October 2007

National Milk Producers Federation

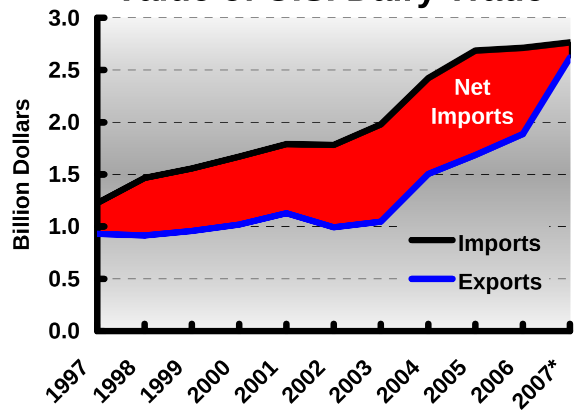
Volume 10, Number 9

Dairy Market Report

Executive Summary

- US skim solids commercial disappearance up only 0.4% for June-August; fat up 1.2%.
- October 1 cheese stocks down 3%, butter stocks up 27%, from last year.
- October 31 blocks up 10½¢ to $2.00½/lb., barrels up 7¢ to $1.92, butter down ½¢ to $1.31/lb., from our last report.
- September milk production up 2.6%.
- Outlook: *More modest price strength in 2008, depending on world markets.*

Value of U.S. Dairy Trade



Source: USDA/FAS *projected

Market Outlook

Exports continue to form our price outlook. U.S. dairy markets once moved based on small changes in domestic supply and demand, with little concern about foreign sources or destinations. Now we are part of a much larger world market, and overseas developments can be as important as those here at home. For example...

Feed supplies for European dairy farmers are very tight, due to poor harvests and European Union biotechnology policies. The US takes 15 months to approve a biotech crop variety; the EU takes more than 2½ years. So, grain exporting countries have often planted new varieties long before they have EU approval. Worse, the EU has a policy of zero tolerance for unauthorized biotech crops: if there is even a trace, an entire shipment is rejected. The EU normally doesn't import coarse grains like corn; but it has faced two poor harvests in a row, and now pay premiums for limited supplies of Brazilian corn and US sorghum, two supplies that happen to be "pure." The same policies are causing difficulties for importers of oilseeds like soy, as well. An EU report on the issue this summer anticipated the problems that EU livestock producers are having this fall: tight feed supplies mean higher costs for European livestock producers, including dairy farmers, which puts them at a competitive disadvantage with the rest of the world. This may have already stymied EU milk production growth despite expanded milk production quotas.

And so a thing as remote as the slowness of the EU biotech crop approval process can lead to less competition and a higher price for US milk producers and dairy processors in the world market. And so we continue to see US commercial disappearance relying on export demand as US prices follow world prices. Even when US prices have fallen below these world prices, this may be partly attributed to the challenge manufacturers face to be confident in, and adapt to, newly opened overseas markets. As this challenge has been overcome (as it has for some cooperative manufacturers with help from the Cooperatives Working Together export assistance program), that gap shrinks. (See graph at Butter.)

Milk and dairy prices will continue drifting down from recent peaks; but 2008 will be the second highest price year ever. We will watch commercial disappearance, which lagged a bit in the last quarter. Stocks will drive short-term price movements, but in today's market, the fundamental signals will come from trade totals and international price comparisons. dmr

The Dairy Market Report is created for Dairy Management Inc.

The Nutshell

Production v. last year:

- August Cheese ⬇ 0.1%
- August Butter ⬆ 23.6%
- Aug. NDM/SMP ⬆ 22.4%
- August Whey ⬆ 3.4%
- September Milk ⬆ 2.6%

Prices:

NASS	Aug.	Sept.
Cheddar	1.91	2.03
Whey	0.62	0.48
Butter	1.44	1.38
NDM	2.05	2.06
Milk	**Aug.**	**Sept.**
Cl. III	19.83	20.07
Cl. IV	21.87	21.61
All	21.60	21.80

Cheese and Whey

In August, total U.S. **cheese** production (excluding cottage cheese) was 795 million lbs., down 0.1% from a year ago. Of this, American types totaled 312 million lbs., down 1.8%, and Italian types were 334 million lb., up 0.2%. For the year to date, total cheese production was up 1.8%.

Natural American cheese stocks were 544 million lbs. on October 1, about even with September and down 3% from a year ago. Stocks of other cheese, including Swiss, began October at 277 million lbs., down 2% from September and down 1% from last year. Total cheese stocks are down 3% from a year ago.

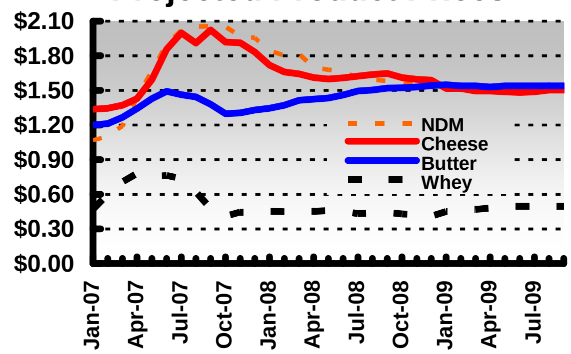
In time, whey prices should return to rough protein parity with nonfat dry milk.

For the three months ending August 2007, commercial disappearance of American cheese was 986 million lbs., down 2.4% from a year ago; other cheese was 1.55 billion lbs., up 6.7% from last year. The total was up 3.0%.

On October 31, CME prices were up from our last report: 40-lb. blocks up 10½¢ to $2.00½ per lb.; 500-lb. barrels up 7¢ to $1.92. Futures markets project a cheddar cheese price averaging $1.73 in the six months ending next April, $1.71 in 2007, and $1.63 in 2008.

The retail prices in September 2007 were $4.48 per lb. for cheddar cheese (up 6% from last year); and $4.05 for American processed cheese (up 8%).

Projected Product Prices



Based on futures as of October 30, 2007

The CME dry whey futures market still projects whey prices in the low to mid-40¢'s throughout 2008. The international whey price is under 50¢ per lb.

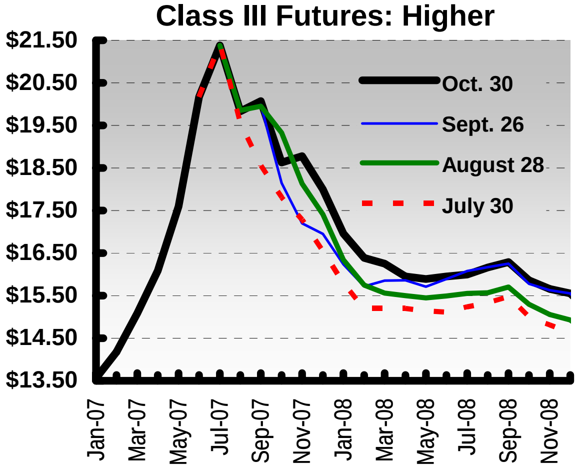
Whey Products				
Product	**August Production**		**September 1 Maker Stocks**	
	Mil. lbs.	**Change v 2006**	**Mil. lbs.**	**Change v 2006**
Whey, food	89.1	1.6	58.6	55.6
Whey, feed	5.6	45.2	6.2	234.6
WPC25-50	19.8	-16.6	18.3	-1.2
WPC50-90	10.4	-8.7	7.8	-9.4
WPI90+	3.0	19.9	n/a	n/a
Total	***127.8***	***-1.0***	***90.8***	***36.5***

U.S. production of dry **whey** for food was 89 million lbs. in August, up 1.6% from a year ago, and up 2.3% for the year to date. (See box.)

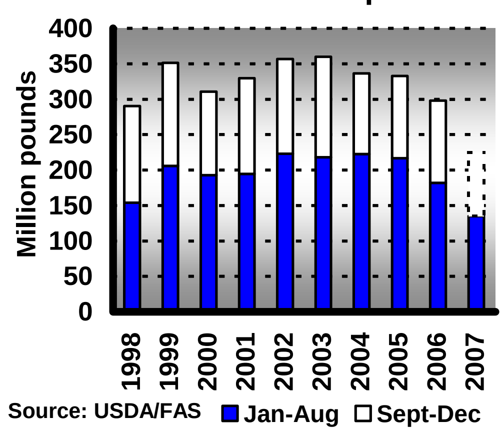
The manufacturers' price of whey was 41½¢ per lb. the week of October 20, according to NASS' survey. WPC-34 prices were down again, to about $1.33, and Western sweet whey was up slightly to about 41¢, per Dairy Market News.

Cheddar cheese prices are around $2.20 per lb. at European ports and $2.10 in Oceania. At these prices, U.S. cheese is competitive on the world market. Net imports of cheese in 2007 will be down by more than 100 million pounds compared with 2005. The graph below shows this projected decline, based on 24 million fewer pounds of cheese imported and 84 million pounds more exported. **dmr**

Class III Futures: Higher



Net U.S. Cheese Imports



Source: USDA/FAS

Butter

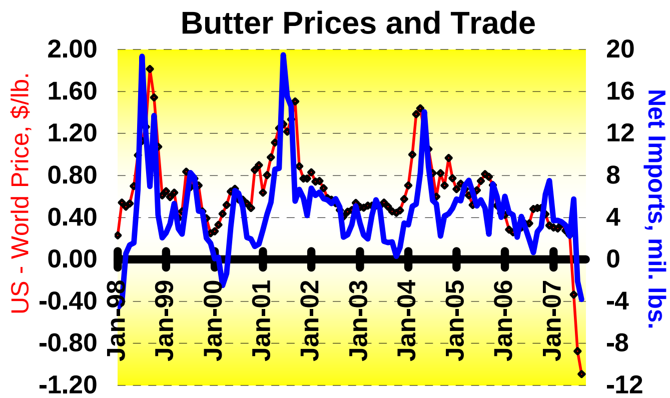
August U.S. butter production was 110 million lbs., up 24% from a year ago; 2007 to date is up 5%.

U.S. butter stocks started October at 243 million lbs., up 27% from a year ago. These are the largest October stocks in at least a decade, but world stocks are falling.

Commercial disappearance of butter in the quarter ending with August was 350 million lbs., up 2.5% from a year ago.

September's retail butter price averaged $3.14 per lb., up 13% from last September. The CME butter price was down ½¢ to $1.31 on October 31. Futures project butter to average $1.37 for the six months through April, $1.35 in 2007, and $1.46 in 2008.

World butter prices approach $1.70 per lb. and U.S. net exports rise (to 4 mil. lbs. in August) as the price gap favors U.S. producers. The graph above shows this close relationship. dmr



Dry Milk Powders

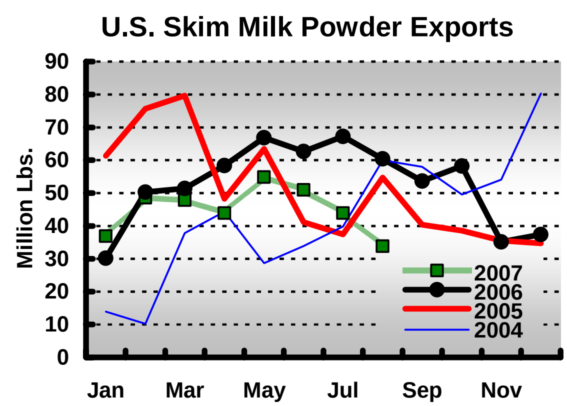
U.S. nonfat dry milk production, adding in protein-standardized "skim milk powders" was 121 million lbs. in August, up 22% from a year ago; and down 6½% for the year to date, to 1.02 billion lbs.

September 1 manufacturers' stocks of (only) nonfat dry milk were 140 million lbs., up 152% from a year ago.

The CME prices of extra grade and grade A nonfat dry milk were $1.93 (unchanged from last month's report) and $2.00 (down 11¢) on October 31; these are below the average surveyed U.S. manufacturers' price of $2.07 the week of Oct. 20.

Overseas powder prices are down to about $2.00. U.S. exports have declined over the summer, due at least partly to short U.S. supplies. August skim milk powder exports were the lowest since the export boom started in 2004; but dry milk and whey exports still equaled 8.8% of U.S. skim solids production.

Overall U.S. commercial disappearance of nonfat dry milk (including exports, but excluding modified "skim milk powders") in the three months ending August was 297 million lbs., down 15.4% from a year ago, according to USDA, contributing to weak disappearance of all skim solids. dmr



Source: USDA/FAS

Yogurt, Ice Cream, and Fluid Milk

U.S. yogurt production was 310 million lbs. in August, up 5½% from last August, and up 6% for 2007 to date.

U.S. ice cream production was 123 million gallons in August, down 3½% from a year ago. Ice cream mix production was 45 million gallons, down 9%. For 2007 to date, ice cream and ice cream mix production is up 2%. September's retail ice cream price was $3.90 per ½-gallon, up 5% from last year.

Fluid milk sales for August were down 0.6%, (down 1.1% calendar-adjusted), in a month with 26% higher retail prices. September's retail whole milk price was $3.84 per gallon, up 26% from last year. dmr

U.S. Fluid Milk Sales

	August 2007		Year-to-Date	
Product	**Mil. lbs.**	**%**	**Mil. lbs.**	**%**
Whole Milk	1,345	-4.1	10,677	-2.7
Flavored Whole Milk	55	-13.7	449	-5.1
Organic Whole Milk	29	36.7	203	28.8
Reduced Fat Milk (2%)	1,542	0.9	11,898	0.9
Low Fat Milk (1%)	542	1.1	4,325	3.0
Fat-Free Milk (Skim)	688	1.2	5,403	1.5
Flavored Fat-Reduced	240	-6.9	2,307	0.0
Organic Fat-Reduced	97	40.5	698	33.7
Buttermilk	44	1.9	344	1.2
Total (including "Other")	**4,594**	**-0.6**	**36,394**	**0.5**
Total (calendar adjusted)	**4,558**	**-1.1**	**36,294**	**0.0**

Source: USDA/AMS, Dairy Market News

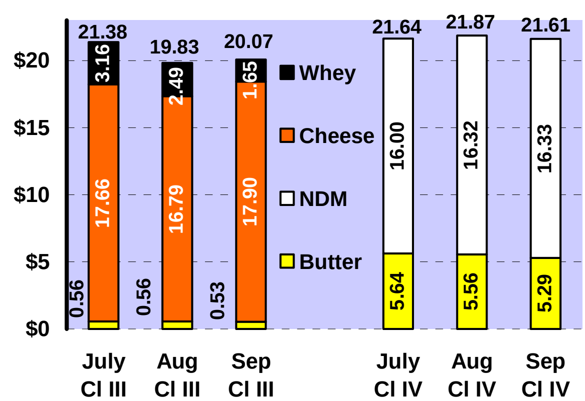
Milk: Production and Prices

U.S. milk production was 14.85 billion lbs. in September, up 2.6% from a year ago, from 0.6% more cows and 1.9% more milk per cow. Of 23 states with USDA-reported monthly production, seventeen showed year-over-year growth, including Arizona (up 9.9%) and Michigan (up 8.0%). Six states were down, including Kentucky (-7.2%) and Missouri (-8.8%). California production was up 3.3% on 0.6% more milk per cow from 2.7% more cows. Wisconsin production was up 3.3%.

USDA projects 2007 growth at 2.0%, and 2.6% for 2008. We still project 2007 production growth of about 2%, based on year-to-year increases of just over 2½% for the rest of 2007.

RBST use is down a quarter over the last five years. This month, USDA's Animal and Plant Health Inspection Service released the first results from its 2007 survey of dairy cattle health and management practices. One result: rBST use fell from 22.3% of cows milked on January 1, 2002, to 17.2% on January 1, 2007.

Class Price Breakdown



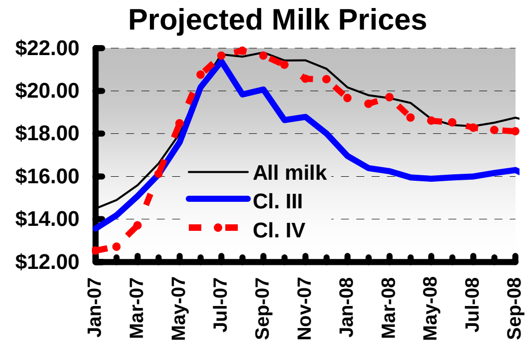
The September Class III price was announced at $20.07 per hundredweight, up 63% from a year ago. October Class III will be announced near $18.60 on November 2.

Class III futures prices for the next six months averaged $17.06 per hundredweight on October 30, and project an average of $17.78 for all of 2007 and $16.08 for 2008. USDA forecasts a 2007 average of $17.70, and $16.00 in 2008. The Class III price is the minimum price paid for cheese milk pooled on Federal orders.

The September Class IV price was $21.65 per hundredweight, up 95% from a year ago. October's Class IV will be near $21.35.

Futures markets project Class IV milk to average about $19.75 for the six months ending April, $18.50 for all of 2007and $18.60 for 2008. USDA forecasts the Class IV price to average $18.60 in 2007, and $17.85 in 2008. The Class IV price is the minimum price for pooled milk used to make butter or milk powder.

September component prices were as follows: $1.5101 per lb. (down 8¢ from August) for butterfat in Class III, Class IV, and producer milk; $4.3929 (up 45¢) for protein in Class III and producer milk; $1.8797 (nearly unchanged) for total nonfat solids in Class IV milk; and $0.2890 (down 15¢) for other solids in Class III and producer milk.



Based on futures as of October 30, 2007

September's Class II price was down 25¢ to $22.16 per hundredweight. This is the minimum price for pooled milk used to make soft dairy products and in most food processing. October's Class II price will be announced near $22.05 on November 2.

The November Class I base price was down another 14¢ from October to $21.45, but 73% above last year and still based on butter/powder values. The December price is projected at $21.00. The Class I base price plus the Class I location differential is the minimum price processors pay at the plant for bottling milk pooled on a Federal order.

We project October's all-milk price at $21.40, down 40¢ from September's record and up 59% from a year ago. Based on futures prices, the six months ending next April are projected at about $20.25, all of 2007 at $19.07, and 2008 at $18.90. USDA lowered its 2007 all-milk price forecast to $19.00, and is projecting 2008 at $18.15. dmr

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