



Australian Dairy Outlook 2018 - *White shoots emerging*

December 2017

Following a number of uncertain years, white (green) shoots are emerging as the Australian dairy sector enters a period of recovery.

Investor sentiment is also shifting with institutional buyers now seeking to consolidate their market position with acquisitions and expansion across the sector including processing and farms operations.

Despite lower production volumes over the last 12 months, and a restructuring of the milk supply chain, total supermarket milk sales grew by 2.5% to 1,414 million litres, with Cheese sales up 2.9%, according to Dairy Australia. On the export front, value grew 3.4% to US\$1,958 million (AU\$2.5 million), despite lower volumes, indicating global markets continue to pay a premium for clean and green Australian products.

The major distraction for the sector has been around the uncertainty of Murray Goulburn. Although this appears to have been overcome with the recent announcement of a AU\$1.3bn cash offer by Canada's Saputo for the major processor. The structure of this deal includes assurances to the farmer through long-term supply agreements, as well as a 40c per kg milk price step up and bonus, if the offer is successful. This announcement has only increased competitive tension across the whole market with Fonterra and Parmalat Australia announcing an overhaul of its relationship with suppliers.

Saputo also have a view to increase Murray Goulburn's milk volume intake by 30% litres driven primarily by global demand for Australian milk products. Fonterra, who have acknowledged the challenging times experienced by dairy communities in Australia over the past year, also have ambitions to grow their milk supply by 50% to 3bn litres.

There has also been investment activity further up the value chain, with the sector seeing a shift in processing towards higher margin products, with a focus on cheese and nutritional powders for both domestic and international consumption.

Evidence of this investment is seen with Fonterra's AU\$140m cheese plant in Stanhope, Victoria, with capacity of 45,000 tonnes per annum, coming online this year. Fonterra has earmarked an additional AU\$100m for further investment in Australia including in Wynard, Tasmania, and Cobden, Victoria.

There have also been a number of greenfield investments with Midfield-Louis Dreyfus, and AU\$80 million joint venture partner Union Dairy Company, beginning operations at its new plant at Penola, South Australia. The primary focus for this plant is on exporting powdered product, with supply to be achieved by sourcing milk from across the south-east of South Australia and western Victoria.

In Western Australia, Brownes, the state's biggest producer of milk and cream and second-biggest producer of yoghurt, was recently sold to Shanghai Ground Food Tech. The deal will improve access to emerging overseas markets with the potential for new product development, including cheese, and will provide more certainty to Western Australian suppliers.

Throughout the last few years quality suppliers have adjusted well to uncertainty, with an increasing need for resilience in 2017 but sentiment across the market is absolutely improving into 2018.

Smith Agri International is proud to support the Australian Dairy Industry. We have developed our market knowledge over recent years in support of institutional grade dairy opportunities, combining in the release of two of Australia's very best dairy farms Balmoral Park Dairy Aggregation and Woodvale Dairy Farm.

We welcome your enquiry and entry into our Virtual Data Room which provides sound independent reports and analytics in support of very sound returns.



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