

Dairy detour

- We revise our 2016/17 milk price forecast down by 50 cents to \$6.00/kg.
- The revision comes on the back of sliding dairy prices at the auction overnight.
- However, while this puts a damper on this season's milk price, our healthy outlook for 2017/18 remains in place.

Summary

This summer has been a good one for the key NZ dairying regions. In fact, recent rain and moderate temperatures have helped farmers recoup some of the early season production losses. For example, we recently lifted our production forecast for the season to a 2% decline on last season, from a 5% drop forecast at one stage.

However, **higher production is a double-edged sword.** That is more than anticipated milk quickly translates into lower dairy prices. Heading into the auction overnight, whole milk powder (WMP) prices had already fallen 10%, before last night's result added an exclamation mark to this year's fall.

That all said, **weather can only have a temporary impact on production and prices – eventually dairy fundamentals kick back in.** On that front, we retain our positive outlook for the milk price over the medium term. And with the global dairy outlook positive, we expect relatively healthy global dairy prices over the second half of 2017 and beyond.

In that sense, we expect the milk price to take a detour downwards in the short-term i.e. this season, but our healthy forecast for next season remains in place. Specifically, **we revise our 2016/17 forecast down by 50 cents to \$6.00/kg, but retain our \$6.75/kg forecast for 2017/18.**

7 March auction comments

Dairy prices slid overnight largely in line with expectations. WMP and SMP led prices lower, dipping 12.4% and 15.5%, respectively. Overall auction prices fell 6.3%.

The price weakness follows a partial turnaround in this season's production. For example, we lifted our nationwide production (i.e. for all dairy companies) forecast to a 2% decline compared to last season, from a 5% decline previously. Fonterra made a forecast change of similar magnitude for its milk collections. In addition last week, Fonterra lifted its forecast auction supply for the next 12 months by 4% from its forecast at the previous auction.

Moreover, this season's weather risks have receded. With recent rain in most parts of the country and autumn underway, the improvements in production are likely to be maintained over the remainder of the season.

As a result, **we expect the price softness may remain over coming auctions.** However heading into next season and as this extra milk clears markets, we expect WMP prices to remain well-supported as the broader production picture remains soft.

Implications

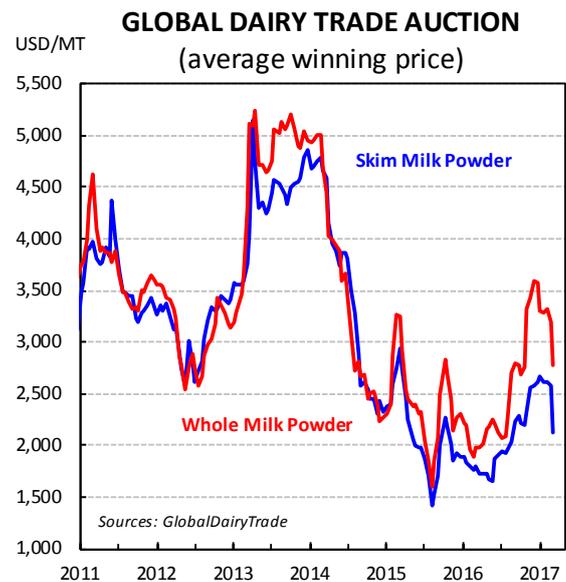
We revise our 2016/17 milk price forecast back down to our original \$6.00/kg from \$6.50/kg. That said, we maintain our relatively healthy outlook for 2017/18 and our \$6.75/kg forecast.

Season-end Forecasts

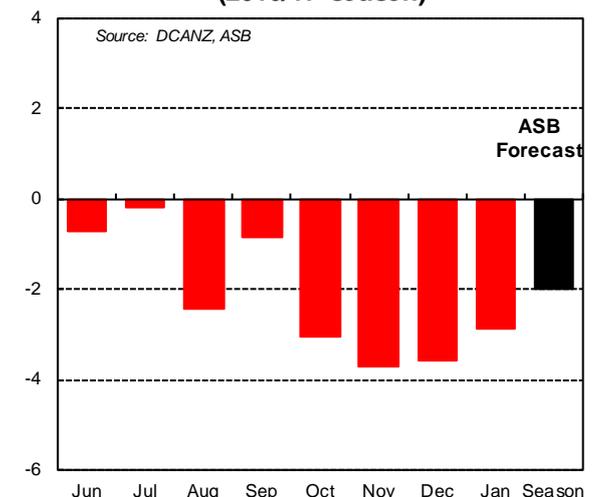
	2016/17		2017/18	Long Run
	Fonterra	ASB	ASB	ASB
Milk Price*	\$6.00	\$6.00	\$6.75	\$6.50-\$7.00

* per kg of milk solids (excluding dividend).

Key Auction Results



MILK SOLIDS PRODUCTION (2016/17 season)



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