

# Dairy Update.

18 November 2021



## One up, followed by one down.

- We have upgraded our 2021/22 farmgate milk price forecast by 40 cents to \$8.90/kg.
- We have also set our opening forecast for the 2022/23 season at a \$6.90/kg.
- For context, we expect the farmgate milk price to fluctuate around \$7.50/kg over the next five years or so.

### Farmgate milk price forecasts

	2021/22		2022/23
	Westpac	Fonterra	Westpac
Milk price	\$8.90	\$7.90-\$8.90	\$6.90

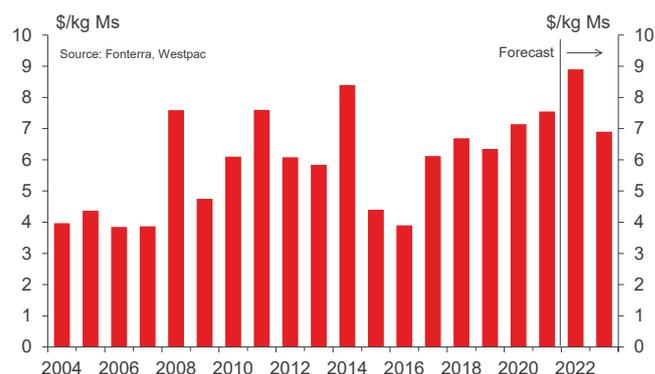
**Nathan Penny**, Senior Agri Economist

+64 9 348 9114

We have upgraded our 2021/22 farmgate milk price forecast by 40 cents to \$8.90/kg. If achieved, this would be a record high, surpassing the previous record of \$8.40/kg set back in 2013/14.

We have set our opening 2022/23 farmgate milk price forecast at \$6.90/kg. This forecast represents a \$2.00/kg drop from our 2021/22 forecast. Moreover, \$6.90/kg is below \$7.50/kg or where we expect the farmgate milk price to average over the next five years.

### Farmgate milk prices



### 2021/22: global supply squeeze leads milk price to record highs.

The key catalyst for the 2021/22 forecast revision is the downgrade to our production forecast for the season. We now expect New Zealand production to fall by 1.5% compared to last season. Previously, we expected production to fall by 1%.

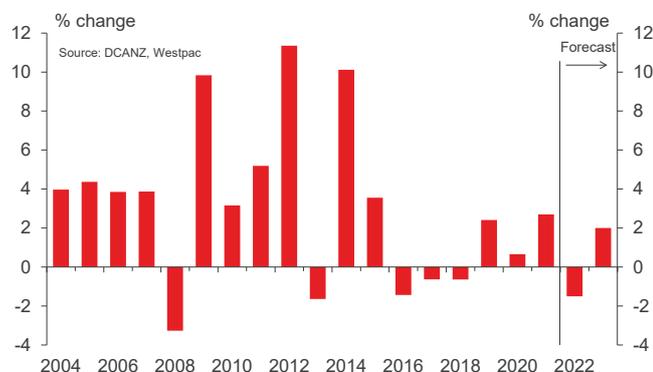
This season, New Zealand production has been on the back foot. Winter and spring have been either wet or cold or both in many parts of the country. As a result, production for the first four months of the season is running at 3.1% behind the same stage of last season.

We expect this production softness to continue in the short term. Anecdotes also suggest that October has been similarly weak, while November hasn't been much better. With the first five months of the year accounting for around a third of the



season's production, it will be very difficult for production to be made up later, particularly relative to last season's record level of production.

### Dairy production growth (all NZ suppliers)



Meanwhile, dairy production elsewhere is also soft. Weather has also impacted European production, with production for the first eight months of the year flat compared to the same period a year ago. In addition, Chinese (domestic), US and EU production all continue to be constrained by very high feed costs and limited feed availability.

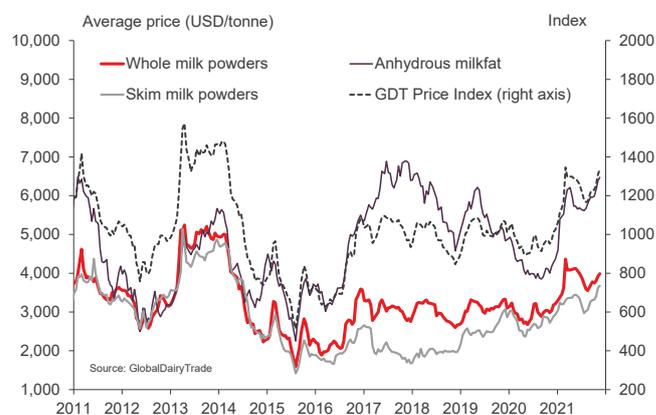
### Corn prices



From a New Zealand perspective, overall and WMP auction prices have lifted by 14% and 12%, respectively, since August.

Moreover, we anticipate that when weak October New Zealand production data are released officially in a week or so's time, they will reinforce prices at their current high levels. Similarly, the slowdown in European production has been reflected in surging cheddar and skim milk powder prices – both prices have jumped by over 20% since August.

### Global dairy prices



### 2022/23: what goes up must come down...

For the 2022/23 season, our opening forecast flags that much of this season's gains are temporary. In other words, global dairy supply will not prove weak across all the key regions indefinitely. And as supply recovers, global dairy prices will fall.

Here in New Zealand, we expect production to rebound over the 2022/23 season. Indeed, we expect the mirror opposite of this season, with our production forecast set at a lift of 1.5%. Next winter and spring are likely to bring more normal growing conditions, meaning local feed availability should improve and feed prices should head lower. And with very strong cashflows (spilling over from 2021/22), farmers will be in a position to fill any feed gaps over the season.

Similarly, we expect supply conditions to improve in the EU. Critically, we expect feed grain prices to moderate from their highs and for this to boost supply. Indeed, for both New Zealand and the EU, we expect 2022 production growth to double from 2021 to 1.5% and 0.6%, respectively (for comparison purposes, these growth rates and those in the table below are shown for calendar years).

### Dairy production growth weighted by export share – Top 3 exporters

Exporter	2021 Forecast (% change)	2022 Forecast (% change)	Export Share	2021 Weighted Forecast % Change	2022 Weighted Forecast % Change
New Zealand	0.7	1.5	37%	0.3	0.5
EU	0.3	0.6	41%	0.1	0.2
USA	1.7	1.2	22%	0.4	0.3
<b>Weighted Total by Export Share</b>				<b>0.8</b>	<b>1.1</b>

Source: DCANZ, Westpac, EU Commission, USDA

## ... albeit more gently than in the past.

The dairy price cycle is alive and well. However, the violent milk price cycles of the past are behind us. Indeed, the milk price dropped \$4.00/kg between the 2013/14 and 2014/15 seasons. In this cycle, we expect a drop of circa half that magnitude i.e. \$2.00/kg.

Of course, this far out it is difficult to be precise. With this in mind, the message is simple: we expect a significant farmgate milk price decline in 2022/23.

For additional context, we see the farmgate milk price averaging around \$7.50/kg over the next five years or so. At around \$6.90/kg, our forecast for 2022/23 represents a below par season, but it is by no means disastrous. And in subsequent seasons, we would expect the farmgate milk price to then gravitate back towards \$7.50/kg.

The key reason for the less violent price cycles is that season-to-season swings in dairy production have moderated considerably in recent years. Here in New Zealand, for example, production growth for the last six seasons has been between -1.5% and +2.5% (rounded to the nearest 0.5%). Compare that to the six seasons prior, where production growth was between -1.5% and a whopping 11.5%.

## Auction results, 17 November.

Dairy auction prices posted solid gains overnight. Both overall prices lifted and key whole milk powder (WMP) prices lifted by 1.9%.

The lift in prices builds on gains over September, October and the first November auction. Overall prices and WMP prices have lifted 14% and 12%, respectively since August. In both cases, prices now sit 30% or more above year ago levels. Taking a longer-term perspective, prices are around a quarter above their five-year average.

The price strength overnight was broad based. All of the products that we monitor posted price gains. Butter prices led the price gains, rising 3.5%. Notably, cheddar prices built on last auction's 14% surge, rising another 2.2%. All other product prices rose by between 1% and 2%.

The result was largely in line with our expectations. We had expected a 2% lift in WMP prices. In contrast, the futures market had expected a larger increase in the vicinity of 5%.

From here, we expect that ongoing weakness in global dairy production will continue to underpin global dairy prices. New Zealand dairy production over September was down 4.0% compared to September 2020. In addition, anecdotes suggest that this production weakness has continued through October and November, while dairy production in other key exporting regions remains similarly soft.

## GlobalDairyTrade auction results

	Change since last auction	Prices USD/tonne
Whole Milk Powder (WMP)	1.9%	\$3,987
Skim Milk Powder (SMP)	1.4%	\$3,676
Anhydrous Milk Fat (AMF)	1.3%	\$6,472
Butter	3.5%	\$5,534
GDT Price Index	1.9%	1,335

# Contact the Westpac economics team.

**Michael Gordon, Acting Chief Economist**

+64 9 336 5670

**Satish Ranchhod, Senior Economist**

+64 9 336 5668

**Nathan Penny, Senior Agri Economist**

+64 9 348 9114

**Paul Clark, Industry Economist**

+64 9 336 5656

**Gregorius Steven, Economist**

+64 9 367 3978

**Any questions email:**

economics@westpac.co.nz

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