

The KDM Dairy Report – December 12th, 2014

What's Bullish:

- Fluid Milk Pacific Northwest: Milk production is unchanged, hovering around the seasonal low point. Manufacturers at some locations indicate the demand from producers of cream cheese, sour cream, heavy cream, aerated cream and eggnog is keeping volumes of milk out of the balancing plants.
- NDM Central: Prices of low/medium heat nonfat dry milk moved lower this week, but those lower prices have caused additional end users to strongly consider taking a position. Buyer interest from the feed industry has picked up. Export orders have improved, most notably destined for Mexico.
- Cheese West: Manufacturing milk availability is variable in the region. Southwest cheese plant operators note gains from the seasonal low point, but Pacific Northwest, Utah, and Idaho cheese manufacturers report milk availability is lower in some areas of the Northwest.
- CWT has accepted 7 requests for export assistance to sell 540,133 pounds of Cheddar, Gouda and Monterey Jack cheese to customers in Asia and the Middle East. The product will be delivered December 2014 through June 2015.
- Grains: Perhaps feed won't be so cheap after all. Corn reached 4-month highs this week on technical buying and strong demand.

Futures Month	Class III 12/12	Class III 12/05	Change	Dry Whey 12/12	Dry Whey 12/05	Change	Cheese 12/12	Cheese 12/05	Change
Dec-14	\$17.75	\$17.80	(\$0.05)	57.600c	59.750c	(2.15c)	\$1.733	\$1.719	\$0.014
Jan-15	\$15.80	\$16.15	(\$0.35)	48.775c	52.500c	(3.73c)	\$1.601	\$1.608	(\$0.007)
Feb-15	\$15.51	\$15.78	(\$0.27)	44.000c	46.750c	(2.75c)	\$1.605	\$1.612	(\$0.007)
Mar-15	\$15.38	\$15.87	(\$0.49)	40.000c	44.000c	(4.00c)	\$1.614	\$1.640	(\$0.026)
Apr-15	\$15.54	\$15.91	(\$0.37)	37.075c	44.000c	(6.93c)	\$1.646	\$1.642	\$0.004
May-15	\$15.78	\$16.21	(\$0.43)	37.700c	43.800c	(6.10c)	\$1.664	\$1.672	(\$0.008)
Jun-15	\$16.05	\$16.45	(\$0.40)	38.350c	44.575c	(6.23c)	\$1.692	\$1.694	(\$0.002)
Jul-15	\$16.17	\$16.59	(\$0.42)	38.800c	45.250c	(6.45c)	\$1.706	\$1.704	\$0.002
Aug-15	\$16.60	\$16.90	(\$0.30)	40.275c	45.775c	(5.50c)	\$1.735	\$1.732	\$0.003
Sep-15	\$16.86	\$17.09	(\$0.23)	41.750c	46.150c	(4.40c)	\$1.759	\$1.752	\$0.007
Oct-15	\$16.87	\$17.08	(\$0.21)	42.250c	47.000c	(4.75c)	\$1.758	\$1.745	\$0.013
Nov-15	\$16.81	\$17.02	(\$0.21)	43.150c	46.000c	(2.85c)	\$1.745	\$1.742	\$0.003
12 Mo Avg	\$16.26	\$16.57	(\$0.31)	42.477c	47.129c	(4.65c)	\$1.688	\$1.689	(\$0.000)

What's Bearish:

- Spot Market: Blocks gained 2¢ during the week to close at \$1.60/lb, but barrels lost 4¢ to settle at \$1.51/lb. There were only 4 block trades, but 30 loads of barrels exchanged hands. Grade A NDM decreased 2½¢ to settle at \$1.08½/lb with no trades, while butter gave up 9½¢ to close at \$1.89/lb on just 3 trades.
- World Ag Supply & Demand Report: USDA lowered their 2015 Class III price estimate by 65¢/cwt from last month's forecast, citing weaker cheese and NDM prices. Large supplies are expected to remain in 2015, putting pressure on prices and causing USDA to revise their estimate to an average of \$16.75/cwt (which is probably still too high).
- Fluid Milk Northeast: Milk production in the Northeast and Mid-Atlantic regions is increasing along the seasonal trend. Milk volumes into balancing facilities vary, with levels above those of the previous year. Class I demand is leveling off after recovering from post-Thanksgiving holiday declines.
- Fluid Milk Southeast: Milk production in the region is level to slightly higher. Surplus milk volumes exceeding bottling needs are clearing to manufacturing facilities across regions. Distributors are looking ahead, as they anticipate heavier than usual milk volumes going into the Christmas holiday week. Florida's milk production is rising. Weather conditions are favorable for milk cows and expected to continue as cows freshen. Florida imported zero loads of milk this week, down from 76 loads last week.
- Fluid Milk Central: Milk production in the Central region is marginally declining following seasonal trends but dramatically above 2013 levels. Factors for the improvements include increasing availability of better feed and increased cow numbers due to reduced cow culling. Milk supplies are steadily growing while spot loads range from \$6.00 under to \$1.00 under Class. There is a growing concern about milk arrangements during the last 2 weeks of the year. Many processors are running at or near capacity levels. To combat the heavy milk supplies, some milk buyers are scaling back premiums to milk producers. Bottling sales are sluggish, but sale improvements are anticipated for next week. Class II production is easing as many holiday orders have been filled already. Ice cream production and sales are reduced, with supplies building.
- Fluid Milk Southwest: CA haulers report milk volumes clearing into processing facilities are steady to increasing compared to last week. Weather in the state is mild. AZ dairy producers report milk production is increasing, and components are recovering from summertime low values. Farm milk intakes in NM are steady, but demand for higher Class end uses is lower. Condensed skim is clearing throughout the region to find processing room. Alfalfa harvesting is complete for the year in most areas, giving dairy operations a boost in stocks on hand for the winter.
- Butter: Print butter ordering for the upcoming holidays is wrapping up. Butter operators are busily filling orders to meet approaching shipment deadlines. The market tone is firm with anticipated softening after holiday demand is complete.
- Dry Whey: Prices for Northeast dry whey trended lower this week. The market is maintaining a weak undertone. As butter and powder prices move lower, additional milk to cheese production is increasing whey solids. Inventories levels are growing. In the Central region, prices of dry whey are steady to slightly weaker and the undertone is softening as buyers note additional offerings at lower pricing. Export orders are slowing as some sellers are reporting shipment cancellations. Western dry whey prices are unchanged to lower, reflecting changes in various bases and manufacturers' interests in decreasing holdings. The market is mixed, with buyers noting additional spot offers available this week.
- NDM East: Nonfat dry milk prices are lower on a weakening market. Most buyers continue to restrict their nonfat dry milk purchases to immediate needs.
- Cheese Northeast: Production remains active as manufacturing orders are seasonally strong leading up to end of year holidays. Sales are good for all types of cheese varieties, but there is concern over what post-holiday sales might be like. The market undertone remains unsettled as prices continue soften.
- Cheese Midwest: Cheese markets have a weak undertone. Domestic sales remain as expected for this time of year but exports are lagging. Various factors are influencing markets. Milk production remains heavy and the flow of milk is driving cheese production. Some spot milk is moving in the Midwest at \$5.00 under Class. Moreover cheese plants with contracted milk supplies are paying producers at price levels not yet lowered to

reflect current lower cheese prices, due to the lag in the milk pricing formulas which is encouraging milk production. International factors are slowing exports of cheese from levels earlier this year. Europe in particular is moving cheese aggressively into export channels at pricing exerting downward pressure on U.S. cheese prices. Heavy cheese production is adding to concern with inventory levels. If cheese prices stay near current price levels, this will continue to expand the volume of cheese going into aging programs, particularly aged cheddar and some hard Italian varieties.

- International: Rabobank's latest quarterly report hints that prospects for dairy operations will be good in the medium to longer term, but will continue to face headwinds in the near term. Slumping dairy prices due to a global oversupply are the latest indicator of slower economic growth as they lower farm incomes and damp consumer spending. Favorable weather has boosted milk output in New Zealand and Australia, while sanctions on Russia have pushed dairy product into other markets, weighing on prices.
- Exports: Cheese exports in October declined 3% vs. 2013, according to U.S. DEC, falling for the fourth straight month. Butterfat exports plummeted 81% below year-ago levels, falling below 2,000 tons for just the second time in the last five years.

Recommendation:

Class III futures continued to sell off this week as product readily showed up at the spot market. Most of the fireworks occurred on Thursday when barrels traded as low as \$1.44/lb, before recovering to \$1.51/lb on 27 loads purchased. As more gloomy international economic numbers came out, along with increasingly bearish dairy supply fundamentals, any intra-day rallies slowly disappeared as sellers continued to pick off bids. Butter began to decline as well, and with holiday orders all but wrapped up, could see some significant declines in the near term. Using a Feb whey price, current spot works out to about \$15.30. Should butter drop from its current \$1.89 to, say, \$1.60, it put's Class III closer to \$15.20. All to say, producers may think \$15 is a bottom, but we wouldn't rule out seeing some \$14's and even possibly \$13's before prices begin to recover. The milk supply will not stop in Q1 and we will most likely be well in to Q2 before any tapering begins. The supplies of cheese going in to aging programs now could keep us stocked up going into Q3 more than we have been the past couple years. In summary, then, the picture looks fairly bleak until at least Q3. The Jan-Jun avg has now fallen to \$15.68, a new daily low. Likewise, the 2015 average is now down to \$16.18 and falling. We never like trying to catch a falling knife, but would still recommend producers sell any decent rallies.

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