

Dairy Situation and Outlook, August 19, 2020  
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In mid-April on the CME 40-pound cheddar blocks were \$1.00 per pound. But prices rallied with blocks setting a new record in June at \$2.81 per pound and continued to increase setting another record at \$3.00 per pound on July 13th. But \$3.00 per pound lasted just one day with prices falling ever since. Blocks were \$2.2350 per pound the end of July and averaged \$2.6466 for the month. Cheddar barrels were also a low of \$1.00 per pound in April, reach \$2.425 in June and \$2.465 in July but fell to \$2.235 the end of July averaging \$2.408 for the month. These price changes resulted in the Class III price to increase from \$12.14 in May to \$21.04 in June and \$24.54 in July.

Unfortunately, milk prices are headed lower with the August Class III around \$19.45 and possibly heading to the \$16's for the remainder of the year. Both 40-pound cheddar blocks and cheddar barrels have weakened considerably. The 40-pound cheddar blocks got as low as \$1.58 per pound and are now \$1.71. Cheddar barrels are now \$1.375. Unless prices strengthen some Class III could fall below \$16. Current Class III September futures are \$15.41. What has changed since June and July to result in lower cheese prices? On the supply side milk production declined 0.5% in May and was up just 0.8% in June as dairy cooperatives implemented base excess plans on their producers. But dairy producers have responded to the higher milk prices in May and June. July milk production was 1.5% higher than a year ago. After cow numbers declined for 4 months July cow numbers increased by 2,000 head and were 0.4% higher than a year ago. Milk per cow improved being 1.1% higher than a year ago.

But several things happened on the demand side. The bright spot is home consumption of dairy products has and continues to run well above year ago levels. Restaurants partially reopened and there was a need to buy cheese and replenish their stocks. But in July the surge in the coronavirus resulted in restaurants being instructed to cut back on their openings. It also looks like food service will be negatively impacted as many schools and colleges open this fall with virtual learning, high school and college fall sports being cancelled, professional sports to have no fans in the stands and conferences and other major events being cancelled. These moves hurt beverage milk, cheese and butter sales. Under the Farmers to Families Food Box program that operated from May 15th to June 30th the government purchased a lot of cheese. The second round of Farmers to Families Food Box program is operating from July 1 to August 31st but the amount of cheese purchased will be reduced.

Demand was also boosted by higher dairy exports in May and June. With the exception of butter nonfat dry milk/skim milk powder and cheese were below world market prices in May and early June. World customers took advantage of these lower prices and increased purchases. May dairy product exports were the most in two years with record exports of nonfat dry milk/skim milk powder, improved exports of cheese and whey products. June exports were up 28% by volume from a year ago. Cheese exports were a record for any given month, nonfat dry milk/skim milk powder exports were up 77%, butterfat exports 15% higher and total whey products 8% higher with dry whey 41% higher as China purchases more whey products as they restock their swine herd following last year's African Swine Fever outbreak. But July exports may have been lower, particularly for cheese as June and July prices were well above world prices.

There remains a lot of uncertainty as to where milk prices are headed for the remainder of the year and for next year. Until the coronavirus comes much more under control and things return more to normal the demand for dairy products will be depressed. Dairy exports could continue to do fairly well as U.S. prices have now come more competitive with world prices. Also, world milk production in other major exporters continues to increase at a relatively slow rate which could give U.S. opportunities for more exports. But with the worldwide spread of the coronavirus there is a concern worldwide recession could dampen demand. The level of U.S. milk production will be very important. USDA is forecasting 2021 milk production to increase 1.9%, adjusted for leap year in 2020, the result of just 0.1% more milk cows and 1.8% more milk per cow. If this materializes, it will take favorable dairy exports to support higher milk prices.

Class III futures are now in the \$15.41 for September and the \$16's for the remainder of the year. But prices could strengthen some with milk production seasonally lower in August and September. Also as in the past the demand for cheese and butter is expected to increase during the holiday season. There is also a third round of the Farmers to Families Food Box that runs from September 1 to October 31, but at lower purchases than the first two rounds.

Class IV futures will be near \$13.10 for August and in the low \$14's November and December. Butter stocks are plentiful, but butter prices could strengthen some during the holiday season. Nonfat dry milk/skim milk powder exports could also stay above year ago levels, both of which could strengthen the Class IV price.

Dairy producers have not seen the same strength in their milk price as the increase in the June and July Class III prices due to relatively high negative producer price differentials (PPD) in the 7 federal order markets that have multiple component pricing. While cheese prices have decreased bringing down the Class III price the spread between the advanced Class III and Class IV prices for August is over \$10. Since the mover of Class I is the average of the advanced Class III and Class IV prices the August Class I price will be below the August Class III price resulting in a negative PPD. As Class III declines further and the spread between Class III and IV narrows negative PPD's will decline and may become positive again later this year.

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