“Ferocious” slump in dairy prices rocks New Zealand economy

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A “ferocious” slump in global dairy prices, down by nearly half in the past year, is spearheading a rapid “cooling down” in the New Zealand economy, according to Westpac Bank economists. Along with an early levelling off in the Christchurch earthquake rebuild and falling business confidence, the bank expects annual economic growth to drop from 3.3 percent to below 2 percent “in short order.”

The economy will worsen markedly across the second half of this year and into 2016. According to Westpac’s Economic Overview report, official unemployment will rise from 5.9 to 6.5 percent, wage increases will remain low and the housing market will slow. New Zealand’s biggest company, the dairy exporter Fonterra, has been put on a negative “credit watch” by international rating agency Standard and Poor’s.

The forecast is an abrupt turnaround from just 12 months ago, when the National Party government and business elite were basking in a claim by another bank, HSBC, that New Zealand was the global “rock star” economy of 2014, with its growth set to outpace most other developed markets. In the March 2015 quarter, however, the economy grew a paltry 0.2 percent.

On August 7, dubbed “Black Friday” in media reports, Fonterra announced a savage cut in its payout to dairy farmers—down to $NZ3.85 ($US2.52) per kilogram for the coming season, from a forecast $5.70 just three months earlier. At its peak in 2014, the price was $8.75 per kilo. Dairy NZ’s latest analysis showed that an average farmer needs a return of at least $5.40 per kilo to break even. Dairy NZ CEO Tim Mackle said farmers would be covering business losses averaging $260,000 to $280,000, but for many it would be “a lot more than that.”

According to Westpac, export revenues will drop by more than $3.5 billion, about 1.5 percent of gross domestic product. Dairy products currently account for more than 20 percent of the country’s exports. The sharp reduction is part of what the ASB bank has called a “gargantuan” global downturn in commodity prices during July. The ANZ Commodity Price Index took its biggest-ever monthly dive in a “broad based fall across all commodity exports.” For a basket of key New Zealand exports, world commodity prices slumped more than 11 percent in the month, to the lowest levels in six years.

Fonterra’s announcement came just days after dairy prices fell for the tenth consecutive time on the Global Dairy Trade auction, the major point of sale for Fonterra’s milk products. As well as the price index falling by 9.3 percent from its previous level, New Zealand’s main exports of whole milk powder and skim milk fell by 10.3 percent and 14.4 percent respectively, to levels not seen since 2002. Milk powder prices have plummeted 51.4 percent at auction since March.

While New Zealand has been hit particularly hard by the downturn in China, and the US-led embargo on Russia, the sudden deterioration in the dairy industry is part of a wider global crisis. *New Zealand Herald* financial commentator Fran O’Sullivan noted on August 11 that “right around the world” dairy farmers and companies are “feeling the impact of the lengthy dairy commodities slump.” Firms are facing “liquidity issues,” even in dairy strongholds such as the Netherlands. The BBC reported last week on widespread protests by British farmers over the price they are paid for their milk.

The dairy downturn is contributing to tensions around the stalled Trans-Pacific Partnership (TPP) agreement. The New Zealand government, a fervent advocate of the TPP, has begun baulking at the deal in its current form, and is publicly seeking some credit for the recent breakdown in negotiations. According to the *Herald* last Saturday, Trade Minister Tim Groser claims he is now coming under “intense pressure” from other governments to cave in on New Zealand’s demands for better access for dairy exports to the major heavily protected markets of Japan, Canada and the United States.

By one estimate, two seasons below “break even” will push 10–20 percent of New Zealand farmers into bankruptcy. Fonterra has announced unprecedented support measures in the form of $430 million in interest-free loans for farmers facing ballooning indebtedness to the banks. Farmers will only have to pay back the loans when and if the farm gate price recovers to above $6 per kilo. Shareholder-farmers in the Fonterra dairy co-operative will also receive a higher than expected payout of 40–50 cents per share. However, these measures are woefully inadequate and will not stave off financial distress. With 10,000 farmers expected to access the loans scheme, each is likely to receive less than $45,000.

The leader of the main opposition Labour Party, Andrew Little, promptly used the crisis to revisit the party’s xenophobic campaign over “foreigners” buying up New Zealand land and housing stock. Speaking on TV One’s “Q&A” program on August 9, Little said another bad season for dairy farmers could cause “New Zealanders to lose some of the country’s best agricultural land to offshore buyers.” He said banks told him they would help farmers for “one tough season” but beyond that there were “uncertainties.” Labour is seeking to divert anger over the deepening social catastrophe by demanding a total ban on sales to foreign investors, singling out Chinese investors for special negative attention.

In a Fairfax Media report in April, analyst Peter Redward said dairy prices would continue to fall “simply because supply is greater than demand.” Melbourne-based analyst Craig Ferguson of Antipodean Capital Management similarly warned that world milk prices were likely to fall further and for longer than “many people think.”

The source of the problem, however, is not “overproduction” of foodstuffs but rather, as the WSWS has explained, the ongoing stagnation of the world capitalist economy and the development of global recessionary trends. The collapse of commodity prices, which includes industrial metals, is producing a swathe of job cuts internationally. The collapse has shattered the myth that China and other emerging markets would provide an ongoing bonanza, including for New Zealand’s primary exports.

Fonterra has declared that it will not cut production volumes. Company spokesman Miles Hurrell told Radio NZ on August 10 that Fonterra is determined to protect its position in global markets and will maintain its strategy of increasing supply from the current level of 22 billion litres of milk annually to 30 billion over the next decade.

The dairy crisis is extending beyond the farm gates. Already-depressed regional areas are expecting to be hit as farmers cut back on expenditure. Retailers in the dairy-producing province of Taranaki told Radio NZ that sales are down by 10–20 percent, affecting everything from farm machinery to household goods such as furniture, whiteware and electronics. According to the *Herald*, there has been a surge in mortgagee house sales as worsening economic conditions hit farming-reliant regions. Five of the country’s 14 regions recorded a jump in forced sales in the last 12 months led by the Waikato, Fonterra’s base of operations, with 117.

Major job cuts are underway. In July, Fonterra held secret meetings with staff to discuss a sweeping restructuring that will eliminate “hundreds” of jobs in the coming months. CEO Theo Spierings said virtually every department in the organisation would be affected. He declared: “To keep ahead of the game, we need to be more agile, reduce costs and generate value”—i.e., eke out more profits.