DATE: January 26, 2018
TO: Directors & Members
FROM: Kevin Abernathy, General Manager

Milk Producers Council
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MPC Friday Market Update

<table>
<thead>
<tr>
<th>CHICAGO CHEDDAR CHEESE</th>
<th>CHICAGO AA BUTTER</th>
<th>NON-FAT DRY MILK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Blocks</td>
<td>Weekly Change</td>
<td>Weekly Average</td>
</tr>
<tr>
<td>Barrels</td>
<td>+ $0.1000</td>
<td>- $0.0191</td>
</tr>
<tr>
<td></td>
<td>Weekly Average</td>
<td>Weekly Average</td>
</tr>
<tr>
<td></td>
<td>$2.1300</td>
<td>$2.1215</td>
</tr>
<tr>
<td>Weekly Average, Cheddar Cheese</td>
<td>Dairy Market News</td>
<td>National Plants</td>
</tr>
<tr>
<td>Blocks</td>
<td>w/e 1/26/18</td>
<td>w/e 1/20/18</td>
</tr>
<tr>
<td>Barrels</td>
<td>$2.6000</td>
<td>$2.6911</td>
</tr>
</tbody>
</table>

Week Ending 1/19 & 1/20

| Calif. Plants | $0.7122 | 9,198,829 |
| Nat’l Plants  | $0.6946 | 19,910,674|

Prior Week Ending 1/12 & 1/13

| Calif. Plants | $0.7110 | 5,284,310 |
| Nat’l Plants  | $0.6896 | 18,263,365|

Fred Douma’s price projections...

<table>
<thead>
<tr>
<th></th>
<th>Quota cwt.</th>
<th>Overbase cwt.</th>
<th>Cls. 4a cwt.</th>
<th>Cls. 4b cwt.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan 26 Final</td>
<td>$14.94</td>
<td>$13.24</td>
<td>$12.94</td>
<td>$13.37</td>
</tr>
<tr>
<td>Last Week:</td>
<td>$15.01</td>
<td>$13.31</td>
<td>$13.06</td>
<td>$13.45</td>
</tr>
</tbody>
</table>

Market commentary

By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com

Milk & Dairy Markets

After a precipitous decline, the foreign butter market seems to have reached its nadir. Indeed, European butter prices have moved quietly higher in the past couple weeks, and – thanks to the slumping U.S. currency – they are noticeably stronger when expressed in dollars. This may help to lift U.S. butter exports; Dairy Market News reports healthy demand for unsalted butter which is likely destined for buyers abroad.

There is plenty of butter to be had. Inventories climbed nearly 10 million pounds from November to December, a slightly larger-than-typical increase. At the end of the year butter stocks totaled 169 million pounds, up 1.8% from December 2016. That marks the first year-over-year growth in butter inventories since March and likely explains the slide in the butter market from mid-December to mid-January. Today, stability reigns. CME spot butter finished today at $2.13 per pound, up a penny from last Friday.

Milk powder demand is respectable, which is helping to support the nonfat dry milk (NDM) market. Rising prices in Oceania also offered a boost. Still, global stocks are burdensome, and there are concerns about the future of NAFTA and the consequences for U.S. NDM exports to Mexico. There is not much cause for a further decline in...
U.S. milk powder prices at the moment, but there is also little prospect for a sustained rally. At the CME spot market, NDM climbed 0.25ȼ to 71ȼ per pound. Nonetheless, most Class IV futures finished between 5ȼ and 20ȼ lower than last week. January through May Class IV and January through April Class III futures stand well below $14 per cwt.

The cheese markets gave back much of last week’s gains. CME spot Cheddar barrels slipped 2.5ȼ to $1.32 per pound. Blocks plunged 9.25ȼ to $1.4725. A rebound in the whey market helped to temper losses for Class III futures. Most contracts finished a few cents lower, but February and March Class III futures moved downward by double digits.

There were 1.28 billion pounds of cheese in storage at the end of last year, 6.9% more than on December 31, 2016. Cheese stocks climbed significantly from November to December, and could not keep up with robust production. Milk remains abundant and cheese vats are running hard.

U.S. milk production reached 18.04 billion pounds in December, up 1.1% from a year ago. Output continues to grow in the Southwest and to a lesser extent in the Midwest, but production is slumping on the coasts. Despite poor margins, dairy producers once again added cows last month. USDA estimated the milk cow herd at 9.4 million head, up 3,000 head from November (after USDA revised upward its estimate of the November milk cow herd) and 46,000 head higher than the year before. The U.S. dairy herd is just 3,000 head smaller than it was at the peak in August.

Judging by slaughter volumes, auction lineups, and springer prices, the U.S. dairy industry is poised to shrink. Poor on-farm margins and anecdotal reports from lenders suggest that a painful but necessary pruning is already underway. The depth and breadth of the dairy downturn will depend in part on how quickly milk production can contract among the major dairy exporters. Milk collections in New Zealand are already in decline. But if the European milk supply continues to grow by enough to offset reductions in the U.S. and Oceania, the pain is likely to drag on until prices are low enough for long enough to spur demand.

Fortunately, the global economy is growing, which has helped to accelerate demand for everything from almonds to zinc. This is particularly true in China, where demand for foreign dairy products has impressed. Although Chinese imports of whole milk powder (WMP) and cheese slowed in December, full year imports for both products were about 12% greater than in 2016. China imported 6.4% more skim milk powder (SMP), 12.6% more ultra-high temperature (UHT) milk, and 19.1% more whey in December.
than the year before. For the year, China imported 3.4% less UHT milk than in 2016. Chinese SMP imports were up 34.5% year-over-year, which helped to sop up a bit of the world’s excess milk powder. Chinese whey imports climbed 7.3%, which was particularly helpful to the oversupplied U.S. whey market. The U.S. accounted for more than half of China’s whey imports in 2017. Going forward, the weakening dollar will make U.S. dairy product exports even more competitive. However, the United States is losing some opportunities as other exporters negotiate aggressive trade pacts.

**Grain Markets**
The feed markets strengthened again this week. March corn settled at $3.565 per bushel, up 4ȼ. March soybeans finished 8.25ȼ higher at $9.855. March soybean meal closed at $335.70 per ton, up $4.10. So far, the weather in South America has been benign. Brazil’s crops are in excellent shape, and Brazilian soybeans continue to move abroad, eroding U.S. marketshare. In Argentina, crops are about to enter the key February filling period, and the forecast is dry. A strengthening La Niña could mean that dry weather persists. Given formidable global demand for soybeans, adverse weather in Argentina could quickly send the market higher. The trade will be watching closely.

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**Coming soon: Dairy Feed Mixing Electrification Program incentive funding enrollment**

*By Kevin Abernathy, MPC General Manager*

Last year, the San Joaquin Valley Air Pollution Control District (Air District) approved a new pilot program for dairies, which provides $4 million of incentive funding to reduce emissions related to feeding activities. The Dairy Feed Mixing Electrification Program (Electrification Program) seeks to expand the installation of electric feed mixing equipment and reduce diesel emissions from tractors and other mobile equipment used on Valley dairies.

The Electrification Program covers up to 75 percent of costs for new projects. Completed applications must be sent to the Air District, with project approval based on total emissions reductions and cost-effectiveness of the plan. If you’ve considered replacing your feed mixing diesel equipment, this pilot program is designed for you.

The Air District will open the enrollment period soon, and MPC staff is ready to assist its members throughout the process. If you are considering installing an electric feed mixing system on your dairy, please contact me at kevin@milkproducers.org or 209-678-0666.

Read the Air District’s summary of the Electrification Program [here](#).

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**Immigration negotiations continue in Congress; MPC remains engaged**

*By Kevin Abernathy, MPC General Manager*

You’ve likely been following the immigration discussions in Washington, D.C. over the past week. We want our membership to know that MPC has been engaged in those discussions, participating through a broad agricultural coalition to represent the best interest of California dairy families. We will provide an update in future Friday Reports on developments and their impacts to you and your business.

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Guest Commentary: ‘Section 199A’ is most important tax reform for farmers and is in jeopardy  
By Kevin Abernathy, MPC General Manager

I want to share a letter I received in my inbox yesterday from dairy farmer and Select Milk Producers cooperative leader Mike McCloskey. In it he says that farmers are “about to lose the most important tax law in their lifetime,” a provision known as Section 199A. This provision of the recent tax reform provides a 20 percent deduction on a farm’s gross sales to a cooperative. McCloskey supports the idea that “all farmers, whether independent or cooperative, should receive the same tax treatment that cooperatives were granted in the new law.”

Below is an excerpt of the letter. You can read the entire letter here.

A piece of the new tax law, known as Section 199A, is the most important tax reform for the farming community in a generation. Unfortunately, Sec.199A has become needlessly controversial among the legislators who wrote and approved it, and among some agriculture companies who purchase farmers’ crops but are not organized as cooperatives. If a farmer belongs to a cooperative, he receives a federal tax deduction equivalent to 20% of the farm’s gross sales to the coop. In most cases, the amount of the deduction will allow farmers to have a substantially lower tax rate than in any other previous federal farm tax law. Farmers who do not belong to a cooperative do not receive this tax advantage, but they still may receive an advantage through the deduction created for pass-through companies.

Select supports the idea that all farmers, whether independent or cooperative, should receive the same tax treatment that cooperatives were granted in the new law. By attempting to compensate for the loss of the old Section199 Domestic Production Activities Deduction (DPAD) from which cooperative farmers have long benefited, Sec 199A creates a strong competitive tool - one which should be expanded to the entire farm sector. Select supports making minor adjustments as needed that would assure ALL farmers could participate without causing any significant additional loss of tax revenue.

CMAB District Meetings scheduled for January-March 2018

The California Milk Advisory Board (CMAB) will host winter district meetings throughout the state beginning next week through March. All dairy farmers are invited to attend their local district meeting, which includes a social, dinner and updates on CMAB programs and activities.

<table>
<thead>
<tr>
<th>District</th>
<th>Date</th>
<th>Venue</th>
</tr>
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<tbody>
<tr>
<td>1</td>
<td>Tuesday, January 30</td>
<td>Ridgetop Café, Fortuna</td>
</tr>
<tr>
<td>3</td>
<td>Thursday, February 1</td>
<td>Washoe House, Petaluma</td>
</tr>
<tr>
<td>7 &amp; 8</td>
<td>Wednesday, February 7</td>
<td>Kings Country Club, Hanford</td>
</tr>
<tr>
<td>9</td>
<td>Thursday, February 8</td>
<td>Tulare Golf Course</td>
</tr>
<tr>
<td>4</td>
<td>Tuesday, February 20</td>
<td>Rolling Hills Casino, Corning</td>
</tr>
<tr>
<td>5</td>
<td>Tuesday, February 27</td>
<td>Papapavlo’s, Stockton</td>
</tr>
<tr>
<td>10</td>
<td>Thursday, March 1</td>
<td>Benji’s, Bakersfield</td>
</tr>
<tr>
<td>*11</td>
<td>Tuesday, March 13</td>
<td>Mission Inn, Ho-o-Kan Room, Riverside</td>
</tr>
<tr>
<td>6</td>
<td>Thursday, March 15</td>
<td>Branding Iron, Merced</td>
</tr>
</tbody>
</table>

Social will begin at 6 p.m. with dinner/meeting to follow at 7 p.m.
*District 11 meeting will begin with social at 5:30 p.m. with dinner/meeting to follow at 6:30 p.m.

To RSVP, please email Kris Costa at kcosta@cmab.net or call/text 209.678.3466.