Milk Producers Council

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TO: DIRECTORS & MEMBERS **FROM: John Kaczor**

MPC FRIDAY MARKET UPDATE

CHICAGO MERCANTILE EXCHANGE
Blocks -$.2100 $1.3025
Barrels -$.1675 $1.3550

Weekly Average
Blocks -$.2845 $1.4000
Barrels -$.1980 $1.4595

CHICAGO AA BUTTER
Weekly Change +$.0600 $1.1700
Weekly Average +$.0085 $1.1960

NON-FAT DRY MILK
Week Ending 12/12 & 12/13

Calif. Plants	$.8416	14,922,131
NASS Plants	$.8393	27,904,594

DRY WHEY
NASS w/e 12/13/08 $.1702 **WEST MSTLY AVG** w/e 12/17/08 $.1550

CHEESE MARKET COMMENTS: It was another week of sharp price declines for blocks and barrels on the CME as prices for blocks lost ground every day of the week. *Dairy Market News* notes that major buyers are expected to sit on the sidelines so long as the weekly average prices (which are used to price many of the large transactions) are substantially higher than the Friday price, which is considered to be the "current" price. Last week, the weekly average price for blocks was 17 cents higher than the Friday price; this week the difference fell to about 10 cents. The difference for barrels was 13 cents last week and is about 10 cents this week. The average price for blocks this week is about as low as it has been for the week in the last 5 years. It looks like that "shaky foundation" for cheese prices may now be close to becoming "solid." Manufacturers are being offered distressed milk at bargain prices; those that take it will likely have to carry the inventory through year end, as sales have tapered off. It's a good time to make Cheddar for aging. The Super Bowl "season" is up next.

BUTTER MARKET COMMENTS: There was a nice price "bounce" this week on the CME, even after a 3 cent per lb drop today. Butter sales apparently held up fairly well into the holidays but, as is the case with cheese manufacturers, a lot of raw product is expected to be offered to churning operations over the next two weeks. Not clear on what effect that may have on butter prices because prices have been falling sharply even as the amount in cold storage has been well below last year's levels. This week's average price on the CME is the lowest it's been in the past 5 years.

POWDER MARKET COMMENTS: Sales to the CCC continue, and the latest prices for the two major weekly sales recaps are hovering about 4 cents above the support price level. USDA, in its latest set of projections for 2009, has **the high end of the price range for nonfat dry milk to be $.935 per lb.** Current sales are sluggish and inventories continue to rise. DMN apparently could not find any truckload-sized sales this week at more than $.88 per lb.

WHEY MARKET COMMENTS: DMN finds this week that manufacturers are trying to reduce year-end inventories the old fashioned way – with deals too good to pass up. Production is reported to be steady. Export interest continues to lag well behind last year. Most of the dry whey sales this week are at or below $.175 per lb. Yet, whey protein concentrate prices continue to edge up as buyers seem to be more interested; current prices moved up a penny this week, and are now several cents above their October lows.

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FRED DOUMA'S PRICE PROJECTIONS…

Dec 19 Est:	**Quota cwt. $14.39**	**Overbase cwt. $12.69**	**Cls. 4a cwt. $10.35**	**Cls. 4b cwt. $13.98**
Last week:	**Quota cwt. $14.62**	**Overbase cwt. $12.92**	**Cls. 4a cwt. $10.23**	**Cls. 4b cwt. $14.55**

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COOPERATIVES WORKING TOGETHER OPENS ITS PURSE; 61,000 COWS TO BE REMOVED FROM PRODUCTION: *(By J. Kaczor)* The removals should begin early in January and should be completed by the end of February. Even though this is a big deal, and should have given hope for what almost surely will result in a further short term reduction in the growth in milk production, its announcement was met with a big collective yawn by virtually everyone in every part of the industry. Butter and cheese prices continued to decline, powder continued to be sold at below market prices to the government, buyers are said to be waiting for further price reductions for almost all products, and the CME futures markets continued to move lower.

This herd reduction is a big deal because the growth in the U.S. dairy herd over the same months in 2007 had been increasing up to this May, after which it began to slow. In May, there were 139,000 more dairy cows on hand than in May 2007; since then, the monthly herd size comparisons steadily fell. By October the growth had dwindled to 90,000 more cows, and by November to 80,000. The amount of milk produced in November was only 1.1% greater than a year earlier, the smallest increase in 18 months. The reduction in the rate of growth since earlier this year is **the industry's natural response** to higher feed costs and lower milk prices. This herd reduction program is **CWT's natural response** to an opportunity to help the industry along the path it already has set for itself.

Unfortunately, even if the U.S. herd size falls to within a few thousand of last year's (which is not a foregone conclusion), industry experts do not offer any hope for anything like the milk price increases that occurred in 2007. Looking back, it's now fairly clear to see that those prices were an unsustainable "bubble," much like the recent run up in housing prices in the U.S. and Europe, the illusionary values claimed by the exotic get-rich schemes concocted by the biggest and best of our financial institutions and the "dot.com" exuberance in 2000-2001. Presently, the U.S., China, Japan, and Europe are facing monumental financial and economic crises, which means we buy less of their products and they buy less of ours and everyone else's, and everyone loses in the short run. A single sentence in USDA's *Outlook* last week sums up what is expected to happen: *"In the face of weakening demand, domestically and especially internationally, milk and dairy product prices will continue to glide downward throughout much of 2009."* **That seems to predict lower prices than those you see reported at the top of today's *Update*.** CWT has done its part in helping to stabilize prices; the rest is up to producers.

CDFA LOWERS CLASS 1, 2 AND 3 MILK PRICES: *(By Rob Vandenheuvel)* This week, the California Department of Food an Agriculture (CDFA) announced that starting on January 1st, they would be cutting the class 1 minimum price formula by $0.35 per cwt and the class 2 and 3 minimum price formulas by $0.26 per cwt. This reduction in the milk price is the result of a recent hearing that, ironically, was ***requested by producer groups***. In August, the Alliance of Western Milk Producers (which represents California Dairies Inc., Dairy Farmers of America and Humboldt Creamery), Western United Dairymen, and the California Dairywomen Association asked CDFA to hold a hearing to consider a temporary increase of approximately $1.00 per cwt in the class 1, 2 and 3 minimum price formulas.

Once the hearing request was granted, processor representatives seized the opportunity to present a proposal to slash the California class 1 minimum price by $1.35 per cwt and the class 2 and 3 minimum prices by about $0.26 per cwt. Their testimony at the hearing explained that these price reductions were necessary if California processors were going to be able to compete with out-of-state processors.

The hearing panel, made up of CDFA economists, actually bought most of the processors arguments and recommended a reduction of $1.01 per cwt in the class 1 formula. Secretary Kawamura opted to reduce this to a $0.35 per cwt cut, but accepted the recommendation to drop class 2 and 3 prices by the processor recommended $0.26 per cwt.

So what do these reductions mean in real dollars? Using October figures, these new formulas would have resulted in approximately **$1.9 million less** per month for California producers from Class 1, 2 and 3 revenues.

COMMENTARY: *(By Geoffrey Vanden Heuvel)* California producers are no doubt upset with CDFA for lowering class 1 prices at this time. They have a right to be even more upset with the Alliance of Western Milk Producers and Western United Dairymen for opening the door for this to happen by petitioning for a class 1 hearing when the facts on the ground were so unfavorable for us.

But we need to get past the emotion and look at the reality of our position. 2008 saw unprecedented disruption in the orderly marketing of milk in California. Not only did California milk production exceed processing plant capacity to a point where there were large amounts of distressed milk sloshing around the state, but another out-of-state bottling plant, built primarily to capture California's fluid market, went into operation in Nevada. The marketing actions of this new plant, in combination with the marketing actions and potential of the other fluid plants in Nevada, Arizona and Oregon continue to put massive price pressure on California's fluid milk handlers. These folks are feeling the heat. So when given the opportunity, the processors put pressure on CDFA to "fix" the problem. Because California has a **state** milk marketing order, and therefore may not – by law – regulate out-of-state milk, they are left with only one tool: lower prices.

The problem of out-of-area milk undermining a local class 1 market is not a new problem. Decades ago there were many state milk marketing orders in the Eastern part of the U.S. just like California's. These state orders were not able to regulate out-of-state milk any better than California is now. Congress provided a solution to this problem by establishing the Federal Milk Marketing Order (FMMO) program. Federal Milk Marketing Orders are not limited by state boundaries. Furthermore, they are designed to protect the local class 1 market from out-of-order milk. They can do this because FMMOs have the power to assess out-of-order handlers a "compensatory payment," which goes to local producers, eliminating the economic incentives that drive the interstate movement of milk. This remedy could also available to California producers, but our major cooperatives and Western United Dairymen (WUD) have stubbornly refused to seriously consider the option.

At the WUD public meeting on December 5, the owner of Producers Dairy, a fluid milk processor from Fresno, explained that his company had just lost the contract to supply 40 Costco stores in California. He said the new Nevada bottler had taken the business with a substantially reduced price. This news troubled the producers at the meeting. There were calls for a committee to look at what can be done. There were calls for the serious consideration of adopting a Federal Milk Marketing Order for California. These calls must be responded to now. In essence, CDFA appears willing to virtually give away most of California's class 1 price in an effort to hang on to that market share. How can we blame them? That is the only tool they have and California producers, through their cooperatives and major trade association have not been willing to take advantage of the Federal program specifically designed to fix this exact problem.

We are in a crisis and if you are a producer **you need to take action TODAY**. You need to call your cooperative board member as well as those who represent you on the trade association boards and demand that a serious effort be made to design a California FMMO that will fix the problem, while being respectful of the unique characteristics of the California dairy industry. This can be done, but it will only happen if California producers demand it. **Get on the telephone!**

A FRIENDLY REMINDER FROM THE WATER QUALITY CONTROL BOARD: *(By Rob VandenHeuvel)* With substantial rainfall across the state this past week and possibly more rain next week, staff from the Regional Water Quality Control Board have asked me to remind producers to inspect your wastewater/stormwater holding ponds daily during storm events and ensure that your containment infrastructure is intact and your holding capacity is not compromised.

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