

The KDM Dairy Report – January 2nd, 2015

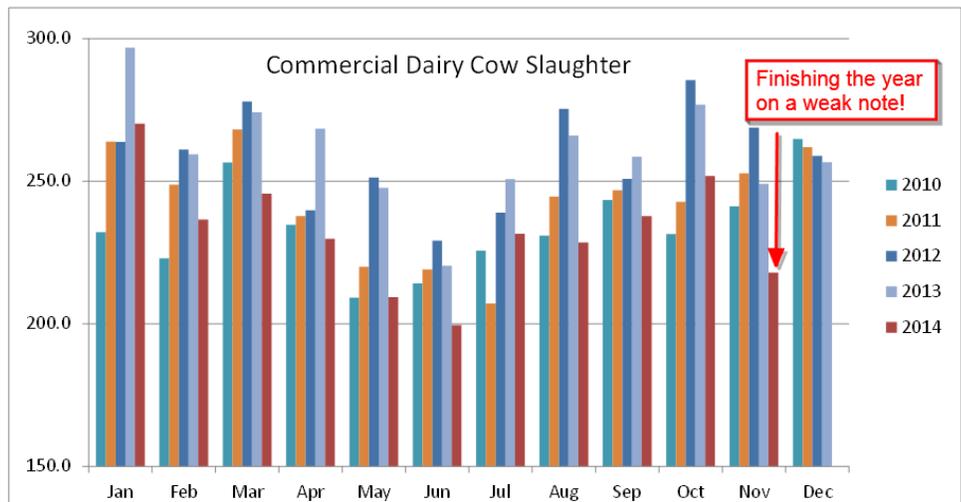
What's Bullish:

- Spot Market: Blocks gained 7½¢ for the week to settle at \$1.57/lb while barrels jumped 12¢ to reach \$1.54/lb. There were no trades in any spot markets this week. NDM and butter finished unchanged at \$1.00/lb and \$1.55/lb respectively.
- Ag Prices Report: The milk-to-feed ratio fell from 2.74 in Nov to 2.38 in Dec, after reaching a recent high of 2.97 in Sep.
- Fluid Milk Southwest: Class I sales improved early in the week as bottlers used the weekend to bring in loads to restock consumer outlets. Sales into Class II are steady to slightly higher. Cheese manufacturers are running close to full at several locations to meet active January demand. Sellers indicate demand from cream cheese, sour cream, and a few ice cream plants is above the usual holiday week volumes. Cream is also clearing into butter churning operations as last minute print orders near completion. Bulk butter production is taking the balance of available cream.
- Cheese West: Production in the region continues to focus on fulfilling contracts. Cheese prices are at a level where manufacturers are comfortable keeping inventories. Recent price decreases have helped demand for domestic and export markets.

Futures Month	Class III 01/02	Class III 12/26	Change	Dry Whey 01/02	Dry Whey 12/26	Change	Cheese 01/02	Cheese 12/26	Change
Jan-15	\$15.92	\$15.75	\$0.17	54.000¢	53.175¢	0.83¢	\$1.573	\$1.565	\$0.008
Feb-15	\$15.49	\$15.22	\$0.27	48.125¢	47.300¢	0.83¢	\$1.579	\$1.551	\$0.028
Mar-15	\$15.27	\$14.94	\$0.33	41.075¢	41.425¢	(0.35¢)	\$1.600	\$1.562	\$0.038
Apr-15	\$14.99	\$14.95	\$0.04	38.000¢	38.500¢	(0.50¢)	\$1.590	\$1.580	\$0.010
May-15	\$15.16	\$15.08	\$0.08	38.375¢	38.500¢	(0.13¢)	\$1.614	\$1.587	\$0.027
Jun-15	\$15.54	\$15.53	\$0.01	38.000¢	37.500¢	0.50¢	\$1.653	\$1.637	\$0.016
Jul-15	\$16.15	\$15.92	\$0.23	38.250¢	38.500¢	(0.25¢)	\$1.700	\$1.670	\$0.030
Aug-15	\$16.32	\$16.10	\$0.22	39.250¢	38.975¢	0.27¢	\$1.715	\$1.692	\$0.023
Sep-15	\$16.63	\$16.40	\$0.23	38.000¢	38.000¢	0.00¢	\$1.746	\$1.721	\$0.025
Oct-15	\$16.65	\$16.54	\$0.11	38.850¢	38.500¢	0.35¢	\$1.747	\$1.732	\$0.015
Nov-15	\$16.55	\$16.46	\$0.09	38.500¢	38.750¢	(0.25¢)	\$1.730	\$1.717	\$0.013
Dec-15	\$16.31	\$16.35	(\$0.04)	38.500¢	38.500¢	0.00¢	\$1.713	\$1.715	(\$0.002)
12 Mo Avg	\$15.92	\$15.77	\$0.15	40.744¢	40.635¢	0.11¢	\$1.663	\$1.644	\$0.019

What's Bearish:

- Dairy cow slaughter for the week ended 12/20 totaled 59,400 head, down 3.4% from a year ago. For 2014, the dairy cull finished the year 9.6% below 2013, slaughtering 300,000 fewer head.
- Livestock Slaughter Report: 217,900 dairy cows exited the milking herd in Nov, down 31,200 head (12.5%) vs. Nov '13.
- Cold Storage Report: American cheese stocks at the end of Nov were 3% higher than the prior year, while total cheese stocks were up 2%.
- Fluid Milk Northeast: Farm milk output is above last year's level at this time in the Northeast and Mid-Atlantic regions. Milk orders have declined at most bottling operations and are increasing the number of loads clearing to balancing and cheese facilities.
- Fluid Milk Southeast: Milk production in the Southeast is up. Distribution operations are managing heavier than usual milk loads with the withdrawal of Class I holiday demand. The cream market continued to show year-end holiday weakness as cream multiples for all Classes ranged 0.95-1.16. Supplies are ample, with some surplus loads moving into a few Midwest butter plants.
- Fluid Milk Central: Milk production continues to exceed expectations. Milk supplies are abundant as many plant schedules are or close to capacity. Processors are having difficulties moving excess milk spot loads, as prices range from \$11.00 under to \$3.00 under Class. Bottling sales are slow, but orders are anticipated to pick up later in the week as schools refill pipelines in preparation for the new semester. Class II orders are slow. Cream supplies are loose.
- Fluid Milk Southwest: Milk production in CA is generally steady, while processors are coordinating efforts throughout the state to place milk loads within reach of plants that have room to process additional loads. Milk production continues to ramp up in AZ. Butter/powder plant operators have some long production runs scheduled to clear both in-state milk volumes and imported loads coming in for the processing room. Recent rainstorms delivered some moisture, which has helped crop conditions. Alfalfa harvesting is ongoing. NM milk production continues to edge higher from week to week.
- Fluid Milk Pacific Northwest: Milk production in the region is mostly unchanged, but surplus cream is available and being distributed to butter churns. UT and ID milk production is steady to climbing.
- Butter: Cream supplies were increasingly available resulting in generally higher butter churn rates. Inventories are mostly growing as domestic sales have slowed seasonally. However, orders are exceeding some manufacturers' expectations. Export interest is minimal.
- Dry Whey Northeast: Prices inched lower this week. Dry whey is realizing an increase in output in the region as heavy milk supplies, over the Christmas holiday period, increased cheese production. The whey market is weak, with ample supplies available. Export interest is sluggish.



- Dry Whey Central: Some cheese plants took on extra milk over the holidays, thus producing cheese at higher levels creating additional dry whey production. Exports are limited. Many buyers are sitting on the sidelines, while anticipating weaker prices available in the future.
- NDM Northeast: Prices are steady to lower while the market continues to weaken. NDM production is at a high level for the week as some manufacturers took in heavier milk loads for processing. Unsuccessful efforts to move oversupplies of condensed skim are challenging the production capability of some plants. Distribution is restricted as truck availability is limited in some cases. Low/medium heat inventories continue to build.
- NDM Central: The market tone is weak. Production rates are generally strong as manufacturers keep up with heavy milk supplies.
- NDM West: The market tone is weak as supplies are higher than near term demand at several locations. Buyers who do not require NDM from approved suppliers are reluctant to commit to any 2015 pricing or volumes due to the continuing weak market. Production is active throughout the region as milk production is steady to higher in many areas.
- Cheese Northeast: Milk supplies to cheese manufacturers are substantial as intakes were heavy over the Christmas holiday weekend, resulting in steady to increased cheese production. With declines in holiday sale volumes, there is nonetheless moderate interest in aged cheddars, provolone, mozzarella and cream cheese. Cheese interest should remain fairly active spurred by playoff events leading up to the Super Bowl. However, buyers favor a wait and see approach, with the expectation prices will move lower and stabilize. Bulk cheese inventories are building at the plant level.
- Cheese Midwest: The market tone is steady with heavy production due to additional milk volumes. Many manufacturers took on additional milk supplies at \$6.50 under Class. Buying is slow due to cheese prices dropping, while inventories are building.

Recommendation:

College and NFL Playoff football games continue to bring in some last-minute demand, but more and more it appears that supply is beginning to get the upper-hand on demand. Lower prices are spurring some additional interest, but we believe that demand will be satisfied at some point, with dairy output only continuing to increase into the spring. We don't know how low prices could go, but we're hearing talk of cheese heading into the \$1.30's and possibly into the \$1.20's. Unless demand from China or other international buyers improves dramatically, that may indeed be where we're headed. Despite gains in spot cheese prices, Class III futures continue to sell off. Rallies do not even appear to last beyond intra-day. That is bearish. Current spot prices work out to about \$15.50 Class III, and that's after this week's rally in cheese prices. Should spot cheese prices begin to head south again after two holiday-shortened trading weeks, Class III futures will once again be on the decline, and likely headed into the \$14's. Cold storage inventory is up while slaughter numbers continue to lag. Until producers feel the incentive to change course, which isn't likely to happen for months, supply levels will likely continue to increase. We continue to recommend producers sell rallies in the first half of 2015. We are hopeful we will see a price recovery sometime in late Q3 or Q4.

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