



# Fortnightly Agri Update

16 April 2015

## Thinking global, acting local

Supply conditions in the global dairy market remain unfavourable for milk prices at the moment. However, the downside pressure on prices is largely coming from New Zealand, rather than overseas.

Fonterra's latest monthly update confirms that the worst effects of the dry weather have passed for the local industry as a whole, though the regional divergence is becoming starker. Milk collection in March was down 3% on last year, but that compares to a 7% shortfall in February. Most of the turnaround has been in the North Island, while South Island production remains well down on last year.

The extent of the dry weather hasn't proven to be as bad as it could have been, with rainfall returning in some areas over March and April. In addition, the contention that the low milk price for this season would discourage farmers from buying supplementary feed hasn't really panned out. The trade data up to February shows that imports of palm kernel expeller (PKE) have fallen from their peaks, but they remain at very high levels compared to past seasons. Anecdotally, demand for PKE has picked up again, as the recent rain has given some farmers hope that milk production levels can be maintained after all.

For the season to date, Fonterra's milk collection is up 1.1% on last season. With only two relatively low-production months left in the season, and recent rainfall providing further relief, the final tally is probably going to end up not too far from that number. That's a marked difference from the outlook early in the year, when Fonterra estimated that production could be down 3.3% for the season.

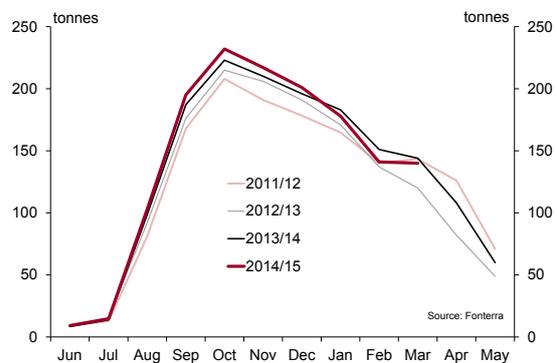
In contrast to the improved outlook for milk production in New Zealand, production among our main competitors in the export market has actually been slowing, as last year's sharp price decline has belatedly fed through. (The chart of European production in our previous issue prompted a question as to whether the slowdown was simply due to farmers approaching their quota levels, something that won't be an issue in coming seasons. However, the fact that production is also slowing in the US suggests it's more likely to be a price effect.)

Better than expected production in New Zealand, combined with the lack of new developments one way or another on the demand side, mean that world prices are likely to remain subdued in the near term. Prices fell another 3.6% in last night's GlobalDairyTrade auction, taking them back to where they were at the end of last year, before the possibility of a drought in New Zealand caught the market's attention.

As signalled in our last issue, we're revising down our milk price forecasts to take account of the softer near-term outlook for prices. We've adopted Fonterra's forecast of \$4.70/kg for this season. And we expect a milk price of \$5.70/kg for next season, slightly below the average of around \$6 for the last decade. This is based on dairy

prices evolving roughly in line with the prices currently implied by futures markets. Our forecast is sensitive to the exchange rate outlook: we expect the NZD/USD exchange rate to average around 0.71 over next season, as a stronger economy prompts interest rate hikes in the US, while market expectations of an OCR cut in New Zealand linger for a while longer.

## Fonterra's monthly milk collection



## GlobalDairyTrade Auction Results, 15 April

	Change since last auction	Price USD/Tonne
Anhydrous Milk Fat (AMF)	2.3%	\$3,744
Butter Milk Power (BMP)	2.1%	\$2,208
Butter	-6.6%	\$3,026
Skim Milk Powder (SMP)	-7.8%	\$2,253
Whole Milk Powder (WMP)	-4.3%	\$2,446
Cheddar	2.7%	\$2,888
GDT Price Index	-3.6%	

## Payout Forecast Table

	2013/14 - Final	2014/15		2015/16
	Fonterra	Fonterra	Westpac	Westpac
Milk Price	\$8.40	\$4.70	\$4.70	\$5.70

**Michael Gordon**  
Senior Economist

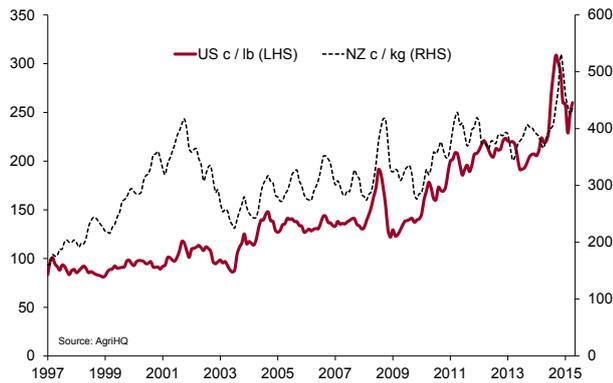
# Beyond the farm gate



## Beef

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

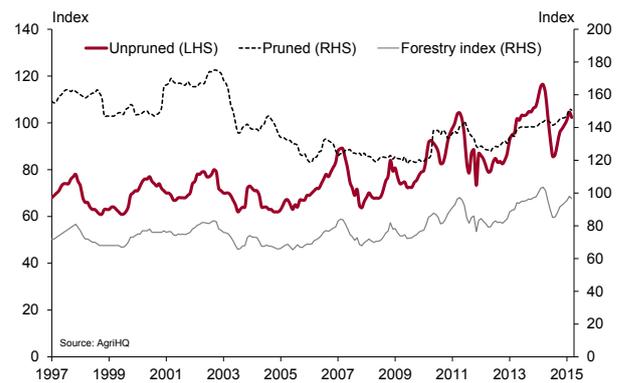
US beef prices are heading higher again as the backlog of imported product is cleared and the summer peak in demand approaches. Locally, cattle slaughter is returning to more normal levels for this time of year, having been higher than normal in late 2014 to take advantage of high US prices. The earlier slaughter will mean reduced supply for later in the season, providing further support for prices.



## Forestry

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

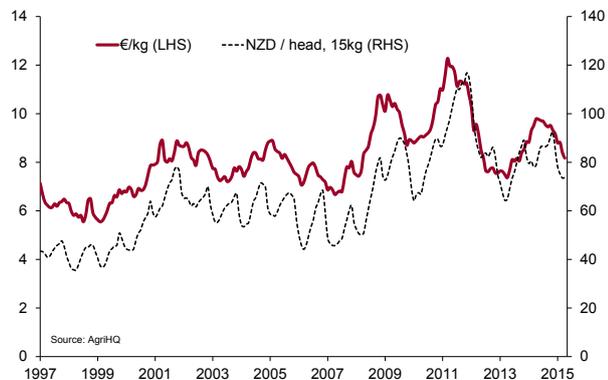
Average prices fell slightly in March but remain 13% above their mid-2014 lows, according to the Agrifax forestry price index. Much of this gain has come from a lower New Zealand dollar and falling transport costs, with world prices for logs steady. Housing construction in New Zealand continues to grow but at a slowing pace, with quake-related building activity in Christchurch expected to peak this year.



## Lamb

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

Dry conditions have led to early slaughter in many parts of the country, putting pressure on processors' capacity and pushing down schedule prices. Early slaughter will reduce the available supply later in the year.



## Kiwifruit

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

The 2015 season has kicked off, with the first shipment leaving in late March. Volumes are expected to be up substantially on the last few seasons - particularly for gold kiwifruit, with the new more Psa-resistant Gold3 variety proving to be highly productive. The sharp rise in volumes will make it difficult to match the high prices received last season.



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

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