



MCT COMPASS

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Killing cows

Record-high cattle prices and the CWT program are encouraging producers to cull at tremendous rates. The prospect is for lower milk supplies for months to come.

Rock bottom milk prices from mid-2002 through mid-2003 were the first blow that sent the U.S. dairy herd into contraction mode. The U.S. dairy herd topped-out with 9,155,000 head in March 2003. By September the herd had declined by more than 100,000 head.

The closing of the U.S.-Canadian border for the importation of live Canadian cattle and meat after discovering a BSE-stricken cow provided dairy farmers a second incentive to cull marginal cows. The cull cow slaughter price went from \$40 per cwt. during the spring of

2003 to nearly \$55 per cwt. this past week at the South St. Paul Terminal Auction.

An additional carrot was offered to dairy producers in the form of the CWT (Cooperatives Working Together) program that paid producers to either retire their entire herd or reduce their production. The CWT program received 2,038 bids from dairy producers for the herd retirement program. Nearly 300 of those bids were accepted, resulting in 32,724 cows being sent to slaughter. Some of those cows were included in the larger-than-usual September slaughter. According to USDA, 248,200 head were culled in September, a 14.3% increase compared with August and 14.5% more than last year. The October cull is also expected to be robust as the bulk of the

CWT cull cows will be slaughtered.

The combined herd retirement and reduced marketings programs are expected to reduce the U.S. milk supply by 696 million lbs. over the next year. That translates into 58.0 million lbs. less milk produced each month, 5.8 million lbs. less cheese manufactured, or 145 fewer potential lots of cheddar cheese available for sale at the Chicago Mercantile Exchange each month.

But the ultimate goal of the CWT program is to reduce the milk supply by 1.2 billion lbs. over the next year, with the additional volume coming from an export assistance program for butter and cheese that has yet to be launched. CWT management is waiting for the gap between U.S. and

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KEN'S CORNER



*by Ken Meyers
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2004 is lining up to be a very interesting and potentially volatile year for milk and dairy

product prices. This week the first cracks emerged in the bull cheese market of 2003, but prospects are

for a soft landing and return to strong markets again next year.

The high cull cow prices in tandem with the CWT program have reduced the U.S. dairy herd, while higher soybean prices may force dairy farmers to feed alternative ingredients that generate less milk. California will show its slowest rate of milk production growth since 1998.

Higher milk prices will enable some

expansion, and the opening of the Canadian border is expected sometime in 2004, which will likely cause slaughter cow and replacement cow prices to fall. As that happens, the industry should be prepared for the CWT program to kick into higher gear.

The potential market impact can not be underestimated when the parties behind the acronyms NMPPF, CWT and DFA work together. **MCT**

Market cracks

The CME block cheese price has entered an adjustment phase after trading at its highest level for the longest sustained period - 62 trading sessions. We expect the block price to settle between \$1.25 and \$1.35 per lb. over the next several weeks.

Dairy product demand is projected to pick-up during the holiday season and draw down inventory levels. Ending stocks will be less than last year but ample, providing a softer year-end landing for dairy

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
OCT	1.5900	1.5400	14.37	1.1860	10.15
NOV	1.4300	1.3950	13.50	1.1950	10.25
DEC	1.3400	1.3050	12.40	1.1800	10.20
JAN	1.3200	1.2900	11.95	1.1950	10.25
FEB	1.2850	1.2550	11.75	1.2350	10.30
MAR	1.2950	1.2650	11.45	1.2500	10.45

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

product prices and a higher price level going into 2004.

The impact of the large dairy cull will set the stage for prices to rebound during the first or second

quarter of 2004.

Butter prices are expected to remain near \$1.20 for the medium term, keeping Class IV prices around \$10.25. **MCT**

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world cheese prices to narrow.

The CWT \$60 million program is bankrolled by dairy producers and cooperatives that have pledged a nickel per hundredweight on 70% of total U.S. milk production. This appears to be just the beginning.

At DairyLea's recent annual meeting, Gary Hanman, CEO of Dairy Farmers of America, the nation's

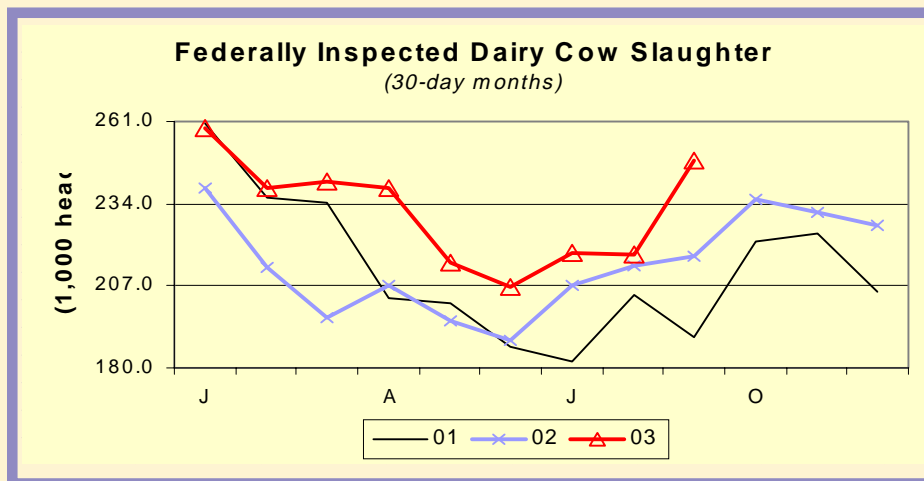
largest dairy cooperative, stated that cooperative leaders would be meeting in November to discuss a bigger and more comprehensive CWT program for next year.

It is likely that the ante for CWT will be increased another nickel or dime to come closer to funding the program at the initial recommended rate of nearly 18¢/cwt. **MCT**

Managing after the kill

If the dairy markets weren't already difficult enough to predict, the implementation of the CWT program has added a new dimension to that complexity. CWT proposes to remove 1.2 billion lbs. of milk in its initial year of operation. That's equal to about 0.7% of total milk production. It's enough milk to produce 120 million lbs. of American cheese, more than 3% of annual production and nearly a quarter of commercial inventories at any given time.

To put the potential market impact of the CWT program in perspective, in 2001, American cheese production fell by 3.1% driven by a 1.3% decrease in milk production. The CME cheddar block price topped out at \$1.78 per lb. in August while CME cash butter soared to \$2.225 per lb. that month. Record dairy product prices resulted in relatively high average Class III and IV prices for the year at \$13.10 and \$13.76, respectively. **MCT**



Dairy cow slaughter jumped 14% in September due to record-high cull-cow prices and 18 months of low milk prices. Source: USDA.

