

Rural Economic Note

Global Dairy Trade Auction

06 June 2018

Taking stock

- Dairy prices were soft in the auction overnight.
- This price softness may reflect firm NZ production over April.
- However, we suspect the global butter shortage remains acute and that this price weakness will be short-lived.

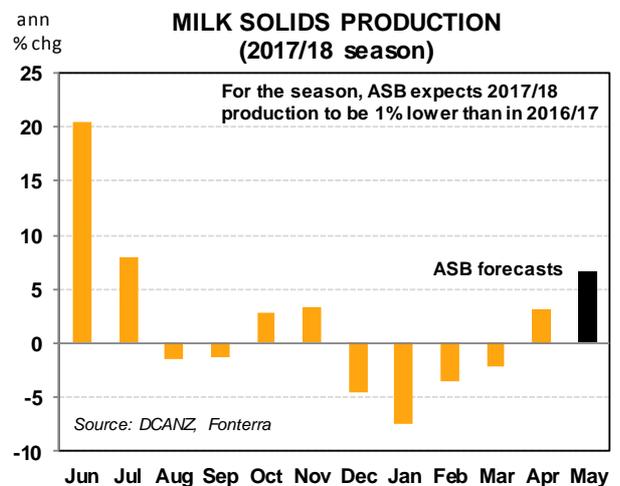
Summary

After significant moves in both milk fat prices and the NZD/USD over May, **June has kicked off on a softer note.** Overall auction prices were down a touch and also softer than we had expected based on futures prices ahead of the event.

This price softness may reflect firm NZ production over April. Nationwide production i.e. for all processors came in 3.1% higher than back in April 2017. That said, April production is modest compared to other months, accounting for around 7% of annual production.

Notably, milk fat prices were weak, albeit after recent price strength. Butter prices fell 3.5%, while anhydrous milk fat prices fell 1.7%.

However, we suspect the global butter shortage remains acute. The boost from firm April production is likely to be short-lived. Indeed, **we still expect butter and/or anhydrous milk fat prices will set fresh record highs over the coming months.**



Auction Results, 5 June

Dairy auction prices were weak overnight. Overall prices fell 1.3%. Similarly, whole milk powder prices fell 1.1%, which was a touch weaker than our expectations for no change.

Meanwhile, milk fat prices were weak overnight, perhaps alleviated by firm April production. Butter prices dipped 3.5%, while anhydrous prices fell 1.7%.

| Product | % change in index since last auction | Annual % change in index | Weighted Average Price US\$/MT |
|--------------------|--------------------------------------|--------------------------|--------------------------------|
| Whole Milk Powder | -1.1% | 2.8% | 3,205 |
| Skim Milk Powder | 0.3% | -7.7% | 2,051 |
| Anhydrous Milk Fat | -1.7% | -5.3% | 6,222 |
| Butter | -3.5% | -3.1% | 5,581 |
| GDT Price Index | -1.3% | -4.0% | n.a. |

However, **we anticipate that this milk fat price weakness will be short-lived and prices are likely to push higher again over coming months.** The weakness follows recent price strength and prices are nearing record highs. Butter prices, for example, had lifted around 9.0% over the past four auctions. Moreover, firm April production can only partially make up for earlier production weakness. In other words, we suspect the global butter shortage remains acute and prices are likely remain under upward pressure.

Looking at other products, skim milk powder prices were up a touch (0.3%), while casein prices lifted 2.7%. In contrast, cheddar prices fell 3.6%. All up, four out of the seven products we monitor posted gains.

Implications

For now, **we stick with our 2018/19 milk price forecast of \$6.50/kg, but note upward pressure remains on this forecast.** Indeed, despite the auction price fall overnight, the ‘spot milk price’ remains above \$7.00/kg. For our part we wait to confirm our suspicions on the upward path of butter prices. With this in mind, we keep our 2018/19 forecast ‘under review’. In contrast, we do not anticipate any further material changes in the 2017/18 milk price forecast from this point.

Farmgate Milk Price Forecasts

| | 2017/18 | 2018/19 | | Long Run |
|-------------|--------------|----------|--------|---------------|
| | Fonterra/ASB | Fonterra | ASB | ASB |
| Milk Price* | \$6.75 | \$7.00 | \$6.50 | \$6.50-\$7.00 |

* per kg of milk solids (excluding dividend).

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