

The KDM Dairy Report – June 30th, 2017

What's Bullish:

- Ag Prices Report: The milk-feed ratio fell for the 5th consecutive month, coming in at 2.21 for May. That's the lowest ratio since July 2016.
- Weekly dairy cow slaughter numbers were higher than a year ago for the ninth straight week. 53,600 head were culled during the week ending 06/17, up 7.6% vs. last year.
- Fluid Milk Southwest: Farm milk production in California dropped slightly this week. Some market participants report seeing a higher decrease in milk produced last week. A number of dairies in Central California are looking for high quality hay from northern California, Utah, and Idaho. According to California Department of Food and Agriculture, May 2017 pool receipts of milk in the state total 3.32 billion pounds. This is 2.2% lower compared to the same month a year ago. Milk output is down in Arizona as the state reached very high temperatures last week and part of this week. According to some industry contacts, this month milk production is on average 3% down compared to last month. The butterfat in milk has started to decrease as well. High volumes of cream are currently moving into ice cream and frozen dessert manufacturing. In New Mexico, milk production is seasonally slowing down. Manufacturers are adequately balancing any milk not used by bottlers.
- Butter Northeast: Print butter sales are active as retail channels advertise butter in weekly announcements. Cream multiples are strong as manufacturers have a high demand for cream. Inventories are adequate for contractual needs. With milkfat in high demand, butter prices are showing strength in domestic and global markets.
- Butter Central: Salted butter supplies are adequate but unsalted volumes are considered tight in some channels. The market is preparing for lower trending milk production and butterfat declines to deter available cream. Hence, in the next few weeks, the producers expect that cream will be readily absorbed into Class II ice cream operations, prompting reductions in churning rates. Some buyers note this as a cause of the premium butter price. Bulk butter prices linger at 4 to 7 cents over the market. The market undertone is steady as prices continue to firm.
- Butter West: Seasonal demand is making cream supplies tighter. Some butter processors are choosing to slow their butter churns and sell off their cream to ice cream and other Class II manufacturers because of the strong milkfat prices. Butter inventories are seasonally high, but manufacturers are managing stocks closely to assure they have the butter needed to meet the expected high Q3/Q4 demand. End users also are very much aware of year-end butter needs. Buyers are eager to secure butter for current and future requirements. Some industry contacts suggest a few end users are seeking quotes for available butter into 2018.
- Foreign cheese: The market undertone for cheese in the European Union (EU) is strong. The demand from retailers and the industrial sector is still up. Exports to Southern European countries continue to grow. Cheese availability is limited. Processors have already sold out their supplies to contractors and are not taking additional requests from new customers. Larger volumes of milk are currently going into the manufacturing of cheese. However, the quantity produced is still not enough to fulfill all the demand. Manufacturers are struggling to find the components needed for extra cheese production. Due to weather conditions, the quantity of milk delivered and the components in milk are expected to decrease.
- CWT has accepted 10 requests for export assistance to sell 1.695 million pounds of Cheddar cheese to customers in Asia, Central America, the Middle East and Oceania. The product has been contracted for delivery in the period from June through September 2017.
- International: May milk output in Australia was down 2.8% vs. May '16, and down 7.6% YTD (July-Jun), according to Dairy Australia stats.

Futures Month	Class III 06/30	Class III 06/23	Change	Dry Whey	Dry Whey 06/23	Change	Cheese 06/30	Cheese 06/23	Change
Jul-17	\$15.72	\$16.05	(\$0.33)	45.350¢	46.300¢	(0.95¢)	\$1.572	\$1.593	(\$0.021)
Aug-17	\$16.58	\$16.97	(\$0.39)	42.000¢	43.750¢	(1.75¢)	\$1.673	\$1.704	(\$0.031)
Sep-17	\$16.73	\$17.16	(\$0.43)	39.450¢	41.050¢	(1.60¢)	\$1.705	\$1.730	(\$0.025)
Oct-17	\$16.93	\$17.20	(\$0.27)	38.350¢	39.750¢	(1.40¢)	\$1.735	\$1.755	(\$0.020)
Nov-17	\$16.97	\$17.12	(\$0.15)	38.250¢	39.425¢	(1.18¢)	\$1.737	\$1.745	(\$0.008)
Dec-17	\$16.80	\$16.96	(\$0.16)	38.000¢	39.175¢	(1.18¢)	\$1.729	\$1.740	(\$0.011)
Jan-18	\$16.55	\$16.68	(\$0.13)	37.875¢	38.025¢	(0.15¢)	\$1.713	\$1.725	(\$0.012)
Feb-18	\$16.55	\$16.65	(\$0.10)	38.075¢	38.250¢	(0.17¢)	\$1.719	\$1.725	(\$0.006)
Mar-18	\$16.53	\$16.65	(\$0.12)	38.250¢	38.250¢	0.00¢	\$1.710	\$1.722	(\$0.012)
Apr-18	\$16.44	\$16.53	(\$0.09)	38.750¢	38.750¢	0.00¢	\$1.703	\$1.710	(\$0.007)
May-18	\$16.40	\$16.60	(\$0.20)	38.300¢	38.300¢	0.00¢	\$1.707	\$1.714	(\$0.007)
Jun-18	\$16.62	\$16.62	\$0.00	38.325¢	38.325¢	0.00¢	\$1.721	\$1.728	(\$0.007)
12 Mo Avg	\$16.57	\$16.77	(\$0.20)	39.248¢	39.946¢	(0.70¢)	\$1.702	\$1.716	(\$0.014)

What's Bearish:

- Spot Market: Block cheese finished the week 1½¢ lower, settling at \$1.52½/lb with 23 trades. Barrels gave up 1¼¢ to close at \$1.35¼/lb on 36 trades. NDM inched ¼¢ down to close at \$0.84½/lb on 10 trades, but butter gained 5¼¢ on 10 trades to settle at \$2.64¼/lb.
- Weekly cold storage numbers indicate cheese stocks increased 4% (4.5 million lbs) over the period 06/01 through 06/26. Butter stocks increased 10% (3.2 million lbs) over the same period.
- Fluid Milk East: Weather patterns are contributing to the steady to slightly lower milk production trend, while further south, heat and humidity levels are affecting farm milk production. However, producers and handlers indicate milk volumes remain substantial, as reports for milk output, in general, stand above previous year levels. Handlers perceive that volumes during the upcoming July 4 holiday period are expected to be heavy into balancing, with active diversions from multiple milk channels to those plants. Operations are likely to run at/near capacity into the first of next week.
- Fluid Milk Central: Farm milk output in the region is steady to lower. However, supplies off the farm remain plentiful, although not as full as previous stages of the flush. Fluid milk sales are sluggish, as school breaks reduce bottling needs. Milk supplies into manufacturing are decreasing, but the likelihood of intakes increasing for some processing facilities are strong, in light of the July 4 holiday. This week, reported milk discount prices range \$1.00 to \$3.50 under Class in spot markets. Surplus volumes of milk could rise over the extended holiday period.
- Fluid Milk Pacific Northwest: Milk intakes are in good balance with processing needs, with generally plenty of milk to go around. Seasonal weather is providing good cow comfort and forages are in sufficient supply and quality. In the mountain states of Idaho, Utah and Colorado, manufacturers report plenty of milk for most processing needs. Processors are operating facilities at or near full production schedules.

- Dry Whey Northeast: The market is showing a bit of weakness as prices dipped at the top and bottom of the range. This week, dry whey spot markets are seeing active trading between buyers/sellers, as some manufacturers clear bulk product with contractual customers taking additional loads. Dry whey supplies are adequate to heavy. The dry whey undertone reveals a softening market.
- Dry Whey Central: The whey market is somewhat stagnant. Whey is moving satisfactorily through contracts, but spot sales are a little harder to come by. A few end users suggest their needs are mostly met through existing contracts and they do not have any desire to take on more whey. In some cases, they would like to unhinge from their existing contracts or push back on shipped loads. Inventories are generally long.
- Dry Whey West: Domestic demand is adequate to move some volumes, but exports are near impossible unless the whey is priced in the lower end of the range. Combined, domestic and international demand are not able to fully keep pace with supplies. Whey production is active and in line with cheese production.
- NDM East: Prices slipped on both ends of the price range and mostly price series this week. Spot sale pricing is decreasing in the market. With milk supplies still long in parts of the East, low/medium heat NDM production is strong as dryers are running on full schedules. Inventories are manageable to long. Interest is steady to weakening as a number of market participants as some dairy industry individuals are in a watch and see approach to the spot prices. The market undertone is showing weakness.
- NDM Central: Prices dipped across both price series this week. Spot transactions have been irregular, but offers remain in good quantity. Low/medium heat NDM production is active as dryers are operating on steady schedules. Inventories are available for contractual needs. The low/medium heat NDM market undertone is unsettled as some market participants do not anticipate changes to near term weakness. Overall, the tone is leaning generally towards a buyer's market.
- NDM West: Prices shifted down on both ends of the price range and the mostly price series. Various f.o.b spot prices and price basing indices moved lower this week. Demand for NDM is mainly steady, although ice cream manufacturers are taking on a few more loads. Spot sales are fair. Production is regular, and inventories are still at elevated levels.
- Cheese Northeast: Eastern cheese manufacturers are not seeing any notable departures from the previous week's production rates. Milk supplies are fairly stable at adequate levels. Interest for natural and process cheeses is somewhat quiet. Sources report some movement on Swiss cheese, as the July 4 holiday approaches. Cheddar cheese interest is slow to fair, catering generally to replacement needs. Inventories are growing.
- Cheese Midwest: Although extra loads of milk are not as prevalent as they were over the last few weeks, some cheese makers report loads of distressed milk are still available at \$1 to \$3 below Class. Manufacturers report running full schedules, but intakes have eased back a load or two. There is an expectation of more available loads over the Fourth of July holiday and cheese makers will have to weigh the pros and cons of taking on any additional milk. Demand is mixed. Some contacts say curds and readily consumed product orders are strong. Some processors report demand from other food manufacturers and food service businesses is steady and cheese continues to move well through regular contracts. And finally, a few other industry contacts think cheese orders are lackluster. Inventories are heavy for both blocks and barrels.
- Cheese West: Cheese inventories continue to be long for both barrels and blocks. Industry contacts say cheese loads with a little more age are proving harder to move. Domestic demand is fair. Food service requests are perhaps slightly lower, but retail demand is steady. Cheese seems to be moving well through regular contracts, but end users are not asking for a lot of extra loads. Industry contacts hope the price differences between U.S. and international markets can help spur on some additional sales, but large volumes of exports have yet to materialize. Production is active and is pushed on by plentiful milk supplies.

Recommendation:

Block and barrel cheese supplies remain long in the U.S. as strong cheese output combined with average demand is keeping inventories high. Barrels put in a 13-month low at \$1.35/lb, before catching a slight bid on Friday. While summer heat has arrived in the southern regions of the country, the Midwest, where cheese output is concentrated, cows have enjoyed temperatures 10-15 degrees below normal. This has allowed spring-type milk output to persist longer than usual. The 10-day forecast for the area is finally calling for warmer temps, but there will be plenty of excess milk over the July 4th holiday weekend. Contrast that to the EU, where cheese demand is strong, supply is tight and manufacturers cannot meet new interest. But unfortunately, it appears export opportunities for the U.S. have been slow to materialize. There is some hope as some reports state that China will need to begin buying powder more aggressively in the second half of the year. Butter continues to be well supported. The market has been depressed longer than we anticipated, but we still think the longer-term move is higher. Recall, April settled at \$15.13, which was the low of the year, and since then have had two higher settlements. June might turn out to be another low month, but we think international demand will begin to help prices from there. The dairy cull rate also continues to increase, which will hopefully help the U.S. turn the corner on its increasing cow numbers.

Note: We will be open on Monday from 7:30am until noon, when the markets will close early. We will be closed all day on Tuesday in observance of Independence Day, and reopen Wednesday morning. Have a safe and happy 4th!

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