

Global Output Strong for Now

At the start of 2018, Dairy producers worldwide were producing more milk than they were in early 2017, but headwinds were also starting to appear. For the first time in several years, lower global dairy product prices were threatening U.S. dairy producers. During



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the 2015-16 downturn in global prices, U.S. dairy producers experienced margins that were far lower than 2014's record-breaking margins. While these lower margins caused discomfort for many of the nation's dairy producers, others thrived, creating what has now become one of the longest periods of expansion in U.S. milk supply on record. Through December 2017, U.S. milk production had bested the previous year's output for 48 consecutive months, and the U.S. milking herd had grown to 9.35 million head as of Jan. 1, 2017, the largest herd since 1996.

During the 2015-16 global downturn, U.S. dairy producers experienced short bouts of lower milk prices, but nowhere near the lows that confronted producers in Europe and Oceania. Stronger domestic butterfat demand

helped lift U.S. butter and cheese prices, and a robust over-order premium structure worked to enhance milk checks east of the Rocky Mountains. Therefore, most U.S. dairy producers were buffered from the declines that overwhelmed dairy producers elsewhere in the world.

Global dairy product prices now appear poised to head lower, but U.S. producers may not have the benefit of rapidly expanding domestic demand for butterfat. And in large swaths of the country, over-order premiums are far less than they were even a year ago. In the near term, the streak of year-over-year production gains will likely continue, but as spring approaches dairy producers' resolve to produce more milk could be tested.

Across the Atlantic, EU-28 milk production got off to a slow start in 2017, but strong year-over-year increases at the end of the year were expected to boost 2017 output by more than 2% over 2016 levels. Strong milk prices, propelled by higher butterfat prices, are once again driving gains in milk production in Germany and France, the EU's two largest milk-producing members. At the same time,

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by Ken Meyers
President, MCT Dairies Inc.

At the start of the year, the United States was holding 141,820 MT (301.7 million pounds) of nonfat dry milk (NFDM) in commercial warehouses, while the European Union had 378,051 MT (over 834 million pounds) of skim milk powder (SMP) in Intervention.

On Jan. 19, the European Commission approved the temporary elimination of fixed-price buying of SMP stocks when Intervention re-opens in March 2018. Instead of being required to purchase up to 109,000 MT of SMP between March 1 and Sept. 30 at a fixed price of €1,698/MT (95 U.S. cents per pound), the Commission will now purchase SMP into Intervention based on a tender process, allowing it to limit, or even avoid, further stock accumulations.

By eliminating the requirement to purchase SMP at a fixed price, the Commission is suspending its support price for SMP, which will allow prices to drop further, theoretically providing a clear market signal for EU dairy producers. However, lower SMP prices may not immediately translate into significantly lower milk checks for European dairy producers because higher butterfat prices could offset some of the declines in SMP prices. Due to the global disconnect between protein and butterfat prices, producers everywhere have not received a clear message that there is too much milk in the system. **MCT**

Prices Poised to Head Lower

Dairy product prices are signaling that markets could head lower before spring. Heftier milk supplies

and mounting skim milk powder stocks in Europe are putting a lid on near-term price expectations. At the same time, supply concerns from New Zealand could provide a floor for prices until the market has a better understanding of weather impacts on milk output. Globally, butter prices remain at historically high levels. Most dairy products are favorably priced and that could encourage greater promotion and consumption. But the same low prices could result in lower milk checks to dairy producers. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Jan	1.4925	1.3425	13.98	2.1625	13.09	0.2725	0.6950
Feb	1.4400	1.3775	13.51	2.1900	12.94	0.2675	0.6675
Mar	1.3900	1.3950	13.32	2.1825	12.87	0.2600	0.6550
Apr	1.3750	1.3825	13.19	2.2175	12.82	0.2600	0.6350
May	1.3775	1.3750	13.13	2.2975	13.03	0.2600	0.6275
Jun	1.4875	1.4450	13.86	2.3325	13.24	0.2650	0.6250

* CME prices.

**NASS prices.

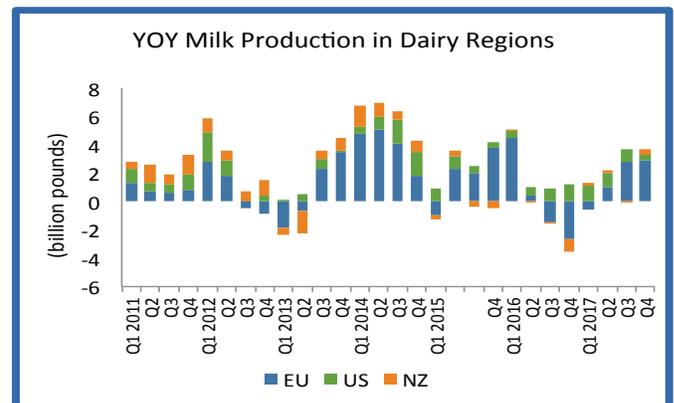
...weather issues surface downunder

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Ireland, Italy, and other member states were logging strong output gains. In 2018, year-over-year EU milk deliveries are expected to grow between 1% and 3%, with most of this year's growth expected to come from improving genetics designed to boost production per cow and European milk prices that are expected to remain above break-even at least through early 2018.

As U.S. and EU milk production continues to grow, New Zealand's 2017-2018 season appears to be hampered by adverse weather. The season started with excessively cold, wet conditions that quickly reversed in November. By December, hot, dry conditions were negatively impacting production, with total output of 2.62 million metric tons (MT) falling 2.6% below the prior year. At this point, however, season-to-date milk production remains 0.9% ahead of the same period a year ago. Looking ahead, poor pasture conditions could negatively impact output per cow in the second-half of the season, and longer term, both changes in land use and maximum environmental carrying capacity could put a limit on the total number of cows that can be milked in New Zealand.

All totaled, milk production ahead of the spring



flush, likely remains well ahead of last year's pace despite possible setbacks in New Zealand. Northern Hemisphere milk is rising seasonally and while demand for some dairy products, particularly butter, is robust, supplies of other products, especially skim milk powder, remain burdensome. As 2018 gets underway, the world market continues to grapple with striking a supply balance that provides enough butterfat to satiate demand but at the same time avoids overproduction of protein. In 2018, price could be instrumental to finding equilibrium between butterfat and protein supplies. **MCT**



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