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MCTCOMPASS

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Producer Margins Have Bottomed

On-farm margins—the milk price minus feed costs as derived from the Margin Protection Program (MPP) calculation—started the year at an optimistic $11.06/cwt. That means dairy producers, after settling their feed bills, had an average of $11.06/cwt. of milk left over to cover other costs and add to savings. According to this formula, national average dairy profit margins in January were higher than in any month since October 2014. However, sustained year-over-year gains in milk production, dairy product output, and stocks have taken their toll on domestic milk prices.

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The national average All-Milk price peaked at $18.90/cwt. in January 2017 and then incrementally declined each month to hit $16.50 in April, recovering slightly in May to $16.70, according to USDA's recently released Agricultural Prices report. Feed costs have not changed appreciably since January. National average prices for corn and alfalfa have moved up a little, while soybean meal prices have retreated. In total, MPP feed costs have increased 13 cents per hundredweight since the beginning of the year. In contrast, the national average All-Milk price has dropped by $2.20 from January to May, and the corresponding national average MPP margin eroded to $8.61 in May.

Dairy producers have the opportunity each year to sign up for the federally sponsored MPP program, which offers: 1) catastrophic bimonthly coverage at $4/cwt. at no cost to the producer, other than an annual $100 administrative fee; and (2) various levels of bimonthly buy-up coverage. Producers can purchase buy-up coverage that provides payments when bimonthly margins are between $4 and $8/cwt. Dairy producers receive payments when the national average MPP margin is less than their selected coverage level. The last time the bimonthly MPP margin fell below $8/cwt. was for the May-June 2016 period. With the May 2017 MPP margin standing at $8.61, the June MPP margin would have to fall by more than $1.20 to trigger a payment to producers who elected the highest coverage level of $8/cwt.

Regional margins vary significantly. For example,

Continued on page 2

Ken's Corner

by Ken Meyers
President, MCT Dairies Inc.

On average, U.S. producers started the year with the highest on-farm margins since 2014, but they watched those margins slowly erode over the first five months of 2017. The tide appears to have turned. Margins should improve barring adverse weather during crop pollination and/or harvest or an unexpected milk price decline.

With the national milking herd at a 20-year high and ample heifers standing in line to join the herd, the U.S. milk supply should continue to flow freely. That should be good for producers—particularly in states where margins are expected to be the highest—as long as there are ready markets for their milk, and it appears there will be.

It seems U.S. consumers can never get enough butter, yogurt, pizza, nachos, and ice cream. Imports of dairy products have also picked up in China, one of the world's largest importers of dairy products, just when the milk production season is winding down in Oceania and European output growth continues to be sluggish.

While U.S. milk prices and on-farm margins should continue to improve this summer and early fall, ample world stocks of cheese and skim milk powder will put the brakes on excessive price acceleration. **MCT**

EU Butter Imports Unlikely

Rising production and growing stocks contributed to eroding prices for cheese, nonfat dry milk, and whey in June. American cheese stocks grew by 1.6% in May to 847 million pounds, up 11.8% or 89.5 million pounds compared to last year. Domestic butter stocks rose by 7.3% in May to 313.6 million pounds but remain 3.5%, or 11.4 million pounds, shy of last year's level. U.S. butter prices near $2.65/lb. are on par with Oceania prices but below European butter prices, which are trading above $3/lb. Over the past two years, but particularly in 2016, the United States imported lower-priced European butterfat to supplement domestic demand. That is unlikely to be an option this year. **MCT**.

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Jun	1.6025	1.3970	16.44	2.5700	15.89	0.4917	0.9137
Jul	1.5700	1.4300	15.40	2.6700	16.85	0.4640	0.9150
Aug	1.7000	1.5300	16.10	2.6700	17.00	0.4550	0.9200
Sep	1.7500	1.5800	16.95	2.6500	17.15	0.4500	0.9350
Oct	1.8300	1.6300	17.35	2.5500	16.65	0.4475	0.9450
Nov	1.8000	1.6000	17.50	2.4200	16.05	0.4500	0.9600

** CME prices.*
***NASS prices.*

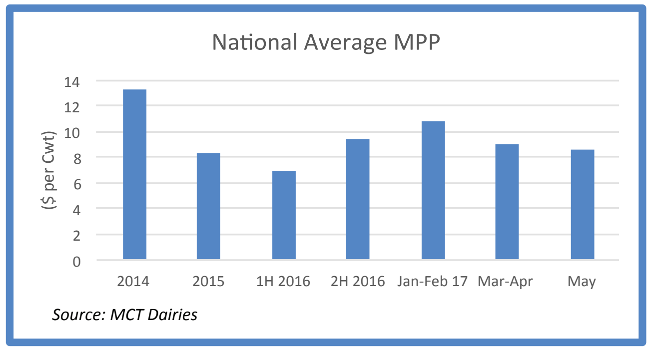
...better margins ahead

continued from page 1

May 2017 margins in California averaged $7.43/cwt. compared to Wisconsin's $9.89/cwt. The chasm between California and Wisconsin margins is due to lower milk prices and higher feed costs in California compared to those in Wisconsin. The May All-Milk price in California averaged $15.86 compared to $17.40 in Wisconsin. California producers shelled out $180/ton for alfalfa hay, while Wisconsin producers paid $120/ton in May.

Generally, returns in states with greater processing capacity fare better than returns in states where milk has to travel great distances to find processing capacity—typically milk powder plants. For example, New Mexico reported the lowest All-Milk price in May of $15/cwt., followed closely by Michigan at $15.30 and Kansas at $15.40. In addition, dairy producers milking higher butterfat-producing cows are experiencing more favorable margins due to escalating butter prices. South Dakota milk with an average of 4.04% butterfat in May sold for an average $18.20/cwt., outpacing the national average All-Milk price by $1.50 and the national average butterfat content of 3.76%.

Using the same MPP calculations, upcoming margin prospects for the second half of 2017 look favorable as seasonally higher butter and cheese prices are expected to offset lower nonfat dry milk and whey prices than experienced during the first six months of the year. The average Class III price for second-half 2016 and first-half 2017 showed little variation at $16.25 and $16.05, respectively. Likewise, current futures prices are predicting an average Class III price near $16.50 for the second half of this year. While the outlook for milk prices, supported by higher-than-average butter prices, appears rosy, higher feed costs could threaten on-farm margins. Much of the U.S. corn crop is expected to pollinate up to two weeks later than last year, which puts this year's crop at greater risk for heat stress during the critical pollination period. **MCT**



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