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The return of milk scarcity – Rabobank on dairy

The global dairy market appears to be heading for a period of renewed supply scarcity in the coming 12 months, according to Rabobank.

Rabobank senior dairy analyst Hayley Moynihan says the impetus for tightening emanates largely from the supply side, where low milk prices, extreme feed costs and pockets of unfavourable weather are expected to slow growth in milk production in export regions.

"We fear that much of the market has been lulled into a false sense of security by the phenomenal growth seasons we saw late in 2011 and early 2012, with the next 12 months to provide a rude awakening," Ms Moynihan says.

"The slowdown in milk production growth in export regions will be sufficient to undershoot even the modest growth in consumption that we expect in advanced economies – given the sobering economic outlook in the EU and US."

Ms Moynihan says this will reduce the exportable surplus available from the 'Big Seven' export regions of the world (EU, US, New Zealand, Australia, Argentina and Brazil) in the closing months of 2012 and the first half of 2013 – the first such reductions in more than four years.

"With little excess inventory in the market, the equation then becomes simple – any increase in import demand from deficit regions will create supply shortages, with the extent of the shortage fuelling an appetite for imports," she says.

Factoring in a modest planned increase in imports over the next 12 months from key buying regions, Rabobank expects prices to rise substantially in the international market in order to bring about the demand rationing needed to balance the market and move prices into alignment with the rallies already evident in US and EU wholesale pricing.

Locally in New Zealand, the new 2012/13 season has started off well. Dairy farms and cows are positioned well for a good start to the season and climate has been relatively kind so far, Ms Moynihan says.

"Milk flows were around 13 per cent high than the previous year for the three months to August," she says.

"However, these months represent the seasonal low-point for milk supply – New Zealand produces only as much milk as Minnesota over this period – and it would be unwise to expect such growth to continue."

Rabobank expects the strength of the New Zealand season will largely be determined by the spring flush over coming months and the capacity of industry to match the phenomenal shoulder period that followed the flush last season.

Fonterra's forecast milk price for the season was moved five per cent lower in August to NZD 5.25/kg Milk Solid and now sits 13 per cent below last season's closing level.

"With most investments in herd and pasture for the new season already made, this wont impact immediate production and prospects," Ms Moynihan says.

"But, at this price there is little incentive to purchase additional feed to extend lactation later in the season should bad weather reduce pasture growth."

Ms Moynihan says that replicating last year's "phenomenal" production levels will also get harder as the year progresses, given the exceptional combination of fabulous weather and higher pricing in place at that time.

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Media contacts:

Denise Shaw
Media Relations Manager
Rabobank Australia & New Zealand
Phone: +61 2 8115 2744 or
+61 439 603 525
Email: denise.shaw@rabobank.com

Jess Martin
Media Relations Specialist
Rabobank Australia & New Zealand
Phone: +61 2 8115 4861

Email: jess.martin@rabobank.com