



Agribusiness Monthly

May 2017

New Zealand

RaboResearch Food & Agribusiness May 2017



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Commodity Outlook



Dairy

Drivers of farmer profitability to continue to point to a better season ahead in 2017/18.



Beef

While there is potential for some easing of cattle prices over the next month, Rabobank doesn't expect any major price movements in the short term.



Sheepmeat

Given the unseasonal early lift in schedule prices through March/April, Rabobank expects schedule prices to lift at a slower rate than is normally experienced through the winter months.



Wool

Producers retain bales as coarse crossbred prices come back to NZc 365/kg.



Wine

The 2017 harvest has created more than its fair share of challenges.



Horticulture

Major rainfall events have continued to challenge the sector, with more vegetable price hikes pending.



Fertiliser

Low demand and high supply are holding global fertiliser markets, while local retail prices remain stable.



FX

Rabobank expects the NZD/USD rate to slip to 0.67 over the next 12 months (another cent further than our expectations last month).



Oil

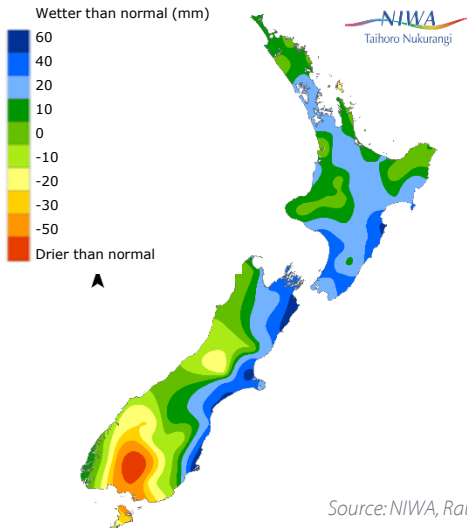
Crude oil outlook remains bullish at 60 USD /BBL Q1 2018, hinging on OPEC deal.

Climate



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Soil moisture anomaly (mm), 9 May 2017



NIWA expects there is a high chance temperatures will be at, or above, average for the north of both islands and the west of the North Island through until July 2017. The remainder of the country is likely to receive average temperatures across this period.

Rainfall for the three months to July 2017 looks most likely to be in the normal range for the top of the North Island and the east of the South Island. The remainder of the country has an equal chance of falling in either the below-normal or near-normal rainfall range across to July 2017.

Soil moisture levels have a mixed outlook from NIWA. The top of the North Island and the east of the South Island have a chance of above-normal soil moisture. The West Coast and the top of the South Island are at risk of below-normal soil moisture levels. The remainder of the country is likely to receive near-normal soil moisture levels through to July 2017.

What-to-watch

- International guidance suggests that **a transition from ENSO-neutral to El Niño conditions over the next three months is more likely than not (56%).**
- **There is a higher chance of El Niño conditions developing as we move through to October 2017, with the chance of an El Niño event rising to over 70%.**



Global Production Decline Is Easing

It has been a bumpy road to the tail of the New Zealand production season. Favourable conditions saw more milk than expected during the shoulder (+9% YOY for March 2017), only for April to bring excessive rainfall in parts of the North Island.

More important for global markets at this time of year is EU milk production, as it reaches its seasonal peak. While production is unlikely to reach the heights of May 2016, we expect the shortfall to be less than evident in recent months.

Overall, global dairy markets remain well balanced and prices continue to trade at elevated levels. **Rabobank expects global dairy prices to trade at or near these levels through much of 2017/18, which will help deliver a higher farm gate milk price for the new 2017/18 season.**

Fresh SMP volumes have begun trickling into intervention stores in Europe through the peak (less than 5,000 tonnes so far). The sizeable stockpile (380,000 tonnes) continues to plague SMP pricing. Inventories will need to be liquidated at some stage this year.

Favourable pasture conditions in many dairy areas will provide a good start to the new 2017/18 season. Healthy supplies of home-grown feed and fodder will be a major driver of positive margins for next season.

What to watch

- **Murray Goulburn's** decision to cancel the Milk Supplier Support Payment (MSSP), and commit to pay an average price of AUD 4.95/kg MS this season (partially funded with debt) is a positive for Australian suppliers in the short term. However, Fonterra is currently working through what this may mean for the coop, given that Fonterra is legally obliged to match or better the farmgate milk price by Murray Goulburn.

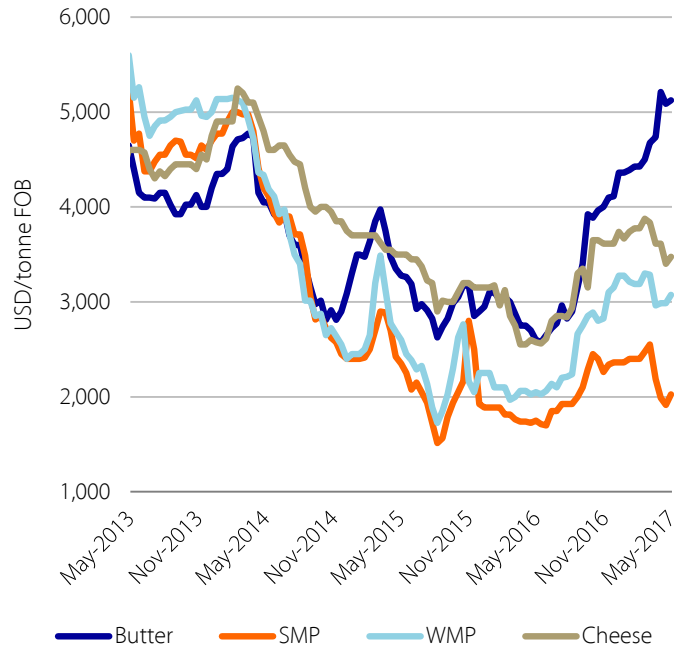
Dairy

Production Declines across the Export Engine Are Slowing



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Global dairy prices, 2013-2017



Source: USDA, Rabobank 2017

Production growth key exporting regions

	Latest month	Last three months
EU	-1.5% (February)	-2.0%
US	1.7% (March)	2.2%
Australia	-5.1% (March)	-6.9%
NZ	-2% (2016/17 season-to-date estimate)	

Source: Rabobank 2017



Beef

Prices Steady after Recent Rises

Cattle prices plateaued over the last month after consistent rises earlier in 2017. As of the start of May, the North Island bull price averaged NZD 5.55/kg cwt—2% lower MOM and 5% higher YOY. The South Island bull price averaged NZD 5.15/kg cwt—1% higher MOM and 8% higher YOY.

Cow slaughter prices have eased slightly as the seasonal increase in supply puts pressure on processors to get cows processed in a timely manner. Early in May, the North Island cow price averaged NZD 3.95/kg cwt, down 6% MOM, but still 13% higher YOY.

B+LNZ's mid-season update was released late April, and estimated that **New Zealand's export cattle slaughter for the 2016/17 season will be down 3.7%** compared with 2015/16, to 2.42m head. This drop is largely driven by a reduced cow kill, with improved milk prices ending the dairy herd retraction.

US imported beef prices continue to sit above both last year's pricing and the long-term (five-year) average, in part, because of the tight supply out of New Zealand and Australia.

While there is potential for some easing of cattle prices over the next month, **Rabobank doesn't expect any major price movements in the short term.**

What to watch

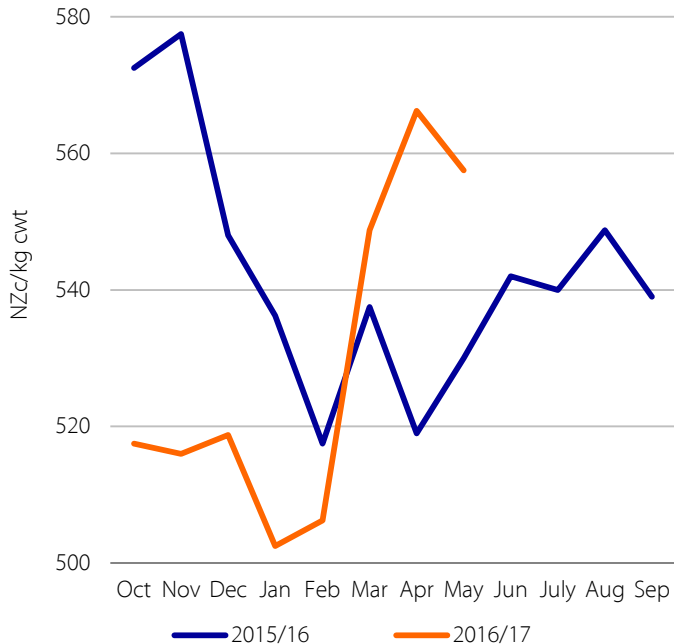
- **Approval for Chinese chilled meat trial plants.** The Ministry for Primary Industries (MPI) is currently awaiting approval from Chinese authorities for the ten meat processing plants that will export chilled meat to China on a six-month trial basis. The list of plants was submitted by MPI late April, and is reported to include two plants each from Silver Fern Farms, Alliance, ANZCO and AFFCO, as well one plant from Greenlea Premier Meats, and one from Ovation.

North Island Beef Price and NZ Cow Slaughter

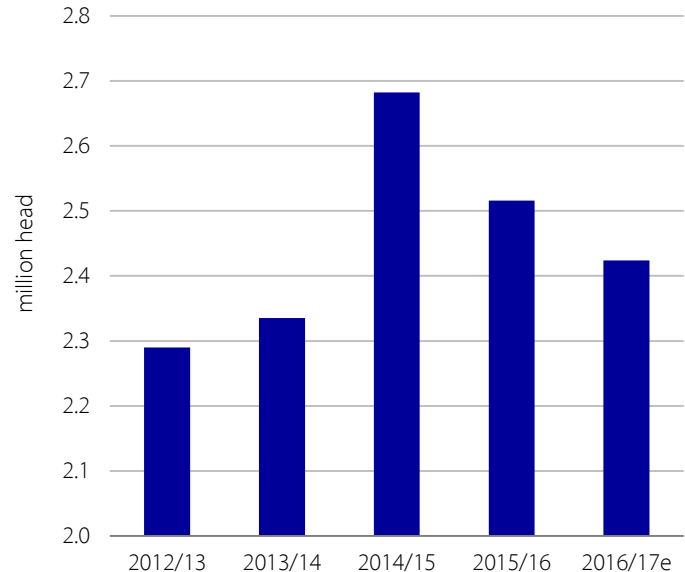


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North Island Bull Price



New Zealand Export Cattle Slaughter 2012/13 – 2016/17e



Source: NZX AgriHQ, Rabobank 2017

Source: B+LNZ Economic Service, Rabobank 2017



Short Supply Continues to Push Prices Higher

Lamb prices have been pushed up towards NZD 6/kg cwt on the back of near-record low lamb supply. As of early May, farmgate prices in the North Island (NZD 6.10/kg cwt) are up 6% MOM and 20% YOY, while South Island prices (NZD 5.90/kg cwt) are up 7% MOM and 24% YOY.

The 2016/17 season is on track to be the second-lowest export lamb slaughter on record. B+LNZ's recently released midseason update forecast export lamb slaughter to decrease 3.6% from the 2015/16 season to 19.2m head. Only the 2011/12 season lamb slaughter was lower (at 18.9m).

Tight lamb supply out of both New Zealand and Australia has meant **in-market prices have continued to rise over the last month.** For example, prices are well up YOY for both french racks (28%) and legs (36%).

The schedule **price for mutton is also well over 50% up YOY** due to strong overseas demand, particularly from China.

Given the unseasonal early lift in schedule prices through March/April, Rabobank expects schedule **prices to lift at a slower rate than is normally experienced** through the winter months.

Sheepmeat

What to watch

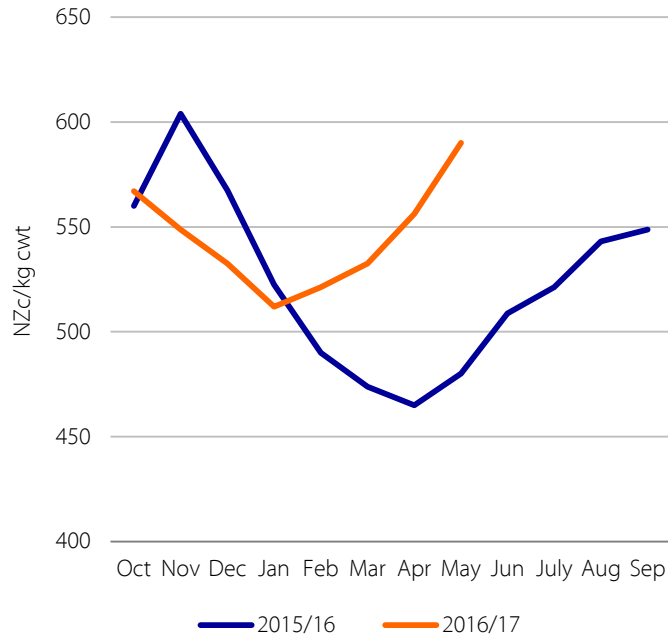
- **Remaining lamb kill for 2016/17 season.** We expect a higher-than-normal supply of lambs available for processing through winter due to early-season weather conditions. Any significant increase in supply may impact the winter schedule price paid.

South Island Lamb Price and New Zealand Lamb Slaughter

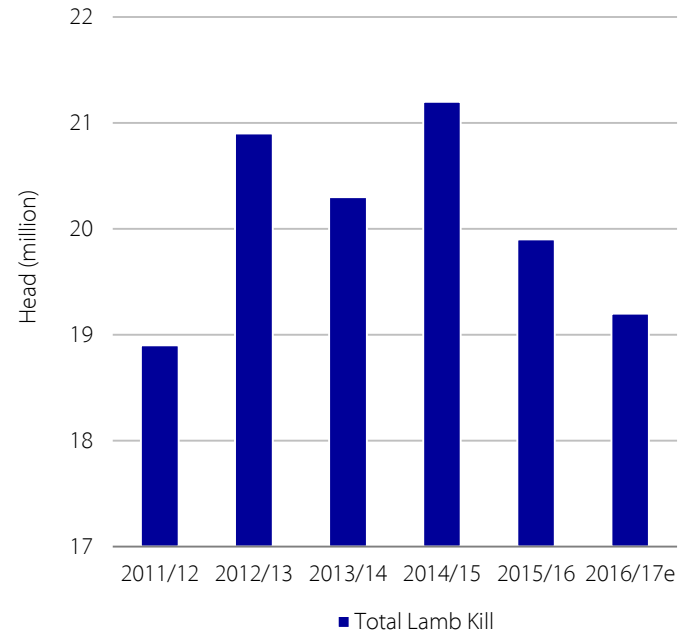


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South Island Lamb Price



New Zealand Lamb Slaughter 2011/12 – 2016/17e



Source: NZX AgriHQ, Rabobank 2017

Source: B+LNZ Economic Service, Rabobank 2017



Wool

Wool Piles up as Market Stays Weak

May prices have been unchanged, but low, in almost all categories of New Zealand wool.

The fine crossbred indicator has hovered at NZc 395/kg clean for the month. Coarse crossbred has come back from last month's high of NZc 375/kg to NZc 365/kg clean at the time of writing.

The low volume on offer is supporting a steady market, with 11% of bales withdrawn prior to sale in the most recent South Island auction. Many producers have held back bales awaiting some price relief. These stockpiles should slowly filter into the market as the production year draws to a close.

There was significant debate at the recent International Wool Textile Organisation Congress surrounding **the drivers of crossbred price declines**. The possible reasoning is either a cyclical downturn after a build-up of Chinese stocks, or alternatively a shift away from natural fibres in carpets, outerwear and Japanese tweed-type fabrics. Fortunately, if influenced by cyclical pressure, price should change direction in the coming months as Chinese stocks wind down.

The New Zealand dollar is providing little relief for wool producers, remaining relatively unchanged month-to-date.

The Australian wool industry is again at extreme highs this month. Booming demand for Merino wool is **widening the disparity globally between the fine and crossbred market sectors**.

What to watch

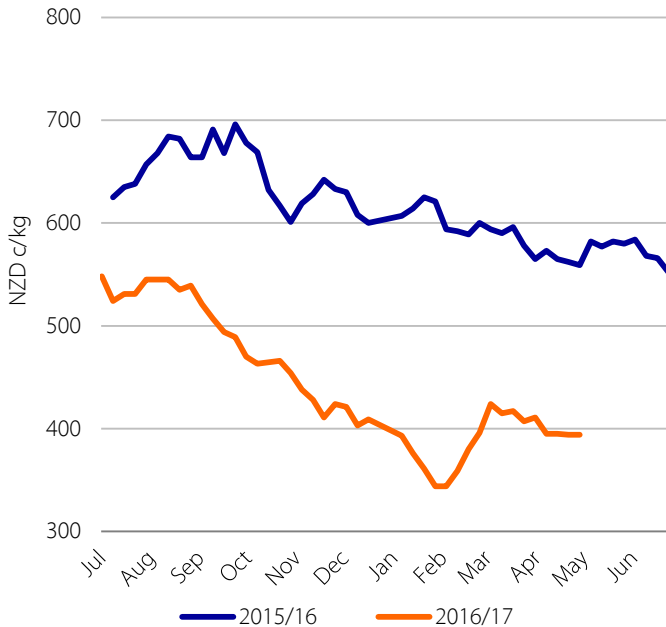
- **The production gap between apparel and interior textiles wool is forecast to widen to 2019.** New Zealand is the only broad wool producer not expected to increase production volume in 2017/18. Mongolia has the largest proportional growth, at 8% and 10% respectively in the next two years.

NZ Wool Unchanged, but Still Low

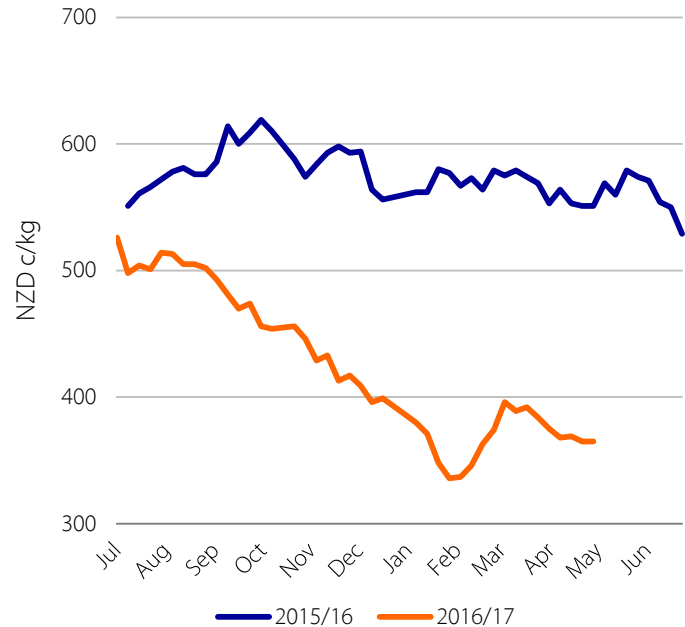


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Coarse Crossbred Indicator



Fine Crossbred Indicator



Source: NZ Wool Services, Rabobank 2017



One of Those Years

New Zealand's status as one of the world's coolest climate wine-growing countries has tested its mettle during the 2017 vintage as especially cool and wet conditions have prevailed. It's unusual years like this that viticulturists and winemakers earn their keep in doing what they can to preserve and promote wine quality.

At this early stage, it appears as though the crop has been affected in some part by disease pressure and the challenges in achieving full maturity in pockets. **The adverse weather impacts have been relatively widespread across the country's major wine-growing regions, but different sub-regions and varieties will naturally be impacted to varying degrees.** On top of other events, the remnants of Cyclone Debbie impacted the harvest at a delicate stage in Gisborne and Hawke's Bay, while the remnants of Cyclone Cook set back what was already a delayed and interrupted harvest in Marlborough. The true extent of the impacts will not be fully known for some weeks to come.

All the while, New Zealand wine exports charged ahead in March as wine companies rushed to empty tanks to make way for the upcoming harvest, at the time still largely unaware of what lay in store for the harvest. Bulk wine shipments jumped for the second consecutive month in March 2017, rising by 36% versus the same month last year, while packaged wines increased by 6% on the same basis. Export shipments in the year ending March 2017 are now 16% higher than last year.

What to watch

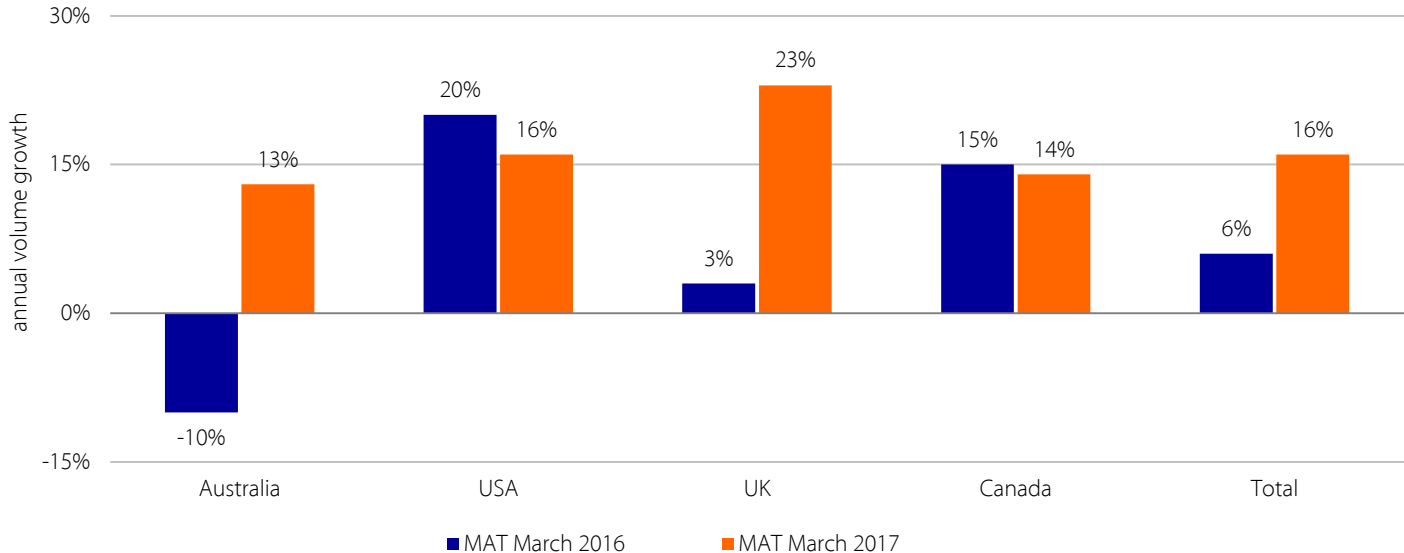
- **Bulk wine shipments.** Given the challenges with the current harvest, it will be interesting to see how wine company stocks and bulk wine exports normalise. It seems likely that the rush to export any surplus inventories may now be tempered as what remains may come in handy as blending stock to supplement 2017 vintage wines.

Wine

Wine Exports Surge Leading into Harvest



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Source: NZ Winegrowers, Rabobank 2017

As higher supplies from the record 2016 harvest came online, wine exports to markets such as Australia and the UK have rebounded strongly, while growth into North American markets has been uninterrupted.



Enough Already

Cyclone Cook crashed into the Bay of Plenty in April, inundating the already drenched region with more rain. Immediate damage to kiwifruit orchards in the Bay of Plenty was reportedly largely limited to isolated flooding, but the heavy rainfall has further delayed the harvest and is likely to compound impacts on average fruit size and dry matter this season.

To the relief of many, the concentrated storm cell avoided the area around Auckland, including important vegetable production regions such as Pukekohe. It did, however, track down the East Coast impacting other significant horticultural regions—most notably Hawke's Bay and Canterbury. The storm hit around halfway through the Hawke's Bay apple harvest, which naturally interrupted picking. The high winds also resulted in some crop loss.

Vegetable production has been heavily interrupted by inclement weather this season, as can be seen in the recently released consumer price inflation (CPI) data for Q1 2017. **Annual vegetable price inflation rose to 7.7% in the March 2017 quarter due to supply disruptions throughout the season.** The most recent storm will only add to this, with shortages in many leafy green vegetable crops being experienced in the wake of the storm.

Despite all the weather interruptions, New Zealand's horticultural exports are revving up as volumes make it to port. The value of New Zealand fruit exports lifted by 23.5% in March 2017 versus the same month last year to a March record of NZD 177.4m.

What to watch

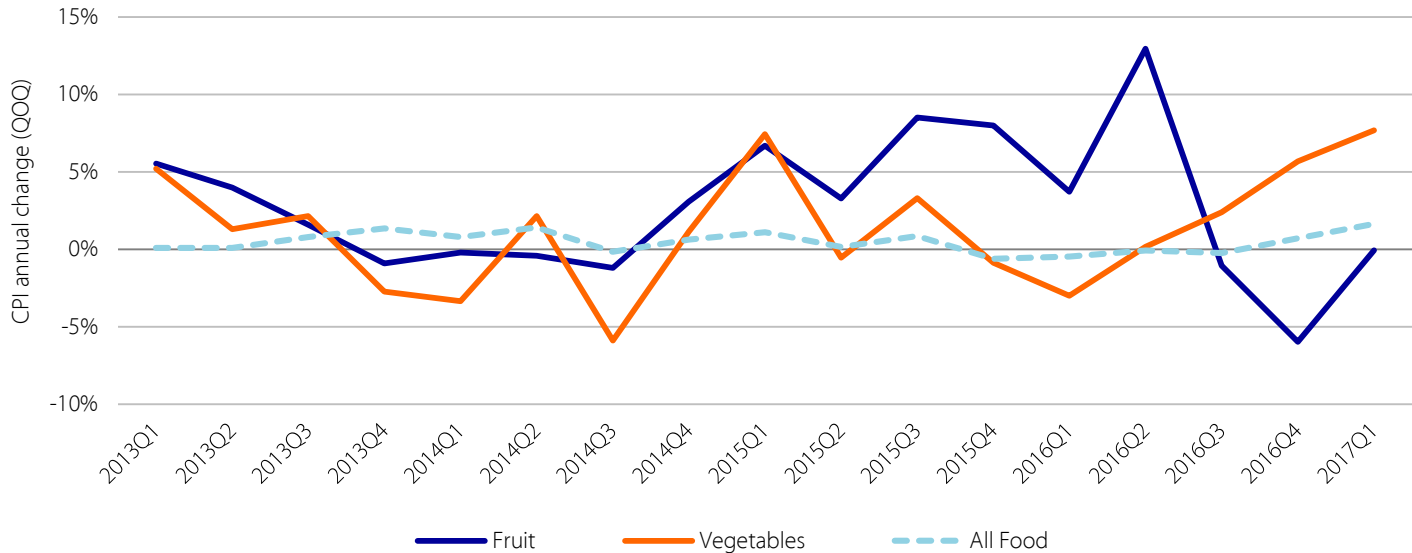
- **PSA disease pressures in kiwifruit orchards.** The relationship between wet orchard conditions—especially early in the growing season around the period of budburst and flowering—and increased risk of *pseudomonas syringae* pv *actinidiae* (PSA) disease pressure is relatively well established. Indeed, New Zealand kiwifruit growers are now much better informed and equipped to manage PSA disease pressure in their orchards. However, the especially wet finish to this growing season will again test their ability to keep this disease at bay.

Horticulture

Rising Vegetable Prices Lift Food Consumer Price Index (CPI)



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Source: Statistics NZ, Rabobank 2017

Vegetable price inflation in New Zealand is headed back towards levels last seen in 2011. Back then, the culprit wasn't supply disruptions, but rather the Goods and Services Tax (GST) rate hike.



Market Remains Low and Slow

Off the back of the March slump, **global urea prices showed little sign of rising**. Demand from major import regions remained lethargic, compounded by growing competition among exporters into the US and China markets.

Across the board, **demand is low in global phosphate markets**. Falling prices prompted some activity in India, although building exports and declining domestic demand in China kept downward pressure on prices. Supply of some New Zealand phosphates are at risk of being late due to controversy over mining rights in the Western Sahara. Although yet to effect price, suppliers are looking for disputes to end quickly. **Potash prices remain weak**, as new Chinese supply contracts are now not expected until June.

New Zealand urea imports were down 9% YOY for Q1 2017, with importers **shifting their demand away from Chinese markets towards Indonesia and Malaysia**. DAP imports more than doubled, while imports of rock phosphate fell 37%, signaling a shift away from processing in New Zealand.

Megamergers continue to shape the seed and crop protection industries. This week **Syngenta's shareholders approved the takeover by ChemChina** and the Dow-Dupont deal passed by the Chinese government. In the short- to medium-term, producers could expect a host of new innovative products as the industry consolidation continues.

Monsanto recently announced a **new investment in gene-editing**, considered a simpler and viable method of improving plant genetics.

What to watch

- **Movements in the NZ Dollar.** Currency remains a significant driver of retail pricing, so expect movement in fertiliser price from strength in the NZ dollar versus the US dollar.
- **Western Sahara phosphate issues.** Suppliers will be looking to put an end to issues to alleviate accessing what is already limited supply.

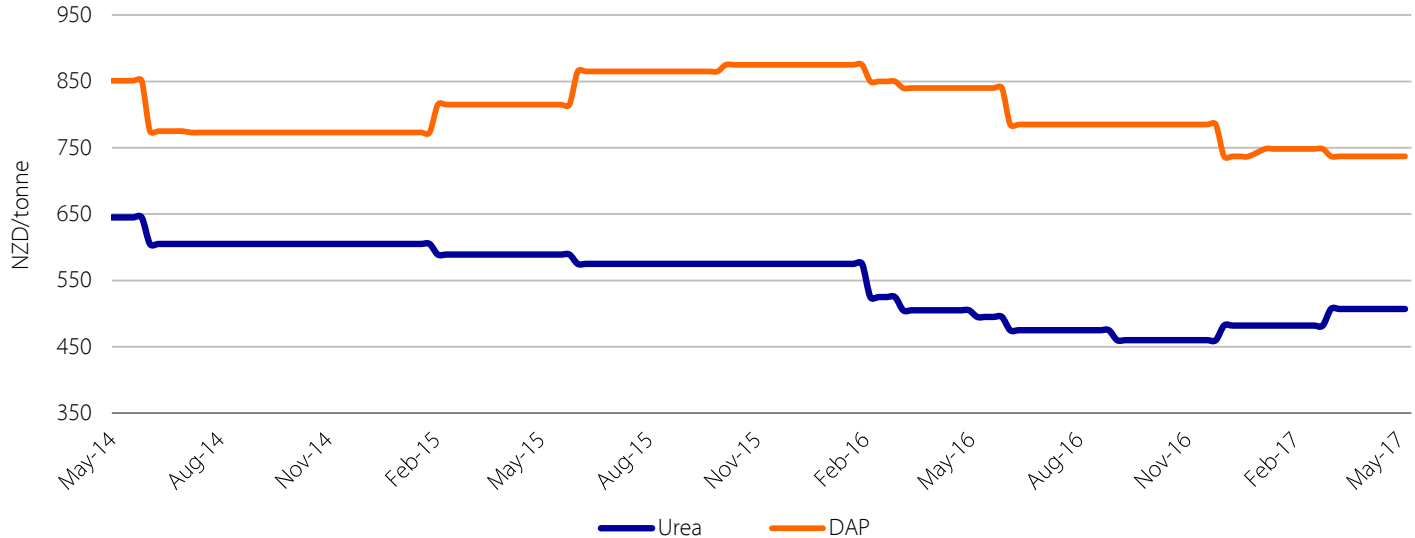
Farm Inputs

Retail Prices Remain Stable



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Reported retail fertilizer prices



Local retail prices remain stable, indicative of a global market suffering from over supply and stifled demand.



Outlook Hinging on OPEC

Peaking at 56 USc/BBL mid-April, the crude oil price moved downward to be **49 USc/BBL Mid-May, which is a fall of 12%. Markets are suffering from over supply**, with concerns rising that the commitment by OPEC members to cut supply haven't been deep enough.

OPEC's two largest producers, Russia and Saudi Arabia have signalled their desire to extend the agreement beyond late May, although no further supply cuts are expected. Contrary to efforts by OPEC, **production in Libya is at two-year highs** after a short interruption. US production continues to rise, although **US crude imports have not decreased meaningfully**.

Rabobank forecasts remain stable at 60 USD/BBL Q1 2018. A bullish outlook is substantiated primarily by **indications from OPEC to continue with supply cuts**, although the effectiveness of the deal is still being established.

In freight markets, **the Baltic Dry Index has fallen 22%** in the four weeks prior to May 9, to sit at 1,004 points. **Grain- and mineral-related movements have been quiet**, while competition between ships is growing.

Oil &
Freight

What to watch

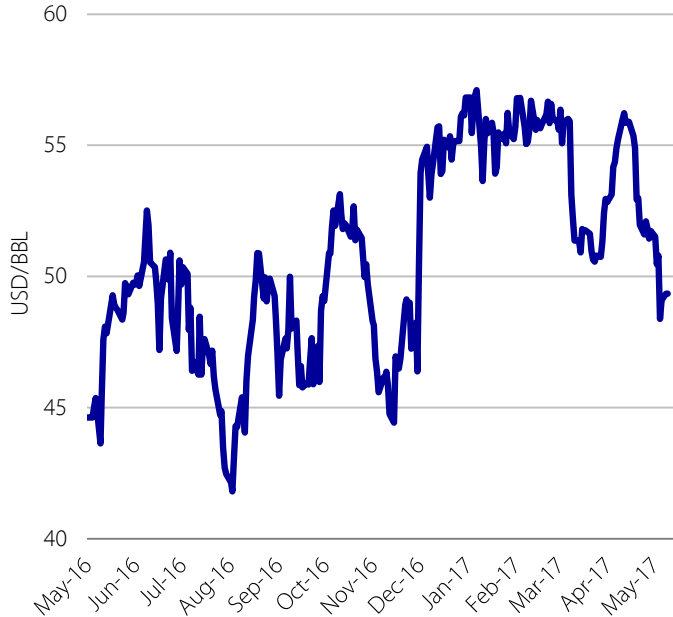
- **The OPEC deal.** Market dynamics largely hinge on the actions of OPEC and whether the deal will be extended beyond May 25.
- **Global Trade Indicators. A decreasing oil price**, the Baltic Dry Index and low commodity prices have led some commentators to conclude global trade growth was slowing. Watch this space as we move towards the end of Q2 and into Q3.

Oil at Pre-OPEC levels, Freight Stagnant



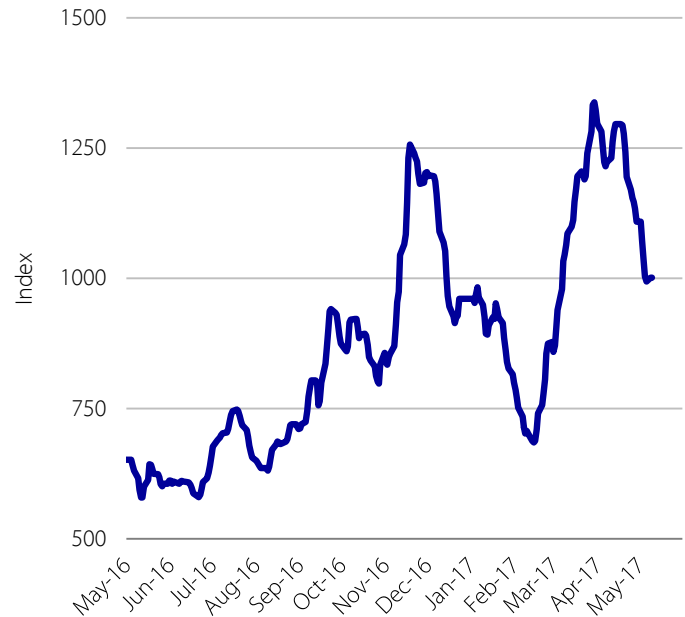
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Brent Crude oil price, May 2016- May 2017



Source: Bloomberg, Rabobank 2017

Baltic Dry Index, May 2016-May 2017



Source: Bloomberg, Rabobank 2017



Fundamentals Suggest a Weaker NZD

In line with Rabobank expectations, the NZD continued to lose value against the USD in the last month. We continue to believe it has further to fall.

The US Federal Reserve elected to leave US rates unchanged in its May meeting. While Q1 GDP growth was weak in the US, the committee viewed the Q1 GDP growth slowdown as likely to be transitory. It noted its expectation that “economic conditions will evolve in a manner that will warrant gradual increases in the federal funds rate”.

For now, **Rabobank expect this year’s second US rate hike in December** (notably later than many forecasters, who are looking for a June hike).

The Reserve Bank of New Zealand keeps its overnight cash rate unchanged at 1.75% in its May meeting. It considered that developments since February had been on balance-neutral for monetary policy including stronger growth in key trading partners, some uptick in commodity prices and a further easing of the Auckland housing market.

The NZD slipped marginally against the Greenback in the month to 9 May, falling just 0.4 cents to sit just above 0.69.

Rabobank expects the NZD/USD rate to slip to 0.67 over the next 12 months (another cent further than our expectations last month). We expect the US Fed to raise rates only once more in 2017, but believe that this will ultimately exert modest downward pressure on the NZD/USD rate.

What to watch

- **Progress (or lack thereof) of fiscal policy and tax reform in the US Congress.** We assume only limited achievements on both fronts. If reform is faster and more substantial than we assume, there is potential for the US economy to outperform in 2017, putting further downward pressure on the NZD/USD exchange rate.

FX

NZ Dollar Slips Marginally against the Greenback in the Month to 9 May



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NZ/US dollar cross rate



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