most university "experts," *The Milkweed* projects very tight U.S. milk supplies in 2005. The current tight supply of nonfat dry milk will probably intensify, as this year

progresses. Tight supplies of nonfat dry milk may presage tight supplies of cheese and butter, later this year.

The big picture: Global Protein Shortage

Using a "big picture" scenario, what's happening is the confluence of three somewhat interconnected events:

—A growing global shortage of human-quality protein, exacerbated by growing demand and constricted production.

—A weakening U.S. dollar, which makes our food exports readily inexpensive to foreign buyers with stronger currencies.

—U.S. milk production capacity is worn down by years of inadequate farm milk prices and non-sustainable farming practices.

Forget the contrived ups and downs of Cheddar prices. Watch the U.S. milk powder situation if you want to know what's really going on!

The U.S. food industry is entering an era of scarcity. Critical resources that have been taken for granted for a long time—food, energy, and capital—may not be taken for granted in the future by wise managers.

January Class III \$14.14; Near-Term Outlook Weak

January's federal order Class III (cheese milk) price was placed at \$14.14/cwt., down a whopping \$2.00 from December.

The big January loss was caused by a big decline in cheese prices at the Chicago Mercantile Exchange during December. CME Cheddar rices stabilized and rose in January, but dropped again in early February, creating the likelihood of more Class III declines over the next couple of months.

USDA said the January federal order Class IV (butter-powder) price had been placed at \$12.52/cwt., down 90 cents from the December Class IV.

Cheese Pendulum: Too High, Too Low

Too high, too low. The destructive pendulum of cheese-pricing swings back and forth, causing havoc and consternation in the dairy industry, from farm to supermarket shelf.

Cash Cheddar prices peaked at the end of January at the Chicago Mercantile Exchange and then plunged sharply. General consensus is that somewhere in the price run that started during the week of January 10-14, that saw block Cheddar prices climb 13.25 cents (to \$1.63/lb.) ... marked a departure from reasonable, seasonal cheese prices to too levels that were too high.

The block Cheddar price run peaked at \$1.7575/lb.—hitting that mark on Friday, January 21 and holding at that level until Friday, January 28, when the plunge began.

At press time, block Cheddar prices had lost

33.75 cents per pound off the late-January peak, falling to \$1.42/lb. on February 9.

Too high. Too low.

Too high. Serious doubts exist about the integrity of the cash dairy markets at the CME. Dairy marketers point to the Cheddar price peaks at CME in late November and late January as the handiwork of a trader bent upon bettering resolutions of his future/options positions.

Too low. When the Cheddar cash prices go south, one can imagine the big dairy co-ops licking their chops, anticipating all the money they can pilfer through "depooling" of Class III (cheese) milk in the federal milk order system, when prices rise sharply again ... as they will.

Dairy's pricing system is corrupt ... high and low.

The Milkweed ^{2/05}

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