



The KDM Dairy Report - March 17th, 2006

On the bright side:

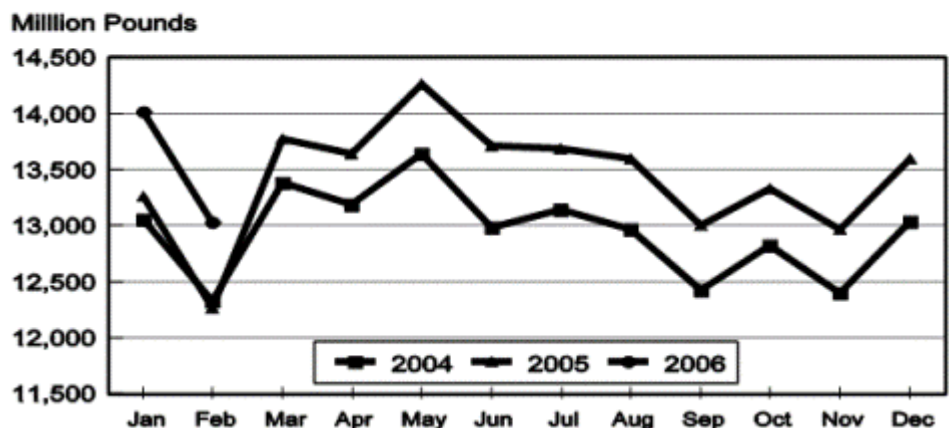
- So far in March cheese [stocks are holding steady](#), according to this week's cold storage numbers. For the period 03/01 through 03/13, USDA indicates only a slight increase of 128,000 lbs.
- After being silent the first four days this week, a lone trader bid cash blocks up a ¼¢, but no sellers hit his bid, so we finished the week at \$1.18¼. Barrels attempted to close the spread and were bid up ½¢ to \$1.13½ before a seller hit their bid and offered another load unchanged. Cash butter managed a ½¢ gain for the week, settling at \$1.17 with 7 loads exchanging hands.
- Weekly dairy cow slaughter numbers [jumped above year-ago levels](#) for the first time in 2006. For the week ending 03/04, 45,400 animals were culled vs. 42,300 last year. Time will tell if this is a new trend in response to lower milk prices.
- A recent [pickup in orders](#) is giving the cheese market a cautious undertone, according to Dairy Market News. Buyers are seeing value at current prices for aging programs and Mozzarella demand remains good.
- International: The latest update from USDA reports stocks of dairy end-products [remains tight](#) in Oceania, and production in Western Europe is [2% behind last year](#).

however....

- Milk Production Report: February milk production in the 23 major states was [up a huge 5.9%](#) over February 2005. Production per cow was up 66 lbs and the number of milk cows was up 121,000 head. Production in all 50 states was up 5.5% while the number of milk cows climbed to 9.088 million head, the highest since July, 2003. From a percentage increase basis, leading the way was NM, up 17.2%, followed by TX up 15.2%, CO up 10.5% and ID up 8.3%. But the real story is CA which really turned on the spigots, up 6.6%, or 189 million lbs of milk. That's more than twice the increase of percentage leader NM, which was up 85 million lbs.
- Livestock, Dairy & Poultry Outlook Report: USDA's latest forecast predicts cheddar cheese will average only \$1.26 this year, a drop of 4½¢ from last month's estimate. They also expect [dry whey to average only 24-26¢](#) during the last half of the year. If that were to happen, it would take about 60¢ off the current Class III price. The report cites an uncharacteristic bunching in the calving cycle putting more cows at peak lactation, a mild winter, adequate forage combined with weak fourth-quarter commercial use as the basis for the downgrades.
- Butter continues to be crammed into storage at an amazing rate. Weekly butter movement into CME-approved warehouses for the week ending 03/11 was 4.2 million lbs, [more than 10 times](#) the 416,000 lbs that were added during the same period a year ago.
- Dairy Market News reports butter orders for Easter/Passover are [below previous year levels](#) for this time period. With production surpassing demand, traders expect the recent up tick in the cash butter price to decline once Easter orders are placed.
- Public schools are or will shortly be closing for Spring break, forcing more milk into already full manufacturing pipelines.
- Western under-grade cheese is [becoming more of a problem to move](#), according to Dairy Market News. And heavy intakes are forcing some plants to sell milk in order to limit building stocks.

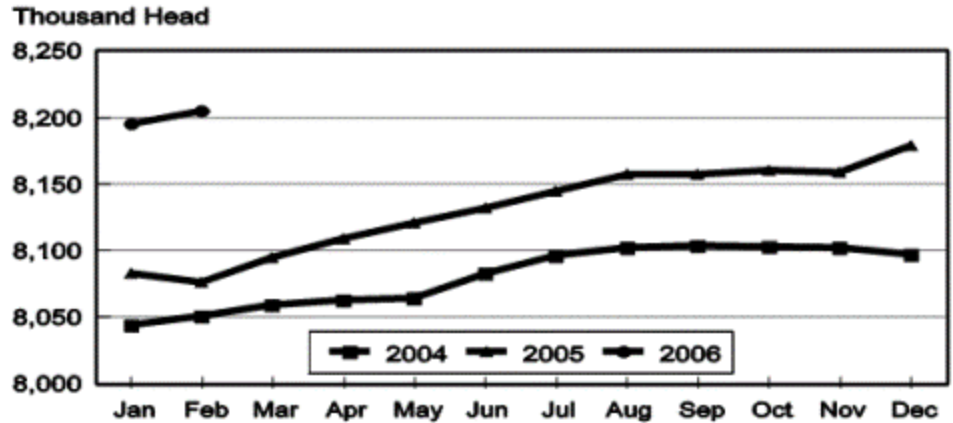
Futures Month	Friday 03/17 Close	Friday 03/10 Close	Change	10-yr Average	Top 3rd Price
Mar-06	\$11.11	\$11.13	(\$0.02)	\$11.88	\$12.60
Apr-06	\$10.97	\$11.09	(\$0.12)	\$12.31	\$13.52
May-06	\$10.96	\$11.10	(\$0.14)	\$12.35	\$13.69
Jun-06	\$11.18	\$11.19	(\$0.01)	\$12.41	\$13.50
Jul-06	\$11.50	\$11.46	\$0.04	\$12.85	\$13.75
Aug-06	\$12.07	\$12.05	\$0.02	\$13.28	\$14.19
Sep-06	\$12.15	\$12.05	\$0.10	\$13.78	\$14.67
Oct-06	\$12.11	\$11.96	\$0.15	\$13.21	\$14.00
Nov-06	\$12.05	\$11.90	\$0.15	\$12.32	\$13.34
Dec-06	\$12.00	\$11.90	\$0.10	\$12.44	\$13.53
Jan-07	\$11.95	\$11.77	\$0.18	\$12.27	\$13.08
Feb-07	\$11.90	\$11.75	\$0.15	\$11.68	\$12.34
Mar-07	\$11.95	\$11.75	\$0.20	\$11.88	\$12.60
Apr-07	\$12.15	\$11.95	\$0.20	\$12.31	\$13.52
May-07	\$12.10	\$11.99	\$0.11	\$12.35	\$13.69
Jun-07	\$12.20	\$12.10	\$0.10	\$12.41	\$13.50
Jul-07	\$12.45	\$12.05	\$0.40	\$12.85	\$13.75
Aug-07	\$12.30	\$12.11	\$0.19	\$13.28	\$14.19
Sep-07	\$12.30	\$12.10	\$0.20	\$13.78	\$14.67
Oct-07	\$12.20	\$12.05	\$0.15	\$13.21	\$14.00
Nov-07	\$12.00	\$11.80	\$0.20	\$12.32	\$13.34
Dec-07	\$11.60	\$11.52	\$0.08	\$12.44	\$13.53

Monthly Milk Production
23 States



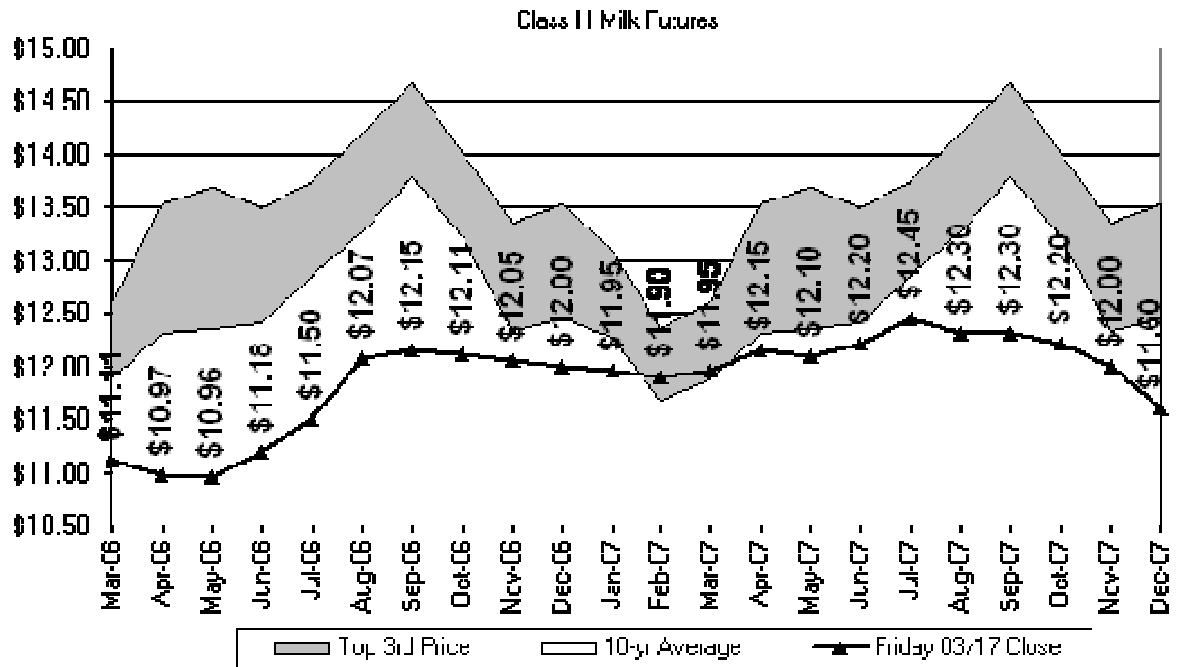
- Milk intakes remain [well above year-ago levels](#) in the Midwest, according to Fluid Milk & Cream Review. They also report that producers looking to switch buyers are finding little interest in adding new patrons due to spring plant capacity concerns.
- Dairy Market News reports the [dry whey market is weak](#) in the central region of the U.S. Some areas are reporting heavier supplies are buyers opt to a hand-to-mouth strategy.
- Fluid Milk & Cream Review reports Florida exported 112 loads of Grade A milk this week, vs. 84 last week. Milk volumes are expected to [remain high into May](#).
- Dry whey exports in January were down 17.5% vs. a year ago, according to Dairy Market News. Supply and demand appear to be in balance, but [prices are beginning to weaken](#).
- The wall of milk continues to grow out West. Fluid Milk & Cream Review reports both California and New Mexico milk output is heavy and not expected to slow in the near future. Excess milk is being discounted and shipped further to keep it moving, while processing capacity is being stretched.
- Dairy Market News says the nonfat dry milk market has a weaker tone as offerings remain heavy. Exports have slowed and stocks are building, to the extent that the CCC made its [first NDM purchase since November 2004](#).
- [Dry whey fell 0.6¢](#) to 34.5¢/lb in this week's NASS survey. That doesn't bode well for the future of Class III prices if it's the start of a trend, as Dairy Market News articles seem to be hinting at. Cheese continued to decline as well with blocks coming in at \$1.15/lb, down 3.2¢, and barrels at \$1.13, down 1.7¢.

Monthly Milk Cows 23 States



Recommendation:

One could go on and on with how bearish today's Milk Production Report was. It was the biggest gain in output since 1981 and was 3.7 million lbs more per day than last year's peak in May, according to today's [Daily Dairy Report](#). Markets should open sharply lower on Monday. We never saw any 12.50 milk like we were hoping for, but the general advice was to sell rallies, and we did, getting several folks covered in the 12.05 – 12.15 levels Aug-Dec. The market may now over-react to the



downside, so our recommendation is to take advantage of it and get some call option protection in place for milk you have already sold or hedged. Tuesday might be a good day to get in some orders. If the Livestock, Dairy & Poultry Outlook report is correct and we do have a "bunching" in the calving cycle, the huge gains we were currently experiencing could taper off in 2-3 months. While we'll still have a lot of milk around, it's best to get your call options purchased when pessimism is at its peak. Call us and we'll help you set targets.

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