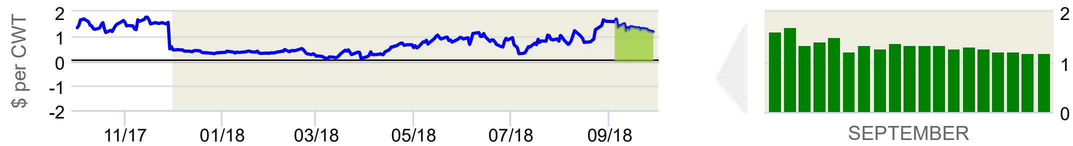
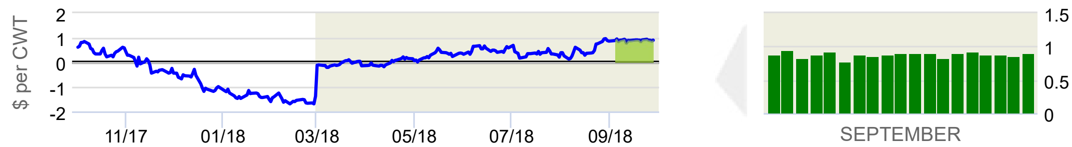
Dairy Margin Watch: September

The dairy market has been fairly steady the past two weeks, as the fundamentals have been throwing around some mixed signals. Milk production in August was stronger than expected, estimated to be 18.3 billion pounds, a 1.4% gain over last year. Production was 1.2% higher in California, even though the herd size dropped by 12,000 head. Nationally, however the number of milk cows on farm dropped by 4,000 head. Cold Storage figures for both butter and cheese indicated monthly draws, but were higher on a yearly comparison by 3.8% and 1.9% respectively. Record inventories of cheese dissipated on a monthly basis by 3.8%, nearly doubling the average July through August draw of 2.0% over the past ten years. Butter supplies on the month were lower by 8.6%, not quite meeting the average July through August pace of 10.5% over the same period. Trumping the USDA updates was NAFTA 2.0 news, which rocked the agricultural and equity markets alike. The U.S. and Canada came to terms on the so-called new U.S.-Mexico-Canada Agreement (USCMA), after tough rhetoric, the impasse was broken right at the deadline. Canada agreed to open up their dairy market to additional U.S. imports and eliminate the Class 6 & 7 milk categories, while the U.S. dropped demands for a new trade dispute regime, a major Trump administration sticking point. Among other new facets, an exchange rate curb to discourage artificial currency manipulation to gain trade advantages was implemented. Many believe this mechanism will be included as a benchmark in all future trade negotiations. U.S., Mexico and Canada all need approval for the new pact, and ratification will likely spill into 2019, as will the phasing in of changes to the Canadian dairy market. The U.S. corn harvest is 26% complete, ahead of the 5-year average of 17%, but pesky rains throughout the belt will slow progress as fields dry out. The Quarterly Grain Stocks report revealed 2.14 billion bushels of corn as of September 1, above expectations by 138 million bushels, but did represent a drawdown of 7% from last year's levels on greater disappearance. The October WASDE report will update yield and production projections, and will incorporate the fresh stocks data as well. Given the seasonal tendency of margins heading into next year, many of our clients are concentrating on maintaining flexibility across the board.

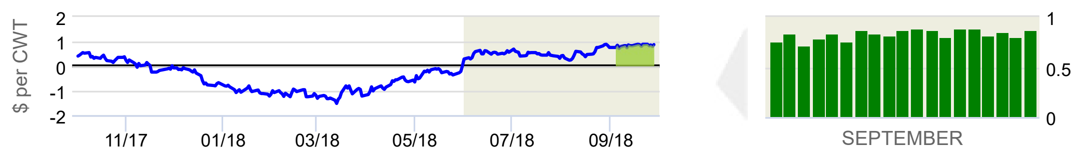
4th Qtr '18 2017 2018 Q4 2018: HIGH **$1.70** LOW **$0.08** LAST **$1.19** 10YR PERCENTILE **67.1%**



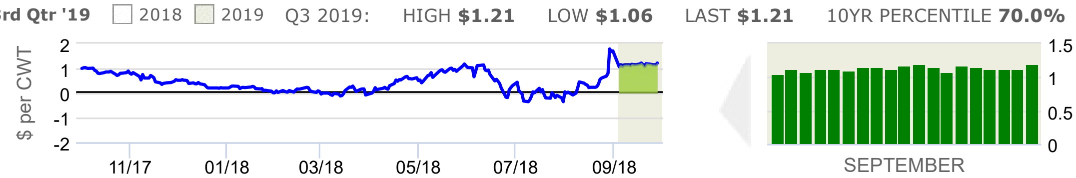
1st Qtr '19 2018 2019 Q1 2019: HIGH **$0.96** LOW **($0.21)** LAST **$0.90** 10YR PERCENTILE **75.9%**



2nd Qtr '19 2018 2019 Q2 2019: HIGH **$0.89** LOW **$0.23** LAST **$0.88** 10YR PERCENTILE **78.7%**



3rd Qtr '19 2018 2019 Q3 2019: HIGH **$1.21** LOW **$1.06** LAST **$1.21** 10YR PERCENTILE **70.0%**



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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