



Horizons.

Our insights
on Today's Global
Dairy Business

July 2022

#02

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Market Direction

**Return to milk
production growth
gets postponed
further.**

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**Scarce European SMP production
rebounding closer to normal numbers
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Editorial Note.

Salutations!

Thank you all for your positive feedback and words of encouragement for our launch of the New Hoogwegt Horizons last month!

This month, we revisit the milk production numbers and concluded that milk production recovery is simply going to take longer than expected. However, with the pace of Chinese imports at the moment, prices are getting some reprieve. We will also discuss demand-side factors on our markets, and do a quick Bull-Bear analysis.

This issue will also see guest contributor Adnan Mikati from our Chicago Office chime in on his experiences in working at Hoogwegt, and some interesting news on our Hoogwegt sponsorship of the Wageningen Student Rowing Club Argo.

We hope you enjoy this July edition of the Hoogwegt Horizons as much as we enjoyed putting it together.

Sincerely,
Hoogwegt Horizons Editorial Team

Market Direction

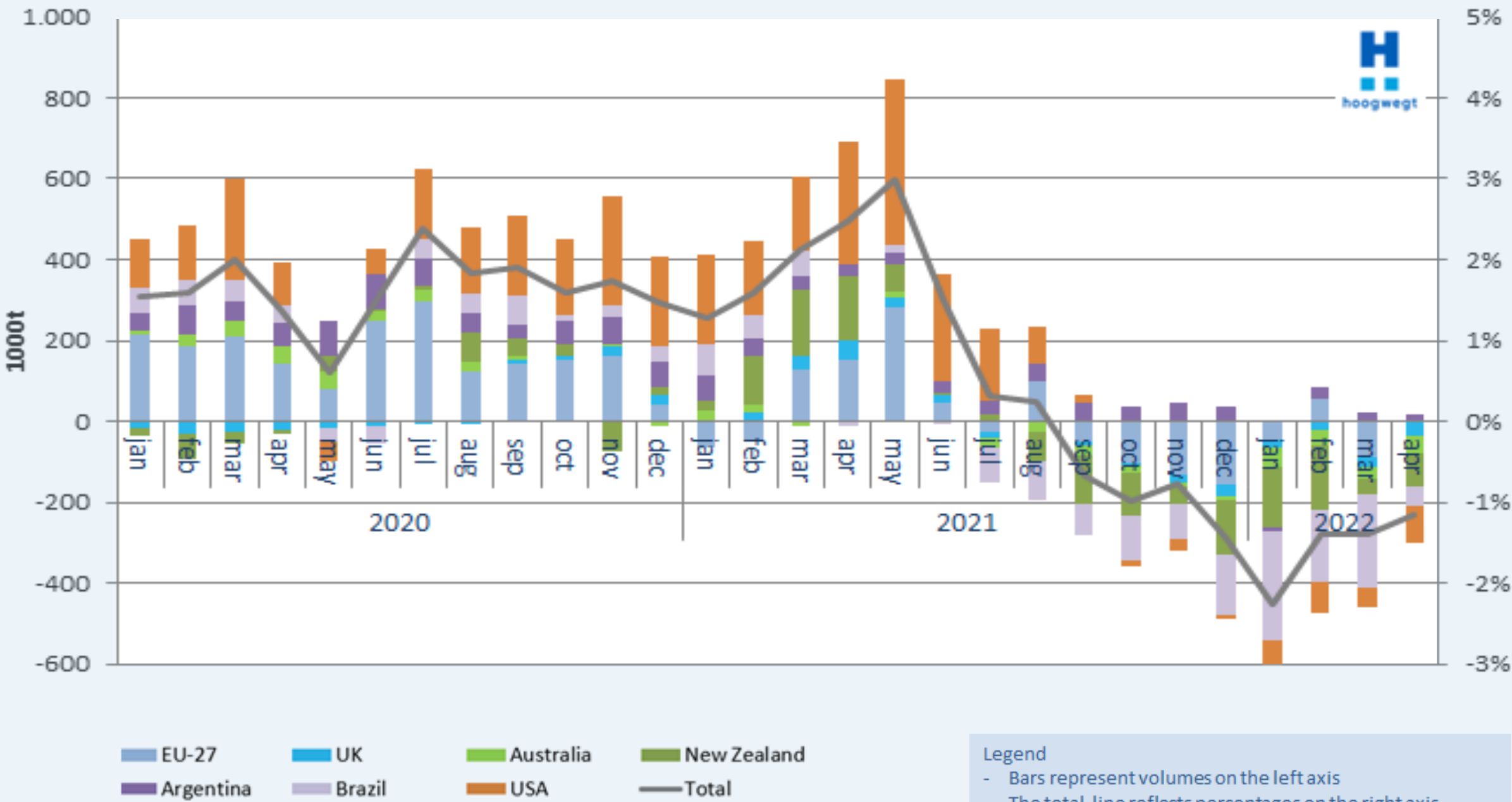
Return to milk production growth gets postponed further.

All major export regions continue to report weak milk supply numbers. US milk production in May was down by 0.7% and weekly June data for the main EU production regions and the UK also indicate continuation of the negative growth rate for all of H1 2021. Brazilian milk production was also much lower than expected in Q1, mostly due to adverse weather.

When Brazilian self-sufficiency declines it usually implies that it will diminish the regional exportable surplus as more Argentinean and Uruguayan exports are expected to remain within the region instead of being exported to the world market. With the Oceania season also ending very weak and a Northern hemisphere summer that has yet to begin, buyers have very little relief to expect from the supply side in the near term.

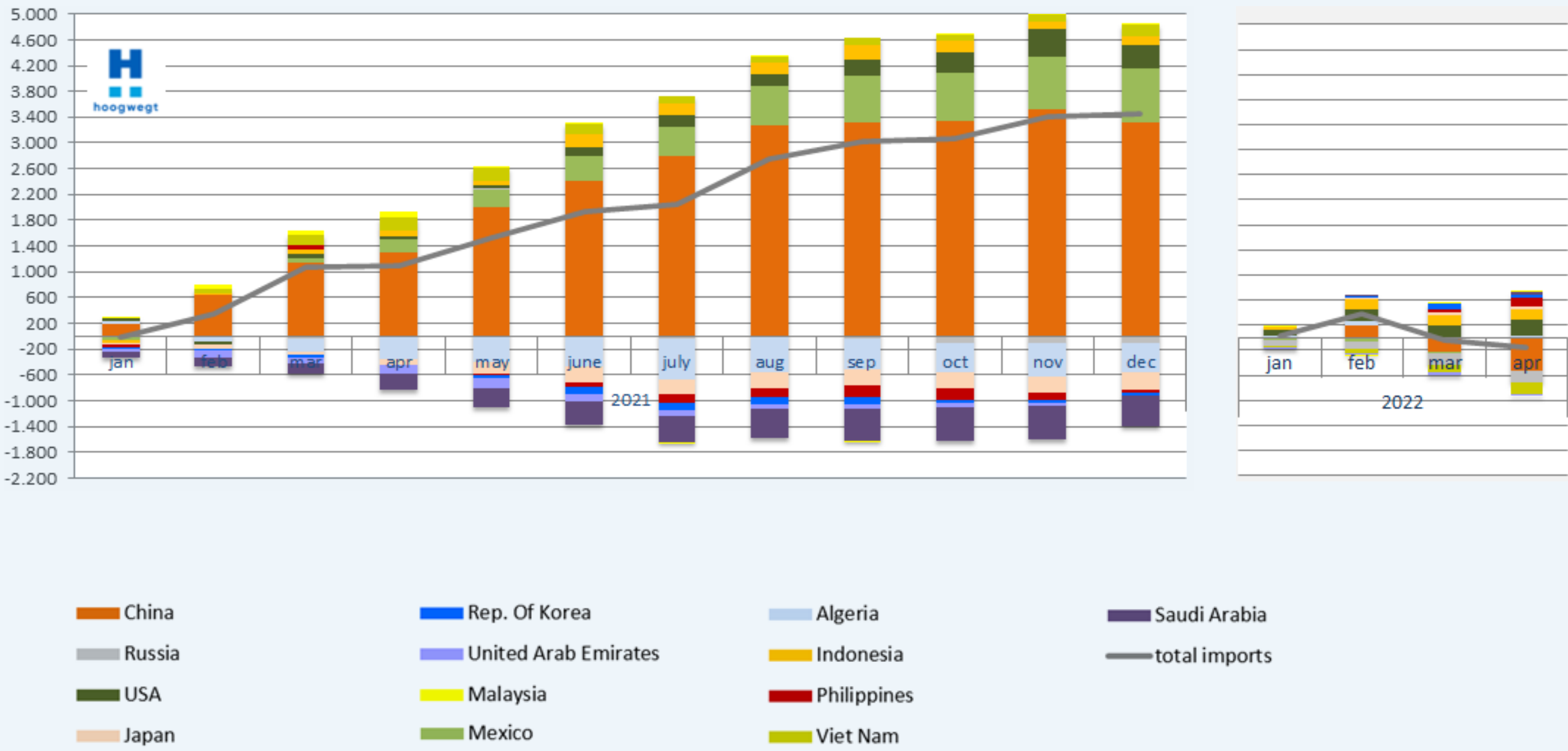
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Milk supply growth in key exporting regions (Y-o-Y change, 1000t)



Legend
- Bars represent volumes on the left axis
- The total-line reflects percentages on the right axis
NB: February 2020 numbers have been leap day corrected
Source: local production statistics reworked by Hoogwegt

Imports by the big-13 importing countries
(cumulative change compared to previous year, total imports in 1000t of MEQ)



NB: The graph displays monthly cumulative changes in import volumes compared to last year for each single country. The grey line is the total cumulative change compared to last year for all 13 countries combined
Source: Dairyntel trade data, reworked by Hoogwegt

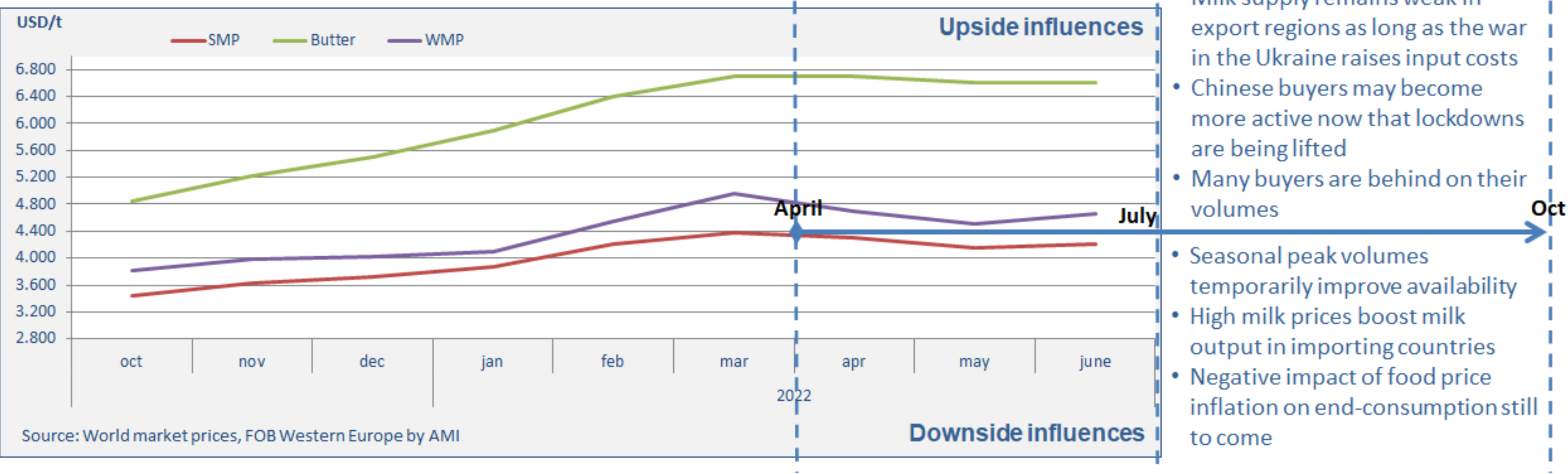
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Despite the US, Mexico and most SE Asian importers increasing their imports compared to last year, total imports by the top-13 importing countries is falling further behind 2021-comparables. Throughout April and May China's May imports were negatively affected by the lockdowns and logistic challenges and this situation may continue for a while. Working capital limitations even forced some local distributors to sell stocks back into the market. For Jan-May all products are considerable behind on last year's numbers except for whole milk powder – which is still the main product category – and lactose. As long as Chinese imports remains relatively weak, Asia Pacific's market balance remains as it is. However, a strong import performance in H2 will definitely also require stronger Oceania supply.

Looking forward

Price movements have become smaller in recent weeks. Fundamentally there are still several developments that could inject new upward price momentum into the market. Firstly, milk supply in both the EU and the US tends to be vulnerable during the summer weeks of July and August. Secondly, it remains to be seen if China's imports remains as lackluster as they have been in the first half of 2022. Thirdly, the buy-side has been focused on the short term for a long time now and buy-side buffers are reportedly very low. Still, sellers seem to be OK with the current price levels and do not feel the need to hurt the buy-side even more. Buyers of course wouldn't mind some further price moderation but the market fundamentals give them very little arguments as long as demand does not really drop away yet. ■

Market Outlook for July – September 2022



Dairy Deep Dive

Scarce European SMP production rebounding closer to normal numbers while Domestic consumption in the Western world is a mixed bag.

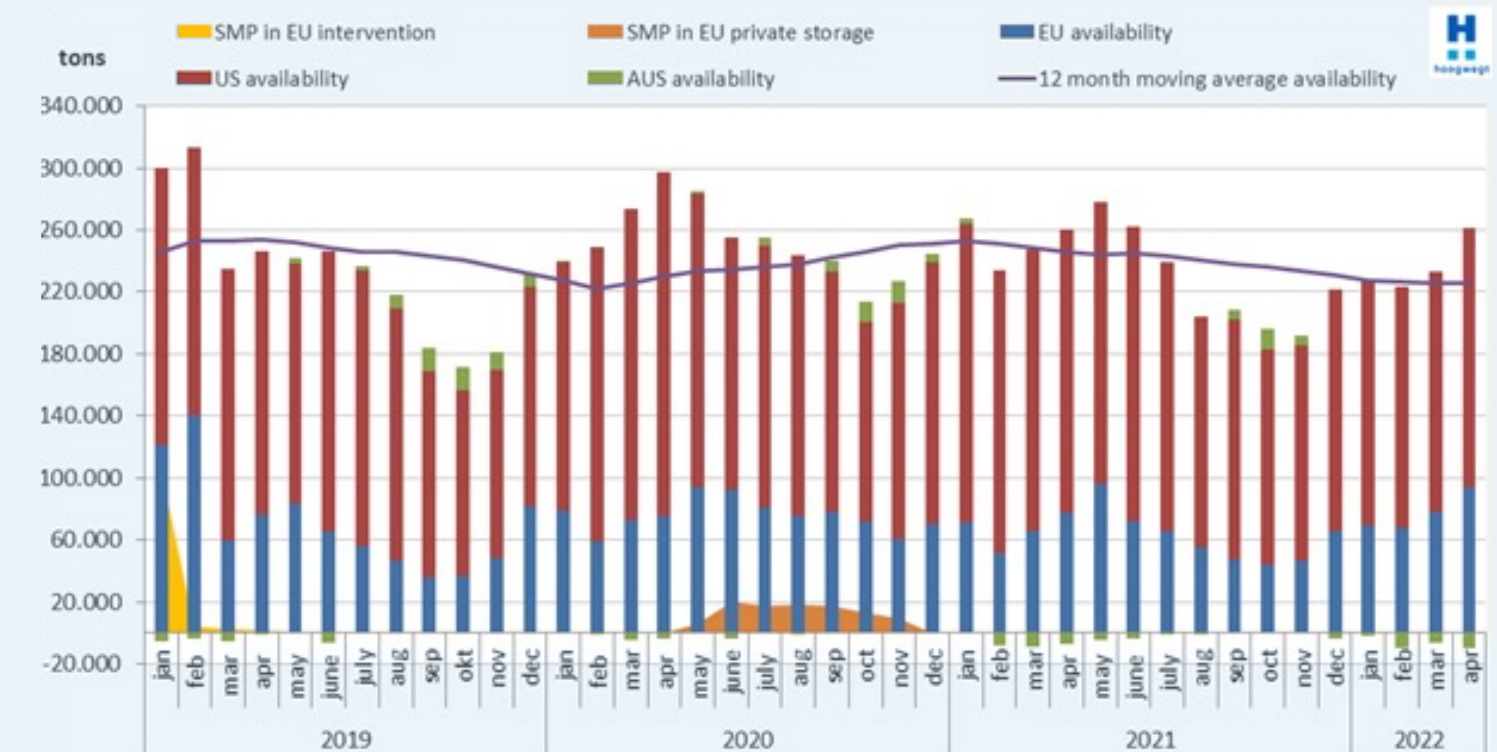
Production

Historically when valorization favored a product for a few months, more of the available milk was used to produce that product group. We recently saw the first sign that this is happening to European SMP in March and April.

At turn of Q1 and Q2 2022 a closer to normal amount of milk went towards SMP after months of decrease, at the cost of cheese production. That could be explained that there was a bit more milk available from the flush, and that it had valorized quite well. Apparently despite the costs to dry. If it continues it could add 100+Kt (+15% YoY) to this year's SMP production, so it's something to keep an eye on, as it's also at the cost of cheese production. US NFDM/SMP production still seems a bit low, almost 15% of the for manufacturing available milk went to NFDM/SMP, while that's usually 16+%. US produced 101Kt in March (-7Kt YoY), April (105Kt NFDM+SMP) showed NFDM production to be up slightly (+1% YoY) but US SMP decreased significantly (-37% YoY). EU produced 133Kt in March (-3Kt YoY) and around 140Kt in April (-4Kt YoY).

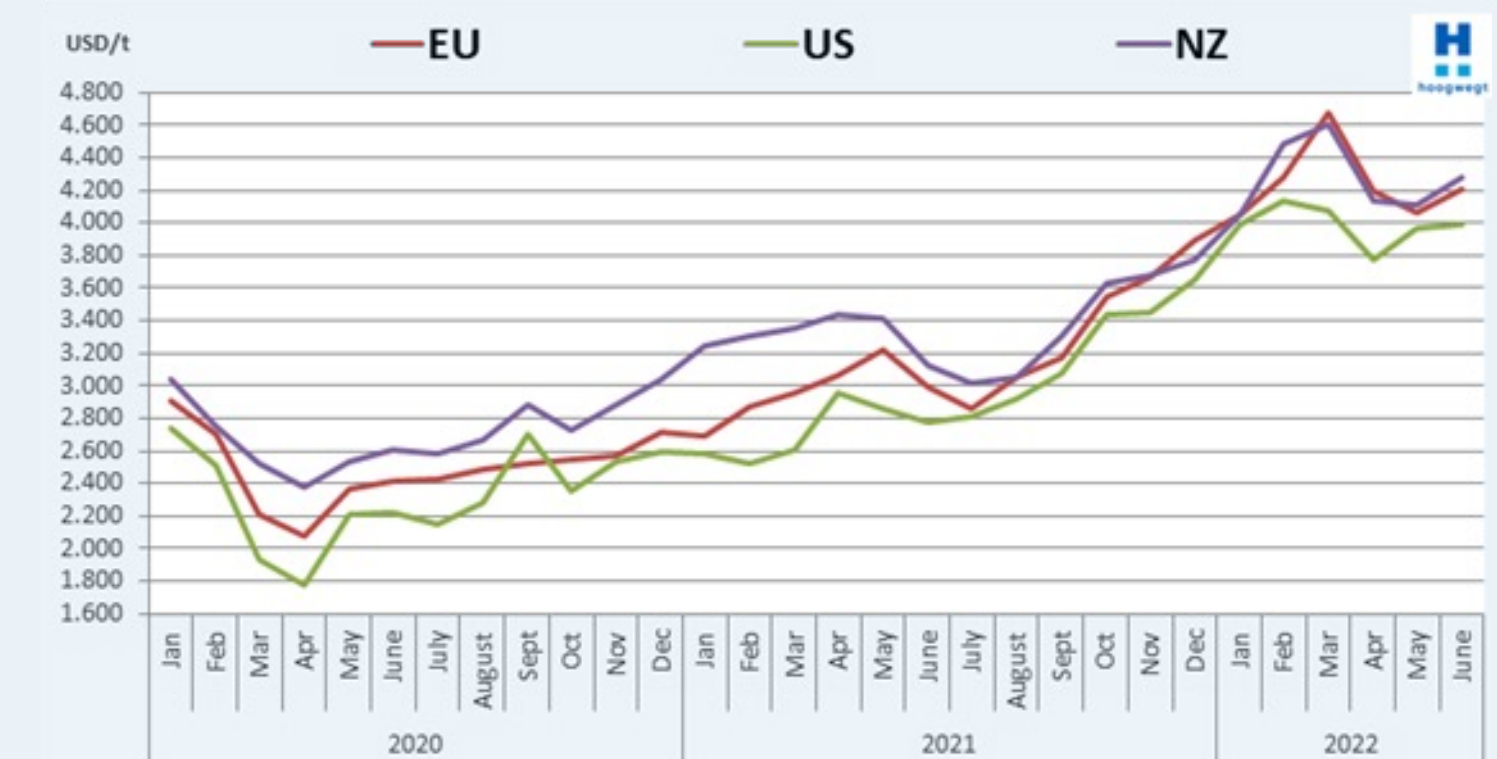
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Production, exports and availability of SMP in EU, US and Australia¹



NB Availability is calculated as production minus exports and changes in stocks and represents volumes available for local consumption and commercial stock building
Sources: Dairyintel trade data, stocks data and local production data reworked by Hoogwegt

Monthly SMP prices in the main export markets



Sources:
- EU: AMI/ZuivelNL quotes W Europe
- US: NFDM CME-spot price
- New Zealand: GDT

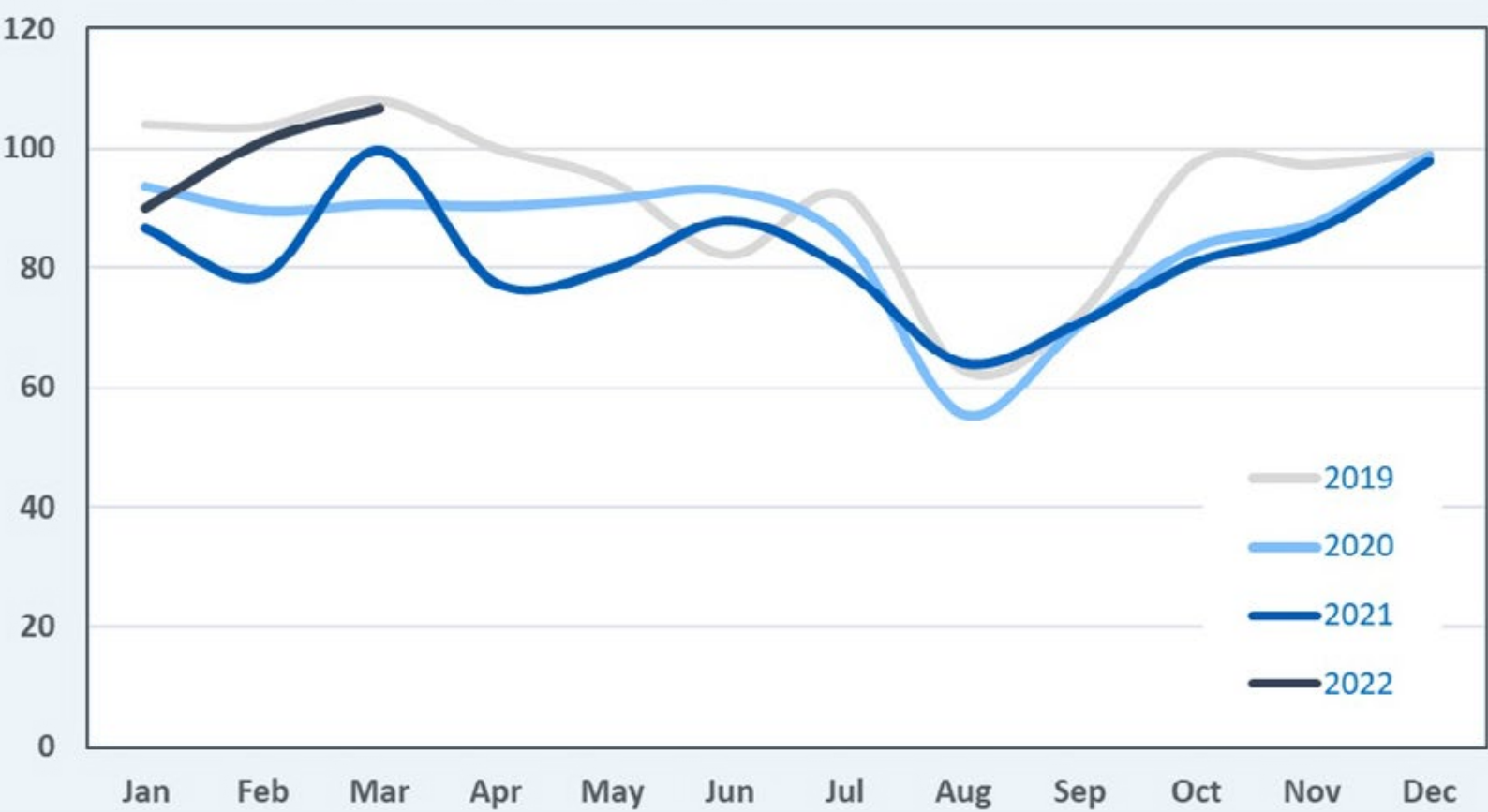
→ continuation

Consumption

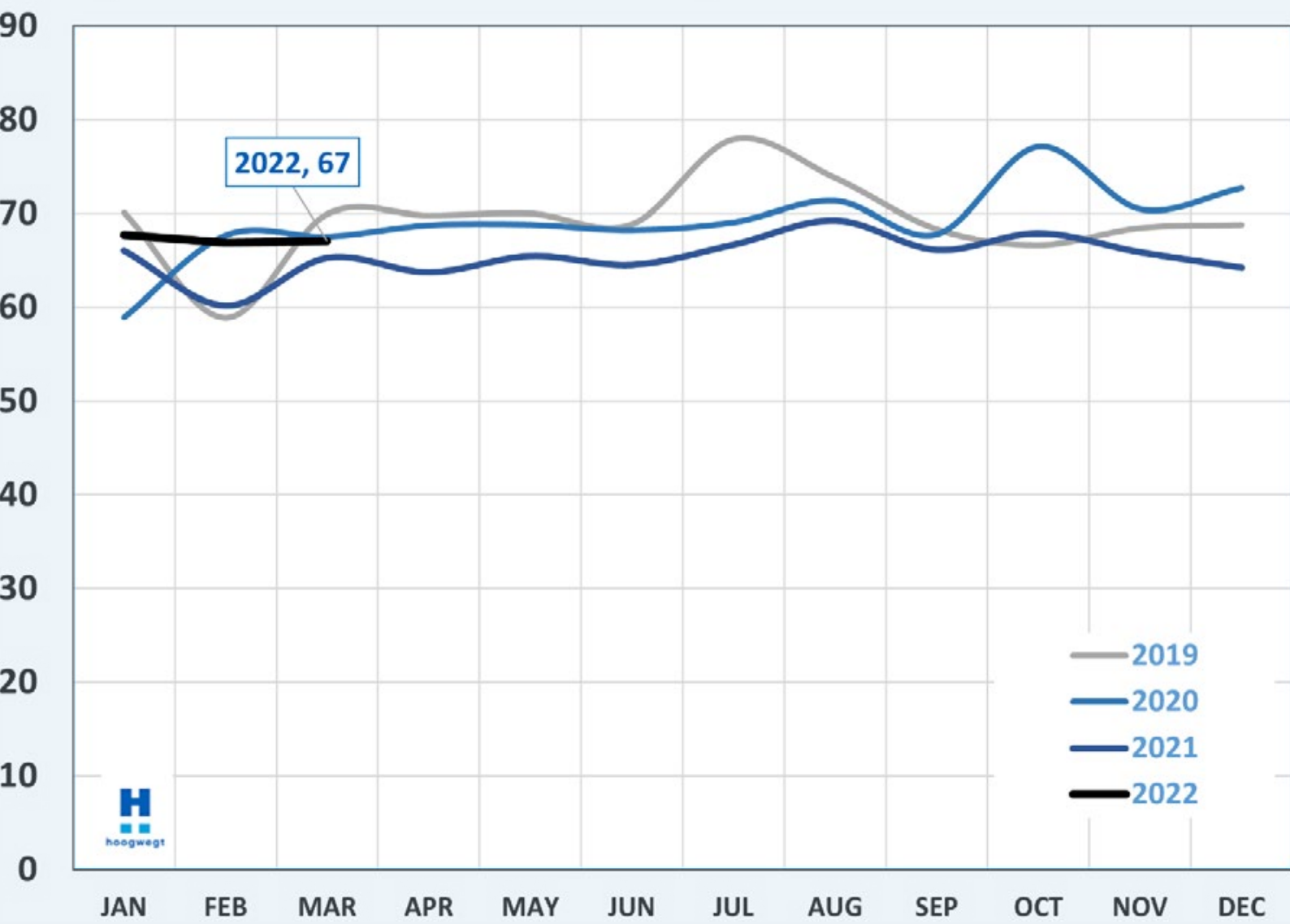
On **the demand-side** in dairy this second quarter is characterized by a big drop in demand because of lockdowns in China, and a silent SE Asia. Now Shanghai has reopened and closed and reopened we have to conclude it's a continuous question mark. Adding to that the uncertainty if China will build safety stocks. Mexico looks pretty positive. European domestic consumption of SMP looks to be slightly up compared to the low covid-2021 demand. But people are expecting drops in demand later in the year due to higher prices. US domestic consumption of NFDM already was on a downwards trend for almost a decade and that seems stable. Comparing to last year, the domestic consumption of butter (and -oils) are down in both regions which was foreseen as the butter consumption during lockdowns was high. People for example liked to bake at home during the pandemic, and they don't feel the need to do that when there is no lockdown. The same goes for the consumption of fresh milk/fluid use across the boards. Cheese consumption in the US remained to be firm in Q1 it should be close to +4% YoY. In Europe we saw demand slowing a bit, again comparing with Q1 2021. All while the global exports for butter and -oils are actually pretty good.

more →

Butterfat exports (total, Kt)



European SMP Domestic Consumption in Kt's/m



→ continuation

Bulls vs Bears... and Grey Swans...

On the bullish side:

- A global decrease in milk production, that started around last year's summer. H2 2022 shows a slight increase in milk in the US and Europe should be close to neutral/small increase. But the needed increase in milk production for significant lower dairy prices is not on the radar with farmers not willing or able to invest in that soon.
- Both production and stock levels for dairy price defining SMP are lower than last year and the 3-year average, especially in powerhouse EU.
- Q3 and Q4 will see shortages of SMP if things go forward like they are now, even with drops in demand. In a way it's a rinse and repeat of last year's scenario.
- US cheese consumption so far seems pretty firm.
- Further out, SE Asia may reopen for Chinese tourists again.

On the bearish side:

- China's drop in demand will be significant across the entire second quarter, spill-overs to SE Asia while other regions might still buy hand to mouth but won't build huge stocks at current prices. We've already seen big double digit drops in April.
- Fluid use and butter consumption are returning to their pre-pandemic levels.
- Summer months usually are easier in terms of demand.
- Some regions where dairy is luxurious and optional will face drops in demand. On top of that there is a risk of recession. retail producers are expecting drops in domestic consumption in dairy products even when alternatives may have gotten even more expensive than dairy itself.
- Exports from Others and NZ are competitive and something to watch, as they could compete with EU and US trade shares more than usual.

Notable question marks: If the uptick in March and April's relative SMP production is here to stay, stock levels should be 80-ish at the end of the year; if SMP production remains to be low, it should be close to 20-30Kt. Very low versus ultra-low in a historical perspective.

- China might step back in the market after controlling their Omicron, or not. Again, with spillover effects for SE Asia. ■

World comment.

**Adnan Mikati,
Director HTM
Americas**



I started my career at Hoogwegt developing Middle East business for North American dairy products during the first export 'surge' out of the US in the late aughts. It was an exciting time starting from scratch and with minimal guidance from typical sources you'd expect these days. I found myself traveling for weeks on end across the Middle East, cold calling customers from the local yellow pages, and chasing down company names at the supermarket. I was able to embark on a career that embraced many passions of mine; traveling and connecting with people across the globe, working together to find creative solutions for their dairy needs, and bridging those needs back to our suppliers in the US and Canada helping them achieve their global ambitions.

As I always had a keen interest on the strategic and analytical side of trading, when the opportunity came by, I was able to shift into the financial trading and risk management aspect of the business. I went from being in the hot seat negotiating with shrewd Egyptian clients, to a different hot seat trading futures and options on the CME. Instead of managing letters of credits and shipment snafus, I started managing portfolios of Greek letters and crafting creative financial instrument mechanisms to augment our physical trading. I was witness to exponential growth and interest in financial instruments in the dairy markets on exchanges around the world.

What was delightful was that I was still able to maintain strong relationships with customers despite now dealing with a different type of business risk management.

From solving physical shipment problems then, to creative derivative solutions now, I feel that customer bonds remain strong, in fact, deeper and even more multi-faceted.

This is a testament to our Hoogwegt Way of doing things – not just a price, just a relationship.

I thought I knew what volatility was until February of 2020, when we started pulling up a daily map of new cases and hospitalizations of a mysterious and highly infectious virus. People need to eat so no big deal for dairy markets, right? Wrong. In certain dairy products, prices plummeted to record lows before rocketing to record highs within 45 days. We went from dumping milk on the streets to empty shelves in the grocery store during that time. This would have spelled complete disaster for the entire industry if not for a robust financial derivatives market. Utilizing these tools during the most uncertain time in recent history helped stabilize not only our organization, but also participants across the industry.

Covid as a market risk factor may have died down, but the use case for financial derivatives remains stronger than ever. Only a small percentage of global milk production is traded on financial exchanges, which leaves room for plenty of growth and improvement. It's an exciting time as ever to be involved in this aspect of the dairy business, and more importantly to do it for an organization at the forefront of these developments like Hoogwegt. It's one of our core services and a key tool to add value to our customers, so I encourage those of you not involved yet in these markets to reach out to us. Together we can find ways to help you stabilize your bottom line in a sustainable fashion.



We are pleased to announce that Hoogwegt Group has extended its proud sponsorship of the Wageningen Student Rowing Club Argo for the 2022/23 season!

Hoogwegt Group previously signed a 3 year sponsorship from 2019 to 2021.

Rowing is the ultimate team sport. Like at Hoogwegt, team members need to operate in perfect unison to achieve the best results, win matches and achieve our goals!

Wageningen (a.k.a. Food Valley) is home to the world renowned Wageningen University in Agricultural, Food and Dairy Sciences. At Hoogwegt, we believe that Food Science is an important part of our future – technical knowledge, on top of commercial and fundamental information, coupled with prudent risk management provides us with an edge in the Dairy Industry.

Do find a video of the Argo rowers at training and wearing the Hoogwegt name on their shirts during the racing seasons.

Hoogwegt Happenings.

[Watch video here →](#)