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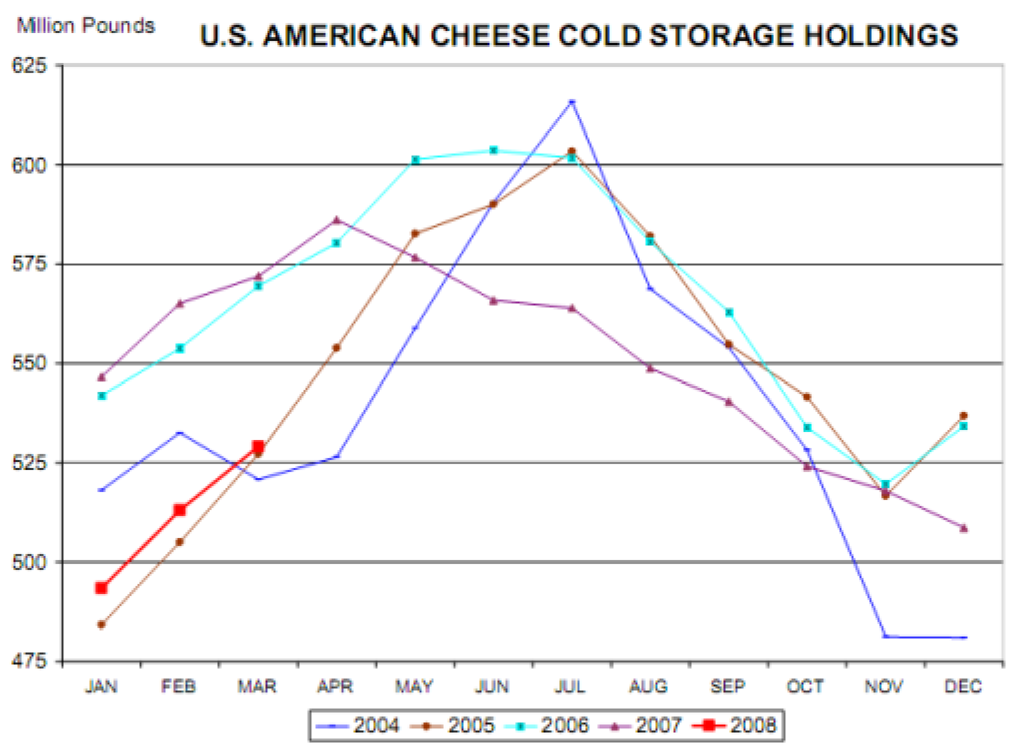
The KDM Dairy Report – April 25th, 2008

What's Bullish:

- Cold Storage Report: American cheese stocks in March were down 7% vs. a year ago, according to USDA, and Total cheese stocks were down 8%. However, butter stocks were up 17% vs. last year.
- Cash Market: Despite coming off mid-week highs, cash cheese finished up for the week, while butter made new highs for the year. Blocks were up 2¢ to settle at $1.92½/lb and barrels increased 4¢ to $1.88/lb. 5 loads of blocks and no barrels exchanged hands. Butter marched 2¢ higher to $1.41¼/lb on 3 trades.
- Weekly cold storage numbers are continuing to indicate a contra-seasonal drawdown in butter and cheese stocks. For the period 04/01 through 04/21, cheese holdings at USDA selected storage centers were down 3.9 million lbs, or 4%. Butter holdings declined by 1.3 million lbs, or 3%.
- NASS Class III components were mostly higher this week. Dry whey increased 0.8¢ to average 25.8¢/lb and nonfat dry milk was up 1.5¢ to $1.26/lb. Butter averaged $1.35/lb, up 0.3¢ from last week, while 40-lb block cheddar gained 3.4¢ to $1.83/lb. Barrels were the only loser, down 0.4¢ to $1.77/lb.
- After several slow weeks, dairy cow slaughter picked up its pace. For the week ending 04/12, 52,000 head were culled, compared to 49,400 during the same period a year ago.
- Northeast cheese plants are running strong, however, orders for reduced fat varieties continue to equal or surpass orders from previous years, according to Dairy Market News, and demand is good to improving for Italian-type cheeses.
- Current cheddar blocks remain in tight supply in the Midwest, according to Dairy Market News. Barrels are in better supply, but process interest is steady to improved, particularly in the fast food segment.
- Despite historically high prices, Western cheese buyers are not put off and continue to make regular purchases as needed, according to Dairy Market News. Small offerings continue to be available, but multi-load offerings are not. Domestic demand does not seem to be at all impacted by gyrating cheese prices.
- According to the Foreign Ag Service, imports of cheddar cheese during the first quarter were down 49% vs. last year, while butter imports were down 66% during the same period.

Futures Month	Friday 04/25 Close	Friday 04/18 Close	Change	5-yr Average	Top 3rd Price
Apr-08	$16.70	$16.74	($0.04)	$14.14	$15.36
May-08	$17.59	$17.78	($0.19)	$14.50	$15.85
Jun-08	$18.21	$18.55	($0.34)	$14.54	$15.63
Jul-08	$18.59	$19.33	($0.74)	$14.66	$15.57
Aug-08	$18.70	$19.62	($0.92)	$14.47	$15.40
Sep-08	$18.88	$19.77	($0.89)	$15.14	$16.02
Oct-08	$18.77	$19.47	($0.70)	$14.78	$15.58
Nov-08	$18.64	$19.51	($0.87)	$14.75	$15.73
Dec-08	$18.65	$19.45	($0.80)	$15.09	$16.18
Jan-09	$18.25	$19.40	($1.15)	$14.40	$15.24
Feb-09	$18.20	$19.14	($0.94)	$14.00	$14.69
Mar-09	$18.05	$19.05	($1.00)	$12.78	$13.50
Apr-09	$18.01	$18.90	($0.89)	$14.14	$15.36
May-09	$18.05	$18.85	($0.80)	$14.50	$15.85
Jun-09	$17.90	$18.86	($0.96)	$14.54	$15.63
Jul-09	$18.01	$18.84	($0.83)	$14.66	$15.57
Aug-09	$18.14	$18.90	($0.76)	$14.47	$15.40
Sep-09	$18.01	$18.97	($0.96)	$15.14	$16.02
Oct-09	$17.85	$18.67	($0.82)	$14.78	$15.58
Nov-09	$18.21	$18.63	($0.42)	$14.75	$15.73
Dec-09	$18.26	$18.66	($0.40)	$15.09	$16.18
Apr-Dec	**$18.30**	**$18.91**	($0.61)		
2009 Avg	**$18.08**	**$18.91**	($0.83)		



- As of April 20th, only 4% of the corn crop had been planted, compared to an average of 17% for that date. Forecasts for more cool and wet weather to come could continue to hamper planting in the Midwest.
- Milk production in California and Arizona is leveling off, according to Fluid Milk & Cream Review. CA producers are feeling the affects of the various base programs in place, with selling of cows and more aggressive culling being common. Excess milk is being priced at lower levels as those that produce above their base level bear the associated costs of marketing the milk. Processing plants in the state are running on steady to reduced schedules. In AZ, the peak has arrived, yet plants in the state are able to handle local milk and additional volumes from out of state. In NM, the haying season has been slow to develop due to cool weather and costs are up $20-30 per ton. Finally, in the Pacific Northwest, the spring flush has been slow to develop as the weather has been generally cool and wet.
- International sales are playing a major role in firming butter prices, according to Dairy Market News. Churning continues to occur for international orders already on the books, and potential new sales are being negotiated. Domestic demand is equally active, as buyers are procuring stocks for both immediate and future needs. Some buyers are wondering what the impact on butter availability will be this fall due to the volume clearing internationally now.
- Central dry whey prices were firmer this week, according to Dairy Market News. Production has been steady to stronger, but some manufacturers are curtailing offers to the spot market to reserve product for contractual fulfillment.
- International: The milk production season in Australia and New Zealand is coming to a close, and estimates are that production will be down vs. the prior year by 5% and 3% respectively, according to Dairy Market News. Farmers are drying off their herds earlier than usual, to focus on herd conditioning for the upcoming season. Dairy product availability is quite limited.
- International: European whey powder markets are firm, according to Dairy Market News. Cheese production is active, but some handlers are indicating whey supplies are lighter than desired.

What's Bearish:

- Livestock Slaughter Report: Dairy cow slaughter for the month of March was 215,100 head, down 6.6% from last March, when 230,400 head were culled. YTD dairy cow slaughter totaled 665,000 head, just slight ahead of last year at 660,000 head.
- Fluid Milk & Cream Review reports milk output in the Eastern region of the country continues to increase seasonally, but the peak may still be a few weeks away. Processing plants in many areas are running near capacity as more milk is now available due to sluggish Class I sales. Weather has been very favorable for com comfort. Cheese manufacturers have been using economically priced nonfat dry milk to boost cheese yields.
- International: Milk production is holding steady at high levels in Europe, according to Dairy Market News. Manufacturing schedules are running at near capacity levels, and stocks of dairy products are starting to build, with offerings available for both domestic and international buyer interest.

Recommendation:

Class III futures were decidedly lower this week as several contracts lost nearly a dollar or more. We stated the past two weeks that we thought prices went up too high too early. After losing momentum to the upside, sellers finally arrived in what were most likely producers, who had stayed on the sidelines for quite some time, establishing new hedges, and speculators taking profits from the recent run-up. It may be messy for awhile as we are entering spring peak production in much of the country, and reports about building dairy inventories in Europe are not conducive to higher prices near term. However, our long-term outlook has not changed, with the potential for much higher prices this fall. As we're seeing even now, CA production is hitting a ceiling due to the new quota programs and may start to drop as warmer weather arrives. World and domestic demand remain steady to improving despite higher prices for dairy end-products, while world stocks remain low. The current sell-off has us temporarily switching long-term strategies. We're not going to get those 18.00 PUTs we talked about for awhile, but this move lower does present an opportunity. For those that have already made marketing decisions on their milk, we would highly recommend buying 19.00 to 20.00 call options Jun-Oct. Premiums have fallen and may continue to fall next week. Take advantage of this! Also, remember to have a "big picture" attitude towards this move lower. Grit your teeth and hang on for the ride. This correction was really healthy and needed, in our opinion. Cheese feels a little heavy short-term, so continue to protect the front months with PUT options. Try to buy the June 18.00 PUT for 30-35¢, which will yield at $17.70 floor should prices continue to head down as we work through the flush.