



The KDM Dairy Report - May 26th, 2006

On the bright side:

- In the cash market, blocks managed a 2½¢ gain for the week, closing at \$1.22½/lb today. Barrels remained unchanged at \$1.19/lb. Five loads of block and two loads of barrel exchanged hands. Butter remained stuck at \$1.17¾/lb with eight loads trading on the week.
- Commercial Disappearance: Use of milk in all products was [up a healthy 4.7%](#) in March, according to statistics released Wednesday by USDA. Individually, milkfat use was up 9.7%, butter use up 15.8%, nonfat dry milk up 5.5% and American cheese use up 4.6%.
- NASS survey [prices were up](#) for most Class III components this week. Significantly, dry whey reversed a several week drop with a 0.3¢ increase to 28.1¢/lb. Block cheese gained ½¢ to \$1.16/lb while barrels were up 1.4¢ to \$1.15/lb.
- Dairy cow slaughter for the week ending 05/13 was [slightly higher](#) than a year ago. 40,600 head were culled vs. 39,400 head a year ago.
- Milk production in California is now [trending lower](#) in several key locations, according to Fluid Milk & Cream Review, and lack of dairy quality hay is affecting output and protein levels. The peak has also probably been reached in Arizona and New Mexico, where 100 degree temps have returned.
- Barrel supplies in the Midwest [remain tight](#), according to Dairy Market News. Demand for process cheese has been good as retailers prepare for the holiday weekend and June promotions.
- Out West, multi-load orders of both blocks and barrels now face of lead time of until the end of June and into July, according to Dairy Market News. Cheese buyers think most is going to end users to supply current needs, and [don't see a slowdown](#) coming in the market.
- There's an [acute shortage of organic milk](#), according to a news story put out this week by Minneapolis/St. Paul news station WCCO. Producers are being courted and given "signing bonuses" by companies desperate for their product, and Wal-Mart, already the largest organic milk seller in the nation, recently announced they plan to double the amount of organic produce sold in its stores. An increase in the number of organic producers could help limit production gains as these operations produce far less milk than conventional farms.

however....

- Weekly cold storage holdings continue to show a 3% [gain in cheese stocks](#) and 13% gain in butter stocks for the week ending 05/22.
- Big [gains in butter stocks](#) again this week at CME warehouses. 5.1 million lbs were added for the week ending 05/20, vs. 3.8 million lbs during the same period last year.
- Milk volumes in the Midwest remain excessive, with plant [capacity being tested](#) at most facilities. Offerings continue to exceed demand, with spot loads of milk going for \$2 to \$3 under class.
- All schools in Florida are now on summer recess and this has [drastically reduced Class I needs](#), according to Fluid Milk & Cream Review. Surplus milk is flooding the system and plants are expected to remain full well into June.
- Dairy Market News reports that nonfat dry milk continues to [clear to the government](#) under the support program, keeping spot prices from rising. Stocks remain heavy.
- Yum! Brands reported [sales slid 7% in their Pizza Hut](#) chain during the four weeks ended May, 20th.

Futures Month	Friday 05/26 Close	Friday 05/19 Close	Change	10-yr Average	Top 3rd Price
May-06	\$10.82	\$10.82	\$0.00	\$12.35	\$13.69
Jun-06	\$11.45	\$11.12	\$0.33	\$12.41	\$13.50
Jul-06	\$11.99	\$11.45	\$0.54	\$12.85	\$13.75
Aug-06	\$12.33	\$11.67	\$0.66	\$13.28	\$14.19
Sep-06	\$12.50	\$12.09	\$0.41	\$13.78	\$14.67
Oct-06	\$12.50	\$12.11	\$0.39	\$13.21	\$14.00
Nov-06	\$12.40	\$12.05	\$0.35	\$12.32	\$13.34
Dec-06	\$12.18	\$11.92	\$0.26	\$12.44	\$13.53
Jan-07	\$12.27	\$11.96	\$0.31	\$12.27	\$13.08
Feb-07	\$12.10	\$11.89	\$0.21	\$11.68	\$12.34
Mar-07	\$12.11	\$11.93	\$0.18	\$11.82	\$12.51
Apr-07	\$12.23	\$12.03	\$0.20	\$12.19	\$13.36
May-07	\$12.19	\$12.10	\$0.09	\$12.35	\$13.69
Jun-07	\$12.43	\$12.25	\$0.18	\$12.41	\$13.50
Jul-07	\$12.63	\$12.58	\$0.05	\$12.85	\$13.75
Aug-07	\$12.74	\$12.72	\$0.02	\$13.28	\$14.19
Sep-07	\$12.92	\$12.87	\$0.05	\$13.78	\$14.67
Oct-07	\$12.67	\$12.63	\$0.04	\$13.21	\$14.00
Nov-07	\$12.49	\$12.45	\$0.04	\$12.32	\$13.34
Dec-07	\$12.30	\$12.16	\$0.14	\$12.44	\$13.53

Recommendation:

Wow! Class III futures came alive this week with gains far exceeding our expectations. The market has a way of humbling all prognosticators at some point without fail. Consider us humbled. It appears we are in a classic short squeeze. As of 5/16, the most recent commitment of traders report from the CME, there were more than twice as many non-commercial short positions as long. As

prices move higher, some of those with short positions are being forced to buy back their contracts at a loss. What does this mean to you, the hedger? This is another great opportunity to get some coverage in the fall months. July-Dec '06 gained 44¢ this week and now averages \$12.32. If you want to keep your upside open, take another look at PUT options. As prices have increased, put option premium has decreased. Try buying the Aug and Sep 11.75 PUT for 25¢. We would continue to hold off on further 2007 sales.

Note: Our office will be closed on Monday, May 29th in observation of Memorial Day. Thank an active soldier or Vet this weekend for the freedom we enjoy in this great country. It was paid for with a high price.

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Class III Milk Futures

