



Fortnightly Agri Update

4 March 2015

Drought update

The dry conditions over much of New Zealand will have a significant impact on agricultural production over the first half of this year. Recently released data gives us an indication of the impact to date.

Dairy: Milk production has been running below year-ago levels since January, having been well up on the previous year until then. While drought has only been officially declared in the South Island, the North Island has been very dry as well, and milk production appears to be down on year-ago levels in most regions. In late January Fonterra advised that it expects full-season milk collection to be 3.3% lower than the previous season; the international market has responded accordingly, with world dairy prices rising 22% in subsequent auctions.

Data released since then indicate that while milk production is indeed on track to be down on last season, we suspect the impact could be less severe than Fonterra has signalled. To meet Fonterra's full-year forecast, production for the remainder of the season would have to fall to around the levels seen in the latter part of the 2012/13 season. Given that dairy cow numbers have increased since then, this forecast would imply an even bigger hit to per-cow production than during the early 2013 drought, which was described as the most severe in decades. That looks to be a bit of a stretch based on the current run rate. We'll reassess our milk production forecast in coming weeks, which will have implications for the extent of the slowdown in GDP growth that we expect over the first half of this year.

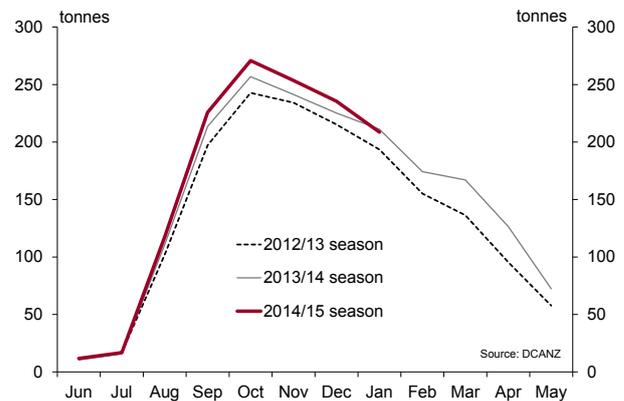
Meat: Livestock slaughter numbers up to January showed a mixed response to the dry conditions. Overall, the figures look to be in line with our assumptions. Meat production will provide a boost to GDP growth in the March quarter of this year (partly offsetting the drop in milk production), but with a corresponding drag on the rate of growth in the June quarter.

Cattle slaughter was higher than normal over December and January, building on a lift in slaughter numbers over the second half of 2014 to take advantage of high beef prices in the US. Average weights are down about 3% on a year ago. The persistence of this high level of cattle slaughter will affect the available supply later in the year.

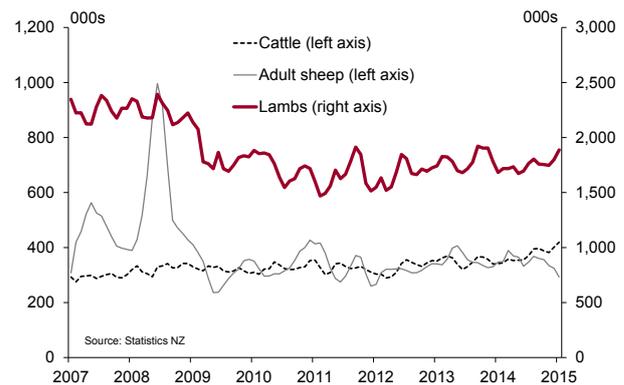
Lamb slaughter numbers have also picked up in the last few months, although the seasonally adjusted figures are not out of line with the trend of the last few years. (In raw terms, however, the uplift has come during the peak of the season, putting a squeeze on processing capacity.) In contrast, processing of adult sheep is well down on last year. Average weights for both lambs and adult sheep are similar to a year ago.

Michael Gordon
Senior Economist

Milk production, tonnes of milksolids



Livestock slaughter, seasonally adjusted



GlobalDairyTrade Auction Results, 4 March

	Change since last auction	Price USD/Tonne
Anhydrous Milk Fat (AMF)	-2.2%	\$4,237
Butter Milk Power (BMP)	6.8%	\$2,681
Butter	2.5%	\$3,912
Skim Milk Powder (SMP)	5.9%	\$2,935
Whole Milk Powder (WMP)	-1.0%	\$3,241
Cheddar	10.8%	\$3,377
GDT Price Index	1.1%	

Payout Forecast Table

	2013/14		2014/15		2015/16	
	Fonterra	Westpac	Fonterra	Westpac	Fonterra	Westpac
Milk Price	\$8.40	\$4.70	\$5.00	\$6.40		

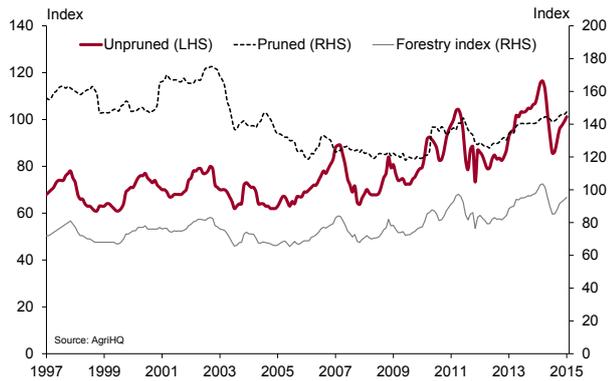
Beyond the farm gate



Forestry

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

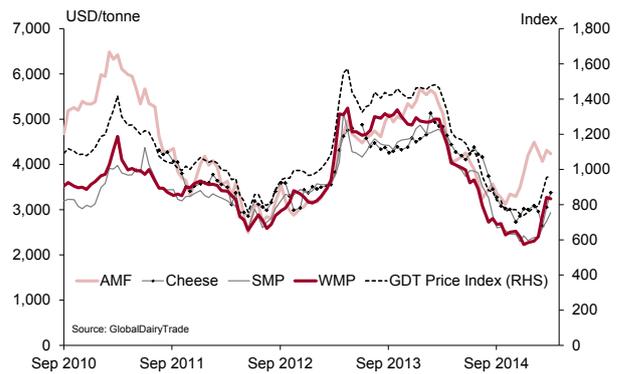
Average prices have rebounded by 12% over the last six months according to the Agrifax forestry price index. However, much of this gain has come from a lower New Zealand dollar and falling transport costs, with world prices for logs steady. There are very tentative signs that steps by Chinese policymakers to revitalise their housing market are having some impact. Housing construction in New Zealand remains on an upward trend, albeit from low levels in recent years.



Dairy

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

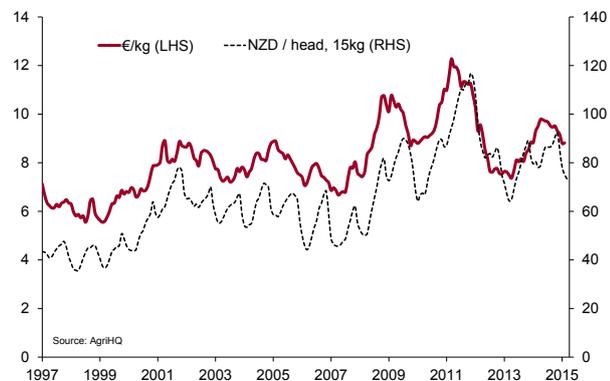
Dairy prices rose 1.1% in the latest GlobalDairyTrade auction. The results were mixed across products, with a small drop in WMP prices but sizeable gains for SMP, butter and cheese. Fonterra has held its farmgate milk price forecast at \$4.70/kg, but we retain our view that the milk price will end the season at \$5.00/kg.



Lamb

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

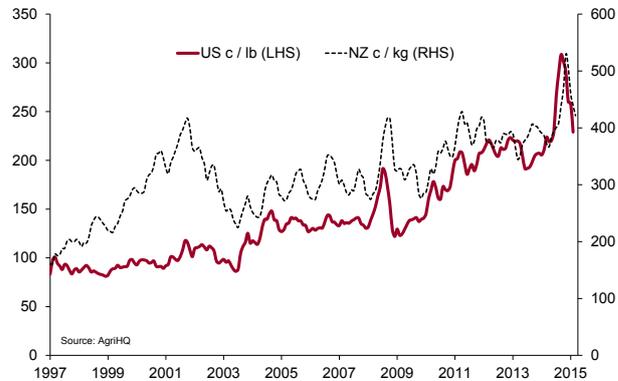
Dry conditions have led to early slaughter in many parts of the country, putting pressure on processors' capacity and pushing down schedule prices. Early slaughter will reduce the available supply later in the year.



Beef

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

The port disputes in the US have been resolved but clearing the backlog of imported meat products will take some time, suggesting the improvement in prices will be gradual. Prices are expected to settle at relatively high levels, with US beef supply still not in a position to gear up quickly.



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

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