

Rural Economic Note

Global Dairy Trade Auction

06 September 2017

It's raining...again

- Overall dairy prices were largely unchanged overnight.
- While whole milk powder (WMP) prices dipped unexpectedly, butter prices have neared a fresh record high.
- Meanwhile, we see potential for a combination of wet NZ weather and surging global butter demand to lift prices over coming months.

Summary

It's raining, again. Indeed, 2017 has been very wet, with NIWA reporting that some parts of the North Island have received their average annual rainfall already this year.

And now the rain is starting to hurt production. Reportedly, production is down versus last season in some key regions. While it is still early spring, if the rain continues and production remains weak, prices will rise.

Meanwhile, global demand for milk fats continues to surge. In Europe, butter shortages have led to a price spike in European prices to \$US7,750/MT, well above current NZ prices. At these levels Europeans buyers are likely to increasingly turn to NZ for butter supply.

These developments are a recipe for higher prices. Time is running out for NZ weather to improve. If it doesn't soon, **we see potential for this season's milk price to quickly move to \$7.00/kg or above.** Watch this space.

Auction Results

Overall dairy auction prices were effectively unchanged overnight (up 0.3%).

However, the overall change masks some changes. Milk fat prices were strong, with butter and AMF lifting 3.8% and 3.6%, respectively. The butter rise takes prices to their second-highest level in auction history. Moreover, the lift suggests that another butter price surge may not be far away. Indeed, European butter prices at around \$US7,750/MT are already sitting considerably higher than NZ prices.

Key auction results

Product	% change in index since last auction	Annual % change in index	Weighted Average Price US\$/MT
Whole Milk Powder (WMP)	-1.6%	11.5%	3,100
Skim Milk Powder (SMP)	-1.2%	-10.9%	1,944
Anhydrous Milk Fat (AMF)	3.6%	36.2%	6,402
Butter	3.8%	57.7%	5,954
GDT Price Index	0.3%	18.7%	n.a.

Season-end forecasts

	2016/17	2017/18		Long Run
	Fonterra/ASB	Fonterra	ASB	ASB
Milk Price*	\$6.15	\$6.75	\$6.75	\$6.50-\$7.00

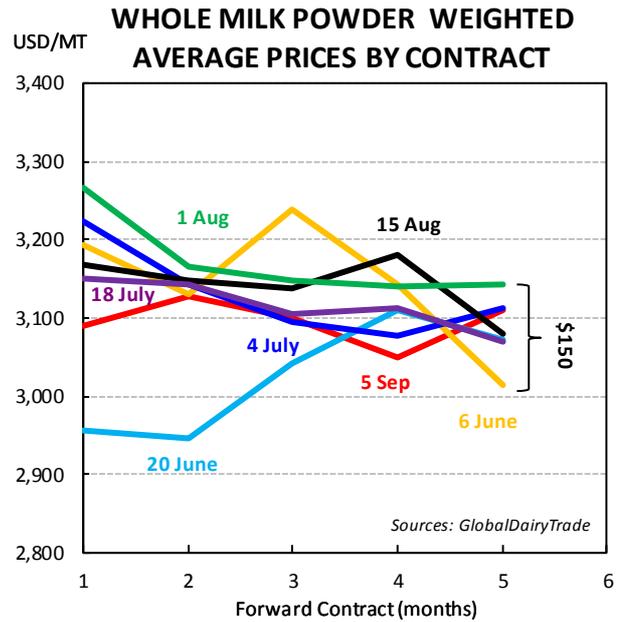
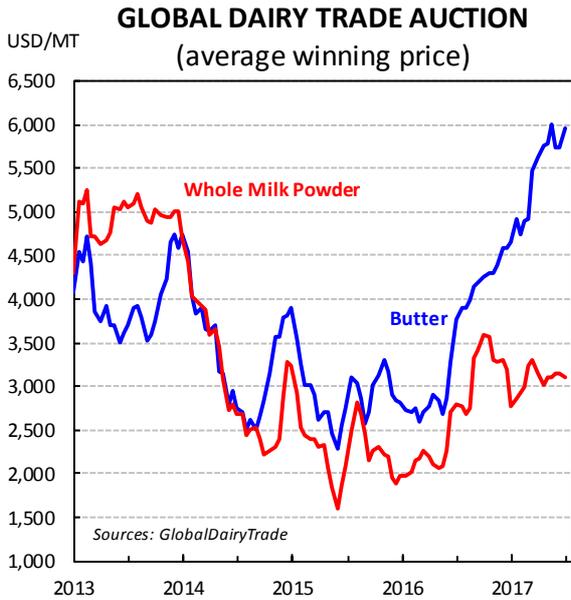
* per kg of milk solids (excluding dividend).

On the other hand, WMP prices fell 1.6%, whereas futures pricing ahead of the auction had pointed to a 3%-5% price rise. This downside surprise continues a recent pattern of futures pricing overestimating the auction result.

All up, the auction result was mixed. Of the products we monitor, four posted price lifts while three fell. Generally,

the holding pattern for (WMP) prices over recent auctions is continuing.

However, we see potential for prices to break this holding pattern and push higher over coming months. Firstly, NZ weather has been poor (very wet) and production is reportedly back on last season in key regions at this stage. Secondly, global milk fat (butter) demand continues to surge, while supply struggles to keep pace.



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