



Dairy Outlook

July 2009

By Jim Dunn

Professor, Penn State University

Market Psychology

The futures market for Class III milk for the remainder of 2009 has fallen once again, as cheese markets have gotten weaker. Cheese prices are at the lowest levels since January and Fall futures have dropped by more than \$1.00/cwt. since last month. The market still expects higher prices by the end of the year, although the levels for rest of 2009 continue to erode, and the better prices are only for 2010. Table 1 shows the futures prices for Class III and IV for the remainder of the year. Another round of buyouts under the CWT (Cooperatives Working Together) program is underway. This should reduce cow numbers somewhat. Cow numbers are below a year ago and edging downward, but still too high given the demand for dairy products. The U.S. Department of Agriculture has announced a new round of the Dairy Export Incentive Program, at least partially in response to the surpluses in Europe and EU subsidies. Global stocks of products are still high, so world prices are not expected to go anywhere soon. Exports are up a bit, but well below last year's levels, which were buoyed by the weak dollar and the drought in Australia. The exception is dry whey, which continues to do well when compared to last year, although 2007 was stronger than either 2008 or 2009.

Nonfat dry milk is going nowhere, staying at the same level for a month. Fall futures prices are higher, but nearby futures are down. Butter is down 3 cents from last month. Butter futures are higher in 2010. Whey powder prices continue to edge up, up to \$0.29 per pound, with futures prices over 30 cents by fall.

As always the market is watching cow numbers and exports. The milk production numbers are the same as last year, despite fewer cows. Given the weakness in exports, the milking herd is still too large. The market cannot absorb the current production, and of course the price support levels are too low to provide a meaningful cushion. Given the economy, whether at home or abroad, customers are not going to buy more cheese or butter, so a decrease in production is the only path to higher prices.

Unfortunately the pattern of higher milk prices always being two months in the future persists. Table 1 has the forecasts based on the futures markets.

Corn and Soybean Markets

Since last month, the price of corn in Chicago has dropped sharply. The December corn contract is selling for \$3.45, 80 cents per bushel lower than last month. Like corn, soybeans



have fallen sharply. Nearby beans are down by \$1.80 per bushel from last month, at \$10.20 per bushel. The harvest November contract has fallen similarly to \$9.05. The estimates of corn usage have fallen and the estimate of the fall crop have risen, to combine with an expected supply for the 2009-10 crop year of over 14 billion bushels. While the usage is expected to be greater than the crop, the increase in ending stocks for the 2008- 09 crop year have reduced fears of a shortage. In the absence of weather problems, there should be enough corn for next year. Ethanol producers continue to do poorly, so estimated corn use for fuel is creeping down. The lower soybean prices for the fall are tied to a bigger crop, which will exceed expected disappearance, unlike the 2008 crop. The estimated carryover for 2010 is reasonably high, so prices have eased. Together the lower feed prices offer some offset to the terrible milk prices. The income over feed costs estimates that follow use data from June and do not reflect this yet.

Income over feed costs

The combination of very low milk prices and continued high corn and soybean meal prices in June meant that June producer margins are very low. Our index of Income Over Feed Costs (IOFC) reflects gross income less feed costs for an average cow producing 65 pounds of milk. As may be seen in Figure 1 and Table 2, the value is at \$4.12, the lowest value in our data, which goes back to 2000. The record lows are worse than the numbers might reflect since \$4.00 doesn't go as far in 2009 as it did in 2006. The daily feed cost values for April and May shown in last month's newsletter were incorrect. The income over feed costs numbers were correct. The values in Table 2 have corrected this mistake.

The allocation of the revenue per hundred pounds of milk is shown in Table 3. This value, the milk margin, is the estimated amount from the Pennsylvania all milk price that remains after feed costs are paid. As with income over feed cost, this shows that June was worse than May, with more than half the milk price going to pay for feed.

Milk Production

Monthly milk production numbers (Figure 2) continue to track last year, which is too much milk given the lower exports in 2009. Apparently California's production is starting to fall, although the cool summer is keeping production up elsewhere. Combined with further culling, perhaps the milk production will fall enough to let the milk price recover.

PA Dairy Income over Feed Costs

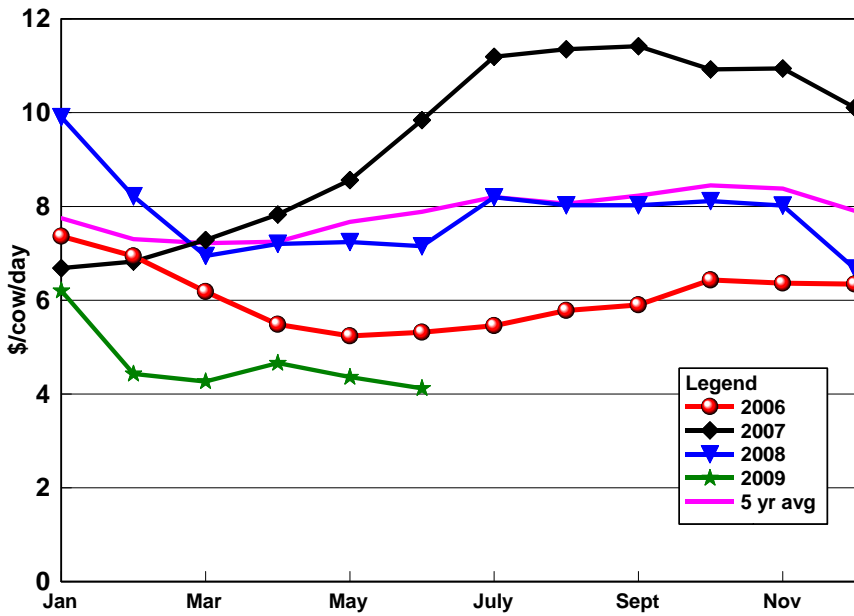


Figure 1. PSU's Income Over Feed Costs (IOFC)

Milk Production

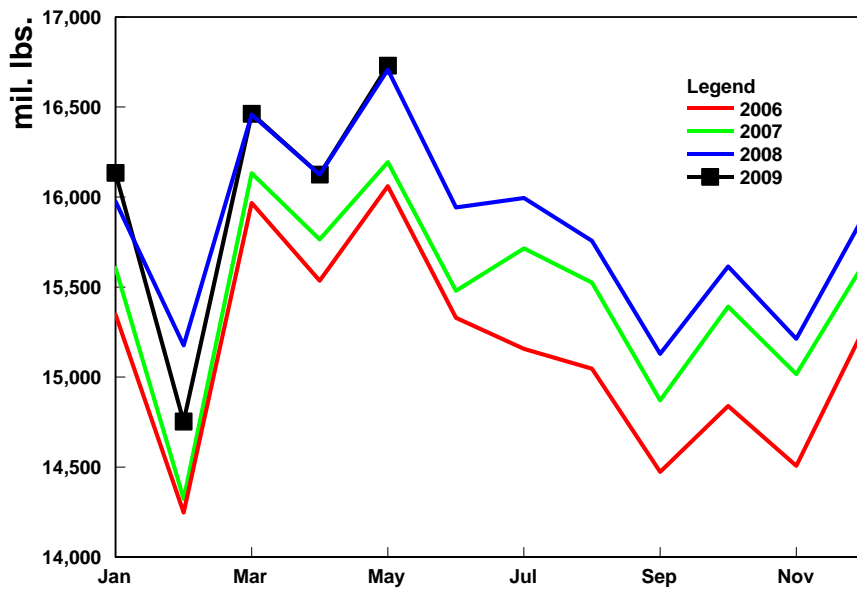




Table 1. Implied Milk Prices and Futures Prices for 2009

(Based on futures prices of July 14, 2009)

	Class III \$/cwt	Class IV \$/cwt	PA All Milk \$/cwt
2008			
Jan	19.32	16.29	22.60
Feb	17.03	14.67	21.00
Mar	18.00	14.17	19.10
Apr	16.76	14.56	19.90
May	18.18	15.26	19.50
Jun	20.24	15.92	20.30
Jul	18.25	16.60	21.40
Aug	17.32	16.64	20.50
Sep	16.28	15.45	20.50
Oct	17.06	13.62	19.40
Nov	15.51	12.25	19.20
Dec	15.28	10.35	17.10
Annual	17.44	14.65	20.04
2009			
Jan	10.78	9.59	16.20
Feb	9.31	9.45	13.50
Mar	10.44	9.64	13.00
Apr	10.78	9.82	13.40
May	9.84	10.14	13.40
Jun	9.97	10.22	13.00
Jul	9.89	10.28	13.40
Aug	10.29	10.51	13.72
Sep	11.14	10.79	14.31
Oct	12.02	11.03	14.91
Nov	13.02	11.43	15.64
Dec	13.35	11.29	15.78
Annual	10.90	10.35	14.19
Annual change	6.53	4.30	5.85
% change	37.5%	29.3%	29.2%

Table 2: Determinants of PA income over feed cost

	all milk price	feed cost/65 lbs milk	Income over feed cost
Jan-08	\$22.60	\$4.79	\$9.90
Feb-08	\$21.00	\$5.43	\$8.22
Mar-08	\$19.10	\$5.47	\$6.94
Apr-08	\$19.90	\$5.73	\$7.20
May-08	\$19.50	\$5.43	\$7.24
Jun-08	\$20.30	\$6.04	\$7.15
Jul-08	\$21.40	\$5.71	\$8.20
Aug-08	\$20.50	\$5.30	\$8.03
Sep-08	\$20.50	\$5.30	\$8.03
Oct-08	\$19.40	\$4.49	\$8.12
Nov-08	\$19.20	\$4.46	\$8.02
Dec-08	\$17.10	\$4.44	\$6.67
Jan-09	\$16.20	\$4.33	\$6.20
Feb-09	\$13.50	\$4.35	\$4.43
Mar-09	\$13.00	\$4.18	\$4.27
Apr-09	\$13.40	\$4.05	\$4.66
May-09	\$13.40	\$4.35	\$4.36
Jun-09	\$13.00	\$4.33	\$4.12



Table 3: Milk Margin (Portion of milk price going to feed and remaining for other expenses)

	all milk price/100 lbs	feed cost/100 lbs milk	Milk Margin/100 lbs
Jan-08	\$22.60	\$7.36	\$15.24
Feb-08	\$21.00	\$8.36	\$12.64
Mar-08	\$19.10	\$8.42	\$10.68
Apr-08	\$19.90	\$8.82	\$11.08
May-08	\$19.50	\$8.36	\$11.14
Jun-08	\$20.30	\$9.30	\$11.00
Jul-08	\$21.40	\$8.79	\$12.61
Aug-08	\$20.50	\$8.15	\$12.35
Sep-08	\$20.50	\$8.15	\$12.35
Oct-08	\$19.40	\$6.92	\$12.48
Nov-08	\$19.20	\$6.87	\$12.33
Dec-08	\$17.10	\$6.83	\$10.27
Jan-09	\$16.20	\$6.66	\$9.54
Feb-09	\$13.50	\$6.69	\$6.81
Mar-09	\$13.00	\$6.44	\$6.56
Apr-09	\$13.40	\$6.23	\$7.17
May-09	\$13.40	\$6.70	\$6.70
Jun-09	\$13.00	\$6.67	\$6.33