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28 February, 2018

## New Zealand Dairy News

### A2 profit more than doubles:

Infant formula maker a2 Milk Company posted a 150% jump in profit to NZ\$98.5m for the first half of FY18. Revenue grew 70% to NZ\$434m for the period, due to strong sales of the a2 Platinum formula in Australia and China, posting growth of 85%. EBIT grew 127% to NZ\$142m. The China and Asian region contributed 33% of EBITDA in the half, up from a 22% contribution a year earlier. Growth of a2 milk products has slowed in Australia however to just 3%, holding a 9.5% share of the category according to the company.

Managing Director Geoffrey Babidge said the financial performance reflects the strength of the company's brand position. He said consumer interest in the benefits of dairy-based products free of the A1 beta-casein protein continues to grow, prompting the company to invest strategically in marketing, promotion and education programs in each market.

### Synlait buys Pokeno site:

Synlait Milk has conditionally purchased a site in Pokeno in the Waikato where it plans to invest NZ\$260m in a second nutritional powder manufacturing facility. The increased capacity is needed to match growing demand for infant formula, however the purchase is subject to Overseas Investment Office approval. The first Pokeno dryer is expected to have an annual capacity of 40,000t, matching dryer 3 at Synlait's Dunsandel site. Chief executive John Penno said the plant gave the company an opportunity to balance its exposure to a single powder manufacturing site and a single milk supply pool at its South Island plant.

### Danone invests NZ\$25m in processing:

French dairy company Danone has completed a NZ\$25m upgrade of its blending and milk processing plant in Auckland. The upgrade doubles the site's production capacity, so it can meet growing demand for its infant formula. Danone's New Zealand processing plants produce base powder for other Danone plants in Asia Pacific, and international products to supply domestic and Asia Pacific markets. According to Danone New Zealand's operations director Cyril Marniquet, the upgrade was needed to service growing demand for its international products such as Karicare and Aptamil in other markets, including China. Australia continues to be Danone's number one export out of New Zealand.

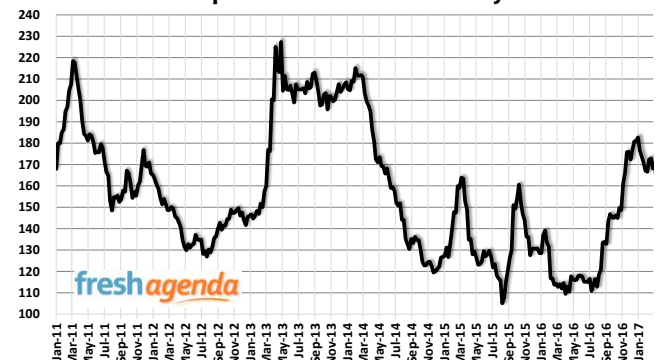
### A2 elite bulls launched:

Following last week's announcement of Fonterra and a2's strategic partnership, herd improvement and agri-technology cooperative LIC has launched a new dedicated team of high breeding a2 bulls. According to LIC's chief executive Wayne McNee, many farmers are already breeding towards a2, however with genotype testing a full a2 status could be achieved much faster.

## NZ Dairy Export Index

**Index up slightly** – The NZ dairy export index rose on mixed prices trends and a steady Kiwi dollar. WMP spot prices lifted US\$40/t to US\$3,250/t. Butter sat at US\$5,300/t and SMP rose US\$50/t to US\$2,000/t. Cheddar prices remained at US\$3,700/t for another week. The NZ\$ was steady at **US\$0.73**, lifting the index by **0.7 of a point to 166.27**.

### NZ export index since January 2011



*Take note: The index is an indicator of spot trends in gross export returns to the industry based on quoted NZ export prices, movements in currency and the total milk usage in exports by the NZ industry. It was set at 100 on 1 January 2000.*

## Australian Dairy News

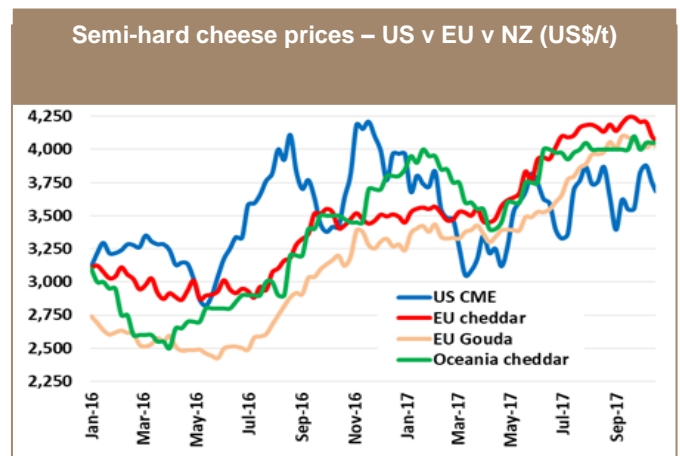
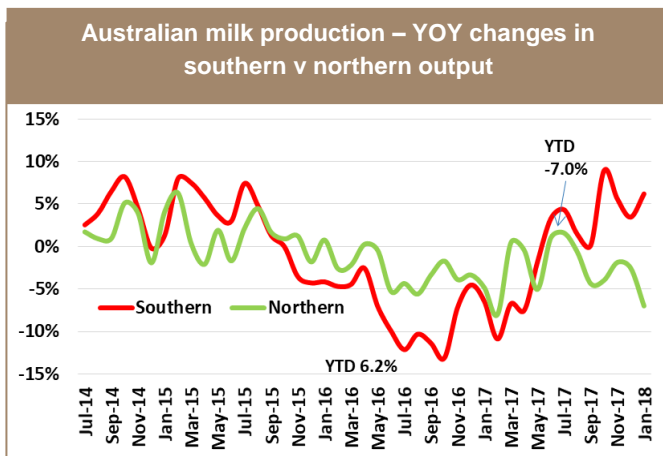
### Milk output up 3.9% in January:

Dairy Australia reports January milk production was up 3.9% YOY, marking the seventh consecutive month of milk production increases, given the large fall in output in the 2016/17 season. This puts season-to-date production ahead 3.1%.

Milk production in the southern region increased 4.7% for the month, while the northern region was 2.7% down. Victorian milk production rose 5.9% YOY, with northern Victoria's output jumping 11.3% YOY, while Gippsland recorded an increase of 8.3% more than offsetting a 1.7% decrease YOY in milk collection in western Victoria. Season-to-date production for the state is 3.9% ahead, although the largest western region is up just 0.3%. Tasmanian production increased 5.7% for the month and 6.4% for the season.

### Cheese, WMP in favour:

Australian manufacturers continue to favour cheese and WMP in half-year product output data, with cheese production up 8% for the season-to-date to December. According to Dairy Australia, cheddar output was 12.5% ahead for the half year, while production of non-cheddar varieties rose 2.5% season-to-date. WMP was also prioritised, production lifted 33.4% for the half year. In contrast, SMP output dropped 23% for the half year. In line with lower SMP production, butter output was behind 19.2% for the season-to-date and butteroil production was down 24.1% for the season-to-date. Whey powder season-to-date production was up 3.4%.



## Global and Corporate Dairy News

### US most competitive in cheese:

US cheddar prices are the most competitive on the global market. American cheese supply and demand, based on disappearance estimates) rose at a near-equivalent pace (approximately 3%) during 2017. Local milk production continues to increase into 2018, however demand has been weaker of late. Oceania SMP prices are at a significant premium to Europe and especially the US (with high inventories). Some buyers are unable to switch product sourcing due to customer taste profiles and superior product perception. The Euro has eased relative to the greenback since mid-February, which may assist European exporters in achieving another record-breaking year of SMP exports.

Oceania is also the most expensive supply region for WMP – reflecting lower New Zealand milk production this season, which most in the industry expect will end lower for the third consecutive year. US butter prices are significantly lower than Oceania's, however Europe is the most expensive supply region - stocks are still relatively low, and there is uncertainty in the market regarding the extent of the European spring flush.

### NZ WMP exports rise:

New Zealand WMP exports increased for the second consecutive month in January, up 16.2% YOY to 151,613t. Weaker shipments to China & HK which fell 14.8% YOY were more than offset by stronger sales to Africa, GCC, ASEAN and South America. Total SMP exports fell 6.5% YOY in January, despite stronger shipments to China & HK.

China continues to be crucial to global balance in the powder market. We estimate this region accounted for 35% of the growth in total SMP export trade in 2017. Cheese and butter exports also declined in January – down 9% and 12% YOY respectively. During the past quarter, cheese exports fell 8% to 94,591t while butter shipments were flat at 82,427t.

### **EU cheese stronger, butter retreats:**

European wholesale cheese prices are now increasing, the result of significantly higher fat valuations as well as solid demand across varieties. German Gouda wholesale prices for the week ending 21 February were reported in the €2,500-2,700/t range. Polish Cheddar prices also rose for the week ending 18 February at €2,500/t – up €170/t from the prior week.

Since the start of the month, butter wholesale prices have increased €900/t to €5,150/t in the week ending 23 February. The futures market retreated late last week however, before recovering some of the losses this Monday as buyers are likely pushing back. EEX butter contracts for delivery through to the end of 2018 are now trading in the €4,850 to €4,950/t range. SMP (food) wholesale prices have fallen marginally to €1,300/t with bulk feed product quoted at €1,200/t for Q2-18 delivery.

### **US milk overshoots expectations:**

USDA's NASS reports milk output rose 1.8% YOY in January – a surprise to many in the industry. Average yield per cow was up 1.3% YOY in January – the largest improvement in nine months, while cow numbers increased 0.5% YOY. This brought the number of milking cows in January to 9.405m nationally, 46,000 more than in the same month in 2017 and 5,000 up on December. Historical figures were revised by the government agency – leap year-adjusted US milk production rose 1.7% in 2017 with national dairy cow numbers rising for the three consecutive months to January 2018.

California's January output rose 2.2% YOY – the first expansion since December 2016. Production in the Desert States (Texas, New Mexico, Arizona and Colorado) remained robust – up 5.9% YOY in January, increasing for the 20th month in a row. Milk supply in the Upper Midwest also rose, but at a more subdued pace of 1.2% YOY in January – the slowest expansion in eight months. According to local analyst Matthew Gould, there have been complaints in the Midwest about the withdrawal of rBST slowing milk growth. Moreover, in the Northeast, there have been feed quality issues reported.

### **Mixed US inventory trends:**

USDA's Cold Storage report reveals American cheese stocks fell 3,917t between December and January. January American cheese stocks were reported at 334,848t, 9.2% above the 5-year average but 2% lower in YOY terms. This trend is indicative of good demand for American cheese at the start of 2018, with oversupply easing since July 2017.

Other-than-American cheese (including Mozzarella) stocks rose 1,485t between December and January – this was 14% higher in YOY terms and 26.8% above the 5-year average, reflecting a weakening foodservice sector. Natural cheese stocks in refrigerated warehouses on January 31, 2018 were down slightly from the previous month, but up 7% from January 31, 2017 and at a record high for the period. Butter stocks were higher in YOY terms for the second consecutive month in January at 101,548t – 22.5% above the 5-year average.

## **Beef and Lamb News**

### **US import prices edge up:**

US imported beef prices were largely unchanged from the week prior. Limited trading between overseas suppliers and US importers saw the US 90CL close at US\$2.145/lbs, down from the week before but still 2.6% up on year-ago levels. According to Steiner Consulting's weekly report, import beef trade remained light as buyers wait for increased offerings instead of chasing limited supply. New Zealand slaughter is seasonally low and NZ packers are unsure about slaughter levels in March. This makes packers cautious about new bookings and firm on prices.

### **Australian wagyu investment grows herd:**

Australian superannuation fund First State Super has invested A\$6.7m in a wagyu beef operation in north-west New South Wales. With the money, Stone Axe Pastoral gets the capital it needs to develop the largest full-blood wagyu cattle herd outside

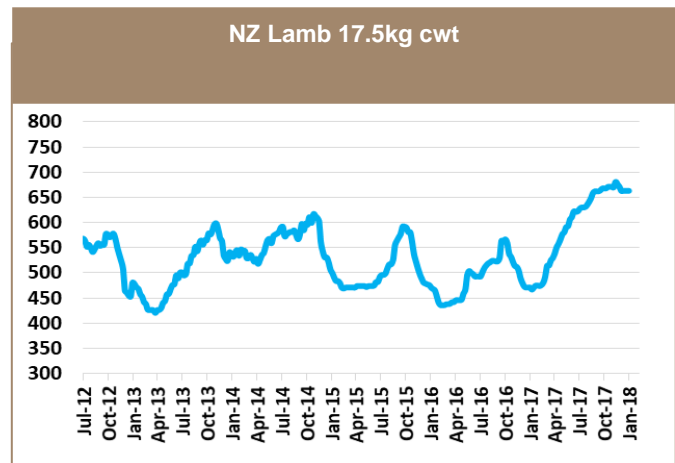
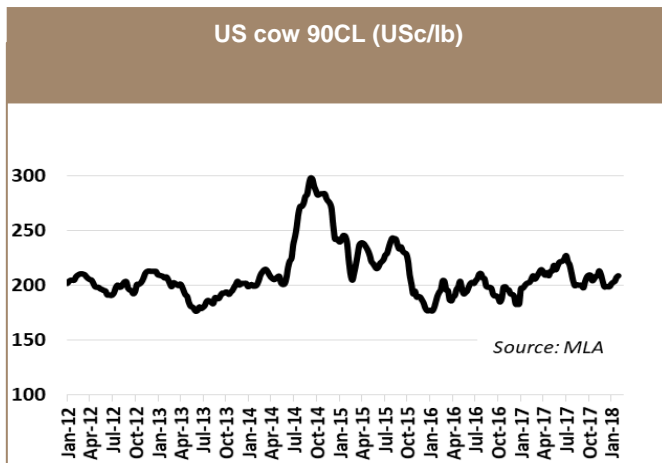
Japan and substantially expand its operations. According to modeling by the Australian Wagyu Association, the investment will boost production to 74,703t by 2022, representing an average increase in production of 21% per year. The NSW Government has invested an additional A\$3m in Stone Axe Pastoral.

### Saudi strikes lamb export deal with UK:

Saudi Arabia has lifted the ban on sheep meat from the UK. The agreement follows ongoing negotiations and inspections by industry representatives from both countries. The new agreement is reportedly worth over £25m over the next five years and exports of lamb could begin as early as next month. UK Agriculture, Horticulture Development Board market development director Phil Hadley said the agreement was a testament to the high regard and quality of UK lamb. At the same time, an agreement has just been made to progress lifting the BSE ban on UK beef exports to China. New Zealand exporters who usually target the Middle East can expect more competition from their UK counterparts. However, a Welsh sheep marketing executive acknowledged it would take work to establish the Welsh lamb brand in Saudi Arabia.

### Australian cattle prices expected to rise:

The Australian Eastern Young Cattle Indicator (EYCI) was down 15% in January compared to the same period last year and currently stands at A\$33.25c/kg. However, recent rains in Queensland may send prices higher. Managing director of Meat and Livestock Australia (MLA) Richard Norton said everything will turn around if there is significant rain through far north Queensland. Before the rains, producers were offloading livestock quickly with processors to push out kill dates. Market analysts Mecardo said while it might appear as though destocking in Queensland was underway, the annual average for female slaughter numbers as a proportion of total kill came in at 40.4% in 2017, compared to 46.5% during the herd liquidation in 2014.



## Feed and Arable News

### IGC downgrades global grain harvest:

The International Grains Council (IGC) cut its estimate for 2017/18 world grains production for the first time since July due to southern hemisphere corn setbacks. The IGC lowered its estimate by 6mt to 2.094bnt for the season. The downgrade of 56mt reflects poorer corn output prospects in Argentina, Brazil and South Africa. Dryness in Argentina and South Africa undermined corn output prospects, while weak prices and a delayed soybean harvest weakened expectations for Brazilian output. The IGC cut its stock forecast by 7mt to 610mt at the close of 2017/18.

### US wheat growers want to join TPP:

US export market development organisation US Wheat Associates (UWA) has increased pressure on President Trump's trade stance. Farmers believe it's just a matter of time before he joins the Trans Pacific Partnership. UWA president Vince Peterson said farmers wouldn't tolerate being left out of the trade deal – as doing so would have great impact on farmers' market access. Australia and Canada stand to gain a much bigger share of the Japanese market, which before NAFTA was the biggest importer of US wheat.