

**The KDM Dairy Report – July 8<sup>th</sup>, 2016**

**What's Bullish:**

- Spot Market: Blocks finished the week up ½¢ on just 3 trades to settle at \$1.63/lb, while barrels gained 5¢ on 18 trades to reach \$1.72/lb, a new high for the year. Grade A NDM increased 5½¢ on 20 trades to settle at \$0.89/lb, but butter fell 6¼¢ on just 1 trade to close at \$2.28¼/lb.
- U.S. dairy exports in May reached an 11-month high (by volume), led by whey, lactose and WMP, according to the U.S. Dairy Export Council. Dairy exports in May represented 13.7% of domestic milk production, the highest since last September.

Futures Month	Class III 07/08	Class III 07/01	Change	Dry Whey 07/08	Dry Whey 07/01	Change	Cheese 07/08	Cheese 07/01	Change
Jul-16	\$15.20	\$15.07	\$0.13	27.375¢	27.850¢	(0.48¢)	\$1.638	\$1.621	\$0.017
Aug-16	\$15.96	\$15.89	\$0.07	29.600¢	29.975¢	(0.38¢)	\$1.697	\$1.687	\$0.010
Sep-16	\$16.06	\$16.04	\$0.02	31.500¢	31.500¢	0.00¢	\$1.696	\$1.706	(\$0.010)
Oct-16	\$16.15	\$16.13	\$0.02	32.150¢	32.350¢	(0.20¢)	\$1.700	\$1.705	(\$0.005)
Nov-16	\$16.10	\$16.11	(\$0.01)	33.000¢	33.350¢	(0.35¢)	\$1.692	\$1.694	(\$0.002)
Dec-16	\$15.90	\$15.89	\$0.01	34.000¢	33.925¢	0.08¢	\$1.675	\$1.675	\$0.000
Jan-17	\$15.82	\$15.82	\$0.00	34.400¢	34.575¢	(0.18¢)	\$1.668	\$1.666	\$0.002
Feb-17	\$15.90	\$15.83	\$0.07	35.350¢	35.350¢	0.00¢	\$1.660	\$1.670	(\$0.010)
Mar-17	\$15.91	\$15.93	(\$0.02)	35.500¢	35.500¢	0.00¢	\$1.669	\$1.682	(\$0.013)
Apr-17	\$16.05	\$16.03	\$0.02	35.550¢	35.550¢	0.00¢	\$1.678	\$1.682	(\$0.004)
May-17	\$16.16	\$16.22	(\$0.06)	35.475¢	36.775¢	(1.30¢)	\$1.691	\$1.695	(\$0.004)
Jun-17	\$16.32	\$16.31	\$0.01	36.000¢	37.000¢	(1.00¢)	\$1.707	\$1.711	(\$0.004)
<b>12 Mo Avg</b>	<b>\$15.96</b>	<b>\$15.94</b>	<b>\$0.02</b>	<b>33.325¢</b>	<b>33.642¢</b>	<b>(0.32¢)</b>	<b>\$1.681</b>	<b>\$1.683</b>	<b>(\$0.002)</b>

- Dairy Products Report: Cheddar cheese output in May was down 2% vs. a year ago and down 2.3% from April. There was a surge in Gouda output (up 43%) as demand for higher end varieties increases. Total cheese output was 3% higher. Butter output climbed just 0.3% compared to last May, and was down 3.7% vs. April.
- Fluid Milk Southeast: Mid-Atlantic milk production is steady to slightly lower this week, as the area faces hot, humid conditions. Cow comfort is being tested in the Southeast. Industry contacts report temperatures reaching seasonal highs this week. Milk production is seasonally declining in the area. Florida farm level milk production continues to fall. There are reports of discarding loads of milk that were unable to be processed in a timely fashion over the weekend. Ice cream manufacturers are reportedly requesting additional loads of condensed skim outside of contracts. Cream availability did increase over the weekend, and spot loads moved at multiples on the lower end of the range. However, market participants feel the cream supply is tightening following the long weekend.
- Fluid Milk Central: Farm level milk production in the region is declining as hot, humid weather prevails. Several milk marketers report decreases in milk components. Overall, spot load availability is slowly disappearing. Cheese makers and butter manufacturers both welcomed additional loads of milk over the holiday. Numerous loads of milk are being diverted to bottling plants as several bottlers in the region report retail outlets discounting gallons of milk in the store and increasing their orders for bottled milk. Furthermore, a few market participants continue to see a growth in demand for bottled milk with a higher fat content. Industry contacts report being in the peak of seasonal ice cream demand and are happy with sales thus far.
- Fluid Milk Southwest: Farm milk production continues decreasing in California. Temperatures are averaging 106 degrees in the Central Valley. According to some processors, the milk butterfat component is at the lowest level of the year. Bottled milk sales are down this week. However, demand for flavored milk is active in some retail and food service channels. Interest for Class 3 (ice cream) is seasonally strong. Condensed milk sales into nonfat dry milk manufacturing are higher. In Arizona, the excessively high daytime temperatures are taking a toll on cows' comfort. Consequently, milk yields are trending lower. Milk components continue decreasing. Class I requests from retailers and food service are steady to lower, but sales into Class II are seasonally strong. Condensed skim demands from ice cream/frozen dessert and NDM processors are active. In New Mexico, farm milk output is steady to lower due to the warmer weather. Class II sales are higher as demand for ice cream continues ramping up.
- Fluid Milk Pacific Northwest: Some heat and dryness in parts of the region have impacted production somewhat. Abnormally dry conditions extend across both Washington and Oregon, with moderate drought persisting in Eastern Oregon. Milk production in the mountain states of Colorado, Idaho and Utah are steady to seasonally lower.
- Cream West: Cream supplies are tight in many processing plants. Ice cream/frozen dessert manufacturers are pulling moderate to heavy cream volumes. In addition, regional farm milk output is lower and the milk butterfat component is low. Cream continues moving into butter churning but at a lower rate.
- Butter Northeast: Cream availability is expected to tighten up. Several manufacturers are choosing to turn down inquiries from buyers, as they anticipate the market to firm in the upcoming months. Industry participants feel market forecasts are sparking buyers' interests to make near-term purchases. Demand for print butter moving into foodservice is strong.
- Butter Central: Manufacturers are taking into consideration what they anticipate to be a strong decrease in cream availability in the upcoming weeks when planning their churn production schedules. Brokers report consistent calls from buyers looking to make purchases. Many inventories in the Central region are reportedly already spoken for. Those with inventories not currently committed are confident in their ability to move butter in the upcoming months. Demand for fresh bulk butter is high, but supply is tight and offers from sellers are rare. Bulk butter prices reported ranged from market to 10¢ over the market, with various time frames and averages used. The market undertone is firm.
- Butter West: Cream is tightening, especially in the Southwest. As ice cream production continues to increase and milk components decrease, fewer spot loads of cream are finding their way into butter churns. Some butter manufacturers are beginning to transition from bulk butter to print butter in advance of increased domestic demand later in the year. Most butter makers are not concerned about inventory levels because they believe strong domestic late-year demand will consume much of the stockpiles.
- Dry Whey Northeast: Industry contacts say seasonal demand is increasing somewhat as a few ice cream producers draw more heavily on whey supplies. Inventories are mixed. A few manufacturers report committed stocks, while other contacts suggest dry whey is readily available.
- Dry Whey Central: Prices in the region are higher. Production is active to increasing as some Midwest cheese manufacturers fill up production schedules. However, several dry whey manufacturers report an increase in demand. Some market participants are receiving calls from end users looking to buy ahead. They speculate end users are looking at 2017 Q1 pricing and are trying to manage the anticipated price climb. A few

manufacturers report being unable to meet requests from buyers interested in additional loads outside of contracts. Interest from international buyers is steady. Some market participants believe there are still sizeable inventories of whey in the Midwest. However, several manufacturers and brokers do report significant stock relief recently. For some contacts, dry whey is being sold before it sees a storage shelf. The market undertone is firming.

- Dry Whey West: Prices continue to inch upward pulled by steady demand to feed Southeast Asia's growing pork industry. Production, although fairly steady, is also starting to come under some pressure. The sum total is demand appears to be starting to pass supply. A few manufacturers have committed Q3 stocks.
- NDM East: Prices moved higher this week. The market undertone is firmer. Demand from bakers is improving. Spot sales in the f.o.b. market are more active this week.
- NDM Central: Prices in the region are mostly higher this week. Dryers are full as manufacturers are running full production schedules. However, current U.S. NDM prices are competitive in the international market, boosting market involvement from international outlets. The market undertone is firming.
- NDM West: Prices are following upward trends in various indices. Spot sales are more active compared to the previous week. The market undertone is firmer. Interest from the bakery sector is improving. Some manufacturers are holding stocks anticipating higher prices in the near future. A few brokers are receiving offers from manufacturers with prices above the top of the range, edging close to one dollar per pound. Condensed skim milk is less available for processing as farm milk output is decreasing in the region. Consequently, NDM production is slightly lower. Inventories are getting tight in many processing plants.
- Cheese Northeast: Manufacturers report running full schedules, bringing in additional loads as plant capacity allows. However, inventories are mixed. A few manufacturers report strong demand, preventing them from building inventories. Industry contacts feel cheddar-type cheeses are seeing a slow climb in sales.
- Cheese Midwest: Several cheese manufacturers took advantage of the holiday weekend and brought in additional loads of milk. However, some manufacturers are seeing a drop in milk receipts. Components are beginning to fall as temperatures and humidity rise. Some cheese manufacturers seem optimistic this week. This may be attributed to reports of growing sales. Numerous manufacturers report increased calls from buyers seeking additional loads of cheese. However, a few of these producers do not have the additional cheese stocks to sell and are having to turn down potential sales. Cheese curd sales are seeing seasonal growth in sales.
- Cheese West: The current cheese level in cold storage continues to be heavy. However, some manufacturers lowered stocks when market prices were lower, while other producers look to slow down production where possible. Although storage space continues to be difficult to find, the decent demand for fresh commodity cheese from buyers is making it economically feasible to keep production stable. There is good domestic demand for readily consumable cheese. Prices have increased heading into the third quarter, and some producers are assuming the domestic demand will hold and carry on into the fall season.
- International: May milk output in the UK was down 3.2% vs. a year ago, according to AHDB data. Above average rainfall, low spring temperatures and low milk prices were all factors in the decline. April output in Australia was down 5.5% vs. last year, according to Dairy Australia stats.
- International: The recent lower EU milk pay prices have led to more commentary about dairy producers struggling to survive. In Germany, for example, there is more awareness of dairy producers losing farms to creditors. The low milk pay prices are often linked to recently lower dairy commodity prices. Recent commodity price increases, however, will not reach producer milk prices for a number of months.
- International: New Zealand dairy producers continue moving into early stages of the new milk production season in a downcast mood. Disappointing recent prices have widely impacted profitability in an unfavorable way. The 2015-16 season will not be fondly remembered. However, culling activity is light at this time, as many dairy producers take a wait and see approach. As last season drew to a close, there was conflicting activity; culling by some and seeking to increase total milk output to increase gross revenues by others. At this time many producers are stepping back to assess what the next move should be.

#### What's Bearish:

- Dairy cow slaughter for the week ending 06/18 totaled 49,000 head, down from 50,500 a year ago.
- After 3 consecutive increases, this week's GDT auction saw the price index decline 0.4%. Butter milk powder saw the biggest drop, falling 7.5%, followed by butter, down 3.1%.
- Fluid Milk Northeast: Balancing plants were busy over the holiday weekend working through additional loads of milk. A few contacts report an incoming supply of milk larger than they can handle. Several Northeast milk marketers feel the climb in milk production has leveled off, and supply is beginning to balance out. Industry contacts report dry, hot conditions in the Northeast that they anticipate will have an effect on milk production in the upcoming weeks. However, with several large herd expansions in the area, some market participants do not believe the drop in milk production will be as significant as in previous years.
- International: Australia is having a good start to the new milk production season as to cropping and pasture feed availability. Decent precipitation patterns in recent weeks have helped pasture health. This has contributed to reduced market purchasing of feed. Of course, relatively high feed prices and overall tight cash flows for many dairy producers, following recent disappointing milk pay prices, are also factors affecting feed purchases. The convergence of rain and resulting better pastures at this time is financially helpful to many dairy producers.

#### Recommendation:

Class III futures largely finished the week near where they left off last week. As is typical, there was a surplus of milk available over the holiday weekend, but that is changing. Heat in much of the country is finally beginning to hurt output and components; we are past the peak in all regions now. In addition, domestic demand is very strong. Fresh cheese suppliers, as well as dry whey, butter and NDM producers are having a hard time keeping up with demand. We have limited barrel cheese-making capacity, and it appears buyers are hungry for it. We just posted an 11-month high in dairy exports, while other dairy producing countries in the EU and Oceania are still financially struggling. The markets are recovering folks. Producers with existing hedges should aggressively purchase upside protection if they haven't done so already. Take advantage of the recent correction before it's gone!

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