NEWSFLASH!!!

SPECIAL REPORT: CALIFORNIA’S COOPERATIVES SUBMIT OFFICIAL PROPOSAL TO CREATE A CALIFORNIA FEDERAL ORDER: (By Rob Vandenheuvel) Normally around this time in the month, I would publish a brief article documenting the significant discount in California’s Class 4b price (for milk sold to California cheese plants) compared to the Federal Order Class III price that serves as a benchmark price for milk sold to cheese plants throughout the rest of the country. In order to keep our readers up to date, I will once again include the information here. This discount represented more than $450 million to California producers in 2014 alone, and more than $1.66 Billion since January 2010.

Fortunately this month, that’s not the end of the story! Today, it was officially announced by the U.S. Department of Agriculture (USDA) that they have received a proposal from California Dairies Inc., Dairy Farmers of America and Land O’Lakes to begin the process needed to create a Federal Milk Marketing Order in California. This marks the first time in our history that California’s major cooperatives – who collectively represent more than 75 percent of our State’s milk production – have asked to initiate this process. This is significant, as the ultimate approval of a Federal Order in California is subject to a referendum vote of dairy farmers (2/3 majority support is needed for approval), and USDA allows cooperatives the option of bloc voting on behalf of their members. The cooperatives’ support for this process has been the key to getting to this point.

In the coming days/weeks/months, there will undoubtedly be articles – both in this newsletter and other publications around the industry – taking a closer look at how Federal Orders operate in general, how the cooperatives’ specific proposal is similar/different to other Federal Orders around the country, and what the process is going forward. But in the meantime, here are some of the highlights:

Under the proposed Federal Order language submitted by CDI, DFA and LOL:

- California would have the same pricing formulas/system as all the other Federal Orders for all our classes of milk (no more “California discount”).
- The California quota program would continue as it is today, providing a monthly payment above the blend price to the owners of quota.
- The transportation and fortification subsidy programs – both currently part of the California system – would continue under the proposed California Federal Order.
- All California plants purchasing milk from California grade A dairy producers would be pool plants. Voluntary depooling of any class of milk will not be permitted. (There will undoubtedly be a lot more discussion in future articles about how pooling works and what this proposal means for producers and processors.)
- All dairy producers throughout California would receive the same blend price (notwithstanding the quota payments received by quota-holders), just as all California producers currently receive the same Overbase price.
There are obviously many more things we could talk about with regard to Federal Milk Marketing Orders, and specifically this proposal from CDI, DFA and LOL. And in future articles, we will begin to delve more deeply into some of those issues. But in the meantime, if you’d like to read more, you can find the actual proposal at: http://www.ams.usda.gov/AMSv1.0/CAOrder. Included in the links on that page are:

1. A 16-page cover letter, summarizing the proposal.
2. The 53-page proposal, with the actual regulatory language being proposed.

I would also refer you to a Q&A document published by USDA several months ago with answers to many of the questions about the process: http://www.ams.usda.gov/AMSv1.0/getfile?dDocName=STELPRDC5106626.

As noted on USDA’s website, between now and April 10th, they will be accepting any additional proposals regarding a potential Federal Order in California. They also plan to conduct a series of “public outreach meetings” in early May. Assuming that USDA does schedule a hearing on this issue, it will be a lengthy process that includes many day or weeks of hearings, and won’t likely conclude until sometime in 2016. While that feels like a very long time away, producers should none-the-less be very encouraged that this process is underway, and that we will finally have a chance to consider a much-needed alternative to the California state system that may have worked well for many years, but has refused to make the changes needed to provide a fair price for the milk you produce.

Producers will never get the $1.66 Billion back we have lost due to the California Discount, but this week marks the first step towards an alternative that can finally put an end to it. So stay tuned…

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**MPC FRIDAY MARKET UPDATE**

**CHICAGO CHEDDAR CHEESE**

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<tr>
<th>Blocks</th>
<th>+$.0025</th>
<th>$1.5350</th>
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<tbody>
<tr>
<td>Barrels</td>
<td>- $.0225</td>
<td>$1.4825</td>
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**CHICAGO AA BUTTER**

<table>
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<tr>
<th>Weekly Change</th>
<th>+$.0450</th>
<th>$1.7950</th>
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<tr>
<td>Weekly Average</td>
<td>+$.1580</td>
<td>$1.8075</td>
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**NON-FAT DRY MILK**

| Calif. Plants | $0.9676 | 19,829,109 |
| Nat’l Plants  | $0.9737 | 33,817,711 |

**DRY WHEY**

| Calif. Plants | $1.0120 | 12,530,493 |
| Nat’l Plants  | $1.0022 | 22,755,290 |

**FRED DOUMA’S PRICE PROJECTIONS…**

**Feb 6 Est:** Quota cwt. $15.76 Overbase cwt. $14.06 Cls. 4a cwt. $13.64 Cls. 4b cwt. $13.77

**Last week:** Quota cwt. $15.74 Overbase cwt. $14.04 Cls. 4a cwt. $13.62 Cls. 4b cwt. $13.75

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**MARKET COMMENTARY: (By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com)**

**Milk & Dairy Markets**

The dairy markets moved higher again this week as they continue to celebrate the potential for lower milk output in New Zealand. The bullish fervor intensified Tuesday in the wake of a very strong Global Dairy Trade (GDT) auction. Most Class III contracts settled around 40ȼ higher than last week. Class IV futures were even stronger, gaining 40 to 60ȼ. The mood was a little less festive in the CME spot market. Spot Cheddar blocks closed at $1.535/lb., up 0.25ȼ. Barrels slipped to $1.4825, down 2.25ȼ. Butter closed at $1.795, up 4.5ȼ from last Friday, but down notably from the mid-week high at $1.85. Spot nonfat dry milk (NDM) tumbled on Monday but then rallied and closed the week at $1.10, up 3ȼ on very heavy trading volume.

<table>
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<tr>
<th>CME Spot Prices</th>
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<tr>
<td>Cheddar Blocks</td>
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<tr>
<td>Cheddar Barrels</td>
</tr>
<tr>
<td>Butter</td>
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<tr>
<td>Grade A NDM</td>
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The Class III and cheese markets managed to keep the party going all the way to the closing bell, but the Class IV markets may already be feeling the hangover. Butter futures were particularly anemic toward the end of the week, with a number of contracts falling to their lower daily trading limit both Thursday and Friday.

Fonterra offered less product at the GDT than it had previously announced and this, coupled with concerns about lower output in the coming months, propelled the GDT index to gain 9.4%. Nearly all products moved higher, including whole milk powder (WMP), which jumped 19.2%. Skim milk powder (SMP) rallied 6.7% and butter climbed 6.1%. In contrast, Cheddar prices fell 11.1% to the lowest level ever at the GDT, equivalent to $1.20/lb.

New Zealand is indeed turning drier, but many key dairy areas are actually doing quite well. In the graphic below, the map on the right shows current soil moisture conditions as compared to normal (left) and last year (center). The North Island is only slightly drier than is typical at this time of year, and the western coast of the South Island is almost soggy. Producers in the driest areas have had at least some opportunity to irrigate, and supplemental feed is readily available. Low margins and dry pastures probably will reduce milk collections, but pockets of drought in the waning months of New Zealand’s season are unlikely to have an outsized impact on global dairy supplies in the long run.

U.S. dairy product output remains formidable. At over one billion pounds, December cheese production was record large and 2.5% greater than the year before. USDA revised its estimate of November butter output upward and reported December production at 167 million pounds, up 3.3% from last year. The fact that cheese and butter stocks waned in December points to robust demand. Exports contributed to the counter-seasonal decline in cheese inventories, but December butter exports were 63% lower than in December 2013. The butter market depends on domestic demand to remain firm.
Combined production of NDM and SMP reached 206 million pounds in December, up 12.3% from the year before and 9.7% greater than November on a daily average basis. Exports were 23% lower on both a month-to-month and year-over-year basis, and manufacturers’ stocks rose to 247 million lbs., a new record for the month. Given the large U.S. dairy herd, West Coast port strikes, the strong dollar and impressive milk powder exports in New Zealand over the past few months, U.S. milk powder inventories are likely to continue to grow.

Milk flows are strong in most of the country. Processors in Utah and Idaho are concerned about having the capacity to handle everything during the flush, according to Dairy Market News. There is no shortage of milk and cream for cheese vats and butter churns in the Midwest and Northeast. However, California milk output is reportedly lower than last year. It seems that heat and humidity in the fall took its toll on cows in the Golden State. Producers there have struggled to achieve the normal winter rebound in production per cow and conception rates.

Dairy producers culled 65,485 head in the week ending January 24, up 8.3% from the same week a year ago. After four weeks, 2015 slaughter is running 1.5% ahead of last year’s pace. Dairy producers are likely to step up cull rates as milk checks shrink. USDA announced the January Class III price at $16.18/cwt., down $1.64 from December and $4.97 lower than December 2013. The Class IV price, at $13.23, was down $3.47 from December and $9.06 below January 2013 levels. Class IV prices have not been this low since March 2010. California 4a milk slipped $3.48 from December to $13.09. 4b milk, at $13.75, was $1.03 below the December 4b price.

Grain Markets
A rising tide lifts all boats, and the grain complex was buoyed by strength in the broader markets this week. March corn gained nearly 16¢ and settled at $3.8575 per bushel. March soybeans added 12.5¢, reaching $9.735. The corn market is likely to remain range-bound although it has gained some support ahead of next week’s World Agricultural Supply and Demand Estimate report as the trade assumes that USDA will have to increase its estimate of U.S. corn exports. A decline in corn acreage this spring could mean lower corn stocks at the end of the 2015-16 season. Soybean prices are likely to slide in the long run, as back-to-back bin-busters in both the U.S. and South America will boost global oilseed supplies.

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A REMINDER FROM CDQAP ON WATER QUALITY REQUIREMENTS DURING THE WET SEASON: (By Kevin Abernathy, Director of Regulatory Affairs) With rains expected throughout the Central Valley this weekend, Dr. Deanne Meyer from the California Dairy Quality Assurance Program (CDQAP) drafted a “Winter Monitoring ‘To-Do’ List” with regard to the Central Valley Regional Water Board monitoring requirements. You can find Dr. Meyer’s list at: http://www.milkproducerscouncil.org/020615meyer.pdf. MPC members with any questions about this can contact me at 209-678-0666 or kevin.abernathy1@gmail.com.