

Dairy Margin Watch: July



Dairy margins strengthened over the last half of July due to a combination of higher milk prices and lower feed costs. With the exception of the spot Q3 period, deferred margins are now above the 80th percentile of the previous 10 years through the first half of 2018. Milk prices have been supported recently by strong demand from China, which may continue providing a tailwind through the fall. The country's dairy imports set a record pace for most products in June, with whole milk powder (WMP) up 65% from May and 57% higher than 2016. Skim milk powder (SMP) imports likewise rose 20% from May and were up 45% from last year. Cheese and whey import volumes also posted impressive year-over-year gains, rising 52% and 25% respectively from 2016. Spot cheddar cheese prices at the CME rose sharply today despite lower results from the latest Global Dairy Trade (GDT) auction. And Fonterra recently increased their forecast for 2017-18 farmgate milk prices, perhaps partly in response to updated June trade data for New Zealand. Meanwhile, feed prices have been under pressure due to improved forecasts and expectations for cooler temperatures and periodic rains in the U.S. Corn Belt. USDA noted improved soybean crop conditions in their latest weekly report, with the share rated in good-excellent condition rising two points on the week to 59%. The August WASDE report will incorporate yield projections from NASS, which takes actual field surveys into account. Most traders are expecting declines in yield and production estimates from July for both corn and soybeans. Our dairy producer clients are both scaling into new coverage following recently improved margins, as well as evaluating adjustments to existing positions. Strengthening both milk and feed hedges has been a focus after recent price action in both markets.



The Dairy Margin calculation assumes, using a feed price correlation model, that for a typical dairy 62.4 lbs of corn (or equivalent) and 7.34 lbs of meal (or equivalent) are required to produce 100 lbs of milk (includes dry cows, excludes heifers not yet fresh). Additional assumed costs include \$0.90/cwt for other, non-correlating feeds, \$2.65/cwt for corn and meal basis, and \$8.00/cwt for non-feed expenses. Milk basis is \$0.75/cwt and non-milk revenue is \$1.00/cwt.

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