



Agribusiness Monthly June 2018

New Zealand

Food & Agribusiness Research and Advisory June 2018



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Commodity Outlook



Most processors have provided strong milk price signals for the 2018/19 season.



Rabobank expects the improved US beef price, and tightening supply of cattle, to hold schedule prices steady over the next month.



Rabobank expects the declining lamb supply to support continued upward price movements throughout June.



Extra volumes of wool still making their way to market continue to limit the upside potential for broad wool.



The announcement of formal negotiations for an EU FTA is a positive move for the sector in New Zealand.



Kiwifruit again dominated the NZ fruit and vegetable export results for the year ended June 2017.



We expect firmer global fertiliser demand on the back of higher crop prices.



Rabobank expects the NZD to fall to USc 67 by May 2019.



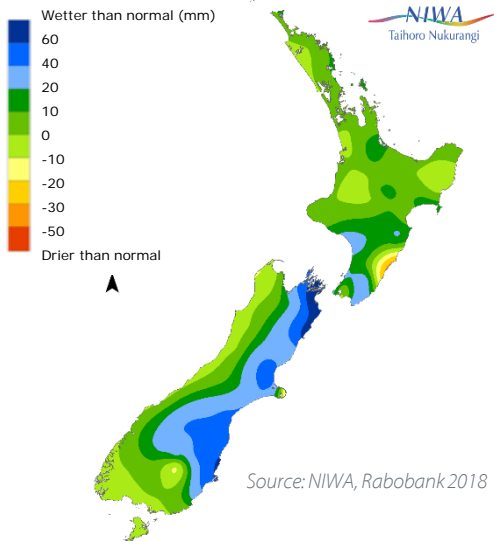
We lift our crude oil price forecast for the rest of 2018.

Climate



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Soil moisture anomaly (mm), 2 June 2018



NIWA are forecasting that temperatures will be average or above-average for the north and the west of the North Island through to August 2018. The east of the South Island is at risk of below-average temperatures, while the remainder of the country is likely to have average temperatures over the same period.

Rainfall totals from June through to August 2018 are equally likely (35% to 40% chance) to be near normal or above-normal for the east of both islands and the top of the North Island. The west of both island is likely to have normal or below-normal rainfall. For the north of the South Island there a likely chance that rainfall will be near normal.

NIWA is forecasting the top of the North Island is likely to have above-normal soil moisture levels. The east of the North Island and the north and west of the South Island are likely to have near-normal soil moisture levels, while the west of the North Island and the east of the South Island is likely to have normal or above-normal soil moisture levels.

What to watch

- **A winter of two halves:** In the first half of winter, the northern parts of the country may experience mild periods due to higher periodic north-easterly air flows. However, the second half of winter may bring colder temperatures in the south and west parts of the country due to westerly-quarter (NW to SW) winds.

Strong Pricing Signals for 2018/19

Weather around the country continued to improve in April 2018 and New Zealand milk production followed suit. National milk supply lifted 3% for April 2018 compared to the prior year. **Season-to-date milk production is tracking only slightly behind the prior season (-0.1% YOY).**

Although the final tallies are yet to be counted, the recovery in milk production over the last few months suggests New Zealand milk production for the 2017/18 season is likely to end up flat on last season. Total milk collections for 2017/18 year will likely end up around 21.4m tonnes of milk – the third-highest of New Zealand milk production level. Stronger milk flows for the second half of the season were supported by improved weather conditions, underpinning a solid finish to the season.

The opening milk prices for New Zealand milk processors have been announced and the **forecasts are pointing towards another profitable season.** Positive pricing signals from milk processors reflect the improved commodity markets over the beginning of 2018 and that markets will remain largely balanced over the coming season months.

Dairy

What to watch

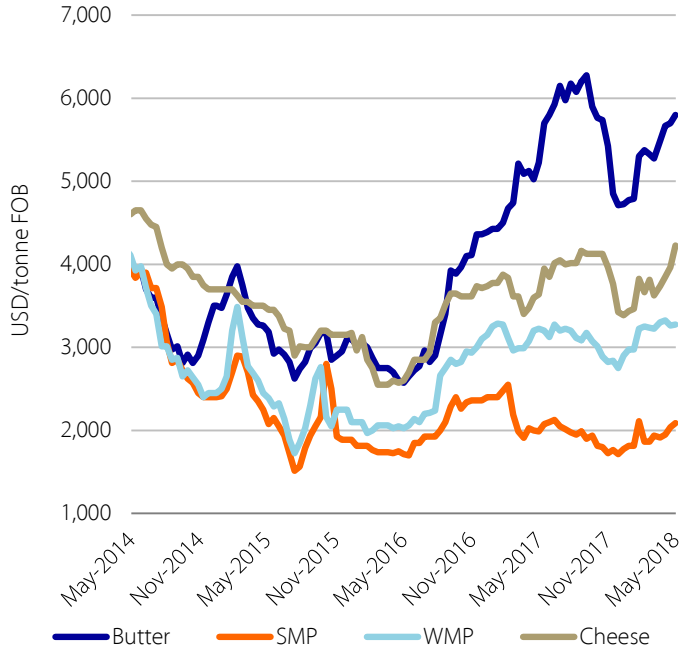
- **Mycoplasma bovis.** Under the current 'phased eradication plan', 126,000 cows are tagged to be culled, in addition to 23,000 already culled. While the estimated 150,000 cows tagged for slaughter are not enough to significantly impact on national milk production forecasts, further testing of the national herd for the bacterium will take place over the coming spring period. A significant lift in the number of infected properties (and therefore herds to be culled) would warrant production forecast revisions.

Strong NZ Output Despite Weather Challenges



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Dairy Commodity Export Prices



Source: USDA, Rabobank 2018

Production growth key exporting regions

	Latest month	Last three months
EU	0.4% (March)	2.3%
US	0.6% (April)	1.2%
Australia	4.5% (April)	3.5%
NZ	-0.1% (season-to-date at 30 April 2018)	

Source: Rabobank 2018



Beef

Prices Stabilise as Cow Kill Slows

After falling steadily during April, schedule prices held relatively steady through May, as the slide in US imported beef prices came to a halt, and domestic cow numbers began to tighten.

As at the start of June, the North Island bull price was 2% higher MOM, averaging NZD 5.25/kg cwt, with the South Island bull price down 1% MOM, averaging NZD 4.90/kg cwt. Prices in both islands are 5% lower than they were at this stage last season.

With US importers aware that supplies of New Zealand manufacturing beef will start to significantly slow down once the seasonal dairy cull ends in early June, the US imported beef price has lifted slightly from where it was late April. With the US entering summer, their domestic beef consumption will peak over the next month. **Rabobank expect this strong consumer demand to hold the US imported beef price around current levels throughout June.** However, further out there are still potential headwinds, with continuing dry conditions making some degree of forced liquidation of the US cow herd likely around August. Should this occur, the increased US domestic supply will reduce the their need for New Zealand's imported product.

As New Zealand production progressively shifts away from cows towards more prime cattle through June, demand in the key Asian markets will become increasingly important. **While Chinese demand is still holding firm, stiff competition in Korea and Japan continues to have a negative impact on prime cut exports into these two markets.**

Rabobank expects the improved US beef price, and tightening supply of cattle, to hold schedule prices steady over the next month.

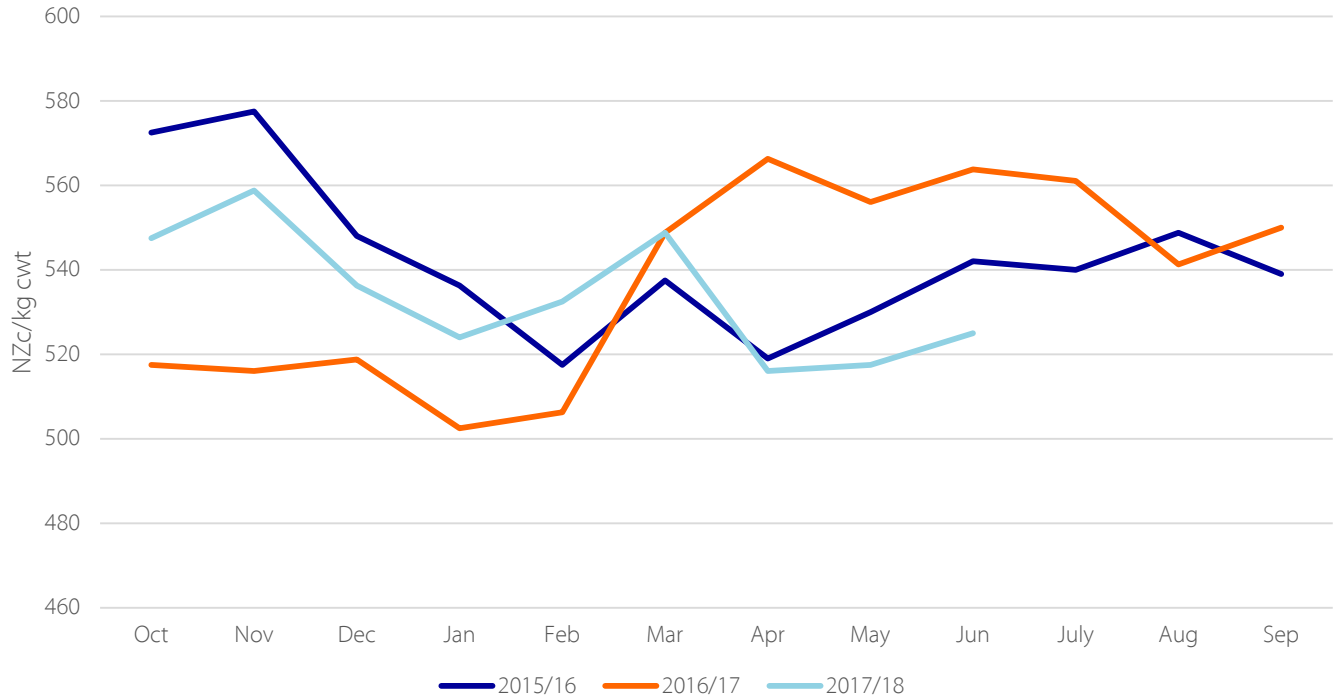
What to watch

- **Impact of Mycoplasma Bovis** – Given that the 126,000 cattle to be culled represents approximately only 5% of New Zealand's annual beef slaughter (2.4m cattle were slaughtered in 2016/17, plus 1.8m bobby veal), and the cull is occurring over a prolonged period of time (1-2 years), it is unlikely that the cull will have a significant impact on the beef schedule. However, this could change if the timing of when the bulk of the culling occurred (which is not yet clear) coincided with either a seasonal influx from the beef industry, or adverse weather conditions. The cull is likely to have some impact on killing space, and will at times prolong waiting times to get stock killed (particularly in the South Island).

North Island Bull Price



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Source: NZX AgriHQ, Rabobank 2018



Tightening Supply to Support Prices

Schedule prices continued to edge higher during May on the back of a seasonal slowdown in the number of lambs available for slaughter. As of the start of June, the slaughter price in the North Island averaged NZD 7.55/kg cwt (3% higher MOM), while South Island lamb averaged NZD 7.35/kg cwt (4% higher MOM).

With the peak of the seasonal kill now over, the supply of lambs will continue to tail off between now and season end in September. This should ensure there is enough **procurement pressure to support some further upward price movement, however, given the already elevated level of schedule prices, it is unlikely the extent of price gains will match those traditionally experienced over this period.**

While New Zealand's overall 2017/18 lamb kill is currently very similar to where it was this time last season (+0.8%), there is a clear split between kill numbers for the North Island (+8.6%) and South Island (-5.3%). With Rabobank expecting the total 2017/18 kill numbers to be approximately the same as last season, this would indicate there is higher proportion of lambs still to come forward in the South Island. **With processors in the South Island facing less procurement pressure, this could widening the gap between North and South Island schedules.**

Export market supply and demand fundamentals remain strong, and continue to support near record in-market prices.

Rabobank expects the declining lamb supply to support continued upward price movements throughout June.

What to watch

Dry conditions increasing Australian lamb kill – Dry conditions in key Australian sheep regions (particularly NSW and Victoria) have resulted in near-record kill numbers during March and April. While the correlating increase in exports has created more competition for New Zealand exports, the markets appear to be sufficiently absorbing the extra supply, with reports that global inventory levels remain low. In the short-term, this will disrupt Australia's recent flock rebuilding activity, but with prices and confidence still high among sheep farmers, rebuilding activity is expected to resume once weather conditions permit.

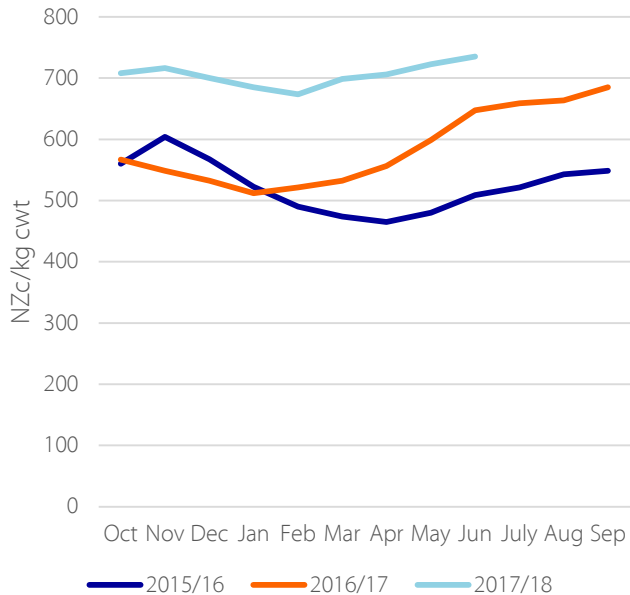
Sheepmeat

South Island lamb price and NZ lamb slaughter

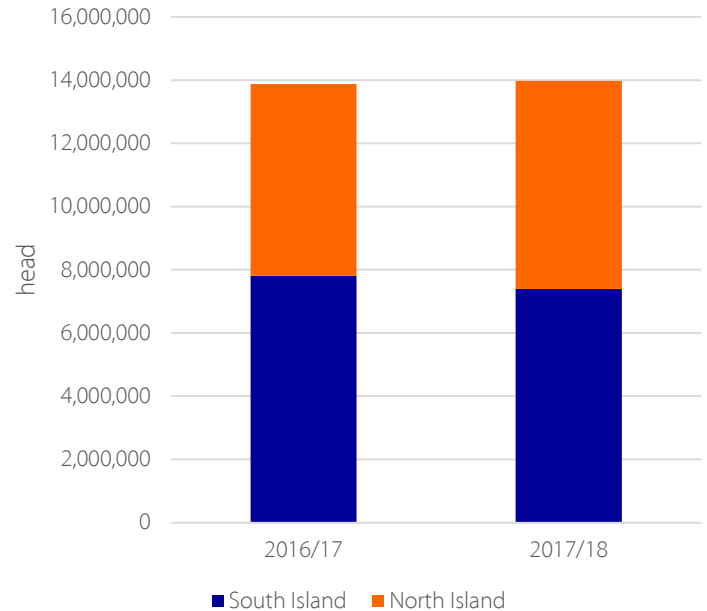


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South Island lamb price



New Zealand lamb slaughter (YTD – 28 April)



Source: NZX AgriHQ, Rabobank 2018

Source: NZ Meat Board, Rabobank 2018



Wool

Wool Market Holds Gains

The merino wool market has rewritten record books in Australia in May, with the Australian Eastern Market Indicator lifting four straight weeks to break through AUc 2,000 clean/kg in the last sale week for the month. All micron indicators below 25 hit lifted above AUD 2,000c/kg clean, and the 28 micron indicator based on some solid gains in 2018 is also in its 100th percentile since 2004.

Wool broader than 30 micron remains more subdued in comparison, reflected in the NZ wool market. However, coarse crossbred wool has also started to lift and managed to sustain these gains through the month. In May, the coarse crossbred indicator lifted 7% and clearance rates at auction averaged 93%. Crossbred lambswool prices, particularly finer than 30 micron, have seen some positive lifts in prices though the month of May in South Island sales.

There have been 25% more bales offered in the 2017/18 season to date, with the improved clearance rates seeing 40% more bales sold. The poor prices through 2016/17 saw stock accumulation on farm. While conditions for the broad wool market continue to improve, these extra volumes of wool, still making their way to market, continue to limit the upside potential for broad wool driving the divergence between markets above and below 30 micron.

China's import demand remains influential for all ends of the wool market, both broad and fine. The volume of wool from all origins imported in the 2017/18 season has risen by 28% on 2016/17, but positively, Uruguay and New Zealand have seen the largest YOY gains as volumes recover from the very poor 2016/17 season.

What to watch

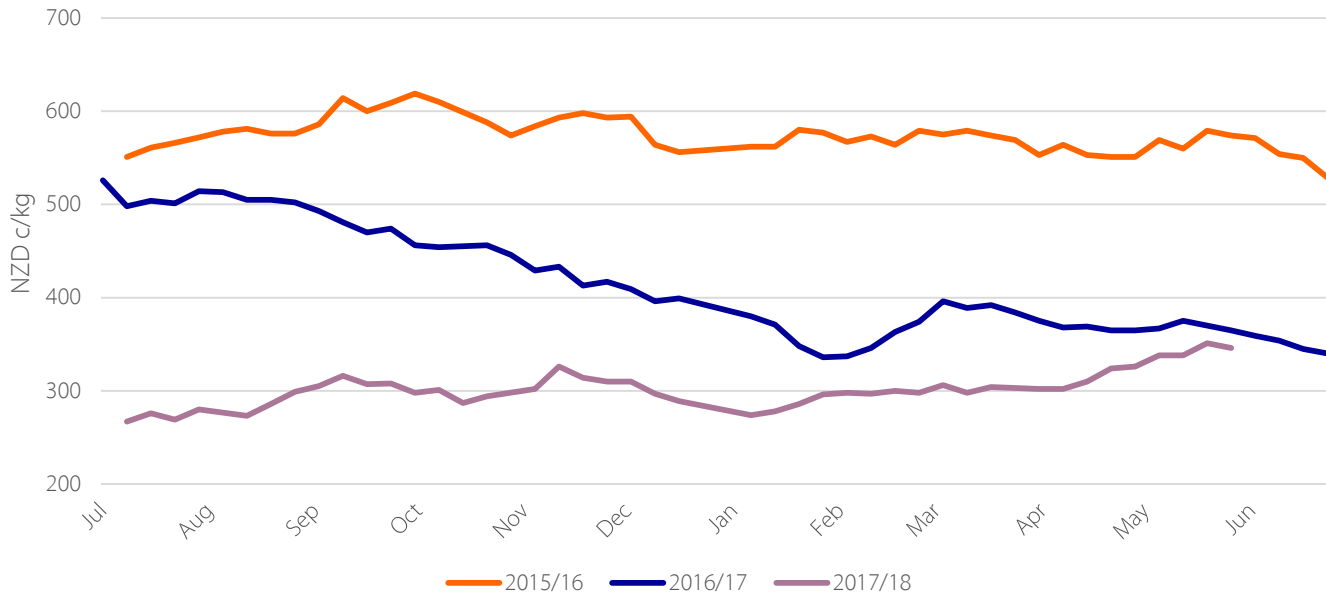
- Ongoing increases in Chinese imports of broader wool will be a good indication of improved demand and clearing of the volume of crossbred wool that had accumulated through the supply chain. This will be critical to realise further price gains in the 2018/19 season.

Finally Some Life In Coarse Wool Prices



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Coarse Crossbred Indicator





US Market Is Strong But UK Remains Important for New Zealand

While NZ produces less than 1% of the world's wine, it still punches above its weight on an export earnings basis. The UK is NZ's largest market by volume, and second largest by value behind the US. Sales of NZ wine to the UK increased YOY to April 2018 by 5% for volume and 4% for value to 8.4m case equivalents and NZD 393m respectively. The average value of these shipments was NZD 5.18/litre.

In our last Agribusiness Monthly, we looked at a comparison on volume and value of Australian wine to the US, showing higher total NZD export receipts on a lower volume. This month, we compare New Zealand's wine sales into the UK against Australian exports, which again **reflect New Zealand achieving a higher value per litre** (the NZD equivalent for Australian wine into the UK was NZD 1.71/litre) **on a lower total export volume vs Australia** (at 31% of total Australian exports to UK) for the 12 month period to the end of April 2018.

The announcement of formal negotiations for an EU FTA is a positive move for the sector in New Zealand. Exports of wine to the EU for the year ended 30 June 2017 were NZD 125m or 15m litres (6% of total export volume by litre, excl UK). The opportunity for tariff reductions is beneficial. An EU FTA would bring benefits for the wine sector, including potential for removal/lowering of tariffs such as EUR 32/100 litres of sparkling wine. How this evolves in tandem with EU negotiations with Australia, **will be tempered by how each country will then deal with UK negotiations post Brexit (given the importance of the UK to both NZ and Australia).**

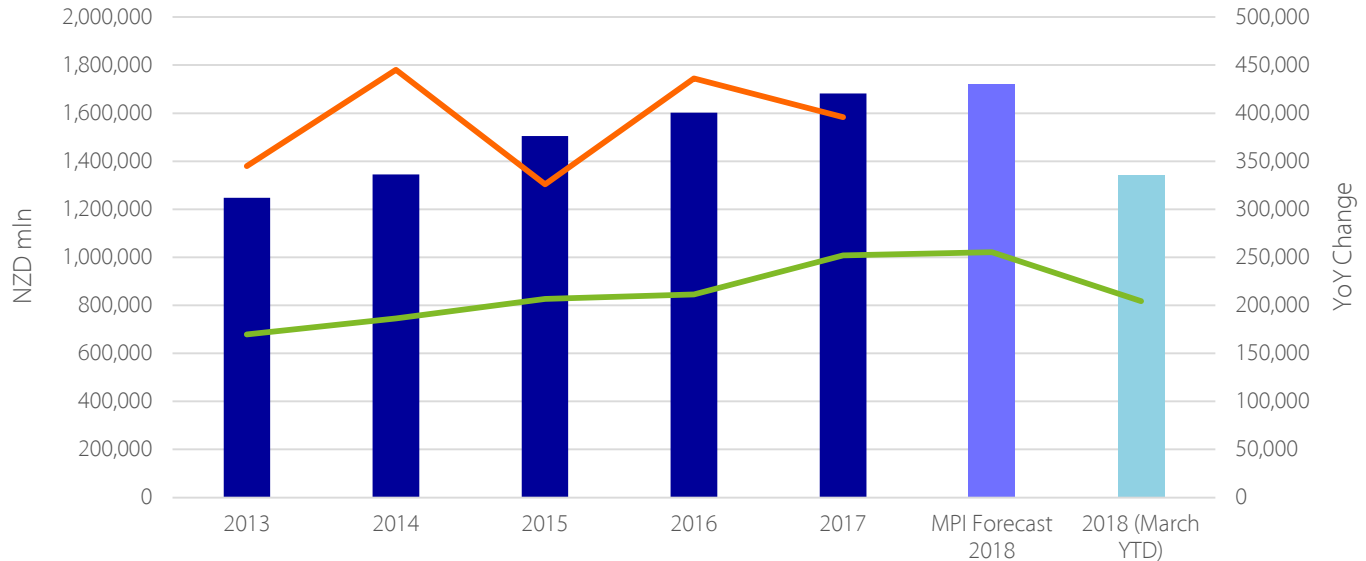
Wine

- **What to Watch – US marijuana legalisation and wine consumption** – Adult marijuana use is now legal in nine US states, with Canada also looking at legalisation. While industry analysts indicate beer is at the top of the cannabis 'hit-list', wine companies should be considering the impacts of legalisation as this is occurring in high wine consumption states and is competing in the relaxation and indulgence categories. Suppliers need to consider what success looks like in a new, marijuana-legalised world. For further information, read our recent report "[**Three Reasons Wine Could Be Hurt by Marijuana Legalization**](#)".

2018 New Zealand Export Sales On Track



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Volume and value YTD March 2018 are actual, with 2018 forecast value and volume an MPI Forecast as a base.

■ Exports (Value) Financial Year
 — Vintage Production (Tonnes RHS)
 — Export Volume (Thousand Litres RHS)

Source: NZ Winegrowers March 2018, MPI SOPI March 2018, Rabobank 2018

If sales volume and value to 30 June remain on their current trajectory of the 2018 YTD (March) numbers of 3% and 5% ahead YOY respectively, sales volumes and values are on track to meet the MPI 2018 Situation and Primary Outlook Forecast. 2018 Vintage (crush) yet to be confirmed.



Kiwifruit Dominates Exports, Labour the Big Issue

Kiwifruit again dominated the NZ Fruit & Vegetable export results for the year ended June 2017, at 46% of total F&V exports of NZD 3.6bn (excluding wine) according to the latest Fresh Facts data. Excluding wine exports, Japan remains New Zealand's highest value single F&V export market at NZD 591m (2016: NZD 583m), followed by Australia at NZD 515m (2016 NZD 453m), China at NZD 470m (2016: NZD 471m), Continental Europe at NZD 231m (2016: NZD 218m) and US/North America at NZD 208m (2016: NZD 225m). ***Collectively they represent NZD 2.1bn/56% of total F&V export receipts to 30 June 2017.***

As referenced in our April Agribusiness Monthly, ***labour constraints continue to ramp up and are a material issue for the horticulture sector.*** Following on from the shortage of people to harvest the apple crop in Hawkes Bay earlier in 2018, the Kiwifruit sector has felt the full impact of this due to a shortage of available labour right across its supply chain. ***The issue is only set to magnify with Zespri wanting to grow the New Zealand crop to greater than 180m trays by 2026.*** New Zealand is not alone here, as other countries grapple with this issue, as covered in our June Podcast on Labour Constraints.

The announcement of formal negotiations for an EU FTA is a positive move for the sector. Exports to continental Europe (excl UK) for year ended 30 June 2017 were NZD 778m (around 15% of total NZ horticultural exports for the period) led by kiwifruit, apples, and onions (at a total of NZD 634m). How this evolves in tandem with EU negotiations with Australia, ***will be tempered by how each country will then deal with UK negotiations post Brexit (with the UK buying NZD 151 m NZ F&V exports in 2017).***

What to watch

- ***Elite Soils and NPS on Versatile Land*** - the government's announcement of this NPS in response to the Our Land 2018 report highlighting the reduction in vegetable growing area by 30,000ha or 29% over the period 2002-16 is welcomed by the sector. A watching brief should be kept on how this NPS, or other bodies of work borne out of the Our Land report, focuses on the impact of Horticulture activities on soils, in particular phosphates and macroporosity.

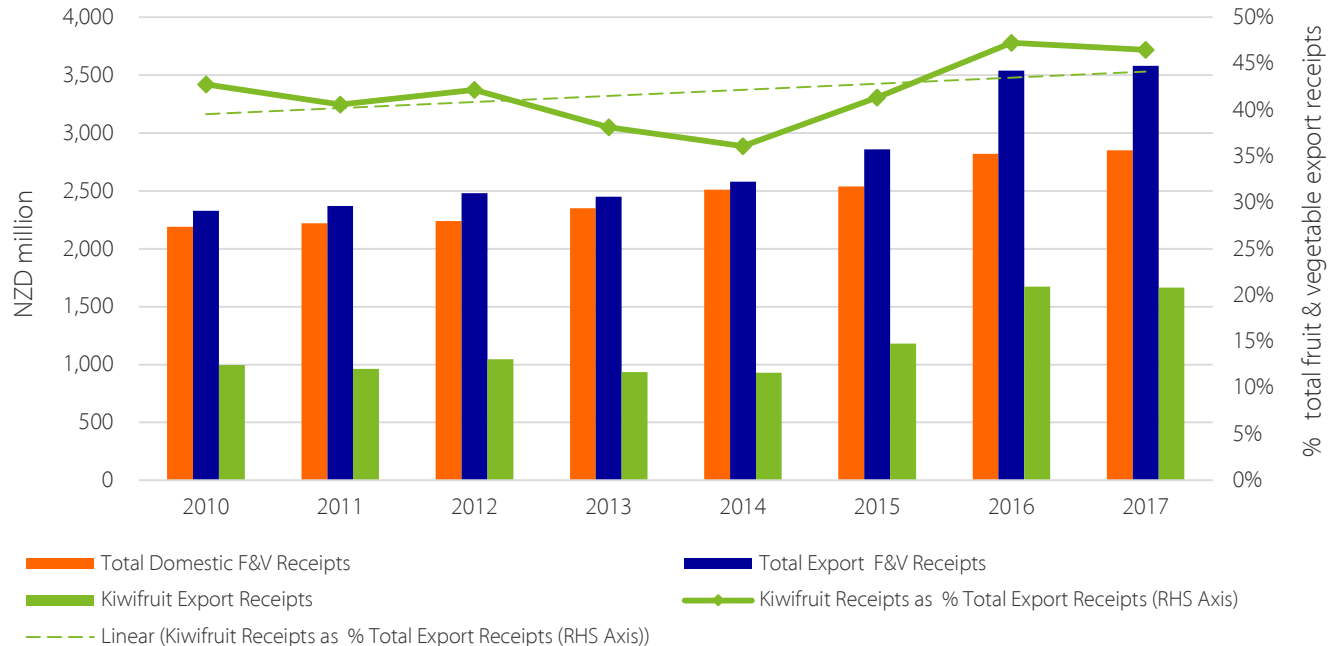
Horticulture

Domestic Sales Remain Strong, Exports Grow with Continued Key Influence of Kiwifruit



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Total NZ Domestic & Export Fruit & Veg Receipts (Excl Wine)



Source: FreshFacts 2017, Rabobank 2018

Global Markets Stable Through April

It was another relatively quiet month for global fertiliser markets. Global benchmark prices for the key nutrients were largely unchanged (in USD terms). On a year-on-year basis prices are stronger, **but compared to the five-year average prices were still subdued.**

There was good news for end-users with local reported retail prices for June showing a small drop in key nutrient prices.

Weather risks, USD strength, and geopolitical instability are driving volatility across the global grains and oilseeds complex. Dry conditions are emerging around the globe and have started to push global wheat prices higher. As a result, there are **signs of firmer fertiliser demand on the back of higher commodity prices and better crop economics.**

Global urea markets have so far remained largely stagnant. Phosphate fertiliser prices have remained relatively firm. Global phosphate markets are being supported by firm India demand, tight inventory levels, and rising raw material costs (phosphoric acid). However, new supply is ramping up in Saudi Arabia and Morocco, which will provide some relief.

Following speculation, the Indian government announce a 10% decrease in the nutrient-based subsidy (NBS) of MOP – the only nutrient to have a lower subsidy which may impact demand.



Fertiliser

What to watch

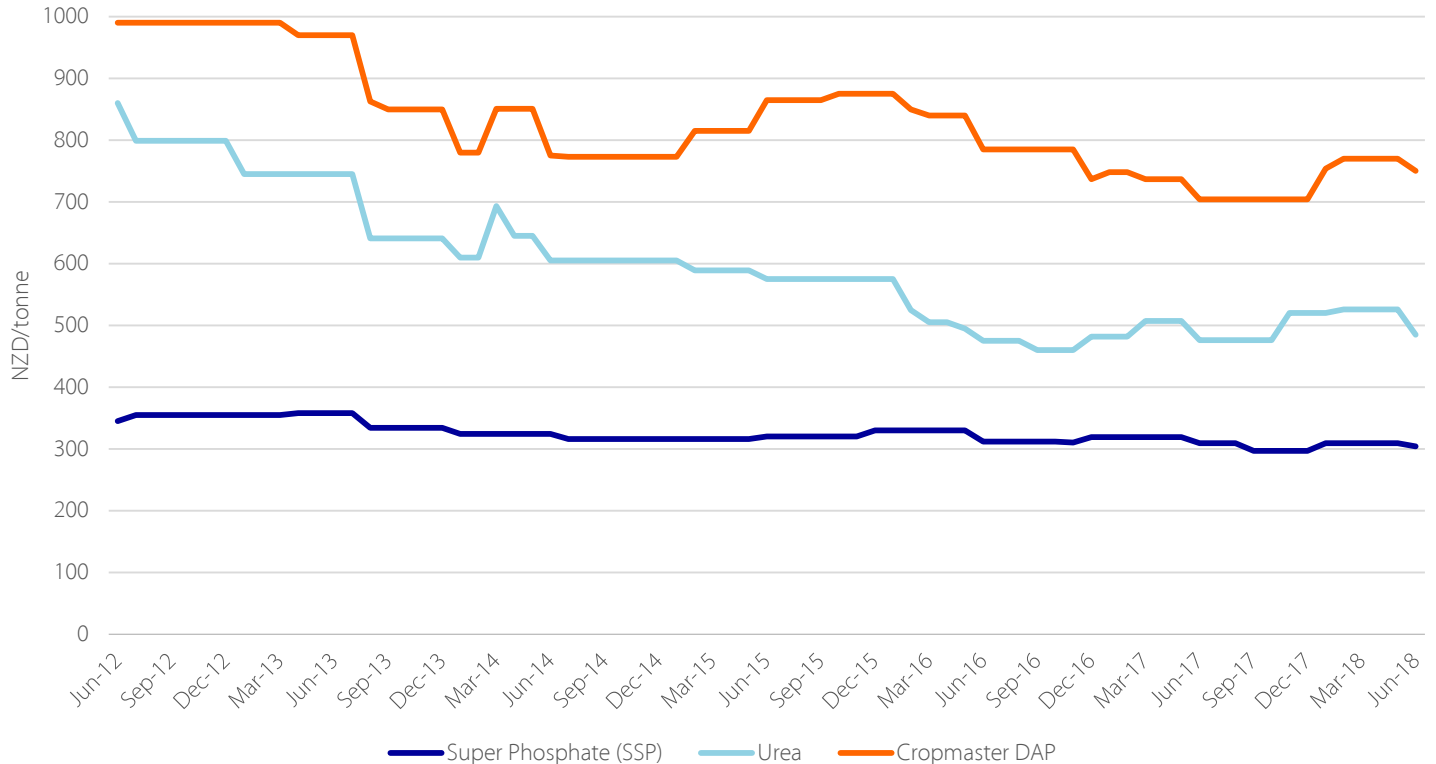
Dairy demand. There has been some very strong milk price forecasts announced for the 2018/19 season. Everything points to a season of healthy dairy farm profitability and supported fertiliser demand across the sector.

Global Stability Reflected in Local Prices



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Local reported prices





NZD Ends May Where it Started

Having continued its recent slide through the first half of May, the NZD recovered against the US dollar in subsequent weeks. By 4 June it was trading at USc 70 – more or less where it started May. The recovery appears to be driven at least in part from improved global risk sentiment, as tensions between the US and China eased somewhat.

In our view, the NZD is likely to trend weaker against the US dollar over the next 12 months.

The US Federal Reserve left its target range for the fed funds rate unchanged at 1.75% in May. But there are highly likely to be more rate hikes in the pipeline. The real question is how many? While US inflation hit the 2% mark targeted by the Fed Reserve in March, the Committee noted that “it was premature to conclude that inflation would remain at levels around 2 percent”, with some participants adding that “recent wage developments provided little evidence of general overheating in the labour market”, seeing “scope for a strong labour market to continue to draw individuals into the workforce.”

We expect the US Fed to increase rates twice in the next six months (in June and September): pushing the funds target rate from 1.75% at the end of May to 2.25%. We then expect rates to be on hold for six months at least thereafter. Core to our view is that there will be a lack of significant wage price pressure.

The case for any increase in central bank rates in NZ is far weaker.

With monetary policy set to tighten faster in the US than in New Zealand, ***Rabobank expects the NZ dollar to fall gradually against the USD over the coming 12 months – reaching USc 67 by May 2019.***

What to watch

- ***Trade tensions between the US and China.*** While US and Chinese officials are due to meet in early May to discuss trade, there is as yet little sign of either side backing down from recent threats. An escalation of tensions would likely exert further downward pressure on the NZD as capital flies to the safety of US financial markets.

FX

NZ Dollar Ends May Much Where it Started



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NZ/US dollar Cross Rate



Source: RBA, Rabobank 2018

Geopolitical Risks Loom Large

Brent Crude oil prices grew sharply in the first three weeks of May, however have since dropped to USD 76.79 /bbl. Geopolitical risks drove oil prices to USD 79.8/bbl during the month, the highest level since November 2014. This price increase was due to Donald Trump imposing sanctions on Iran, curbing its exports, thus reducing global supply. Furthermore, political and economic turmoil in Venezuela led to a plunge in output and contributed to supply fears in the oil market, contributing to the upward price trend.

In the last week, OPEC and Russia have signalled that they intend to increase production by 800,000 to 1m barrels per day to reduce supply fears. These nations will meet on 22 June to discuss production. Looking ahead, **our forecast average price for Brent Crude has been lifted from USD 68/bbl to USD 70/bbl for the remainder of 2018.** Despite this, the current geopolitical environment means that volatility is likely to continue rising and price action will continue to be driven by headlines on a day-to-day basis.

The Baltic Dry Index dropped 18% since the beginning of May. The Index rose to 1476 points in the first two weeks of May, however has since dropped to 1090 points. This is due to low demand for larger ships (Capesize) to cart high grade iron ore from Brazil to China.

Demand for iron ore in China has reduced significantly, due to large stockpiles. Furthermore, steel mills in some areas have been ordered to close for up to a month to meet air quality rules. This trend will lead to reduced demand for ships carrying iron ore from Australia and Brazil placing downward pressure on the Baltic Dry Index going forward.

What to watch

- **Supply Issues** – There is a chance that shrinking global oil supply and hawkish US foreign policy could push oil prices up to USD 100/bbl in the next 12 months.



Oil &
Freight

Crude Oil Reaches Three-and-a-Half Year High



Brent Crude Oil, May 2017 to May 2018



Source: AIP, Bloomberg, Rabobank 2018

Baltic Dry Index, May 2017 to May 2018

Rabobank



Source: Bloomberg, Rabobank 2018

Agri Price Dashboard

As of 31/5/2018	Unit	MOM	Current	Last month	Last year
Grains & oilseeds					
CBOT wheat	USc/bushel	▼	526	530	429
CBOT soybeans	USc/bushel	▼	1,019	1,043	912
CBOT corn	USc/bushel	▼	394	397	371
Australian ASX EC Wheat	AUD/tonne	▲	327	310	267
Australian Canola	AUD/tonne	▲	533	521	497
Beef markets					
Eastern Young Cattle Indicator	AUc/kg cwt	▼	467	502	655
Feeder Steer	AUc/kg lwt	▼	266	272	349
North Island Bull 300kg	NZc/kg cwt	▲	525	510	555
South Island Bull 300kg	NZc/kg cwt	▼	490	495	500
Sheepmeat markets					
Eastern States Trade Lamb Indicator	AUc/kg cwt	▼	595	597	671
North Island Lamb 17.5kg YX	NZc/kg cwt	▲	755	725	630
South Island Lamb 17.5kg YX	NZc/kg cwt	▲	735	710	615
Venison markets					
North Island Stag	NZc/kg cwt	▲	1,060	1,045	395
South Island Stag	NZc/kg cwt	▲	1,110	1,100	850
Dairy Markets					
Butter	USD/tonne FOB	▲	5,800	5,668	5,225
Skim Milk Powder	USD/tonne FOB	▲	2,088	1,950	1,987
Whole Milk Powder	USD/tonne FOB	▼	3,275	3,325	3,225
Cheddar	USD/tonne FOB	▲	4,225	3,850	3,637

Agri Price Dashboard

As of 31/5/2018	Unit	MOM	Current	Last month	Last year
Cotton markets					
Cotlook A Index	USc/lb	▲	100	93	87
ICE No.2 NY Futures (nearby contract)	USc/lb	▲	93.2	85.1	77.6
Sugar markets					
ICE Sugar No.11	USc/lb	▲	12.79	11.69	14.23
ICE Sugar No.11 (AUD)	AUD/tonne	▲	373	344	425
Wool markets					
Australian Eastern Market Indicator	AUc/kg	▲	2,027	1,846	1,472
NZ Coarse Crossbred Indicator	NZc/kg	▲	346	324	365
Fertiliser					
Urea	USD/tonne FOB	▼	240	252	210
DAP	USD/tonne FOB	▼	407	411	355
Other					
Baltic Dry Index	1000=1985	▼	1,090	1,327	850
Brent Crude Oil	USD/bbl	▲	78	73	51
Economics/currency					
AUD	vs. USD	▲	0.757	0.749	0.737
NZD	vs. USD	▼	0.700	0.701	0.706
RBA Official Cash Rate	%	•	1.50	1.50	1.50
NZRB Official Cash Rate	%	•	1.75	1.75	1.75

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