



The KDM Dairy Report - November 18th, 2005

On the bright side:

- This week the CWT Export Assistance Program accepted a bid from DFA to [export 277,000 lbs of cheddar cheese](#) to South Korea.
- Though cheese prices continue to languish, prices for dry products remain strong. The NASS dry whey price hit 31¢, more than a [five-year high](#).
- For the first two weeks of November, butter stocks fell 8% and [cheese stocks fell 1%](#), according to weekly cold storage numbers.
- Dairy cow [slaughter numbers continue to benefit](#) from the CWT herd retirement program. 52,200 head were culled for the week ending 11/05 vs. 47,300 during the same period last year.
- Milk [supplies have tightened](#) in the Midwest, and Class I and II interest is up, according to Fluid Milk & Cream Review.
- Despite lower cheese prices, there is still [good demand for extra milk](#) from Western cheese makers. Fluid Milk & Cream Review reports orders for milk are higher this week, and handlers don't expect plants to have any problems processing milk volumes over the holiday period. And in the Pacific Northwest, dairy quality hay is in tight supply, with many buyers going home empty handed.
- Dairy Market News reports dry whey prices will likely [continue to trend higher](#) due to limited availability and fuel surcharges.
- Butter [demand is strong](#), according to Dairy Market News. But they caution it might only be a reaction to recent price declines. They also report that above quota imports are only 522,000 lbs year-to-date, vs. 18.0 million lbs at this time last year.

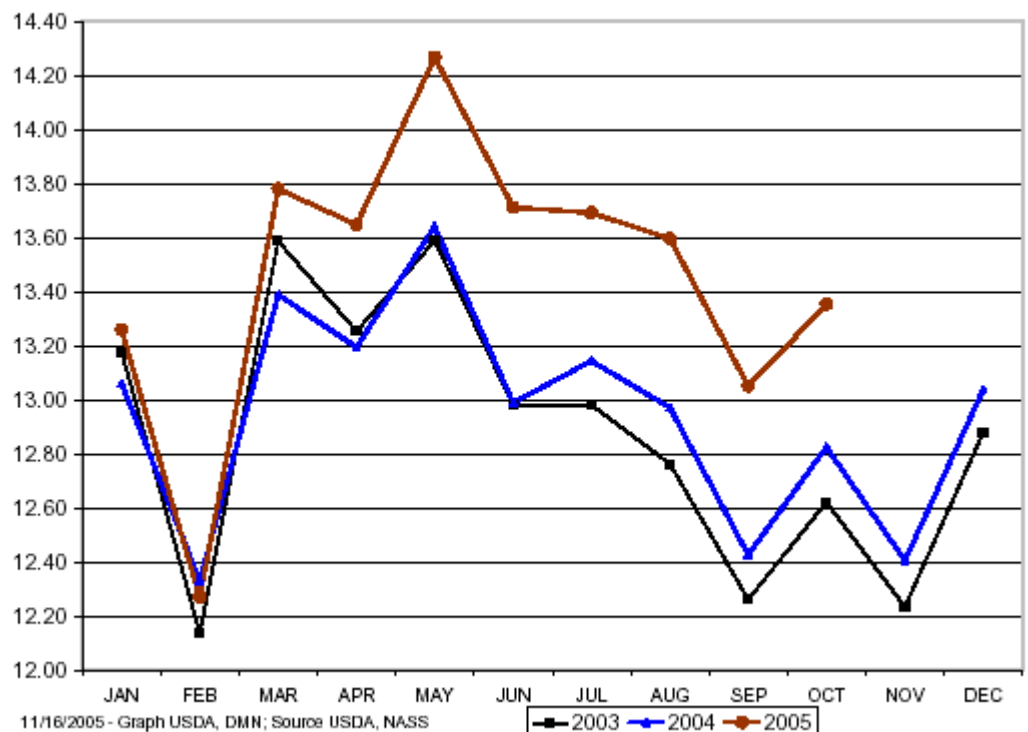
Futures Month	Friday 11/18 Close	Friday 11/11 Close	Change	10-yr Average	Top 3rd Price	Top 5th Price
Nov-05	\$13.35	\$13.38	(\$0.03)	\$12.22	\$13.29	\$14.34
Dec-05	\$12.92	\$13.02	(\$0.10)	\$12.34	\$13.49	\$14.61
Jan-06	\$12.66	\$12.86	(\$0.20)	\$12.10	\$12.93	\$13.74
Feb-06	\$12.49	\$12.62	(\$0.13)	\$11.64	\$12.33	\$13.00
Mar-06	\$12.51	\$12.54	(\$0.03)	\$11.88	\$12.60	\$13.30
Apr-06	\$12.47	\$12.47	\$0.00	\$12.31	\$13.52	\$14.71
May-06	\$12.50	\$12.51	(\$0.01)	\$12.35	\$13.69	\$15.01
Jun-06	\$12.62	\$12.61	\$0.01	\$12.41	\$13.50	\$14.56
Jul-06	\$13.20	\$13.17	\$0.03	\$12.85	\$13.75	\$14.64
Aug-06	\$13.45	\$13.42	\$0.03	\$13.28	\$14.19	\$15.09
Sep-06	\$13.69	\$13.65	\$0.04	\$13.78	\$14.67	\$15.54
Oct-06	\$13.21	\$13.15	\$0.06	\$13.21	\$14.00	\$14.77
Nov-06	\$12.90	\$12.87	\$0.03	\$12.22	\$13.29	\$14.34
Dec-06	\$12.82	\$12.76	\$0.06	\$12.34	\$13.49	\$14.61

however....

- Milk Production Report: Milk output was [up more than 4% for the sixth straight month](#). October production in the 23 major states was up 4.1% vs. a year ago, led by Idaho up 13.2%, Texas up 9.4% and New Mexico up 8.1%. Wisconsin continued to show strong gains, up 4% on virtually unchanged cow numbers. The number of milk cows on farms was 58,000 head more than a year ago, and 4,000 more than September 2005. Output per cow in October was 1,636 lbs, 53 pounds higher than last year.

Billion Pounds

MILK PRODUCTION - 23 SELECTED STATES



- Livestock, Dairy & Poultry Outlook Report: USDA reports that the trend of heavier milk supplies will probably be felt after holiday needs are met. They expect [dairy prices to head lower](#) as demand is overcome by supply, and are now forecasting a 2006 Class III annual average of \$12.30.
- NASS surveyed prices for butter and cheese [continued to grind lower](#). 40lb blocks fell 3.8¢ to average \$1.40/lb, 500lb barrels dropped 2.6¢ to \$1.38/lb and butter plunged 8.3¢ to \$1.46/lb.
- Fluid milk supplies in the Southeast are [more than ample](#) leading into the Thanksgiving holiday, according to Fluid Milk & Cream Review.

Recommendation:

Cash cheese managed a small ¼¢ gain this week, closing today at \$1.37¼. Barrels managed to climb 2¢ to \$1.34¼ on what was largely a “window-dressing” move to get the spread back to 3¢. Cash butter managed a 4½¢ increase to settle at \$1.44½.

This type of price gain is nothing to get excited about. Commercial contacts we talked to indicated

a few users needed a few loads of cheese but were doubtful about their long-term needs. The significant drop in the 2006 first quarter contracts indicates to us that traders aren’t convinced cheese will be able to hold above \$1.35 after the first of the year. They may be right. Despite the CWT programs, cheese plants we talked to this week weren’t having any trouble getting extra milk, and why should they? October production was up more than 4%. In addition, orders appear to be on again, off again; not the type of high demand situation we’d like to see at this time of year. This comes from a Midwest perspective, but we can’t be all that different from the rest of the country. Finally, word from the dairy pit hints that long hedgers (commercial users) are further along on their hedge programs than people think. The supportive buying we saw today, for example, may dry up soon. Yes, it’s tough to sell your milk when it looks like prices are going up, but when the buyers are gone, who will you sell to? Chances are it will be at a much lower price.

Short-term: Sell December at \$12.95 or higher, then buy a \$13.00 call for 7¢ to protect your upside.

Long-term: We continue to have a negative outlook for 2006 and recommend getting covered on 75% of your milk. The rapid drop in 2006 first-half prices leaves Jan – Jun averaging only \$12.54. We don’t get too excited about locking in and selling there, so consider again this options strategy. Sell January through June 12.00 put options and 13.00 call options, collecting 40¢ premium (\$800 per contract). If cheese prices remain under pressure and remain between \$1.25 and \$1.45, both options would expire worthless, allowing you keep the 40¢, adding that to your final milk price. If the market conditions look like they’ll change, we can cover the options with futures positions. Prices would need to move below \$11.60 or above \$13.40 to lose money on the trade, otherwise you would keep all or part of the initial premium received.

July – Dec currently averages \$13.19. Sell your milk; simple as that.

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