

Dairy Update.

18 November 2020



2021/22: Opening gambit.

- We set our initial 2021/22 farmgate milk price forecast at \$7.00/kg.
- Our positive view centres on further likely improvements in global dairy demand as the world gradually gets on top of Covid by the 2021/22 season.
- The level of the NZD/USD is a key risk and could prove a fly in the ointment for our forecast.

Farmgate milk price forecasts

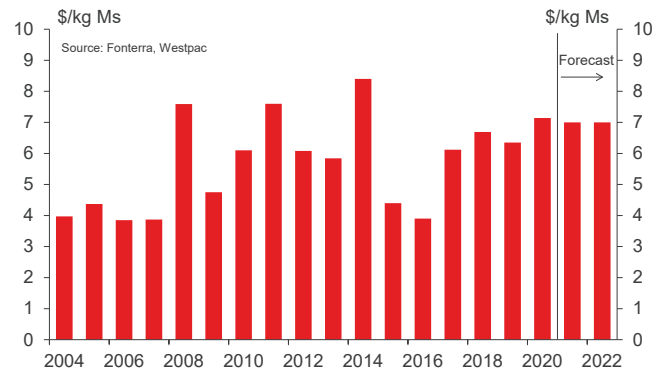
	2020/21		2021/22
	Westpac	Fonterra	Westpac
Milk price	\$7.00	\$6.30-\$7.30	\$7.00

Nathan Penny, Senior Agri Economist

+64 9 348 9114

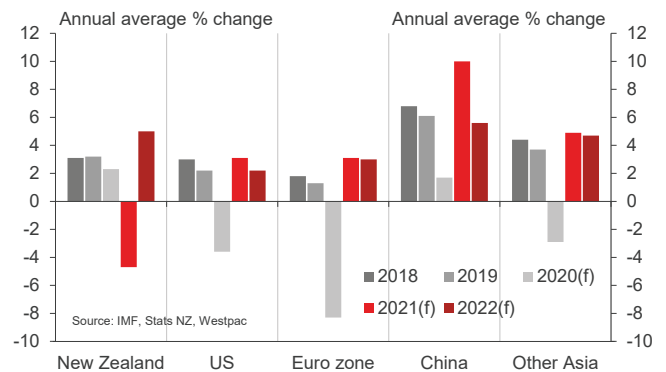
We have set our initial 2021/22 farmgate milk price forecast at \$7.00/kg. This forecast is equal to our forecast for 2020/21 and similar to the \$7.14/kg achieved in 2019/20. Our forecast is higher than the long-run average milk price, although the difference is smaller when the prices are adjusted for inflation.

Farmgate milk prices



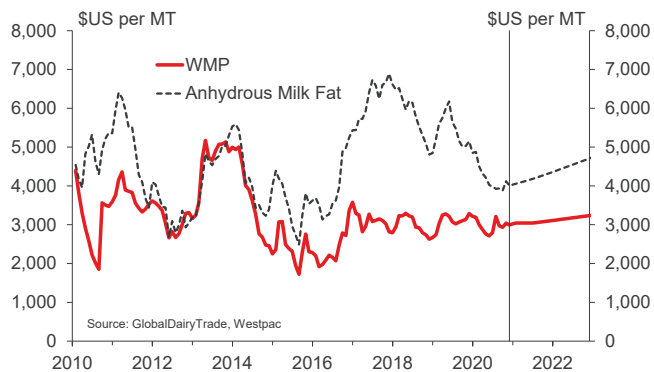
We anticipate that overall global dairy demand will firm over 2021 and 2022 as countries gradually get on top of Covid and the global economy rebounds. This trend has already started in China and East Asia where dairy demand has rebounded from its lows earlier in the year, with overall dairy prices regaining some lost ground.

Global GDP growth



Looking by product, the key change we expect at this horizon is that demand and prices for milk fat will begin to normalise. Currently, milk fat prices are soft as consumers eat less cream and other milk fat products in settings such as restaurants. In particular, we expect that the rollout globally of Covid vaccines will gradually allow more people to return to restaurants and other venues that milk fat consumption relies on.

Wholemilk powder and anhydrous milk fat prices



On the supply side and in aggregate, we expect moderate growth in the key exporting countries over the period ahead. Over recent years, annual growth has averaged in the vicinity of 1%. This relatively modest growth is another reason why prices have held up well during the global Covid recession. Moreover, we see a low probability that global supply will deviate materially from these trends by enough to offset the impact on prices from rising demand.

There are a few other forecast risks that we should point out. The first is the New Zealand dollar, which we've seen jump two cents to US\$0.69 over the past week or so. We expect the NZD/USD to remain firm around or slightly above this level over the remainder of this season and into 2021/22. We note that there is a risk that, if the New Zealand economy's resilience continues to surprise and local interest rates rise, then the NZD/USD could rise beyond what we have assumed. In this event, the milk price would be lower.

Other (downside) risks include the possibility that dairy buyers run down stocks after having built them up during Covid to protect against supply disruptions. In addition, there is uncertainty around global agricultural trade policy. For example, Joe Biden's US presidency may take a more trade- and China-friendly stance, thus allowing the US more access to China's market and thus more competition for New Zealand dairy exports. Finally, we assume normal weather conditions going forward. In the case of a New Zealand drought, global dairy prices are likely to be modestly higher all else being equal.

Auction Results, 18 November.

Dairy auction prices lifted overnight. Both whole milk powder (WMP) and overall prices posted a 1.8% rise.

All the key products posted price gains. Anhydrous milk fat (AMF) led the price rises, jumping 4.1%. Skim milk powder prices posted the next-largest gain, rising 2.1%. Butter prices lifted a touch, while lactose and cheddar prices fell.

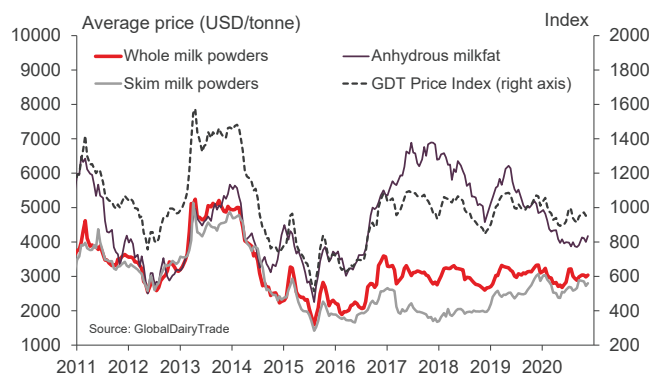
The price rise effectively erases the fall at the previous auction. Compared to both this time last year and pre-Covid levels, overall prices now sit around 8%-9% lower.

The result was in line with market expectations. The futures market was pointing to a WMP lift of around 1.5% prior to the auction. The result was higher than our expectation for WMP to remain flat, although our expectation was set on data as at Friday last week.

GlobalDairyTrade Auction Results, 18 November 2020

	Change since last auction	Prices USD/tonne
Whole Milk Powder (WMP)	1.8%	\$3,037
Skim Milk Powder (SMP)	2.5%	\$2,799
Anhydrous Milk Fat (AMF)	4.1%	\$4,175
Butter	0.4%	\$3,838
GDT Price Index	1.8%	970

Global dairy 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

Nathan Penny, Senior Agri Economist

+64 9 348 9114

Paul Clark, Industry Economist

+64 9 336 5656

Any questions email:

economics@westpac.co.nz

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