

**The KDM Dairy Report – May 22<sup>nd</sup>, 2015**

**What's Bullish:**

- Livestock Slaughter Report: 242,800 dairy cows were removed from the herd in April, up 5.7% vs. last April.
- Dairy cow slaughter for the week ending 05/09 totaled 51,600 head, up 5.7% vs. the same period a year ago. YTD the dairy cull is up 3.5%.
- Weekly Cold Storage: Cheese stocks at USDA-selected storage centers fell 1%, or 1.3 million lbs, through the first 18 days of May.
- Fluid Milk Southwest: CA producers indicate a decline in milk production due to poor feed quality. Class I demand is mixed. Finding trucking to haul milk from

Futures Month	Class III 05/22	Class III 05/15	Change	Dry Whey 05/22	Dry Whey 05/15	Change	Cheese 05/22	Cheese 05/15	Change
May-15	\$16.22	\$16.21	\$0.01	45.000c	44.225c	0.77c	\$1.656	\$1.656	\$0.000
Jun-15	\$16.47	\$16.57	(\$0.10)	43.950c	42.800c	1.15c	\$1.688	\$1.695	(\$0.007)
Jul-15	\$16.65	\$16.70	(\$0.05)	41.400c	41.000c	0.40c	\$1.713	\$1.725	(\$0.012)
Aug-15	\$16.89	\$17.04	(\$0.15)	41.000c	40.700c	0.30c	\$1.740	\$1.758	(\$0.018)
Sep-15	\$17.25	\$17.39	(\$0.14)	40.000c	39.750c	0.25c	\$1.787	\$1.800	(\$0.013)
Oct-15	\$17.32	\$17.48	(\$0.16)	40.000c	39.525c	0.48c	\$1.796	\$1.819	(\$0.023)
Nov-15	\$17.26	\$17.38	(\$0.12)	39.750c	39.750c	0.00c	\$1.795	\$1.808	(\$0.013)
Dec-15	\$17.20	\$17.24	(\$0.04)	39.750c	39.500c	0.25c	\$1.789	\$1.790	(\$0.001)
Jan-16	\$16.91	\$16.93	(\$0.02)	39.000c	40.000c	(1.00c)	\$1.760	\$1.764	(\$0.004)
Feb-16	\$16.79	\$16.90	(\$0.11)	40.250c	40.900c	(0.65c)	\$1.755	\$1.760	(\$0.005)
Mar-16	\$16.93	\$16.90	\$0.03	40.500c	40.800c	(0.30c)	\$1.755	\$1.761	(\$0.006)
Apr-16	\$16.91	\$16.90	\$0.01	40.700c	40.800c	(0.10c)	\$1.753	\$1.750	\$0.003
<b>12 Mo Avg</b>	<b>\$16.90</b>	<b>\$16.97</b>	<b>(\$0.07)</b>	<b>40.942c</b>	<b>40.813c</b>	<b>0.13c</b>	<b>\$1.749</b>	<b>\$1.757</b>	<b>(\$0.008)</b>

plant to plant continues to be an issue. AZ milk production continues to decline as the weather is warmer. NM milk intakes are slightly lower this week, but are expected to increase next week. There has been no out of state spot cream coming into California. Manufacturers are using available cream for a variety of products. Cream supplies are flat to slightly down.

- Butter Central: Most butter producers are at full capacity, but demand is still strong. Some contacts suggest that this is because bakeries and other end users are going back to using butter instead of other fat sources. Inventories are low and some manufacturers are content with that as they are selling this week what they anticipate they will make next week in order to keep butter moving.
- Butter West: Production appears to have slowed somewhat this week. Some manufacturers expressed a willingness to increase their cream sales as opposed to making more butter to add to inventories. Other butter manufacturers suggest the competition from ice cream producers for available cream have caused them to reduce their butter output.
- NDM West: Prices are steady to lower this week, but there were reports of some increased buying where prices were at discounted levels. Export sales are steady. Inventory levels are mixed as some producers are concerned about the decline in milk supply.
- CWT accepted 6 requests for export assistance to sell 692,252 pounds of Cheddar, and Gouda cheese, and 330,693 pounds of butter to customers in Asia, the Middle East, and South America. The product has been contracted for delivery in the period from May through November 2015.

**What's Bearish:**

- Spot Market: Butter finished the week down 8¼c to settle at \$1.89/lb on 13 trades, but Grade A NDM managed a ¼c increase to close at 90c/lb on 5 trades. Block cheese picked up 3c to settle at \$1.65/lb on 13 trades, but barrels were down ¼c to \$1.62/lb on heavy trading of 19 loads.
- Milk Production Report: U.S. milk output in April increased 1.7% compared to last April, which was on the upper end of analyst expectations. In addition, cow numbers grew month-to-month by 1,000 head and milk per cow jumped 19 lbs over a year ago. Production declined in the West, with CA down 2.1% and NW down 1.4%, but was strong in the Midwest, with SD up 9.8%, MI up 6.5% and WI up 4.0%.
- Cold Storage Report: Butter stocks in April were 23% higher than a year ago and 25% higher than in March, according to USDA. American cheese stocks were down 1% vs. last year, but Total cheese holdings were 4% higher than April '14.
- Weekly Cold Storage: Butter stocks at USDA-selected storage centers increased 23%, or 4.4 million lbs, through the first 18 days of May.
- Fluid Milk Northeast: Milk volumes are at/near peak levels leading into the Memorial Holiday weekend. Manufacturers and milk handlers are experiencing significant challenges, with the capacity to process those loads at the forefront of concerns. Driver availability is limited, and milk tankers are delayed for hours unloading in some instances. Northeast and Mid-Atlantic balancing plants are operating at full capacity. Class I demand is steady to lower with school closings still in process.
- Fluid Milk Southeast: Manufacturing plants are busy as seasonally heavy milk volumes peak. Bottling plants decreased their orders with dips in Class I demand. Milk exports totaled 10 spot loads compared to 4 the previous week. Florida's milk production is steady. Temperatures vary between the high 80s to low 90s, with humidity on the rise. Class I sales are steady but a downturn can be expected as remaining schools close. Milk export shipments totaled 120 spot loads, 15 more than the previous week. Cream is readily available. Ice cream demand, although good, is expected to see a slight downturn over the course of the Memorial Holiday. Condensed skim supplies are considered somewhat burdensome, as they look for homes for surplus loads.
- Fluid Milk Central: Milk production in the region is up as the spring flush is in full swing. Sources report that some milk is being put on the ground. Current spot sales are at \$2 to \$5 under Class, with some reports showing as much as \$8 under. This may continue to go lower as the holiday approaches and plants want to find a home for excess milk. Bottling demand is slowing as more educational institutions let out for summer. Cream supplies are plentiful.
- Fluid Milk Pacific Northwest: Milk production is beginning to plateau, but manufacturers and bottlers continue to report adequate milk intakes to meet production needs. The upcoming holiday weekend and end of school terms are expected to also increase milk available to processing in the near future. Currently, there have not been any indications of weather or feed issues impacting milk production. ID and UT milk is still readily available. Recent rains have helped improve the water levels stored in area reservoirs.
- Butter Northeast: An overall rise in churning is lending to moderate to heavy butter output. Active butter production will continue through the Memorial Day weekend for butter operations, as ice cream plant closings add to available cream supplies. Holdings of both salted and unsalted butter are building incrementally. Demand is light to moderate.

- Dry Whey Northeast: Prices are lower due to declines in spot prices and various indices. Dry whey production parallels regional heavy cheese output. Export sales are sluggish, prompted by competitive international pricing. The market undertone is weak. The Foreign Agricultural Service (FAS), reports that March 2015 U.S. dry whey exports totaled 39.0 million pounds, a 24% decrease from a year ago.
- Dry Whey Central: Prices were mainly lower this week. Whey production is steady as contract orders are being fulfilled. There have been several spot offers, but few spot sales this week.
- Dry Whey West: Prices were steady to lower this week. Industry contacts note that although food grade whey may be tight in some locations, product is generally available and a few spot sales have been made. Buyer interest remains subdued in making purchases and is focused mostly on filling immediate needs. There is a generally bearish view of market prices and without renewed buyer activity, no impetus for the market to strengthen in the near future.
- NDM East: Prices are lower for the mostly series. Regional drying operations are handling heavier condensed skim volumes, leading to increased production of low heat nonfat dry milk. With increases in production, inventories are growing steadily. Buyers are continuing to defer purchases around their immediate needs, in anticipation of a softer market as milk supplies increase.
- NDM Central: Production remains active as manufacturers are choosing to make NDM over other dry products. Inventory levels are high.
- Cheese Northeast: Cheese production is mostly steady as seasonal milk output inches closer to peak levels. Inventories, particularly aged cheddar, continue to build. Cheese sales are active in retail and food service markets as the upcoming Memorial Day weekend encourages interest, but demand for spot loads of cheese is fair.
- Cheese Midwest: Milk volumes being utilized by many Midwest cheese plants this week have reached all time high levels for this year, even up from recent weeks which have had high volumes. The volume of milk reaching cheese plants has resulted some running 7 days a week every other week to keep up with contracted orders, with existing sales contracts extending weeks into the future. There is a feeling among workers at some plants of "hanging on", striving to simply cope with the relentless pressure of high daily milk intakes and keep going until the flush begins to fade away, the flood of milk slows, and schedules can be eased. Many plants will be in operation on Memorial Day. There are plants with enough milk availability and buyer interest that production schedules could be set for 7 days a week, but they only run six days because not enough workers are available to staff a 7 day operation. Cheese sales are good all over the region and that applies to the range of varieties offered by plants. No indication was heard of plants facing difficulties in finding buyers for the volumes of cheese being manufactured. Memorial Day often marks the approximate point where increasing milk production slows, before beginning to decline. So far this week, there is no sign that the tide has turned yet. Surplus milk is being shopped around at prices reaching \$4.00 below Class midweek and \$5.00 below Class over the holiday weekend. Surplus milk is already being shopped for delivery in June, also \$5.00 under Class for multiple loads. Some of the surplus milk volumes are resulting not only from the flush, but from the ending of school year fluid milk contracts, which then leaves processors with that milk to find other customers for. This phenomenon may counterbalance the impact on cheese plant milk availability of any decline in milk production in coming weeks, if the flush begins to recede then. With many cheese plants already having very full schedules, sellers typically have to work to find a plant with capacity to absorb surplus milk. In part of the region, surplus milk is reportedly being dumped because no buyers can be found. There are indications that the recent heavy demand for cheese barrels has eased, with large orders driving the demand being close to being filled.
- Cheese West: Ample milk production has been driving steady cheese output in the West. There appears to be firm contract sales. However, some industry participants note an increasing desire by manufacturers to offer spot loads of cheese, possibly to keep inventories in check. Completed spot transactions have been limited as buyers focus on immediate needs and hold some expectation that prices may soften slightly.
- International: This week's Global Dairy Trade auction resulted in a 2.2% decline in the dairy price index. It was the fifth straight month of declines. Cheddar cheese fell 7.1% to a U.S.-equivalent \$1.25/lb.
- International: Australian milk production in April was up 2.9% vs. a year ago, according to Dairy Australia. YTD, (July-April) production is also 2.9% higher than the previous milking season. Cheddar cheese output in March was 14.4% higher than a year ago and up 15.1% YTD.

#### Recommendation:

About the only thing positive in the current market are strong sales. It appears we could literally double the amount of milk in the country but really can't make any more cheese than we already are. Cheese plants everywhere are running all out, to the extent that works are getting tired and worn out by the frantic pace of having to handle the milk inflow and turn it in to something. But on the other hand, they're selling about everything they can make, with some being sold out months in advance. The million dollar question is where is all this cheese going? If it is being eaten by the public, that is genuinely impressive. But if it is fall demand being brought forward by buyers to ensure a stable supply, we could be in for a demand lull. We're starting to hear about some warehouses finally getting full, and this week's Dairy Market News highlighted the fact that barrel demand is starting to slow a bit. The spot market bears this out as trade volume in both blocks and barrels were higher than in several weeks. Both block and barrel cheese supplies appear to be loosening up. We think it means there is limited upside in cheese prices from here, with stronger odds that we even start to see a little pressure going forward. With current strong demand, however, we don't see a collapse either. That said, June Class III already has one week priced in at around \$16, with a short week next week due to the Memorial Day holiday on Monday. Many cheese plants usually take this day off to perform maintenance and give workers a break, but not this year. Most will still be running at full capacity in order to keep their milk silos under control. That means more cheese is likely to show up in the spot market. With a settlement of \$16.47, we still think June Class III is a sale at current prices, and certainly any rally. The milk supply glut is not likely to be abated by July either, so rallies in that month should be sold as well. Or, buy PUT options to get a floor price established. Beyond July/Aug we're not too keen on hedgers taking overly large positions. Milk production in CA is struggling, while international markets are starting to carve out a bottom. A natural event like heat/drought could be very supportive, and if the apparently insatiable appetite for cheese in the U.S. does not let up, we may not have a lot of excess cheese in the fall.

**NOTE:** KDM Trading will be closed on Monday in observance of Memorial Day. Thank a service man or woman for your freedom!

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