



## The KDM Dairy Report - January 6<sup>th</sup>, 2006

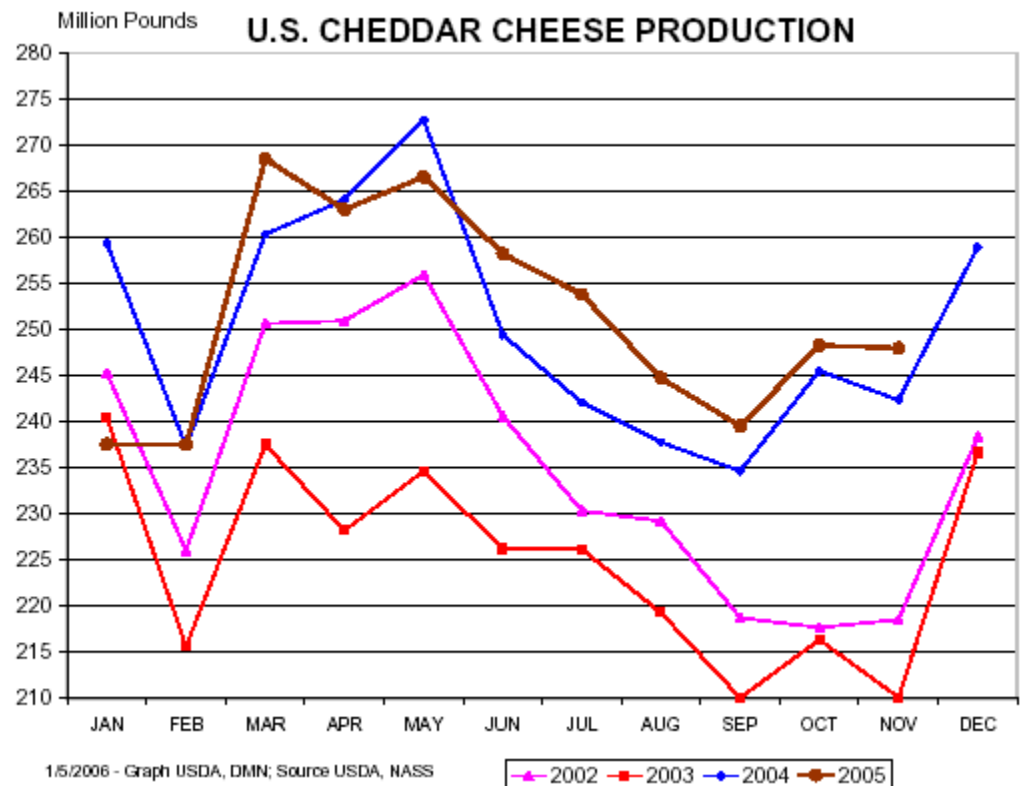
### On the bright side:

- NASS cheese prices managed a [small gain](#) this week, with blocks up 1.1¢ to \$1.43/lb and barrels up 0.6¢ to \$1.41/lb. Nonfat dry milk increased 3.9¢ to hit \$1.00/lb while dry whey continued to be strong, moving 0.3¢ higher to 33.1¢/lb.
- Weekly dairy cow slaughter for the week ending 12/24 was [2,000 head higher](#) than a year ago.
- Though manufacturing plant schedules were heavy over the holiday weekend, contacts report milk [supplies were handled with ease](#), according to Fluid Milk & Cream Review. Some even reported milk volumes were lighter than the previous holiday weekend.
- The Pacific Northwest is saturated from recent storms, and Fluid Milk & Cream Review reports [herd health stress is increasing](#). California also received a lot of moisture, but the effects on production are still unknown.
- International: Milk production in Oceania [continues to wind down](#) seasonally, with New Zealand output off 2% and Australia up 1%. Because most products are pre-sold before the milk production season, traders are not typically accepting additional buy interest.
- [Demand for dry whey is firm](#) and inventories are light to nonexistent, according to Dairy Market News. World whey prices continue to increase and are not competitive with the U.S. price.
- Economy: U.S. jobless claims hit a [5-year low](#) this week, according to the Labor Department.
- Cash blocks and barrels settled unchanged on the week at \$1.36¾ and \$1.34 respectively, while butter gained 5½¢ to \$1.40. Cheese demand appears to be in balance as there were no trades the entire week in blocks or barrels. Only 6 loads of butter traded for the week.

| Futures Month | Friday 12/30 Close | Friday 12/30 Close | Change | 10-yr Average | Top 3rd Price | Top 5th Price |
|---------------|--------------------|--------------------|--------|---------------|---------------|---------------|
| Jan-06        | \$13.37            | \$13.25            | \$0.12 | \$12.10       | \$12.93       | \$13.74       |
| Feb-06        | \$13.05            | \$12.91            | \$0.14 | \$11.64       | \$12.33       | \$13.00       |
| Mar-06        | \$13.00            | \$12.80            | \$0.20 | \$11.88       | \$12.60       | \$13.30       |
| Apr-06        | \$12.88            | \$12.65            | \$0.23 | \$12.31       | \$13.52       | \$14.71       |
| May-06        | \$12.80            | \$12.58            | \$0.22 | \$12.35       | \$13.69       | \$15.01       |
| Jun-06        | \$12.83            | \$12.73            | \$0.10 | \$12.41       | \$13.50       | \$14.56       |
| Jul-06        | \$13.19            | \$13.16            | \$0.03 | \$12.85       | \$13.75       | \$14.64       |
| Aug-06        | \$13.42            | \$13.35            | \$0.07 | \$13.28       | \$14.19       | \$15.09       |
| Sep-06        | \$13.61            | \$13.55            | \$0.06 | \$13.78       | \$14.67       | \$15.54       |
| Oct-06        | \$13.19            | \$13.12            | \$0.07 | \$13.21       | \$14.00       | \$14.77       |
| Nov-06        | \$12.88            | \$12.85            | \$0.03 | \$12.32       | \$13.34       | \$14.35       |
| Dec-06        | \$12.77            | \$12.74            | \$0.03 | \$12.44       | \$13.53       | \$14.60       |

### however....

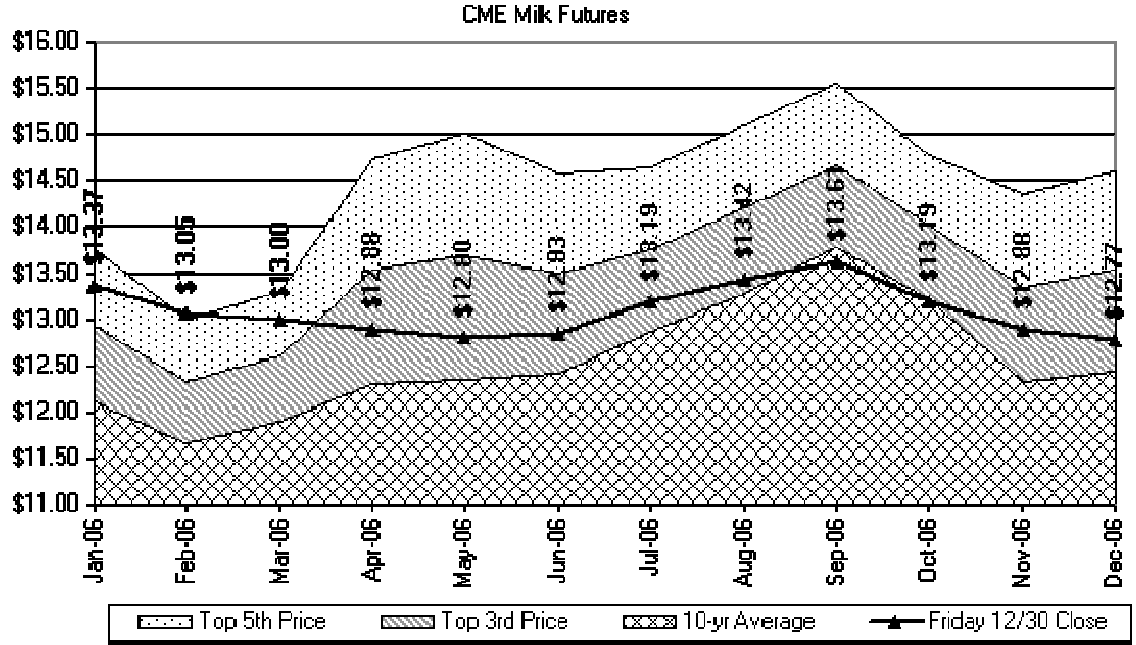
- Dairy Products Report: More milk resulted in [more cheese in November](#). American cheese output was 3.2% above November 2004, and 0.2% above the prior month. Cheddar cheese output was 3.2% above last year, while Total cheese output was up 0.9%. Butter production was 8.6% higher than a year ago, and 2.7% above October.
- Fluid Milk & Cream Review reports that both milk and cream supplies are in [excess of current needs](#). Some loads were moved to Class IV operations and discounted as a way to clear product.
- Excessive cream supplies have resulted in so much fresh butter being offered, that less than usual amounts have come out of the freezer, according to Dairy Market News. Churning activity is [expected to remain heavy](#), as milk production has rebounded.
- Contacts we spoke to this week indicated expansions in ID, NM and TX are running full speed ahead. Dairy Market News reports this is keeping heifer prices very firm.



- A hearing on cheese "make allowances" will be on January 24<sup>th</sup>. If make allowances are raised for cheese makers, Class III prices could drop about a dime.

**Recommendation:**

We all know how the funds can move the grain markets, despite where fundamentals say prices should go. Funds have been present in the milk market as well, but not for a long time. That all changed Tuesday when a trader stepped up to the plate and aggressively bought Jan-Apr futures. The same buyer showed up on Wednesday and continued their buying spree, driving prices to new contract highs, despite bearish fundamentals. Word has it that milk was added as an asset class to a fund, which was obligated to



purchase milk futures up to a designated allocation percentage. The furious trade caught everyone off guard, but once again provided some fantastic hedging opportunities. February 13.00 put options were bought for as little as 12¢, while many producers sold their milk outright at well over 13.00. Aggressive buying dried up on Thursday and Friday, and after a slightly bearish Dairy Products report, prices have steadily eased back. Even so, we finished the week with gains across the board, with the 2006 annual average now at \$13.08. Take a look at the chart above. Jan-Mar are above top-third prices, with Feb even above its top-fifth price by a nickel. What are you going to do with this information! We don't know if fund interest will return next week – it may well, but even so, you need to take some action and put a floor under your milk! Buy the Feb 13.00 PUT for 15¢ or better, or sell Q1 outright. The April-December average increased 9¢ to \$13.06. Consider selling at this level, which is above average. The time to sell is when prices are going higher and buyers are present. It's a lot tougher to sell when the writing is on the wall and everyone wants to sell.

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