

Milk Producers Council

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CHICAGO MERCANTILE EXCHANGE

Blocks +\$.1350 \$1.5675
Barrels N/C \$1.4400

CHICAGO AA BUTTER

Weekly Change +\$.0025 \$1.3275
Weekly Average -.0676 \$1.3269

NON-FAT DRY MILK

Week Ending 12/18 & 12/19

Calif. Plants \$1.2781 12,778,676
NASS Plants \$1.2893 17,459,613

Weekly Average

Blocks -\$.0611 \$1.6394
Barrels -\$.0210 \$1.4350

DRY WHEY

WEST MSTLY AVG w/e 12/24/09 \$.3988
NASS w/e 12/19/09 \$.3678

CHEESE MARKET COMMENTS: “Unsettled” describes the CME cheese market this week. Prices on the CME for block cheese fell sharply this week, with an \$.11 per lb drop occurring on Wednesday. Barrel prices lost a penny on Monday and gained it back two days later. The price spread between blocks and barrels was halved in two days of trading which came from offers to sell from someone with too much block cheese on hand. Wednesday, after the market had closed, USDA released its report on the amount of cheese in storage at the end of November. The report showed that stocks of American cheese (which is 3/4ths cheddar) have been steadily increasing since May and, for the first time in five years, increased in November. The monthly “overhang” is about twenty-five million lbs higher than anticipated, is not following its expected path, and seems to make a clear case that **U.S. plants are simply producing more cheese than is needed at the present time.** Despite reports to the contrary, sales of cheese are not keeping up with production. Wednesday’s price drop for blocks, resulting from five sales at progressively lower prices, suggests that the market believes there is now too much block cheese. Last week’s comment, made here, inferred that the block price appeared to be well-supported. The comment was based on a recurring daily pattern that had each day finishing with the block price unchanged after heavy trading. This week’s activity tells a different story. Caution is expected to guide cheese buyers until the block-barrel price spread approaches normalcy.

BUTTER MARKET COMMENTS: The sharply lower amounts of butter produced in August, September, and October (and presumably in November), compared to a year earlier, has helped to control inventories during that period. USDA’s report on the amount of butterfat products in storage at the end of November is below the amount two years ago and is approaching, but still above, last November’s total. Based upon reports by *Dairy Market News (DMN)*, some of that butter could be destined for export. School closures this week and next reduces the amount of milk used by bottling plants, which means additional butter production should occur. Prices on the CME this week added \$.0025 per lb after losing \$.1250 last week. Retail sales into this holiday week are reported to have been very good. The butter market continues to appear to be in good balance.

POWDER MARKET COMMENTS: DMN finds that the market for nonfat dry milk is firm and prices are steady with lighter buyer activity over the holidays. Production has increased because more milk is becoming available. Production of buttermilk powder is also up, in pace with the higher production of butter, and prices are about even with nfdm prices. Prices reported by the two major reporting agencies for nfdm sales last week remain close to where they have been for the previous two weeks, but with slightly higher volumes. The latest reports on milk production from Oceania continue to show lower than expected volumes; Australian milk production for the period July-October is 5% lower than the same period a year ago, and New Zealand milk production is running only about 2% above last year’s disappointing output. They are approaching their peak production months. The dairy industries in both of these countries are structured to enable moving milk into the highest valued commodities. Let them produce whole milk powder.

WHEY PRODUCTS MARKET COMMENTS: This week's assessment of the markets and prices for dry whey and whey protein concentrate (34% protein) continues to be positive. The markets are strong and prices continue to rise. The West's "mostly" price added a fraction of a penny this week, and the WPC average is now in the mid 80's. Demand for domestic and export sales are reported to be steady.

FRED DOUMA'S PRICE PROJECTIONS...

Dec 24 Final:	Quota cwt. \$ 16.13	Overbase cwt. \$14.44	Cls. 4a cwt. \$14.67	Cls. 4b cwt. \$15.04
Last Week:	Quota cwt. \$ 16.19	Overbase cwt. \$14.49	Cls. 4a cwt. \$14.66	Cls. 4b cwt. \$15.18

MILK PRODUCTION TREND: DOWN? UP? LEVEL?: (By J. Kaczor) In a short article last week about milk production in November it was mentioned that the number of cows this November was 242,000 fewer than last November but the decline in number of cows, compared to previous month-to-month changes, had tapered off. The October to November change was only 8,000. [The decline in number of cows for California was incorrectly stated as 70,000 fewer than last November; the correct number is 80,000 fewer dairy cows.] That leads to a logical question; what's next – for the U.S. and for California? Will the heavy culling in most of the major milk producing states, with or without CWT's herd removal programs continue, or will most producers do as they always have – respond to the rising milk prices by adding cows as fast as practicable, with the blessing of their lenders and their milk plants?

Recent history (since at least the year 2000) has shown that to be the common sense, tried and true, business plan. Herd expansions have accelerated after every substantial herd contraction, regardless of whether the contractions were "natural" such as in 2000, 2003, and 2006, or assisted by CWT's herd buy-outs as in 2004, 2005, and 2007. The herd contraction resulting from CWT's last four herd buy-outs, covering a thirteen month period from last December to this December, is still being measured. Those herd buyouts are the major contributor to the 242,000 decline thus far; we'll be able to estimate CWT's part of the total 2009 dairy herd contraction on January 19th, when USDA issues its milk production estimates for December. After which, most observers believe herds will begin to expand. How soon, and by how much? If the pattern that followed the six periods of major contraction mentioned above is followed, the noticeable expansion will begin almost immediately, even before the bottom is reached, and will grow fast until all or virtually all of the 2009 contraction is erased.

However, some of the conditions facing milk producers this time are different from previous rebounds. For one thing, credit availability is very tight, and there is belief that some lenders simply will not extend any more. Another is operating costs are generally higher than in the past, and feed costs, too. A third is that expected increases in milk prices, indicated by CME futures prices for cheese, butter, and powder, through next year presently are not promising much more than break even returns for producers. And finally, the Great Recession continues to impede businesses from expanding their workforces. Those considerations alone could significantly dampen or delay an otherwise certain herd rebound. On the other hand, there were almost forty-three affordable heifers available in July for every one hundred dairy cows (forty-seven is the expected number in January, and more than half of them are expected to be already bred), the use of sexed semen is reported to be growing, and all four of the major dairy commodities that generate milk prices in the U.S. have risen by substantial amounts and there is hope they are headed even higher.

Reasonable people, looking at the same set of facts, can reach opposite conclusions. USDA's Economic Research Service (ERS), in the December 17th edition of *Livestock, Dairy, and Poultry Outlook*, reports they expect the dairy herd contraction to continue well into 2010, and will reach and remain below nine million cows for all four quarters of the year, although with a higher than average increase in production per cow. A reasonable case is provided to support that position, including an increase in exports. Very bullish, that projection, one that seemingly would beget industry prosperity. Unfortunately, it is contrary to some very smart industry economic models that say the herd will expand in response to higher milk prices, on schedule, just as it

always has, and in doing so will take milk prices back down too soon. Part of the ERS thinking is contained in an interesting Special Article included in the *Outlook* that was also published in last week's *Dairy Market News*. It's written by Rachel J. Patton, USDA, ERS. Look it up, it's worth a read. It makes a case against an early and rapid herd expansion, partly because CWT removed so many whole herds on the condition that the facilities not be used for milk production for one year. Patton minimizes the near-term effect of sexed semen usage because of the higher net cost per calf, the time it takes from birth to when the heifer is bred, and the need to first expand production facilities.

This is not to say the ERS analysis is without merit, but it seems to me the determining factor on when and how fast cows are added to the U.S. milking herd may be the ability of producers to refinance or to extend existing credit to enable them to begin to substantially reduce existing debt. Herd liquidations won't do it; \$2 or \$3 or \$4 million doesn't buy much liquidity in the dairy industry these days. Sufficient credit may not be readily available to most, but it should be for enough to aggressively expand by using existing animal assets or by buying some that are available. Isn't it already happening? Maybe, maybe not. It should take several more months before a clear enough picture is available to say one way or another. Opportunity does exist. Use the advice of your lender and your broker to sort through what can be done to take advantage of what becomes available.

FAREWELL AND BEST WISHES TO AN OLD FRIEND: *(By Geoffrey Vanden Heuvel)* Tom Gossard, senior economist with the Dairy Marketing Branch of the California Department of Food and Agriculture is retiring this month after decades of service to the State of California and the dairy industry. Tom is one of the first people I learned about the California milk pricing system from back in the early 1980's.

Tom is a very helpful public servant. Always returning phone calls and answering any questions that arise. He has exceptional skills at pricing analysis. On the other hand I was never able to get him to share with me his "advice to the Secretary" on the many price hearings where he has been a panel member and I have been a witness. He would always remind me that his advice to the Secretary was confidential. I understood and respected his integrity.

In some ways the relationship with CDFA is adversarial. As producers, it seems we seldom get our way at price hearings, but Tom never appeared to take the criticism that is often sent CDFA's way personally. He was always nice and always helpful. We thank him for his service to the dairy industry and wish him all the best in his retirement.

ADDENDUM TO THE ABOVE: *(By J. Kaczor)* I second the comments made in the preceding article. I've found over the years in dealing with Tom that he helped to make doing business a pleasure. He was easy going, gracious, knowledgeable, and professional – and I couldn't wear him down.

REMINDER FOR SOUTHERN CALIFORNIA DAIRYMEN – WATER BOARD ANNUAL REPORTS DUE ON JANUARY 15th: *(By Rob Vandenheuvel)* As a reminder, the annual reports to the Santa Ana Regional Water Quality Control Board are due on January 15, 2010. This is the report that includes your "annual report of waste discharge," your manure tracking forms, and a summary of your weekly inspections of your wastewater ponds.

The Water Board sent out a letter with some blank annual report forms a couple weeks ago, but due to a glitch in their system, about half of them went to the wrong addresses. They have resent the letter and the forms, and you should be receiving them shortly. If any members need assistance in filling out those forms, please contact the office at (909) 628-6018.

On behalf of the MPC staff, we'd like to wish everyone a wonderful Christmas!