

**The KDM Dairy Report – August 3<sup>rd</sup>, 2018**

SPOT MARKET	7/27	8/3	Change	Trades
Cheddar Blocks	\$1.5200	\$1.5875	<b>\$0.0675</b>	3
Cheddar Barrels	\$1.5200	\$1.4750	<b>(\$0.0450)</b>	52
Butter	\$2.2625	\$2.3200	<b>\$0.0575</b>	25
Grade A NDM	\$0.8175	\$0.8275	<b>\$0.0100</b>	21
Dry Whey	\$0.4250	\$0.4350	<b>\$0.0100</b>	0

Futures Month	Class III 07/27	Class III 08/03	Change	Dry Whey	Dry Whey 08/03	Change	Cheese 07/27	Cheese 08/03	Change
Aug-18	\$15.02	\$14.88	<b>(\$0.14)</b>	35.450¢	35.750¢	<b>0.30¢</b>	\$1.564	\$1.557	<b>(\$0.007)</b>
Sep-18	\$15.64	\$15.68	<b>\$0.04</b>	36.500¢	36.500¢	<b>0.00¢</b>	\$1.626	\$1.629	<b>\$0.003</b>
Oct-18	\$16.13	\$16.18	<b>\$0.05</b>	35.700¢	37.025¢	<b>1.33¢</b>	\$1.678	\$1.683	<b>\$0.005</b>
Nov-18	\$16.08	\$16.23	<b>\$0.15</b>	35.750¢	37.000¢	<b>1.25¢</b>	\$1.676	\$1.685	<b>\$0.009</b>
Dec-18	\$15.92	\$16.02	<b>\$0.10</b>	35.475¢	36.075¢	<b>0.60¢</b>	\$1.666	\$1.672	<b>\$0.006</b>
Jan-19	\$15.74	\$15.79	<b>\$0.05</b>	34.925¢	36.000¢	<b>1.08¢</b>	\$1.645	\$1.652	<b>\$0.007</b>
Feb-19	\$15.57	\$15.60	<b>\$0.03</b>	34.800¢	35.150¢	<b>0.35¢</b>	\$1.640	\$1.642	<b>\$0.002</b>
Mar-19	\$15.54	\$15.56	<b>\$0.02</b>	34.650¢	35.000¢	<b>0.35¢</b>	\$1.633	\$1.633	<b>\$0.000</b>
Apr-19	\$15.72	\$15.70	<b>(\$0.02)</b>	34.450¢	35.100¢	<b>0.65¢</b>	\$1.654	\$1.643	<b>(\$0.011)</b>
May-19	\$15.83	\$15.87	<b>\$0.04</b>	33.975¢	35.100¢	<b>1.13¢</b>	\$1.670	\$1.662	<b>(\$0.008)</b>
Jun-19	\$15.92	\$15.99	<b>\$0.07</b>	34.100¢	35.675¢	<b>1.58¢</b>	\$1.680	\$1.670	<b>(\$0.010)</b>
Jul-19	\$16.17	\$16.08	<b>(\$0.09)</b>	33.100¢	36.000¢	<b>2.90¢</b>	\$1.700	\$1.693	<b>(\$0.007)</b>
12 Mo Avg	FALSE	<b>\$15.80</b>	<b>\$15.80</b>	<b>34.906¢</b>	<b>35.865¢</b>	<b>0.96¢</b>	<b>\$1.653</b>	<b>\$1.652</b>	<b>(\$0.001)</b>

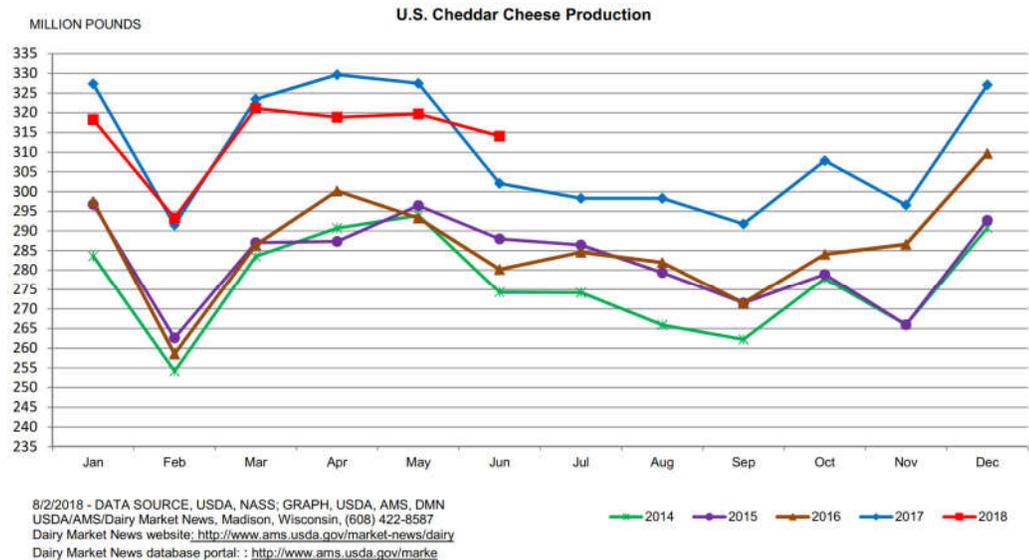
**What's Bullish:**

- Ag Prices Report: The June milk-feed ratio came in at 1.98, up from 1.90 last month, but still well below a level that would encourage expansion.
- Fluid Milk Northeast: Temperatures have been manageable compared to recent weeks, although milk volumes are still down. Class I sales are steady to gradually picking up as some bottling facilities are preparing for schools to reopen soon. Mid-Atlantic balancing plants are in fairly good balance with milk production as volumes are lower and operations have space for more milk.
- Fluid Milk Southeast: Milk volumes are a little bit lower as storms and humid weather dampen the area. Many facilities are not receiving adequate milk loads for their production needs. Moreover, many manufacturers are not able to fulfill their customers' requests. Class I sales have increased and bottlers are receiving the majority of milk loads as schools are reopening. Florida's milk production is still dropping as the weather is hot and cow comfort is decreased. Class I sales have increased as schools are about to be back in session. There are reports of milk staying in the area for production needs.
- Fluid Milk Central: Cheesemakers who received some deeper discounts this week are not expecting those same lower prices next week. Cream markets remain steady to strong, as supplies are being pulled in myriad directions. Ice cream makers, particularly soft serve producers, are pulling more cream than suppliers expected this late in the summer.
- Fluid Milk Southwest: In California, milk output is still low. Milk output is not expected to drop significantly below its current levels for the rest of the summer. Arizona farm milk production continues at a lower rate. Humidity caused by the monsoons, accompanied by higher temperatures, is contributing to an uncomfortable environment for cows' wellbeing. Most schools in the state are back from the summer break. As a result, milk intakes for Class I have increased throughout the week as school pipelines get filled. Climatic conditions have been impacting New Mexico milk yield. This week, milk production has decreased, but remains in line with seasonal norms.
- Butter Northeast: Production is somewhat limited to a few large operations that have commitments to fill. Stable demand, as some buyers resume regular buying patterns, combined with slower churning as cream circumvents butter makers, pinches some of the region's butter stocks. Generally, supplies are in close balance. Food service consumption is seasonally good, particularly in resort areas.
- Butter Central: Butter makers continue to sell cream back onto the spot market in lieu of churning. With cream supplies remaining tight, and some scheduled plant maintenance in recent weeks, packaged/print butter availability has tightened. Salted butter is being sought after with more interest than unsalted varieties. Butter producers maintain that retail/food service sales are meeting summer expectations. Midwestern butter industry participants' outlooks regarding the fall market are mixed, but more lean bullish than not.
- Butter West: Tighter cream stocks are restricting butter manufacturing as ice cream and butter makers compete for available loads of cream. Issues with trucks' obtainability combined with higher temperatures are making it tougher to move cream in some areas. Furthermore, some butter processors are selling part of their cream to take advantage of higher cream premiums and to save on butter storage handling. As a result, butter stocks, although still abundant, are not building.
- Dry Whey Northeast: Prices inched slightly higher this week. Spot activity is active as buyers are frequently purchasing loads. Additionally, market participants are requesting extra loads from manufacturers. Furthermore, some traders are seeking specific brands, as their customers have a high interest in certain dry whey currently. Manufacturers' supplies are balanced to tight, as regular and spot load customers are buying weekly loads and inquiring for additional loads. Some operations are not able to offer extra loads. As a result, many market participants are sourcing via resellers. Market conditions are stable and many dairy contacts note seeing a solid demand for dry whey.
- Dry Whey Central: Offers are shifting toward the \$.40+ target, while end users who are stocked and/or contractually covered for the near term are taking a step back. Dry whey inventories are generally reported as tight, although some contacts suggest condensed whey drying has recently started to increase. Dry whey market tones are gathering strength in the near term.
- Dry Whey West: Prices continue to march higher. Heavy global milk production, trade issue concerns, and a whey product recall have made for a tempestuous dairy market this summer. However, dry whey buyers have not been reticent with their purchases. In particular, favored brands are seeing strong demand. Some industry contacts suggest they could sell more dry whey if they had it. Inventories of dry whey are tight.
- NDM Northeast: Markets pushed NDM prices higher this week, leaving a few buyers puzzled. Nonetheless, markets were abuzz with active trades taking place as prices increased, on average, \$0.0150 at the upper and lower points in both DMN pricing series. Production levels have declined around lesser fluid milk supplies and good condensed skim sales. Inventories are considered adequate to tight, depending on the source, and held with extreme confidence.
- NDM Central: Prices shifted up in all positions on a busy spot market. Market participants in the Central region have suggested that a number of trades/offers are nearing or in the mid-\$.80s. Production has seen a slowdown, as condensed skim, while still available, is not as abundant as it was in the spring. Recently dried low/medium heat NDM loads are reportedly tightening.

- NDM West: Prices for low/medium heat NDM have raised on both ends of the range and the mostly price series. The market seems to be strengthening. Customers are looking into buying fresh low/medium heat nonfat dry milk, which is currently tight in the market. According to many contacts, sales have been strong this week due to large domestic buyers purchasing more low/medium heat nonfat dry milk to guarantee coverages. Buyers from neighboring countries that were withdrawing from the U.S. nonfat dry milk market due to new tariff regulations are coming back to some extent. Current low/medium heat nonfat dry milk production is steady to decreasing in that condensed skim stocks are tight.
- Foreign Cheese: Recent heatwaves in some parts of the EU have affected total farm milk output. As the result, cheese production has been steady to decreasing this week. Cheese sales to domestic and international customers have remained active. New cheese orders are coming from newly acquired market share, giving an extra boost to demand. However, the downside is that inventory levels are lower and cannot satisfy all short-term demand, somewhat limiting spot trading activities. The European Union cheese market undertone is currently firm.
- Cheese Midwest: Pizza cheesemakers are gearing up for heavier sales as schools/colleges prepare to open their doors, and as football season draws near. Cheese curd producers report steady to strong sales, while barrel producers saw an uptick in interest late last week. A majority of spot milk purchases moved closer to flat market. The reported range was \$3 under to \$1 over Class III. Cheese producers who took on discounted spot milk do not expect the same deals next week.
- CWT accepted offers of export assistance to sell 908,305 lbs of Cheddar cheese and 14.495 million lbs of whole milk powder going to customers in Asia and Oceania. The product has been contracted for delivery in the period from August through December 2018.
- International: Drought conditions in some Northern European countries has begun to affect overall milk production. While EU milk production was up 1.7% in May, the increase percentages are expected to moderate when June and July data become final, due to unusually hot weather.

### What's Bearish:

- Dairy Products Report: Cheddar cheese output in June was 4% higher than a year ago, while total cheese output was up 1.8% YoY. Butter output increased 3.1% vs. last June, but dry whey output declined 0.7% and NDM production was off 9%.
- Dairy cow slaughter for the week ending 07/21 totaled 56,100 head, down 1.2% vs. the same period a year ago.
- Weekly cold storage numbers show both cheese and butter stocks at USDA-selected storage centers increased over the period 07/01 through 07/30. Butter stocks climbed 3% (1.3 million lbs) while cheese stocks were 2% (1.8 million lbs) higher.
- Fluid Milk Pacific: In the mountain states of Idaho, Utah and Colorado report milk supplies remain long. Milk production is relatively steady and heavy. While much of the region has had a run of very hot days, nights are cooler, to the point of cows being able to eat, drink and recharge for the next day. Manufacturers are getting more than enough milk. Some heavily discounted loads are finding homes in surrounding states, often with the added pain of freight charges. Dairy contacts say feedstocks are ample and of good quality.
- Cheese Northeast: Despite heat that continues to engulf the area, cheese makers report receiving enough milk to run at full production. There are reports of domestic cheese demand picking up. Cheddar and provolone cheese interest in retail and restaurant sectors is stable, as grocers are advertising 8-ounce cheddar cheese at a discount and restaurants' provolone orders are fairly strong. Mozzarella demand has increased as educational institutions are resupplying their inventories for the start of school. Although cheese demand is higher, overall cheese inventories are steady to higher, as Northeast cheese production is strong.
- Cheese West: Manufacturers say they have plenty of milk for cheese vats. Even with summer heat suppressing milk volumes and components, cheese production has been active. The statistics suggest cheddar stocks are in relatively good balance, while mozzarella and hard Italian cheeses are long. Industry contacts say some manufacturers are planning to shift production back to cheddars to try to bring the composite cheese portfolio into better balance. Cheese purveyors describe demand as not good enough.



### Recommendation:

July Class III final settlement was \$14.10/cwt, it's lowest close since 2010. Trade talks continue to dominate headlines, with hope coming from the idea that a bilateral resolution with Mexico may happen in August, but little hope of a resolution with China, as new and increasing tariffs were announced this week. However, while there will undoubtedly be an export price to pay, product is still moving offshore, and it appears some buyers are coming back. Everything but barrels finished high in this week's spot market, with the word "tight" starting to be used to describe everything from cream, to dry whey, to fresh NDM, to butter. Some schools are already open in the south, with more and more opening in the coming weeks. Football season is around the corner. Meanwhile, producers' budgets were made leaner by their July milk checks. The rubber band keeps getting stretched. Jan – Jun 2019 Class III contracts all settled under \$16/cwt. We just don't see how that can remain, but maybe we're missing something. At a minimum, we see more upside risk than downside risk at those prices, so would not recommend producers locking in milk at those levels. Current spot prices work out to about \$14.90 Class III; then accounting for NASS survey premium, call it \$15.40 or so. So Sep-Dec '18 are carrying a premium to the spot market, but not a lot. With milk beginning to tighten and butter/powder seeing an active bid, perhaps we will continue to see the fall months edge higher. Producers should consider buying call options Sep-Dec to protect existing contracts, or to "sell in to" should a rally occur. It's high time!