

Westpac forecasts of Fonterra milk price

	2012/13		2013/14		2014/15
	Fonterra	Westpac	Fonterra	Westpac	Westpac
Milk Price	\$5.80	\$5.90	\$7.80	\$8.30	\$6.70

It has been a pretty incredible year so far as prices for New Zealand's primary exports go – the global price of food has defied gravity in the face of slowing economic growth in many developing countries.

This is most apparent in the dairy industry, where we get very public price updates on a fortnightly basis. Last night's GlobalDairyTrade auction registered another small increase in the average price.

The fly in the ointment is the exchange rate, which has risen from US 78 cents to US 82 cents over the past fortnight. Markets have gone weak in the knees about whether the US Federal Reserve will really "taper" its quantitative easing program – we will find out for sure tonight.

Still, the \$8.30/kg milk price forecast we issued a fortnight ago was based on twin assumptions that the price of whole milk powder would fall 10% by the end of the season, and the exchange rate would rise to US 83 cents. So far, those assumptions still look reasonable, so our milk price forecast is unchanged.

"Fix or float" now a tougher call

The other key financial factor that affects farmers is interest rates. And on that score, there has been a great deal of change.

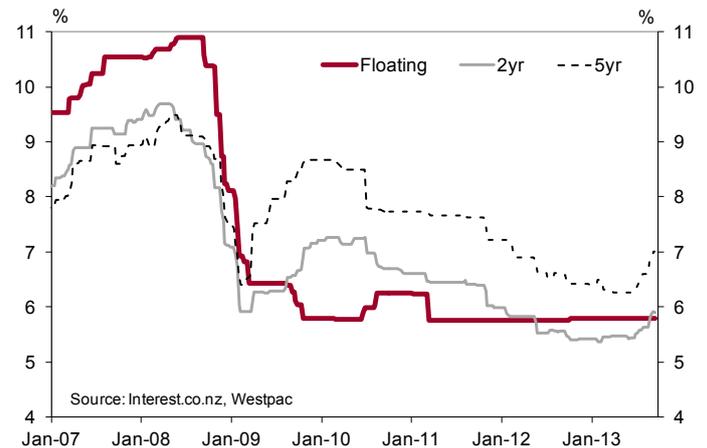
Until recently, long-term interest rates were not much different to short-term rates. We felt this presented an opportunity for borrowers to lock in relatively low fixed rates. Our long-held view was that a construction boom and rising house prices would force the Reserve Bank to hike the OCR from 2.5% to 5.5% over the course of three years. And that would make fixed interest rates a better proposition for borrowers.

Over the past month or two, financial markets have done an about face. Fixed interest rates have been pushed much higher on wholesale markets. This has now translated to higher long-term mortgage rates, with little change for short-term or floating rates. And that means the "fix or float" calculation has changed.

In our opinion, long-term fixed rates are now a fair reflection of where short-term rates are heading over the next few years. That means there is no obvious opportunity to "beat the market" by taking one term rather than another. At this stage, the best way to make the "fix or float" decision is to base it on the risk tolerance and cash-flow needs of your business.

While market pricing looks sensible for now, if it does get out of whack again, we will be the first to write about it!

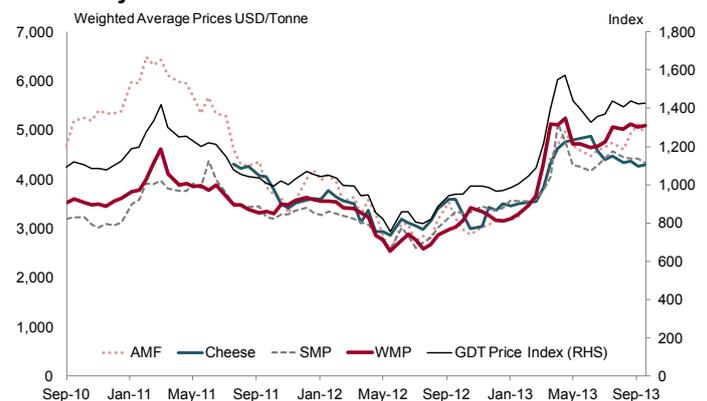
Average advertised mortgage rates



Global Dairy Trade Auction Results, 17 September 2013

	Change since last auction	Price USD/Tonne
Anhydrous Milk Fat (AMF)	-3.3%	\$4,940
Butter Milk Power (BMP)	5.2%	\$4,805
Butter	5.4%	\$3,911
Skim Milk Powder (SMP)	-2.1%	\$4,330
Whole Milk Powder (WMP)	0.8%	\$5,096
TWI (All Products)	0.3%	

GDT Dairy Auction Prices



Dominick Stephens
Chief Economist

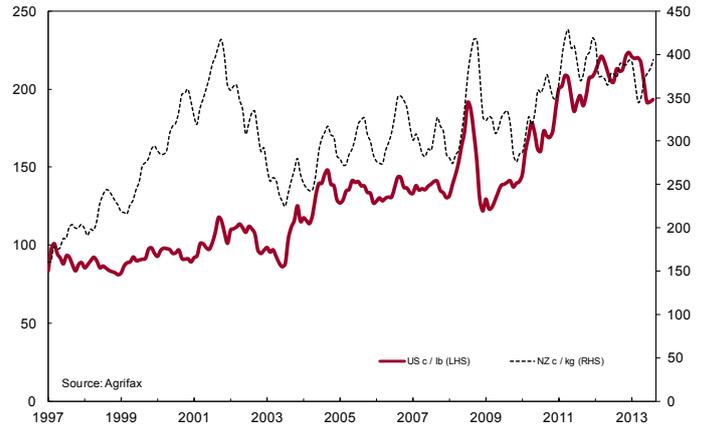
See overleaf for sector outlooks.

Beyond the farm gate

Beef

	Current price level compared to 10 year average	Next 6 months
Trend	High	→

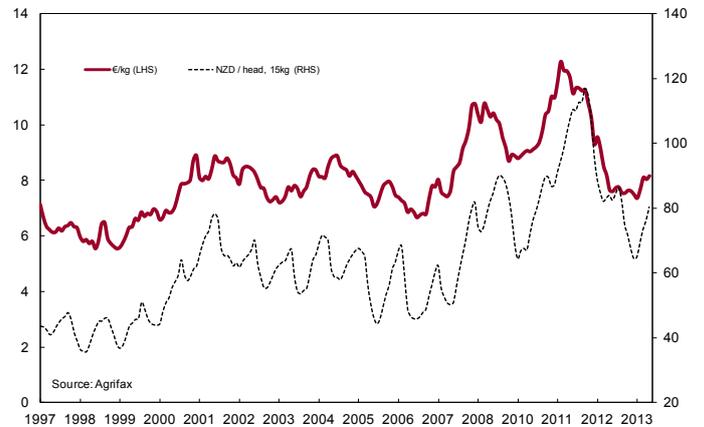
The strong run for beef continues unabated, with US-dollar prices still steady at a high level. We expect this situation to remain in place over the coming six months. US slaughter levels remain low, limiting the global supply of beef. Meanwhile, demand for New Zealand beef should get a boost from Indonesia's recent decision to allow more imports. However, the recent rise in the New Zealand dollar – which we expect will be maintained – will erode returns in New Zealand dollar terms.



Lamb

	Current price level compared to 10 year average	Next 6 months
Trend	Average	↑

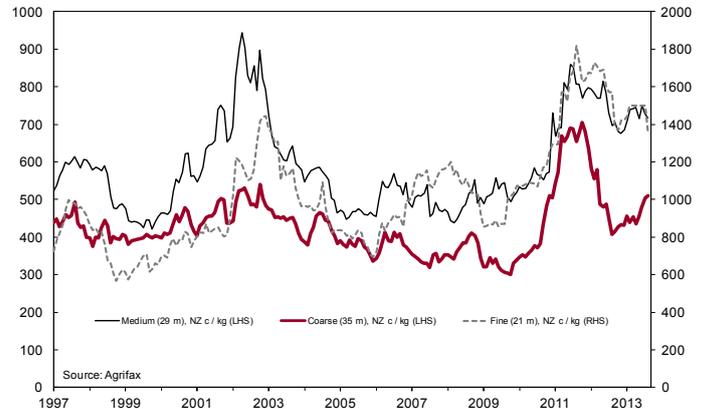
After the lows of last year, global lamb prices are steadily pushing higher and can now be described as “average” rather than “below average”. We expect lamb prices to continue rising over the next six months as demand recovers in Europe, Chinese consumption rises, and supplies out of Australia and New Zealand remain constrained. However, the strong New Zealand dollar and the damage wrought by this year's drought mean that times remain relatively tough for the industry.



Wool

	Current price level compared to 10 year average	Next 6 months
Trend	Above Average	Coarse ↑ Fine/Medium ↓

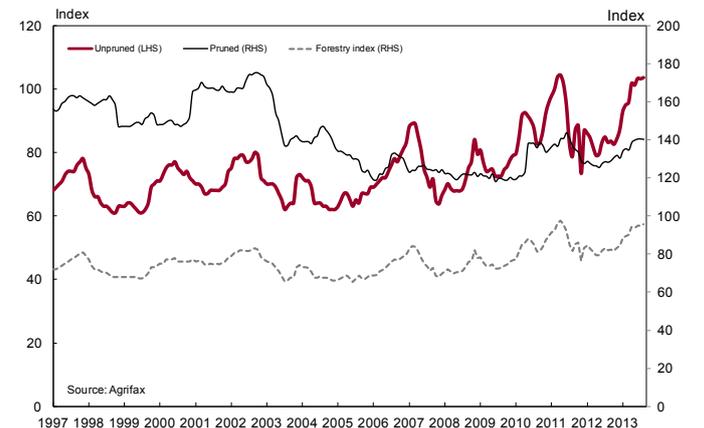
The wool market has split, with coarse wool prices continuing to firm while fine and medium wool prices head in the opposite direction. Coarse wool prices have risen 17% since April. This improvement is in line with the improving housing market in the US. As the US housing market recovers further, the rise in coarse wool prices is expected to continue. On the other hand, the outlook for fine and medium wool prices is subdued. Fine prices fell 10% in August, while medium prices also fell (down 1%). With demand for end products weak, particularly in Europe, we expect fine and medium wool prices to fall further over the next six months.



Forestry

	Current price level compared to 10 year average	Next 6 months
Trend	High	↓

To date the so-called ‘wall of wood’ appears to be finding a Chinese home. The forestry price index rose a touch in August. Unpruned log prices are the third highest on record, while pruned log prices remain well above their ten-year average. This is particularly impressive given that export volumes in the first half of 2013 were 14% higher compared to the same period a year ago. With the Chinese economy entering a soft patch we expect forestry prices to come off the boil, but to remain high by historical standards. Forestry prices will be supported by the recovery in the US housing market.



NB: Trend arrows indicate direction of change in world prices.

Westpac economics team contact details

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Felix Delbrück, Senior Economist
+64 9 336 5668

Any questions email:
economics@westpac.co.nz

For email address changes contact:
WNZRResearch@westpac.co.nz

Disclaimer

Things you should know: Each time someone visits our site, data is captured so that we can accurately evaluate the quality of our content and make improvements for you. We may at times use technology to capture data about you to help us to better understand you and your needs, including potentially for the purposes of assessing your individual reading habits and interests to allow us to provide suggestions regarding other reading material which may be suitable for you.

If you are located in Australia, this material and access to this website is provided to you solely for your own use and in your own capacity as a wholesale client of Westpac Institutional Bank being a division of Westpac Banking Corporation ABN 33 007 457 141 AFSL 233714 ('Westpac'). If you are located outside of Australia, this material and access to this website is provided to you as outlined below.

This material and this website contain general commentary only and does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material and this website may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material and this website does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. The forecasts given in this material and this website are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Transactions involving carbon give rise to substantial risk (including regulatory risk) and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. Statements setting out a concise description of the characteristics of carbon units, Australian carbon credit units and eligible international emissions units (respectively) are available at www.cleanenergyregulator.gov.au as mentioned in section 202 of the Clean Energy Act 2011, section 162 of the Carbon Credits (Carbon Farming Initiative) Act 2011 and section 61 of the Australian National Registry of Emissions Units Act 2011. You should consider each such statement in deciding whether to acquire, or to continue to hold, any carbon unit, Australian carbon credit unit or eligible international emissions unit.

Additional information if you are located outside of Australia

New Zealand: The current disclosure statement for the New Zealand division of Westpac Banking Corporation ABN 33 007 457 141 or Westpac New Zealand Limited can be obtained at the internet address www.westpac.co.nz. Westpac Institutional Bank products and services are provided by either Westpac Banking Corporation ABN 33 007 457 141 incorporated in Australia (New Zealand division) or Westpac New Zealand Limited. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QFE Group Financial Advisers Act 2008 Disclosure Statement at www.westpac.co.nz.

China, Hong Kong, Singapore and India: Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking license and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activity.

Disclaimer continued overleaf.

Disclaimer continued

Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking Regulatory Commission (CBRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

U.K.: Westpac Banking Corporation is registered in England as a branch (branch number BR000106), and is authorised and regulated by the Australian Prudential Regulatory Authority in Australia. WBC is authorised in the United Kingdom by the Prudential Regulation Authority. WBC is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority in the United Kingdom. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. This material and this website and any information contained therein is directed at a) persons who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services Act 2000 (Financial Promotion) Order 2005 or (b) high net worth entities, and other persons to whom it may otherwise be lawfully communicated, falling within Article 49(1) of the Order (all such persons together being referred to as “relevant persons”). The investments to which this material and this website relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this material and this website or any of its contents. In the same way, the information contained in this material and this website is intended for “eligible counterparties” and “professional clients” as defined by the rules of the Financial Services Authority and is not intended for “retail clients”. With this in mind, Westpac expressly prohibits you from passing on the information in this material and this website to any third party. In particular this material and this website, website content and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission (“CFTC”) as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC (“WCM”), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 (“the Exchange Act”) and member of the Financial Industry Regulatory Authority (“FINRA”). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.

For the purposes of Regulation AC only: Each analyst whose name appears in this report certifies that (1) the views expressed in this report accurately reflect the personal views of the analyst about any and all of the subject companies and their securities and (2) no part of the compensation of the analyst was, is, or will be, directly or indirectly related to the specific views or recommendations in this report.