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DATE: March 3, 2017 **PAGES: 4**
TO: Directors & Members **FROM: Kevin Abernathy, General Manager**

MPC FRIDAY MARKET UPDATE

CHICAGO CHEDDAR CHEESE		
Blocks	*- $.0950*	$1.4800
Barrels	*- $.0800*	$1.4375
Weekly Average, Cheddar Cheese		
Blocks	*- $.0366*	$1.5065
Barrels	*- $.0809*	$1.4760

CHICAGO AA BUTTER		
Weekly Change	*+ $.0352*	$2.1625
Weekly Average	*+ $.0501*	$2.1795
DRY WHEY		
Dairy Market News	w/e 03/03/17	$.5000
National Plants	w/e 02/25/17	$.5042

NON-FAT DRY MILK		
Week Ending 2/24 & 2/25		
Calif. Plants	$0.9619	5,072,529
Nat'l Plants	$0.9549	11,488,726
Prior Week Ending 2/17 & 2/18		
Calif. Plants	*$1.0099*	*4,705,718*
Nat'l Plants	*$0.9820*	*11,874,320*

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FRED DOUMA'S PRICE PROJECTIONS…

March 3 Est:	**Quota cwt. $16.49**	**Overbase cwt. $14.79**	**Cls. 4a cwt. $15.12**	**Cls. 4b cwt. $14.27**
Feb '17 Final:	**Quota cwt. $17.21**	**Overbase cwt. $15.51**	**Cls. 4a cwt. $15.42**	**Cls. 4b cwt. $15.81**

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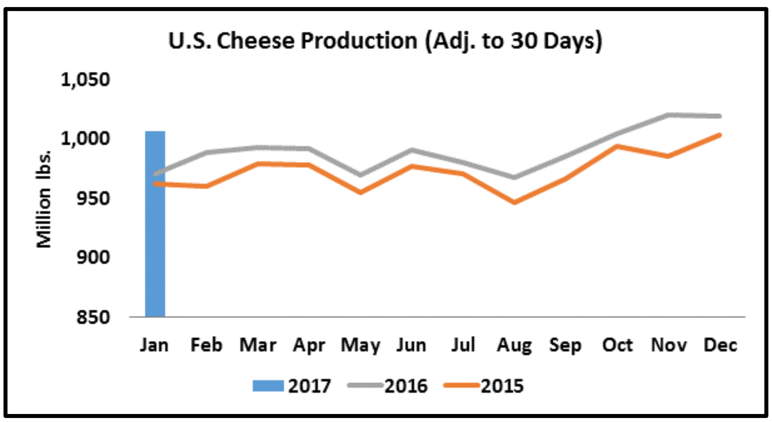
MARKET COMMENTARY

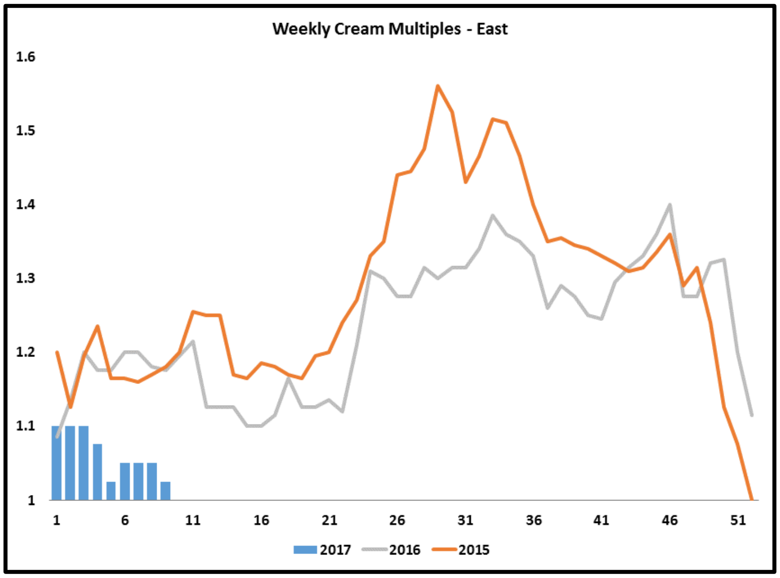
By Sarina Sharp, Daily Dairy Report, sarina@dailydairyreport.com

Milk & Dairy Markets



Milk is flowing to cheese vats, and the market is in retreat. This week CME spot Cheddar blocks dropped 9.5¢ to $1.48/lb. Barrels fell 8¢ to an eight-month low at $1.4375. Class III futures settled 20 to 55¢ lower than last week. Cheese has been piling up, and the market has feared a decline in American's formerly voracious appetite for cheese. But it appears that demand is still growing, just not as quickly as output. U.S. cheese production reached 1.04 billion pounds in January, up an impressive 3.7% from a year ago. Assuming exports are doing little to absorb the excess, this implies domestic demand is growing at a respectable 2% to 3% pace. But output remains strong. *Dairy Market News* reports, "With plenty of discounted milk, cheese contacts are attempting to find a middle ground between utilizing milk stocks and reining in growing cheese inventories."

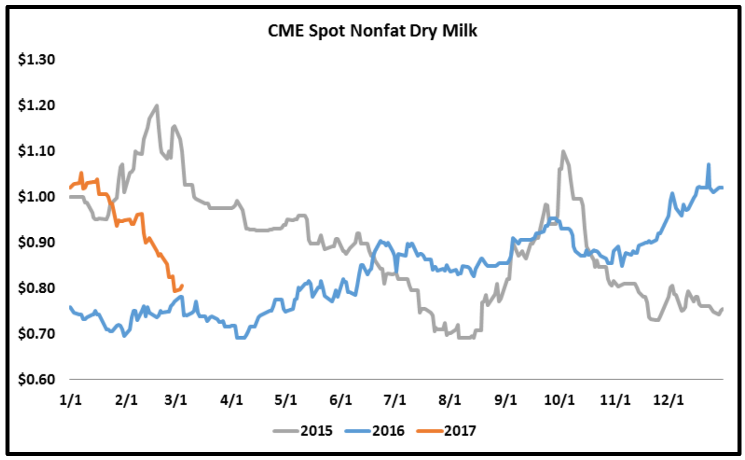
In contrast, the butter market is showing only modest growth in output, which hints at slowing demand. Butter production grew 1.2% year-over-year in January, reaching 177.8 million pounds. That is not a large enough increase to explain the big boost in butter stocks earlier this year. It is also curious given historically low cream multiples, which typically encourage butter makers to ramp up output. Cream multiples remain depressed, particularly in the East, suggesting butterfat in abundance.



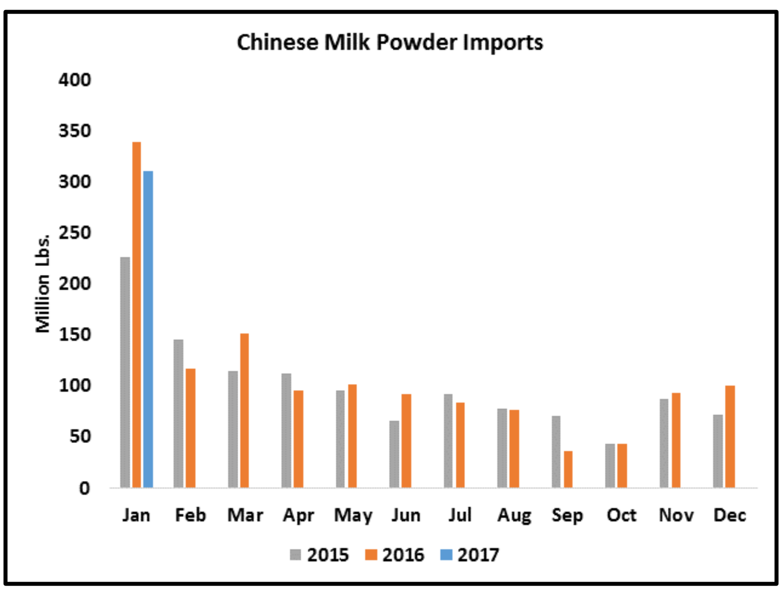
Nonetheless, butter prices held strong. The volume of supplies eligible for delivery to the CME diminished Wednesday as the calendar turned to March, and spot prices surged. But the "new crop" butter rally was short-lived; on Thursday prices lost all the ground they had gained and then some. Spot butter finished at $2.1625, up 3.25¢ from last Friday.

The milk powder market continues to flounder. This week spot nonfat dry milk (NDM) dipped below 80¢ for the first time since June. It closed at 80.5¢, down 1.75¢ from last week. Combined output of NDM and skim milk powder (SMP) totaled 205.6 million pounds in January, up 9.6% from a year ago. Manufacturers' stocks of NDM climbed 1.1 million pounds from December to January and were 1.1% greater than year-ago volumes.

There are wars and rumors of wars in the battle for milk powder market share, with speculation that Mexican buyers will look to European stockpiles. Meanwhile, Fonterra will offer 49% more SMP at next week's Global Dairy Trade auction than at the previous event. Milk powder makers are jockeying for sales while buyers remain patiently on the sidelines, a recipe for continued decline. However, the U.S. is likely to attract some bargain shoppers. The best cure for low prices is low prices, but the medicine is bitter and the convalescence could be prolonged.

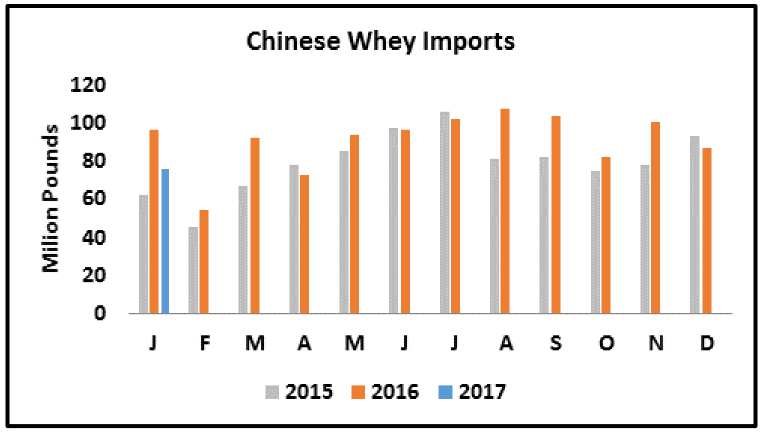


Chinese milk powder imports jumped in January, as they usually do when the volume of low-tariff import quotas resets at the turn of the year. China brought in 310.7 million pounds of SMP and whole milk powder (WMP) in January, 8% less than in January 2016 but considerably more than any other month last year. New Zealand accounted for 96% of China's WMP imports and 76% of its SMP shipments, highlighting the advantage that lower tariffs and free trade agreements offer.



Whey prices perked up a bit this week, but the days of quiet, steady strength in the whey market are a relic of the past. It is difficult for the value of whey protein to rally while NDM prices plummet. Manufacturers continued to favor high-protein whey products in January. Output of dry whey for human consumption was down 0.8% from last year, while production of whey protein concentrate with 50% to 89.9% protein was up 4.4% and output of whey protein isolates (WPI) jumped 12.8% from a year ago. Stocks of WPI surged 38.7% from year-ago levels, while dry whey stocks were down 18.9%.

Overseas demand is in question. Chinese whey imports in January fell 21.1% short of year-ago levels. Chinese imports of cheese and ultra-high temperature milk, which had been running hot throughout 2016, also cooled a bit in January.



Cows continue to struggle in the cold and the mud from California to Idaho, but things are a bit sunnier and warmer than they were a few weeks ago. Elsewhere, mild temperatures are heralding an early start to the spring flush. *Dairy Market News* reports that in the East, "milk production is strong. Each week, production continues to grow, filling manufacturing plants full with abundant volumes of milk." In some regions, milk is backing up as production climbs and a few processors navigate unplanned downtime.

For the week ending February 18, dairy cow slaughter totaled 62,643 head, up 6.5% from the same week a year ago. This brings year-to-date slaughter down 1.6% from the 2016 pace. Cull rates remain elevated in California, Idaho, Oregon, and Washington.

Grain Markets

May corn futures gained a dime this week. May soybean futures settled 13¢ higher. The strength is more about politics and big-money, big-picture traders than fundamentals. Assuming that inflation will accelerate, funds continue to pour into commodities. Investors have added money to commodity exchange-traded funds for six consecutive quarters, the longest streak of net inflows since before the financial crisis. Not all of that money is making its way into grains and oilseeds, but the buy-in is large enough to provide a noticeable boost in prices.

On Monday Bloomberg reported that Carl Icahn, the billionaire investor who is advising the Trump administration on ways to reduce regulation, brokered a compromise that would shift the burden of compliance with renewable fuels mandates from refiners to blenders. Mr. Icahn, who owns a majority stake in a major refiner that would benefit from the rule change, suggests that refiners would agree to the switch if Congress reinstates the expired biofuels tax credit and allows the use of higher ethanol blends in gasoline throughout the year. Both accommodations to the biofuel industry are likely to increase demand. The tax credit would make it difficult for imports to compete with domestic biofuels, boosting utilization of domestic soybean oil. The impact of increased use of higher ethanol blends would be felt more slowly, as there are a limited number of gas pumps offering higher blends of the more corrosive, less efficient fuel. The policy change and accompanying handouts are not a done deal, but the possibility had the markets salivating this week.

Meanwhile, South American weather prospects are excellent, with regular rains and intermittent sunshine in the forecast. South American soybean production is probably at least 5 million metric tons larger than the market assumed a month ago. In a vacuum, this would pressure prices considerably. But today, money flow and political bargains reign supreme.

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THE CALIFORNIA FEDERAL MILK MARKETING ORDER: WHAT IS HAPPENING NOW?

By Geoff Vanden Heuvel, MPC Board Member and Economics Consultant

On February 14, 2017 the United States Department of Agriculture published a Recommended Decision that proposes a Federal Milk Marketing Order that would cover the entire state of California. They established a deadline of May 15, 2017 for interested parties to submit comments on the Recommended Decision. After the initial comment period USDA reviews all the comments and makes whatever adjustments they deem necessary over the next 90 days or so, and then publishes a Final Decision which producers will vote on. It is only producers who vote and the cooperatives may "block vote" for all of their members. But the vote is yes or no, not maybe so getting this right is a big deal.

It is important to remember that it was the three major California cooperatives, California Dairies, Inc., Land of Lakes and Dairy Farmers of America who petitioned USDA for a hearing to consider establishing a California FMMO. If you remember, it took those cooperatives and their professional staff well over a year to actually draft a detailed, fully complete proposal to USDA for consideration. After USDA received that petition and scheduled a hearing, the Dairy Institute representing the processors also developed a detailed, complete alternative proposal for USDA to consider. Then the producer-handlers in California and Nevada submitted two other more narrow alternatives addressing their particular concerns. So there was a lot of material to cover in a hearing and the hearing consisted of 40 days of testimony in late 2015. After the actual hearing was completed there was another almost 6 month period for the various interested parties to complete and file post-hearing briefs. It is from this mountain of material that USDA constructed the Recommended Decision. This Decision is unique, that is, it does not exactly follow any particular parties' proposal.

So what is happening now is that there is a lot of analyzing, thinking and talking going on by the people most intimately involved in putting the proposals together in the first place. As they begin to sharpen their perspectives we will no doubt be able to more clearly understand the benefits and risks of what USDA has proposed along with what tweaks producers may propose to improve the program.

One of the early issues that needs clarity is the role the California Department of Food and Agriculture would play in operating the quota program. Since there was no communication between USDA and CDFA prior to the public release of the Decision on February 14, CDFA was not able to determine ahead of time whether or not current law gives them the authority to perform the role that the USDA has envisioned for them to do. The State of California currently operates a milk pooling plan that includes quota under the authority of state law. Division 21 of the Food and Agriculture Code contains Chapter 3 which granted the authority for the state to form "Equalization Pools." This chapter was originally adopted in 1967. Among the provisions that is part of Chapter 3 is Section 62726 which says: "The director is the instrumentality of this state for the purpose of administering and enforcing the provisions of this chapter and to execute the legislative intent which is expressed in this chapter, and is hereby vested with the administrative authority which is described in this chapter. Notwithstanding other laws to the contrary, in the event a marketing order under the jurisdiction of the United States Department of Agriculture or other appropriate federal agency, is created by referendum or under the applicable laws and procedures relating there to, in this state or in any geographical area within this state, the provisions of this chapter or any part thereof which is in conflict with such federal order, or which is unnecessary or is a duplication thereof, shall be suspended in the geographical area covered by and during the existence of such federal order. The director shall take such steps and procedures as are necessary to wind up and conclude the administration and enforcement of the provisions of this chapter, or any part thereof, prior to the suspension date."

So what does this statute mean? That is why lawyers exist, but an argument could be made that USDA is proposing to take over part of the marketing order functions, but is specifically granting the State of California the right to operate a quota program side by side with the federal order. The federal order is not proposing to duplicate the State of California's quota administration function. So it seems that since currently all market milk in California is eligible to participate in the quota program and presumably would still be able to participate under a California FMMO, then the State should be able to enforce the financial requirements of the program on all market milk under its jurisdiction like it does now. It is complicated and some good and smart folks are working to sort it out. So stay tuned and rest assured that an enormous amount of effort is being expended to get the answers to these and other important questions. If you have any questions you would like an answer to, send them in an email to office@milkproducers.org and we will do our best to get you an answer.