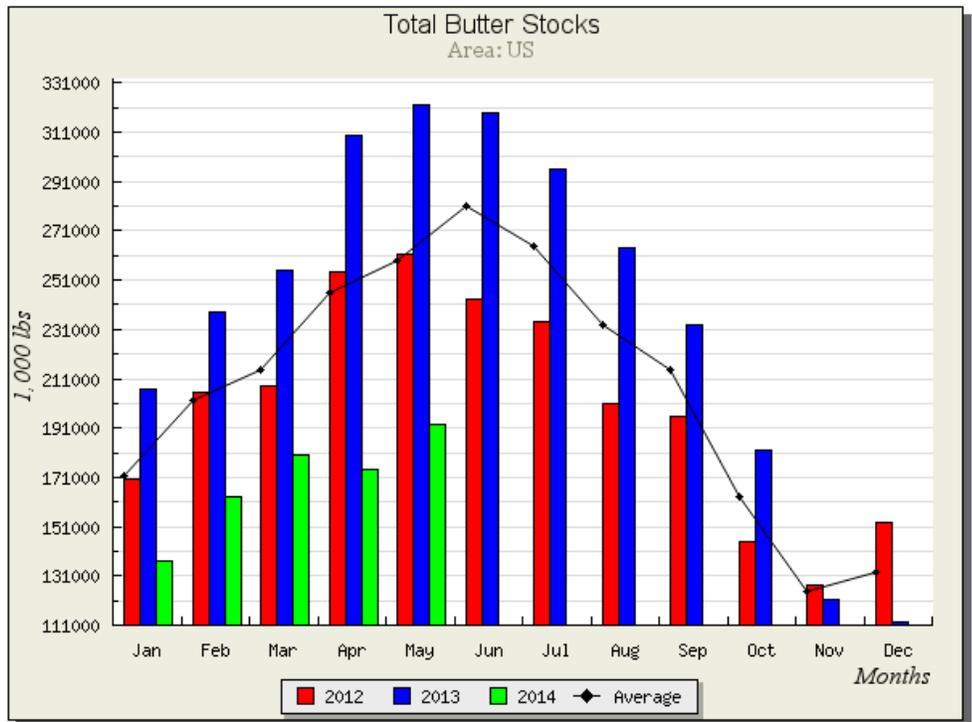


The KDM Dairy Report – June 27th, 2014

What's Bullish:

- Spot Market: Butter gained 15½¢ for the week on just 4 trades, settling at \$2.39/lb. Blocks picked up 2¢ to close at \$2.02/lb on 14 trades, but barrel finished unchanged at \$2.01/lb on 4 trades. Finally, NDM gave up 1¼¢ to settle at \$1.80¼/lb on 3 trades.
- Cold Storage Report: Butter stocks at the end of May were down 40% vs. a year ago, according to USDA. American cheese stocks were 8% less than last year while total cheese stocks were down 7%.
- Fluid Milk Southeast: Farm-level milk production saw substantial decreases this week especially in the southernmost states. Florida's milk production continues to decrease at heightened rates. Current weather conditions with temperatures above 100 degrees and consistent afternoon thunderstorms factor into adverse cow comfort levels. Class I demand is holding steady. Increased volumes of cream are clearing to the region's ice cream, ice cream mix and cream cheese manufacturers. Demand is strong across the board as tight supplies and opportunistic market developments lend to moderate butter production in some channels.
- Fluid Milk Central: Milk production in the region is mostly flat with a few slightly reduced farm intake levels. Milk handlers note butterfat levels coming down a bit as the cows' intake increased amounts of water to remain comfortable. Spot loads of milk ranged from \$2.00 under to Class, supplies are not as loose as previous weeks. Some bottlers noted improved sales, otherwise mostly steady. Class II demand is very good, most notably sour cream sales as a result of a holiday push. Cream cheese makers are trying to catch up on inventory, taking additional amounts of cream supplies. An increasing number of butter churn operators are electing to sell instead of putting cream into production.
- Fluid Milk Southwest: Milk production in CA has plateaued in recent weeks, though alfalfa prices continue to be troublesome, with premium dairy quality hay well into the \$300 per ton range. Hot weather in the triple digits is reducing milk intakes in AZ and NM, though monsoon humidity levels have yet to affect the states. Cream demand is good with cream moving from some contracted destinations to higher priced destinations. Ice cream, frozen confection mixes and butter plants are competing for available supplies.
- Butter Northeast: Very tight cream supplies have hindered butter production in the Northeast. Contracted suppliers delivered minimal loads as insufficient cream supplies spilled over into this week. Strong multiples continue to encourage butter manufacturers to sell cream supplies rather than churn. In consideration of the cream market's opportunistic underlying and steady butter exports, some market participants are stating, "if you can find it buy it," as a slight indication of the region's butter inventory levels.
- Butter Central: Prices surged this week on a bullish market as butter sales continue above historical trends resulting in tighter than typical inventories. More churn operators backed off highly sought after cream supplies as cream prices are rising to unprofitable levels to produce butter. Due to cream prices, use and demand for bulk butter is picking up steadily. However, buyers are finding supplies difficult to secure. Production rates are steady to lower. Some butter manufacturers noted lower butterfat levels in the milk. Domestic demand is very good.
- Butter West: Prices continue to show strength in the West. Tight supplies have buyers looking to acquire inventory for future needs. Domestic sales for retail have slowed, but end users are buying spot loads of bulk butter when available. Butter production is steady to lower. Some manufacturers continue to sell cream to satisfy demand.
- Dry Whey West: Milk deliveries to cheese plants remain heavy so whey stream production is strong. However, whey prices are mostly steady with some firmer noted in spot sales, as domestic demand is good due to ice cream plants at heavy stages of production. Export demand is steady, but meeting price competition from the EU.

Futures Month	Class III 06/27	Class III 06/20	Change	Dry Whey 06/27	Dry Whey 06/20	Change	Cheese 06/27	Cheese 06/20	Change
Jun-14	\$21.36	\$21.34	\$0.02	67.800¢	67.650¢	0.15¢	\$2.035	\$2.038	(\$0.003)
Jul-14	\$21.34	\$21.55	(\$0.21)	65.750¢	67.500¢	(1.75¢)	\$2.040	\$2.060	(\$0.020)
Aug-14	\$21.30	\$21.33	(\$0.03)	64.250¢	64.600¢	(0.35¢)	\$2.044	\$2.059	(\$0.015)
Sep-14	\$21.26	\$21.30	(\$0.04)	61.500¢	62.500¢	(1.00¢)	\$2.070	\$2.069	\$0.001
Oct-14	\$21.13	\$20.86	\$0.27	59.100¢	59.750¢	(0.65¢)	\$2.072	\$2.043	\$0.029
Nov-14	\$20.65	\$20.28	\$0.37	57.725¢	58.000¢	(0.27¢)	\$2.036	\$1.997	\$0.039
Dec-14	\$20.17	\$19.77	\$0.40	56.375¢	56.000¢	0.38¢	\$1.997	\$1.950	\$0.047
Jan-15	\$19.45	\$18.97	\$0.48	54.000¢	54.000¢	0.00¢	\$1.941	\$1.900	\$0.041
Feb-15	\$18.85	\$18.50	\$0.35	53.500¢	52.775¢	0.73¢	\$1.900	\$1.852	\$0.048
Mar-15	\$18.62	\$18.38	\$0.24	52.500¢	52.500¢	0.00¢	\$1.875	\$1.850	\$0.025
Apr-15	\$18.57	\$18.37	\$0.20	52.250¢	52.000¢	0.25¢	\$1.866	\$1.850	\$0.016
May-15	\$18.37	\$18.32	\$0.05	52.000¢	52.000¢	0.00¢	\$1.860	\$1.850	\$0.010
12 Mo Avg	\$20.09	\$19.91	\$0.17	58.063¢	58.273¢	(0.21¢)	\$1.978	\$1.960	\$0.018



- Cheese Midwest: Some Wisconsin cheesemakers have been offered spot milk at \$5.00 under class while also experiencing peak levels of patron milk intakes. But many are unable to take advantage of the surplus milk because, as one cheese plant manager observed, his operation is already scheduled for 7 days a week and can't physically make any more cheese. Other plants have noticed slight reductions in patron milk volumes. Cheese buyers, looking for blocks as well as barrels this week, are being told by many manufacturers that no cheese is available, due to existing commitments. A few cheese plants are dipping into inventories to make sales. Inventories are described as tight to comfortable.
- Cheese West: Wholesale prices are firmer for process, steady for Swiss and lower for the other varieties. Cheese production is steady with sufficient milk available to meet demand. Retail demand is good with little pushback. Commercial users are still buying to rebuild inventories when price breaks allow.
- CWT has accepted 5 requests for export assistance to sell 158,733 pounds of Cheddar and Gouda cheese, 2,315 million pounds of butter (82% butterfat) and 1,574 million pounds of whole milk powder to customers in Asia and the Middle East. The product will be delivered June through November 2014.

What's Bearish:

- Dairy cow slaughter for the week ended 06/14 totaled 47,100 head, down 8,200 head (-14.8%) vs. the same period a year ago. YTD the cull is behind last year's by 155,200 head (-10.3%).
- Fluid Milk Northeast: The Northeast and Mid-Atlantic northernmost regions are noted as experiencing somewhat of a late flush. Temperatures conducive to cow comfort are prompting marginal increases in milk production levels in these areas. Manufacturing milk supplies are plentiful and highly disproportionate to Class I demand. Most balancing plants are running full.
- Fluid Milk Pacific Northwest: Milk production in the region has leveled off, but current volumes are holding at high levels. Temperatures are comfortable for dairy cows with cool evenings relieving any heat stress. UT and ID milk production is above year ago levels. Favorable weather with some scattered rains is helping to alleviate dry pastures and help spring crops. Alfalfa harvesting is ongoing. Most manufacturing plants report sufficient milk is available within the region.
- Dry Whey Northeast: Prices adjusted slightly lower. Production is fairly steady and demand is good, but buyers are inclined to exercise caution when purchasing, as expectations of regressing dry whey prices loom. Inventories are adequate and building marginally. The market undertone is weakening.
- Dry Whey Central: Prices were mostly lower this week and the market tone is softening as many end users report having sufficient supplies on hand. Production levels remain at higher levels, while export orders have dropped with limited new sales. Inventory levels are rising.
- Cheese Northeast: Manufacturing milk supplies for Northeast cheese makers are favorable for 6-7 day production schedules, with noted increases in inventory levels. Export demand is steady, with some additional forward sales receiving support.
- During April, 4.1 billion pounds of packaged fluid milk products is estimated to have been sold in the United States. This was 4.5% lower than April 2013. Estimated sales of total conventional fluid milk products decreased 5% from April 2013.
- International: Ag analysts at Rabobank predict dairy prices will not recover for another six months. In their Q2 report, they blame a pullback in Chinese purchasing as the main reason. They suggest that China actually purchased more than it needed through Q1, and must now work through their accumulated stocks before prices can rise again in late 2014 or early 2015.

Recommendation:

Butter is the new price leader, it would appear. After grabbing 29 loads three weeks ago, 37 loads two weeks ago and 30 loads last week, buyers in the spot market were only able to purchase 4 loads this week, with bidders hiking the price to \$2.39/lb. The spot price was risen an impressive 20½¢ in two weeks! While strong cheese exports in Q1 have kept commercial buyers from building inventory in again programs this year, it appears that the U.S.' new-found ability to export butter in the format it prefers (82% unsalted), has left butter inventory levels low for this time of year. Indeed, this week's cold storage report puts butter stocks at the end of May 40% below last year's levels. With most of the country now past peak milk production, components declining from warmer weather and seasonal competition from ice cream production, cream is tight. While the butter/cream picture is bright, there is plenty of manufacturing milk available for cheese production. Buyers continue to be active in the spot market as they build inventory for fall, but as cheese plants work 6-7 day schedules, we wonder where cheese prices could go once that demand is satisfied. During Friday's spot session, both blocks and barrels fell, with offers being the aggressors. Class III sold off fairly hard, and we anticipate more selling next week as cheese manufacturers actively manage their inventory. Up front then, Class III looks a little heavy, and we would look to sell Aug at \$21.45 or better. However, the strength in butter/powder should act as some support. Class IV currently enjoys a \$2.40 premium over Class IIC, but probably won't be allowed to gain too much ground before there's a bigger incentive to make cheese. Last week we mentioned the Dec 17.00 put options as a decent, cheap "disaster insurance" strategy, and they filled this week at 12¢. Consider this simple plan if it makes sense for your operation, Sep-Dec. Looking at grains, demand is good but acres and near perfect weather has fundamentals in the bear column. The USDA Acreage and Grain Stocks reports on Monday could offer some surprises, but may also serve to remind traders of record acres and near record conditions. Falling feed prices will help fuel a milk production resurgence eventually, so don't abandon your risk management!

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