

Buyer Appetite Present, But Not Willing to Pay Up; GDT Index Needs to Find Strong Footing to Support \$7.00/kgMS Forecast

<p>Key Statistics from Tuesday's Auction Total Volume Sold: 21,580MT (47.6 million pounds) UP 3,419MT (+19%) from last auction DOWN 424MT (-2%) from last year Winning Bidders: 118 (+7 from last auction) Participating Bidders: 179 (+15 from last auction)</p>
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KEY POINTS:

- **Fonterra's Nine-Month Business Update:** For the first nine months to 30 April, sales volumes were down 5% reflecting lower opening inventory and low spring milk collections.
- Revenues grew 7% because of higher prices, but this was insufficient to offset higher input costs leading to margin compression.
- Gross margin declined from 18% to 16% on the previous comparable period; primarily due to lower margin percentages in Consumer and Foodservice ([source](#)).

The first auction of the 2018/19 season prompted little excitement as stronger indices are important now, more than ever, to support a high \$7 milk price forecast from Fonterra. It remains favorable that the average winning price has been above prior year each auction since February, and those prices have been on top of what were already strong gains last year. There was likely a push to clear inventories to get ready for winter milk and plant maintenance; the premium built in for Instant (slightly higher fat content, enriched w/ vitamin A & D) WMP (~\$105/MT) over Regular indicates that volumes for that spec are harder to come by. For four months, C2 regular WMP has been trading within a \$90/MT range in either direction – the tightest on record for this time of year.

The NZ Dollar (Kiwi) is DOWN 5% against the US Dollar from the rise seen in April and on par with prior year levels, but values have improved over the past three weeks, which may be putting a damper on farmer confidence following the neutral-to-bearish GDT event. Analysts [were](#) expecting the Kiwi to continue to drop near 65c but nearby strength came instead. Furthermore, while the average mortgage across agriculture has decreased in the past six months, it is up from \$4.6 million to \$5.1m for dairy - the highest level since the surveys began in August 2015.

Medium heat SMP for July delivery jumped 7.3% from prior auction to \$2,285/MT or \$1.04/lb, a 15-month high that created an extremely inverted forward curve. C1 holds a \$285/MT premium over C5, the highest on record. Immediate needs for product remain intact following the late start to the Northern Hemisphere spring flush that is being followed up by record-breaking heat

across the US. NZ is the highest price in the world of the primary exporting regions and buyers continue to pay up for product. Fonterra's forecast offer volumes for event 213 were 3,925MT but product sold was nearly 15% higher.

The weighted average price for butter experienced the steepest decline for the calendar year while NZX traders were expecting a less aggressive drop near \$5,700/MT on C2 August delivery. With AMF falling at a slower pace, the premium moved higher from prior auction on a fat equivalent basis to +\$474/MT (C2). Butter prices are falling around the world and NZ must follow suit to remain competitive.

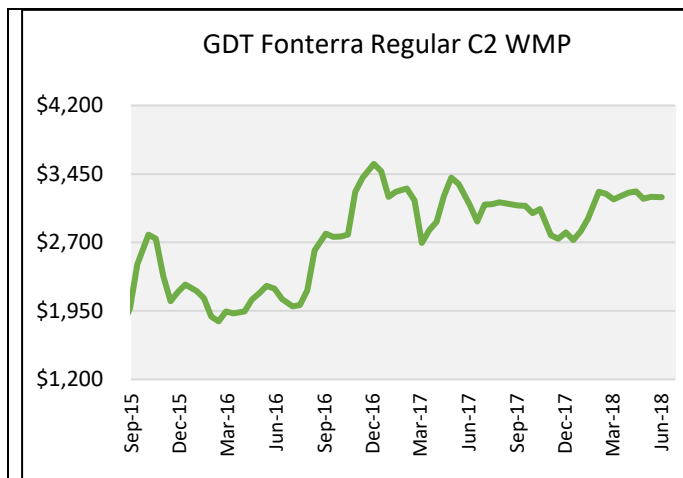
Global Dairy Trade Auction			
Trading Event 213 Results - 5 June 2018			
Commodity	Average Winning Price		% Change*
	\$/MT	\$/Lb	
Whole Milk Powder (WMP)	\$3,205	\$1.45	-1.1%
Skim Milk Powder (SMP)	\$2,051	\$0.93	0.3%
Anhydrous Milkfat (AMF)	\$6,222	\$2.82	-1.7%
Butter	\$5,581	\$2.53	-3.5%
Buttermilk Powder (BMP)	\$2,314	\$1.05	17.7%
Cheddar Cheese	\$3,998	\$1.81	-3.6%
Rennet Casein	\$5,015	\$2.27	2.7%
Lactose	\$714	\$0.32	3.9%
Avg Winning Price	\$3,487	\$1.58	-1.3%

*Change in GDT Price Index vs. last auction



Whole Milk Powder – Ho Hum... C1-C5 Declines Slightly, Forward Curve Flat

Supported above \$3,000/MT, extremely narrow range over past four months



- Since February (past nine auctions), the price of Contract 2 Regular-spec WMP has nestled into a tight, \$90/MT range (\$3,170 - \$3,260). There has been little to say during this time frame other than buyers remain supportive of the market above \$3,000/MT.
- While limited supply out of NZ was thought to have been the primary culprit for the elevated range, better-than-expected milk collections in April/May and a very aggressive initial price forecast for the 2018/19 season have done little to send buyers to the sidelines for “new crop” product.

- **HighGround’s Take:** WMP buyers have plenty to think about when it comes to supply in the coming season, whether it be the bullishness of Fonterra’s initial milk price forecast (NZ\$7.00 per mgMS), the challenges behind Mycoplasma bovis eradication, or restricted use of palm kernel expeller. Thus far, buyers have maintained an elevated, but non-aggressive forward curve in WMP prices. HighGround sees prices holding near or slightly above the \$3,000/MT range through NZ’s winter months as the industry waits for early-season production results.

Commodity	Contract 1 (July)		Contract 2 (Aug)		Contract 3 (Sep)		Contract 4 (Oct)		Contract 5 (Nov)		Contract 6 (Dec)	
	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.
Whole Milk Powder	\$3,186	\$1.45	\$3,222	\$1.46	\$3,195	\$1.45	\$3,211	\$1.46	\$3,208	\$1.46	\$3,281	\$1.49
Fonterra (regular)	\$3,175	\$1.44	\$3,195	\$1.45	\$3,165	\$1.44	\$3,185	\$1.44	\$3,190	\$1.45	\$3,275	\$1.49
% vs. last reported price	-2.0%		-0.2%		-1.4%		-1.1%		-0.5%		0.2%	
Amul (regular)			n.s.									
% vs. prev event												
Fonterra (Instant)	\$3,205	\$1.45	\$3,300	\$1.50	\$3,270	\$1.48	\$3,290	\$1.49	\$3,295	\$1.49	n.s.	
Premium to regular spec	\$30		\$105		\$105		\$105		\$105			
Fonterra - Guaranteed ATOD	n.s.		n.s.		n.s.		\$3,230	\$1.47	\$3,235	\$1.47	n.s.	
Premium to regular spec							\$45		\$45			
n.s. - No Product Sold												

Cheddar Cheese & Casein

Fonterra does not offer any product for August delivery, no matter the contract period, which means C2 will have nothing on offer in June. Contract 3 was not offered during May auctions, so the percentage increase below is being compared to the final event in April.

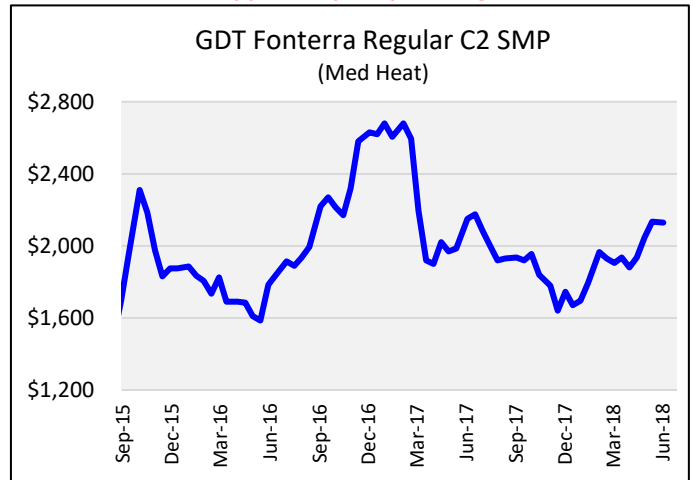
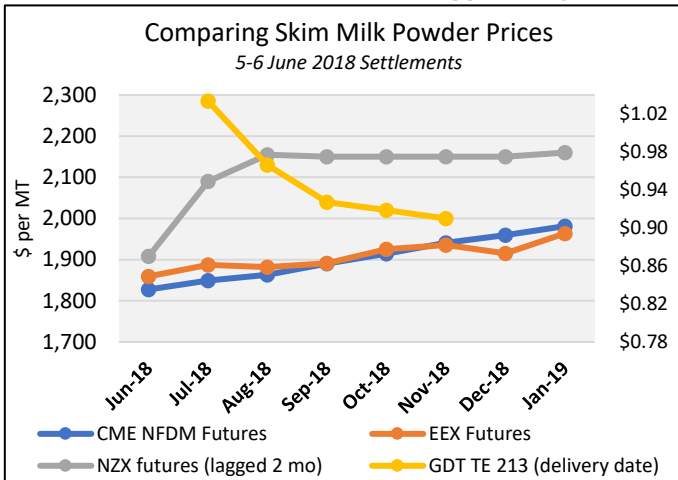
Commodity	Contract 1 (July)		Contract 2 (Aug)		Contract 3 (Sep)		Contract 4 (Oct)		Contract 5 (Nov)	
	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.
Cheddar Cheese	\$4,098	\$1.86			\$3,983	\$1.81	\$3,972	\$1.80	\$4,060	\$1.84
% vs. last reported price	-6.9%				3.3%		-2.5%		-0.8%	
Rennet Casein	\$5,175	\$2.35	\$5,004	\$2.27	\$4,985	\$2.26	\$5,010	\$2.27	\$5,065	\$2.30
% vs. last reported price	6.6%		2.4%		3.3%		2.2%		2.4%	
n.s. - no product sold if cell left blank - No Product Offered										

This is the first time in five auctions that Cheddar saw declines and likely due to a sharp increase in offer volumes for the coming season.

Casein prices rebounded after two straight declines in March, with C2 losing nearly 16% of its value. Casein is valued 24% below last year’s levels (C2 GDT).

Skim Milk Powder – Mixed Bag From Fonterra; Fifth Consecutive Increase for Arla

But inverted Fonterra GDT curve suggests buyers will take a more cautious approach for upcoming season needs



- Fonterra SMP posted a mixed bag at this week's event, with prices moving higher in C1, C4 and C5 while posting declines in C2 and C3, a somewhat unexpected result. That said, the key takeaway from this week's results is the inverted curve in Fonterra medium heat, with expectations that there will be plenty of supply later in the year. Nearby months carry a premium as those short Fonterra-spec (likely Asia) buyers must reach to grab limited supply at the tail-end of the NZ season.
- Arla SMP posted its fifth consecutive increase as limited fresh supply has the market creeping higher. In USD terms, EU SMP prices on GDT have increased by 19.2% since late March. Per the chart at top left, both the EU and US maintain a very tight spread to one another over the next eight months per their respective futures forward curves.

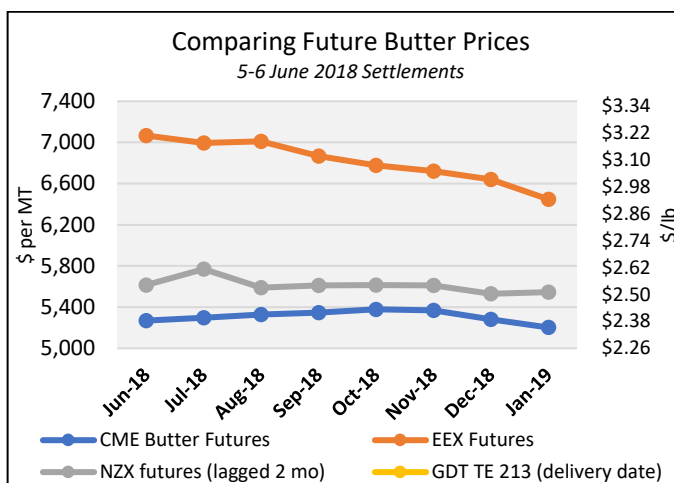
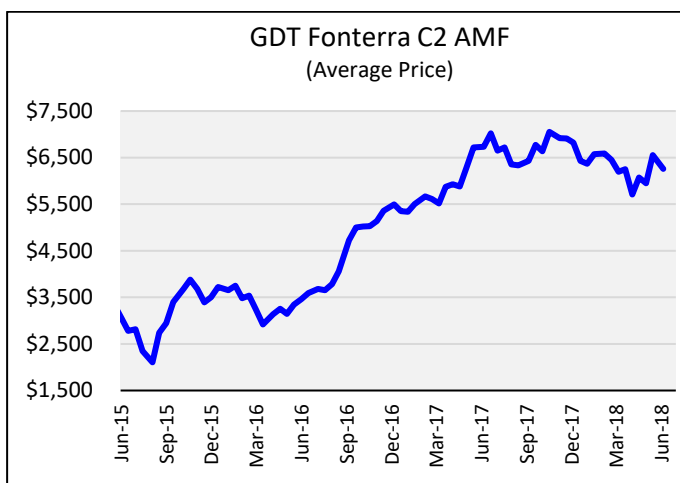
Commodity	Contract 1 (July)		Contract 2 (Aug)		Contract 3 (Sep)		Contract 4 (Oct)		Contract 5 (Nov)	
	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.
Skim Milk Powder	\$2,285	\$1.04	\$2,078	\$0.94	\$2,053	\$0.93	\$2,029	\$0.92	\$2,007	\$0.91
Fonterra - NZ (med heat)	\$2,285	\$1.04	\$2,130	\$0.97	\$2,040	\$0.93	\$2,020	\$0.92	\$2,000	\$0.91
% vs. last reported price	7.3%		-0.2%		-3.8%		1.3%		3.1%	
Fonterra - UHT	n.s.		\$2,195	\$1.00	\$2,110	\$0.96	\$2,070	\$0.94	\$2,050	\$0.93
Premium to regular spec			\$65		\$70		\$50		\$50	
Fonterra - Guaranteed ATOD (med heat)					n.s.		n.s.		n.s.	
Premium to regular spec										
Fonterra - NZ (low heat)			n.s.		n.s.		n.s.		\$2,000	\$0.91
% vs. last reported price									2.3%	
Amul (med heat)			\$2,500	\$1.13						
% vs. last reported price			-10.7%							
Arla (low heat - SE)			\$1,865	\$0.85						
% vs. last reported price			1.1%							
Arla (med heat -EU)			\$1,865	\$0.85						
% vs. last reported price			2.5%							
Polish Dairy (med heat)	n.s.									
% vs. prev event										

n.p. - No Price Published n.s. - No Product Sold if cell left blank - No Product Offered

Fonterra starting bid prices shown above

Milkfat Products – Disappointing Butter Result; AMF Mostly Lower But in Line with Expectations

Buttermilk powder rallies hard in both New Zealand and Europe



- Primary milkfat products (butter/AMF) took the prize for the most bearish results at this week’s auction, though AMF’s C2 declines were largely in line with expectations after the explosive move higher three weeks ago. The forward curve remains elevated from the unexpectedly lower price range in April but is still fairly flat, with just a slight inverse into next season’s peak months; all Contract periods are above \$6,100/MT.
- Butter prices were expected to see slight gains at this month’s auctions but fell short of that goal, down an average of 3.5% across all contract months. No delivery month was spared the losses though most were consistent. This could be the “[canary in the coal mine](#)” signaling further declines in global butter prices in the near term, though HighGround feels it would be too early to call a top to this market in 2018 as the hot summer months lie ahead. [EEX butter futures](#) are off sharply in early Wednesday trade and weakness has infiltrated the US CME butter futures market as well in recent days.
- While most butterfat products came in bearish versus expectations, buttermilk powder results were a different story. Holding the auction open an additional few rounds, BMP prices soared this week as buyers jumped on acquiring both Fonterra and Arla given its sharp discount to WMP. Fonterra’s 23.8% gain versus last month was the sharpest bounce since July 2017 (28.4%) and its spread versus Arla (+\$435/MT) is its widest since December. There is little to say in the BMP market other than it has been at a drastic discount to WMP for several months and is working to get back in line to historical levels.

Commodity	Contract 1 (July)		Contract 2 (Aug)		Contract 3 (Sep)		Contract 4 (Oct)		Contract 5 (Nov)	
	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.	\$/MT	\$/lb.
Anhydrous Milk Fat	\$6,258	\$2.84	\$6,255	\$2.84	\$6,194	\$2.81	\$6,169	\$2.80	\$6,173	\$2.80
% vs. last reported price	0.7%		-4.5%		0.0%		-1.5%		0.8%	
Butter	\$5,530	\$2.51	\$5,585	\$2.53	\$5,570	\$2.53	\$5,590	\$2.54	\$5,615	\$2.55
Fonterra (unsalted)	\$5,530	\$2.51	\$5,585	\$2.53	\$5,570	\$2.53	\$5,590	\$2.54	\$5,615	\$2.55
% vs. last reported price	-4.1%		-3.7%		-4.1%		-2.6%		-3.2%	
Buttermilk Powder (Fonterra - UHT)	\$2,650	\$1.20	\$2,525	\$1.15	\$2,275	\$1.03	\$2,300	\$1.04	\$2,180	\$0.99
% vs. last reported price	30.9%		23.8%		13.8%		15.0%		8.5%	
Buttermilk Powder (Arla - EU)			\$2,090	\$0.95						
% vs. last reported price			14.5%							

n.p. - No Price Published if cell left blank - No Product Offered

Lactose – EU Product Moves Lower; US Pool Currently Suspended

- Arla lactose rebounded this past week, though virtually back to the same price from two auctions prior after rolling back three weeks ago. The last four auctions have posted results in a tight range (\$29/MT) though the general sentiment of the market is steady to slightly firm.
- Polish Dairy offered M100 and M200 spec lactose but failed to report a price (as shown below).

Sweet Whey Powder – None sold at this week’s auction

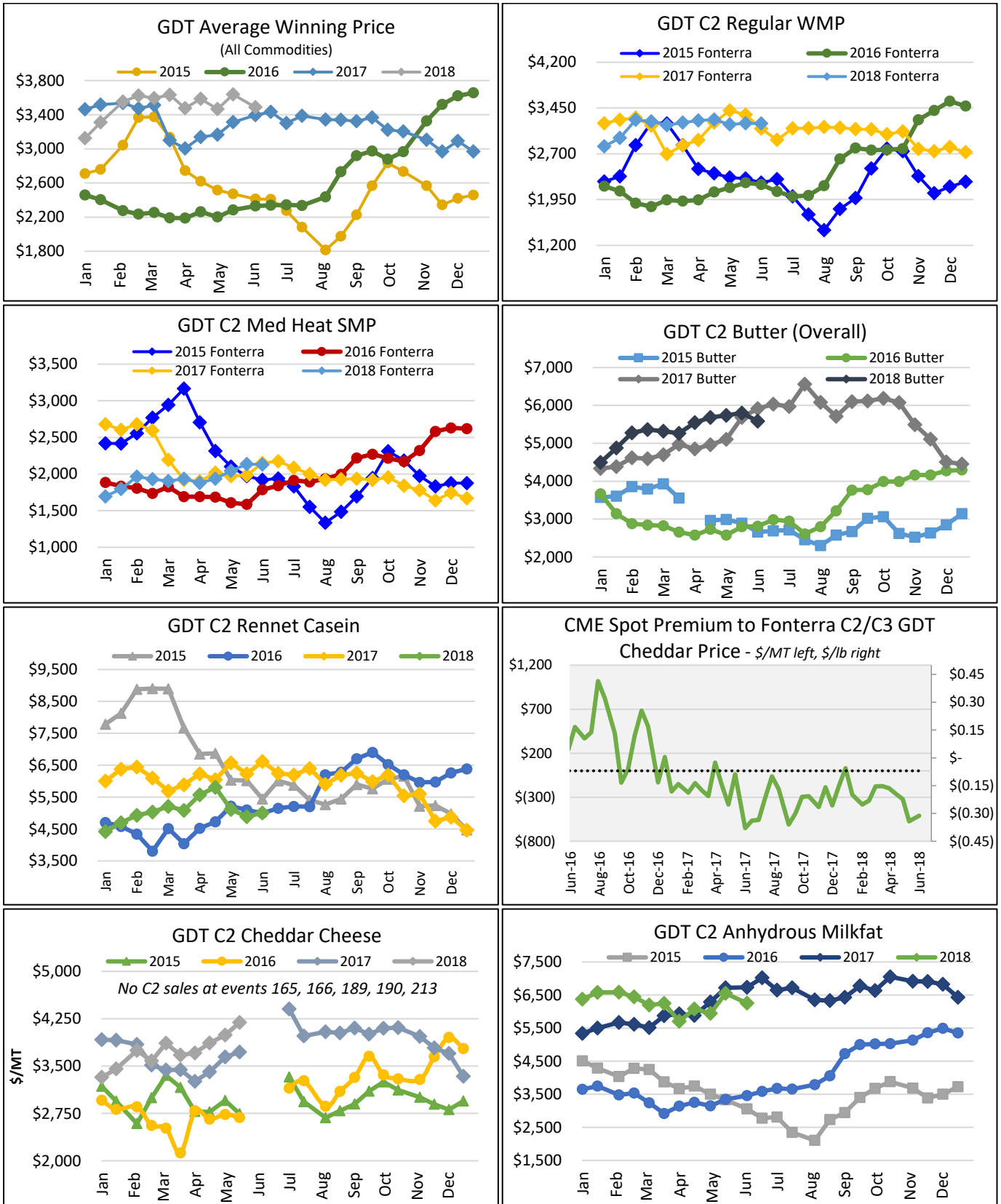
Commodity	Contract 1 (July)		Contract 2 (Aug)	
	\$/MT	\$/lb.	\$/MT	\$/lb.
Lactose	n.a.		\$714	\$0.32
% vs. last reported price			3.9%	
Lactose - Arla Food UM/M100/200 avg			\$714	\$0.32
% vs. last reported price			3.9%	
Lactose - Polish Dairy Food M100, M200	n.p.			
% vs. last reported price				
Sweet Whey Powder Polish Dairy	n.s.			
% vs. last reported price				
n.p. - No Price Published n.s. - No Product Sold If cell left blank - No Product Offered				

Eric Meyer | Alyssa Badger | Lucas Fuess

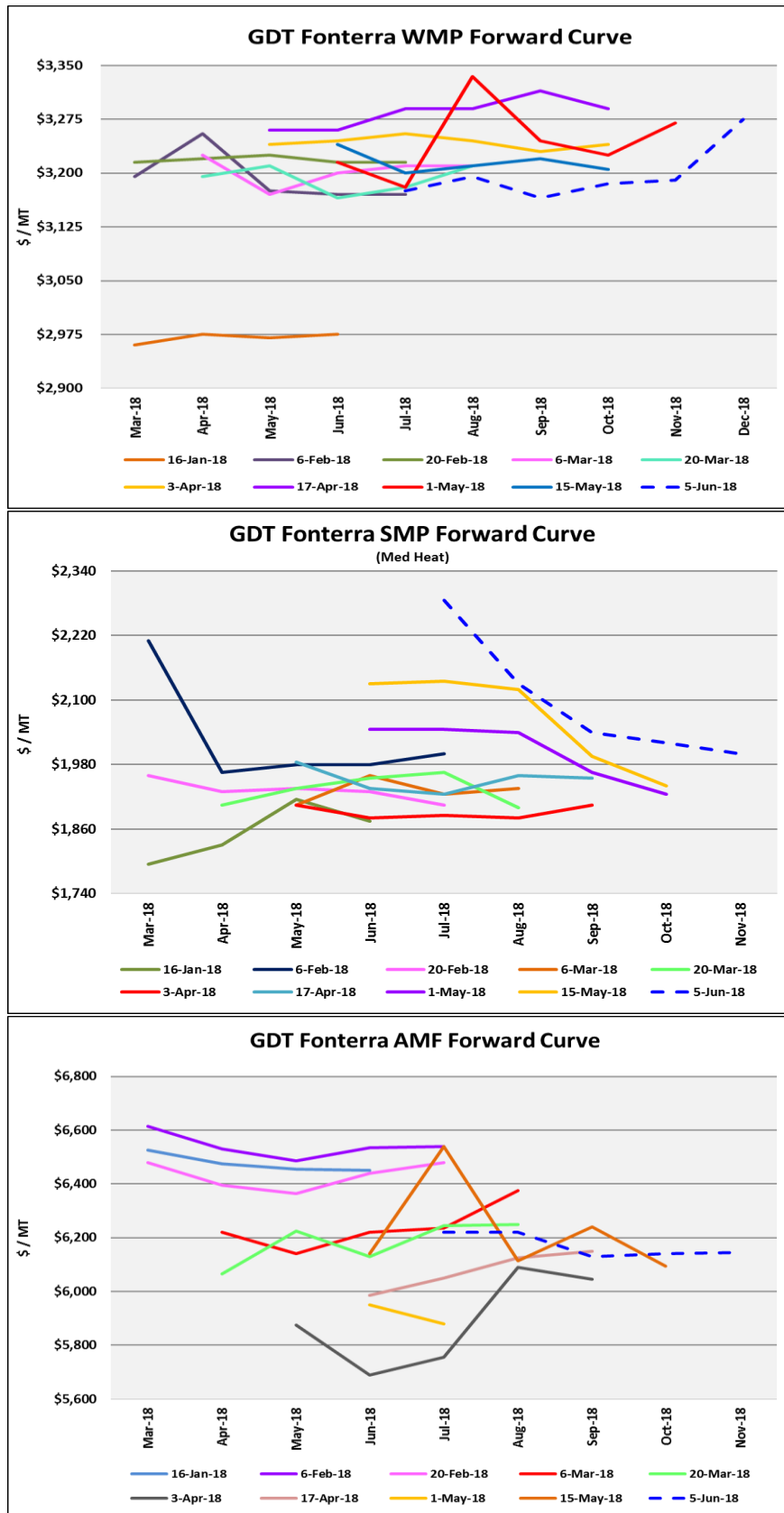
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Global Dairy Trade Trends

*All graphs are quoted in USD/metric ton



Forward Curve Historical Graphs



Prices Compared by Delivery Month

*All prices are quoted in USD/metric ton

<u> Fonterra Whole Milk Powder Results </u>				<u> Fonterra Skim Milk Powder Results </u>			
Delivery Month	TE 212 May 15	TE 213 Jun 5	% change	Delivery Month	TE 210 Apr 17	TE 211 May 1	% change
Jul-18	\$3,200	\$3,175	-0.8%	Jul-18	\$2,135	\$2,285	7.0%
Aug-18	\$3,210	\$3,195	-0.5%	Aug-18	\$2,120	\$2,130	0.5%
Sep-18	\$3,220	\$3,165	-1.7%	Sep-18	\$1,995	\$2,040	2.3%
Oct-18	\$3,205	\$3,185	-0.6%	Oct-18	\$1,940	\$2,020	4.1%

<u> Fonterra AMF Results </u>				<u> Fonterra Unsalted Butter Results </u>			
Delivery Month	TE 212 May 15	TE 213 Jun 5	% change	Delivery Month	TE 212 May 15	TE 213 Jun 5	% change
Jul-18	\$6,540	\$6,220	-4.9%	Jul-18	\$5,800	\$5,530	-4.7%
Aug-18	\$6,115	\$6,220	1.7%	Aug-18	\$5,810	\$5,585	-3.9%
Sep-18	\$6,240	\$6,130	-1.8%	Sep-18	\$5,740	\$5,570	-3.0%
Oct-18	\$6,095	\$6,140	0.7%	Oct-18	\$5,800	\$5,590	-3.6%

<u> Fonterra Cheddar Cheese Results </u>			
Delivery Month	TE 212 May 15	TE 213 Jun 5	% change
Jul-18	\$4,180	\$4,070	-2.6%
Aug-18	n.o.	n.o.	
Sep-18	\$4,055	\$3,960	-2.3%
Oct-18	\$4,065	\$3,960	-2.6%

About HighGround Dairy

HighGround Dairy launched in 2012 by industry veteran, Eric Meyer. Affiliated with HighGround Trading LLC, HighGround Dairy services all those interested in trading dairy futures and options markets. Through the brokerage division and its related consulting company, HighGround Advisory Group, it specializes in dairy hedging, risk management and market analysis services for farmers & cooperatives, processors, manufacturers, distributors, traders and end-users.

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