

Commodities Weekly

For the week ending Friday 13th November



No news is good news

Prices lift a modest 1.8% at GDT auction as ASB retains \$6.75 forecast

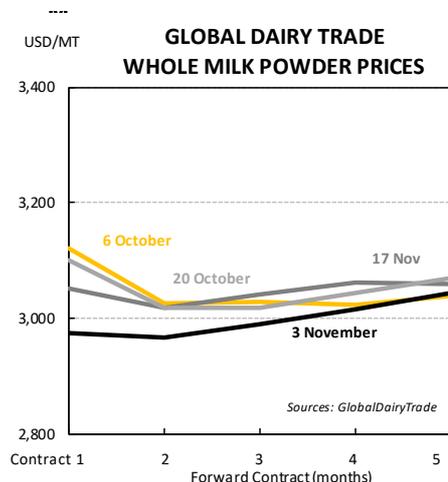
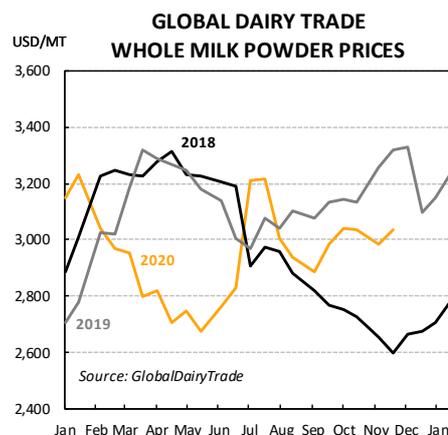
Prices firmed at the latest Global Dairy Trade Auction. The overall price index rose 1.8%, as did the underlying whole milk powder (WMP) index, reversing most of the easing we saw at the previous auction a fortnight ago. Skim milk powder (SMP) prices lifted 2.5%. Butter prices were mostly flat (+0.4%) after strong growth over recent auctions off the back of lower volumes on offer. **All up, the overall quantity sold was down about 7% on the same time last year.**

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder (WMP)	1.8%	-7.8%	3,037
Skim Milk Powder (SMP)	2.5%	-7.8%	2,799
Anhydrous Milk Fat (AMF)	4.1%	-19.0%	4,175
Butter	0.4%	-7.2%	3,838
GDT Price Index	1.8%	-1.2%	n.a.

The result was broadly in line with what we've seen at other recent auctions – prices moving less dramatically than earlier in the year, volumes down modestly on year-ago levels, and a relatively flat contract curve. In aggregate, the results continue to suggest a more settled market than we had earlier in the year, when sharp falls and steep lifts were the order of the day and COVID-driven uncertainty was at its peak.

We retain our \$6.75 milk price forecast for the 2020/21 season – near the Fonterra midpoint of \$6.80 – and we see the risks to this as balanced. Prices have continued to firm up nicely over recent auctions (despite last week's fall), and the WMP contract curve is stabilising just above the USD\$3000/MT mark. While China's WMP inventories are reportedly well stocked, domestic consumption is still on the up, which should help support demand at coming auctions. **On the whole, it's a far cry from the beginning of the season, when we were concerned that a sub-\$6 milk price was a real possibility**

The biggest uncertainty around our forecast is still domestic production. As we noted in our last update, grass growing conditions have been strong so far and season-to-date milk production is currently running about 3% ahead of last year. Still, there is a real risk that conditions could dry off substantially over the summer amid hotter temperatures and lower-than-average rainfall in the South Island.



ASB no longer expects OCR to move negative in 2020

In other news, we've also revised our forecast for the Official Cash Rate, and now expect it to remain at 0.25% through next year, rather than moving into negative territory. At last week's Monetary Policy Statement, the Reserve Bank of New Zealand (RBNZ) emphasised the resilience of the domestic economy, but highlighted ongoing uncertainties and unveiled further details around a new tool to provide further monetary stimulus – its Funding for Lending Programme (FLP). The FLP – which the RBNZ suggests will be operational from December – will provide banks with a source of cheap funding, that will place further downward pressure on retail interest rates. The tool is likely to have an incentive mechanism attached to it too, to drive banks to increase their lending.

Despite our change in forecast, we still expect the RBNZ to keep a negative OCR as a tool in its toolbox, and the risks remain skewed towards further support. Whilst the domestic economy has held up remarkably well in many respects, there is still plenty of uncertainty around the global outlook. Whilst last week's vaccine news was a very positive development, there are still plenty of downside risks in the near term. In particular, it looks like it will be a grim winter in the Northern Hemisphere amid rising COVID cases and new restrictions. A lot will depend too on how effective the FLP is at driving interest rates even lower – more details are to come in the weeks ahead.

Whatever the case, we expect interest rates to remain historically low for quite some time. Both lending and deposit rates are at historic lows, and our forecasts suggest there is further room for them to fall. Whilst rates will move higher eventually, that prospect is still several years away and interest rates will remain well below long-run averages for some time to come.

Corrections and Clarification on Brexit and NZ access to the UK market

Following our comments in last week's report, the Ministry for Primary Industries has provided us with clarification on several points regarding access to the UK market for NZ meat exporters. From 1 January 2021 (the end of the Brexit transition period), New Zealand exporters will still have access to the 'Country Specific Tariff Quotas' (CSTQs) for the UK, which incurs zero duty for sheep meat, and a 20% ad valorem duty for beef.

The "12% tariff" we referred to in our report (in reality a mixed tariff comprising a 12% rate and an additional GBP cost per 100kg of meat, based on the type) would only apply to volumes above that CSTQ. We have also updated last week's report on our website to clarify the situation as it stands and apologise for any confusion.

ASB Commodities Index

The ASB Commodities index fell 0.1% NZD terms last week, amid continuing gains for the NZD/USD. The USD index rose 0.7%, off the back of lifts in both the dairy index (+0.7%) and the sheep/beef index (+0.6%). Still, once again, the week's big story was the lift in the NZD.

The NZD/USD continued to advance (+0.8) as positive market sentiment continued in the aftermath of the US Presidential election and the COVID-19 vaccine news, as well as the RBNZ announcement.

ASB New Zealand Commodity Price Indices As at Friday 13th November 2020

	Index*	Week%	Year%**
Total NZD	100.6	-0.1%	-11.7%
Total SDR	95.1	0.7%	-8.8%
Total USD	97.5	0.7%	-5.7%
Dairy USD	97.0	0.6%	-6.4%
Sheep/beef USD	97.2	0.7%	-13.5%
Forestry USD	94.0	0.8%	6.7%
Fruit USD	102.4	0.8%	-6.5%
NZD/USD	0.6835	0.8%	6.8%

* For all indices 2017 average = 100

** Percentage change since same week last year

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