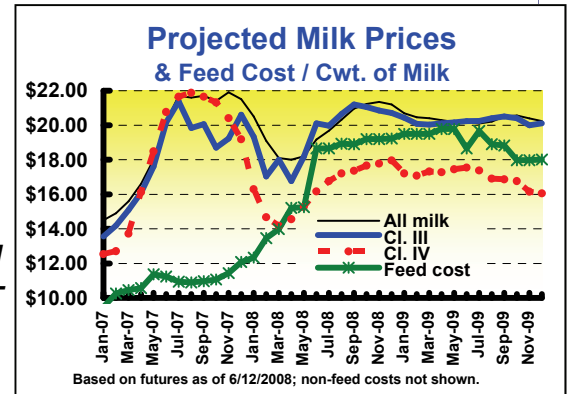




Dairy Market Report

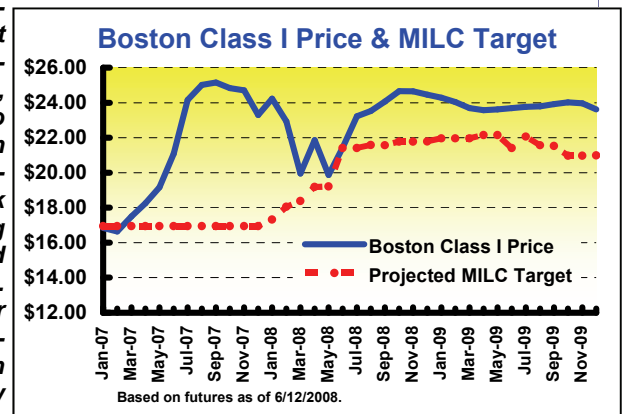
Executive Summary

- ➔ Daily domestic disappearance: skim solids up 5.2% in 1st quarter 2008, milk fat up 1.6%.
- ➔ Commercial exports: solids down 9% in 1st quarter, fat up 111%.
- ➔ Cheese prices remain above \$2: June 13th blocks were down 24½¢ to \$2.04/lb., barrels down 10¢ to \$2.15; butter down 1¼¢ to \$1.47¾/lb. since last report.
- ➔ Outlook: Milk prices will keep chasing feed prices up, but gain little ground. Self-grown feed masks milk losses for some, but CWT, poor margins will slow U.S. herd growth.



Market Outlook

Low milk-feed margins are slowing milk production, but less than economic theory would suggest. (See “feed costs”, page 4.) Production continues to grow from the cow number momentum of the last year’s high prices. Cheese makers are reluctant to make and hold cheese made from milk paid for at high product-driven milk prices. In some states this has contributed to milk backing up and even being dumped, although this should ease as the short season approaches. Meanwhile milk powder is moving overseas in ever-growing volumes, constrained primarily by manufacturing capacity. The recent announcement of a new round of herd retirements by Co-operators Working Together (see page 4), and the adoption of a feed cost adjustor to the Milk Income Loss Contract program in the new Farm Bill, both highlight the milk-feed price squeeze. Despite record milk prices, dairy farmers are either losing money overall, or using their valuable feed crops to subsidize their milking operation. High feed prices drove the MILC target for Boston Class I milk from the \$16.94 baseline to over \$19 in May and, based on corn and soybean futures, this target will likely go above \$21 this year. (Despite this rising target, no payments are yet projected for 2008 or 2009.)



The futures markets for feed crops have come under scrutiny. With financial and real estate markets in turmoil, a lot of money has moved into farm commodities, creating a possible bubble. Some futures prices have recently closed well above the underlying commodity value. This distorted “basis” between futures prices and crop cash prices may be based on the new money in the market overwhelming the available product that meets the specifications to settle the contracts. This wreaks havoc with the risk management choices of both crop and livestock farmers. For example, many grain elevators will not forward price feed for dairy farmers because they cannot rely upon futures markets to effectively hedge their risks. The Commodity Futures Trading Commission (CFTC) has already withdrawn proposals to expand speculators’ access of these futures markets, and will meet with the agriculture sector’s representatives to consider other remedies.

Note that dairy futures are primarily cash-settled; that is, they are settled with cash payments, instead of delivering commodities. This reduces the threat of disruption, as long as the USDA-announced settlement prices remain relevant. **dmr**

The Dairy Market Report is created for Dairy Management Inc.



The Nutshell

Production v. last year:

- April Cheese ↑ 1.4%
- April Butter ↑ 14.8%
- Apr. NDM/SMP ↑ 21.7%
- April Whey ↓ 0.1%
- April Milk ↑ 2.2%

Prices:

	Apr.	May
NASS		
Cheddar	1.82	1.95
Whey	0.26	0.27
Butter	1.35	1.42
NDM	1.25	1.30
Milk		
Cl. III	16.76	18.18
Cl. IV	14.56	15.26
All	18.00	18.20

Cheese and Whey

Total U.S. **cheese production** (excluding cottage cheese) was 815 million lbs. in April, up 1.4% from a year ago and up 0.9% from March, on an average daily basis. Of this, American types totaled 337 million lbs., up 3.4% from last year, and up 2.7% (daily) from March. Italian types were 345 million lb., down 0.1% from last year and down 0.5% from March, on a daily basis.

Natural American cheese **stocks** for the end of May/beginning of June will be published on June 20.

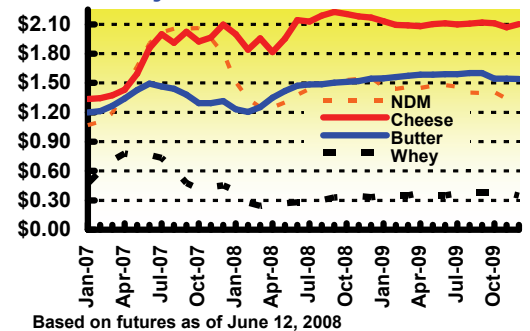
For the three months ending March 2008, **commercial disappearance** of American cheese was 991 million lbs., up 2.7% from a year ago (1.6% adjusted for leap day); other cheese was 1.5 billion lbs., up 2.3% (1.2% adjusted) from last year. The total was up 2.4% (1.3% adjusted).

CME cheese prices remained high. On June 13th, blocks were down 24½¢ from last month's report, but still at a relatively high \$2.04 per pound, and barrels were down only 10¢ from last month's

record peak, to \$2.15. Class III futures markets continue to rise, projecting new records later in the year, and cheese prices above \$2.20 in the summer months.

June 12 futures markets project the NASS cheese price to average nearly \$2.20 over the next 6 months (July through December), and over \$2 for all of

Projected Product Prices

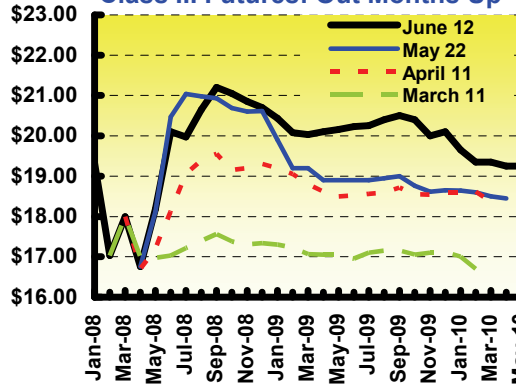


cheese averaged \$4.08 at retail, up 5%.

Total **production** of dry **whey** for food was 91.7 million lbs. in April 2008, down 0.1% from a year ago. (See box.)

The manufacturers' **price** of whey was 28¢ per lb. the week of June 7, according to NASS' survey. WPC-34 prices are about \$1.00, per **Dairy Market News**. This is 40¢ to 45¢ lower than nonfat dry milk spot prices, but 3½ times the Western sweet whey price of 28¢. (See graph on page 3.) The **CME** dry whey futures project average whey prices of 32¢ in 2008, just over half the 2007 average. The international whey price is about 45¢ per lb., per USDA's **Dairy Market News**.

Class III Futures: Out Months Up



2008 and 2009. U.S. cheese **exports** in April were 29 million pounds, up 55% from a year ago and equivalent to 3½% of U.S. production. In addition, imports were down 18%, so **net cheese imports are down 96% to less than one million pounds: U.S. cheese trade is nearly balanced, on a pound basis, and may already be in surplus in May.**

The **retail price** of cheddar cheese in May was \$4.40, up 11% from last year. Processed

“Class III futures continue to rise, projecting new records later in the year, and cheese prices above \$2.20 in the summer months.”

Whey Products				
Product	April Production		May 1 Maker Stocks	
	Mil. lbs.	Change v 2007	Mil. lbs.	Change v 2007
Whey, food	91.7	-0.1	59.9	37.5
Whey, feed	5.3	5.5	2.7	-26.0
WPC25-50	23.2	7.5	26.2	65.7
WPC50-90	11.6	1.1	14.4	50.9
WPI90+	3.1	-6.0	n/a	n/a
Total	134.9	1.3%	103.2	42.3%

Exports as % of US Production

Product group	Total 2007	Jan-Mar 2008
SMP/NDM	39%	48%
Butter/AMF/butteroil	6%	11%
Cheese	2%	3%
Total whey	58%	45%
Milk solids	9.5%	10.7%

Sources: NMPF, USDEC

Butter

April U.S. [butter production](#) was 153 million lbs., up 15% from a year ago.

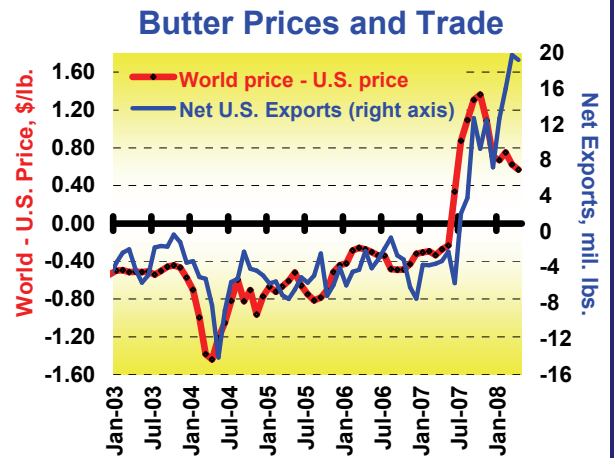
[Commercial disappearance](#) of butter in the three months ending with March was 402 million lbs., up 17% from a year ago (15% adjusted for leap day). Average daily disappearance of all milkfat was up 3.8% for the same three months.

The [retail](#) butter price averaged \$3.26 per lb. in May 2008, up 7% from 2007.

The [CME](#) butter price was down 1¼¢ to \$1.47¾ on June 13. Fu-

tures project NASS butter at \$1.51 for the six months through December, \$1.41 for all 2008, and \$1.57 for 2009. [Net butter exports](#) totaled 68 million pounds in the first four months of 2008, compared with net [imports](#) of 14 million pounds in the same months in 2007. A widening in the price gap between the U.S. and the world will assist these crucial exports. USDA reports international butter spot prices 30¢ to 40¢ above U.S. domestic prices.

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Dry Milk Powders

U.S. [nonfat dry milk production](#), including protein-standardized "skim milk powders" was 169 million lbs. in April, up 22% from a year ago.

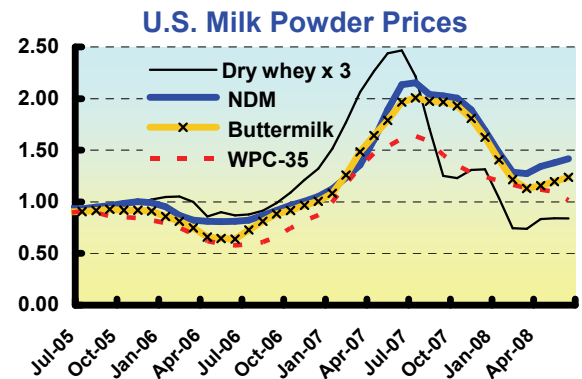
May 1 manufacturers' stocks of (only) nonfat dry milk were 136 million lbs., up 46% from last year.

The [CME](#) price of grade A nonfat dry milk was unchanged at \$1.46½, extra grade was down ½¢ to \$1.46, on June 13, 10¢ above the average surveyed U.S. manufacturers' [price](#) of \$1.36 the week of June 7.

Skim powder prices are near \$1.60 in Oceania and above \$1.70 in Western Europe, per [USDA](#). U.S. powder continues to be competitive. In April 2008 exports of nonfat dry milk and skim milk powders were 82 million pounds, up 88% from a year ago, and equal to 49% of production.

Overall U.S. [commercial disappearance](#) of nonfat dry milk (including exports, but excluding modified "skim milk powders") in the three months ending March was 375 million lbs., up 17% from a year ago, (16% calendar-adjusted) ac-

cording to USDA. For the same quarter, average daily commercial disappearance of all skim solids was up 3.2%. **dmr**



Source: Dairy Market News, USDA

Yogurt, Ice Cream, and Fluid Milk

U.S. [yogurt production](#) was 300 million lbs. in April, up 1.9% from last year. For the year to date, it is up 3.1% to 1.2 billion pounds.

April [ice cream production](#) was down 4% from a year ago to 113 million gallons. Ice cream mix production was 43 million gallons, down 4%. For the year to date, ice cream production was down 3% and mix was down 4%. May's

[retail](#) ice cream price was \$4.08 per ½-gallon, up 5% from last year.

April [fluid milk sales](#) fell only 0.7% from a year ago (calendar-adjusted), though the [retail](#) price of whole milk rose 21%. May fluid milk was \$3.76 at retail, up 15% from a year ago.

dmr

U.S. Fluid Milk Sales

Product	April 2008		Year to Date	
	Mil. lbs.	%	Mil. lbs.	%
Whole Milk	1,220	-6.2	5,050	-6.3
Flavored Whole Milk	49	-13.1	194	-16.8
Organic Whole Milk	31	32.3	126	29.5
Reduced Fat Milk (2%)	1,486	2.6	6,059	1.3
Low Fat Milk (1%)	559	3.4	2,259	1.8
Fat-Free Milk (Skim)	677	1.8	2,748	0.4
Flavored Fat-Reduced	380	11.5	1,417	0.9
Organic Fat-Reduced	103	24.7	438	30.8
Buttermilk	44	4.2	199	14.0
Total (including "Other")	4,562	1.1	18,541	-0.4
Total (calendar adjusted)	4,556	-0.7	18,382	-1.1

Source: USDA/AMS, Dairy Market News

Milk and Feed

U.S. [milk production](#) figures will be posted June 16. We project continued growth in cow numbers and moderating milk per cow.

The CWT program announced its fifth round of herd retirements, setting no *a priori* targets in order to maintain flexibility to pursue program aims "in a cost-effective and frugal manner." Bids will be accepted through June 30, and cow removals are expected to begin before the end of July. If history is a guide, this means the herd retirement will begin to have its full impact on production in August and September.

May's Class III price was announced at \$18.18 per hundredweight, up \$1.42 from April, and up 58¢ from a year ago. June will be up again, above \$20.00. Class III [futures](#) prices for the next six months (July through December) averaged \$20.74 per hundredweight on June 12, and project averages of \$19.48 for 2008 and \$20.22 for 2009. USDA has raised its [forecasts](#) to \$18.35 in 2008 (up more than a dollar from USDA's May forecast) and \$17.60 in 2009. The Class III price is the minimum price paid for cheese milk pooled on Federal orders.

The May Class IV price was \$15.26 per hundredweight, up 70¢ from April, but down \$3.22 from a year ago. June's Class IV is projected up again to about \$16.20. [Futures](#) markets project Class IV milk to average about \$17.45 for the next six months, \$16.30 for 2008 and \$17.00 for 2009. USDA forecasts \$15.80 in

2008 and \$17.10 in 2009, both up slightly from May's forecast. The Class IV price is the minimum price for pooled milk used to make butter or milk powder.

May component prices: \$1.5562 per lb. (up 8¢ from April) for butterfat in Class III, Class IV, and producer milk; \$4.1108 (up 35¢) for protein in Class III and producer milk; \$1.1301 (up 5¢) for total nonfat solids in Class IV milk; and \$0.0766 (up 1¢) for other solids in Class III and producer milk.

May's Class II price was up 22¢ to \$15.51 per hundredweight. This is the minimum price for pooled milk used to make soft dairy products and in most food processing. June is projected at about \$16.20.

As we reported last month, June's Class I base price was \$18.18, 34¢ higher than last June, up \$1.56 from May, and based on cheese/whey values. The Class I base price plus a location differential is the minimum price processors pay at the plant for bottling milk pooled on a [Federal order](#).

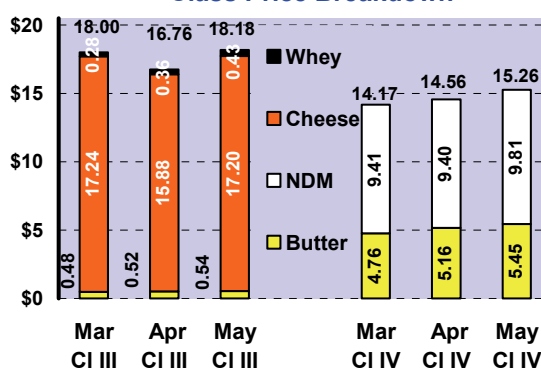
May's [all-milk price](#) was \$18.20, up 20¢, both from April and from a year ago. June is projected at \$19.20. Futures project the next six months at \$20.80, 2008 at \$19.80, and 2009 at \$20.35.

Feed costs continue to rise, as weather has

slowed planting and flooded fields across the corn belt. July corn futures are \$7.09 per bushel., and spring 2009 futures are over \$7.50. July soybean [futures](#) are \$15.36, and every contract month through August 2009 is over \$15.00. Confusing this is the increasingly uncertain basis between futures prices and elevator prices, which is making forecasting and risk management more and more difficult. There is almost no question, however, that feed costs will continue at record levels through the year and beyond.

The effect of these extremely high feed costs on milk production is being tempered, though, by those dairy farmers who grow valuable corn and soybeans and hay, account for it as cheap feed, and then believe their money-losing cows are profitable. In theory, cropping and milking should be evaluated separately, but in practice, this isn't always easy. This helps to explain the unexpectedly high dairy cow replacement prices, despite poor dairy margins and large replacement supplies. **Jmr**

Class Price Breakdown



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Dairy Management Inc.™ and state, regional, and international organizations work together to drive demand for dairy products on behalf of America's dairy farmers, through the programs of the American Dairy Association®, the National Dairy Council®, and the U.S. Dairy Export Council®.



The National Milk Producers Federation (NMPF) is a farm commodity organization representing most of the dairy marketing cooperatives serving the U.S.