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MCT COMPASS

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Experts Predict High Prices to be Sustained

Last year at this time, NASS prices for nonfat dry milk were over $2.01/lb., whey prices were close to 73 cents, and the U.S. economy was still growing at a fairly strong rate of more than 4%. My how things change. The economy is now teetering on recession, nonfat dry milk (NFDM) prices have dropped by 30% and whey prices of about 23 cents per pound are roughly 25% of last year's value. Yet milk prices are still close to last year's levels.

Why? Strong cheese exports and lower domestic cheese production due to today's high-cost of inputs, particularly energy costs. Like manufacturers in many other industries, cheese makers have moved to a just-in-time inventory model. The general overall commodities boom has also given dairy product prices a psychological boost. And increased demand from China as well as a continuation of tight world supplies of dairy products have all helped buoy the U.S. dairy market.

To get a sense of where markets might go from here, *MCT Compass* once again collected midyear forecasts from six of the nation's top dairy analysts: Bill Brooks, e-Dairy Inc.; Bob Cropp, University of Wisconsin; Wilson Gray, University of Idaho; Mary Ledman, Keough Ledman Associates; Alan Levitt, Levitt Communications; and Mark Stephenson, Cornell University. Their forecasts were then added to futures prices for July 23, when applicable, and merged into a consensus forecast.

Five of the six economists believe that the U.S. dairy industry has reached a new higher sustainable price level. They reason that higher energy costs and strong exports will support dairy prices long term. "We are now a major player in world dairy markets and this has happened in a couple of short years," says one of our experts. The group's average Class III price for the remainder of 2008 is $18.66. The most bullish of the six analysts expects the Class III price to hit $19.99 in October. Looking ahead, the consensus forecast for 2009 is nearly as strong with a projected Class III average of $18.51. The 2009 average Class III price predictions range from $17.27 to $19.56. The analysts' forecasts for the average NASS cheese price for 2009 range between $1.82 and $2.05.

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KEN'S CORNER

by Ken Meyers
President
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Another year has passed and milk prices are still at historically high levels. Oceania's output has not recovered fully, and demand from China and other Asian countries continues unabated. At the same time, though, the world economy is toying with recession, consumers worldwide have been pinched by high food and energy costs, and commodity prices, in general, have reached bubble levels.

So what can one do when trying to develop a strategic plan for the remainder of this year and next? We turned to our trusted panel of economists as we do each year at this time to get a second-half 2008 and 2009 forecast. Their forecasts are, one might say, reassuring. No one is predicting a sharp drop in prices this year or next, and interestingly, no one expects major volatility. Their range of forecasts is also surprisingly narrow.

Our panel of economists expects the United States dairy industry to continue to hold onto its share of the world market in 2009. They also expect U.S. milk production to continue to give us enough milk so that we can continue to feed global markets.

One can't help but think, however, that the big wild card is the value of the U.S. dollar. If the dollar strengthens substantially, it will be interesting to see whether the loyalty of some of our new found customers remains intact, and how our competitors react. MCT

A true consensus..

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Our panel of experts expects Class IV prices, while strengthening from current levels, to remain substantially below Class III. Their average forecast places the July through December Class IV price at $17.06, and the range in their forecasts is fairly narrow, between $16.73 and $17.28. The group expects both butter and nonfat dry milk prices to slowly build through the fall before dropping back only slightly. The consensus forecast for the second half 2008 NASS butter price is slightly over $1.52, and for NFDM, $1.44. Next year, the consensus calls for an average NFDM price of $1.44 as well, with the most pessimistic of the group calling for an average price near $1.38 and the most optimistic looking for an average near $1.49.

"Milk production growth will slow in the second half of 2008 and into 2009, which will tighten supplies of butter and powder, but it won't have an effect on cheese," says one panelist. "With continued strong global demand for butter and powder, those markets will remain firm through the end of 2009."

The impact of this year's farm bill, however, will be minimal. "Two negatives of the bill are continuing the DEIP program when it is no longer needed and the assessment on imports," another says. "The import assessment could lead to retaliatory measures on our increasing export market or dairy importers using the assessment to promote their products here." MCT

Consensus Forecast

	Cheese	Class III	Butter	Class IV	Whey*	NFDM
July	1.9461	18.01	1.5073	16.65	23.41	1.40
Aug	1.9798	18.64	1.5117	16.91	28.08	1.42
Sept	2.0060	18.94	1.5169	17.12	28.79	1.44
Oct	1.9865	18.82	1.5344	17.28	29.45	1.46
Nov	2.0122	18.99	1.5485	17.28	29.88	1.46
Dec	1.9681	18.61	1.5229	17.09	29.78	1.45
Avg	1.9831	18.66	1.5236	17.06	28.07	1.44
2009	1.8206	18.51	1.4685	17.42	32.91	1.44

* Whey in cents

What the experts are saying...

Bill Brooks: "I'm not ready to say that the industry has entered a new world dairy market with higher price levels that are sustainable for the long term, at least not yet. There is still a huge potential for increasing milk production in the world and that could push prices back down toward historical levels at some point in the future."

Bob Cropp: "Feed prices will stay relatively high for the foreseeable future, which means we have built in a higher milk production cost—$2.00 to $3.00 higher. Thus, higher milk prices are necessary to produce enough milk for market needs. Commercial dairy exports will also help support prices at a higher level."

Wilson Gray: "Dairy producers will face tight margins as input costs continue to rise. Market volatility for inputs and production will be a major risk factor—$20 milk doesn't mean that risk is now gone. It may be more problematic over the next 12 to 24 months."

Mary Ledman: "A looming issue for the industry is the recent outbreak of TB in California. One of the infected California herds is a large, seller of breeding stock. Several dairy producers have been contacted and requested to have their herds tested. Understanding how this outbreak occurred, tracking potential carriers, and the ultimate eradication of infected herds could result in public policy decisions/requirements regarding bio-security."

Alan Levitt: "Structural changes have taken place in the global agri-food complex, primarily higher energy costs and growing demand in developing countries, which will keep prices generally higher for the foreseeable future. There may be times when prices cycle back down to historical levels, but I believe, in general, higher price levels are here to stay."

Mark Stephenson: "Over the past year, energy has been the big rock in the pond that has created ripples throughout the dairy industry. Ethanol production has had a tremendous impact on feed prices, and high energy costs for consumers have even been implicated in the collapse of housing markets, which has caused changes in food purchases and out-of-home eating."

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