



The KDM Dairy Report - July 16th, 2004

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On the bright side:

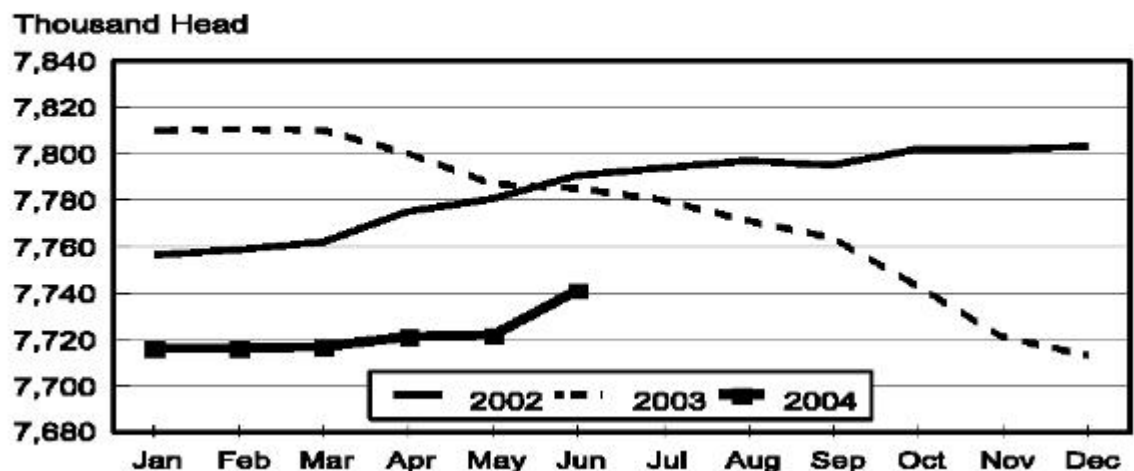
- Milk Production Report: June marked the 11th straight month of declining milk production, but once again, only by a whisker. June output in the 20 major states was 12.4 billion lbs, down 0.2% vs. June 2003. For all 50 states, production was down 0.4%, while the number of milk cows declined 44,000 head.
- Late Friday afternoon, CWT announced it had raised the target price for its export assistance program by a dime, to \$1.40 per pound for cheese, and \$1.30 per pound for butter.
- After the CWT announcement, spot cheese was immediately bid up on Monday to \$1.4050, and recorded a gain of 10¢ for the week to finish at \$1.46. Barrels were bid up as well to maintain a 3¢ spread, increasing 7.25¢ for the week to \$1.43. Only two loads of blocks traded all week, and no barrels.
- Hot and humid conditions have finally arrived in the Southwest, with the forecast calling for more of the same.
- Jerry Dryer writes in the most recent Food & Dairy Market Analyst, that retail sales of cheese are, "better than many expected", though process sales are weak.
- Economy: Food and energy prices fell slightly in June according to government numbers, easing worries that inflation was taking hold.

however....

- Milk Production Report: While June production was down vs. a year ago, May production was revised up 13 million lbs, or 0.1%, making May 2004 production only 6 million lbs less, or statistically even with May 2003. In addition, while lower than a year ago, the number of milk cows climbed 19,000 head month-to-month, and though California dropped 10 lbs of milk per cow, they added 41,000 head to increase output by 1.9%. Finally, despite the shortage of Posilac, output per cow was 7 lbs above year ago levels.
- NASS averages for cheese took their expected plunge, with blocks down 15.5¢ to \$1.60 and barrels down 16.7¢ to

Futures Month	Friday 07/16	Friday 07/09	Change	Avg Since 1995	Top 3rd Price	Top 5th Price
Jul - 04	\$14.69	\$14.78	(\$0.09)	\$12.46	\$13.38	\$14.28
Aug - 04	\$13.79	\$13.38	\$0.41	\$13.16	\$14.17	\$15.17
Sep - 04	\$14.55	\$14.06	\$0.49	\$13.61	\$14.59	\$15.56
Oct - 04	\$13.75	\$13.55	\$0.20	\$12.98	\$13.82	\$14.65
Nov - 04	\$12.85	\$12.92	(\$0.07)	\$11.92	\$12.97	\$14.00
Dec - 04	\$12.55	\$12.40	\$0.15	\$11.92	\$12.97	\$14.01
Jan - 05	\$12.55	\$12.39	\$0.16	\$11.89	\$12.71	\$13.52
Feb - 05	\$12.45	\$12.35	\$0.10	\$11.34	\$11.90	\$12.45
Mar - 05	\$12.54	\$12.32	\$0.22	\$11.66	\$12.34	\$13.01
Apr - 05	\$12.35	\$12.46	(\$0.11)	\$12.08	\$13.31	\$14.52
May - 05	\$12.37	\$12.40	(\$0.03)	\$12.21	\$13.60	\$14.98
Jun - 05	\$12.45	\$12.70	(\$0.25)	\$12.26	\$13.38	\$14.49
Jul - 05	\$12.85	\$12.99	(\$0.14)	\$12.46	\$13.38	\$14.28
Aug - 05	\$13.20	\$13.40	(\$0.20)	\$13.16	\$14.17	\$15.17
Sep - 05	\$13.20	\$13.40	(\$0.20)	\$13.61	\$14.59	\$15.56
Oct - 05	\$12.65	\$12.70	(\$0.05)	\$12.98	\$13.82	\$14.65
Nov - 05	\$12.35	\$12.35	\$0.00	\$11.92	\$12.97	\$14.00

Monthly Milk Cows 20 States



\$1.56. Butter dropped 2¢ to \$1.87 while dry whey continued moving away from its 30¢ recent high, falling 0.7¢ to 26.2¢/lb.

- Weekly dairy cow slaughter for the week ending 07/03 was 39,500 head, down 1,800 head, or 4.4%
- Fluid Milk & Cream Review reports that milk flow in the Southeast is not falling as quickly as anticipated. They also note the weakness in fluid cream demand, with excess supply and "loads looking for a home".
- We've heard rumors from more than one source that Monsanto may increase their Posilac allocation from 50%, to 60-70%, before the end of the year, depending on inventory levels.
- Cash butter dropped 20¢ from last Friday, settling at \$1.66 today, with a total of 45 loads exchanging hands for the week.

Recommendation:

Following the CWT press release Friday, blocks were bid higher on Monday to meet the new support level of \$1.40, giving the Class III market a psychological bump. Then, the same bidder pushed the price up to \$1.45 unopposed on Wednesday which moved the markets even higher. On Thursday, the same bidder was there again, only this time, after bidding blocks up a penny, a load was sold at \$1.46. When the buyer didn't come back to bid on another load, the markets reversed course, as sellers

determined the cheese price wasn't going any higher, and futures were trading at a premium to cash. Prices continued to erode today over nervousness about the production report, and the possibility of higher output due to the cool June we had nationally. With production actually declining, we expect the markets to open higher on Monday in response. However, the Cold Storage report will be released on Wednesday, which could put a damper on things. The report for May showed a 4% increase in American Cheese holdings, and we all know a lot more cheese was purchased on the cash market in June.

At this time, we're not recommending any long-term sales in 2004. The new cheese support at \$1.40 works out to about a \$12.50 floor price, so selling November or December at just slightly north of those numbers is not gaining you much protection. We think another run on the cheese price is possible later this year, and would look to add more sales or purchase PUT options at that time.

We still believe 2005 offers good value, with the January through June average at \$12.45.

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CME Milk Futures

