



MCT COMPASS

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Gauging Demand

It is common knowledge that milk and dairy product prices are a function of supply and demand. Information on the supply side of the equation is deep and detailed. USDA collects monthly milk production data in 23 states and quarterly production for all 50 states. On the dairy products side, output data for nearly 50 different types of dairy products are published monthly by USDA.

Unfortunately, the information on the demand side of the equation tends to be shallow and vague. USDA's primary indicator of demand is its calculation of commercial disappearance. Yet USDA does not actually collect sales data to derive commercial disappearance, but rather backs into

the number. USDA first calculates supply by adding commercial stocks to the current month's production plus imports. From that number, USDA then subtracts ending commercial stocks and net government removals to derive commercial disappearance.

USDA recognizes that its estimate of commercial demand is just that, an estimate. It couches the number with the following footnote: *"Disappearance is a residual figure and therefore can be affected by any inaccuracies in estimating milk production, on-farm use, stocks and imports."*

In other words, estimating commercial disappearance, or demand, for milk and dairy products is not an exact science. All the data points obtained by USDA are voluntarily submitted. For example, dairy

producers are not required by law to participate in the production survey. Dairy processors are not required by law to report their monthly output. And commercial warehouses are not mandated to submit the volume of dairy products held within their facilities.

As a result, the base for deriving dairy product demand appears to be built on a weak foundation. Any crack in that foundation, such as a large correction in any of the data points, can and does lead to marketplace turmoil.

Another factor contributing to the industry's inability to track demand is the timeliness of USDA's report. Commercial disappearance of milk and dairy

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KEN'S CORNER



*by Ken Meyers
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The dairy industry needs to refine its tool box for determining demand. One key question comes to

mind: whose responsibility is it to provide this information? Often where there is demand someone offers the supply. Commercial sources of milk

and dairy product demand do exist; however, they typically represent only certain segments and not the aggregate.

The most comprehensive dairy demand data comes from USDA. It has the systems and non-biased analysts in place to collect, analyze, and publish production, inventory and even price data.

Granted, information from USDA's reports would serve the

industry better if they were published on a timelier basis. Many release dates for USDA reports have not been changed despite advances in electronic data movement. More timely release dates followed by greater industry cooperation in supplying reliable timely data to USDA are just a few refinements that would improve dairy product demand information. **MCT**

Hmmmm

It's a head scratcher. Dairy product prices are softening just as the industry enters its peak demand season. Through most of 2005, dairy product prices have remained strong in the face of heavy milk production. The question is whether seasonal demand can be met by current cheese production. Typically, it isn't, but in light of ever-increasing milk production and

MCT Forecast					
	Block*	Barrel*	Class III	Butter*	Class IV
Oct	1.4470	1.3961	14.37	1.6204	13.62
Nov	1.4150	1.3750	13.55	1.5775	13.40
Dec	1.3900	1.3575	13.35	1.5175	13.10
Jan	1.3800	1.3475	13.00	1.4150	12.55
Feb	1.3500	1.3200	12.80	1.4225	12.30
Mar	1.3300	1.3000	12.45	1.4575	12.40

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

additional cheese manufacturing capacity, it could. Both American cheese and butter stocks are

modestly below last year's levels and will provide an adequate market buffer. **MCT**

Making sense of it...

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products is reported almost two months after the fact. For example, commercial disappearance for milk and dairy products during August was published in the Oct. 28 issue of USDA's *Dairy Market News*. In that report, USDA indicated that commercial disappearance from January through August 2005 for American cheese was up 1.2%; "other cheese" was up 3.9%; nonfat dry milk was up 1.5%; butter was up 0.2%; and fluid milk products were unchanged. While these numbers are positive, only the "other cheese" category posted a greater increase in commercial disappearance than the 3.5% increase in milk production during the same period.

Along with the *Milk Production*, *Dairy Products*, and *Cold Storage* reports, USDA relies on actual fluid milk product sales in the federal milk marketing order areas and California to determine commercial disappearance of fluid milk products.

Over the years, there has been discussion on whether actual sales data for non-fluid dairy products could also be collected through the federal milk marketing orders. However, even if this were allowed, it would only account for milk and dairy products converted from about 60% of the U.S. milk production.

What else is out there?

Another source of demand information can be found in industry publications that periodically publish category reviews with scanner data from Information Resources, Inc. (IRI). IRI provides retail sales comparisons and is an indicator of what is happening in the retail market; however, it does not include any data from the largest U.S. retailer, Wal-Mart.

IRI data through Aug. 7, 2005 indicate that the retail natural cheese category was up 6.1% in sales dollars and up 1.4% in sales units vs. a year ago. The natural shredded cheese category also posted positive gains of 4.7% in sales and 2.9% in units.

The food service and food

ingredient part of the puzzle is more difficult to piece together and likely represents more than 60% of the demand for cheese, butter and dairy powders.

Industry publications for the restaurant and food service sectors may be the best source of public information regarding the growth status of that sector. For example, if same store sales are up or down significantly, we may be able to extrapolate the directional change to dairy demand as well.

Putting the pieces together

After reviewing supply data, commercial disappearance, retail and food service reports, we can glance at the Census Bureau's Consumer Price Index and the Confidence Board's Consumer Confidence Index. The Consumer Price Index indicates whether dairy products are a good value and the Consumer Confidence Index provides a glimpse into whether consumers are likely to spend or pinch pennies. Both can be valuable tools in predicting near-term demand. **MCT**

