

**The KDM Dairy Report – June 1<sup>st</sup>, 2018**

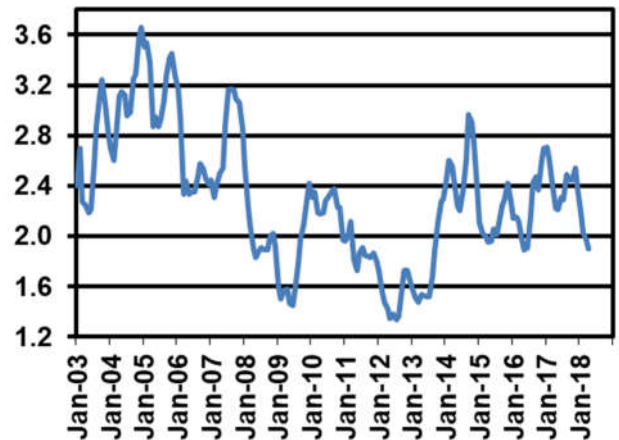
SPOT MARKET	5/25	6/1	Change	Trades
Cheddar Blocks	\$1.6100	\$1.5975	(\$0.0125)	7
Cheddar Barrels	\$1.5450	\$1.5200	(\$0.0250)	26
Butter	\$2.4150	\$2.3775	(\$0.0375)	65
Grade A NDM	\$0.8425	\$0.8250	(\$0.0175)	6
Dry Whey	\$0.3725	\$0.3850	\$0.0125	9

Futures Month	Class III 05/25	Class III 06/01	Change	Dry Whey	Dry Whey 06/01	Change	Cheese 05/25	Cheese 06/01	Change
Jun-18	\$15.67	\$15.49	(\$0.18)	30.425¢	30.200¢	(0.23¢)	\$1.663	\$1.648	(\$0.015)
Jul-18	\$16.35	\$16.23	(\$0.12)	33.950¢	33.950¢	0.00¢	\$1.708	\$1.698	(\$0.010)
Aug-18	\$16.75	\$16.79	\$0.04	35.500¢	35.500¢	0.00¢	\$1.741	\$1.747	\$0.006
Sep-18	\$16.92	\$16.96	\$0.04	36.000¢	35.450¢	(0.55¢)	\$1.753	\$1.761	\$0.008
Oct-18	\$16.83	\$16.83	\$0.00	35.700¢	35.575¢	(0.13¢)	\$1.743	\$1.750	\$0.007
Nov-18	\$16.64	\$16.63	(\$0.01)	36.000¢	35.125¢	(0.88¢)	\$1.725	\$1.732	\$0.007
Dec-18	\$16.55	\$16.44	(\$0.11)	35.750¢	34.900¢	(0.85¢)	\$1.715	\$1.719	\$0.004
Jan-19	\$16.24	\$16.16	(\$0.08)	36.175¢	34.600¢	(1.58¢)	\$1.694	\$1.698	\$0.004
Feb-19	\$16.18	\$16.10	(\$0.08)	35.500¢	34.075¢	(1.43¢)	\$1.690	\$1.695	\$0.005
Mar-19	\$16.10	\$16.08	(\$0.02)	35.725¢	35.050¢	(0.68¢)	\$1.691	\$1.696	\$0.005
Apr-19	\$16.09	\$16.10	\$0.01	36.200¢	35.000¢	(1.20¢)	\$1.690	\$1.693	\$0.003
May-19	\$16.23	\$16.14	(\$0.09)	36.200¢	34.675¢	(1.53¢)	\$1.694	\$1.698	\$0.004
<b>12 Mo Avg</b>	<b>\$16.38</b>	<b>\$16.33</b>	<b>(\$0.05)</b>	<b>35.260¢</b>	<b>34.508¢</b>	<b>(0.75¢)</b>	<b>\$1.709</b>	<b>\$1.711</b>	<b>\$0.002</b>

**What's Bullish:**

- Cheese stocks at USDA-selected storage centers declined 1% over the period 05/01 through 05/28.
- Ag Prices Report: The milk-feed ratio for April was 1.90, the lowest level since May 2016 (see graph).
- Outlook for U.S. Ag Trade Report: USDA forecasts higher dairy exports for 2018, raising their estimate by \$200 million to a total \$5.8 billion, due to the higher pace of shipments of milk powder, cheese and whey products in Q2.
- Dairy cow slaughter for the week ending 05/19 totaled 54,500 head, up 4.6% vs. the same period a year ago.
- Fluid Milk Southwest: California milk output is steady to down this week. Hotter climatic conditions are starting to somewhat impact total milk output levels. Although milk supplies were abundant over the Memorial Day weekend, it was handled well, with limited issues noted. Arizona farm milk production trends are down. In New Mexico, milk production is mostly even, though warmer weather conditions are present in the state and are impacting milk fat and solid contents.
- Butter Northeast: The butter market continues to be bullish. Bulk butter trades, in the region, are 5 to 8 cents over the CME Group, with various time periods and averages used. The market, in general, continues to move higher with improved exports and rising global prices. Producers' inventories tend to be in good shape.
- Butter Central: In the upper Midwest, butter makers report that cream is unexpectedly tight. Buying interest remains generally healthy in both salted and unsalted varieties.
- Butter West: Production remains active, although ice cream manufacturers are pulling more cream. Butter inventories are growing, but industry contacts say current domestic demand is solid, as indicated by lively participation in the butter spot market and regular calls to manufacturers.
- Dry Whey Northeast: Prices moved up on the bottom of the range in the Northeast this week. Even with the shortened trading week, many buyers are purchasing regular spot loads. Inventories are steady to tight, as contracts and spot sales are taking up the majority of supplies. Moreover, some manufacturers are not able to offer spot loads at this time. The demand is strong as industry contacts continue to purchase whey at higher prices. The market tone is firm.
- Dry Whey Central: Dry whey remains difficult to find in the region, and around the country, as a growing number of buyers and end users relay that spot loads are becoming difficult to come by. As a result, producers are firmer with spot prices. After a slow pre-holiday trading week, reported Central whey prices climbed this week in all facets. Some producers report that spot supplies will not be available through the month of June, and some producers in the southern Central region have suggested that lower milk output due to heat has them scrambling to find adequate milk supplies. Dry whey market tones are somewhat bullish, as supply is not keeping up with current demand.
- Dry Whey West: Prices are higher on the range and the mostly price series. Sales are good both in the export and domestic markets. As market players expect whey prices to further increase in the forthcoming period, they are working on locking in Q3 contract coverages. Dry whey inventories are mostly tight, but remain in check. Overall, the market undertone is strong.
- Cheese Midwest: Cheese demand is steady to slower for most types of processors. However, cheese curd makers are an exception. The seasonal return of outdoor events, such as fairs and street festivals, has renewed cheese curd buying vigor.
- Cheese West: Cheese output is active as more fluid milk clears to cheese plants, yet the cheese market seems to be balanced. Cheese inventories are up, but staying manageable. Domestic and international sales are both solid. The U.S. cheese market is currently very competitive as U.S. cheese prices continue to be below international prices.
- Foreign Cheese: The German semi-hard cheese market is firm. Cheese requests from all sale channels have remained high. Export sales to southern European holiday countries are good. Stocks for some types of cheese are below seasonal norms. Reports suggest that sellers are demanding higher prices in current hard cheese price negotiations.
- CWT accepted offers of export assistance to sell 202,825 lbs of Cheddar cheese, 1,661 million lbs of butter and 2,646 million lbs of whole milk powder, to customers in Asia, Europe, the Middle East and Oceania. The product has been contracted for delivery in the period from May through October 2018.

**Milk-feed Ratio**



- International: New Zealand plans to cull as many as 150,000 head of dairy cattle in an attempt to eradicate mycoplasma bovis. The loss of cows could cause a 3% drop of that country's milk supply.

### What's Bearish:

- Geopolitical: The EU, Mexico and Canada have announced plans to impose retaliatory trade measures affecting certain U.S. products, in response to the Trump administration's announced tariffs on steel and aluminum imports. The list from Mexico included "various cheeses". Currently Mexico is the largest imported of U.S. cheese.
- USDA's new Dairy Margin Protection Program will now cover up to the first 5 million lbs of milk production (about the amount a 300 cow dairy produces in one year), and was made retroactive to Jan 1<sup>st</sup>. For just 14¢/cwt, producers can receive \$8 margin protection, guaranteeing a payment through at least June. With the average herd size in Wisconsin at 148 cows (April 2018 data), much more than half of the nation's second largest milk producing state will be eligible for these payouts.
- Butter stocks at USDA-selected storage centers have increased a strong 19% over the first 14 days of May.
- Fluid Milk Northeast: Milk production in the region is higher. Milk loads are heavy and available for processing needs. Class III manufacturers report cheese operations are at capacity and still have pressure to clear extra milk loads. Class I sales are lower due to educational institutions closing up for the school year. Some cream salvage and tolling are happening in the region. Mid-Atlantic milk production is moving up. Balancing operations are running on full schedules.
- Fluid Milk Southeast: Market participants report milk production has been dropping. When there are upticks in production it seems to go right back down. However, with less milk going into bottling, manufacturing plants are receiving heavy loads for near to full capacity.
- Fluid Milk Central: The Memorial Day weekend heatwave may have caused the spring flush to be short lived. Milk production is expected to dwindle near term. That said, this week milk for all uses was widely available. Cheesemakers are taking advantage of the surplus as Class III milk prices were reported at \$5 under. More cheese producers relayed taking on spot milk loads this week.
- Fluid Milk Pacific Northwest: Milk production in the region is strong, but the peak of spring flush appears to be in the rearview mirror. Industry contacts report there is still plenty of milk for most processing needs. Bottling demand has slowed somewhat as schools let out for the summer. As a result, milk handlers are shifting more milk loads toward manufactured dairy products.
- Cheese Northeast: Cheese makers are receiving heavy milk loads, and production schedules are at near to full capacity. Moreover, some market participants report more pressure to take extra milk loads when there is a local oversupply. Cheddar cheese processing is fairly steady and inventories are stable to increasing. Cheddar cheese demand from retail stores is steady to a tad higher as the holiday kicked off the grilling season. Provolone and mozzarella production are stable. There are reports of stable sliced provolone orders, but mozzarella orders are a bit lower as schools are letting out for the summer.

### Recommendation:

The dairy markets started the holiday-shortened week on an upswing, as 90-100 degree weather hit even the Midwest. Ideas that the heat might prematurely shorten the peak in an already tight butter/cream market helped boost futures. However, the U.S. announcement that it would be slapping tariffs on imported steel and aluminum was met with an announcement by Mexico that it would retaliate with a tariff on cheese. With Mexico being our biggest dairy export destination by far (see graphic), markets were quick to react and reversed course. In addition, the new Dairy Margin Protection Program is deeply flawed. By making it retroactive to Jan 1, it's like allowing someone to buy car insurance AFTER they've had an accident, on the taxpayer's dime. While it's noble to want to protect smaller family farms, by guaranteeing profitability for some, the government enables false market signals for these producers to keep making more milk, while we are still dealing with a national milk glut. Crazy, and it exacerbates the problem. But, it is the market we have to deal with. Current spot prices work out to just \$15.28/cwt. Even adding 50¢ basis for NASS survey numbers leaves Class III futures, July on out, at a large premium. With tariffs hanging over the market and smaller producers protected to some extent, the near term now feels heavy, unless we get a good helping of heat across the country. Producers should consider buying PUT options July-Aug to buy some time and allow the market to work through these new fundamentals. The tariffs announced by Mexico are only "proposed" at this point, and as we have seen with China, may never happen, should NAFTA negotiations make new headway. In the meantime, uncertainty reigns.

U.S. DAIRY EXPORTS, TOP 10 MARKETS		
<i>in millions</i>		
	2017	change vs. prior year
Mexico	\$1,312	+8%
Southeast Asia	\$690	+3%
Canada	\$636	+1%
China	\$577	+49%
Japan	\$291	+41%
South America	\$288	+3%
South Korea	\$280	+21%
Oceania	\$258	+50%
Middle East/North Africa	\$234	+21%
Caribbean	\$221	+3%

*Source: U.S. Dairy Export Council, USDA.*

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