

WESTPAC DAIRY UPDATE

Forecast update and GlobalDairyTrade auction results.

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Hit and stick II.

- Dairy auction prices took another hit overnight as expected.
- The Omicron outbreak in China and the Sri Lankan crisis have combined to whack prices lower over the last five auctions.
- As a result, and as announced yesterday in our Economic Overview, we have downgraded our 2021/22 milk price forecast by 20 cents to \$9.30/kg.
- However, we expect much of this price hit to prove temporary. Thus, we stick with our 2022/23 forecast of \$9.25/kg.

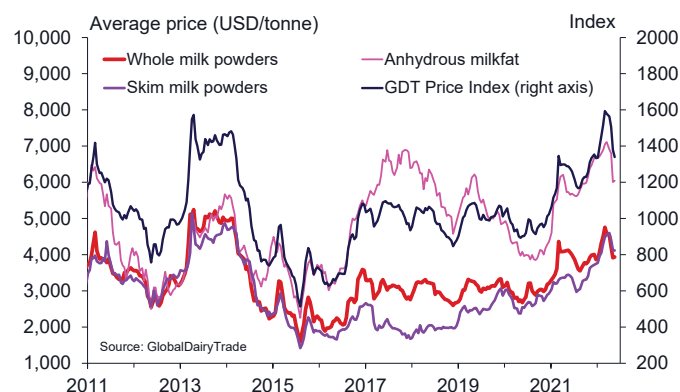
GlobalDairyTrade auction results

	Change since last auction	Prices USD/tonne
Whole Milk Powder (WMP)	-4.9%	\$3,934
Skim Milk Powder (SMP)	-0.6%	\$4,116
Anhydrous Milk Fat (AMF)	0.6%	\$6,043
Butter	-1.0%	\$5,750
GDT Price Index	-2.9%	1,340

Dairy auction prices took another hit overnight. Overall prices slipped 2.9%, while key whole milk powder (WMP) prices slid by 4.9%. We had expected a price fall overnight, although the magnitude of the fall was larger than the 2% WMP price fall we had pencilled in late last week.

Prices have now decreased materially over the last five auctions. Over that period, overall prices have dropped 15.9%, while WMP prices have fallen 18.1%.

Global dairy prices



The chief reason for the fall, as we have discussed previously, is the Omicron outbreak in China. But the impact of the Sri Lankan crisis has also played an important role.

Previously, Sri Lanka had been a small, but nonetheless, highly profitable market for Fonterra, including for some of its consumer brands. The Sri Lankan political and economic crisis

has essentially caused this market to collapse. And the milk that was previously earmarked for consumer goods in Sri Lanka has been re-routed into commodity markets instead, i.e. sold on the dairy auction platform as milk powders. To a degree, it's likely that this re-routing is also true for some consumer products that were destined for China.

Notably, this re-routing of product has occurred over May, causing much of the additional price weakness that we have seen in the last two auctions. WMP prices fell 11.1% over the two May auctions, after falling 7.8% over the previous three.

With the above in mind and following Fonterra's downgrade last week, we have trimmed our 2021/22 forecast by 20 cents to \$9.30/kg. That is consistent with the midpoint of Fonterra's forecast range of \$9.10/kg to \$9.50/kg. Note, at this late stage of the season, we usually adopt Fonterra's forecast (give or take) as Fonterra has the best information on the likely final milk price.

Farmgate milk prices



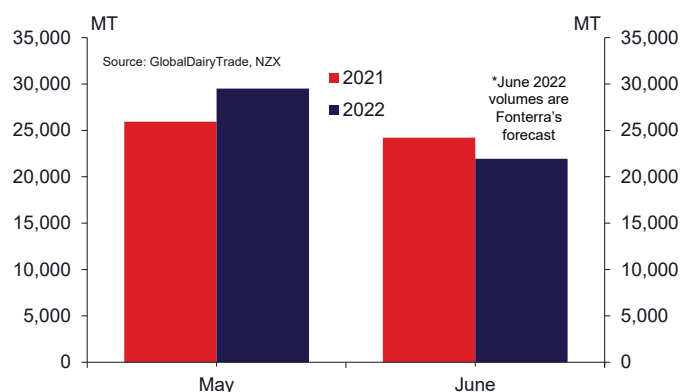
However, we are sticking with our 2022/23 forecast of \$9.25/kg. We still expect this dip in Chinese demand will prove temporary as Covid restrictions will eventually ease. Indeed, in Shanghai, Covid restrictions are starting to wind back and daily case numbers are falling.

Farmgate milk price forecasts

	2021/22		2022/23
	Westpac	Fonterra	Westpac
Milk price	\$9.30	\$9.10-\$9.50	\$9.25

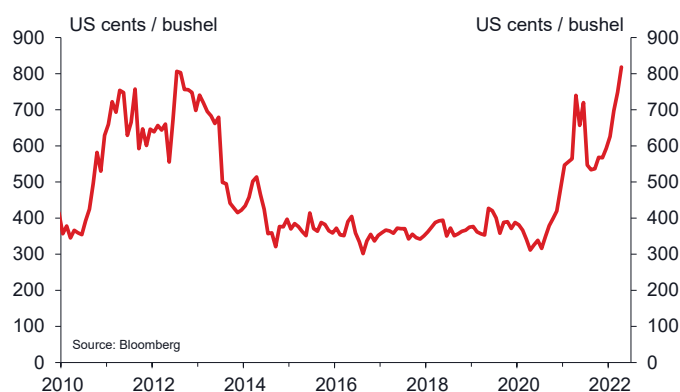
In addition, the re-routing of product into commodities is now complete. May WMP auction volumes sold were up around 14% on May 2021. And interestingly, looking at volumes for just the first two contracts (i.e. for product produced from this season's milk), volumes were up around 29%. Whereas, the scheduled volumes for June are forecast to be down on June 2021 by around 10%.

Whole milk powder dairy auction volumes sold



Meanwhile, fundamentally global supply remains tight and we expect this tightness to support prices over the second half of (calendar) 2022 and into 2023. Indeed, global grain feed prices remain very high and continue to put the squeeze on farmer margins in the US, Europe and Australia.

Corn prices



Lastly, the dip in the New Zealand dollar is putting the milk price on the front foot for the new season. The NZD/USD has been as low as US\$0.62 over the last week and is currently trading at US\$0.635. The current level is a marked drop from around US\$0.68 just a month ago.

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