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No Longer Insulated

Reports out of China indicate that blue-ear pig disease, also known as Porcine Reproductive and Respiratory Syndrome, has spread to 26 of China's 33 provinces threatening the viability of China's pork industry. Considering China produces over 50% of the world's hogs, a swine epidemic there takes on regional if not global significance, according to USDA's Foreign Agricultural Service.

So what does that have to do with the U.S. dairy industry, you might ask? Well China is a significant buyer of U.S. dairy ingredients. Significant as in it imports more than 25% of the U.S. dry whey production and more than 10% of the U.S. lactose/lactose blends production. Considering that

the United States exports over half of its dry whey and 75% of its lactose/lactose blends, whether China is in or out of the market will have a strong ripple effect on both the global and U.S. markets.

China has been the largest importer of U.S. dry whey for at least the past five years. During the first half of 2007, exports to China were down almost 20%. However, the real drop did not occur until the second quarter. Granted this was when U.S. dry whey prices topped the market at nearly 80 cents per pound. Regardless of whether China's pullback in dry whey imports is due to price or a smaller hog population, the short-term impact is the same—a reduction in demand that has led to a price decrease.

Since the April 2007 peak of 80

cents per pound, the dry whey price has tumbled to 55 cents and is expected to be closer to 45 cents by the end of the year. This is still 200% higher than the historical average dry whey price.

Why the drop in price? In some cases, food and feed manufacturers have reformulated their products without whey. In addition, increased competition from whey permeate and lower exports to China have both contributed to softening dry whey prices. Keep in mind that a penny change in the dry whey price equates to a 6-cent per hundredweight change in the Class III and California 4b prices.

Therefore, the expected 30-cent drop in the dry whey price will

Continued on page 2

KEN'S CORNER



*by Ken Meyers
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If one says the cure for high prices is high prices and that stimulates production in the

United States, then prices are destined to fall off their highs. The question becomes

not only when but to what level.

One can speculate that a new floor will be higher than we've seen in the past because U.S.-based customers will not be the only ones looking to take advantage of this price drop. Export opportunities are likely to hold prices higher as the new world dairy economy expands

through increased dairy consumption.

The enhanced protein diets of the world's middle class is not a short-term market aberration, but rather a long-term market opportunity as these consumers continue to enhance their and their children's diets and lifestyle. **MCT**

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Fall demand arrives...

The American cheese market remains tight and inventories are now 6.5% less than they were last year. Fluid milk demand is also strong as bottlers continue filling school and university pipelines. The butter market, which unlike the cheese and nonfat dry milk markets, has traded within a historic price level over the past several months, but could now be

| MCT Forecast | | | | | | | |
|--------------|--------|---------|---------|--------|--------|-----------|----------|
| | Block* | Barrel* | Butter* | Whey** | NFDM** | Class III | Class IV |
| Aug | 1.9554 | 1.9107 | 1.4464 | 0.6197 | 2.055 | 19.83 | 21.87 |
| Sep | 2.0725 | 2.0300 | 1.5400 | 0.5319 | 2.075 | 20.45 | 22.20 |
| Oct | 2.0100 | 1.9675 | 1.5750 | 0.5112 | 2.014 | 20.60 | 22.00 |
| Nov | 1.9750 | 1.9425 | 1.5950 | 0.4997 | 1.928 | 20.00 | 21.35 |
| Dec | 1.9500 | 1.9175 | 1.5575 | 0.4995 | 1.852 | 19.80 | 20.65 |
| Jan | 1.9500 | 1.9175 | 1.5300 | 0.5077 | 1.819 | 18.25 | 20.20 |

* Block, barrel and butter are monthly averages of CME prices.
 **Whey and NFDM are monthly averages of NASS prices.

in a position to see price escalation as global butter prices continue to

increase, making U.S. butter more competitive on world markets. **MCT**

Relief ahead...

Continued from page 1

lower cheese milk prices by \$1.80/cwt. This is much welcomed relief to those cheese manufacturers whose whey revenues have not offset the escalating dry whey price impact on their milk costs.

Cheese manufacturers looking for relief from high nonfat dry milk prices will have to wait longer. About 40% of U.S. nonfat dry milk is exported. Despite domestic production being down 13.4%

through first half 2007, exports were down just 10%.

The global market has come to rely on U.S. dairy ingredients. The figure below illustrates that nonfat dry milk exports increased from 126,000 metric tons in 2002 to 287,000 metric tons in 2006. The U.S. share of the global nonfat dry milk market increased from slightly more than 10% to almost 28%.

Recent government outlook reports from Europe and Oceania indicate that skim milk powder production is expected to fall in the EU-25, and New Zealand dairy export prices are forecast to peak in the first and second quarters of 2008.

The key factors impeding EU skim milk production, hence exports, include a change in the manufacturing

mix toward cheese, existing milk supply quotas, and constrained exports subsidies.

New Zealand is optimistic that export prices will continue to rise through June 2008 as forward contracted sales are realized. Thus no significant price relief in the global skim milk powder market is expected until mid-2008. However, New Zealand cautions that in response to current high dairy prices, increasing export supply will come from New Zealand and other low-cost producers, such as Argentina, Uruguay, Brazil, and the Ukraine.

Thus, all U.S. dairy manufacturers and end users, no matter what their product mix, are affected by increasingly less regulated world dairy markets. Whether it's a pizza-cheese manufacturer sourcing nonfat dry milk to standardize the cheese vat, or a specialty cheese manufacturer optimizing its whey value, both feel the impact of global markets. **MCT**



Source: USDA/Foreign Agricultural Service



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