



MCT COMPASS

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Got milk?

U.S. milk production is finally slowing down after more than four years of posting increases versus the prior year. USDA reports that milk production in the selected 20 states, which account for 85% of U.S. milk production, increased by just 4 million lbs. in December 2000 compared with December 1999. USDA further estimates that for the entire country, milk production actually fell by 8 million lbs., marking the first decline in monthly milk production versus the prior year since the summer of 1996.

Typically milk production increases by 1.1% annually. However, exceptionally strong milk prices during the second half of the 1990s triggered expansions on the farm. Cow numbers began climbing in early 1999 and producers enjoyed a 22-month stretch in which they expanded their herds by 156,000 head (+2.0%).

In November, the expansion came to an abrupt halt. Cow numbers sank 8,000 head that month, and another 4,000 in December.

While the number of cows in the U.S. dairy herd has begun to drop off, the most significant contributor to slowing milk production growth is lower milk production per cow. The early winter across most of the United States contributed to some of the decline.

In addition, dairy producers are managing their herds differently in response to lower milk prices by feeding their cows lower-cost rations and using less bST. In the selected 20 states, milk production per cow in December was 1.0% lower (-16 lbs.) compared with December 1999.

The Western states are bearing the brunt of the decline: output-per-

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KEN'S CORNER



**by Ken Meyers
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The New Year is a little more than a month old and there's plenty happening out there. Slowing

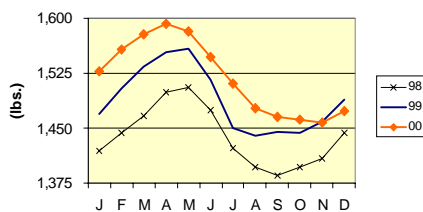
milk supplies both domestically and abroad are providing reason to believe we'll see higher dairy prices in 2001.

Meanwhile, on the policy front, USDA's now-you-see-it-now-you-don't Class III butterfat price has caused tremendous uncertainty in cream and butterfat prices. It remains to be seen if the chaos we saw in cream marketing last month will be alleviated by the Jan. 31 ruling.

Note that last week's ruling on butterfat pricing pertains to the Class III price only. No one has challenged the tentative Class IV pricing formula, which increased the Class IV skim price by 40 cents per hundred-weight.

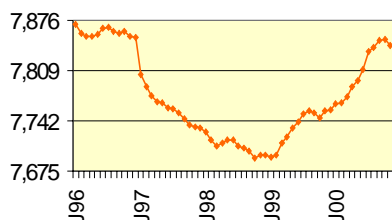
The real wild card for 2001 is the California situation, from energy to weather to environmental pressures. In the next issue of the *MCT Compass*, we'll provide an update from the Left Coast. □

Milk Production Per Cow
(20 selected states, 30-day months)



Milk Cows

(20 selected states, in thousands)



Growth in productivity and cow numbers have begun to reverse.

Bulls look for recovery

Bullish factors are rearing their heads, but it's questionable whether or not barrel cheese demand will pull block prices up in the near term.

The slowdown in milk production, in tandem with the California utility crisis, has many end-users of

dairy products worried about a return to higher price levels in 2001.

Butter buyers have a short memory and are trying to protect themselves from a repeat of 2000, when butter prices spiked to \$1.85 in the fall. This is providing earlier-than-usual strength to the butter market. □

Got milk ...

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cow in Washington fell by 95 lbs. in December vs. a year ago, -85 lbs. in Texas, -50 lbs. in New Mexico, -35 lbs. in California and -10 lbs. in Idaho.

We'll be watching these numbers closely in 2001 to see how dramatically milk production turns around. It may not be quick enough for some people's liking; even though milk production per cow is below trend, the number of cows in the nation's herd is still 69,000 head (+0.8%) higher than a year ago. □

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV
FEB	1.1500	1.1500	10.12	1.2850	12.55
MAR	1.1975	1.1750	10.55	1.3400	12.78
APR	1.2010	1.1805	10.57	1.3500	12.87
MAY	1.2170	1.1920	10.67	1.2750	12.55
JUN	1.2600	1.2350	10.92	1.3200	12.74
JUL	1.2800	1.2550	11.26	1.3500	12.89

* Block, barrel and butter are monthly averages of CME prices.

An update on Class III butterfat pricing

The dairy industry – both producer and processor interests – has finally found something to agree on: USDA's proposed separate Class III butterfat price calculated from the cheese market was not a good idea. A joint letter signed by all major processors and cooperative organizations is on its way to USDA.

In addition, three producer groups asked a Washington, D.C., district court to step in and issue a preliminary injunction preventing the implementation of the separate Class III butterfat price prior to the Feb. 2 announcement of the January Class III price. Judge Lambreth

granted the preliminary injunction against USDA on Wednesday, Jan. 31.

The ruling simply means that the Class III price for January 2001, and for the foreseeable future, will be calculated the same way it was throughout 2000, except for two changes: the make allowance is reduced from \$0.1702 per lb. to \$0.165 per lb., and 38% moisture barrel cheese price is used instead of 39% moisture barrel cheese price. The lower make allowance and lower moisture cheese price enhance the Class III price at 3.5% butterfat about a dime versus the Class III price formula as proposed in the tentative final

decision

The industry was able to rally around this cause because the separate Class III butterfat price – calculated from the cheese price – was disrupting the marketplace. It was sending a market signal to cheese manufacturers in the Federal Orders to skim their incoming milk and sell the cream to butter and ice cream manufacturers, while buying cream from California to put into their cheese vats.

Meanwhile, producers were concerned that when the day comes that the Class III prices sets the fluid milk price, the reduction in the skim value of milk would have hit them in the pocketbooks. □

