

Milk Producers Council

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MPC FRIDAY MARKET UPDATE

CHICAGO MERCANTILE EXCHANGE

Blocks + \$.0250 \$1.2000
Barrels + \$.0400 \$1.2200

Weekly Average

Blocks - \$.0430 \$1.1770
Barrels - \$.0085 \$1.1960

CHICAGO AA BUTTER

Weekly Change +\$.0175 \$1.1675
Weekly Average +\$.0250 \$1.1590

DRY WHEY

WEST MSTLY AVG w/e 03/06/09 \$.1675
NASS w/e 02/28/09 \$.1568

NON-FAT DRY MILK

Week Ending 2/27 & 2/28

Calif. Plants \$.8040 18,175,298
NASS Plants \$.8192 31,383,507

CHEESE MARKET COMMENTS: Activity on the CME this week was a bit slower than last week, but still good, and prices for blocks and barrels made up some of last week's losses, ending the week with two days of increases. Dairy Market News observes a pattern of possible over-stocking by buyers in anticipation of higher prices later in the year. That's o.k. for aging purposes, but has shown that it results in slack-time buying periods down the road, and lower prices. Cheese production in January was 1% above last January, but 4.4% lower than in December. Cheddar production was up by 4.5%. Retail sales are reported to be fairly good.

BUTTER MARKET COMMENTS: Good news this week: no more sales to the CCC, and prices continued to edge up on the CME. DMN reports that retail sales are good, supported by price ads and promotions. Butter production in January was a record high, up by about 4%, which helps to explain that huge increase reported for butterfat products in storage at the end of the month. One more week of even small price increases could put CCC butter purchases away for the year. With very low export interest again the norm, good retail butter sales and an uptick in fluid milk consumption because of the very low prices during February and March are needed to keep butter inventories under control.

POWDER MARKET COMMENTS: Sales to the CCC continued this week, but at a much lower rate than what has been happening. But production of nfdm in January was up by about 36 million lbs over January 2008 and about even with December's output. Production of all nonfat powders was about 9 million lbs over a year earlier. Skim milk powder, for the export market presumably, was 61% below a year earlier, and even with December. Grim satisfaction: prices are about as low as they are going to go, but there is no real hope for anything close to a recovery on the horizon. 188 million lbs of nfdm must be sold by the CCC at \$.88 per lb, or given away, before commercial prices can reach the \$.90 per lb level, and Europe and New Zealand have many million of lbs of product in storage.

WHEY MARKET COMMENTS: Good news in small packages again; prices continue to edge up and DMN says that their contacts say that demand is definitely increasing, including interest of exporters. But the average of the West "mostly" price this week was unchanged, at a level below the cost of producing the product. Prices for whey protein concentrate (wpc) also seem to have flattened out, although February's average price was \$.015 per lb higher than January's, but more the \$.60 below where it was last year. Demand for wpc also is affected by weaknesses in some buyer areas, and from imports.

FRED DOUMA'S PRICE PROJECTIONS...

March 06 Est: Quota cwt. \$ 11.34 Overbase cwt. \$ 9.64 Cls. 4a cwt. \$ 9.61 Cls. 4b cwt. \$10.05
Feb 2009 Final: Quota cwt. \$ 11.32 Overbase cwt. \$ 9.63 Cls. 4a cwt. \$ 9.40 Cls. 4b cwt. \$10.11

A SHORT NOTE ON CALIFORNIA'S JANUARY PRODUCTION AND USAGE: (By J. Kaczor) The beginning of the new year brought with it some big changes in milk production, usage, and pooling in California. According to CDFA, total milk production decreased by 1.3% compared to January 2008.

- Production of market grade milk decreased by 143.4 million lbs, 4.2%
- Production of manufacturing grade milk increased by 100 million lbs, 167.2%
- Imports of bulk milk increased by 3.6 million lbs, 5.7%
- Exports of bulk milk increased by 8.7 million lbs, 25.6%

The increase in the amount of manufacturing grade milk resulted largely from a fairly large number of market grade producers who notified CDFA that they decided to de-pool for the year. In addition to that, another 44 million lbs of market grade milk was shipped directly to non-pool plants during the month. The combination of the lower total production and the shipments to non-pool plants resulted in reduction in the amount of pooled milk of 187.2 million lbs for the month, compared to the previous January. The usage of **the milk that was pooled** also underwent a substantial change:

- Class 1 pooled total solids decreased by 4.8 million lbs, to 14.5% of pool usage
- Class 2 & 3 usage increased by 0.5 million lbs, to 7.6% of pool usage
- Class 4a usage increased by 12.8 million lbs, to 39.2% of pool usage
- Class 4b usage decreased by 33.8 million lbs, to 38.7% of pool usage

The decrease in Class 1 usage of pool milk amounted to about 150,000 gallons per day, compared to last January. Most of that decrease is the result of the recent loss of box store volume in northern California to an unregulated processor located in northern Nevada. That loss is expected to increase each month until the change over of suppliers to those stores is completed. Total anticipated loss of these changes was estimated in an earlier report on inter-state packaged milk sales to exceed 4 million gallons per month.

The combination of increased 4a usages and decreased 4b usages has, I think, for the first time in more than 25 years, resulted in 4a pool usage exceeding 4b pool usage. However, total cheese production in the state for the month was down only 5% and continues to represent about 42% of total milk usage in California.

QUESTIONS REMAIN ABOUT WHO PROFITED FROM 2008'S EXPORTS OF NFDN: (By J. Kaczor) Even though California producers already have more than their fair share of problems that are threatening their financial survival (lowest "mailbox" prices and lowest percentage of Class 1 usage in the U.S.; increasing loss of Class 1 sales to non-California processors; credit availability), there is **one more bad news story**, first mentioned here two years ago, that deserves a fitting follow-up, and maybe a final note on the subject.

Regular readers of this *Update* will remember questions that were asked about why the monthly California weighted average prices (CWAP) for sales of nonfat dry milk (NFDN) reported to the California Department of Food and Agriculture (CDFA) by California manufacturers were consistently lagging **behind and below** all other published prices for that product. Those prices directly affected prices for Class 2, 3, and 4a milk, about 40% of California's total usage.

The questions were answered with reminders from *Dairy America* and its members that the majority of California's NFDN was being sold for export under fixed priced contracts ranging from three to nine months long and, when current prices were rising (which they were in 2007), the combined monthly average prices for current sales and export sales **naturally would be lower** than the prices charged for current sales only. However, producers were told, **there was a silver lining to that dark cloud because the situation would reverse itself when current prices fell**, because the combined monthly averages for the current sales and contracted export sales **naturally would then be higher** than the prices charged for current sales only. The reason why the rising sales prices reported to NASS in 2007, for use in federal order areas, were higher than the prices reported to CDFA was because **NASS accepts current sales only** while CDFA accepts reports that include prices as much as one year old.

It was a relatively small matter at first, but grew into something very large and costly. For years, the effects

of the differences in reporting rules cost California producers less than a million dollars a month, but that difference began to increase in the second half of 2006 when NFDM prices began to rise. In a hearing in August 2007, Milk Producers Council reported that the affect of the differences in reporting rules for sales of NFDM between California and federal order areas had risen to **\$10.1 million** in January 2007 and continued rising each month through July 2007, **for a total estimated loss of more than \$174 million for the seven month period.**

By the end of 2008, a full cycle of rising and falling prices for NFDM had occurred. Current prices (NASS) rose from January through October 2007, then began to fall throughout 2008 right up to the most recent week. Prices for exported NFDM and skim milk powder (SMP) followed behind, reaching their peak in October and November 2007, and then also started downward, but at a much lesser rate than current prices. The following table shows these full price cycles. The monthly average NFDM prices per lb shown in the table for 2007 and 2008 are those used to set California and federal order prices for milk used to produce NFDM and skim milk powder. The prices shown for exported powders are the monthly average values reported to the U.S. Census Bureau by the exporters on their Shippers Export Declarations at places where the products left the U.S.

	2007			2008		
	CWAP	NASS	Exports	CWAP	NASS	Exports
January	\$1.027	\$1.068	\$1.000	\$1.551	\$1.509	\$1.870
February	1.070	1.102	1.010	1.319	1.333	1.830
March	1.135	1.190	1.040	1.274	1.251	1.710
April	1.257	1.435	1.040	1.239	1.251	1.610
May	1.375	1.667	1.110	1.297	1.299	1.580
June	1.473	1.901	1.410	1.335	1.351	1.540
July	1.807	2.018	1.660	1.365	1.405	1.510
August	1.975	2.055	1.840	1.348	1.384	1.530
September	2.053	2.056	1.660	1.236	1.231	1.590
October	2.064	2.062	1.970	.977	.999	1.560
November	1.968	1.956	1.970	.868	.870	1.560
December	1.815	1.803	1.850	.835	.845	1.080

The table shows that the CWAP lagged behind the NASS prices in the early part of 2007, but made up ground and finally caught up to the NASS prices by September 2007 as older export contracts expired and were replaced by new contracts with more current prices. The table also shows that the differences between the CWAP monthly averages and the NASS averages **had somehow virtually disappeared once the two series reached parity in September 2007.** Therefore, the profit recovery that California producers had been told to expect once the higher export prices received by California plants were combined with the falling domestic prices **did not happen.** It looks like California plants found ways to avoid reporting the higher value of products that were exported.

The values in the table for powder exported in 2008 are what might reasonably be expected to have been negotiated in September, October, and November 2007 for contracts extending three, six, and nine months beyond the inevitable lead times that we were told fell between negotiation and finalization of the contracts and the period of actual shipments. [Read the CDI hearing brief, dated 8/31/2007 at www.cdfa.ca.gov/dairy/pdf/hearings/2007/CDIresponsetoposthearingbriefAug28.pdf] The price drop of \$.48 per lb in December 2008 was unusually large but was similar to the increase of \$.43 per lb from June to August 2007, each representing completion of major export commitments and the beginning of new contracts. Note that the December 2008 drop had no apparent affect on the level of prices reported for the month by California plants.

So, who got the profits from the exports of NFDM and SMP in 2008? Last Fall, MPC asked the USDA agency responsible for verifying the accuracy and correctness of the sales reports that are used in federal order milk price formulas to see if they could find a logical reason for the newfound correlation between the CWAP series and the NASS current price series. Unfortunately, USDA's response to the request appeared to reflect indifference at best – nothing looked wrong with the reports; they knew nothing about what ultimately happened to the products (nor did they care); and the pattern of prices reported to CDFa appeared to be what should be expected, based on patterns that existed several years earlier. **MPC disagrees with USDA's conclusions, and**

faults them for their total lack of interest in who did what to cause the two major NFDM price series to stay close together throughout 2008, when one includes a major amount of powder that was exported at relatively high prices and the other includes almost no export sales. An honest effort by USDA could have found the answer.

Why even ask this question? Well, in the first place, the differences between the values of powder exports and the CWAP prices, times the volume of exports included in the CWAP reports for 2008, amounts to an estimated \$200 million. It's a big deal; big enough to invite thoughts by some about how they can come out ahead one year after they looked pretty dumb. Second, **those export values clearly were not included in prices payable to producers.** Third, **the hearing held by USDA in 2007 on mandatory sales reporting rules laid out paths that can be followed by manufacturing plants to avoid reporting certain sales, and showed how desired sales prices can be constructed for reporting purposes before the product's ultimate sale occurs at a later time at a higher price.** (Incidentally, the comment period on that part of the hearing closed in September 2007.) Fourth, whatever was done in 2008 to cause the expected profits from exports to "vanish" can be un-done at any time to restore prior relationships (yes, **that means when current prices begin to rise, the CWAP level can manage to again lag behind and below the current NASS prices**). Finally, the CWAP's monthly levels in 2008 cannot logically be explained without believing that specific significant changes were made in the way prices for exported products were recorded and accounted for – changes which shifted many millions of dollars away from California producers. So, the question seems fair, doesn't it: **who wound up with the money?**

Addendum: A brief reply was offered when this question was raised last August, and was repeated this week. That answer: the higher prices for exported products in 2008 were averages of low prices for NFDM and much higher prices for a high volume of SMP that had been contracted for lengthy periods. (If all SMP that was manufactured in the U.S. in 2008 was exported, a reasonable assumption, that product represented about 43% of total exports of nonfat powders for 2008, and was spread fairly evenly over the year.) That would mean that the average 2008 price for exported SMP was about \$2.20 per lb, and the average price for exported NFDM was about a dollar lower. If true, that's really amazing, and we're waiting for a clarification of that answer. But, if so, the estimated \$200 million of identifiable profits for a form of NFDM that was exported in 2008 that was not passed through to all producers in their milk prices was channeled instead to the plants that manufactured the SMP, and to their owners. And it still would not explain why the CWAP averages which contained substantial sales volumes under fixed-priced contracts did not lag behind **and above** the current NASS prices in 2008 when current prices were falling. And then more questions arise. If SMP is so highly prized by other nations, why did CWT recently decide to offer subsidies for exporting the product? And finally, there is the question about how long a high volume shelf-stable product, SMP, that is readily manufactured in large quantities and competes head to head with NFDM, should continue to be excluded from the price formulas for milk used to clear the market?

GROWTH MANAGEMENT PLAN GAINING INTEREST THROUGHOUT THE COUNTRY: *(By Rob Vandenheuvel)* California producers that read this newsletter have been hearing about the Growth Management Plan (GMP) for quite some time *(and if you haven't, please check out our article from last week's Update: http://www.milkproducerscouncil.org/q&a_gmp.htm).* But **the program has been getting an increasing amount of attention from other parts of the country as well.** On March 20th, a producer group in Vermont called "Dairy Farmers Working Together" (www.dfwt.org) is hosting a "Northeast Dairy Summit" in Burlington, VT. Dr. Chuck Nicholson from Cornell University (who provided the economic analysis of the GMP) will be presenting his analysis of the GMP at the Summit. In addition to the dairy leaders from the Northeast that will be in attendance, leaders from other areas such as California, the Southeast and more are expected to attend.

Producers throughout the U.S. are looking for solutions to this extreme milk price volatility, and the GMP appears to be the only plausible option being discussed. **I continue to urge producers to impress upon their coop and trade association managers the importance of supporting the Growth Management Plan.** We have a limited window of opportunity to make real policy change. If this opportunity passes without real change, and we are left with the boom/bust cycle that has become the status quo, we will only have ourselves to blame.

If anyone is interested in attending the "Northeast Dairy Summit," you can contact Dairy Farmers Working Together at 802-848-7466.

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