

The KDM Dairy Report – July 1st, 2016

What's Bullish:

- Spot Market: Blocks finished the week up 11¼¢ on 6 trades to settle at \$1.62½/lb. Barrels shot 13½¢ higher to \$1.67/lb with 28 loads exchanging hands. Grade A NDM gave up 6¼¢ to \$0.83½/lb on 36 trades, but butter managed to end the week ¼¢ higher to close at \$2.35/lb on 6 trades.
- Ag Prices Report: The milk-feed ratio for May was just 1.89, down from 1.97 in April and the lowest level since Sep 2013.
- Weekly cold storage numbers indicate cheese stocks at USDA-selected storage centers were drawn down by 5% (5.2 million lbs) over the period 06/01 through 06/27.

Futures Month	Class III 07/01	Class III 06/24	Change	Dry Whey 07/01	Dry Whey 06/24	Change	Cheese 07/01	Cheese 06/24	Change
Jul-16	\$15.07	\$14.84	\$0.23	27.850¢	27.725¢	0.13¢	\$1.621	\$1.598	\$0.023
Aug-16	\$15.89	\$15.91	(\$0.02)	29.975¢	29.975¢	0.00¢	\$1.687	\$1.693	(\$0.006)
Sep-16	\$16.04	\$16.34	(\$0.30)	31.500¢	30.700¢	0.80¢	\$1.706	\$1.729	(\$0.023)
Oct-16	\$16.13	\$16.34	(\$0.21)	32.350¢	32.000¢	0.35¢	\$1.705	\$1.721	(\$0.016)
Nov-16	\$16.11	\$16.18	(\$0.07)	33.350¢	32.000¢	1.35¢	\$1.694	\$1.703	(\$0.009)
Dec-16	\$15.89	\$15.93	(\$0.04)	33.925¢	33.875¢	0.05¢	\$1.675	\$1.699	(\$0.024)
Jan-17	\$15.82	\$15.90	(\$0.08)	34.575¢	32.900¢	1.68¢	\$1.666	\$1.678	(\$0.012)
Feb-17	\$15.83	\$15.95	(\$0.12)	35.350¢	34.000¢	1.35¢	\$1.670	\$1.696	(\$0.026)
Mar-17	\$15.93	\$15.95	(\$0.02)	35.500¢	34.450¢	1.05¢	\$1.682	\$1.692	(\$0.010)
Apr-17	\$16.03	\$16.18	(\$0.15)	35.550¢	35.200¢	0.35¢	\$1.682	\$1.704	(\$0.022)
May-17	\$16.22	\$16.20	\$0.02	36.775¢	35.000¢	1.78¢	\$1.695	\$1.710	(\$0.015)
Jun-17	\$16.31	\$16.30	\$0.01	37.000¢	35.000¢	2.00¢	\$1.711	\$1.725	(\$0.014)
12 Mo Avg	\$15.94	\$16.00	(\$0.06)	33.642¢	32.735¢	0.91¢	\$1.683	\$1.696	(\$0.013)

- Fluid Milk Southeast: It is hotter in the region, resulting in steady to lower milk output. Load rejections, due to temperature issues, continue to be a problem with transports out of the most southern areas of the region. Florida's milk output continues to plunge, as high temperatures and humidity reduce cow comfort. Contrariwise, fluid orders are increasing, as milk loads lighten at the farm. With the spike in Class I demand there is no clear picture as to the cause of increased interest. As such, 35 loads of milk were imported into the state this week, compared to 125 loads exported last week.
- Fluid Milk West: Warm temperatures in the California Central Valley reduced cow comfort and suppressed milk production. Although temperatures are expected to moderate a bit in the next few days, industry contacts do not expect the milk outputs to recover too much. Arizona milk production continues to drop as summer heat builds throughout the state. Bottling demand is relatively steady and local handlers are pulling more milk into ice cream and cheese production. New Mexico milk production continues to decline along seasonal patterns, though milk intakes are keeping balancing plants very busy. Class I sales are slightly higher, while Class II sales are lower. Milk shipped into Class III and Class IV are steady to slightly lower this week. Industry contacts report western cream is tightening slightly as milk production slows and milk components decline.
- Butter Northeast: Due to tighter cream supplies, the butter production rate in the region has fallen. In recent weeks, it has been advantageous for some butter manufacturers to price and sell available cream to Class II operations rather than churning butter. On the heels of the recent Cold Storage report, a few butter processors describe current inventory levels as suitable for anticipated contract needs. Retail and contract sales are steady to good. The bulk butter price is reported 5 to 8 over the market, based on the CME Group with various time frames and averages used.
- Butter Central: Some manufacturers are keeping churns running full schedules. Other butter plant managers are slowing down production. A few butter plants are reportedly shut down for maintenance this week. Demand for butter is high. However, many stockholders are choosing to hold on to their inventories, or have stocks that are already committed. Industry participants comment that retail outlets show more interest in planning ahead and are locking in prices. Some end users have reportedly set up contracts through the end of the year. This has several butter manufacturers packing ahead for the fall. Market participants speculate that a large portion of inventory in the Central region is committed print butter. Industry contacts comment that bulk butter is hard to come by in the Central region. Bulk butter prices reported ranged from market to 10 cents over the market, with various time frames and averages used. The market undertone is firm.
- Butter West: Cream supplies are tightening as ice cream manufacturers begin to use more cream. A few processors have slowed or suspended butter production, in favor of selling off some of the milkfat. Although butter inventories are high, and may build a little further, butter makers are comfortable with current butter holdings. Continued strong domestic demand, coupled with the slowdown in production, may soon help slow or reverse the growth of butter inventories.
- Dry Whey: While domestic demand remains mixed, international buyers continue to have a strong presence on the spot market. Several contacts mention that international outlets are inquiring about loads through the end of the summer months. Prices seem to be creeping up slowly, pushed along by the strengthening Southeast Asian demand for whey, whey permeate and other feedstocks, needed to rebuild their pork herd.
- NDM East: Prices for low/medium nonfat dry milk advanced across the pricing series. Sources suggest that prices are stronger than initially anticipated by the market. There are manufacturers that tend to resist lower priced bids as they feel the current heat wave in parts of the East will affect nonfat dry milk inventory levels in the near future. Stocks are building, but are not considered burdensome by producers. The export market is seeing good interest. The market undertone continues to firm.
- NDM Central: Prices in the region are higher this week, and stronger than anticipated. Milk intakes remain high and dryers are running near or at full schedules producing low/medium heat NDM. Inventories are generally long. However, current market prices are reportedly competitive in the international market and some manufacturers are exporting loads. A few market participants anticipate prices to climb higher. The market undertone is firming.
- NDM West: Prices are higher in a firming market. Domestic NDM markets, to some, are firmer than anticipated. Market sources note the perceptions that milk supplies are not strong currently influence the price of low/medium heat NDM. End user demand is moderate to good. The market undertone is steady to firm.
- Cheese Midwest: Milk intakes remain high, and plant managers report little change in milk components and yields. Some cheese manufacturers continue to run full schedules, testing their plants' capacities. However, demand from retail and foodservice are both strong. Buyers continue to inquire about additional loads of cheese outside of commitments. A few manufacturers of Italian varieties of cheese report sales into food service

approaching record highs. Cheese stocks are seeing relief as strong sales prevail. Manufacturers producing cheese varieties requiring little to no aging report light inventories.

- Cheese West: Cheese production remains full and active. A few cheese manufacturers, however, are looking for ways to reduce their cheese production in order to keep inventories from growing more. Inventories have grown to the point that some industry contacts say there are challenges in finding available warehouse space. However, cheese makers note retail sales remain strong. In addition, a few other manufacturers say they have seen good demand for their commodity type cheeses and have comfortable inventories besides. They say they are getting more inquiries from domestic and export buyers looking for fresh blocks and barrels to blend with their stocks, to meet customer requirements.

What's Bearish:

- Dairy cow slaughter for the week ending 06/18 totaled 49,800 head, down from 50,600 a year ago.
- Fluid Milk Northeast: East balancing plants are prepared for near capacity production with a surge in milk supplies, prompted by declines in Class I demand and various holiday related plant closures. In parts of the Northeast, milk production is seeing some increase. Mild temperatures encourage cow comfort. In general, Class I and III sales are down, while Class II sales are level. Mid-Atlantic farm milk output is steady to higher. Manufacturing milk supplies continue to be above year ago levels. Class I demand is near its seasonal low point as all schools have closed for summer break.
- Fluid milk Central: Several milk processors report noticeable decreases in milk intakes this week. However, industry contacts feel farm level milk production in the region continues to be strong. Spot loads are available and are reported at flat to \$3.00 under class. Market participants anticipate more cream spot load availability at the end of the week with the upcoming holiday weekend. Overall, industry contacts report more readily available cream this week when compared to last. Ice cream and frozen dessert manufacturers are capitalizing on cream availability and report running full schedules. Cream multiples are lower this week.
- Fluid Milk Pacific Northwest: Milk intakes are relatively steady and manufacturers report no issues getting milk for processing runs. Some milk handlers are juggling a few loads in advance of the holiday weekend. Milk production in the mountain states of Idaho, Utah and Colorado is fairly stable. A few manufacturers report getting regular offers for some excess milk floating around the region. A few processors have started trying to push some of the extra milk off to other manufacturers within the region or nearby states.
- Cheese Northeast: Cheese operations are maintaining full production schedules. Milk supplies into production are likely to increase into the July 4 holiday weekend, pushing some operations a little closer to capacity levels. Output over that period will likely add to stock accumulation. Processors are seeing slight growth in demand for natural cheese varieties, however.

Recommendation:

As expected, after 2 days of Brexit panic, the stock market has since rallied 4 straight days and is completely back in its pre-Brexit trading range. The USD is still higher, but only rose to levels going back to March. It will take about 2 years for Britain to exit the EU, so this vote's effect on international trade in the short term is zilch; nada. It's effect on domestic dairy demand is even less. While other markets have stabilized, the dairy complex saw continued volatility this week. Spot market cheese prices jumped as bidders appear to be scrambling to get fresh cheese. This week's Dairy Market News (DMN) updates appear to confirm plants we've talked to, that domestic cheese demand is strong. Buyers are looking for cheese beyond contracted orders. So while cheese stocks in warehouses are at or near record levels, those stocks are mostly aged. With the warmer weather now hitting much more of the U.S., cream is tightening, just when ice cream season is taking off. Demand for butter is also strong as eating habits in the U.S. continue to swing more towards a "natural foods" diet. Even demand for whole milk is up! While spot cheese prices did finish the week higher, they did come off their highs, after barrels briefly traded above \$1.70/lb. The willingness of sellers to let go of product around this level took a lot of upward momentum out of the market, and will provide resistance going forward. Profit-taking ensued, leaving most Class III and cheese futures in the red for the week. Dry whey futures, however, finished solidly higher. DMN reports that demand for dry whey is up, and this is helping support prices. Much of this dry whey is being exported to Asia as the pork herd is being rebuilt there. Recall, every penny move higher in dry whey, increases Class III by 6¢, so continued strength in this market could also support milk futures. Demand for NDM is also on the rise, with manufactures hanging on to stocks with confidence. With an extended holiday weekend upon us, there will be plenty of surplus milk available for processing of all types. With sellers eager to let go of product over the past two days' spot market, we'd expect some follow-through selling when the markets re-open on Tuesday. But once that is absorbed, we see cheese prices stabilizing and then continuing to move higher into the fall. Dairy producers who failed to purchase call options to cover Aug-Dec contracts, may have another opportunity to do so on further market weakness. Get on it! Those that still have milk to market should wait out this correction, then look for PUT option coverage the remainder of the year.

Note: Our offices will be closed on Monday, July 4th, in observance of Independence Day. Enjoy your freedoms. Be thankful to those purchased them. Be safe.

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