Kraft Foods Up to Its Old Tricks … As Cheddar Prices Fall

by John Bunting

The concept of absolute monarchs, with divine rights, has long been discredited. But, in dairy, we see a general acceptance of the "divine rights of markets." For dairy farmers, "the market" is the cash commodity trading of Cheddar, Grade AA butter, and nonfat dry milk at the Chicago Mercantile Exchange (CME). Farm milk checks are essentially produced from cash market data originating at CME.

Some of the ups and downs of CME cash Cheddar trading should not be misinterpreted as an accurate or honest "market."

Statistically, a near perfect correlation — 95.9% — exists between Cheddar trading at the CME and dairy producers' "all milk price." The "all milk price" is a compilation of USDA's National Agricultural Statistical Service (NASS) and includes data from all states. The "all milk price" includes quality, quantity, and other premiums, before hauling charges are deducted. Hauling subsidies are excluded.

All factors determining dairy farm milk prices should be open and transparent. However, the myths of the market and transparency are not compatible. Nevertheless, the "secrets" of dairy trading are known to insiders. There are several confidential suppliers of daily trading data, which generally include the floor traders' symbols. The Milkweed obtains data from several sources in an effort to confidently understand the CME trading. Keep in mind: CME floor trading information is technically not verifiable — because the CME rules prohibit revealing trader's activity.

Kraft Foods Has a New Trick

August 2011: Kraft's signals help pull down Cheddar market

August 2011, was an important month at the CME. For August 2011, there were 45 loads of block Cheddar traded at CME, compared with a total of only four loads traded in August 2010.

The month began with Darigold initially dropping prices. Darigold is the predominant dairy farmers' cooperative in the Pacific Northwest. On August 11, 2011 Kraft moved into the market. Since the spot cash Cheddar trading moved from the old National Cheese Exchange in Green Bay, Wisconsin in early 1997, Kraft has tended to use surrogates at the CME. This year, Kraft moved from the old National Cheese Exchange in Green Bay, Wisconsin in early 1997, Kraft has tended to use surrogates at the CME. This year, Kraft moved from the old National Cheese Exchange in Green Bay, Wisconsin to the CME. Kraft, in order to sell the cheese at the CME, first had to buy relatively expensive Cheddar to crash the price. Kraft then refused to sell the cheese at the CME. Since the trading moved to Chicago and Class III milk futures were instituted.

There is no reason to think Kraft's motivations in 2011 are any different than they were in the 1990s. Cheaper Cheddar boosts net profits. Kraft, in order to sell the cheese at the CME, would have had to buy relatively expensive Cheddar to crash the price. Kraft has closed its U.S. Cheddar plants in recent years.

The CME is purported to be a place where "surplus" Cheddar is sold. Kraft, nevertheless, walked away from a bid for barrel Cheddar on August 23, 2011, which would have raised the price. The bid was by Grain Mills (based in Minnetonka), which might have gotten its signals crossed, because the next day the opening bid by Grain Millers was less than the closing price of the previous day.

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Kraft Foods has played a part by increasing cheese yields through the use of unapproved food ingredients such as, milk protein concentrate (MPC). On December 18, 2002, the U.S. Food and Drug Administration (FDA) sent a stingering letter to Betsy Holden, CEO of Kraft Foods. The letter stated, "These products declare milk protein concentrate in their ingredients listings."
Milk protein concentrate (MPC) is not listed as an optional dairy ingredient in any of the standardized cheese products governed by a standard of identity, and therefore standardized cheese products are not permitted to contain MPC as an ingredient.

At issue: Kraft’s failure to comply with federal standards of identity, by using an unapproved ingredient in a food for which a federal standard of identity existed. Kraft was never punished or fined by FDA for these violations. Kraft continued to use MPC and simply changed the name of the “Singles” product from “processed cheese food” to “processed cheese product.”

Kraft has continued to “scheme” around the standards of identity embedded in the Code of Federal Regulations (CFR). U.S. patent number 6,406,736, granted on June 18, 2002 for a “cream cheese” which has a moisture content of 65%. CPN# 133,133 (cream cheese) limits the moisture content to 55%. More water equals less cheese is needed boosting profits, if not compromising product integrity. (Editor’s note: Look closely at the Kraft offerings in the array of products in the “cream cheese section” of you local supermarket’s dairy case. Most of the “Philadelphia” branded products are technically not cream cheese. Kraft has simply taken the good name of its old-line, “Philadelphia Cream Cheese!”, kicked out the “Cream Cheese” label (along with requisite ingredients), and continues selling the “stuff” with the implication that “Philadelphia is cream cheese!”

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Federal Standards of Identity for foods were instituted by FDA to promote honesty and fair dealing in the interest of consumers. Regulations were promulgated as a means of protecting consumers from deception and fraud in the practice of commerce. Regulations were promulgated to preserve the standard of quality, and/or reasonable standards of fill-of-container. Then U.S. patent number 6,183,804, granted February 6, 2001 promotes “the use of knowledge” with CME prices over two dollars per pound. The thinking is supported to go, with Cheddar prices falling on the CME more cheese will be consumed. The obvious flaw in that argument is the Kraft does not consume any cheese, nor does any other traders on the CME for all practical purposes.

It is the public who consumes cheese, which they buy at retail price.

In 1984 the spread between the NCE block Cheddar price and the retail price was $1.724 per pound. In 2011, the average spread between the CME block Cheddar price and retail Cheddar price is $3.43 per pound. For July 2011 the spread was $3.481 per pound. Clearly, if there is “buyer resistance” to the “high cheese prices” at the supermarket, the commodity price (per pound) is not to blame.

However, even the argument about price at the CME fails because there is absolutely no correlation between commercial disappearances and farm milk price — none.

The root problem here lies in the willing acceptance of bullies as representatives of a functioning market. In theory, a market is a knowledge tool and as Nobel laureate F.A. Hayek stated in his 1945 essay “The Use of Knowledge.”

“...The problem of a rational economic order is determined precisely by the fact that the knowledge circumstances of which we must make use never exist in concentrated or integrated form but solely as dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess.”

That is to say, it isn’t possible for a corporation such as Kraft to be “the market.” Essentially, the value of the market over centralized planning, and centralized planning can either be state or corporate, is efficient allocation of resources.

How far dairy has strayed from fundamentals

Look at the dairy industry in America. The dairy cow is a wonderful creature capable of taking renewable resources, primarily grass grown on hillsides unsuitable to cultivated crops, and converting that grass to a fine human food. The process is a perfect example of the efficient allocation of resources.

What we now have in America, is a system which takes primarily imported fossil fuel-based fertilizer, which is dumped in excess amounts in the corn states, thereby creating a “dead zone” in the Gulf of Mexico, to be trucked for hundreds, or thousands of miles to feed dairy cows in dry lot settings.

Kraft Foods represents a system which reduces margins on its suppliers to such an extent that efficient allocation of all resources is no longer even talked about. Kraft is corporate planning with official sanctioning from government officials — the detriment of dairy farmers and consumers.

“Buyer resistance” to cheese prices? Don’t blame farmers!

The next argument made by the “market” apologists has to do with “buyer resistance” with CME prices over two dollars per pound. The thinking is supported to go, with Cheddar prices falling on the CME more cheese will be consumed. The obvious flaw in that argument is the Kraft does not consume any cheese, nor does any other traders on the CME for all practical purposes.

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