

The KDM Dairy Report – June 2nd, 2017

What's Bullish:

- Spot Market: Butter finished the week up 12½¢ to close at \$2.48½/lb on 14 trades, while NDM picked up 2¢ to close at \$0.94¼/lb on 18 trades. Barrels gained 1¢ to settle at \$1.49/lb on 35 trades, but blocks lost 3¼¢ to close at \$1.70/lb on 14 trades.
- Ag Prices Report: The April milk-feed ratio came out to 2.23, the lowest level since July, 2016, and the 4th consecutive month of declines. Generally, expansion signals get stronger above a 3.0 ratio.
- Fluid Milk East: Milk production is holding relatively steady in the Mid-Atlantic area and into New York and Southern New England. The peak of the flush appears to be on the downside in the Southeast as milk production decreases at varying rates. Florida temperatures are hot. Highs range in the 90s to 100. Hence, current conditions are advancing the drop in milk production. Ice cream production is moderate to heavy as warmer conditions in the south create better demand for the ice cream trade.
- Fluid Milk West: In California this week, many contacts report lower milk production, while others suggest that it is flat to up. In addition, some plant managers indicate that less milk is going to the dryers. Milk production continues to trend downward in Arizona due to higher daytime temperatures. Manufacturers report temperatures topping 100 degrees in some areas. In New Mexico, farm milk production is trending lower as the weather continues to be hotter. Class I interest is lower as schools close, but Class II milk orders from ice cream and frozen desert manufacturers are increasing.
- Butter Central: Churns are active, as producers are looking to pack away butter for the late summer and early fall. Class II interests continue to increase, some butter makers are expecting multiples to increase as early as next week. Retail and food service demand continues to be strong, as butter makers report increased sales week over week.
- Butter West: Butter makers are holding back on production schedules when they can. Cream is generally plentiful, but a number of processors anticipate cream supplies will tighten as summer takes hold and ice cream manufacturers pull more cream supplies. Inventories are mixed. Some manufacturers report comfortable stocks. However, in some secondary markets, butter supplies are tight. Buyers are looking for loads of butter they can buy at favorable prices and put into storage. Some end users are eager to gain coverage of late year butter needs. A few industry contacts describe demand to be better than expected for this time of year.
- NDM Northeast: Prices for low/medium nonfat dry milk shifted upward on both ends of the range and mostly price series this week. With U.S. low/medium heat NDM prices below the global market, and stable domestic trading activity, prices look to be firming. Some participants are being quoted low/medium heat NDM extended contracts at higher prices.
- NDM Central: Prices increased on the price range and mostly price series. Some contacts believe with inventories available and production ongoing, low/medium heat NDM prices are near their peak. Other contacts suggest buyers are willing to take on spot loads at current prices, as exports of low/medium heat NDM are reportedly increasing and futures markets hover near to over \$1.00.
- NDM West: Some manufacturers believe that the market is tightening. As a result, they are hedging CME prices by buying more NDM. A few contacts suggest that sales to Mexico, China, and the Southeastern markets have strengthened lately. Inventories of NDM are plentiful; however, a number of producers report having lower supplies. Production is steady to declining since many processors are making NDM to order and selling condensed skim to ice cream makers.
- Cheese Midwest: Milk is readily available for cheese production. However, cheese sales are generally strong. Packaged retail cheese, pizza cheese and specialty type cheeses are selling well. Some process cheese producers report contractually steady demand, but barrel sales are expected to pick up in line with warming temperatures. Cheese producers' reports on inventories vary. Barrel inventories are generally long. Some block producers report balanced inventories.
- Cheese West: Cheese is moving well through regular contracts, but buyers are not seeking a lot of additional loads. Some export opportunities are developing as U.S. cheese prices coincide well with international prices and the dollar has weakened a little against other currencies. A few industry contacts say warehouses are full and that warehouse operators are charging premiums for any additional space. Contacts further suggest barrels are heavy, but blocks are tight.
- CWT has accepted 25 requests for export assistance sell 3.536 million pounds of Cheddar and Monterey Jack cheese and 703,275 pounds of butter to customers in Asia, Europe, the Middle East, and Oceania. The product has been contracted for delivery in the period from May through August 2017.
- Exports: Data from the U.S. Dairy Export Council shows total dairy exports by aggregate volume in April were up 12% vs. a year ago. Butterfat led the way with a jump of 30% YoY, with cheese exports up 27% YoY.

Futures Month	Class III 06/02	Class III 05/26	Change	Dry Whey	Dry Whey 05/26	Change	Cheese 06/02	Cheese 05/26	Change
Jun-17	\$16.52	\$16.51	\$0.01	47.925¢	48.925¢	(1.00¢)	\$1.642	\$1.637	\$0.005
Jul-17	\$16.95	\$17.04	(\$0.09)	46.400¢	47.000¢	(0.60¢)	\$1.693	\$1.706	(\$0.013)
Aug-17	\$17.18	\$17.40	(\$0.22)	44.250¢	45.350¢	(1.10¢)	\$1.735	\$1.750	(\$0.015)
Sep-17	\$17.33	\$17.44	(\$0.11)	43.600¢	44.700¢	(1.10¢)	\$1.756	\$1.760	(\$0.004)
Oct-17	\$17.25	\$17.24	\$0.01	42.250¢	43.125¢	(0.88¢)	\$1.756	\$1.751	\$0.005
Nov-17	\$17.12	\$17.08	\$0.04	41.900¢	42.000¢	(0.10¢)	\$1.741	\$1.740	\$0.001
Dec-17	\$16.95	\$16.86	\$0.09	41.250¢	41.075¢	0.17¢	\$1.729	\$1.725	\$0.004
Jan-18	\$16.72	\$16.71	\$0.01	41.475¢	39.975¢	1.50¢	\$1.710	\$1.718	(\$0.008)
Feb-18	\$16.57	\$16.65	(\$0.08)	41.100¢	39.400¢	1.70¢	\$1.700	\$1.707	(\$0.007)
Mar-18	\$16.59	\$16.61	(\$0.02)	40.000¢	39.000¢	1.00¢	\$1.705	\$1.710	(\$0.005)
Apr-18	\$16.45	\$16.50	(\$0.05)	41.050¢	38.000¢	3.05¢	\$1.702	\$1.704	(\$0.002)
May-18	\$16.47	\$16.52	(\$0.05)	38.900¢	37.000¢	1.90¢	\$1.703	\$1.702	\$0.001
12 Mo Avg	\$16.84	\$16.88	(\$0.04)	42.508¢	42.129¢	0.38¢	\$1.714	\$1.718	(\$0.003)

What's Bearish:

- Fluid Milk Central: With average temperatures in the 50s in parts of the upper Midwest, cow comfort is ideal. Milk yields, consequently, are strong and remain at flush levels. Class I demand is seasonally slow with school districts beginning to break for the summer. Bottlers are preparing to scale back production. Some Central region bottlers anticipate that retail demand will help offset school breaks, as retail milk purchases typically

increase while vacationing students are at home. Cheesemakers in the Midwest are taking on spot milk loads at discounted rates. Generally, Class III spot milk ranged from \$3.50 to \$6.00 under Class.

- Fluid Milk Pacific Northwest: Milk production is edging higher. With the end of the school year, some milk intakes are shifting from bottling to manufacturing. Industry contacts report no trouble getting the milk needed for most processing needs. Milk production in the mountain states of Colorado, Utah and Idaho is strong. Milk per cow may be a little lower than previous years, but a strong crop of replacement dairy cows has helped refill milk tanks. Milk intakes are plentiful and manufacturers are having no trouble getting the milk needed for processing.
- Butter Northeast: Butter production remains active. As Class II cream demand shows strength, those processors are seemingly comfortable, for now, clearing extra cream loads to their contractual customers. Cream, however, remains plentiful, as multiples are steady to lower. Butter inventories are sufficient for near term requirements.
- Dry Whey Northeast: Prices shifted lower on both ends of the range this week. Some market individuals are trading their whey supply at lower costs to decrease inventories. Northeast cheese production is strong, leading to heavy dry whey processing. Inventories are manageable to building.
- Dry Whey Central: The spot market saw lots of offers, but completed transactions were limited. Some end users are stocked, and are confident that prices are fair and will remain in the current range for the near term. Whey producers are expressing concerns regarding inventories, which are building.
- Dry Whey West: Some manufacturers say inventories have grown from balanced to a little heavy. A few market participants suggest there may be sellers that are wanting to move significant volumes of whey stocks to clear out their supplies. Whey production is up somewhat and buyers are more willing to manage their contracts than look for extra loads of whey.
- Cheese Northeast: Cheese production is strong. Some manufacturers are running at full capacity to manage high levels of milk intakes. Cheese output is abundant and building balanced to long inventories. With the United States cheddar cheese prices below the global market, export sales are steady to improving. The market undertone is stable to improving.

Recommendation:

Class IV was the star this week as spot butter reached its highest price since Dec, 2015. And, there was good news on the export front as April numbers showed solid gains. Low U.S. prices, relative to the rest of the world, appear to be finally paying dividends in increased export opportunities. But it wasn't all good news and the U.S. continues to be plagued by overproduction and a heavy barrel cheese supply. Both blocks and barrels fell from their mid-week highs, causing Class III futures to give up much of their gains. Predicting short-term price direction continues to be a challenge under these conditions, but we remain optimistic in the long term. We're back to our old, boring recommendation for producers to take advantage of this price correction to purchase upside risk protection on existing hedges/sales to plants. With summer now upon us, there is an expectation for increased demand in the process cheese market (barrels). That could help alleviate some of the oversupply we are now dealing with. In addition, we are now past the peak in many parts of the country, with typical heat starting to set in. Milk production is going to drop from here on out. And while barrels are still in long supply, blocks are actually tight in the west. Despite the current 21¢ spread between blocks and barrels, with blocks being in shorter supply, the gap is likely to be closed with a barrel rally. If and when that happens, we could see an explosive move to the upside, thus our previously mentioned recommendation to purchase upside protection. Expect more volatility ahead as the market deals with these diverse and often opposing fundamentals!

This material has been prepared by a sales or trading employee or agent of KDM Trading, Inc. and is, or is in the nature of, a solicitation. This material is not a research report prepared by R.J. O'Brien's Research Department. By accepting this communication, you agree that you are an experienced user of the futures markets, capable of making independent trading decisions, and agree that you are not, and will not, rely solely on this communication in making trading decisions. DISTRIBUTION IN SOME JURISDICTIONS MAY BE PROHIBITED OR RESTRICTED BY LAW. PERSONS IN POSSESSION OF THIS COMMUNICATION INDIRECTLY SHOULD INFORM THEMSELVES ABOUT AND OBSERVE ANY SUCH PROHIBITION OR RESTRICTIONS. TO THE EXTENT THAT YOU HAVE RECEIVED THIS COMMUNICATION INDIRECTLY AND SOLICITATIONS ARE PROHIBITED IN YOUR JURISDICTION WITHOUT REGISTRATION, THE MARKET COMMENTARY IN THIS COMMUNICATION SHOULD NOT BE CONSIDERED A SOLICITATION. The risk of loss in trading futures and/or options is substantial and each investor and/or trader must consider whether this is a suitable investment. Past performance, whether actual or indicated by simulated historical tests of strategies, is not indicative of future results. Trading advice is based on information taken from trades and statistical services and other sources that KDM Trading, Inc. believes are reliable. We do not guarantee that such information is accurate or complete and it should not be relied upon as such. Trading advice reflects our good faith judgment at a specific time and is subject to change without notice. There is no guarantee that the advice we give will result in profitable trades. © Copyright 2017 - KDM Trading, Inc. All Rights Reserved