

Milk Producers Council

5370 SCHAEFER AVE. SUITE A - CHINO, CA 91710 - (909) 628-6018 - Fax (909) 591-7328

E-mail: mpc@milkproducers.org

Website: www.MilkProducersCouncil.org

DATE: October 24, 2008
TO: DIRECTORS & MEMBERS

PAGES: 4
FROM: John Kaczor

MPC FRIDAY MARKET UPDATE

CHICAGO MERCANTILE EXCHANGE

Blocks -\$0.0525 \$1.7375
Barrels -\$0.2150 \$1.6850

CHICAGO AA BUTTER

Weekly Change +\$.0100 \$1.7500
Weekly Average -\$0.0020 \$1.7480

NON-FAT DRY MILK

Week Ending 10/17 & 10/18

Calif. Plants \$.9314 12,233,991
NASS Plants \$.9840 25,883,514

Weekly Average

Blocks -\$0.0875 \$1.7825
Barrels -\$0.0750 \$1.8170

DRY WHEY

NASS w/e 10/18/08 \$.1916 WEST MSTLY AVG w/e 10/23/08 \$.1750

CHEESE MARKET COMMENTS: The cheese market is unsettled and antsy. Prices on the CME fell hard today to about where they were three times earlier this year, but a bit lower than the pattern that began the middle of last year. Clearly, there is concern about the ability of domestic and export sales to clear the market. The dreadful domestic economy has begun to affect cheese sales, as expected, and buyers are concerned about being caught with too much product on hand. Tightness of credit also has been mentioned as a reason why buyers may be putting off buying now on the hope that enough product will be available at reasonable prices when it is needed later this year.

BUTTER MARKET COMMENTS: Last week's report of continuing strong exports of butterfat products through August **and** Wednesday's report that butter and butterfat products in storage at the end of September was about 23% lower than last September **and** today's announcement that there will likely be a perceptible slowing in milk production because of CWT's herd retirement program, are bullish indicators for butter prices. However, the prospects for exports continuing at the surprisingly high level reported for August may be in question because of the turn-around in the U.S. dollar (which is more based on weakness in the economies of other nations rather than on the strength of the U.S. economy) and because New Zealand's milk production is recovering strongly. On balance, it looks like butter prices may be under some pressure, and without consensus for direction, over the next few months.

NONFAT POWDER MARKET COMMENTS: More sales to the CCC by California plants and lower national average prices paint a dreary picture for what can be expected. Despite record high exports this year, inventories have not decreased to the point where buyers believe they need to start negotiating for supplies and manufacturers seem to want to do almost anything to get the stuff out of their warehouses. International prices continue to move downward; domestic sales are stagnant at best. Prices are back to where they were in 2006. Based on discussions with Dairy Market News people, CDFA, and others, a plausible explanation why the sales to the CCC are being routed through a third party is to clear the balance sheets of inventory, rather than to improve cash flow. That makes sense.

WHEY MARKET COMMENTS: A glimmer of hope, possibly, is in the remark by DMN that the spot market for whey protein concentrate is showing some firmness. Every other product in the whey stream is either sitting at what is hoped to be the bottom or, in the case of lactose, still edging downward. Among other things, it's the strengthening in the U.S. dollar combined with tight credit and the weakening in international demand for virtually everything that is weighing (no pun) on this very important part of the milk disposal dilemma.

FRED DOUMA'S PRICE PROJECTIONS...

Oct. 24 Est:	Quota cwt. \$17.16	Overbase cwt. \$15.46	Cls. 4a cwt. \$13.75	Cls. 4b cwt. \$16.63
Last Week:	Quota cwt. \$17.21	Overbase cwt. \$15.51	Cls. 4a cwt. \$13.88	Cls. 4b cwt. \$16.64

SOME BACKGROUND ABOUT THE CME AND HOW IT WORKS: *(By J. Kaczor)* Not a week passes without reference to what has happened to Cheddar cheese and butter prices (and occasionally, nonfat dry milk prices) on the CME. It's important to follow those prices because they are the most current indication of changes in cheese and butter prices – two of the major three products that are used in milk price formulas in California and federal orders, and (we are told) by plants in unregulated areas that compete with plants that are regulated.

Disclaimer. CME Group and its predecessor, the Chicago Mercantile Exchange, stand behind the market it provides for Spot sales of Cheddar cheese, butter, and nonfat dry milk. They believe it represents a fair and open market for informed parties to buy or sell those products through bids and offers made in a public place under agreed upon rules. When criticized about the “thin” trading that takes place (few traders making few trades representing a small percentage of all sales), CME responds, quite correctly, by saying the CME Spot market offers a public way to determine current values for the products that are traded, and has not been represented as being useful or appropriate for setting milk prices. The idea to use the Spot markets for purposes of setting milk prices originated with milk producers, manufacturers, and distributors, and is supported by producers, manufacturers, and distributors.

Spot trading of butter in Chicago began in 1898. Spot trading of Cheddar cheese in Chicago began in 1997. (The National Cheese Exchange which had operated in Green Bay, Wisconsin, was closed down shortly before cheese trading began in Chicago.)

Some of the questions that have been asked include:

- Who are the people who make the trades that change the prices?
- How do the prices change?
- Where does this happen?
- What are the rules regarding payment and delivery of products that are traded?
- How are the rules enforced?
- How do buyers and sellers in different parts of the country get together?
- Can anyone find out who are the buyers and sellers and bidders?
- Who makes sure that the rules are followed and that inappropriate things do not happen?

The Spot market for the three dairy products mentioned above takes place in a designated place on the floor of the Exchange. The market is open Monday through Friday; each product is given about five to fifteen minutes to transact business. Bids to buy and offers to sell may be posted on a board prior to each session, and additional bids and offers may be made during the session. The bids and offers are handled exclusively by accredited commodity brokers on behalf of their clients, who can be anyone who has product to sell or who wishes to buy. If you want to buy or sell butter, cheese, or nonfat dry milk on the Spot market, you must contact a broker who has a license to trade.

The identity of bidders is not made public. When a bid to buy is made, the potential buyer does not know who and where the seller might be; likewise for potential sellers. The buyer and the seller must file a report with the CME Market Regulation Department by 3:00 p.m. the day of the trade to disclose their identity. (Although it is not public information, there are some reports that participants generally know which brokers represent which clients.) In cases where an offer or a bid moves a price, the identity of the broker who made the offer or bid is recorded.

A sale is a sale. The seller agrees to follow the buyer's instructions on when to ship the product. **The buyer pays the freight cost**, but can receive an allowance from the seller to cover part of that cost. Payment for butter is made the first business day after the sale; payment for cheese is made within three days of the sale. Payment is made through charges and credits through registered accounts.

Butter is sold f.o.b. Chicago. The buyer receives a predetermined allowance **from the seller** depending on how far the point of delivery is from Chicago. The maximum allowance is \$.055 per lb for deliveries beyond 1,600 miles from Chicago. Cheese is sold f.o.b. Green Bay, Wisconsin. The allowance the buyer receives **from the seller** depends on the distance between buyer and seller, and how far the seller is from Green Bay. (Simple examples: if the buyer and seller are located in central California, no allowance is given; if the seller is located in Wisconsin and the buyer is located in central California, no allowance is given; if the seller is located further away from Green Bay than from the buyer, the buyer receives an allowance for the freight from the seller's location.) In addition to allowances for delivery, other allowances include how long and where and how butter has been stored, and the moisture content of cheese, and others.

The Exchange has established rules for product grades, packaging requirements, and sizes of transactions. A "carlot" of butter (40,000-43,000 lbs) is the specified transaction size for butter; a "carload" of cheese (40,000-44,000 lbs) is the specified transaction size for cheese. Prices change (up or down) when an offer to sell or a bid to buy is accepted at a price that is different from the existing price. Prices also change (down) when **an offer to sell at a price lower** than the existing price is not covered, or (up) when **a bid to buy at a price higher** than the existing price is not accepted. Failure to follow through on a bid or offer is subject to fines and reprimands, and could lead to suspension of trading privileges. Disputes between parties are resolved by the CME.

Concerns about manipulation of prices in a "thin" market are valid, but the CME and industry participants generally agree that there is little evidence of manipulation, and if it occurs it likely cannot be sustained for very long because of the number of parties who represent all aspects of the dairy industry can and do observe the daily activity. While sales on the Spot market represent a very small percentage of all sales, the description of the CME Spot markets for dairy product as thin is disputed because almost all butter and cheese cash and contract sales use the Spot prices as a reference point, and there are few who propose discontinuing its use. **The point made is that it is thin in fact but is very broad in practice.** Even so, there are some who say it is disconcerting to note that a single transaction on the Spot market, whether or not it involves a trade, does affect the value for virtually all cheese that is sold in the U.S.

The CME has in the past four years improved its oversight of the dairy Spot market. Among other controls, a "market surveillance analyst" is assigned to the Spot market to review transactions and consider possible connections between Spot trades and positions held on the futures market, and an investigator looks for signs of price manipulation and may interview brokers, buyers, and sellers about particular actions. The end.

COLD STORAGE REPORT FOR SEPTEMBER: *(By J. Kaczor)* The amount of butter, butteroil, and anhydrous milkfat in storage at the end of September was **46 million lbs less than last September** and is tracking closely with 2006 levels. This very good news was greeted with a yawn by butter traders yesterday. The amount of American cheese was 13 million lbs higher (2%) and the amount of all cheese was 19 million lbs higher. Cheese was steady yesterday on the CME, but fell hard today.

CWT ANNOUNCES SECOND HERD RETIREMENT PROGRAM IN 2008: *(By Rob VandenHeuvel)* This morning, Cooperatives Working Together (CWT) announced a second Herd Retirement Program (HRP) for 2008. According to the press release (which can be found at <http://www.cwt.coop>), bids will be accepted from now until November 24th. This very encouraging news comes after numerous industry groups, including Milk Producers Council, urged CWT to implement an additional HRP this year (*you can read MPC's letter to CWT on our website: <http://www.milkproducerscouncil.org/091808cwt.pdf>*).

WE NEED TO SPREAD THE WORD: PROPOSITION 2 SETS A DANGEROUS STANDARD: *(By Rob VandenHeuvel)* If you're like most Americans, you are probably sick of campaign advertisements by now. But for the next 11 days, we will be bombarded with campaign ads for the various political offices, as well as the 12 statewide propositions on the upcoming ballot.

One of those measures is Proposition 2, which would turn back the clock on modern farming practices for raising chickens, pigs and veal calves. With almost no major pig and veal presence in California, this measure is mostly aimed at the California chicken and egg industry.

You've probably already seen some of the emotional ads sponsored by the Humane Society in support of Proposition 2. These animal rights **extremists** are preying on the emotions of an uninformed public, hoping that voters will blindly follow. **The truth is that this proposition ignores decades of research on animal welfare and food safety that have led to the modern farming practices we have today.**

Fortunately, those that have seriously considered the ramifications of Prop 2 have agreed that it is a misguided public policy for California. Just look at the major newspapers throughout California. Liberal papers like the *LA Times* and the *San Francisco Chronicle*, and many other major papers throughout the state, are opposing Prop 2. They see serious flaws with the measure, not the least of which is that it will drive the chicken and egg industry out of California to other states (or possibly other countries) that allow modern and safe farming practices to be used.

Californians for Safe Food (<http://www.safecaliforniafood.org>) is a coalition aimed at stopping Proposition 2. Milk Producers Council has been a supporter of this coalition. I urge you all to visit their website and see the expansive list of veterinarians, food safety and public health experts, agricultural groups, labor groups, elected officials and many others that have supported this coalition and oppose Proposition 2. While this measure is not directly aimed at dairies, it is a foot-in-the-door for allowing these extremist groups to ignore modern, science-based farming practices and tell you how to run your farms. **They need to be stopped now.** Please tell your neighbors and friends how important it is to defeat Proposition 2. **And then make sure to vote!**

TWO MORE WORKSHOPS NEXT WEEK ON UPCOMING WASTE DISCHARGE REQUIREMENTS FOR CENTRAL VALLEY DAIRIES: *(By Rob VandenHeuvel)* Next week, there will be two more workshops looking at the paperwork that must be filed by December 31st under the new "waste discharge requirements" for dairies in the Central Valley. The workshops will be held in Glenn (Tuesday) and San Joaquin (Thursday) Counties. For more information on times and locations, please see CDQAP's flyer posted on our website: <http://www.milkproducerscouncil.org/fall08wdrworkshops.pdf>.

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