

The KDM Dairy Report – May 24th, 2013

What's Bullish:

- Livestock Slaughter Report: 268,400 head of dairy cows were removed from the herd in April, the highest total on record (for April) and an 11.9% increase over 2012.
- Fluid Milk Central: As the manufacturing community prepares for the upcoming extended holiday weekend, some processors note they received few calls to place milk loads. In years past, milk would often sell well below Class prices during this weekend. With recent additions to Central region milk processing capacities, bargain priced loads are scarce. Reports continue regarding the feed challenges facing Central region dairy producers. A week of storms limited access

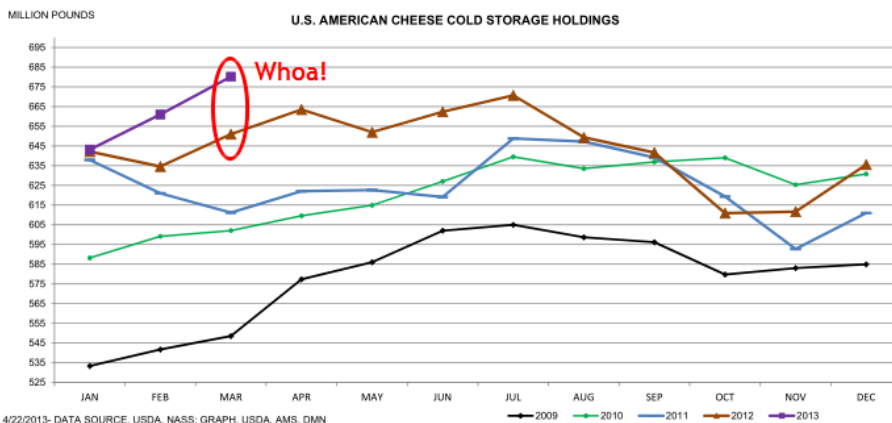
Futures Month	Class III 05/24	Class III 05/17	Change	Dry Whey 05/24	Dry Whey 05/17	Change	Cheese 05/24	Cheese 05/17	Change
May-13	\$18.51	\$18.52	(\$0.01)	57.75c	57.98c	(0.23c)	\$1.826	\$1.826	\$0.000
Jun-13	\$17.91	\$18.36	(\$0.45)	57.05c	57.25c	(0.20c)	\$1.764	\$1.804	(\$0.040)
Jul-13	\$18.45	\$18.73	(\$0.28)	57.50c	57.25c	0.25c	\$1.823	\$1.852	(\$0.029)
Aug-13	\$18.80	\$19.01	(\$0.21)	56.75c	57.75c	(1.00c)	\$1.853	\$1.869	(\$0.016)
Sep-13	\$19.00	\$19.12	(\$0.12)	57.00c	57.00c	0.00c	\$1.885	\$1.900	(\$0.015)
Oct-13	\$18.79	\$18.84	(\$0.05)	56.00c	56.00c	0.00c	\$1.860	\$1.878	(\$0.018)
Nov-13	\$18.48	\$18.43	\$0.05	55.25c	56.00c	(0.75c)	\$1.835	\$1.821	\$0.014
Dec-13	\$17.98	\$17.98	\$0.00	55.50c	55.50c	0.00c	\$1.786	\$1.780	\$0.006
Jan-14	\$17.46	\$17.55	(\$0.09)	54.35c	54.35c	0.00c	\$1.749	\$1.760	(\$0.011)
Feb-14	\$17.30	\$17.35	(\$0.05)	50.00c	50.00c	0.00c	\$1.752	\$1.752	\$0.000
Mar-14	\$17.15	\$17.17	(\$0.02)	49.00c	49.00c	0.00c	\$1.742	\$1.750	(\$0.008)
Apr-14	\$17.15	\$17.16	(\$0.01)	48.00c	48.00c	0.00c	\$1.752	\$1.752	\$0.000
12 Mo Avg	\$18.08	\$18.19	(\$0.10)	54.51c	54.67c	(0.16c)	\$1.802	\$1.812	(\$0.010)

- to pasture in many areas. Some producers reformulated to lower energy rations as a way to bridge the gap between stored feed and 2013 feed crop availability. The lower energy rations result in less milk production, yielding fewer dollars on milk checks. Some hay prices reported this week ranged from \$350 - \$450/ton delivered in the Central region. Anecdotal reports indicate winter wheat and barley fields planted as early feed crop alternatives are struggling and may yield limited feed value. Several milk handlers indicate the flush is apparently behind them as milk intakes are declining seasonally.
- Dry Whey Central: Prices stepped lower this week, but interest in dry whey is steady to somewhat higher. Some market participants are filling near and mid-term needs while the current downside price risk seems to be less than upside risk. Cheese production is steady to lower at a few locations. A few plant managers who were looking to fill up their plants indicated spot loads of milk were not being offered at any great volumes.
- Dry Whey West: Prices were mixed this week and trading ahead of the holiday was mostly lackluster. However, export demand continues to move much of the Western production.
- Cheese Midwest: The week leading into Memorial Day Weekend historically has been a week with cheese plants being offered spot milk at noticeable discounts below class. That is not the case this year. Some milk spot sales have occurred but relatively few, and at prices only slightly below Class - or even at Class prices. All of the plausible reasons are mentioned but most often cited is an earlier and/or less significant flush this year. A cheese manufacturer commented "there was no real flush this year so production was up in April and mostly leveled off".
- Cheese West: Cheese plants are operating busy schedules. However, demand from retail accounts is good, with comfortable inventories reported at the plant level. Export demand is increasing as block prices continue to moderate.
- CWT has accepted nine requests for export assistance to sell 3.016 million lbs of Cheddar and Monterey Jack cheese to customers in Asia, the Middle East and North Africa. The product will be delivered May through September 2013.
- International: Cooler conditions are prevalent over much of Western Europe and the slow start of the spring season is delaying pasture and crop growth. Milk output remains muted and overall levels are tracking several percentage points behind a year ago. The milk season is moving towards peak levels, yet the concern is over the length of the shoulder period after the peak. Current output remains lower than a year ago in France, the United Kingdom, and Ireland to name a few countries.
- International: Aussie milk production in April was down a significant 9.6% vs. a year ago, according to Dairy Australia. That's puts the current milking season output down 2.3% YTD.
- International: The New Zealand milk production season is moving towards the lower point of the year. Milk cows are being dried off or culled. The pasture conditions are poor to fair; only marginally helped by recent rains. The impacts of the cooler weather and slowing of the growing season are noted. More processing plants are reducing schedules or closing on or before schedule. Overall, processing has been scaled back to products of greatest needs as the milk flow has shorted ahead of most projections. March milk production numbers, Dairy Companies Association of New Zealand reports, are 16.8% lower than March 2012. Australian milk output is trending lower along seasonal patterns. The growing season is waning and grass and pastures are less conducive to needs. There has been mostly adequate moisture, but temperatures are cooling. More cows are being dried off for the season. Manufacturing milk supplies are slowing and more plants are being shut down for maintenance and idling.

What's Bearish:

- Spot Market: Sellers returned to the CME pit this week as the spot market see-saws up and down. Blocks declined 1¼¢ to settle at \$1.75¼/lb while barrels lost 3¼¢ to close at \$1.72¼/lb. Trading was moderate with 13 loads of blocks and 7 loads of barrels exchanging hands. NDM was unchanged at \$1.68/lb, but butter fell 6¼¢ to settle at \$1.55/lb on active trading of 18 loads.
- Milk Production Report: Output in April was up a surprising 0.2%, after showing year-over-year declines in February and March.

- Cold Storage Report: Butter stocks at the end of April were 22% higher than a year ago, a new record level. Stocks increased a record 22% from March as well. American cheese stocks were 5% higher than in 2012 and 2% higher than in March (see graph). Total cheese stocks were up 4% and 1% over the same periods.



- Crop Progress Report: 71% of the corn has been planted in the U.S. compared to the five year average of 79%. The rate increased 43 points in one week.
- Fluid Milk Sales: During March, 4.4 billion pounds of packaged fluid milk products is estimated to have been sold in the United States. This was 4.2% lower than March 2012.
- Most Class III components were lower in this week's dairy products sales report. Butter fell 4¢ to average \$1.64/lb, dry whey lost 0.5¢ to 57.2¢/lb and NDM gave up 0.6¢ to \$1.63/lb. 40-lb cheddar blocks lost 0.4¢ to average \$1.88/lb, but 500-lb barrels were up 2.1¢ to \$1.76/lb.
- Butter and cheese holdings continue to increase in May. Over the first 20 days of the month, butter stocks at USDA-selected storage centers are up 11%, or 1.8 million lbs. Cheese stocks are up 1%, or 1.4 million lbs over the same period.
- Dairy cow cull numbers fell for the fourth straight week. Just 55,500 head were slaughtered for the week ended 05/11, compared to 57,300 during the same period last year.
- Fluid Milk East: Milk production is nearing the seasonal peak and may well plateau as weather conditions are near perfect for milk production. Planting schedules are ahead of the 5 year average in the region and over 60% of the pastures are rated as good or excellent. Milk production in the Mid-Atlantic region is just beyond the seasonal peak. Manufacturing milk supplies for both regions will be heavy going onto the holiday weekend. Milk production in Florida has declined as the weather has turned hot and humid, lowering cow comfort levels. However, Class I demand has dropped as schools are beginning to close. The decline in fluid demand pushed the number of export spot loads to 110 this week, up from 90 last week. The coincidental occurrence of the Memorial Day holiday weekend and numerous school closings for summer break, have brought about a significant increase in manufacturing milk supplies in the Southeast region. Nearly all available auxiliary manufacturing plants are receiving moderate to heavy volumes of milk. Cream supplies remain heavy in the East prior to the holiday weekend.
- Fluid Milk West: Weather conditions continue to be very moderate in CA. There have been a few hot days, but not enough to stress the milking herd. Nights remain very cool and comfortable. There is not expected to be too much of a problem handling milk over the holiday, but cream could be another issue. Over the holiday weekend, demand is expected to slow even more with some real problems expected in clearing cream to churns or anywhere. Parts of the south are on their third cutting of alfalfa. Prices for supreme dairy hay are running \$230-240/ton FOB in the southern part of the state. Milk production is past the peak in AZ, but now schools are beginning to wind down for the summer so that plants are running full out. It is difficult enough to process the milk, but the real concern is cream over the holiday weekend. Discounts were heavy last week and they will be worse this week. Plants are running near full in NM, though more heat is expected at midweek and into the weekend. Milk production in the Pacific Northwest is following expected volumes. Moderate daytime temperatures and cool nights are adding to comfort levels for dairy cows. Milk production is still building towards peak and is above year ago levels. Some milk is being moved within the region to handle the supplies. Class I usage is expected to decline with the end of the school year. UT and ID milk volumes are increasing seasonally.
- Butter: Production is very active in the Central Region, helped by Eastern cream shipments. Northeast Butter production is increasing due to cream supplies which are expanding ahead of the upcoming holiday. The increase in cream supplies is prompting increased production of bulk butter as numerous butter makers are forced to expand inventories. Western Region butter production schedules remain heavy with cream continuing to find its way to butter churns.
- Dry Whey East: Prices marginally declined again this week in the face of production increases going into the holiday weekend. Triggering dry whey production expansion is the increased supply of manufacturing milk going to cheese plants. Current production is adding to most manufacturers' inventories. Domestic demand remains sluggish as most buyers are purchasing for immediate needs only, preferring to have a clearer picture of market, prior to expanding inventories.
- Cheese East: Increases in manufacturing milk supplies, due to reductions in Class I demand ahead of the upcoming holiday, are channeling more milk to cheese plants. For most cheese makers, the increases in production are adding to inventories with some plants expanding cheese volumes going into aging programs. Demand for cheese is mixed with cheddar retail sales sluggish, but orders for mozzarella remain fairly strong with good pulls from pizza makers. Export interest remains fairly good.

Recommendation:

Dairy prices continue to drift lower as near term excessive supply issues are balanced with longer term fears of tightness. Feed issues in the Midwest were highlighted in USDA updates this week. That, along with lower output in both the EU and Oceania probably mean there is less downside risk from here than upside risk. June Class III futures took the biggest hit this week, as near term fundamentals remain bearish. But losses in July on out were far less. We continue to recommend aggressive operations lift their hedges in July-Sep and take profits now. Those wanting to keep their hedges should buy upside insurance in the form of CALL options. With spot cheese in the \$1.70's again, international demand is picking up. And once we're well and truly past peak production in the U.S., buyers for fall needs will likely be back. For those that are looking for disaster insurance, consider the 17.25 or 17.50 PUT, July-Oct. **Note:** Our offices will be closed on Monday in observance of Memorial Day. Have a great weekend, and don't forget to thank a Veteran or active service member for your freedom!

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