

MPC WEEKLY FRIDAY REPORT

DATE: AUGUST 23, 2019
 TO: DIRECTORS & MEMBERS
 FROM: KEVIN ABERNATHY, GENERAL MANAGER
 PAGES: 7



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MPC FRIDAY MARKET UPDATE

| CHICAGO CHEDDAR CHEESE | | | CHICAGO AA BUTTER | | | NON-FAT DRY MILK | | |
|-------------------------------|------------------|----------|-------------------|------------------|----------------|----------------------------|-----------------|------------|
| Blocks | N.C. | \$1.8800 | WEEKLY CHANGE | -\$.1125 | \$2.2275 | WEEK ENDING 08/17/19 | | |
| Barrels | -\$.1000 | \$1.6650 | WEEKLY AVERAGE | -\$.0435 | \$2.2940 | NAT'L PLANTS | \$1.0380 | 19,861,747 |
| WEEKLY AVERAGE CHEDDAR CHEESE | | | DRY WHEY | | | PRIOR WEEK ENDING 08/03/19 | | |
| Blocks | +\$.0165 | \$1.8965 | DAIRY MARKET NEWS | W/E 08/23/19 | \$.3400 | NAT'L PLANTS | \$1.0405 | 15,085,557 |
| Barrels | -\$.0500 | \$1.6940 | NATIONAL PLANTS | W/E 08/17/19 | \$.3676 | | | |

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 |
|-------------------|---|-----------------------|------------------------|-----------------------|
| AUG 23 EST | \$19.49 - \$19.99 | \$17.56 | \$17.59 | \$16.66 |
| AUG 16 EST | \$19.49 - \$19.99 | \$17.55 | \$17.62 | \$16.63 |



Milk, Dairy and Grain Market Commentary

By Sarina Sharp, Daily Dairy Report

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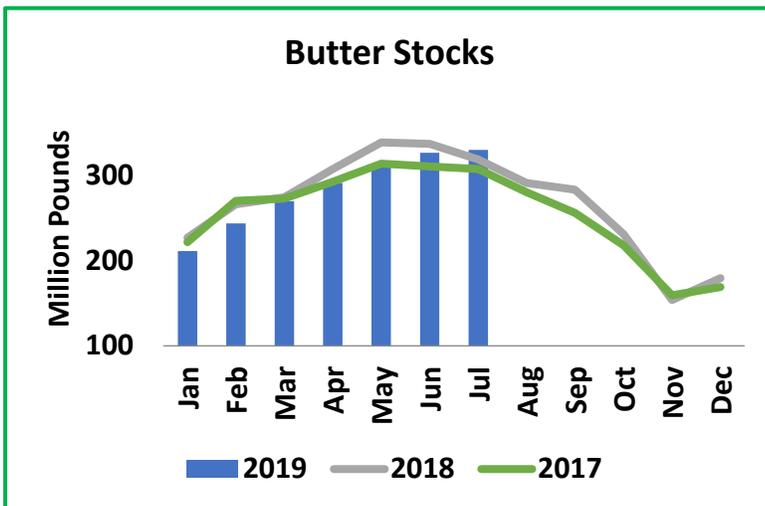
Milk & Dairy Markets

In a series of tweets heard round the world, President Trump lambasted China for stealing America's intellectual property and "ordered" American companies to look for ways to move their foreign operations out of China. According to President Trump, "We don't need China and, frankly, would be far better off without them." The latest fusillade in the trade war pummeled the markets. Stocks, bond yields, and commodities plummeted. The trade war has weakened the dairy markets on multiple fronts, skewering whey values, subjecting U.S. cheese sales to Mexico to one year of stepped-up taxes and introducing the idea that U.S. suppliers may be unreliable, as the rules and transaction costs for overseas buyers could change in an instant. Less directly, the trade war has slowed global commerce and stunted business investment with crippling uncertainty. This has reduced demand for goods of all kinds.

The macroeconomic environment surely pressured the dairy markets this week, and the bulls remained cowed. September Class III futures plunged 63¢, and most Class III contracts lost around 20¢ this week. Class IV futures settled 30¢ to 40¢ lower than last Friday. Skim milk powder (SMP) and butter prices retreated at the Global Dairy Trade (GDT) auction on Tuesday, further weighing on Class IV values.

However, GDT Cheddar rallied and whole milk powder (WMP) posted a surprisingly strong 2.1% increase.

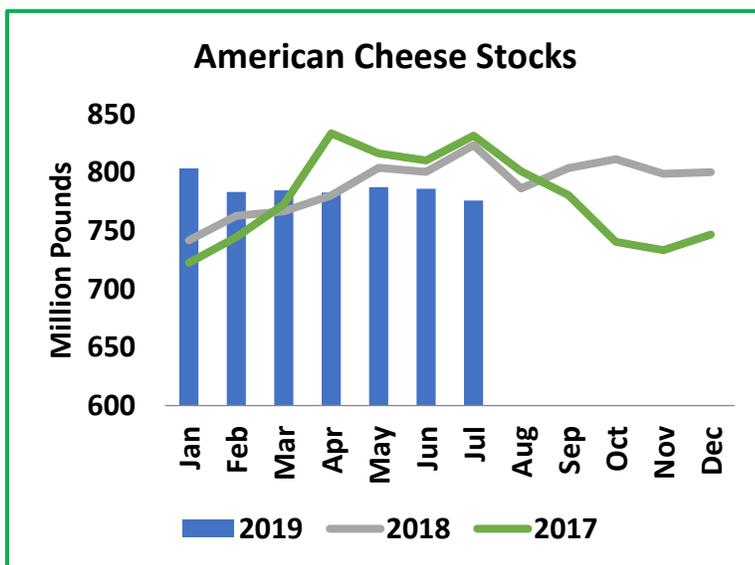
The bad news for butter continued Thursday in the form of USDA's Cold Storage report, which showed a counter-seasonal increase in butter supplies. In a typical year, butter inventories decline 4.5 million pounds in June and another 8.3 million pounds in July. This year, butter inventories grew 12.5 million pounds in June and 3.5 million pounds last month. The summer increase pushed butter stockpiles up to 329.8 million pounds on July 31, 3.6% higher than the prior year. It's likely that cheap imported butterfat has boosted U.S. supplies, and this is finally having an impact on U.S. butter values.



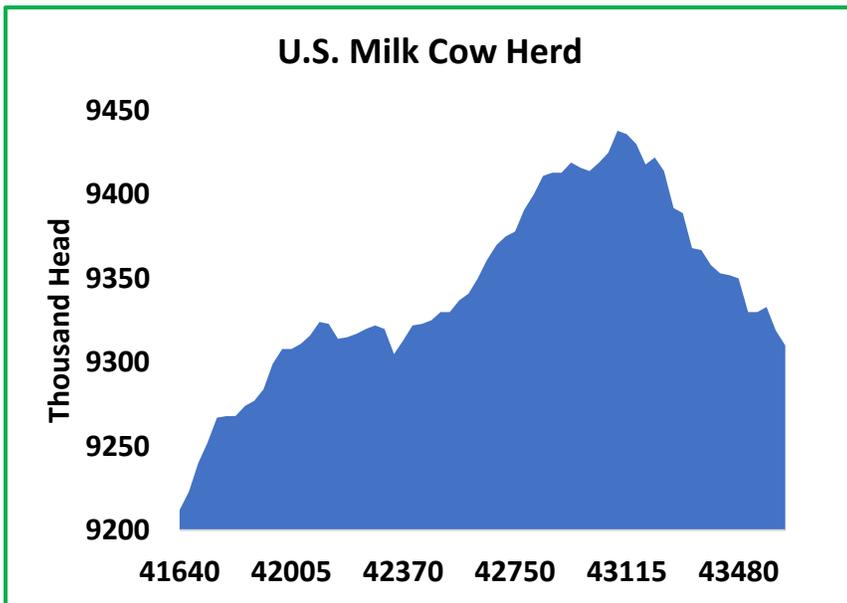
CME spot butter fell to a seven-month low of \$2.2275 per pound, down 11.25¢ from last Friday. A number of butter futures contracts closed a nickel in the red today, at their daily trading limit. End users who were getting anxious about securing product for the holiday baking season now feel that they can afford to be patient.

While bearish for butter, the Cold Storage report was decidedly bullish for cheese. There were 1.36 billion pounds of cheese in inventory on July 31, 3.5% less than at the end of July 2018. Cheese stockpiles typically grow more than 24 million pounds from June to July, but this year they fell 18.3 million pounds, the largest July

drawdown in USDA records dating back to 1915. American cheese stocks fell 10 million pounds last month to 776 million pounds. They are 5.8% lower than inventories in July 2018 and the smallest volume for any month since March 2018. In short, cheese stocks are shrinking when they should be growing, evidence of tighter milk supplies and booming domestic demand. These fundamentals propelled CME spot Cheddar blocks to new multi-year highs at \$1.91 on Tuesday. However, blocks fell back to \$1.88, steady with last Friday. Barrels continued to slip, losing a dime this week and closing at \$1.665, a two-month low.



The other spot markets managed to shrug off the outside pressures. CME spot nonfat dry milk (NDM) climbed 0.75¢ to \$1.0375. Whey powder rallied 3¢ to 39.5¢. This marks spot whey's third straight weekly gain, suggesting that the bad news has been fully priced into whey values.

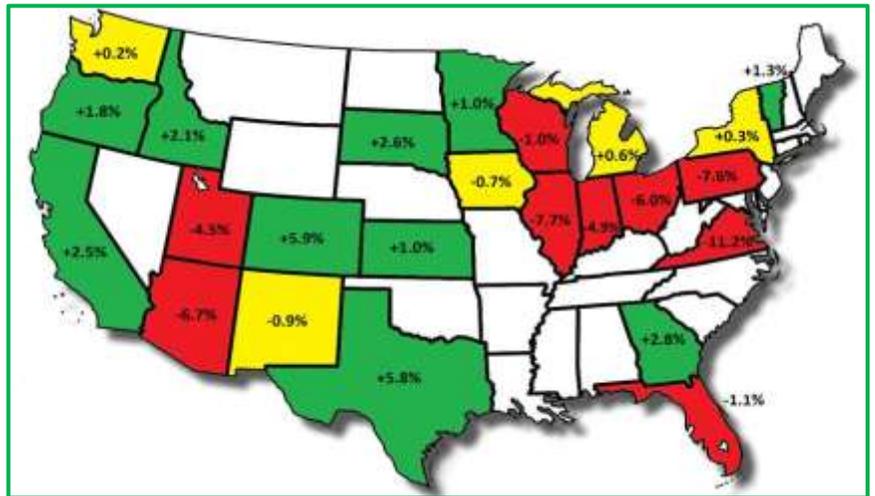


Despite the rough week in the dairy pits, there are reasons to believe that dairy product prices in general and Class III values in particular will soon find their footing. They may not soar, but they will likely remain well supported. Cheese demand is excellent, the whey market is recovering, and milk output is generally steady around the globe. Milk is hovering around \$17 per cwt. That's sufficient to pay the bills but not enough to stimulate much expansion or reassure lenders. Contraction is likely to continue for now, prolonging the potential for adequate milk prices.

In July, U.S. milk output was 18.33 billion pounds, on par with last year. The industry made exactly as much milk with fewer cows, thanks in large part to improved production per cow in the mountain states and California, where summer heat was not as extreme as it was in July 2018.

The dairy herd continues to shrink. USDA revised downward its assessment of the June milk-cow herd by 4,000 head and reported a further 9,000-head decline last month. At 9.31 million head, the U.S. milking herd is smaller than it has been since January 2016 and some 82,000 head smaller than in July 2018. The industry has been decimated in the Midwest and along the East Coast. Compared to the prior

year, there were 35,000 fewer milk cows in Pennsylvania, 14,000 fewer in Ohio, and 9,000 fewer in Virginia. However, in the past year, dairy producers added 27,000 milk cows in Texas and 10,000 in both Idaho and Colorado. Further expansion in the mountain states will likely be limited until new processing capacity comes online late next year. With noticeably fewer cows, growth in U.S. milk output is likely to remain limited in the near term, helping to undergird the markets.



Grain Markets

Grain futures took another sizeable step back this week. Timely rains improved conditions in the field. Reports from crop scouts suggest that, while USDA's August projections may be a bit too high, a dramatic drop in the national average corn yield is unlikely barring an extremely early frost. Soybean pod counts imply considerably lower yields than last season, but stockpiles are large and demand is in question. The soybean market was hit hard by the latest escalation in the trade war, and September futures fell 24¢ this week to \$8.4325 per bushel. September corn futures lost more than a dime and closed at \$3.5975.



Sustainable Groundwater Management Plans Released for Public Comment

By Geoff Vanden Heuvel, Director of Regulatory and Economic Affairs
Geoff@MilkProducers.org

Over the past several weeks, many Central Valley Groundwater Sustainability Agencies (GSAs) have released their proposed Groundwater Sustainability Plans (GSPs) for public comment. These are typically very large documents which contain a tremendous amount of information concerning the known condition of the groundwater in their particular area. The GSPs also make an estimate of how much water can be sustainably extracted over the long term. Many areas are extracting more water out of the ground than is being recharged and GSPs from these areas must contain a suite of projects and management actions that will lead to a sustainable condition by the year 2040.

I have been actively following the progress of GSAs in “Critically Over-Drafted” parts of the Central Valley where there is a dairy presence. Generally, this runs from south of Bakersfield all the way to Stockton with the exception of the Turlock area, which the State has classified as a medium priority sub-basin. The most relevant parts of these plans for the affected farmers is the projects and management actions section. It is in that section where you find out what approach your GSA is going to take, at least in the first five years, to address the overdraft problem.

There are two basic approaches that GSAs are taking. Some GSAs will be allocating water to individual farmers, usually along with the ability to initially use about what is being used today but with a ramp down strategy that will eventually restrict pumping to a sustainable level by 2040. This strategy is coupled with land taxes and extraction fees on pumping that will generate money to fund the development of water supply projects as well as potentially providing money to farmers who voluntarily fallow their ground.

Another approach GSAs are taking is to do projects to bring in more surface water as well as establish voluntary fallowing programs but to NOT establish a specific allocation for each farmer. These GSAs are making a commitment to solving their overdraft problem over the next 20 years but at least initially are not going to be allocating the available groundwater supply to individual farmers. Almost all of these GSAs have, or plan to put in place, a land-based fee and often, in addition, an extraction fee which accomplishes two objectives. One, it raises revenue for the GSA to do the projects they have planned and two, putting a charge on groundwater extraction creates an incentive for farmers who have access to surface water to take the surface water instead of just pumping the groundwater for free.

It is very important for dairymen to know what GSA you are in and to understand what strategy your GSA is taking. Each area has its own unique circumstances, but in my opinion the best early strategy for most GSAs is to avoid giving specific groundwater allocations to individual landowners. Once a GSA allocates water to an individual landowner, it becomes a right that is very difficult to take back. And unfortunately, the allocation the landowner would get would be between 6 and 12 inches per acre, per year, which is not enough to grow a crop. This then creates an immediate need for a water market and the potential for winners and losers in the competition for an inadequate supply. A much less damaging path is to instead implement modest extraction fees on groundwater pumping and have the GSA use that money to reduce the overdraft. To do this you need a way to measure groundwater usage which should be an early action item for every GSA. The use of satellite measurement of crop Evapotranspiration has progressed to a point of commercial viability with amazing accuracy. It can be installed over the entire land surface of a GSA for a very reasonable cost. See presentation [here](#).

Once a measuring system is in place, groundwater extraction fees can be collected, and collective water supply projects can be implemented. I believe substantial progress on reducing the overdraft can be made in the early years with this approach.

Meanwhile, the entire Central Valley needs to pull together to support efforts to improve the delivery capability of the backbone water supply systems. The organized effort to accomplish this part of the strategy has started and is called the San Joaquin Valley Water Blueprint. Milk Producers Council, along with our other dairy industry colleagues, are fully engaged in this effort, which you will be hearing more about in the weeks and months to come.

The Sustainable Groundwater Management Act will change the Central Valley. But continuing to pump groundwater without accountability could not continue. The decisions we collectively make now will have a profound impact on generations to come. Every day I see folks wrestling with what to do and acting in good faith and with energy to try to achieve a sustainable future in the least damaging way possible. I know that there has been lots of skepticism about whether the Central Valley was up to this challenge. I have seen firsthand, enormous effort and good will displayed as all of our communities have wrestled with this huge problem. In the end, despite all the work that has been accomplished to date, there is going to need to be a significant investment from the State and Federal governments in water infrastructure improvements. And to accomplish that, we are going to need to work in collaboration and partnership with our community neighbors, who will also be profoundly impacted by this law. Are we up to the task? I would say: So far, so good.

If you have any questions or comments, feel free to contact me at Geoff@MilkProducers.org.

Cows and Climate Video Series

Courtesy of Dairy Cares

Milk Producers Council has been a longstanding member of Dairy Cares, a coalition of dairy trade groups, cooperatives, processors, and allied industry members working together on industry sustainability issues. The below video published by Dairy Cares details how California is leading the industry in climate sustainability.



From Dairy Cares

Dr. Frank Mitloehner (@GHGGuru) puts greenhouse gases from livestock into perspective, in this introductory video. The Cows and Climate series aims to explain livestock's role in the global food system and our environment, focusing on climate change, and promoting collaborative and research-based solutions that can further reduce emissions. Dr. Mitloehner's participation in the Cows and

Climate video series is a part of his research and extension activities at the University of California, Division of Agriculture and Natural Resources.

This is the second video in an on-going series. Watch the full video [here](#).

August 27 Field Tour: Subsurface Drip Irrigation Using Dairy Manure

Courtesy of Sustainable Conservation



Sustainable Conservation welcomes you to join a field day to learn about subsurface drip irrigation systems utilizing dairy lagoon water. Visit and hear from dairy owners about why they're using manure-drip irrigation on forage crops.

- Tour the subsurface drip irrigation system
- Learn about how the system works and its results
- Hear from dairy producers directly about their experiences
- Ask questions



The group will meet at Willow Ranch Restaurant, 27770 Lagoon Dr., Buttonwillow, CA 93206 at 10 a.m. on August 27th.

To RSVP, contact John Cardoza at jcardoza@suscon.org or 209.576.7731.

On Her Farm With Allison Kasbergen

Courtesy of Tastemade



From Kevin Abernathy, General Manager

MPC Chairman Cornell Kasbergen and his family were recently featured in the #AllTogetherBetter video produced by the food website Tastemade. Check out the video below.

From Tastemade

As a member of Land O'Lakes farmer-owned co-op, dairy farm Rancho Teresita strives to change the dairy industry. How? By focusing on sustainability efforts to better traditional farming practices for future generations to come. Watch the full video [here](#).

PG&E Bailout Bonds Pass Costs to Ratepayers

Courtesy of Agricultural Energy Consumers Association



PG&E claims that shareholders will pay for their risky bailout bonds scheme. Nothing could be further from the truth. After all, why should anyone believe a convicted felon who has a reputation for falsifying information to the CPUC and rap sheet for obstruction of justice. PG&E is also facing potential criminal charges in the Paradise fire that killed eighty-six residents and left tens-of-thousands more homeless. Customer groups agree that ratepayers, not

shareholders, will end up footing the bill for the mountains of debt PG&E's shareholders want to add to their balance sheet.

While they are hoodwinking legislators, PG&E and their shareholders are simultaneously seeking massive rate increases at the CPUC, greatly increasing their profits so ratepayers end up footing the bill. In addition to a 20-50 percent increase in its Return on Equity (ROE), the utility is also actively seeking a \$2 billion increase in annual revenue. The ROE increase alone will cost ratepayers \$500 million a year or more. Their general rate increase will add another \$1 billion in 2020, \$1.5 billion in 2021 and \$2 billion every year thereafter, further increasing their earnings. That's a whopping \$30 billion in higher rates over the next decade, increasing profits more than enough to offset any bond expenses they may incur.

Clearly, by increasing PG&E's earnings and profits, customers, not shareholders, end up picking up the tab.

Say NO to PG&E hedge fund investors
Say NO to PG&E bailout bonds

