

The KDM Dairy Report – October 9th, 2015

What's Bullish:

- Dairy cow slaughter was strong for second week in a row. 58,800 dairy cows were culled during the week ended 9/26, up 6.1% vs. the same period a year ago.
- Fluid Milk Southeast: Milk production volumes are unchanged, but bottling plants continue to increase orders, leaving fewer loads to manufacturing. Florida's milk production continues a slight downslide and bottling sales are steady. Imports milk shipments are unchanged at 220 spot loads.
- Fluid Milk Central: Milk production has slowed seasonally. Processors are comfortable at current levels, but components are dropping. Cream is available, though as ice cream demand has tapered, other cream-based products have seen strong demand.

Futures Month	Class III 10/09	Class III 10/02	Change	Dry Whey 10/09	Dry Whey 10/02	Change	Cheese 10/09	Cheese 10/02	Change
Oct-15	\$15.79	\$15.69	\$0.10	26.125¢	24.600¢	1.53¢	\$1.693	\$1.685	\$0.008
Nov-15	\$15.83	\$15.63	\$0.20	28.025¢	26.700¢	1.33¢	\$1.705	\$1.695	\$0.010
Dec-15	\$15.93	\$15.69	\$0.24	31.700¢	29.850¢	1.85¢	\$1.705	\$1.690	\$0.015
Jan-16	\$15.98	\$15.72	\$0.26	34.000¢	32.000¢	2.00¢	\$1.700	\$1.682	\$0.018
Feb-16	\$16.07	\$15.77	\$0.30	34.500¢	32.650¢	1.85¢	\$1.695	\$1.682	\$0.013
Mar-16	\$16.19	\$15.88	\$0.31	34.300¢	32.925¢	1.38¢	\$1.709	\$1.700	\$0.009
Apr-16	\$16.19	\$16.01	\$0.18	35.750¢	32.525¢	3.23¢	\$1.719	\$1.705	\$0.014
May-16	\$16.29	\$16.15	\$0.14	36.500¢	33.050¢	3.45¢	\$1.722	\$1.711	\$0.011
Jun-16	\$16.49	\$16.35	\$0.14	36.000¢	33.775¢	2.23¢	\$1.741	\$1.740	\$0.001
Jul-16	\$16.75	\$16.50	\$0.25	35.750¢	32.500¢	3.25¢	\$1.761	\$1.760	\$0.001
Aug-16	\$16.81	\$16.60	\$0.21	35.750¢	33.350¢	2.40¢	\$1.776	\$1.760	\$0.016
Sep-16	\$16.80	\$16.51	\$0.29	36.125¢	34.000¢	2.13¢	\$1.775	\$1.756	\$0.019
12 Mo Avg	\$16.26	\$16.04	\$0.22	33.710¢	31.494¢	2.22¢	\$1.725	\$1.714	\$0.011

- Fluid Milk Southwest: Milk output is lower in California. A raise in humidity in the Central Valley is adversely affecting the milk yield. The interest of NDM processors for condensed skim is increasing. Harvesting of alfalfa hay and corn for silage is limited due to severe shortage of water. Thus, some dairy operators are buying these feeding crops from out of the State. A combination of heavy rains and high humidity is decreasing the milk production in Arizona. Sales of spot condensed skim loads to Class IV products manufacturers are higher. Milk output is steady to lower in New Mexico. Wet conditions associated with scattered thunderstorms are taking a toll on the milking cows' comfort. Class I sales to the retail and food service sectors are steady to higher.
- Fluid Milk Pacific Northwest: Pacific Northwest milk production is steady to lower. Processors report milk supplies are adequate to meet most processing needs. The lighter milk intakes make it possible for manufacturers to schedule maintenance. Utah and Idaho milk production is following a typical seasonal decline.
- Butter: Prices have moderated this week after reaching a record high two weeks ago, and seeing sharp declines last week. Churning is active for those butter operations looking to take advantage of good demand at current prices. Most manufacturers seem fairly satisfied with current stock balances. Bulk butter pricing is 4 to 6 over the market in the East, 2 under to 7 over in the Central, and 4 under to 3 over in the West. Stronger butter sales are noted.
- Dry Whey West: Some manufacturers note a surge in buyer interest. Inquiries have increased as buyers seek to replenish their stocks and capitalize on low prices. Although most industry contacts suggest there is plenty of product available, a few contacts are reporting tighter or committed stocks at their facilities. Whey production is steady to lower as cheese production slows seasonally.
- Dry Whey Northeast: Overall, demand is strong in the region. However, as the region experiences seasonal declines in cheese output, some whey channels are seemingly tight on product. Some market participants expect prices to rise, with the suggestion that sellers are confident with current stocks levels.
- NDM East: Prices for low/medium nonfat dry milk climbed higher in a firming market. This week, nonfat dry milk production dropped slightly. Extreme weather conditions in the region increased Class I demand. Processors in the region are comfortable with current NDM inventories, as diminishing milk supplies lead to reductions in low/medium heat drying schedules. Much of the current low heat nonfat dry milk is moving through sales contracts. Demand is good, with sources noting that buyers are showing active interest in securing product.
- NDM Central: Prices for Central low/medium heat nonfat dry milk are up in a mixed market. Contract negotiations for Q1 2016 are underway as most buyers and sellers understand that the prices are starting to stabilize.
- NDM West: Prices are higher on the range and the mostly series. Production is steady to higher, though inventories are mixed throughout the West. The market undertone is stronger.
- Cheese Northeast: Inventories are sufficient for near term needs. Supplies are being added to at some cheese operations, but demand is good for mozzarella, provolone and low fat cheddar. Advance cheese purchases for holiday needs are being evaluated against current price levels, as volatility grips the market.
- Cheese Midwest: Cheese production is easily accommodating regular milk supplies, with little availability of extra milk. Over the last month or so, American cheese sales have been quite strong and helped prevent recent increased American cheese production from leading to burdensome inventories. Strong but typical early fall demand for Mozzarella cheese has helped manufacturers move higher regional production out the door. Manufacturers in the U.S. note the narrower difference between U.S. cheese prices and GDT prices compared with earlier in the year, as easing the pressure from cheese imports. Cheese inventories are being held with confidence for sale in coming months.

What's Bearish:

- Spot Market: Barrels managed a ¼¢ gain to close the week at \$1.62/lb with 15 trades, but blocks were down 4¼¢ to settle at \$1.70/lb on no trades. Grade A NDM lost 6½¢ to close at \$0.99½/lb on 10 trades and butter shed 8¼¢ to settle at \$2.41¼/lb on 18 trades.
- Fluid Milk Northeast: Parts of the East coast were battered by rain and historic flooding. However, most milk delivery routes and milk receipt locations experienced minimum complications from the storm situation. Northeast and Mid-Atlantic milk production are flat. Class I sales are mostly steady to marginally higher, attributable to pulls from the Southeastern storm situation. Manufacturing milk supplies have declined slightly, but remain adequate for fulfilling contractual needs. Spot milk is in strong demand.

- Dry Whey Central: Buyers and seller note that there is plenty of product available. Demand is increasing but, some sellers believe that this level of demand will not last as end users are stocking up while prices remain low. Production is steady to lower. Manufacturers report having comfortable inventories.
- Cheese West: Output is steady to lower and following the typical seasonal declines in milk production. An increase in milk components is helping to boost cheese yields. Domestic demand continues to be strong, especially for natural cheese varieties. Cheese consumption in the U.S. has helped support prices while export opportunities have been limited. Manufacturers report cheese inventories in general are creeping up. Industry contacts note barrels are somewhat longer than blocks.

Recommendation:

Despite a lackluster performance in this week's spot market, Class III futures finished solidly higher. The idea that higher butter prices might be the new norm as well as the sense that both NDM and dry whey prices have already bottomed out and are now climbing has lent some support to the market. In addition, concerns over future milk production in 2016 due to very low milk prices in Oceania and the potential for a strong El Niño weather pattern may cause some commercial hedgers picking up the long hedge activity. Indeed, after bottoming at a low average price of \$15.84 on August 24th, it has climbed an impressive 57¢ to today's close of \$16.41. Recall that just last week we had proposed waiting for a \$16.50 average before hedging any of 2016, so we are getting very close to that target. Individual operations will need to determine if that is a smart level for them to begin their hedge program. Technically, with the momentum now behind the 2016 contracts, we wouldn't be surprised to see the average surpass that level, so be careful how many lbs you are marketing. We would keep it at 20% or under. Other than that it was a quiet week. Typical fall demand is holding cheese inventories in check, but there still appear to be extra barrels floating around the country. It's hard to say at this point when this market will have a breakout, one way or the other, as current fundamentals suggest support for powder, but resistance to higher cheese prices. Time will tell!

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