

The KDM Dairy Report – February 12th, 2016

What's Bullish:

- Spot Market: Block cheese gained 2¢ for the week on 13 trades, to settle at \$1.49/lb. Barrel cheese increased 1½¢ on no trades, to \$1.48/lb.
- Fluid Milk Pacific Northwest: Milk production is inching higher, but output in Utah and Idaho is at or slightly below normal seasonal levels. Although milk supplies are mostly well balanced with milk needs, a few contacts say there are some occurrences of tightness of milk supplies. Dairy officials report some farmers are hesitant to expand their herd at this time because of higher replacement heifer costs and anticipated lower milk prices through 2016.

Futures Month	Class III 02/12	Class III 02/05	Change	Dry Whey 02/12	Dry Whey 02/05	Change	Cheese 02/12	Cheese 02/05	Change
Feb-16	\$13.87	\$13.83	\$0.04	24.700¢	24.375¢	0.32¢	\$1.525	\$1.520	\$0.005
Mar-16	\$14.06	\$13.96	\$0.10	24.475¢	24.050¢	0.43¢	\$1.540	\$1.535	\$0.005
Apr-16	\$14.11	\$13.96	\$0.15	25.400¢	24.225¢	1.18¢	\$1.541	\$1.532	\$0.009
May-16	\$14.19	\$14.15	\$0.04	25.900¢	24.875¢	1.03¢	\$1.547	\$1.555	(\$0.008)
Jun-16	\$14.50	\$14.63	(\$0.13)	25.575¢	25.025¢	0.55¢	\$1.585	\$1.593	(\$0.008)
Jul-16	\$14.95	\$15.02	(\$0.07)	26.025¢	25.750¢	0.27¢	\$1.624	\$1.634	(\$0.010)
Aug-16	\$15.29	\$15.41	(\$0.12)	26.125¢	26.275¢	(0.15¢)	\$1.664	\$1.672	(\$0.008)
Sep-16	\$15.64	\$15.71	(\$0.07)	27.000¢	27.250¢	(0.25¢)	\$1.690	\$1.694	(\$0.004)
Oct-16	\$15.80	\$15.86	(\$0.06)	28.000¢	28.000¢	0.00¢	\$1.703	\$1.703	\$0.000
Nov-16	\$15.81	\$15.85	(\$0.04)	28.525¢	28.525¢	0.00¢	\$1.701	\$1.699	\$0.002
Dec-16	\$15.82	\$15.77	\$0.05	29.500¢	29.500¢	0.00¢	\$1.700	\$1.693	\$0.007
Jan-17	\$15.60	\$15.58	\$0.02	29.775¢	29.775¢	0.00¢	\$1.682	\$1.680	\$0.002
12 Mo Avg	\$14.97	\$14.98	(\$0.01)	26.750¢	26.469¢	0.28¢	\$1.625	\$1.626	(\$0.001)

- Dry Whey: Prices are unchanged on the range, but higher on the mostly price series. The market tone is mostly steady to firm as some contract and f.o.b. spot prices adjust to variable indices. Recent strong availability of higher protein content WPCs has spurred additional interest in dry whey in the Central region from several feed blenders. Some western manufacturers report inventories are stable, but fairly committed.
- CWT has accepted 5 requests for export assistance to sell 101,413 pounds of Cheddar and Gouda cheese and 4.133 million pounds of whole milk powder to customers in Asia, Central and South America. The product has been contracted for delivery in the period from February through July 2016.

What's Bearish:

- Spot Market: While cheese prices increased, butter lost 6¢ to \$2.11/lb on heavy trading of 23 loads. NDM declined 1¼¢ to \$0.73¼/lb on 10 trades.
- WASDE Report: USDA increased their 2016 milk production forecast as cow numbers as of Jan 1 were revised higher. Beginning stocks for cheese were also revised higher, due to end-of-year stocks for 2015 being higher than expected. As a result, USDA lowered their Class III price forecast another nickel from last month, to \$14.40/cwt.
- Butter stocks at selected storage centers jumped 13% in just the first 8 days of February, according to USDA. Cheese stocks were flat over the same period.
- Fluid Milk Northeast: Milk production in the region is steady. Class I sales dipped slightly. Manufacturing supplies are slightly higher. Milk production in the Mid-Atlantic is mostly flat. Class I sales are showing a slight uptick, while Class II and III sales are level.
- Fluid Milk Southeast: Milk output is rising in the Southeast. Milk handlers report that bottlers are applying significant cuts to orders this week. As a result, surplus milk is being shipped to a few supporting cheese plants as cancellations of loads from the Mid-east occur. In Florida, temperatures are abnormally cool. Milk production is reported flat for most of the area, but bottling sales are down. Class IV drying is very active, and regional supplies are above current demand. Cream quantities are available, though somewhat tighter than the previous week. Coming into the week, multiples were much stronger, but demand took a dive by mid-week causing a slight drop.
- Fluid Milk Central: Milk production continues its steady march higher from week to week. Bottled milk sales are steady to somewhat lower as school districts adjust orders to account for the upcoming holiday-shortened school week. Demand from cheese plant operators is steady to lower. With Super Bowl related sales completed, cheese sellers indicate they have a long stretch ahead of them to get to grilling season. Some manufacturers indicate they want to moderate cheese inventories carefully through Q1-Q2. Butter plant operators at some locations are reluctant to take on additional cream as internal cream supplies are ample.
- Fluid Milk Southwest: Milk production at the farm level is steadily climbing in California. Manufacturing milk volumes are heavy. Farm level milk output is higher in Arizona as the weather remains advantageous for the dairy herds. Bottled milk sales into retail and food service accounts are steady to higher, but sales into Class II are slightly lower this week. Condensed skim volumes moving into Class IV (butter/powder) are increasing. According to NASS, in January 2016, alfalfa conditions were mostly good to excellent in Arizona and harvesting occurred on at least 70% of the acres across the state. Compared to the previous week, milk production is steady in New Mexico. Manufacturing milk volumes moving into processing plants are improving gradually. Cream supplies are higher throughout the West. Most of the cream is moving into butter manufacturing. Many butter processors indicate their churns are running at full capacity. Some western cream loads are clearing into the Central region.
- Butter: Production continues to be active throughout the country as cream availability is fairly strong. Many butter churn operations are running full. Butter processors are still interested in building inventories ahead of the summer. The market undertone is unsettled in the East and steady to mixed in the Central region. Interest from food service is steady to lower as many restaurants already placed orders to cover the upcoming weekend highlighted by the Super Bowl.
- NDM East: Prices lower in a weak market. Low/medium heat nonfat production is steady. Drying is heavy, 6 to 7 days at some plants, although increasing interest in condensed skim is easing the burden. Discussions that are ongoing reflect a lack of buyer interest at this point. Some expect prices to move lower and are careful not to over-expand stocks in a downward trending market.
- NDM Central: Low/medium heat nonfat dry milk prices are mostly lower. Some producers indicate they would like to sell additional NDM, but are finding limited interest in the marketplace. Low/medium heat NDM production is active throughout the region as milk intakes step seasonally higher. With progressively lighter interest from Classes I/III manufacturers, more farm milk is clearing through balancing plants into NDM. Low/medium heat NDM inventories are building.

- NDM West: The market undertone is unsettled. Sales in the spot market have been slow throughout the week. Demands from buyers/end users are light. Production of low/medium heat NDM is higher as heavy condensed skim volumes continue to clear into dryers. Inventories are steady to building.
- Cheese Northeast: Milk supplies are at levels that continue active cheese production at area plants. Sales remain good, as demand exceeds the expectation of a few cheese manufacturers. However, supplies are starting to build for some cheese operations.
- Cheese Midwest: Cheese output is steady, with milk supplies remaining mostly even. Demand is slower at many packaging firms, which has rippled back to manufacturers. Concern with inventory levels is increasing in many cheese plants.
- Cheese West: Cheese production is active and stable. Most cheese makers say they have plenty of milk for all their processing needs. Cheese demand is mostly steady. Any Super Bowl effect has now ended and cheese makers are hoping domestic demand can continue to be strong. Concern is building somewhat over the limited amount of export opportunities and heavy cheese inventories.
- International: In a news article this week, Rabobank dairy analysts were quoted as saying they think Ireland can exceed its target to increase milk production 50% by 2020, in a post-quota environment. Irish milk supplies in 2015 were already 13.3% higher than in 2014.

Recommendation:

Decent domestic demand continues to support spot cheese prices, but both NDM and butter were lower this week. With international butter prices in the \$1.30's and Super Bowl demand over, butter futures took a big hit as spot prices faded. June butter futures traded as high as \$2.40 on 01/15 and \$2.24 on Monday, but hit a low of \$2.14 today. We expect further weakness ahead as churning operations deal with higher milk output going in to spring. While spot cheese prices increased this week, we question how long this can be sustained. The milk supply across the U.S. is on the rise, and as the country begins to warm, that flow will only increase, at an increasing rate. Processors of all milk classes will be pushed to their limits. With several months until grilling season, manufacturers face growing concern over inventories, which are approaching burdensome levels in the West. We still recommend getting further coverage in the 2nd half of the year, which dropped a nickel from last week to a \$15.55 average. Current spot prices work out to about \$13.60 Class III. With the drop in spot butter this week, Class IV at \$13.35 fell below Class III for the first time in a long time. Further predicted drops in the butter price will give more incentive to shift milk into cheese, putting further pressure on prices. As we wrote last week, this bear market may still be in its early stages. Sell while you can, not when you have to.

Note: Our offices will be closed on Monday in observance of President's Day. Markets will be closed.

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