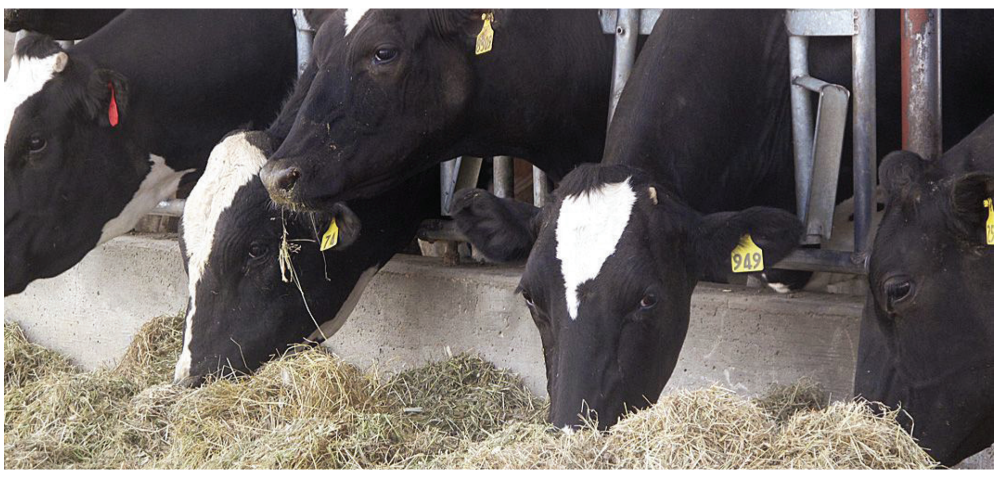

Capital Press File

High feed prices continue to restrict milk production.

Feed costs limit U.S., global milk production

By CAROL RYAN DUMAS
Capital Press

Record-high milk prices prompted only a minimal expansion in the U.S. dairy herd, as high feed prices continued to limit milk production in the second quarter.

Nonetheless, U.S. cheese stocks continued rising to record highs.

U.S. milk production in May was 0.7% lower year over year despite the cow herd increasing by 2,000 head from April. Totaling 9.4 million head, the U.S. milk cow herd is still short 102,000 head versus a year ago, CoBank reports.

"Record-high feed costs, extremely tight heifer inventories and high construction costs continue to limit expansion potential," Tanner Ehmke, CoBank's lead economist for dairy and specialty crops, said in the report.

Although feed costs eased at the end of the quarter, only incremental increases in cow numbers and milk production are expected for the remainder of 2022, he said.

Expansions have thus far been limited to states like Texas and South Dakota in the central U.S. where dairies typically grow their own crops and have more control over feed costs. New dairy barn construction is underway in some regions, notably in areas where plant expansions have been announced, he said.

"Globally, milk supplies remain constrained with Europe and Oceania struggling with inclement weather, high feed prices and regulatory pressures to reduce greenhouse gas emissions," he said.

Combined milk production in the EU and UK in April was down 0.9% year over year, while New Zealand production was down 5.6%, he said.

"Ongoing cost and regulatory pressures are expected to limit milk production growth for the remainder of 2022, tightening the world dairy product balance sheet and sending more export business to the U.S.," he said.

On the processing side, milk in the U.S. continued to flow to cheese vats in the second quarter with cheese manufacturers building inventories to record levels. Cheese production at the start of the second quarter also continued its push to record highs, he said.

But in a concerning sign of consumers responding to high food prices, American-style cheese disappearance fell 10% year over year in April. Demand for other cheeses inched up only 0.6%. Retailers note consumers are also switching to lower-priced and private label cheeses to save on cost, he said.

"The sharp slowdown in domestic cheese demand coupled with rising production pushed U.S. cheese inventories to new record highs, especially with American-style cheeses," he said.

Total cheese stocks were 1.5 billion pounds in May, surging 31 million pounds from the previous month.

Dairy economist considers the impacts of inflation, interest rates

By CAROL RYAN DUMAS
Capital Press

With June's inflation rate at 9.1% — the highest in 41 years — and the Federal Reserve raising interest rates to tame it, many in the dairy industry are concerned about how the upheaval will impact them.

"Obviously, a concern here with inflation and interest rates rising so quickly is that the Fed may make a misstep and tip U.S. economy into recession, and that may impact consumption habits," said Tanner Ehmke, CoBank's lead economist for dairy.

"That may impact the consumer's ability or willingness to buy dairy products," he said during the latest "Dairy LiveStream" webinar.

Consumers are already trading down from branded products to private labels or shrinking the size of packages they're purchasing, such as buying a half gallon of milk instead of a full gallon, he said.

"We're already seeing these inflationary pressures now," he said.

So the question is, What's going to happen in the dairy industry if the Fed continues raising interest rates aggressively? he said.

"The obvious initial impact would be on borrowing costs for dairy farmers and dairy processors. It's going to become more costly to borrow," he said.

But he stressed the need to do the math on the nominal interest rate versus the real interest rate.

"The real interest rate is the nominal interest rate, which is what you are paying your bank, minus inflation," he said.

For instance, if a farmer is paying 6% on an operating loan and inflation is 9%, the market is paying the farmer 3% to borrow money. So there's still an incentive to borrow, he said.

CoBank's been watching USDA's monthly milk reports, and the size of the U.S. dairy herd is only increasing incrementally. So there are a lot of things going on to curb expansion, including high feed, labor and material costs, he said.

"If we start to see the inflation numbers tick down and the interest rate numbers come up, then we're going to see a penalty there for borrowing. So perhaps what we'll see then is another disincentive to expand," he said.

For processors, another major cost is their cost to carry inventory, and that's going to increase as borrowing costs go up, he said.

"So what they may do there is reduce inventory, and that may show up in tighter stocks for dairy products in the U.S.," he said.

Another part of that equation is consumer behavior, he said.

"If the consumer's going to be slowing down in their purchases, that would have the opposite effect perhaps on what is stored in inventory," he said.

There are a lot of things that are pushing and pulling against each other, and there's no clear answer for what rising interest rates could do on inventories and incentives to borrow money.