



MCT COMPASS

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Pie in the sky no longer

Early returns show pizza is having another off year. Is it time for mozzarella makers to push the panic button?

In the late 1990s, driven by Americans' seemingly insatiable appetite for pizza, many U.S. cheese manufacturers made a decision: go mozzarella. For the last quarter of the 20th century, mozzarella consumption grew 7% annually. From 1997 to 2001, plants boosted capacity further, expanding production of mozzarella by well over a million lbs. a day in just four years.

Last year, however, the usual growth wasn't there. Production was up just 1.7% in 2002, the third-lowest figure in the last three decades.

Of course, though rare, the mozz market has had off years before;

production declined fractionally in 1981, 1993 and 1997. But in those previous cases, production snapped back strong in the following year.

This time around is shaping up differently. Instead of a rebound, in the first quarter of 2003, mozzarella production is *down* 1.9% vs. a year ago. And declining consumption of pizza, the major mozzarella user, is identified as the culprit.

Tellingly, same-store sales at most leading pizza chains are sliding this year. In the first quarter, sales at Pizza Hut were off 3%, Domino's -1%, Papa John's -5%, Chuck E. Cheese -3% and Pizza Inn -5%. Most of these companies blame the downturn on the competitive foodservice environment and weak economy.

Restaurant traffic overall has declined for three straight quarters,

according to market researchers NPD Group, the first time that's happened since the company began tracking industry trends more than two decades ago. Further, lower-income consumers are the ones who have traditionally driven the pizza/fast-food markets, and they're the ones hurt most by the economic slowdown.

Demographic shifts play a role as well. Pizza sales have grown by leaps and bounds over the last 30 years because it's been a convenient meal option for families. But the aging U.S. population has left more empty-nesters, who are more inclined to pass on pizza for other alternatives. While the burger and pizza segments struggle, so-called "quick-casual" restaurants – establishments offering

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KEN'S CORNER



*by Ken Meyers
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As the U.S. pizza industry approaches a saturation point, the dairy industry must be

mindful of two issues:

1. Make sure we aren't losing customers due to lower quality. In tight-margin times, manufacturers

may be tempted to fill the vats with cheaper dry ingredients, but in the long run it just leaves consumers unsatisfied and turning elsewhere.

2. Escape the commodity mindset. I understand that mozzarella is a volume business, but aging consumers are seeking out new challenges for their taste buds. Manufacturers and marketing organizations need to keep working with pizza operators to encourage menu development that keeps people in the category.

The "administrative tilts" USDA is considering are a step in the right direction (*see story on p. 2*) to correct what ails the support price system. However, it's critical that any change made reflects actual costs of selling product to the government. Tougher grading standards, higher packing costs and longer ripening before grading make CCC our toughest customer, adding expenses that are not reflected in the current purchase price calculations. **MCT**

Turnaround around the corner

In the first four months of the year, milk production was up just 1.1% from a year ago; meanwhile, total cheese production was down 1.1% in the first quarter, while butter output was up 1.1%. Slowly but surely, low milk prices are starting to have an impact on supplies.

Over the next month, we expect the cheese market to start a seasonal climb. Blocks are forecast

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
MAY	1.1425	1.1150	9.72	1.0925	9.73
JUN	1.1725	1.1425	9.85	1.1000	9.80
JUL	1.2700	1.2400	10.70	1.1275	9.95
AUG	1.3000	1.2700	11.30	1.1400	10.10
SEP	1.3300	1.3000	11.60	1.1800	10.40
OCT	1.3500	1.3200	11.95	1.2000	10.50

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

to top \$1.30 by late summer, leading to Class III prices near \$12.00 this fall. **MCT**

Pie in the sky ...

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lighter fare like salads and sandwiches – continue to do well. In 2002, the 15 largest quick-casual chains enjoyed collective sales growth of 12%, according to foodservice consultancy Technomic Inc.

It's probably not a coincidence that one of the few leading pizza chains that did post same-store sales gains in the first quarter was California Pizza Kitchen (+3%). On CPK's menu, older, sophisticated consumers will find tantalizing pies like Caramelized Pear and Gorgonzola, Tandoori Chicken and Carne Asada. Better than any other national chain, CPK combines Baby Boomers' love of experimentation, bold flavors and ethnic influences.

But perhaps pizza chains' fiercest competition comes from the freezer case. The quality gap between take-out and frozen has narrowed considerably, as food processors have added rising/stuffed crust, better toppings and fanciful flavors to their lines. Consumers can now get a near-

take-out quality pie in their grocers' freezer case for half or one-third the cost of ordering out.

Retail sales of frozen pizza and snacks increased 2.1% in the year ending March 22, 2003, according to ACNielsen Scantrack data. That figure doesn't suggest consumers are completely abandoning foodservice for frozen, but the segment is significant (\$3 billion in sales) and growing.

Before cheese manufacturers push the panic button, note that there is still no consensus about the extent of the pizza industry's "demise." Many suppliers and industry watchers report that overall, pizza consumption is doing just fine. Anecdotal accounts also suggest that though chains may be struggling, independent pizza operators are increasing share.

In short, the pizza market seems to be maturing along with its customers. The dairy industry may just need to come to terms with the fact that 7% annual growth could be a thing of the past. **MCT**

USDA mulls more 'tilts'

Last month, USDA implemented changes in the yield and make allowances in its Federal Order Class III and IV milk prices. As a result, the department is considering changes in its purchase prices of butter, nonfat dry milk and cheese.

USDA is proposing the change in the Class IV formula be borne by a 2¢ increase in the support price for butter, with no change in the price for nonfat dry milk. Changes to the Class III formula would result in a small (less than a penny) increase in the support price for cheese. A decision memo is on the Secretary's desk that could make this "administrative tilt" a reality in the near future. But if implemented, it would count as one of the two "tilts" the Secretary is allowed to make each year.

The department has another "tilt" to consider as well. Earlier this year, NMPF requested adjustments in CCC purchase levels for cheese, butter and nonfat dry milk to reflect the additional costs manufacturers face when selling products to the government. NMPF requested purchase prices be raised 5.6¢ on cheese, 1.5¢ on butter and 2.25¢ on nonfat dry milk. This also would count against the "two-tilt" limit, however, USDA has yet to respond to NMPF's request. **MCT**

