

**The KDM Dairy Report – April 11<sup>th</sup>, 2008**

**What's Bullish:**

- World Ag Supply & Demand Report: USDA reduced their 2008 milk production forecast in anticipation of slower growth in output per cow, caused by higher feed costs. As a result, they [expect tighter supplies of milk](#), and coupled with strength in both domestic and export commercial use, have raised their Class III price forecast 45¢/cwt from last month, to average \$16.80/cwt. USDA also upped their cheese price forecast 1¾¢ on tight supply issues.
- For the first week in April, weekly cold storage numbers are indicating a 3% drop in cheese stocks at USDA selected storage centers. A net 3.4 million lbs of cheese were [pulled from inventory](#).
- After being much higher earlier in the year, butter stocks at CME-approved warehouses are [approaching last year's levels](#). For the week ending 04/05, 120.9 million lbs were on hand, compared to 117.4 million lbs a year ago at this time.
- International sales of butter continue to be filled and additional buyer interest is still being reported, according to Dairy Market News. Butter exports for the first 2 months of 2008 totaled 13,067.3 metric tons, compared to only 1,018.7 metric tons during the same period in 2007, an [increase of 1,183%](#). Wow! Total butter exports in 2007 amounted to 32,917.7 metric tons.
- Cheese exports for the first 2 months of 2008 totaled 10.9 million lbs, up 4.4 million lbs (67%) from 2007, according to Dairy Market News. Cheddar cheese exports accounted for 8.6 million lbs, [up 205.8%](#) vs. a year ago.
- Fluid Milk & Cream Review reports growth in milk production in California is moderating as producers under base programs [sell cows](#) to remain at or under their base-level. Some of the cows are moving out of state.
- The Western dry whey [market is firm](#), according to Dairy Market News. Domestic and export accounts are actively trying to secure nearby and longer term needs, while Western whey output was down 9.1% in Feb.
- Cheese [demand in the Northeast is robust](#), according to Dairy Market News. Production is near capacity, but orders for low fat cheese varieties are strong.
- NASS cheese prices fell (see below), but other Class III [components were higher](#) this week. Butter increased 1.3¢ to average \$1.34/lb, nonfat dry milk bumped up 0.7¢ to \$1.25/lb and dry whey gained a penny to average 25.5¢/lb.
- International: In New Zealand, the lack of moisture during Jan and Feb caused irrecoverable losses in milk production. Some areas are reporting milk volumes [down as much as 40%](#) compared to last year as farmers were forced to adjust their milking cycles to once per day and to dry off cows earlier than usual. In Australia, better milk production in the second half of the season is narrowing the gap from last year's levels, but overall production is still estimated to be 5.8% below 2007. Production of manufactured dairy products is winding down, along with the milk production season, and traders comment there is basically nothing available to offer on a spot basis. Some indicate they will need to reach to outside sources to fulfill commitments of the current season.
- International: Milk sales within Australia are up 2.5% YTD, according to DairyAustralia. The increase in domestic demand makes less available for export. They also reported Jul-Feb total dairy exports were [down 19.9%](#) on a tonnage basis. Wow!

| Futures Month   | Friday 04/11 Close | Friday 04/04 Close | Change        | 5-yr Average | Top 3rd Price |
|-----------------|--------------------|--------------------|---------------|--------------|---------------|
| Apr-08          | \$16.70            | \$16.72            | (\$0.02)      | \$14.14      | \$15.36       |
| May-08          | \$17.20            | \$17.31            | (\$0.11)      | \$14.50      | \$15.85       |
| Jun-08          | \$18.12            | \$18.06            | \$0.06        | \$14.54      | \$15.63       |
| Jul-08          | \$19.05            | \$18.39            | \$0.66        | \$14.66      | \$15.57       |
| Aug-08          | \$19.39            | \$18.57            | \$0.82        | \$14.47      | \$15.40       |
| Sep-08          | \$19.55            | \$18.73            | \$0.82        | \$15.14      | \$16.02       |
| Oct-08          | \$19.16            | \$18.56            | \$0.60        | \$14.78      | \$15.58       |
| Nov-08          | \$19.20            | \$18.60            | \$0.60        | \$14.75      | \$15.73       |
| Dec-08          | \$19.20            | \$18.55            | \$0.65        | \$15.09      | \$16.18       |
| Jan-09          | \$19.20            | \$18.33            | \$0.87        | \$14.40      | \$15.24       |
| Feb-09          | \$19.05            | \$18.03            | \$1.02        | \$14.00      | \$14.69       |
| Mar-09          | \$18.80            | \$17.77            | \$1.03        | \$12.78      | \$13.50       |
| Apr-09          | \$18.61            | \$17.82            | \$0.79        | \$14.14      | \$15.36       |
| May-09          | \$18.50            | \$17.87            | \$0.63        | \$14.50      | \$15.85       |
| Jun-09          | \$18.53            | \$17.87            | \$0.66        | \$14.54      | \$15.63       |
| Jul-09          | \$18.56            | \$17.90            | \$0.66        | \$14.66      | \$15.57       |
| Aug-09          | \$18.60            | \$17.92            | \$0.68        | \$14.47      | \$15.40       |
| Sep-09          | \$18.71            | \$17.99            | \$0.72        | \$15.14      | \$16.02       |
| Oct-09          | \$18.55            | \$17.85            | \$0.70        | \$14.78      | \$15.58       |
| Nov-09          | \$18.54            | \$17.80            | \$0.74        | \$14.75      | \$15.73       |
| Dec-09          | \$18.60            | \$17.80            | \$0.80        | \$15.09      | \$16.18       |
| <b>Apr-Dec</b>  | <b>\$18.62</b>     | <b>\$18.17</b>     | <b>\$0.45</b> |              |               |
| <b>2009 Avg</b> | <b>\$18.69</b>     | <b>\$17.91</b>     | <b>\$0.77</b> |              |               |

**What's Bearish:**

- Cash Market: Block cheese managed to gain 2¼¢ from last Friday, but came well off its high mid week. Settlement today was \$1.83½/lb, which was down 5¼¢ for the session. Barrels were all over the place this week, trading as low as \$1.69, rising to \$1.81, then falling 6¢ in today's session to finish down ½¢ for the week. Both buyers and sellers

seemed motivated as 20 loads of blocks and 17 barrels exchanged hands. Butter, on the other hand, was very quiet. A total of 2 cars exchanged hands, with butter up 1¾¢ to settle at \$1.39/lb today.

- February fluid milk sales were [1.9% lower](#) than Feb 2007, according to Dairy Market News. Sales of organic whole milk, 1%, organic fat-reduced and butter milk increased, but sales of whole milk, flavored whole milk, 2%, skim and flavored fat-reduced milk all decreased.
- Fluid Milk & Cream Review reports balancing plants in the Southeast and Mid Atlantic areas are receiving more milk from regular suppliers as well as shipments from the Southwest. Florida exported 100 loads of milk this week, compared to 86 last week. Production is on the rise in the Northeast, aided by warmer weather. Plants are [running on heavy schedules](#) to maximize production of butter, butterfat products and nonfat dry milk, and to clear intakes. Bottler demand is uneven, while ice cream manufacturers are waiting for a sign that warmer weather has arrived before ramping up production.
- Current cheese interest in the Midwest is generally slower this week, according to Dairy Market News. Grilling season can't get started with the lingering cold weather, and process movement is sluggish from food service and retail. [Offerings are increasing](#) as cheese makers try to minimize inventory building, while there is some thought that offerings from Europe may increase as their cheese production builds seasonally in spring.
- There has been [some slowdown in exporting](#) Western cheese, according to Dairy Market News, and domestic buyers are more easily able to secure current and upcoming needs. Producers are in better inventory shape and able to cover projected orders.
- Spot loads of manufacturing milk in the Central region are going from -\$0.50 to -\$3.00 under class, according to Fluid Milk & Cream Review. Milk volumes are [well above a year ago](#) with some plants operating near capacity.
- Weekly dairy cow slaughter for the week ending 03/29 was [only 48,700 head](#), far below the 55,300 head culled during the same week a year ago.
- Average cheese prices were [down again](#) in this week's NASS survey. 40-lb blocks fell 4.2¢ to \$1.79/lb and 500-lb barrels lost 2.4¢ to \$1.79/lb.
- International: Heavy milk receipts at many plants in Western Europe are [challenging plant capacity](#), according to Dairy Market News. Handlers feel they may be in the peak as production has been strong and continues to expand.

### **Recommendation:**

It was an incredible week. The Apr-Dec avg gained 45¢/cwt while the 2009 averaged jumped 77¢ to \$18.69/cwt. That's huge! The Feb and Mar '09 contracts were up more than \$1/cwt for the week! We won't argue that these prices are not justified, we think they are. And we've been writing for months now about the potential for \$20+ milk (which we briefly hit this week) in the second half of the year. But we certainly did not expect this to happen in April! We had lots of calls this week inquiring what's going on and whether it's now time to sell some milk. We would hold off selling contracts here. While we will need to deal with our spring flush over the next 3-8 weeks, the bottom line is we just blew through some major resistance levels as far as price is concerned. Look at exports! Butter up more than 1000% with the two month total equal to 40% of ALL butter we exported in 2007. That's amazing. And cheese exports were much higher as well. We heard this week that domestic automotive sales in China for Q1 2008 were up 21%! Can you imagine that type of growth in the USA? It confirms the growing middle class and purchasing power of consumers in that country, who will not only be filling all those gas tanks (supporting the crude oil, ethanol, corn chain), but are adding protein to their diets in the form of more milk and cheese. There's a big world to feed and it's adopting more Western eating habits. We took a lot of jibes a couple weeks ago when mentioning the *possibility* of \$25+ milk – suddenly it's looking a whole lot more possible. So, what do you with this? Near term, May and June are vulnerable to our flush as well as higher output in Europe. Try to buy the May-June 17.25 PUT for 30¢ each. Then enter a long-term order to buy the 18.00 PUT, July-Oct for an average of 30¢ each. For milk you already have sold, there's the very real potential for a significant break in prices as we head into peak production. If/when that happens, you need to hustle and get some CALLs bought for the fall.

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