



## Perspective: Dairy Markets

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## The longest participant in dairy is still looking for a way out of its position

A little over a year ago, I wrote an article about the longest participant (in terms of stocks sitting in storage) in the dairy industry — the European Union (EU) and their intervention scheme. The amount of skim milk powder (SMP) held in the intervention scheme justified the statement and more than 12 months later, the same holds true.

The good news? The totals are decreasing with July, August and September figures below year-ago levels, which is the first time that can be said in this context. The bad news? Despite the minimal decreases, the total number of stocks still exceeds 380,000 metric tons, which continues to loom over the market like a dark cloud.

I have found myself in multiple conversations with different people speaking about the ins and outs of the powder market and no matter what was said previously, the chat would usually end with a version of “yes, but do not forget about the EU stocks in intervention, they have to go somewhere.” This fundamental aspect of the market could not be forgotten.

So, what do you do with 380,000 metric tons of aging skim milk powder in storage while the bid around it dissipates? EU

Commissioner Phil Hogan has some ideas, which he addressed a little over a month ago. But if you look at current prices, those ideas clearly have consequences in the sensitive market atmosphere that we find ourselves in today.

To get a clear picture of what the future looks like, one has to understand the past. Year-ago stocks have been steadily decreasing while the price has been doing the same. At the same time, though, the fat component was doing the exact opposite. The price for butter in the EU screamed higher for almost six months straight topping out around 6,775 euros per metric ton or ~\$3.60/pound. This has only added to the dismay of powder in two different ways.

First, because of the outrageous value of butter, manufacturers have tolerated the fact of more skim production. Typically if a certain dairy commodity is low in value, milk is allocated to a different production stream — cheese or whey for example. But with consumers tripping over butter bids, SMP did not catch a break.

Second, let's not forget the primary reason for the intervention scheme — to protect dairymen from depressed farmgate milk prices. But what happens

when all the other components of milk (particularly cheese and butter) are at prices that produce a higher-than-average farmgate milk price? It lowers the justification for an intervention scheme.

Cue Hogan's comments from a little over a month ago, as reported in the German publication, *Agrarheute*. There are two huge aspects that need to be focused on. First, was his comment about essentially shutting down the intervention scheme. He proposed that instead of continuing to buy at a fixed price, the Commission move to a tendering system of buying at “market value.” That initial market value? “Close to zero.”

Secondly, he referenced the overwhelming stocks currently in storage. While understanding what a major reduction would do to the 2018 market, the sense of urgency remains high with hints of the possibility of moving the majority to feed use instead of human consumption. Keep in mind, if this were to happen, the ripple effect could cause a major move downward in dry whey prices as old SMP stocks could be used as a substitute. Clearly, futures prices on the Chicago Mercantile Exchange (CME) were paying attention as prices in the first quarter of 2018 fell by an average of 3 cents the day after the comments.

Not surprisingly, the same can be said for nonfat dry milk (NDM) on the CME. On the same day dry whey tumbled, the first quarter futures dropped from an \$0.8600 average to \$0.7825, an almost 8-cent drop in just three trading days. More recently, the CME spot market made new lows for 2017 by dropping to the low-\$0.70s.

A nonexistent fixed-price intervention scheme in the EU will not only affect the NDM market, but it also has the potential to pull the rest of the dairy complex down with it. As butter has come back down to earth, manufacturers will have more incentive to produce Class III components — cheese and dry whey, which are two markets that have their own fair share of supply issues. Also, the less expensive nonfat becomes, the higher the chances that cheese processors will procure and fortify using the cheaper product. At that

point, protein is protein.

So where's the bottom? The bear staring the market in the face right now has a few strong fundamental aspects behind it with the largest being the growth in European milk production (September estimated to be around 3 percent higher year over year). Nonfat production in the United States grew by 6.2 percent in September versus 2016 and stocks continue to grow as well, reaching more than 320 million pounds at the end of the month and let's not even talk about the possibility of no NAFTA. With all this said, the market is sitting near historical lows, so how bearish can one be? Year-to-date imports for SMP are all higher year over year for large consuming countries like Mexico (+24.2 percent), Algeria (+46.6 percent) and China (+29.4 percent). The United States' largest milk producing state, California, has its own set of producing issues (down 3.4 percent versus last year in September) that will not be fixed overnight.

Ultimately, there is no clear picture ahead with uncertainty surrounding the commission pricing support. Perhaps the market is better off without the scheme since there clearly needs to be a sort of “wash-out” of product globally. One thing is for sure — the road ahead does not look easy as the longest participant in dairy still is looking for a way out of its position. CMN

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## NEWS/BUSINESS



## Dairy Farmers of America opens new dairy ingredient plant in Garden City, Kansas

**KANSAS CITY, Kan.** — Dairy Farmers of America (DFA), a national dairy cooperative owned by family farmers, recently celebrated the opening of DFA Garden City, a new, state-of-the-art dairy ingredients plant located in southwest Kansas.

DFA Garden City is a partnership between DFA and 12 of its member farms in southwest Kansas and will help support the industry's continued growth in the region, as well as meet rising demand for U.S. dairy both domestically and globally, DFA says.

“As a cooperative owned by family farmers, we are always looking for opportunities to help grow the dairy

industry and provide value to our dairy farmer-owners,” says Rick Smith, president and CEO, DFA. “This investment not only fills an important need for the region by providing a local home for DFA members' milk, which was previously being transported to other areas of the country, but it also supports and enhances our global ingredients strategy, which benefits all our farmer members.”

Construction started on the Garden City facility in October 2015, and the first load of milk was delivered in late September 2017. The plant, which has brought 66 new jobs to the area, produces whole and skim milk powder,

nonfat dry milk powder and cream, and receives approximately 4 million pounds of milk a day from regional farms.

“As a farmer invested in this plant, it's exciting because we're connecting our family farms to family tables in a truly sustainable and traceable way,” says Dan Senestraro, who also serves on the board of directors for DFA. “This plant allows us to trace the product from the time it leaves the farm as raw milk to the time it arrives at the store, which is important to many consumers today.”

Beyond the traceable aspects of the product, DFA says the new Garden City plant also focuses on sustainability, including operating as a water-neutral

facility. With this process, all the water utilized at the plant is recycled and ultimately used to water landscaping and parks throughout the city.

During yesterday's open house ceremony and ribbon cutting, representatives from DFA were joined by Kansas Gov. Sam Brownback and Garden City Mayor Melvin Dale to mark the official opening of the state-of-the-art dairy ingredients facility. Rick Smith and DFA Chairman of the Board Randy Mooney thanked those individuals who have been instrumental in the plant's development, including 12 DFA farm family owners and members who invested in the facility. CMN