

**The KDM Dairy Report – May 1<sup>st</sup>, 2009**

**What's Bullish:**

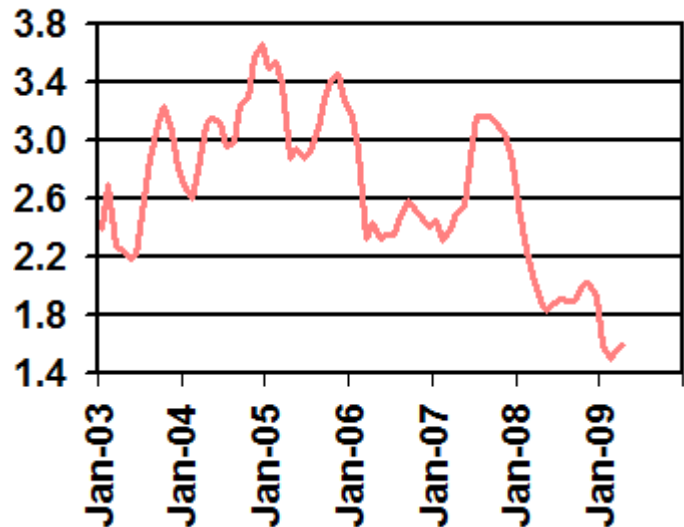
- Ag Prices Report: April's milk-feed ratio remained near historic lows at 1.59, up just slightly from March, which was revised to 1.57. A ratio below 3.0 discourages herd and milk production expansion.
- Plants in the Pacific Northwest are not seeing as much milk as anticipated, according to Fluid Milk & Cream Review. Continued financial stress is cited as the main reason, with the spring flush very slow in building. Plants are having no problems handling the milk this spring. Contacts we were in touch with this week mentioned some plants in the NW are running only 4-5 days due to less milk, with some plants in Idaho running under 50%. They are concerned about the effects CWT might have on their already dwindling milk supply, and if they'll be able to cover all the orders coming in for powder.
- Western dry whey production is even to short of anticipated levels, according to Dairy Market News. Supplies remain tight, keeping prices firm, but some price resistance is noted.
- Northeast dry whey prices were stronger this week as the market remained firm. Dairy Market News reports production is heavy, yet there were still instances of delayed contract shipments.
- International: Dairy exporter giant Fonterra has forecast its dairy exports to China are set to triple this year, in the wake of last year's melamine scandal. Consumers in China have lost faith in domestic products and are turning to what as seen as reliable imports.
- Economy: There are small signs the economy may be coming back to life. While the auto sector remains a wreck, consumer sentiment in April made its biggest one-month jump since October 2006.

Futures Month	Friday 05/01 Close	Friday 04/24 Close	Change
May-09	\$9.94	\$10.20	(\$0.26)
Jun-09	\$10.65	\$11.28	(\$0.63)
Jul-09	\$12.15	\$12.73	(\$0.58)
Aug-09	\$13.30	\$14.00	(\$0.70)
Sep-09	\$14.05	\$14.73	(\$0.68)
Oct-09	\$14.68	\$15.20	(\$0.52)
Nov-09	\$14.79	\$15.20	(\$0.41)
Dec-09	\$14.82	\$15.21	(\$0.39)
Jan-10	\$15.00	\$15.33	(\$0.33)
Feb-10	\$14.99	\$15.40	(\$0.41)
Mar-10	\$15.18	\$15.45	(\$0.27)
Apr-10	\$15.45	\$15.72	(\$0.27)
May-10	\$15.50	\$15.75	(\$0.25)
Jun-10	\$15.75	\$15.84	(\$0.09)
May-Dec	\$13.05	\$13.57	(\$0.52)
Q1Q2 2010	\$15.06	\$15.39	(\$0.34)

**What's Bearish:**

- Cash Market: Buyers continue to be on the defensive as sellers continue to unload excess product. Blocks fell 2¾¢ to \$1.15¼/lb, while barrels were pushed below support to \$1.08¾/lb, a loss of 2¢ for the week. Trading was steady, with 14 loads of blocks and 15 barrels exchanging hands. Butter picked up ¾¢ to settle at \$1.23 on light trading of only 3 cars.
- NASS cheese prices were sharply lower this week compared to last. 40-lb blocks fell 2.9¢ to average \$1.25/lb and 500-lb barrels dropped 7.1¢ to \$1.18/lb as they follow recent declines in the cash market. Butter lost 0.9¢ to average \$1.16/lb, but powders continue to show strength, with nonfat dry milk gaining 0.3¢ to average 82¢/lb and dry whey increasing 0.5¢ to 20.7¢/lb.
- Weekly cold storage stats indicate cheese stocks at USDA selected storage centers increased 6.1 million lbs, or 6% from 04/01 through 04/27.
- Weekly dairy cow slaughter fell for the sixth week in a row, according to USDA. 48,000 head were culled for the week ending 04/18, compared to 50,700 head a year ago. The decline may be due to waiting on CWT bid acceptance.
- Florida exported 157 loads of Grade A milk this week, up from 145 last week, according to Fluid Milk & Cream Review. Early indications are that exports will increase even more next week as peak production approaches. Balancing plants are running at 80% capacity, and there is fear that the H1N1 flu outbreak could stifle milk consumption at Florida theme parks and the cruise business.
- Fluid Milk & Cream Review reports processors continue to run on heavy seasonal schedules in the Central region. Class I interest is average and demand for manufacturing milk is light as cheese makers try to keep inventory from building.
- Plants continue to run very full in California, according to Fluid Milk & Cream Review. Milk has to move longer distances to find a processing home, even with milk production down in the state. Ice cream operations are not taking as much cream as expected, resulting in heavier offerings to churns.

**Milk-feed Ratio**



- The Western nonfat dry milk market is not as aggressive as a few weeks ago, according to Dairy Market News. Many buyers have stockpiled inventory at prices below current levels and have little incentive to add any more to their warehouses. Powder production remains heavy to handle milk receipts, with clearing to the government support program the busiest in weeks.
- Milk production in the Northeast continues to move toward the flush, leaving a very ample supply for cheese makers, according to Dairy Market News.
- In the Midwest, few private label cheese packers need overtime to fill orders, according to Dairy Market News. In addition, regular variety offerings of cheese are becoming much more available as cheese production continues to increase seasonally.
- Western cheese buyers are taking good volumes of cheese at current low prices; however, offerings are sufficient for the current level of interest. In fact, some plants indicate that their stocks are heavier than desired and have been that way for awhile.
- International: Milk receipts are increasing seasonally in Europe with the peak expected in a few weeks, according to Dairy Market News. While output lags year ago levels, export interest remains light.
- International: The milking season is winding down in Oceania, with New Zealand output forecast to be 6% higher than last season, according to Dairy Market News. Recent rains in Australia have allowed for a solid start to the planting of fall crops.

### **Recommendation:**

It's no fun being the bearer of bad news. Cash cheese prices continued to hover around an equivalent \$9.60/cwt Class III price for the third week in a row, causing more and more premium to be erased from the front months. There really is nothing positive to say about the next 4-8 weeks. We're hearing that warehouses of cheese buyers who were much more active in the last few months are getting full. USDA's weekly cheese updates indicate production is still heavy, while offerings and inventory are building. Milk production is hitting its stride nationally, which is making the powder markets, which were making a comeback, appear to be weakening again. Last week we said, "*We could see May below \$10, June below \$11 and July below \$12*". We're 2 for 3 so far, and pretty close on July. CWT bids are due today, but the extended period allowed for bids has meant that most cows won't be culled until June or July. This is likely going to postpone real recovery in milk prices until Q4. Recall that earlier this year, after the first major fall in cheese prices, Class III milk futures were below \$14/cwt through the April 2010 contract. It looks like we're headed for another sell-off across the board as producers might jump at whatever upper-\$14 and \$15 milk they can. Aggressive hedgers should consider selling milk Jun-Dec '09, with the intention of buying back the hedge early, at a profit. As low as they already are, the front months appear especially vulnerable, considering their premium to the cash market and the unlikely chances of a major cheese rally. Looking for positives this week was tough, but we are starting to see signs the U.S. economy is finding a bottom, and that dairy export markets are reviving slightly. We also remain convinced that we will eventually see commodity inflation once the recovery is confirmed. Farms should consider looking at what they can do on the input side as far out as they can. With interest rates near historic lows, they should also consider what rates they can lock in as far out as possible. The Fed will be forced to raise interest rates to combat inflation, should that occur.

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