

Commodities Weekly

For the week ending Friday 11th December

Ending 2020 on a more uplifting note

ASB lifts 20/21 milk price forecast to \$7.00 as we reflect on rural resilience

Prices edged up again at the latest GlobalDairyTrade auction overnight. After bumper gains a fortnight ago, the overall price indices rose another 1.3%. Gains were strongest for the fat products, with butter prices up 6% and AMF up 1.9%, while whole and skim milk powder prices held onto last auction's gains and lifted 0.5% and 1.2%, respectively. The result wasn't too dissimilar from where the futures market was pointing prior to the auction.

The result reflects the fact that global demand is still holding up well, providing support for dairy prices. For whole milk powder, the key product for NZ, the last few month's gains mean prices have now edged ahead of where they were a year ago – just on USD\$3,200MT. Recent auctions have been marked by strong demand from China amid the recovery there, and the continued focus on food security. Pleasingly, the contract curve remains flat and stable, so price gains aren't being driven by short-term supply fears, but by steady demand thanks to rising consumption. The futures market is pricing whole milk powder north of the USD\$3,200MT out to the end of the season too.

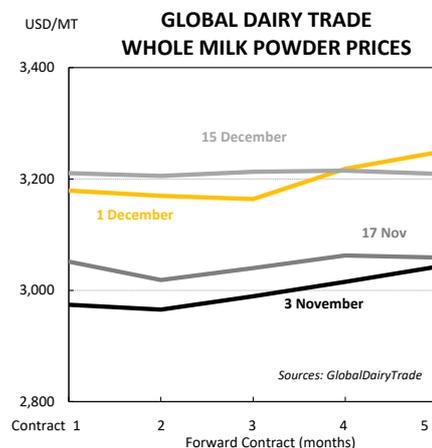
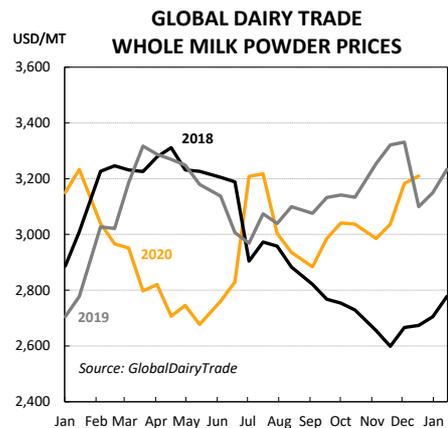
ASB is lifting its farmgate milk price forecast for the 20/21 season to \$7.00. This places it exactly in the middle of Fonterra's milk price range of \$6.70-6.30, which was raised earlier this month. The big factor to watch now is production over the summer, as the weather heats up. The strength of the NZD recently isn't likely to be much of a factor from here given Fonterra's hedging policies, but is likely to be more of a factor next season.

Our forecast revision is sign of how resilient the dairy sector has been through the pandemic. Back in March, at the height of COVID-related uncertainty, we thought there was a risk the milk price could go below \$6.

2020/21		
	ASB	Fonterra
Milk Price*	\$7.00	\$6.70-7.30

* per kg of milk solids (excluding dividend).

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder (WMP)	0.5%	4.2%	3,210
Skim Milk Powder (SMP)	1.2%	1.2%	2,930
Anhydrous Milk Fat (AMF)	1.9%	-10.5%	4,360
Butter	6.0%	10.0%	4,221
GDT Price Index	1.3%	10.5%	n.a.



By contrast, a figure closer to \$7 would represent only a small drop from last season's \$7.14.

Reasons to be thankful

The improving dairy outlook is part of a broader story – the rural sector has weathered the chaos of 2020 remarkably well. When the pandemic ramped up in earnest, we feared the year could be marked by steep falls in commodity prices that would really hit producers hard. Whilst we've seen some dramatic movements, our indices didn't fall by nearly as much as they did in the commodity price shock of 2014. Export activity has held up much better than many feared too.

Indeed New Zealand's primary sector has been a real blessing this year, amid the struggles other sectors have faced. Whilst tourism, education and the hospitality sector have faced plenty of challenges thanks to border restrictions, there have been some real standout performers on the rural side of the fence. Notably, NZ's kiwifruit harvest and export values hit a record high this season, and forestry prices have also proven remarkably resilient

That's not to say everything is hunky dory – with sheep and beef prices still soft. Both commodities are struggling amid continued restrictions in parts of Europe and ongoing Brexit-eve uncertainty – lamb prices are now down about 22% on this time last year, and beef prices are down 20%. With China steadily rebuilding its pig herd post-African Swine Fever, the global protein shortage that's supported prices over the last couple of years might also be less of an influence in 2021.

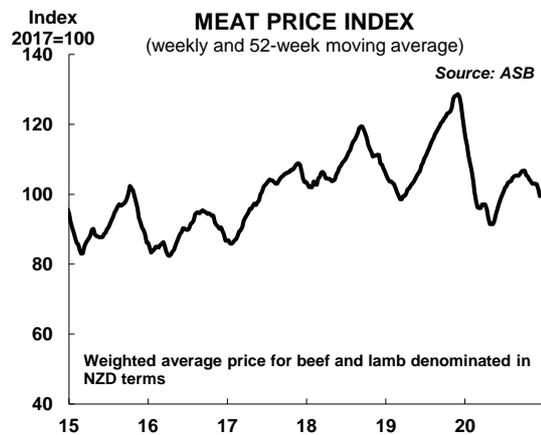
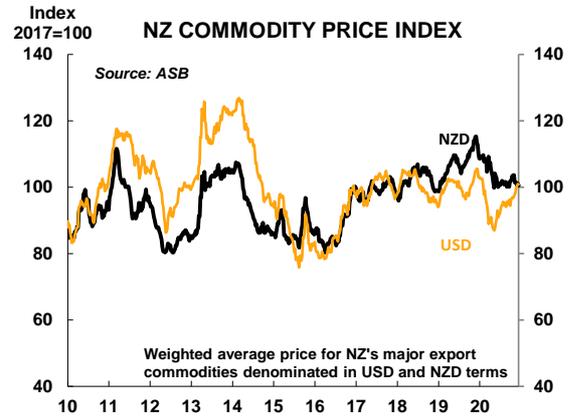
As we've noted in recent publications, increasingly the big headwind facing exporters is the strength of the NZD. Still, its all part of the same story – for a pro-cyclical currency like the kiwi, its hard to keep your head down if the global outlook is improving, our terms of trade remain high, and the strength of the domestic economy means a negative OCR is less likely.

ASB Commodities Index

The ASB Commodities Index eased 0.6% in NZD terms last week, as the strong kiwi continued to weigh on the index. The underlying USD indices were little changed over the week (down 0.1%). Once again, the NZD/USD was the main source of price movement (+0.5%), hitting a new two-year high north of the 0.7100 mark towards the end of last week.

Sheep and beef prices fell again (-1.2% in USD and -1.7% in NZ terms). With no auction last week, the dairy indices were fairly stable, lifting 0.2% in USD terms.

This is our last Commodities Weekly for 2020 before we break for the Summer (and what a year its been). We'll be back in the New Year. See you then.



ASB New Zealand Commodity Price Indices As at Friday 11th December 2020

	Index*	Week %	Year %**
Total NZD	100.5	-0.6%	-10.8%
Total SDR	97.7	0.3%	-7.8%
Total USD	100.9	-0.1%	-4.3%
Dairy USD	99.6	0.2%	-4.8%
Sheep/beef USD	97.1	-1.2%	-14.8%
Forestry USD	98.7	0.5%	5.5%
Fruit USD	118.6	0.5%	6.6%
NZD/USD	0.7081	0.5%	7.3%

* For all indices 2017 average = 100

** Percentage change since same week last year

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