

The KDM Dairy Report – April 24th, 2009

What's Bullish:

- Livestock Slaughter Report: 762,500 dairy cows exited the milking herd in March, up 10.7% from a year ago (see graph below). Jan-Mar, 762,500 head were culled, 14.7% higher than the same period a year ago.
- Dairy Market News reports a major Midwestern butter producer announced the closing of a Wisconsin butter plant this week. Printing has not declined as much as expected since holiday orders were shipped, while at the same time, producers are trying to build inventory for use later in the year. Producers feel that future pricing for butter will be near current levels or higher, so stock generated at this time will be price competitive when removed from inventory.
- Central dry whey producers are getting calls from new potential customers from both the East and West coasts, according to Dairy Market News. Product is becoming more difficult to attain, with premiums over the market moving incrementally higher.
- Western whey prices continue to increase as buyers are often not able to get all the product that they need in a timely fashion. Dairy Market News reports sellers are struggling to keep up with orders, and inventories range from tight to short of full needs. In addition, exporters are taking good volumes of product.
- Dairy Market News reports Northeast dry whey inventories are short to tight, and producers are breaking up contracted loads into smaller sizes to keep buyers supplied on an interim basis. Prices are higher on a firming market.
- At the 2009 National Dairy Leaders Conference held this week in Colorado, Dan James, V.P. commercial lending at Mountain Plains Farm Credit Services, said

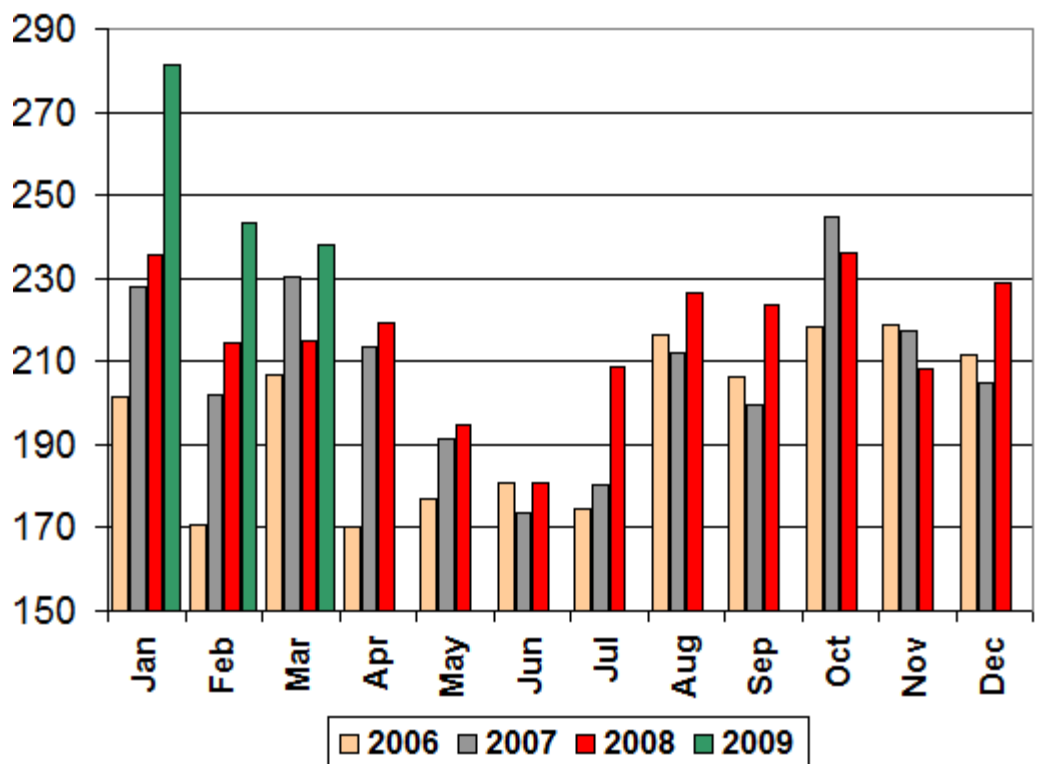
there are difficult times ahead. Many Western dairies have lost \$300-450 per cow for the first quarter, with second quarter losses expected in the \$200-300 range. Losses for the first half of the year could add up to \$500-750 per cow, leading to his comment that some dairymen and lenders will be forced to make some very difficult and painful business decisions in the next few months. While the human tragedy side of this story is sad, the potential for milk prices to recover in the last half of the year will be greater should more operations go out of business.

- Economy: Durable goods and new home sales were better than expected in March, raising hopes that the long slides in manufacturing and housing are coming to an end.

- International: At the "Australia and New Zealand Dairy Co-operative Leaders Forum" held this week in Melbourne, delegates heard that the long-term outlook is bright for dairying and that the current challenges are temporary. With a world population expected to increase 50% by 2050, the dairy industry has a huge opportunity to feed hundreds of millions out of malnutrition.

Futures Month	Friday 04/24 Close	Friday 04/17 Close	Change
Apr-09	\$10.77	\$10.76	\$0.01
May-09	\$10.20	\$10.31	(\$0.11)
Jun-09	\$11.28	\$11.44	(\$0.16)
Jul-09	\$12.73	\$12.56	\$0.17
Aug-09	\$14.00	\$13.85	\$0.15
Sep-09	\$14.73	\$14.54	\$0.19
Oct-09	\$15.20	\$14.94	\$0.26
Nov-09	\$15.20	\$14.96	\$0.24
Dec-09	\$15.21	\$15.02	\$0.19
Jan-10	\$15.33	\$15.11	\$0.22
Feb-10	\$15.40	\$15.09	\$0.31
Mar-10	\$15.45	\$15.20	\$0.25
Apr-10	\$15.72	\$15.57	\$0.15
May-10	\$15.75	\$15.68	\$0.07
Jun-10	\$15.84	\$15.77	\$0.07
Apr-Dec Q1Q2 2010	\$13.26	\$13.15	\$0.10
	\$15.39	\$15.13	\$0.26

Dairy Cow Slaughter (in 1000's)



What's Bearish:

- Cash Market: Blocks gained a penny for the week, settling at \$1.18/lb, but barrels lost ¼¢ to close at \$1.10¾/lb. In addition, sellers didn't allow exuberant buyers to gain much headway, forcing them to take on 29 loads of blocks and 13 barrels for the week. Butter ticked 2¢ higher to close at \$1.22¼/lb on 22 trades.
- Cold Storage Report: American cheese stocks in cold storage were up 7% in March, compared to a year ago, and total cheese stocks were up 8%. Butter stocks were down 4% over the same period, but up 5% from February.
- Cheese stocks are up 5% for the first 20 days of April, according to USDA weekly cold storage numbers. Holdings increased 5.4 million lbs over the period.
- 500-lb barrels averaged \$1.25/lb in this week's NASS survey, down 4.9¢ from last week. 40-lb blocks were up just 0.1¢ to \$1.28/lb, butter increased 1.6¢ to \$1.17/lb and dry whey pushed 0.8¢ higher to 20.2¢/lb. Nonfat dry milk decreased 0.1¢ to 82¢/lb.
- For the second week in a row, weekly dairy cow slaughter was behind last year's numbers. For the week ending 04/11, 49,400 head were culled, compared to 52,000 during the same period in 2008. Farmers could be holding off due to bidding in the CWT program.
- Fluid Milk & Cream Review reports milk volumes are running strong in the Northeast, with peak levels still a few weeks away. Manufacturing plants are running on heavy schedules to handle the milk. Class I demand remains strong as most schools are back in session following spring break, however, by mid May, schools will start to recess for the summer and milk will start to back up.
- Milk processing plants continue to run full in California, according to Fluid Milk & Cream Review. Green chopping is common in the Central Valley, boosting milk output as well as cheapening feed costs and the need to buy as much hay. Culling has been modest as producers assess the CWT herd kill program to see if their bids get accepted.
- Demand for Western nonfat dry milk has slowed as many buyers are comfortable with holding some stocks and aware that the market is in a surplus state. Dairy Market News reports shipments continue to clear to the CCC at the support price, while export shipments have slowed and only limited, spotty new interest developing. Production, however, remains active with plants running full.
- Dairy Market News reports most Northeast Class III plants are running at or near capacity production levels. Wholesale cheese prices are markedly lower following declines in the cash market.
- Midwest cheese is available, with traditional natural varieties like mild cheddar the most plentiful, according to Dairy Market News. Lack of financing to purchase product for aging programs has hindered some would-be buyers. Lead times are steady to shorter for new orders.
- Western cheese demand has slowed since the recent holidays, according to Dairy Market News. Contacts are expecting that when prices begin to cycle higher again, buyers will reenter the market, but until then are waiting for weekly average pricing to drop further.

Recommendation:

Last week we said that while bullish long term, the milk production report did nothing to fix the today's problems. On Monday, we had none of the fireworks we promised, but on Tuesday, prices across the board rocketed higher as block buyers in the cash market aggressively bought 25 loads. But just like fireworks, they didn't last long, and on Wednesday's spot session, when everyone expected both sides to do battle again, nothing happened. They didn't show up Thursday or Friday either, and as a result, the front months sold off their premium in a hurry. It certainly was an opportunity to sell the front months. We still have plenty of cheese, as evidenced by cash sellers, USDA's weekly cheese updates and our contacts in the industry. Tuesday's "mega buy" could simply have been commercial interests restocking, knowing that they had little downside left in cheese prices with barrels just a penny above support. Why not buy as much as you can now at fire sale prices and sell it later in the year? Domestic demand appears to be good, but we still have too many cows and too much milk left over from supplying the strong export market of a year ago. More cows need to be removed, and with the current cash price working out to about \$9.70 milk, we could see May below \$10, June below \$11 and July below \$12, unless cash buyers are able to move prices higher, soon. If we have any hope of recovery for the second half, low prices now is what we need to entice enough operations to exit the business via CWT or banker. We do have several rough months ahead, but we are still unapologetically bullish long-term. Dry whey continues to strengthen and there are a few signs the economy could be putting in a bottom. We remain very concerned about the possibility of wide-spread commodity inflation. With our government printing money as fast as it can, the value of the dollar could continue to weaken. Then if our economy starts to rebound, watch out! Everything from crude oil to grains to milk could go for quite a ride. As seen in the weekly price summary, despite the drop off in the front months, the back months continue to gain, and at a quicker pace. For those of you who have milk sold \$15-18 in the second half of the year, we would use any correction in the market to get call options purchased to cover your upside risk.

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