

The KDM Dairy Report – September 6th, 2013

What's Bullish:

- Spot Market: Blocks gained 2¼¢ for the week to close at \$1.81/lb, it's highest level since May. Barrels jumped 3¢ to settle at \$1.80. It was bids only, with no trades taking place. Grade A NDM increased 1½¢ to settle at \$1.81½/lb on 7 trades, but butter decreased ¼¢ to close at \$1.43/lb on just 2 trades.

Futures Month	Class III 09/06	Class III 08/30	Change	Dry Whey 09/06	Dry Whey 08/30	Change	Cheese 09/06	Cheese 08/30	Change
Sep-13	\$18.06	\$17.83	\$0.23	58.25¢	58.00¢	0.25¢	\$1.787	\$1.763	\$0.024
Oct-13	\$17.86	\$18.19	(\$0.33)	57.88¢	57.25¢	0.63¢	\$1.766	\$1.799	(\$0.033)
Nov-13	\$17.37	\$17.53	(\$0.16)	57.50¢	57.03¢	0.48¢	\$1.719	\$1.737	(\$0.018)
Dec-13	\$16.83	\$16.90	(\$0.07)	57.50¢	57.05¢	0.45¢	\$1.655	\$1.665	(\$0.010)
Jan-14	\$16.56	\$16.51	\$0.05	54.25¢	54.03¢	0.23¢	\$1.662	\$1.652	\$0.010
Feb-14	\$16.46	\$16.41	\$0.05	53.10¢	53.00¢	0.10¢	\$1.660	\$1.649	\$0.011
Mar-14	\$16.53	\$16.40	\$0.13	52.75¢	52.50¢	0.25¢	\$1.662	\$1.651	\$0.011
Apr-14	\$16.47	\$16.35	\$0.12	51.25¢	51.50¢	(0.25¢)	\$1.675	\$1.642	\$0.033
May-14	\$16.48	\$16.40	\$0.08	50.50¢	51.50¢	(1.00¢)	\$1.672	\$1.652	\$0.020
Jun-14	\$16.72	\$16.69	\$0.03	50.50¢	51.53¢	(1.03¢)	\$1.706	\$1.677	\$0.029
Jul-14	\$17.00	\$16.99	\$0.01	49.50¢	49.50¢	0.00¢	\$1.740	\$1.718	\$0.022
Aug-14	\$17.11	\$17.02	\$0.09	49.00¢	48.00¢	1.00¢	\$1.740	\$1.730	\$0.010
12 Mo Avg	\$16.95	\$16.94	\$0.02	53.50¢	53.41¢	0.09¢	\$1.704	\$1.695	\$0.009

- Fluid Milk East: Manufacturing milk supplies in the Northeast and Mid-Atlantic regions are fairly tight coming out of the holiday weekend, due to strong pulls from Class I, along with increased demand from Class II and III manufacturers. Heat and humidity continue to lower cow comfort levels and milk production in Florida with daytime highs in the 90's and overnight lows in the 70's. A drop in fluid demand had 10 fewer loads entering the state this week, but the 180 loads that were imported was still far higher than the 72 loads imported a year ago. In the Southeast, manufacturing supplies are being held to contract minimums to ensure bottling plant needs are covered. Milk production continues to decline along the seasonal trend. Cream supplies going into the holiday period were readily available, but improved demand coming out of the weekend tightened supplies. Cream cheese manufacturing continues to show strong pulls for cream. Condensed skim milk supplies have tightened following the holiday as more milk is being directed to bottling plants. Demand has improved as Class II plants resume regular production schedules with cheese plants also on the lookout for additional loads to increase yields. Condensed skim supplies are fairly tight with some balancing plants preferring to dry their available volumes.
- Fluid Milk Central: Milk handlers in the upper Midwest report tankers are traveling a little lighter this week as the toll from last week's heat spell continues. Cooperative and independent cheese plant operators described juggling milk among various cheese plants as time consuming and expensive. Individual plant managers also indicate they are operating below capacity on a day to day basis, with some shaving weekly production by partial days. Balancing plant and cheese plant operators report milk sales into Class I facilities continue actively this week. Shipments are stairstepping toward the Southeast. Some butter/powder plant managers report they are churning or drying intermittently because of the decrease in availability of manufacturing milk. Cheese plant operators are in the hunt for spot loads of milk, but offers are infrequent. Prices hover in the \$2.00 - \$2.25 over Class range.
- Fluid Milk West: CA milk production is lower this week, being pulled down because of warmer weather conditions affecting the milking herds. While milk prices have improved, stress at the production level remains a factor. Class I needs are higher to service school and retail needs. AZ milk production is holding fairly steady, but temperatures are forecast to reach near record highs for this week. Handlers are pulling increased Class I needs as some local retailers have been running ad specials. NM milk output has been uneven, affected by variable weather conditions and an unsettled market economy. Processing plants are on reduced schedules with more milk leaving to service fluid and other accounts. Cream prices are firming this week. Demand is fair to good with some renewed interest developing following the holiday weekend.
- Butter: Over the long weekend, many churn operators enjoyed improved availability of cream spot loads, but once other plants were back on line, cream supplies tightened. Domestic print demand is strong into retail accounts rebuilding for late summer and fall promotions. The National Dairy Retail Report shows national ad numbers are up by 50% compared to two weeks ago.
- CWT has accepted requests for export assistance to sell 1.8 million lbs of butter and 1.3 million lbs of Cheddar, Gouda and Monterey Jack cheese. The product will be delivered August 2013 through February 2014. July butter and milkfat exports were 147% higher than July 2012 exports, and year to date exports are up by 26% compared to the same time span in 2012. Cheese exports for July 2013 were 22% higher than a year ago. The three largest importers of U.S. cheese are Mexico at 98.2 million pounds (+18%), South Korea 62.9 million pounds (+9%) and Japan at 43.0 million pounds (+9%). These three customers make up 52.6% of U.S. cheese exports.
- Dry Whey Northeast: Prices moved higher this week. Dry whey production is trending lower as Class I demand has pulled milk away from some plants and also due to lower milk component levels reducing yields. The lower production schedules and recent sales have improved some manufacturers' inventory levels and reduced the need to discount sales to better manage inventories. Domestic demand is slow to develop following the holiday, but export demand is reported to be improving with increased interest from Mexico and Asia.
- NDM East: Nonfat dry milk prices for low heat firmed, while holding steady for high heat. The combination of increased Class I demand and lower milk production has lowered manufacturing milk supplies and nonfat dry milk production. Domestic demand for high heat NDM has increased, but low heat demand is about steady with pre-holiday levels. Inventories for high heat remain tight with reduced low heat inventories as production has declined.
- NDM Central: Prices in the region shifted higher on steady demand from contract purchasers as well as some F.O.B. spot sales. Nonfat dry milk inventories are steady to lower as production sinks toward the annual low point. Strong demand from fluid accounts is reducing manufacturing milk availability, as well as strong demand from Class III producers who are also clearing milk loads into bottling. Anecdotal reports indicate the draw from the Southeast for milk is particularly strong this week as some bottlers are running consumer promotions.
- NDM West: Demand remains good and product is clearing into export channels. The news continues to be supportive of the SMP market. Producers' holdings are light to moderate.

- Cheese East: Fall orders for cheese are increasing with numerous cheese operations moving inventories through cut and wrap operations in order to fill orders. Cheese production continues to be on 6-7 day schedules with some plants seeking additional loads of nonfat solids to increase yields. Cheese going into aging programs remains strong. Demand for cheese is good with especially good sales going to pizza manufacturers. Export interest remains good.
- Cheese Midwest: Milk available to cheese plants is tightening and spot milk is getting more costly. Early week spot milk is up to \$2.25 over class in parts of the Midwest - when it can be readily obtained. This has led to some plants reducing production schedules, rather than pay to supplement milk supplies. Cheese inventories remain comfortable for anticipated demand, but sentiment heard from varied sources is that long-term, the tone of the cheese market is positive.
- Cheese West: Cheese sales are moving well for contracted volumes, but the higher prices have slowed spot sales activity. Tighter milk supplies are slowing cheese production, but some plants are willing to take any surplus milk offered. Export demand remains good and with added assistance from the CWT program, sales are clearing extra inventory.

What's Bearish:

- This week's GDT auction saw the dairy price index decline by 1.1%. Cheddar cheese fell 3.2% to a U.S. equivalent \$1.93/lb.
- Dairy cow slaughter for the week ended 08/24 totaled 58,700 head, down 2.2% from the same period a year ago.
- Dry Whey Central: Dry whey spot loads are available from several manufacturers within the region. Some producers are balancing inventories at other locations with Central loads, which is keeping contract shipments on time within organizations as a whole. While there has been little change in market conditions during the summer, dry whey producers note in the past year the Central region has gained dry whey production capacity through plant expansions and modernizations.
- Dry Whey West: Higher cheese production has increased available whey supplies for drying and inventories are increasing compared to a year ago. Manufacturers' stocks at the end of July for edible whey are 63.5 million pounds, up 39.8% from last year's unadjusted total. Buying interest is said to be increasing, but buyers are price conscious and looking for best deals.

Recommendation:

Well, we're back to scratching our heads again this week. The spot market made an unopposed move higher in cheese, NDM is tight, milk output is dropping around the country, demand is increasing with plants on lighter schedules around the country, and....Oct Class III finished the week 33 lower. Numerous sources we talked to this week, from traders to cheese plants, were perplexed as well. With spot cheese at \$1.80, it's interesting to note that October cheese futures settled at \$1.76. Current spot prices work out to about \$18.37 Class III, yet October milk futures, which will start pricing after next week, settled at \$17.86 today. Typically, futures will carry a slight to generous premium to the spot market, converging as time goes on, so this is very atypical. Either someone in the trade knows that cheese prices are set to fall in the near future, or Class III futures will eventually rise to close the gap. It could go either way, but based on the fundamentals as we know them, the downside in the spot market, as well as futures, seems limited. To us, the risk remains to the upside. We could be wrong, however! That said, our hedge recommendation for hedgers from last week remains unchanged. Look at selling Oct milk in the upper \$18's, Nov in the upper \$17's to low \$18's and Dec in the low to mid \$17's. While the front months finished the week lower, the 2014 contracts enjoyed a modest recovery, with the Jan-Jun pack gaining 8¢ from last Friday to an average of \$16.54. We recommend keeping that \$16.70 avg as a target, selling up to 25% of your milk there if it is profitable for your operation. Something is up with this market. Irrational moves like this could be the start of a volatile move. Hang on and have your orders in place!

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