

The KDM Dairy Report – April 24th, 2015

What's Bullish:

- Spot Market: Butter gained 2¢ on just 3 trades to close the week at \$1.85/lb and Grade A NDM inched $\frac{3}{4}$ ¢ higher to 93 $\frac{3}{4}$ ¢/lb without a trade. Block cheese was steady at \$1.61/lb on just 4 trades, while barrels were down $\frac{1}{4}$ ¢ to \$1.61 $\frac{3}{4}$ /lb on no trades.
- Ag Prices Report: The milk-feed ratio for March came in at 2.00, down from 2.02 in Feb and the lowest ratio since Sep 2013. Despite lower feed costs, more rapidly deteriorating milk prices are to blame.
- Fluid Milk West: Milk production in California is steady to marginally lower. The relocation of a few dairy operations caused some seesawing of milk intakes at a few plants. Water availability is still a

Futures Month	Class III 05/01	Class III 04/24	Change	Dry Whey 05/01	Dry Whey 04/24	Change	Cheese 05/01	Cheese 04/24	Change
May-15	\$16.26	\$16.60	(\$0.34)	45.350¢	45.075¢	0.27¢	\$1.657	\$1.694	(\$0.037)
Jun-15	\$16.45	\$16.97	(\$0.52)	44.000¢	43.000¢	1.00¢	\$1.683	\$1.744	(\$0.061)
Jul-15	\$16.53	\$17.23	(\$0.70)	42.025¢	42.250¢	(0.23¢)	\$1.704	\$1.776	(\$0.072)
Aug-15	\$16.82	\$17.41	(\$0.59)	41.500¢	41.500¢	0.00¢	\$1.738	\$1.794	(\$0.056)
Sep-15	\$17.19	\$17.39	(\$0.20)	40.500¢	40.475¢	0.02¢	\$1.780	\$1.803	(\$0.023)
Oct-15	\$17.36	\$17.35	\$0.01	39.825¢	40.500¢	(0.67¢)	\$1.805	\$1.805	\$0.000
Nov-15	\$17.38	\$17.35	\$0.03	40.050¢	40.000¢	0.05¢	\$1.805	\$1.799	\$0.006
Dec-15	\$17.35	\$17.26	\$0.09	39.800¢	39.500¢	0.30¢	\$1.802	\$1.798	\$0.004
Jan-16	\$16.96	\$16.90	\$0.06	40.500¢	40.250¢	0.25¢	\$1.763	\$1.760	\$0.003
Feb-16	\$16.95	\$16.87	\$0.08	41.000¢	40.900¢	0.10¢	\$1.762	\$1.755	\$0.007
Mar-16	\$16.83	\$16.81	\$0.02	41.000¢	41.000¢	0.00¢	\$1.748	\$1.745	\$0.003
Apr-16	\$16.68	\$16.65	\$0.03	41.000¢	41.000¢	0.00¢	\$1.741	\$1.741	\$0.000
12 Mo Avg	\$16.90	\$17.07	(\$0.17)	41.379¢	41.288¢	0.09¢	\$1.749	\$1.768	(\$0.019)

- concern as the growing season advances. Retail orders for bottled milk are steady. Arizona dairy operators note milk production has plateaued. Components are steady to declining as daytime temperatures increase. This week's forecast shows 100 degrees as the daytime high for the areas around Phoenix and Yuma. New Mexico dairy processors note volumes hauled into processing plants eked out another increase this week. However, they predict the peak of the flush is nearing as the week over week increases are declining. There are some shortages of forages. Sales into Class I are steady to slightly higher. Cream sales in the Western region are active. A few butter manufacturers continue to actively buy weekly cream loads available via resellers and dairy plant operators. Ice cream/frozen dessert producers' demand for cream has ticked up slightly as warmer weather arrives in the Western states. Buyers are learning they have to respond quickly to f.o.b. and broker-based spot offers because cream demand is firm.
- Butter: Production is steady to active throughout the regions. Demand remains stronger than expected. Some producers are trying to build inventories but are having difficulties doing that while meeting current demand. Spot availability of cream is increasing but ice cream manufacturers are pulling heavily. Some butter producers are selling extra cream while others are buying from other states to support current production.
- Cheese West: Most cheese plants in the region have active schedules and there is good demand for the output. Customers are still buying good volumes of cheese. Sales are strong and that is enough to keep production schedules active. Recent demand spikes for barrels were taken as typical by some manufacturers who cite building inventories for the grilling season as a factor in higher seasonal demand for process cheese, made primarily from barrel cheese.
- International: Western European milk production is increasing seasonally, but reportedly below year ago levels. Milk delivery data for the first two months of 2015 shows a decline from year ago levels. Milk production growth in April following the end of quota system has been below the expectations of many in the dairy industry. Dairy product production schedules are mixed with cheese and whole milk powder production restricted, while production of butter and skim milk powder has only marginally increased.
- International: A growing number of analysts think dairy prices will start to trend higher later this year. Current low prices are not encouraging expansion, while demand from China is expected to return after their stocks decline.

What's Bearish:

- Butter and cheese stocks continue to build at USDA-selected storage centers. Through 04/27, butter stocks have increased 2.8 million lbs (27%), while cheese stocks are up 3.7 million lbs (4%).
- Fluid Milk East: The capacity to handle projected milk supply volumes, generated from the flush, is a subject of interest for most plant managers in the East. As it now stands, Class I demand is becoming progressively weaker, and adding to those volumes, as schools draw nearer to the end of the semester. Milk production in the Northeast and Mid-Atlantic is moving up seasonally. Balancing plants are receiving heavy milk volumes and working actively to clear intakes. Contacts point to lots of milk in the Southeast region. Manufacturing plants are nearing capacity levels. Farm-level production in Florida is showing a slight uptick. This week, exports moved lower with 80 spot milk shipments, but that is expected to increase next week. Heavy cream supplies are advancing butter production.
- Fluid Milk Central: The warmer weather in the Midwest is aiding in milk production. Some processors' intakes are 3 to 4% above year ago levels. Retail promotions are down and spot loads are available and selling at \$1 to \$2 under Class. Bottling demand is light. Cream supplies are available, even with ice cream manufacturers pulling heavily.
- Fluid Milk Pacific Northwest: Milk production is increasing as expected for this time of year. Weather is good for cows and crops, with daytime highs in the 70's and down to the 50's at night in much of the region. Milk is moving smoothly. Corn planting is underway with good progress being made, especially in Washington. Idaho and Utah milk production is also increasing as expected. The volumes of milk keep manufacturing plants operating with busier schedules. Alfalfa growth is looking good and corn planting is underway. Rain occurring in Utah this week is welcome to help crop progress.
- NDM: Manufacturers continue to dry around heavy scheduling in the Northeast. Producers' stocks are heavy in most instances, while suggesting a buyer's market. In the Central region, growth in current milk supplies is keeping nonfat dry milk production strong. Inventories are building as buyers are taking a wait-and-see approach, purchasing only for current needs. Domestic and international demand is weak as buyers are looking for optimum pricing levels, even from international suppliers or other protein sources. Production of low/medium heat NDM is very active throughout the West. Inventories vary from comfortable to heavier than needed/wanted.

- Cheese Northeast: Production is steady to increasing. A few regional cheese plants are taking advantage of discounted condensed skim offerings to increase yields. Domestic demand is fair. Orders are declining, which is typical, in advance of the current school term winding up at educational institutions.
- Cheese Midwest: Most cheese plants in the region remain busy, pushed along by the higher volumes of milk being produced. The volume of plant production for several weeks is taking a personnel toll, leaving some cheese facility staff feeling "exhausted". Some extra barrel production is occurring, but less so than last week, because customers are increasingly stocked to suit their needs. Interest in Cheddar remains strong, but Italian varieties, while still receiving good demand, are closer to a desired balance.
- International: Whole milk powder imports to China in March were just a third of the volume they imported last year, according to recently released data. Skim milk powder imports fell as well, but not to the same level. Q1 imports of SMP dropped 38% vs. last year.
- International: Australian milk production is showing some increases, due to favorable weather conditions. Trading activity for most dairy commodities has slowed. Demand for dairy commodities has declined as many buyers have recently made purchases and have their near term needs covered. There is a building consensus among dairy analysts that dairy commodity markets are at or near the low point, but it will take a considerable amount of time for prices to substantially recover. Dairy Australia reports that March 2015 milk production in Australia was 4.9% above March 2014. Beneficial rains have covered major portions of New Zealand over the past few weeks. Milk production continues to decline in New Zealand, but the close of the season will not be as quick as once thought as the recent rains have prompted some producers to extend the milking season a bit longer.

Recommendation:

Cheese demand continues to hold prices in a steady spot market. The annual ADPI conference likely kept some market players away this week as we saw just 4 block cheese trades and 3 butter trades all week. From talk we heard from those at the conference, there are folks in both the bull and bear camps. Butter continues to be firm as California is now past the peak and they account for 30%+ of the butter made in the U.S. On the opposite coast, we appear to be awash with milk while balancing plants are getting pushed to capacity. Cheese seems to be a little looser there as well. The upper-Midwest is dry. We heard accounts this week of large-scale alfalfa loss/reseeding efforts in some areas. On the international side, the lack of quotas in the EU has not resulted in the type of production increases yet that many had expected. And there was some encouraging news that China may be back as a buyer later this year, once their stocks run lower. The front months in Class III gave up much of their gains from the prior week; perhaps in anticipation of a drop in spot prices. That didn't happen this week, but with everyone back from ADPI, next week might get interesting. Hedgers should get Jun-Aug covered as they are the most vulnerable to fall in spot prices. Further out we're more optimistic. Basic PUT option coverage at the \$15.25 level for Sep-Nov averages just 24¢/mo. That's not a great floor, but it's cheap and covers a disaster situation. For those getting upwards of \$2/cwt component pay, it may even cash-flow your operation should it come to that.

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