Dairy Situation and Outlook

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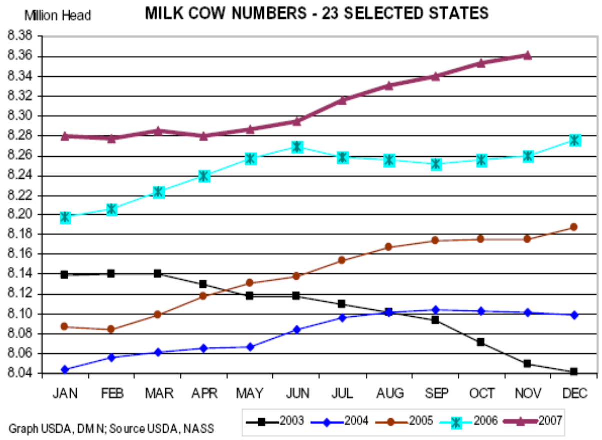
Year-end Milk Markets

Milk production continues to make large gains. November milk production for the 23 dairy states rose 3.8% from 1 year ago. Milk cow numbers were up by 101,000 while milk per cow was up by 40 pounds. Iowa milk production rose only 0.9% even though milk cow numbers were 6,000 higher. Iowa milk production was held back because milk per cow was 30 pounds lower, -0.88%.

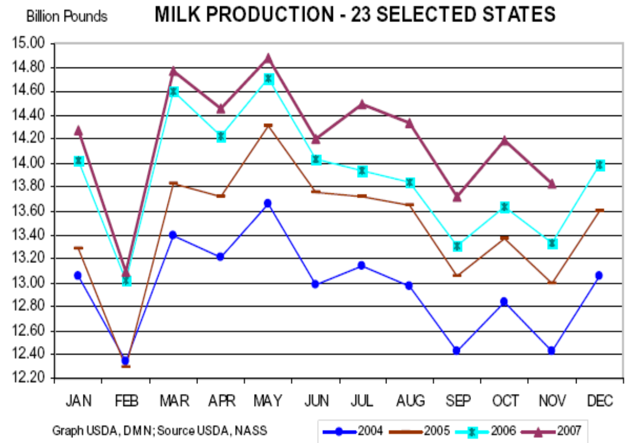
Milk Production: Selected Dairy States, November 2007

State	thousands 2006 cow numbers	thousands 2007 cow numbers	% change cow numbers	pounds 2006 milk per cow	pounds 2007 milk per cow	% change milk/cow	million pounds 2006 total milk production	million pounds 2007 total milk production	% change total milk
Iowa	209	215	2.87%	1620	1590	-1.85%	339	342	0.88%
MN	450	463	2.89%	1495	1490	-0.33%	673	690	2.53%
WI	1245	1249	0.32%	1500	1545	3.00%	1868	1930	3.32%
IL	103	103	0.00%	1510	1470	-2.65%	156	151	-3.21%
CA	1782	1829	2.64%	1760	1810	2.84%	3136	3310	5.55%
CO	113	120	6.19%	1870	1885	0.80%	211	226	7.11%
ID	497	522	5.03%	1790	1800	0.56%	890	940	5.62%
NM	360	337	-6.39%	1650	1780	7.88%	594	600	1.01%
PA	550	550	0.00%	1560	1580	1.28%	858	869	1.28%
NY	626	626	0.00%	1515	1575	3.96%	948	986	4.01%
TX	342	349	2.05%	1675	1770	5.67%	573	618	7.85%
23-State	8260	8361	1.22%	1614	1654	2.48%	13332	13833	3.76%

Milk cow numbers have been increasing month-to-month since May 07. Since July monthly year-over-year milk production increases have been over 3%. Strong milk prices, even in the face of much higher feed costs, have encouraged dairy producers to keep cows and build herd numbers. Dairy cow slaughter in November was down 27,200 from October and 1600 less than November 06.



Source: Dairy Market News



Source: Dairy Market News

Dairy Product Demand

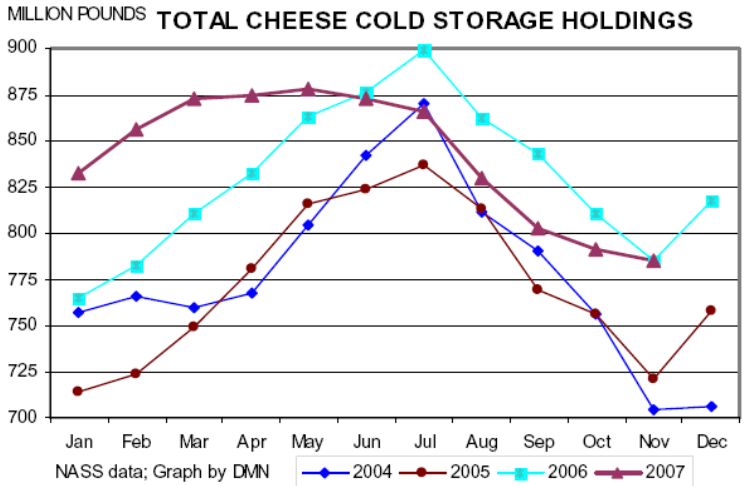
Cheese prices have been on a roller coaster the past six weeks. A new record price for 40-pound block cheddar blocks was set Nov 26 07, $2.2025 per pound. They declined nearly 10% three days later but rebounded to $2.1925 on Dec 12. On Dec 31 block cheese traded at $2.03, up $0.025 from the previous Friday. Barrel cheese finished at $1.98. Much of the price movement has been due to bids and offers rather actual sales according to Dairy Market News. The first Dairy Market News of 2008 comments that the cheese market remains firm. But cheese buyers are cautious at current prices.

Butter markets are weak with prices near year ago levels. Most butter makers appear to be at capacity. Butter sales have been slow however and inventory is building. Butter exports do appear good.

Nonfat dry milk (NDM) product sale prices are weakening due both to supply and demand factors. Cheese producers aren't using NDM as much as expected for cheese vat addition. Nor is export demand quite as strong since European prices are beginning to soften. Whey powders are also weakening. Stocks are building with little buying interest. Buyers are indicating little purchasing interest until the market settles. Dry whey producers are beginning to contact users to contract sales. But with dry product prices trending lower, that may be difficult.

Fluid milk consumption was lower for October 07, -1% and -0.2% year-to-date. The drop was in flavored milks while conventional milk was up 1%. Organic milk consumption continues to show strong gains, but is not large enough to affect decreases elsewhere.

Cheese in cold storage on Nov 30 was about equal to one year ago. From Jan-May, storage totals were above year ago, June about equal, and July-Oct below 2006



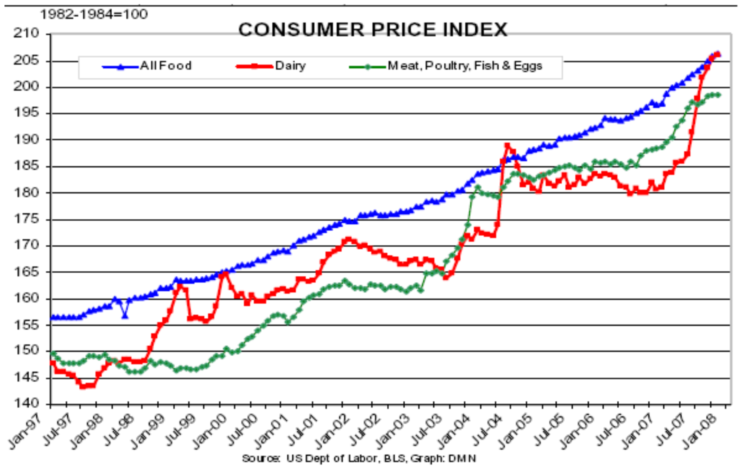
Source: Dairy Market News

Analysis

Milk prices appear to be headed for lower levels than we are now experiencing. Dr Robert Cropp is estimating an average first quarter 08 Class III price of $16.30, second quarter $15, third quarter $16.35 and fourth quarter $15.70. That would make an average Class III price at $15.85, $2 lower than 2007 but much above the 5-year average. The average Class III futures price for 2008 was $16.94 on December 28. 2007 Class III prices finished at a $20.49 average.

Lower prices could result if the apparent weakness of the US continues. Export demand has been a strong and one of the reasons 2007 milk prices raised so much. But reports are circulating that indicate export demand is weakening.

The most recent Milk-Feed ratio was 2.82 due to higher feed costs. A ratio below 3 usually indicates lower future milk production. That could be useful to maintain milk prices as the US weakens and dairy product demand slackens. Some commentators have remarked that Very high milk prices are followed 18 months later by a new low. If that bears out, it would put milk prices at a low point about Oct 2008. We have been having anti-historical corn patterns lately, maybe milk will follow.


1982-1984=100
CONSUMER PRICE INDEX
All Food
Dairy
Meat, Poultry, Fish & Eggs
210
205
200
195
190
185
180
175
170
165
160
155
150
145
140
Jan-97
Jul-97
Jan-98
Jul-98
Jan-99
Jul-99
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Jan-08
Source: US Dept of Labor, BLS, Graph: DMN