



The KDM Dairy Report - August 19th, 2005

On the bright side:

- Weekly cold storage stats for the first half of August show butter stocks down 7% and [cheese stocks down 1%](#).
- Butter stocks at CME-approved warehouses continues to fall and is now [16.8% below last year's](#) levels. 86.7 million lbs are on hand vs. 104.3 million a year ago.
- Interest in manufacturing milk is improved, with spot loads going for \$1-2 over class, according to Fluid Milk & Cream Review. Demand for ice cream has been good, with some plants [running 6-day schedules to keep up](#) with orders.
- 204 loads of Grade A milk were sent to the Southeast part of the country this week, an increase of 39 loads from last week.
- Dairy Market News reports that churners would like to put more butter away for the holiday season, but are finding it difficult to do so. Butterfat [levels are much lower](#) than usual for this time of year.
- The barrel [supply is tight to short](#), according to Dairy Market News, and has resulted in an inverted barrel to block price.
- Cash cheese came off its lows, with blocks gaining 6¾¢ to settle at \$1.47 today, while barrels gained 12¢ to close at \$1.48. 19 loads of blocks trade, and no barrels.

Futures Month	Friday 08/19 Close	Friday 08/12 Close	Change	Avg Since 1995	Top 3rd Price	Top 5th Price
Aug-05	\$13.58	\$13.54	\$0.04	\$13.25	\$14.21	\$15.16
Sep-05	\$13.95	\$13.84	\$0.11	\$13.72	\$14.66	\$15.58
Oct-05	\$13.75	\$13.96	(\$0.21)	\$13.10	\$13.91	\$14.71
Nov-05	\$13.40	\$13.53	(\$0.13)	\$12.22	\$13.29	\$14.34
Dec-05	\$13.18	\$13.44	(\$0.26)	\$12.34	\$13.49	\$14.61
Jan-06	\$12.65	\$12.86	(\$0.21)	\$12.10	\$12.93	\$13.74
Feb-06	\$12.53	\$12.70	(\$0.17)	\$11.64	\$12.33	\$13.00
Mar-06	\$12.55	\$12.71	(\$0.16)	\$11.88	\$12.60	\$13.30
Apr-06	\$12.49	\$12.75	(\$0.26)	\$12.31	\$13.52	\$14.71
May-06	\$12.55	\$12.74	(\$0.19)	\$12.35	\$13.69	\$15.01
Jun-06	\$12.74	\$12.90	(\$0.16)	\$12.41	\$13.50	\$14.56
Jul-06	\$13.18	\$13.25	(\$0.07)	\$12.85	\$13.75	\$14.64
Aug-06	\$13.24	\$13.25	(\$0.01)	\$13.25	\$14.21	\$15.16
Sep-06	\$13.53	\$13.52	\$0.01	\$13.72	\$14.66	\$15.58
Oct-06	\$12.97	\$12.95	\$0.02	\$13.10	\$13.91	\$14.71
Nov-06	\$12.84	\$12.80	\$0.04	\$12.22	\$13.29	\$14.34
Dec-06	\$12.79	\$12.77	\$0.02	\$12.34	\$13.49	\$14.61

however....

- Milk Production Report: July milk [production was up 4.2%](#) in the 23 major states, and up 3.9% for all 50 states. Production per cow was up 59 lbs vs. last year and the milking herd grew by 48,000 head. 12,000 head were added in July alone. Gains were led by CO up 13.8%, ID up 13.4% and TX up 11%. Despite 4,000 fewer cows and July heat, WI was up 4.9% on a gain of 80 lbs/cow. The lone bright spot was CA, up only 1.5% despite 30,000 more cows due to a loss in production of 5 lbs/cow.
- Livestock Slaughter Report: Dairy cow slaughter for the month of July was 162,400 head, down 12.4% vs. a year ago, and the [lowest monthly cull number in 16 years](#), according to today's Daily Dairy Report. Ouch! YTD, dairy cow slaughter is down 6.6%.
- The recent drop in cash cheese prices finally caught up to NASS numbers. [Blocks dropped 7.5¢](#) this week to average \$1.39/lb, while barrels fell 4¢ to \$1.41/lb.
- Dairy cow slaughter for the week ending 08/06 was [down 13.7%](#) vs. the same period a year ago. Only 38,800 head were culled vs. 45,000 last year.
- Mexico has [imposed a 30% tariff](#) on "food prep powder", which will impact NDM exports.

Recommendation:

We've been talking about selling some of 2006 for awhile now, and Monday's big production report was enough incentive for some producers to begin hedging. The annual average dropped 10¢ to \$12.84, while the first half of the year was down by an average 20¢.

The front months were hit hard too, with double-digit losses for the week Oct-Dec. Aug and Sep rallied off their lows and finished higher due to the move in cash cheese.

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The cash market is quite confusing at the moment, with buyers and sellers both practicing price discovery. As a result, we saw up and down trade during some sessions.

Our recommendation remains the same this week. While the front months may recover with a move up in cheese, we don't expect to see \$15-16 milk. The risk reversal is a great way to establish a floor with limited upside range. Buy the October 13.50 put for 28¢ and sell the 14.50 call for 15¢ for a net cost of 13¢. The result gives you floor price protect at the strike price of the put, and a ceiling or cap at the strike price of the call. Do the same for November and December. Give us a call and we'll help you put together a plan.

For 2006, continue to target above \$12.90 for the year, or \$12.80 for the first half.

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