

The KDM Dairy Report – July 7th, 2017

What's Bullish:

- Spot Market: Block cheese finished the week 2¼¢ higher, settling at \$1.55¼/lb on 7 trades. Barrels gained 2¼¢ to close at \$1.37¼/lb on 19 trades. NDM increased 2¼¢ to settle at \$0.86¼/lb on 22 trades, but butter decreased 5¼¢ to close at \$2.58½/lb on 26 trades.

Futures Month	Class III 07/07	Class III 06/30	Change	Dry Whey	Dry Whey 06/30	Change	Cheese 07/07	Cheese 06/30	Change
Jul-17	\$15.58	\$15.72	(\$0.14)	46.650¢	45.350¢	1.30¢	\$1.549	\$1.572	(\$0.023)
Aug-17	\$16.48	\$16.58	(\$0.10)	43.600¢	42.000¢	1.60¢	\$1.658	\$1.673	(\$0.015)
Sep-17	\$16.76	\$16.73	\$0.03	41.150¢	39.450¢	1.70¢	\$1.699	\$1.705	(\$0.006)
Oct-17	\$17.00	\$16.93	\$0.07	40.000¢	38.350¢	1.65¢	\$1.739	\$1.735	\$0.004
Nov-17	\$17.01	\$16.97	\$0.04	39.500¢	38.250¢	1.25¢	\$1.742	\$1.737	\$0.005
Dec-17	\$16.84	\$16.80	\$0.04	39.150¢	38.000¢	1.15¢	\$1.732	\$1.729	\$0.003
Jan-18	\$16.63	\$16.55	\$0.08	38.525¢	37.875¢	0.65¢	\$1.715	\$1.713	\$0.002
Feb-18	\$16.58	\$16.55	\$0.03	38.675¢	38.075¢	0.60¢	\$1.720	\$1.719	\$0.001
Mar-18	\$16.56	\$16.53	\$0.03	38.500¢	38.250¢	0.25¢	\$1.714	\$1.710	\$0.004
Apr-18	\$16.47	\$16.44	\$0.03	38.750¢	38.750¢	0.00¢	\$1.712	\$1.703	\$0.009
May-18	\$16.47	\$16.40	\$0.07	38.300¢	38.300¢	0.00¢	\$1.714	\$1.707	\$0.007
Jun-18	\$16.61	\$16.62	(\$0.01)	38.325¢	38.325¢	0.00¢	\$1.724	\$1.721	\$0.003
12 Mo Avg	\$16.58	\$16.57	\$0.01	40.094¢	39.248¢	0.85¢	\$1.702	\$1.702	(\$0.000)

- The recent heatwave that hit California overwhelmed a rendering plant in the Fresno area, according to several news articles this week. County authorities were allowing dairy farmers to compost or bury hundreds of carcasses due to the plant not being able to handle the volume of dead animals.
- Fluid Milk Northeast: Milk production is easing throughout the East region. Off-farm loads are lighter weights, with some haulers consolidating routes. Contacts note milk intake tests for butterfat and protein content are lower.
- Fluid Milk Southeast: In Florida, hot weather has taken a toll on cows and milk output. The number of milk loads shipped out of state for processing has dropped significantly over the past few weeks. In most other parts of the region, temperatures and humidity are rising as well. Less than burdensome milk supplies are moving into manufacturing for processing. The fluid cream market is steady to strengthening. Supplies are not as available, with good demand. Soft serve demand is improving as hotter weather encourages interest up and down the East coast. Cream churning is lighter at most butter plants.
- Fluid Milk Southwest: In California, warmer weather conditions are negatively affecting cows' milk output. Production is declining according to some processors, and milk butterfat is also lower. Bottlers' intakes are seasonally down. In Arizona, the weather is predominantly hotter for cows' comfort. As so, milk yield is trending down. In New Mexico, milk production is seasonally lower.
- Butter Northeast: The demand for retail butter in the East is very good as sales have been heavy from the holiday festivities. Cream multiples are stable as manufacturers in Class II and IV have high demand for cream. Butter prices are strong in the global market. Domestic bulk butter prices are 5-7 cents over the market of the CME Group.
- Butter Central: Producers report storing butter for upcoming upticks in demand. Butter inventories are building, but producers are comfortable with current levels. However, some producers report that unsalted inventories are a bit light. Butter contacts expect cream to resume its recent tightness post-holiday, when other processing plants go back to regular schedules.
- Butter West: Cream supplies are less available as the seasonal demand from Class II manufacturers is active. Butter production is stable to light. With the strong milkfat price, a number of butter makers have reduced butter production to market their cream. Some manufacturers are overseeing inventories steadily to confirm adequate butter supply for future demand. A handful of market participants are securing butter for current and Q3/Q4 needs. In addition, a number of end users are looking into available butter for 2018.
- Exports: The U.S. Dairy Export Council reported dairy exports reached a two-year high in May. Strong exports to Mexico, as well as record shipments of cheese, accounted for the increase. Sales to Mexico were 71% higher than a year ago, while cheese exports were up 75%, followed by NDM up 62%. Total dairy exports in May worked out to 14.7% of U.S. milk production.
- International: EU farm milk production declined from January to April 2017. However, during the same period, cheese production was prioritized over other dairy products and saw a 1.1% increase compared to the previous year. Cheese inventories remain low as demand continues to be higher. Exports to South America are growing. Orders from Asia and other countries are larger as well. Domestic demand is strong. Currently, cheese buyers are more likely to cover their short-term needs than usual. Prices for the month of July are strengthening at the highest end of the price curve.
- International: Rabobank dairy analyst Sandy Chen says milk output in China is on the decline, and summer heat is likely to increase the need for imports. At the same time, dairy consumption is increasing at a rate of 2 to 2.5% per year. After a two-year absence from global markets, China's appetite for dairy imports is returning.
- International: Milk production in the primary milk producing areas of Western Europe is declining seasonally. Preliminary estimates are that milk production in Germany during the second to last week of June, declined 0.8% from the previous week. In France, the estimate is that production declined 3.3% from the prior week. Continuing very hot weather since then is believed to have further taken a toll on milk production.
- International: Butter prices in Western Europe strengthened at each end of the price range for the ninth consecutive report period. It is believed that a number of domestic European buyers have not yet covered butter needs for later in 2017. EU butter averaged a U.S. equivalent \$2.92/lb in June, up 120% vs. a year ago.

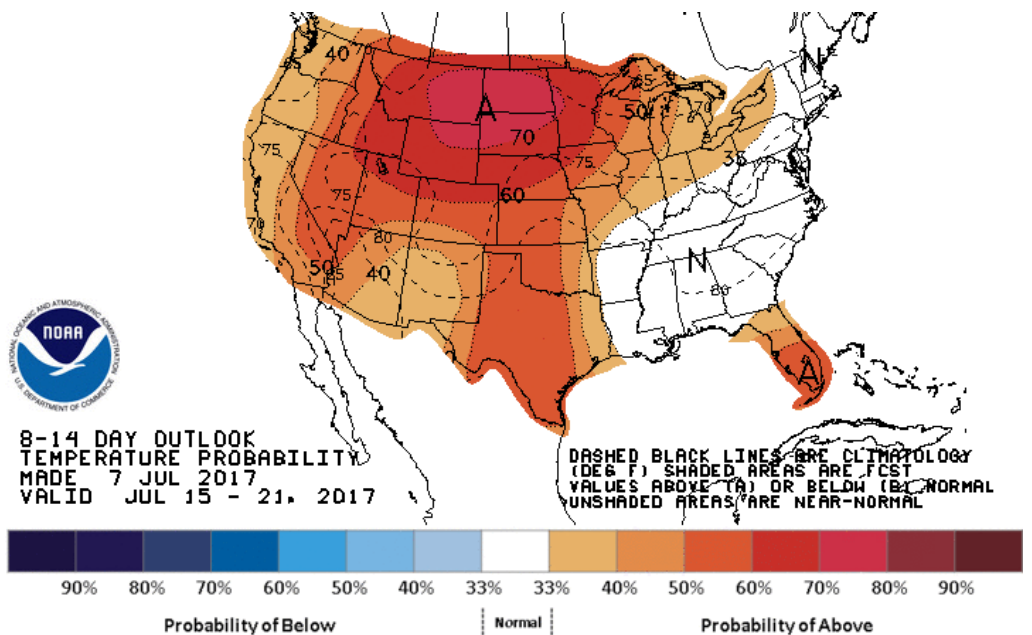
What's Bearish:

- Dairy Products Report: Cheddar cheese output in May jumped 6.9% compared to a year ago, while total cheese output was 4% higher. As we have been doing most of the year, the May output number is a new all-time high. While cheese output was higher, butter production in May was down 1.5% vs. May '16.
- Fluid Milk Central: Milk production in the Midwest remains steady. Warming temperatures have tapered milk yields slightly, but some contacts suggest that relative to other regions, Midwestern milk production is maintaining significant yields. Fourth of July plant closings have kept milk at bargain rates for multiple types of processing outlets.

- Fluid Milk Pacific Northwest: There is an adequate supply of milk for processing activities. Pasture and range conditions are good to excellent in 64% of Oregon and 77% of Washington. In the mountain states of Idaho, Utah, and Colorado, milk is readily available for processing needs. Manufacturing plants are working at near or full capacity.
- Dry Whey Northeast: Demand for dry whey remains moderate and intermittent as some buyers note waiting for prices to move lower. The market mostly defines the undertone as weak.
- Dry Whey Central: Prices slightly declined on the top of the range, but held steady on the mostly price series. Whey buyers continue to receive discounted offers from large producers on the Eastern seaboard. Domestic demand is steady to increasing. Producers of sought after brands of whey are seeing low inventories, elsewhere inventories remain plentiful.
- Dry Whey West: The market undertone is weak. Demand is good, although not enough to keep up with production. High volumes of dry whey are being produced due to an increase in cheese output. Inventories continue to grow from day to day. Some industry contacts suggest that manufacturers are having a hard time moving dry whey. They claim that competitive European prices are hindering U.S. sales into the international market.
- NDM East: Prices shifted lower on the top of the range price series. With milk supplies available in the region, low/medium heat NDM production is operating on steady schedules. Inventories are adequate for contractual needs. The demand is showing signs of weakness as some market participants are not looking to buy low/medium heat NDM and are watching to see where the prices will go. The market tone has softened.
- NDM Central: Production is ongoing, at fairly active rates. Inventories are available for contractual obligations and are fairly balanced according to most producers in the Midwestern region. The low/medium heat NDM market undertone is steady, with signs of softening.
- NDM West: Prices moved lower on the bottom of the price range and stayed steady on the mostly price series. Inventories are fair to plentiful in most parts of the West. Production is active; however, it is expected to start declining as the summer advances. The market undertone is weak, but starting to settle.
- Cheese Northeast: Milk supplies remain at levels that encourage active cheese output at some plants. Other cheese plants are adjusting their production schedules as surplus milk receipts decline and milk solids weaken around the seasonal factors. Inventories are sizable in some instances. A forethought of some market participants is the uncertainty of when prices will trend higher and how much coverage is in place for near term needs. Cheddar demand is fair with offerings available from most producers.
- Cheese Midwest: As milk production has begun to taper in the Midwest, cheese plants continue to take in spot loads at \$1.00 to \$3.00 under Class. Cheese production continues to be strong, with a little more time for plant maintenance as milk intakes are not as heavy as they were during spring flush. Cheese demand is somewhat steady. Some mozzarella producers, and other pizza cheese producers, report orders are meeting seasonal expectations. Most reports on cheese inventories, particularly process cheeses, are long.
- Cheese West: Cheese production is strong due to higher volumes of milk available to processors. Although they are mostly limiting their intakes to contractual needs, cheese demand from end-users/buyers is good. Food services are taking in fewer loads. Supplies are plentiful for barrels and blocks and keeping processors busy.
- This week's GDT auction saw the dairy index decline 0.4%, its second consecutive loss. Cheddar cheese declined 3.2% to a U.S. equivalent \$1.84/lb.
- International: Milk production continues to increase in most countries of the Southern Cone of South America. During the last two weeks, the dry climate and comfortable temperatures for dairy herds have dominated the aforementioned areas. Manufacturing milk intakes are expected to increase in the coming few days. Compared to a few weeks ago, cheese production is more active, mainly prompted by higher regional milk intakes. The cream market is starting to stabilize as supplies become more available. In general, the dairy industry in the Southern Cone of South America continues to recover from past rains/floods and is in better shape, compared to a few months ago.

Recommendation:

U.S. dairy prices have been low enough, long enough, to finally start generating some export business. A lot, in fact, as May dairy exports reached a two year high. It's quite likely that June exports will be similar, if not better. Multiple sources now concur that China is likely to step up its buying in the second half of the year, due to lower domestic milk output and depletion of powder stocks. With globally strong butter prices helping, NDM and dry whey appear to be forming a bottom. The 8-14 day forecast is calling for above normal temperatures across much of the nation. We could see prices begin to firm even more quickly if significant heat arrives. Finally, grain prices have seen some solid gains, led by spring wheat. Feed costs could be on the rise if weather fears persist. We continue to recommend producers cover their upside risk on existing 2017 contracts with call options. For unsold milk, they can be used as triggers to sell, with upside risk already mitigated. We continue to recommend holding off on marketing any 2018 milk. Have a great weekend!



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