

The Milkweed



Dairy's best marketing info and insights

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Sky-High Global Prices = Future U.S. Prices, /F ...

by Pete Hardin

What's the best current measure for estimating future U.S. dairy commodity and farm milk prices? That's the big question on the minds of many persons in our industry ... especially on the farm, where many producers are still digging out from underneath mountains of bills and debts that piled up in 2006.

"If I could get six months of \$20/cwt. milk, then I'd clean up last year's bills," concedes one Southern California dairy producer. His comments reflect the reality for many U.S. dairy farmers, who've got one eye on the weather ... and the other eye on price signals from the dairy market place.

What's the trend for U.S. farm milk prices? Higher? Lower? Holding in the low-to-mid-\$20/cwt. range?

Rising production costs—energy, interest, hay, feed, parts, etc.—worry dairy farmers because they cannot afford to go backwards on net margins, not after 2006's disaster. Unless financial returns for producing milk show reasonable signs for *getting* better and *staying* better, many U.S. dairy farmers who have survived to this point don't have much gumption for going through financial Hades again.

Ignore CME Class III Futures!

Many of the usual baloney-peddlers—university dairy economists and other systemic "experts"—point to December 2007-January 2008 Class III (cheese milk) futures prices at the Chicago Mercantile Exchange (CME). Those prices range near \$16 per cwt.—about \$5.00/cwt. below the final July 2007 Class III price for USDA's milk order system. If those Class III futures prices are accurate, such a \$5/cwt. decline in cheese-milk prices (from current levels) would be hard to swallow for dairy farmers.

Dairy farmers worrying about a big decline in milk prices commonly cite Class III futures prices at CME.

Are those CME Class III projections for a \$5/cwt. milk price drop by early winter accurate??? *The Milkweed* would argue NOT, and all we need to do is to look at recent history to show how far off CME Class III futures can miss the market, so as to disregard them as legitimate price predictors. Dairy farmers merely need to go back to late January 2007. CME Class III futures for June 2007 finished trading on January 31, 2007 at \$14.88/cwt. In fact, the June 2007 Class III price for USDA's federal milk orders came in at \$20.17/cwt. The CME Class III futures in the early two months of 2007 missed the June 2007 Class III price by \$5.29/cwt. ... way off the mark!

Sadly, any dairy farmer who made business decisions, such as locking in future milk prices based on those Class III futures using CME futures prices in early 2007, has missed out on a huge chunk of milk income. (Imagine the pain felt by some dairy farmers who locked in annual contracted prices for their milk in early 2007, using CME Class III price quotes in the \$14.50-15.00 range! Those farmers got suckered by "experts" telling them to sign future price deals based on market projections that widely missed the mark.)

Simply stated: *The Milkweed* advises persons to disregard CME Class III as future milk price indicators. CME's dairy programs operate as a network for thieves and manipulators.

Global markets: Better future price indicators

Hard to believe the accuracy of CME "futures" prices projecting coming months' eroding futures prices at CME, when one takes a good look at global dairy commodity price trends. Around the world, scarce supplies of dairy commodities are finding impossibly high demand. Global scarcity of dairy products is driving commodity prices sky-high.

According to Dairy Market News, significant measures of global dairy commodity prices are far higher than current cash market prices traded at CME. Dairy Market News is USDA's dairy marketing information branch, publishing weekly a variety of important dairy data and analysis each month.

Western Europe, in particular, is under great stress for current dairy product supplies. Years of low prices and some adverse weather a couple years ago have constricted milk production in that region.

Butter prices up to \$2.50/lb. in Europe: Commodity butter prices in western Europe have basically DOUBLED in the past three months. According to Dairy Market News, in early July the high-end of the price range for butter sales in Europe rose to \$5500 per metric ton—or almost exactly \$2.50 per pound. Since early July, Dairy Market News' international reporter Steve Schneeberger has reported the high-end of the western European butter price range is firm, while the bottom of the range is advancing.

\$2.50 per pound butter as the top end of the butter price range in western Europe? That's roughly \$1.00/lb. HIGHER than current cash prices for Grade AA butter at CME! These dairy commodity prices will likely remain firm in western Europe for at least the next year.

(Separately, *The Milkweed* is picking up rumors from subscribers with family contacts in western Europe that the European Union is considering imposing a ban on dairy product exports, in order to keep product shortages from hitting citizens of the EU nations. A ban on food exports would likely violate "Free Trade" rules of the World Trade Organization. But bureaucratic rules don't mean beans, when a free nation's senior citizens remember the long-suffering hunger during the 1940s.)

Skim milk powder up to \$2.50/lb. in EU: Curious, but the recent high end of Dairy Market News' price survey for skim milk powder in western Europe in recent weeks has hit \$5500/metric ton—same as butter's high-end range. (Skim milk powder is similar to nonfat dry milk, but has one to two percent less protein content.) Global supplies of skim milk powder and nonfat dry milk are very, very tight. Global demand for high quality dairy proteins is very, very strong.

As of August 8, 2007, the CME price for Grade A nonfat dry milk was \$2.11/lb. Meanwhile, the National Agricultural Statistics Service survey in late July ranged around \$2.01—significantly below the western European market.

Cheddar Cheese \$2.00-\$2.12/lb F.O.B. NZ: Hard to believe, but according to Dairy Market News, the high end of the commodity Cheddar cheese price survey in Oceania (New Zealand-Australia) was about \$4400-4700/metric ton, or \$2.00-2.12/lb., at the end of July. That range was \$.15 to \$.25 cents per pound higher than the July 31, 2007 block Cheddar cash market price at CME.

Seldom in the history of global dairy market analysis has the price of Cheddar cheese at the dock in New Zealand been so far above the commonly-referenced U.S. cash market for Cheddar.

EU Butter/Powder: \$30/Cwt.!

Currently, commodity prices for butter and skim milk powder (SMP) in western Europe are very high. SMP is a dairy protein powder, with slightly less protein content than nonfat dry milk. USDA's Dairy Market News reports current top end of price ranges for both butter and SMP are \$2.50 per pound. Commodity butter prices have doubled in Europe in the past three months.

What if such sky-high prices for butter and nonfat dry milk were plugged into USDA's federal milk order pricing formula? At \$2.50/lb. for both butter and nonfat powder, the Class IV price in the federal milk order system would be \$30.14/cwt. And that price would lift Class I (fluid) and Class II (cultured products prices) above \$30/cwt.

Do not underestimate the combined forces of global scarcity of and desire for high-quality dairy proteins, along with a weak U.S. dollar.

Imagine: European prices for butter/milk powder translating into \$30/cwt. prices here!

Weak U.S. dollar means "higher" prices

Without any consideration to global milk production and demand factors, the weakened value of the U.S. dollar is also helping spur "higher" global dairy prices. The U.S. dollar is so weak that the Canadian dollar has climbed to within a few cents of the greenback!

When defined in terms of today's weak U.S. Dollars, global dairy commodity prices appear especially high in the U.S. But foreign buyers using strong currencies think they're getting a bargain, sort of.

There's a serious downside to a weak U.S. dollar driving up global dairy commodity prices: costs of many dairy production inputs that are based upon global costs, are getting downright expensive for American farmers!

High global dairy prices should hold for YEARS!

As noted earlier, it looks as if it will take the major dairy nations some time to rebuild milk production levels. More optimistically, a Rabobank dairy expert last spring projected at least five years of high global dairy commodity prices.

Structurally, it looks as if global dairy commodity prices have sought a new high ground, so to speak.

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Will U.S. dairy farmers fully benefit?

Will U.S. dairy farmers see most of the benefits of higher global dairy commodity prices? Yes, to a degree. Global dairy prices have been a major factor driving up U.S. milk powder prices. And now global butter prices are riding up fast, if European butter prices' doubling in three months is an indicator!

But the matter of European dairy commodity skyrocketing far above U.S. prices presents a chilling scenario to U.S. dairy farmers: how much of the global "pie" will dairy farmers be allowed to enjoy? Will global butter prices fail to materialize in the U.S. market place—either through parties holding down CME cash markets, or else due to butter exporters either selling low or not passing through the higher prices to USDA's weekly NASS survey?

It's a serious worry: will butter pricing events—domestic and global/CME and USDA—repeat the recent scenario of the milk powder pricing scandal??? That scandal featured U.S. dairy commodity exporters failing to properly analyze global supply/demand and prices, and then failing to report accurate dairy commodity prices to USDA. U.S. dairy farmers have lost hundreds of millions of dollars on the milk powder pricing scandal, and now may watch U.S. dairy marketers aim low on global butter export opportunities.

"Global markets ... global market prices"

In days of yore, when "Free Trade" advocates (like Farm Bureau wind-ups) extolled the merits of "Free Trade," American farmers were promised "global markets and global market prices." Of course, back when U.S. dairy commodity prices were much higher than world market prices, such promises were hollow and suspect.

media is having trouble getting any kind of focus.

Today ... global prices for scarce dairy commodities—cheese, nonfat dry milk, skim milk powder, and butter—are shooting up fast. And the "same-old, same-old" tools of milk price thievery are in place again:

* Grade AA butter cash market prices at CME are nearly \$1.00/lb. below the high end of the western European butter price range estimated by Dairy Market News. (Sounds like recent milk powder thievery.)

* Butter marketers talk of several months needed to contract and deliver product to Europe—a factor which would keep those prices out of USDA's weekly NASS surveys. (Sounds like recent milk powder thievery.)

* CME Cheddar prices are roughly 20-25 cents/lb. lower than Cheddar prices f.o.b. the dock in Auckland, New Zealand. (That's a rarity.)

Global dairy commodity prices are sky-high ... \$2.50/lb. for butter, \$2.50/lb. for nonfat dry milk, and \$2.00-2.12/lb. for Cheddar. If fully passed through the federal milk order pricing system, those commodity price levels would yield Class III (cheese milk) prices in the \$23/cwt. range ... **and Class IV (butter-powder) milk prices just above \$30.00/cwt.**

The way USDA's federal order system works, a \$30/cwt. price for butter-powder milk would drive up Class II (cultured products—yogurt, sour cream and ice cream) and Class I (fluid) to prices above \$30/cwt.

One more time, the money is in the market place ... BIG MONEY—\$30/cwt.! And U.S. dairy farmers had better vigilantly pay attention to how much of the higher global prices actually comes back to their farm through this nation's corrupt, crooked, convoluted and constipated milk pricing system.