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# The KDM Dairy Report – September 5th, 2014

**What's Bullish:**

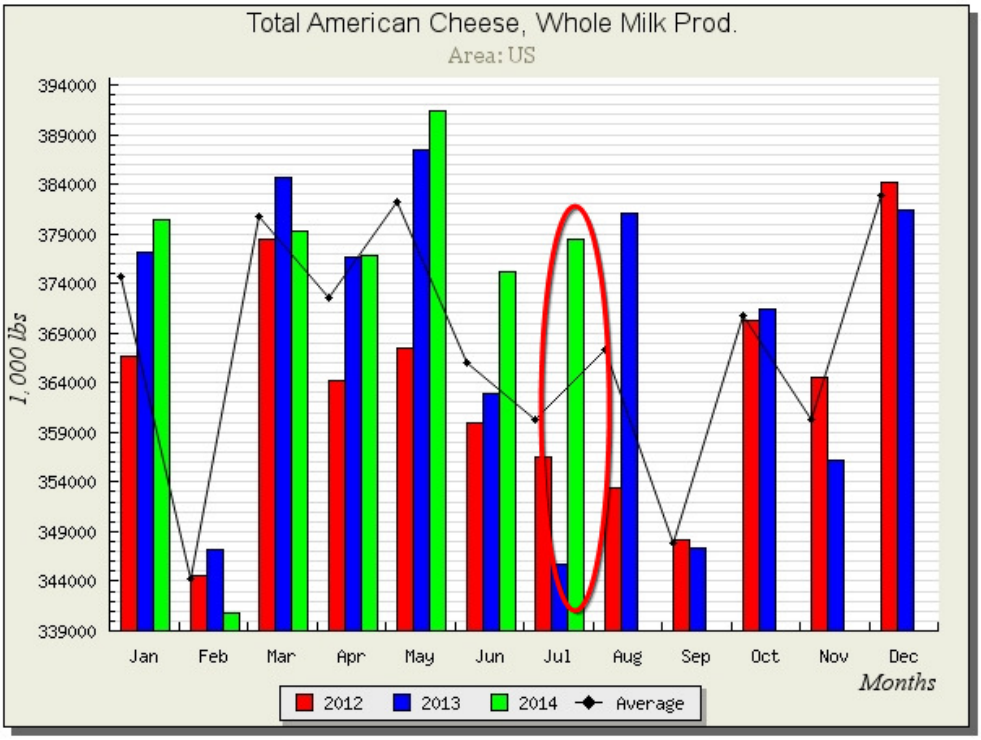
| Futures Month | Class III 09/05 | Class III 08/29 | Change | Dry Whey 09/05 | Dry Whey 08/29 | Change | Cheese 09/05 | Cheese 08/29 | Change |
|---|---|---|---|---|---|---|---|---|---|
| Sep-14 | $24.28 | $23.95 | $0.33 | 66.750¢ | 65.875¢ | 0.88¢ | $2.316 | $2.298 | $0.018 |
| Oct-14 | $22.67 | $22.87 | ($0.20) | 62.250¢ | 62.500¢ | (0.25¢) | $2.186 | $2.202 | ($0.016) |
| Nov-14 | $20.49 | $21.00 | ($0.51) | 59.000¢ | 60.000¢ | (1.00¢) | $1.990 | $2.040 | ($0.050) |
| Dec-14 | $19.47 | $19.80 | ($0.33) | 57.500¢ | 57.500¢ | 0.00¢ | $1.900 | $1.948 | ($0.048) |
| Jan-15 | $18.45 | $18.60 | ($0.15) | 54.000¢ | 54.500¢ | (0.50¢) | $1.838 | $1.856 | ($0.018) |
| Feb-15 | $18.01 | $18.21 | ($0.20) | 52.300¢ | 52.250¢ | 0.05¢ | $1.808 | $1.822 | ($0.014) |
| Mar-15 | $17.89 | $18.10 | ($0.21) | 51.000¢ | 51.800¢ | (0.80¢) | $1.802 | $1.813 | ($0.011) |
| Apr-15 | $17.84 | $18.04 | ($0.20) | 50.000¢ | 51.000¢ | (1.00¢) | $1.803 | $1.812 | ($0.009) |
| May-15 | $17.85 | $18.00 | ($0.15) | 51.000¢ | 51.000¢ | 0.00¢ | $1.802 | $1.816 | ($0.014) |
| Jun-15 | $17.87 | $18.05 | ($0.18) | 50.250¢ | 50.250¢ | 0.00¢ | $1.812 | $1.825 | ($0.013) |
| Jul-15 | $18.00 | $18.04 | ($0.04) | 50.625¢ | 52.000¢ | (1.38¢) | $1.816 | $1.830 | ($0.014) |
| Aug-15 | $18.00 | $18.02 | ($0.02) | 51.750¢ | 52.000¢ | (0.25¢) | $1.815 | $1.820 | ($0.005) |
| **12 Mo Avg** | **$19.24** | **$19.39** | **($0.16)** | **54.702¢** | **55.056¢** | **(0.35¢)** | **$1.907** | **$1.924** | **($0.016)** |

- Spot Market: Blocks gained 2¢ on the week to settle at $2.35/lb, while barrels lost 2¢ to close at $2.32½/lb. There were no trades in blocks, but 4 loads of barrels exchanged hands. Grade A NDM gained ¾¢ to settle at $1.33¼/lb on just one trade, while butter shot up 9¢ to $2.84½/lb on 17 trades.
- Fluid Milk East: Milk production in the Northeast and Mid-Atlantic regions is seasonally high, but showed some declines as heat and humidity hampered cow comfort. Class I demand is good as school re-openings continue to drive bottling sales. Milk supplies are meeting increasing Class I demand in the Southeast. Production continues to decline along seasonal trends. In Florida, weather conditions are furthering the decline in milk output. Bottlers are ramping up production as orders surge with classes resuming in the state. Spot imports totaled 200 loads this week, an increase of 40 truckloads from the previous week. Cream supplies are beginning to tighten as cream cheese demand continues to prompt substantial cream usage in manufacturing.
- Fluid Milk Southwest: NM milk production is steady while bottler demand is higher, along with increasing interest from out of state buyers. A shortage of drivers is causing some slowdown in transportation. AZ haulers and processors indicate high daily temperatures, along with occasional rain storms and higher humidity, are impacting milk production and components. Processors expect little improvement in milk intake volumes until cooler temperatures arrive in the next few weeks. Butterfat components are trending lower as the 100+ degree daytime temperatures decrease cow comfort. Processors are hoping to cover cream contracts with internal cream loads and cream from intrastate milk loads. Transportation costs from other areas are limiting options for those operators running short on cream.
- Butter: Despite the current high prices, domestic demand continues to outpace supplies, hindering inventory levels as fourth quarter demand looms. Some buyers noted lead times for new orders are growing. Butter producers are increasingly concentrating on filling retail orders for upcoming fall needs. Butter stocks are tight with spot loads hard to find.
- Cheese Northeast: Cheese manufacturers are continuing heavy production, but milk supplies going into cheese production are marginally reduced as schools ramp up Class I demand after the holiday weekend. Milk volumes are adequate for fulfilling current cheese orders, but inventories remain fair to tight.
- Cheese Midwest: Most cheese plants are near full production, yet buyer demand is characterized as "hungry". Milk supplies to cheese plants remained on schedule to maintain planned cheese production, while strong cheese orders are keeping plants busy. Some manufacturers have noted that a number of buyers looking for spot loads of cheese, aware of the challenge of finding cheese not already committed to orders, seem to be initially making inquiries for less than desired amounts. When the buyers find available spot loads, a number quickly ask to buy more. When a pending cheese export order was canceled, the cheese was quickly sold domestically. Orders for pepper jack and Colby jack are noted to be increasing. Filling barrel orders is delayed in some plants due to specific factors leading to production refocusing to increase product profitability. Interest in aged cheddar is expected to increase in coming weeks. Finished natural orders are generally steady to improved with overtime needed on some lines such as shreds.
- Cheese West: Increased milk supplies are being directed to cheese production to meet the demand. Domestic cheese demand is good with retail orders steady to strong and institutional food service demand increasing as schools return. Export sales have slowed as U.S. prices are above international prices. However, cheese stocks are tight for barrels. Blocks supplies are adequate for current demand.

**What's Bearish:**

- Exports: The pace of exports in July slowed to its lowest in six months, falling a sharp 9% from June, according to statistics released by the U.S. Dairy Export Council this week. More competition from Oceania and the E.U., with lower priced product, were most likely the main factor. Exports as a percent of production was 15.9% in July, down from 16.4% in June and the Jan-July avg of 16.4%.
- Prices for dairy products in this week's Global Dairy Trade auction fell an average of 6%. Cheddar cheese declined 4.9% to a U.S. equivalent price of $1.48½/lb. Yikes!
- Dairy Products Report: American cheese output in July jumped 9.5% above a year ago (see chart below), while Total Cheese production increased 7%, according to USDA numbers. Butter output was 2.6% higher than last July, but down 3% from June.
- Dairy cow slaughter for the week ended 08/23 totaled 54,500 head, down 4,200 head (-7.2%) vs. the same period a year ago.
- Fluid Milk Central: Improved feed quality and higher cow numbers are pushing milk production rates higher in the Central region. All schools are back in session, pushing bottling sales higher. However, some bottlers noted declining year-on-year fluid sales. Ice cream/frozen dessert production rates are being scaled back as new orders are slowing. Cream demand is seasonally weaker as Class II manufacturer ingredient purchases are changing as fall nears. Cream supplies are higher as additional volumes became available over the holiday weekend.
- Fluid Milk West: Processors report milk production in CA as mostly steady, with some occurrences of marginal volume increases. Demand is flat from bottlers as the school pipeline is completely full and consumer demand is at seasonal levels. Producers indicate feed availability is adequate to maintain production at reasonable costs.

- Fluid Milk Pacific Northwest: Market participants note additional Grade B cream loads offered to the market this week. Cream demand from cream cheese, sour cream, and ice cream manufacturers is active. Milk production continues to drop off seasonally, but increased cow numbers are helping to keep volumes above year ago levels. Favorable rains and adequate irrigation water have the corn silage crop nearly ready for harvest. UT and ID milk supplies are up from year ago amounts. Processors are finding sufficient supplies for most of the demand in the region. Milk component levels remain favorable and are helping to increase yields.
- Dry Whey Northeast: Prices were steady to lower this week. Production is edging higher while paralleling cheese production for the region. Sales have slowed significantly into ice cream production. Limited transactions are occurring in the spot market. Some resellers note losing orders because of market competition. The market undertone is weak.




- Dry Whey Central: Prices shifted mostly lower as weaker global whey prices along with cheaper alternative proteins are putting downward pressure on spot load pricing. The undertone is softening. Production rates are generally improved as cheese makers are increasing vat schedules.
- Dry Whey West: Prices are lower and the market tone is weak, as increased volumes of whey are being offered to the domestic market. Whey production is steady to higher as cheese plants continue to run heavy schedules. Domestic demand is good with some buyers filling immediate orders, but others are cautious about securing additional loads as the market exhibits weakness. International demand for U.S. whey is being challenged by increasing amounts of E.U. whey being offered at lower prices. U.S. whey stocks continue to build for both manufacturers and brokers.
- NDM: The nonfat dry milk market is weak and prices are mostly lower. The global market is also reporting lower prices for nonfat dry milk and skim milk powder. With lower international prices as a backdrop, domestic buyers are less interested in discussing contracts at prices that are not in step with the perceived world market for nonfat dairy solids.

**Recommendation:**

With the exception of the front month September contract, Class III futures finished in the red this week. Yes, cheese is still tight in the short term, but there is a growing understanding that supply may be catching up with demand (or demand is about to decline). Of course the market has factored much of this in, with Jan futures nearly $6/cwt lower than Sep. Or has it? We are dependent on strong exports to support dairy prices, so it was more than a little concerning to read that July dairy exports were off 9% from June. With our stratospheric cheese and butter prices here in the U.S., we're willing to bet that Aug exports were even lower than July. We've heard through our connections that butter and cheese will be landing on our shores soon. This week's GDT auction priced cheddar at $1.48/lb! We're not saying we're going that low, but we could end up heading much lower than people expect. That is the way of markets! Grain prices continue to erode making it all but sure feed prices will be low well into 2015. And cow numbers continue to rise as culling rates decline. We might be headed for a train wreck folks, unless there is a sudden pick up in international demand in Q4 (which did in fact happen last year). We think it's time for producers get more aggressive in their hedging and suggest selling Nov-Mar or Nov-Jun. The Nov/Dec avg is $19.98; sell at $20.00 or better. The Jan-Jun ave is $17.98; sell at $18.00 or better. We would consider marketing 25-50% of your milk here. In summary, despite the discount the futures market has priced in going forward, we may end up heading much lower before coming back up. We think it's only a matter of 10-60 days before demand is satisfied and we start a correction lower.