



# Dairy Outlook

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## Market Psychology

The futures market for Class III milk for the remainder of 2009 has fallen by more than \$1.00/cwt. since last month. Nevertheless the market still expects higher prices by the end of the year. However, each month as I write this, the month when the higher prices will occur moves another month into the future. One reason is that the expected decrease in cow numbers is delayed. From March to April cow numbers didn't fall at all, despite the low prices. Class IV futures prices for the remainder of the year have not changed from last month, although they never were expected to increase as much as Class III.

Nonfat dry milk continues to be depressed, stuck just a bit above support, and largely unchanged, although fall futures are 7 cents/lb. higher than current prices and early 2010 futures are another 20 cents/lb. higher. Butter is trading on the CME at around \$1.22 per pound, down 2 cents from last month. Like the nonfat dry milk, butter futures are higher in the fall and higher yet in 2010. Whey powder prices continue to climb, up to \$0.26 per pound, with futures prices over 30 cents by fall.

As always the market is watching cow numbers and exports. Dairy cow slaughter is tailing off. However, the continuing low milk prices will take their toll as the year progresses. Clearly the futures market is expecting this. The US Department of Agriculture has announced bonuses for cheese exports under the Dairy Export Enhancement Program, which should induce more exports. The higher futures prices for the second half of the year suggest markets expect further shrinkage in cow numbers. Exports are another factor. The dollar has fallen recently making our products more competitive in world markets. World export markets are in a bit of turmoil. Some economies are very hard hit by the world economic problems and buying fewer products. Just one example is Russia. Russia gets most of its milk from backyard cows and the rest from commercial dairy farms. The former milk is low quality and the latter isn't very high quality either. Between the two sources, they traditionally need to import 20% of their dairy products. Much of this has come from Belarus. However, Russia is taking a variety of actions to stop imports from Belarus (similar to those regarding US poultry from time to time). In response the president of Belarus skipped a big international meeting of the former Soviet states this week. Russia is also buying skim milk powder to support the price. The stories vary by country, but between weak economies, plummeting exchange rates, and political turmoil, the demand for dairy imports in much of the world is lower.

It looks like we will have a low milk price through July, with it rising after that, based on the futures market. I would repeat that higher milk prices have seemed to be two months away for a few months,



but as time passes the higher prices are still two months in the future. While I hope that this time prices will really rise in a couple months, this pattern is not encouraging. Table 1 has the forecasts based on the futures markets.

### **Corn and Soybean Markets**

The price of corn in Chicago has fallen to about \$4.00 per bushel for the nearby contract, after rising above \$4.50 in the past 6 weeks. December corn is selling for \$4.25, but is also off 50 cents from its recent highs. Like corn, nearby soybeans have fallen by \$0.50 per bushel recently, but are still over \$12.00 per bushel. The harvest November contract has risen a dollar since last month, although it also has slipped lately. The higher corn prices are because of late planting. The crop estimate has been reduced by 1.5% from last month. The higher soybean prices are tied to export demand, both because of smaller crops in Argentina and more exports to China. For both corn and soybeans, carryover into the next crop year is expected to be low, so prices are very vulnerable to bad weather here or abroad.

### **Income over feed costs**

The combination of low milk prices and continued high corn and soybean meal prices has kept producer margins 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. That index rose to over \$10 per cwt in the second half of 2007 and then declined steadily in 2008 (Figure 1). Since February the index has been in the \$4.50 per cow range. This is the lowest values we have seen in the nine years of data we have, and the most comparable period in 2003 was better because the cost of the other things farmers must buy were lower then. This is especially true of fuel. These low margins continue to hurt dairy producers badly. The expected higher prices later this year will help some, but even these will be well below the 2008 levels. The greater culling rates and decreases in cow numbers reflect this, and I would expect both to continue for the near term. Table 2 shows the monthly values.

I have included a similar measure based on the revenue per hundred pounds of milk 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 for a simple ration. It shows that in May almost half of the milk price went to feed costs, a very high value.

### **Milk Production**

The March and April milk production numbers are almost exactly at their values from last year, which would be good if exports were as high as last year. They are not and so too much milk is

being produced still. No doubt it will fall because of culling and liquidations. Higher feed prices will discourage output growth as well.

## PA Dairy Income over Feed Costs

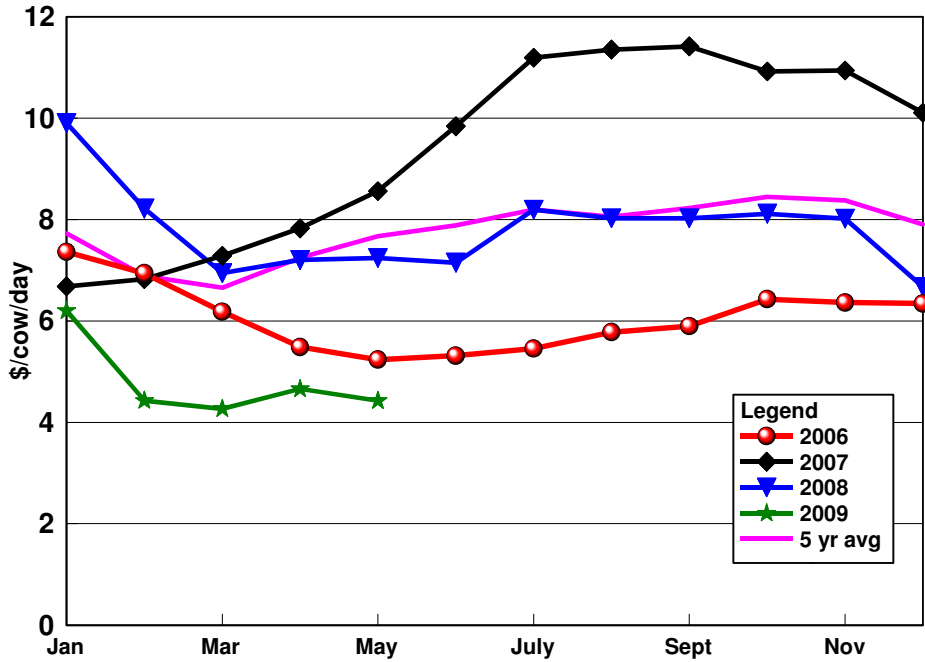


Figure 1. PSU's Income Over Feed Costs (IOFC)

# Milk Production

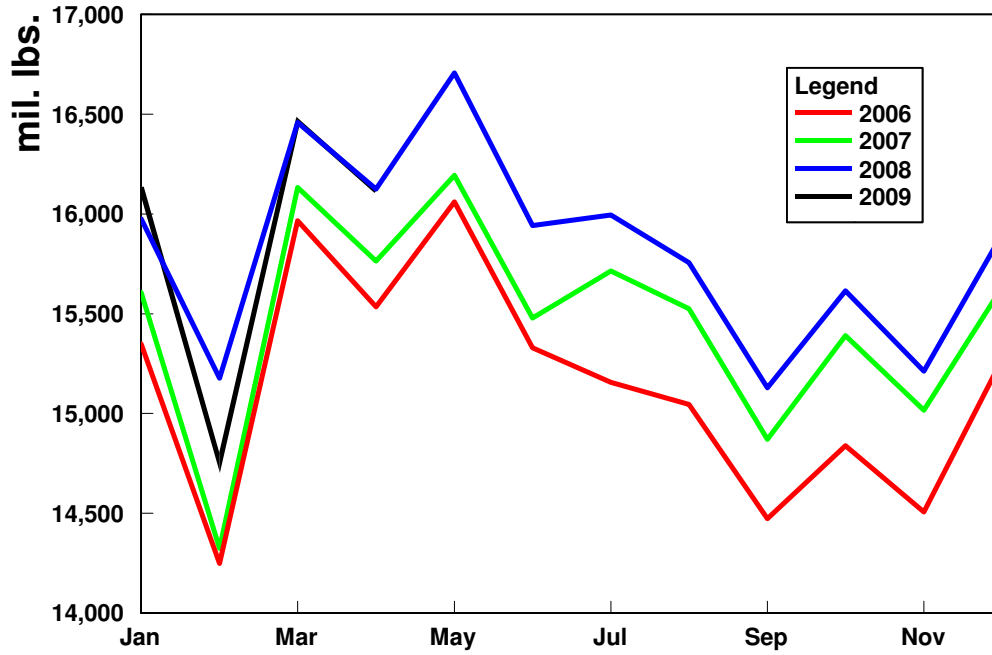


Table 1. Implied Milk Prices and Futures Prices for 2009

(Based on futures prices of June 15, 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	12.24	19.20
Dec	15.28	10.35	17.10
Annual	17.63	15.04	20.31
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	9.91	10.58	13.51
Jul	10.35	10.90	13.89
Aug	11.20	11.04	14.44
Sep	12.30	11.60	15.29
Oct	13.22	11.80	15.90
Nov	13.76	11.83	16.23
Dec	14.03	11.85	16.40
Annual	11.33	10.69	14.60
Annual change	-6.31	-4.35	-5.71
% change	-35.8%	-28.9%	-28.1%

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	\$5.43	\$4.27
Apr-09	\$13.40	\$6.04	\$4.66
May-09	\$13.40	\$5.71	\$4.42

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	\$6.59	\$6.81