

**The KDM Dairy Report – May 27<sup>th</sup>, 2016**

**What's Bullish:**

- Spot Market: Blocks gained 6½¢ during the week to settle at \$1.38/lb, while barrels jumped 8½¢ to close at \$1.44/lb. Trading was active with 9 loads of blocks and 15 loads of barrels exchanging hands. Butter finished the week down ¼¢ to settle at \$2.06½/lb on 5 trades, while NDM gave up 2¢ to close at \$0.79½/lb on 25 trades.
- International: Western European milk production increases are up 5.4% Jan-Mar from year ago levels, a continuing outcome following the termination of quotas last year. However, supplies of cheese continue to tighten, primarily attribute to strong consumer demand.

Futures Month	Class III 05/27	Class III 05/20	Change	Dry Whey 05/27	Dry Whey 05/20	Change	Cheese 05/27	Cheese 05/20	Change
May-16	\$12.80	\$12.82	(\$0.02)	25.300¢	25.375¢	(0.07¢)	\$1.413	\$1.415	(\$0.002)
Jun-16	\$12.85	\$12.48	\$0.37	25.250¢	25.975¢	(0.73¢)	\$1.416	\$1.373	\$0.043
Jul-16	\$13.15	\$12.93	\$0.22	26.250¢	25.700¢	0.55¢	\$1.440	\$1.421	\$0.019
Aug-16	\$13.85	\$13.64	\$0.21	27.250¢	26.275¢	0.98¢	\$1.509	\$1.486	\$0.023
Sep-16	\$14.56	\$14.45	\$0.11	28.000¢	27.500¢	0.50¢	\$1.573	\$1.560	\$0.013
Oct-16	\$14.85	\$14.73	\$0.12	28.875¢	27.975¢	0.90¢	\$1.600	\$1.592	\$0.008
Nov-16	\$14.96	\$14.87	\$0.09	29.500¢	29.000¢	0.50¢	\$1.607	\$1.598	\$0.009
Dec-16	\$15.03	\$14.95	\$0.08	29.750¢	29.350¢	0.40¢	\$1.615	\$1.609	\$0.006
Jan-17	\$15.10	\$14.98	\$0.12	30.375¢	29.475¢	0.90¢	\$1.617	\$1.615	\$0.002
Feb-17	\$15.19	\$15.11	\$0.08	30.000¢	29.025¢	0.98¢	\$1.629	\$1.625	\$0.004
Mar-17	\$15.35	\$15.32	\$0.03	30.025¢	29.025¢	1.00¢	\$1.638	\$1.641	(\$0.003)
Apr-17	\$15.43	\$15.38	\$0.05	30.025¢	29.000¢	1.03¢	\$1.638	\$1.636	\$0.002
<b>12 Mo Avg</b>	<b>\$14.43</b>	<b>\$14.31</b>	<b>\$0.12</b>	<b>28.383¢</b>	<b>27.806¢</b>	<b>0.58¢</b>	<b>\$1.558</b>	<b>\$1.548</b>	<b>\$0.010</b>

- Demand for both packaged and bulk butter has been strong. Recent weaker dairy product prices have been cited as a significant factor in keeping the consumer price index in Germany negative as of the end of April.
- International: The dairy production season in Australia is nearing an end, and the feed supply in some areas of the country are becoming thin. Australia recently received widespread rainfall across southern regions, but the North continued drying. Producers in the North have had less need to purchase feed but if drying continues, affecting pastures, feed prices in the North may be increasing soon.
- Butter Central: Production is steady this week for many butter manufacturers. Retail and food service demand is consistent. Some sellers report increases in sales due to the upcoming holiday weekend. Cream remains plentiful and spot loads are readily available for any interested buyer. Several industry participants are capitalizing on low cream prices and making more butter than needed for the short term. Manufacturers are also microfixing bulk butter to prepare for upcoming contracts and Q3/Q4. Overall, butter stocks are building, but remain at comfortable levels as warmer months approach.
- Butter West: Contacts say they are closely monitoring their supplies and production in order to be in balance with late year butter needs. A few butter makers are purchasing extra loads of cream to run churns at full capacity. Cream is readily available and most processors can get what they need. Butter production remains active. Inventories, although higher than last year, are increasing along seasonal trends and do not seem to be a major concern to industry contacts. Manufacturers say domestic sales are good and butter is moving well through existing contracts.
- Dry Whey Northeast: Prices are higher as prices adjusted to f.o.b. spot sales and pricing indices. Surplus milk supplies are likely to move into cheese production, during the holiday weekend, leading to heavier dry whey processing, but negotiations for Q3 contracts are giving a steady to firm undertone to the market.
- Dry Whey Central: A few industry contacts feel whey prices are firming. Whey production is steady this week. Following a week of active trading, domestic whey sales slowed for some sellers, but several contacts report interest from international buyers. The majority of sales for these whey marketers are being exported.
- Dry Whey West: Prices are steady to higher this week. While domestic demand has been slow, a few manufacturers have been able to ease inventories slightly through large export sales.
- NDM Northeast: Prices advanced incrementally higher in the mostly price series on f.o.b. spot sales transactions. Over the holiday weekend, increased condensed skim supplies could drive low/medium heat nonfat dry milk production to capacity levels for regional dryer operations. As output expands, sources point out inventories are building; however, those volumes are needed for future contract commitments, as a few buyers hedge. Good sales activity over the past few weeks lowered uncommitted supplies available for cash sales. The export market is fair to steady. In general, the low/medium heat NDM market currently resonates a firm undertone.
- NDM West: Overall, the market undertone is firmer. Nevertheless, a few processors are clearing old inventories at lower prices, close to the bottom price of the range. Demands from bakers and dry mix manufacturers are good.
- Cheese: Inventories are long and cheese vats are full as manufacturers across the nation run at or near full schedules. However, sales are strong for many industry participants. A few Midwest suppliers experienced a slowdown in interest outside of contracts, but the holiday weekend sparked additional retail promotions, aiding sales. Several Northeast and Midwest contacts report an increase in demand for processed cheese. The international market's interest in U.S. cheese is growing.
- CWT has accepted 12 requests for export assistance to sell 2.776 million pounds (1,259 metric tons) of Cheddar, Gouda and Monterey Jack cheese; 771,618 pounds (350 metric tons) of butter and 88,185 pounds (40 metric tons) of whole milk powder to customers in Asia, the Middle East, Oceania, and South America. The product has been contracted for delivery in the period from May through November 2016.
- International: April milk production in Australia was down 2.7% vs. a year ago. YTD (July-Apr), output is now 1.2% below last season's levels.

**What's Bearish:**

- Cold Storage Report: American cheese stocks at the end of April were 15% higher than a year ago, and the highest April total for 30 years! Not to be outdone, total cheese stocks were up 12% vs. April '15, setting a new all-time high (going back to 1918!) for the month. Ouch. Butter stocks over the same period were up 28%.
- Weekly cold storage numbers are showing cheese stocks up 3% so far in May (through the 23<sup>rd</sup>) at USDA-selected storage centers. Butter holdings over the same period are up 5%.

- Fluid Milk Northeast: Farm milk output is on the rise and demand from all Classes is plummeting ahead of the Memorial Day holiday. The end of spring term at college campuses reduced bottling orders significantly. Manufacturing milk supplies are heavy. Plant managers anticipate capacity level intakes over the course of the holiday period.
- Fluid Milk Southeast: Milk production is steady on the down side of the seasonal peak. Fluid milk demand driven by foodservice needs declined due to school closings and the forthcoming holiday. Manufacturing milk supplies will be heavy into the weekend with all available auxiliary manufacturing facilities being utilized to handle additional milk volumes. Florida's farm milk production continues to decline. Also, fluid milk sales decreased this week with schools/universities closing for summer break. This week, export milk shipments for the state totaled 190 f.o.b. spot loads, 30 above the previous week.
- Fluid Milk Central: Temperatures are rising across the region, but farm level milk production continues to be strong. Many states in the Central region are at the peak of spring flush, reporting plentiful milk available on the spot market. The upcoming holiday weekend has milk processors working hard to make sure weekend milk intakes are processed. Spot loads are being reported at \$1.25-\$4.00 under class. However, spot loads for the end of the week and weekend are anticipated to move at larger discounts. Some manufacturers will continue to run full schedules through the holiday weekend to ensure all milk intakes are processed. Bottlers report slowing orders as education institutions close for the summer. Milk marketers noted lighter interest in bottling but stronger interest for Class II cream going into ice cream. Warming temperatures are spurring some climb in ice cream demand. However, this growth in interest is not large enough just yet to tighten cream supplies in the Midwest.
- Fluid Milk Southwest: Farm level milk production is flat, as the weather conditions remain unchanged from last week. Bottled milk orders from educational institutions are even. However, requests from retailers and food service are steady to lower as the Memorial Day holiday weekend approaches. In addition, some customers are replacing bottled milk consumption with popular summer drinks. Alfalfa hay harvesting is active throughout the state. In Arizona, cows' comfort is stable because the weather is cooler this week. Consequently, milk yields have plateaued after a six-week downward trend. Bottled milk orders from educational institutions are considerably lower as many K-12 schools are finishing this week. However, some Class I processors are pulling a little bit heavier volumes to fill new product lines. New Mexico milk output continues steady on the top of the seasonal peak. Butterfat components are steadily decreasing. Milk volumes are moderate to heavy, keeping many processing plant operators busy. Class I sales are lower as most educational institutions are closing this week.
- Fluid Milk Pacific Northwest: Pacific Northwest milk production has hit its high mark according to some processors. Milk is readily available for almost all processing needs. Bottling demand is following normal patterns for this time of year and is slowing as many schools close for summer breaks. Utah and Idaho dairy farms are supplying a steady supply of milk for processing. Industry contacts report there is little milk moving in to or out of the region. Many area processors are running fairly full production schedules and expect a small increase of milk available for processing over the holiday weekend and as schools close for the year.
- Butter Northeast: Heavy cream supplies continue to advance active butter churning at area operations. While the market notes good post-holiday sales, butter supplies in the bulk variety steadily builds. In some cases, manufacturers are quite content holding/storing bulk stocks, in lieu of selling, although purchase inquiries are frequent. Export demand is sluggish due to current U.S. butter prices exceeding global markets.
- NDM Central: Production is active in reaction to heavy farm milk intakes. Many industry participants have adequate supplies of nonfat dry milk. Few buyers are looking for NDM on the spot market. Therefore, minimal transactions were carried out this week outside of contracts. A few contacts noted that condensed skim is being offered at large discounts and some processors may turn to that in lieu of NDM.

#### Recommendation:

In the face of a very bearish cold storage report, the current glut of cheese in the U.S. is even catching some media attention, with TV coverage on Fox Business this week and the Wall Street Journal last week, among others. Some would say that by the time mainstream media decides to report about it, the market is about to turn. And wouldn't you know, spot cheese prices sported a respectable rally this week. We all know the bearish facts, so we won't rehash them. On the positive side, we're hearing cheese is getting a little tighter in the EU on strong demand, while the production season is ending in Oceania. Domestic demand remains strong, with hotter weather around the corner. Long-term weather experts predict a strong La Nina pattern developing, which would mean hot and dry in the grain belt, and also including the Midwestern milk shed. Just

look at what soybean meal prices have done in the last 30 days (see chart). \$400/ton protein and \$12 milk is not sustainable long term. Class III's, dry whey and cheese futures all saw decent rallies this week. While much of the industry is still convinced we will see no meaningful improvement in milk prices until 2017, we are more optimistic. We continue to recommend purchasing upside protection on existing contracts Aug-Dec. On a final note, the markets will be closed on Monday in observance of Memorial Day. Enjoy this special weekend, in particular, your freedom!



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