

# Rural Economic Note

Global Dairy Trade Auction

20 September 2017

## Recipe brewing for higher dairy prices

- Overall dairy prices lifted a touch overnight.
- Butter prices set a fresh record high – the eighth record high this year.
- Meanwhile, we see potential for a combination of wet NZ weather and surging global butter demand to lift prices over coming months.

### Summary

**Butter prices continue to boom.** Indeed overnight, butter prices have set their eighth auction-record high already this year.

**Meanwhile closer to home, the wet weather rolls painfully on and is beginning to weigh on production.** August production, for example, was down 1.5% versus August last season. While it is still early spring, if the rain continues, production will stall further and then send dairy prices higher.

As we mentioned in our previous report, the wet NZ weather and the global butter shortage are a recipe for higher dairy prices. The global butter shortage won't correct until sometime in 2018. Meanwhile, D-Day is fast approaching for NZ production. **If the weather doesn't improve soon, we expect to lift our milk price forecast to \$7.00/kg or above in the next month or so.**

### Auction Results

**Overall dairy auction prices were largely unchanged overnight (up 0.9%).** WMP prices were also effectively flat (up 0.6%), in line with expectations.

Notably though, **butter prices set a fresh record high – the eighth record high this year.** Indeed milk fat prices were generally strong, with butter and AMF lifting 5.3%. Global butter demand continues to surge, while supply is struggling to keep pace. Moreover, global inventory levels are low. This dynamic suggests that records may continue to tumble through to the end of the year.

#### Key auction results

| Product                  | % change in index since last auction | Annual % change in index | Weighted Average Price US\$/MT |
|--------------------------|--------------------------------------|--------------------------|--------------------------------|
| Whole Milk Powder (WMP)  | 0.6%                                 | 12.4%                    | 3,122                          |
| Skim Milk Powder (SMP)   | -1.2%                                | -14.5%                   | 1,920                          |
| Anhydrous Milk Fat (AMF) | 5.3%                                 | 37.0%                    | 6,764                          |
| Butter                   | 1.2%                                 | 54.0%                    | 6,026                          |
| GDT Price Index          | 0.9%                                 | 17.8%                    | n.a.                           |

#### Farmgate Milk Price Forecasts

|             | 2016/17      | 2017/18  |        | Long Run      |
|-------------|--------------|----------|--------|---------------|
|             | Fonterra/ASB | Fonterra | ASB    | ASB           |
| Milk Price* | \$6.15       | \$6.75   | \$6.75 | \$6.50-\$7.00 |

\* per kg of milk solids (excluding dividend).

Looking over a 3-month period, **overall auction prices continue their holding pattern.** WMP prices have lifted a modest 2.7% over this period, while overall prices have fallen a similarly modest 1%.

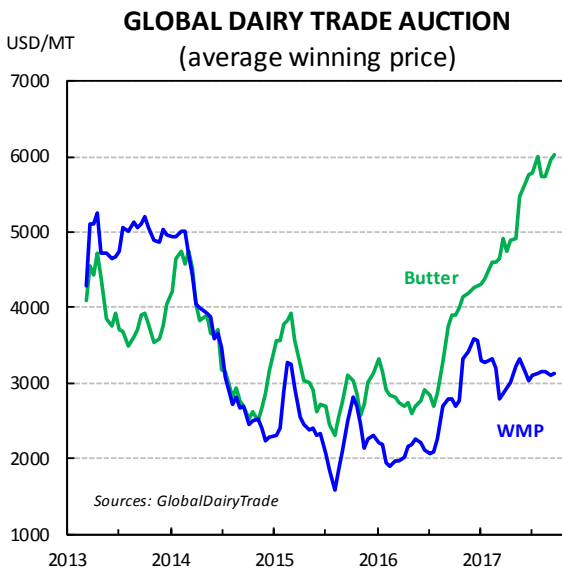
Stepping back from the auction result, we see potential for overall dairy prices, **particularly for WMP, to break this**

holding pattern and push higher over coming months.

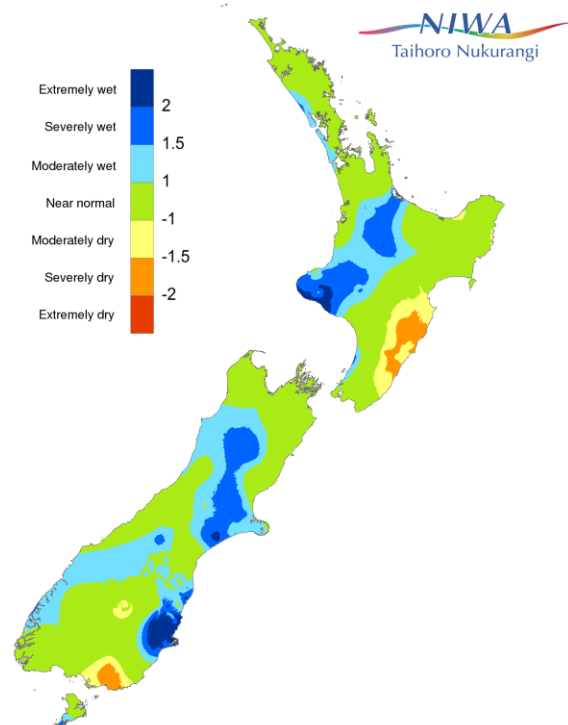
First, **NZ weather has been poor (very wet) and production is reportedly back on last season in key regions at this juncture.** Indeed, we forecast a lift of 4% for this season compared to last, but that will prove optimistic without a return to more normal spring weather over coming weeks. We also note that NZ production is highest over spring, with October the seasonal high.

Second, as mentioned above, global milk fat (butter) demand continues to surge, while supply struggles to keep pace. With the supply struggles in mind, **the global butter shortage is unlikely to correct until sometime in 2018.**

**In the short-term, NZ weather is the key to keeping the lid on global dairy prices.** If, however, wet weather continues and production stalls further, then we expect to move our milk price forecast to \$7.00/kg or above in the next month or so.



SPI Drought Index for 9am 21/07/2017 to 9am 19/09/2017



**ASB Economics & Research**

Chief Economist  
Senior Rural Economist  
Senior Economist  
Senior Economist  
Senior Economist, Wealth  
Economist  
Data & Publication Manager

Nick Tuffley  
Nathan Penny  
Jane Turner  
Mark Smith  
Chris Tennent-Brown  
Kim Mundy  
Judith Pinto

[nick.tuffley@asb.co.nz](mailto:nick.tuffley@asb.co.nz)  
[nathan.penny@asb.co.nz](mailto:nathan.penny@asb.co.nz)  
[jane.turner@asb.co.nz](mailto:jane.turner@asb.co.nz)  
[mark.smith4@asb.co.nz](mailto:mark.smith4@asb.co.nz)  
[chris.tennent-brown@asb.co.nz](mailto:chris.tennent-brown@asb.co.nz)  
[kim.mundy@asb.co.nz](mailto:kim.mundy@asb.co.nz)  
[judith.pinto@asb.co.nz](mailto:judith.pinto@asb.co.nz)

**Phone**

(649) 301 5659  
(649) 448 8778  
(649) 301 5853  
(649) 301 5657  
(649) 301 5915  
(649) 301 5661  
(649) 301 5660

[www.asb.co.nz/economics](http://www.asb.co.nz/economics)

@ASBMarkets

**Disclaimer**

This document is published solely for informational purposes. It has been prepared without taking account of your objectives, financial situation, or needs. Before acting on the information in this document, you should consider the appropriateness and suitability of the information, having regard to your objectives, financial situation and needs, and, if necessary seek appropriate professional or financial advice.

We believe that the information in this document is correct and any opinions, conclusions or recommendations are reasonably held or made, based on the information available at the time of its compilation, but no representation or warranty, either expressed or implied, is made or provided as to accuracy, reliability or completeness of any statement made in this document. Any opinions, conclusions or recommendations set forth in this document are subject to change without notice and may differ or be contrary to the opinions, conclusions or recommendations expressed elsewhere by ASB Bank Limited. We are under no obligation to, and do not, update or keep current the information contained in this document. Neither ASB nor any person involved in the preparation of this document accepts any liability for any loss or damage arising out of the use of all or any part of this document.

Any valuations, projections and forecasts contained in this document are based on a number of assumptions and estimates and are subject to contingencies and uncertainties. Different assumptions and estimates could result in materially different results. ASB does not represent or warrant that any of these valuations, projections or forecasts, or any of the underlying assumptions or estimates, will be met.