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DATE: May 27, 2016
 TO: Directors & Members

PAGES: 4
 FROM: Rob Vandenhuevel, General Manager

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE

Blocks +\$.0650 \$1.3800
 Barrels +\$.0850 \$1.4400

Weekly Average, Cheddar Cheese

Blocks +\$.0510 \$1.3520
 Barrels +\$.0475 \$1.4030

CHICAGO AA BUTTER

Weekly Change - \$.0050 \$2.0650
 Weekly Average +\$.0245 \$2.0760

DRY WHEY

Dairy Market News w/e 05/27/16 \$2.388
 National Plants w/e 05/21/16 \$2.487

NON-FAT DRY MILK

Week Ending 5/20 & 5/21

Calif. Plants \$0.7643 7,591,388
 Nat'l Plants \$0.7841 13,007,601

Prior Week Ending 5/13 & 5/14

Calif. Plants \$0.7306 15,274,342
 Nat'l Plants \$0.7508 20,066,230

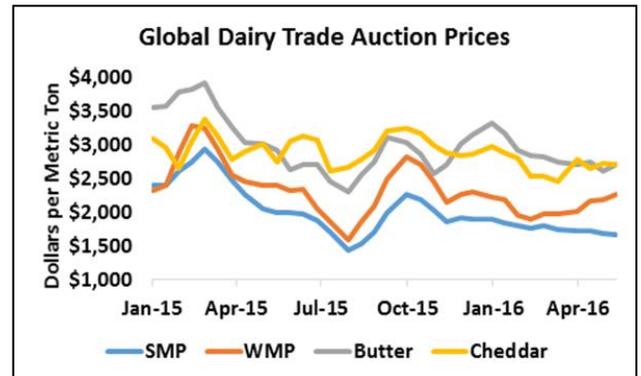
FRED DOUMA'S PRICE PROJECTIONS...

May 27 Final: Quota cwt. \$13.60 Overbase cwt. \$11.91 Cls. 4a cwt. \$12.55 Cls. 4b cwt. \$11.37
 Last Week: Quota cwt. \$13.58 Overbase cwt. \$11.88 Cls. 4a cwt. \$12.51 Cls. 4b cwt. \$11.35

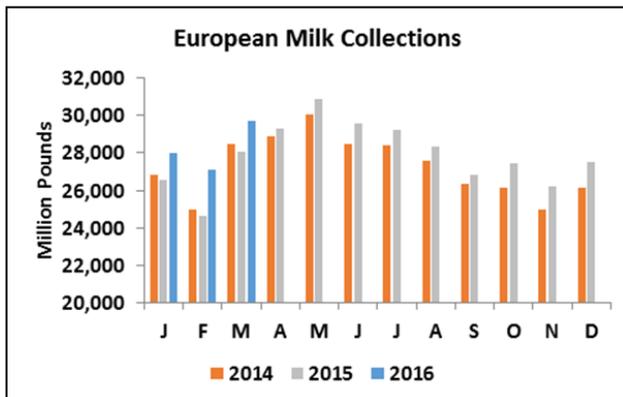
MARKET COMMENTARY: (By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com)

Milk & Dairy Markets

Over the past two weeks, the markets have been flooded with milk and deluged with data pointing to burdensome supplies. And yet, for the most part, prices have started to climb. Since mid-May, CME spot Cheddar blocks have jumped a dime, to \$1.38/lb. Barrels are even stronger, up 12¢ in two weeks to \$1.44. Spot butter gained 2.75¢, finishing at \$2.065. Under the weight of the stronger dollar, nonfat dry milk (NDM) prices retreated 2¢ to 79.5¢. Over the same period, most Class III futures contracts advanced by double digits; the June contract surged 59¢. Class IV futures showed similar strength.



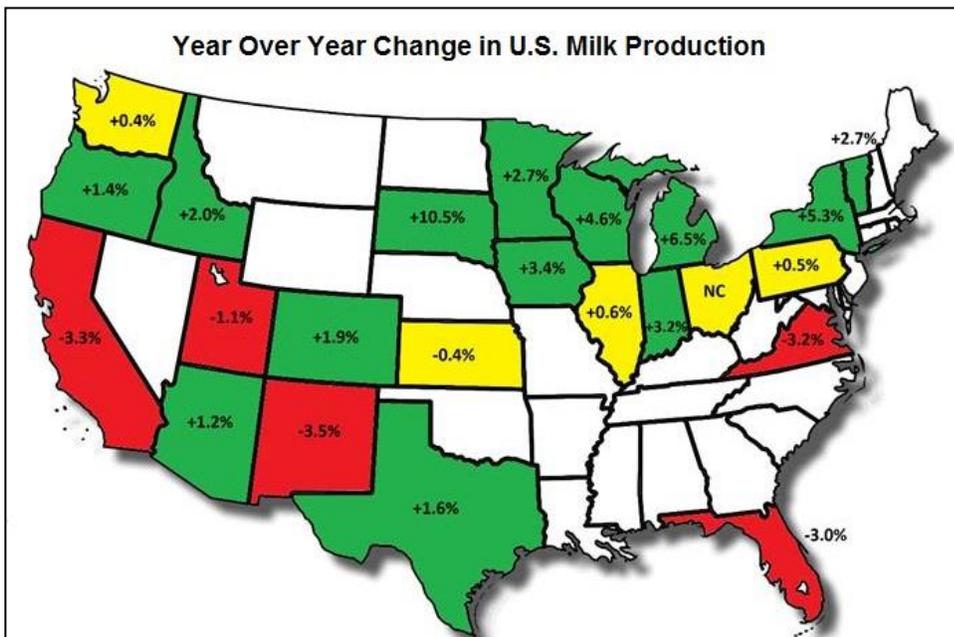
Overseas prices are also starting to recover. In early May Dairy Market News reported average Cheddar prices in Oceania at around \$1.16/lb., the lowest value since mid-2009. But last week they bounced back, averaging \$1.185. European cheese prices have rebounded from the multi-decade lows scored in March and April. A similarly fledgling recuperation is underway in the global butter market. But in a world awash in dairy products, such gains are neither universal nor guaranteed. Last week's Global Dairy Trade (GDT) auction featured a mixed performance. The GDT index rose 2.6% and whole milk powder (WMP) prices were up 3% from the previous event. However, skim milk powder (SMP) dropped 0.9%, and Cheddar prices slipped 0.8%.



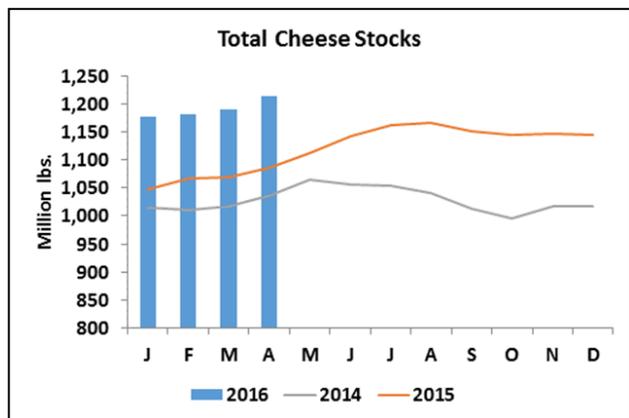
The modest rebound seems to be driven by the sentiment that today's despondence will bring about an eventual revival in the dairy markets. This assumes that low prices will entice demand and constrict supply. There is evidence of the former, but the latter has been fleeting. New Zealand remains in a milk

production deficit. With just one month until the end of the season, collections are 2.1% below last year. But that is a much smaller decline than was forecast when the season began. Meanwhile, European milk output climbed 5.8% from a year ago in March, and growth in Europe dwarfs shortfalls in New Zealand, or anywhere else for that matter.

In the U.S., production continues apace. April output totaled 18 billion pounds, up 1.2% from a year ago. In California, where margin pain is most acute, production dropped 3.3%, and the milking herd was 6,000 head smaller than a year ago. But dairy producers elsewhere have continued to expand; the national herd reached 9.331 million head, the largest in any month since December 2008. Output in the Midwest and Northeast has been particularly strong, and the spring flush is overwhelming processing capacity in those regions.



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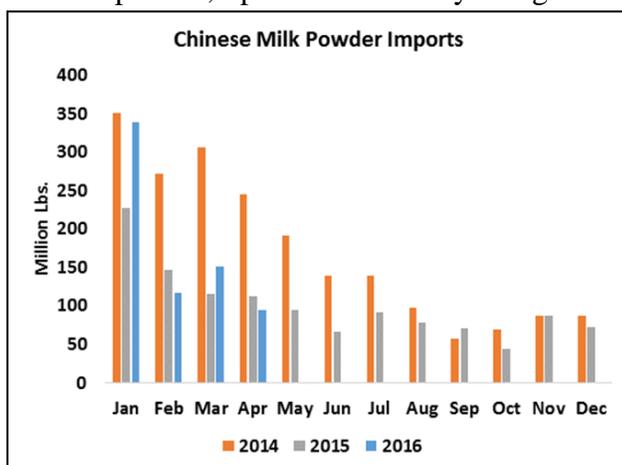


Indeed, capacity is the issue in many aspects of today's oversupplied dairy markets. Milk will move at steep discounts over the long weekend, searching for a little extra space in already overburdened balancing plants. In barns around the country, every stall is full; springer prices are starting to decline in earnest due to a lack of demand for replacements. Europe doubled the size of its SMP intervention purchase program, but after just five weeks they have once again bumped into the self-imposed ceiling. And U.S. warehouses are overflowing with cheese.

On April 30, there were 1.21 billion pounds of cheese in cold storage, more than in any month since March 1984. Cheese stocks were up 11.8% from the previous year and up 22.65 million pounds from March, an increase of 1.9%. *Dairy Market News* reported last week that in the Midwest, "a large quantity of storage facilities are at or near capacity." Furthermore, "although sales are strong, active production is filling any empty stock shelves right back up."

Butter inventories also jumped last month. Stocks totaled 298.2 million pounds, up 28.3% from a year ago. The 55 million pound stock build from March to April was the largest for those months since 1992. It was hot this week in the Midwest, but milk flows remain heavy and ice cream demand has not risen enough to lap up all the excess cream. Multiples are moving counter-seasonally lower, signaling surplus. With cream both cheap and plentiful, butter production in May is likely to be quite heavy.

Chinese milk powder imports slipped in April. Combined purchases of WMP and SMP totaled 94.6 million pounds, down 15% from a year ago and down 35% from March on a daily average basis. Chinese cheese and whey imports were also down relative to the previous month and compared to



year-ago volumes, but the declines were moderate. China's appetite for imported fresh milk remains strong. Imports of UHT milk stood at 110.2 million pounds in April, up 70.3% from a year ago, but down 4.1% from March on a daily average basis.

U.S. dairy cow slaughter continues to lag 2015 volumes. Through mid-May the cull rate is 1.5% behind last year's pace. Waning springer values and an increase in the number of dispersal auctions suggest that slaughter volumes are likely to rise, but they have not yet.

Grain Markets

Crops in the U.S. are off to a fabulous start; the Corn Belt has been favored with warm temperatures and fairly regular rains. But amidst concerns about damage to South American crops and booming U.S. exports, the trade has priced in a sizeable weather risk premium. July corn futures settled at \$4.1275 per bushel, up 22¢ over the past two weeks to a ten-month high. July soybean futures gained 21.5¢ and closed at \$10.865, up 21.5¢. July soybean meal futures finished at \$402.60 per ton, up an astounding \$39.80 in just two weeks. Since early April, July soybean meal futures have surged more than \$125.

The ebullient soybean meal market is a reminder of just how much demand for oilseeds has grown in the past decade. Since the 2005-06 crop year, global oilseed use has jumped 50%. Production has failed to keep up, climbing 36% over the same period. As demand continues to climb, the world is perpetually one crop disaster away from a sudden surge in protein prices.

CDDFA PERMANENTLY EXTENDS THE CURRENT CLASS 4B CALCULATION: *(By Rob Vandenhuevel)* Last Friday, CDDFA Secretary Karen Ross announced the results from the recent hearing on California's Class 4b calculation. Her decision was to permanently extend the current temporary calculation of the Class 4b price that has been in place since August 2015 and was set to expire at the end of July 2016.

So what does that mean to California producers? It means that our Class 4b price should maintain a closer relationship with the Federal Order Class III price than under the previous calculation. For example, since August of last year, the Class 4b price has averaged \$0.82/cwt below the Federal Order Class III price, while in the twelve months leading up to that calculation change, the Class 4b price averaged \$2.09/cwt below the Federal Order Class III price.

Is an \$0.82/cwt discount in California's Class 4b price compared to the national benchmark price for milk sold to cheese plants an acceptable long-term solution? Of course not. In fact, even Secretary Ross indicated in her announcement that, "I still believe adjustments to the pricing formulas are inadequate to address long-term structural challenges facing the dairy industry." California producers believe participation in the national regulatory structure is our best path forward, in the form of a California Federal Milk Marketing Order. We believe that by entering into that national framework, our producers have the best opportunities to compete on an even playing field with our competition around the country.

Having said that, this announcement by Secretary Ross was welcome news for the State's dairy producers, who will continue to operate under California's milk pricing system for the near term, as USDA puts together what we hope will be a California Federal Order that producers can ultimately support. Given the devastating financial challenges being faced by California dairy families, which has led to 16 straight months of year-over-year declines in milk production, we could not afford to see the California Discount on Class 4b milk prices expanded with the expiration of the temporary milk price calculation. Fortunately, we don't have to.

As an interesting side note, Secretary Ross' hearing decision actually went beyond what was recommended by CDDFA's hearing panel, which was made up of economists within CDDFA. While the hearing panel noted the financial challenges being faced by California dairies, they nonetheless recommended a calculation that would have generated a *lower* Class 4b price than the current temporary (now permanent) calculation generates. In fact, as CDDFA's announcement indicates, the Hearing Panel's recommended calculation would have generated a Class

4b price about \$0.35/cwt lower over the past five years (March '11 – Feb '16) than what Secretary Ross ultimately implemented.

Given the evidence of the financial pain being felt by California's dairy families (much of that evidence in the form of CDFA's own data!), it's difficult to fathom how the Hearing Panel could recommend an *expansion* of the California Discount from where it is today. Fortunately, it became a moot point when Secretary Ross used her discretion to overrule that recommendation and extend today's calculation into the foreseeable future.

CALIFORNIA ASSEMBLY SET TO VOTE ON AG OVERTIME BILL NEXT WEEK: (By Rob Vandenheuvel) AB 2757, introduced by Assembly member Lorena Gonzalez from the San Diego area and referred to as the "Ag Overtime Bill," has been sent to the Assembly floor for a vote **sometime next week**. In case you haven't heard about this bill, it would – over the next couple years – require agricultural employers to pay overtime wages for any hours worked above 8/day or 40/week. California is currently one of the few states that even requires overtime pay for agricultural employees, for hours worked above 10/day or 60/week.

California dairies already operate in one of the most regulation-heavy States in the Union. Every year, Sacramento Legislators dream up a seemingly endless supply of anti-business bills to propose, and as business operators trying to create jobs and economic activity in the State, it feels like a basketball game where you never leave the defensive side of the court! However, this latest effort by Assembly member Gonzalez would not only create more potential costs and regulatory hurdles for California's agricultural employers, but it would create the likely result of reducing the wage-earning hours available to our agricultural **employees**.

If this bill were made law, in a few short years agricultural employers would be faced with the decision of whether to shorten their workers' hours or pay at least \$22.50/hour for any work above an 8-hour shift (once the \$15/hour minimum wage kicks in). Dairies have great respect for their employees, and the average wages reported for California dairy employees are well beyond the minimum wage. But at the end of the day, the dairy cannot afford to pay wages with money it doesn't have. And given the state of the California dairy industry, our dairy families simply cannot afford the massive increase in labor costs associated with this proposed change in overtime rules. Instead, our employees who may want to work more hours to earn more money for their families could be forced to end their work day at 8 hours to avoid overtime pay requirements.

There is still time for dairies and their employees to contact your local Assembly member to urge them to vote against AB 2757. **The vote will come sometime before the end of next week, so the earlier the better!** If you're not sure who your Assembly member is or how to contact them, please feel free to shoot me an email (rob@milkproducers.org) or give me a call (909-628-6018) and I can help steer you to the right person.

PRODUCERS INVITED TO A COUPLE DAIRY MARKET SEMINARS NEXT MONTH: (By Rob Vandenheuvel) HighGround Dairy and AgriCFO, risk management firms that work in dairy markets, are hosting two seminars in California next month for producers, free of charge. The seminars, which will be held on June 7th (Tulare) and 9th (Modesto), will cover issues such as: (1) A Dairy Market Outlook; (2) Managing the Financial Complexities of the Dairy Business; and (3) Developing a Comprehensive Risk Management Strategy. And at a minimum, you'll get a free lunch!

The first seminar will be held on **June 7th at noon at the International Agri-Center in Tulare (4500 S. Laspina St)** and the second seminar will be held on **June 9th at noon at the Stanislaus County Agricultural Center in Modesto (3800 Cornucopia Way)**. Interested producers should RSVP by June 1st to Curtis Bosma with HighGround Dairy at: curtisb@highgroundtrading.com or (312) 870-1185.

MPC would like to wish you and your family a happy and safe Memorial Day weekend! We all owe a huge debt of gratitude to the men and women who have died while fighting for the freedom we enjoy in this country.