

From the Trading Floor

KEY MARKET DRIVERS

- CME Cheese Futures go nuts
- gDT disappoints
- Australian Dairy areas get good late Autumn / early winter rain
- Reports that E.U. and U.S. Cream is tight
- Australia experiencing demand for milk pricing

- Have we seen the first evidence of a Hedge Fund being attracted to the U.S. Dairy derivative markets now that volume has increased to a level that can support big positions? Since the beginning of June we have seen CME Class 3 and Cheese block futures rising rapidly (going limit-up on two days) on the back of a player coming in to "Go Long" and thereby cause an almighty short covering rally. Spot trades have somewhat gone out in sympathy, rising from US\$1.30/lb levels to US\$1.50s. Despite some fears of a long, hot, dry summer on the way, cheese seems to be still plentiful out of the Mid-West so the rally seems to be overplayed. It will lead to continued milk supply on back of good pricing for milk, lower exports and even more imports. So even if the hot summer eventuates economics says that the large inventories will continue to build.
- On the back of rising prices out of Europe and US (see above) there was an expectation that we would see a rally in gDT pricing on Wednesday night, especially in SMP. The result was pretty much a flat line from the previous event. The disappointing results are due to reports are that the Chinese remains extremely subdued in their demand. With volumes on gDT ramping up from here on in as we deal with the Oceania peak, the outlook returns to being bearish in nature.
- On the back of a very dry and hot summer across Australia, due to the very strong El Nino event, we are now seeing very welcome rain right across Australia. We have seen good falls in all major Dairying areas which are expected to continue across Winter. This will bode well for a good start to the next Dairy season beginning in August (for milk anyway, not so much for milk prices).
- We are hearing reports of Cream being in high demand and in short supply across Europe and USA. E.U. Manufacturers got on the front foot earlier in the year and locked in strong sales to deal with their peak milk. Actual milk flows have come in lower than forecast (still growing but not as much as thought) which has led to short supply of cream in many cases. On the US side it is more a demand driven shortness as the domestic market has huge demand for Cream at this time of the year particularly from the Ice Cream segment.
- We are seeing emerging demand in the dairy farming community in Australia for transparency and risk management tools to combat volatility as fallout from retrospective milk price cuts continues. We expect this to develop and challenge the status quo, although, we question if there is enough momentum to force real change. What we may see is simply a % of milk changing hands, from processors who dropped prices to processors who did not, and the new cycle starts again.

Matt Cooper, Director, Ausfine Foods

FUTURES

- The biggest story in futures world is definitely US CME cheese, which has rallied from approx. \$1.30/lb to near \$1.55/lb in the last month – over USD\$500/MT, in spite of record high stock levels, strong milk production in key cheese states and a still moribund global market which is seeing more and more cheese added to production schedules every day. Why the rally? A lot of the industry has focused in on rumors of large fund activity, looking to buy an oversold market as part of a general "weak USD / strong commodity price" theme through broader asset markets. Funds are always looking for new ways to get exposure to such themes, and given their large participation in other agri markets it is no surprise they have turned to dairy, especially given increasing futures liquidity. If this is the case, then it could mark a turning point for dairy – and bring the potential for more volatility, as it did to grains and softs in the mid 2000's.

Scott Briggs, Derivatives Trading Manager, Ausfine Foods

DAIRY EXPORT INDEX

Positive run ends – After three consecutive rises, our index gave up ground this week, down 0.8% on softer SMP and a stronger A\$. After rising strongly last week, SMP shed US\$50/t to US\$1,800/t. Butter and WMP were steady at US\$2,800/t and US\$2,200/t, respectively. Cheddar and whey steady at US\$2,800/t and US\$1,000/t. The A\$ rose to **US\$0.738**, shaving **1.2 points** from the index to **146.5**.

Australasian dairy export index (Jan 2011-now)



AUSTRALIAN INDUSTRY NEWS

WCB opens at \$4.80kgMS, announces capital raising

Warrnambool Cheese & Butter (WCB) will open the 2016/17 season at A\$4.80kgMS. Senior vice president and general manager Richard Wallace said WCB wasn't immune to the fluctuations of the commodity price cycle. WCB doesn't expect a recovery in global dairy market conditions until calendar year 2017. WCB has also announced an equity capital raising of up to A\$142m through a three-for-eight rights offer at A\$6.75 a share. Proceeds from the Entitlement offer will be used to repay debt, strengthening WCB's balance sheet, and allowing it to invest in strategic initiatives, including cheese and other product manufacturing capacity expansion, scheduled to commence in 2016/17 and cost around \$40m.

Push for MG EGM

A group of Murray Goulburn (MG) suppliers are reportedly pushing for an extraordinary general meeting, and are "quite close to achieving the necessary number of shares to trigger an EGM", according to a Gippsland farmer. While some reports claim the purpose of the EGM will be to challenge and spill the MG Board, the farmer says it will be supportive of the cooperative, offer the right forum for questions to be asked and ideas shared, and for guidance to be given. Publicly MG has stated "The board believes it continues to enjoy strong support from supplier-shareholders," according to a spokesman.

Weather highlights

- In Australia, showers in western and southern Gippsland over the weekend, showers in central NSW.
- In NZ, passing showers and cloudy in the north of the North Island. Central region of the South Island dry with possible showers during the weekend.
- In the US, soaring temperatures are expected to hit the southwest with record-breaking highs. Warm in the Midwest.
- Hot and humid in the central regions of Brazil and northern Argentina.
- Rain and thunderstorms in Bavaria clearing early next week. Thunderstorms also expected in Normandy.

Synlait opens at NZ\$4.50kgMS

Synlait Milk announced its forecast milk price for the 2016/17 season at NZ\$4.50kgMS, and will pay farmers a higher than usual advance rate of NZ\$3.50kgMS. The higher advance payment is aimed to get cash in farmers' pockets as early as possible. Synlait revised their 2015/16 price down, however, to NZ\$3.90kgMS, from NZ\$4.20kgMS in February.

Brazil's WMP imports on the rise

During the first 5 months of 2016, Brazil imported 42,376t of WMP. Uruguay and Argentina were the main suppliers during this period, with YTD WMP quantity market shares of 63% and 29% respectively. Other smaller suppliers include Chile and Paraguay. During the January-May 2016 period, Brazil exported only 4,161t of WMP, down 47% YOY.

Last week, Brazil announced a lift in the limit on imports to a maximum quota of 4,300t of milk powder per month from June 2016 to May 2017, and 4,500t from June 2017 to June 2018.



WASDE: higher US output 2016 & 2017

The latest WASDE report from the USDA has raised milk production forecasts for 2016 and 2017, as herd expansion continues. Export forecasts for 2016 and 2017 on a fat and skim-solids basis are lowered as international supplies of dairy products remain plentiful and US prices are uncompetitive. Fat and skim-solids basis stocks are forecast higher. Fat basis imports are reduced for both 2016 and 2017 on expectations of slower imports of butterfat

products, and to a lesser extent, cheese. The all milk price is forecast higher at US\$14.95 to US\$15.35 per cwt for 2016, but is unchanged at US\$15.25 to US\$16.25 per cwt for 2017.

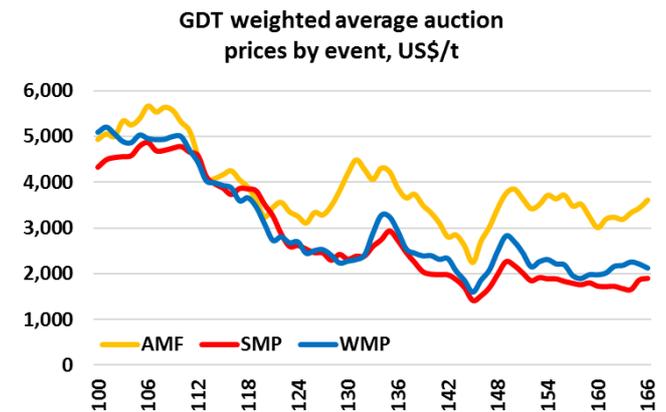
EU exports mixed

EU April exports were once again a mixed bag with a 13% rise in cheese shipments over the same month in 2015. However SMP was down more than a quarter as exporters preferred the Government bunkers as an outlet. Butter and butteroil exports continue to surge, up 57% over the comparative on combined tonnes shipped. Other products were generally higher across the board. For the four months to date, the trends are similar but the monthly totals of SMP sales will dry up as sales into intervention continue to strengthen.

GDT flatlines

This week's GDT event yielded no change in prices on the 23,089t on offer – slightly down on the previous event.

The average weighted WMP price fell 3.9% to US\$2,118/t, with contract periods 1 to 3 taking a significant hit compared to previous trends. Average SMP price rose 1.8% to US\$1,901/t, while butter and AMF rose 5.4% and 5.1% to average US\$2,910/t and US\$3,619/t respectively. Cheddar price rose 8% to US\$2,882/t while rennet casein average US\$5,116/t, up 1.6%.



DAIRY FUTURES

15-Jun	SMP	NDM	WMP	Cheese	AMF	Butter
Exchange	NZX	CME	NZX	CME	NZX	CME
Jul-16	1,855	1,913	2,200	3,651	3,540	5,225
Aug-16	1,920	2,056	2,225	3,807	3,640	5,357
Sep-16	2,100	2,152	2,370	3,794	3,670	5,383
Oct-16	2,150	2,205	2,390	3,763	3,800	5,377
Nov-16	2,200	2,239	2,395	3,706	3,600	5,338
Dec-16	2,225	2,287	2,440	3,657	3,405	5,024
Change	7%	3%	2%	8%	1%	9%
Op interest	3,141	4,676	13,860	21,527	260	4,809