

Rural Economic Note

Global Dairy Trade Auction

03 October 2018

NZ production hits the ground running

- Dairy prices posted a broad-based fall overnight.
- With recent price weakness reflecting strong NZ production.
- For now, we maintain our 2018/19 milk price forecast of \$6.50/kg, but continue to note downside risks.

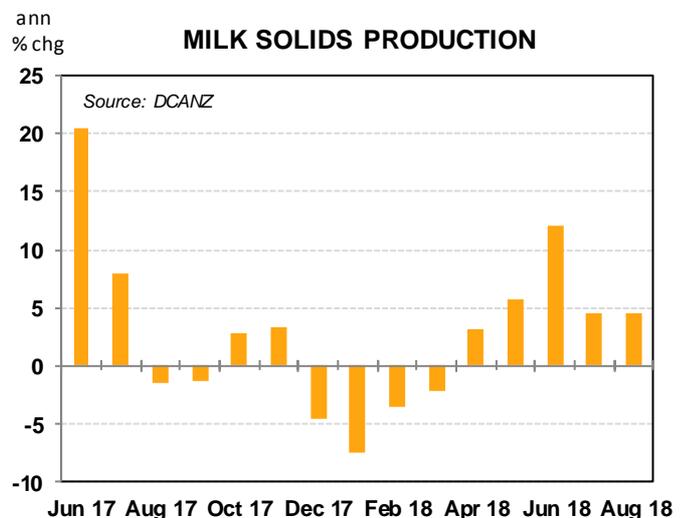
Summary

2018/19 NZ production has hit the ground running. For the first three months of the season, production is running 5.4% ahead of the same three months last season.

So far the weather has been very helpful for production. Mild winter temperatures and soil moisture levels have both supported growing conditions. In addition, farm cashflows are positive, helping farmers purchase the necessary feed and fertiliser to maintain healthy levels of production.

It is, however, still early days in the season. The first three months of the season traditionally account for just 8% of the season's production. Hence there is a lot of water (or milk) to go under the bridge.

From here, **NZ production will be a key factor for the direction of dairy prices over the remainder of the season.** We anticipate production growth of 2% compared to last season. Production growth in excess of this level would likely lead to additional dairy price weakness and vice versa. Indeed, **our \$6.50/kg 2018/19 milk price forecast is also based on our 2% NZ production growth forecast.**



Auction Results, 2 October

Dairy auction prices dipped 1.9% overall overnight.

Overall prices have now fallen in eight out of the last nine auctions, and are down 15.7% over that period.

The price weakness was broad-based, with five out of the six products we monitor posting falls. Key whole milk powder (WMP) prices dipped 1.2%, while skim milk powder prices slipped 0.3%. The WMP price fall was in line than the fall signalled by the futures market ahead of the auction.

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder	-1.2%	-7.8%	2,753
Skim Milk Powder	-0.3%	-0.7%	1,982
Anhydrous Milk Fat	-4.4%	-22.4%	5,069
Butter	-5.9%	-30.9%	4,016
GDT Price Index	-1.9%	-14.5%	n.a.

In annual change terms, overall prices have fallen 14.5%. Moreover, overall prices are now at their lowest since October 2016 in USD terms. **In NZD terms, however, the annual fall is a much more modest 2.4%.**

In the short-term, we expect more downward pressure on dairy prices. NZ is at its seasonal peak in production in October and in line with this peak auction volumes are also at their highest level for the year. This additional auction product will keep the downward pressure on prices for the time being.

Looking over the rest of the season, broader NZ production trends will be a key factor for prices. At this stage we anticipate NZ production growth of 2% for this season compared to last. Production growth in excess of this level would likely lead to additional dairy price weakness and vice versa.

Implications

For now, we stick with our 2018/19 milk price forecast of \$6.50/kg, but continue to note the downside risks.

Farmgate Milk Price Forecasts

	2018/19		Long Run
	Fonterra	ASB	ASB
Milk Price*	\$6.75	\$6.50	\$6.50-\$7.00

* per kg of milk solids (excluding dividend).

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