

The KDM Dairy Report – April 8th, 2016

What's Bullish:

- Spot Market: While most Class III components were lower, butter rocketed 16¢ higher for the week to close at \$2.12/lb, its highest price since Feb. 26 loads exchanged hands.
- Fluid Milk Pacific Northwest: Milk production is following seasonal trends, but some manufacturers suggest milk intakes are not showing a lot of year to year growth right now. Other processors say milk production seems to have hit a little plateau and is currently in good balance with manufacturing needs. Bottling demand is returning to more typical patterns, as many educational institutions resuming classes after spring break. Milk intakes are balanced with processing needs in Utah and Idaho. In parts of the region, precipitation has made farms a little sloppy. In some cases, the mud and weather conditions have bumped somatic cell counts up a little or created other small production issues.
- Butter: Although spring holidays have ended, the butter prices continue rising. Some industry participants admit confusion over the sudden high trend in butter prices. However, some sources credit this strength in prices to buyers' purchases ahead of summer needs. In the East, sales transactions are fair to good. In the Central region, the pace of retail sales is slower than the previous month. Demand from food service is steady. In the West, demand from retailers continues to be strong.
- Land O' Lakes announced this week that they will have a nationwide base plan implemented this year. While this was introduced last year in the Eastern region, it would be a first in the Midwest. It's currently unknown if other co-ops will also implement quotas in the Midwest, but if others follow suite, it could support milk prices in the second half of the year.
- International: U.S. dairy exports were up 4% vs. a year ago, according to USDEC. Total exports were equivalent to about 13.4% of domestic milk production, their highest level since October. Gains were led by butterfat up 63% and NDM/SMP up 16%, but cheese exports were down 18%.

Futures Month	Class III 04/08	Class III 04/01	Change	Dry Whey 04/08	Dry Whey 04/01	Change	Cheese 04/08	Cheese 04/01	Change
Apr-16	\$13.74	\$13.81	(\$0.07)	24.250¢	24.250¢	0.00¢	\$1.515	\$1.526	(\$0.011)
May-16	\$13.67	\$13.98	(\$0.31)	24.375¢	24.500¢	(0.13¢)	\$1.504	\$1.540	(\$0.036)
Jun-16	\$13.87	\$14.05	(\$0.18)	24.925¢	24.750¢	0.18¢	\$1.521	\$1.542	(\$0.021)
Jul-16	\$14.17	\$14.29	(\$0.12)	25.000¢	24.750¢	0.25¢	\$1.550	\$1.570	(\$0.020)
Aug-16	\$14.59	\$14.63	(\$0.04)	25.125¢	24.975¢	0.15¢	\$1.592	\$1.604	(\$0.012)
Sep-16	\$14.87	\$14.85	\$0.02	25.600¢	25.250¢	0.35¢	\$1.615	\$1.622	(\$0.007)
Oct-16	\$14.97	\$14.95	\$0.02	26.075¢	25.750¢	0.32¢	\$1.625	\$1.634	(\$0.009)
Nov-16	\$15.00	\$14.95	\$0.05	26.350¢	26.000¢	0.35¢	\$1.624	\$1.628	(\$0.004)
Dec-16	\$14.92	\$14.90	\$0.02	26.775¢	26.500¢	0.27¢	\$1.621	\$1.625	(\$0.004)
Jan-17	\$14.90	\$14.76	\$0.14	27.025¢	27.700¢	(0.68¢)	\$1.615	\$1.614	\$0.001
Feb-17	\$14.91	\$14.70	\$0.21	27.225¢	28.425¢	(1.20¢)	\$1.616	\$1.601	\$0.015
Mar-17	\$14.98	\$14.72	\$0.26	27.500¢	28.025¢	(0.52¢)	\$1.630	\$1.607	\$0.023
12 Mo Avg	\$14.55	\$14.55	\$0.00	25.852¢	25.906¢	(0.05¢)	\$1.586	\$1.593	(\$0.007)

What's Bearish:

- Spot Market: Block cheese lost 5¢ during the week to close at \$1.42/lb, while barrels gave up 3¼¢ to settle at \$1.41¼/lb. Trade volume was light, with just one load of blocks exchanging hands and 5 loads of barrels. Grade A NDM finished the week down 2¼¢, a new low for 2016, and tied the historical low made in Aug '15, at 69¢/lb. 14 loads exchanged hands.
- Dairy Products Report: American cheese output in Feb was up a leap-adjusted 1.24% compared to a year ago, while total cheese output was up 4.04%. Butter output climbed 5.8% vs. Feb '15.
- Dairy cow slaughter for the week ending 03/26 totaled 54,400 head, down 8% vs. the same period a year ago.
- Fluid Milk East: As temperatures and weather conditions vary in the Northeast and Mid-Atlantic regions, milk production is reported steady to increasing. In the Southeast, milk production is seeing seasonal gains, with noted increases in plant milk intakes. Condensed skim is very ample. Regional balancing plants are sending significant volumes to drying. F.O.B. sale transactions are few. Most cash sales that occur usually trade with a considerable discount. Regional cream availability is substantial, with most going into butter production.
- Fluid Milk Central: South Central milk production is managing week over week gains, although the increases are getting smaller compared to a few weeks ago. In the North Central, farm milk pickups continue to trend higher. Although weather throughout the region has been changeable, with freezing nighttime temperatures alternating with and relatively warm days, these issues have not impacted cow comfort.
- Fluid Milk Southwest: California milk production is flat to slightly higher. Bottled milk sales are mixed, with orders from grocery stores and food service slightly lower throughout the week. Sales into Class III are gradually rising as summer approaches. Arizona milk output is up, at the peak of spring flush. Some local processing plants are clearing milk volumes from nearby states. In New Mexico, milk production continues rising. Favorable weather conditions are boosting cows' comfort. Some processing plants from nearby states are still clearing milk volumes from state's producers. Class I demand is steady to slightly lower as school pipelines are starting to be fulfilled.
- Dry Whey Northeast: Output is steady as cheese plants run full production schedules to handle seasonal milk receipts. Manufacturers report a slight drop in dry whey demand, which is leading to increases in stocks. The market undertone remains weak.
- Dry Whey Central: The market tone is weak following several weeks of active cheese/dry whey production and light to moderate interest outside of contracts. Resellers have put some offers in play, but report some sales are solidifying losses. Buyers are choosy and content to shop through multiple outlets. Dry whey production is active. With heavy milk supplies, discount priced spot loads of milk are helping defray production costs for some cheese vats, as well as the dry whey. Manufacturers' inventories are steady to higher.
- Dry Whey West: Production remains relatively stable and active. Manufacturers say their inventories are a little heavy, but not at the levels that create concerns. In effect, western processors are more apprehensive about whey stocks and production in other regions. Western dry whey is moving in domestic and export markets, but some processors say demand is flat. Industry contacts describe the market tone as becoming weaker in the upcoming months.
- NDM Northeast: Prices declined this week. Manufacturers' low/medium heat NDM production runs are active, with heavy output, as milk intakes increase. Condensed skim sales outside of contracts are sluggish, and adds to NDM production output. Sources note that milk deliveries are experiencing short delays when unloading at some plants. Low/medium NDM holdings are substantial at most manufacturing plants and growing.

- NDM Central: The market tone is weak. Manufacturers at some locations are faced with mounting NDM inventories as milk intakes climb seasonally. Buyers are looking for loads with price as the first consideration. Market participants report blocks of loads are being offered from some manufacturers, with price discounts to the current market. Low/medium heat nonfat dry milk production is active at most locations throughout the Central region. Inventories are building.
- NDM West: Prices are lower on a weaker market. The usage of NDM for cheese fortification is active. However, the interest from the bakery sector is steadily waning. Some buyers/end users continue putting pressure on the market anticipating lower prices in the near future.
- Cheese Northeast: Milk volumes into cheese are backing full production schedules for both cheddar and mozzarella manufacturers. The market undertone is relaxed with buyers waiting to see where the market will level out.
- Cheese Midwest: This being the flush time of year, milk available for cheese making is increasing. Spot sales of milk offered below class prices are reported. Some processors with heavy milk supplies, wishing to sell non committed milk, report that it can be difficult to find a buyer. Many Midwest cheese plants are operating at full capacity as a result of purchasing available spot milk. Domestic sales have been decent but export sales remain challenging. Awareness of tight cold storage availability weighs on the minds of a number of cheesemakers. Aging programs are well stocked. Mozzarella and cheddar production are particularly strong. Makers of specialty cheese, often made in relatively smaller plants than plants making commercial volumes of more common cheeses, particularly welcome the availability of discount milk to reduce the cost basis.
- Cheese Northeast: Cheese production continues to increase seasonally. A few cheese makers say mozzarella and provolone production is steady to higher with strong sales into food service. Some manufacturers note a slight decrease in commercial cheese demand. Cheese is moving, but it takes a little more work and in some cases price concessions to complete the transactions. End users seem to want to reduce their own inventories, rather than take on more cheese. Industry contacts say there is still a lot of cheese available. Barrel cheese stocks are heavy. While inventories of blocks of cheese are also long, they are more comfortable than barrels. The market tone is unsettled and a little bearish.

Recommendation:

Heavy milk and cheese supplies continued to weigh on front-month contracts this week, but we did see quite a bit of resilience in the deferred months. While milk output is hitting its heaviest time of the year domestically, we are already at or past the peak in the Southwest, with components starting to decline. In addition, output in the Pacific Northwest is less than overwhelming, putting in to question when or if they've already reached their peak. Domestic demand for dairy is off to a robust start, which is helping move product at current prices. A specialty cheese maker we spoke to this week is sold out of hard Italian, with most future production committed. Despite spot cheese prices declining this week, a steady bid in both cheese and Class III futures had us scratching our heads again this week. A news article released yesterday, announced that Land O' Lakes was rolling out a nationwide milk base program in an effort to control some of the current milk glut. Faced with the possibility of being overwhelmed this spring, it will be interesting to see if other co-ops follow in their steps, to avoid a "processor-constrained" situation. It may have been rumors of this program that have supported the market for the past week; time will tell. Certainly an industry-imposed quote system could support the futures market later this year. In the nearby months, however, current spot prices work out to just under \$13/cwt. With weekly NDPSR numbers continuing to carry a premium to spot prices, don't expect Class III to fall below \$13 just yet. However, with both long block and barrel supplies, and commercial storage facilities tipping to the full side, fresh cheese production will need to find a home. If it can't, it will most likely show up at the CME Group spot market and pressure prices. Most buyers can be patient at this point. With the uncertainty of a potential base program and weather issues, now is still a good time to get existing hedges protected. Get those call options purchased July-Dec to open up those fixed plant and futures contracts!

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