

**The KDM Dairy Report – January 4<sup>th</sup>, 2008**

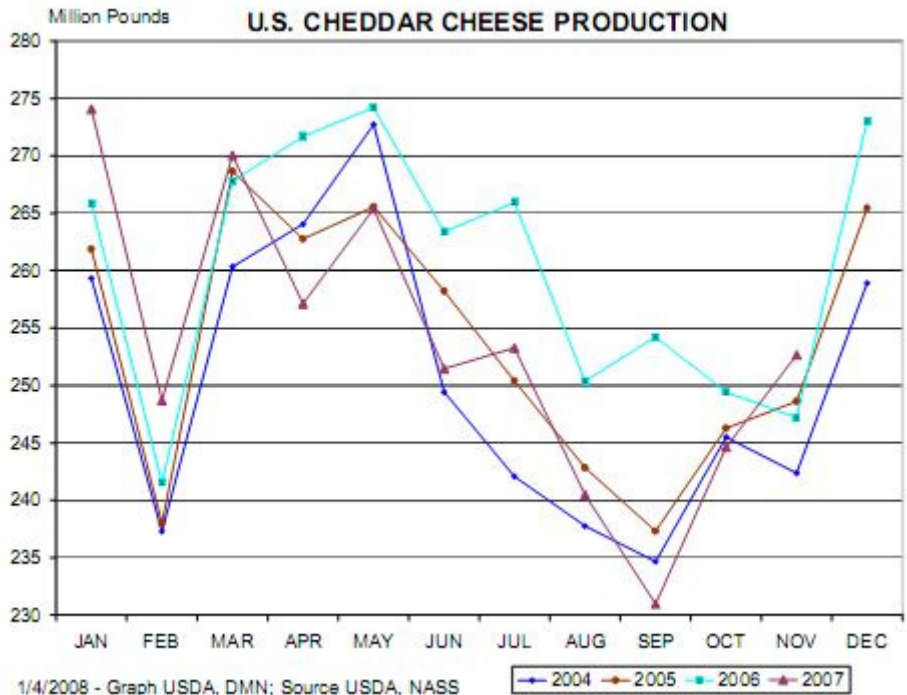
**Bullish Fundamentals:**

- Cash Market (cheese): Block sellers were no where to be found, so bidders were able to move the price up 12¼¢ for the week to close at \$2.15¼/lb today. Barrels followed, up 11¢ to \$2.09/lb. Buyers came up empty on blocks but 4 loads of barrels exchanged hands.
- Despite being past the holiday period, cheese makers report they have some [good quantities of cheese have been booked for exports](#) in the first quarter. And, at a time when cheddar aging programs should begin rebuilding inventory, many gaps are appearing as buyers consider cheese prices too expensive.
- International: Though rainfall has occurred in Australia and helped green up pastures, hot summer weather of 100 degrees plus is quickly returning moisture to drought levels, according to Dairy Market News. Things are better in New Zealand, where production is up 2-3% above last year, but even so, most handlers and traders in the region indicate that they have [no uncommitted stock](#) available for sales.

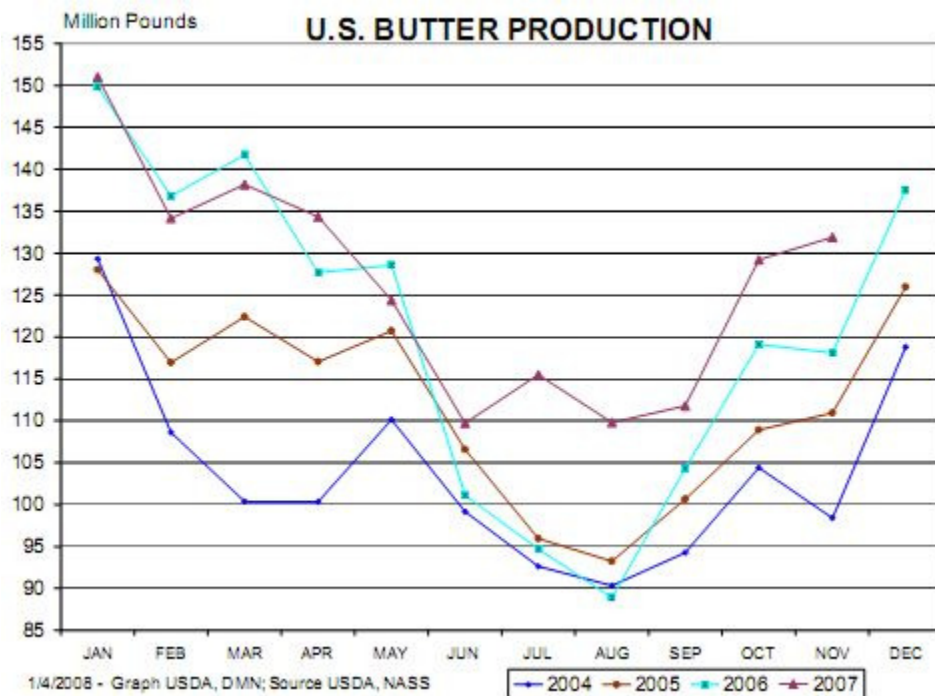
Futures Month	Friday 01/04 Close	Friday 12/28 Close	Change	5-yr Average	Top 3rd Price
Jan-08	\$19.95	\$18.88	\$1.07	\$12.50	\$13.33
Feb-08	\$18.88	\$17.87	\$1.01	\$12.53	\$13.21
Mar-08	\$18.06	\$17.44	\$0.62	\$12.78	\$13.50
Apr-08	\$17.23	\$16.75	\$0.48	\$14.14	\$15.36
May-08	\$16.95	\$16.54	\$0.41	\$14.50	\$15.85
Jun-08	\$17.00	\$16.59	\$0.41	\$14.54	\$15.63
Jul-08	\$17.02	\$16.60	\$0.42	\$14.66	\$15.57
Aug-08	\$17.11	\$16.75	\$0.36	\$14.47	\$15.40
Sep-08	\$17.16	\$16.89	\$0.27	\$15.14	\$16.02
Oct-08	\$16.50	\$16.45	\$0.05	\$14.78	\$15.58
Nov-08	\$16.30	\$16.26	\$0.04	\$14.75	\$15.73
Dec-08	\$16.29	\$16.20	\$0.09	\$15.09	\$16.18
Jan-09	\$15.91	\$15.65	\$0.26	\$12.50	\$13.33
Feb-09	\$15.99	\$15.50	\$0.49	\$12.53	\$13.21
Mar-09	\$16.00	\$15.46	\$0.54	\$12.78	\$13.50
Apr-09	\$15.96	\$15.70	\$0.26	\$14.14	\$15.36
May-09	\$15.95	\$15.60	\$0.35	\$14.50	\$15.85
Jun-09	\$15.70	\$15.59	\$0.11	\$14.54	\$15.63
<b>2008 Avg</b>	<b>\$17.37</b>	<b>\$16.94</b>	<b>\$0.44</b>		

**Bearish Fundamentals:**

- Cash Market (butter/powder): Spot butter prices continued to wilt under massive production. Sellers were the aggressors, driving the price down 3¼¢ from last week to close at \$1.21¾/lb today. And, Grade A nonfat dry milk was offered 5½¢ lower to \$1.67½/lb. No buyers came forward for either commodity.
- Economy: Today's jobs report showed only 18,000 new jobs were created last month when expectations were for an increase of 70,000. Unemployment jumped to 5% from 4.7% in November, the [largest monthly rise](#) since October 2001, just after the 9/11 attacks. As a result, the stock market was punished today with the Dow down 256 points on fears of recession.
- Dairy Products Report: USDA reports cheddar cheese production in November was [up 2.2%](#) vs. a year ago, and up 3.3% from October. Total cheese production was up 1.2% from last year, but down 1.9% from the prior month. Finally, butter output was strong, up 11.7% vs. 2006 and up 2.1% vs. October.
- NASS numbers [fell across the board](#) this week. 40-lb blocks dropped 9.5¢ to average \$1.99/lb while 500-lb barrels slipped 7.7¢ to \$2.02/lb. Butter continued to trend lower, losing 0.6¢ to average \$1.31/lb and dry whey lost 0.3¢ to 44.3¢. Finally, nonfat dry milk plummeted 20¢ in response to a lower cash market, averaging \$1.64/lb.



- Balancing plants in the Eastern region of the country are still dealing with [extra milk](#) from the holiday period as well as slow Class I sales. Strong milk production is sending more volumes of milk to the dryers and supplies of cream are heavy to burdensome.
- Fluid Milk & Cream Review reports the same is true in the Central region. Overall Class I demand continues to lag pre-holiday levels. Handlers are still working through extra bulk fluid and cream supplies as they [work to empty silos](#) that filled over the holidays. Heavy discounts for spot loads of milk continue.
- Weather in California has been good for milking cows, and they've responded, according to Fluid Milk & Cream Review. Milk production is strong and capacity at processing plants is [being stretched](#), with more reports of milk being dumped. Excess milk is being shipped out of state, much of it ending up in Arizona and New Mexico. Plants in those states are busy as well, and dealing with their own strong production.
- Excess Western cream is making its way into the Central region, curtailing movement of Eastern cream, according to Dairy Market News. Cream [supplies are heavy](#) across the country and churning activity is strong. Butter sales are slow, so much of the new production is being cleared to inventory, which is building.
- Nonfat dry milk inventories are [heavy and building](#), according to Dairy Market News. Production was heavy over the year end as processors continue to struggle with the milk supply. Demand is light and world prices are lower.
- International: Trading of dairy products in Western Europe has slowed due to the yearend holiday period, according to Dairy Market News. Stocks of dairy end products [are now available](#) for immediate and future needs. Prices are weakening as buyers wait for prices to stabilize.



### Recommendation:

The cash market continued to be the star this week, and the rocket fuel for the markets. Cheese not only held but marched more than 12¢ higher on uncontested bids. The high for the week came Thursday when the 2008 average settled at \$17.63. Buy orders literally blew through any resistance and soon sellers were hard to be found. No doubt there were those trying to cover short positions, but as well, it seems the reasoning that many of the months trading in the \$16.50 range were simply too low in light of current grain and energy prices could have played a role too. Finally, commercial end users of milk and cheese might have been waiting for the market to collapse after the year end, and found it quickly going the other way may have provided motivation to get some long hedge coverage. Either way, we ended the 2008 average up 44¢ for the week. Once again, it's hard to say where we go from here. Cheese made a solid move up today but futures were decidedly lower, perhaps due to profit taking. If cheese continues to hold or go higher, the January contract will fire right back up, up and away. But this scenario of excessive milk and tight cheese cannot go on forever. Butter and powder prices continue to slide lower, and eventually some of that powder will get cheap enough to introduce to the vat and increase yields. But probably most concerning is our U.S. economy. We can have the best export year ever in 2008, but if domestic demand falters, we will have way too much milk floating around. We could continue to target protecting the front months with PUT options. Enter orders to buy the Feb 18.25 PUT and the March 17.25 PUT for 25¢ each. Despite the run-up in the rest of the 2008 contracts, we're still not ready to pull the trigger.

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