

The KDM Dairy Report – March 31st, 2017

What's Bullish:

- Spot Market: Both block and barrels cheese gained 8¢ this week, settling at \$1.52/lb and \$1.47/lb, respectively. 19 loads of blocks and 38 loads of barrels exchanged hands. NDM lost 2¢ to settle at \$0.80/lb on 3 trades, but butter saw a 1¢ increase to close at \$2.10¼/lb on 6 trades.
- Dry Whey Northeast: Manufacturing plants are working hard producing cheese up to 7 days a week, keeping whey levels high. However, there are spot limitations beyond arranged agreements and inventories are tightening. The dry whey demand is good.
- Dry Whey Central: Some contacts report export interest has increased from both

Futures Month	Class III 03/31	Class III 03/24	Change	Dry Whey 03/31	Dry Whey 03/24	Change	Cheese 03/31	Cheese 03/24	Change
Mar-17	\$15.83	\$15.82	\$0.01	52.400¢	52.000¢	0.40¢	\$1.557	\$1.557	\$0.000
Apr-17	\$15.31	\$14.99	\$0.32	50.325¢	49.100¢	1.23¢	\$1.517	\$1.499	\$0.018
May-17	\$15.75	\$15.26	\$0.49	47.725¢	45.475¢	2.25¢	\$1.580	\$1.545	\$0.035
Jun-17	\$16.01	\$15.70	\$0.31	44.525¢	43.000¢	1.53¢	\$1.625	\$1.598	\$0.027
Jul-17	\$16.59	\$16.29	\$0.30	42.500¢	41.650¢	0.85¢	\$1.696	\$1.681	\$0.015
Aug-17	\$16.85	\$16.64	\$0.21	40.750¢	40.000¢	0.75¢	\$1.738	\$1.721	\$0.017
Sep-17	\$16.96	\$16.74	\$0.22	40.975¢	39.950¢	1.03¢	\$1.747	\$1.731	\$0.016
Oct-17	\$16.86	\$16.59	\$0.27	39.750¢	38.825¢	0.92¢	\$1.747	\$1.723	\$0.024
Nov-17	\$16.78	\$16.44	\$0.34	39.000¢	37.950¢	1.05¢	\$1.740	\$1.715	\$0.025
Dec-17	\$16.67	\$16.35	\$0.32	38.000¢	37.000¢	1.00¢	\$1.731	\$1.705	\$0.026
Jan-18	\$16.56	\$16.30	\$0.26	36.725¢	35.900¢	0.83¢	\$1.721	\$1.710	\$0.011
Feb-18	\$16.51	\$16.28	\$0.23	37.500¢	36.000¢	1.50¢	\$1.722	\$1.715	\$0.007
12 Mo Avg	\$16.39	\$16.12	\$0.27	42.515¢	41.404¢	1.11¢	\$1.677	\$1.658	\$0.018

- Asia and Latin America. Domestic demand reports point to an uptick as well, adding to near term firmness.
- International: Butter prices in Western Europe firmed, as did butteroil prices. The current supply of butter in Western Europe is seasonally low. With greater consumer interest in dairy fats, some manufacturers are evaluating whether the butter market might face an undersupply situation in the coming months. In other words, butter supplies may remain in short supply during 2017. Supplying domestic markets is expected to be a priority over exports, so exports could suffer if tightness continues. Butter production in Western Europe during January this year was 1.1% lower than January last year according to Eurostat, while exports of butter during January 2017 declined 10.5%. EU imports of butter during January 2017 increased 42.1% from January one year earlier.
- NDM Central: Low/medium heat nonfat dry milk (NDM) prices were mostly steady. Spot market activity for low/medium heat NDM was active, and some large volume spot exchanges were reported again this week. Some contacts expect a near term firmness of low medium heat NDM with increased interest from international markets.
- CWT has accepted 21 requests for export assistance from member cooperatives that have contracts to sell 2.381 million pounds of Cheddar and Monterey Jack cheeses plus 52,360 pounds of butter to customers in Asia and Oceania. The product has been contracted for delivery in the period from March through June 2017.
- International: Butter prices moved higher in Oceania, following the trend in many areas of dairy fats showing price strength. New Zealand is regarded as the dominant exporter of butter globally. Some concerns are voiced as to the ability of New Zealand butter manufacturers to meet global demand if European butter exports pull back. Sellers and buyers in Oceania butter markets are much attuned to the tightness of butter supplies in Europe, substantially diminishing a potential alternative source.
- International: With one of the main dairy cooperatives closing some processing plants due to financial problems, there is uncertainty about the future of the Argentina's dairy industry. At this point, milk volumes are sufficient to process cheese, but are less than adequate to produce milk powders. Demands for cream based products such as butter, milk caramel and canned sweetened condensed milk are improving as the fall holidays approaches. However, cream supplies are seasonally tight. Thus, premiums for milk fat remain high. In 2016, farm milk production in Argentina totaled 9,895 million liters, down 13% from the previous year.
- International: In Uruguay, milk production is improving slightly, as early autumn temperatures are becoming comfortable for dairy herds. However, requests for cream from butter and milk caramel manufacturers continue to be strong on a bullish market. Uruguay farm milk volumes sent to processors in February were 112.3 million liters, 23.5% below the previous month, and 2.3% lower than a year ago.
- International: In Brazil, farm milk output is mostly variable. In some dairy basins, cow productivity remains depressed due to the effects of drought prolongation, which is decreasing the quality and availability of pastures/fodders. Overall, milk supplies are well below manufacturing needs. Fluid/UHT requests from several private and public market channels remain strong.

What's Bearish:

- Weekly cold storage numbers reflect a large build in both cheese and butter stocks in March. Over the period 03/01 through 03/27, butter stocks at USDA-selected storage centers increased 24% (4.8 million lbs) while cheese stocks jumped 12% (10.5 million lbs).
- Fluid Milk East: Milk production continues to climb throughout most of the region. For the current week, Northeast and Mid-Atlantic milk volumes continue to increase as spring flush nears. Contacts report that milk supplies are more abundant into balancing. In the Southeast, milk production is robust. Milk volumes tend to be excessive of Class I needs. As a result, manufacturers who process southeast milk note stronger milk intakes. Florida's milk production continues to leisurely climb. With spring break still in effect, Class I milk sales remain somewhat suppressed. Cream remains very accessible in the East region. Marketing agents are clearing surplus cream to Class II and Class IV plants in the East and other regions. Condense skim supplies are still heavy, prompted by Eastern milk output. Demand is slow as volumes clear to Class III and IV plants. However, suppliers find it challenging to move burdensome condensed skim loads in the East.
- Fluid Milk Central: Processing plants are reportedly at or near capacity, thus downtime is very limited. Some contacts are anxious as to what will result from a strong spring flush, with production and processing activity so strong this soon. Cheesemakers in the upper Midwest are getting spot milk offers from \$1 to \$4 under Class III. Cheese plants undergoing maintenance are cooperating with other cheese producers in order to find a home for the abundant milk supply. Once again, with an abundance of cream, butter makers in the Central region report churning cream and storing and/or selling the butter, instead of offering cream on the spot market.
- Fluid Milk Southwest: Farm milk output is up in California. Some industry contacts believe that the spring flush has started this week. Temperatures are getting nicer and more favorable to cows' comfort. Arizona's milk yield is lower, but in line with processing needs. Some contacts report that

the region is coming into the home stretch of its spring flush. In many manufacturing plants, farm milk is mostly clearing into dry lactose and nonfat dry milk. However, sales have been slower. Milk production in New Mexico continues to increase. Class II sales are slightly lower. Most balancing plants are working at full capacity and meeting processing needs. A few plants have dryer repairs and maintenance works that reduced their Class IV intakes. As a result, more condensed skim is clearing into Class III. Contacts report that some handlers have additional loads of milk and are looking for out of state sale outlets.

- Fluid Milk Pacific Northwest: Milk production is stable to higher as spring weather builds into the region. Milk intakes are strong along the coast and are a little slower to develop inland. Industry contacts believe production to grow there as well in the next few weeks. There is plenty of milk available for processing and many manufacturers are at or near capacity. Milk production in the mountain states of Idaho, Utah, and Colorado continues to climb as cow comfort improves. Pastures and hay fields are greening. Manufacturers report plenty of milk available for processing.
- Butter: The United States is heavy with cream supplies clearing to butter manufacturers who are busy churning to reduce the surplus cream supply. Product continues to be toppling producers' near term accounts. Butter inventories are building.
- Dry Whey West: Market views vary widely among industry contacts. Some market participants suggest tight inventories warrant stable to higher prices. However, others see lower international prices and future prices as signals of impending weakness in the market. Some buyers in Mexico and other Latin America countries are getting Canadian whey offers below U.S. dry whey published prices. In addition, some domestic buyers are hesitant to buy additional loads.
- NDM Northeast: At this point, buyers are mainly brokers looking for bargain prices, as most wait for market make-up to pressure prices even lower. Some manufacturing sources indicate that market improvements may be unlikely through next month, which provides a temporary bleak domestic NDM picture, particularly following last week's very brief rally. The low/medium heat NDM market undertone is steady to weak.
- NDM West: Several NDM customers have a wait and see approach, putting pressure on the market in order to get lower prices. Low/medium heat NDM production is ongoing, with some plant running at full capacity as farm milk intakes increase seasonally. As NDM inventories grow throughout the spring flush, producers are looking for NDM inventories to move continuously. Therefore, manufacturer's offers to traders and end-users are very active. NDM/SMP demand from Mexico is sluggish as SMP/NDM stocks are plentiful in this country.
- Cheese Northeast: Cheese facilities are running at full speed 7 days a week. Food service channels are stable, but with schools still out for break, institution channels are lower. Cheese trading activity continues to be light, with some traders holding off on purchases and waiting to see if the prices shift downward even more.
- Cheese Midwest: Milk continues to be available for cheesemakers in the Midwest. Reports from some cheese processors point to an inability to take on any extra spot milk. Spot milk prices have been reported from \$1 to \$4 under Class. Cheese production, with the exception of some plant updates/maintenance, has been active. Some producers are comfortable with current stocks, while others have started to sell discounted spot cheese in order to maintain inventory levels.
- Cheese West: Milk volumes are plentiful and clearing into the vats. A few cheese plants seem to be running below capacity, but for the most part, cheese processors are operating at or near full capacity. Cheese is moving well through contracts, but any additional demand is light. Orders for processed cheese are slower and some market participants are hoping for favorable spring weather to prompt the summer grilling season. Barrel cheese supplies are abundant, somewhat due to additional manufacturing plants coming on line in other regions. Industry contacts suggest warehouses are getting filled, and available storage space is hard to find. Block cheese inventories are ample.
- International: Many Western European dairy processors are expecting to return toward a more normal market in 2017. While the first half of 2017 milk production is generally expected to be lower than the first half of last year, second half production is expected to increase over the corresponding period last year.
- International: Dairy producers in Australia continue to benefit from good pasture conditions. This has slowed interest in purchasing hay, as well as the need to purchase hay. Also benefitting producers is decreasing prices for water. Concerns lie ahead associated with expectations of autumn being hotter and drier than desired. For now however, cow culling rates have slowed.

Recommendation:

Most dairy futures contracts finished solidly in the green this week as bidding in the spot market finally took cheese prices an 11-month low. That said, being the bearish fundamental picture is still out there in the near term, there was some chatter that this week's support in the spot market amounted to "window dressing" the valuation of quarter-end cheese inventories. It will be interesting to see if the support seen this week will last much beyond next week. Until the country gets past peak production and the southern regions of the USA heat up, there is going to be more than ample milk available to processors. Current spot prices work out to about \$15.00 milk. Throw in USDA survey premiums and it gets to about \$15.50, so Class III's May on out are trading a premium to cash. While we predicted more upside this week (in last week's report), it may be starting to run out of gas. While most Class III's were higher for the week, most suffered double-digit losses in Friday's trade. Producers with unprotected output should look to buy PUT options May-July to protect near-term downside risks. On the bright side, the dry whey market is still solid, and butter consumption has gone from a 40-year, to now a 50-year high, with a forecast 8% increase in 2017.

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