



MCT COMPASS

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It's the Cows

Historically, the U.S. dairy herd declined by about 1.0% annually and output per cow increased by nearly 2.0%. And that meant net-net the industry had 1.0% more milk to market each year.

Since the arrival of the new millennium, those statistics have not followed the historical trend. The average number of milk cows in the U.S. dairy herd actually increased in 1999, 2000 and 2002. From 1998 through 2003, the annual average number of milk cows in the U.S. dairy herd varied by just 96,000 head, or 1.0% for the entire six-year period.

In 2003, after enduring more than 12 months of exceptionally low milk prices, dairy farmers culled 2,857,000 cows. That was 250,000 head more than the prior year.

In 2004, just the opposite is true. Record-high milk prices have persuaded producers to cull fewer cows. The dairy cow slaughter from January through July totaled just 1,353,000 head. That's 280,000 head less than 2003's slaughter for the same period.

Now that farm level milk prices have fallen from May's historic high to just above average in August, the Cooperatives Working Together (CWT) committee has voted unanimously to initiate another herd

retirement program. In 2003, the CWT program removed 33,000 head from the U.S. dairy herd under its herd retirement program.

In mid-August, the CWT committee voted to allocate 80% of its 2004-05 funds to the Herd Retirement Program and 20% of its funds to the Export Assistance Program. The committee also plans to utilize money left over from the previous year.

Just how big is the CWT budget? According to an earlier press release, dairy farmers that produced approximately

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KEN'S CORNER



*by Ken Meyers
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The CWT program was originally intended to be a self-help, safety net program

to boost milk prices to dairy farmers. It appears that the next round of herd reduction is just around the corner. Some argue that

the CWT committee should wait until prices are really low before pulling the trigger. Others claim that the program should be implemented to prevent milk and dairy product prices from falling too low.

The long-term viability of the CWT program will be tested when and if dairy product prices (cheese and butter) fall below \$1.20 per pound. Will CWT be able to decrease the nation's milk herd by enough cows to reduce milk

marketings quickly enough to enhance farm milk prices? Will there be a home on the world market for the surplus cheese and butter? Will there be support to increase the nickel assessment to meet program goals? These are questions that the program has yet to answer because dairy product prices have been above the historical average since the program was implemented. **MCT**

Stocks in Place

The latest Cold Storage report pegged commercial stocks of American cheese at 614.5 million pounds. Passing the 600 million pound mark served the cheese market a corrective blow. For the most part, milk and dairy product demand and supply appear to be in balance as the industry enters its seasonally high-demand

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
Aug	1.5733	1.5444	14.03	1.5406	12.42
Sept	1.5750	1.5450	14.60	1.6400	12.40
Oct	1.5375	1.5075	14.45	1.5900	12.40
Nov	1.4400	1.4100	13.65	1.5300	12.00
Dec	1.3800	1.3500	13.00	1.3800	11.50
Jan	1.3575	1.3275	12.40	1.3100	10.95

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

period. And consumers are likely to see lower prices during the second half of 2004, which should boost demand. **MCT**

the cows..

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68% of U.S. milk production are contributing a nickel per hundredweight to the program. With U.S. milk production near 172 billion pounds that yields revenue of nearly \$58.5 million for the program. Based upon the 80% budget allocation for the herd reduction program, CWT has nearly \$46 million to remove cows from the U.S. dairy herd.

How many cows will \$46 million buy? The best-case scenario is that the CWT program buys the cows at the \$850 per head price tag like it did last year. At that price, CWT can remove 55,000 head, or 0.6% of the current dairy herd.

Given that milk and dairy product prices remain

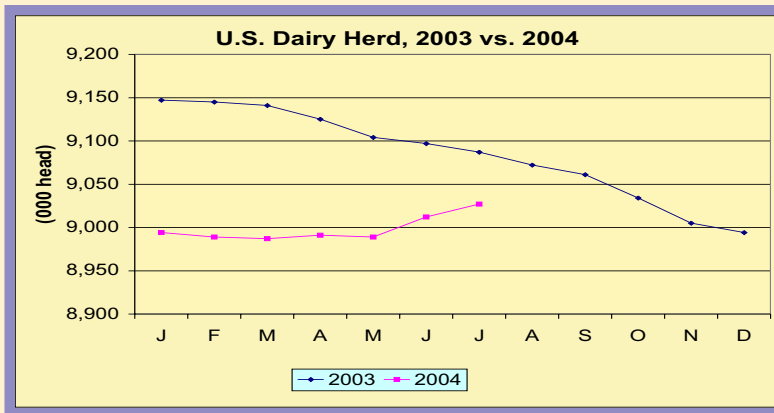
above historical averages, one might ask why kill the cows now? The simple answer is that cow numbers are rising.

The chart below illustrates that the dairy herd was on a downward slide all during 2003. Cow numbers bottomed out at 8,987,000 head in March 2004. In June, the herd was back above 9,000,000 head and growing.

By the fourth quarter of 2004, the U.S. dairy herd is expected to

be even with a year ago (see chart). As the number of dairy cows increases, so does milk production. In addition, dairy producers across the United States indicate that this summer's exceptionally cool weather resulted in higher conception rates. This is likely to translate into an earlier flush in 2005.

The combination of a growing dairy herd and a bumper corn crop usually means cheap milk. Just as the perfect storm for high milk prices developed in 2004, the same perfect storm for lower prices is forming in 2005: more cows, more calves, more corn and more milk. **MCT**



Cow numbers have bottomed out and are poised to match last year's levels. Source: USDA.

