



Milk Producers Council

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DATE: February 10, 2017
 TO: Directors & Members

PAGES: 5
 FROM: Kevin Abernathy, General Manager

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE

Blocks - \$.1300 \$1.6100
 Barrels - \$.0575 \$1.6500

Weekly Average, Cheddar Cheese

Blocks - \$.1115 \$1.6360
 Barrels + \$.0870 \$1.6790

CHICAGO AA BUTTER

Weekly Change - \$.0550 \$2.1025
 Weekly Average - \$.0525 \$2.1550

DRY WHEY

Dairy Market News w/e 02/3/17 \$.4950
 National Plants w/e 02/4/17 \$.4685

NON-FAT DRY MILK

Week Ending 2/3 & 2/4

Calif. Plants \$1.0276 9,282,681
 Nat'l Plants \$1.0189 19,929,057

Prior Week Ending 1/27 & 1/28

Calif. Plants \$0.9975 6,023,728
 Nat'l Plants \$1.0218 14,890,456

FRED DOUMA'S PRICE PROJECTIONS...

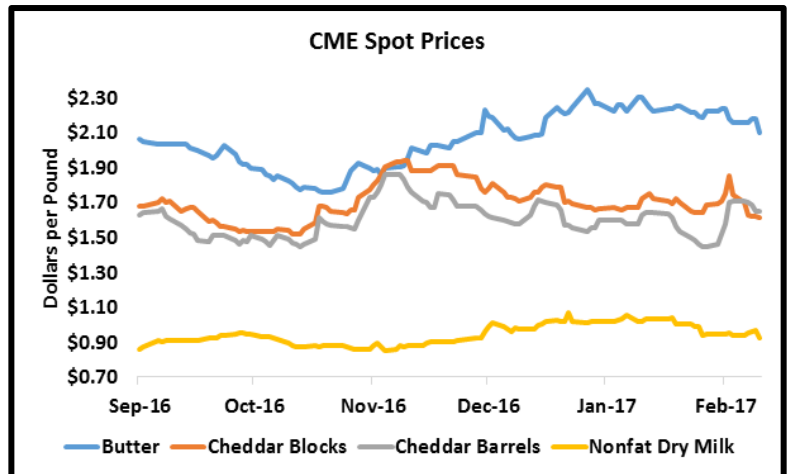
Feb 10 Est: Quota cwt. \$17.27 Overbase cwt. \$15.57 Cls. 4a cwt. \$15.40 Cls. 4b cwt. \$15.94
 Last Week: Quota cwt. \$17.63 Overbase cwt. \$15.94 Cls. 4a cwt. \$15.33 Cls. 4b cwt. \$16.78

MARKET COMMENTARY

By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com

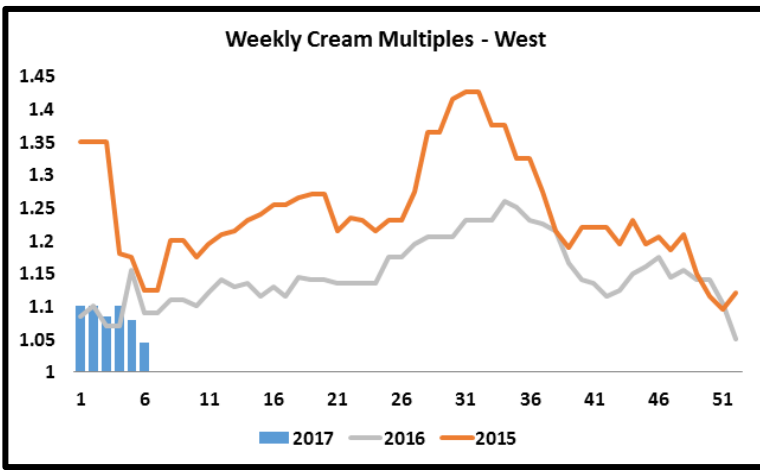
Milk & Dairy Markets

Dairy demand is fighting a losing battle with the calendar. Commitment to New Year's resolutions has faded, and yogurt consumption is down. The Super Bowl is over and cheese manufacturers are reassessing demand. Spring Break and the hiatus from school milk programs are fast approaching. Easter is more than two months away, and it'll be a while before consumers start thinking about grilling cheeseburgers or cooling off with ice cream. Outside of the storm-afflicted mountain states, milk is plentiful and moving to manufacturers at a discount. Time marches inexorably on, and demand is likely to improve, but supplies are sure to grow as well. Given the size of the dairy herd, the spring flush promises to be formidable.



CME spot dairy product prices moved lower across the board this week. Cheddar blocks were hardest hit; they dropped 13¢ to \$1.61/lb. Barrels shed 5.75¢ and finished at \$1.65. Butter fell 5.5¢ to \$2.1025. Spot nonfat dry milk (NDM) slipped to an 11-week low of 92¢, down 2¢ from last Friday. Class III and Class IV futures were mixed, but second quarter contracts were decidedly lower.

Cream is sloshing around. In the West, cream multiples – the factor used to convert the CME spot butter price to a raw cream price – ranged from 0.91 to 1.18, putting the midpoint at a four-year low. Dairy Market News reports, “Most cream buyers are making bulk butter. Due to an unsettled cheese market, some Class III processors are

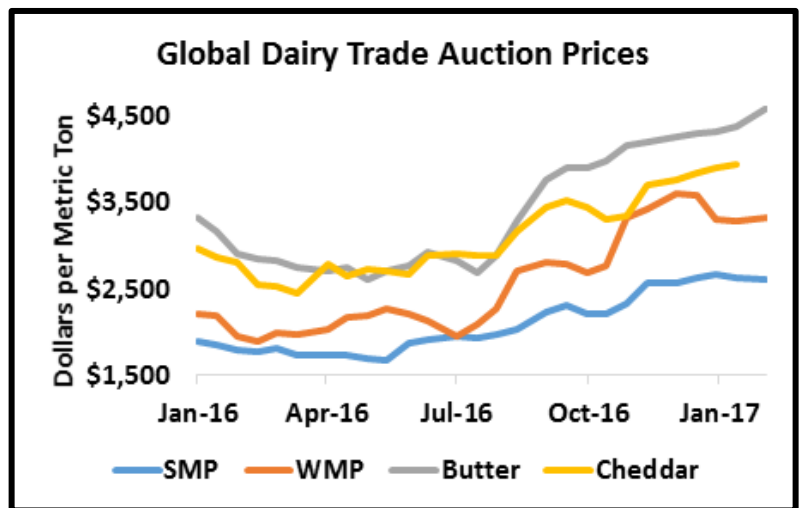


pushing back their cream after separating. Canada has once again reentered the market as a buyer of U.S. cream, but Mexico has not.” Mexico accounted for 15% of U.S. cream exports last year.

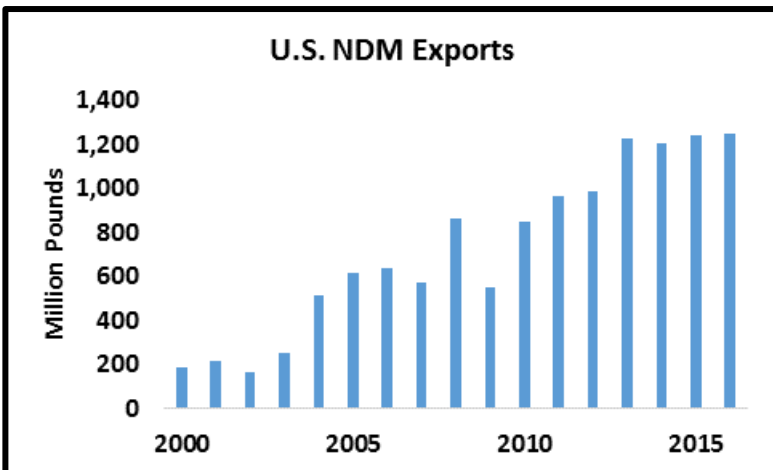
The milk powder markets are similarly unsettled. Politics has entered the mix. According to *Dairy Market News*, some Mexican buyers prefer to source NDM “from other countries aside from the United States. In addition, Mexican SMP production has been stronger compared to a couple weeks ago.” Mexico accounted for 43% of U.S. NDM and skim milk powder (SMP) exports in 2016.

At this point, the U.S.-Mexico trade war is one of grandstanding and conjecture rather than policy. The dairy markets in general and the milk powder market in particular have priced in a sizeable trade risk discount. The Trump Administration has a propensity to surprise; a single tweet esteeming NAFTA or punting trade discussions to a later date could quickly propel the markets back to recent highs.

In the meantime, Mexican buyers will most likely look to Europe to meet their milk powder needs. European inventories remain colossal. The European Commission once again rejected all bids on its fourth attempt to sell some of the older product in its Intervention program. In Oceania, milk powder is more costly. At this week’s Global Dairy Trade (GDT) auction, SMP averaged \$2,608 per metric ton. Adjusted for protein, this is equivalent to NDM at \$1.26/lb. February through June NDM futures contracts settled below a dollar at the CME today.



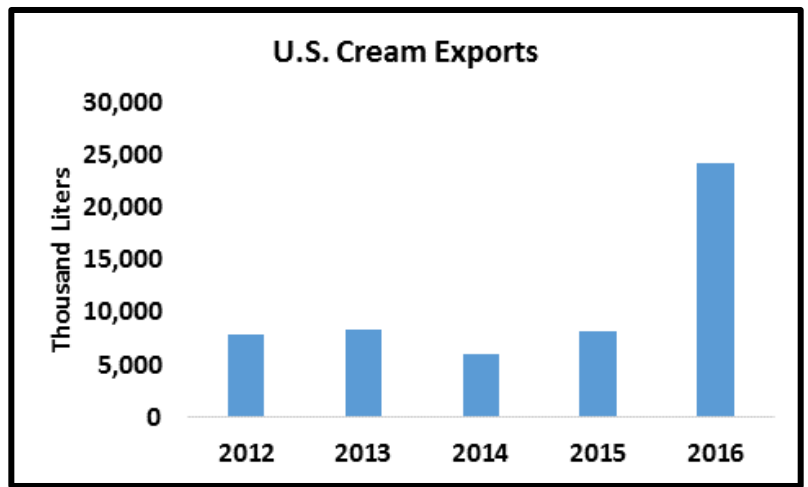
Whole milk powder (WMP) prices rallied at the GDT, gaining 1% from the previous auction. Butter climbed 4.9% and anhydrous milkfat gained 4%. The average winning price for Cheddar slumped 3.7%. The GDT Index finished 1.3% higher.



They remains the brightest star in the dairy galaxy. A number of futures contracts settled at 50¢ today, a two-year high. Demand has been excellent, but manufacturers are cautious given the uptick in output that is certain to accompany the spring flush. Meanwhile, the falling milk powder market offers a competing source for inexpensive protein. For now, though, the strong whey market has given Class III futures a decided boost. Every penny increase in the dry whey price raises Class III prices

by 6¢. The *Daily Dairy Report* estimates that the February 2017 Class III price will be \$1.50 higher than it would have been had whey prices remained at year-ago levels.

International milk production trends also offer reason for optimism. European cow slaughter for January through November is up 10.7% from 2015. Europe reports dairy and beef cow slaughter together, so an increase in beef cow slaughter could skew these numbers upward, but the bulk of the increase is likely from dairy. Year-to-date slaughter was particularly strong in Ireland (+35%) and the Netherlands (+27%). After the rapid expansion in the dairy herd in 2014 and 2015, this contraction is a healthy adjustment that will likely stave off a quick return to the immense volumes of milk the market had to absorb in the first half of 2016. At the same time, financial troubles in Oceania and South America are likely to restrict expansion in those regions, leaving greater opportunity for U.S. dairy exports.



All told, U.S. dairy product exports were 3% larger in 2016 than 2015, thanks to a 19% surge in fourth quarter shipments. U.S. exports of NDM, whey products, fluid milk, and cream were record-large last year. Exports accounted for 14.2% of U.S. milk solids production in 2016, according to the U.S. Dairy Export Council.

Grain Markets

The grain and oilseed markets continued to march higher this week. March corn finished at \$3.745 per bushel, up nearly a dime. March soybeans settled at \$10.59, up 14¢. There were no major surprises in USDA’s monthly update to its World Agricultural Supply and Demand Estimates. USDA made no changes at all to its domestic soybean balance sheet. The agency increased its estimate of corn demand, but corn supplies remain abundant. USDA lowered its estimate of global corn, soybean, and wheat stocks compared to the previous month, but inventories of all three crops remain higher than at the end of the 2015-16 season.

Going forward, crop prices will depend on the weather, of course, and on perceptions of demand. Brazilian weather remains excellent, while conditions in Argentina are mixed. Crop analysts have been revising upward their expectations for the Brazilian harvest, while in Argentina they are taking a wait-and-see approach.

Demand for grain and oilseeds continues to grow. Given the increase in global inflation, speculative traders assume that demand growth will accelerate. Investment funds are pouring money into commodities, boosting corn, soybean, wheat, and cattle prices.

THE DAIRY INSTITUTE PETITIONS CDFA FOR A HEARING TO REDUCE PRODUCER PRICES

By Geoff Vanden Heuvel, MPC Board Member and Economics Consultant

This week, California’s processor trade association petitioned the California Department of Food and Agriculture for a hearing to consider raising the make allowance factors in the California milk pricing formulas. The effect of the Dairy Institute proposal if adopted would be to drop the class 4a regulated price by \$0.36 per cwt. and the California class 4b price by \$0.415. Any adjustment in the class 4a make allowances also impacts the class 2 and 3 regulated prices. The total reduction on the overbase price that would result from an adoption of the DI proposal would be in the range of \$0.33 per cwt.

The justification DI gives in their petition is that “Failure to maintain adequate make allowances in the formula results in an overvaluation of producer milk and margins that are inadequate for the maintaining of necessary plant capacity. The current situation is unsustainable and necessary market outlets for producer milk will be put in jeopardy unless the formulas are updated.” Remember these sentences when processors come to your farm

soliciting you to leave your cooperative and direct ship to them. California production dropped for nearly 20 straight months and while seeming to stabilize recently is nowhere near its historical peak. So lack of plant capacity is not an imminent issue. Producer profitability is. The average California mailbox price in 2015 was \$15.08 per cwt. compared to an average cost of production of \$18.26. In 2016, through three quarters, the cost of production was \$18.17 compared to a 2016 average California mailbox price of \$14.26.

Obviously Milk Producers Council strongly opposes the granting of a hearing on the DI petition. We sent a letter of opposition to CDFA in conjunction with the California Dairy Campaign and Western United Dairymen. You can read that letter here: <https://goo.gl/vp2dJk>

STATE WATER RESOURCES CONTROL BOARD PROJECTS FEE INCREASE FOR DAIRIES

By Kevin Abernathy, MPC General Manager

The State Water Resources Control Board is forecasting another fee increase for Confined Animal Facilities, including dairies, in next year's state budget.

Water Board staff are reporting that due to a combination of rising costs and declining revenues, they plan to increase fees by 4.7 percent in the 2017-18 budget year. Dairies can expect to receive the invoice for 2017-18 in December of 2017.

The decision won't be final until August or September, when the Water Board adopts its fee schedule. The proposed fee increase could end up being lower or higher depending on any changes in the state budget before its adoption this summer.

Even though no regulatory staff have been added to the dairy program, cost of employing the existing staff has risen, according to the Board. They also reported declining revenues from dairies, as more have gone out of business or certified for environmental compliance through the California Dairy Quality Assurance Program.

Other farmers face an even sharper fee hike. The Board is proposing a nearly 22 percent increase to farmers who participate in Irrigated Lands Regulatory Programs (IRLP). The IRLPs continue to build and add staff at the direction of the state Legislature.

As our members know, MPC has consistently opposed water quality fee increases. We joined other dairy groups in January 2015 in a lawsuit against the Board related to previous, much larger water quality fee increases in 2013 and 2014. That litigation remains on hold awaiting the outcome of a similar fees lawsuit filed by the California Building Industry Association. While we wait for the court to decide that case, MPC will keep up our efforts to try to get Sacramento legislators and regulators to understand the folly of never-ending fee increases.

USDA RELEASES A RECOMMENDED DECISION FOR A CALIFORNIA FMMO

By Geoff Vanden Heuvel, MPC Board Member and Economics Consultant

On Thursday, February 9, USDA released a 213-page document outlining their proposed decision regarding a California FMMO. As you can imagine, there is much to wade through in this document. On milk pricing, the recommended decision does adopt a regulated price structure that is the same as all the other Federal Milk Marketing Orders. The mechanics of the order proposed by the recommended decision are different than what the California cooperatives proposed when they petitioned for a hearing to consider a California FMMO. So it will take time to analyze and understand how the recommended decision would work here in California.

Here is what we can say for sure. This is not the final decision. There is a 90-day comment period where improvements can be proposed for USDA to consider. There is a public meeting that USDA is going to conduct in

Clovis, California at the Veterans Memorial District Building, 808 Fourth Street, at 9 a.m. on February 22 to review the process and explain and answer questions relating to how the proposed California FMMO would operate.

With regards to quota, on page 78 of the document, USDA says: “Throughout the hearing and in post-hearing briefs, dairy farmers and their Cooperative representatives stressed that while a California FMMO would provide them a more equitable price for their milk, entry into the FMMO system must not diminish or disturb, in any form, California quota values. This decision finds that the package of FMMO provisions recommended in the decision would create more orderly marketing of milk in California, adhere to all the provisions of the AMAA, and allow the California quota program to operate independently of the FMMO. In doing so, the California quota program will not be diminished or disturbed in any form by California’s entry into the FMMO system.” So that is USDA’s intention and MPC along with many others will be evaluating the details in the weeks to come to assure that this aspiration can be realized.
