

**The KDM Dairy Report – March 17<sup>th</sup>, 2017**

**What's Bullish:**

- Dairy cow slaughter for the week ending 03/04 totaled 62,200 head, up 5.2% vs. the same period a year ago.
- Butter Northeast: Milk input levels continue to encourage the region's seasonally strong butter production. However, retail business is good. Heavy print volumes are set to clear ahead of the approaching holiday period, with scattered retail feature activity in the plans. Meanwhile, kosher butter transactions are above producers' expectations. The market reports an increase in the margin, well over the previous year.

Futures Month	Class III 03/17	Class III 03/10	Change	Dry Whey 03/17	Dry Whey 03/10	Change	Cheese 03/17	Cheese 03/10	Change
Mar-17	\$15.73	\$15.74	(\$0.01)	51.400c	50.900c	0.50c	\$1.551	\$1.560	(\$0.009)
Apr-17	\$15.28	\$15.61	(\$0.33)	49.000c	48.750c	0.25c	\$1.520	\$1.552	(\$0.032)
May-17	\$15.40	\$15.76	(\$0.36)	45.250c	46.025c	(0.77c)	\$1.556	\$1.585	(\$0.029)
Jun-17	\$15.84	\$16.10	(\$0.26)	42.025c	43.525c	(1.50c)	\$1.612	\$1.636	(\$0.024)
Jul-17	\$16.37	\$16.53	(\$0.16)	39.125c	42.275c	(3.15c)	\$1.686	\$1.690	(\$0.004)
Aug-17	\$16.64	\$16.83	(\$0.19)	39.000c	41.525c	(2.53c)	\$1.729	\$1.727	\$0.002
Sep-17	\$16.75	\$16.93	(\$0.18)	38.525c	40.500c	(1.98c)	\$1.730	\$1.737	(\$0.007)
Oct-17	\$16.57	\$16.75	(\$0.18)	38.000c	40.250c	(2.25c)	\$1.717	\$1.727	(\$0.010)
Nov-17	\$16.42	\$16.68	(\$0.26)	37.250c	39.500c	(2.25c)	\$1.708	\$1.726	(\$0.018)
Dec-17	\$16.33	\$16.54	(\$0.21)	36.250c	39.500c	(3.25c)	\$1.705	\$1.715	(\$0.010)
Jan-18	\$16.30	\$16.50	(\$0.20)	37.000c	39.000c	(2.00c)	\$1.702	\$1.715	(\$0.013)
Feb-18	\$16.25	\$16.50	(\$0.25)	37.000c	39.375c	(2.38c)	\$1.715	\$1.715	\$0.000
<b>12 Mo Avg</b>	<b>\$16.16</b>	<b>\$16.37</b>	<b>(\$0.22)</b>	<b>40.819c</b>	<b>42.594c</b>	<b>(1.78c)</b>	<b>\$1.661</b>	<b>\$1.674</b>	<b>(\$0.013)</b>

- Butter Central: There is no shortage of cream in the region, keeping butter production active. Butter inventories are building when demand allows. However, there are reports of butter orders increasing as spring approaches. Despite heavy inventories, some Central contacts suggest demand is strong, and inventories are comfortable for late summer/early fall ordering rushes.
- Dry Whey Northeast: Market participants are actively seeking purchases, although uncommitted inventories are limited. Loads clearing to contracts are on schedule. Inventories continue to tighten. Most reports point to a decreasing level of production in dry whey. Some large cheese producers have cut back on production this week for maintenance, which has limited the amount of whey on the market.
- Dry Whey Central: Demand is increasing domestically. Some cheese producers in the Midwest continue to see Southeast Asian interest. However, other contacts report a slight decline in requests as China's inventories are currently comfortable. Inventory reports range from tight to adequate.
- Dry Whey West: The market tone is relatively stable. Inventories remain comfortable to tight and some contacts report resales above published prices. Production is steady and domestic buyers are taking regular shipments.
- International: European cheese manufacturers are aware of the need to increase cheese production. Increased per capita demand for cheese within the European Union during 2016, the third consecutive year of increases, is expected to continue, according to the Agriculture and Rural Development section of the European Commission. Internal EU cheese consumption during 2016 increased 1.3% per capita and production increased 1.4%. During 2017 and 2018, cheese production is projected to increase 2%. With late 2016 cheese sales having required cheese to be removed from storage to meet demand, cheese manufacturers are looking ahead with expectations of needing to ramp up production to meet 2017 demand.
- International: Milk production in Western Europe continues to increase seasonally. However, current estimates are that in Germany production this week is between 2% and 3% below volumes one year ago. Production in France this week is estimated at about 1.5% below volumes one year ago. Russian imports of butter in December 2016 increased 3.4% from one year earlier, according to Eucolait. Belarus has become a significant supplier of dairy products to Russia.
- International: Butter prices in Western Europe continued the recent firming trend after a 2017 early year dip. Butteroil prices also strengthened. Butter prices in Germany and Netherlands are higher, with French prices mostly stable. Demand for butter in Europe is called dynamic, consistent with global interest in dairy fats. Growing butter demand is also characterized as signaling a new consumer love affair with butter. Demand for packaged and block butter is firming.
- International: January 2017 milk production in Australia was 5.9% below January 2016. July 2016-January 2017 cumulative production is 8.2% below the same period one year ago. In New Zealand, bank economists have cut their 2016-17 milk price forecasts following recent lower dairy product prices and indicators of higher milk production than recently forecast. January 2017 New Zealand milk production was 2.41 million MT, down 10.4% from December and down 0.82% vs. Jan '16, according to DCANZ. January milk solids, at 209.69 million kg, were down 7% from December.
- International: Oceania butter prices strengthened at the bottom of the price range. Butter price strength continues even with weakness in some other dairy products. Greater anxiety over tighter dairy fats supplies is sustaining this market. 82% butterfat averaged a U.S. equivalent \$2.15/lb.
- International: The dairy industry in Argentina is in crisis, according to several market participants. The adverse effects of recent floods in the main dairy basins are still taking a toll on farm milk yields. In addition, the summer weather and the scarcity of feeding stocks are limiting cows' productivity. As a result, milk intakes are less than adequate for several processing needs. A few dairy manufacturing companies are closing some plants and reducing personnel due to economic issues. Fluid/UHT milk demands from some educational institutions and retailers are strong. In the same way, ahead on the upcoming fall holiday season, demand for cream is robust. However, butterfat supplies remain below adequate to cover all buyers/end users' needs. Milk production at the farm level is steady in Uruguay, following seasonal patterns. However, farm milk intakes are expected to increase in the next few weeks, when temperatures start to drop. Milk components remain low. The demands for cream from butter and milk caramel processors are high on a strong market. In Brazil, farm milk production is down, following the usual summer patterns. The lower milk supply is helping to maintain high farm gate prices. After the past holiday celebration, bottled milk/UHT sales to retailers are improving. The consumption of cream is improving. However, current cream supplies are less than sufficient to meet the strong demand. Thus, buyers are paying higher premiums for milk butterfat.

**What's Bearish:**

- Spot Market: Blocks managed to gain 1½¢ to settle at \$1.40/lb on 16 trades, but barrels finished the week down 3½¢ to close at \$1.36½/lb on 23 trades. NDM edged ¼¢ lower to \$0.80½ on 13 trades, while butter declined 3¼¢ to close at \$2.13/lb on 32 trades.

- Butter holdings at USDA selected warehouses are up 21% over the period 03/01 through 03/13, according to USDA. Cheese holdings are up 2% over the same period.
- Fluid Milk East: Farm milk production in the Eastern region of the United States continues to produce ample volumes of milk. In the Southeast, manufacturing plants are full with milk, with no delays in distribution. Milk production in Florida is steady. Eastern Class I sales are down currently with schools closed for spring break. Condensed skim continues to be plentiful all over the East.
- Fluid Milk Central: Milk production is in an upward trend in the region. Even with a short stint of single digit temperatures in the Upper Midwest early in the week, contacts do not foresee a production slowdown. South Central contacts report the weather has been beneficial for cow comfort, with few extreme temperatures and low precipitation. Class I demand has not picked up after weeks of slow orders. Some educational institutions are on spring break now, and many more will be away next week. Spot milk prices ranged from \$2.00 to \$5.00 under Class. Cream continues to be readily available.
- Fluid Milk Southwest: Dairy producers in California suggest that milk output is higher this week. Cows are back to their comfortable temperatures as the weather remains dry and warm throughout the week. Arizona milk yield is rapidly increasing as weather continues to be warmer. Bottled milk intakes by schools are lower as some students are currently on spring break. Dairy processors expect to see their peak flush very soon. Milk production in New Mexico is building up following its normal course. The weather is getting warmer as days go by. As the result, farmers expect milk output to reach its peak before long. Class II demands are still on the down side as many manufacturers have enough stocks to meet processing requests. Class I sales continue to be lower with spring break around the corner.
- Fluid Milk Pacific Northwest: Milk production is seasonally climbing due to the lengthening days and slightly warmer temperatures. Milk is readily available for most processing needs. Industry contacts say the region has gotten plenty of rain and snow and should be in good shape for irrigating crops this summer. Contacts in the mountain states of Idaho, Utah, and Colorado report steady to rising milk intakes. Manufacturers say there isn't any difficulty getting enough milk for processing.
- Butter West: Cream is readily available for butter production, and manufacturers seem willing to actively churn in order to fill current orders. Domestic demand is steady, but processors say interest is light outside of contracted purchases. End users are focusing predominantly on immediate needs, buying hand to mouth as opposed to putting up large volumes of butter into storage. Inventories are generally growing seasonally. Industry contacts expect more U.S. processors will shift more butter production from print to bulk once the spring holidays pass.
- NDM East: Prices decreased on the top of the range and both ends of the mostly price series. Low/medium heat NDM production is not slowing down as milk remains readily available. The spot market was relatively active as producers attempt to clear stores of 2016 production low/medium heat NDM. Domestic demand is steady, but some end users are stocked and expect lower prices to come.
- NDM Central: Prices decreased on the top of the range and both ends of the mostly price series. Some end users report being well stocked and have no urge to take on spot market NDM. Contacts propose various factors are putting downward pressure on low/medium heat NDM including: trade concerns with Mexico, a strong U.S. dollar and projected spring flush milk surpluses. Low/medium heat nonfat dry milk production continues apace with plentiful milk supplies.
- NDM West: Prices for low/medium heat nonfat dry milk are lower, in line with downward movement in various pricing indices and recent offshore auction results. The domestic market condition is unbalanced as the current heavy NDM supply is above the sluggish buyers/end users' demand. In order to mitigate the growth of NDM supplies over the spring flush, manufacturers are offering/selling several loads at lower prices near the bottom of the price range. NDM stocks continue building as on-farm milk production ramps up toward the flush. This week, NDM spot trading activity varies as some buyers/end users postpone purchases, waiting for lower prices in the short term. Mexican NDM/SMP demand continues to be light due to currency matters and uncertainty on trade policies.
- Cheese Northeast: Manufacturing plants continue to have abundant milk volumes accessible for cheese production. Cheddar plants are running 7-day work schedules. Interest for mozzarella remains steady. Food service orders are stable to lower as schools are on spring break. Generally, cheese-buying activity is steady to lower, as some market participants hold off on purchases to see if the prices will continue to shift downward.
- Cheese Midwest: Production in the region is active, keeping pace with readily available milk. Even with spot milk as low as \$5 under Class III, cheesemakers are turning offers away as contractual milk supplies are meeting production needs. The challenge for some Midwestern cheese manufacturers is finding a middle ground between cheese production and managing cheese inventories, which are reportedly long. Demand reports are mixed. Some contacts report steadiness in retail and specialty orders following a post-Super Bowl lull. However, some Midwest cheese producers report a softness on spot orders, suggesting buyers are holding off while cheese prices continue to weaken.
- Cheese West: Milk is readily available and keeping cheese makers busy. Current cheese production is meeting most buyer requests. Some end users suggest their cheese needs are fully satisfied and they are hesitant to increase their purchases further. Cheese inventories are still heavy and available storage space is limited. Contacts suggest barrel stocks are long, and block volumes are also above current buyer needs.

#### Recommendation:

Demand weakens so prices go down, then buyers wait for a bottom. After solid demand leading into the Super Bowl, this vicious cycle has brought the dairy market down much further than we anticipated. Add to the mix the U.S. is flush with milk as we head towards the peak and things look pretty ugly right now. Spot cheese prices reached a new low for the year this week, before bouncing back slightly on Friday. Class III's finished solidly higher on the day, but not enough to erase double-digit losses for the week. In just six trading days, April Class III traded as high as \$16.23 on 03/08, before putting in an intra-day low (and new contract low) of \$14.96 yesterday, before recovering to \$15.28 today. The sell-off has been brutal, knocking out multiple levels of support. How much more downside is there? Class III futures would be not much. In fact, they predict a recovery in spot prices, which currently work out to just a little over \$14/cwt. Throw in a 50¢ NASS premium and we're still well below front month settlements. Spot prices are now low enough to attract some international interest, while dry whey and butter demand are still small bright spots in the market. Despite less than stellar production and solid demand in other parts of the world, we don't expect a substantial rally from current prices until our domestic over-supply situation slowly begins to work itself out. That won't happen, most likely, until we get past peak production. Producers with existing hedges should look to protect upside risk July-Dec using call options, which have come down in price due to the sell-off.

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