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MCT COMPASS

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Will Complacency Give Way?

Over the past year, a slow rebound in the world economy has helped increase dairy commodity demand worldwide. In fact, U.S. year-over-year exports in May increased for the 12th consecutive month and were equivalent to 14.7% of milk production on a total solids basis. Low feed prices and robust domestic demand for dairy products have also supported U.S. milk prices. As a result, the U.S. midyear market forecast looks fairly upbeat.

"The U.S. midyear forecast for dairy product prices looks fairly upbeat."

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 economists: Bill Brooks, INTL FCStone; L. J. "Bees" Butler, University of California; Bob Cropp, University of Wisconsin; James Dunn, Pennsylvania State University; Mary Ledman, Keough Ledman and Associates and the *Daily Dairy Report*; and Mark Stephenson, University of Wisconsin. We then added their forecasts to the CME Group futures settlement prices for July 24, 2017, to create a consensus forecast.

Our panel's average Class III price for second-half 2017 is $16.53/cwt. The group expects the Class III price in 2018 to average $16.95. The most bullish of the analysts expects a 2018 Class III average of $18.40, while the most bearish anticipates a 2018 average of $15.73. The futures market was predicting a price of $16.67. Forecasts for the average NASS cheese price for the next six months fall between $1.57 and $1.70. For the 2018 average, the experts' cheese price forecasts range from $1.58 to $1.80. The analysts were not as optimistic on 2018 whey prices, with the consensus forecast at 44 cents, identical to their average second-half 2017 price.

Forecasts for Class IV market prices are mixed, with butter prices declining in 2018—but remaining relatively high—and nonfat dry milk prices recovering. The consensus forecast for the second-half 2017 average Class IV price is $16.74, or 21 cents higher than the Class III forecast. In 2018, the panel anticipates an average annual Class IV price of $16.16, which is 79 cents lower than the 2018 Class III forecast. For the second half of this year, the group expects nonfat dry milk prices to average near 92 cents per pound, with the butter price forecast near $2.58. Next year, the panel sees nonfat dry milk prices rising to an average of $1.01 and butter prices averaging near $2.28.

"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," says one analyst. "If feed prices increase and milk supply decreases, it would seem

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Ken's Corner

by Ken Meyers
President , MCT Dairies Inc.

It's easy to become complacent in a Goldilocks market—one that's not too hot and not too cold—or in a market that mostly continues to inch slowly in the right direction. A steadily improving market or one that's flat can lull market participants into complacency—until the unexpected occurs. And it always occurs.

Last year at this time, dairy markets were filled with uncertainty. Many of those uncertainties are still lurking in the background today including struggling economies in Latin America, the continued ban on dairy products to Russia (a situation that could escalate), Brexit, a glut of oil and gasoline that continues to dampen dairy exports to oil-rich countries, ongoing terror attacks, and the threat that rising interest rates will raise the value of the dollar.

At the same time, the U.S. economy has been slowly growing, the world economy has been quietly picking up, and demand for dairy products has been steadily rising both here and abroad. Throughout it all, the U.S. dairy industry has been in the enviable position to be able to meet rising global demand more so than any other supplier. And it appears that will continue to be the case well into 2018—barring a weather and/or crop catastrophe, geopolitical upheaval that causes the U.S. economy and domestic demand to contract, or some other unknown waiting to ambush the market. **MCT**

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that current inventory is sufficient to take up most of the slack, at least in the short term. There seems to be a sort of equilibrium in place at the moment with respect to milk supply, demand, international markets, prices, and inventory. Some have referred to this as complacency in the market."

This complacency should be viewed cautiously, however, as this year's experts also point out both the obvious and the not-so-obvious market movers. For example, one analyst points out that "over-order premiums continue to come under pressure as does the ability of producers to use rBST. As a result, 2017's higher dairy product prices are not necessarily translating into equivalently high mailbox milk prices."

It appears butter could continue to be the star product in 2018. "A few years ago, milk protein prices were dragging butterfat prices along. Today, the opposite is true. When the medical community declared a truce with milkfat, consumers came running back to the full flavor and mouth feel that butterfat delivers to dairy products," one economist notes. But will that enthusiasm for butter last? For the foreseeable future it will, the panel says. **MCT**

Consensus Forecast

	Cheese	Class III	Butter	Class IV	Whey	NFDM
July	1.5520	15.52	2.61	16.64	0.45	0.92
Aug	1.6209	16.11	2.69	16.91	0.44	0.91
Sept	1.6610	16.48	2.65	17.13	0.44	0.92
Oct	1.7049	16.88	2.55	17.14	0.43	0.93
Nov	1.7264	17.05	2.55	16.60	0.43	0.93
Dec	1.7166	17.11	2.40	16.02	0.43	0.93
2H 2017 Avg	1.6636	16.53	2.58	16.74	0.44	0.92
2018 Avg	1.7146	16.95	2.28	16.16	0.44	1.01

What the experts

Bill Brooks: Large stocks of EU and U.S. nonfat dry milk and skim milk powder (NFDM/SMP) overhang the market, but there is a chance that EU SMP stocks might not ever make it to the market for human consumption due to age. U.S. stocks of NFDM are very heavy, but there has not been much downward pressure on prices because of persistent concerns over production in California, the leading NFDM-producing state.

L. J. "Bees" Butler: Milk prices have held up reasonably well over the last couple of years because U.S. exports of dairy products have been relatively well maintained despite a strong dollar and surplus dairy products in both the United States and Europe. Global Dairy Trade (GDT) prices have not given any indication of a trend in global dairy product prices for almost a year, which would indicate that current trends in U.S. milk prices are fairly stable and likely to remain so for at least next year.

Bob Cropp: Global economic growth will continue at a relatively slow pace. Oil prices are not expected to increase much, dampening dairy imports by oil-producing countries. But world supply and demand is much tighter than a year ago and world dairy product prices have increased making all U.S. dairy products competitive.

James Dunn: Worldwide inventories of dairy products are a problem. With milk production relatively strong, it will take a long time to work through world stocks, and that will limit prices on the upside.

Mary Ledman: Canada's implementation of a new ingredient class of milk has resulted in Canada being able to price domestically produced milk proteins at a level lower than imported milk proteins. As a result, several U.S. manufacturers of milk protein concentrates have lost markets. In addition, Canada has increased exports of SMP, which it believes will not be subject to subsidy restrictions. Through May 2017, year-over-year Canadian SMP exports are up 281%. U.S. SMP exports to its largest market, Mexico, are the most at risk—especially considering the possibility of renegotiating the North American Free Trade Agreement.

Mark Stephenson: We have been fortunate to have a relatively strong economy and robust domestic demand for dairy products. This has largely managed to offset the loss of export sales in the past couple of years. However, we have seen stocks building and unless we can pick up more export sales, prices will have to decline to reflect our ability to oversupply the market.

 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.