

The KDM Dairy Report – November 9th, 2007

Bullish Fundamentals:

- Cash Market: Blocks surged 4½¢ this week in whip-saw fashion as both buyers and sellers explored price discovery on both ends. Bidders won this week with blocks closing at \$2.05½/lb on only 3 trades. Barrels closed their wide spread from last week, gaining a stellar 9¢ for the week to settle at \$2.00¼/lb on 11 trades. Butter continued to pull itself up through sheer buying power as bidders took on 34 cars for the week and in the process raised the price 7¢ to \$1.38½/lb.
- World Ag Supply & Demand Report: USDA's monthly look at international supply and demand was largely favorable to dairy. They reduced their milk production estimates for 2007 and 2008 due to the declining pace of increases in cow numbers. The weak U.S. dollar and tight milk supplies in other countries should result in lower imports into the U.S. and aid in exporting dairy products out of the U.S. USDA revised their 2008 price [forecast higher](#) for both Class III milk and cheese as a result.
- Dairy cow slaughter [continues to be robust](#). For the week ending 10/27, 53,500 head were culled vs. 50,600 during the same period last year.
- International: Milk production in New Zealand is below expected levels, and output in Australia for the first quarter of the production year is off 8.2%, according to Dairy Market News. Rain has come to drought-stricken areas, [but was insufficient](#) to help replenish water levels. What rain did fall, came as farmers were trying to harvest forage, hurting quality. Product availability remains very limited.
- Class I interest has improved and cheese makers [want more milk](#) in the Midwest, according to Fluid Milk & Cream Review. Production of holiday items like dips, eggnog and sour cream are also stronger, and some cheese buyers are still short on product.
- Dry whey prices saw increases over last week, according to Dairy Market News. Supplies are in balance and demand has improved, causing the [market to firm](#).
- It's a Catch-22 in the cheese market, according to Dairy Market News. Both cheese makers and buyers are nervous at current \$2+ prices, so buyers are limiting purchases and makers are limiting production to avoid high-priced inventory. Cheese makers in the Midwest have largely switched to non-cheddar varieties, resulting in current cheddar supplies being [tight in the region](#). Packagers are working overtime to fill orders prior to the holidays and also to fill stronger export demand.
- Dairy Market News reports demand for Western cheese is strong. Buyers are looking for cheese for both domestic and export needs, with some stating there is a [ready home for cheese](#) in the export market if domestic buyers don't want it.
- International: Cheese demand is strong in Oceania and [stocks are fully committed](#) through the end of the calendar year. Handlers feel the supply situation will change very little after the new year due to less than desired milk volumes.

Futures Month	Friday 11/09 Close	Friday 11/02 Close	Change	5-yr Average	Top 3rd Price
Nov-07	\$19.20	\$18.77	\$0.43	\$12.88	\$13.86
Dec-07	\$18.45	\$17.80	\$0.65	\$12.92	\$14.01
Jan-08	\$17.39	\$16.73	\$0.66	\$12.50	\$13.33
Feb-08	\$16.59	\$16.21	\$0.38	\$12.53	\$13.21
Mar-08	\$16.38	\$16.17	\$0.21	\$12.78	\$13.50
Apr-08	\$15.95	\$15.91	\$0.04	\$14.14	\$15.36
May-08	\$15.88	\$15.87	\$0.01	\$14.50	\$15.85
Jun-08	\$15.95	\$15.98	(\$0.03)	\$14.54	\$15.63
Jul-08	\$16.09	\$16.08	\$0.01	\$14.66	\$15.57
Aug-08	\$16.26	\$16.20	\$0.06	\$14.47	\$15.40
Sep-08	\$16.40	\$16.31	\$0.09	\$15.14	\$16.02
Oct-08	\$16.10	\$15.95	\$0.15	\$14.78	\$15.58
Nov-08	\$15.80	\$15.72	\$0.08	\$12.88	\$13.86
Dec-08	\$15.71	\$15.61	\$0.10	\$12.92	\$14.01
Nov-Dec Avg	\$18.83	\$18.29	\$0.54		
2008 Avg	\$16.21	\$16.06	\$0.15		

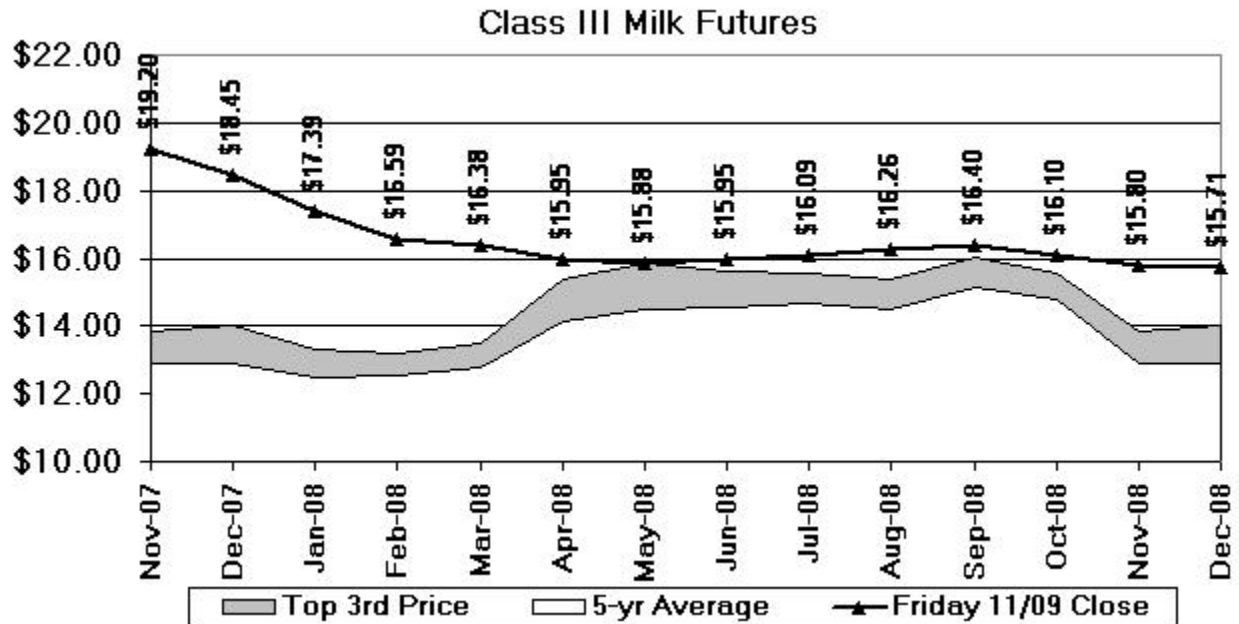
Bearish Fundamentals:

- Milk output in California is 3-5% higher than a year ago and well above last year in Arizona, according to Fluid Milk & Cream Review. Processing plants in AZ are handling local supplies as well as milk from nearby states. There are some reports that higher retail prices are [impacting consumer demand](#) as sale slip. Plants in the Pacific Northwest have slightly more milk than anticipated as fall weather conditions have been good in the region.
- After rising two weeks in a row, [dry whey dropped](#) 1.3¢ in this week's NASS survey, averaging 42.1¢/lb. 40-lb blocks lost 0.6¢ to average \$1.87/lb but barrels inched 0.7¢ higher to \$1.91/lb, butter was up 0.2¢ to \$1.27/lb and nonfat dry milk increased 2.2¢ to \$2.07/lb.
- Milk shipments into the Southeast were down significantly this week as milk production has begun to rebound in the region, according to Fluid Milk & Cream Review. 154 loads were imported into the milk deficit area vs. 356 last week. Class I sales are steady, making [extra milk available for manufacturing](#) use.

- International: Favorable milk prices appear to be spurring producers in the EU to generate as much milk as possible, according to Dairy Market News. Manufacturing plants are putting out more finished products and depleted stock levels are [starting to rebuild](#), causing prices to weaken.

Recommendation:

The milk market did not correct this week as we thought it might.....yet. We're hearing reports on both sides this week. Bulls – lots of new reports on fresh export interest (see above), tight current cheddar supply and hungry buyers. Maybe we'll sustain the cheese market for yet another week, which will certainly help



the front months. Bears – domestic sales are being hurt by high prices, the stock market was walloped this week, local cheese plants stating they're starting to get enough milk to meet needs and reports of lots of animals freshening in the coming months. We still feel a correction in the front months is coming, so would strongly urge producers to get PUT option coverage for Dec and Jan. Buy the Dec 1775 PUT for 20¢ or the 1800 PUT for 30¢. There prices are just under their settlement today so you could get filled next week if the cheese rally continues. Nothing new to report for 2008. We would not sell large percentages of production at this time. 2008 settled at a new annual high today of \$16.21. The market may be coming to grips with export potential combined with radically higher production costs. That said, a continued and sustained wipeout in the stock market will not equate to solid domestic demand. Need to keep an eye on that.

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