



Horizons.

Our insights
on Today's Global
Dairy Business

July 2023

#07

Page 3

Market Direction

**Southern
hemisphere
keeps milk
supply
in positive
territory**

[Read more →](#)

Page 7

**Dairy Deep Dive:
Chinese Demand
for NZ WMP:
Lust or Love?**

Page 12

**World
Comment.**

Page 13

**Hoogwegt
Happenings.**

Page 14

**Hoogwegt
Dairy Spew
Podcast.**

Editorial Note.

Hello!

In this issue, we discuss milk production in the main regions, and discuss in greater detail the Chinese Demand. Is it really down across all products? Are we seeing pick-ups from other demand points?

Our usual quick notes on Whey and the Futures Market will take a broad look into the whey powder outputs in USA and EU, and explore the situation we see on the EEX.

We invite Charles Tey to share his thoughts and experience in moving from Hoogwegt Singapore to Pacific Dairy Ingredient Shanghai.

Also, tune in for our latest episode of Hoogwegt Dairy Spew Podcast – Cool, Calm & Collected.

Enjoy!

As always,

Hoogwegt Horizons Editorial Team

Disclaimer

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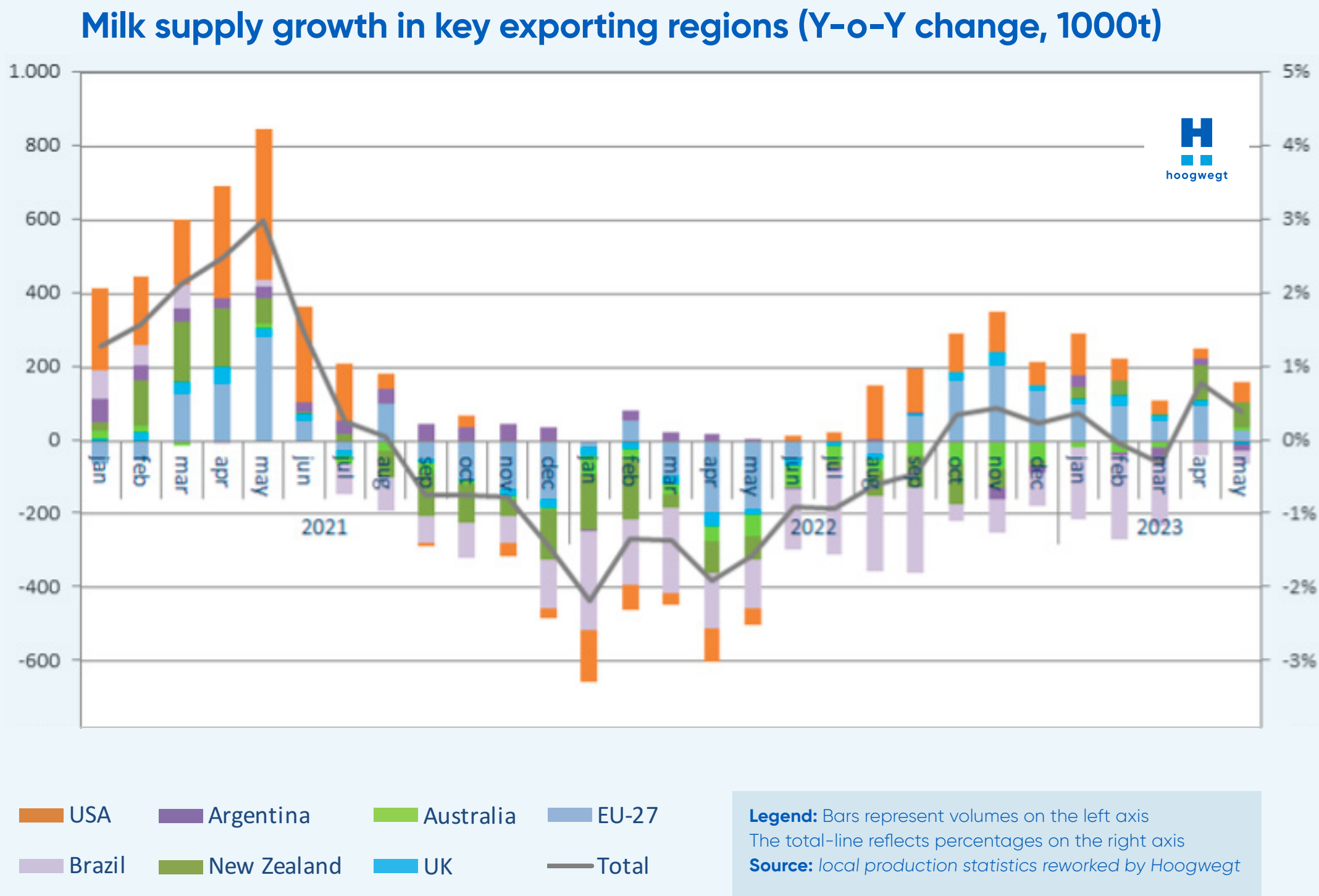
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Market Direction

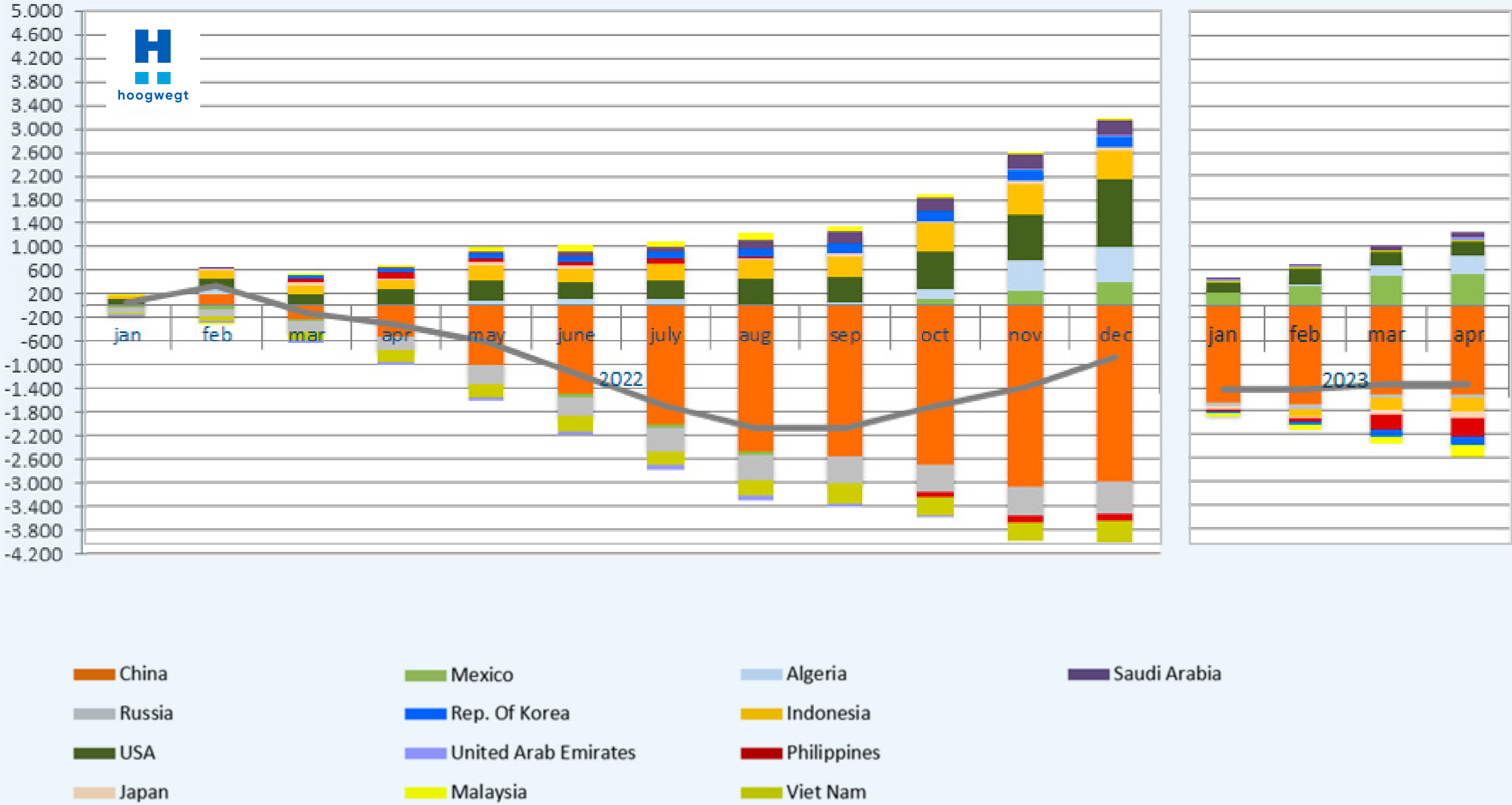
Southern hemisphere keeps milk supply in positive territory

The strong shoulder of the Southern hemisphere season makes the difference this time of the year. New Zealand produced a strong + 7% in May compared to last year and even Australian milk production turned positive again after going backwards for 24 months in a row. In the next two to three months however, it will be Northern hemisphere supply that will be critical for the way the market balance develops. Milk prices in both the EU and the US are at a level where dairy farmers are no longer encouraged to increase productivity or invest in expansion. This makes a supply scenario likely that global supply will continue to Hoover at around 0.5% growth in the remainder of the year. Due to the weakness of global consumption in general and Chinese import demand in particular, a growth rate of 0.5% appears to be good enough to keep up with demand growth going forward. However, the capacity to deal with summer weather disruptions or accelerating end consumption and import demand seems entirely absent.

[more →](#)



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 countries combined
Source: Dairyntel trade data, reworked by Hoogwegt

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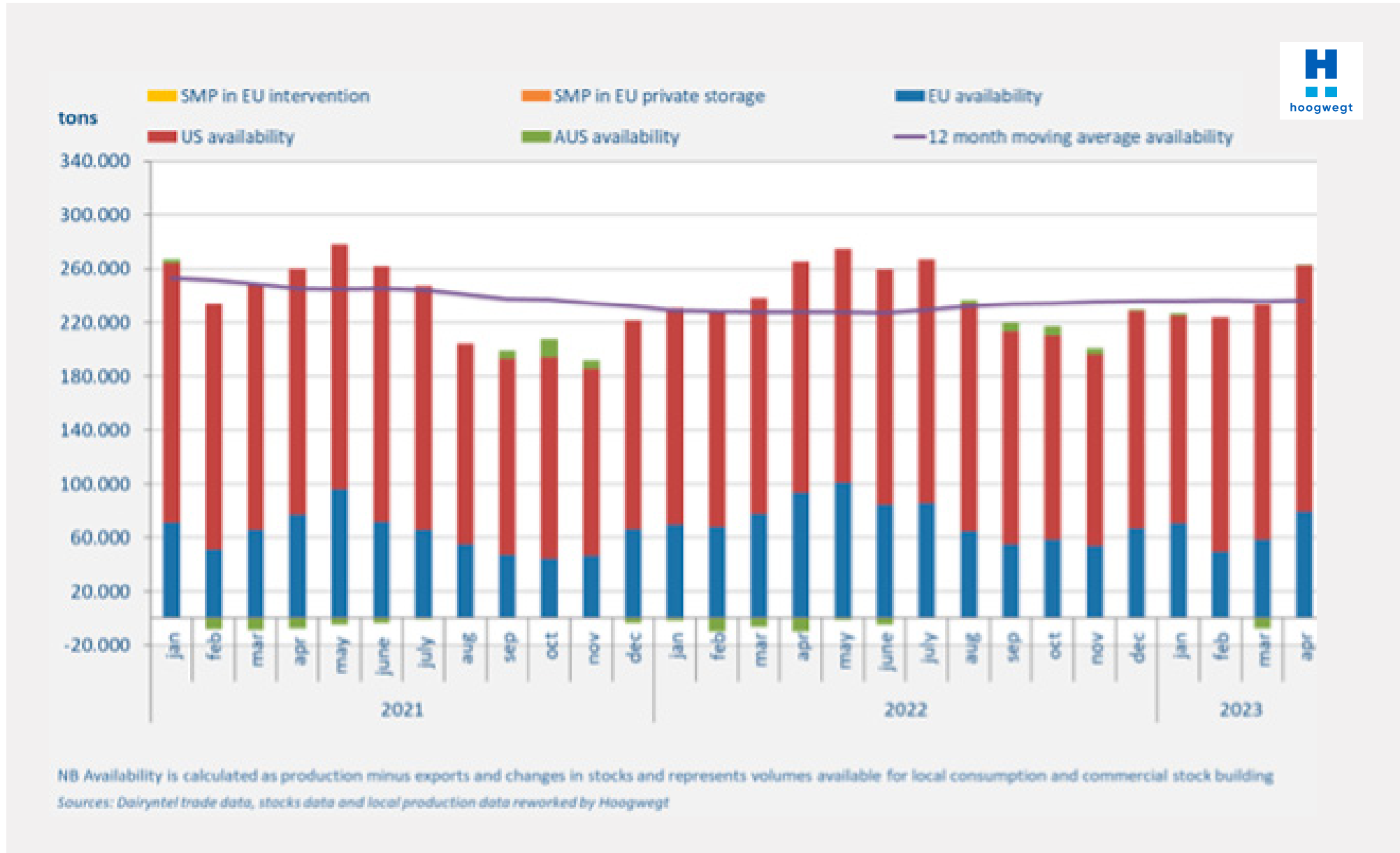
Import patterns hardly changed in April. Chinese import demand did not catch up any further with last year and all countries that are behind on last year's performance continued to fall short. Likewise, all countries that improved on last year's performance in Q1 continued to do so in April. So South Asia as a region remains significantly behind on their usual imports while Algeria in particular did very well in April. Price levels and availability can hardly be the reason for weak import demand so in Southeast Asia in particular, end consumption appears to be weak at the moment due to the combined impact of the recent food price inflation and weak economic development. In H2 of 2023, we may see the impact of food price inflation gradually evaporate because end consumer prices are bound to eventually follow the recent decline of dairy commodity prices. So what remains is whether the global economy will be able to inject some life into global dairy demand.

SMP/NFDM: All dairy protein markets remain bearish

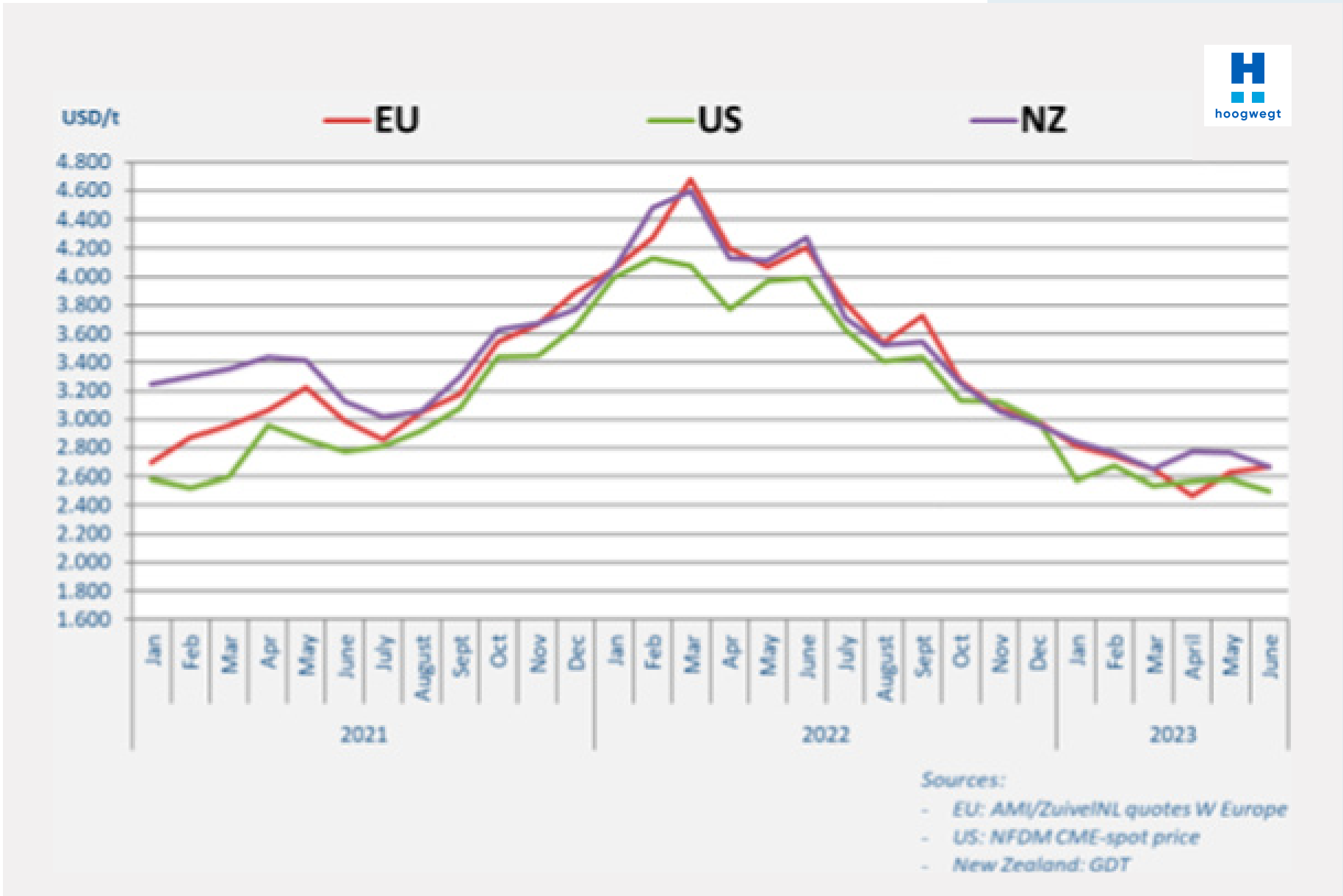
The market for dairy proteins still appears to be very weak for a number of reasons. NZ wants to clear its remaining seasonal inventories and therefore keep export sales competitive. US origins are currently most competitive in export markets, partly because of some currency tailwind in recent weeks. Casein and whey markets also remain bearish as demand in all protein markets is simply not strong enough to keep up with supply. What may relieve some of the supply side pressure is that since the EU flush is now behind us, capacity constraints no longer

play a role. Even during the peak month of April SMP production in important countries like Ireland and Germany was already down, so when capacity is no longer a constraint and cheese valorization remains strong, EU surpluses available for SMP/butter may quickly diminish. How quickly this will change the market balance in SMP/NFDM is a question mark though. Many buyers still have to buy for the final quarter of this year but price developments provide very little incentive to step in in a hurry.

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



Monthly SMP prices in the main export markets

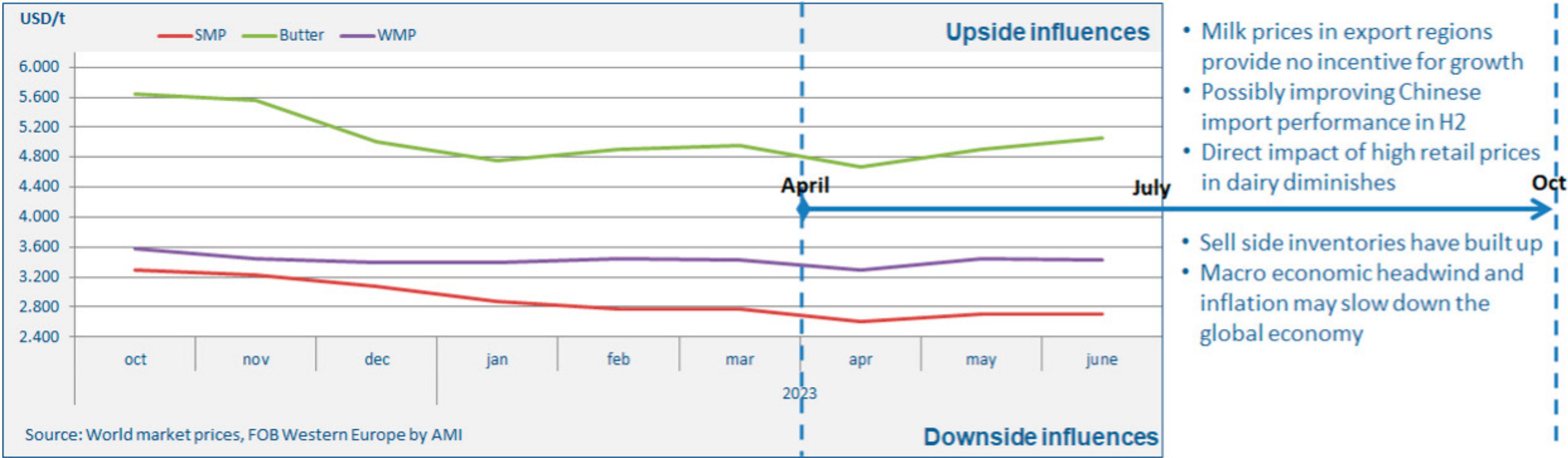


Looking forward

Supply in the export regions monitored for this report is cruising at a growth rate of around 0.5% for the next couple of months. Given where milk prices are currently going, it is difficult to identify upsides for global milk production. This probably makes the supply side the least important part of the market balance and the direction of prices going forward. The chances of dairy demand surprising positively is therefore the key driver for the chances and timing of price appreciation going forward. The large number of upward risks,

- Northern hemisphere summer heat, better end consumption when consumer prices eventually follow dairy commodity prices downward, stronger import Chinese demand - seem to outweigh the downside risks of a weakening global economy and ongoing lackluster Chinese import demand. However, getting the timing and magnitude of price recovery in H2 right remains the biggest challenge, especially because of the many unknowns around China. ■

Market Outlook for July - September 2023



Dairy Deep Dive

Chinese Demand for NZ WMP: Lust or Love?

Whenever there is a debate on import demand involving China, WMP usually stands out. Close to 90% of imported WMP in China originates from New Zealand (NZ). In previous issues of the Horizons, we discussed the symbiose between NZ and China on this particular product. This season, there's a lot of unprecedented things going on: we've got changes to agreements and tariffs, a reopened China, a good local milk production and a mixed bag of reports on the Chinese economy. Let's not forget that we saw a different product mix in NZ this season, meaning less WMP production.

One could look at NZ Exports, from the perspective of a ship leaving the NZ port to China. Previously, the export data (Figure 1) peaks in Q4, however, this was due to an incentive to get the product into China before the 1st of January. As discussed before, things were different this year, and indeed, NZ lost 210Kt of Exports from 1st of September until December 31st 2022.

Note that this is against a strong season of 2021, indicated by the upper end of the grey bandwidth. The 3- and 5-year averages are indicated by the black and green dotted lines respectively. Q1 2023 had a bad start with numbers dropping compared to Q1 of 2022, losing another 47Kt.

WMP (HS:040221, HS:040229) Exports in New Zealand in 2023 (kg)

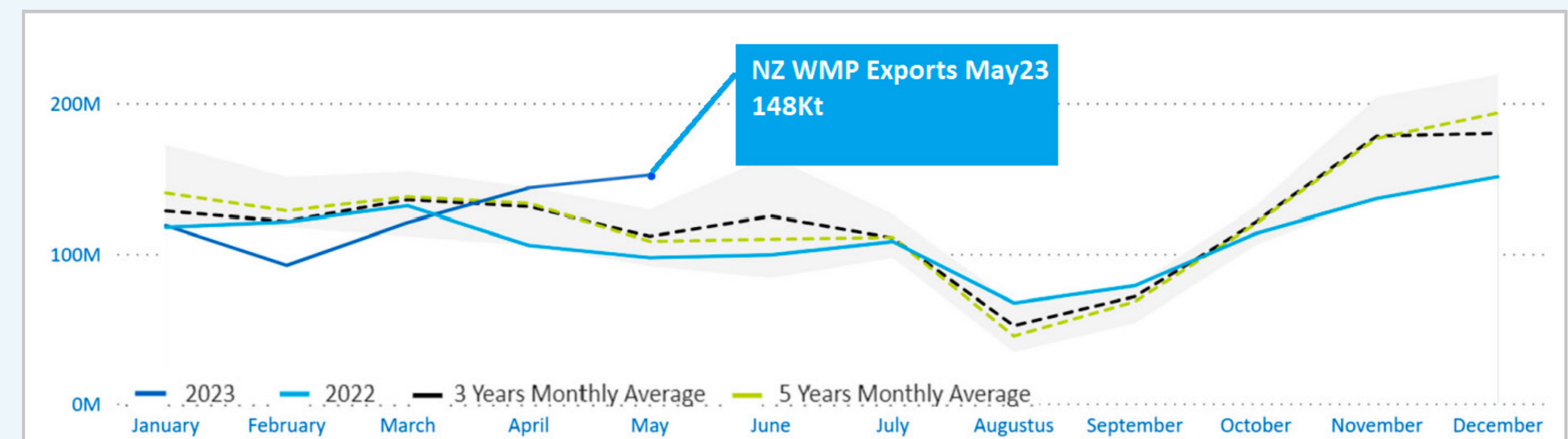


Figure 1

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In past days, NZ Export data and the Chinese Import data were published, indicating a YoY increase.

April was up 49Kt (+12Kt YoY), and so was May (50Kt, +27Kt), regaining almost 40Kt of the losses prior to these months. So far, the loss of Chinese import this season is still significant, and calendar summer months are usually a bit easier in terms of demand.

So while WMP exports to China show increasing numbers in the past few months, which is a good sign for NZ, but there is still much to catch up on. It takes time to recover from those losses, especially when they're compared to calendar year 2021 or the 21-22 season.

The trendline of Figure 2 emphasizes the loss as well. Plotting the NZ WMP Exports to China in a rolling average visualizes both:

While NZ WMP exports to China registered two consecutive months with YoY increasing volumes, the losses in prior months were significant. Anecdotally we are hearing of droughts in some parts of China, but local Chinese milk production is still reported to be positive, and we're nowhere near the trendline yet.

The loss in WMP production in NZ due to product mix changes do offer another light in this dark tunnel. And let's not forget stronger demand from North-Africa and the Middle-East. These particular regions' import demand eased the pain for NZ by a combined +/- 30Kt increase YoY since September 2022. One thing we are sure - don't expect Chinese demand to be back on par with the 2021 import demand any time soon.

NZ WMP Exports to China (Tonnes, 12m rolling average)

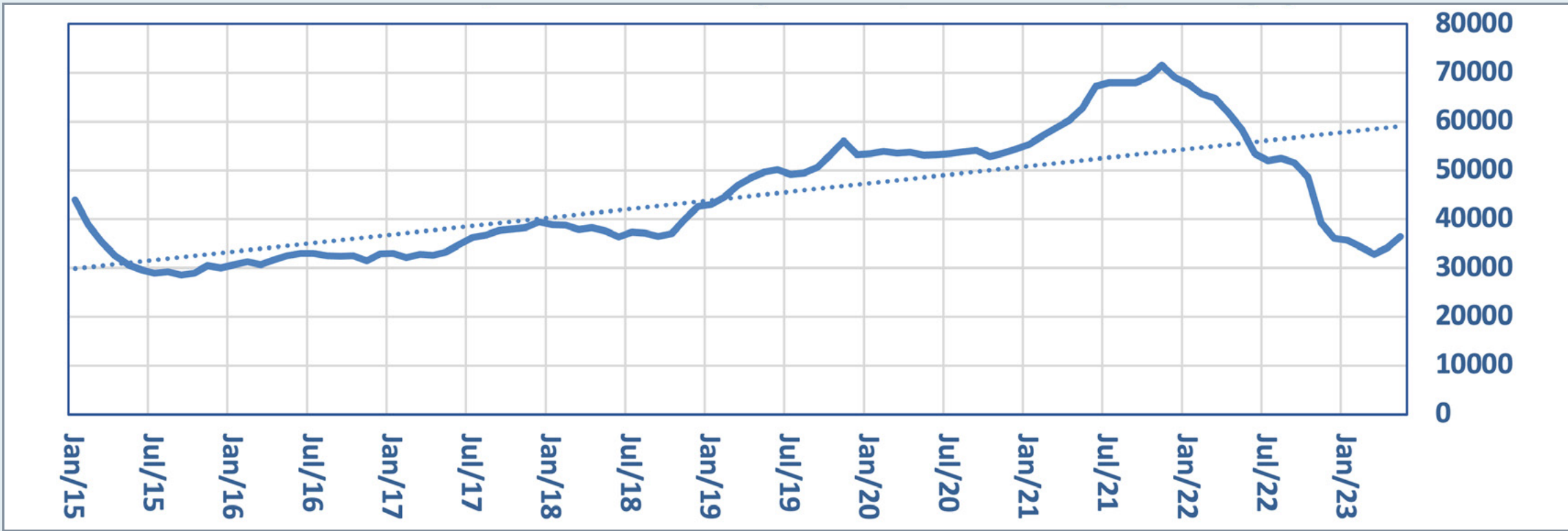


Figure 2

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Bulls vs Bears...

On the bullish side:

- Milk is seasonally going down in the Northern Hemisphere and while margins are dropping, don't be surprised to see negative milk growth in Europe's H2, the same could be the case for the US.
- Unlike WMP; China's demand for SMP has been quite strong and May imports showed some sparks.
- Prices dropped; this should attract some buyers.
- Money isn't free anymore and stricter loans could limit farmers in their investments leading to scarcity.

On the bearish side:

- Domestic consumption in Europe is still struggling, Recessions, inflation, leading to drops in demand.
- SE Asian demand seems to be low. While others who bought might have enough for now.
- Fresh consumption closer to pre-pandemic levels leading to better availability of the milk flowing into commodities.
- Chinese milk production is still reported to be good.

Things we watch:

- Geopolitical turmoil shifting away from free trade.
- NZ's next season; Cows, slaughter, payout prices and product mixes as analyst's projections are pretty broad on both the positive and negative side of milk production for next season.
- Slaughter rates in US and NZ saw upticks, will that continue and increase the negative effect on milk production? EU farmers could be in a similar position, so everything on cows is on our watchlist.

A Quick Note on...

Whey

By John Kramer, Global Head – Whey, Lactose & Permeates

For this issue, we will try to focus a bit on the actual produced volumes of Whey Powders in leading regions – USA and EU.

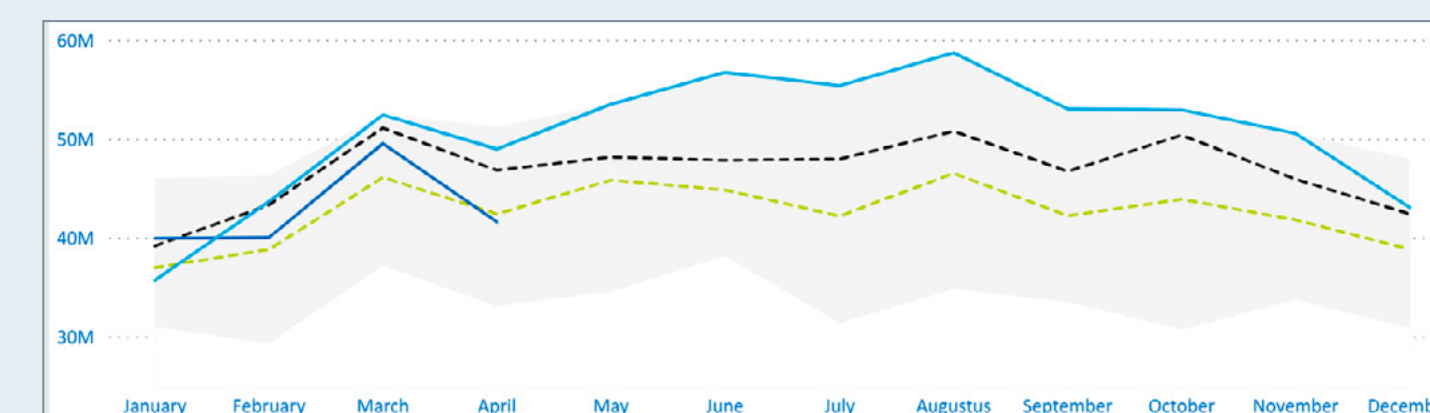
Disclaimer:

This is a tricky operation since rock hard statistics (especially from EU) are not available and most of the time, it's unclear if Permeate is in our out of the figures published (due to it having the same HS classification).

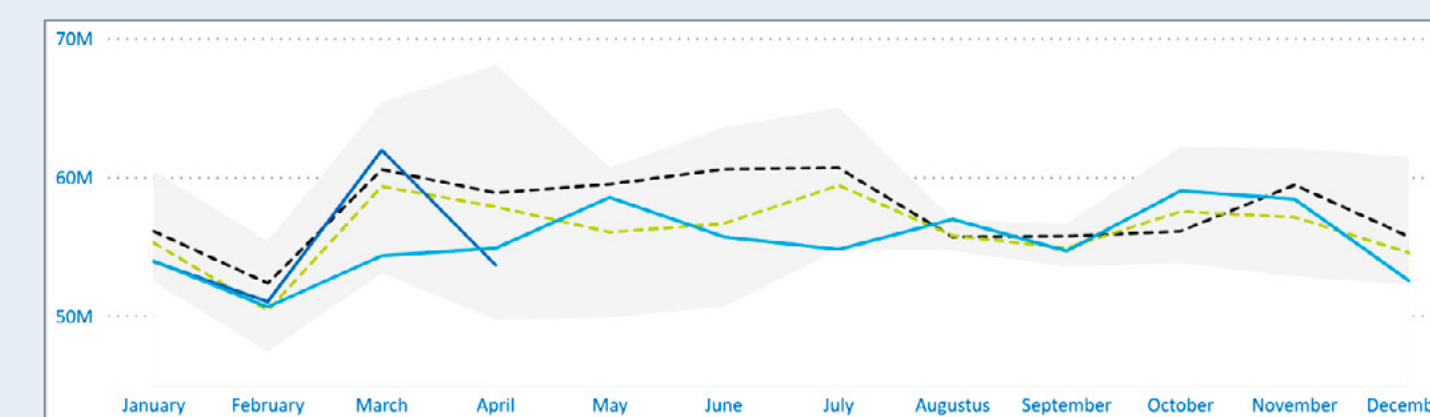
- Diving in to some high-over figures, we see global output of whey powder in 2015 at 2.275 Mio Mt and in 2020, reached 2.300 Mio Mt.
- Outlook is that by 2025, we will be at 2.335 Mio Mt.
- Europe covers about 1.2 Mio Mt and North America 0.55 Mio Mt of this.
- Roughly 60 % of the production reaches Food applications leaving still a considerable 40% for the Feed Industries.
- In the last decades, Industry has converted large streams of whey to higher segment products such as demineralized whey and whey concentrates etc., leaving less for straight forwarded whey powders.
- With increasing WPC, larger streams of by-product Permeate (or Lactose derived from that) entered the market place.
- Broadly speaking, about 50 % of the produced whey volumes are for domestic usage, leaving the balance to be exported to global markets. This underlines the fact that both USA and EU need healthy exports to keep their Supply and Demand in balance.
- As direct effect of the global food inflation, the demand side has been struck hard both on home front, as well as in the global markets as an immediate consequence of very low prices we face today.
- In recent issues of Horizons, we pinpointed the influence of Feed usage on the whey complex.
- With the 40 % estimated usage still pending, we can explain why the whey markets have been hit hardest reaching low price levels not seen since many years.

- Lower animal numbers (driven by either market dynamics or governmental/environmental changes) created considerable lower consumption patterns across the globe.
- As things are at the moment, we don't see this trend turning around any time soon. At the same time, the current prices seem to be at a critical bottom level where all bad news is already priced in.
- Interesting background on this: China imported their second highest ever volume of whey products during May 2023 and YTD May, China has absorbed 80% more whey products than in 2022.
- Still, this massive number does not keep USA market clean where formidable production outpaces demand and continues to depress prices.
- It's fair to assume Europe shows a similar picture.

Dry Whey (HS:040410) Exports US in 2023 (kg)



Dry Whey (HS:040410) Exports European Union (EU-27) in 2023 (kg)



Futures

By Ton van den Oever, Managing Director – Hoogwegt Trade Management

- The EEX SMP market has been in a horizontal range since the beginning of the year. To illustrate, the third continuation has been trading between EUR 2370 and 2720 since January. The potential for price growth is constrained due to lacklustre demand in export markets and the presence of competitive supply from the United States and New Zealand.
- Conversely, the potential for price decline is also limited. Anticipated constraints in raw milk production during the latter half of 2023 serve as a deterrent against aggressive selling. Producers are especially reluctant to offer futures contracts, fearing that they would sell at unfavourable prices.
- This leaves trading companies seeking to hedge their physical spot purchases as the only entities offering futures in current market. Due to the high cost of carry, (i.e. storages fees and finance costs), they need a significant premium versus the spot price to make it worthwhile.

- As the summer holiday season approaches in the upcoming weeks, substantial alterations in market dynamics are not expected. Presently, there are no indications suggesting an imminent shift in the pattern.
- EEX Butter faces a situation similar to SMP. Upon analyzing the market trends, it is evident that the market is experiencing a horizontal movement. Since the beginning of March 2023, there have been no significant price fluctuations. Additionally, the market exhibits a steep contango due to the high cost of carry.
- Moreover, the availability of cold storage facilities is limited, making it challenging to find suitable storage options. As a result, traders interested in engaging in the carry game (i.e. purchasing spot contracts, storing the product, and selling futures) are unable to do so due to the lack of storage capacity. This market dynamic exacerbates the contango effect.



World Comment.

Charles Tey Senior Account Manager Pacific Dairy Ingredients



"It's a rather amusing reality that we spend more than 80% of our lives toiling away at work. But you know what? I've decided to turn this into an epic adventure" That's exactly what I conveyed to my first manager, Rogier Lankamp, during my interview with Hoogwegt.

Looking back, my milk journey over the past 5+ years has been nothing short of amazing. As a starry-eyed young man, I had two ambitions: to explore the world and to face thrilling challenges.

In the early years, my primary focus was trading huge volumes of milk powder and expanding our market share in various destination markets. In fact, I might just be the first trader in the industry to make the initial intervention powder sales into SEA. Talk about making history!

As I became more commercially savvy, I was offered an opportunity to oversee the Global BMP positions. With the support of my talented colleagues, we transformed a small product group into the largest BMP book in the world. I've donned different hats along the way, taking on roles as a salesperson, a businessman, and a global trader. After five years, it feels like my journey with Hoogwegt is only just beginning.

Just a month ago, I relocated to the beautiful city of Shanghai, China with my wife and our three cats. Am I ready for China? Or is China ready for me?

China produces close to 40 billion liters of milk, almost twice as much as New Zealand. It's a country where milk production is on the rise, while also maintaining its status as the world's largest importer. Any changes in the local dynamics will undoubtedly impact market fundamentals and sentiments, especially regarding WMP.

When I attended the FIC Shanghai in March 2023, I was surprised by the drastic difference in local sentiment compared to the global outlook. As a foreigner, I was quite bullish, considering the full reopening post-COVID, rising PMI index, and high expectations of economic growth. However, the local market had a completely different perspective due to a surplus of milk, increasing local stocks, and a lack of enthusiasm about consumer spending. Fast forward two months, the markets remained subdued with articles flooding Bloomberg about weakness in China's economy. Being physically in China has allowed me to have a pulse and timing of the market, allowing me to uncover fantastic trading opportunities.

China is poised to steer the world's economic growth in the years to come, and that means bigger opportunities for Hoogwegt. I'm grateful to represent the largest dairy trader and to contribute to expanding our business in the world's biggest importer. I have full confidence that we will achieve big success as a team!

Hoogwegt Happenings.

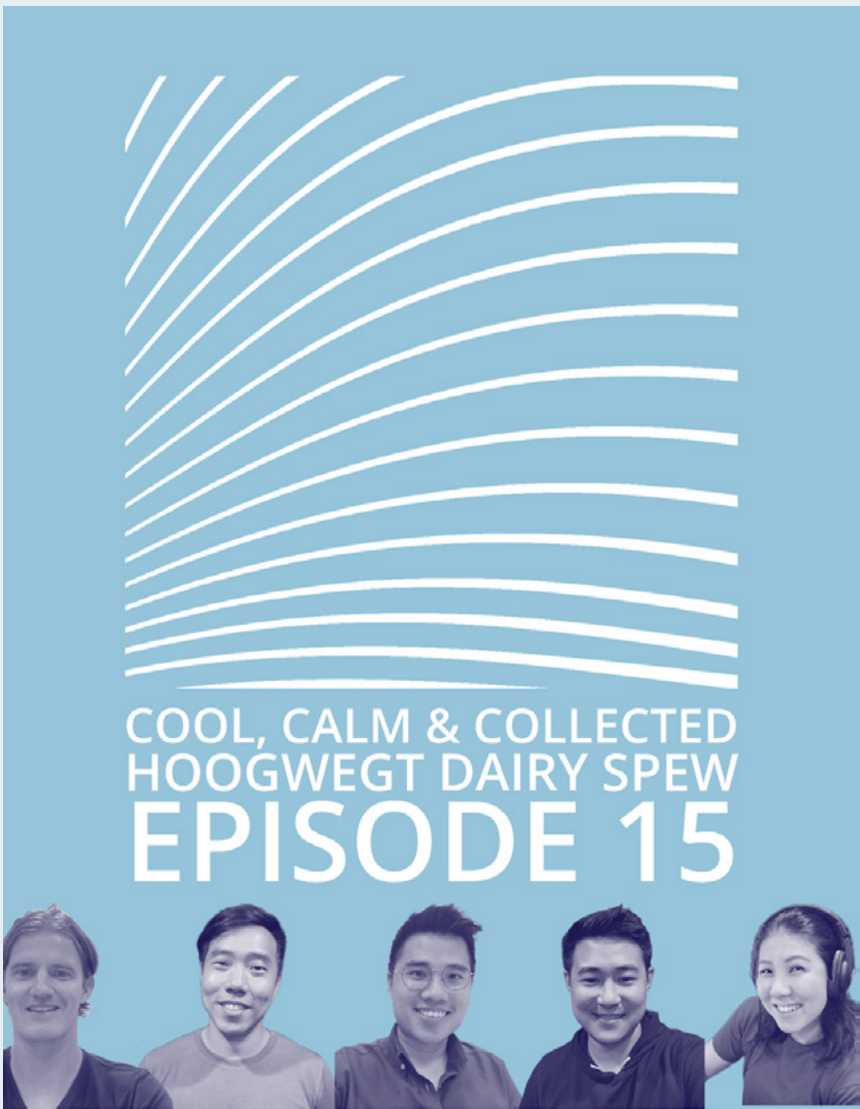
In an Offsetting Project powered by Climate Neutral Group (CNG), Hoogwegt succeeded in offsetting the CO₂e-emissions of our global offices in FY20-21!

This biogas project invests in methane fermentation and energy generation in the Netherlands and is an example of a project which minimizes climate impact and uses circular business operations.

(Co-)fermentation is a natural degradation process in which biogas is released under controlled conditions. The biogas produced is then converted in a combined heat and power installation (CHP) into sustainable electricity, which is then supplied via a green power supplier to many thousands of households in the Netherlands.

The advantages of this project includes:

- Reduction of CO₂ and methane (CH₄). This combats climate change. Methane is a strong greenhouse gas: 1 kg of methane has the same effect as 28 kg of CO₂.
- Avoidance of fertiliser production.
- Prevention of nitrogen emissions from manure and waste because fermentation now takes place in a closed environment. It also contributes to the solution of the current nitrogen problem.



Cool, Calm & Collected.

Join us for Episode 15 as we discuss the **Cool, Calm & Collected** buying behaviour given the calm market and low prices.

In this episode, we discuss the Supply Outlook in EU, US and Oceania and then do a deep dive into the Demand in South East Asia as well as China. Lastly, we also discuss the Contango in the Futures Market.

Learn more about **MyHoogwegt Portal** and how it can be utilized to increase efficiency for you and your logistics team!

We have also added in **Transcripts** of this episode on our Buzzsprout website. You can find it [here](#).

Listen in to find out more!

Note:
Podcast was recorded on 16/ June/2023.
Transcript was generated automatically. Its accuracy may vary.

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Comments / suggestions / collaborations are welcome!
Do let us know if you would like to be a guest speaker on our upcoming Episodes!

--- Hoogwegt Dairy Spew Team



Episode Guide:

- 0:26 Introduction
- 1:12 EU Supply Outlook
- 2:32 Is Current Milk Price Attractive for EU Farmers?
- 3:52 US and Oceania Supply Outlook
- 5:08 Quick Discussion on Energy Prices
- 6:20 Short Update on FC Lochem Situation
- 7:45 Quick Update on GDT
- 8:55 Cool, Calm & Collected Demand
- 18:45 MyHoogwegt Portal
- 19:19 Talk About The Panda (China)
- 23:45 Is the Current Contango in the Futures Market Justified?
- 26:51 Summary & Closing

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