Milk Producers Council

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DATE: April 13, 2018 **PAGES: 5**
TO: Directors & Members **FROM: Kevin Abernathy, General Manager**

MPC Friday Market Update

CHICAGO CHEDDAR CHEESE		
Blocks	*+ $.0025*	$1.6050
Barrels	*+ $.0100*	$1.4600
Weekly Average, Cheddar Cheese		
Blocks	*+ $.0630*	$1.6215
Barrels	*+ $.0230*	$1.4705

CHICAGO AA BUTTER		
Weekly Change	*No Change*	$2.2875
Weekly Average	*+ $.0355*	$2.3095
DRY WHEY		
Dairy Market News	w/e 04/13/18	$.2638
National Plants	w/e 04/07/18	$.2548

NON-FAT DRY MILK		
Week Ending 4/6 & 4/7		
Calif. Plants	$0.6894	16,491,606
Nat'l Plants	$0.6962	17,717,544
Prior Week Ending 3/30 & 3/31		
Calif. Plants	*$0.7103*	*13,104,302*
Nat'l Plants	*$0.6926*	*18,873,523*

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Fred Douma's price projections…

April 13 Est:	**Quota cwt. $15.27**	**Overbase cwt. $13.58**	**Cls. 4a cwt. $13.26**	**Cls. 4b cwt. $14.21**
Last Week:	**Quota cwt. $15.26**	**Overbase cwt. $13.56**	**Cls. 4a cwt. $13.27**	**Cls. 4b cwt. $14.16**

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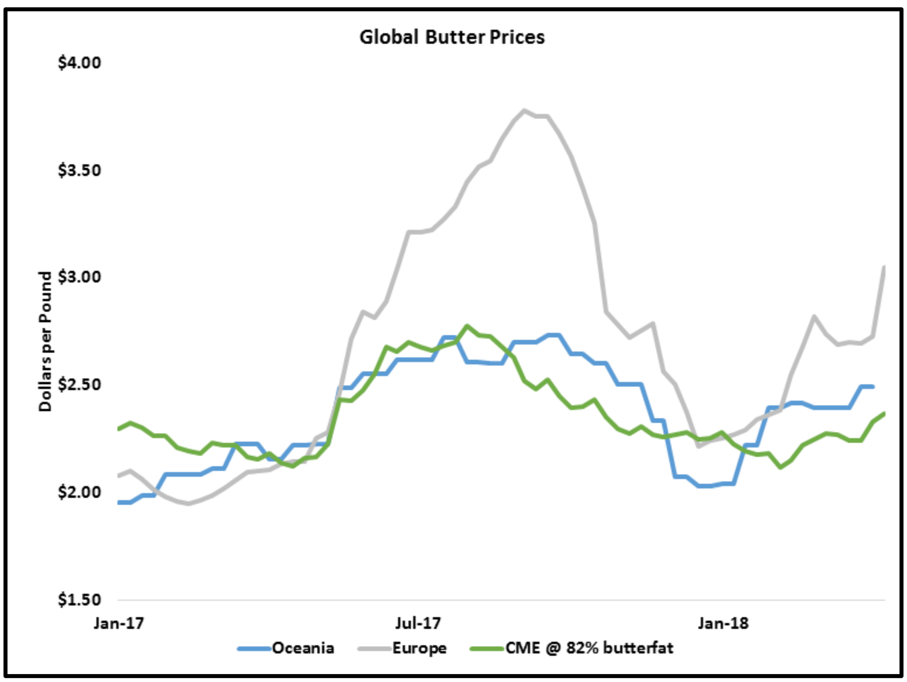
Market commentary

By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com

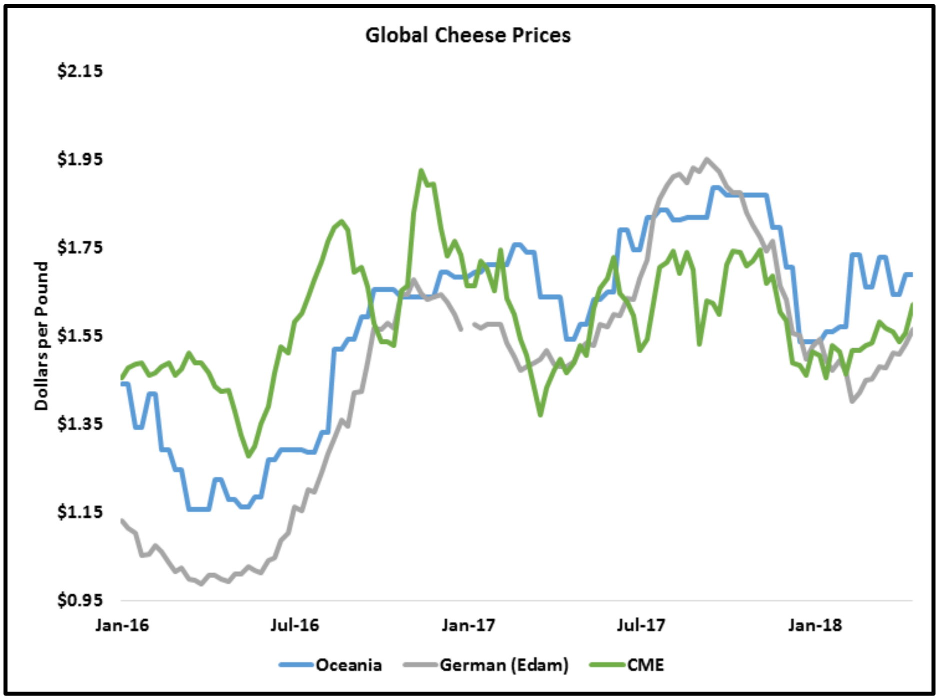
Milk & Dairy Markets

European dairy demand is brisk and prices are climbing. The rally in the European butter market gained momentum this week, and prices stand at their highest level since October. The German butter market is roughly $3 per pound. "Higher prices do not seem to be crimping sales" according to *Dairy Market News*, and butter makers are fielding inquiries from buyers both foreign and domestic. Europe boosted butter exports by 36% in January, thanks to stronger demand from the U.S. and the Middle East.



European cheese prices are higher, and cheese manufacturers are reportedly struggling to keep up with orders. "Cheese is being made with confidence that there are eager customers," according to *Dairy Market News*. Prices are rising in Oceania as well.

With a boost from abroad, the U.S. dairy markets perked up again this week. CME spot butter came charging out of the gate on Monday, prompting the August futures contract to close a nickel higher Monday. A number of other futures contracts traded near the upper daily trading limit. By Friday, the spot market slipped back and finished unchanged at $2.2875 per pound. The futures managed to hold to modest gains. U.S. butter is a bargain, and global buyers seem to have noticed.

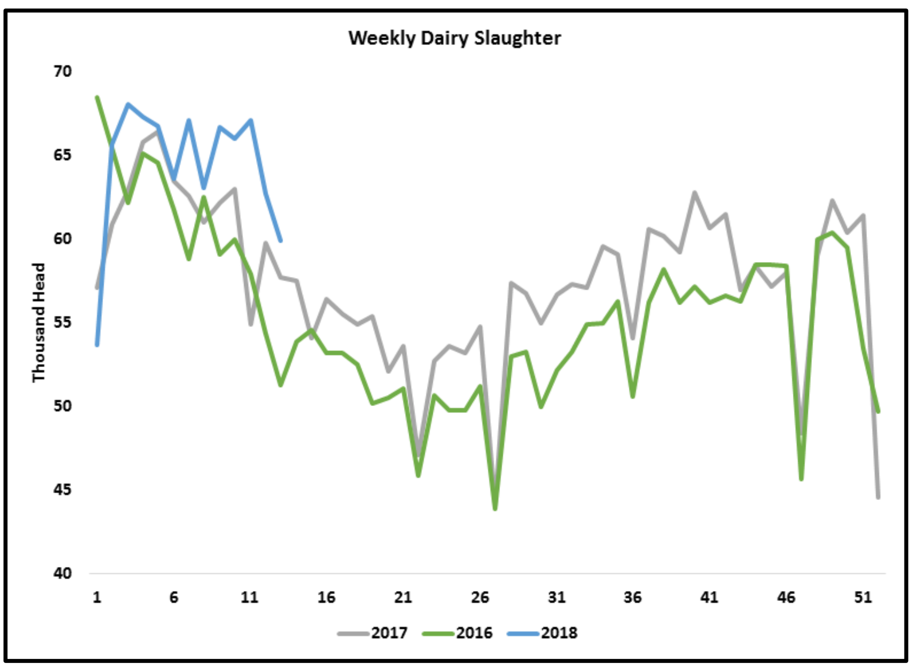


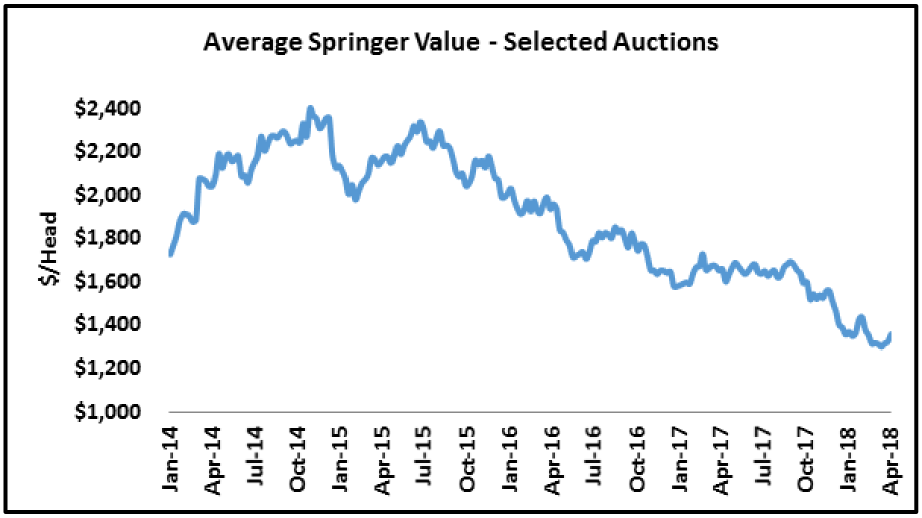
The CME spot cheese markets put in a similar performance, with a strong start and a weak finish. Still, spot Cheddar blocks closed at $1.605, up 0.25¢ to the highest price since November. Barrels closed a penny higher at $1.46. Despite a selloff in the spot block market today, cheese and Class III futures settled higher. This resilience is bullish and suggests that demand may be outpacing supply despite the spring flush and the typical post-Easter lull. Nearby Class III futures were unchanged from last week, while June through December futures traded 5¢ to 13¢ higher than last Friday. Most contracts are 30¢ to 50¢ higher than where they stood five weeks ago.

CME spot dry whey took a step back to 30.5¢, down 1.5¢ from last Friday. Given strong milkflows and heavy cheese output, whey production is robust. Whey represents an inexpensive source of protein, and demand is respectable, but stocks are heavy.

Spot nonfat dry milk (NDM) added a half-cent this week, reaching 73.25¢. The world is awash in milk powder, so here too the rising market hints at better demand. Strength in milk powder pricing and mostly higher butter futures allowed Class IV futures to post sizeable gains this week. Most contracts settled 20¢ to 50¢ higher than last Friday. Compared to early March, May through December futures are generally 40¢ to 70¢ higher.

Better prices are coming too late to help some dairy producers. There are herds for sale throughout the Northeast and the Lake States. *Dairy Market News* reports that "a number of farms closing this month are more sizeable than the average Midwestern farm." Planting season – along with extra labor and expenses – is fast approaching. Lenders are taking a cautious approach as they weigh their commitments to dairy producers with strained finances. Meanwhile, slaughter volumes remain high. For the week ending March 31, which included Good Friday, dairy cow slaughter was 59,933 head, up 3.8% from the same week a year ago. Over the past six weeks, dairy cow slaughter has





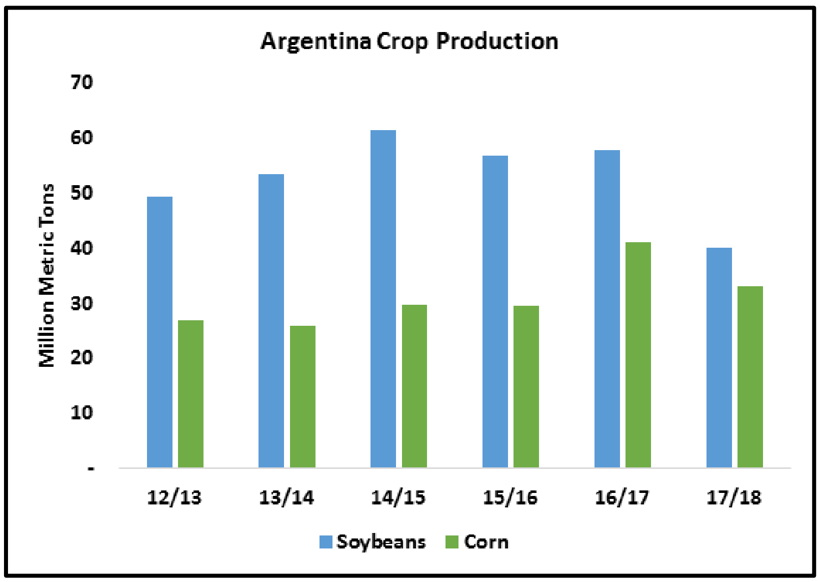
been 7.5% higher than during the same period in 2017.

There are plenty of heifers, so it is possible for U.S. dairy producers to grow their herds even with high cull rates. However, springer values are sliding, suggesting there is little appetite for such growth. Limited processing capacity and the poor basis that accompanies an oversupplied market will also restrain expansion in most of the major dairy regions.

Although dairy cow numbers continued to climb in January and February, there are a number of factors that portend slower growth in U.S. milk production – if not outright contraction – in the months to come. Given improving demand, slower growth will likely be enough to lift dairy product prices. Indeed, it seems that the rally is already underway. However, the road to recovery could be rocky and fraught with unexpected twists, particularly in light of heavy cheese, whey, and milk powder inventories.

Grain Markets

It was another exciting week in the soy complex. May soybeans settled at $10.545 per bushel, up 20.5¢ from last Friday to a five-week high. In contrast, May soybean meal futures closed at $382.80, down $3.80 for the week. On Tuesday USDA lowered its estimate of Argentine soybean production 40 million metric tons, a decline of seven million metric tons from their March estimate. The market had already anticipated a sizeable decline in the Argentine soybean crop, so the change had little impact on the markets. USDA also made minor changes to its U.S. soybean supply and demand, resulting in a five million bushel decline in end-of-season soybean stocks.



This week Argentina purchased 240,000 metric tons of U.S. soybeans for delivery in the 2018-19 crop year. These mark the largest U.S. soybean export commitments to Argentina in 20 years, and the U.S. Soybean Export Council expects more will follow. Prospects for U.S. soybean exports are strong, putting pressure on crop yields in the upcoming season. If the weather does not cooperate, soybean and soybean meal futures will likely head higher.

The corn market was relatively quiet, moving a penny or two every day. May corn futures closed at $3.8625 per bushel, down 2.5¢ from last Friday. USDA lowered its domestic corn demand estimates, boosting its end-of-season stocks projection by 55 million bushels. There is plenty of grain in the world today, but the winter wheat crop is in terrible condition, and demand for grain is likely to rise as China ramps up its ethanol program in the coming years. Nearby corn futures have had a hard time breaching the $4 mark, but they aren't likely to head back down to $3.50.

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USDA hosts public meeting on Proposed California Federal Milk Marketing Order

By Geoff Vanden Heuvel, MPC Board Member and Economics Consultant

On Tuesday, April 10 in Clovis, California, USDA officials held a public meeting to explain to the industry the features of the Proposed California Federal Milk Marketing Order (FMMO). Video of the public meeting is available here (audio begins at minute mark 25:00). FMMO materials related to producers, handlers and the referendum process were distributed at the meeting and are available here.

USDA Dairy Program Deputy Administrator Dana Coale addresses dairy farmers, processors and allied industry members at a public meeting in Clovis, California about the Proposed California Federal Milk Marketing Order.

USDA Dairy Program Deputy Administrator Dana Coale stressed that while she understood the inclination to focus on a number, what producers really needed to consider is that the decision before us is about whether to go to a new *system* of milk regulation.

The FMMO system is significantly different from the familiar California state system. While the state system enforces the regulated minimum prices on ALL grade A milk produced and marketed in California, the FMMO system only price regulates pooled grade A milk, and the only milk that *must* be pooled is Class 1 milk. This fact can be challenging for California producers to comprehend. The mandatory nature of our current system is something that we have supported for decades because of our perception that if the government did not enforce a minimum price, then processors would not pay us that price.

This perception is the result of decades of living in an industry with a surplus milk mentality. Our historical experience in the California dairy industry is always having too much milk and therefore having concerns about where we would ship our milk, and how much we would be paid for it. Our answer was to have the state government strictly regulate the marketplace. The result of that was a state government policy that took a very conservative view on how much they could stress the processing sector with minimum price requirements since they were using the power of the government to require the processors to pay that minimum price. For many years, the state set prices at levels that would allow even the least efficient manufacturing plants to make money because we needed the plant capacity to process the growing milk supply.

Milk in California is a valuable commodity, not just a chronically surplus by-product of dairy farming. The FMMO system sets up the dynamics for processors to compete for a milk supply in a way that the tightly regulated current state order never could.

The FMMO system has an entirely different approach. Its primary function is to make sure that the Class 1 needs of the market are met. It regulates manufacturing plants only to the extent that they can demonstrate some connection to the Class 1 market. If those manufacturing plants meet the criteria spelled out in the FMMO regulations for connection to the Class 1 market, which in the California FMMO means they need to divert 10% of their supply to a Class 1 distributer, they can share through the pool in the added revenue that comes from the Class 1 market. If they seek to do that, then they are regulated and must pay the regulated price.

So why would they do that? In a word, competition. Milk in California is a valuable commodity, not just a chronically surplus by-product of dairy farming. The FMMO system sets up the dynamics for processors to compete for a milk supply in a way that the tightly regulated current state order never could.

The much less regulated FMMO system creates opportunities for innovation and competition, but with that also comes the risk that some will do better than others. The reason most people think milk prices in California will be higher under a FMMO is because the regulated prices for the various classes of milk, even though not enforced on non-pooled milk, become the benchmark prices that producers compare against when selling their milk. Once the lower state order prices are no longer in effect in the marketplace, the higher FMMO prices become the standard starting point for contracts with milk processors.

This has been the 80-year experience of our colleagues in the other FMMOs in the country. Yes, milk can and does get sold under class in the FMMO system, but typically only during surplus periods and only on that surplus volume. Compare this to our state system, where ALL the milk gets discounted, ALL the time, so that no milk gets discounted when surplus occurs.

Dairy industry members learn about the recently released California Federal Milk Marketing Order, which producers will consider for adoption by a May 5, 2018 vote.

So, this is question on the table: Is the risk worth the reward? California producers are at a point where we need more money from our processors. It is clear our state system will not use the power of the government to mandate that our processors pay us more. The FMMO will set higher prices, but it will not force all processors to pay it to us. It will be up to us, working through our cooperatives, to negotiate those higher prices from our buyers. Our fellow producers and their cooperatives have successfully accomplished this everywhere else in the country, so it seems reasonable we should be able to do it here in California as well. Therefore, from my perspective, voting for a California FMMO does not seem like an unreasonable leap of faith.

Over the next couple of weeks, the cooperatives and others will be having meetings to provide more details about the mechanics of the FMMO plan and the economic modeling work prepared by the various economists who have looked at this issue. I will do my best to share what I learn along with you in this space. We have until May 5, 2018 to get our ballots mailed to USDA. If you are a member of a cooperative that has chosen to block vote, your cooperative board members need to finalize their vote before May 5 as well.

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Water Fix gets financed

By Geoff Vanden Heuvel, MPC Board Member and Economics Consultant

On Tuesday, April 10, the Metropolitan Water District (MWD) of Southern California Board of Directors voted to provide the extra financing needed to build both tunnels proposed by Governor Brown. Officially known as the California Water Fix, the *Sacramento Bee* does a good job of explaining this issue in a recent article titled "Southern California water agency backs 2 Delta tunnels in breakthrough vote." Read the article here.

In the future I will be writing more about the California water situation and its impact on the dairy industry. But, for now the vote by MWD is a very significant development in a story that stretches back decades.

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