



Milk Producers Council

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MPC FRIDAY MARKET UPDATE

CHICAGO MERCANTILE EXCHANGE

Blocks +\$.0400 \$1.9550
Barrels +\$.0175 \$1.9175

CHICAGO AA BUTTER

Weekly Change - \$.0850 \$2.0050
Weekly Average -\$.0515 \$2.0465

NON-FAT DRY MILK

Week Ending 2/11 & 2/12

Calif. Plants \$1.3120 15,601,007
NASS Plants \$1.3614 17,310,034

Weekly Average

Blocks +\$.0565 \$1.9435
Barrels +\$.0580 \$1.9065

DRY WHEY

WEST MSTLY AVG w/e 02/11/11 \$.4663
NASS w/e 02/12/11 \$.4201

CHEESE MARKET COMMENTS: The amount by which prices increased this week on the CME were not impressive (blocks added \$.04 per lb; barrels added \$.0175 per lb) but the form and order of the activity was remarkable. Block prices advanced each day; all actions began with a bidder wanting cheese now, who was willing to offer a higher price for it. Block prices advanced Wednesday through Friday; all increases began with bids. Combined, there were five buyers and four sellers accounting for a modest total of 13 trades. Very fine; very orderly. There doesn't seem to be much on the negative side of the equation: the record high cold storage volumes are not a secret; international prices are steady in Oceania and very firm (and high) in Europe; cheese production in those regions is mostly accounted for by buyer-seller contracts. On the other hand, imports could increase (they were down sharply last year), exports could decrease (domestic sales are now very attractive compared what is involved with having to export the stuff), and consumers could turn away from the higher prices (the CPI food index is moving up). CME's class III milk futures prices for the March through June period did decrease this week, but most if not all of the decreases occurred today, the day before a three day weekend, which is not an unusual thing to happen. And besides, the resulting prices more than fully support cheese prices at least \$.10 per lb higher than they presently are. And for those who are concerned about that mythical \$.03 per lb spread between blocks and barrels, don't fret: it's no longer a usable benchmark. Rarely in the past four years has the weekly average difference between the two styles of cheese closed at a \$.03 per lb difference, and differences of \$.04 or more per lb **in either direction** far exceed all that closed with lesser differentials than that. It's self correcting, one way or another.

BUTTER MARKET COMMENTS: What should one think when a manufacturer who is known to be a major exporter of butter begins to take butter to the CME and offer it at a price lower than the existing price? A reasonable conclusion would be that exports may be slowing down or that company simply produced too much butter in recent weeks. For whatever the reason, butter prices have now fallen 6 straight trading days – all from offers. This week, 3 carloads were sold. The price lost \$.06 per lb. \$2.005 per lb for butter in mid February is not to be considered a calamity, but there are signs that the tightness of supply in the U.S. may be nearing an end. Butter production has increased four months in a row through December and is almost sure to have increased even more in January. A lot of people will be looking closely at January's production, exports, and end of month inventories. Virtually all of the price increases from the past two months have been passed through to retailers or end users. Interestingly enough, even as the butter price lost some ground this week, cash-settled butter futures prices increased for the April through September period, and the week's trading activity ended with a bid to buy which moved the price \$.005 per lb higher (was that strategy or need? you decide).

POWDER MARKET COMMENTS: Offers and bids moved powder prices up this week to levels rarely seen on the CME. Spot prices for grade A closed the week at \$1.83 per lb; extra grade closed at \$1.80 per lb. NFDN futures prices also advanced for all months through October; they average \$1.65 per lb. Prices also were higher for the two major sales reporting series for shipments made last week (see them above). The California plant average price is now the highest it's been since January 2010, and is not far below where it was two years before

that. Production is about steady, with demand for condensed skim affecting plants' output objectives. Spot prices again moved sharply higher, although it appears most of the sales at the high end of the range continue to be resales. The market for nonfat powders is reported to be firm, and supplies to all but those with contracts are limited. Prices and demand for buttermilk powder and whole milk powder are firm and have increased somewhat this week. Production of both products is reported to be lower than what was planned because of demand for condensed fluid products.

WHEY PRODUCTS MARKET COMMENTS: Export demand remains strong; stocks remain tight; prices continue to increase. That explains the condition of the markets for dry whey and commodity grade whey protein concentrates. A large portion of production of both products is being sold solely under existing contracts. Attempts to negotiate positions are on-going. The NASS average price has now gained \$.025 per lb over the past three weeks. The west's "mostly" price is now averaging \$.4663 per lb, up \$.035 for the week.

FRED DOUMA'S PRICE PROJECTIONS...

Feb 18 Est:	Quota cwt. \$18.31	Overbase cwt. \$16.61	Cls. 4a cwt. \$17.63	Cls. 4b cwt. \$16.90
Last Week:	Quota cwt. \$18.26	Overbase cwt. \$16.56	Cls. 4a cwt. \$17.66	Cls. 4b cwt. \$16.75

ONCE AGAIN, MORE COWS AND MORE MILK – JANUARY'S MILK PRODUCTION REPORT:

(By J. Kaczor) As they do every February, USDA gathered up additional reports for the previous year and sorted out discrepancies, and in the process found a few thousand more milk cows, a bit more milk per cow, and more milk than had been reported earlier. The changes are important but not significant, although the estimate for December's milk production was lowered a bit, which reduced the increase over the previous year from 2.5% to 2.4%. (Economists use the revised numbers to fine tune their industry models which, we all hope, will make them better forecasters.)

The more important part of this monthly report always is what's happening in recent months – in order to either verify what was believed at the time, to help explain unusual events, and to try to get a sense what may be happening now and what may happen next. The reference to more cows means the national herd grew by 16,000 cows in January, on top of the 16,000 that were added in December. USDA reports January's herd is larger than a year ago by 68,000. Production per cow increased by 25 lbs per cow for the month, which is a little less than the increase reported for last January. Total milk production is reported to be 235 million lbs more than December and 365 million lbs more than last January. The year to year increase amounts to 2.28%.

While the increase in number of milk cows in December was a surprise, this month's report was not. About 50,000 more dairy cows were culled in November and December than a year earlier; they were replaced with 66,000 fresh cows. In January about 35,000 more cows were culled than a year earlier (back then CWT's herd retirement program was busy clearing some away) and they were replaced with 51,000 fresh cows. Producers can count; high beef prices and relatively low heifer prices apparently add up to short term profits per trade-out. CDFA's cost of production figures show a high rate of culling in California. But what about the additional cows? That's answered by noting producers can also see and read about the higher milk prices coming on fast. It looks like the race between higher milk prices and higher feed costs is where our eyes should be focused. Considering the near all time record increase in production per cow last year, this year's increase per cow should be considerably lower. January's increase was 5 lbs per cow lower than where last year began.

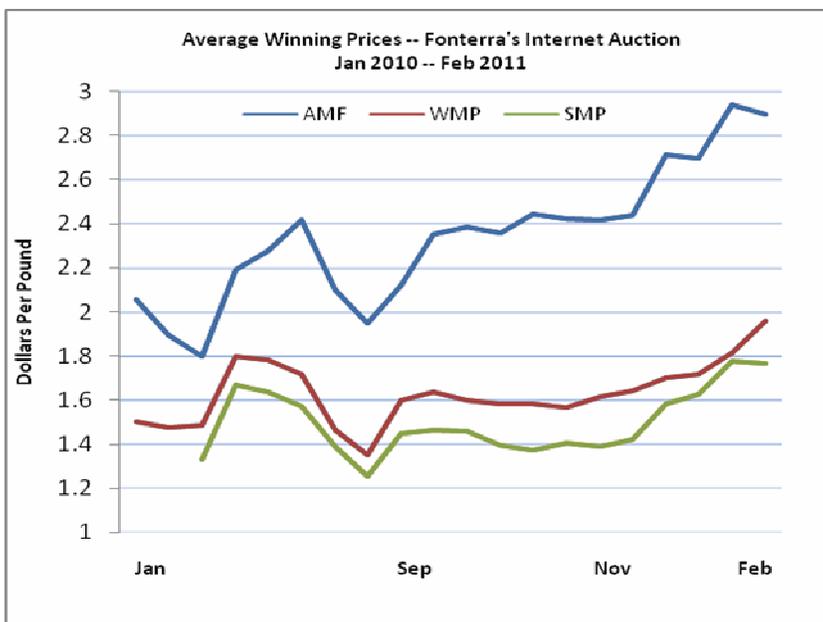
The twenty-three largest milk producing states had 82,000 more cows than a year ago. That means the large are getting larger and the twenty-seven smaller producing states are going the other way, milking 14,000 fewer cows than twelve months ago. Once again, California and four (smaller) Midwestern states are the only ones among the 23 largest producers who still (or, now) have fewer dairy cows than they had a year ago. California's production per cow in January increased by 25 lbs, about the average of the other 22 largest producers, and was exceeded by only 5 others.

That additional amount of milk means, of course, that more butter, powder, and cheese will have been produced in January than a year earlier and a month ago. The milk collection system works; let's hope some thought was put into where it went and what was done with it. That report will be available about two weeks from now.

FONTERRA'S MID-MONTH AUCTION RESULTS SHOW MORE PRICE INCREASES, REFLECTING CONTINUING STRONG DEMAND: (By J. Kaczor) Prices bid for anhydrous milkfat, after climbing fairly steadily since the August 3, 2010, auction, gave up some of the gains in this week's mid-month auction. AMF prices were lower for all three of the contracts, which cover deliveries from April through October. The price for skim milk powder gained \$.06 per lb for April deliveries, but lost a few cents for the other months. Prices for whole milk powder were sharply higher for all three contracts, gaining \$.16, \$.17, and \$.09 per lb, respectively. One hundred and twelve bidders participated; 68 were successful.

The graph shown here updates the previous graph, and now shows the results of twenty auctions held over the past fourteen months. (Two auctions per month began in September.)

In the auction review two weeks ago, a discussion about whether the recent price increases were sustainable pointed out some similarities and differences between the current situation and what was happening in 2007-2008 when prices for virtually all dairy and non-dairy commodities sky-rocketed. Since then, there are some signs that at least some of the supply shortages of butterfat (or the demand for it) is changing. Butter prices on the CME have edged downward in the past six trading days, and the prices bid for AMF



in the global auction this week also eased back, but are still well above equivalent prices for butter (which is about \$2.36 per lb for April, 2011). Based on the other results, it appears WMP demand (at least relative to supply) is very strong and SMP demand is at least steady at recent levels. The SMP prices over all three contracts is virtually flat, averaging \$1.77 per lb – April's price is \$.10 per lb above the CME NFDN futures price for that month, the May-July price is \$.04 per lb above the CME, and the three outlying months' price is more than \$.15 above the somewhat less sure CME prices for those same months.

The good news is that there are reasons to believe prices like those shown on this graph, as well as Dairy Market News reports of similar prices for export in Europe and our own experience with virtual across the board increases for all dairy commodities, could be around at least through mid-year and maybe longer. Stories from Australia and New Zealand this week are definitely bullish about prices. By far, the major reason for last year's increase in demand for whole milk powder is China, but other, oil-rich countries in Asia and Africa, are also showing increasing interest in using more of a full line of dairy commodities.

Fonterra is the major benefactor of the Chinese demand, and all other suppliers benefit at least indirectly from a shortening of supply that results from that major supplier filling that major increase in demand. China increased its imports of WMP by more than 400,000 metric tons last year and Fonterra doesn't appear to expect that demand source to be much different this year. *Bloomberg News* this week says Fonterra's CEO believes WMP prices "will likely" remain above 50% of their historical averages over the foreseeable period. "Higher prices are the new normal," says Mr. Ferrier. Even if that is so, the road ahead should not be considered to be necessarily smooth. A related story from Australia, referring to steady global demand and limited supplies, says prices are approaching buyer resistance levels, and an economist at the *Bank of New Zealand* points out a dairy industry truism: "When you get quite a tight market and stocks are on the low side, it doesn't take much of a change in outlook of supply to create volatility. You'd be unwise to think...volatility isn't going to be around for a while." So, once again, it seems merely to be a matter of supply and demand and who is better situated for getting the business. On that note, the weakness in the U.S. dollar continues to make U.S.-sourced dairy products an attractive option. But do keep an eye on how much more milk may be produced in New Zealand and Australia from July forward; both countries are poised for substantial rebounds from this year's disappointing output.