

The KDM Dairy Report – April 17th, 2014

What's Bullish:

- Spot Market: Blocks gained 11¢ for the week to settle at \$2.28/lb, while barrels jumped 17¾¢ higher to \$2.25¾/lb. Trading was light with just 4 block trades and no barrel trades.
- Weekly cold storage numbers are showing a continued anti-seasonal drawdown in cheese stocks. Over the first 14 days of April, cheese holdings at USDA-selected storage centers are down 1%, or 764k lbs.
- Fluid Milk Central: Milk processors are noting even with the high milk prices they are seeing an increase in the number of retirements in small to medium-sized producers. The dairy farmers feel it is a great time to sellout given high replacement heifer and slaughter cow prices.
- Fluid Milk West: Farm milk intakes are stepping lower throughout CA. The modest upticks registered last week at some locations last week flattened out this week. Dairy producers point to higher than historical, average daytime temperatures as one probable cause of the decrease in milk production. Processors note the flush arrived early in many areas of the state, and has surpassed the peak. Demand from Class 3 (ice cream) processors is increasing weekly.
- Fluid Milk Northwest: Milk intakes in the region are variable this week. While milk production is building slowly in most of the region, some manufacturers are reporting tighter volumes this week. UT and ID milk production is building seasonally, but is still short of manufacturing demand. Excess loads of local milk are having no problems finding buyers.
- Dry Whey Northeast: Prices continued to firm this week. Manufacturers are focused on fulfilling customers' near term orders, while some buyers are purchasing product through the resale market. Demand for dry whey is steady and inventories are modest, giving the market tone a firm undertone.
- Dry Whey Central: Prices moved higher on stronger sales and index pricing. The market tone is firm with tight supplies. Contacts indicated buyers are looking at protein alternatives given the market firmness and prices of dry whey. Manufacturers dried steady to marginally higher volumes of whey following generally greater cheese production levels. However, cheese prices increased as the week went on, and a few manufacturers mentioned potentially scaling back production rates next week.
- Dry Whey West: Prices are higher this week as indices continue to firm and are moving contract prices upward. Spot activity is coming from resellers, with manufacturers' offerings being mostly committed. Sweet dry whey production is down as more of the whey stream moves into concentrated whey protein products. Demand for whey is good.
- Cheese Northeast: Production is steady and supplies are adequate for fulfilling short-term commitments, but tight inventories are limiting the number of spot market transactions. Domestic demand is good, while export interest remains solid with some additional forward sales.
- Cheese Midwest: Output is steady to higher in many areas of the Midwest as in the southern parts of the region milk production is coming up. Cheese plants having access to those increasing milk volumes are increasing cheese output. However, in the upper parts of Wisconsin and Michigan, winter lingers and stored hay and feed quality is poor. These factors are believed to be holding back milk production increases and thus, cheese production. Cheese sales have been good for many Midwest manufacturers, even though prices this year have been higher than the same date in recent years. The need to keep retail coolers stocked has largely supplanted previous retail store buyer tentativeness. Order patterns and order volume received by many cheese manufacturers now leads them to believe that higher prices have been accepted as reality for the time being, leaving buyers to respond to relative changes within the new higher level of prices rather than expect any significant price decline in the near term. Manufacturers report that declining weekly averages for the last two weeks have helped cheese sales. Thus, cheese manufacturers continue to manufacture cheese at levels possible with milk supplies available to them.
- Cheese West: Prices are rebounding higher this week. While some buyers took advantage of recent lower prices, others are still looking to make purchases. Barrel and block supplies are in balance with current needs. Cheese production is increasing slowly as milk volumes increase in the West.
- CWT has accepted 28 requests for export assistance to sell 5.340 million lbs of Cheddar, Gouda and Monterey Jack cheeses, 2.260 million lbs of 82% butter and 837,757 lbs of whole milk powder to customers in Asia, Central America, Europe, the Middle East, North Africa and the South Pacific. The product will be delivered April through October 2014.
- International: Monsoon season and the shortage of rains has caused a milk supply crisis in India, according to an article in The Times of India, this week. There is a milk shortage of about 15% which has caused prices for all dairy-related goods to jump. The situation is expected to last until the end of May.
- International: Cubans are getting squeezed by soaring milk prices, according to a CBS News article. The cost to the state to supply subsidized powdered milk to the population has dramatically increased, and now some of those costs are being passed on to consumers.

Futures Month	Class III 4/17	Class III 4/11	Change	Dry Whey 4/17	Dry Whey 4/11	Change	Cheese 4/17	Cheese 4/11	Change
Apr-14	\$24.21	\$24.02	\$0.19	67.175¢	67.850¢	(0.67¢)	\$2.344	\$2.321	\$0.023
May-14	\$22.14	\$21.50	\$0.64	66.000¢	64.750¢	1.25¢	\$2.143	\$2.091	\$0.052
Jun-14	\$20.37	\$20.05	\$0.32	64.100¢	61.450¢	2.65¢	\$1.975	\$1.955	\$0.020
Jul-14	\$19.48	\$19.55	(\$0.07)	61.250¢	58.750¢	2.50¢	\$1.893	\$1.924	(\$0.031)
Aug-14	\$19.28	\$19.45	(\$0.17)	59.000¢	57.000¢	2.00¢	\$1.891	\$1.926	(\$0.035)
Sep-14	\$19.21	\$19.41	(\$0.20)	57.125¢	56.025¢	1.10¢	\$1.895	\$1.919	(\$0.024)
Oct-14	\$18.92	\$19.04	(\$0.12)	57.000¢	56.875¢	0.13¢	\$1.865	\$1.882	(\$0.017)
Nov-14	\$18.55	\$18.71	(\$0.16)	56.075¢	55.775¢	0.30¢	\$1.832	\$1.853	(\$0.021)
Dec-14	\$18.30	\$18.35	(\$0.05)	56.050¢	56.700¢	(0.65¢)	\$1.805	\$1.820	(\$0.015)
Jan-15	\$17.97	\$18.17	(\$0.20)	55.500¢	56.050¢	(0.55¢)	\$1.800	\$1.820	(\$0.020)
Feb-15	\$17.96	\$18.07	(\$0.11)	54.000¢	54.000¢	0.00¢	\$1.817	\$1.827	(\$0.010)
Mar-15	\$17.94	\$17.95	(\$0.01)	53.250¢	53.250¢	0.00¢	\$1.798	\$1.798	\$0.000
12 Mo Avg	\$19.53	\$19.52	\$0.01	58.877¢	58.206¢	0.67¢	\$1.922	\$1.928	(\$0.007)

What's Bearish:

- Spot Market: While cheese prices saw a strong rally, Grade A NDM fell 4½¢ to settle at \$1.86½/lb and butter dropped 8¢ to close at \$1.89/lb. NDM loads traded were heavy at 12, while butter saw 7 transactions.

- Dairy slaughter numbers continue to show producers' desire to hang on to cows longer. For the week ended 04/15, 56,000 head were culled, down 6,400 head (-10.3%) vs. the same period last year.
- Fluid Milk East: Milk production at the farm level is up in the Northeast and Mid-Atlantic regions. Milk supplies are plentiful, with steady Class I demand. The Southeast region's warm temperatures are facilitating increases in milk production. Shipments of milk supplies are being transferred from bottlers to various manufacturers, due to a decline in Class I demand. Production in Florida is flat to strong this week. Weather conditions are conducive to cow comfort levels. Dairy cows are being moved from field grass over to feed as contacts note that an early flush is possible, due to early lactation. Class I demand is strong this Easter/Passover week, although tourists are returning to the North as warmer temperatures prevail. Cream supplies are strong with increasing milk production.
- Fluid Milk Central: Many producers in the Central region continue to add cows to their herds as milk processing facilities note milk supplies are slowly climbing higher. Bottling demand is flat with orders sluggish within the region. Contacts noted greater volumes of condensed skim available at reduced prices. Class II demand is reduced as orders are backing off from the past weeks' holiday-driven sales.
- Fluid Milk Southwest: Bottler orders in NM shifted sharply lower this week. Sales into Class II are strengthening, but fall short of easing the burden on drying plants for handling the pushback from fluid accounts. Balancing plant operators are monitoring the loads carrying over from one day to the next to make sure all milk is processed within allowed time limits. AZ milk production is mostly steady. Processors report they are busy handling in-state volumes, and have turned back some offered loads from out-of-state balancing plants.
- Butter Northeast: Domestic sales have slowed with the settling of buyer interest, which was spawned by butter demand for the Easter/Passover holiday. Inventories are sufficient for contractual commitments. Export interest is active, but the market tone is weakening.
- Butter Central: Prices are trending lower as post-holiday domestic sales slow and Oceania prices decline. The market tone is weakening as buyers are in a "wait and see" purchase approach. Some butter manufacturers are fulfilling prior export orders of 82%. International demand is good, but is slowing.
- Butter West: Prices are lower this week. The market is exhibiting a weak undertone. Retail demand has slowed slightly after holiday orders shipped. Export demand is mixed.
- NDM East: Prices are trending lower as heavy milk supplies are boosting production in a weak market. Sluggish condensed skim sales to Class III and Class II operations are adding to increases in dryer volumes. Spot transactions are limited as buyers are content with minimizing purchases, while waiting for possible lower nonfat dry milk prices, as inventory volumes increase.
- NDM Central: Prices moved lower on active spot trading and decreased pricing indexes. Many buyers are purchasing in a hand-to-mouth fashion with anticipations of deeper declines forthcoming. The market tone is weak.
- NDM West: The market tone is weak. Prices are moving lower, which pleases buyers, but there is no rush to contract for mid to long-term needs as buyers expect further price reductions.
- International: This week's GDT auction resulted in a 2.6% decrease in the dairy price index. The biggest decliners were butter milk powder down 8.6% and MPC down 7%. Cheddar cheese fell 3.3% to a U.S.-equivalent \$1.94/lb.

Recommendation:

Spot cheese prices made a dramatic reversal this week as Class III took a sizeable leadership role over Class IV for the first time in months. Despite having the most expensive cheese in the world, weakening dairy prices in Oceania and the EU, the 5th GDT auction in a row with a lower settlement and the prospect of rising domestic milk production, bidders went after product, getting only 4 loads of blocks. No doubt buyers had hoped for a more substantial fall in prices, but it appears that solid domestic and export demand throughout the first quarter has limited resellers' abilities to build inventory for aging programs and retail coolers. When the price "crash" didn't occur, buyers had to step up and purchase regardless of price. Futures continue to predict further price declines in the second half of the year, which all registered weekly declines. But up front, May finished up 64¢. Spot prices work out to about \$23.50 Class III and we are in the May calculation period. If bidders return next week, expect the May contract, which settled at \$22.14, to close the spread with cash even more quickly. From a fundamental standpoint, it doesn't appear that we have an over-abundance of cheese, but with Class III above Class IV, the vat may now attract more milk. And spring will eventually get to the upper Midwest and spur on production in the region. In the bull camp is CA which is past its peak and still in drought. Meal prices are climbing and hay is expensive. We would continue to look at buying call options July-Dec on milk you have already sold, and buy put options May and June for protection against a swing back down. With a shortage in India and continued demand in China, there is still a lot of uncertainty in this market. July-Dec settled at an \$18.96 average. While we might see more pressure near term, we think there is more upside risk than downside at these prices.

Note: Our offices will be closed tomorrow in observance of Good Friday. Markets will be closed. We wish you and your family a safe and blessed Easter!

This material has been prepared by a sales or trading employee or agent of KDM Trading, Inc. and is, or is in the nature of, a solicitation. By accepting this communication, you agree that you are an experienced user of the futures markets, capable of making independent trading decisions, and agree that you are not, and will not, rely solely on this communication in making trading decisions. DISTRIBUTION IN SOME JURISDICTIONS MAY BE PROHIBITED OR RESTRICTED BY LAW. PERSONS IN POSSESSION OF THIS COMMUNICATION INDIRECTLY SHOULD INFORM THEMSELVES ABOUT AND OBSERVE ANY SUCH PROHIBITION OR RESTRICTIONS. TO THE EXTENT THAT YOU HAVE RECEIVED THIS COMMUNICATION INDIRECTLY AND SOLICITATIONS ARE PROHIBITED IN YOUR JURISDICTION WITHOUT REGISTRATION, THE MARKET COMMENTARY IN THIS COMMUNICATION SHOULD NOT BE CONSIDERED A SOLICITATION. The risk of loss in trading futures and/or options is substantial and each investor and/or trader must consider whether this is a suitable investment. Past performance, whether actual or indicated by simulated historical tests of strategies, is not indicative of future results. Trading advice is based on information taken from trades and statistical services and other sources that KDM Trading, Inc. believes are reliable. We do not guarantee that such information is accurate or complete and it should not be relied upon as such. Trading advice reflects our good faith judgment at a specific time and is subject to change without notice. There is no guarantee that the advice we give will result in profitable trades.

© Copyright 2014 - KDM Trading, Inc. All Rights Reserved - www.kdmtrading.com