



The KDM Dairy Report - October 28th, 2005

On the bright side:

- Weekly cold storage numbers showed a [drawdown in both cheese and butter](#) stocks in October. For the period 10/01 through 10/24, butter inventories fell 10% and cheese stocks dropped by 2%.
- Dairy cow slaughter for the week ending 10/15 was [48,100 head vs. 45,100](#) during the same period a year ago. The increase is likely due to the CWT herd retirement program getting started, but good news nonetheless.
- Replacement animals are still expensive. Dairy Market News reports Supreme quality fresh milking cows sold at a Wisconsin dairy auction ranged from \$2,100 - \$2,550 per head. Supreme quality springing heifers were sold for \$2,100 - \$2,225 per head. This is approximately \$100 more per head than a month ago.
- Economy: Third quarter [GDP rose 3.8%](#) despite hurricanes and high energy prices, according to figures released by the Commerce Department. The number beat expectations of analysts, who had expected a rise of 3.5%.

Futures Month	Friday 10/28 Close	Friday 10/21 Close	Change	10-yr Average	Top 3rd Price	Top 5th Price
Oct-05	\$14.39	\$14.39	\$0.00	\$13.10	\$13.91	\$14.71
Nov-05	\$13.57	\$13.67	(\$0.10)	\$12.22	\$13.29	\$14.34
Dec-05	\$13.36	\$13.51	(\$0.15)	\$12.34	\$13.49	\$14.61
Jan-06	\$12.95	\$13.04	(\$0.09)	\$12.10	\$12.93	\$13.74
Feb-06	\$12.60	\$12.70	(\$0.10)	\$11.64	\$12.33	\$13.00
Mar-06	\$12.65	\$12.77	(\$0.12)	\$11.88	\$12.60	\$13.30
Apr-06	\$12.50	\$12.61	(\$0.11)	\$12.31	\$13.52	\$14.71
May-06	\$12.55	\$12.57	(\$0.02)	\$12.35	\$13.69	\$15.01
Jun-06	\$12.65	\$12.76	(\$0.11)	\$12.41	\$13.50	\$14.56
Jul-06	\$13.18	\$13.15	\$0.03	\$12.85	\$13.75	\$14.64
Aug-06	\$13.42	\$13.45	(\$0.03)	\$13.28	\$14.19	\$15.09
Sep-06	\$13.66	\$13.75	(\$0.09)	\$13.78	\$14.67	\$15.54
Oct-06	\$13.17	\$13.18	(\$0.01)	\$13.10	\$13.91	\$14.71
Nov-06	\$12.85	\$12.90	(\$0.05)	\$12.22	\$13.29	\$14.34
Dec-06	\$12.78	\$12.76	\$0.02	\$12.34	\$13.49	\$14.61

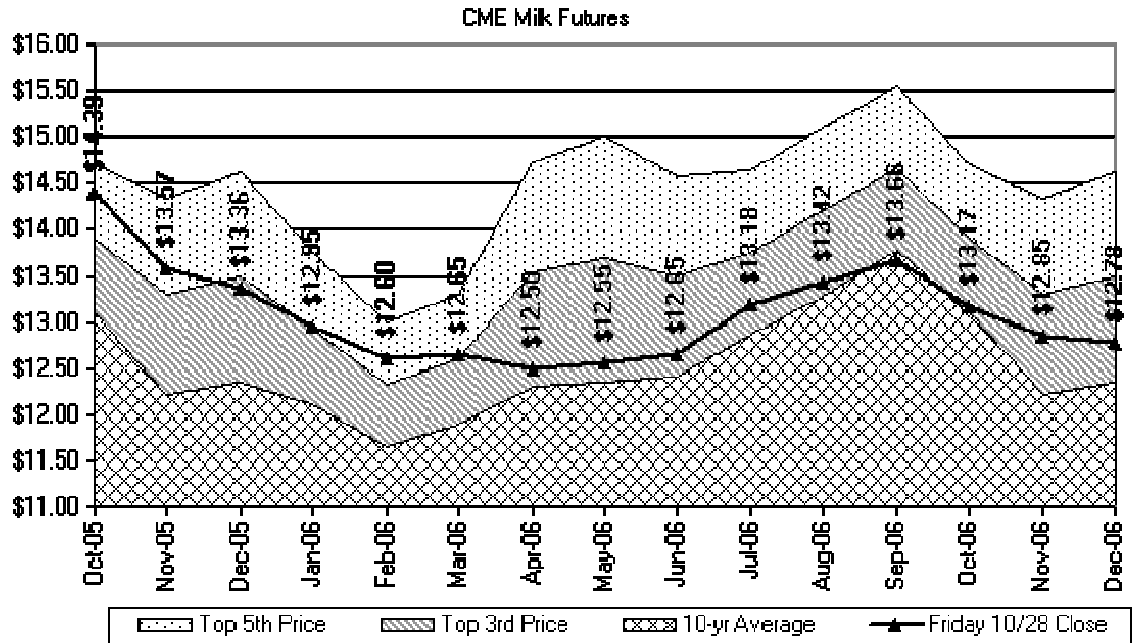
however....

- The cash cheese market held through Wednesday, but then [eroded on Thursday and Friday](#). Blocks lost 6¾¢ during the week to settle at \$1.40/lb today, while barrels fell 4¢ to \$1.35/lb. Butter shed 5¾¢ from last Friday, closing at \$1.57¾/lb.
- Commercial Disappearance: Updated numbers for August paint a mainly negative picture. Demand for American cheese was [down 4.6%](#) vs. a year ago, while butter demand was [down 4.9%](#) and nonfat dry milk was down 4.2%.
- NASS surveyed prices for cheese [continued to move lower](#) this week. Blocks fell 4¢ to \$1.47/lb and barrels dropped 3½¢ to \$1.42/lb.
- Fluid Milk & Cream Review reports that [Class I interest is slow](#) in the Midwest, with lighter interest in the spot market. At the same time, cream supplies are heavy, with most going into butter production.
- Despite the disruptions caused by Hurricane Wilma in Florida and the Southeast, Fluid Milk & Cream Review reports that [milk supplies are long](#) and manufacturing schedules are being stepped up to handle the extra milk.
- Weather is favorable and [more cows are expected to freshen](#) in the coming weeks in California, according to Fluid Milk & Cream Review.
- Butter handlers expect holiday [orders to be average at best](#), according to Dairy Market News. Butter production is quite heavy, and with butter stocks higher than a year ago, they don't expect prices to rally like they did last year.

- Dairy Market News has the cheese market “weak” due to [slow to fair interest in cheddar](#) and American varieties.
- Cheap feed. Grain prices continue to grind lower. Dec corn breached \$2/bushel this week and with piles at elevators getting ever larger, bean and meal prices look to continue the trend lower as well.

Recommendation:

The good news is it appears we have a very resilient economy. Despite significantly higher energy costs and natural disasters, the economy continues to create jobs and increase output. In light of growing milk production, we'll need a strong economy next year to consume the



higher dairy output that looks headed our way. If this week was any sign, however, it's not starting out very positive. Aggressive block buying in the cash market fizzled out on Thursday, with selling getting the upper hand, in spite of what should be a seasonal push for product. We may see another wave of buying over the coming weeks, but for now, supply looks to be more than adequate for needs. The sell-off in the cash market awoke producers, who sold the 2006 contracts more aggressively to get covered.

Short-term: Early in the week we continued to buy November \$13.75 put options for between 11-12¢. The best offer at the close of today's trade was 32¢, so we're glad we were able to purchase what we did. It's a tough call now what to do with November and December. For November, you could sell futures or to your plant at \$13.60, then buy a \$13.75 call option for 4¢ in case it comes roaring back. The call would cover your sold position above \$13.75. We'd wait on December for another mini rally, knowing it may never come.

Long-term: We continue to have a negative outlook for 2006. We successfully sold Apr-Dec at \$13.00 average again several times this week. After today's losses, the average is now \$12.97. The annual average fell from \$12.97 to \$12.91. We would continue to sell Apr-Dec at \$13 average or higher. Sell January at \$13.10 or higher and February and March at \$12.90 or higher. Get 75% covered April through December.

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