



The KDM Dairy Report - March 30th, 2007

Bullish Fundamentals:

- March Class III was announced today at \$14.96, the highest settlement price since December, 2004.
- Commercial Disappearance: USDA released commercial disappearance numbers for January, and it shows 2007 is [off to a strong start](#). Use of American cheese was up 2.8% vs. last year while use of all other types of cheese was up 5.6%. Butter use was up a very strong 37.5%, with nonfat dry milk use up 2.5%. Finally, use of milk in all products was up a respectable 5.4% over last January.
- Ag Prices Report: USDA's monthly look at prices paid and received by farmers showed that the milk-to-feed ratio is beginning to improve with the higher milk prices, but is [still well below the 3.0 threshold](#) associated with herd expansion. For March, the milk-to-feed ratio was 2.41, increase from a revised 2.31 in February, but below last March at 2.70.
- NASS [powder prices shot higher](#) this week, led by nonfat dry milk, up 6.5¢ to average \$1.23/lb and dry whey up 2.1¢ to 72.8¢/lb. Cheddar blocks also moved higher, up a penny from last week to reach \$1.36/lb, while barrels were essentially unchanged at \$1.37/lb. Butter saw the lone drop, losing 0.3¢ to average \$1.29/lb.
- Cash Market: At this point, cheese buyers appear to have more bullets than sellers, as prices were bid slightly higher while trade volume dipped. Blocks and barrels both settled at \$1.42/lb, which represented a 2¢ increase over last week for blocks and a penny gain for barrels. Butter stayed steady at \$1.33/lb. 3 loads of blocks, 9 loads of barrels and 14 cars of butter exchanged hands.
- Central nonfat dry milk supplies remain [short of demand](#), with some contracts being shorted, according to Dairy Market News. Producer list prices this week were as high as \$1.80/lb, far above reported NASS numbers. Out East, nonfat dry milk production is behind last year with some drying operations not expecting to have enough milk to operate until fall.
- Dairy Market News reports international interest for Western nonfat dry milk continues to be strong, even as prices rise. Contacts note some [buyers are short of needs](#), having misjudged the market, and are still short of powder.
- While price resistance is noted for domestic dry whey, the European whey market is at about [82¢/lb](#), according to Dairy Market News. This should keep the domestic price from falling too far.
- The cheese market is firming, according to Dairy Market News. Demand for current blocks and barrels is more than what's being offered, as buyers look for more cheese to fill needs and put some away for use later in the year. Some end-users are [concerned about cheese availability](#) later this summer so are trying to buy early.
- 52,800 dairy cows were slaughtered during the week ending 03/17, [7,500 head more](#) than the same week last year, according to USDA Market News.
- Butter stocks at CME-approved warehouses totaled 113.9 million lbs for the week ending 03/24, [just 3 million lbs](#) (2.7%) more than last year at this time.
- Milk production along the eastern corridor is steady to slightly higher, however, balancing plants throughout the region are reporting milk intakes [well behind historical levels](#), according to Fluid Milk & Cream Review. These same plants are receiving more calls for condensed products, but have to turn these requests down due to lack of milk.
- Milk production in New Mexico is higher than in February, but is still behind year ago levels, according to Fluid Milk & Cream Review. New crop hay is coming, but it will be expensive. Much the same in the Pacific Northwest, where production is increasing slowly, but [behind last year](#). Milk processors have additional plant capacity that is going

Futures Month	Friday 03/30 Close	Friday 03/23 Close	Change	5-yr Average	Top 3rd Price
Apr-07	\$15.77	\$15.62	\$0.15	\$13.09	\$14.31
May-07	\$15.54	\$15.60	(\$0.06)	\$13.14	\$14.49
Jun-07	\$15.50	\$15.52	(\$0.02)	\$12.54	\$13.63
Jul-07	\$15.50	\$15.70	(\$0.20)	\$12.25	\$13.16
Aug-07	\$15.90	\$16.11	(\$0.21)	\$12.41	\$13.34
Sep-07	\$16.14	\$16.35	(\$0.21)	\$13.11	\$13.99
Oct-07	\$15.79	\$15.95	(\$0.16)	\$13.19	\$13.98
Nov-07	\$15.55	\$15.60	(\$0.05)	\$12.88	\$13.86
Dec-07	\$15.18	\$15.30	(\$0.12)	\$12.92	\$14.01
Jan-08	\$15.10	\$15.18	(\$0.08)	\$12.50	\$13.33
Feb-08	\$14.98	\$15.15	(\$0.17)	\$12.53	\$13.21
Mar-08	\$14.88	\$15.05	(\$0.17)	\$11.89	\$12.61
Apr-08	\$14.93	\$15.06	(\$0.13)	\$13.09	\$14.31
May-08	\$14.95	\$15.10	(\$0.15)	\$13.14	\$14.49
Jun-08	\$15.00	\$15.12	(\$0.12)	\$12.54	\$13.63
Jul-08	\$15.11	\$15.24	(\$0.13)	\$12.25	\$13.16
Aug-08	\$15.18	\$15.26	(\$0.08)	\$12.41	\$13.34
Sep-08	\$15.29	\$15.38	(\$0.09)	\$13.11	\$13.99
Oct-08	\$15.00	\$15.10	(\$0.10)	\$13.19	\$13.98
Nov-08	\$14.74	\$14.85	(\$0.11)	\$12.88	\$13.86
Dec-08	\$14.54	\$14.70	(\$0.16)	\$12.92	\$14.01
Mar-Dec Avg	\$15.65	\$15.75	(\$0.10)		
2008 Avg	\$14.98	\$15.10	(\$0.12)		

unused, so some loads are coming in from Western sources. Expensive feed has some producers cutting back on hay in the ration and using more silage, as hay growers report they have nothing left.

- International: Although a few European countries will exceed their quota milk production, stocks of dairy end-products [remain tight](#). International buyer interest for the upcoming production season is strong, competing directly with the European food industry for product. Buyers are reluctantly paying higher prices for the dairy component of their formulations; otherwise they would be forced to cease operations.
- International: Milk receipts are falling off faster than expected in New Zealand due to lack of moisture. For the year, milk production in New Zealand should be up 1½-2%, but the continuing drought in Australia has the region facing an uncertain supply situation well into 2007-2008. Current stocks of dairy end-products are fully committed with [nothing additional available](#) to buyers. Customers are expressing increased concern over product availability next season.

Bearish Fundamentals:

- Prospective Plantings Report: USDA reported corn growers intended to plant 90.5 million acres of corn this year, up 15% from 2006 and up 11% from 2005. The number is the [highest acreage since 1944!](#) The additional corn acres come at the expense of soybeans acres, which are down 11% from last year to 67.1 million acres. Corn futures on the CBOT finished limit down (20¢) today in the May '07 through July '08 contracts.
- California may be nearing its peak as fewer animals are now freshening, but milk production remains strong and processors continue to run on extended schedules in order to handle current supply, according to Fluid Milk & Cream Review.
- Trade activity in dry whey was very light this week, according to Dairy Market News. Even though dry whey traded mostly between 75-78¢ per pound, buyers are watching the new dry whey futures contracts which trade on the CME, observing that prices have fallen into the low 60¢ range beyond July. This is [encouraging buyer resistance](#), and some sellers have now offered contracts at prices below earlier negotiated deals.

Recommendation:

A comment on grains: Today's highly anticipated Prospective Plantings report did not disappoint. With news that more corn acres would be planted this year than in any previous year since 1944, the corn futures market settled limit down in the May '07 through July '08 contracts. If feed grains continue to trade lower next week, it may provide a great opportunity for those who haven't hedged their input costs to get some protection. However, we would caution producers against buying the physical grain and signing a contract with your feed provider, but instead, buy call options to protect against a potential rapid price increase this summer due to weather and demand. Why? There is the potential that we see high grain prices at the CBOT, but a growing basis at the local level due to more and more grain piling up and filling available storage. Locking in locally will not allow you, the feed buyer, to benefit from this situation, but owning a call option will, while at the same time protecting you if prices rebound later this year. Give us a call if you have any questions on this or want to take a look at what's available.

After being the price leader for most of the year, dry whey appears to either be topping out, or taking a breather. While the international price for dry whey remains high and foreign demand continues to be strong, sellers trying to extract higher prices are having a tougher time at it. However, just like last fall when wheat was the price leader, only to pass the baton to corn, similarly it appears dry whey may stall, but cheese may be ready to take its place. Cheese sellers in the cash market seemed less aggressive this week and bidders were able to take the price higher. Dairy Market News noted above that demand for current blocks and barrels is stronger than offerings, while the world-wide protein shortage continues. And, our first commercial disappearance numbers of 2007 indicate demand for dairy products has been robust.

No doubt today's drop in the grains could provide some financial relief to some dairy operations and move our milk-to-feed ratio higher, but even another 2 limit down days in corn is still expensive feed. We continue to have a positive bias on the market longer term, but as we continue to work through spring, higher milk production could make the front months vulnerable. With that said, we would still stick with PUT options and our recommendation from last week. Try to buy the May-Jun 15.00 PUT options for an average of 15¢ each (currently 18¢) and the July-Sep 15.00 PUT options at 25¢ each (currently 32¢).

Note: The markets will close at noon on Thursday, April 5th and all day Friday, April 6th in observance of Good Friday. Our offices will be closed after noon on Thursday and will re-open on Monday, April 9th. We wish you and your families a wonderful Easter!

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