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DATE: July 17, 2015 **PAGES: 3**
TO: Directors & Members **FROM: Rob Vandenheuvel, General Manager**

BREAKING NEWS: CDFA ANNOUNCES SIGNIFICANT INCREASE TO CLASS 4B PRICE!

(By Rob Vandenheuvel)

For the past several years, we've kept a close eye in this newsletter on the significant gap between California's Class 4b price *(which applies to milk sold to California's cheese manufacturers)* and the Federal Order Class III price *(the benchmark price used around the country for milk sold to cheese manufacturers)*. We've dubbed it the "California Discount" and kept a running tally on the impact it has had on California's producers.

This week, following a hearing held on June 3rd, **Secretary Karen Ross and the California Department of Food and Agriculture (CDFA) took a significant bite into that California Discount, albeit on a temporary basis**. The announcement, which goes into effect on August 1 and is in place for 12 months, would bring our Class 4b price in much closer alignment with the Federal Order Class III price.

Now closer does not mean equal. Regardless of what our cheese making colleagues might think or say about this Class 4b price increase, they will still be benefiting from a lower regulated price than exists anywhere else in the country. **However, had this new calculation been in place last month, the Class 4b price would have been $0.69/cwt higher ($16.24/cwt) and would have been $0.48/cwt below the Federal Order Class III price (compared to the actual discount of $1.17/cwt).**

Looking at Fred Douma's price projections below, if this new calculation were in place for July, our estimated Class 4b price would be $15.39 ($0.55 higher), and our estimated overbase and quota prices would be $16.27 and $14.57 respectively ($0.25 higher).

The changes in the Class 4b formula are related to how the market price for dry whey is incorporated in to the milk price calculation. So looking forward, if the CME futures markets are any indication, the dry whey markets are expected to be at or below their current levels for the foreseeable future. Plugging in those dry whey prices into this new Class 4b calculation indicates that our Class 4b price on average over the next year should be roughly $0.50/cwt below the Federal Order Class III price. *(The gap between these prices will likely vary from month to month due to other differences between the two formulas, so this is a long-term average estimate.)* **While this represents a continued discount, it is a far cry from the $1.84/cwt average monthly California Discount we've seen since 2010!**

Of course, producers must continue to work towards a long-term policy that facilitates milk prices that are at-or-above the rest of the country, as we can no longer afford to be the low-cost-milk-leader in this high-cost environment. That is why MPC and our fellow producer groups and cooperatives must continue to press forward in promoting a California Federal Milk Marketing Order. Having said that, today's announcement represents good news for California's dairy families, providing them with a much-needed immediate adjustment that will result in more market-based revenue for California's dairy families and put us in a better position to compete with our fellow out-of-state dairymen.

(Note: If you'd like to read through all the details of CDFA's announced changes, you can find that material on CDFA's website at: http://cdfa.ca.gov/dairy/uploader/postings/hearings/)

CHICAGO CHEDDAR CHEESE		
Blocks	*- $.1125*	$1.6125
Barrels	*- $.0650*	$1.5950
Weekly Average, Cheddar Cheese		
Blocks	*- $.0180*	$1.6480
Barrels	*- $.0020*	$1.6120

CHICAGO AA BUTTER		
Weekly Change	*- $.0800*	$1.8400
Weekly Average	*- $.0555*	$1.8685
DRY WHEY		
Dairy Market News	w/e 07/17/15	$.3900
National Plants	w/e 07/11/15	$.4041

NON-FAT DRY MILK		
Week Ending 7/10 & 7/11		
Calif. Plants	$0.8905	10,311,468
Nat'l Plants	$0.8621	15,282,763
Prior Week Ending 7/3 & 7/4		
Calif. Plants	*$0.8835*	*7,631,303*
Nat'l Plants	*$0.8770*	*12,570,063*

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FRED DOUMA'S PRICE PROJECTIONS…

July 17 Est:	**Quota cwt. $16.02**	**Overbase cwt. $14.32**	**Cls. 4a cwt. $13.31**	**Cls. 4b cwt. $14.84**
Last Week:	**Quota cwt. $16.29**	**Overbase cwt. $14.59**	**Cls. 4a cwt. $13.47**	**Cls. 4b cwt. $15.32**

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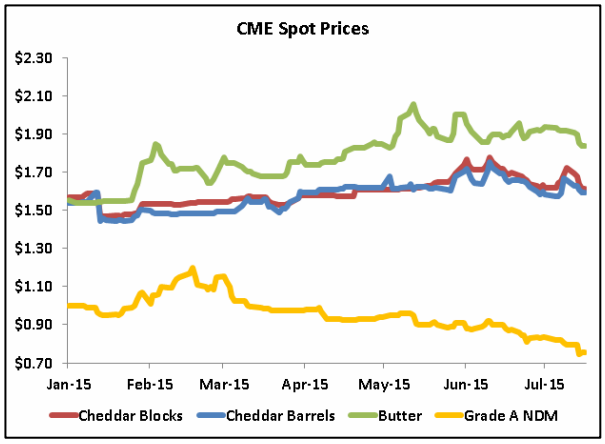
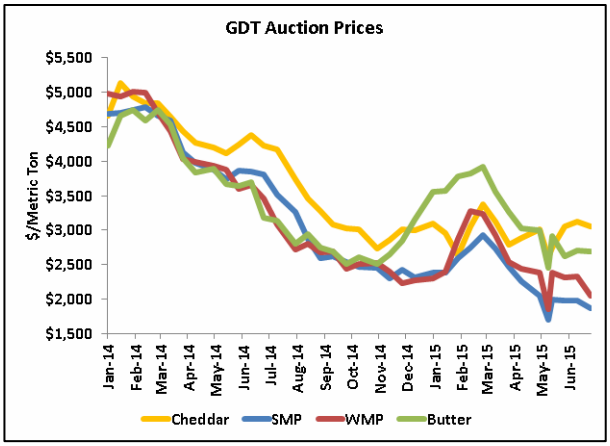
MARKET COMMENTARY: *(By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com)*



Milk & Dairy Markets

For months, the embattled U.S. dairy markets have managed to hold strong in the face of punishing opposition. They were buffeted by a strong currency, much lower markets overseas, a Russian dairy import ban, a slowdown in Chinese purchases and a veritable flood of milk at home and abroad. They suffered some bruises but fought on, succored by strong domestic demand. Now, they appear to be reeling.

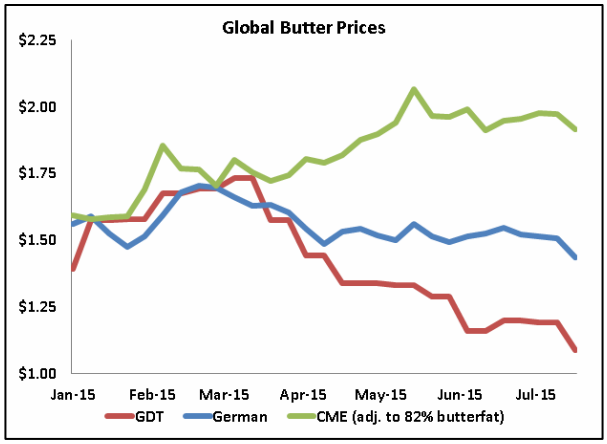
The butter market has been most resilient, but this week it succumbed. CME spot butter dropped to $1.84/lb., down 8¢ from last Friday to the lowest level since early May. CME spot Cheddar blocks fared even worse, falling 11.25¢ to $1.6125. Barrels slid 6.5¢ to $1.595. Milk powder prices continued their descent. On Monday, Grade A nonfat dry milk (NDM) hit fresh all-time lows at 74.5¢. They regained a penny and ended at 75.5¢, down 4¢ on the week. Dry whey futures moved lower. Most Class III futures contracts lost 50¢ to 60¢, while Class IV futures were generally 20¢ to 50¢ lower.



Dairy product prices were expected to fall at the Global Dairy Trade (GDT) auction, and fall they did. The poor performance at the GDT is the most conspicuous catalyst for the rout in the domestic dairy markets this week. The trade-weighted index dropped 10.7% to its lowest level ever. Butter (-9.5%), Cheddar (-13.9%), rennet casein (-8%) and skim milk powder (SMP; -10.1%) all plunged to new record lows at the GDT. Whole milk powder (WMP) prices lost 13.1%.

The worse-than-feared decline in milk powder prices was particularly troubling for dairy producers in New Zealand. The WMP price drives about 75% of the Fonterra payout, which is likely to be revised downward from the current forecast of NZ$5.25/kg of milk solids. Most of New Zealand's dairy producers cannot operate at a profit at the current forecast, much less at significantly lower levels. The Australia New Zealand Bank expects a payout between NZ$3.75 and NZ$4.00, while Westpac Banking Corp. called for NZ$4.30 for the 2015-16 season. At today's exchange rate, a NZ$4 milk price is comparable to US$8.40/cwt. These lower pay prices suggest that New Zealand's dairy producers will be less likely to spend on supplemental feed this year, which could lower milk output at the margins.

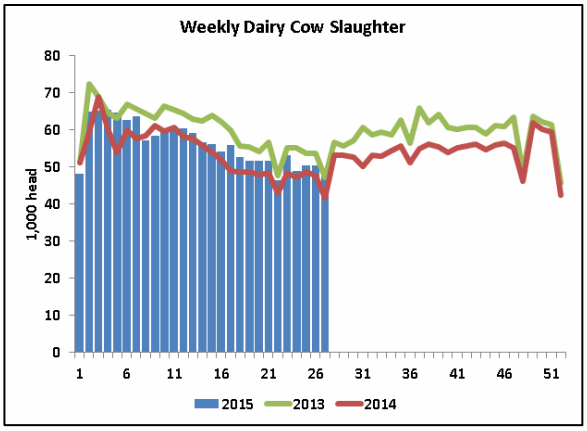
Dairy product prices continue to slide in Europe as well, and producers there are clamoring for support. Dutch SMP prices are within a hairsbreadth of the intervention price, at €1,698/metric ton (MT). In Germany, SMP has fallen to €1,735/MT. When SMP prices fall below intervention levels, the EU can purchase up to 109,000 MT of SMP from March to August. As the *Daily Dairy Report* notes, "Historically, public intervention removes dairy products from the market for a much longer time frame than purchases by end users – a move that could potentially support prices as it artificially rebalances supply."



Both CME spot and GDT milk powder prices are well below EU intervention levels, so at best intervention purchases would serve as a temporary, localized anesthetic. In response to calls for the EU to raise the intervention price, EU Agriculture Commissioner Phil Hogan stated, "It is of paramount importance that farmers and economic operators follow market signals." Raising the intervention price could be counter-productive as it mutes signals for dairy producers to slow production amidst a global surplus. "It would do nothing but delay the inevitable necessary adjustment and make it even more painful in the future," according to Hogan.

In the U.S., dairy producers in the Midwest are still unlikely to slow production. Recent declines notwithstanding, milk checks remain large enough – and weather mild enough – to encourage strong output in the heart of the country. Producers in areas with heavy butter and milk powder utilization must contend with Class IV prices in the low $13 range. But in Wisconsin and Minnesota, milk checks are almost entirely based on the much higher Class III market. Class III futures exceed Class IV by at least $2/cwt. through April 2016, and at $16.01, the September Class III contract is $3 higher than the comparable Class IV contract.

The wide spread between cheese and milk powder prices has encouraged cheese makers to fortify their vats with cheap powder, allowing them to run at capacity despite the calendar. Large volumes of cheese are likely destined for cold storage. *Dairy Market News* noted this week, "Manufacturers say their current inventories can easily meet regular customer requests. However, end users and cut and wrap operators have rebuilt their inventories."



For the week ending July 4, dairy cow slaughter totaled 48,500 head. This was 16.6% greater than the same week a year ago, but this is likely somewhat skewed because last year the Independence Day holiday fell on a weekday. Just over halfway through the year, dairy cow slaughter is 4.9% ahead of the 2014 pace.

Grain Markets

After soaring to new heights last week, most grain and oilseed prices took a step backward. December corn futures settled at $4.3125/bushel, down 14.25¢. November soybeans dropped 15.5¢ to $10.0675. But soybean meal prices remain stubbornly high. August soybean meal futures added another $4.40/ton this week, climbing to $361.10. In the past month and a half August soybean meal futures have climbed $70. With many crushers taking seasonal downtimes, cash prices have jumped even more.

The grain trade continues its focus on the weather, and the markets will likely remain volatile until harvest allows for a better assessment of the crop. Another week has gone by without any adverse weather, and conditions outside of the soggy eastern Corn Belt are excellent. Corn and soybean condition ratings in Iowa and Minnesota exceed those of last year, which is impressive given the record-shattering yields achieved in 2014. If the weather remains benign through the pollination phase, crop prices are likely to continue to erode. However, a change in the forecast could cause the markets to heat up once again.