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DATE: September 7, 2012 **PAGES: 5**
TO: Directors & Members **FROM: John Kaczor**

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE		
Blocks	*+$.0100*	$1.8300
Barrels	*- $.0025*	$1.7750
Weekly Average, Cheddar Cheese		
Blocks	*- $.0230*	$1.8275
Barrels	*- $.0232*	$1.7763

CHICAGO AA BUTTER		
Weekly Change	*+$.0250*	$1.8650
Weekly Average	*+$.0378*	$1.8663
DRY WHEY		
Dairy Market News	w/e 09/07/12	$.5850
National Plants	w/e 09/01/12	$.5597

NON-FAT DRY MILK		
Week Ending 8/31 & 9/1		
Calif. Plants	$1.2647	8,700,856
Nat'l Plants	$1.3263	13,326,460
Prior Week Ending 8/24 & 8/25		
Calif. Plants	*$1.2571*	*8,773,562*
Nat'l Plants	*$1.2955*	*15,725,977*

CHEESE MARKET COMMENTS: A little less cheese trading activity this week and prices were mixed. Blocks continued to move upward, ending with a penny per lb increase; barrels lost a quarter cent. Nine of the eleven block trades occurred on Thursday, rising to $1.855 per lb before ending at $1.84. Two more sales on Friday trimmed another penny per lb from the small weekly gain. The trading and price spread between blocks and barrels suggests a real or perceived over supply of barrel cheese, but not something likely to cause precipitous change to the overall strength of the market. One more week's comments on U.S. crop conditions did not add much to clear away last week's uncertainty about future milk supplies and product price levels. Domestic demand is steady to slightly higher, led by improving sales of Mozzarella, and affected by concerns about future market conditions. Export demand is light to moderate, as higher U.S. prices are said to be affecting buyers' interests. CWT assistance continues to help their members' ability to obtain orders for shipments through the end of this year. *Dairy Market News* says milk supplies in the East are tight, affecting cheese plants' wishes to increase their output, but supplies are adequate elsewhere. Class III futures prices this week averaged $.44 per cwt lower over the October-March period. November is highest, at $19.67 per cwt; all prices through January remain above the $19.00 level. Cheddar cheese futures also were uniformly lower this week, losing an average of $.022 per lb through next March; all prices through January remain above the $1.90 per lb level.

BUTTER MARKET COMMENTS: Butter prices this week rose again, this time by $.025 per lb. Eleven carloads traded this shortened holiday week. A bid and an offer on Tuesday moved the price up by $.02 per lb and 8 of the 9 Friday trades were at the week's high, $1.87 per lb, and the last one was $.005 lower. The activity ended with an unfilled bid slightly below the last trade price and two uncovered offers slightly above. *DMN*'s market comment this week focused on the steady sales, typical for this time of year, aided by increased retail sales, supported by good ad offerings, offsetting the slower sales to food service buyers who served vacation related businesses. Production ticked upward this week, with a little more milk and cream available from bottling plants and ice cream operations, allowing some butter plants to store some of what was produced. CME butter futures this week were essentially unchanged: four of the months through next April were unchanged while the three that changed averaged $.003 per lb lower. All prices through next September are above the $1.80 per lb level, reflecting strong belief that butterfat is and should remain in relatively tight supply for some time to come.

POWDER MARKET COMMENTS: This week's report on July dairy product production also updated month ending stocks of nonfat dry milk. U.S. stocks fell by 14.9 million lbs during July (June's stocks were 71 million lbs lower than May's). California production was 18.7 million lbs lower than in June, accounting for all but 0.8 million lbs of the total U.S. production change for the month. U.S. production of skim milk powder increased by 11.9 million lbs, virtually all of which is believed to have been produced in California for export. Shipments of nonfat dry milk in June exceeded June's production by 62 million lbs. Production of both nonfat powders is expected to continue to decline for the next several months, pointing to continuing inventory declines, which should fall below the 100 million lb level by September. *DMN* reports NFDM spot prices this week ranging from $1.32-$1.65 per lb in the West and $1.39-$1.62 in the central/eastern region. Weighted average prices reported for shipments last week are $1.326 to AMS, the "national" price, and $1.265 for California plants. See the recaps under the letterhead above. The market is firm. Those buyers who were expecting a correction appear to have guessed wrong and are now searching for loads needed for their operations. SMP prices on the global auction this week continued their amazing climb. Dairy America limited their offerings this week to shipments only for October, and the winning price was as much as $.34 higher (at $1.664 per lb) than winning prices bid for their product in August for October shipments. Arla Foods' SMP for November shipments was bid up to $1.57 per lb which was $.154 higher than the winning prices bid for Fonterra's like products for that month. [It should be noted, based upon data through June 5th, which is the latest report available, the combined volume of SMP offered by AF and DA in the global auction looks to total no more than 2.5 million lbs per auction, about one-tenths that offered by Fonterra, but still….]

WHEY PRODUCTS MARKET COMMENTS: Manufacturers of dry whey are presently in a good position. Domestic demand appears to be steady to firm, and running just a little higher than current production. Export demand continues to be strong. *DMN* reports prices rose in all regions this week as current supplies continue to go first to contracted buyers and then, occasionally, to others. The re-sale market is active and selling for prices above the reported ranges. Production varies by region depending, as always, first on cheese plant outputs then on how much is used for condensed whey and for higher concentrated products. Stocks are reported to be "comfortable" or "in balance." Production of dry whey in July was 7.1 million lbs higher than in June and stocks fell by 4.4 million lbs. Production of whey protein concentrates was 4.6 million lbs lower and stocks were only marginally higher. *DMN* says WPC-34 prices are mostly higher, in a "firming market." However, the low end of the "mostly" price range continues to lag well lower (by $.18 to $.25 per lb) than the low ends of the price ranges for WPC's major alternate product with comparable components, NFDM. CME dry whey futures prices this week increased strongly over the next seven months, averaging $.041 per lb higher than last week. The high price through next April is December's $.626 per lb, up $.047 per lb.

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FRED DOUMA'S PRICE PROJECTIONS…

Sep 7 Est:	**Quota cwt. $18.10**	**Overbase cwt. $16.41**	**Cls. 4a cwt. $16.34**	**Cls. 4b cwt. $16.99**
Last Week:	**Quota cwt. $18.02**	**Overbase cwt. $16.32**	**Cls. 4a cwt. $16.17**	**Cls. 4b cwt. $16.92**

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CONGRESS RETURNING TO WORK NEXT WEEK…TIME TO PASS THE FARM BILL!: *(By Rob Vandenheuvel)* After spending the last five weeks back in their districts, the House of Representatives is returning to Washington, DC next Monday, with a major piece of legislation awaiting their action: the 2012 Farm Bill.

The Farm Bill is a comprehensive package of agriculture and nutrition policy proposals for the next five years. The U.S. Senate has already approved their version of the bill, and the House Agriculture Committee has approved their version. **The next step in the process is for the full House of Representatives to vote on the House Ag Committee's version of the bill.** Included in both the House and Senate bills is a package of reforms to the U.S. dairy safety net policies. Both bills would eliminate the Milk Income Loss Contract (MILC) and the Dairy Product Price Support (DPPSP) programs. Both bills would put in their place a two pronged safety net program for U.S. dairy farmers. Those two parts of the proposal are the Dairy Producer Margin Protection Program (DPMPP) and the Dairy Market Stabilization Program (DMSP).

The DPMPP is a voluntary "margin protection" program that dairies can sign up for. It provides direct cash payments to dairymen during periods of time when on-the-farm margins are severely compressed or negative. The DMSP is a program that provides a direct incentive for dairies to temporarily cut back milk production when those on-the-farm margins reach severely compressed or negative levels. However, it should be noted that the DMSP ***only applies to dairies that decide to sign up for the government funded and subsidized DPMPP***.

This newsletter has devoted a significant amount of space to why this two pronged approach to Federal dairy policy is a vast improvement over the current policies that apply to our industry. We've written numerous pieces on why MPC and other dairy organizations around the country are so supportive of implementing this well-thought-out and wise policy.

With the U.S. House of Representatives coming back to Washington, DC to hopefully take up their version of the 2012 Farm Bill, it's important that dairy farmers know how our current situation might be different if this policy were in place.

The DMSP is a completely new approach to empowering the dairy producer sector to collectively take the steps necessary to bring milk production into better balance with demand. It represents a rational and quick-acting method of correcting an oversupply of milk, as opposed to our current methods of supply corrections that include "hoping that the heat or the drought will reduce production" or "hoping that my neighbor will go out of business so that our national production will be reduced." ***(Isn't it a pathetic statement for our industry that these are the main "tools" we have to bring about milk supply corrections??)*** However, while the DMSP is a valuable tool that is a critical part of the 2012 Farm Bill, for the purposes of this article, I'm going to focus only on the DPMPP.

As a reminder, the DPMPP provides two levels of margin protection:

- A government-funded **"basic program"** that makes direct payments to enrolled dairy farmers when the national "milk-price-minus-feed-cost" margins calculated in the program drop below $4.00 per hundredweight.
- A partially-subsidized **"supplemental program"** that allows dairies to customize their margin protection. This program includes a premium paid by the dairymen, but provides direct payments when "milk-price-minus-feed-cost" margins calculated in the program drop below a customized trigger (such as $5.00 per hundredweight or $6.00 per hundredweight, etc.)

Looking at the margin calculations in both the House and Senate Farm Bills (they have identical margin calculations), direct payments would have been made under the "basic program" for the months of May, June, July and August. For an average California dairy, milking 1,000 cows producing 65 pounds of milk per cow per day, those payments would have equaled $51,867 for those four months.

If that same 1,000-cow dairy had decided to enroll in the "supplemental program" and opted to provide margin protection up to $6.00 per hundredweight, the dairy would have had to pay an annual premium of $29,496 (in the House version of the bill) or $27,829 (in the Senate version of the bill). In return, both versions of the Farm Bill would have generated direct payments for the months of March, April, May, June, July and August. **Collectively that average 1,000-cow California dairy would have received <u>direct payments totaling $230,096 during those six months</u> (an average of $2.22 per hundredweight).** *(How does that compare to the MILC payments your dairy received earlier this year…the payments that a 1,000 cow dairy "exhausted" in only 1 ½ months?)*

Clearly, the dairy reforms in the current House and Senate versions of the 2012 Farm Bill represent a **huge improvement** for California's dairies. It not only does a better job of protecting the margins of our dairy farmers *(without discriminating against dairies due to size)*, but it also gives us a valuable tool (the DMSP) to help restore supply/demand balance. **MPC is proud to stand side-by-side with organizations like Dairy Farmers of America and Land O'Lakes, who also represent many California dairy families, in supporting this much needed reforms.**

We are urging all California dairy families to get active as the House of Representatives comes back into legislative session. **<u>Please pick up the phone ASAP and call your Congressman's office.</u>** Ask them to urge their House leadership to bring this much-needed reform to the House floor for a vote. The House of Representatives has scheduled only 8 more legislative "work days" before the current 2008 Farm Bill expires, **<u>so time is of the essence</u>**!

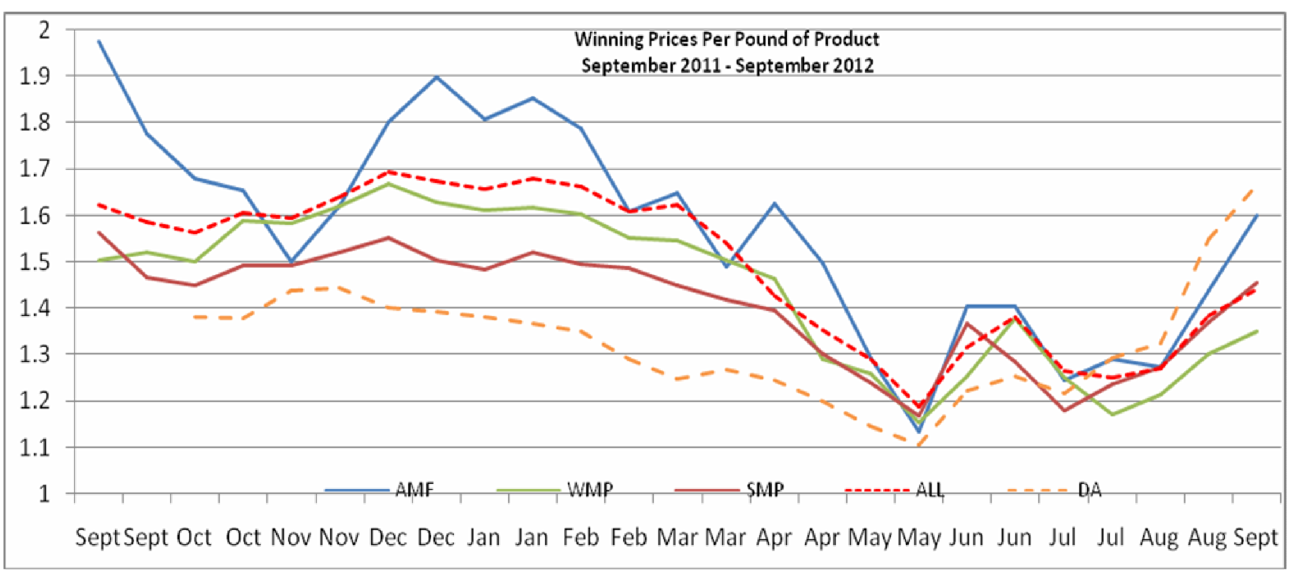
Contact information for your Congressman's office can be found at www.house.gov, but for starters, here is the contact information for some of the California Congressmen who represent our dairies:

- **Wally Herger (Orland):** (202) 225-3076
- **Jerry McNerney (Escalon/Lodi/Tracy):** (202) 225-1947
- **Jeff Denham (Madera/Chowchilla/Kerman):** (202) 225-4540
- **Jim Costa (Fresno/Hanford/Bakersfield):** (202) 225-3341
- **Devin Nunes (Tulare/Visalia):** (202) 225-2523
- **Kevin McCarthy (Bakersfield):** (202) 225-2915
- **Joe Baca (Ontario):** (202) 225-6161
- **Gary Miller (Chino):** (202) 225-3201
- **Ken Calvert (Corona):** (202) 225-1986
- **Jerry Lewis (Redlands):** (202) 225-5861
- **Mary Bono-Mack (Moreno Valley):** (202) 225-5331

The message to your Congressman is simple: **"We need the House of Representatives to pass their version of the Farm Bill now."** If you have any questions, please don't hesitate to give MPC a call at (909) 628-6018.

RECORDS ARE SET FOR VOLUME, BIDDERS, AND WINNERS IN THIS WEEK'S GLOBAL AUCTION: *(by J. Kaczor)* If three in a row makes a trend, the price trend for global auction prices is pointing upward. The summary of this week's auction reported 717 qualified bidders, 203 of which entered volumes, with 143 of them ending up with winning bids. The auction covered delivery periods ranging from October through March. The average winning price for all products to be delivered over the six months was $1.440 per lb, $.059 per lb higher than the winning price in the auction held two weeks ago, $.171 per lb higher than one month ago, and $.19 per lb higher than the most recent low point that was reached in mid-July. The volume reported sold in this auction was 129.6 million lbs, a record high. A year ago, 97 million lbs of product was sold in the first September auction. For a second time in a row, prices for all product categories were higher than the previous bidding.

The chart below shows the changes in winning prices for the three major product categories in the auction for the past thirteen months, along with the weighted average winning price for all products. It also separately shows the estimated winning prices for Dairy America's skim milk powder, which are included in the "all product" and the skim milk product categories, and therefore has some effect on the level of those two categories. The all product indicator reflects prices for the following additional products which are not included in the chart: Fonterra's buttermilk powder (occasionally), rennet casein and milk protein concentrate-70 (from May, 2011), and cheddar cheese (from July, 2011); Arla Foods' skim milk powder and Murray Goulburn's lactose were added in April 2012.



The all product category currently reflects 127.8 million lbs of Fonterra's products, including 118.2 million lbs of AMF, WMP, and SMP, and is believed to represent somewhere between 30% and 40% of Fonterra's production. While there is no way to determine the full effect of these prices on the price Fonterra ultimately pays its member and non-member suppliers, they are given what reads like high importance in Fonterra's comments about current and future prices and payouts.

The chart shows how much higher Dairy America's SMP was bid ($1.664 per lb) compared to all SMP, but DA offered it only in contract #1 for delivery in October. The maximum volume DA has been offering in contract #1 was about 1.1 million lbs so it is hard to place too much credence on this particular result. The winning price for Arla foods' SMP for contract #2 (November delivery) was $1.57 per lb; the estimated average price for Fonterra's SMP for contracts 2, 3, 4, and 5 was $1.44 per lb. That is one of the odd things about this auction, and, as noted, may be partly but likely not completely explained by the lower volumes offered by DA and AF.

The second oddity is the continuing "imbalance" between Fonterra's SMP and WMP, which has widened to an estimated $.09 per lb. That has happened in the past, but only for brief periods; perhaps bidders foresee a surplus developing down there with milk production expected to rise by about 5% this year over last year's record output while China and other Asian nations (recently identified by Fonterra as their prime sales territory) face slowing economic growth. A surplus of a major dairy powder sold by Fonterra does not seem likely, considering Fonterra's deft ability to switch milk flows from one product to another in a seamless manner without affecting overall efficiency.

The question about future price movements has been at least tentatively been answered by Fonterra's CEO this week. Three weeks ago he said "forecasting anticipates some recovery in global dairy prices but we don't know how strong the recovery will be or when it will kick in." This week he noted the third straight increase in the GDT auction prices, and mentioned the poor weather in Europe, the monsoon season in India, and the drought in the U.S. as "not so favorable" milk production conditions in those regions this year compared to last year. He said he believes the low prices in May and June were over-reactions to sudden supply surplus and weakening demand. So, let the recovery continue, and let it be led by SMP, AMF, and cheese demand.

MONTHLY MPC BOARD MEETING TO BE HELD NEXT TUESDAY: *(By Rob Vandenheuvel)* MPC's monthly board meeting will be held next Tuesday (September 11th). This month's meeting will be held in Bakersfield, CA, in the board room of the Kern County Farm Bureau (801 S. Mount Vernon Avenue, Bakersfield). The meeting will start at 11 am. **All current and prospective MPC members and associate members are welcome to attend.** If you plan to attend, please RSVP by calling (909) 628-6018.