

NZ Forecast Update: Farmgate milk price

1 February 2022



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Contact

Susan Kilsby for more details.

Farmgate milk price forecast revised up

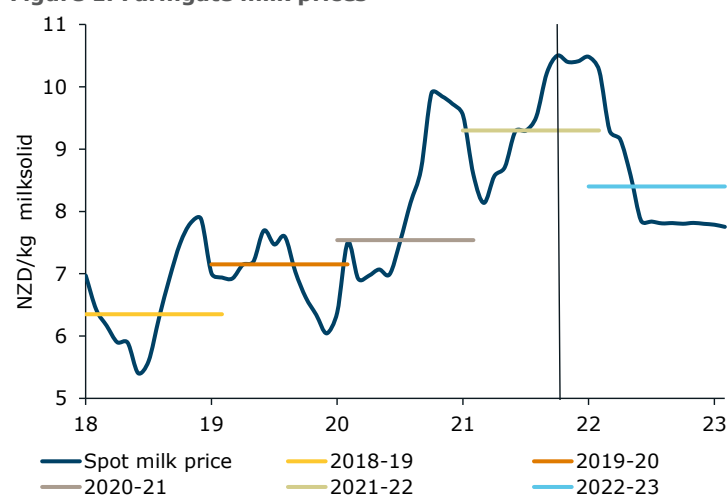
Key points

- We have revised our farmgate milk price forecast for the 2021-22 season up another 50c to \$9.30/kg milksolid (MS).
- Our forecast for the 2022-23 season has also lifted slightly from \$8.00/kg to \$8.40/kg MS. Prices are expected to moderate as demand and supply start to realign.
- The NZD is assumed to appreciate steadily across our forecast period to reach USD0.70 by the end of the 2022 calendar year.

Prices become more certain as the season progresses

We have revised up our farmgate milk price forecast for the 2021-22 season to \$9.30/kg MS (from \$8.80/kg MS). This puts our forecast just above the mid-point of Fonterra's latest milk price guidance of \$8.90 - \$9.50/kg MS.

Figure 1. Farmgate milk prices



Source: Fonterra, ANZ Research

Farmgate milk prices have benefitted from both the sharp lift in global dairy commodity prices and the softer NZD. Dairy prices lifted much faster than anticipated in January as the impact of tight global supplies for milk started to have a material impact.

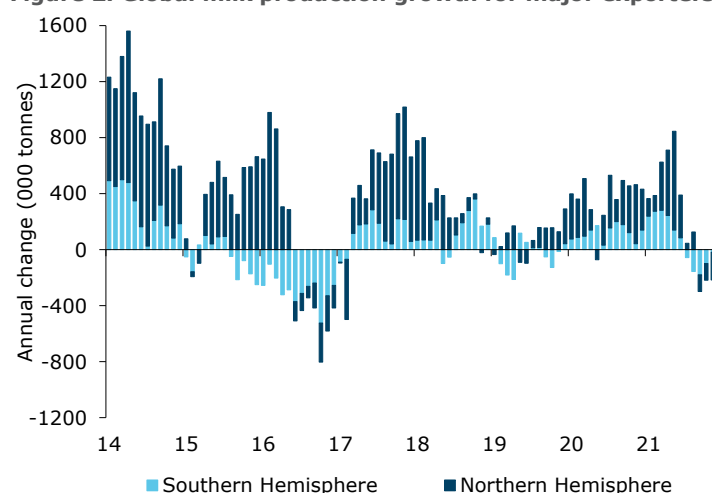
Table 1. Farmgate milk price sensitivity table (2021-22 season)

		NZD/USD effective					
Commodity price basket		USD/t	0.680	0.685	0.690	0.695	0.700
	10%	4560	10.65	10.55	10.50	10.40	10.30
	5%	4365	10.10	10.05	9.95	9.85	9.75
	Base	4150	9.50	9.45	9.30	9.25	9.20
	-5%	3945	8.95	8.85	8.80	8.70	8.60
	-10%	3735	8.35	8.25	8.20	8.10	8.05
	-15%	3525	7.75	7.70	7.60	7.55	7.50

Source: ANZ Research

Milk supplies in all of the major milk producing countries are either tracking behind last season or growing only modestly. This lack of additional supply is now being felt in the global markets.

Figure 2. Global milk production growth for major exporters



Source: DCANZ, Dairy Australia, Eurostat, USDA, CLAL, ANZ Research

The most recent milk production data from New Zealand, supported by dairy company announcements, means buyers are now well aware that there will not be a lot of additional product available from New Zealand during the latter part of the milk production season. New Zealand's milk supply is tracking 3.2% behind for the season to December, with production for the month of December down 5.5% on the same month last season. Dry conditions throughout January mean milk supplies are likely to be curtailed for much of the remainder of the season.

\$8.40 forecast for next season

Looking ahead, the 2022-23 season is also expected to deliver an above-average milk price. We have upgraded our forecast by 40c to \$8.40/kg MS. But we remain very cautious, as dairy commodity prices tend to have a habit of correcting quite quickly when prices reach high levels.

Global milk supplies will lift again when the Northern Hemisphere production hits in seasonal peak in about April/May. At this stage it seems unlikely that supply will surge more than normal, but strong prices may result in more milk being produced – particularly in the US.

Table 2. Farmgate milk price sensitivity table (2022-23 season)

		NZD/USD effective					
		USD/t	0.64	0.66	0.68	0.70	0.72
Commodity price basket	20%	4500	11.30	10.90	10.50	10.15	9.80
	10%	4125	10.15	9.80	9.45	9.10	8.80
	Base	3750	9.05	8.70	8.40	8.10	7.80
	-10%	3375	7.95	7.65	7.35	7.05	6.80
	-20%	3000	6.80	6.55	6.30	6.05	5.80
	-30%	2625	5.70	5.45	5.25	5.00	4.80

Source: ANZ Research

We are also likely to see some decrease in demand for dairy products. Prices are now at such exceptionally high levels that they will be priced out of reach of consumers in some of the poorer nations. Typically, demand from North Africa/Middle East, and parts of South East Asia tends to ease when prices are this strong. Demand from China tends to be less price sensitive, but any

reduction in demand from this massive importer of dairy products would have a meaningful impact on the dairy markets.

At present the NZX futures market is pricing in much stronger dairy commodity prices and the milk price contract for next season (Sep 23) is priced at \$9.35/kg MS. That is nearly \$1 above our forecast.

Steady lift in NZ dollar anticipated.

We anticipate a gradual increase in the NZD across the forecast period. The NZ dollar has remained very subdued and hasn't strengthened in response to the RBNZ starting to tighten monetary policy. Most central banks around the globe are now poised to commence monetary policy tightening, so it is not just New Zealand that is experiencing rising interest rates. If New Zealand's interest rates are higher than other countries then we tend to attract more money flowing into New Zealand which puts upward pressure on our exchange rate. We now anticipate the NZD will gradually firm to USD0.70 by December 2022

Figure 3. NZD/USD



Source: Bloomberg, ANZ Research

Overall the outlook for the farmgate milk price remains very robust in the near term. Unfortunately, on-farm costs have also risen rapidly, due to rising compliance costs, higher interest rates and increasingly scarce and expensive labour. These factors are taking the shine off of the record milk price that is expected to be delivered this season.



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Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 27 664 3554
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)



David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 4 576 1022
Email: david.croy@anz.com



Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com



Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com



Finn Robinson
Economist

Macroeconomic forecasting, economic developments, labour market dynamics, inflation and monetary policy.

Telephone: +64 21 629 553
Email: finn.robinson@anz.com



Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com



Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 21 253 6808
Email: natalie.denne@anz.com



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