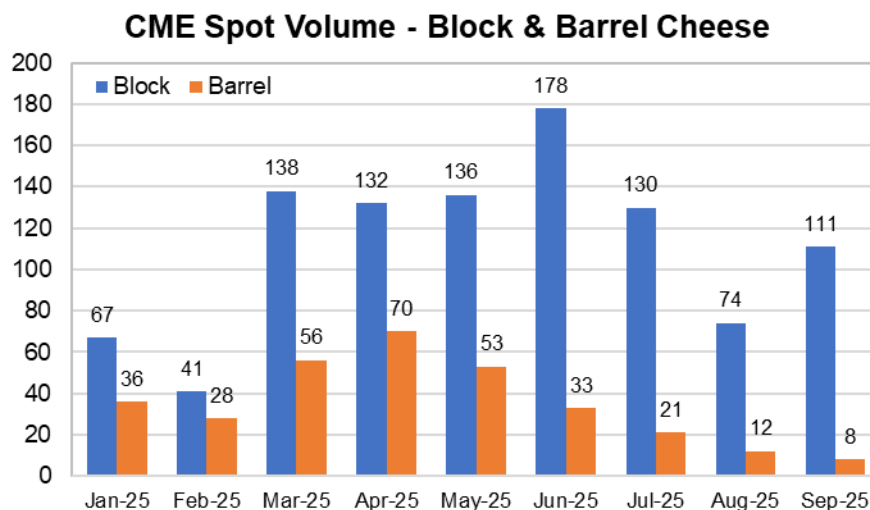


Time to Retire the CME Barrel Cheese Market
Cheese Market News Guest Column
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Who remembers the CME spot market for Grade A and Grade B butter? If so, you've been around for a while. Cash trading in butter used to occur once a week as did cheese. Up until the late 1990's, during the CME cash butter trading session, all three grades of butter were bought and sold – AA, A, and B. However, given that most of the butter produced was grade AA, volume on the grade A and B cash markets was very low, which led to them being discontinued.

In 1999, butter trading moved from once a week to three times per week before eventually moving to daily trading. These moves were made in attempt to increase liquidity in cash butter trading as well as provide more frequent price signals to the developing CME dairy futures markets.

Fast forward to 2025 and the same dynamics are at play with the CME spot market for barrel cheese. After the decision to remove the barrel cheese price from the class 3 milk calculation, the cheese industry has largely moved to CME block cheese for price discovery of Cheddar cheese in 500 lb. barrels. Trading volume for barrel cheese has dropped sharply to only 8 loads in September, down from 70 in April. Through mid-October, 46 loads of blocks traded compared to only 3 loads of barrels. If the barrel volume continues to dwindle to near zero, the CME should discontinue spot trading in barrel cheese as it ceases to have a role in price discovery.



Over the last decade, a pain point for many in the cheese industry was the volatile block-barrel spread. In the prior FMMO milk pricing formula, block and barrel prices were used to calculate the Class 3 milk price. The volatility in the spread created serious financial challenges at times, particularly for barrel cheese plants. As part of

the 2023-24 FMMO hearing, some advocated to remove barrels from the milk price calculation.

While there was little opposition to the change, there were legitimate concerns about further narrowing cheese price discovery to only 40-pound blocks. Instead of removing barrels from the formula, 640-pound blocks could have been added to dilute the influence of barrels in the class 3 milk price formula. But the decision was to remove the barrel price from the formula, and as of June 1, the National Dairy Products Sales Report ceased publishing data on barrel cheese prices and volumes.

The cheese industry mostly waited until early 2025 to decide how to price barrels going forward. Once the date was known, buyers and sellers of cheese discussed different methods of pricing barrel cheese in the future. The simple answer was to just move to pricing barrels off either CME or NDPSR block cheese. This was not a great leap into the unknown as most other cheese styles are priced off the 40-pound block Cheddar cheese price. The changes happened relatively quickly with most buyers and sellers moving to a block cheese basis for barrels.

This change has also improved the ability to hedge barrel cheese as it's now directly linked to the block cheese price, which is what futures and options contracts settle to. There is no more worrying about the block-barrel spread and impacts on hedges or milk costs.

The argument for keeping the CME spot barrel market is that there is a need for a centralized marketplace to buy or sell barrel cheese. This could be a credible argument when barrels played an important role in determining the cheese price that was used in the class 3 FMMO milk price formula. But with that not being the case, cheese in a barrel is no different than Mozzarella, Monterey Jack, or most any other style of cheese, which is priced off the 40-pound block cheese market.

More broadly, the dairy industry should consider moving to a different method of price discovery. The CME spot markets trade the marginal load of product in essentially the market of last resort. Trading is very thin with only a small number of traders and few commercial firms participating in the price discovery process. The volume of dairy products traded on the CME is a very small percentage of total production. At times, the market moves on no volume. And that price sets the price for practically all cheese and butter in the country, and by extension, most of the milk. Try to name another agricultural product, or any product, that values billions of dollars of production in the manner that dairy does.

Instead of using thinly traded spot markets, imagine getting daily reports from the USDA with prices for many dairy products – cheese, butter, milk powders, and whey products, as well as milk and components. The report could also include milk volume and other important market factors. This would create a new price discovery

mechanism which captures a much larger number of products and transactions. The interplay between cash and futures prices would continue, and over time, futures markets could be used for price discovery like they are for other ag commodities.

To be clear, the spot markets have generally benefitted the dairy industry over the years. Despite their shortcomings, the industry has validated their credibility by using the spot prices in commercial transactions. There will be some that will oppose any change to how dairy prices are discovered. Others simply are afraid of the uncertainty that would come with a new pricing system.

As the industry adapts to the recent FMMO milk price changes, there is a need to look ahead to developing a pricing system that helps U.S suppliers compete in a global marketplace. These changes will not be easy, but the industry can develop a price discovery system similar to other agricultural commodities that could result in less volatility, better price transparency, and improved ability to manage price risks.