

MPC WEEKLY FRIDAY REPORT

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 TO: DIRECTORS & MEMBERS
 FROM: KEVIN ABERNATHY, GENERAL MANAGER
 PAGES: 8



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MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE			CHICAGO AA BUTTER			NON-FAT DRY MILK		
Blocks	+ \$.0175	\$1.6850	WEEKLY CHANGE	-.0125	\$2.2700	WEEK ENDING 04/20/19		
Barrels	+ \$.1150	\$1.6300	WEEKLY AVERAGE	-.0090	\$2.2635	NAT'L PLANTS	\$0.9680	26,257,904
WEEKLY AVERAGE CHEDDAR CHEESE			DRY WHEY			PRIOR WEEK ENDING 04/13/19		
Blocks	+ \$.0166	\$1.6785	DAIRY MARKET NEWS	W/E 04/26/19	\$3.787	NAT'L PLANTS	\$0.9543	27,773,869
Barrels	+ \$.0270	\$1.6020	NATIONAL PLANTS	W/E 04/20/19	\$3.903			

CALIFORNIA FEDERAL MILK MARKETING ORDER PRICE PROJECTIONS

PRICE PROJECTIONS	CLASS I ACTUAL (RANGE BASED ON LOCATION)	CLASS II PROJECTED	CLASS III PROJECTED	CLASS IV PROJECTED
APRIL 26 EST	\$17.36 - \$17.86	\$16.42	\$15.97	\$15.81
APRIL 22 EST	\$17.36 - \$17.86	\$16.42	\$15.92	\$15.83



Milk, Dairy and Grain Market Commentary

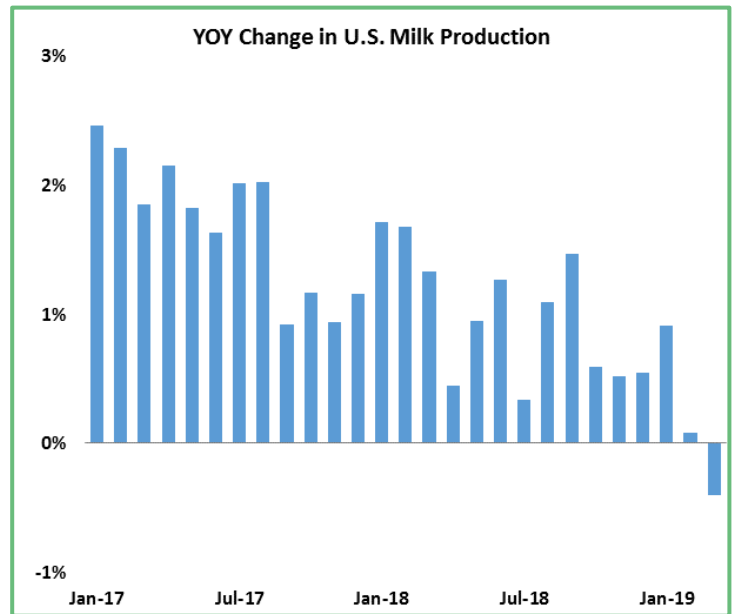
By Sarina Sharp, Daily Dairy Report
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Milk & Dairy Markets

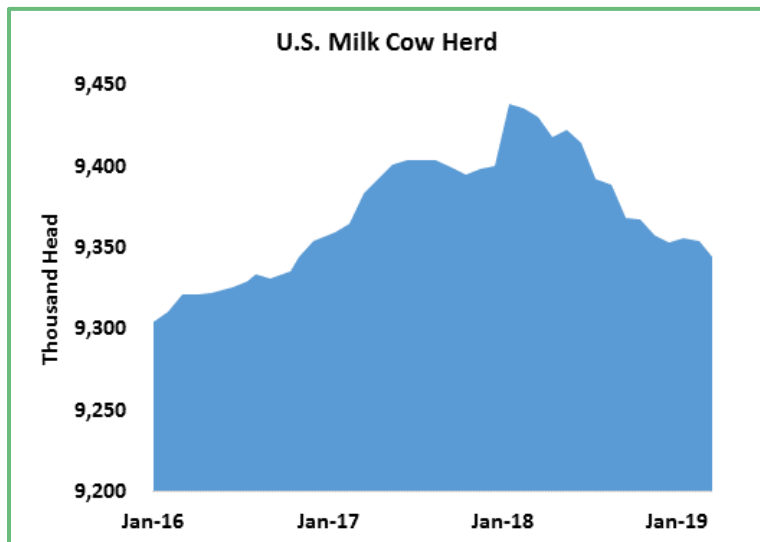
The dairy markets have had a slew of data to digest in the past two weeks, providing plenty of fodder for the bulls. The Global Dairy Trade (GDT) auction kicked things off last Tuesday with a mostly higher performance. Strong gains in butterfat products and cheese more than offset a 0.7% decline in the average winning price for whole milk powder (WMP), allowing the GDT index to inch up 0.5%. That marks the index's tenth consecutive increase, its longest winning streak since the GDT made its debut in 2008.

U.S. trade data for February echoed the GDT; butterfat and cheese exports impressed, while milk powder shipments stalled. Exports of nonfat dry milk (NDM) fell 17% short of February 2018 volumes. Cheese exports jumped 16% from the prior year and reached the second-highest daily average volume on record. Cheap cheese attracted new business in spite of stepped-up tariffs. Sales to Mexico climbed 9% from a year ago. Shipments to South Korea surged 71%. Thankfully, U.S. cheese prices have rallied considerably since the turn of the year. However, this suggests that cheese exports may slow in coming months as buyers no longer view U.S. cheese as a bargain.

Perhaps the biggest news this week came from USDA's Milk Production report, which showed March milk output at 18.9 billion pounds, down 0.4% from a year ago. That's the first year-over-year decline in national milk output in six years. Modest improvements in milk production per cow were more than offset by a marked decline in cow numbers. In USDA's previous report, the agency reported no change in cow numbers from January to February, despite record-breaking February dairy cow slaughter. The agency amended its error, reporting a still perplexingly low 2,000-head decline in February and a further 10,000-head reduction in March. At 9.344 million cows, the dairy herd is 86,000 head smaller than it was a year ago. Judging by slaughter volumes and auction lineups, contraction continues.

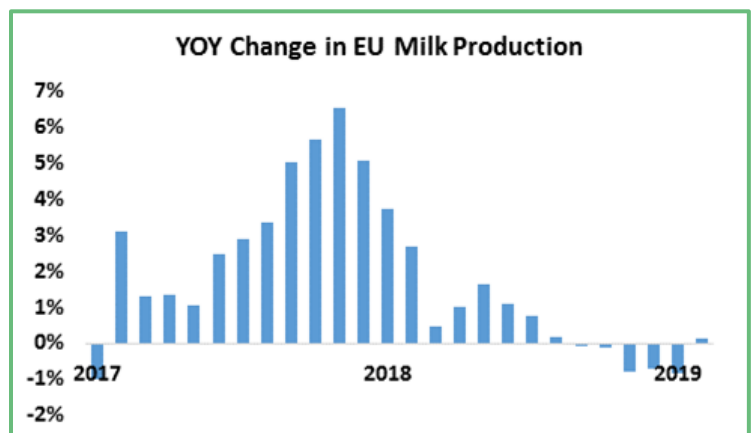


Less milk and more processing capacity is making for a tight milk market in the Midwest despite the spring flush. Spot milk is selling at par with Class III, compared to an average discount of \$3 per cwt. at this time last year. That will make cheese producers think twice about topping up vats and stocking warehouses with Cheddar barrels. American-style cheese inventories are already becoming less burdensome. They did not move appreciably higher from February to March and end-of-March stocks stood just 2.3% above year-ago levels. Inventories of cheese of all varieties on March 31 were 4.3% higher than the prior year.



On the other side of the Atlantic, milk output is holding steady. European milk collections totaled 26.7 billion pounds in February, up just

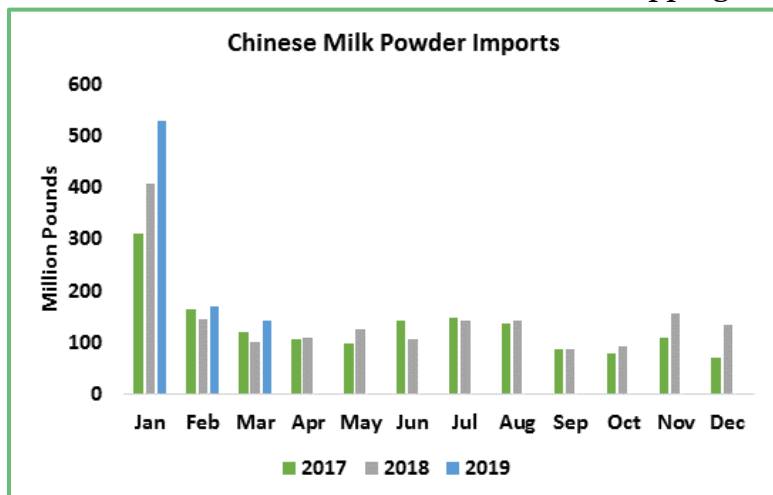
0.1% from the prior year. That's a shift to the plus column after five months of deficits, but it's a rather paltry increase. Collections were 29 million pounds higher than in February 2018, roughly equivalent to a single day's milk output in Michigan or Pennsylvania, or six hours of production in California.



In New Zealand, milk collections are slumping as the season wanes. In March, fluid milk output fell to 1.713 million metric tons, down 8.2% from the prior year. For the season to date, collections exceed the 2017-18 season by 3.2% on a fluid basis, while milk solids collections are 3.5% higher than last season. Parched pastures are likely to continue to weigh on milk yields; full

season collections are expected to be up 3% from last year. That's a sizeable increase, but it represents a disappointing finish for New Zealand's dairy producers after a very strong start.

Meanwhile, New Zealand's dairy product exports remain strong, which is likely depleting dairy product inventories. Robust demand from China is chipping away at the world's once-burdensome milk powder

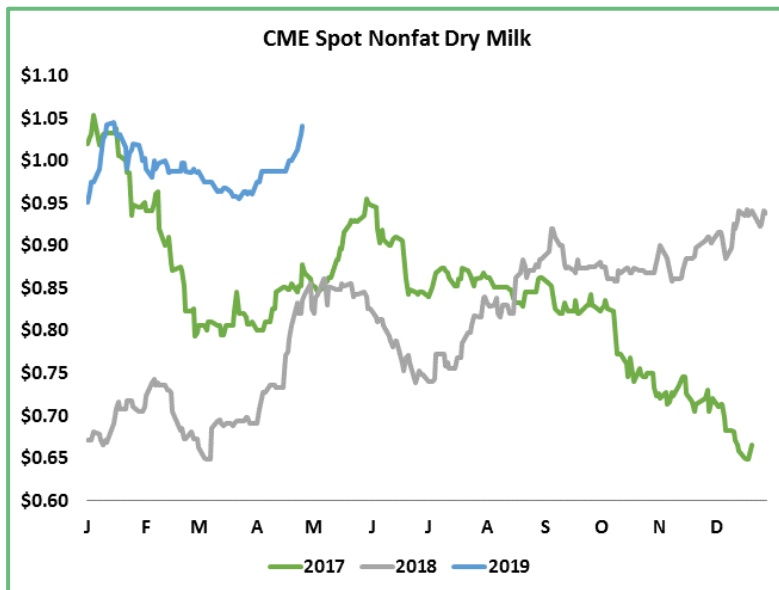


stockpile. In March, China imported 60.6% more WMP than it did in March 2018, and China stepped up skim milk powder (SMP) imports by 15.3%. For the year to date, Chinese milk powder imports are up 29%. First-quarter milk powder imports were the second-highest on record, trailing only the sky-high volumes set in 2014.

As African swine fever sweeps through China's hog herd, Chinese demand for whey for feed rations has plunged. Chinese whey product imports fell 27.1% from the prior year in March, pushing year-to-date volumes down

15.8%. Bludgeoned by the trade war, U.S. whey continues to lose market share. Chinese imports of U.S. whey products in March fell to their lowest daily average volume in more than eight years. The U.S. share of Chinese whey product imports dropped to 29.7%, its lowest point since September 2007.

The loss of sales to China has clearly taken a toll on U.S. whey prices. CME spot whey slipped to 32.75¢ per pound today, down 3¢ in the past two weeks. But the bulls bellowed in the other dairy product markets. Spot butter climbed 1.25¢ in the past two weeks and closed today at \$2.27. Cheddar blocks added 4¢ and reached \$1.685. Barrels retreated last week but then came roaring back. They closed today at a new 2019 high of \$1.63, up 1.25¢ over the past two weeks. Spot NDM has not posted a single day in the red all month. It climbed today to \$1.04, up a formidable 5.25¢ in the past two weeks. The futures are looking much stronger as well. May through September Class III contracts are more than 40¢ higher than they were in mid-April, and most Class IV contracts logged gains of a similar magnitude. Compared to the same period in 2018, April through December Class III futures are \$1.71 higher, and Class IV contracts are up \$2.29.



Grain Markets

Bumper harvests in South America are weighing on crop prices. 2019 corn futures posted life-of contract lows this week, although they bounced back in the final trading sessions. July corn settled today at \$3.6125 per bushel, down 8.25¢ from mid-April. July soybeans closed at \$8.67, down more than 40¢ over the past two weeks.



How We Got the Fixed Differential

By Geoff Vanden Heuwel, Director of Regulatory & Economic Affairs
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A few weeks ago, I wrote an [article](#) for the MPC Friday Report that told a bit of the history of how the California quota system came into being back in the 1960s. I linked that article to some very informative histories that have been put together which give perspective and context to why producers at that time did what they did. I mentioned in that article that maybe someday I would tell my version of how the fixed \$1.70 quota differential came into being in the early 1990's. Well, here goes.

I will start this story with the passage of 1977 Farm Bill. That bill raised the Federal Support Price for milk from \$8.26 per cwt. in 1977 to \$13.49 in 1981. You can imagine what a \$5 per cwt. increase in the milk price did to production in the United States, and especially in California. It skyrocketed. The only limiting factor for California producers was the fact that we did not have enough plant capacity to handle all that new milk, so the state responded by raising the make allowance as an incentive to build more processing plants. California milk production doubled in the decade that followed, passing Wisconsin as the nation's #1 milk producing state in the early 1990s.

With that information as a back drop, let's look at the quota story. When the system started in 1969, all the producers then in business received California "production base" for all their milk production during the base period of 1965/66. They were then issued pool quota based on what percentage of their "production base" was used as class 1 (fluid milk) during the base period. Right away, some producers got more quota than others because they were selling to plants that had a higher class 1 utilization than other plants. BUT the commitment was there to eventually cover everyone's "production base" with quota as new class 1 sales took place in subsequent years. Class 1 sales growth was slow.

Consequently in 1976/1977, "blue sky" quota was issued to all of the original 1969 producers so that everybody was "equalized." By 1977, the original intent of the pooling program was met. We had a statewide pooling system that allowed all producers to share in class 1 proceeds regardless of where they shipped their milk because everyone had quota. The original crafters of the pooling system never imagined that California dairy farmers would be willing to produce milk for "overbase" prices. Enter the 1977 Farm Bill.

With the price of milk shooting up, not because of any market demand, but because of federal law that committed USDA to purchasing butter, powder and cheese at

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prices which would enable dairy product manufacturers to pay at least the support price for milk, it was a whole new ball game in the California dairy industry. Suddenly producing overbase milk was profitable and having quota was not that big of a deal. The higher make allowance in California brought about the California cheese industry with big increases in butter and powder production not far behind. The days of California being just a fluid state were over and we became a major player in the manufactured dairy product market.

In the early years, the biggest buyer of this increased California production was the federal government and eventually something had to happen – so it did. Starting in 1981, the federal government began to ratchet back the support price and implemented a variety of programs to cut milk production. You might remember the milk diversion program of 1983 or the whole herd termination program of 1985. So, the economics were getting tougher on producers in California as huge amounts of milk were now being produced. This milk was not covered with quota and the state’s ability to help producers by raising class 1 prices was limited because all class 1 money went only to the quota holders. Eventually the concerns of overbase producers got to a point where the legislature got involved and asked the California Secretary of Agriculture to set-up a Dairy Industry Review Committee to come up with some answers.

That committee was established in 1991 and started its work by holding seven meetings around the state to take input from producers on two specific questions: “What problems, if any, are there in the pooling and quota system?” and “What long-term improvement, if any, can be made in the pooling and quota system to strengthen the program for all producers?” You can read the 1991 meeting notice and committee roster [here](#).

These meetings were set up with the Dairy Industry Review Committee sitting at a table in the front of the room and anybody could come up and speak. The committee members would ask questions and engage with the speakers and each other, with a court reporter transcribing the meetings. After the series of meetings was concluded, the Dairy Industry Review Committee began regularly meeting in Modesto and working its way through the issues and developing and debating various options for change. It took a while, but it was a serious group of producers with varied perspectives and experiences that in good faith wrestled with how to proceed. The reality we struggled with was that milk income was too low and the state believed that it was very limited in raising milk prices for butter/powder and cheese because it felt we needed to keep our manufacturing plants operating. Therefore, class 1 was the only price that could be raised without hurting sales, but increased class 1 money would only go to the quota holder and there were now a lot of producers who did not have much or any quota.

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Eventually the solution emerged. We would fix the differential between quota and overbase at its historic average of \$1.70 and then the state would significantly raise the class 1 price. Because the differential was fixed, the extra class 1 revenue would then flow over to the overbase price. That

was essentially the deal. The overbase producer received access to class 1 money in exchange for giving the quota holder a fixed return on the quota. It took a while to get all this put in place, but on January 1, 1994 the fixed differential took effect and the class 1 price was simultaneously raised by nearly \$2 per cwt. As a member of the Dairy Industry Review Committee, I was proud of this compromise which was done to help all producers, but especially the overbase producers who for the first time had access to class 1 revenue.

But of course, that is not the end of the story. Now that California class 1 prices had been raised to very high levels, opportunity to exploit the inherent weakness of a state milk marketing order came into play.

Because a state may not regulate interstate commerce, those high class 1 prices became a magnet for out of state milk coming into California and skimming off those class 1 dollars. Very soon after the implementation of the fixed \$1.70, out of state milk began coming in. The industry tried a variety of regulatory methods to try to stem the tide, but at the same time the state began to lower class 1 prices to try to limit the huge financial incentive for out of state milk to come in here.

Obviously, lowering class 1 prices diminished the benefit to overbase producers that they thought they were getting with the fixed differential, but overall the fixed differential was still a positive. And of course, to have any benefit from class 1 sales in California we had to stem the tide of out of state milk. In the end, none of the state's regulatory fixes proved successful and the only thing that kept the flow of out of state milk from growing is that the class 1 prices were moderated to a point where the hauling cost to bring out of state milk into California became the limiting factor.

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Meanwhile the California industry continued to grow. We had our ups and downs. Collectively producers came to a point where the high make allowance policies of CDFR were opposed. The policy received a nickname called the "California discount" and pressure for change mounted. In the subsequent years, California's cost of production competitive advantage on the rest of the country had diminished and running a state order that could not regulate interstate commerce and insisted on establishing discounted prices for manufacturing milk became a problem that required a change.

The cooperatives took the lead in proposing a Federal Milk Marketing Order for California that would address these fundamental problems with the state order. It took years, but that has happened and most California producers should have more money in their pocket today because of the FMMO than they would have had otherwise. However, there is this lingering question about quota and how does it fit into where we are today. It appears that question is the next challenge facing California producers.

We have faced tough issues before and dealt with them. This issue should be no different. We stand on the shoulders of those who went before. Each generation in its time did its best to address the problems of its day. I am confident that this generation will do the same.

**U.S. House Agriculture Committee to Hold Hearing
Reviewing State of Dairy Economy on April 29**
By Geoff Vanden Heuvel, Director of Regulatory & Economic Affairs
Geoff@MilkProducers.org



The Livestock and Foreign Agriculture Subcommittee will hold a hearing on Tuesday, April 30 at 10 a.m. titled, "Reviewing the State of the Dairy Economy." This hearing was called by

Congressman Jim Costa (D-Fresno), Chairman of the subcommittee and member of the U.S. House of Representatives' Committee on Agriculture. MPC extends its appreciation to Congressman Costa for elevating this critical issue in Congress.

The hearing will be livestreamed on the House Ag Committee website at <http://agriculture.house.gov>, however the page to listen to the hearing has not been created yet. Be sure to check the website before 10 a.m. on Tuesday, April 30 to find the link to the hearing.



NBC Left Field: Can California Get Cows to Burp Less Methane?

By Kevin Abernathy, General Manager

Kevin@MilkProducers.org

NBC Left Field, a video unit of NBC News aimed at “understanding human beings through film, technology and heaps of creativity,” recently published a short documentary featuring efforts to reduce methane from the beef and dairy sectors. The roughly 12-minute video titled, “Can California Get Cows to Burp Less Methane,” features interviews with a beef rancher, scientists and Michael Boccadoro, Executive Director of the [Dairy Cares](#) coalition. Dairy Cares also contributed video footage to the documentary. See the video [here](#).



Los Angeles Times: California Utilities Use Wildfires as an Excuse to Wring Ratepayers Dry

By Michael Hiltzik

From Kevin Abernathy, MPC General Manager

MPC holds a seat on the Agricultural Energy Consumers Association (AECA) Board of Directors, which represents the interests of more than 40,000 agricultural operations from Redding to San Diego. The primary goal of AECA is controlling the rising costs of energy. This article was forwarded to me by AECA and we thought it was worth sharing with our readers.

Los Angeles Times

California Utilities Use Wildfires as an Excuse to Wring Ratepayers Dry

By Michael Hiltzik

It always was predictable that California’s utilities would ask for a heap of government assistance to cover their financial liabilities resulting from two years of epic wildfires.

What wasn’t so predictable was how deep they would try to reach into their customers’ pockets.

Now we know. As [my colleague Sammy Roth has reported](#), Southern California Edison, Pacific Gas & Electric and San Diego Gas & Electric are asking state and federal regulators to saddle their ratepayers with massive rate increases. The companies all assert that they need a higher rate of return — that is, higher rates — to attract investors to businesses that suddenly seem riskier than ever.

The regulators’s task here is obvious. They should just say no. Let’s start with the utilities’ rate requests, which are outrageous by any measure.

Edison is [seeking an increase from the state Public Utilities Commission](#) of more than 6% in its allowable return on equity, which would result in a 12.2% increase in its average customer’s monthly bill — \$12.20 a month on an average bill of \$100. That’s on top of a rate increase averaging \$2.20 a month that Edison previously requested from [the Federal Energy Regulatory Commission](#).

PG&E is asking state regulators for an average residential electric increase of \$7.85 a month, or 7%. Gas customers would face an increase of \$4.25 a month, or 7.7%. Sempra, the parent of SDG&E, is seeking an increase amounting to an average of \$5.59 a month.

The utilities acknowledge that much of this money would go into investors’ pockets. Edison, in announcing its rate request, called the increase “a near-term necessity in order to attract the capital needed to provide safe, reliable electricity” — in other words, to lure investors.

It’s probable, of course, that the utilities are high-balling the regulators — they’re hoping the PUC will split the difference and award them rate increases that aren’t outrageous, merely egregious.

“Rate requests are the beginning of a conversation” with regulators, says Steve Weissman, a former PUC administrative law judge who now teaches at the UC Berkeley law school. “The utilities clearly are perceiving that they’re riskier than they were before, but it’s up to the regulators to decide whether that’s a legitimate concern and to figure out what the appropriate return may be.”

There’s no question that the physical landscape has shifted under the companies’ feet. Climate change appears to be leading to longer and more intense wildfire seasons. That’s a problem for the companies, because their power lines crisscross fire zones, and the utilities’ inattention to vegetative growth near their lines leads to fire-causing sparks. State authorities have blamed some of the most damaging fires on utility operations, with the causes of major recent fires still undetermined.

Continue reading [here](#).

