

**The KDM Dairy Report – March 20<sup>th</sup>, 2008**

**What's Bullish:**

- Cash Market: Blocks traded as low as \$1.73/lb on Monday, but crawled their way back to \$1.80/lb by the end of the week, losing just a penny from last week. Barrels fell to \$1.69/lb, but bounced back to \$1.77½/lb to end the week 6¼¢ higher, while butter made further gains, climbing to \$1.38¾/lb, up 4¼¢ for the week. Butter buyers had only to bid the price higher, as no trades were reported, but cheese buyers showed their mettle, picking up 21 loads of blocks and 22 loads of barrels in a strong showing.
- Cold Storage Report: American cheese stocks in February were [down 8%](#) vs. a year ago, according to USDA. Total cheese stocks were also down 8%, but butter stocks were 8% higher.
- Livestock, Dairy & Poultry Outlook Report: USDA's look at various domestic ag sectors includes some encouraging news with dairy. While milk production is expected to increase 2.7% in 2008, commercial use of dairy products is forecast to increase by [better than 3%](#), well above the trend of recent years. They also say, "Milk yield will grow more slowly in 2008 as a near-term response to high feed prices. Milk production will continue upward through most of 2008, lowering prices. Exports will continue to figure prominently in dairy product price formation. Prices will be lower than in 2007, but not as low as they would be without exports."
- Livestock Slaughter Report: February dairy cow slaughter was 214,800 head. Adjusted for the extra day, it comes out to 207,400, which was [2.7% more](#) than a year ago, when 201,900 were culled.
- Weekly dairy cow slaughter numbers [were strong](#). For the week ending 03/08, 53,100 head were culled, compared to 51,600 during the same period last year.
- Cream supplies in the Central region are [tighter this week](#), according to Fluid Milk & Cream Review. Stronger retail and food service orders due to the holidays and the NCAA basketball tournament are cited as reasons for the drop.
- Dairy Market News reports the butter market in the Central region is firm. Ice cream production is starting to acquire increasing volumes of cream, and butter orders during the pre-holiday period were [stronger than current production](#) could fill. Suppliers had to reach into inventoried stock to meet commitments.
- Butter stocks at CME-approved warehouses fell by 2.8 million lbs for the week ending 03/15. During the same period last year, only 864,000 lbs were pulled. Total stocks at 118 million lbs are still above last year's levels of 112.4 million lbs, but [the gap is closing](#).
- Central dry whey prices were slightly higher and the market is firming, according to Dairy Market News. Production is steady and inventories are described as [adequate to slightly short](#). New orders are requiring some lead time before they can be filled.
- Western dry whey prices were up as well this week. Dairy Market News reports prices were higher because of inventories being in much close balance and demand steady to improving. Buyers who were operating on very short stocks are now [trying to build better working levels of inventories](#), with interest from both domestic and export sources.
- Nonfat dry milk prices were firming this week, according to Dairy Market News. Current offerings are lighter than they have been in several weeks, and product is moving better to both domestic and export accounts. With some parts of the world running below expected production levels, [buyers are looking to the U.S.](#) for their needs.

Futures Month	Thursday 03/20 Close	Friday 03/14 Close	Change	5-yr Average	Top 3rd Price
Mar-08	\$17.99	\$18.03	(\$0.04)	\$12.78	\$13.50
Apr-08	\$16.69	\$16.86	(\$0.17)	\$14.14	\$15.36
May-08	\$16.97	\$16.91	\$0.06	\$14.50	\$15.85
Jun-08	\$17.02	\$17.00	\$0.02	\$14.54	\$15.63
Jul-08	\$17.08	\$17.18	(\$0.10)	\$14.66	\$15.57
Aug-08	\$17.25	\$17.36	(\$0.11)	\$14.47	\$15.40
Sep-08	\$17.43	\$17.52	(\$0.09)	\$15.14	\$16.02
Oct-08	\$17.26	\$17.32	(\$0.06)	\$14.78	\$15.58
Nov-08	\$17.26	\$17.32	(\$0.06)	\$14.75	\$15.73
Dec-08	\$17.25	\$17.36	(\$0.11)	\$15.09	\$16.18
Jan-09	\$17.10	\$17.40	(\$0.30)	\$14.40	\$15.24
Feb-09	\$17.03	\$17.34	(\$0.31)	\$14.00	\$14.69
Mar-09	\$16.96	\$17.25	(\$0.29)	\$12.78	\$13.50
Apr-09	\$16.91	\$17.25	(\$0.34)	\$14.14	\$15.36
May-09	\$16.97	\$17.30	(\$0.33)	\$14.50	\$15.85
Jun-09	\$17.04	\$17.38	(\$0.34)	\$14.54	\$15.63
Jul-09	\$17.12	\$17.30	(\$0.18)	\$14.66	\$15.57
Aug-09	\$17.02	\$17.30	(\$0.28)	\$14.47	\$15.40
Sep-09	\$17.10	\$17.35	(\$0.25)	\$15.14	\$16.02
Oct-09	\$17.06	\$17.32	(\$0.26)	\$14.78	\$15.58
Nov-09	\$17.04	\$17.28	(\$0.24)	\$14.75	\$15.73
Dec-09	\$17.14	\$17.28	(\$0.14)	\$15.09	\$16.18
<b>Mar-Dec 2008</b>	<b>\$17.22</b>	<b>\$17.29</b>	<b>(\$0.07)</b>		
<b>2009 Avg</b>	<b>\$17.04</b>	<b>\$17.31</b>	<b>(\$0.27)</b>		

- Lower cheese prices are generating an [increase in the demand](#) in the Midwest for cheddar headed to aging programs, according to Dairy Market News. Interest in hard Italian remains solid with good movement of fresh supplies in, and aged product out of inventory. Current American varieties are in limited spot supply, while interest remains good.
- Western cheese demand has started to improve as average prices have declined. Dairy Market News reports some cheese is available, but multi-load [offerings are not all that common](#). Supply and demand are in close balance.

#### What's Bearish:

- Milk Production Report: Adjusted for leap-year, February milk production in the U.S. was up 1.9% vs. a year ago, while cow numbers were [up 112,000 head](#). Milk per cow showed a 67 lb increase, and cow numbers were up 8,000 head from January.
- Grain prices. The current free-fall in grains is giving producers an excellent opportunity to cover their input costs. Further declines will aid profitability and encourage more milk production.
- Despite Dairy Market News telling us cheese stocks are somewhat tight, and a bullish Cold Storage Report, weekly cold storage holdings numbers show a [7% increase in cheese stocks](#) and 10% increase in butter stocks for the period 03/01 through 03/17.
- NASS surveyed prices for Class III components were mostly down this week. 40-lb blocks averaged \$2.00/lb, down 4.8¢, while 500-lb barrels fell 2.7¢ to \$1.97/lb. Nonfat dry milk lost 3¢ to average \$1.24 and dry whey have up 0.3¢ after two weeks of increases, to average 24.4¢/lb. Butter was the only star, gaining 7.9¢ to average \$1.28/lb.
- Balancing plants in the Northeast are [running on heavy schedules](#), according to Fluid Milk & Cream Review. Intakes are up as fluid sales drop due to various schools being off for Spring Break. Excess volumes, as well as milk making its way all the way from the West, is heading into Class III operations.
- Fluid Milk & Cream Review reports plant capacity in California continues to be "maxed out". Milk and components are still moving out of state to find a home. Production is trending higher in AZ and NM, with [little extra processing room](#) available. Plants are expected to be stretched over the holiday weekend.

#### Recommendation:

We could hardly watch milk prices this week as our eyes were glued to our flat screens watching about nearly every other commodity plummet. On one hand, we'd like to see higher trading volumes in Class III milk futures as it allows for more opportunities to trade with better liquidity. On the other hand, we've been largely avoided by professionally managed commodity funds, which began selling en masse in reaction to a smaller than anticipated fed rate cut and rebound in the U.S. dollar. We were thus spared (so far) the massive sell-off that affected everything from energy, to precious metals, to grains. The current crash in grains in the face of unchanged, bullish fundamentals, is in our opinion a great opportunity for dairies to get covered on their feed costs well in to 2009. Continue to watch for a bottom next week and then book your feed in 25% increments, taking advantage of further drops if they come. As far as milk, we were down for the week as there was some reaction to falling grain prices and a weak economy. The 2009 average lost 27¢ but probably got a little ahead of itself and needed a correction. We continue to hear some positives out there. A couple large cheese makers were offering \$1.80+ cheese contracts to their producers this week. Evidently they have customers who are looking to lock in their cheese price over fears of higher prices later. They might be right. The powder market is showing some signs of recovery, and USDA's estimate of 2.7% more milk, but 3.0% higher commercial use strikes us as supportive. Certainly buyers in the cash market were aggressive this week in the number of loads they were willing to pick up. But a strengthening dollar could hamper export demand, and a weak economy could slow domestic demand. Combine that with the volatility we're seeing in the other commodities and it looks like we could yet have a wild year. In light of the very real risks in the economy, exports and falling grain prices, we are putting out a **Trade Alert**. Buy the 15.25 PUT, May-Oct at an average price of 15¢ per month, the 15.50 PUT for an average of 19¢ per month, or the 15.75 PUT for an average of 24¢ per month. Pick your price point. Yes, it's a lot lower than selling outright, but with the huge market moves we're seeing in other markets, who's to say it won't happen in milk, up or down, too? For most producers that are getting a premium above Class III settlement, this will allow them to cash flow, while leaving 100% of their production open to (hopefully) higher prices later this year. It's time to stop sitting on your hands and leaving yourself 100% at risk to the whim of the market. This is cheap insurance. Call us next week to get something done.

**Note:** We will be closed tomorrow in observance of Good Friday. All U.S. markets are closed. We wish everyone a wonderful Easter celebration this weekend!

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