



Milk Producers Council

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MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE

Blocks - \$.0350 \$1.6150
Barrels - \$.0100 \$1.5225

Weekly Average, Cheddar Cheese

Blocks - \$.0020 \$1.6080
Barrels +\$.0007 \$1.5245

CHICAGO AA BUTTER

Weekly Change +\$.0175 \$1.4175
Weekly Average +\$.0104 \$1.4085

DRY WHEY

Dairy Market News w/e 06/08/12 \$1.4838
National Plants w/e 06/02/12 \$1.5166

NON-FAT DRY MILK

Week Ending 6/1 & 6/2

Calif. Plants \$1.1040 16,578,191
Nat'l Plants \$1.0957 30,601,990

Prior Week Ending 5/25 & 5/26

Calif. Plants \$1.1302 21,155,940
Nat'l Plants \$1.1317 34,457,764

CHEESE MARKET COMMENTS: With milk production now headed downward, boosted along by a number of base plans which encourage purposeful cut-backs by dairy farmers, cheese plants once again are more able to settle into their optimal patterns of production in terms of total volume and combination of products. With a little less milk available and milk components dropping, more nonfat dry milk is being used to fortify or standardize cheese vats to help plants maintain efficiencies. Trading this week for blocks had buyers and sellers trading offers and bids from day to day which moved prices up by \$.07 per lb and down by \$.105 per lb, ending with a net decrease of \$.035 per lb. Barrel prices lost a net \$.01 per lb after a Friday sale at \$1.55 was followed by an offer \$.0275 per lb lower. The spread price between blocks and barrels narrowed to \$.0925 on Friday. The overly wide differences between the two have not been incorporated into prices reported to AMS; average price differences for shipments over the past five weeks have not reached \$.04 per lb, and last week's average was less than \$.02 per lb. The average price for block cheese shipped last week was \$1.5163 per lb, about \$.093 per lb lower than the CME average for the week. Sales, helped by steady to strong exports (11.9 million lbs of cheddar and 41.4 million lbs of other cheese in April), appear to be keeping pace with production, and many manufacturers are telling *Dairy Market News* their stocks on hand are not considered too large. CME futures prices for class III milk and cheddar cheese responded positively to what they saw this week. Futures traders include market makers (the speculators) as well as plants and producers who seek to protect their positions on future prices. Milk futures for the July-December period were up by an average of \$.56 per cwt; September's \$16.69 per cwt is the high. Cheese futures increased by \$.026 per lb; November's \$1.685 per lb is the high.

BUTTER MARKET COMMENTS: Less milk and cream available to butter plants is helping to firm up butter prices. After getting off to a slow start earlier this year, cream for ice cream production is now at its seasonal high, and cream multiples have moved to above 130, according to *DMN*. Prices reported to AMS for shipments last week are keeping pace with the weekly average price changes on the CME. Domestic sales are reported to be steady; resorts and vacation locations are laying in supplies. Export sales continue to lag last year's very good volumes over the first half of the year. April's butter exports totaled 12.0 million lbs, 3.1 million lbs lower than the previous year. Butter placed into storage in Europe for later sale is 60% higher than the year before, about 180 million lbs. Buyers are weighing the chances that butter prices will turn downward again against getting caught short if what has been forecast for U.S. milk production later this year comes to be. Current CME prices are now a little more than \$.10 per lb above their low point of the past two and a half years. Butter futures were mixed this week, ranging from \$.01 lower to \$.02 per lb higher; December's \$1.53 per lb is the high for the year.

POWDER MARKET COMMENTS: Prices for nonfat dry milk appear to be firming, according to *DMN*. Production has slowed and domestic and export sales continue to be steady to strong. April exports of nonfat powders totaled 86.6 million lbs, which was 13 million lbs higher than last April. Exports over the first four months this year total 25 million lbs more than for the same period last year. Current spot prices are moving

slowly upward while prices tied to various indexes, according to *DMN*, could edge somewhat lower. Prices for all dairy powders in this week's global auction were sharply higher, but that may not be representative of current U.S. market conditions. Fonterra does not have anything like the small mountain of powder on hand that has been reported for the U.S. Prices reported to AMS and CDFA for shipments last week were lower by \$.03 to \$.035 per lb; the national price has slipped below \$1.10 per lb. The CME price for grade A NFDM increased by \$.025 per lb this week, to \$1.21 per lb, supported by four more sales. Stocks of buttermilk powder are in better balance with production and usage, although prices are reported to be mostly unchanged.

WHEY PRODUCTS MARKET COMMENTS: Production of dry whey in April was 6.3% lower than the previous year while production of whey protein concentrates was 4.7% and 9.7% higher than last April (depending on level of concentration). Production of isolates was up by 16.2%. Stocks on hand at the end of the month also were higher. Exports of WPC in March and April have been very good – well above the same months last year, while exports of dry whey continues to lag last year's levels somewhat. *DMN* has mentioned lower priced DW from Europe (helped by their weakening currency) is affecting U.S. sales. U.S. buyers may be leaving manufacturers to handle their reserve needs as they appear to be slowing their purchases. Prices appear to be holding steady for the full line of whey protein products except for lactose prices, which are lower on a weaker market because of offers from Europe. Dry whey futures prices this week rose strongly across the board with increases averaging just short of \$.05 per lb; the high for the year is \$.5277 per lb for July.

FRED DOUMA'S PRICE PROJECTIONS...

June 01 Est:	Quota cwt. \$15.69	Overbase cwt. \$13.99	Cls. 4a cwt. \$13.34	Cls. 4b cwt. \$14.54
Last Week:	Quota cwt. \$15.83	Overbase cwt. \$14.14	Cls. 4a cwt. \$13.37	Cls. 4b cwt. \$14.84

SENATE FARM BILL VOTE: *(By Rob Vandenheuvel)* The U.S. Senate took a big step forward this week in the process of approving a 2012 renewal of our U.S. Farm Bill policies. By a 90-9 vote, the Senate voted to invoke "cloture" on the Farm Bill, which limits the amount of additional debate that can occur on the bill and prevents the bill from filibuster. Under the Senate rules, once a cloture vote has been approved, no more than 30 additional hours of debate can be conducted on the Senate floor on the bill. The rules also limit the amount of time an individual Senator can speak on the bill to one hour and limits any amendments to issues relevant to the Farm Bill. Over the coming weeks, the Farm Bill is expected to be heavily debated on the Senate floor, with a final vote on the bill coming at the end of that debate.

In the House of Representatives, rumors are starting to surface that the House version of the 2012 Farm Bill will be considered by the House Agriculture Committee in the next couple weeks. Ultimately, both the House and Senate must pass identical Farm Bill legislation, so MPC and others supporting the dairy provisions included in the current Senate Farm Bill will be watching both the House and Senate proceedings very closely. So stay tuned...

DAIRY PRODUCER COALITION FILES POST-HEARING BRIEF: *(By Rob Vandenheuvel)* As regular readers of our newsletter are well aware, last week the California Department of Food and Agriculture (CDFA) held a hearing to consider changes to our State's Class 4b (milk sold to cheese plants) formula. Specifically, the hearing focused on proposed adjustments to how the Class 4b price is impacted by the market prices for dry whey.

This week, the Coalition of dairy producer organizations/cooperatives filed a post-hearing brief aimed at amplifying and further explaining our testimony. As a reminder, the Coalition is made up of California Dairies, Inc., Dairy Farmers of America, Land O'Lakes, Security Milk Producers Association, California Dairy Campaign, Milk Producers Council and the Alliance of Western Milk Producers.

For those interested in reading the full post-hearing brief, it can be found on MPC’s website at: <http://www.milkproducerscouncil.org/coalitionbrief.pdf>. While much of the brief is an amplification of the economic arguments laid out at the hearing by the Coalition members, there is also an in-depth look at the California laws that are in place with regard to establishing regulated prices for each of the five classes of milk.

Included in that legal discussion, which is taken from the California Food and Agricultural Code (the “Code”) – the laws that are approved by the California Legislature – are the following points:

- In California, the legislature has authorized CDFA to formulate stabilization and marketing plans. CDFA has chosen to implement two similar “Stabilization and Marketing Plans for Market Milk,” one for Northern California and one for Southern California. However, the director’s discretion in structuring these plans is limited by the law. Section 61805(c) of the Code specifically states that *“The purposes of this chapter are to...Authorize and enable the director to formulate stabilization and marketing plans, subject to the limitations prescribed in this chapter with respect to the contents of the stabilization and marketing plants, and to declare the plans in effect for any marketing area.”* (emphasis added)
- **So what are those limitations?** The most direct limitation is spelled out in Section 62062 of the Code. That section gives CDFA broad discretion in how to establish prices for the five classes of milk (the prices can simply be designated or CDFA can establish methods/formulas that determine a price). In our current system, CDFA has chosen to utilize “end-product pricing formulas” that determine the value of raw milk on the farm using the values of some combination of butter, nonfat dry milk, cheddar cheese and dry whey. However, Section 62062 goes on to state, *“If the director adopts methods or formulas in the plan for designation of prices, the methods or formulas shall be reasonably calculated to result in prices that are in a reasonable and sound economic relationship with the national value of manufactured milk products.”* (emphasis added)
- **What is the significance of the use of the words “shall be” in Section 62062 of the Code?** To determine that, we need to look at how the Code views the word “shall.” Fortunately, Section 47 of the Code includes precisely such a definition: *“‘Shall’ is mandatory, and ‘may’ is permissive.”* (emphasis added)

There are other sections of the Code that outline economic data that CDFA “shall consider” or “shall take into consideration,” but as the Coalition’s post-hearing brief points out, only Section 62062 includes the strong mandatory language, “shall be.”

Given this clear legal interpretation, there was understandably a significant amount of testimony from the producer side of our industry about what should be considered the “national value of manufactured milk products.” With the discussion in the hearing focused on the Class 4b price, producers made a strong case that the Federal Order Class III price is the best benchmark price to use when making a comparison. Federal Orders oversee most of the milk-producing regions outside of California. In fact, about 80% of the milk produced and sold outside of California is in Federal Order areas. Federal Orders also utilize an end-product pricing formula similar to California’s system, making a comparison between our Class 4b price and the Federal Order Class III price a logical and economically sound evaluation.

So with all this information on the table, can we call the relationship between the California Class 4b price and the Federal Order Class III price “reasonable” and “economically sound”? You can judge that for yourself. To the right is a comparison of the two price series in just the past nine months since CDFA last “fixed” the Class 4b formula.

	CA Class 4b	F/O Class III	Diff.
Sep-11	\$16.33	\$19.07	(\$2.74)
Oct-11	\$15.78	\$18.03	(\$2.25)
Nov-11	\$17.19	\$19.07	(\$1.88)
Dec-11	\$15.14	\$18.77	(\$3.63)
Jan-12	\$14.23	\$17.05	(\$2.82)
Feb-12	\$13.42	\$16.06	(\$2.64)
Mar-12	\$13.67	\$15.72	(\$2.05)
Apr-12	\$13.43	\$15.72	(\$2.29)
May-12	\$13.56	\$15.23	(\$1.67)
Average	\$14.75	\$17.19	(\$2.44)

To put these numbers in perspective, we can roughly estimate that our State’s cheese manufacturers are buying more than 1.3 billion pounds of milk each month from the California “pool.” At that level, an average \$2.44 per hundredweight difference equates to more than \$30 million per

month, or **more than \$270 million in the nine months since the last change to the Class 4b formula!** With figures like that, the producers and their representatives that spoke at the hearing were able to make a very strong case that our Class 4b price has certainly *not* been in a “reasonable and sound economic relationship” with what comparable milk is worth around the country.

So with the post-hearing brief filed, producers have finished making our case to CDFA. As we wrote in last week’s newsletter, CDFA now has up to 52 days to announce any changes to the Class 4b formula (about July 20th). Until then, we wait and focus our efforts on other important initiatives, like the Congressional debate of the 2012 Farm Bill. Policy work in the dairy industry is certainly not boring these days...

PRICES SHARPLY HIGHER IN GLOBAL AUCTION: *(by J Kaczor)* The weighted average winning price in this week’s global dairy product auction, covering all products in all six contract periods, is \$1.315 per lb, which is \$.127 per lb higher (10.7%) than the winning price in the auction held two weeks ago. The summary published on the globalDairyTrade site showed the number of certified bidders increased to 649. 106 of the 170 who actively participated in the bidding wound up with some of the 63.3 million lbs of product sold. The number certified and the number that bid this week are record highs.

The increase in average price was the biggest in almost two years. However, prices for most of the products offered in the auction are still not back to where they were in April, and are still almost a third below where they were in the June auctions held one year ago. Most of the comments coming from New Zealand, while citing the results as verification of continuing global dairy product demand, are not declaring this week’s results as the sustainable recovery ultimate expected. That depends on an expected slowing in the global milk supply which Fonterra foresees beginning in the latter half of this year.

Prices for all products except the occasional offering of limited volumes of lactose were sharply higher. The general price pattern for anhydrous milkfat, cheese, and skim milk powder was higher prices for the early months, then lower. The pattern for whole milk powder was the opposite. The total volume of all products offered in this auction was low, June being one of the two lowest milk production months for New Zealand.

The weighted average price for anhydrous milkfat in the Spot Month contract #2 rose by 42%, to \$1.539 per lb. The average increase for all AMF was 24% – an apparent correction to price levels beaten down too far by the global butterfat surplus that became evident about a year ago. Skim milk powder prices were also sharply higher – prices for all grades and styles were up by an average \$.20 per lb, are again substantially higher (\$.112 per lb) than average winning prices for whole milk powder, and continue to reflect huge premiums for Fonterra’s products compared to those for Arla Foods and Dairy America. For example, the winning price for Arla Foods’ medium heat SMP in contract #2 was \$.45 per lb lower than the winning price for Fonterra’s same product sold in the same contract period. Dairy America’s average prices for its low heat SMP increased by \$.115 per lb, to an average \$1.218 per lb. Winning prices for cheddar cheese, rennet casein, and MPC-70 each rose by at least ten percent.

The flip-flop in SMP and WMP prices may have resulted from reports about a slowing in China’s economy and a decision to cut back on imports of WMP and increase its imports of SMP. China is the world’s largest single importer of dairy products and Fonterra is their largest supplier of anhydrous milkfat and milk powders. China responded to the report on its slowing growth by announcing intention to provide additional economic stimulus. [Imagine that, increase governmental stimulus to create more economic growth. That is something the U.S. Congress used to do before ideology trumped common sense.]

Price increases like those in this week’s auction were not foreseen. Changes in global milk supply, demand, and stocks of products do not change quickly, but anticipations sometime trigger the unexpected and unexplainable. Global milk production is likely to continue to exceed current international demand at least for a while more until expected cutbacks in Europe and the U.S. exceed expected milk production increases in the southern hemisphere. Concern about the effect on demand of a possible financial crisis in Europe is at a high level. Stocks of skim milk powder and butter in the U.S. and Europe are very high and will take time to fall to normal levels. Fonterra

is sure to accommodate China's need for more SMP and less WMP simply by shifting production between plants, so windfall demand increases for others is not likely to happen, and the net result should be more New Zealand butterfat looking for buyers.

And, setting concern about supply and demand aside for a moment, one wonders how much longer Arla Foods and Dairy America will continue to accept prices for a basic dairy commodity that are so much lower than those offered by bidders to the other supplier. There is a theory that bidders see an opportunity to sweep up extra product at bargain level prices so long as the products are available. That price disparity is not what *Dairy Market News* finds in their twice monthly price discovery exercises. Those differences exist for a reason, but just what that might be is illusive. Different buyers for different sellers, apparently, but why and how, and for how much longer?

MONTHLY MPC BOARD MEETING TO BE HELD NEXT TUESDAY: *(By Rob Vandenheuvel)* MPC's monthly board meeting will be held next Tuesday (June 12th). This month's meeting will be held in Bakersfield, CA, in the board room of the Kern County Farm Bureau (*801 S. Mount Vernon Avenue, Bakersfield*). The meeting will start at 11 am. **All current and prospective MPC members and associate members are welcome to attend.** If you plan to attend, please RSVP by calling (909) 628-6018.