Milk Producers Council

13545 S. Euclid Avenue, Unit B ~ Ontario, CA 91762 ~ (909) 628-6018
801 S. Mount Vernon Avenue ~ Bakersfield, CA 93307 ~ (661) 833-2549
222 S. Thor Street, Suite 20 ~ Turlock, CA 95380 ~ (209) 250-1801
Fax (909) 591-7328 ~ office@milkproducers.org ~ www.MilkProducers.org

DATE: January 25, 2013 **PAGES: 4**
TO: Directors & Members **FROM: Rob Vandenheuvel, General Manager**

MPC FRIDAY MARKET UPDATE

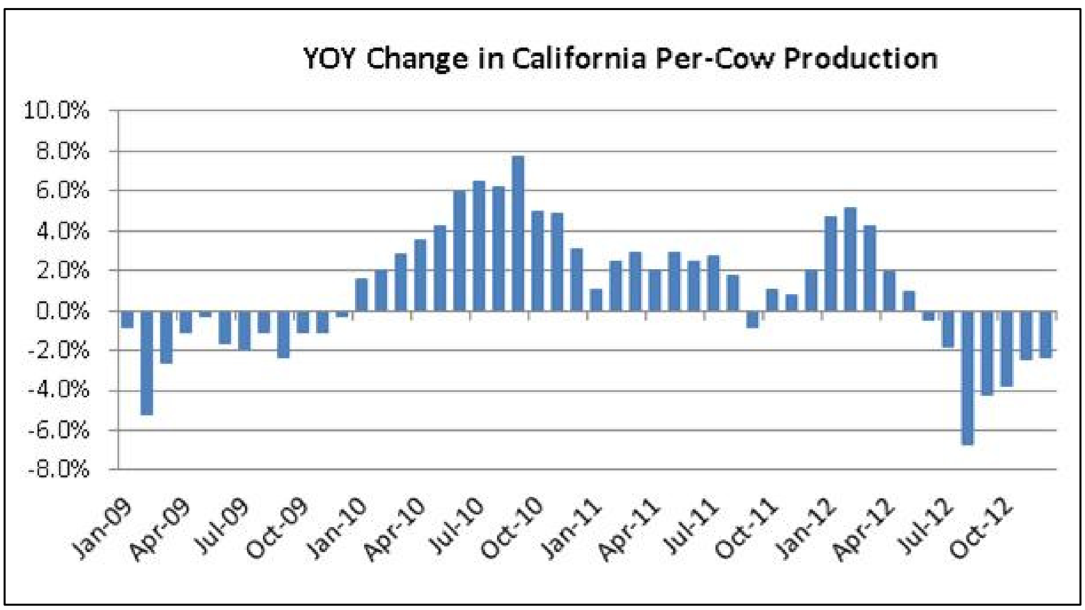
CHICAGO CHEDDAR CHEESE		
Blocks	*- $.0425*	$1.6450
Barrels	*- $.0650*	$1.5725
Weekly Average, Cheddar Cheese		
Blocks	*- $.0510*	$1.6525
Barrels	*- $.0732*	$1.5863

CHICAGO AA BUTTER		
Weekly Change	*N/C*	$1.5050
Weekly Average	*+$.0165*	$1.5050
DRY WHEY		
Dairy Market News	w/e 01/25/13	$.5900
National Plants	w/e 01/19/13	$.6449

NON-FAT DRY MILK		
Week Ending 1/18 & 1/19		
Calif. Plants	$1.5460	9,442,188
Nat'l Plants	$1.5714	19,695,531
Prior Week Ending 1/11 & 1/12		
Calif. Plants	*$1.5362*	*8,377,860*
Nat'l Plants	*$1.5482*	*17,265,637*

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

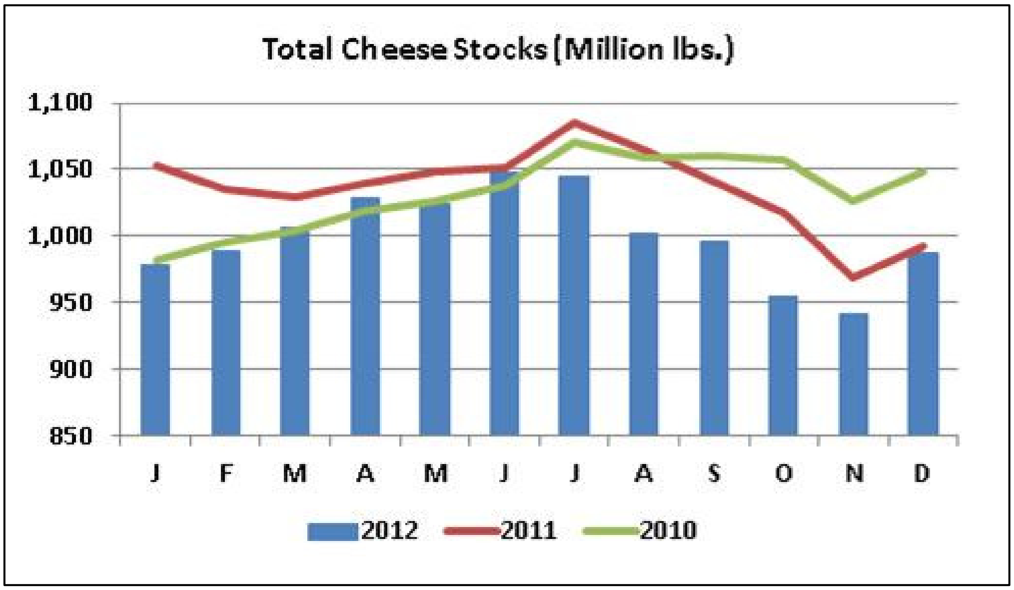
Milk & Dairy Markets
Milk prices moved a little lower again this week, pressured by the Milk Production and Cold Storage reports, both of which were bearish. December milk production totaled 16.8 billion lbs., up 1.6% from December 2011. The milk herd averaged 9.213 million head, up 16,000 head from November but down 10,000 cows from a year ago. USDA revised upward its estimate for the November milk cow herd by 4,000 head, making for a 20,000 cow increase in the herd from report to report. Per cow production remained very strong, averaging 1,826 lbs., up 1.7% from December 2011.



Of the 23 major dairy states, California reported the largest decline in production, falling 2.3% from a year ago. Despite heavy culling and herd liquidations, the cow herd was steady with last year; the contraction was driven by lower per cow production. Most states reported stronger milk production in December, with Michigan and Wisconsin up 5.5% from a year ago. Colorado milk production was 6.3% higher. Milk production declines were confined to the Southwest. Texas production fell 0.7% and New Mexico and Arizona shed 0.3%, largely due to lower cow numbers.

Given such strong milk production in the final quarter of last year, it is unsurprising that stocks of dairy products moved higher. However, the size of inventory builds, particularly for butter, was impressive. Butter stocks at year end were 152.85 million lbs., up 25.6 million lbs. or more than 20% since November. Butter stocks typically grow by a more modest 6-7% in December. Stocks were 43% higher than at the end of 2011. This report explains the recent softness in the butter market, as end users have been able to remain on the sidelines and simply wait for lower prices.

Cheese stocks also increased from November to December, but they remain below year ago levels. Cheese stocks of all varieties on December 31 were 987.9 million lbs., 5% higher than November, but slightly lower than December 2011. American cheese stocks were up 4% from November but down 1% from the prior year. Cheese stocks in the Pacific region were 5% lower than a year ago, but they increased by 8% in December.



The market was offered a distraction from the bearish Cold Storage and Milk Production reports on Thursday, in the form of a food safety scare in New Zealand. Trace levels of Dicyandiamide (DCD), a fertilizer used in pastures which prevents nitrogen leaching, were found in Kiwi milk powder. In high doses, this substance can be toxic to humans. However, the amounts found in New Zealand's dry milk products were small, and only products made with September milk tested positive. The higher volumes of milk produced in October through December were clean. Less than 4% of dairies in New Zealand use the product, and the impact of the news appears to be minimal. Class III futures bounced on the news, in hopes that U.S. exports could become more competitive. However, by day's end Class III futures settled lower. New Zealand's dairy products are perfectly safe, and this scare might cause only a slight interruption to the flow – and not the volume – of dairy products out of New Zealand. Still, this issue represents a blight on New Zealand's reputation for quality dairy products, and her largest customer, China, is particularly sensitive to reputation and appearances.

Cheddar blocks lost 4.25¢/lb. at the CME spot trade this week. Barrels fell 6.5¢ amidst heavy offers. CME spot barrels settled at $1.5725/lb., their lowest settlement in over seven months. Butter and NDM were steady. For the week ending January 19, National Dairy Products Sales Report prices moved mostly lower, with the exception of nonfat dry milk (NDM), which added 2.3¢/lb. Butter prices fell 4.4¢. Dry whey shed 1.2¢. *Dairy Market News* dry product prices were also mostly lower. The California Weighted Average Price for NDM moved nearly a penny higher on slightly better sales volume.

The California Department of Agriculture amended California's pricing formulas for February through May 2013, adding 30¢ per cwt. to Class 4a and 4b payments, a dime to Class 2 and 3 prices, and a nickel to the Class 1 price.

For the week ending January 11, dairy cow slaughter totaled a shockingly large 72,474 head. This was the highest weekly slaughter since January 1997. Slaughter rates have been elevated for some time, but given high mailbox milk prices and mild weather in the final months of 2012, dairy producers were incentivized to increase production despite high feed prices, and the market was flooded with milk. Now milk checks are considerably smaller, temperatures are lower and culling is at 16-year highs. The near term outlook is painful, with high feed costs and relatively low milk prices. However, given such heavy culling, the dairy cow herd will likely contract, and per cow production is expected to fall from its current heady levels. Assuming normal weather, feed prices should moderate by fall. The long term outlook for dairy producers is much brighter.

Grain and Hay Markets

Feed prices ended this week basically where they began it, but trading was volatile as the market followed South American weather forecasts with single-minded obsession. Generally the South American soybean and corn crops are good but not spectacular. Rains are plentiful in northern Brazil, which is good for yields but stressful during the early harvest, which is underway. Ships are already lined up in Brazil's ports to export beans as quickly as possible and capture premiums which will quickly fade when the full harvest pressures the market. Ships can expect to wait 45 days in line in order to be loaded for export in February, and Argentine supplies will not be available until March.

Southern Brazil and Argentina are mostly dry. There have been enough light, scattered showers or hints of rain in the long term forecast to pressure soybean prices. However, it does not appear to be enough rain to help the crop much through this critical growth stage.

The demand picture is largely unchanged. Corn exports remain almost nonexistent, and U.S. soybean exports are strong but fading as buyers turn their attention to the Southern Hemisphere. Feed demand is very strong, while ethanol demand has weakened. Expect feed prices to continue bouncing around within the recent range with soybean prices under the strong but erratic influence of South American weather forecasts.

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FRED DOUMA'S PRICE PROJECTIONS…

Jan 25 Final:	**Quota cwt. $18.33**	**Overbase cwt. $16.63**	**Cls. 4a cwt. $17.07**	**Cls. 4b cwt. $15.84**
Last Week:	**Quota cwt. $18.33**	**Overbase cwt. $16.63**	**Cls. 4a cwt. $16.99**	**Cls. 4b cwt. $15.89**

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CDFA ANNOUNCES RESULTS FROM DECEMBER 21, 2012 HEARING; A TEMPORARY INCREASE OF $0.25 PER CWT TO THE STATEWIDE BLEND PRICES: *(By Rob Vandenheuvel)* This week, the California Department of Food and Agriculture (CDFA) announced that for the months of February through May 2013, the minimum prices for the five classes of milk will be increased by varying amounts, resulting in an overall blend price increase of about $0.25 per hundredweight.

As noted in Sarina's narrative above, CDFA increased the Class 1 (fluid) price by $0.05 per hundredweight, the Class 2 (soft products) and 3 (frozen products) prices by $0.10 per hundredweight and the Class 4a (butter/powder) and 4b (cheese/whey products) prices by $0.30 per hundredweight. Given recent statewide utilization of each of these classes of milk in California, the increases blend out to a temporary bump of approximately $0.25 per hundredweight in producer pay prices.

While California dairy families certainly appreciate the recognition that **increases to our producer pay prices are warranted**, the **announced changes fall significantly short of what producers hoped for going into this hearing process**. For the past three years, California dairy families have urged CDFA and Secretary Karen Ross to make permanent changes to our Class 4b price that would bring us into closer alignment with the Federal Order Class III price, which is the benchmark price for milk sold to cheese plants in Federal Milk Marketing Order areas (which is the regulatory structure overseeing about 80 percent of the milk produced and sold outside of California). As MPC has reported numerous times, since the beginning of 2010, CDFA's unwillingness to make those changes to our Class 4b pricing formula has resulted in the California cheese manufacturers getting a **state-sponsored discount of more than $700,000,000**, all on the backs of the roughly 1,600 dairy farms that are left in California. With California's Class 4b prices averaging almost $2.00 per hundredweight below the Federal Order Class III price in 2011 and 2012, **obviously dairy farmers are very disappointed to see CDFA only willing to provide a four-month increase of $0.30 per hundredweight to the California Class 4b price.**

At the hearing, several proposed increases to the various class prices were presented to the CDFA staff. Most producer organizations/cooperatives proposed increases that would have resulted in a net increase of about $0.70-

$1.00 per hundredweight to the producer pay price. Milk Producers Council testified in support of increasing the Class 1, 2, 3 and 4b prices by at least $1.00 per hundredweight, while leaving the Class 4a formula unchanged (we testified that since the Class 4a processing plants were almost exclusively owned by dairy farmers, increases to that monthly price did not represent additional revenue for the dairy farming community, which was the reason for holding the hearing). In the end, however, CDFA chose to make much more modest increases (to say the least), and included all five classes in the equation.

So what can we learn from the recent actions by CDFA? The most basic lesson we can learn from not only this recent hearing, but also from previous hearings, is that our State's dairy farmers are in need of fundamental, large-scale changes to the way we price the milk sold by our dairies, and **it is abundantly clear that the relief we need will not come from the CDFA hearing process.** California's dairy families, their trade associations and their cooperatives need to be working on reforms that don't rely on the discretion of CDFA. That process has already begun, and quite frankly, cannot happen fast enough. So stay tuned…

CENTRAL VALLEY DAIRYMEN, PLEASE MARK YOUR CALENDARS FOR THE CVDRMP ANNUAL MEETING: *(By Kevin Abernathy)* For those Central Valley dairies that are members of the Central Valley Dairy Representative Monitoring Program (or CVDRMP), an annual meeting of the organization is scheduled for January 30th at the Fresno County Farm Bureau. This dairymen-funded initiative has helped reduce the costs for its member dairies by implementing a regional monitoring program (as opposed to a dairy-by-dairy monitoring program, as originally crafted by the Central Valley Water Board). For more information on this annual meeting (including an agenda for the meeting), check out this letter that was recently sent to the member dairies of the CVDRMP: www.milkproducerscouncil.org/cvdrmpmtg.pdf

DAIRYMEN REMINDED TO LOG YOUR DECEMBER 31, 2012 ODOMETER READING ON YOUR CARB-REGISTERED DIESEL TRUCKS: *(Kevin Abernathy, Director of Regulatory Affairs)* Over the past couple years, most of the dairies in California registered their heavy-duty diesel engine trucks with the California Air Resources Board (CARB). With CARB in the process of requiring equipment upgrades to these vehicles to reduce emissions, dairies and other agricultural interests were able to enroll in a temporary exemption program that delayed implementation of these upgrades until 2017 or later. As part of that process, the owners of these agricultural trucks must log their December 31 odometer readings and report them on CARB's website.

The deadline to report the 2012 annual odometer reading is January 31, 2013. More information can be found on CARB's website at http://www.arb.ca.gov/msprog/onrdiesel/reportinginfo.htm. MPC members that have any questions about their dairy's compliance can contact Rob Vandenheuvel at (909) 628-6018, Betsy Hunter-Binns at (661) 205-6721 or Kevin Abernathy at (209) 678-0666.