



The KDM Dairy Report - February 24th, 2006

On the bright side:

- Hay prices in California are firm, from \$150-160 or \$200 delivered, according to Dairy Market News.
- The NASS dry whey price continued to break new ground, climbing ½¢ to 35.6¢/lb.
- Dairy Market News reports demand for specialty cheeses and for aging programs [remains solid](#).
- Economy: Unemployment numbers dropped by a larger than expected amount last week, according to the Labor Department. It was the [biggest drop in five weeks](#) and an indicator that the labor market remains strong.
- Though blocks and barrels were offered lower in the cash market today, 3 different buyers purchased 6 loads of blocks. Are we establishing some support here?

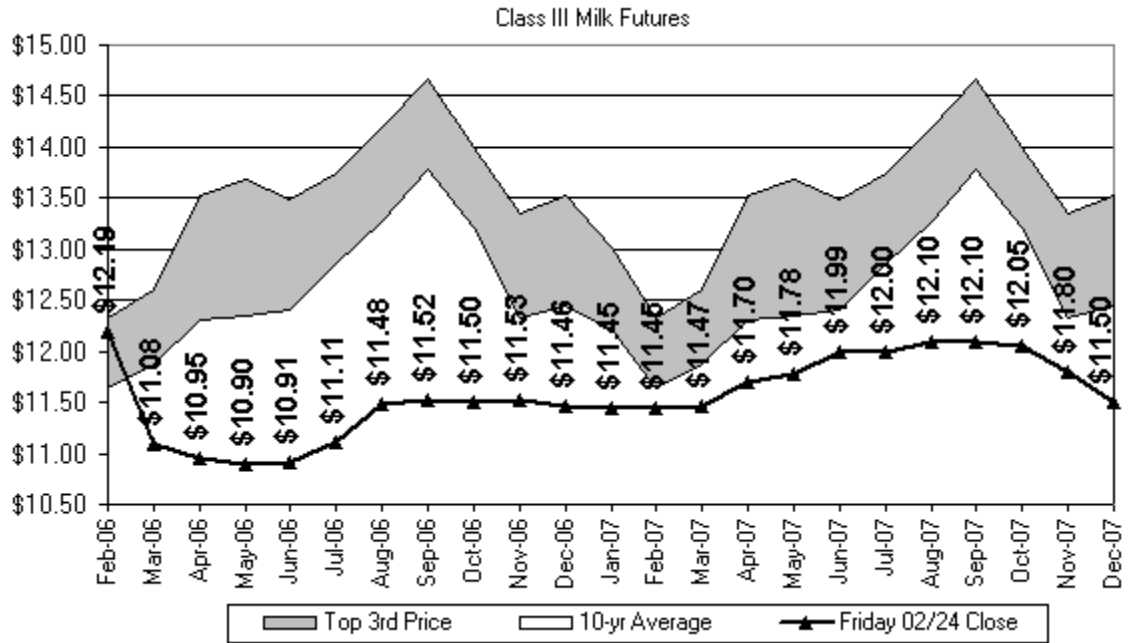
however....

- Cold Storage Report: January American cheese stocks were 526.2 million lbs, a [record for that month](#), and up 9% vs. last year. They were, however, down 2% from December. Butter stocks were up an even more impressive 48% from last year and up 95% from last month!
- Cash blocks fell below the support price, settling at \$1.12¾ today, down 3¾¢ for the week. Barrels fell 4¢ to \$1.10½ to maintain the spread with blocks. Cash butter slipped another 1¼¢ to \$1.15¾.
- NASS [cheese averages fell again](#) last week, with blocks shedding 2.7¢ to \$1.25/lb and barrels losing 1.6¢ to average \$1.22/lb. Butter fell to \$1.22, down 2¢ for the week and NDM decreased 1.6¢ to 87.1¢/lb.
- Weekly cold storage numbers continue to show a [rapid inventory build](#) in butter. For the period 02/01 – 02/20, butter stocks are up 19%, and cheese stocks increased 3%.
- Dairy cow slaughter for the week ending 02/11 was 43,400 vs. 46,200 during the same week a year ago.
- For the week ending 02/18, butter stocks at CME-approved warehouses increased by 7.8 million lbs., compared to only a 4.4 million lb increase during the same period a year ago.
- In what appears to be a repeated bullet point now, Fluid Milk & Cream Review continues to highlight the concern about plant capacity, stating some operators have reported milk intakes are already [higher than their peak level last year](#).
- Contacts for Fluid Milk & Cream Review indicate the California cream market has not been this weak for many years. Supply is heavy but [buyers are few](#). Butter manufacturers are less likely to be buyers knowing their finished product is destined for storage.
- Further cracks in the dry whey market seem to be appearing. Dairy Market News reports some [increased buyer resist](#) at the current price level, while some plants have increased supplies. Contacts are calling the market steady with a softer undertone developing, noting the firm trend is “definitely losing its momentum”.
- Dairy Market News reports the nonfat dry milk market is weak as production levels are heavy due to the constant flow of milk. Dryers are running at capacity, but cheese interest in NDM is light and buyers continue to wait on the sidelines. As powder [piles up on the floor](#) with no home, talk has turned to surplus product being offered to the CCC to clear some of the building inventory.
- Butter orders for the Easter/Passover holidays are [lighter than usual](#), according to Dairy Market News. The weak market has some believing that after the holiday, offers to the CCC are likely.

| Futures Month | Friday 02/24 Close | Friday 02/17 Close | Change | 10-yr Average | Top 3rd Price |
|---------------|--------------------|--------------------|----------|---------------|---------------|
| Feb-06 | \$12.19 | \$12.10 | \$0.09 | \$11.64 | \$12.33 |
| Mar-06 | \$11.08 | \$11.12 | (\$0.04) | \$11.88 | \$12.60 |
| Apr-06 | \$10.95 | \$11.10 | (\$0.15) | \$12.31 | \$13.52 |
| May-06 | \$10.90 | \$11.00 | (\$0.10) | \$12.35 | \$13.69 |
| Jun-06 | \$10.91 | \$11.27 | (\$0.36) | \$12.41 | \$13.50 |
| Jul-06 | \$11.11 | \$11.46 | (\$0.35) | \$12.85 | \$13.75 |
| Aug-06 | \$11.48 | \$11.90 | (\$0.42) | \$13.28 | \$14.19 |
| Sep-06 | \$11.52 | \$11.90 | (\$0.38) | \$13.78 | \$14.67 |
| Oct-06 | \$11.50 | \$11.95 | (\$0.45) | \$13.21 | \$14.00 |
| Nov-06 | \$11.53 | \$11.91 | (\$0.38) | \$12.32 | \$13.34 |
| Dec-06 | \$11.46 | \$11.80 | (\$0.34) | \$12.44 | \$13.53 |
| Jan-07 | \$11.45 | \$11.30 | \$0.15 | \$12.20 | \$13.01 |
| Feb-07 | \$11.45 | \$11.25 | \$0.20 | \$11.64 | \$12.33 |
| Mar-07 | \$11.47 | \$11.25 | \$0.22 | \$11.88 | \$12.60 |
| Apr-07 | \$11.70 | \$11.50 | \$0.20 | \$12.31 | \$13.52 |
| May-07 | \$11.78 | \$11.80 | (\$0.02) | \$12.35 | \$13.69 |
| Jun-07 | \$11.99 | \$11.70 | \$0.29 | \$12.41 | \$13.50 |
| Jul-07 | \$12.00 | \$12.00 | \$0.00 | \$12.85 | \$13.75 |
| Aug-07 | \$12.10 | \$12.15 | (\$0.05) | \$13.28 | \$14.19 |
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| Oct-07 | \$12.05 | \$12.15 | (\$0.10) | \$13.21 | \$14.00 |
| Nov-07 | \$11.80 | \$11.80 | \$0.00 | \$12.32 | \$13.34 |
| Dec-07 | \$11.50 | \$11.50 | \$0.00 | \$12.44 | \$13.53 |

Recommendation:

This week saw continued producer selling as prices settled in to their new range. Most of the damage was done during the beginning of the week, and there are signs that the market is catching its collective breath after shedding so much value in such a short time. So goes the dairy market – always faster on the way down. But today’s cash market may be an indication there is some short-term support here, with



the current block and barrel prices calculating out to \$10.97 milk. If prices hold into next week, expect Class III futures to react upward despite the bearish demand picture, as specs take profits. That could provide a new selling opportunity for hedgers. Call us for price objectives. Looking at the last part of the year, consider selling November and December 13.25 calls on any unsold milk, collecting 25-30¢ for each one. It would cap your price in those months at 13.25, but add 25-30¢/cwt to your milk check should we close those months below 13.25, which seems likely at this point. Our recommendation remains the same for 2007 at this point – stand aside for now.

Please feel free to call us anytime for help in setting up a hedge program for your operation!

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