

Milk Producers Council

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MPC FRIDAY MARKET UPDATE

CHICAGO MERCANTILE EXCHANGE

Blocks +\$.0025 \$1.8125

Barrels +\$.0275 \$1.7550

Weekly Average

Blocks +\$.0080 \$1.8085

Barrels -\$.0220 \$1.7410

CHICAGO AA BUTTER

Weekly Change +\$.0125 \$1.3725

Weekly Average -\$.0025 \$1.3650

DRY WHEY

NASS w/e 3/29/08 \$.2453 WEST MSTLY AVG w/e 4/03/08 \$.2600

NON-FAT DRY MILK

Week Ending 3/28 & 3/29

Calif. Plants \$1.2391 15,470,736

NASS Plants \$1.2415 24,020,799

CHEESE MARKET COMMENTS: The cheese market appears to be steady at the moment. Production is increasing as more milk shows up in the receiving bays. Sales are reported to be good. Imports continue lower than last year and exports are continuing at their recent good levels. Inventories are expected to remain under control. Prices on the CME this week should be described as good, but not solid. Barrel supplies appeared to be heavy and prices moved down two days, followed by increases. The price gap between blocks and barrels narrowed a bit. Production of cheese in February, up 1.1% per day from a year earlier, was announced after the market's close today.

BUTTER MARKET COMMENTS: Despite production continuing at near record levels, there are positive comments this week from Dairy Market News about the steadiness, even strength, of the butter market. Imports are lower and exports are higher, and domestic demand is said to be surprisingly strong for this time of year. There are some reports of concern about adequate supplies later this year. That sounds like speculators trying to stir things up. Speculators strive on uncertainty and confusion. Butter production for February, up 5.5% per day from a year earlier, was announced after the market closed today.

POWDER MARKET COMMENTS: Spot prices for nfdm in the central and western regions moved up again this week. The reason given by DMN for the movements is that stocks are in better balance than in recent months and supplies offered by plants were lower. Sales volumes reported by California plants and by NASS have been very high, with much of it believed to be for the export market. Prices reported for these recent sales do not reflect DMN's spot prices – the California average price last week fell by about 7 cents and the NASS price by about 2 cents. But a flattening out of prices after they drop back down every other week or so does give some hope that the bottom has been reached and higher prices may be ahead. Production of nonfat powders in February was announced today. Production of nonfat dry milk was 18% higher per day than a year earlier. **Production of skim milk powder was 196% higher per day than a year earlier. The combined production was up by 36% on a per day basis.** That point about stocks being in better balance will be checked.

WHEY MARKET COMMENTS: DMN reports that export volume remains good, domestic sales are good, and inventories are reported to be in fairly good position. They say **the whey market has a firming undertone.** But, as is true with weekly sales of nfdm, the sales reports by NASS for dry whey do not reflect anything but flat prices. The firming undertone may be coming in part from the futures market for dry whey. While the volume for whey futures is still not to the point where it should be used as a reliable basis for decision-making, the pattern of changes in that market is starting to become more logical. Production of dry whey in February was reported to be down by 5.8% per day compared to a year earlier. That does help the inventory situation. Increased production of whey protein concentrate accounted for usage of the rest of the wet whey.

FRED DOUMA'S PRICE PROJECTIONS...

April 04 Est: Quota cwt. \$17.45 Overbase cwt. \$15.75 Cls. 4a cwt. \$14.33 Cls. 4b cwt. \$16.29
Last Week: Quota cwt. \$17.87 Overbase cwt. \$16.17 Cls. 4a cwt. \$14.35 Cls. 4b cwt. \$16.94

LATEST U.S. MILK-FEED PRICE RATIO SPELLS RED INK FOR PRODUCERS: (By J. Kaczor) Last week, USDA published its estimate of the **U.S. milk-feed price ratio** for March. (The ratio is a measure of how many lbs of a standard feed ration can be bought relative to the current national average milk price.) **The number is 2.05**, meaning the price for a lb of milk equals the cost of 2.05 lbs of that standard feed ration. Most producers understand that the feed ration that is used in the U.S. M-F ratio is not what is actually being fed to cows, and the milk price that is used is a national average so, generally speaking, that number itself is not meaningful to them. But the index can be looked at as a barometer, good for measuring changes, and is used by those who have an interest in how much milk may be produced in the future and what quantity of dairy products may become available.

The U.S. feed ration model in the index consists of 51% corn, 8% soybeans, and 41% alfalfa. Its purpose is to provide a guide that is general enough to be understandable to almost anyone who has an interest in dairy industry issues and activities. The following table shows the prices used to compute the ratio for March and comparable months.

	February 2007	March 2007	February 2008	March 2008
Corn, bu	\$3.44	\$3.43	\$4.53	\$4.83
Soybeans, bu	6.87	6.95	11.70	11.90
Hay, ton	115.00	121.00	138.00	143.00
Milk, cwt	14.90	15.60	19.10	18.30
Milk-Feed Ratio	2.33	2.39	2.34	2.05

By coincidence, the two lowest months in 2007 were February and March. The ratios for the two lowest months in 2006 were 2.32 and 2.33. Remember 2006? The February comparisons suggest that the \$4.20 per cwt increase in the average milk price was almost completely absorbed by increases in feed costs. (The blend prices in California also increased by more than \$4.00 per cwt; did higher feed costs take that entire increase away?) **The March ratio is the lowest reported for any month in the past 24 years.** That strongly suggests that the **current cost** of feed is very high relative to the **current price** for milk, and "gross margins" for milk producers (the difference between feed costs and milk prices per pound, per cow, or per dairy) may be the lowest in a generation. The experts are opining that there is now a huge incentive developing for producers with suitable land to shut down their dairy operations and begin to grow crops, for some to re-think plans for expansion, and for others to simply retire. That mind-set has already resulted in some **projections for lower rates of increased milk production** in the U.S. later this year, and **for corresponding increases in the prices of various dairy commodities and, of course, milk.** They could be right. Contributing to the recent positive "sense of the market" is the implementation of base production plans affecting the majority of producers in California and the current favorable balance between imports and exports of major dairy commodities.

Producers who keep track of the total amount spent for feed in a given period compared to the gross revenue for their milk sales, probably also have a good idea of their future feed costs, and are now facing what could be critical decisions about what to do. The almost unanimous sentiment for corn and soybean meal prices is to expect continuing increases through this year. (Yesterday, corn prices for April on the Chicago Board of Trade reached \$6.00 per bushel.) For milk prices, it's beginning to look like there may be a plausible case building for a better than expected second half of the year. The critical question is will better milk prices be able to keep pace with higher feed and operating costs and, if so, does that mean gross margins are only as good as they are going to be? Those who may want to draw a parallel with 2006 should consider how much lower milk prices and feed and operating costs were then compared to now, and should consider what are the prospects for current milk prices to outpace costs, which is something that appears to be required in order to restore gross profits.

SOME INTERESTING FACTS ON DAIRY FARMING IN THE U.S.: (By Rob VandenHeuvel) Recently, one of our members mentioned an interesting fact that I thought I'd pass along:

- According to USDA's National Agricultural Statistics Service (<http://www.nass.usda.gov>), in 1944, the U.S. reached its peak with **25,597,000 milk cows**. These cows produced about 117,023,000,000 lbs. of milk.
- Last year, there were approximately **9,158,000 milk cows** in the U.S., producing about 185,602,000,000 lbs. of milk.

In other words, when comparing 1944 to 2007, U.S. dairy farmers now produce 59 percent more milk with 64 percent less cows! Through improvements in feed and nutrition management and better cow comfort, U.S. dairy farmers have made the modern dairy cow incredibly efficient. So the last 63 years has brought a 64 percent reduction in the milk cow population – can automakers make that same claim? **Remember that the next time someone tries to blame cow burps for the growth in “global greenhouse gases.”**

REMINDER – FSA TOWN HALL ON DISASTER RELIEF NEXT WEDNESDAY: (By Rob VandenHeuvel) this is a final reminder for those of you interested in filing for the Dairy Disaster Assistance Program (DDAP-III). As I've mentioned in prior newsletters, the San Bernardino and Riverside County Farm Service Agencies (FSA) have scheduled a town hall meeting on Wednesday, April 9th at 10 am at the Chino Fairgrounds/Brinderson Hall. Dairies in these counties should have received a flier in the mail announcing this meeting. If you didn't receive the flier, it can be found at: <http://www.milkproducerscouncil.org/0408ddapflyer.pdf>. **The deadline to sign up for these benefits is May 4th. If you're able, please bring a copy of your annual 2003-2007 creamery statements and inventory records to the meeting next Wednesday.**

AN OUTSIDER'S PERSPECTIVE ON CALIFORNIA'S CURRENT DAIRY CLIMATE: (By Ben Yale, *Courtesy of Dairy Producers of New Mexico*) The most recent newsletter for the Dairy Producers of New Mexico featured a column by Ben Yale – an attorney who works extensively on Federal milk pricing issues. The piece was entitled “California Nightmare.” I thought our readers would appreciate seeing an outsider's perspective on California's current milk situation.

California Nightmare

By Ben Yale

Dairy farm policy in much of the United States since the late 19th century has been one to protect dairy farmers from other dairy farmers. That is, by assuring every producer fundamentally the same price for milk regardless of its use, or volume, prices for milk could be increased based upon use. This classified pricing and pooling system has done its job well. For example, where early in the 20th Century, very little milk was of sufficient quality for drinking, today nearly 99% of the milk produced today is Grade A. At the same time, production of milk continues to grow; we are approaching 200 billion pounds per year nationwide.

As I have explained in earlier columns and at presentations, these pricing and pooling programs have their limits. They were designed in the 19th century to satisfy nearby markets for milk (less than 100 miles). Today, milk and milk products move from border to border and also internationally. Last year, the international market dictated domestic milk prices for the first time. Despite such radical changes in markets and supplies, our system is still based upon the antiquated regional marketing model. In addition to ten federal marketing orders, there are several state marketing orders and areas that are unregulated. Although the regulations play within their defined markets, because those regulated markets overlap and interact with other regulated and unregulated markets, it is an illusion that such regulations control the pricing and marketing. Interfere would be a more accurate term.

California dairy regulations and markets today show how a system that once worked well has outgrown its effectiveness and is now a hindrance to orderly marketing. Presently, the following market conditions exist in California:

- California mandates that California plants pay minimum prices based on use. The only exception is that cooperative plants can pay their members less than the minimum price.

- California dairymen are producing more milk than ever before and more than their plants can handle.
- Some California dairymen are being told to dump their milk because there is no home for the milk.
- Some cheese plants are working at less than capacity. The California price for milk use in making cheese (Class 4b) is based upon the Chicago Mercantile Exchange (CME) price. That price is being held up by a few buyers because there is a lack of inventory in cheese which is due to the fact that the price for milk used in cheese is too high and plants fear a drop in milk prices and, consequently, the value of their inventory. Less cheese made, more cheese demanded, higher prices for cheese, higher prices for milk in cheese, higher prices in cheese, less cheese made, more cheese demanded and so on and so forth.
- At the same time powder plants are at and over capacity. Powder inventory continues to climb and prices for NFDN drop (50 to 60 cents in the last several months).
- The milk that is not made into powder or other dairy products is dumped and its value is zero.
- Because cheese plants must pay the minimum price, they cannot purchase any of the distressed milk. Instead the distressed milk is moved out of state at steeply discounted prices or dumped. Anecdotally, some cheese plants are taking advantage of the state border and the back haul and bringing in out of state milk at a discount to remove capacity for in state milk processing.
- At the same time that cheese prices remain high, bottled milk prices remain high. Higher milk prices have caused a small reduction in demand for the milk, hence less processing capacity there.
- A plant in Fresno is reducing its processing and approximately 25 producers have been notified that their contracts end in June. No one else wants their milk.
- To add to the woes of the California system, bottling plants outside of California are shipping milk into California (about 20% of the bottled milk). Two years ago, some dairy producer organizations and others promoted a bill in Congress that was purported to stop a plant in Arizona from shipping milk into California. The price for that bill was authorization for a permanent exemption from federal rules on milk processed in Nevada. Two new plants in Nevada are now shipping milk into California and that Arizona plant, still shipping.
- For a whole lot of reasons, not just dairy regulations, no new cheese plants have been built for years in California. Two cheese plants have closed in recent months. There is a new and modern powder plant near Visalia, but that will not be enough.
- All along, because producers receive a blend price, the same price as their neighbor, growth continues. Even today new dairies are going up.
- The result is that some cooperatives are now instituting base programs for paying producers and reblending members for the value of the dumped milk.
- A major part of the solution would be to allow plants to purchase distressed milk rather than have it dumped or sent out of state. Federal orders have allowed that for decades.
- The California regulatory system, touted as quick to respond to needs, cannot do that because it requires legislation to change.
- Growth in international markets for cheese are being largely satisfied from plants in Idaho and the Southwest due to the pricing regulations in California.

What does this bode for the rest of the dairy industry? First, California's problems, though self-inflicted, also are our problem because California is very much a part of our national and international marketing. Just as a drop of lemon can sour a gallon of milk, if California cannot sell what it produces, we will smell it. Second, this collapse of the regulatory markets signals a future for the FMMO system as well. Although it has a number of relief valves, it is not immune from the economic forces now at work not the least of which is California's system imploding. Third, when California comes up with a patch that mitigates this crisis and restores some order to its marketing, and it will, it can only do so by shifting the costs and the risks of its "cure" on the rest of the nation.

A national policy designed both for domestic and international markets rather than regional self-centered programs for domestic markets would solve the crisis in California and benefit the nation as a whole. Hopefully, the California nightmare does not become a reality for the rest of us.