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The KDM Dairy Report – March 20th, 2009

What's Bullish:

Futures Month	Friday 03/20 Close	Friday 03/13 Close	Change
Mar-09	$10.51	$10.31	**$0.20**
Apr-09	$11.41	$10.87	**$0.54**
May-09	$11.96	$11.07	**$0.89**
Jun-09	$12.68	$11.86	**$0.82**
Jul-09	$13.78	$12.99	**$0.79**
Aug-09	$14.91	$13.96	**$0.95**
Sep-09	$15.47	$14.47	**$1.00**
Oct-09	$15.94	$14.80	**$1.14**
Nov-09	$16.10	$14.98	**$1.12**
Dec-09	$16.05	$15.05	**$1.00**
Jan-10	$15.90	$15.09	**$0.81**
Feb-10	$15.50	$15.09	**$0.41**
Mar-10	$15.55	$15.05	**$0.50**
Apr-10	$15.57	$15.10	**$0.47**
May-10	$15.55	$15.10	**$0.45**
Jun-10	$15.55	$15.15	**$0.40**
Mar-Dec	**$13.88**	**$13.04**	**$0.84**
Q1Q2 2010	**$15.65**	**$15.08**	**$0.57**

- Milk Production Report: February milk production was up just 0.6% in all 50 states, down from a 1.1% adjusted increase in January. Cow numbers fell 18,000 head from Jan, and are up only 11,000 head from a year ago. Milk per cow fell in all but 3 of the 23 biggest milk producing states. Output in CA was down 2.5% due to a 90-lb drop in milk per cow and decrease in the herd of 16,000 cows.
- Livestock Slaughter Report: Feb dairy cow slaughter totaled 243,500 head up 29,200 head from a year ago, a strong 13.6% increase. Jan-Feb combined, 2009 is ahead 74,600 head compared to last year, or an increase of 16.6%.
- Livestock, Dairy & Poultry Outlook Report: Lower dairy product prices have prompted stronger-than-projected domestic use and tighter supplies, according to USDA. As a result, price forecasts have firmed compared with earlier USDA forecasts. USDA also expects the cow herd to decline 1.3% in 2009.
- Butter and powder increased in this week's NASS survey. Butter jumped 1.2¢ to average $1.13/lb, nonfat dry milk was up a marginal 0.1¢ to 82¢/lb and dry whey was up 0.3¢ to 16.5¢/lb.
- Culling was strong again in this week's cow slaughter report. For the week ending 03/07, 60,500 head left the milking herd, compared to 53,100 during the same period a year ago. YTD the dairy cow cull is ahead of last year by 106,000 head.
- Fluid Milk & Cream Review reports contacts in California are not expecting much of a flush this year. Output has been flat despite ideal milking conditions, but culling has been aggressive, with cow numbers trailing last year by 16,000 in this week's Milk Production report. Dairy quality hay has dropped from $210-225 a year ago, to $115-125. But sales have been much lighter as dairymen are not willing or able to pay.
- Dairy Market News reports Central butter producers indicating cream supplies have tightened, especially during the week. Butter orders have been very good in recent weeks, and future orders are not significantly lighter. Retail sales remain strong due to favorable prices.
- Western contacts are indicating that butter sales are excellent for this time of year, according to Dairy Market News. Churning is not quite as heavy this week because of less cream being available, due to increased demand from ice cream and cream cheese manufacturers.
- Central dry whey prices edged higher again this week, according to Dairy Market News. Market sentiment points to slow, continued firming in the near term. Buyer orders have increased over the past few weeks, and this has thinned holdings in the region. Some facilities are even below what is needed to comfortably offer any product into the spot market.
- Dairy Market News reports both domestic and export buyers are looking for additional volumes of Western dry whey. Prices are not being discounted any longer and more is being sold at premiums. Production is steady to lower, and any stocks at the producer level are being held with confidence.
- Eastern dry whey prices are firming as potential customers face having to work hard to find it. Dairy Market News reports a significant percentage of Eastern dry whey production is already committed under contracts, and the remaining volume available on spot markets is relatively small. Some producers are currently sold out and report receiving multiple inquiries seeking spot purchases, however, they are mostly left unfilled.
- Western nonfat dry milk that had to be discounted heavily a few weeks ago has now all been cleaned up, according to Dairy Market News. Some contacts are surprised that this is occurring just as the Spring flush hits much of the country, but offerings of powder from other regions are tighter as well.
- Dairy Market News reports Central nonfat dry milk prices were slightly higher this week, driven by tightening supplies. Production schedules have been trimmed back from full capacity as more milk is needed to satisfy higher bottler demand this week. Class I sales have been boosted as several retailers offered sub $2.00 per gallon, spurring mid week restocking demand. Inventories are not considered burdensome and in some cases, production is sold almost as fast as it can be produced.
- Demand for Italian cheese varieties continues at high levels in the Eastern region, according to Dairy Market News. Production is up to meet current demand, which has been enhanced by widespread retail promotions for brand and private label cheese. Expectations of increases in future milk prices is also motivating buyers to add inventory now. Manufacturing demand for harder cheese that can be stored for a longer time, is also high.

- Barrel offerings in the Midwest are minimal, according to Dairy Market News. Buyers have cleaned up most supplies when prices started to rise. Process interest is steady to improved as demand typically improves with warmer weather.
- Dairy Market News reports Western cheese buyers are aggressively looking for additional loads as the market has moved higher. Under grade cheese is cleaned up, and most demand is centered on cheese for current use, although some is going into storage for later use.
- International: Traders and handlers in Europe continue to report slow and unaggressive sales activity, according to Dairy Market News. However, reports indicate buyers are returning to the marketplace and are questioning supply availability and price levels. Traders and handlers feel that these inquiries will continue to increase as buyers realize that international supplies in other markets are no longer available.
- International: Renewed cheddar interest in Oceania is creating a more comfortable supply situation than just a few weeks ago, according to Dairy Market News. Prices are steady to up slightly as the milk production season winds down.

What's Bearish:

- Cash Market: Blocks jumped 4¼¢ for the week to close at $1.29¼/lb. But barrels, which had been up 5¼¢ for the week, gave it all back and then some on Friday, finishing at $1.29¾/lb, a loss of 2¢ for the week. Buyers were aggressive every day, picking up 22 loads of blocks and 12 barrels. Butter lost ¼¢ to close at $1.18¼/lb on very light trading of 2 loads.
- Cold Storage Report: Stocks of American cheese in February were up 13% compared to last year and up 5% from Jan. Total cheese stocks were up 11% in vs. last Feb and up 3% from Jan. Butter stocks were down 2% vs. 2009 but up 17% from Jan. Not sure what to make of this when reading about aggressive cheese buyers and tight cheese supplies around the country. It doesn't jive. One possible explanation for both is that cheese buyers were aggressively putting product in storage in Feb due to the very low price, for use later in the year when prices would be higher.
- Plants in the Southeast are coping with intensified milk receipts due to schools being on Spring break, according to Fluid Milk & Cream Review. Plant operators in the area also note there has been little evidence of herd culling reducing milk intakes. Florida shipped out 200 loads of Grade A milk this week, unchanged from last week and up from only 66 a year ago.
- Dairy Market News reports lead times on new bulk cheese orders in the Midwest are getting shorter. They also report a number of plants are again starting to have a little extra inventory to move.
- Despite recent gains in both the cash market and NASS survey, cheese prices were lower this week; a strange occurrence. 40-lb blocks dropped 3¢ to average $1.22/lb and 500-lb barrels fell 2.7¢ to $1.23/lb.

Recommendation:

Wow! We said last week's report was bullish, but certainly didn't expect the markets to rocket this week like they did. What's behind it? A lot of things. On Wednesday, the Fed announced they would be buying $300 billion of Treasurys to help support the economy and spur lending. That caused the U.S. dollar to make its biggest one-day drop since 1985, while the Euro and other currencies rallied. Fears of inflation due to the weak dollar had just about every commodity from crude oil to cotton up yesterday, as fund managers and investors poured money into commodities as a hedge against inflation. Within dairy, many were still holding short positions and taking a licking. As prices moved steadily higher on Thursday, the cash market made a strong move up, which put buyers in a frenzy. Most of the front months finished limit up 75¢. Finally, despite the dour economic picture, domestic demand for milk and cheese has been solid; even above expectations. As families have traded down from fine dining to fast food and more in-home meals, more fluid milk and process cheese is being consumed. With no new barrel plants having been built in the past several years, manufacturing capacity is somewhat fixed, leaving barrels tighter than blocks across the country. The inverted block / barrel spread may stick around for awhile. Reports on the powder markets were also encouraging this week, with multiple references to supplies beginning to get tight and prices firming. Internationally, market news this week sounded somewhat supportive, with reports of more buyer interest over a range of products. On Friday, the cash market gave back some of its gains, and Class III futures finished lower, but they did not give back even half of Thursday's gains. Impressive. This leads us to believe that long term we're still going to head higher. With cow numbers in Feb up only 11,000 head from last year, we would expect the March or April production reports to reflect cow numbers below a year ago. That should support our back months. So, what to do. If cheese buyers come back next week, the front months may overheat to the upside. Buy PUT options May-July to protect the downside. We would still leave the last half of the year open, as we believe the long term trend is up.