



Issue Brief

Challenges Facing the Dairy Production Industry: Dairy Lenders' Perspectives

Dairy producers are scrambling. Their industry has always been highly cyclical, but the cyclical swings during the past year have been exceptionally volatile. After surging to a peak last year, the industry has been on a pronounced downswing since late last year. Analysts and industry insiders alike are wondering when and where the cyclical bottom will occur and, in particular, whether this downturn will be as bad as the one in 2009.

For insight into current and prospective market conditions and also into the other major challenges faced by dairy operators, we turned to five experienced Farm Credit lenders to the production dairy industry, all located in different regions of the country within the CoBank District. (See *text box*.) We asked each the same ten questions. Following is a synthesis of their answers.

1. What are the major challenges facing the dairies in your region?

While the five respondents' answers varied widely and with surprisingly little overlap, two challenges were mentioned several times – price volatility and water scarcity.

Price volatility is at or near the top of dairy producers' lists of major challenges. It's not just volatility in milk prices that's problematic for them, but also volatility in feed prices. Last year, the stars aligned, and dairy farmers nationwide enjoyed the best of both worlds – sky-high milk prices combined with sharply lower feed prices. This year, feed prices have remained low, but milk prices have fallen sharply. Margins have already narrowed, with further compression to come.

Water was the other major concern. California is now in its fourth year of drought, and dairies there are bracing for tough times. Feed supplies, much of it locally grown,

represent their highest operating cost. With California growers expected to fallow as much as one million acres of otherwise irrigated land this year, hay and silage costs are likely to ratchet higher, even as farmgate milk prices have plummeted nearly 40 percent from a year ago. The number one challenge facing California dairies in 2015 will be to keep their margins positive. But not all will succeed in doing so.

Another Western lender based in Colorado emphasized that water was a major challenge in his territory too. Most dairies currently have enough water, he said, to meet present needs. But it's difficult and costly to acquire additional water rights; and without them, expansion is out of the question. Such constraints on dairy production expansion are often key considerations in processors' decisions about where to locate new processing facilities.

Following are the five Farm Credit dairy lenders who were interviewed for this report:

Michael Haycook – Farm Credit East, Vice President and Branch Manager

Craig Shindler – Northwest Farm Credit Services, Branch Manager and Vice President

Dan James – American AgCredit, Vice President of Commercial Lending

Phil Kemp – Farm Credit West, Vice President and Key Relationship Manager

Kevin Kuper – Farm Credit of New Mexico, Senior Vice President and CCO