MPC WEEKLY FRIDAY REPORT

DATE: JUNE 26, 2020
TO: DIRECTORS & MEMBERS
FROM: KEVIN ABERNATHY, GENERAL MANAGER
PAGES: 9

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MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE		
Blocks	*- $.0750*	$2.5750
Barrels	*+ $.1150*	$2.4000
WEEKLY AVERAGE CHEDDAR CHEESE		
Blocks	*+ $.1185*	$2.6485
Barrels	*+ $.0705*	$2.3785

CHICAGO AA BUTTER		
WEEKLY CHANGE	*- $.0850*	$1.7650
WEEKLY AVERAGE	*- $.0330*	$1.7925
DRY WHEY		
DAIRY MARKET NEWS	W/E 06/26/20	**$.3500**
NATIONAL PLANTS	W/E 06/20/20	**$.3553**

NON-FAT DRY MILK		
WEEK ENDING 06/20/20		
NAT'L PLANTS	**$0.9200**	17,221,431
PRIOR WEEK ENDING 06/13/20		
NAT'L PLANTS	$0.9047	26,385,681

CALIFORNIA FEDERAL MILK MARKETING ORDER PRICE PROJECTIONS

PRICE PROJECTIONS	CLASS I ACTUAL (*RANGE BASED ON LOCATION*)	CLASS II PROJECTED	CLASS III PROJECTED	CLASS IV PROJECTED
JUNE 26 EST	**$13.02 - $13.52**	**$13.04**	**$20.93**	**$13.02**
LAST WEEK	**$13.02 - $13.52**	**$13.19**	**$20.99**	**$13.34**

Milk, dairy and grain market commentary

By Sarina Sharp, Daily Dairy Report
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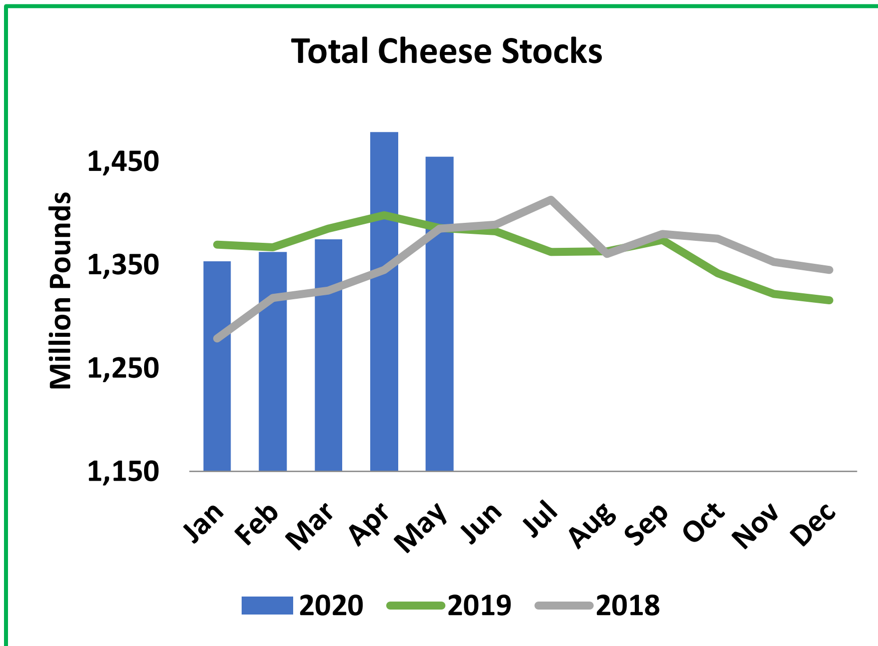
Milk & Dairy Markets

The fireworks boomed on LaSalle Street a week ahead of schedule. CME spot Cheddar blocks rocketed to an all-time high at $2.81 per pound. Then they flamed out, fading to $2.575, down more than 12¢ from the highs and 7.5¢ lower than last Friday. Barrels rallied 11.5¢ this week to $2.40, only 2.5¢ off the record high set earlier this month. Fears that the meteoric rise was all sparkle and no substance were doused by buyer's willingness to step in and make a purchase, rather than sit on the sidelines and let the selloff run its course. Four loads of blocks changed hands on Thursday and Friday at $2.575, confirming that end users are still ready to pay historically high prices for cheese. The

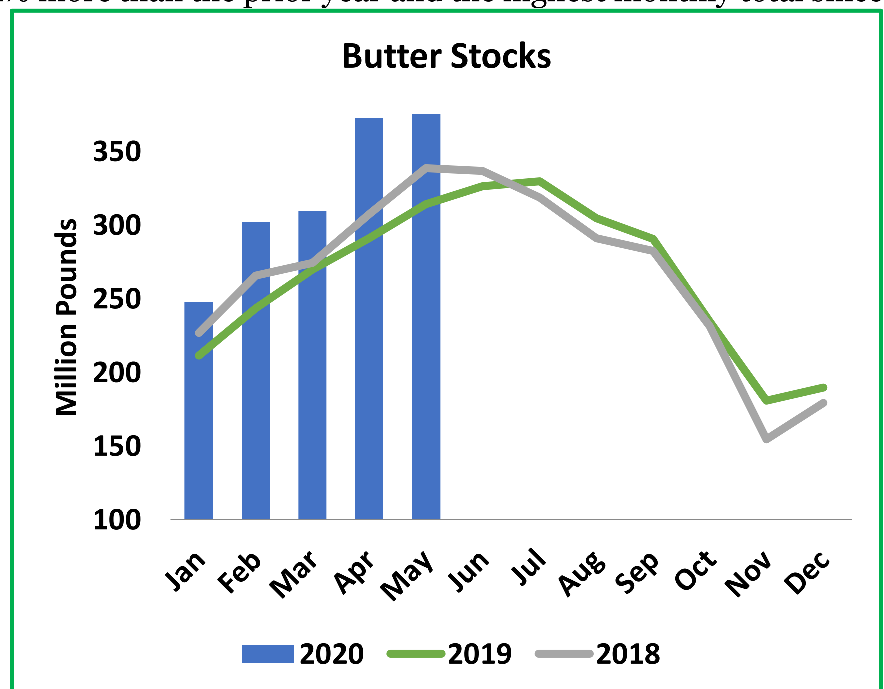


mid-week highs lifted the weekly Cheddar block average 11.85¢ above the already lofty values established the week before. Weekly average spot values help to set the final price for July Class III milk.

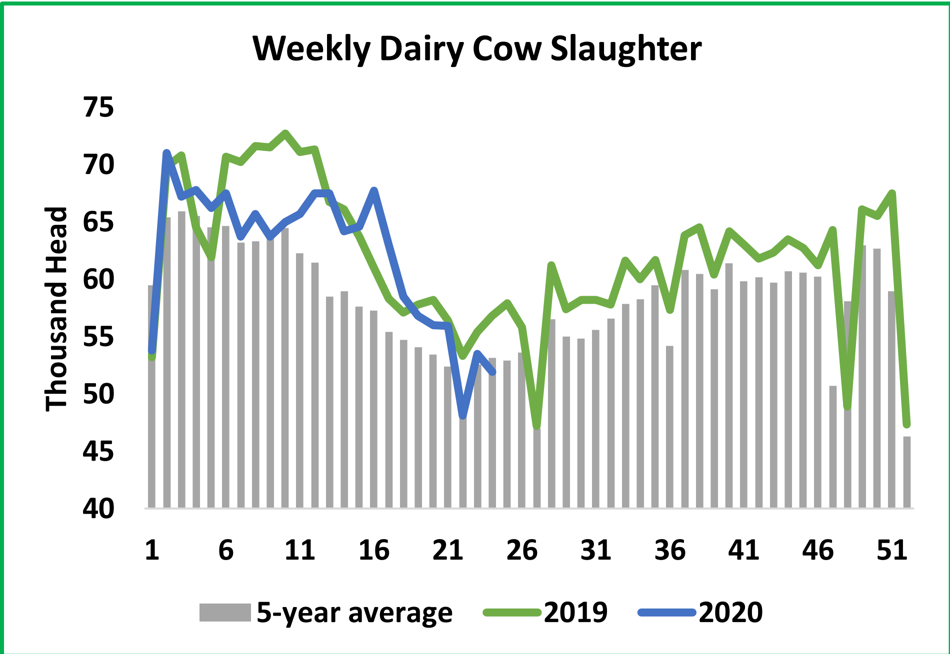
Cheese inventories typically grow in the spring, but this year they fell 1.6% from April 30 to May 31 thanks to the strong draw from retailers and from restaurants readying to reopen. Still, at 1.45 billion pounds, cheese inventories were 5% greater than in May 2019. There is a mountain of aging cheese in storage, and there are signs that the fresh cheese shortage is starting to ease. While at least one buyer stepped into the fray of the spot markets, others were more reticent. Meanwhile, milk is noticeably easier to come by in the Upper Midwest. Cheesemakers paid steep premiums for spot milk in the first three weeks of June, but now they are buying at a discount, which suggests they have all the milk they need even as some plants run seven-day work weeks. Across the nation, processors are fortifying with powders to boost throughput. The industry is likely to have more than enough cheese later this year.

With cheese vats full to the brim, whey output is going strong and inventories are building. CME spot whey slipped 1.5¢ this week to 31.25¢. Most Class III futures finished deep in the red. However, the July contract cheered the spot market spectacle and climbed 46¢ this week to $21.64 per cwt.

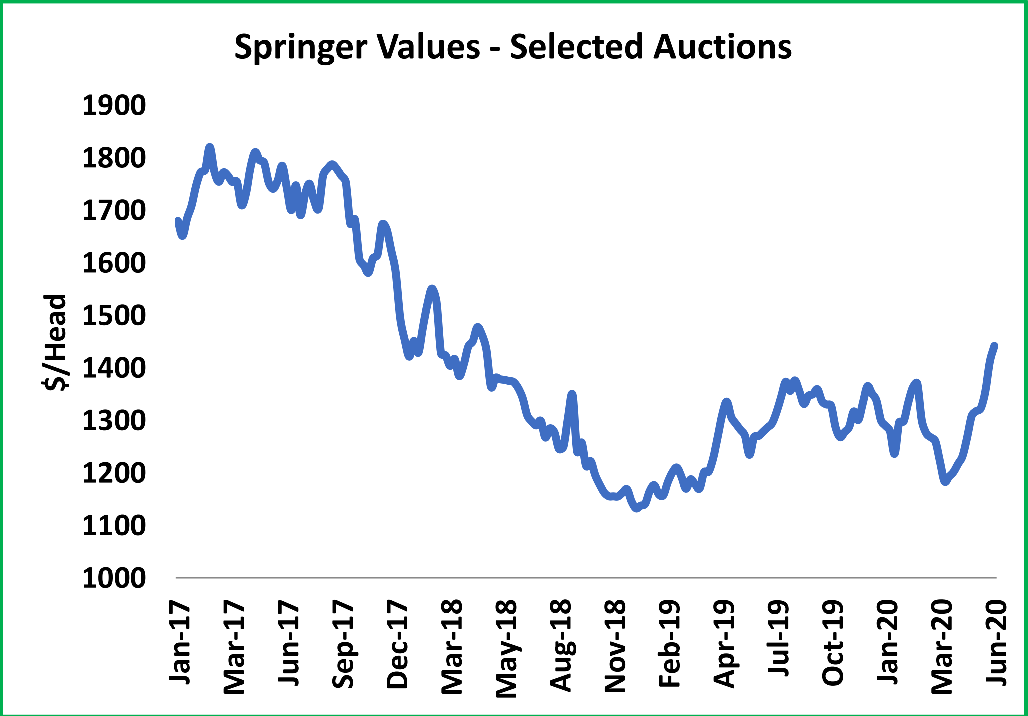
The other spot markets fizzled. Spot butter tumbled 8.5¢ to $1.765. There were 380.2 million pounds of butter in cold storage on May 31, 21.2% more than the prior year and the highest monthly total since 1993. Butter makers are trying to pare down stocks by cutting and wrapping blocks into retail-friendly packaging, as food service demand for bulk butter is limited. Churns are mostly idle as ice cream and cream cheese production is keeping cream values out of reach.



CME spot nonfat dry milk (NDM) dropped 1.25¢ to $1.02. Milk powder buyers seem inclined to wait for prices to break before stepping up their purchases. With both butter and powder losing ground, Class IV slumped. Second-half futures contracts lost an average of 56¢ this week. June, July, and August futures are floundering below $15.



It is difficult to slam on the brakes in the spring and then open the throttle in the summer. But $20 milk is a powerful motivator, and dairy producers are doing their darnedest. Whatever they did to reduce milk output – feeding a cheaper ration, drying early, culling aggressively, or milking less frequently – they are undoing today. The industry cannot fill the parlor and the bulk tank immediately, but the impact of this new trajectory will surely add up to more cows and more milk over time. In the three weeks ending June 13, dairy slaughter volumes have fallen 12% behind the 2019 pace, an about-face from April and early May, when slaughter accelerated to a 34-year high. Springers are selling for the highest values in more than two years, which suggests that dairy producers are anxious to fill every stall. Processing capacity and heifer inventories are likely to put a ceiling on expansion eventually, but the industry is clearly leaning in that direction. After another dismal spring, dairy producers have surely earned the thrill of a big summer milk check, and they should milk it for all its worth. But it seems likely that the industry will overdo it and wake up from this celebratory season with a harrowing hangover.



Grain Markets

The grain markets took a big step back this week. September corn futures dropped 18¢ this week to $3.1925 per bushel, near the life-of-contract low. August soybeans settled at $8.60, down 16¢. After widespread rains, crops are thriving. The Corn Belt's two-week forecast looks nearly ideal. Meanwhile, demand is in question. The U.S. and China are at odds on international diplomacy, and Beijing has tacitly warned U.S. officials that this could put Phase One agricultural purchases in jeopardy. China has already cleaned out Brazil's soy stocks and will have to shop in the U.S. eventually. But these geopolitical disagreements give China every incentive to slow purchases to gain leverage. The feed markets are caught in the crossfire.

Volatility in the new world of the California Federal Order

By Geoff Vanden Heuvel, Director of Regulatory and Economic Affairs
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It may seem obvious, but it bears repeating that the price of milk a dairyman receives is based on the value of the products that are made from that milk. California now operates under a Federal Milk Marketing Order (FMMO), which is very different from the old California State Order. Under the California State Order, the proceeds from nearly all the milk produced and sold in the state were rolled into one pot of money. That money was then distributed out to all the California producers based on their share of that pot and their quota holdings. If you were a Grade A milk buyer in California, the minimum price you had to pay for milk was dictated by the California Department of Food and Agriculture (CDFA). With a few exceptions, the proceeds from those purchases were not directly distributed to their producers, but were pooled with all the other milk in California. There were consequences to having the rules structured in this way. For one thing, because CDFA was using the power of the government to set and enforce the milk price processors were required to pay, it was extremely sensitive to setting that minimum price too high. The second consequence is that because the milk prices were lower and because nearly all the milk money was pooled, processors did not have to worry too much about being competitive with other processors.

The Federal Order program rules create a very different competitive environment. For one thing, in the FMMO, only Class I milk must pay a minimum price and pay its money into the common pool. For the other classes of milk, pooling is optional. This means that the handlers of non-Class I milk can decide every month whether they want that milk to be associated with the pool. The only reason to associate with the pool is to get a share of the Class I money that is in the pool. Because the government is not forcing anyone into the pool (since associating with the pool is voluntary), it is much less sensitive to setting minimum prices for cheese milk and butter/powder milk at levels that are favorable to processors.

You might wonder if paying minimum prices is not mandatory, what is their use in the market? Mostly, the Class III (cheese) and Class IV (butter/powder) prices serve as benchmarks in the contracts that producers and cooperatives have with processors. Secondly, because cheesemakers and butter/powder processors have the option to not pool and keep the money if their prices are higher, there is a built-in opportunity for competition between processors for who is in the best position to pay higher prices to producers. The other rule in the FMMO is that cooperatives can, and often do, act as the handler who decides whether to pool, rather than the actual cheesemaker or butter/powder maker.

In the FMMO, who you sell your milk to matters a great deal to the price you get paid for that milk. California producers found this out right away when the FMMO started in November 2018. At that time, the Class IV price was quite a bit higher than the Class III price, and consequently, handlers that were weighted more heavily to Class IV were able to out-pay handlers that were weighted more toward cheese. Suddenly producers had a reason to start paying attention to where their milk was being sold. In the processing community, that competition forced everyone to sharpen their pencils and think about how to best position themselves for the new competitive environment.

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Enter 2020 – the most bizarre year in any of our collective memories, not just in the dairy industry, but in life. Everything we thought about the world six months ago has been turned upside down. In the last 60 days we have seen cash cheese prices go from a low of $1 per pound to $2.81 per pound and then begin to fall. There have been price swings for the other classes of milk as well, but not near as great as what has happened to cheese prices. As these volatile prices work their way through the FMMO formulas, and as the impact of these prices filter through the competitive environment that is the California dairy industry, there will be those who will see much higher milk prices than others in the near term. The three major cooperatives in California are all committed to paying their producers consistent with the FMMO published blend price, but that blend price will be highly impacted by the reality that almost no cheese milk will be associated with the pool. In addition, the Class I prices for June were set based on cheese, butter and powder prices from the first two weeks of May – before cheese prices took off. Therefore, the June Class I price is low. Because of this, the pay prices of the individual cooperatives will no doubt be quite variable for June depending on how they decide to distribute the money they will receive or earn from the milk they handled for their members.

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All three cooperatives have some exposure to both Class III and Class IV buyers, but that exposure is not identical. California also has several processors who buy milk from independent producers. Most of those processors are either cheese companies or powder manufacturers and pay their producers accordingly. Obviously, the cheese plants are in a much better position to pay higher milk prices than the powder plants under current market conditions. But cheese and butter/powder prices do tend to converge over time. When cheese is this much higher in value compared to powder, cheese plants begin to purchase powder to add into their cheese vats to increase cheese production. This increases the cheese supply and tightens the powder supply which tends to bring the values of these two into closer balance.

So, what can you do about this? In the short term, not much. It is a good thing that cheese prices have rebounded. A rising tide lifts all boats. But unlike the tide, not all boats will rise at the same rate. This will create differences in producer pay prices. But these experiences will force producers and processors alike to evaluate vulnerabilities and threats as well as opportunities and strategies for how to protect and profit from the challenges we are facing today. Isn't that what a free people do? We learn, we adjust, we adapt, and we get better. Yes, there will be some pain and collateral damage. But the FMMO structure provides an amazing amount of market freedom to incentivize improvement across the board.

Also, there are now some risk management tools that were not available in the past, like the Dairy Revenue Protection crop insurance program that is available to every producer. We know these remarkably high cheese prices are not likely to last forever. So, getting some protection from that future risk is certainly something producers should consider doing. One other thing to keep in mind is the rules that are in place in California now, are the same rules that apply to our competition in the rest of the country. How we respond to these challenges is really our test. While 2020 is certainly a crazy year, eventually all waves pass over and storms quiet down. What we learn from these experiences can make

us better. Dairy farmers are an amazingly resilient group and I have no doubt we will survive this calamity and that better days are ahead.

National Milk Producers Federation President's Update

Courtesy of Jim Mulhern, National Milk Producers Federation

NMPF Asks USDA to Reassess CFAP Payment Limits – After working hard to successfully change the initial CFAP program payment limits proposed by USDA, we've now had to raise concerns about the way USDA's county FSA offices are interpreting the revised payment limits that were included in the final plan.

This week we wrote to Agriculture Secretary Sonny Perdue, asking that USDA expand its interpretation of the three entity/$750,000 total payment limit. **We remain concerned that a strict interpretation is hurting the ability of family dairy operations to fully benefit** from the CFAP, as we continue to hear reports that local Farm Service Agency offices are not accommodating some farm business structures, including those established as trusts.

The letter reminds USDA that there is no statutory provision to require any payment limitation due to farmers having more complex operating structures. We also reiterated our concern that seasonal dairy operations are disadvantaged by the use of the first three months of the year as the production base for the payments. We hope USDA will revise some of the restrictive interpretations being implemented across the country, and if not, it is possible Congress may weigh in to direct the agency to reassess its CFAP procedures.

In USDA's weekly update from Monday, the department reported that it has now distributed one-quarter of the total $16 billion allocated for the CFAP program. **Just over 15,000 dairy farmers have received nearly $900 million of the $4 billion** being paid to date for all commodities. Other livestock producers split $2 billion, with farmers of row crops receiving about $1 billion.

In addition to good news in the form of the direct payments, **the markets are suggesting that the worst of the coronavirus-induced plunge in the dairy economy may be over.** The next steps in the recovery are the subject of this month's NMPF *Dairy Market Report*, which tracks the rebound that began in May and is continuing into June. This market turnaround has been caused by actions that have reduced milk supply and strengthened dairy product demand.

The author of the *Dairy Market Report*, **our chief economist Peter Vitaliano, further explains in this podcast that the rebound in cash market prices was driven by the dramatic cutbacks in farm-level milk output** earlier in the spring, coupled with retail store demand and government product purchases supplanting the drop-off in foodservice sales. He said the continued spread of the coronavirus and whether milk production increases remain in check are significant questions that will affect dairy's further recovery.

New NMPF Task Force Considers Ways to Improve Producer Payment Guarantees – The latest effort National Milk is undertaking to shore up the economic situation of farmers and their cooperatives is exploring what changes may be needed to ensure that in the face of a processor bankruptcy, co-ops and Federal Milk Marketing Order (FMMO) producer settlement pools can recover money not paid to them.

The task force was set up by NMPF Chairman Randy Mooney at the June NMPF Board meeting in response to concerns from member co-ops that had been shorted by Dean Foods failure to make final payments for April 2020 milk to co-ops and FMMO pools. We convened the first meeting this week of the new task force to examine what can be done to ensure payments to producers in the event of handler bankruptcies.

The task force will examine options and offer recommendations for our Board to consider, both about the immediate concerns regarding the Dean Foods situation, and also on opportunities to work with USDA or Congress to prevent farmers from being harmed in the future by handlers failing to meet their payment obligations.

Growing Climate Solutions Bill Earns Positive Marks in Senate Hearing – The new bill intended to help establish the terms of a carbon credit market for agricultural producers received positive responses during a Senate hearing Wednesday. Witnesses ranging from Land O'Lakes/Truterra to the American Farm Bureau to the National Farmers Union agreed that having USDA play a central role in verifying farm-centered carbon reduction practices is essential to establishing a viable carbon credit market.

A bipartisan coalition of senators introduced the Growing Climate Solutions Act earlier this month, and a House companion version debuted this week as well. The bill is designed to accelerate the growth of ag carbon credit trading by authorizing USDA to certify third-party verifiers and technical service providers. The third-party verifiers will in turn certify the validity of credit-generating farm practices.

NMPF supports the bi-partisan legislation and provided the committee a statement for the hearing record. Several lawmakers stressed the need for the carbon credit system to benefit farmers, not just carbon brokers or food marketers seeking a marketing advantage. NMPF supports this approach, as a well-regulated carbon market will play an important role in the dairy sector's goal of achieving net-zero emissions by 2050.

U.S., UK Finish Second Week of Talks – Trade negotiations between the U.S. and the United Kingdom continued this week, as trade negotiators attempt to reach a consensus on dozens of contentious issues to achieve a bilateral free trade agreement. As we wait to see what progress is being made, here's a reminder of the dairy-specific issues we have asked our government to address:

- Remove geographical indication restrictions preventing the U.S. from selling common cheese types with names in wide-spread usage to the UK and establish robust safeguards for the use of common food names.
- Recognize the safety of the U.S. dairy product system and eliminate unscientific requirements that unduly burden commerce without a genuine food safety basis.
- Establish enforceable commitments for sanitary and phytosanitary standards and technical barriers to trade.
- Simplify and streamline border administration measures for dairy tariff rate quota management and licensing procedures.

- Establish rules of origin that focus the benefits of the agreement on the dairy sectors of the U.S. and the UK and do not allow for the EU dairy industry to utilize the UK as a processing hub for exporting their milk to the U.S.
- Provided non-tariff concerns addressed, eliminate dairy tariffs in a coordinated manner.

We continue to provide input to the U.S. Trade Representative's office about the need to favorably resolve these issues as the talks continue.

Prevent heat illness with water, rest, shade

Courtesy of the State of California Department of Industrial Relations

Cal/OSHA is reminding all employers with outdoor workers to review high heat advisories in effect across California and to take steps to prevent heat illness.

California's heat illness prevention standard applies to all outdoor workers, including those in agriculture, construction, landscaping and those that spend a significant amount of time working outdoors such as security guards and groundskeepers, or in non-air-conditioned vehicles such as transportation and delivery drivers.

Employers with outdoor workers must take the following steps to prevent heat illness:

- **Plan** – Develop and implement an effective written heat illness prevention plan that includes emergency response procedures.
- **Training** – Train all employees and supervisors on heat illness prevention.
- **Water** – Provide drinking water that is fresh, pure, suitably cool and free of charge so that each worker can drink at least 1 quart per hour, and encourage workers to do so.
- **Shade** – Provide shade when workers request it or when temperatures exceed 80 degrees. Encourage workers to take a cool-down rest in the shade for at least five minutes when they feel the need to do so. They should not wait until they feel sick to cool down.

To read more about precautions employers should take during high heat situations, please visit this link.

New California COVID Assessment Tool available

Courtesy of the Governor's Press Office

Governor Gavin Newsom on Thursday released tools, technology, and data that will allow scientists, researchers, technologists, and all Californians to better understand the impact of COVID-19. This includes the California COVID Assessment Tool, or CalCAT, a "model of models" that contains assessments of the spread of COVID-19, short-term forecasts of disease trends, and scenarios of the course of the disease from modeling groups across the country. The state is also making the source code of CalCAT available to the public. Additionally, the Governor has directed that the state's COVID-19

data be open and machine-readable by default, except to preserve privacy; that data be provided via dashboard, on California's open data portal; and that the data be available by direct connection to a database.

The goal is to refine California's and our counties' insights and knowledge, and to spur collaboration with other states and researchers. To this end, the Governor's Office is instructing all state agencies and departments to make COVID-19 data and information publicly accessible, provided it does not include information that will violate privacy.

CalCAT includes:

- "Nowcasts," the rate at which COVID-19 is estimated to be spreading;
- Short-term forecasts, which show what various models predict will happen over the next few weeks in California; and
- Scenarios, which show what could happen over the next few months under different conditions.

To learn more about the California COVID Assessment Tool, visit calcat.covid19.ca.gov. To access the open-source code, go to https://github.com/StateOfCalifornia/CalCAT.

To learn more information about California's efforts around COVID-19, go to covid19.ca.gov.

Read the full article here.