



MCT COMPASS

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Markets in Flux

In the past 90 days, the CME cash Cheddar block market has gone from a trading high of \$2.285/lb. to a trading low of \$1.695/lb. Granted this has not occurred at NASCAR speed, but then again, we're talking about a commodity market that is typically flush with product in May when milk production is at its peak and short of product in August as milk production declines seasonally and the demands from the fluid sector increase as schools reopen.

Once again, this shows that our market is anything but typical. Or perhaps we need to approach our analysis from an atypical perspective. In May, for example, Oceania's milk production, which

was lower than expected, was coming to a quick end. With sale commitments in place and lack of product, global markets remained strong.

As August approached, much-needed precipitation rained down on Australia and New Zealand, which provided optimism for a robust milk production season. Thus far, Oceania's production is reportedly stronger and earlier than expected. In addition, milk production in the EU is also reported to be higher than last year. The combination of additional milk production and the *anticipation* of greater milk production have taken the air out of global dairy markets, which has had a domino effect on our domestic markets.

On the demand side of the equation, the cure for high prices has been high prices. A glimpse into the dry whey and whey protein concentrate markets illustrates that lower domestic and global demand has dealt these markets a crushing blow. In April 2007, dry whey traded at a record-high 77.8 cents per pound. This week, that market is trading closer to 21.5 cents per pound, the lowest price level since August 2004.

In some cases, non-dairy ingredients have replaced whey derivatives in feed and food formulations. In addition, earlier this year, surplus milk production in California displaced milk

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KEN'S CORNER



by Ken Meyers
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Comparing the Oceania Cheddar cheese price as reported bimonthly in USDA's *Dairy Market News* to

CME cash Cheddar cheese prices is a bit like comparing apples to oranges. The global Cheddar market is quoted at

35% to 36% moisture, whereas the CME market is based off of a 39% moisture level. The difference in moisture alone commands a double-digit premium vs. the CME cash market. In addition, logistics and financing costs can easily add an additional 15 cents per pound. As a result, our domestic price would need to be closer to \$1.60/lb. to compete in today's global cheese market.

Earlier this year, the United States was competitive in the global cheese

market because the world market price was over \$5,000/ton. As the global cheese market drops closer to \$4,000/ton, it is possible that export volumes will continue to decline.

The question is whether domestic consumption will pick up the slack, or will production be curtailed, or will domestic prices converge with the world market in order to maintain export volume? **MCT**

Before the rebound

A month ago, the tea leaves were pointing to even stronger dairy markets this fall. That still could be the case. Margins to cheese manufacturers have been slim in August and we expect that there will be periods when the availability of 4- to 28-day-old Cheddar is tight in the upcoming weeks, but overall there appears to be enough cheese to satisfy the

MCT Forecast							
	Block*	Barrel*	Butter*	Whey**	NFDM**	Class III	Class IV
Jul	1.7400	1.7000	1.6277	0.2440	1.375	17.25	16.55
Aug	1.7750	1.7500	1.6110	0.2300	1.360	16.00	16.45
Sep	1.8600	1.8350	1.5950	0.2350	1.355	16.70	16.20
Oct	1.8700	1.8450	1.5675	0.2450	1.355	17.10	16.00
Nov	1.8500	1.8250	1.5150	0.2550	1.353	17.00	15.90
Dec	1.8250	1.8000	1.4450	0.2550	1.345	16.80	15.55

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

market. Butter and butteroil exports and could have more upside price have remained strong through June, risk. **MCT**

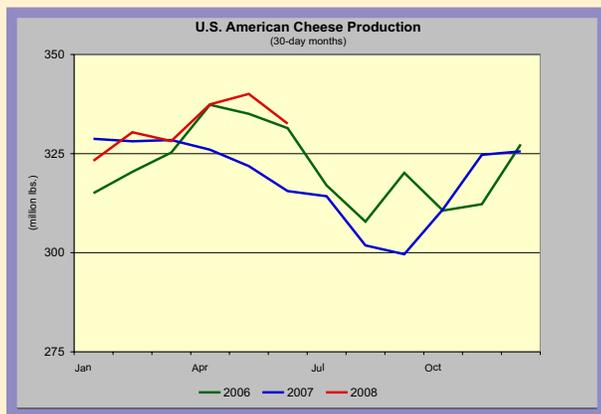
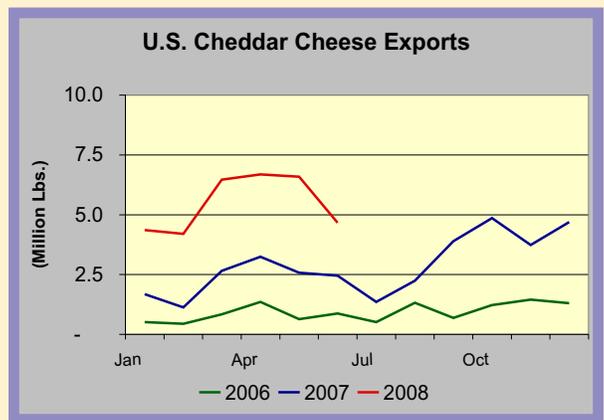
Whey build up...

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replacer (a key user of whey and lactose) on calf ranches. As a result, there are simply more whey products on the market.

What is difficult to measure is how much is too much. Take, for example, American cheese production. Through the first half of 2008, American cheese production increased 2.2%. During the second quarter, production was more than 5% higher than 2007 levels, but only slightly greater

than in 2006. Exports of Cheddar cheese help explain the increase in demand for American-style cheese during this period. However, due to increased production from other suppliers or a slowdown in demand, Cheddar cheese exports declined by 1.9 million pounds in June vs. May 2008. That's equal to about 45 cash lots of cheese.



The current global dairy markets are in flux as decreased demand and price resistance for whole milk powder is creating a shift in the product mix in which more milk is being drawn primarily into cheese production. However, a spillover into the skim milk powder and butter markets could bring

about further downward price pressure.

While the 30% reduction in the cash cheese market price comes as some relief to buyers, it along with further softening of the global dairy markets will provide heartburn to milk producers. After 13 months of ever-increasing cow numbers, expansion of the U.S. dairy herd came to a halt in July 2008. Further contractions are likely due to declining milk prices. And then the market will be in flux again—just in the opposite direction. **MCT**



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