

Commodities Weekly

Dairy and NZD decline continues.



ECONOMICS

5 Feb. 10

CBA NZ Commodity Price Indices

As at Friday, 29th January 2010.

Series	Index *	Week %	Year % **
Total NZD	144.8	0.3%	-1.8%
Total SDR	136.4	-0.2%	30.3%
Total USD	153.5	-1.0%	35.3%
Dairy USD	191.8	-1.5%	55.3%
Sheep/beef	139.3	0.6%	25.4%
Forestry	124.5	-0.6%	27.7%
NZD/USD	0.7010	-1.3%	37.8%

* For all indices 1997 average = 100

** Percentage change since same week last year

The CBA NZ Commodity Price Index eased in SDR and USD denominations last week, with drops recorded in the dairy and forestry categories offsetting a pick up in sheep/beef. The NZD was down 1.3%, which saw the commodity index rise in NZD terms.

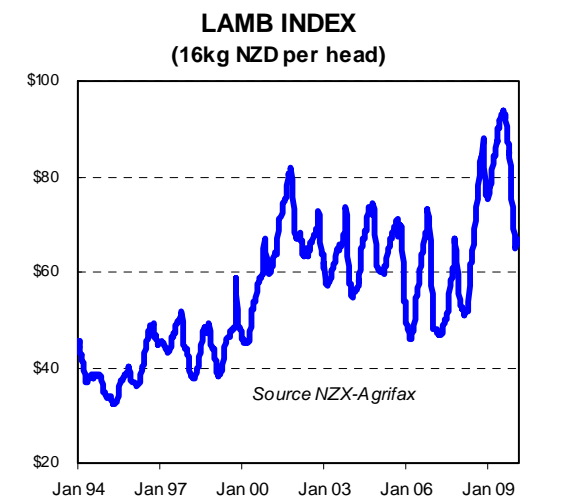
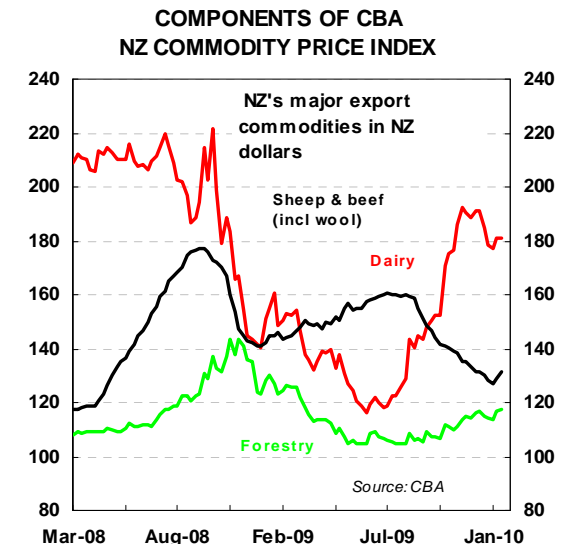
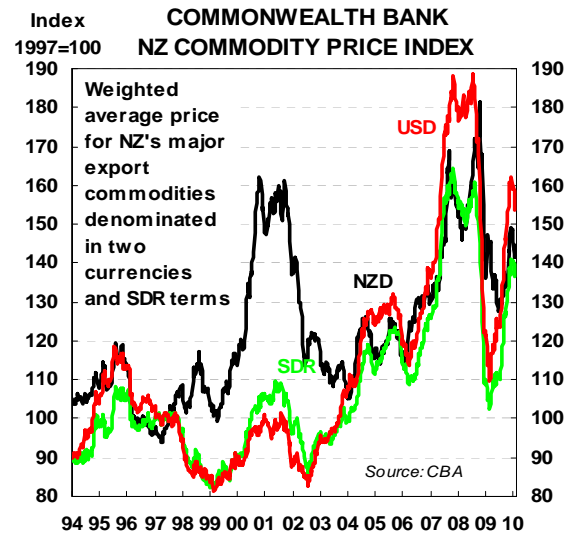
NZX Agrifax reports a slowdown in lamb kill. Kill numbers for January are 8% down on year-ago levels. Good grass cover and recent rain is behind the slowing. Exporters are now looking for product to fill chilled orders for the Easter period, boosting lamb schedule prices. Prices lifted 5c-10c/kg last week. NZX Agrifax also reported an average 5c/kg lift in beef schedule prices. The recent decline in the NZD against the USD is certainly a help for beef exporters.

There were a few surprises in the US Department of Agriculture report on cattle last week – particularly for the dairy sector. With all the talk of herd retirement programs through 2009, most were predicting the US dairy herd to shrink by close on 2.5% this year. However, it seems that dairy heifers have been held back and the herd has in fact increased by 2.4%. Higher US production would likely be negative for world dairy prices.

Whole Milk Powder prices dipped in the latest global DairyTrade auction on Tuesday. Average WMP prices were down 1.6% from a month ago. Global Dairy Fonterra commented "We've just been through a period of supply restocking which appears to have come to an end." Some of the supply concerns that led to the huge lift in prices over the last year seem to be easing, and this is likely to continue as production picks up the northern hemisphere.

Guest dairy comment from Professor William C Bailey, Chair, Department of Agriculture, Western Illinois University.

World dairy prices were broadly lower last week with nonfat dry milk powder prices leading the way down. –see over



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General Advice Warning

As this report was prepared without taking into account your objectives, financial situation or particular needs, you should not take any action in reliance of this report without considering your particular circumstances and, if necessary, obtaining professional advice.

Butter prices also dropped slightly while cheese prices were mostly unchanged. Fonterra's latest trading session took place on Feb. 2, when 3,000 metric tonnes of anhydrous milk fat and 21,000 tons of whole milk powder (WMP) were auctioned. [Auction results noted above]

In March, 7,500 tonnes skim milk powder (SMP) will be offered for the first time. The SMP volume is set to increase to 15,000 tonnes by July 2010.

Recent US government data shows milk production margins continue to improve as feed costs declined about 1% from December levels. An important reason for the feed price decline is the impact of a record US corn crop on prices. Corn prices have dropped more than 15% since the start of 2010 with soybean prices off more than 10%. In addition to declining feed prices, the US government also reported of an excellent supply of heifers available to the market. In fact, replacement heifer numbers are at their highest level in nearly a quarter century. Some analysts see the two factors supportive of ideas that US milk production could increase from last year's level.

It could have been a combination of a stronger kiwi dollar, higher prices and slowing world demand that resulted in a decline in New Zealand dairy exports during the December 2009 Quarter compared to 2008 levels. The value and volume of milk powder, butter, casein and cheese exports all declined.

Interest Rates and Currency

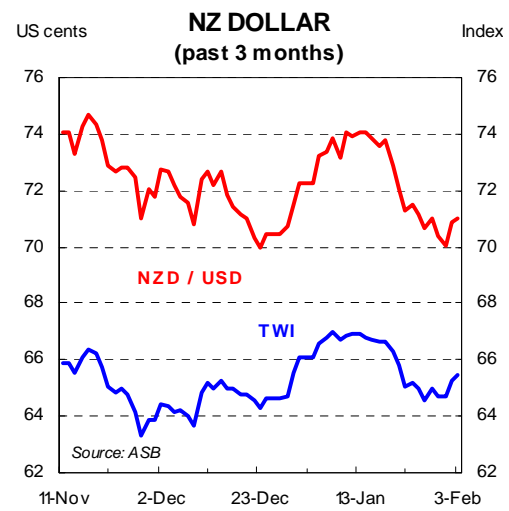
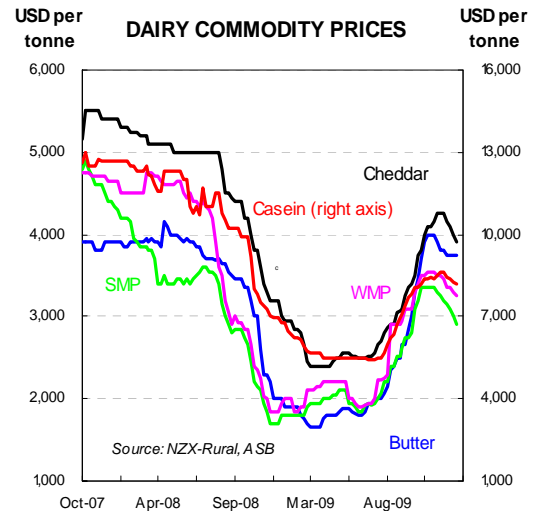
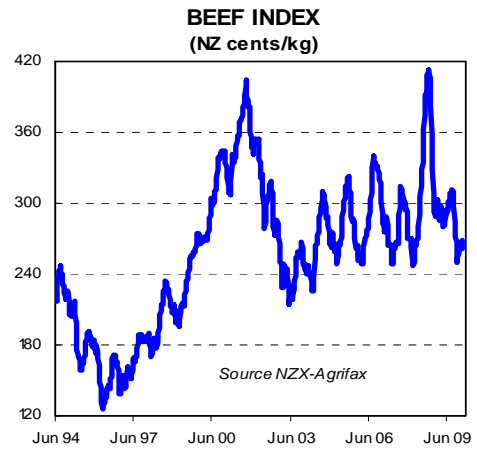
NZD was mixed last week, but little changed on a trade weighted basis. Over the week, the NZD met resistance around 0.715 and found support at 0.70 against the USD. By the end of the week the NZD was at the bottom of the range. This week the NZD has traded below 0.69. A USD recovery, further Europe-related risk aversion and a higher than expected unemployment rate released for Q4 2009 on Thursday 4th has sent the NZD to new 2010 lows.

Local interest rates were little changed last week. There were no surprises in the Bank's decision to hold the OCR at 2.5%, and the RBNZ toed a very similar line to the December statement (even going so far as to specifically note that). [Click here for our RBNZ review.](#)

Interest rates showed little reaction to the RBNZ announcement with swap rates ticking up by only 2-3 basis points on Thursday. Dr Bollard's on the record speech of Friday also had little impact the market. However, the softer than expected labour market report mentioned above did cause short-term interest rates to drop this week. Q4's headline unemployment rate is disappointingly high, and the weakness fuels thoughts the RBNZ will be in no hurry to raise interest rates. Our view is for a 0.25% April hike, timed after key GDP, CPI and business confidence releases. However, the HLFS data do skew risks to a later move, in June.

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