

# WESTPAC DAIRY UPDATE

## GlobalDairyTrade auction results.

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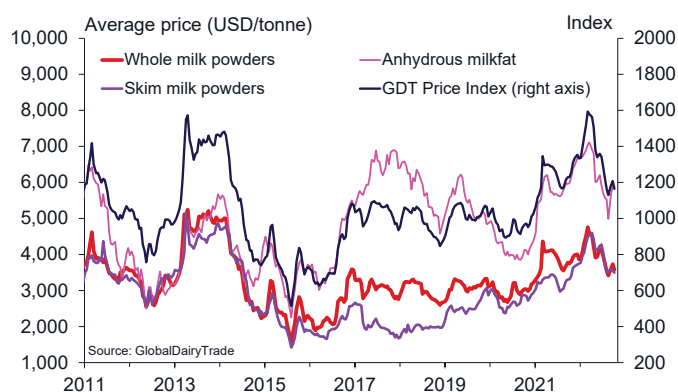
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## Be careful what you wish for.

- Dairy auction prices slid overnight.
- The fall comes as the US dollar has surged.
- Indeed, US dollar strength is not necessarily a good thing.

Global dairy prices



GlobalDairyTrade auction results

	Change since last auction	Prices USD/tonne
Whole Milk Powder (WMP)	-4.0%	\$3,573
Skim Milk Powder (SMP)	-1.6%	\$3,497
Anhydrous Milk Fat (AMF)	-1.7%	\$5,811
Butter	-7.0%	\$4,983
GDT Price Index	-3.5%	1166

Dairy auction prices dropped overnight. Overall prices dipped 3.5%, while key whole milk powder (WMP) prices slid 4.0%. Prices have essentially given back their gains at the previous auction.

The weak result was broad-based. All six of the products we monitor posted price falls. Butter prices led the falls, plunging 7.0%. Butter milk powder and cheddar prices both posted falls around 4%. Meanwhile, skim milk powder and anhydrous milk fat prices fell 1.6% and 1.7%, respectively.

This result was below even our muted expectations. We had anticipated that whole milk prices would be flat, while the futures market was pricing in a circa 2% gain.

The negative result comes against a backdrop of very nervous financial markets. Markets are increasingly concerned that the global economy may slip into recession as global central banks aggressively hike interest rates in their battle against surging inflation. One of the key market moves has seen investors buy safe haven assets like the US dollar in favour of currencies

perceived to be riskier like the New Zealand dollar. This move has led the NZD/USD to as low US\$0.56 this week.

On the surface, a weak NZD/USD boosts farmer incomes, including the milk price. Focusing only on the currency and using our current dairy commodity price forecasts, a one cent move in the NZD/USD would add up to 18 cents to our milk price estimate.

However, a weaker NZD/USD can impact dairy markets in other less favourable ways. First up, other currencies like the Chinese yuan have also fallen against the USD. As a result, dairy commodity prices have become more expensive for buyers in our largest dairy market. And as we have seen overnight, with dairy auction prices falling, this can lead to lower dairy demand. Secondly, the strong US dollar may also be a symptom of or a signal that the global economy is weakening. A weaker global economy can also lead to lower demand for goods, including for dairy products.

At this stage, we expect the overnight price fall will prove temporary. Indeed, we put the price fall overnight down to the rising dairy prices in local currency terms (due to the higher USD) and a degree of cautiousness in dairy markets following the broader financial market nervousness of the last few weeks.

Moreover, dairy fundamentals remain strong. For example, in August New Zealand dairy production was down 4.9% versus August 2021. And anecdotally, production has continued on this weak note over September and into October. In other words, tight dairy supply should support dairy prices over coming months.

That said, the question around just how strong or weak global dairy demand is remains. While financial markets are nervous about the global economic outlook, an outright recession is still only a risk at this stage. On the dairy front, we will get further evidence either way over coming auctions.

The weak result overnight does remove the upside risks to our 2022/23 milk price forecast of \$9.25/kg. As a result, the risks to our forecast are now more balanced. On the upside we have the ongoing weakness to global dairy supply, while on the downside we have the fragile global economy and its potential negative implications for global dairy demand.

#### Farmgate milk price forecasts

	2022/23	
	Westpac	Fonterra
Milk price	\$9.25	\$8.50-\$10.00

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