

They're Off

While the dog days of summer are looming in the Northern Hemisphere and milk production is seasonally declining, Oceania is ramping up for its new season of milk production. In some years, fresh product out of the Southern Hemisphere offsets



In some years, fresh product out of the Southern Hemisphere offsets decreasing output from the Northern Hemisphere, capping prices.

decreasing output from the Northern Hemisphere, capping prices. That is unlikely to occur this year because both hemispheres are expected to post lower year-over-year (YOY) milk output.

Oceania's Australia and New Zealand account for nearly 2% and 4.4% of global milk production, respectively, according to USDA. Despite their small stature in terms of production, both command a greater presence in the export market. In 2015, Australia ranked fourth or fifth in butter, cheese, whole milk powder (WMP), and skim milk powder (SMP) exports. New Zealand dominated the WMP and butter trade, accounting for 66% and 60% of 2015 WMP and butter exports, respectively. New Zealand was a distant second in cheese exports, following the European Union, and ranked third in skim milk powder (SMP) trade, following the European Union and the

United States.

Australia is reeling from a management decision that likely resulted in greater milk output in the 2015-16 season but that will contribute to lower milk production in the upcoming season. Australian milk output for July 2016 was 10.3% (153 million pounds) lower than last year. YOY milk output was down in four out of the country's five milk-producing regions. Output in Victoria, the largest milk-producing state in Australia accounting for nearly two-thirds of the continent's production, was off 11.2%.

The Australian dairy sector is in turmoil due to the country's largest milk buyer, Murray Goulburn, paying

producers more for their milk in the 2015-16 season than the dairy cooperative could afford as dairy product prices continued to weaken throughout the production season. In April 2016, the cooperative announced it would struggle to meet even half of the net profit forecast outlined in its prospectus less than a year ago. ASX shares in Murray Goulburn fell 42% in a single day. Since then, the stock

Continued on page 2

Ken's Corner



*by Ken Meyers
President, MCT Dairies Inc.*

Given New Zealand's dominant position in the global WMP and butter markets, the possibility of a 3% YOY decrease in milk production following last season's 2% decline was enough to propel the latest Global Dairy Trade (GDT) WMP and butter markets 18.9% and 14.1%, respectively, above the prior

bimonthly auction.

The GDT WMP index of \$2,695/ton is the highest since Oct. 15, when the market was on the cusp of a multi-month decline. The current WMP index represents the third consecutive auction gain.

Could this latest market trend replicate the 2012 GDT WMP market? At that time, the WMP index averaged \$2,870/ton on Aug. 12 and moved higher into mid-October, topping at \$3,421, only to slide into the \$3,100 range until mid-January 2013. The WMP index continued to increase, surpassing \$4,500 in March 2013, and remained above this level for the next 12 months.

A lot has changed in global dairy markets since 2012. There is greater plant capacity and more opportunities to move milk into the highest-value proposition. As a result, milk powder markets are bouncing off their lows and moving the entire dairy pricing complex higher—proving once again that the cure for low prices is low prices. However, it's yet to be seen just how large the recovery will be and how long it will last. **MCT**

Record Stocks and Weak Lifeline

Ample cheese and butter stocks are weighing on CME cash markets, while rising global milk powder prices are buoying the domestic nonfat dry milk powder

market. USDA's latest Cold Storage report shows month-ending July cheese stocks at a record high and butter stocks at their highest level since January

1993, when the government was acquiring stocks. The cheese market rallied in July after the National Milk Producers Federation asked USDA to buy up to \$150 million in surplus cheese, but retreated when USDA offered the industry a modest \$22-million lifeline to buy 11 million pounds of cheese from private stocks to assist food banks and pantries across the United States. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Aug	1.7826	1.8110	16.90	2.1780	14.65	0.2850	0.8595
Sep	1.6850	1.6250	16.65	2.1550	14.55	0.3055	0.9000
Oct	1.7150	1.6350	16.15	2.2250	15.75	0.3150	1.0000
Nov	1.7000	1.6250	16.25	2.1500	16.15	0.3250	1.0625
Dec	1.6950	1.6250	16.15	2.0000	16.10	0.3375	1.1250
Jan	1.6850	1.6500	16.20	1.8750	15.90	0.3500	1.1650

* CME prices.

**NASS prices.

...payback time

continued from page 1

has fallen below \$1(AUS). Murray Goulburn also informed nearly 2,500 dairy farmers that they owed the cooperative an estimated \$200 million (AUS), which is equal to \$151 million (U.S.). Murray Goulburn's CEO and CFO were terminated due to the overly optimistic 2015-16 milk price forecasts and payouts. The cooperative has lowered its price forecast for the 2016-17 season and other Australian milk buyers have followed suit. The situation is so heated that Australia's prime minister and his deputy sought a meeting to seek an explanation from the cooperative's existing key management. The net result is double-digits lower YOY milk production as dairy producers increase culling in an effort to create more cash flow. Initial estimates peg Australian milk production for the 2016-17 season at 1% below last season, following the 2% YOY decrease in 2015-16.

Amid an outlook suggesting tighter margins, and in some cases negative margins, the current season's milk production will depend heavily on seasonal conditions. More favorable weather conditions have improved pastures and reduced the

need for supplemental hay purchases. Nevertheless, lower YOY milk production is forecast for Australia.

New Zealand dairy producers learned early in the 2015-16 season that they faced a challenging year financially. In addition, the largest dairy-exporting country braced itself for potential negative impacts from a strong El Niño. In the end, large negative margins took their toll on the industry. New Zealand milk production declined 2% in 2015-16 to 47.4 billion pounds. Fonterra, the country's largest dairy cooperative and milk buyer, forecasts that 2016-17 output will fall 3%. Fonterra's July milk intake trailed last year's by 1.4%.

According to USDA's Foreign Agriculture Service, the New Zealand dairy herd has shrunk by more than 170,000 head, which will drive much of the YOY contraction in milk production. However, New Zealand pastures are in good condition, and recent gains in global dairy product prices could push milk output above Fonterra's current estimates but not enough to offset the expected decline in Australian milk production. **MCT**



The information contained in this newsletter is for general guidance only. It is not intended to constitute or substitute investment, consulting or other professional advice or services. The information presented is not an offer to buy or sell commodities. Compass accumulates then distributes opinions, comments and information from and based upon other public and reliable sources, but it cannot warrant or guarantee the accuracy of any of the data included in the newsletter. From time to time MCT Dairies, Inc. may hold futures positions in commodities discussed in the newsletter. Always contact a registered financial advisor before making any decisions. MCT Dairies, Inc. shall not be held liable for any improper or incorrect use of the information contained in the Compass or for any decision made or action taken in reliance on the information in this newsletter. Reproduction with permission only. **MCT Dairies, Inc., 15 Bleeker St., Millburn, NJ 07041 (973) 258-9600 fax: (973) 258-9222 www.mctdairies.com.** For more information, email info@mctdairies.com.