

The KDM Dairy Report – December 24th, 2008

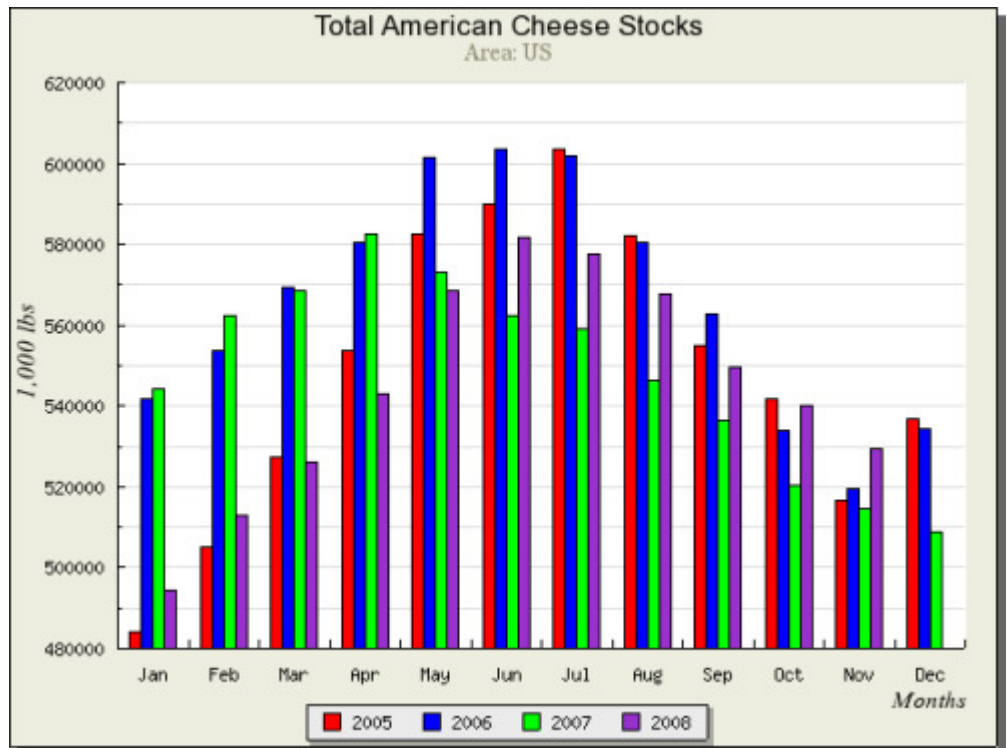
What's Bullish:

- Dairy cow slaughter for the week ending 12/13 was above 50,000 for the second straight week. 52,300 animals were culled.
- Butter stocks at CME-approved warehouses stand at 34.8 million lbs, 30.7 million lbs less than a year ago, when stocks totaled 68.5 million lbs.

What's Bearish:

- Cash Market: In the shortened holiday week, spot cheese managed to lose more ground. Blocks fell 3¼¢ since last Friday to settle at \$1.27/lb and barrels dropped 4¾¢ to \$1.30¾/lb. Buyers were willing to take on more product at these levels, picking up 13 loads of blocks but no barrels. Butter gave up 3¢ to settle at \$1.14/lb on just 1 trade.
- Cold Storage Report: American cheese stocks on the 30th of November were up 2% compared to a year ago, according to USDA. Monday's Daily Dairy Report stated this was the most American cheese ever for this date (see graph). Total cheese stocks were also up 2% vs. last year, however, butter stocks were down 16% over the same period.
- Weekly cold storage stats continue to reflect a growing cheese buildup. Cheese stocks for the period 12/01 through 12/22 are now showing a 12% increase, up from 10% last week.
- 357 loads of milk were shipped out of the Southeast this week, up 276 loads from just 81 last week, according to Fluid Milk & Cream Review. Slow retail sales and school closing are accounting for the surplus and balancing plants in the region are struggling to handle all the milk. There is legitimate concern that some milk may have to be dumped, even though manufacturing capacity is operating at maximum levels.
- Surplus milk and cream volumes are sharply higher in the Central region this week, according to Fluid Milk & Cream Review. Spot loads of milk are selling for \$5-6 under class but are still having a hard time finding a home. Plants are running on extended schedules, but silos are filling up, so rolling storage tankers will be needed to handle the extra volumes. Handlers are saying that this is probably as bad a holiday backup as they have seen in years, and that some milk may be dumped due to lack of manufacturing capacity.
- Fluid Milk & Cream Review reports that milk and components are moving out of California to find homes. Production is about steady, but limited bottled milk demand has made handling the milk supply challenging. In Arizona, processing plants are full and expected to stay that way over the next several weeks, with no ability to handle additional surplus milk. Plants in New Mexico are full to overfull and are working hard to help balance the milk supply. Bottlers have cut orders so the need for Class I milk has slowed. Cream offerings are heavy and stretching the capacity to handle. In the Pacific Northwest, heavy snowfall has

Futures Month	Wednesday 12/24 Close	Friday 12/19 Close	Change
Dec-08	\$14.97	\$15.02	(\$0.05)
Jan-09	\$11.56	\$11.96	(\$0.40)
Feb-09	\$11.56	\$12.06	(\$0.50)
Mar-09	\$11.93	\$12.23	(\$0.30)
Apr-09	\$12.49	\$12.61	(\$0.12)
May-09	\$12.70	\$12.86	(\$0.16)
Jun-09	\$13.09	\$12.96	\$0.13
Jul-09	\$13.68	\$13.50	\$0.18
Aug-09	\$14.25	\$14.08	\$0.17
Sep-09	\$14.68	\$14.37	\$0.31
Oct-09	\$14.75	\$14.48	\$0.27
Nov-09	\$14.73	\$14.50	\$0.23
Dec-09	\$14.69	\$14.40	\$0.29
Jan-10	\$14.40	\$14.35	\$0.05
Feb-10	\$14.42	\$14.40	\$0.02
Mar-10	\$14.40	\$14.44	(\$0.04)
Apr-10	\$14.54	\$14.54	\$0.00
May-10	\$14.73	\$14.73	\$0.00
Jun-10	\$14.94	\$14.94	\$0.00
2009 Avg	\$13.34	\$13.33	\$0.01
Q1Q2 2010	\$14.41	\$14.40	\$0.01



impacted milk routes and some milk has been dumped, however, plants are running as full as they want to be, processing milk from as far away as California.

- Western butter buyers have all their holiday needs covered and have little interest in owning any additional butter at this time, according to Dairy Market News. With current heavy production and slow domestic and export sales, contacts believe butter stocks will not begin to build rapidly. Cream offerings are heavy and expected to get worse in the next two weeks.
- Cheese supplies exceed the current demand in the Midwest, according to Dairy Market News. Interest is very light as most buyers are on vacation, while others are waiting until January to make further purchases. Cheese returning from planned exports is also growing the supply, as is heavier production as surplus milk backs up over the holidays.
- Western cheese buyers are in no hurry to make additional purchases, according to Dairy Market News. Holiday sales are covered, so buyers are waiting for price averages to fall in line with recent declines in the cash market.

Recommendation:

It appears as though there was a dramatic slowdown in cheese orders from mid-October through November, as American cheese stocks over this period climbed to a new record level, according to the November Cold Storage Report. The slow down in the economy and uncertainty over holiday cheese sales has buyers very nervous, and unwilling to take on more product. Suddenly the spigots closed on sales and as we've seen, it does not take long for excess volumes to show appear. Sellers in the cash market have had their way, and to emphasize their convictions, we saw multiple 10 or 15 lot offers of cheese this week. There is still a lot of disbelief out there that prices can go much lower, but it is very possible. Jan and Feb both settled at about \$11.70, but plugging in today's cash numbers calculates to \$10.88 Class III, so amazingly, they are still trading quite a premium to cash. The short-term future does not look bright, but take a look at what the June-Dec contracts did this week; up double digits! Whether it comes to pass or not, the market is predicting a shorter period of pain than we've experienced in previous low milk markets. Also encouraging is the long-term outlook for dairy, which we believe is still bright. The population of the world is not decreasing. When the world's economies finally begin to recover, demand for protein will too, especially in Southeast Asian countries. With New Zealand land-locked and limited to some extent on how much more milk they can produce, the U.S. will be in a great position to be a major global dairy supplier when that time comes. We're seeing first hand how a quick drop in demand can squash prices; the opposite is also true. Producers who have sold milk at higher prices should continue to work to get call options purchased for the second half of the year. If the uptrend in the last half continues, call options will not get cheaper. Get protected!

On an administrative note, MILC program signup began on 12/22. You should contact your local FSA office to get signed up and if you are a larger producer, to choose which months you want to participate in. We would suggest starting with Jan if you can take multiple months, or perhaps select Feb if your entire 2.4 million lbs of production falls in a single month.

Lastly, on behalf of KDM Trading, Inc., we want to sincerely wish you all a very Merry and Blessed Christmas! Our offices will be closed until Monday, Dec.29th



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