

Overcooked

- Dairy prices lifted by more than expected overnight.
- As dairy markets react further to the potential for recent wet weather to disrupt NZ supply.
- However, we think this price lift has been overdone, and prices may give back some of these recent gains.

Summary

If forecasting the milk price is hard, try forecasting NZ weather. Indeed, this growing season has been one of extremes. First the spring was very wet, then growing conditions were excellent over the summer and early autumn. Now we're back to very wet, and in some areas flooding.

These swings in weather and their impact on dairy production have kept dairy markets guessing. **By bidding prices higher overnight (and at previous auctions), markets are factoring a material impact on NZ production from the recent cyclones and the accompanying wet.**

However, we think this has been overdone. While it is very wet, and there has been flooding in areas like the Bay of Plenty, we don't expect a large impact on NZ production this season. **As a result, dairy auction prices may give back some of their recent gains.**

Auction Results

Dairy prices jumped overnight by more than expected. WMP (up 5.2%) and AMF (up 4.7%) and butter milk powder (up 21.8%) led the way. Overall auction prices lifted 3.6%; auction prices have now posted four consecutive gains.

However, the recent price rises feel a little overdone – as a result, we expect some pullback in prices over coming auctions. Dairy markets have reacted to the recent very wet weather, sending WMP prices 11.5% higher over the last three auctions.

While the severe weather has stymied an otherwise strong end to the NZ season, there potentially are a number of saving graces.

Firstly, the wet weather has come late in the season. Secondly, it followed generally good growing conditions over summer and early autumn. For example, March production spiked over 10% higher than March 2016. Lastly, the major dairying regions have escaped the worst of the production impacts.

With this in mind, **we expect production to fall by up to 2% compared to last season.** Although, we note that production will vary widely across the country by season end. For example, some areas of the North Island are likely to be well short of that number, whereas in many South Island areas production may be close to on par with last season.

Implications

This boost to auction prices and the lateness in the season raises the possibility of a higher milk price this season. As result, we place our 2016/17 milk price under review.

Looking to next season, we expect prices to remain firm at or near current levels. **In terms of next season's milk price, we stick to \$6.75/kg,** with the recent auction price strength offset by our view that the NZD is likely to climb over 2017.

Season-end Forecasts

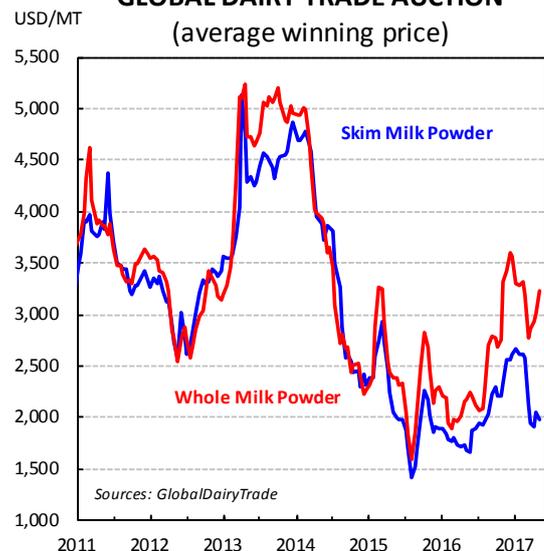
	2016/17		2017/18	Long Run
	Fonterra	ASB	ASB	ASB
Milk Price*	\$6.00	\$6.00	\$6.75	\$6.50-\$7.00

* per kg of milk solids (excluding dividend).

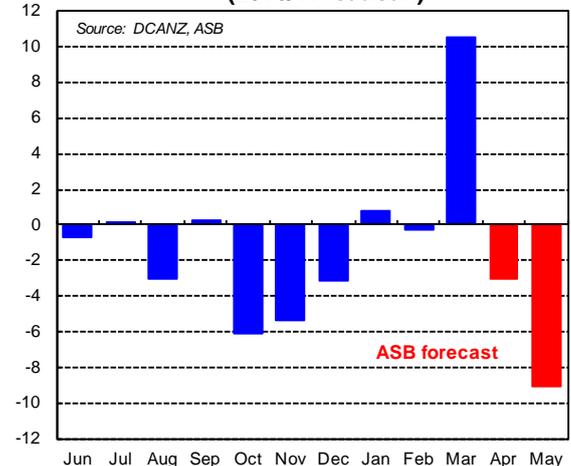
Key Auction Results

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder (WMP)	5.2%	50.9%	3,233
Skim Milk Powder (SMP)	-0.9%	20.2%	1,982
Anhydrous Milk Fat (AMF)	4.7%	94.4%	6,185
Butter	1.1%	92.5%	4,911
GDT Price Index	3.6%	60.7%	n.a.

GLOBAL DAIRY TRADE AUCTION
(average winning price)



NZ MILK SOLIDS PRODUCTION
(2016/17 season)



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