

Rural Economic Note

Global Dairy Trade Auction

4 March 2020

Down smalls

- Dairy auction prices fell modestly overnight and are showing signs of stabilisation.
- Our view remains that the dairy market impact of the virus outbreak will prove modest and short-lived.
- We stick with our 2019/20 milk price forecast of \$7.40/kg, but also note upside risks to our 2020/21 forecast.

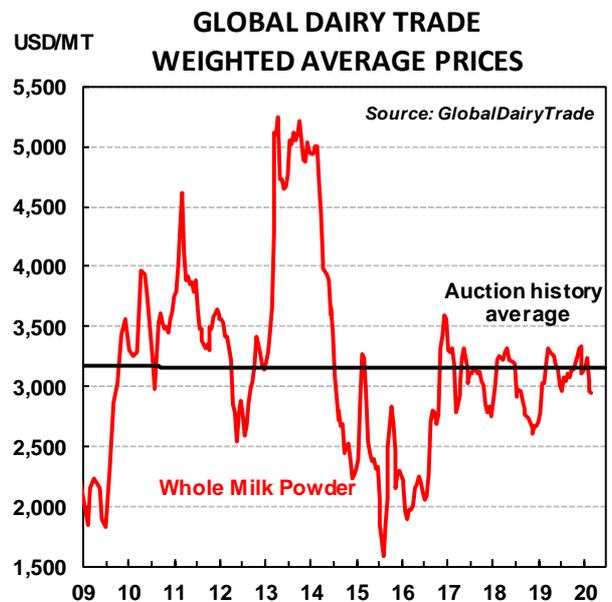
Summary

Dairy prices are showing signs of stabilisation. After initially falling in response to the coronavirus by 6.2%, key whole milk powder prices have fallen by progressively smaller amounts in the two auctions since.

Meanwhile, the number of new virus cases in China is falling. In addition, some normality is returning to the Chinese economy, albeit in patches. Encouragingly, Fonterra reported last week that while there was some disruption, its products were reaching Chinese markets.

These developments are consistent with our view that the virus impact on dairy markets will prove modest and short-lived. Note this view hasn't changed with the outbreak spreading to new hotspots, including South Korea, Italy and Iran. Note, we remain focused on Chinese market developments as NZ dairy exports to China dwarf exports to the more-recent virus hotspots of South Korea, Italy and Iran.

Despite the encouraging signs, we acknowledge there remain many moving parts to dairy markets. With this in mind, **we will continue to review our 2019/20 milk price forecast \$7.40/kg as information comes to hand.**



Auction results, 3 March

Dairy auction prices fell modestly overnight and by less than expected. Key whole milk powder (WMP) prices drifted 0.5% lower, while overall prices fell 1.2%. The 0.5% WMP price fall was noticeably less than the circa 3.5% fall indicated 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	-0.5%	-8.4%	2,952
Skim Milk Powder	-3.2%	10.8%	2,747
Anhydrous Milk Fat	-1.7%	-26.6%	4,302
Butter	1.0%	-13.6%	4,131
GDT Price Index	-1.2%	-3.2%	n.a.

Prices are now beginning to stabilise. Over the three auctions since the coronavirus outbreak began to impact dairy markets, WMP and overall prices have slipped by around 9%. Focusing on WMP prices, most of the 9% fall came at the 4 February auction (-6.2%), with the magnitude of the price falls then reducing in the two auctions since (-2.6% on 18 February, followed by -0.5% overnight).

This pattern fits with our view that the coronavirus impact will prove modest and short-lived. As business as usual conditions slowly return to normal in China, both dairy demand and prices are likely to rebound over coming months. Indeed, we took comfort in Fonterra’s statement last week that while *“there has been a slow-down in processing... at ports. [Importantly though], our product is continuing to be cleared by customs and quarantine officials.”* Note, we remain focused on Chinese market developments as NZ dairy exports to China dwarf exports to the more-recent virus hotspots of South Korea, Italy and Iran.

Meanwhile, **we remain bullish on the prospects for 2020/21.** We anticipate that global dairy markets will return to normal by the time the new season begins in earnest. If this is indeed the case, then market fundamentals, including tight global dairy supply, are likely to be supportive of global dairy prices. Moreover, the recent NZ dollar falls (currently trading at around US\$0.6290) is providing an opportunity to hedge at a very supportive level for the season ahead.

Implications

We stick with our 2019/20 milk price forecast at \$7.40/kg. That said, we point out that there remain many moving parts to dairy markets currently and our forecast may require tweaking over the coming months.

As discussed above, we are bullish on the prospects for 2020/21 and see upside to our milk price forecast of \$7.50/kg.

Farmgate Milk Price Forecasts

	2019/20		2020/21	Long Run
	Fonterra	ASB	ASB	ASB
Milk Price*	\$7.00-\$7.60	\$7.40	\$7.50	\$6.50-\$7.50

* per kg of milk solids (excluding dividend).

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