MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE

<table>
<thead>
<tr>
<th></th>
<th>Blocks</th>
<th>Barrels</th>
</tr>
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<tbody>
<tr>
<td>Weekly</td>
<td>$1.300</td>
<td>$1.500</td>
</tr>
<tr>
<td>Average</td>
<td>$1.300</td>
<td>$1.700</td>
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CHICAGO AA BUTTER

<table>
<thead>
<tr>
<th></th>
<th>Weekly Change</th>
<th>Weekly Average</th>
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<tbody>
<tr>
<td>Blocks</td>
<td>$-1.550</td>
<td>$2.8950</td>
</tr>
<tr>
<td>Barrels</td>
<td>$-1.500</td>
<td>$2.9080</td>
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NON-FAT DRY MILK

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<tr>
<th></th>
<th>Calif. Plants</th>
<th>Nat’l Plants</th>
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<tbody>
<tr>
<td>Week Ending 9/26 &amp; 9/27</td>
<td>$1.4273/240</td>
<td>$1.4422/225</td>
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DRY WHEY

<table>
<thead>
<tr>
<th>Dairy Market News</th>
<th>National Plants</th>
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<tbody>
<tr>
<td>w/e 10/03/14</td>
<td>w/e 09/27/14</td>
</tr>
<tr>
<td>$.6050/240</td>
<td>$.6675/225</td>
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</table>

FRED DOUMA’S PRICE PROJECTIONS...

Oct 3 Est: Quota cwt. $23.28 Overbase cwt. $21.58 Cls. 4a cwt. $22.21 Cls. 4b cwt. $20.48
Sept ’14 Final: Quota cwt. $24.24 Overbase cwt. $22.54 Cls. 4a cwt. $22.72 Cls. 4b cwt. $22.39

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

Milk & Dairy Markets

Sellers came charging out of the gate on Monday, and the formerly formidable butter market suffered its worst loss in two years. CME spot butter lost 9¢ Monday and another 6.5¢ on Tuesday. But then it held at $2.895/lb., down 15.5¢ from last week. Butter futures were sharply lower in the first half of the week, including a more than 17¢ decline in the November futures contract on Wednesday under expanded trading limits. Butter futures regained some ground late in the week.

Pressure was no less intense in the Cheddar markets. Blocks and barrels lost 5¢ and 7.5¢, respectively, on Monday, marking their steepest decline since... last Friday. The wounded cheese market limped along for the rest of the week, sustaining more losses before a modest recovery on Friday. All told, both blocks and barrels shed 13¢ this week. Class III futures were sharply lower.

The milk powder market was quiet by comparison. CME spot nonfat dry milk (NDM) held steady at $1.395/lb. Class IV futures followed the butter market downward, with 2014 contracts settling at least a dollar lower. USDA announced the September Class IV milk price at $22.58, down $1.31 from August. The California 4a milk price for September was $22.72, $1.11 lower than the previous month. However, for most dairy producers, mailbox...
prices moved higher again last month. At $24.60, the September Class III milk price was $2.35 higher than August and the California 4b price of $22.39 was up $2.43.

While U.S. dairy producers are greeting their milk checks (and their bankers) with a smile, their competitors overseas are forced to grin and bear it. Pay-prices in Europe and Oceania are sharply lower than they were just a few months ago, and they are likely to diminish further as dairy product prices continue to fall. The Global Dairy Trade (GDT) index plunged another 7.3% on Tuesday. Every single product moved lower, and whole milk powder (WMP) prices dropped 10% to the lowest level since August 2009. Skim milk powder (SMP) prices fell 2.7% to their lowest level ever at the GDT. Butter also scored a new low for its tenure at the auction after dropping 6.6%.

The laws of supply and demand state that lower milk prices will result in increased demand and a reduction in supplies. In the long-run this is certainly true. But in the short-run, external factors can mitigate market signals. With prices falling, buyers who were sidelined by high prices are starting to restock their empty cupboards. But this may not be enough to offset declining demand from a couple major players. China is well supplied and Russia has closed her doors to much of the West. Russia will have trouble procuring an equal amount of cheese from politically favorable sources and will probably make do with less.

Meanwhile, global dairy production continues to rise. European processors have expressed hope that dairy producers will get the signal to slow production. Some will. But for those who have been adding cows and capacity in anticipation of the end of quota, such pleas are likely to fall on deaf ears. More than half of New Zealand’s annual milk production will occur between now and the end of January. Producers there are not going to start culling cows at the onset of the flush. If margins remain painful, they may reduce their herds in the off-season. But it will be some time before lower prices will meaningfully affect milk flows in New Zealand.

In the U.S., the market is not yet signaling to dairy producers that global supplies are burdensome. Domestic cheese and butter inventories are low, and the holiday buying season is upon us. This will likely cause volatility in those markets for the next six weeks. Thereafter, inventories are likely to grow and prices could head lower. Still, U.S. dairy producers are not likely to curtail production. Even if margins turn negative, producers will probably try to offset losses – at least initially – by making more milk. Given low feed costs and much-improved bank accounts, they could endure such losses for some time.

A decline in U.S. dairy product exports is likely to further pressure domestic dairy prices next year. Due to the
lag between contracting a sale and actual shipment, U.S. exports remained robust throughout the summer even as U.S. prices rose. With U.S. markets now vastly over-priced relative to those overseas, exports will be quite weak in the first half of next year. Butter and milk powder sales are already showing signs of fatigue. Butter exports in August were 60% lower than August 2013. NDM/SMP exports fell 10% from last year. Cheese exports remained strong. They were 11.4% greater than a year ago and were just 2.6% lower than in July.

USDA confirmed that high cream prices and competing manufacturers deterred butter production in August. Butter output dropped to 131.2 million pounds, down 4.3% from July and 2.4% less than in August 2013. Milk powder production was 6.8% greater than last year, and manufacturers shifted capacity back from NDM to SMP after a pronounced decline in SMP output in July. NDM stocks fell slightly from the record-high levels of July, but they remain 25% higher than last year.

Weekly dairy cow slaughter totaled 55,324 head in the week ending September 20, down 9.2% from the same week a year ago. So far, dairy culling has fallen 10.5% short of last year.

Grain Markets
Corn and soybean futures barely moved this week. Rains are delaying the harvest, but by all accounts the crop is huge. With the market focused on field reports, USDA’s quarterly Grain Stocks report met with little fanfare. Corn inventories on September 1, the beginning of the new crop year, were even larger than expected. There is certainly no shortage of grains. However, USDA estimated soybean stocks at just 92 million bushels, the lowest figure since the early 1970s. As a percentage of annual use, this soybean stocks number is by far the lowest on record. The soybean market could remain volatile as soybeans move from the combine to processors and exporters who have been anxiously awaiting the new crop.

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ANOTHER MONTHLY UPDATE: GOOD PRICES OVERALL, BUT STILL A HUGE CALIFORNIA DISCOUNT: (By Rob Vandenheuvel) Given the historically high milk prices paid in recent months, it’s easy to overlook the disparities in prices paid locally vs. around the country. However, with this week’s announcement of the final class prices for September, we see that the “California Discount” bestowed upon our State’s cheese manufacturers is alive and well.

Last month, California’s Class 4b price (for milk sold to CA cheese manufacturers) was $2.21 per hundredweight below the Federal Order Class III price (benchmark price for milk sold to cheese manufacturers around the country). Since 2010, the gap represents more than $1.5 Billion in forgone revenue that never made it into the California pool. What does that mean for the average CA dairy? If you’re a 1,000-cow dairy
producing 65 lbs of milk/cow/day, this $1.5 Billion represents nearly $880,000 since 2010 to your dairy alone!

The status quo is unacceptable, and only you as dairy producers pay the price of inaction. The three cooperatives have been developing a proposed California Federal Milk Marketing Order that could put California producers on an even playing field with their out-of-state colleagues. While we understand that is a lengthy process, producers need that effort to come to fruition so they can have that as a real option. We’ve heard that progress continues to be made on that front, so we look forward to those detailed discussions in the hopefully very near future.

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REMINDER: FINAL TWO MPC AREA MEETINGS NEXT WEEK TO DISCUSS MARGIN PROTECTION PROGRAM: (By Rob Vandenheuvel) As you all know, from now through November, U.S. dairies are able to sign up for the new “Margin Protection Program,” a Federal safety net program created in the 2014 Farm Bill. In an effort to bring our members up to speed on how the program works, what decision-making resources are available for the program, and how to sign up, we have scheduled a series of area meetings to delve into the issue.

Next week, we will hold the last two area meetings in this series. MPC invites our members, prospective members and allied industry partners to come out to any one of these meetings.

Tuesday, October 7, 11 am (lunch provided)  
Fresno Region: Maddox Dairy  
(12863 W. Kamm Avenue in Riverdale)

Wednesday, October 8, 1 pm  
Southern California: Chino Fairgrounds  
(5410 Edison Avenue in Chino)

In order to prepare for the meetings, RSVP’s are appreciated. Please send an email to rob@milkproducers.org or kevin@milkproducers.org to let us know you’re coming. We look forward to seeing you there!

![Difference between California 4b and Fed Order III](chart.png)