

Rural Economic Note

Fonterra Milk Price Forecast Update

20 October 2021

ASB lifts 21/22 Milk Price forecast to \$8.75 per kgms

Milk Price Forecast Update

	2021/22	
	ASB	Fonterra
Milk Price*	\$8.75	\$7.25- \$8.75

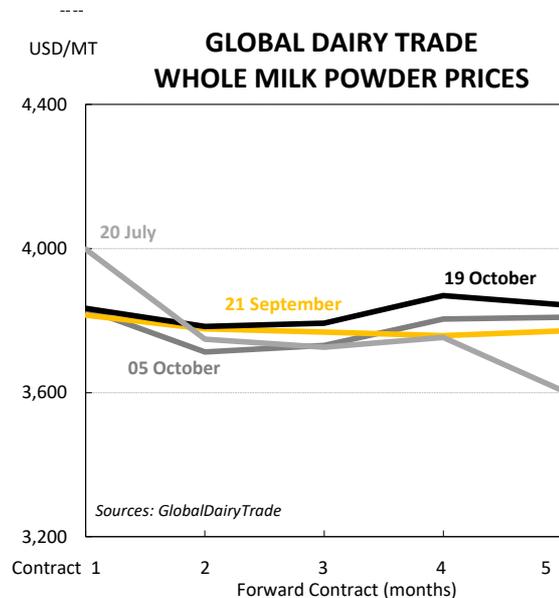
* per kg of milk solids (excluding dividend).

Dairy prices gained in line with market expectations last night. The overall Global Dairy Trade (GDT) auction price index lifted 2.2%, with Whole Milk Powder (WMP) up about 1.5%. That result aligns roughly with where futures pricing was sitting pre auction. Still, it's not the headline moves that are key.

The real story is that forward contracts point to prices maintaining momentum well into the latter half of the season. The GDT contract curve developed a sharpish downward slope over the winter, but spring developments have seen the curve flatten over the past few quarters (see chart opposite) with prices stabilising in a healthy USD\$3700-3900/MT range. There will be further movement here as we head into summer, but the implication is that buyers expect supply to remain tight moving into the latter half of the season.

On that note, it looks increasingly likely production will undershoot the expectations most of us held earlier in the year. At the beginning of the season, the general expectation was that higher prices would produce a supply response that would in turn ease future pricing pressures, in line with the usual dairy cycle. That dynamic now looks much less likely – NZ milk production has been slow to ramp up as it heads into the peak production months. Production is down 4% year-on-year over August and likely remained soft in the September and October. According to our friends at the NZX, pasture growth continues to be hampered by the prevailing weather conditions. We now expect NZ production to wind up 0.5-1% lower than last season.

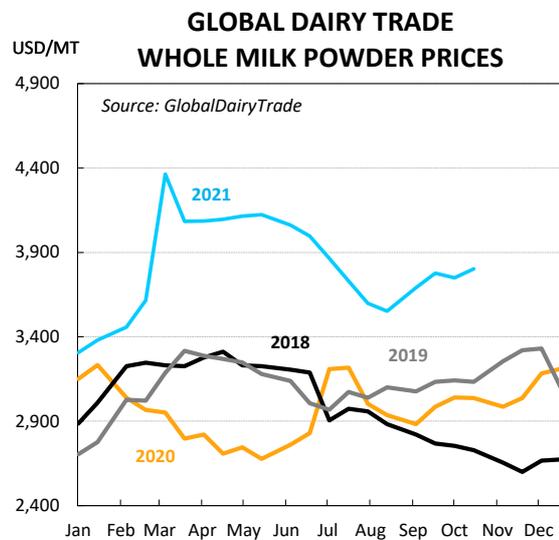
The Southern Oscillation Index (a weather measure that correlates with dairy production) suggest that conditions



could improve in the months ahead, but with feeds cost high and logistics issues prevalent, farmers may struggle to ship in feed – there’s not a lot of room for error. **It’s those supply anxieties that have seen auction buyers shift their expectations and futures prices rally sharply over recent weeks.**

We’ve lifted our 2021/22 season forecast by 55c to \$8.75 per kgms. GDT events over the first half of spring have shown no sign of demand softening and, with supply continuing to look tight, we’re comfortable making a sizeable upward revision. Fonterra should also be around 80%+ hedged by this point in the season, and we expect the co-op could wind up with an effective exchange rate just north of the 0.69 mark – a favourable exchange rate considering where NZ commodity prices are.

We caution there’s still an awful lot of uncertainty – commodity markets have been particularly volatile over 2021 thus far. **Still, the trends over the beginning of spring suggest that the possibility a record farmgate milk price for the season is very much live.**



GlobalDairyTrade Auction Results

Stream	Product	% change in index since last event	Annual % change in index	Weighted Average Price US\$/MT
Milk Powder Stream	Whole Milk Powder (WMP)	1.5%	25.2%	3,803
	Skim Milk Powder (SMP)	2.5%	20.3%	3,401
	Anhydrous Milk Fat (AMF)	2.5%	50.1%	6,151
Mixed Stream	Butter	4.7%	38.8%	5,111
	Butter Milk Powder (BMP)	0.0%	0.0%	n.a.
Cheese	Cheddar	2.9%	28.8%	4,426
	GDT Price Index	2.2%	36.7%	n.a.

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