



# Fortnightly Agri Update

2 June 2016

## Off to a head start

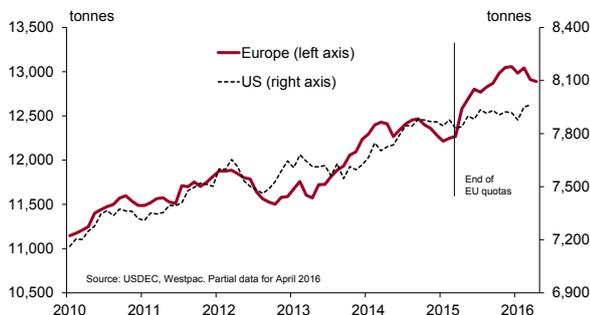
World dairy prices rose a further 3.4% in last night's GlobalDairyTrade auction. On the whole, this result was stronger than we expected. Prices for whole milk powder – New Zealand's main export product – were down 1.7% in the auction, which was broadly in line with what the futures market had been signalling. But there were sizeable gains across most of the other product lines, including a 12.1% jump in skim milk powder prices. We note that the ratio of WMP to SMP prices had blown out to a record high in May, so it seems that the time was ripe for some convergence.

Last night's auction was the first of the 2016/17 dairy season. Obviously a lot can happen between now and when the season's farmgate milk price is finalised next year. But the last two auction results provide mild support for our view that the risks are to the upside of Fonterra's opening forecast of \$4.25 per kilo of milk solids. We currently expect the milk price to end the season at \$4.60/kg.

It's been a while since Fonterra's outlook for world dairy prices has been less positive than ours. Fonterra's \$4.25/kg milk price forecast for the new season seems to be based on an assumption that world prices will remain at current levels throughout the whole season, with an uplift in prices presumably coming in later seasons. In contrast, we're a bit more hopeful of seeing an improvement in world prices over the second half of this season.

In the near term, though, we agree that Fonterra's caution on world prices is warranted. Global milk production surged last year, particularly after the European Union's long-standing quota system was removed. And while the rate of growth has flattened out since then, the level of production remains very high, and has been slow to adjust to the reality of extremely poor returns to dairy farmers worldwide.

## Northern Hemisphere milk production



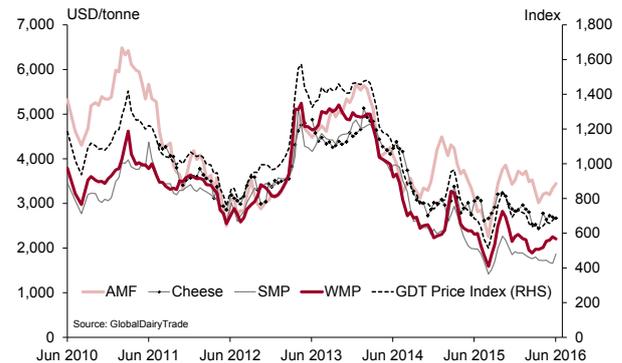
There are some early signs that production in Europe is now falling, but we're taking this with a degree of caution – these figures have a habit of being revised upward over time, and they've given us false hope in the past that European production had rolled over. What's more, even if Europe is genuinely slowing, milk production has been picking up in the US recently. The US

cow cull in April was the lowest in seven years, with the El Niño weather pattern helping to break the drought in some parts of the country. Overall, milk production among the world's top exporters appears to be flat rather than falling.

Meanwhile, the world demand picture remains muted. So far this year, Chinese imports of dairy products have remained as subdued as they were last year, aside from a flurry in January (which would have filled the small tariff-free quota). Venezuela – which was New Zealand's second-biggest market for whole milk powder not that long ago – is in dire straits. It's possible that the recent bounce in world oil prices will help to revive dairy demand from the oil-producing nations, but we'll wait for some more tangible evidence.

**Michael Gordon**  
Senior Economist

## Dairy prices



## GlobalDairyTrade Auction Results, 2 June 2016

	Change since last auction	Price index USD/Tonne
Anhydrous Milk Fat (AMF)	2.8%	\$3,444
Butter Milk Power (BMP)	14.2%	\$1,765
Butter	3.2%	\$2,762
Skim Milk Powder (SMP)	12.1%	\$1,867
Whole Milk Powder (WMP)	-1.7%	\$2,205
Cheddar	7.8%	\$2,669
GDT Price Index	3.4%	

## Payout Forecast Table

	2015/16		2016/17	
	Fonterra	Fonterra	Fonterra	Westpac
Milk Price	\$3.90	\$4.25	\$4.60	

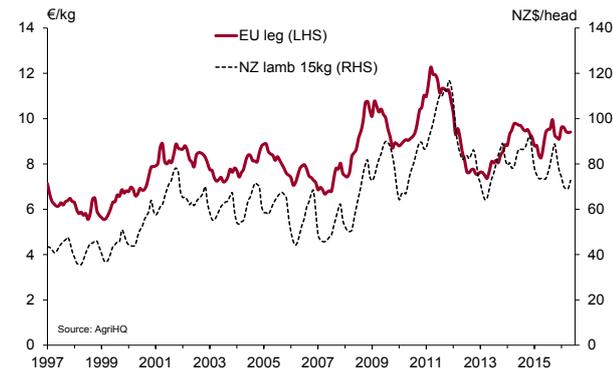
# Beyond the farm gate



## Lamb

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

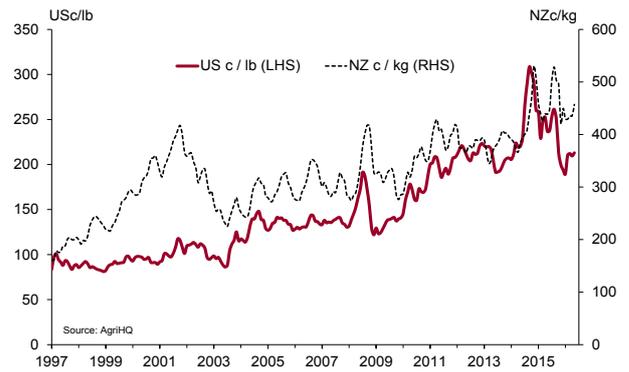
Lamb supplies are expected to tighten over the next couple of months, which could support local prices in the near term. However, internationally there is little change to the bigger picture of tight global supplies and weaker growth in demand in key markets such as China and the Middle East. The newly announced agreement with China, which opens up that market to chilled NZ meat exports, is a positive development for the sector that should eventually provide an additional source of demand for higher-value exports.



## Beef

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

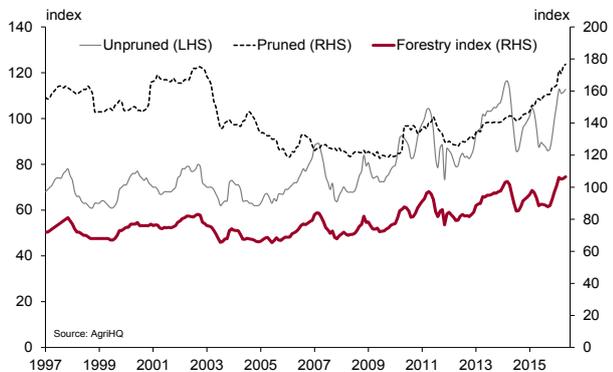
Over the medium term, international beef prices are likely to be underpinned by relatively tight global supply as beef exports from Australia, and to a lesser extent New Zealand, contract. However, this will be balanced against increasing domestic supplies in the US, with changes to market access for Brazil's chilled beef exporters an important wild card that could influence prices. A lift in New Zealand's cow cull at the end of the local dairy season will also add to domestic supply in the coming months.



## Forestry

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

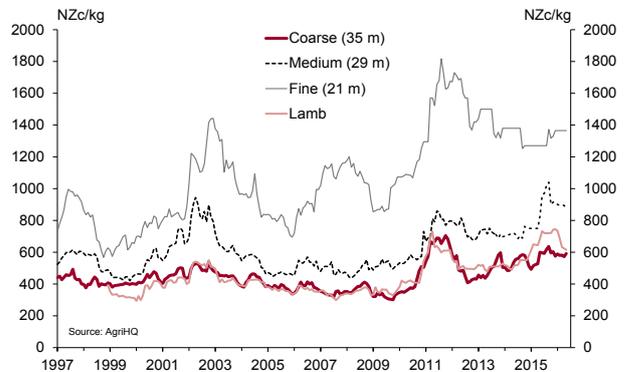
International log prices continued to improve in May, and are continuing to hold up better than we had anticipated. Domestically, the buoyant construction sector continues to support local prices. While building consents in Auckland have slowed recently, this likely reflects uncertainty around the Unitary Plan which should be finalised in coming months. Internationally, reported supplies remain relatively tight, but slower growth in key export markets and an eventual increase in supply are still expected to weigh on export prices over the rest of the year.



## Wool

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

Wool prices are likely to remain under pressure in the coming months, due to a combination of low oil prices making synthetic alternatives to wool more attractive and a soft demand outlook from China.



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

## Contact the Westpac economics team

**Dominick Stephens**, Chief Economist +64 9 336 5671

**Michael Gordon**, Senior Economist +64 9 336 5670

**Satish Ranchhod**, Senior Economist +64 9 336 5668

**Anne Boniface**, Senior Economist +64 9 336 5669

**David Norman**, Industry Economist +64 9 336 5656

**Any questions email:** [economics@westpac.co.nz](mailto:economics@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](http://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](http://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](http://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.

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

## Disclaimer continued

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. 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.