Milk Producers Council
5370 SCHAEFER AVE. SUITE A - CHINO, CA 91710 - (909) 628-6018 - Fax (909) 591-7328
E-mail: mpc@milkproducers.org Website: www.MilkProducersCouncil.org

DATE: January 23, 2009 PAGES: 3
TO: DIRECTORS & MEMBERS FROM: John Kaczor

MPC FRIDAY MARKET UPDATE

CHEESE MARKET COMMENTS: This week prices for barrel cheese on the CME moved up to the CCC support price, but block prices remained $.055 per lb below support. Still no offers of cheese to the CCC, but Dairy Market News say they hear some are expected, at least from the West. The amount of American cheese in cold storage at the end of December was 6% higher than a year earlier. Sales are reported to be moderate to retail outlets, but disappointing to food service (restaurant) customers. DMN reports that supplies of milk and condensed skim at prices below Class prices are still being offered and accepted by cheese plants.

BUTTER MARKET COMMENTS: Prices held fairly steady this week on the CME. No significant changes in sales are reported, but there are expectations for increased retail sales, which are offset by continuing weakness in food service orders. Approximately 25 truckloads of butter were sold by California plants to the CCC this week ($1.05 per lb). The amount of butter and other butterfat products in cold storage at the end of December was 23% lower than the previous December and 1% lower than the amount in storage at the end of November. According to DMN, surplus cream from bottling plants continues to move considerable distances to churning plants; it’s still a bit early for ramping up ice cream production, and the other heavy cream usage for holiday items has tailed off.

POWDER MARKET COMMENTS: Significant sales from California plants continue to be made to the CCC at $.80 per lb. Average prices for the two major weekly price series continue to hover just above the support price level. Current prices for export purposes are apparently at or below CCC support levels, which means relatively few new contracts for export of nonfat dry milk are being negotiated; skim milk powder (now eligible of CWT subsidies) should be filling that need. The stock of CCC held powder, available for sell back at $.88 per lb, is approaching 140 million lbs.

WHEY MARKET COMMENTS: Prices for dry whey continue to be weak and there is no perceptible increase in domestic or export demand at this time. Prices for whey protein concentrate remain relatively firm, although DMN reports that WPC from Canada, and more recently from South America, is entering the U.S. at competitive prices, presumably helped by the recently strong U.S. dollar. Lactose prices, and demand, remain very low.

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FRED DOUMA’S PRICE PROJECTIONS...

<table>
<thead>
<tr>
<th>Week</th>
<th>Quota cwt.</th>
<th>Overbase cwt.</th>
<th>Cls. 4a cwt.</th>
<th>Cls. 4b cwt.</th>
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<tr>
<td>Jan 23 Est</td>
<td>$12.11</td>
<td>$10.41</td>
<td>$ 9.53</td>
<td>$ 9.02</td>
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<tr>
<td>Last Week</td>
<td>$12.10</td>
<td>$10.40</td>
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URGENT ACTION NEEDED ON CCC PURCHASES OF CHEDDAR CHEESE: (By Rob Vandenheuvel)
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URGENT ACTION NEEDED ON CCC PURCHASES OF CHEDDAR CHEESE: (By Rob Vandenheuvel)
This week, MPC urged USDA to take immediate steps to fix the Dairy Product Price Support Program (DPPSP),
which was recently reauthorized by Congress in the 2008 Farm Bill. Under the DPPSP, the Commodity Credit Corporation (CCC) is authorized to purchase basic dairy commodities – such as butter, powder and cheese – at specified prices.

Congress set the CCC-purchase price for 40-lb blocks of cheddar cheese at $1.13 per pound. However, 40-lb blocks have traded below this level on the Chicago Mercantile Exchange (CME) every trading day in 2009. This week ended with the current price of $1.075 per lb, and last week it closed as low as $1.04 per lb. It’s important to remember that the price formulas in California are based on the CME price for 40-lb blocks, regardless of whether or not that price is below the CCC-purchase price.

So with the CCC willing to purchase cheese at $1.13 per pound, why are manufacturers willing to sell their products on the CME at a discounted price? The reason has to do with the different standards that CCC requires versus the standards cheese must meet to be traded on the CME spot market. Manufacturers are processing, grading and packaging their cheese to meet CME standards, and the CCC has made it their policy to maintain a separate standard for the cheese they purchase. So with the CCC unwilling to purchase perfectly-good cheese that meets the CME standard, we are left without any kind of “market support” for cheese. The “price support” program that Congress reauthorized just months ago is completely unable to keep cheese at or above $1.13 per lb.

What does this mean for California dairy farmers? Cheese on the CME has traded as low as $0.09 per lb below the CCC-purchase price. Plugging that price into our formula would result in a reduction in the class 4b price of $0.91 per cwt – or $0.39 per cwt on your overbase price. For a 1,000 cow dairy, that would be $7,600 per month that you’re losing because the CCC is unwilling to buy cheese at the price Congress authorized them to.

MPC has written USDA and our representatives in Congress urging them to take immediate steps to fix this problem and restore the DPPSP to what Congress intended it to be – a market for 40-lb blocks of cheddar cheese at $1.13 per lb. We believe CCC has the authority to begin purchasing cheese that meets the CME spot market standard. This adjustment would allow cheese to be sold to the CCC at $1.13 per pound and would clear the market of excess inventory.

National Milk Producers Federation (NMPF) has been pushing for this change as well, and we greatly appreciate their efforts. In order to make this change in CCC policy quickly, we also need our Federal legislators to apply pressure on USDA. Congress needs to hold USDA accountable for implementing the price support program as they intended in last year’s Farm Bill. I encourage all of you to contact your Congressman and ask for their help in urging USDA to make this change. Dairy families are already going through the worst economic times we’ve ever faced – the last thing we need is to lose more money because the Federal government is incapable of properly implementing the price support program Congress reauthorized just last year.

Here are the phone numbers to some of the Congressmen that represent dairies in California. If you live in a district other than one of these, please call MPC at (909) 628-6018 and we can get you the proper contact information.

<table>
<thead>
<tr>
<th>District</th>
<th>Congressman</th>
<th>Phone Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tulare</td>
<td>Rep. Devin Nunes</td>
<td>(202) 225-2523</td>
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<tr>
<td>Fresno</td>
<td>Rep. Jim Costa</td>
<td>(202) 225-3341</td>
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<tr>
<td>Modesto</td>
<td>Rep. Dennis Cardoza</td>
<td>(202) 225-6131</td>
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<tr>
<td>Bakersfield</td>
<td>Rep. Kevin McCarthy</td>
<td>(202) 225-2915</td>
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<tr>
<td>Ontario</td>
<td>Rep. Joe Baca</td>
<td>(202) 225-6161</td>
</tr>
<tr>
<td>Chino</td>
<td>Rep. Gary Miller</td>
<td>(202) 225-3201</td>
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DECEMBER MILK PRODUCTION AND WHAT MAY LIE AHEAD: (By J. Kaczor) What a difference a year makes. California milk production in December 2007 was 4.9% higher than the year before, with 48,000 more cows in the herd, which were producing 40 lbs more milk per month. That was then. In December 2008 milk production was 0.8% lower than December 2007, with 9,000 more cows, which were producing 25 lbs less milk than the year before. Of course, the reasons for this turn about included the hard decisions made necessary...
by higher costs, catastrophic prices, and dim prospects for timely recovery. Contributing factors included less usage of rBST, mandatory production controls, feed reformulations, aggressive culling, and business closures including those who used CWT’s spring herd retirement program.

Milk production in California has now been lower than year-earlier periods for five of the past six months. The number of cows on California dairies in 2008 was surprisingly steady, ranging from a low of 1,839,000 in January to 1,848,000 in May and June. **Production per cow has been lower than the previous year each month from July through December.** Because of relatively high participation by California producers in CWT’s second herd retirement program, and others electing to shut down on their own, the number of dairy cows in California in January and February is expected to be lower than the same months in 2008.

But prospects for milk prices in California will continue to be affected by what is happening in the rest of the country. **For the entire U.S., milk production in December increased by 1.4% over the previous December,** with 75,000 more cows producing 10 more lbs of milk for the month. Major increases in cow numbers were reported for Idaho, Kansas, and Texas. Major increases in production per cow were reported for Arizona, Missouri, New Mexico, Oregon, and Texas. Because of the huge fall in milk prices affecting all producers everywhere, it’s expected that a considerable number of producers beyond those included in CWT’s herd retirement program will shut down by Spring. That could come close to bringing the U.S. dairy herd down to or even below the numbers that were being milked in the early part of 2008. See the following article on what that could mean.

**WHY CHEESE PRICES COLLAPSED, AND WHAT COULD HELP THEM IMPROVE:** *(By J. Kaczor)*

This was one of the subjects of a roundtable discussion held during Wisconsin’s Agricultural Economic Outlook Forum on January 16th, which included University of Wisconsin Professors Ed Jesse, Brian Gould, Robert Cropp, and Dr. Larry Salathe, senior staff economist at USDA. While it doesn’t appear that the discussion uncovered anything not already known – a culmination of a number of things resulting in the perfect set of conditions for the price collapse – it did pinpoint a number of things relative to supply and demand that could bring about a much needed turn around, and therefore gives everyone who is interested something to focus on and hope for.

Two principal reasons were cited for the price collapse: a gradual increase in Cheddar cheese production at the time when domestic consumption began to decline and exports “tailed off,” and an over-reaction to that by buyers and sellers on the CME, amplified by the well known “thinness” of that market and its general usage as a basis for determining wholesale cheese prices. The following comments from the report are noteworthy: “...market fundamentals do not appear to be dismal enough to justify cheese prices under CCC support levels, especially in light of moderating milk production and an anticipated increase in domestic cheese sales in response to much lower wholesale cheese prices. A key factor is that cheese stocks are not out of line with commercial use, are not growing, and will likely decline as milk production falls and consumption increases.” “Prices [on the CME] increase only when there are unambiguous indications that supply is tightening.” (Note: prices on the CME increase for a number of reasons, but the general point made above is accepted.)

Regarding the supply side, three factors were mentioned that would stimulate a clear downward adjustment: (1) “extensive dairy farm attrition” (that means your neighbor, not you), (2) “substantial increase in culling” (that means you), and (3) “significant ration adjustments resulting in lower per-cow yields” (that means Arizona, Missouri, New Mexico, Oregon, Texas, and others). Factors that would help to increase a rapid increase in demand: (1) a quick retail price response to current wholesale prices, helped by extensive cheese promotions, (2) substitution of cheese for meat in meal planning, and (3) expanded federal cheese purchases for feeding programs.

It all appears to be straightforward and doable, but the recovery will have to overcome depressed consumer sentiment in the middle of the longest and most widespread, and deepest, economic recession in this country’s history. And when using cheese instead of meat, be sure to make that Cheddar, please.

*End*