DERCO FOODS.®

INTERNATIONAL DIVISION

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May 2006 Almond Position Report

May 2006 shipments were 79.882 million pounds. This is up about 18% from the May 2005 shipments of 67.335 million pounds.

Carry-in from last year: 137.7 million pounds
Crop receipts to date: 911 million pounds
Less 4% loss / exempt: (36 million pounds)
Total Supply: 1.012 billion pounds
Less shipments to date: (773.6 million pounds)
Supply Remaining: 238.9 million pounds

Shipments

Seller's Perspective: Don't send that Hummer back to the dealer just yet....the sun is shining bright once more in the San Joaquin Valley! This is the most that we have ever shipped for the month of May. We have exceeded last season's shipments for three months in a row now. The goal when we started this year was to reduce shipments by about 15% as compared to last season, to account for the smaller crop. Thanks to the last three strong months, we are down only 10% now – and so we are seeing limited availability from origin. We tried to sell less…we honestly did….we just couldn't do it. Are we good or what?

Buyer's Perspective: We have been expecting this number for over a month now. You are the only ones surprised by it. The market has already factored it in. If you look at the majority of the prices on the contracts which have shipped during the past three months, you will realize that they were done when the market was at much lower levels. The mistake that some traders and importers admittedly made was to maintain short positions, betting on lackluster demand throughout the spring and summer despite the attractive prices. Now they are forced to cover bits and pieces, in thin trading, at higher levels…creating to some in California the illusion that the market as a whole is accepting these prices. Oscar Wilde said that "illusion is the first of all pleasures" – so knock yourselves out and slap some FOOSE spinner rims on those Hummers.

Inventory

Seller's Perspective: 238.9 million pounds left to sell with 2 months to go in the year and a new crop harvest that may be late by as much as 10 – 14 days. If you consider the committed inventory figure, then we are already down to 109.6 million pounds of almonds to sell. So if we don't sell another pound, we would still have the lowest carry-out we have had since the 2002-2003 season (80 million pounds).

Buyer's Perspective: The impact of your inventory is limited to this season and to the transition period through September. We are seeing this reflected in the higher and higher prices quoted from California each day for current crop and for the premium commanded by September over October onwards shipments. We feel that the impact the current crop prices have had on the new crop are exaggerated and not justified. Come October or November, you may think so too.

Domestic

Seller's Perspective: Domestic shipments were essentially the same as last May. Year to date, the domestic market is down only 9.7% as compared to last year…also ahead of the reduction target set.

Buyer's Perspective: You will need to regain the full support of the domestic market for the coming season and especially for the seasons to come, as your supply grows. Creating this instability in the market by withdrawing for long periods of time will result in more domestic companies looking for other alternatives to almonds. Almonds are more price elastic than you think. You stimulated sales at $2.00 per pound and now

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you think that you will get the same results at $3.00 per pound. You will see that you cannot move the same tonnage at the higher levels. As usual, you will all see at the same time, and thus too late to save your half of the ship from sinking.

Demand

Seller's Perspective: Did we mention that we were keeping those Hummers….oh yeah…demand? How does "more robust than we could have imagined" sound? Buyers played the game to see who would blink first. California won. Now they have shown that they need product late in the year and this strength will carry into next season. Look at how much inshell India has already bought and the major players have not yet entered that market.

Buyer's Perspective: Is this demand we are seeing being used to build inventory or is it going directly to consumption? Demand these past few weeks for current crop has been from importers and traders who are primarily short on BSU5% and Cal SSR 27/30 AOL. There is also demand from some buyers in the Middle East looking to cover Nonpareil Supreme and Extra #1 and Carmel Supreme (they obviously waited too long). Ramadan starts on September 24 – once this buying interest is finished (vast majority from current crop), it will not come until next summer. How about new crop demand? It's coming mostly from thin trading activity, spurred on primarily by limited origin selling interest. It's easy to be disciplined in offering out product when the barns are empty. Will this resolve hold in October?

Other Nuts?

Seller's Perspective: There really is no substitute to almonds. We are still a competitively priced nut and the versatility and health benefits of almonds are unmatched.

Buyer's Perspective: When we don't think that prices reflect a rational correlation between supply and demand, we look for alternatives. Hazelnuts are arguably the closest substitute. Prices for current and new crop are on the way down. Current crop is around $2.60 per pound and new crop is heading closer to $2 per pound with each passing day. During the past couple of years, as almond prices reached record levels, hazelnut prices were at historic highs also. But with a good crop in Turkey this year, it does not appear that hazelnuts will help buoy the almond market.

Currency

The USD had been getting weaker for the past few weeks and nearly cracked the €1 = $1.30 level. But in recent days, it has become clear that the Federal Reserve intends to raise interest rates at least one more time (though some experts have speculated that 2 or 3 more rate increases are much more likely). This has given a boost to the USD and it has strengthened this week from the $1.29 levels back down to $1.265 against the Euro.

The Federal Reserve is concerned that we are seeing signs of "stagflation" – or a period of high inflation coupled with a stagnating or recessionary economy. This is a phenomenon that we really have not seen in the USA since the 1970s. To fight stagflation, the Federal Reserve has two choices: (1) lower interest rates and try to stimulate the economy (thus further increasing the inflationary rate); or (2) raise interest rates in an attempt to bring inflation down (potentially resulting in a further slowing down of the economy). Chairman Ben Bernanke seems to believe that fighting inflation is the priority. Higher interest rates would make certain US investments more attractive to investors and thus would likely result in a stronger Dollar. A stronger Dollar would make almonds more expensive overseas.

The European Central Bank has just also raised its key interest rate by a quarter point to 2.75% - the goal is also to keep inflation under control.

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Conclusion

There are cogent arguments in favor of both a stronger and weaker market.

Those arguing in favor of a firm market will point to:

- Demand – Why talk about lowering prices when monthly shipments are so strong? Typically we see corrections after several weak shipment months. It is unlikely that we will see anything weak heading into December. The summer months are virtually guaranteed to be strong – with the exception of August which may be lower than expected only because of a delayed new crop and a lack of inventory to sell. September is already shaping up to be strong, with a healthy premium being asked (and often paid) for early shipments.

- Stability – Demand will come with a stable market. If we can avoid over-reacting to monthly shipment data, we will still move our nuts and at higher levels. Intelligent inventory management is the key.

- Currency – If the USD stays weak, price increases from origin will be absorbed in certain regions of the world like Europe.

- Supply – 1.02 billion pounds is not an impressive amount of almonds to sell and we are going to have a minimal carry-out going into the 2006 season. There is no reason to panic. If we get a 1.02 billion pound crop and a carry-in of 100 million pounds – that will leave us with 1.08 billion pounds to sell. If we ship 980 million pounds (we have shipped this amount twice and 1 billion once), that will leave us with a carry-out in 2007 of only 100 million pounds. If the crop comes in at 1.1 billion pounds, and we ship 980 million pounds, we will still have a manageable carry out of 175 million pounds.

- The 2007 Crop - It could be big, but it's not going to be around until August 2007. Look at this season – prices dropped in anticipation of a big crop in August 2006, but buyers realized that they still needed to buy almonds in the spring and summer months and prices shot up in response. What will be different next year as long as shipments are reasonably healthy heading into 2007?

- Spain – They will not sell early and undercut California. They see how strong demand is and will ensure that they maximize their returns by being disciplined and allocating their crop throughout the entire year.

- Inventory – Those holding high priced contracts in Europe (or waiting for high priced contracts to be delivered) are benefiting from these higher prices. In fact, they are helping create a shortage by metering out their inventory in a measured way. Thanks to this increase in prices, they are either able to turn profits or minimize what would have been much heavier losses. The lack of a strong movement from European buyers to push prices down will keep things firm longer than people expect.

- Grower Field Prices – Packers are having to pay higher grower field prices in order to get their growers to release any appreciable quantity of almonds. Once these commitments are made on the part of packers, they will have a vested interest in maintaining firm prices.

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Those arguing in favor of a weaker market will point to:

- Elasticity of Demand – California stimulates demand by lowering prices, and then raises prices too high thinking that the demand paradigm has shifted. You won't see robust demand from the markets where we need to increase sales if you raise prices too high. But by the time this translates into the monthly shipment figures, an undisciplined correction will be under way.

- Grower Inventory – Growers are holding inventory in a call pool. They are likely going to use the May shipment figures to ask for higher prices for their inventory. Eventually, they have to sell the 2005 crop, as harvest of the 2006 crop, even if delayed, will start in about 70 days or so. Once new crop Nonpareils are available – even at $2.65 per pound – they will be a lot cheaper than the $3.15 or more being quoted for current crop. If they release their remaining inventory at the same time, prices could fall.

- Bigger than Expected Crop – This crop will come in over 1.1 billion pounds when all is said and done. We may not have the final figure until the end of November. By that time, those who are still holding a higher percentage of their crop than they want to be will see: (a) a lull in sales once the holiday season has passed; (b) the looming prospect of a 2007 crop; (c) a realization that the most we have ever shipped is 1.02 billion pounds in one season. In that 2003-2004 season, Spain had a 27,000 ton crop. This was followed by a 15,000 ton crop in 2004-2005. This "pending" shortage was known in California in the spring of 2004 and Spain bought actively from both the 2003 and the 2004 crops to cover for the domestic shortage. The average prices that season were $1.90 per pound for BSU5% and $2.12 per pound for NPS 23/25 AOL. For the 2006-2007 season, Spain has a 60,000 – 70,000 ton crop; the price in California for BSU5% is $2.25 per pound and for NPS 23/25 AOL is $2.60 per pound +.

- Price of Other Nuts – most nuts are trading off their higher levels. Almonds will not get "lost in the mix." If buyers cannot make money with almonds, they will decrease quantities or shift entirely to other nuts. They did this a year ago and they will do it again.

- Inshell Nonpareil Sales to India – The Indian market will not be able to sell in a timely manner and pay for all the inshell NP they have bought. Financing costs will mount and prices in the local market will come down in order to stimulate sales and cash flow. This will have a trickle down effect.

- Spain is likely to be happy to sell cheaper than California and take strong September and October positions (depending on their processing capacity, which was the bottleneck last year). If they do this, California shipments will lag. And missed September shipments are hard to make up.

Ultimately, whether you favor a bull market or a bear market, Winston Churchill said it best: "Everyone has his day, some days just last longer than others."

Best Regards,
DERCO FOODS