

## A Tale of Two Commodities

Two of the most frequently asked questions in the dairy industry today are: How long can the butter market remain above \$2.00/lb., and how long can the cheese market ignore growing stocks? The answer to both questions is the same, longer than anyone would have guessed.



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USDA's recent Cold Storage report left no doubt that plenty of cheese is sitting in warehouses. According to the report, American cheese stocks totaled 635.6 million pounds as of September 2010, an increase of 6.6% vs. September 2009. But perhaps even more important than the absolute volume of cheese in storage, is the fact American cheese stocks actually increased during September. That is something that has not happened in 27 years. For the past decade, the average stock draw down in September has been 22.5 million pounds. The combination of a stock build in September and the highest level

of stocks ever for September makes one question the current price level of block and barrel cheese at Chicago Mercantile Exchange.

Granted a stock devaluation is not in the interest of companies holding larger than desired inventory levels. And we can all hope for a stronger-than-anticipated holiday demand period or greater exports to clear out inventory. However, if those things don't happen, the industry is likely to experience a stronger-than-anticipated correction in the cheese market.

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### Ken's Corner



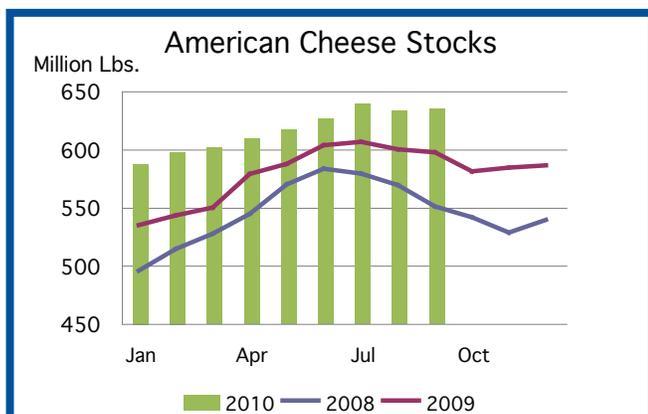
*by Ken Meyers  
President, MCT Dairies Inc.*

This week the Conference Board released its Consumer Confidence Index that showed public gloom is slowly lifting but remains well below levels required for consumers to begin spending freely again. The index grew from 48.6 in September to 50.2 in October, hardly anything

to cheer about.

Whether consumers—at least those who are fully employed—spend readily during the upcoming holiday season and what they choose to spend their money on will determine cheese and other dairy product prices going forward. According to a *Consumer Reports* poll out this week, one out of every three Americans plans to spend less this year than they did during the 2009 holiday season. They also are insisting on value, and about four out of 10 plan to cut back on credit and debit card spending. The survey also shows that 13.6 million Americans are still paying for last year's holiday credit card spending.

That said, the question remains whether grocers will feature butter and cheese for the upcoming holidays and whether consumers will be able to find appetizing substitutes if discounting does not occur. Even without hefty retail sales of butter over the Thanksgiving holiday, butter supplies will likely remain tight. And while it's fine to hope for the best, the industry needs to start moving American cheese, or prices could soon plunge over that proverbial cliff. **MCT**



# Sales dependent...

The highest milk prices in two years are expected to result in greater milk production during the final

three months of the year. More milk will likely put downward price pressure on dairy product markets.

It will take another month to realize just how great an impact higher commodity prices will have on retail sales during the upcoming Thanksgiving season. Continuing specials on pizza are expected to keep Mozzarella cheese moving, but building American cheese stocks are becoming more worrisome. **MCT**

MCT Forecast

	Block*	Barrel*	Class III	Butter*	Class IV	Whey**	NFDM**
Oct	1.7250	1.7120	16.95	2.1895	17.05	0.3675	1.1600
Nov	1.5900	1.5700	16.00	2.1500	17.00	0.3750	1.1650
Dec	1.5200	1.4950	15.00	1.8500	16.00	0.3800	1.1700
Jan	1.4900	1.4650	14.70	1.7000	15.15	0.3825	1.1400
Feb	1.4750	1.4500	14.45	1.6500	14.20	0.3750	1.0900
Mar	1.4300	1.4050	14.00	1.6200	14.10	0.3650	1.0900

\* CME prices.  
\*\*NASS prices.

## butter stocks falling...

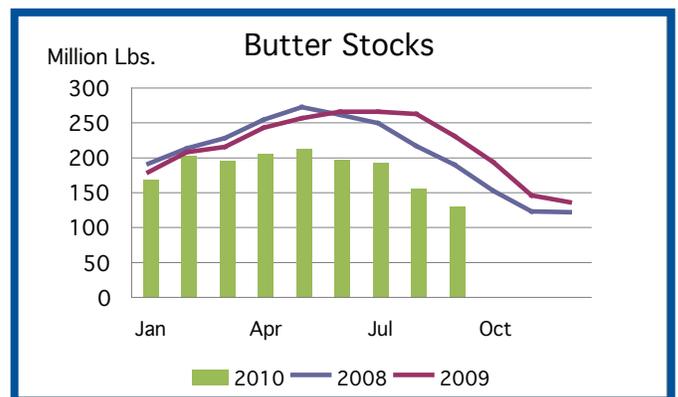
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### What About Butter?

Unlike cheese stocks, which have grown throughout the year as milk production has increased, butter stocks have trailed the prior year since the onset of 2010 and butter production has weakened. As of Sept. 30, 2010, butter stocks totaled 129.8 million pounds, almost 100 million pounds less than prior-year stocks. Butter production from January 1 through August 2010 was just 58.4 million pounds below the comparable period a year earlier.

Could it be possible that both butter production and butter stocks are lower this year due to increased domestic production of anhydrous milkfat and butteroil? Historically, most butteroil was made from butter, but it also can be made from fresh cream. As a result, increased domestic butteroil production can reduce both stocks and production of butter.

An additional factor affecting the supply of butter is global demand. U.S. exports of butter and milkfat through August 2010 totaled 85.9 million pounds and accounted for 8.3% of total butter production. The key destinations



for U.S. butterfat include the Middle East, North Africa, Mexico, and Russia. As long as the crude oil market remains strong and the U.S. dollar remains weak, export markets will likely continue to be strong outlets for U.S. butterfat.

Looking forward, the outlook for the U.S. butter price is largely dependent on the holiday sales period. If consumers ignore the price tag on butter and sales are within the historical average, U.S. butter stocks could enter 2011 at an all-time low. **MCT**



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