

# Dairy Update.

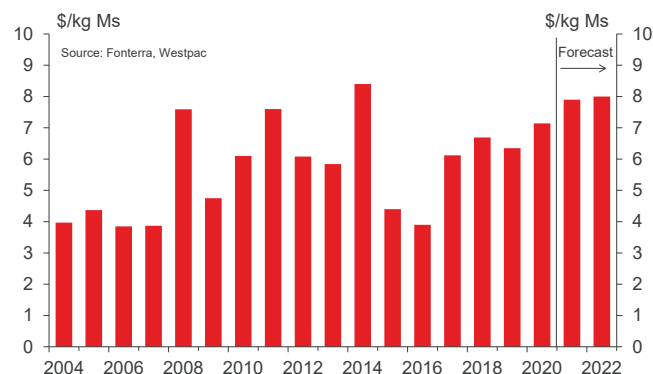
21 April 2021



## Stronger for longer.

- We upgrade our 2021/22 farmgate milk price forecast by 75 cents to \$8.00/kg.
- At the same time, we stick with our similarly healthy \$7.90/kg forecast for 2020/21.
- We expect high grain prices, environmental constraints and competition for land and water from other industries to rein in the usual global dairy supply response to very strong global demand.
- With that in mind, we now expect global dairy prices to remain stronger for longer in this dairy price cycle.

### Farmgate milk prices



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### Farmgate milk price forecasts

	2020/21		2021/22
	Westpac	Fonterra	Westpac
Milk price	\$7.90	\$7.30-\$7.90	\$8.00

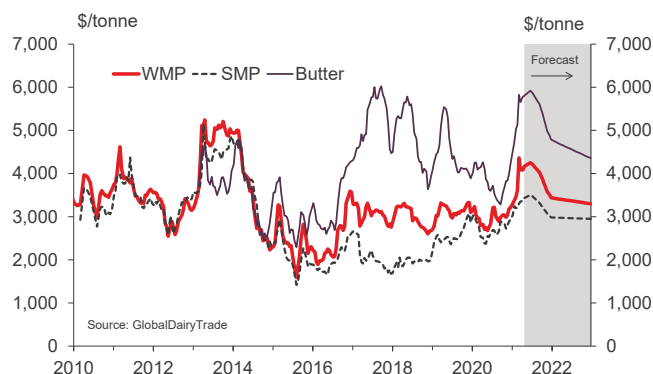
We have upgraded our 2021/22 farmgate milk price forecast by 75 cents to \$8.00/kg. At the same time, we have reaffirmed our 2020/21 forecast at \$7.90/kg. If realised, these will be the 3rd and 2nd highest milk prices on record.

### Starting 2021/22 on the front foot.

Compared to our previous forecasts set back in March, we now expect dairy prices to start the 2021/22 season firmly on the front foot. For example, in milk price terms, the auction result overnight (using the auction results and today's level of the NZD/USD) equates to a milk price of over \$9.00/kg. Since March, we have also lowered our NZD/USD forecasts by around two cents over the season, adding further upward impetus to our milk price forecast in NZ dollar terms.

From the stronger starting point, we have built in a moderation of global dairy prices over the New Zealand dairy season. Specifically, we forecast for whole milk powder prices (WMP) to fall by 18% over the season. In other words, we have built in a supply response to the higher milk price.

### Key dairy commodity prices and forecasts



## New Zealand dairy supply is constrained.

That said, we expect a very modest supply response to the high milk price by historical standards. As such we expect that dairy prices will remain stronger for longer. New Zealand dairy supply is constrained for a range of reasons, including:

- **Environmental constraints** – limits on cow numbers, limits on fertiliser usage and higher compliance costs are constraining production increases. At this stage, indicators point to a smaller dairy herd next season compared to this season.
- **Strong competition for land and water** from other uses such as horticulture, forestry, drystock and urban uses (housing and lifestyle blocks). Based on anecdotes, we expect the land area devoted to dairy to shrink next season.
- **Capital constraints** – overseas investment is limited given overseas investment restrictions on farmland purchases and credit availability is tighter than in the past.
- **Labour constraints** – farmers are facing ongoing worker shortages.

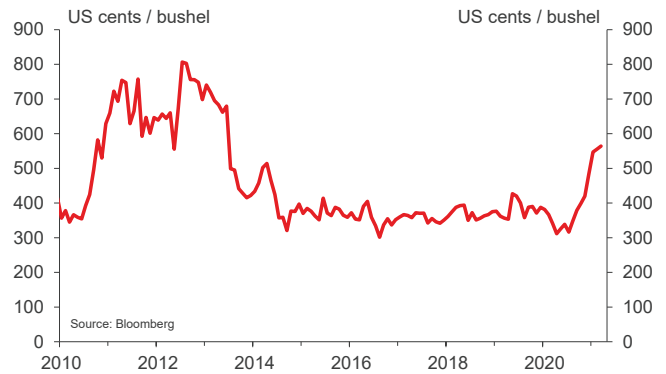
As a result, we expect modest production growth next season of 2%. While this would be in addition to the 1% growth we expect this season, it is modest given the very healthy milk price. Indeed, following the record milk price in 2013/14 production grew a whopping 10% over the season.

## Global supply constrained too.

Global dairy supply is similarly constrained. The European Commission and the USDA expect relatively modest growth over 2021 of 1% and 2%, respectively. Weighting those production forecasts by export shares sees production in the three major dairy exporters forecast to be up just 1.6% over 2021, compared to the 1.2% increase over 2020 (see table below).

The constraints that New Zealand farmers are facing are similar to those facing European and American farmers. However, in the short term, northern farmers are also battling very high grain feed prices (see corn price chart). When combined with somewhat subdued milk prices US and EU farmers have little incentive to increase production beyond what is currently forecast.

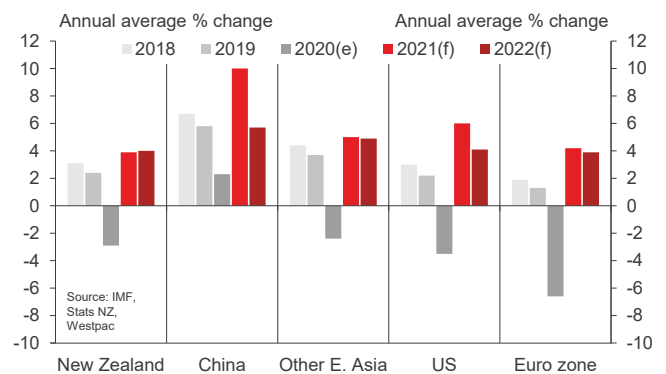
## Corn prices



## Global demand is strong and ongoing.

On the demand side, we expect robust demand to continue. As we have noted over recent months, strong Chinese and South-East Asian demand is underpinning the price strength and we expect this to be ongoing through 2021. Notably, we expect the Chinese economy to expand by 10% over 2021.

## Global GDP growth



At this juncture, we see risks on both sides of our 2021/22 forecast. The key downside risk to our 2021/22 forecast is the level of the NZD/USD. We have pencilled in for the NZD/USD to reach 0.74 by the end of 2021. However, a stronger global economy, for example, could push that even higher and thus drag down the farmgate milk price. On the flipside, the relatively modest supply response may not be enough to push down global dairy prices, which would mean a higher

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

Exporter	2020 actual (% change)	2021 forecast (% change)	Export share	2020 weighted actual (% change)	2021 weighted forecast (% change)
New Zealand	0.8	2.0	41%	0.3	0.8
EU	1.0	1.0	38%	0.4	0.4
USA	2.2	2.0	20%	0.4	0.4
<b>Weighted total by export share</b>	–	–	–	<b>1.2</b>	<b>1.6</b>

Source: Westpac (2021 New Zealand production forecast), DCANZ (2020 New Zealand production actual), European Commission, USDA

milk price than we have forecast. Note there is unlikely to be much change from here for the 2020/21 forecast as it's so late in the season.

## Auction Results, 21 April.

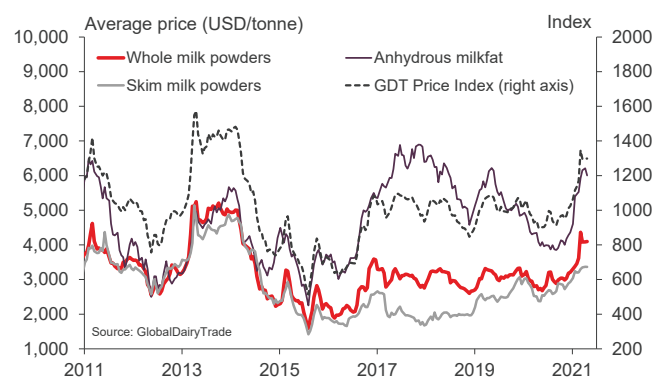
Dairy auction prices were steady overnight. WMP prices nudged higher (up 0.4%), while overall prices fell a touch (down 0.1%).

The result further consolidates the big price gains over March. WMP prices are now up 28% over 2021. Looking back to 2020, WMP prices now sit 50% higher than as at the same auction last year.

By product the auction result was mixed. Anhydrous milk fat price and lactose led the falls, both dipping over 3%. Butter prices also fell, while skim milk powder prices were flat and cheddar prices rose.

The result was weaker than expectations. Futures market pricing was signalling a whole milk powder price lift of 2%, similar to the lift we had pencilled in last week.

## Global dairy prices




## GlobalDairyTrade Auction Results, 21 April 2021

	Change since last auction	Prices USD/tonne
Whole Milk Powder (WMP)	0.4%	\$4,097
Skim Milk Powder (SMP)	0.0%	\$3,365
Anhydrous Milk Fat (AMF)	-3.3%	\$6,003
Butter	-0.6%	\$5,736
GDT Price Index	-0.1%	1,298

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