

From the Trading Floor

KEY MARKET DRIVERS

- NZ send belated price signal to farmers / E.U. & USA not so much
- gDT horrible
- US Lactose pricing firming / WPC stabilizes & firms (slightly)
- Could Russia be back earlier than expected?

- We now have advice from the majority of NZ's major dairy companies (with exception of Tatua) that they have reduced their forecasted milk prices for the 2015/16 season on the back of continued poor returns on the commodity market. It is a price signal which will, eventually, put downward pressure on milk flows, although likely be too late to have a huge impact this season. Fonterra had started out with an anaemic opening price for 2015/16 but then quickly revised up on the hope of better times ahead. The about-face certainly resulted in stronger milk than would otherwise have been the case. The same price signal has not been received by EU or US farmers who are still receiving milk prices above cost of production, indicating that milk will be strong through the Northern Hemisphere peak
- gDT again threw up a very disappointing result last night. Everything was down to various degrees. WMP probably the most disappointing at -10%. E.U. SMP again failed to clear.
- Reports that US lactose and WPC80 prices have bounced off its very low levels due to disruptions in supply to the big West Coast USA producers, which was caused by the compounding effects of YoY drought conditions which have smashed Californian milk production (recent rains have been welcomed).
- Reports from various sectors that some E.U. Members would welcome the dropping of economic sanctions against Russia, which would hopefully result in the re-opening of the borders to EU dairy trade and an important (albeit poorer) market. Other E.U. Members and USA may not be so keen on that. Watch this space as it can be very unpredictable.

Matt Cooper, Director, Ausfine Foods

DAIRY FUTURES

3-Feb	SMP	NDM	WMP	Cheese	AMF	Butter
Exchange	NZX	CME	NZX	CME	NZX	CME
Feb-16	1,730	1,649	1,980	3,382	3,650	4,733
Mar-16	1,730	1,698	2,000	3,364	3,720	4,826
Apr-16	1,740	1,706	2,040	3,375	3,550	4,850
May-16	1,760	1,714	2,110	3,450	3,570	4,831
Jun-16	1,800	1,773	2,200	3,532	3,600	4,856
Jul-16	1,850	1,808	2,250	3,620	3,650	4,894
Change	-5%	-2%	-5%	1%	-2%	-3%
Op interest	2,281	5,050	15,333	19,251	384	3,723

AUSTRALIAN INDUSTRY NEWS

Murray Goulburn wins Coles contract

Murray Goulburn has entered into a five year private label contract to supply Coles brand Australian cheese. The contract includes supply of Coles brand cheddar-style cheese including tasty, Colby, mild and light cheese in blocks, shreds and slices across Australia starting 1 January 2017. Murray Goulburn projects the contract will generate \$130m in additional sales every year.

WCB reassures on price

Warrnambool Cheese and Butter has sent a letter to its suppliers, stating it is maintaining its milk payout at \$5.60kgMS, despite world dairy markets deterioration at the start of the season. Despite the strong growth in EU output, declining Chinese demand and the Russian ban on dairy imports, Warrnambool says the weak A\$ has made it possible for the company to maintain its price.

Wetter outlook

Australia's south east is in for a much wetter late summer and autumn, according to the Bureau of Meteorology (BoM)'s latest seasonal outlook for February to April. Temperatures are likely to be cooler in the central regions, but warmer in the far south.

The BoM noted that although the El Niño event is now abating, most indicators remain well above El Niño thresholds. Models forecast a return to a neutral ENSO pattern in late autumn to early winter.

Kiwi payout forecasts cut

Fonterra's milk price forecast for 2015/16 has been revised down to NZ\$4.15kgMS from NZ\$4.60kgMS – a response to weak international prices, flattening demand and strong EU supply. Synlait Milk also revised its forecast milk price for the current season to NZ\$4.20kgMS from NZ\$5kgMS. According to Synlait chairman Graeme Milne, the cut in price is a response to low global commodity prices with a slower than expected recovery.

FUTURES by Scott.Briggs - Sbriggs@ausfine.com

Prior to this week's GDT, the NZX futures came off very hard – with the actual result then confirming very soft physical buying interest out there. That said WMP for H2 2016 delivery can now be bought for between \$2300-2500/t, which will start to look attractive to buyers as we begin focussing on that period. Pls let us know if you have interest at these levels as these can be worked back into physical prices.

Weather highlights

- In Australia, ex-cyclone Stan is generating rain and strong winds over western Vic. Possible showers in western NSW, possible showers and thunderstorms in southwest Qld.
- In NZ, rain is expected to move over southwestern parts of the South Island. Rain is expected to move across the North Island leading up to the weekend.
- In the US, a storm system building across eastern states brings bursts of rain. Winterstorm Kayla will bring severe winds across the Plains and Midwest and snow to the eastern Great Lakes. Tornado warnings have been issued for the Midwest.
- Dry and hot across central Brazil with possible thunderstorms and rain moving across the region over the weekend.
- Storm warnings in Scandinavia and northern parts of central Europe. Dry weather on the weekend.

China cracks down on IMF brands

Beijing authorities have introduced tougher safety laws, limiting manufacturers to only three brands in China. The new laws are aimed at improving food safety and tightening supply chains, as a manufacturer cannot use the same formula in different brands. According to Lei Yongjun, chairman of consulting firm Proper Tao Ltd, as many as 80% of the baby formula brands sold in China could disappear as domestic manufacturers operate multi-brand strategies. He said it would most likely benefit big international baby formula manufacturers, who could take the market share from local rivals.

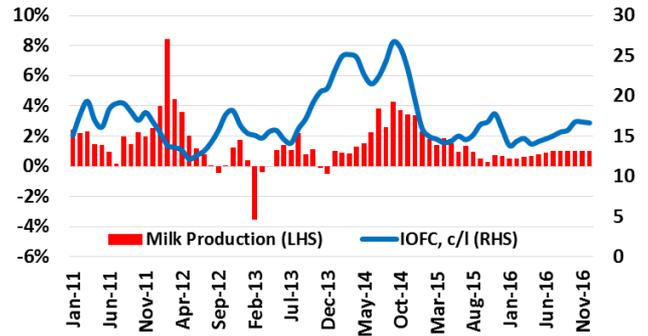
Margins still support US growth

The average December 2015 income-over-feed cost (IOFC) totaled US\$9.63/cwt, representing the 29th consecutive month of margins that in theory support milk expansion (i.e IOFC is above US\$7-7.50/cwt).

During the full 2015 year, the IOFC averaged close to the 5-year average, US\$9.01/cwt compared to US\$9.53/cwt, but well below the 2014 level of US\$14.47/cwt. But the US is diverse and different regions achieve a range of margins dependent on market mix and feed supplies.

Analysis suggests the IOFC will improve slightly from here throughout 2016, which will continue to support modest output growth.

YOY growth in US milk production v IOFC



GDT smashed again

The GDT price index dropped 7.4% at this week's auction, continuing the negative trend of the previous two auctions. The WMP index fell 10.4% (to US\$1,952/t), followed by the butter index which shed 8.3% (to US\$2,905/t). The AMF index dropped 6.6% (to US\$3,486), cheddar decreased 4.2% (to US\$ 2,807/t) and SMP shed 2.2% (to US\$1,792/t).

The drop came despite the limited volumes on offer, 24,474t compared to the average 29,076t over the past 12 months, however, the drop in the GDT indices corresponds to the drop in dairy futures yesterday with WMP February contract dropping below US\$2,000/t.

GDT weighted average auction prices by event, US\$/t

