

The KDM Dairy Report – July 17th, 2015

What's Bullish:

- Dairy cow slaughter for the week ended 07/04 totaled 48,500 head, up a strong 16.6% vs. the same period a year ago.
- Fluid Milk Northeast: Northeast, milk production has plateaued around the peak, but temperatures have been mostly moderate, helping to maintain output above previous year levels. Mid-Atlantic farm-level milk is flat. Sources report that supplies are not as burdensome into manufacturing as in past weeks.
- Fluid Milk Southeast: Milk production in the region continues to decline as the heat takes a toll on cow comfort. Limited milk volumes are clearing into processing plants.

Futures Month	Class III 07/17	Class III 07/09	Change	Dry Whey 07/17	Dry Whey 07/09	Change	Cheese 07/17	Cheese 07/09	Change
Jul-15	\$16.31	\$16.47	(\$0.16)	39.700¢	39.325¢	0.38¢	\$1.696	\$1.714	(\$0.018)
Aug-15	\$16.07	\$16.56	(\$0.49)	38.050¢	38.150¢	(0.10¢)	\$1.679	\$1.721	(\$0.042)
Sep-15	\$16.05	\$16.44	(\$0.39)	35.350¢	36.050¢	(0.70¢)	\$1.695	\$1.731	(\$0.036)
Oct-15	\$16.12	\$16.48	(\$0.36)	32.800¢	34.100¢	(1.30¢)	\$1.719	\$1.741	(\$0.022)
Nov-15	\$16.10	\$16.50	(\$0.40)	32.250¢	33.325¢	(1.08¢)	\$1.724	\$1.755	(\$0.031)
Dec-15	\$16.14	\$16.45	(\$0.31)	32.175¢	32.375¢	(0.20¢)	\$1.730	\$1.755	(\$0.025)
Jan-16	\$15.83	\$16.27	(\$0.44)	32.250¢	32.250¢	0.00¢	\$1.700	\$1.736	(\$0.036)
Feb-16	\$15.76	\$16.23	(\$0.47)	33.000¢	32.975¢	0.02¢	\$1.690	\$1.728	(\$0.038)
Mar-16	\$15.68	\$16.08	(\$0.40)	33.850¢	33.875¢	(0.02¢)	\$1.680	\$1.709	(\$0.029)
Apr-16	\$15.64	\$16.05	(\$0.41)	34.625¢	35.100¢	(0.48¢)	\$1.672	\$1.705	(\$0.033)
May-16	\$15.73	\$16.21	(\$0.48)	35.750¢	36.025¢	(0.27¢)	\$1.679	\$1.705	(\$0.026)
Jun-16	\$16.05	\$16.50	(\$0.45)	37.000¢	36.950¢	0.05¢	\$1.699	\$1.720	(\$0.021)
12 Mo Avg	\$15.96	\$16.35	(\$0.40)	34.733¢	35.042¢	(0.31¢)	\$1.697	\$1.727	(\$0.030)

- Florida's milk production is declining and expected to continue on that trend. Current cream prices remain high enough that plants with the option to delay churning continue to sell cream.
- Fluid Milk Central: Milk production is plateauing as the warmer weather sets in. Some bottlers are saying they have seen some upticks in tourist demand for fluid milk. Class II demand is strong. Ice cream orders are starting to decline seasonally but cream supplies are still tight. Some processors are reporting that they are keeping available cream supplies.
- Fluid Milk West: Milk output in California is lower. The water crisis continues to negatively affect major parts of milk operations. Some dairy farmers are leasing out hay/corn land to mitigate shortened returns related to expensive feed and water costs. Sales for Class I and II are steady. The milk production in Arizona is trending lower as an extended string of hot days is decreasing cow comfort. Local demand for Class I is higher. The school terms will resume in a few weeks, and bottlers are beginning the process of refilling milk pipelines. The interest for cream is strong. Ice cream and frozen dessert plants continue to clear up cream volumes. Cream inventories are tight.
- Butter Northeast: Churning is steady to lighter as available cream has declined marginally, due to active Class II demand. Butter makers seem content with cream levels, as inventories are adequate for current needs. Food service needs are moving good volumes, in response to summer vacation and resort activities.
- Butter Central: Cream supplies are tightening and multiples are moving higher. Central butter sales remain strong. Some contacts are noting orders for food service and restaurants are picking up.
- Butter West: Steady demand from ice cream manufacturing continues to pull cream away from butter production. Some butter makers say it is currently more advantageous to sell the cream than churn. Many producers have reduced production over the last few weeks.
- Cheese Midwest: Many manufacturers are still running full production schedules in order to absorb available milk, but also note a decrease in milk components. Demand remains steady and buyers are still active in contacting cheese makers for barrels. With football season and school terms resuming in a little over one month, some manufacturers are planning to transition a part of their production to mozzarella over the next few weeks.
- CWT has accepted 9 requests for export assistance to sell 1.294 million pounds of Cheddar, Gouda, and Monterey Jack cheese, and 661,387 pounds of whole milk powder to customers in Asia, Central America, South America. The product has been contracted for delivery in the period from July through December 2015.

What's Bearish:

- Spot Market: Block cheese finished the week down 11¼¢ to settle at \$1.61¼/lb while barrels gave up 6½¢ to close at \$1.59½/lb. Trading was moderate with 14 loads of blocks and 8 loads of barrels exchanging hands. NDM set new all-time lows, losing 4¢ to settle at 75½¢/lb on 18 trades. Butter fell 8¢ to close at \$1.84/lb with 11 loads exchanging hands.
- Fluid Milk Southwest: New Mexico milk production is waning. However, in-state processing plants are handling plentiful intakes. Some loads of milk are going out of state to be processed. The state is between the third and fourth cutting of alfalfa hay. Dairy farmers are expecting an improvement in the quality of feeding hay due to recent showers.
- Fluid Milk Pacific Northwest: Milk production in the region is slowing somewhat, but manufacturers still report plenty of milk is available for processing. Slightly lower temperatures have provided some relief to cows across Utah and Idaho. Processors are reporting a decline in milk components, especially in pasture-based herds. Overall, however, milk volume is still plentiful to keep plants running at capacity.
- Dry Whey Northeast: Prices moved lower this week. Production is active, paralleling strong cheese output. The bulk of whey is moving through contracts, as spot transactions remain limited. Brokers are reporting quiet sales activity. Export interest remains sluggish.
- Dry Whey Central: Prices eroded this week, and manufacturers believe that there is pressure on the market for prices to go even lower. Some manufacturers are selling at current pricing levels because they do not want to hold stocks in a downward trending market. Production continues to be strong as cheese manufacturers are reporting solid production rates.
- Dry Whey West: Price moved lower this week in a market that remains soft. Inventories are long and demand has been limited. Industry contacts suggest prices may need to be lower to compete in world markets.
- NDM Northeast: Prices continue to trend lower. Dryers continue to operate near capacity to process heavy condensed skim volumes. Demand is light to fair. Stocks are noted as plentiful.

- NDM Central: Some manufacturers are concerned that the lower pricing levels will continue longer than expected. Nonfat dry milk production is active as most manufacturers are foregoing other dry products and making NDM. Demand is poor as most buyers are waiting to see what the prices will do.
- NDM West: The low/medium heat nonfat dry market tone is weak. Demand is light outside of contracts. Buyers are fishing for discount prices to make any purchase. The inventories are steady to building.
- Cheese Northeast: Most processors are maintaining active production schedules. The availability of milk supplies continues to support strong cheese output. New production is being channeled heavily into cheddar aging programs. The demand for aged cheddar is good. Demand varies amongst the other varieties.
- Cheese West: Although cheese yields have dropped a little, many cheese makers report plenty of milk to keep plants at full production. Manufacturers say current inventories can easily meet regular customer requests. They also note exports of American style cheese have dropped off. Industry contacts are trying to assess the chances of a slowdown in domestic demand. Through the first half of this year, domestic demand has been stronger than anticipated. However, they are unsure whether private cheese holdings will become saturated and if those buyers will slow their purchasing through the end of the year.
- International: This week's GDT auction resulted in a sharp 10.7% decline in the GDT price index. Powders were weak again, but losses were led by cheddar cheese, down 13.9%, to a U.S.- equivalent \$1.19/lb.

Recommendation:

This week's GDT auction really took the wind out of any hope of a rally this week. Down 10.7% overall and the ninth consecutive drop (going back to the March 3rd auction) put a bearish grip on the market. And no wonder! Consider these "international" prices (based on GDT settlement) the U.S. must compete with: Cheddar cheese - \$1.19/lb, butter - \$1.12/lb, skim milk powder \$0.77/lb. After seeing an increase last week, spot cheese prices gave up ground this week, with nonfat dry milk setting an all-time low. Current spot prices work out to about \$15.45 Class III and just \$12.37 Class IV. If this spread hangs on, negative PPDs will start showing up in producers' milk checks. And under \$16 milk appears to be an area that is not profitable for a majority of the nation's dairies. Clearly the short-term trend is down. Cheese is available, though not yet burdensome, and will likely continue to look for a home next week as well. Up front, Aug and Sep Class III are still pricing in a premium to spot and are susceptible to further declines. About the only positives are the coming of school, with fluid pipelines starting to refill, and a switch to more mozzarella output in anticipation of football season (first NFL pre-season game just 4 weeks away). We are past the peak as a nation, but much of the cheese-making part of the country has plenty of milk. 2016 contracts continued to erode as bearishness/negativity sink in. We're still not sure we'd go all in on 2016 yet. Current pay prices will be brutal for Oceania producers, while the cost of production in the EU remains high. At some point the herd/milk production will start to decline. Even here in the U.S., cull rates could pick up quickly once the first few low milk checks arrive. Finally, we still think China will come back as a buyer at some point, even if not at the same levels of last year. In summary, there remains lots of uncertainty in this market. Producers should protect margins where they can. Consider selling rallies in Aug/Sep Class III.

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