

**The KDM Dairy Report – January 9<sup>th</sup>, 2015**

**What's Bullish:**

- Spot Market: Blocks finished week up 2¢ to \$1.59/lb on no trades, while barrels managed a ½¢ increase to \$1.54½/lb on just one trade.
- Fluid Milk East: Milk production in the Northeast and Mid-Atlantic regions is steady to heavy. But Class I demand is good with the reopening of schools and conditions at balancing plants are more manageable. Milk supplies in the Southeast are avoiding most manufacturing facilities as bottling add-ons increase, prompted by a wintery snow and ice scare. Florida is seeing plenty of milk produced at the farm level, but milk shipments in and

Futures Month	Class III 01/09	Class III 01/02	Change	Dry Whey 01/09	Dry Whey 01/02	Change	Cheese 01/09	Cheese 01/02	Change
Jan-15	\$15.97	\$15.92	<b>\$0.05</b>	56.000c	54.000c	<b>2.00c</b>	\$1.581	\$1.573	<b>\$0.008</b>
Feb-15	\$14.84	\$15.49	<b>(\$0.65)</b>	45.750c	48.125c	<b>(2.38c)</b>	\$1.521	\$1.579	<b>(\$0.058)</b>
Mar-15	\$14.66	\$15.27	<b>(\$0.61)</b>	40.250c	41.075c	<b>(0.83c)</b>	\$1.539	\$1.600	<b>(\$0.061)</b>
Apr-15	\$14.41	\$14.99	<b>(\$0.58)</b>	35.250c	38.000c	<b>(2.75c)</b>	\$1.540	\$1.590	<b>(\$0.050)</b>
May-15	\$14.52	\$15.16	<b>(\$0.64)</b>	34.150c	38.375c	<b>(4.23c)</b>	\$1.561	\$1.614	<b>(\$0.053)</b>
Jun-15	\$15.00	\$15.54	<b>(\$0.54)</b>	34.000c	38.000c	<b>(4.00c)</b>	\$1.608	\$1.653	<b>(\$0.045)</b>
Jul-15	\$15.76	\$16.15	<b>(\$0.39)</b>	34.500c	38.250c	<b>(3.75c)</b>	\$1.683	\$1.700	<b>(\$0.017)</b>
Aug-15	\$16.09	\$16.32	<b>(\$0.23)</b>	35.500c	39.250c	<b>(3.75c)</b>	\$1.715	\$1.715	<b>\$0.000</b>
Sep-15	\$16.34	\$16.63	<b>(\$0.29)</b>	35.000c	38.000c	<b>(3.00c)</b>	\$1.737	\$1.746	<b>(\$0.009)</b>
Oct-15	\$16.35	\$16.65	<b>(\$0.30)</b>	35.000c	38.850c	<b>(3.85c)</b>	\$1.740	\$1.747	<b>(\$0.007)</b>
Nov-15	\$16.36	\$16.55	<b>(\$0.19)</b>	36.100c	38.500c	<b>(2.40c)</b>	\$1.736	\$1.730	<b>\$0.006</b>
Dec-15	\$16.20	\$16.31	<b>(\$0.11)</b>	36.000c	38.500c	<b>(2.50c)</b>	\$1.718	\$1.713	<b>\$0.005</b>
<b>12 Mo Avg</b>	<b>\$15.54</b>	<b>\$15.92</b>	<b>(\$0.37)</b>	<b>38.125c</b>	<b>40.744c</b>	<b>(2.62c)</b>	<b>\$1.640</b>	<b>\$1.663</b>	<b>(\$0.023)</b>

- out of the state remain balanced. Class I demand is steady to higher following the New Year's holiday and schools reopening. Cream supplies are moving toward equilibrium as manufacturing plants in the Northeast and Mid-Atlantic resumed ice cream production.
- Fluid Milk West: Milk production in CA is flat to slightly lower throughout the state. Dairy industry members indicate the decrease in milk prices, coupled with assessments from some processors, has hit dairy operators doubly in the last few months. Some operators are trying to stretch feed inputs on hand until new crop hay becomes available in late March. Operators are also changing rations to stretch feed dollars. Class I sales are steady to higher for the week as K-12 schools start the new semester. Some universities have another week before resumption of classes, and orders for bottled milk are building to accommodate demand from that sector.
- Exports: U.S. dairy exports in November fell 7% by volume and 14% by value vs. Nov '13, according to the U.S. Dairy Export Council. Cheese exports dropped 13% (down for the 5<sup>th</sup> straight month) while butterfat exports plummeted 70%.
- International: Australian milk production is on its typical seasonal downward trend. Dry conditions in some areas have accelerated milk production declines in those regions. Current market outlooks estimate this season's production to be about equal to last year. Supplies of high quality hay are in short supply.
- International: The combination of low payout prices and hot, dry weather, which is limiting pasture growth, are bringing about accelerated declines in New Zealand's milk production. Manufacturers will be keeping a close eye on milk production declines and available supplies to ensure that future contract commitments can be met.
- International: Current Oceania cheddar supplies are filling contract commitments. A majority of supplies for some cheddar manufacturers are committed through Q1. There is increased competition coming from Europe and the U.S. Demand for cheddar in Asia is active.

**What's Bearish:**

- Cash Market: While spot cheese prices made small gains, Grade A NDM lost 1¼¢ for the week to settle at \$0.98½/lb on 3 trades, while butter gave up 1¼¢ to close at \$1.54 on 5 trades.
- Dairy Products Report: American cheese output in Nov was up 4.5% vs. a year ago, while total cheese output increased 2.9%. However, butter production decreased 4.7% from last Nov '13.
- Dairy cow slaughter for the week ended 12/27 totaled 42,400 head, down 3,200 head (7%) from a year ago.
- Fluid Milk Central: Milk supplies remain abundant with milk spot loads ranging from \$12 under to \$2.00 under Class. Most condensed skim volumes are exchanging hands with discounts. Class II sales on items such as yogurt and sour cream are slow. Cream is plentiful with most interest coming from butter churn operators.
- Fluid Milk Southwest: AZ milk production is steady to marginally higher. Plant operators are managing the intakes, but some delays in unloading are occurring from time to time. Milk production in NM is steady. Processing plant operators are putting in long hours to keep equipment running during a spate of low temperatures. Cream is readily clearing into churns this week as sales into holiday-related products are lower. Ice cream plants also took in some cream to start production of the favorite flavors. Demand from aerated cream and sour cream producers is lower.
- Fluid Milk Pacific Northwest: Milk production in the region is still showing higher than normal volumes. Some manufacturers are reporting a 4% increase in fluid milk intake over this time last year. Weather conditions are not causing any difficulties in either moving milk or stressing of dairy cows. UT and ID milk production is mostly steady to increasing slightly. Processing capacity in the region is almost at full capacity with current production levels. Manufacturers state they are using milk supplies on hand or taking contract loads but they do not have capacity for any extra.
- Butter: Production is exceeding incoming orders, resulting in inventories to moderately grow. Demand for bulk butter is reduced as prices range from market to 6¢ over the market. Export orders are light, while imports continue to come in to the U.S.
- Dry Whey Northeast: Prices are steady to lower this week as the market undertone continues to soften. Cheese production is robust, increasing liquid whey volumes clearing to the dryers. Inventories are sufficient for contract needs with available stocks on-hand for spot market transactions. The market is fairly quiet as a majority of buyers utilize a wait-and-see approach.
- Dry Whey Central: Prices are mostly lower on moderate spot activity. Some buyers were able to secure heavily discounted loads in the spot market. New contracts are generally steady to lower with reduced volumes being committed. The market tone is softening. End users note

supplies are becoming more available. Some purchasers are working current inventories lower, prior to taking a new position. Production rates are steady to higher following strong cheese production. Supplies are steady to growing.

- Dry Whey West: Prices are weaker. Demand is decreasing although product still seems to be moving. Export demand is steady.
- NDM: Buyers are delaying or choosing not to renew contracts. The market tone is weak. Production remains strong, with some manufacturers running full schedules with heavy incoming milk. Buyer interest domestically is light to moderate as buyers are mainly bargain shopping. Export orders are limited. Supplies are steady to growing.
- Cheese: Throughout the country more milk is flowing toward cheese plants than most people would have expected for the first full week of January, based on looking at this period in recent prior years. Many plants are producing cheese well ahead of orders. There is uncertainty about cheese prices in coming weeks and months, due to the new reality of milk supplies and production levels as well as the difficulty of exporting cheese considering global pricing and currency factors. In fact, increased cheese imports are challenging domestic cheese production. According to GTIS, European cheese exports for October to the U.S. were 25% higher than year ago levels. Discounted milk continues to be available this week. In some parts of the Midwest, spot milk has moved to cheese plants at \$6.00 to \$6.50 below Class, depending on location and timing. Sales are mixed, with some plants moving increased product along but others report some diminished buyer interest attributed to adopting more hand to mouth patterns hoping for further price weakness. This leads some plants to sustain building inventory levels beyond preferences.
- International: Western European milk production is increasing and remains above year ago levels. Lower dairy commodity prices are foretelling additional declines in future farmgate price adjustments. Producers over quota are putting on the milk production brakes to avoid paying super levees, while lower producing milk cows are being culled at an increasing rate. However, weather conditions are not seen as restricting milk production and butter and skim milk powder lines are seeing expanding production schedules. Milk production in Eastern Europe is increasing and above year ago levels. Loads of milk and cream going into Belarus have been restricted, and as a result, various commodity supplies have increased and are readily available for export.

#### **Recommendation:**

New week, same story. Spot cheese up slightly, Class III rallies mid-week, then sells off. No one knows why spot cheese prices keep inching higher, but apparently no one believes it either. Word we're hearing is that there is plenty of cheese available. Maybe it's going in to aging programs for now, but we believe it's only a matter of time until spot cheese heads lower. Current spot prices work out to about \$16 Class III, but that's using the Jan dry whey price. Fast forward to May dry whey and Class III falls to about \$14.75, and that's assuming current cheese prices hold where they're at. With May Class III settling at \$14.52 today, it's obvious the market thinks there's even more room to head lower. Drop both blocks and barrels a dime from current spot prices and May Class III heads to about \$13.75. As we hinted last week, even that might not be the bottom. There are some bright spots, however. Producers in the EU are beginning to pull back on production, as lower pay prices have already arrived there. And parts of Oceania are dry. There are still lots of unknowns that could move the market, but it still looks like supply will overwhelm demand over the coming months. Hedgers should still sell rallies Feb-Jun.

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 2015 - KDM Trading, Inc. All Rights Reserved – www.kdmtrading.com