



The KDM Dairy Report - July 9th, 2004

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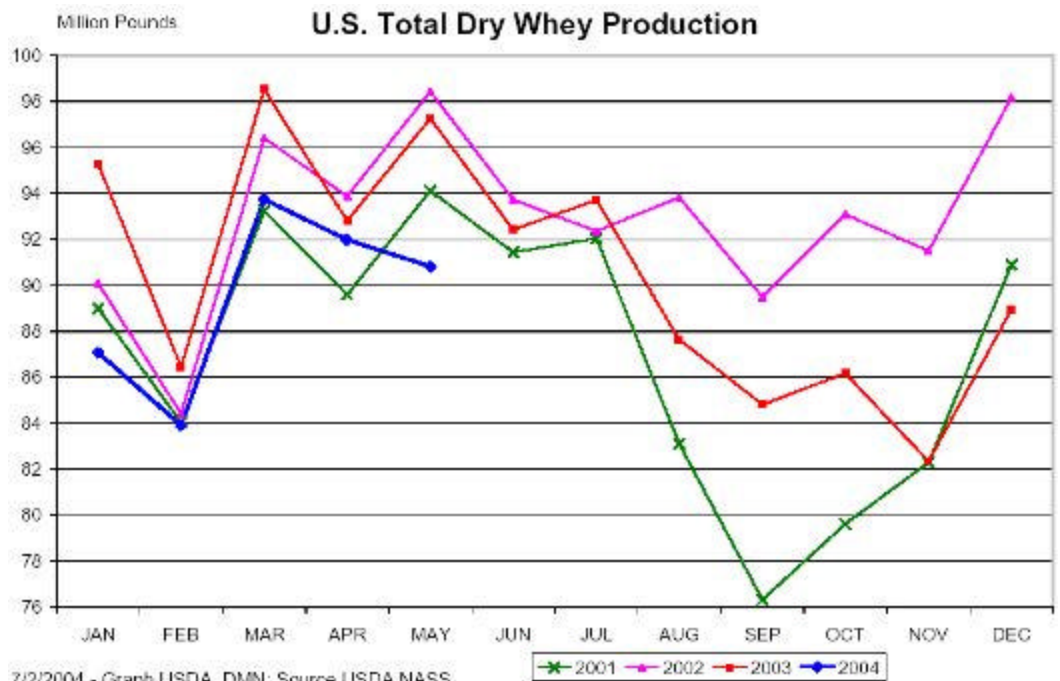
On the bright side:

- Last Friday's Dairy Products Report showed a significant drop in dry whey production see chart below). According to USDA, May output was the lowest since 1985. That should help support the price at near current historical highs.
- Fluid Milk & Cream Review reports this week that the hot, muggy weather is causing Florida production to drop at a more rapid pace. Florida shipped only 45 loads of milk out-of-state this week, vs. 101 last week (a 55% drop), and should become a milk deficit state again within a month.
- Economy: US jobless claims fell to their lowest levels since October of 2000, according to figures released by the U.S. Labor Department released this week. The drop in claims far exceeded analyst expectations, and is a sign of an improving labor market.
- Only 12 loads of blocks and 1 load of barrels were traded this week in the cash cheese market, down significantly from prior weeks. Despite reports of burdensome inventory, suddenly sellers are have disappeared.

Futures Month	Friday 07/09	Friday 07/02	Change	Avg Since 1995	Top 3rd Price	Top 5th Price
Jul - 04	\$14.78	\$14.90	(\$0.12)	\$12.46	\$13.38	\$14.28
Aug - 04	\$13.38	\$13.65	(\$0.27)	\$13.16	\$14.17	\$15.17
Sep - 04	\$14.06	\$13.83	\$0.23	\$13.61	\$14.59	\$15.56
Oct - 04	\$13.55	\$13.50	\$0.05	\$12.98	\$13.82	\$14.65
Nov - 04	\$12.92	\$12.80	\$0.12	\$11.92	\$12.97	\$14.00
Dec - 04	\$12.40	\$12.35	\$0.05	\$11.92	\$12.97	\$14.01
Jan - 05	\$12.39	\$12.34	\$0.05	\$11.89	\$12.71	\$13.52
Feb - 05	\$12.35	\$12.28	\$0.07	\$11.34	\$11.90	\$12.45
Mar - 05	\$12.32	\$12.32	\$0.00	\$11.66	\$12.34	\$13.01
Apr - 05	\$12.46	\$12.35	\$0.11	\$12.08	\$13.31	\$14.52
May - 05	\$12.40	\$12.35	\$0.05	\$12.21	\$13.60	\$14.98
Jun - 05	\$12.70	\$12.65	\$0.05	\$12.26	\$13.38	\$14.49
Jul - 05	\$12.99	\$12.99	\$0.00	\$12.46	\$13.38	\$14.28
Aug - 05	\$13.40	\$13.40	\$0.00	\$13.16	\$14.17	\$15.17
Sep - 05	\$13.40	\$13.40	\$0.00	\$13.61	\$14.59	\$15.56
Oct - 05	\$12.70	\$12.70	\$0.00	\$12.98	\$13.82	\$14.65
Nov - 05	\$12.35	\$12.35	\$0.00	\$11.92	\$12.97	\$14.00

however....

- NASS averages continued easing down. 40 pound blocks fell 4.6¢ to \$1.75/lb, while barrels dropped 5.4¢ to \$1.73/lb vs. last week. Butter decreased 12.9¢ to \$1.89/lb, NDM decreased 0.4¢ to 84.5¢/lb and dry whey decreased 0.9¢ to 27¢/lb. Expect a more significant drop in the cheese price next week, as the lag in the NASS prices catches up to the recent fall in cash prices.
- Dairy cow slaughter for the week ending 06/26 was 6,000 head fewer than the same period a year ago, representing a drop of 12.8%.
- Milk output remains seasonally strong in California, and they expect a large number of cows will be freshening in July, according to Fluid Milk & Cream Review. The delay is a result of the heat last summer, when cows couldn't get pregnant until fall.
- Dairy Market News reports current cheddar stocks are long, and plant inventories have yet to decline appreciably, as



buyers continue to delay purchases in hopes of lower prices.

- Cash cheese continued to ease lower, with blocks down 5¢ vs. a week ago, to settle at \$1.36/lb today, and barrels dropped 2.5¢ to \$1.3575/lb. Butter also finished lower for the week, falling 3.25¢ to \$1.8625/lb.

Recommendation:

Lackluster trade in a holiday shortened week resulted in very low trade volumes and a sideways market which saw the front months lose ground, and the deferred months make small gains. Cash cheese has seemed to find some support at the \$1.36 level, as we saw unfilled bids come in for the first time in several weeks. That did little, however, to convince the trade that we've hit bottom, as prices tended to drift lower on no news in the afternoons.

Next Friday, the Milk Production Report will be released, which should offer some guidance to the market, however, with cool weather prevailing over much of the country in June, it could end up having a negative affect on prices. Curiously, volume in the cash cheese market has dried up as well, despite the ominous inventory levels being reported. It could be that there is a lack of "under 30-day" aged cheddar available, which is what trades on the CME, since 450+ loads were purchased the past couple months. Or, sellers might not be as willing to offload their product at these prices, in hopes of a rebound later this summer. Meanwhile, cheese buyers remain on the sidelines for the most part, waiting for the bottom. One cheese plant we work with did report an increase in orders this week, and said that the phone would ring "off the hook" should the cash price start to move higher.

While we're reluctant to sell August at current prices, the fact is, they could continue to drop without some summer heat and a growing economy to improve demand. Look to sell August on any bumps higher in the market, then immediately buy an August CALL option to protect your upside. Today, you could have sold August at close to \$13.50, then bought a \$14.00 CALL for 27¢.

For 2005, our recommendation remains unchanged. The March '05 contract is still above its top 1/3 historical price, so look at selling 20-50% of your milk, at or slightly above current price levels. The current January through June average is \$12.44, which represents a good historical price for these months.

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