

Tariffs Create Uncertainty

A year ago, leading U.S. dairy economists were talking about a complacent dairy market in a state of equilibrium. “There is little on the horizon that would appear to have much impact on supply and demand for dairy products over the next 12 months,” said



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one. But then the unexpected occurred. China, Mexico, and Canada placed retaliatory tariffs on U.S. imports including some dairy products after President Donald Trump singlehandedly placed tariffs on imports from China, Canada, Mexico, and the European Union, causing great uncertainty for U.S. dairy exporters. While last summer, the future looked upbeat for dairy producers, markets now appear tenuous for a number of reasons.

The proposed House and Senate versions of the 2018 farm bill are also advancing. The bills include two notable proposals worth watching. The House bill increases work requirements

for recipients of the Supplemental Nutrition Assistance Program (SNAP), and both the House and Senate versions of the bill contain a provision to remove the “higher of” from the Class I calculation, which could help slow declines in fluid milk consumption by providing a way for bottlers to stabilize prices to consumer.

To get a sense of where markets might go from here, *MCT Compass* collected midyear forecasts from four of the nation’s top dairy economists: Bill Brooks, INTL FCStone; Bob Cropp, University of Wisconsin; Sara Dorland, managing partner at Ceres Dairy Risk Management and analyst with the *Daily Dairy Report*; and Mark Stephenson, University of Wisconsin. We then added their forecasts to CME futures settlement prices for July 24, 2018, to create a consensus forecast.

Our panel’s average Class III price for second-half 2018 is \$15.44/cwt., and the group expects the Class III price next year to average \$16.01. The most bullish of the

analysts expects a 2019 Class III average of \$16.20, while the most bearish anticipates a 2019 average of \$15.79. The analysts’ forecasts for the average NASS cheese price for the next six months range from \$1.58 to just over \$1.61/lb., and their average 2019 cheese price forecasts range from just under \$1.65 to \$1.68/lb. The consensus on the average 2019 whey prices is 35.38 cents per pound.

As for Class IV, the consensus forecast for the

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Ken’s Corner



by Ken Meyers
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What a difference a year makes. The current market situation is probably more uncertain that it ever has been since I entered the industry more than three decades ago. While USDA’s \$12 billion aid package for farmers, who are being hurt by the tariffs, is an indication that we can expect the trade disputes to persist for some time, the deal the United States is currently negotiating with the European Union regarding tariffs could portend more compromise with our other trading partners.

If the trade battles persist, cheese is likely to be hit hardest by the tariffs. Current price levels indicate that the whey and milk powder markets will be less affected than cheese because exporters have more alternative markets for whey and NDM.

As our panelists note, Europe and New Zealand will likely try to make inroads into both the Chinese and Mexican markets, dislodging U.S. market share for cheese. Changes in an existing agreement between Europe and Mexico and a new agreement between New Zealand and China could make it harder for the United States to recover lost cheese sales into these markets long term. That would be a shame given the decades of work the U.S. dairy industry has invested in developing these foreign markets. **MCT**

...low returns to persist

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second-half 2018 average is \$14.70, or 74 cents lower than Class III. In 2019, the panel anticipates an average Class IV price of \$15.32. For second-half 2018, the group expects a nonfat dry milk (NDM) price near 82 cents per pound, rising to 87 cents next year. The average butter price forecast drops from \$2.32 for second-half 2018 to near \$2.28 next year.

Besides the uncertainties mentioned earlier, analysts will also be watching weather, farm finances, and world economies, but their biggest concern is trade. "The United States is struggling to renegotiate existing trade agreements much less contemplate new ones," one analyst says. "The protectionist perspective is keeping the United States on the sidelines and allowing Europe and Oceania to strike deals that will impact trade flow for the next decade."

That uncertainty is amplified by farm finances. "Producers in Oceania and Europe are feeling as though they are crawling out from under our last milk price trough and are feeling better about their prospects in the year ahead," says another leading expert. "The same can't be said for U.S. dairy producers who are either making plans for another year of low or negative returns, or are considering liquidation of their assets." **MCT**

Consensus Forecast						
	Cheese	Class III	Butter	Class IV	Whey	NFDM
July	1.4873	14.19	2.26	14.09	0.35	0.78
Aug	1.5447	14.83	2.31	14.42	0.36	0.80
Sept	1.6065	15.49	2.34	14.76	0.37	0.82
Oct	1.6609	16.02	2.37	15.01	0.37	0.84
Nov	1.6761	16.71	2.35	15.00	0.37	0.84
Dec	1.6585	15.96	2.32	14.92	0.37	0.85
2H 2018 Avg	1.6056	15.44	2.32	14.70	0.37	0.82
2019 Avg	1.6641	16.01	2.28	15.32	0.35	0.87

What the experts say...

Bill Brooks: From a historical perspective, the current economic expansion has lasted a long time and would seem to be primed to reverse course soon. That said, the slow growth pattern has probably helped with longevity. There were some economic warning signs from some parts of the world before the implementation of tariffs, and if the tariff situation escalates, we could see economic problems within the next 12 months. For demand, the risk is a stronger economic slowdown in developing countries that import a large quantity of dairy products.

Bob Cropp: Over the past 12 months, the growing economy has improved the Consumer Confidence Index and the Restaurant Performance Index. This has been positive for cheese and butter, while fluid (beverage) milk continues to decline. Through May, dairy exports have been well above year-ago levels, with April setting a new record equivalent of 18.8% of U.S. milk production. Looking ahead, low milk prices will likely result in a decline in cow numbers and dampen increases in milk per cow. How low milk prices go will be affected by how the trade war plays out.

Sara Dorland: Some analysts are concerned the increase in interest rates, assuming \$5,000 in average U.S. household debt on credit cards, could erase the positive impact of the recent tax reductions as soon as the end of next year. Real wages are increasing as employers work to retain and recruit high-quality workers; however, higher interest rates on homes, cars and credit cards could consume most of the wage increases, resulting in slower consumer spending. That on its own is unlikely to tip the economy into a recession, but delays on new investments, market uncertainty, and potential layoffs or operations moving overseas in response to the U.S. trade war could be the straws that break the camel's back.

Mark Stephenson: The trade battles could have a long-lasting impact on U.S. dairy exports. Early discussions about immigration and NAFTA pushed Mexico to diversify its portfolio of suppliers. And since the United States has stepped out of the Trans Pacific Partnership, the European Union has aggressively pursued bilateral agreements with other countries, often managing to include geographic indicators. All of this has created long-lasting damage with our foreign customers that will be hard to win back. Customer relationships are important and can be fragile.



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