



Milk Producers Council

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PAGES: 4

TO: Directors & Members

FROM: Rob Vandenheuvel, General Manager

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE

Blocks +\$.0725 \$1.7475
Barrels +\$.0900 \$1.7400

Weekly Average, Cheddar Cheese

Blocks +\$.0260 \$1.6980
Barrels +\$.0190 \$1.6810

CHICAGO AA BUTTER

Weekly Change +\$.0300 \$1.4900
Weekly Average - \$.0185 \$1.4850

DRY WHEY

Dairy Market News w/e 07/19/13 \$.5913
National Plants w/e 07/13/13 \$.5735

NON-FAT DRY MILK

Week Ending 7/12 & 7/13

Calif. Plants \$1.6732 10,967,840
Nat'l Plants \$1.7189 18,946,768

Prior Week Ending 7/5 & 7/6

Calif. Plants \$1.6695 9,791,590
Nat'l Plants \$1.7060 14,573,488

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

Milk & Dairy Markets

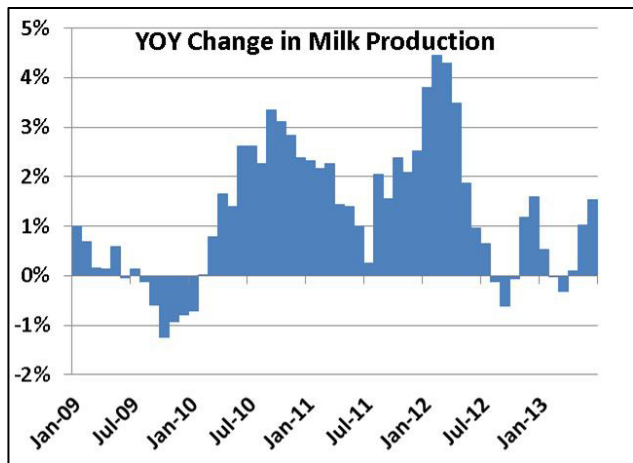
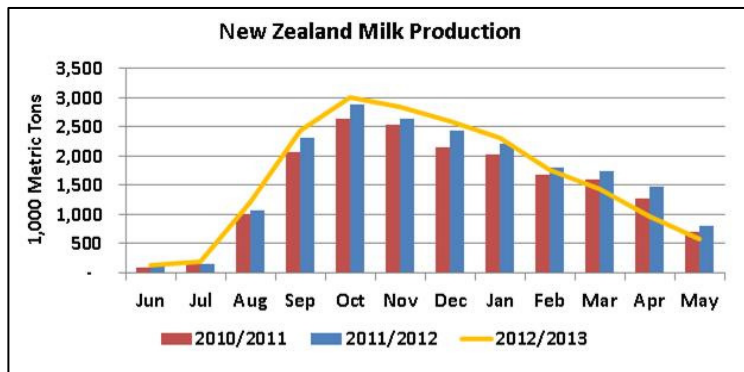
Heat from coast to coast spurred Class III futures to steep gains Tuesday amidst heavy trading volume. But while temperatures remained elevated, bullish enthusiasm cooled, and futures retreated on Wednesday and Thursday, only to surge again Friday. The September contract rallied most, adding 68¢ Tuesday and 27¢ Friday, settling at \$19.04. On average, August through December Class III futures added a half dollar this week. Class IV futures also enjoyed steep gains on Friday and ended 8 to 59¢ higher than last Friday.

The spot markets took on a similarly bullish tone this week. There is plenty of fresh cheese and domestic butter is plentiful, but end users are actively securing product. CME spot dairy product prices moved steadily higher session after session, and bids came thick and fast in the cheese trade Friday. Cheddar blocks settled at \$1.7475/lb., up 7.25¢ on the week. Barrels added 9¢ and butter settled 3¢ higher. Grade A and Extra Grade nonfat dry milk (NDM) settled 2.5¢ and 0.5¢ higher, respectively.

Domestic end users may be taking their cue from global dairy product prices, which have continued to rise. *Dairy Market News* reported steady to higher dairy product prices in Western Europe. Prices rose across the board in Oceania. The Global Dairy Trade auction confirmed the upward trend; the trade weighted index increased 4.9%, its largest biweekly increase since the height of the drought panic in March and early April. Only butter and casein prices moved lower at the GDT, and they remain at historically high levels. The average winning Cheddar price was \$2.03, up 2.1%. Skim milk powder (SMP) settled at \$2.17, up 3.3%. Whole milk powder (WMP) prices rose to \$2.29/lb., an increase of 7.7%. WMP and SMP contracts posted 4-7% gains in October through December.

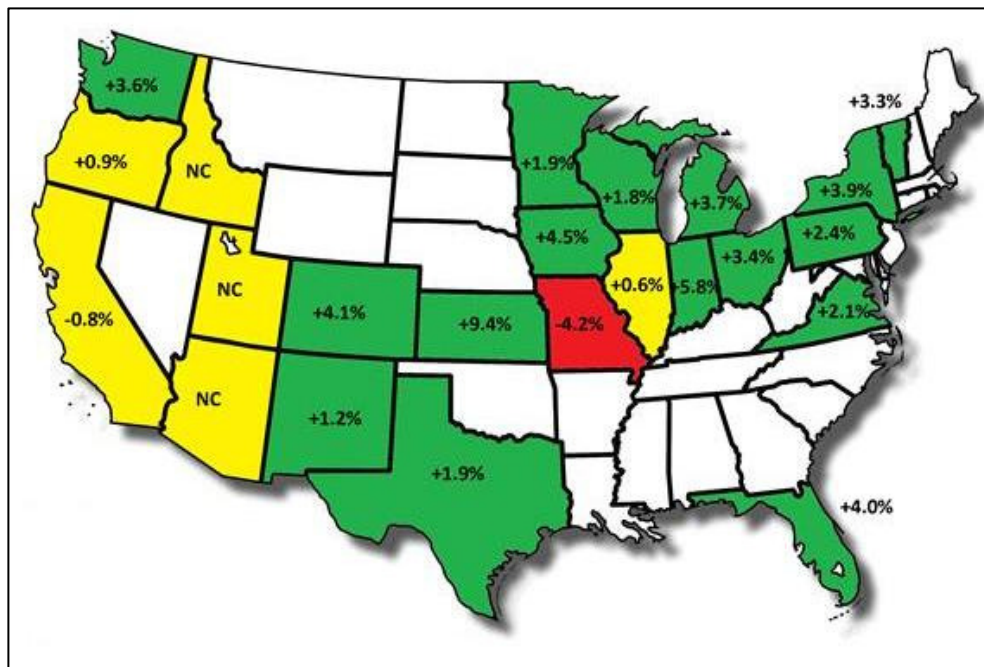
The futures markets promise larger milk checks and lower feed costs this fall. Improved margins could lead to stronger milk production, particularly in the U.S. and Europe if the weather allows. However, end users seem content to secure deferred dairy products at historically high prices, revealing uncertainty about global milk production and dairy product inventories this fall. Outside the U.S., months of adverse weather have restricted production, and foreign dairy product inventories are low. Denmark's Arla Foods added to concerns about the availability of milk powder earlier this month when they announced that they will limit offerings of SMP at the GDT through October due to reduced European milk flows during their low season.

New Zealand wrapped up its 2012-2013 milk production season with an unimpressive 580 thousand metric tons of milk production in May, 28% lower than May 2012. Full season volume was down 1% from the record large 2011-2012 season, the first year-over year decline since the drought-reduced 2007-2008 season.



In contrast, U.S. milk production remains very strong. National production totaled 16.93 billion lbs. in June, down 1.6% from May on a daily average basis but up 1.5% from June 2012. This was the largest year over year gain in six months and it was on the high end of pre-report expectations. This could pressure the dairy markets when they reopen next week. USDA revised its estimate of May milk production downward by 39 million lbs. California milk production totaled just shy of 3.5 billion lbs., 0.8% lower than June 2012. Missouri was the only other major dairy state to report a year over year decline in milk production; volumes there were down 4.2%.

Oregon, New Mexico and Texas reversed a trend of deficits and increased production relative to year ago levels. Most other states reported a larger year-over-year increase in June milk production than in recent months. Once again, states in the Midwest and Northeast reported the highest production gains. USDA did not estimate the size of the milk cow herd or issue its biannual Cattle report, which estimates July 1 dairy cow and heifer replacement inventories. The slower slaughter rate in June and strong milk production suggest that cow numbers likely increased in June. Increased cow numbers and the potential for better profit margins suggests that, once the heat abates, milk production could move quickly higher, particularly in areas with heavy milk powder utilization.



For the week ending July 6, dairy cow slaughter totaled 47,195 head, up 5.4% from a year ago. Slaughter volumes were lower than normal because it was a holiday week. Year to date slaughter is 3.5% higher than in 2012.

Dairy cow cull beef revenue is based on the lean beef price, which remains at historically high levels. However, it has trended lower since peaking in March, as retailers are struggling to move beef given much lower poultry and pork prices. Beef demand has been further dampened by the heat wave which has reduced grilling demand. However, cattle numbers remain low, and when pasture conditions improve and cattle producers begin

restocking, finished cattle supplies could fall further. According to USDA's Cattle on Feed report, cattle producers placed 5% fewer cattle on feed last month than in June 2012. There were 3% fewer cattle on feed than last year. These figures are bullish relative to pre-report expectations, and they could support deferred cattle prices.

Grain and Hay Markets

December corn prices shed 8.5¢ this week, as the crop generally remains in good condition. High temperatures have doubtlessly increased water intakes, and most fields would benefit from a slow, soaking rain. Widespread rains are expected this weekend, with more early next week, but the Plains and Western Corn Belt could get short-changed thereafter. The extent and amount of weekend rainfall across the Corn Belt and the latest forecast will be the key determinants of price direction next week.

August soybean futures added 60¢ this week. November soybeans followed, adding 17¢. Supplies are tight, but favorable crushing margins are spurring processor demand for soybeans and lifting nearby prices. U.S. soybean and meal exports are unusually strong for this time of year, as importers who typically turn to South America are buying U.S. soybean meal due to concerns about the quality of Argentine soybean meal. Domestic users are thus competing with foreign buyers, and the soybean meal basis has moved ever higher. There will be little leftover by harvest, making a large crop even more important.

FRED DOUMA'S PRICE PROJECTIONS...

July 19 Est: **Quota cwt. \$18.61** **Overbase cwt. \$16.92** **Cls. 4a cwt. \$18.48** **Cls. 4b cwt. \$15.64**
Last Week: **Quota cwt. \$18.50** **Overbase cwt. \$16.80** **Cls. 4a cwt. \$18.41** **Cls. 4b cwt. \$15.44**

THE "CHEAP MILK POLICY" CONTINUES; WHEN WILL THE INSANITY END? *(By Rob Vandenheuvel)* For regular readers of our newsletter, this article is nothing new. It's merely the latest update in a long, painful story that California dairy families are living every day. With the June 2013 monthly minimum prices announced by the California Department of Food and Agriculture (CDFA), we are once again reminded of just how discounted our California Class 4b price (for milk sold to cheese manufacturers) is relative to the Federal Order Class III price (which is the benchmark price for milk sold to cheese manufacturers throughout the country).

As you can see in this chart, our California Class 4b price once again lagged below the Federal Order Class III price by \$2.11 per hundredweight (and \$1.71/cwt since 2010, when this disturbing trend first began).

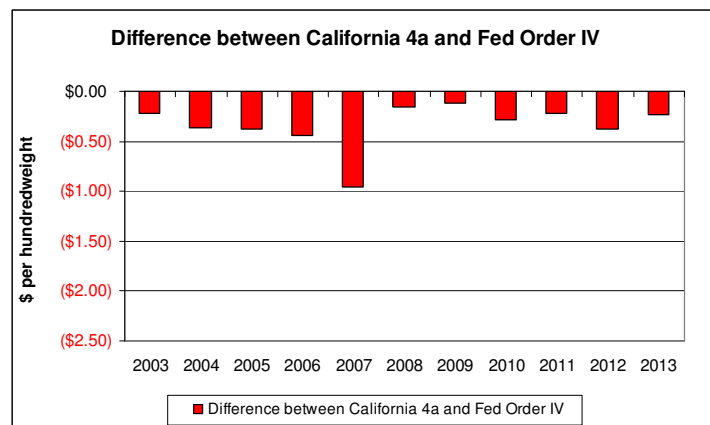
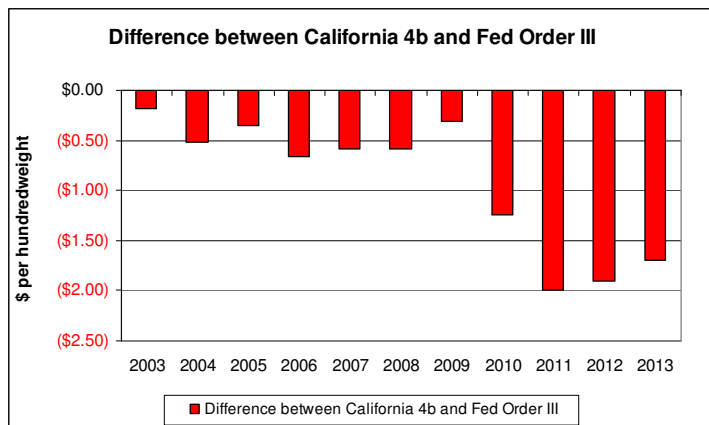
The "California Discount" for our State's Cheese Manufacturers		
	June 2013	Jan '10 – Jun '13
California Class 4b Price	\$15.91	\$15.17
FMMO Class III Price	\$18.02	\$16.88
Difference	(\$2.11)	(\$1.71)
<i>The "California Discount": \$871,000,000 since January 2010</i>		

What does this mean in real dollars? It means that **the "California Discount" being enjoyed by California's roughly 60 cheese manufacturers has now reached about \$871,000,000 since January 2010, all on the backs of the roughly 1,600 dairy farms left in California.** That represents more than **\$511,000 per 1,000-cow dairy!**

California's dairy families have long argued that this gap runs directly against the guidelines in California law that require our prices to be in a "reasonable and sound economic relationship" with what comparable milk is sold for around the country. The State's cheese manufacturers come up with excuse after excuse about why it's perfectly appropriate to have this huge discount in the price they pay for milk, but the facts simply don't support their claims.

About 75 percent of California's milk production is sold to make either cheese or butter/nfdm. These are our two main manufacturing classes. Those two types of manufacturers have two separate prices they must pay for the

milk they buy: Class 4a (butter/nfdm) and Class 4b (cheese). Below are two charts showing how those two prices have compared to the comparable Federal Order prices: Class IV (butter/nfdm) and Class III (cheese):



Notice anything about these two charts? There is a huge difference in what is considered a “reasonable and sound economic relationship” for these two class prices! While the California Class 4b price averaged about \$0.45/hundredweight less than the Federal Order Class III price from 2003-09, the gap has blown up to \$1.71/hundredweight in the three-plus years since then. On the other side of the ledger, the Class 4a price has averaged \$0.34/hundredweight below the Federal Order Class IV price during the entire ten year period.

So why is it “reasonable” to have a \$0.34/hundredweight gap for our butter/nfdm manufacturers, while allowing the gap to grow to \$1.71/hundredweight for our cheese manufacturers? We submit that it is NOT.

The law specifically states that the purpose of CDFA’s involvement in establishing milk prices is to, “enable the dairy industry, with the aid of the state, to develop and maintain satisfactory marketing conditions, **bring about and maintain a reasonable amount of stability and prosperity in the production of market milk....**” (*excerpt from Section 61805(D), emphasis added*). How is an artificial discount on California-produced milk helping to achieve that goal? In a state where dairy farmers face some of the highest feed and regulatory costs in the country, how does CDFA expect our dairy farmers to continue with the lowest milk prices in the country? And finally, why – after several years now of watching this disgusting trend and the resulting reality of bankrupt dairy families and shut down operations – do we still find ourselves in the same predicament?

The answers to these questions are exactly why we are seeing an increasing effort by the State’s dairy farmers to develop a path towards a Federal Order in California. Many questions still need to be answered as to the details of this type of proposal, but the reality is that unless something **dramatic** were to change, California dairy farmers are making the fundamental statement that the leadership at CDFA can no longer be trusted to be involved in establishing milk pricing policies for our dairies. We are clearly on an unsustainable path.