



MCT COMPASS

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Has CWT Met its Match?

The cooperative's Working Together (CWT) program was credited, in part, with ridding the market of surplus milk production in 2004, but since March of this year, monthly milk production has been running 2.7% to 5.2% higher than year-earlier output. Year to date, production is up nearly 3%. Not only has milk per cow held strong despite higher input costs and sweltering heat and humidity, but producers have been adding cows as well. Whether CWT's third buyout program will remove enough milk to sustain 2006 milk prices is today's \$64,000 question.

Before we take a stab at answering that question, however, let's look at the recent milk

production report. Total U.S. output in July, compared with a year ago, was up a robust 3.9%. However, July's heat and humidity tempered the actual milk solids contained in the milk. USDA estimates that the butterfat content averaged 3.53% in July 2005 vs. 3.57% in July 2004. Adjusted for butterfat composition, the milk production gain was closer to 2.8%. Protein tests are expected to have suffered a similar decline.

Reported numbers in July show that milk production per cow rose 3.6% to 1,682 lbs. The per cow increase was much larger than the average trend gain of about 2%. Since March, cow numbers have been above year-earlier levels and the gap has grown larger each month (see chart, page 2).

Together, producers in the 23 states tracked monthly by USDA milked 48,000 more cows than a year ago.

With summer nearly behind us, milk prices still relatively strong, and the replacement herd recovering, analysts are beginning to wonder what, if anything, will stop the rush to fill both old and new barns. A shortage of hay could certainly cut into milk yields and cow numbers if the feedstuff becomes too pricey as could CWT. Yet the strategy of adding cows to capitalize on strong milk prices has gained momentum and it is questionable whether CWT will be able to curtail output enough in 2006 to support block cheese prices near \$1.40/lb.

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KEN'S CORNER



*by Ken Meyers
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CWT's two herd buyouts have gone a long way toward supporting milk and cheese prices since the program's inception in 2003. However, CWT is not nearly big enough to stem the

onslaught of dairy farm expansions brought on by several years of strong milk prices. An expanding milk herd, coupled with above average increases in per cow output, can mean only one thing: cheese manufacturers will be busy in 2006.

That said, a market crash is not in the 2006 forecast, either. Class

III milk prices will still average close to \$12.50/cwt. next year. While that may seem low compared with 2004's \$15.39 and this year's projected average price of \$13.85, historically, \$12.50/cwt. is a price that allows efficient producers and skilled cheese makers to prosper. **MCT**

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Fall Supply Ample

The dynamic demand combination of exports and strong domestic commercial disappearance continues to soak-up additional milk supplies from the industry's evermore productive and growing population of dairy cows. As the milk continues to flow, dairy product prices are expected to trade within a seasonal trading pattern. We think there is still some price upside ahead, but with ample milk supplies

| MCT Forecast | | | | | |
|--------------|--------|---------|-----------|---------|----------|
| | Block* | Barrel* | Class III | Butter* | Class IV |
| Aug | 1.4269 | 1.4222 | 13.58 | 1.6925 | 13.31 |
| Sep | 1.5300 | 1.5050 | 14.25 | 1.7000 | 13.60 |
| Oct | 1.5025 | 1.4700 | 14.70 | 1.7250 | 13.65 |
| Nov | 1.4450 | 1.4225 | 13.75 | 1.6350 | 13.30 |
| Dec | 1.4000 | 1.3700 | 13.25 | 1.5075 | 12.65 |
| Jan | 1.3800 | 1.3400 | 12.90 | 1.4625 | 12.25 |

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

in the forecast, we don't foresee any type of price run-up reminiscent of

last November's 40-cent price leap to \$1.9525/lb. for block cheese. **MCT**

Will it or Won't it?...

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Since the program's inception in July 2003, CWT has removed more than 83,000 cows in two separate buyouts. Program managers estimate that CWT buyouts were responsible for removing 1.6 billion pounds of milk from the market. On Aug. 10, CWT announced a third buyout program that will cull 70,000 cows from the nation's dairy herd. The program's goal is to reduce future milk output by 1.9 billion pounds over an 18-month period beginning in September.

We asked six analysts whether CWT would succeed in removing the surplus milk from the market in 2006. While the program will most certainly take the edge off the surplus, all six said the string of high milk prices, which has given producers a strong incentive to expand, will outweigh the buyout.

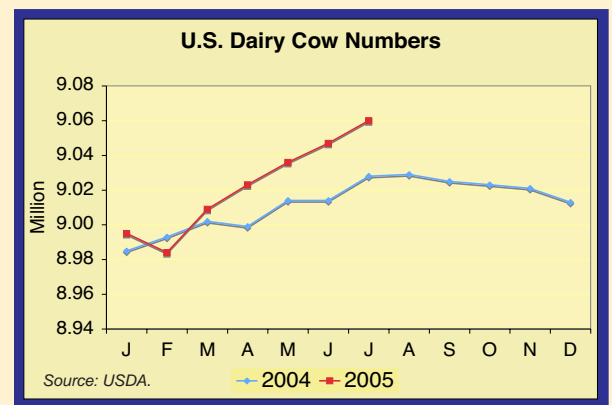
"The 70,000 cows in Round III equals less than 1% of the cow herd and a little more than one week's normal dairy cow slaughter, which can easily be offset by expansions and improved milk per cow," says economist Bob Cropp, University of Wisconsin. "

CWT's estimate that culling 70,000 cows from the market will remove 1.9 billion pounds of milk is probably high. "If you factor in some 'air,' producers that would have gone out of business anyway as well as the likelihood that the majority of these cows are less-than-average specimens, we are probably talking about an impact of closer to 0.5%," says Mark Stephenson, economist with Cornell University.

Over the past 24 months, the Class III milk price averaged \$14.67, says analyst Al Levitt, with Levitt Communications. In that time, he says, California, Idaho, New Mexico and Arizona producers added 142,000 cows above and beyond those culled due to CWT. He expects expansion in the West to continue through 2006.

CWT has given producers who have wanted to exit the industry an out, says economist Wilson Gray, University of Idaho. "But it has also been a good place to dump cows," he notes, and that has little impact on total output and cow numbers

Expansion is not a light switch



that can be turned on or off at will, says Mary Ledman of Keough Ledman & Associates. No doubt, a CWT buyout will remove milk from the market, but it will take several months of lower milk prices or much higher input costs to significantly cut into cow numbers, she says.

Any impact from CWT will be minimal, agrees eDairy Inc.'s Bill Brooks, who expects weather, both here and in key production regions worldwide, to play a much larger role in dairy product prices next year.

U.S. producers appear to have beat this summer's oppressive heat. Their next challenge will be dealing with higher feed costs. If they make it through that, cow numbers will stay strong until lower prices weed out the marginal herds. **MCT**

