

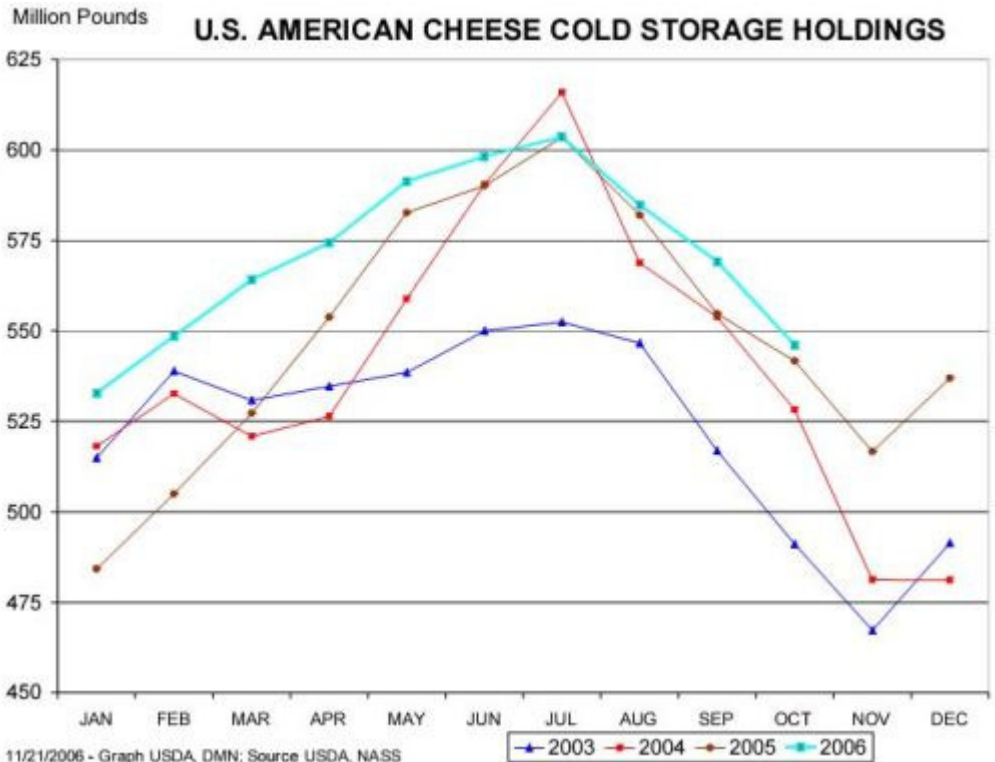


The KDM Dairy Report - November 22nd, 2006

Bullish Fundamentals:

- Cold Storage Report: Stocks of American cheese in October were 1% lower than in 2005 and 4% lower than September, according to USDA figures released this week. Butter stocks were up 39% year-to-year, but down a much stronger than average 19% vs. September. Total cheese stocks were 6% higher than last year, but 3% lower than September.
- Weekly cold storage numbers continue to [reflect good demand](#). Cheese stocks are down 2% for the first 20 days of November, with butter stocks down 12%.
- Butter [stocks continue to fall](#) at CME warehouses. 8.7 million lbs were pulled from storage last week, vs. 6 million lbs during the same period last year. Total stocks are now at 46.7 million lbs, still above last year at 34.8 million lbs, but declining at a faster rate.
- Fluid Milk & Cream Review reports Class I [demand was very strong](#) early this week as holiday orders made up for a slow down from school accounts due to the holiday period. Milk supplies are still very tight, but loosen some later this week.
- Two drying facilities out East that were expecting to gear up over the holiday weekend will remain idle due to lack of milk, according to Fluid Milk & Cream Review. Milk handlers in the Northeast are wondering, "Where's all the milk?" after projecting the supply would increase by now, but it hasn't. Class I sales remain strong, with any [surplus milk being quickly absorbed](#).
- Processors in California would like additional milk to help catch up on orders, according to Fluid Milk & Cream Review. Milk output is rising slightly in the Southwest, but [high feed costs remain a big concern](#). Producers anticipate very tight margins despite the higher futures prices at the CME, as input costs bite into the bottom line.
- Dry whey prices are higher on a firm market, according to Dairy Market News. Some buyers are resisting significant premiums being requested for 2007 contracts, however, [limited availability is increasing their anxiety](#) about being able to secure product for their needs. Resale prices have been reported as much as 10-12¢ above the market.
- Western whey [demand remains excellent](#) from both domestic and export accounts, according to Dairy Market News. Higher prices have not deterred demand. Deliveries are often delayed as production is not at anticipated levels due to reduced cheese production.
- Dairy Market News report good volumes of national and store brand butter are being moved due to [aggressive feature activity](#).
- Butter producers are [eager to absorb additional cream](#), usually available during the holiday week, to generate fresh product, according to Dairy Market News. Orders for the upcoming year end holiday period are reported to be strong.

Futures Month	Wed 11/22 Close	Friday 11/17 Close	Change	10-yr Average	Top 3rd Price
Nov-06	\$12.90	\$12.87	\$0.03	\$12.32	\$13.34
Dec-06	\$13.70	\$13.87	(\$0.17)	\$12.44	\$13.53
Jan-07	\$13.47	\$13.79	(\$0.32)	\$12.27	\$13.11
Feb-07	\$13.40	\$13.79	(\$0.39)	\$11.68	\$12.37
Mar-07	\$13.40	\$13.89	(\$0.49)	\$11.82	\$12.54
Apr-07	\$13.70	\$13.93	(\$0.23)	\$12.30	\$13.51
May-07	\$13.71	\$13.97	(\$0.26)	\$12.32	\$13.67
Jun-07	\$13.83	\$14.11	(\$0.28)	\$12.39	\$13.49
Jul-07	\$14.04	\$14.30	(\$0.26)	\$12.82	\$13.74
Aug-07	\$14.36	\$14.51	(\$0.15)	\$13.23	\$14.17
Sep-07	\$14.44	\$14.60	(\$0.16)	\$13.79	\$14.68
Oct-07	\$14.04	\$14.01	\$0.03	\$13.19	\$13.98
Nov-07	\$14.00	\$14.00	\$0.00	\$12.32	\$13.34
Dec-07	\$13.96	\$13.96	\$0.00	\$12.44	\$13.53
Jan-08	\$13.50	\$13.52	(\$0.02)	\$12.27	\$13.11
Feb-08	\$13.45	\$13.45	\$0.00	\$11.68	\$12.37
Mar-08	\$13.45	\$13.45	\$0.00	\$11.82	\$12.54
Apr-08	\$13.45	\$13.45	\$0.00	\$12.30	\$13.51
May-08	\$13.30	\$13.30	\$0.00	\$12.32	\$13.67
Jun-08	\$13.30	\$13.30	\$0.00	\$12.39	\$13.49
2007 Avg	\$13.86	\$14.07	(\$0.21)		
Jan-Jun '08	\$13.41	\$13.41	(\$0.00)		



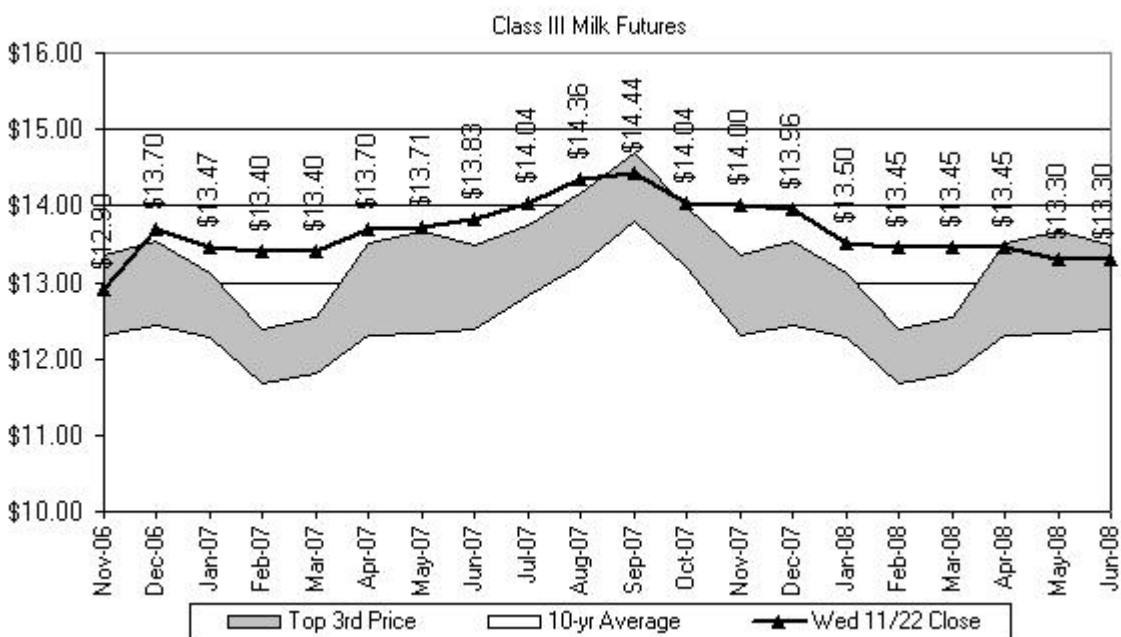
- Western contacts report that some current cheese is available, but [not large volumes](#). Cheese production is flat to lower, but buyers are still looking for cheese for end-of-the-year sales programs.
- Eastern contacts report good demand for current cheese, but [supplies remain limited](#) due to the shortage of milk and nonfat dry milk to fortify the vat. Cheese makers would welcome any additional milk.
- International: The refund aid for Western European producers of whole milk powder was reduced 40% and for cheese 13%, at the Dairy Management Committee meeting in Brussels last week. The move could [further firm European-priced dairy products](#) during the upcoming milk production season, at a time when domestic demand is leaving little finished dairy products available for export.
- International: Stocks of finished dairy products in Oceania are nearly fully committed. The uncertain milk situation in New Zealand and Australia due to drought has some customers nervous about supply commitments to them. Traders expect dairy prices to remain firm in 2007 due to [limited supply on a global basis](#).

Bearish Fundamentals:

- USDA announced this week a decision to [increase the make allowances](#) for cheese, butter, nonfat dry milk and dry whey. If approved by, which is likely, it could result in a 20-26¢/cwt drop in Class III prices starting early next year.
- Cash Market: The prominent barrel buyer was less aggressive in this holiday-shortened week, which allowed sellers to get the upper hand. Barrels fell 1¼¢ from last Friday to settle at \$1.42¾/lb today. Blocks were even weaker, falling 4¢ to close at \$1.38¼/lb., while butter lost 1¾¢ to finish the week at \$1.28/lb. Block buyers were nowhere to be seen as there were no trades, but 11 loads of blocks and 6 cars of butter exchanged hands.
- 16 fewer loads of milk were imported into Florida this week, as favorable weather is allowing production to inch upwards, according to Fluid Milk & Cream Review. Handlers expect supply and demand to come into better balance going forward.

Recommendation:

Prices were hit hard this week on news of the "make allowance" decision by USDA and a drop in cash cheese prices. As we mentioned last week, the near term picture looked susceptible to a correction, which is what happened. Further pressure to the downside is likely as the cheese buyer in the cash market may have less urgent needs next week, however, we would maintain selling targets above the current prices. Feed costs and a tight global powder supply will continue to be long-term drivers of this market.



Target to sell a portion of your Jan-Mar production at a \$13.75 average. If prices move sharply lower, let's buy call options and sell in to them if prices head back up due to our feed cost / powder issue. Target to sell up to 25% of your 2007 production at a 14.15/cwt average or higher. Also consider selling additional milk that is trading significantly above its top 3rd historical price. The chart above shows both Feb and Mar 2007, and Feb and Mar 2008 meet that criteria.

Note: Our offices will be closed on Thursday and Friday for Thanksgiving. Milk markets are closed on both of these days.

Have a safe and blessed Thanksgiving!

Trading futures and commodities involves substantial risk and may not be suitable for all investors. You should carefully consider whether the risks involved in trading in commodities is suitable for you or your organization in light of your financial condition. While the information we gather and present is deemed to be reliable, it is in no way guaranteed. Neither the opinions expressed on this website nor in "The KDM Dairy Report", shall be construed as an offer to buy or sell any futures or options on futures contracts. In addition, past performance is not necessarily indicative of future results.