

The KDM Dairy Report – April 13th, 2017

What's Bullish:

- Dairy cow slaughter for the week ending 04/01 totaled 57,700 head, up a strong 11.6% vs. the same period a year ago. YTD, the dairy cull is up 2.6% (23,000 head) compared to 2016.
- Fluid Milk Southwest: Arizona milk production is steady. However, it is lower compared to last month production. Temperatures are getting warmer and may result in lower milk output toward the weekend. With the spring holiday nearby, milk requests from ice cream producers are higher. Milk output in New Mexico is increasing at a lower rate than earlier this year. Milk is becoming richer in components. Cheese processors reduced their daily milk intakes as they are running very full. Class I demand is slightly higher. Surplus milk intakes by out-of-state processors declined by a few loads.

Futures Month	Class III 04/13	Class III 04/07	Change	Dry Whey 04/13	Dry Whey 04/07	Change	Cheese 04/13	Cheese 04/07	Change
Apr-17	\$15.23	\$15.10	\$0.13	52.225c	50.525c	1.70c	\$1.498	\$1.498	\$0.000
May-17	\$15.20	\$15.10	\$0.10	48.250c	46.925c	1.33c	\$1.525	\$1.519	\$0.006
Jun-17	\$15.38	\$15.33	\$0.05	44.625c	43.500c	1.13c	\$1.563	\$1.560	\$0.003
Jul-17	\$15.86	\$15.95	(\$0.09)	40.600c	40.750c	(0.15c)	\$1.638	\$1.646	(\$0.008)
Aug-17	\$16.28	\$16.43	(\$0.15)	38.000c	39.700c	(1.70c)	\$1.698	\$1.700	(\$0.002)
Sep-17	\$16.48	\$16.55	(\$0.07)	38.100c	38.675c	(0.57c)	\$1.714	\$1.717	(\$0.003)
Oct-17	\$16.50	\$16.50	\$0.00	37.000c	38.000c	(1.00c)	\$1.719	\$1.720	(\$0.001)
Nov-17	\$16.40	\$16.46	(\$0.06)	36.600c	37.500c	(0.90c)	\$1.715	\$1.729	(\$0.014)
Dec-17	\$16.37	\$16.41	(\$0.04)	36.250c	36.825c	(0.58c)	\$1.714	\$1.720	(\$0.006)
Jan-18	\$16.26	\$16.31	(\$0.05)	35.100c	36.600c	(1.50c)	\$1.705	\$1.714	(\$0.009)
Feb-18	\$16.27	\$16.25	\$0.02	35.975c	36.000c	(0.02c)	\$1.708	\$1.714	(\$0.006)
Mar-18	\$16.26	\$16.22	\$0.04	35.300c	35.300c	0.00c	\$1.705	\$1.713	(\$0.008)
12 Mo Avg	\$16.04	\$16.05	(\$0.01)	39.835c	40.025c	(0.19c)	\$1.659	\$1.663	(\$0.004)

- International: Milk production in Australia during the current production season, which is nearing Dry end, is not expected to rebound during the remaining months. Moreover milk prices are at levels that have fueled the lower production by encouraging culling and producers leaving dairy farming. While recent prices have firmed, they are still too little to matter much in the short term to make much of a difference in milk production volumes in the near term. A significant agricultural lender has projected 2016/17 milk production to be 7% lower than the previous season.
- International: An average finish to the milk season is now expected in New Zealand. Recent heavy rains and resulting very serious flooding have slowed production. Cyclone Debbie has taken the edge off a potential stronger finish to the season.
- International: Farm milk production is mixed in Argentina due to variable weather conditions throughout the country during the past two weeks. Overall, milk intakes are enough for most processing needs. However, cream supplies remain very short on a bullish market. Milk fat premiums remain high, elevating manufacturing costs of many cheese processors. Milk output is steady in Uruguay, in line with seasonal trends. Milk intakes are adequate for processing needs. Fluid milk demands from several supermarkets and restaurants are fair to good. The competition for cream among some processors, including butter churners, is strong as supplies are very tight.
- International: European Union (EU) cheese demand from food retailers and export markets continues to increase as the holiday approaches. The demand is expected to remain high in the coming weeks, whereas inventories continue to decline to low levels. Some manufacturers have sold out their stocks of cheese. Current prices are lower, but slowly increasing. Exports to non-EU countries are steadily growing.

What's Bearish:

- Spot Market: Block cheese finished the week up 1½¢ to settle at \$1.47½/lb on just 3 trades, but heavy offers of barrels resulted in a ¼¢ lower settlement at \$1.42¼/lb on 37 trades. Butter declined 1¢ to settle at \$2.08¼ with 28 trades, but NDM managed to pick up 3½¢ on just 1 trade to close at \$0.84½/lb.
- Cheese and butter stocks continue their seasonal build. Butter holdings at USDA-selected storage centers increased 5% (1.2 million lbs) over the period 04/01 through 04/10, while cheese holdings increased 4% (3.6 million lbs) over the same period.
- Fluid Milk East: Because of the new Class 7 pricing policy, Canadian markets are no longer available for milk export volumes from some Northeast milk producers. As such, companies currently processing producers' milk shipments to Canada will no longer accept area milk volumes starting May 2017. Meanwhile, Northeast milk moving into Class I is seeing a few kickbacks, but demand is improving for Class II processing needs. In the Mid-Atlantic, balancing facilities are operating close to full as increases in milk production lead to surplus volumes clearing into those plants. Some pipelines that support Class I report drops in purchases due to upcoming school holiday closings. Southeast farm milk output continues to rise. Milk distributions into bottling plants are down. Some handlers are having to push loads West, to butter and powder facilities, as most auxiliary cheese processing plants maintain sufficient supplies of milk. Florida is very dry with reports of a number of fires. Hence, milk production has declined due to the hot spell that has stretched over the past few weeks. However, export milk shipments totaled 150 loads this week, unchanged from last week.
- Fluid Milk Central: Milk production continues briskly in the region. South Central contacts report that consistent and moderate rainfalls are benefiting crop production in areas of North Texas and Oklahoma. Current milk components are generally protein and fat heavy. Some contacts are expecting a veritable spring flush to begin by the end of April. This concerns Central milk producers, as locating new processors to take on milk is becoming increasingly difficult. Class III producers have started to turn away spot milk, reported from \$1.50 to \$5.00 under Class, due to cheese stocks being at or near capacity. Class I demand is not helping the supply situation. School districts are reportedly not ordering as much as expected following spring break, and many institutions will break for spring holidays this week and into early next week.
- Fluid Milk West: Milk production in California continues to be up. Some reports suggest that the supplies are in excess of plants' capacities. The spring flush is approaching its peak and tankers continue to be limited for milk hauling. Bottled milk demand is steady. Contacts report that raw milk will be available at discounted prices sometime this week.
- Fluid Milk Pacific Northwest: Milk production is slowly climbing. Wet conditions in March provided good amounts of moisture to get pastures and forages growing. Milk volumes are readily filling bottling and processing needs. Idaho, Utah and Colorado milk production is increasing along seasonal trends. Some industry contacts suggest the spring flush has entered into the region earlier than usual.

- Butter Northeast: Butter production remains active. The cream supply is readily available for churns. With the heavy cream loads, and active butter production, butter inventories are building. Class II is showing more demand for cream, taking some pressure off the cream supply, but the demand for butter has been quiet this week.
- Butter Central: Butter demand is mixed, but cream is readily available to butter makers in the Midwest. Butter inventories are adequate.
- Butter West: Inventories are heavy, but still manageable. Some butter production is shifting from print to bulk butter. Cream is plentiful and a few manufacturers are opting to sell off the extra cream as opposed to churning it all. Butter makers and end users are both trying to keep inventories in check.
- Dry Whey Northeast: Whey production is strong. Prices held steady on the bottom half of the range, and shifted downward a tad on the top half of the price range this week. Industry contacts have reported seeing resale loads at prices lower than published prices.
- Dry Whey Central: Prices decreased on the bottom of the range and remained steady in the mostly price series. Export interest from Asia continues, while domestic demand is limited. Spot market offers were heavy this week, although transactions were fairly light. Domestic buyers and end users continue to wait out current prices and expect the market to see some downward pressure.
- Dry Whey West: Some market participants believe that current prices are top heavy. A number of industry contacts report offers at the bottom of the price range, or even below published prices. Domestic demand is mixed. Demand has generally slackened off.
- NDM East: Prices in the mostly series are steady to lower. Farm milk output continues to increase, encouraging NDM production. As well, NDM output is receiving a boost as a few cheese plants moderate production, making more condensed skim available for drying. Stocks are building at plants, with supplies ranging from balanced to long. Spot buyers, who search around, considers purchases on the low end at most times. Those buyers also see no need to purchase too far ahead.
- NDM Central: Prices shifted lower this week. The market undertone is slightly weaker from last week. Offers from manufacturers/brokers are ample, but the demand looks to be quiet. Production is active, supported by heavy regional milk supplies. Low/medium heat NDM inventories are steady to building.
- NDM West: Buyers of western NDM are mostly interested in discounted offers. In this way, buyers continue putting pressure on the market in order to get lower prices. Inventories are steady to building.
- Cheese Northeast: Cheese production is strong in the region. With high milk availability, cheese facilities are able to take in as much as they can to fulfill production needs. Cheese inventories continue to build. Mozzarella interest is moderate, and the overall cheese supply might be overshadowing demand.
- Cheese Midwest: Production is active. Some cheesemakers have even cancelled some planned production downtime in order to keep up with the milk surplus. Readily available milk continues to flow into cheese vats. Class III spot milk prices are unchanged from last week, \$1.50 to \$5.00 under Class. Some cheese processors are hesitant about using stored nonfat dry milk to fortify their cheese because milk is so abundant. Cheese order reports vary from steady to strong. Even with some good sales reports, some contacts question whether demand will keep up with supply, as most reports point to long inventories of both block and barrel cheeses.
- Cheese West: Cheese production is increasing, but at a declining rate in the region. Sales are lower and reports suggest that people are buying only what they need. Most cheese processors are only selling contracted amounts and they have little opportunity for sales outside of contracts. Some end users have already bought and stored the cheese needed for later in the year. Export sales are picking up, but storage spaces are currently limited.
- International: Expectations are developing for higher milk production in Western Europe than had been projected several months ago. An increase for 2017 of about 0.6% is now more widely accepted as likely. This is a reflection of growing confidence of dairy producers in sustained price strength sufficient to increase herd sizes and supplement feed.

Recommendation:

Cheese stocks are heavy, especially in barrels, as we traded 37 loads in a holiday-shortened week. Arizona is the only state past its peak, with the rest of the nation still on the rise. With the loss of the UHF export market to Canada, there will be plenty of milk available in the Midwest and Northeast for a while, keeping processors busy. Meanwhile, dairy products in cold storage are at very high levels and domestic demand is good but not great. Fundamentals, then, at least for the near term, look pretty ugly. However, more bright spots are appearing as well. February dairy exports set a 21-month high, while milk production is struggling in other parts of the world (South America, Oceania). Producers in Australia and New Zealand have been suffering from low milk prices for close to two years now, so the chances of a strong recovery when their next milking season begins in Jun/Jul is not good. EU producers are being incentivized by the government to reduce milk production, with nearly 50,000 farms signing up. Cheese stocks are getting tight in the EU. Here in the U.S., we expect culling to rise as some Midwest and Northeast farms are sadly forced out of business. Uncertainty about Hispanic labor policy will keep major dairy expansions under wraps. The labor is just not there. Globally, dairy fat is still on the tighter side and in strong demand. Finally, recall that our spot market is a young cheese, or 30-day cheddar specification. Mother nature can play a big role here, giving us a situation where cheese stocks are heavy, but 30-day and under cheese gets tight due to heat. Finally, the tensions in the Middle East are ratcheting up with the U.S. retaliatory strike in Syria, a targeted bombing in Afghanistan, and a significant naval deployment near North Korea. In times of conflict, energy prices typically rise. If crude oil begins to rally, it will most likely bring grains along with it. It seems \$15 Class III is a level of support with which we bounced off this week. We think the next 3-4 weeks could keep us somewhat range-bound with the current near-term fundamentals, but the market feels like it's getting poised to make a move. Producers with existing contracts should continue to cover their upside risk in the second half of 2017. Remember, there are end users who are long hedgers in this market too. They know the same fundamentals and uncertainty facing this market, and may look to cover some of their upside risk in the weeks ahead, especially if the we've found a bottom here at these prices. Expect volatility ahead!

Note: Our offices will be closed tomorrow for Good Friday. We wish all of you a very safe and blessed Easter.