VALLEY FUTURES TRADING

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Weekly Dairy Report

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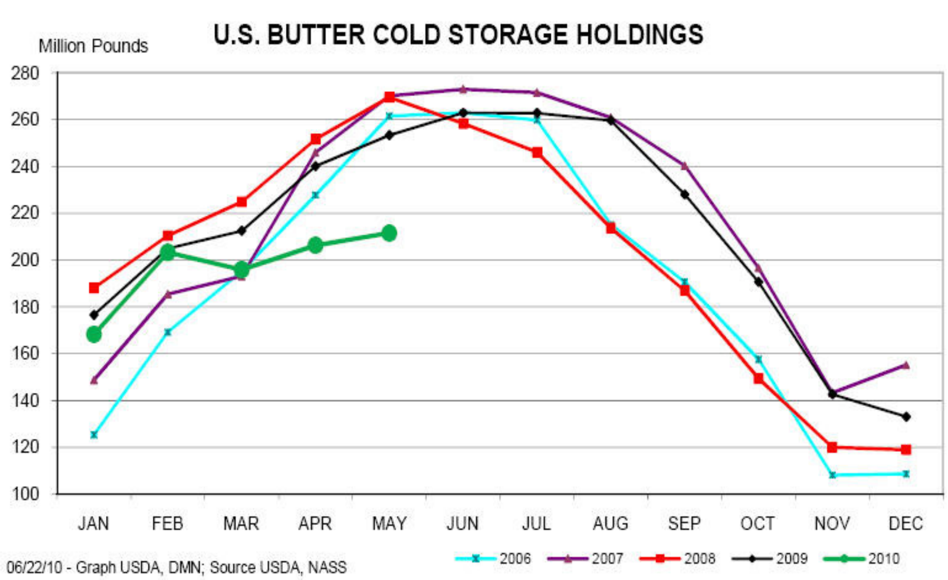
Vol. 10, No. 25 – June 25, 2010

Bull vs. Bear

Bull Horns:

✓ The USDA's monthly Cold Storage report showed butter inventories lagging last year by 16% (see graph below).



- ✓ CME cash prices were higher this week. Butter closed at \$1.72, up 8½¢; Cheddar blocks closed at \$1.41, up ½¢; barrels closed at \$1.39½, up 1¢.

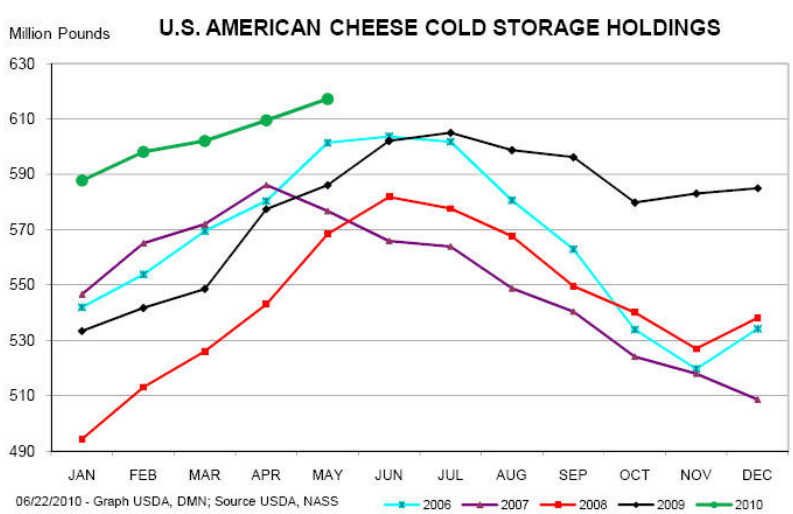
- ✓ Fluid Milk & Cream Review reported this week that cream demand is chaotic as demand often exceeds the supply. Through much of the country, the butterfat content on incoming milk is trending below levels of recent years, generating less cream.

- ✓ According to Dairy Market News, heat and humidity are beginning to bring steeper declines in milk production in the Mid Atlantic and a majority of the Northeast region. Specifically, Florida has seen a decline in production due to persistent heat and exports from that state were 216 loads, down 133 loads from last week.

- ✓ International butter prices averaged \$1.84 last week and Cheddar prices averaged \$1.79.

Bear Claws:

- ✓ On the bearish side of this month's Cold Storage report, American cheese stocks and Total cheese stocks both remain 5% above last year, which are record high inventories (see graph below).



- ✓ The Livestock Slaughter report released on Friday morning showed that dairy producers sent fewer cows to slaughter in May. They culled 209,000 head in May 2010, down from 235,000 in April 2010. On a daily adjusted basis, that's over 1000 cows per day less.

- ✓ According to Dairy Market News, the cheese market is unsettled. Most traders feel that the current supply/demand situation really does not warrant higher prices in the short term and demand is described as fair at best.

- ✓ In economic news, the Commerce Department reported that demand for durable goods fell 1.1% last month. It was the first decline in six months, following April's strong 3 percent increase.

Mixed & Other News:

- ✓ Dairy & Grain reports due out next week include (central time):
  - Crop Progress / Ratings: Monday, June 28th @ 3:00pm
  - Ag Prices Report: Tuesday, June 29th @ 2:00pm
  - Quarterly Grain Stocks: Wednesday, June 30th @ 7:30am
  - Planted Acreage: Wednesday, June 30th @ 7:30am
  - Monthly Dairy Products: Thursday, July 1st @ 2:00pm

Week-End Price Summary:

CME Cash Cheddar & Butter Prices	Closing Prices 6/25	Closing Prices 6/18	Change
Cheddar Blocks	$1.4100	$1.4050	$0.0050
Cheddar Barrels	$1.3950	$1.3850	$0.0100
Butter	$1.7200	$1.6350	$0.0850

For the week, the remaining 2010 average **gained 3¢ to close at $13.85**, while the 2011 average **lost 14¢ to close at $14.500**.

2010 Milk Futures Prices

Contract Month	Closing Prices 6/25	Closing Prices 6/18	Change	5-year Average
June-'10	$13.63	$13.58	$0.05	$15.12
July-'10	$13.55	$13.39	$0.16	$14.95
Aug-'10	$13.85	$13.84	$0.01	$14.59
Sept-'10	$14.64	$14.50	$0.14	$15.01
Oct-'10	$14.68	$14.70	($0.02)	$15.05
Nov-'10	$14.59	$14.55	$0.04	$15.00
Dec-'10	$14.50	$14.55	($0.05)	$15.54
Remaining 2010 Average	**$13.85**	**$13.82**	**$0.03**	

2011 Milk Futures Prices

Contract Month	Closing Prices 6/25	Closing Prices 6/18	Change	5-year Average
Jan-'11	$14.45	$14.55	($0.10)	$14.24
Feb-'11	$14.33	$14.55	($0.22)	$13.48
Mar-'11	$14.40	$14.49	($0.09)	$13.72
Apr-'11	$14.24	$14.47	($0.23)	$13.83
May-'11	$14.32	$14.54	($0.22)	$14.04
June-'11	$14.33	$14.47	($0.14)	$15.12
July-'11	$14.40	$14.69	($0.29)	$14.95
Aug-'11	$14.53	$14.64	($0.11)	$14.59
Sept-'11	$14.60	$14.74	($0.14)	$15.01
Oct-'11	$14.70	$14.85	($0.15)	$15.05
Nov-'11	$14.84	$14.85	($0.01)	$15.00
Dec-'11	$14.84	$14.85	($0.01)	$15.54
2011 Average	**$14.50**	**$14.64**	**($0.14)**	

General Market Comment:

The light at the end of the tunnel for this bear market continues to get brighter, as butter prices jumped above $1.71 this week and cheese prices were steady to higher. In addition, international prices for both butter and cheese remain strong and domestic milk production is showing signs of weakness due to hotter weather. Further, with the US Dollar dropping more than 3.5% since June 7th, the milk market looks like it is setting up for a rally.

Could this be the beginning of a sustained bull market? Maybe.

IF the global economic crisis is behind us and IF demand continues to be as good as it has been this year, then we are going to see milk prices rebound. Of course, those are two big IFs, but they are certainly in the realm of possibility.

Another factor that will eventually come into this market is the banks. We sat down with multiple bankers in January 2009 (just as this bear market began) and asked them how long they would be able to support dairy producers at unprofitable milk prices. Most of them were totally committed to sticking with their producers for "as long as it takes". Of course, many producers were flush with cash and equity because of the 2007 & 2008 record-breaking bull markets and this fact made the banks secure.

We've stayed in touch with many of those banks over the past several months and continued to ask "how much longer"? In the beginning, some felt they could sustain producers for 12 months; some felt 18 months, but none felt the crisis would last 2 years. Well, from our perspective, the two-year mark is the breaking point for the banks and they are eventually going to cry "uncle". This means that there will be cutbacks (not necessarily bankruptcies, but cutbacks) and this will affect milk production.

But what do we mean by cutbacks? Well, our guess is that asset valuations such as land, cows, machinery, barns, etc. are all going to take a serious percentage hit, potentially up to 35%. This will force new debt-to-equity ratios and limit expansion from a producer financing perspective. By limiting financing, the banks may actually be the key to a milk supply shortage. If this process begins in mass AND the heifer replacement inventories get worked down to 35% of the herd (instead of 50% of the herd) then we will get a ranging bull market.

For producers, you need to hang in there, but don't leave yourself unprotected from another unforeseen downturn. If our theory of "asset revaluation" doesn't occur in an orderly fashion, then the futures market may have another downturn coming as milk production continues to grow.

As for next week, we look for butter prices to test the $1.80 because of the international butter price and tight supply. The jury is still out on if cheese prices can rally in the face of record seasonal supplies. Based on the international price and a weakening U.S. Dollar, we think cheese has a good chance to test $1.50 again.

As always, please contact us with any comments or suggestions.

Call us at 1-800-423-4665.