



The KDM Dairy Report – September 24th, 2004

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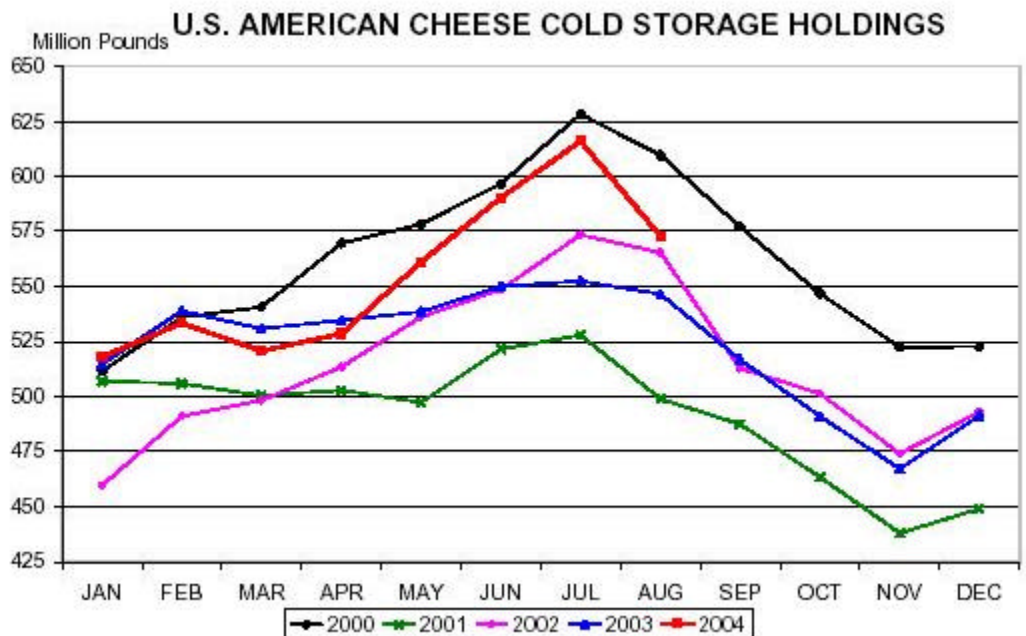
On the bright side:

- Cold Storage Report: The commercial American cheese drawdown for August was the 2nd largest in history (see chart), according to Daily Dairy Report. While still above year ago levels, they dropped 7% vs. the previous month. July stocks were also revised down 5.7 million lbs. Total cheese stocks were also lower, falling 6% vs. July. Finally, butter stocks were down a whopping 16% from last month, and 36% vs. a year ago.
- Americans are eating more cheese than ever, according to survey results released Tuesday. Consumption is up more than 30 lbs per person annually.
- NASS numbers released today work out to a supportive \$14.69 Class III price. Blocks were \$1.57, barrels were \$1.56, butter at \$1.77, NDM at 86.5¢ and dry whey came in at 21.6¢.
- Weekly cold storage numbers are showing butter stocks down 19% since the first of the month. Cheese stock were down 2%.
- Fluid Milk & Cream Review reports that milk supplies are tight in the Midwest, and that manufacturing milk demand remains strong.
- Papa Murphy's chain of 'take-n-bake' pizza stores is planning to add 130 new stores in 2005, nearly double their normal rate of expansion.
- An article in this week's Cheese Reporter indicates 2004 cheese exports may reach record levels - exports were up 16% in the first half of the year.

Futures Month	Friday 09/24 Close	Friday 09/17 Close	Change	Avg Since 1995	Top 3rd Price	Top 5th Price
Sep-04	\$14.72	\$14.65	\$0.07	\$13.61	\$14.59	\$15.56
Oct-04	\$13.95	\$13.60	\$0.35	\$12.98	\$13.82	\$14.65
Nov-04	\$12.89	\$12.75	\$0.14	\$11.92	\$12.97	\$14.00
Dec-04	\$12.44	\$12.25	\$0.19	\$11.92	\$12.97	\$14.01
Jan-05	\$12.15	\$12.07	\$0.08	\$11.89	\$12.71	\$13.52
Feb-05	\$12.10	\$12.03	\$0.07	\$11.34	\$11.90	\$12.45
Mar-05	\$12.10	\$12.15	(\$0.05)	\$11.66	\$12.34	\$13.01
Apr-05	\$12.01	\$12.05	(\$0.04)	\$12.08	\$13.31	\$14.52
May-05	\$12.09	\$12.00	\$0.09	\$12.21	\$13.60	\$14.98
Jun-05	\$12.35	\$12.45	(\$0.10)	\$12.26	\$13.38	\$14.49
Jul-05	\$12.78	\$12.81	(\$0.03)	\$12.70	\$13.62	\$14.53
Aug-05	\$13.15	\$13.15	\$0.00	\$13.25	\$14.21	\$15.16
Sep-05	\$13.38	\$13.45	(\$0.07)	\$13.61	\$14.59	\$15.56
Oct-05	\$12.75	\$12.85	(\$0.10)	\$12.98	\$13.82	\$14.65
Nov-05	\$12.15	\$12.15	\$0.00	\$11.92	\$12.97	\$14.00
Dec-05	\$12.05	\$12.05	\$0.00	\$11.92	\$12.97	\$14.01
Jan-06	\$11.80	\$11.80	\$0.00	\$11.89	\$12.71	\$13.52

however....

- Livestock Slaughter Report: Dairy cow slaughter is off 15.8% year-to-date. From Jan - Aug 2004, 1,553,800 animals were culled vs. 1,845,200 during the same period a year ago.
- Milk receipts in California continue to rise, and are above last year's levels, according to Fluid Milk & Cream Review.
- Cheese yields continue to be higher than normal for this time of year, according to Dairy Market News. In addition, increased production of cheese is encouraging more movement of NDM to cheese plants.



- 55 loads of blocks had to be purchased this week on the CME cash cheese market to hold prices steady at \$1.5675/lb. Sales on 7 loads of barrels caused the price to drop 2.75¢ from the previous week, to settle at \$1.5025 today.
- Cash butter fell 11.25¢ to settle at \$1.75/lb today. Buyers purchased 34 loads during the week.

Recommendation:

While demand for current cheese and butter appears to be good, we continue to be concerned about the deferred contracts. Rising milk production, higher cow numbers, a slow cull rate and cheaper feed don't usually add up to higher milk prices long term. While the economy and dairy demand appear to be improving, reports of renewed expansion out West and new dairy construction in the Texas panhandle cause us to

wonder if current prices in the last nine months of 2005 can be maintained. On the bright side, commercial buyers still remember the high prices they were forced to pay this year, and continue to hedge their upside risk by buying 2005 contracts at current levels. This gives us the chance to protect some milk.

At this time, we would leave the balance of 2004 open to the market, unless the current rally reaches levels that justify putting floor price protection in place. For 2005, look to sell April - Dec at a \$12.50 average or higher, then buy cheap upside protection in the form of 30-40¢ CALL options for selected months. Or, our recommendation of the last few reports, to buy \$11.00 or \$11.25 PUT options would be another alternative.

Give us a call if you'd like help setting up a marketing plan for your operation!

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