

Dairy Market Continues to Struggle

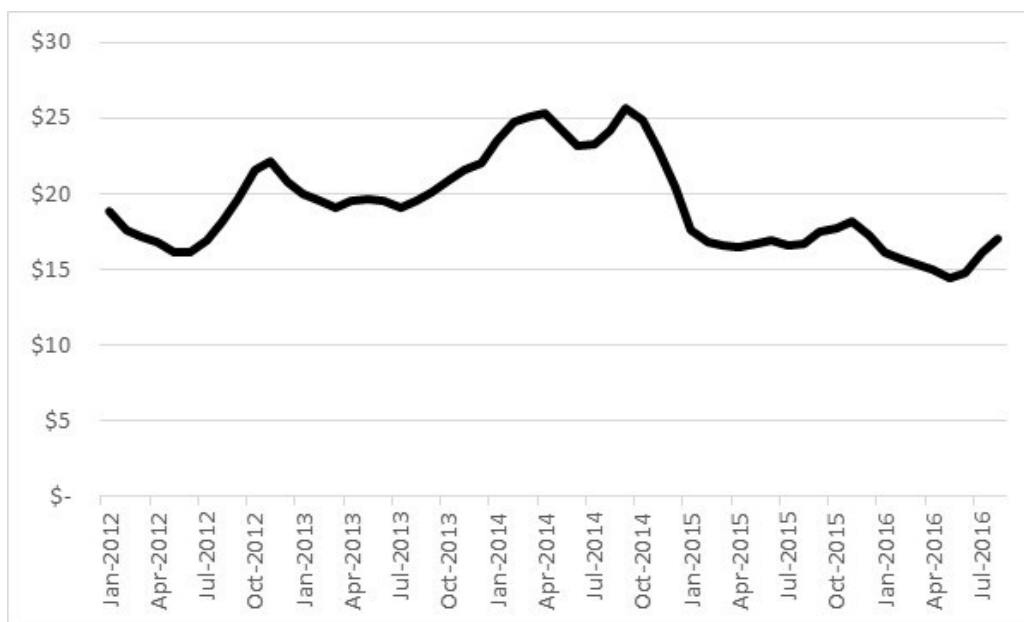


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Like many agricultural sectors, 2016 has not been kind to dairy producers. The decrease in farm-level milk prices over the last 24 months has rivaled that of any two-year period in recent history. All the usual suspects have contributed to the decline including increased production, decreased export levels, and weaker markets for most dairy products. Figure 1 shows US All Milk price from 2012 to 2016. Note the sharp drop starting in the fall of 2014 and the steady decline from fall 2015 through this summer.

Figure 1: US All Milk Price Jan 2012 to Aug 2016 (\$ per cwt)



Declining feed prices have only softened the blow somewhat and margins remain very tight. US corn price was \$0.42 per bushel lower in August of 2016 than August of 2014, while US All Milk price was down by \$7.10 per cwt. Figure 2 depicts MPP-Dairy margin from January 2012 to August 2016, which is the last month that data was available at the time of this writing. The margin calculation used in the MPP-Dairy program includes US All Milk, corn, alfalfa hay, and soybean meal. While the MPP margin doesn't perfectly describe an individual dairy operation, it does do a good job capturing the overall milk / feed price relationship and is relevant, as over 58% of dairy operations are now enrolled in the MPP-Dairy program (USDA FSA).

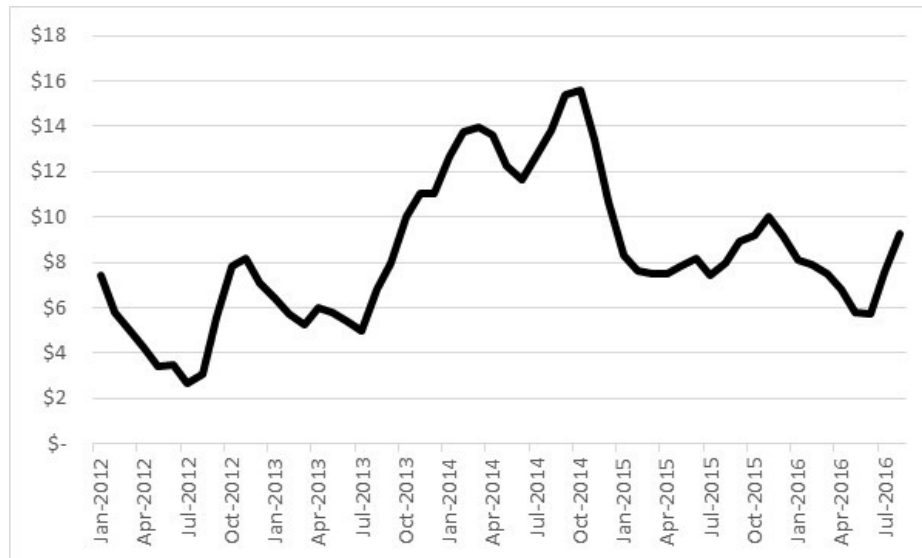
Much discussion this summer centered around the first sizeable payments made from this program as the MPP-Dairy margin averaged \$7.15 for the March-April couplet and \$5.76 for the May-June couplet. This was the first time, since the program's inception, that payments were received at a coverage level lower than \$8. To put this in perspective, a producer enrolled at the \$8 level would have a received payment of \$0.85 per cwt on 1/6 (two months) of their annual enrollment for March-April and \$2.24 per cwt for May-

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June. The two payments combined would be a little over \$0.51 per cwt if annualized, which would have slightly exceeded the \$8 premium level of \$0.48 per cwt for covered milk under 4 million lbs. Put simply, producers who enrolled in MPP-Dairy at highest \$8 level would have received slightly more in payments than they spent in premiums in 2016. And, it is possible that additional payments could be received for the September-October and November-December couplets.

Figure 2: MPP-Dairy Margin Jan 2012 to Aug 2016 (\$ per cwt)



While over half of dairy operations are enrolled in the MPP-Dairy program, very few chose coverage levels that would have received payments in 2016. According to FSA, over three-fourths chose the lowest \$4 coverage level and over 97% chose \$6.50 or lower. So payments that were made this year went to a small number of operations that enrolled at higher levels.

Given the current state of profitability in the dairy sector, it is very likely that many producers will choose to enroll at higher levels for 2017. Further, USDA has extended the deadline for enrollment for 2017 into December of 2016. So, producers will have the ability to decide on their enrollment levels up until about two weeks before the new year begins. By all means, producers should consider their options with this program and see how it might fit within their overall risk management plan.

We would also add that producers may want to consider other risk management strategies in addition to MPP-Dairy. Producers currently enrolled in MPP-Dairy are ineligible for the LGM-Dairy program, but this remains an option for many. Further, producers still have the ability to utilize contracting, futures, options, and other risk management strategies to manage downside risk on milk price and upside risk on feed prices. There is no single solution for managing risk for a dairy operation and no policy tool will work perfectly. Rather, producers should be aware of all the tools at their disposal and make an informed decision about which fit best given their goals.