MPC Weekly Friday Report

Date: April 23, 2021
To: Directors & Members
From: Kevin Abernathy, General Manager
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MPC Friday Market Update

Chicago Cheddar Cheese			Chicago AA Butter			Non-Fat Dry Milk		
Blocks	*+ $.0125*	$1.7925	Weekly Change	*- $.0800*	$1.7700	Week Ending 04/17/21		
Barrels	*+ $.1150*	$1.8050	Weekly Average	*- $.0870*	$1.7940	Nat'l Plants	**$1.1645**	19,970,007
Weekly Average Cheddar Cheese			**Dry Whey**					
Blocks	*+ $.0880*	$1.7905	Dairy Market News	w/e 04/23/21	$.6487	Prior Week Ending 04/10/21		
Barrels	*+ $.0035*	$1.7925	National Plants	w/e 04/17/21	$.6093	Nat'l Plants	$1.1645	17,226,117

California Federal Milk Marketing Order Price Projections

Price Projections	Class I Actual (range based on location)	Class II Projected	Class III Projected	Class IV Projected
April 23 Est	$17.11 - $17.61	$15.59	$17.64	$15.52
Last Week	$17.11 - $17.61	$15.64	$17.64	$15.47

Milk, Dairy and Grain Market Commentary

By Sarina Sharp, Daily Dairy Report
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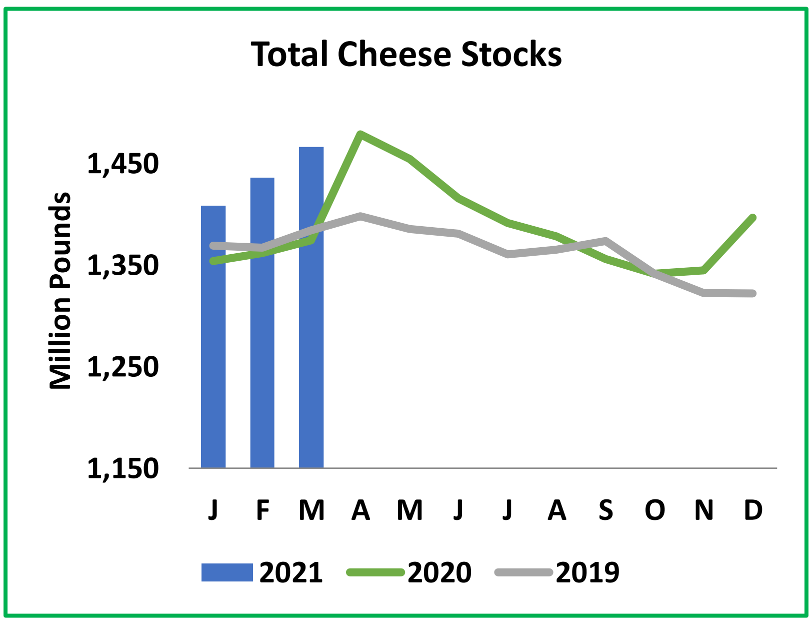
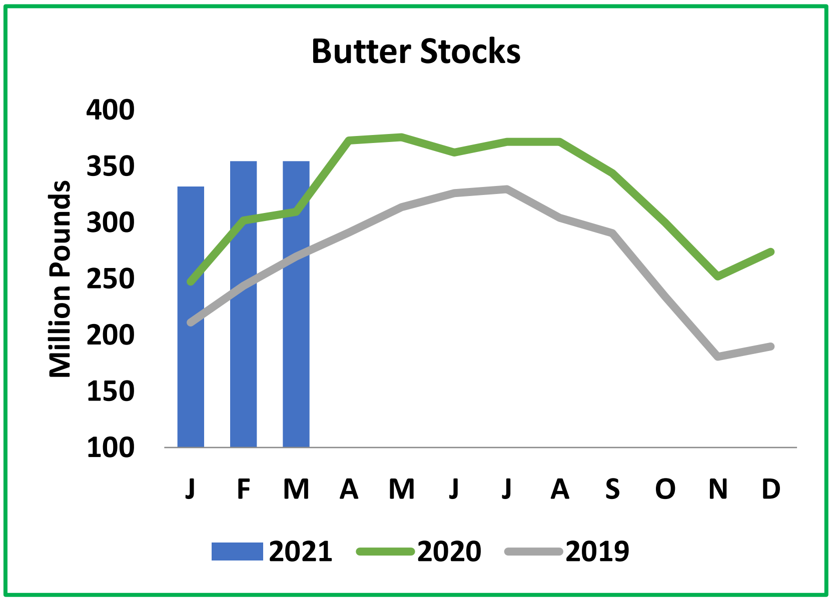
Milk & Dairy Markets

The Class III markets ended the week not far from where they began, but the calm on the surface belied the roiling waters below. CME spot whey powder, which has long had the wind in its sails, was buffeted by the waves this week. It dropped 5.5¢ to 62¢ per pound. Orders remain aggressive for high protein whey products, but some buyers are starting to balk at lofty whey powder values. Whey futures reached 14-year highs early in the week but then retreated.



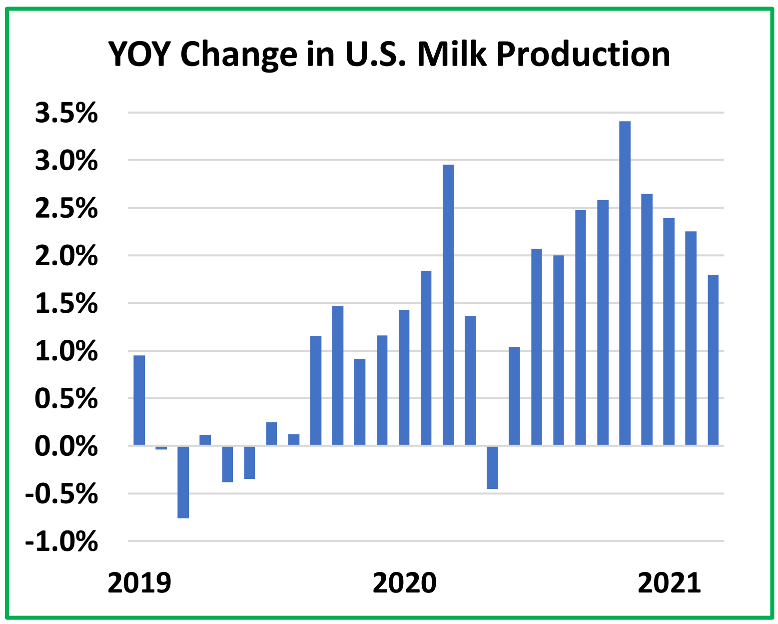
After much back and forth, CME spot Cheddar blocks closed at $1.7925 today, up 1.25¢ from last Friday. Blocks are plentiful,



but barrels are tighter, and the imbalance is reflected in the price. Barrels jumped 11.5¢ this week to $1.805, their highest value since November. Barrels are now worth more than blocks for the first time since July.

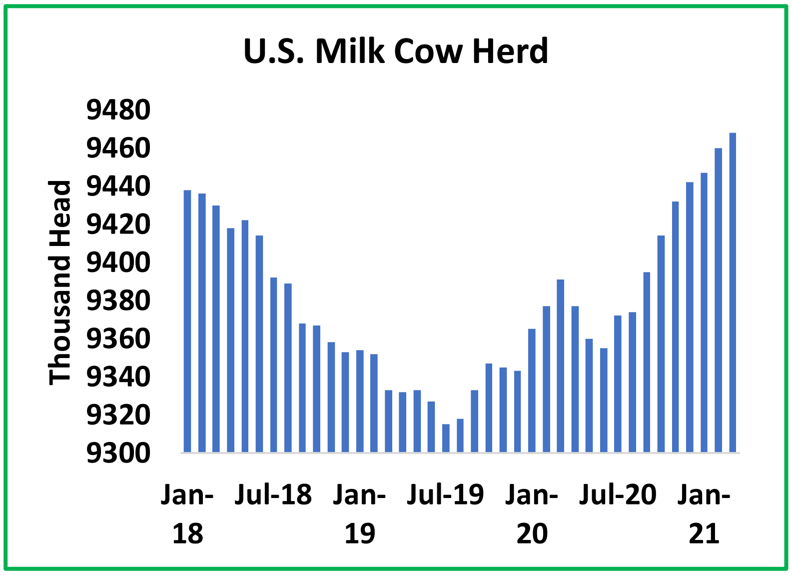
Barrel supplies may be a little snug, but there is more than enough cheese to go around. USDA reported 1.47 billion pounds of cheese in cold storage at the end of last month, the second-highest total ever and the highest March volume on record. Stocks increased 30 million pounds from February to March, nearly twice the normal rate.

Butter inventories are also extremely heavy. There were 354.6 million pounds of butter in cold storage on March 31, the highest March total since 1993. Stocks are 14.5% greater than they were a year ago. However, as more milk heads to cheese vats, the year-over-year butter surplus is shrinking. Butter stocks grew at roughly half the typical pace from February to March and they did not grow at all last month. A plateau is rare at this time of year, and it confirms reports of strong demand from foodservice. However, USDA's *Dairy Market News* notes that retailers are starting to slow their orders. At the spot market, butter continued to fade this week. CME spot butter fell 8¢ from last Friday and closed at $1.77.



Spring is here. Tankers are lining up at milk powder plants around the nation, although the queue is a little shorter in the Midwest than it was last year, thanks to expanded cheese capacity. A shortage of trucks and drivers is complicating the annual rush to move milk from regions with surplus to regions with spare balancing capacity, which is exacerbating discounts for milk in the Southwest. Milk powder demand remains strong. Exporters continue to move big volumes to Asia, and Mexican orders are picking up steam even as prices rise. CME spot nonfat dry milk rallied 3.75¢ this week to a fresh 14-month high at $1.2525. That helped to lift Class IV values. Nearby contracts added a nickel, while most deferred contracts climbed at least 20¢. Second-half Class IV values are now comfortably above $17 per cwt.

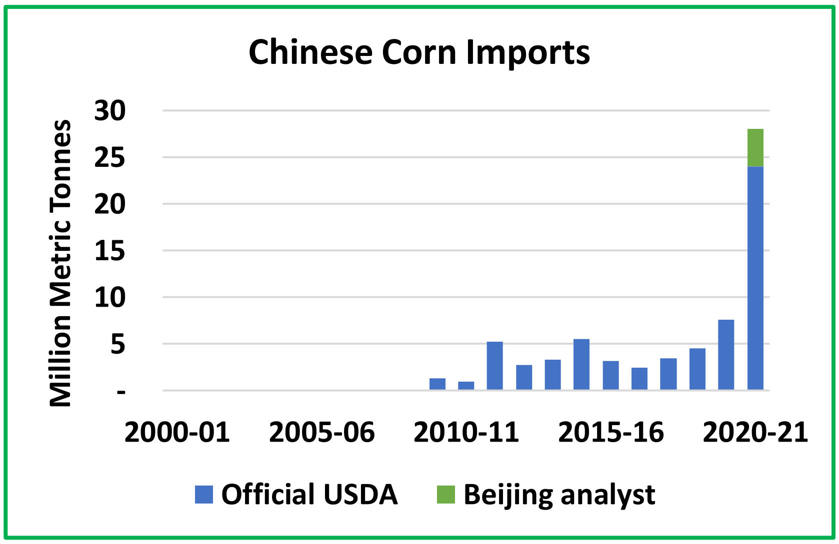
China's appetite for foreign dairy continues to astound. In March, China imported record-breaking volumes of cheese and whey, with arrivals up 74% and 77%, respectively, from a year ago. Chinese first-quarter skim milk powder (SMP) imports were record-large, up 35.5% from the first three months of 2020. Chinese imports of whole milk powder (WMP) in the first quarter were 22% higher than the prior year and were just shy of the breakneck pace set in 2014.



China's aggressive purchases have largely cleaned up New Zealand's dairy product stockpile. In Europe, slower milk output has tightened their exportable inventories, particularly for milk powders. In January and February, European SMP production was 7% lower than the prior year, adjusted for leap day. As long as we can secure the containers and ships needed to send product abroad, the United States is well-positioned to capture a greater share of China's burgeoning dairy market. That's welcome news because we have a lot of milk to move.

U.S. milk production totaled 19.75 billion pounds in March, up 1.8% from a year ago. That's a slight slowdown in year-over-year growth, which has been 2% or higher since July 2020. However, the headline figure is misleading in its modesty because this represents a respectable increase on top of the strong 3% growth reported in March 2020. Milk output was 4.8% greater than March 2019, the strongest two-year increase since September 2015. Production was particularly formidable in the Plains states and the Midwest.

Dairy producers added another 8,000 cows in March, which will fuel further growth in the months to come. There are now 9.468 million cows in U.S. milk parlors, 77,000 more than there were a year ago. The U.S. dairy herd hasn't been this large since 1995. We're going to need to sustain big exports, or we'll be drowning in milk.



Grain Markets

Someone tied a rocket to the corn market and lit the fuse. July corn futures closed today at $6.325 per bushel, up nearly 60¢ since last Friday. Corn futures jumped more than 10% this week and are up 32% for the year to date. Corn prices have not been this high since 2013, on the heels of a paltry harvest after the 2012 drought. These prices suggest that last year's corn crop may be smaller than previously thought. And demand is daunting. USDA's analyst in Beijing raised his estimate of 2020-21 corn imports to a record-shattering 28 million metric tons, which is 4 million metric tons higher than USDA's official projection. That's a difference of 157 million bushels. If correct, this would significantly tighten U.S. corn stocks, putting more pressure on farmers to deliver a bumper crop this season. Light rainfall in Brazil suggests their second corn crop will disappoint, pushing even more demand to the United States.

With corn prices at such heights, soybeans are losing acreage they desperately need to meet global protein demand. Struggling to keep pace with the grains, the soy complex shot higher this week. July soybeans settled at $15.16, up 93.5¢ from last Friday. July soybean meal rallied nearly $20, to $425.80 per ton. Even these sky-high values understate the cost to many dairy producers, who must pay unusually high premiums for freight to keep their cows fed.

Water & Milk Policy News

By Geoff Vanden Heuvel, Director of Regulatory and Economic Affairs
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Recent Groundwater Data Reveal Significant Overdraft

It's dry. There has not been much moisture this past winter and surface water deliveries to the Central Valley this summer will be small to non-existent. Last winter was pretty dry too. Dry winters are not unusual in California. But now, access to groundwater – our reserve water supply – is regulated. The Sustainable Groundwater Management Act (SGMA) was passed in 2014 as a result of the last serious dry period. This legislation prompted the formation of locally controlled Groundwater Sustainability Agencies (GSAs) throughout California. The GSAs in the Central Valley have been established, Groundwater Sustainability Plans have been drafted by the GSAs, and those plans are now being implemented. An early action item in those plans is the tracking and reporting of water use in their jurisdiction to the state. On April 1, all the GSAs in the Central Valley reported their water use for the period October 2019-September 2020. You can see this information here.

Of particular interest in the reports is the change in storage number. This number is a gauge of overdraft. If the number is negative, more water was removed from the ground than was recharged. A positive number would represent an increase in groundwater storage. In the April 1 report, all the subbasins I am following (because they have a dairy presence) reported a negative change in storage. Cumulatively, those subbasins reported a negative change in storage of 3,453,081 acre feet. This was the first annual report since many GSAs put in place their monitoring and data collection protocols. The data is imperfect and can be spotty in some places. But the picture this gives is certainly a concerning one.

With another low surface water year upon us, the groundwater table will once again be tapped hard to maintain agriculture's cropping demands. But change is coming. We do need to put in place the infrastructure to capture and recharge all the water that may be available in a wet year. There is a growing recognition that there needs to be public financial participation to make that happen. But business as usual is not sustainable. This challenge is very location specific. Some areas have much better access to surface water. And even though there will not be much surface water this year, when the rains return, those areas have the ability to recover. Areas without access to surface water are in a much different position. Many GSAs are working to attempt to supplement their water supplies, but there are some where the GSA is leaving it to landowners to fend for themselves. As far as I know, no GSAs are yet mandating a reduction in groundwater pumping, but many are putting in place allocation systems that will use financial tools to incentivize reduced groundwater usage. Learning about your situation and getting involved in your local GSA is a wise investment of effort. As always, I am happy to share what I have learned about your area if you want to contact me.

Class I "Higher of" vs. "Average of" Policy Debate Continues

The Class I formula is the topic of intense attention by the dairy industry right now. The Federal Milk Marketing Orders (FMMO) utilize a classified pricing system to regulate milk prices. Class I is fluid milk and is the only classification of milk that is required to both pay a minimum price and participate in the pooling of that revenue with all the participants in the order. Participation by the other classes of milk, Class II (soft products), Class III (cheese) and Class IV (butter/powder) is voluntary. Those classes participate primarily to obtain a share of the class I revenue. It is pretty easy to figure out that for this system to work, Class I prices need to be higher than all the other classes or there will not be any money to share. That is why when USDA reformed the system in 2000, creating a separate formula using product values for Class III and Class IV, it established the base price for Class I as the **HIGHER OF** either the Class III or the Class IV prices to make sure the Class I price stayed in its proper alignment.

The International Dairy Foods Association (IDFA) approached National Milk Producers Federation (NMPF) in 2018 and asked them to consider changing the "higher of" to the "average of" Class III and IV so that hedging Class I would be easier. NMPF was willing to consider this if IDFA was willing to support an add on to the Class I price to compensate producers for the elimination of the benefit of the "higher of." The data since 2000 showed that the "higher of" policy resulted in a Class I price that was on average $0.74 per cwt. higher than it would have been if the "average of" was used as the base price. IDFA agreed to support adding $0.74 per cwt. to Class I price and Congress approved changing the Class I formula to the "average of" plus $0.74 through legislation. Then the pandemic hit.

The huge and unprecedented gap between Class III and Class IV prices in 2020 created all sorts of problems – not the least of which is that the new Class I formula, based on the "average of" Class III and IV produced Class I prices that were vastly lower than they would have been under a "higher of." This led to significant misalignment of class prices and contributed to de-pooling and negative producer price differentials. It's estimated that Class I prices under the "average of" formula were lower by more than $700 million. This has resulted in calls for change from the producer community.

NMPF is proposing to increase the $0.74 to a much higher number that would reflect the huge change in the relationship between Class III and IV during the past year. IDFA has rejected this approach saying the issue needs more study. NMPF appears likely to petition for a hearing at USDA to propose its change. Other voices in the producer community are suggesting different numbers or time periods. There are also voices in the producer community who are advocating going back to the "higher of" as the right approach.

My take is that the change that Congress made in 2019 had a huge negative impact on producers which in turn has raised all kinds of questions and doubt about the FMMO system. We need to recognize that there are constituencies in the dairy industry who would prefer a deregulated market. I am a big supporter of the value of the FMMO system to producers. The government plays an important role as the referee between producers and processors. Without FMMOs, I think the big box retailers would set Class I prices in America and producers who still must sell milk every day to a buyer who does not have to buy milk every day would be at a huge disadvantage at the milk price negotiating table. The FMMO system has been the referee and lasted 85 years by being based on solid economic and policy principles.

I believe how we react to this challenge will lay the groundwork for what follows. Tweaking adjusters to achieve a particular result as opposed to adopting policy based on principles could ultimately undermine support for the FMMO system and lead to its demise. That would not be a good result in my view, but some would cheer. We can be sure there is much more to come.

Mailbox Alert! CVDRMP Sends Invoices for Groundwater Monitoring, Salt and Nitrate Regulatory Compliance

Courtesy of the Central Valley Dairy Representative Monitoring Program

Over the past month, most dairy producers who are members of the Central Valley Dairy Representative Monitoring Program (CVDRMP) have received an invoice for 2021 membership dues. In addition to the usual annual membership dues related to the coalition's groundwater monitoring network, producers will note additional items on this year's invoice for compliance with new Central Valley Water

Board regulations related to Salt and Nitrate Control Programs. More detailed information about the new regulations – and CVDRMP's work to streamline compliance for its members – is available here.

CVDRMP members located entirely outside a nitrate management zone (NMZ) or in a so-called Priority 2 NMZ were the first to receive invoices in late February. Invoices for Priority 1 NMZs – Modesto, Turlock, Chowchilla, Kaweah, and Tule – were mailed earlier this month to members located in those zones. CVDRMP members located in the Priority 1 Kings NMZ (Kings and Fresno counties and the northwest portion of Tulare County) should expect to see invoices in their mailbox by the end of April.

Included with the invoice is a cover letter from CVDRMP Chairman and dairy farmer Scott Wickstrom. Producers are encouraged to the read the letter and supporting materials, which explain changes CVDRMP made to its program to help its member dairy farmers comply with recently adopted regulations. Timely payment of the CVDRMP invoice will ensure each dairy is in compliance with Water Board regulations for groundwater monitoring, salt, and nitrate programs.

For any questions related to CVDRMP membership and compliance with the Salt and Nitrate Control Programs, producers are encouraged to call 916-594-9450 or email cvdrmp@gmail.com.

NMPF President's Update

By Jim Mulhern, President & CEO of National Milk Producers Federation

NMPF Board of Directors Endorses Class I Mover Reform – NMPF's Board of Directors today endorsed revamping the current Class I formula, established in the 2018 farm bill, so that it restores equity to the pricing of fluid milk products. NMPF's proposal, which will go to USDA as a request for a national federal order hearing, would modify the Class I mover, which currently adds $0.74/cwt to the monthly average of Classes III and IV. Our proposed change would adjust this amount every two years, to "true-up" the current calculation with the "higher of" Class III or IV, with the current mover remaining the floor. NMPF will prepare a formal request to the USDA asking the agency to hold a hearing specifically on a change to the Class I mover, after which USDA would have 30 days to issue an action plan that determines whether USDA would act on an emergency basis.

The current mover was intended to be revenue neutral while allowing fluid milk handlers to better hedge future price risks. But the revised formula contributed to severe disorderly marketing conditions last year during the height of the pandemic, reducing dairy farm revenue by more than $725 million. NMPF's proposal would help recoup the lost revenue and ensure that neither farmers nor processors are disproportionately harmed by future significant price disruptions.

April NMPF *Dairy Market Report* Assesses 2021 Price Outlook – Our latest monthly analysis of dairy markets finds several bullish indicators for milk prices, including rising domestic dairy demand resulting from relaxation of restrictions on restaurants, growing ranks of the vaccinated, and a resumption of in-person schooling. Internationally, U.S. dairy exports surged in February, while dairy imports have dropped to multi-year lows as a percentage of domestic milk solids production. But rising demand isn't keeping pace with milk production, and stocks of major dairy products are rising.