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MCTCOMPASS

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No Surplus, No Subsidies

World market prices for dairy products were stifled for the better part of the last three decades. It has only been recently that markets have been driven by changes in internal dairy policy within the European Union and the United States. The continual enlargement of the EU from eight to 15 to 27 member countries has resulted in a greater amount of dairy product production consumed within the member states. In other words, new member countries that were once exporters on the world market are now suppliers to the internal EU market.

On this side of the Atlantic, the U.S. government made a conscious effort to reduce its burdensome holdings of nonfat dry milk powder from over 1 billion pounds in 2002 to less than 100 million pounds by year-end 2005.

Many economists speculated that a world dairy market absent of surplus and subsidies would result in higher dairy product prices. To date, just the elimination of surplus government stocks in tandem with slower Oceania milk growth and strong global demand for dairy products has been sufficient to send world market dairy prices to new highs.

Whey Margin Squeeze

Whey has a long history of being a challenge. At first, the challenge was how does a cheesemaker get rid of the unwanted liquid? Over time through research and technology, higher-valued uses of whey were developed and then dairy producers challenged the Federal Order and California milk pricing schemes to incorporate a whey value into the value of their milk used to make cheese in 2000 and 2004, respectively.

In both milk pricing systems, the milk used to manufacture cheese was enhanced by a "whey-factor." For example, every penny increase in the dry whey price results in a 6-cent increase in the milk price used to make cheese. Since midyear 2006, the dry whey price has increased from 27.5 cents per pound to 77.5 cents per pound. That 50-cent increase has

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KEN'S CORNER

by Ken Meyers
President
MCT Dairies Inc.

Adding dry whey to the milk price formulas was an acknowledgement that there is additional revenue from this by-product. No one considered that the lowest common denominator in the whey market could become a scarce product. That is the case today and it is causing tremendous economic stress and inequity within the cheese industry.

It is time for the industry to unite and request legislative action to remedy the problem.

For those who believe the present shortness in supply is temporary, for your businesses sake, please revisit this view. The United States is presently the lowest-cost supplier of many dairy commodities. We have talked of this day coming and although this may be a 6 to 18 month phenomenon in the short run, it is indicative of a longer-term trend.

Our milk pricing system will be tested by more than just the whey component scheme presently plaguing cheesemakers. In order to adapt to the needs of our global consumers, our pricing system must allow for longer-term contracts to be in place that not only do not negatively affect producers, but also enhance incomes for the whole marketing complex. MCT

Soaking it up

MCT Forecast							
	Block*	Barrel*	Butter*	Whey**	NFDM**	Class III	Class IV
Apr	1.4628	1.4490	1.3725	0.7785	1.455	16.50	16.30
May	1.5900	1.5650	1.4250	0.7650	1.650	17.55	18.25
Jun	1.6150	1.5850	1.4500	0.7550	1.750	17.75	19.25
Jul	1.6350	1.6100	1.5000	0.7550	1.855	18.00	20.35
Aug	1.6500	1.6250	1.5000	0.7550	1.888	18.15	20.75
Sep	1.6725	1.6500	1.5000	0.7550	1.888	18.35	20.75

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

The dairy markets are firm and milk prices continue to increase even as milk production increases seasonally. Strong world demand will absorb any excess production, bolstering domestic dairy product prices. The U.S. economy continues to show resiliency in light of the housing market's woes. And the stock market's rise, particularly over the past month, appears able to continue to sustain consumer spending. **MCT**

Soaring raw milk costs...

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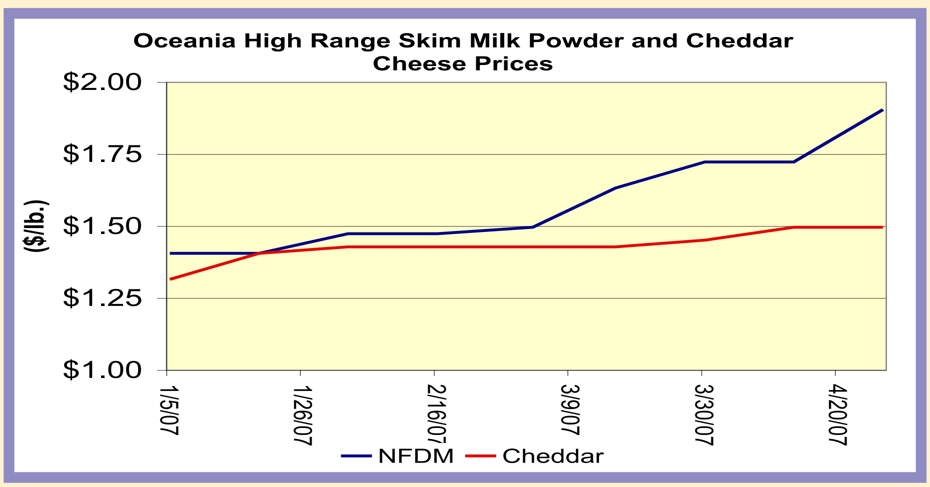
added $3.00/cwt to the regulated price of milk used to manufacture cheese.

Unfortunately, many cheese manufacturers do not manufacture good old-fashioned dried sweet whey. Some of the older cheese factories and particularly specialty cheese manufacturers rarely have whey drying capacity. These manufacturers are forced to recover the $3.00/cwt increase in their milk cost by increasing their cheese price. To date, manufacturers refer to increases of less than a nickel per pound rather than the 30-cent increase they need to be whole.

The newest cheese manufacturing facilities are also feeling the margin squeeze. These facilities invested in the production of higher-valued whey protein concentrates and isolates. Unfortunately, the sales prices of whey protein concentrates and isolates have not increased nearly as much as the sale price of dry whey.

Unfortunately for cheese manufacturers, a timely remedy for the whey induced margin squeeze is not on the horizon. During a recent Federal Order hearing, the topic was broached, but that hearing has been continued to July and implementation of any decision is unlikely for at least a year. A quicker remedy could be legislative, but to date, nothing has been introduced and any legislation that would likely reduce the value of milk used to manufacture cheese is also likely to be controversial. **MCT**



Source: Dairy Market News, complied by MCT Dairies.