DERCO FOODS.®
INTERNATIONAL DIVISION

2670 West Shaw Lane, Fresno, California 93711 U.S.A.
Telephone (559) 435-2664 • Fax (559) 435-8520 • www.dercofoods.com • e-mail: derco@dercofoods.com

May 2008 Almond Position Report

May 2008 shipments were 88.4 million pounds. This is up about 15% from the May 2007 shipments of 76.7 million pounds.

Analysis

Carry-in from the 2006 crop year: 134 million pounds
2007 crop receipts: 1.38 billion pounds
Less 3% loss / exempt: (41 million pounds)
Total Supply: 1.470 billion pounds
Less shipments to date: (1.058 billion pounds)
Less estimated carry out: (235 million pounds)
Estimated Remaining Supply: 177 million pounds[1]

We came across two pieces of correspondence that we wanted to share.

A letter from a California almond processor to one of his growers

Mr. G. D. Gold
Perko's Café
Off any Highway 99 Exit
Pickyurtownen San Joaquin
USA

Dear Groen,

During the past couple of weeks, the current and new crop markets are firmer by $0.05 - $0.10 per pound. This is due primarily to the well-publicized notice of water rationing issued by the Westlands Water District on May 30th.[2] This district is the largest water district in the USA. It covers over 600,000 acres and accounts for about $1 billion in farm production.

You have been inundated (no pun intended) with lots of information on this topic during the past week. You have heard about the fact that we have just lived through the driest spring we have had since 1924 and of the lighter than expected snow pack in the mountains (67% of normal). You have heard more about the endangered fish, the Delta Smelt, and the federally mandated reduced pumping from the Sacramento-San Joaquin River Delta (the source for the Westlands water) in order to save this fish. You have read the newspaper and watched the news. You know water is short.

The bottom line is that as an almond grower in this district, you will likely get no more than 25% of your needed water through the summer months. You can't resort to pumping water, because as you know, the groundwater in your area is too salty. If you are a big grower and also farm row crops like tomatoes, alfalfa, etc., you may have some options. You can cut off the water to those crops and divert your allocation of water to your almonds. Not an exciting choice, but an available option. If you don't have this "luxury" (to kill off your other crops) – and all you farm is almonds – then pray for your trees, for your crop, and for any hidden benefits of deficit irrigation. You may still be able to salvage your 2008 almond harvest, though it may be less than you were expecting just a few weeks ago. As for the potential damage to your trees and for your 2009 crop, it's too

[1] Committed inventory is 223 million pounds and this is not factored into the above figures.
[2] In case you want to read the full text of the notice, it can be found at:
http://www.westlandswater.org/short/200805/notice244.pdf?title=05/30/2008

2670 West Shaw Lane, Fresno, California 93711 U.S.A.
Telephone (559) 435-2664 • Fax (559) 435-8520 • www.dercofoods.com • e-mail: derco@dercofoods.com

early to know but that seems to be the area of greatest concern at this time. Your local politicians are working on getting high-level government attention and Governor Schwarzenegger has declared California to be in an official state of drought. The bureaucratic wheels are in motion. That should put your mind at ease, though it's tough, even for the Governator, to manufacture water. Seems someone should have remembered a bit earlier what Robert Fulghum said: "The grass is not, in fact, always greener on the other side of the fence. Fences have nothing to do with it. The grass is greenest where it is watered. When crossing over fences, carry water with you and tend the grass wherever you may be."

Still, it's not all bad news. You can thank most of the other tree nuts that are currently priced more than $1 per pound higher than almonds. That gives you some breathing room to move prices up and to account for what could be lower than expected yields per acre and higher production costs. You can also thank the US economy. More sub-prime scandals, more investment banks needing bailouts, more ignorant and short-sighted people buying homes they can't afford and signing documents they don't understand (and blaming everyone but themselves for it). Add to this the highest unemployment rate in 21 years and a near zero growth rate…and what do you get? An economy that is a mess and a weak US dollar still hovering between $1.55 - $1.58 against the Euro. Sure, most of this is bad news for those who don't export and who rely solely on the domestic market, but heck, we control about 80% of global production and ship about 70% of our crop overseas! Yet another reason to love almonds.

Buyers who have been sitting on the sidelines are going to be calling me and asking me to offer almonds. But don't worry…I won't be doing much selling anytime soon. Still too much uncertainty, doubt and concern. So here's what I'm going to tell these prospective buyers:

"Hello dear *[insert name here]* – sorry I missed your call from ten days ago. We are not able to offer almonds at this time. We just don't have grower support. Our growers will not pull the trigger on anything under $1.80 per pound and you're trying to buy at $1.70 per pound. You were holding out for $1.55 per pound several weeks ago. Well, sorry that did not happen. Standards haven't gone that low since May 2003 and we've moved three one-billion-pound-plus crops since then. Plus, this water thing really has my field managers worried and my growers keep hearing that these walnut guys are talking about prices well above $3 per pound next season. I know lots of people are saying that the June 30th objective estimate can be as big as 1.5 billion pounds, but none of my growers are going to pay any attention to that number. With this water shortage, who knows what's going to happen to their trees? There are guys talking about a harvest in July if the situation does not improve. We're going to see lots more shrivel, lighter weight nuts and possibly damaged trees. The situation is bad, it's real bad. We're off the market until after harvest."

Hope that sounds good to you. See you at our annual Christmas party in December. Until then, don't sell a pound. Ramadan is coming early next year and you can sell all your Nonpareils in the spring. Stay strong. Stay withdrawn.

Best regards,

Ahlweis B. Booluhsh
Neighborhood Processor

2670 West Shaw Lane, Fresno, California 93711 U.S.A.
Telephone (559) 435-2664 • Fax (559) 435-8520 • www.dercofoods.com • e-mail: derco@dercofoods.com

Random e-mail intercepted from overseas importer to his client in Scandinavia:

Dear Tueleite Tuebai –

Hope you are having a good evening. The May shipments were just released in California. As we expected, a new record for May, up 15% over May 2007 and exceeding the previous record of 79 million pounds set in May 2006. Export shipments were another record 60.6 million pounds, surpassing the previous record of 52.9 million pounds also set in May 2006.

There was a report released this week that indicated US consumption of nuts has increased by 45% in the past ten years. Nevertheless, domestic shipments in May were not a new record and lower than last May (record 31 million pounds) by 10%. This is only the third time in the past ten months (and the first time in five months) that domestic shipments were not a record. Conversely, export shipments have been a record every single month this season.

The committed inventory figures are massive. Domestic commitments are up 43% and export commitments are up 91% from last year. Combined, these commitments total 223 million pounds. This leaves an uncommitted inventory of 190 million pounds – and that's not factoring in a carry out. Of course, some of these commitments will carry into the new crop season. But it seems a certainty that California will ship around 1.2 – 1.25 billion pounds this season. Carry-out into the 2008 season will almost certainly be well below 250 million pounds and supply in the transition may be tight once again for people who need additional cover of particular varieties or sizes.

Logistics challenges have moved to the forefront of all export transactions. Decisions on whether or not to be able to do new business depend on when the product is shipping, where it is going, and how it is going to get to the final destination. This equipment shortage, seriously curtailing export volume, is happening just as the US is seeing the largest trade deficit ($60.9 billion) in over a year. Can you taste the irony? That's why we have to offer you product as *"June or July shipment, as soon as the shipper can secure equipment and vessel space."*

Of course, you keep telling me that you have bought more heavily than usual to account for these shipping delays and that the purchases you made for June – August shipment will reduce from your needs during September – October. I believe you, but many in California think you're posturing. They still think you have more to buy and that the demand is growing, especially at these relatively attractive prices.

You have probably heard by now that they also seem to be running out of water in California. Someone is trying to remind these people that they are farming in a man-made oasis that is naturally a desert and that continuing to use flood irrigation is probably not the best way to conserve water. They never want to invest in dams and other water storage infrastructure (no new taxes) and then they want to declare states of emergency as if they are surprised by a water shortage that has been predicted for decades. Seems they should at best declare a state of denial or at worst a state of stupidity. Remember, their politicians are no different than ours: apathy until emergency, followed by feigned empathy and a contrived sense of urgency on topics essential for re-election.

2670 West Shaw Lane, Fresno, California 93711 U.S.A.
Telephone (559) 435-2664 • Fax (559) 435-8520 • www.dercofoods.com • e-mail: derco@dercofoods.com

Nevertheless and unfortunately for you, lack of planning on their part may actually constitute an emergency for you. It seems you may in fact have missed the boat. Not sure if you truly are covered until the last quarter of 2009, as you have been saying for the past 3 months, but unless you buy from that second hand trader who has been shorting his brains out at $363 (for an eventual but certain shipment of your 2008 contract *definitely* not later than the 2010 season), it doesn't seem that California is going to be offering much, or at the levels you were expecting, in the near future. You know, 1.4 billion pounds plus is barely enough to meet the growing global demand for almonds…...

Best regards,
Tuobaed Aymshuhrt

<u>Conclusion</u>
This was a bullish number. Not as bullish as people were talking about – but tough to put a negative spin on a 15% increase in May and a committed inventory figure of 223 million pounds out of a total remaining availability of 413 million pounds.

With a record crop coming, and an intense emphasis on monthly position reports, the current strategy in California leaves little room for marginal shipping months. If that happens, the pressure to lower prices will be intense. But at these levels, the downside risk just does not seem to be very significant and California knows it. Growers are going to be reluctant to discount when they feel that prices are already in a very reasonable trading range and when they see that their neighbors are getting considerably more money for their walnuts, pecans and pistachios. Any serious weakness may come only after disappointing new crop shipments in September and October. Otherwise, and until such weakness is proven, California will be unlikely to deviate from its current strategy of marrying the market to the monthly shipment reports and creating artificial shortages by withdrawing from the market. This strategy has worked too well for too long now.

Furthermore, if the Westlands Water District sticks to its current water allocation plans and if the growers who are farming almonds within that 600,000 acre district[3] only get the 25% share that they are talking about now, any discussion of lower prices is going to be countered with arguments of damage to the trees and a compromised <u>2009</u> crop. We cannot comment on what will happen to the production of trees next season that are denied all the water they need during this summer, but you can bet that there will not be a shortage of people in California voicing their doomsday opinions. This discourse may have a larger than expected impact on pricing. If a grower believes that the following year's crop is not going to be a good one, then all of a sudden the huge carry-out fear-factor is greatly diminished and the size of the current crop is effectively reduced – even if only psychologically. That's all that matters.

We hope that California will sell into the strength and give buyers a good chance to average their prices up. The variables are present to make that scenario happen. Extended withdrawals from the market may not be the appropriate strategy this season. There is a real crop on the trees and that crop needs to be sold sooner or later.

In the meantime, we cannot help but think of the old African saying, which seems à propos at this juncture: "A fool and water will go the way they are diverted." Let's hope for more water, good judgment and responsible marketing.

Best Regards,
DERCO FOODS

[3] Almond acreage in this district is estimated at around 100,000 acres.