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TO: Directors & Members **FROM: John Kaczor**

MAJOR DEVELOPMENTS IN WASHINGTON, DC

U.S. Senate Ag Committee Unveils Their Draft of the 2012 Farm Bill

MPC Joins Dairy Organizations/Cooperatives from Around the U.S. in Support

By Rob Vandenheuvel

The debate over the 2012 reauthorization of our nation's Farm Bill policies is officially heating up in Washington, DC. Both the U.S. House of Representatives and Senate announced activities for next week aimed at advancing the debate with the goal of passing the 2012 Farm Bill later this year. The House Agriculture Committee's Subcommittee on Livestock, Dairy and Poultry announced a hearing for next Thursday to specifically look at our nation's dairy policies, while the Senate Committee on Agriculture, Nutrition and Forestry scheduled a "markup" of the 2012 Farm Bill for next Wednesday (a "markup" is DC-talk for the Committee process of actually approving a bill and sending it to the full Senate for consideration).

In announcing their markup, Senate Agriculture Committee Chairwoman Debbie Stabenow (D-Michigan) released a draft of the 2012 Farm Bill, which included dairy provisions modeled after the "Dairy Security Act" (a.k.a. DSA, H.R. 3062 or the "Peterson-Simpson Bill"). In short, the draft Senate Farm Bill includes the two main pieces of the DSA, which are:

- **Dairy Producer Margin Protection Program (DPMPP)** – This is commonly referred to as the "insurance" part of the bill. Under the DPMPP, a producer could choose to enroll in a direct-payment program run by the U.S. Department of Agriculture. The basic program (which would come at no cost to individual dairies) would provide cash payments directly to dairy farmers when the national "margin" between milk prices and feed costs dropped below $4.00 per hundredweight. In other words, when the average milk price across the country drops to less than $4.00 per hundredweight over the "feed cost calculation" (a formula that incorporates national values of corn, soybean meal and alfalfa), a payment would be made to all dairymen enrolled in the program. Unlike the MILC program, this insurance program would not be capped at a specific volume of milk – instead it would cover 80% of the "historical production" of each dairy facility (which would be determined by the highest annual production for each dairy over the past three years). In addition, a supplemental program would be available for dairies that wish to generate payments from the program at higher margin levels. In other words, an individual dairyman could choose to customize the program so that a payment is generated whenever the price of milk is less than $5.00 per hundredweight above the feed cost calculation. Or $6.00. Or $7.00. This additional coverage would include an annual premium paid by the dairy farmer. The supplemental program could be customized to cover up to 90% of a dairy's annual production.

- **Dairy Market Stabilization Program (DMSP)** – This is commonly referred to as the "market management" part of the bill. ***The DMSP would only apply to dairies that choose to enroll in the insurance program outlined above (the DPMPP).*** If a dairy is enrolled in the DPMPP, they would be automatically part of the DMSP. Under the DMSP, when the margin falls below $6.00 per hundredweight for two consecutive months (the national average price of milk falls to less than $6.00 per hundredweight above the feed cost calculation), USDA would notify the dairies enrolled in the DMSP that in the following month, they would only be paid for 98% of their "base production" (which can be determined by either the dairy's production three months leading up to that point, or the production in the same month the prior year). Milk produced above that level by a dairy enrolled in the DMSP would still be paid for by the milk handler, but these dollars would be diverted to a fund used to buy excess dairy products to be donated to food banks and feeding programs. If the margin continues to fall below $5.00 or $4.00 per hundredweight, the DMSP would adjust to only pay enrolled dairy farmers for 97% and 96% of their "base production." At no point would the DMSP authorize payments below 96% of a dairy's base production. Once the margin recovers to above $6.00 per hundredweight for two consecutive months, the DMSP is de-activated and all calculations of "base production" are eliminated. If the DMSP re-activates at a later time, the calculations will re-start from scratch.

A few modifications from the original "Peterson-Simpson Bill" also surfaced in this Senate draft of the Farm Bill. These modifications were largely known to those who have been following this process, and have played a key role in helping build additional support among the dairy industry for these policy changes. Two of the most notable modifications include:

- The proposed reforms to the Federal Milk Marketing Order regulations are *not* included in the Senate draft.
- Dairies choosing to enroll in the "supplemental" portion of the Dairy Producer Margin Protection Program would be subject to a lower premium on the first 4 million lbs of milk produced per year. This lower premium would be available to *all* dairies, regardless of size.

While some other differences exist from the original "Peterson-Simpson Bill," the fundamental structure of the policies included in the Senate draft remains unchanged.

While the two Houses of Congress have been busy, so have dairy organizations and cooperatives from around the country. This week, Milk Producers Council (MPC) joined 28 other organizations/cooperatives in sending a joint letter to the Senate Ag Committee members urging them to support the DSA provisions outlined above as the dairy portion of the Farm Bill. The groups, which represent a vast majority of the milk produced throughout the U.S., include:

- Agri-Mark
- Alabama Dairy Producers
- Associated Milk Producers Inc. (AMPI)
- Dairy Farmers of America (DFA)
- Dairy Farmers Working Together
- Dairy Producers of New Mexico
- Dairy Producers of Utah
- Dairylea Cooperative Inc.
- Ellsworth Cooperative Creamery
- Holstein Association USA, Inc.
- Idaho Dairyman's Association
- Iowa State Dairy Association
- Land O'Lakes
- Maryland Dairy Industry Association
- Michigan Milk Producers
- Midwest Dairy Coalition
- Milk Producers Council
- Missouri Dairy Association
- National Council of Farmer Cooperatives
- National Farmers Organization
- National Milk Producers Federation
- Northwest Dairy Association / Darigold
- Oregon Dairy Farmers Association
- South Carolina Dairy Association
- South Dakota Dairy Producers
- St. Albans Cooperative Creamery
- United Dairymen of Arizona
- Upstate Niagara Cooperative, Inc.
- Washington State Dairy Federation

The letter (which can be read at http://www.milkproducerscouncil.org/041912coalitionletter.pdf) said that, **"The Dairy Security Act is an update to our safety net policies for the 21st Century. It provides flexibility and options for each individual dairy. Not only can the provisions in the legislation be customized to each dairy, there is also the option for any dairy to completely exempt itself from the programs. The authors of the DSA recognized that a one-size-fits-all approach simply doesn't work in our modern industry and have**

cooperated fully with our organizations in making further improvements to broaden the support for the dairy reform package."

The letter went on to say that, **"As the list [above] clearly shows, the U.S. dairy industry is demonstrating a level of unity and support for the Dairy Security Act that is unprecedented for our industry. These organizations share the belief that the status quo is not an option for our future, and we stand united behind the Dairy Security Act as a rare opportunity for the dairy industry to collectively support reasonable, sound changes to our Federal policies."**

This week's progress in moving forward with much-needed reforms to our Federal safety net policies for the dairy industry is the latest culmination of years worth of work. Regular readers of this newsletter will recall that MPC has been actively involved in developing and promoting reforms to our dairy policies. It started in 2007 with MPC's development of the "Growth Management Plan." Those efforts helped set the stage for the introduction of H.R. 5288/S. 3531, also known as the "Costa-Sanders Bill." While that legislation was ultimately unable to garner enough support in the Legislature to be approved, it was a key factor behind some of the provisions included in Foundation for the Future, a legislative proposal outlined a couple years ago by the National Milk Producers Federation. Fast forward to today: those provisions are the backbone of the dairy policies that are included in the Senate Ag Committee's version of the 2012 Farm Bill.

While this has been a long and laborious process (most legislation is), MPC is proud to stand side-by-side with the organizations listed above in moving forward with the dairy policy changes outlined above. **It should be noted, however, that much work still needs to be done.** Opponents of this package of policy changes – most notably the International Dairy Foods Association (IDFA, which represents many of the nation's dairy product processors) – are in full force trying to kill some/all of the dairy provisions being promoted. Specific to IDFA, there is a deep-rooted dislike for any policy that would empower dairy farmers to collectively respond to supply/demand imbalances with quick and temporary changes in milk production. As dairy farmers, if we want the U.S. Congress to provide the nation's dairy farmers with those valuable tools, **we need to fight for them**. Dairy families that support the pro-producer provisions outlined above need to pick up the phone and contact their elected officials.

Start with your Senators; **call both of your State's Senators and urge them to support the dairy provisions outlined by the Senate Ag Committee**. Opponents of this legislation have been and will continue to be making calls, urging our elected officials to reject the dairy provisions. **Don't let them speak for you! Your silence hands IDFA and others who are opposed to this legislation the power to kill this rare opportunity.** We've reached a critical point in this process, so please: **<u>Pick up the telephone!</u>** If you need help contacting your elected officials, feel free to contact Milk Producers Council at (909) 628-6018.

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE		
Blocks	*+$.0400*	$1.5275
Barrels	*N/C*	$1.4600
Weekly Average, Cheddar Cheese		
Blocks	*+$.0155*	$1.5030
Barrels	*+$.0105*	$1.4600

CHICAGO AA BUTTER		
Weekly Change	*- $.0125*	$1.4125
Weekly Average	*- $.0085*	$1.4175
DRY WHEY		
Dairy Market News	w/e 04/20/12	$.5025
National Plants	w/e 04/14/12	$.5935

NON-FAT DRY MILK		
Week Ending 4/13 & 4/14		
Calif. Plants	$1.3034	14,255,528
Nat'l Plants	$1.2672	25,380,070
Prior Week Ending 4/6 & 4/7		
Calif. Plants	*$1.2980*	*14,814,431*
Nat'l Plants	*$1.2605*	*22,270,600*

CHEESE MARKET COMMENTS: Today's report on the amount of cheese in long-term storage facilities showed American cheese stocks (read Cheddar) rose by 14 million lbs since February 29th, and stocks of all cheese moved back above the 1 billion lb level for the first time since November. However, the numbers were not unexpected, and therefore should have already been reflected in current prices. Stocks of American cheese remained within 10 million lbs of where they were a year ago and stocks of Italian cheese were lower. CME trading activity this week mirrored last week's pattern – no trades for blocks and heavy trading for barrels. Last week prices were unchanged for both styles; this week blocks gained $.04 per lb from bids. CME Class III milk futures trading, which had been moving prices lower day by day through Wednesday, finally may have acknowledged what was happening with spot prices, and changed direction on Thursday, but not by nearly enough to erase the earlier losses. The week ended with prices for all months lower, ranging from a low of $14.65 for June to a high of $16.25 for September.

BUTTER MARKET COMMENTS: *Dairy Market News* says butter production continues to be heavy but domestic orders are on the light side as many buyers expect lower prices may develop as milk and cream volumes increase seasonally. The time line referred to is not clear because we are within weeks of the peak milk production season and rarely is butter production higher in April than in March. Today's report on butterfat in cold storage at the end of March was surprisingly positive, showing only 5.4 million lbs more than at the end of February, while production in March is typically among the year's highest. There is little doubt but that the majority of the increased milk production is moving to butter and powder, the traditional market-clearing products; it is well beyond current market needs, but the butter output does not appear to be over-whelming. Exports may be occurring under the radar. Butterfat for other seasonal usages continues to increase, which also helps to clear the market. Trading was light this week on the CME; a single sale pulled the price down by $.0125 per lb on Wednesday. Butter futures prices were mixed, ranging from spot level prices for May up to $1.5675 for December.

POWDER MARKET COMMENTS: Prices for nonfat dry milk continue to be weak, generally moving lower, depending on particular strategies used in this buyers' market. Dryers appear to be handling the milk expeditiously, but inventories continue to grow. *DMN* says export volume is somewhat lighter than expected, and prices are reported to be weakening, in response to the trend in international markets. Prices reported for last week's shipments were mixed, reflecting close to average volumes. Prices for buttermilk powder are lower in the west and unchanged elsewhere, with demand remaining on the sluggish side.

WHEY PRODUCTS MARKET COMMENTS: The market tone for dry whey is weak. Demand is steady, but production continues to rise and prices for all but contracted sales tied to various indexes continue to weaken. WPC-34 prices also are trending lower as buyers become aware of spot loads readily available at prices lower than contract prices. Prices for the major dairy protein powder, NFDM, also weighs heavily of whey protein product prices. Inventories for all product categories are reported to be rising. Dry whey futures this week firmed up for April and May and were unchanged or lower for the rest of the year. Futures prices continue to point downward, reaching a low for the year of $.415 per lb for December.

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FRED DOUMA'S PRICE PROJECTIONS…

Apr 20 Est:	**Quota cwt. $15.90**	**Overbase cwt. $14.20**	**Cls. 4a cwt. $14.98**	**Cls. 4b cwt. $13.44**
Last Week:	**Quota cwt. $15.86**	**Overbase cwt. $14.16**	**Cls. 4a cwt. $14.99**	**Cls. 4b cwt. $13.35**

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MARCH MILK PRODUCTION INCREASES BY 4.2% WITH 1% MORE COWS: *(by J. Kaczor)* Heavy culling of milk cows in March (278 thousand) was offset by the addition of 290 thousand young animals for a net expansion of 12 thousand head over February, and 86 thousand over last March. The number of milk cows in California increased by 1 thousand from February and 25 thousand over a year ago. The increases over the past year were mostly gradual until December when the national expansion began to accelerate; a net 53 thousand cows were added in the four months since November. Production per cow was 59 lbs higher this March than a year ago. Milk production rose by 708 million lbs above last March, an increase of 4.2%. The weather was grand, and still is.

The production increases in March among the 23 top milk producing states were somewhat more balanced than has been the case for so many months. All but one state in that group expanded production during the month (Pennsylvania was the exception). Only three of the 23 states had fewer cows this March than last year. Seven of the sixteen states with increases of 3% or more were in the Midwest or northeast, as were three of the eight states producing 5% or more milk.

So far this year U.S. milk production has increased at a daily rate of 4.2%, twice that of a year ago. The increases carry forward the turn around that began last August, when producers began to respond to then-outstanding milk prices and projections for only slightly lower prices for 2012. California's overbase price for May, June, and July last year averaged $18.77 per cwt, $3.22 per cwt higher than the same period in 2010. Federal order class III prices for that period averaged $19.61 per cwt, $6.03 per cwt higher than the year before. The comparisons for August were even better, +$4.79 and +$6.49 per cwt, respectively.

Why wouldn't production expand under those conditions, with those positive market signals? The favorable price comparisons continued through this January, although at gradually lower differentials. However, February's price comparisons with the same month a year earlier turned negative, March's worsened, and April's are not expected to be any better than March. USDA's Economic Research Service, in its November Outlook, noted a substantial expansion in milk production in the southern hemisphere. In its April Outlook, all thought about level milk production this year was set aside, exports were projected to be lower than last year, and projected milk and dairy product prices were adjusted still lower.

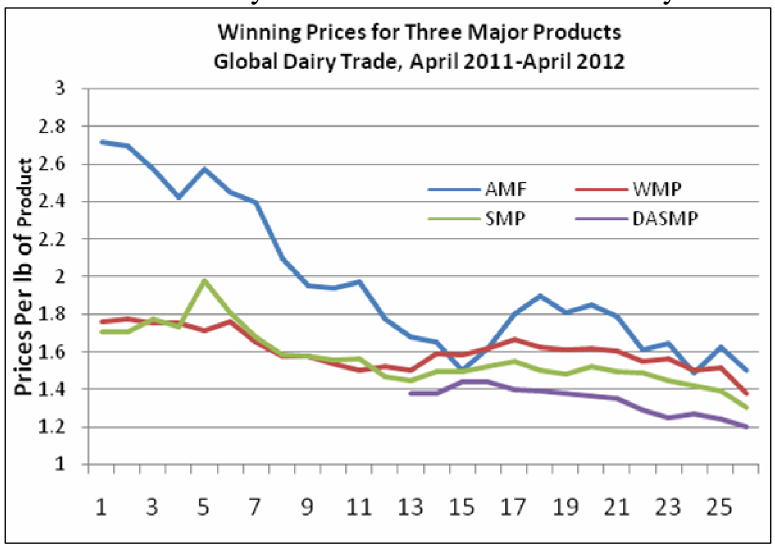
Under those conditions, with those negative market signals, why wouldn't milk production be cut back? The answer could be "for the same old reasons." Because the expansion in number of cows accelerated when milk prices were off their highs for the year and on their way downward, it appears many producers may have moved their eyes from a moving target. Perhaps a great many of them hedged their 2012 prices to levels that satisfied them. But it is Spring, and production per cow should continue to increase through May. Along with ERS, most forecasts for milk production and prices not so long ago were for cow numbers to continue to increase through the first half of the year, with prices gradually falling to the point where producers would alter the quality of feed and either leave the business or cut sharply back on the number of cows being milked. Removal of "gradually" from the preceding sentence may be appropriate.

In an article titled *"Milk Price Forecasts Are Aligned; Focus Is On Milk Production And Exports,"* published March 16th in MPC's *Friday Market Update*, it was noted that information published over the following six weeks should either confirm those forecasts or cause them to be reset. The forecast for milk production was for an increase averaging 1.8% for the year, starting with more cows and higher production. Feed costs were presumed to be a factor in causing a number of producers to give up or to give in, and others to cut back. Milk prices were forecast to be somewhere from $1.50 to $2.70 per cwt lower than 2010's. The lower end of those forecasts could still be reasonable but do depend on the anticipated cutbacks to happen and for exports to clear away unwanted inventories. Today's report on the amount of butter and cheese in cold storage was mixed. The amount of butterfat products in cold storage at the end of March was encouraging – an increase of only 5 million lbs from a month earlier. While butter production in March is still not known, the increase is expected to again be large so the relatively small growth in stocks during the month suggests that exports may actually have shown a solid increase. American cheese stocks increased by 15 million lbs and stocks of all natural cheese again moved above the 1 billion mark. Not so good about cheese, but certainly not unexpected. It looks like six weeks worth of data was not sufficient to give a clear enough picture, particularly regarding exports. Another six weeks, then, and that will bring us to about mid-year.

Looking beyond the U.S. the amount of milk production hitting the markets throughout the world looks like it simply is a matter of too much too soon. Too soon because the virtual certainty that, in the long run, global population will increase far faster than milk and dairy product production, does not mean now. Too much because supply is clearly outpacing the predicted demand from the large percentage of the fast growing number of people in north Africa and Asia anticipated to incorporate more western style foods into their diets. Too bad, because it appears Fonterra is doing what U.S. exporters only hope to do – get in on the ground floor first, using a unique combination of market knowledge and operational skills to establish ongoing relationships in a down market and, when they want, take back what they may have recently lost.

Long run plans and anticipations are not bankable. They do not do anything to help shore up current U.S. dairy product prices. U.S. exporters have the supply of milk they so badly want; U.S. milk producers badly need exporters to do whatever is necessary to not only maintain last year's business but to increase exports by volumes proportionate to the increase in the U.S. milk supply. If there is a race to see who can out-produce all others, the U.S. dairy industry simply cannot afford to compete. That message needs to be given by the exporters themselves instead of beating their chests about possible shortages of milk resulting from their unwillingness to pay an appropriate price.

PRICES SHARPLY LOWER IN LATEST GLOBAL AUCTION: *(by J. Kaczor)* The lead comment in a story out of New Zealand on Tuesday regarding the auction's latest results was "prices plummet." That sentence could have continued to read "to new lows for the year." Fonterra's fiscal year ends with the month of May. The chart displayed here shows where prices for anhydrous milkfat, whole milk powder, and skim milk powder were in April 2011 through this week's auction. 610 bidders are now certified; 134 participated this week; 118 wound up with some of the 70.8 million lbs of products that were sold.



In one sense the prices are disappointing because they are considered by some to be harbingers for future prices. In another way it may be somewhat reassuring for some to see the prices may, in fact, be more representative than they appeared to be almost up to this time. As we know, prices for dairy commodities have been under pressure for some time – that is, from the time huge milk production increases began to show themselves in South America and New Zealand – but winning prices in the twice monthly auctions seemed for a time to be immune to silly things like supply and demand imbalances.

The chart shows the somewhat steady decline in prices for whole milk powder and skim milk powder over this full period. Prices for anhydrous milkfat are by far the most volatile as well as the most mysterious (why would milkfat of such high quality in such compact form, usable for so many purposes around the world, be priced so much lower than milkfat in the form of butter? Some U.S. sellers say their prices for AMF are, on a per lb of milkfat, higher than milkfat in butter.).

The chart continues to show estimated average prices for Dairy America's skim milk powder, but does not show that the price Arla Foods is receiving for their high quality powder is also at about where DA's is. However, the difference in prices between those prices and Fonterra's SMP appears to be narrowing somewhat. Also not shown is lactose powder, the new product, first offered on April 3rd (it wasn't offered in this auction).

On May 1st, the structure of the contract periods will reflect six one month delivery periods stretching out the six months following the month of the auction. That should make comparisons between periods more meaningful for buyers, sellers, and on-lookers.