

Rural Economic Note

Global Dairy Trade Auction

5 February 2020

It could have been worse

- Concerns around the coronavirus outbreak drove dairy prices lower overnight.
- However, there were signs in the auction detail that virus impact on dairy markets will prove short-lived.
- We maintain our 2019/20 milk price forecast at \$7.50/kg, but note ongoing risks.

Summary

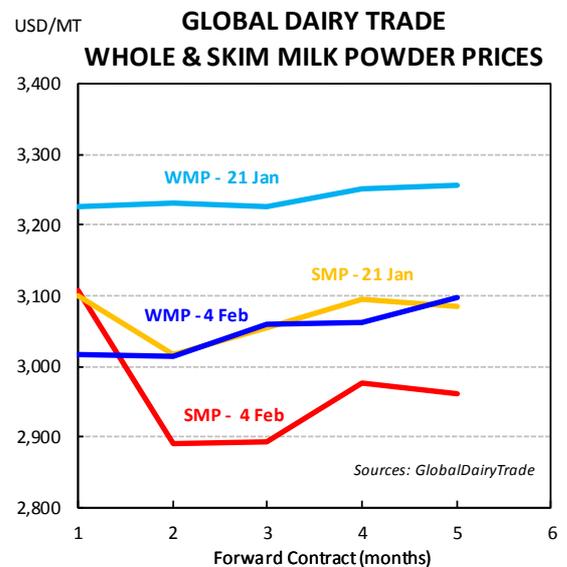
It could have been worse. Whole milk powder prices fell overnight, but the fall was no worse than expected. Indeed, prices fell by more back on 17 December, and the price fall overnight didn't even make the top 30 of auction price falls.

Moreover, **the auction detail was encouraging.** For example, Chinese buyers remained active at similar levels to recent auctions. In addition, three product prices actually rose, while the overall auction price fall was a moderate 4.7%.

These signs are consistent with our central view that the coronavirus impact on dairy markets and prices will be modest and short-lived. In other words, we expect dairy market fundamentals to reassert themselves as the dominant driver of prices before too long.

Nonetheless, we remain vigilant. The outbreak situation is very fluid and, with that in mind, dairy price implications are subject to change. Indeed, another false step by auction prices at this relatively late stage of the season and we will reassess our 2019/20 milk price forecast of \$7.50/kg.

At the same time, **we re-cast one eye on NZ weather and drought conditions.** A fully-fledged drought has the capacity to throw dairy prices equally in the opposite direction. In short, watch both spaces!



Auction results, 4 February

Concerns around the coronavirus outbreak drove dairy auction prices lower overnight. Key whole milk powder (WMP) prices slid 6.2%, while overall prices fell a more moderate 4.7%.

The WMP price fall was on the positive side to expectations.

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder	-6.2%	0.6%	3,039
Skim Milk Powder	-4.2%	15.4%	2,907
Anhydrous Milk Fat	-4.5%	-17.4%	4,626
Butter	0.2%	-6.6%	4,258
GDT Price Index	-4.7%	4.2%	n.a.

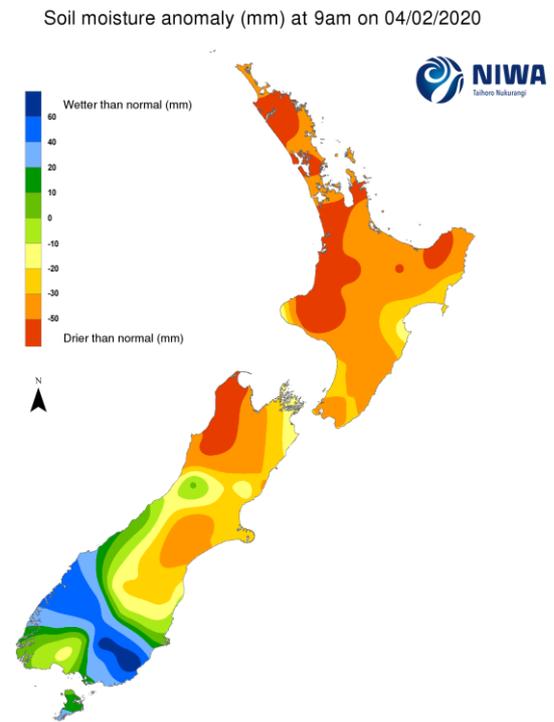
Futures pricing ahead of the auction had pointed to a circa 7% fall. We also note that the 6.2% is relatively modest by historical auction standards. For example, roughly 14% of auctions have recorded larger than falls than the auction overnight.

Other auction prices fared better. Three products recorded price gains (cheddar, casein and butter) while the overall index was down a more modest 4.7%.

Meanwhile, other details hinted that the price fall may be short-lived. Prices for later-dated contracts were higher than for shorter-dated ones. Notably, Chinese buyers were still active, with the number of buyers from North Asia bang on the average number for the last three months.

Nonetheless, we remain vigilant. The outbreak situation is very fluid and, with that in mind, dairy price implications are subject to change. Over the coming days, we will monitor the dairy futures market for further market developments ahead of the next auction in two weeks' time.

At the same time, **we also begin to return our gaze to NZ drought conditions.** In particular, the key Waikato region is very dry in parts, while the Taranaki, Northland, Nelson and parts of Canterbury are also very dry. If drought conditions continue to worsen over coming weeks, dairy prices have the potential to swing quickly back the other way.



Implications

At this juncture, **we stick with our 2019/20 milk price forecast of \$7.50/kg**, while noting the risks on both the downside (from coronavirus) and upside (from drought).

Farmgate Milk Price Forecasts

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

* per kg of milk solids (excluding dividend).

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