



MCT COMPASS

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Information-starved industry

The industry looks to the U.S. Department of Agriculture as the source of key information. Markets react – often dramatically – to favorable and unfavorable releases. But how much stock should we place in these reports?

The three USDA reports with the most potential to move the market are *Milk Production*, *Cold Storage* and *Dairy Products*. All three contain preliminary estimates for the latest month and revisions for the prior month. Monthly figures are revised again the following spring in an annual summary.

Over the years, the *Cold Storage* report has received the most criticism for its revisions. *Milk Production* is regarded as the most reliable. An analysis of preliminary and revised

data from the last three years (2000-2002) shows those perceptions to be accurate (see chart on page 2).

In our study, in which we compared preliminary estimates to final revisions, actual **milk production** in the 20 selected states deviated from the initial estimate by an average of 0.34% — roughly 41 million lbs. Two-thirds of the time, the preliminary figure has over-estimated or under-estimated the actual production figure by at least two-tenths of a percent (24 million lbs.). More than a quarter of the time it's been off by at least half a percent.

Production was overestimated in 21 of the 36 months, by an average of 0.38%. In the 15 months of underestimation, USDA revised up by an average of 0.28%.

The **American cheese produc-**

tion figure in *Dairy Products* is closely watched in terms of its market impact. But revisions are common. Since 2000, final revisions have deviated from the initial estimate by an average of 1.58% — the equivalent of almost 5 million lbs. per month. Two-thirds of the time, the preliminary figure has over-estimated or under-estimated the actual production figure by at least 1%. Almost a quarter of the time it's been off by at least 2%.

Production was overestimated exactly half the time in the last three years, by an average of 1.73% (5.2 million lbs.). The other half of the time, production was underestimated by an average of 1.43%.

The least reliable of the three reports has been *Cold Storage*, with

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KEN'S CORNER



*by Ken Meyers
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In an environment starved for accurate, real-time information, the dairy industry

looks at any and all reports to get a sense of what's going on in the market. Complicating matters, they

build expectations for reports into the way they price the markets, and depending on whether the reports tell them what they expected to hear, react accordingly.

Such was the case with the July "Milk Production" report released in mid-August. The industry expected July milk production to come in lower; instead, it came in six-tenths of a percent higher. The market responded

swiftly the following trading day, with September through April contracts plunging an average of 61¢.

Trouble is, not all information is created equal. As our feature story this month details, all USDA reports are subject to revision that can change the way we interpret the data. How much will the preliminary July number be revised? Stay tuned. We'll find out on Sept. 17. **MCT**

Cheese stalls

After rocketing from support to \$1.60 in just 40 trading days, the block cheese market remained at that level throughout August. With Labor Day behind us, buyers and sellers alike are trying to determine how much longer the market will hold.

Based on the tightness of current natural cheese, we think the market will hold for at least another month or two. And when

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
AUG	1.6000	1.5736	13.79	1.1708	10.20
SEP	1.6400	1.6050	14.40	1.1785	10.10
OCT	1.6100	1.5725	14.70	1.2500	10.40
NOV	1.5200	1.4850	14.10	1.2500	10.45
DEC	1.4300	1.3975	13.05	1.2115	10.35
JAN	1.3600	1.3300	12.35	1.2000	10.30

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

the market does break, lower milk supplies should keep prices from falling too low.

The butter market should see a small seasonal bump ahead of the holiday buying period. **MCT**

Information-starved ...

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an average deviation on **American cheese inventories** of 2.08% — the equivalent of 10.7 million lbs. monthly. Half the time it's been off by at least 1.5% and more than a quarter of the time it's been off by at least 3%. However, it's worth pointing out that the *Cold Storage* report has improved its accuracy considerably in the last two years. In 2000, the average deviation was a troubling 3.65%, and 8 of the 12 months were revised by at least 3%. In 2001 the deviation was 1.53%. In 2002, it was just 1.06%.

USDA is far more likely to under-count inventories than over-count. Stocks were underestimated 23 of the 36 months, by an average of 2.73%. In the other 13 months USDA revised inventories down by an average of 0.92%.

Milk Production, Cold Storage and Dairy Products

are compiled by the National Agricultural Statistics Service (NASS) branch of USDA. A separate branch of the department, the Economic Research Service (ERS), publishes the "Livestock, Dairy & Poultry Outlook" each month, providing forecasts on prices, production and myriad other indicators.

To gauge ERS' forecasting accuracy, we looked at its Class III forecast for each year in the January report back to 1995. ERS typically

gets the direction of price movements from year to year correct in its forecasts, but almost always underestimates the magnitude.

Despite allowing itself an 80-90¢/cwt. range in its outlook, ERS has correctly called the actual Class III price just once in the last nine years. The other eight years the actual price has fallen outside ERS' forecasted range. On average, the actual Class III has varied from the mid-point of ERS' January forecast by \$1.29/cwt. **MCT**

USDA Report Revisions: How much are they off, how often?

percent change of preliminary estimate to final revision, 2000-2002 (36 months)

	0-1%	1-2%	2-3%	3+%	Average deviation
<i>Cold Storage:</i>					
American cheese inventories	11 mos.	11 mos.	4 mos.	10 mos.	2.08%
<i>Dairy Products:</i>					
American cheese production	12 mos.	16 mos.	3 mos.	5 mos.	1.58%
<i>Milk Production:</i>					
20-state milk production	12 mos.	11 mos.	7 mos.	6 mos.	0.34%

About two-thirds of the time preliminary Cold Storage and Dairy Products reports under- or overestimate actual figures by at least 1% and preliminary Milk Production reports under- or overestimate by at least two-tenths of a percent.

