

**The KDM Dairy Report – May 30<sup>th</sup>, 2008**

**What's Bullish:**

- Ag Prices Report: The milk to feed ratio in May fell to a [new record low](#) of 1.83, down from 1.89 in April and 2.54 a year ago. Historically, a milk-feed ratio below 3.0 discourages expansion as the cost of production goes up. However, futures prices above \$20/cwt should increase the ratio going forward.
- Outlook for U.S. Ag Trade Report: USDA increased their forecast for dairy exports for fiscal 2008 to a record \$3.7 billion. They site [stronger demand than expected](#) and tight global dairy supplies due to the drought in Oceania as causes.
- NASS cheese prices [continued to climb](#) in this week's survey. 40-lb cheddar blocks increased 3.6¢ to average \$1.99/lb while 500-lb barrels were up 5¢ to \$2.02/lb. Butter gained 3.1¢ to average \$1.46/bl, nonfat dry milk was up 2¢ to \$1.31/lb and dry whey increased 0.4¢ to 27.7¢/lb.
- Generic cheddar and natural American cheese [supplies remain tight](#) in the Midwest, according to Dairy Market News. Traders have commented how record high prices have slowed sales, but that a retreat back to \$2/lb would cause exporters to resume sales.
- Western cheese buyers are aggressively looking for any cheese available, even under grade supplies, according to Dairy Market News. Some fear an upcoming shortage and there are no additional supplies of cheese available in the region. [Anything produced has a waiting buyer](#) with

more interest than can be met. Factors contributing to the tight cheddar market were that production is down, stocks are down and exports are up.

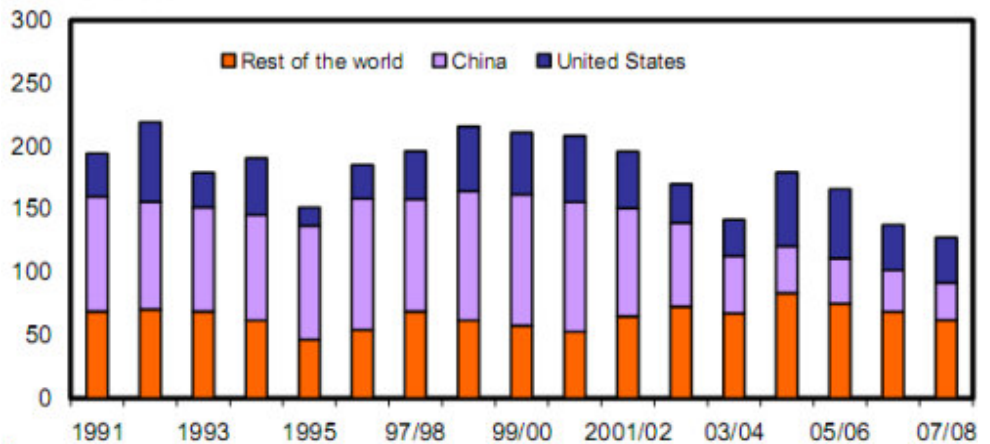
- The nonfat dry milk market remains firm, according to Dairy Market News. Interest slowed over the holiday weekend, but buyers returned by midweek. Production remains active to process seasonally heavy milk supplies, but many NDM buyers are [not getting all the loads](#) they would like to secure. Stocks are light with volumes committed to future export sales.

- Western dry whey prices were steady this week supply and demand remain in balance. However, contacts are watching [European whey prices firm](#) and wondering if this will have an impact on U.S. prices.
- Weekly dairy cow slaughter numbers were higher than a year ago for the [second week in a row](#). For the period ending 05/17, 44,100 head were culled compared to 42,200 head last year.
- Butter stocks at CME-approved warehouses fell by nearly 4 million lbs this week, compared to a 4.1 million lb increase during the same period a year ago. Total stocks are now at 130 million lbs, 12.7 million lbs [below last year's levels](#).
- According to the Foreign Ag Service, cheese imports in April were [down 32%](#) compared to a year ago, and Jan-Apr imports were down 18%.
- Butter imports in April were [down 70%](#) vs. last year, according to the FAS, and are at only 8% of the annual quota.

Futures Month	Friday 05/30 Close	Friday 05/23 Close	Change	5-yr Average	Top 3rd Price
May-08	\$18.18	\$18.19	(\$0.01)	\$14.50	\$15.85
Jun-08	\$20.15	\$20.88	(\$0.73)	\$14.54	\$15.63
Jul-08	\$20.43	\$21.42	(\$0.99)	\$14.66	\$15.57
Aug-08	\$20.48	\$21.25	(\$0.77)	\$14.47	\$15.40
Sep-08	\$20.55	\$21.16	(\$0.61)	\$15.14	\$16.02
Oct-08	\$20.16	\$20.79	(\$0.63)	\$14.78	\$15.58
Nov-08	\$20.00	\$20.68	(\$0.68)	\$14.75	\$15.73
Dec-08	\$19.95	\$20.59	(\$0.64)	\$15.09	\$16.18
Jan-09	\$19.65	\$19.85	(\$0.20)	\$14.40	\$15.24
Feb-09	\$19.05	\$19.20	(\$0.15)	\$14.00	\$14.69
Mar-09	\$19.02	\$19.20	(\$0.18)	\$14.55	\$15.28
Apr-09	\$18.72	\$18.90	(\$0.18)	\$15.61	\$16.83
May-09	\$18.73	\$18.90	(\$0.17)	\$14.50	\$15.85
Jun-09	\$18.76	\$18.90	(\$0.14)	\$14.54	\$15.63
Jul-09	\$18.74	\$18.90	(\$0.16)	\$14.66	\$15.57
Aug-09	\$18.80	\$18.95	(\$0.15)	\$14.47	\$15.40
Sep-09	\$18.97	\$19.00	(\$0.03)	\$15.14	\$16.02
Oct-09	\$18.78	\$18.76	\$0.02	\$14.78	\$15.58
Nov-09	\$18.70	\$18.61	\$0.09	\$14.75	\$15.73
Dec-09	\$18.73	\$18.66	\$0.07	\$15.09	\$16.18
<b>May-Dec</b>	<b>\$19.99</b>	<b>\$20.62</b>	<b>(\$0.63)</b>		
<b>2009 Avg</b>	<b>\$18.89</b>	<b>\$18.99</b>	<b>(\$0.10)</b>		

**Coarse grain ending stocks**

Mil. metric tons



- Hay supplies are very tight in the Southwest and Pacific Northwest, according to Fluid Milk & Cream Review. Hay buyers are [calling on a daily basis](#) to find out when some will become available as they are close to running out. Some are hoping for some CRP acres for haying and grazing, because, "every little bit will help". Cost for hay delivered ranges from \$235-255/ton.
- Grains: As of Tuesday, corn is 88% planted compared to the 5-year average of 94%, but the percent emerged is quite a bit [lower at 52%](#), compared to an average of 76%.
- Grains: USDA released it's annual Feed Yearbook report this week, showing the despite higher production, world coarse grain ending stocks in 2007/08 will be at their lowest levels in more than 30 years (see chart above).

### What's Bearish:

- Cash Market: Cheese prices slipped this week after setting record highs last week, but did recover some lost ground on Friday. Blocks lost 5½¢ to settle at \$2.23/lb while barrels fell 5¢ to \$2.20/lb. Trading was light as only 4 blocks and 5 barrels exchanged hands for the week. Butter lost 1¢ to close at \$1.48, coming off a low of \$1.47 mid-week. 14 cars of butter exchanged hands.
- Commercial Disappearance: Commercial use of American cheese in March was [down 1.4%](#) compared to a year ago, and down 2.3% for other-than-American varieties. However, user of butter was up 17.8%, use of nonfat dry milk up 16.5% and use of milk in all products increased a small 0.1%
- Milk [supplies are heavy to burdensome](#) in the Central region, according to Fluid Milk & Cream Review. Class I interest is down due to school closings and high milk prices affecting sales. Spot loads of milk for manufacturing are going for \$1.50 to \$4.50 below class, and handlers are getting calls to see if any plant capacity has opened up.
- The current strength in North Eastern milk production combined with school closings is [causing some concern](#) as to whether regional processing capacity will be able to handle milk receipts. Fluid Milk & Cream Review reports balancing plants are handling intakes so far, but lighter needs for foodservice milk could change that. Balancing plants in the Southeast continue to run at capacity to handle both regular and outside milk loads, while milk production is steady.
- Weekly cold storage stats continue to reflect a [buildup of cheese](#) at USDA selected storage centers. For the period 05/01 through 05/26, cheese stocks increased 11%, or 11.3 million lbs. Butter stocks, however, fell by 10%, nearly 4 million lbs.
- Churning activity was heavy over the Memorial Day weekend, according to Dairy Market News, and the market felt weaker. Both international and domestic buy [interest has been slow](#) as inventory levels are assessed and lower prices slow order placement.

### Recommendation:

Where we go near term from here is anyone's guess. Some are predicting \$1.90 cheese, but \$2.00 at this time looks like a pretty good floor considering what appears to be a tight cheese market. Cheese producers are not likely to increase production and put product in storage at current prices, which should propagate the "make to order" policy they have now and keep offerings on the lean side. Bidders on Friday pushed cheese 2¢ higher, indicating they are still there as well. Long-term, things still look well supported. Highlighting the international picture once again was USDA's increased forecast on dairy exports and report on world grain stocks. We also came across a compelling article this week in the business section of The Australian, writing about the business opportunity for Australian dairymen as China's middle class expands. Several quotes are below. You can read the full article [here](#).

- *Over the next five, 10, 20 years the demand will increase incredibly.*
- *The middle class now is about 250 million. That will move to about 400 million to 500 million by 2010 and easily about 600 million by 2020.*
- *Once people start eating better, that is one thing they never stop.*
- *We have less milk to export, but the world market is very short of products.*
- *The two top dairy exporters are New Zealand and the EU and both have faced limitations. There was a pretty poor season last year in Argentina, a drought in New Zealand this year, and the EU is capped by quotas still. You have all these major suppliers that haven't been able to grow milk supply. Only the US has been able to grow its milk production.*
- *Cheese consumption in China is moving strongly. The figures are daunting. We are looking at 50,000 tonnes total consumption. They import about 7000 tonnes. They are going to be moving to about 180,000 tonnes of demand. Imports are going to move to about 40,000 tonnes. They are just not going to be able to increase production.*
- *This is not going to abate. You are not going to get the Chinese eating less. Agricultural prices have been undervalued for some time.*

Do you want to sell milk in 2009/10? Not us. Keep your orders in for 18.00 to 19.00 PUTs for the balance of 2008.

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