Agribusiness Monthly August 2019

New Zealand

RaboResearch Food & Agribusiness

1 August 2019

Rabobank

Commodity Outlook

Regulation	Farmers have the opportunity to comment on proposals to introduce a farm-level price on livestock emissions by 2025, including what actions should be taken between now and 2025.
Dairy	Rabobank expects weaker commodity prices in coming weeks as inventory builds.
Beef	Rabobank expects farmgate prices to firm slightly over the next month as domestic cattle supplies hit their seasonal low.
Sheepmeat	Rabobank expects farmgate prices to steadily climb between now and the end of the season, driven by strong market fundamentals both locally and globally.
Wine	Rabobank expects the United Kingdom to again feature prominently in New Zealand wine exports in 2019-20.
Horticulture	Rabobank expects ongoing competition growth in key export markets for fresh cherries and ongoing supply and demand changes in global fresh avocado export markets.
Fertiliser	We expect that global phosphate benchmarks will remain under pressure from low demand and over-supply until at least the end of Q3 2019.
FX	We maintain our forecast for the NZD to hit USc 63 by June 2020.
Oil	The fundamental outlook for Brent Crude is as bullish has it has been for quite some time. We forecast Brent Oil to reach 75 USD/bbl during Q3 2019.

Feedback Sought on Emissions Price

Farmers have the opportunity to comment on the government's proposal to introduce a farm-level price on livestock emissions by 2025, including what actions should be taken between now and 2025 in order to best transition to any potential farm-level pricing. On 16 July, the government released the 'Action on Agriculture Emissions' discussion document seeking public feedback on how it proposes to address greenhouse gas emissions from New Zealand's agricultural sectors.

To incentivise on-farm reductions it is proposed that, from 2025, farmers would have to pay for excess livestock emissions, or could earn credits if their emissions are negative (i.e. their carbon sinks (trees) and free allocation of units were greater than their emissions). The government is also proposing investigating options to recognise and reward carbon removals from vegetation that is not currently eligible under the Emissions Trading Scheme (ETS). In the interim, two options have been proposed for what is done between now and 2025 in order to have a farm-level emissions price in operation.

Option 1 is that emissions are priced through the ETS at the processor level (dairy, meat and fertiliser) by 2021. The government has committed to initially providing 95% free allocation of emissions if agriculture is included in the ETS. At a carbon credit price of NZD 25, that would translate to an average emissions price of NZD 0.01/kg milk solids, NZD 0.01/kg of beef and NZD 0.03/kg of sheep meat. The funds raised would be recycled back to support the actions required to prepare the sector for a farm-level emissions price.

Option 2 is for a formal sector-governmental agreement whereby industry groups would fund and implement a programme of action called 'Our Future in Our Hands' to support on-farm emission reductions, and progress towards implementation of farm-level pricing.

Blake Holgate
Analyst
Animal Protein and Sustainability
+64 3 955 4603
blake.holgate@rabobank.com

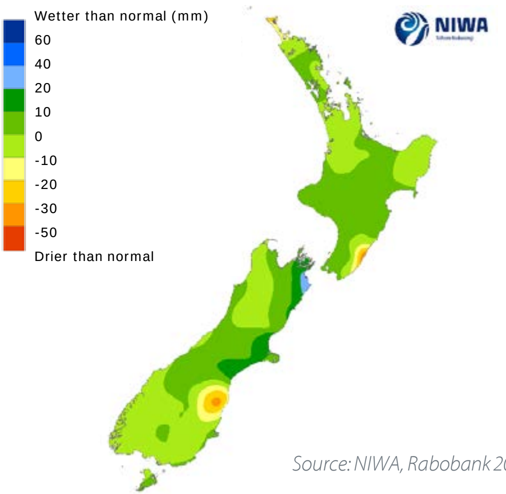
Regulation

What to watch

- ***Deadline for providing feedback –*** the public have until 13 August to provide feedback on the proposals included in the 'Action on Agriculture Emissions' discussion document. The government will then make its final decision on the proposed polices it will pursue via a Climate Change Response Bill, which it expects to introduce to Parliament late 2019. Information on how to provide feedback (including links to the relevant documents mentioned above) can be found at https://www.mfe.govt.nz/consultation/action-agricultural-emissions

Climate

Soil moisture anomaly (mm), 24 July 2019



Source: NIWA, Rabobank 2019

NIWA notes all New Zealand regions are forecast to experience either near-average or above-average temperatures through to September 2019.

Rainfall totals from July to September are equally likely to be normal or below-normal for north of both Islands and the east of the South Island. Other New Zealand regions are forecast to have near-normal rainfall levels over the same period.

NIWA is forecasting an equal chance of near-normal or below-normal soil moisture levels for the north of the South Island through to September. The top of the North Island is likely to have below-normal soil moisture levels. The remainder of the country is likely to have near-normal soil moisture levels through to September.

What to watch

- ***A mixed bag of weather through to September.*** With more frequent westerly winds forecast than usual, NIWA notes that "a trend towards more unsettled weather" is possible – particularly over the month of September 2019. Unsettled weather may follow patches of warm spells throughout July and August: a result of warm air flowing across the Tasman from Australia.

Back to the Future?

Low volume winter milk collections have been boosted by 14% YOY for June 2019, as weather patterns across the key milk-producing regions replicate last season's mild winter conditions. NIWA forecasts mostly favourable weather for the coming three months as calves make their appearance around the country: a crucial period for setting the production tone for the remainder of the season.

Broad-based improvement was evident across the dairy complex in July. All Oceania dairy commodity prices saw an uptick for the month of July, with the biggest price increase evident in SMP. The theme of tight milk supplies from major exporting regions is still very much at play and remains an underlying factor for price pressure.

Despite this, Rabobank believes that inventory is building in China and we anticipate some price weakness to eventuate over the coming weeks. The strength of Chinese purchasing has underpinned elevated Oceania commodity prices and extraordinary volumes shipped from New Zealand to China. Exports for the last four months have pipped peak volumes shipped to China back in 2013, when measured on a rolling 12-month basis. Some price recalibration is expected in light of full inventory pipelines and modest end-demand.

Emma Higgins
Analyst
Dairy

+64 3 961 2908
emma.higgins@rabobank.com

Dairy

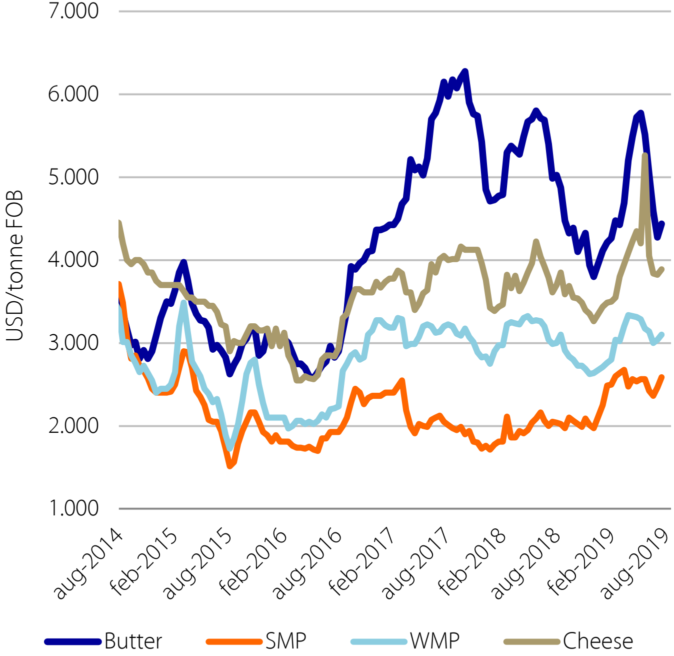
What to watch

- ***Increased milk supply competition at the farmgate for Canterbury -*** The sale of Westland Milk Products to Yili is now approved and on track for an ownership change on 1 August 2019. With a more attractive milk price on offer, combined with a UHT plant that historically operated below full capacity, competition for milk supply has the potential to ramp up on the Canterbury side of the Southern Alps.

Milk Supply Tap to Slowly Turn on in 2H 2019

Rabobank

Global dairy prices, 2014-2019

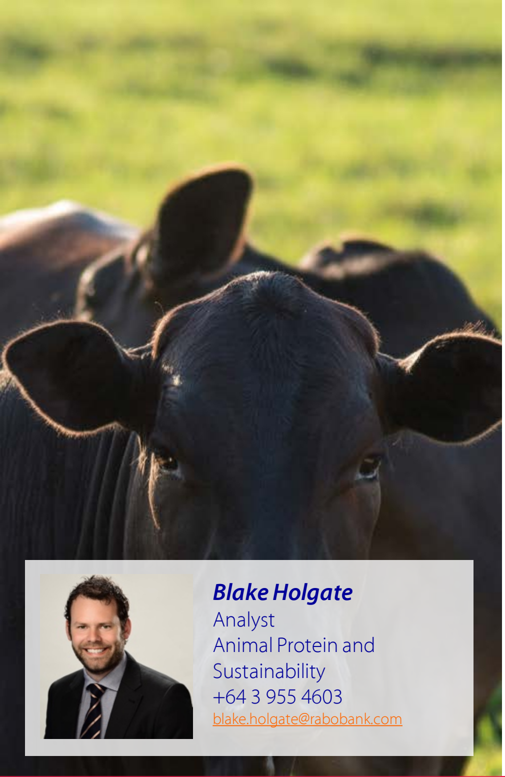


Source: USDA, Rabobank 2019

Production growth, key exporting regions

	Latest month	*Last three months*
EU	0.1% (May 19)	1.0%
US	-0.3% (Jun 19)	-0.17%
Australia	-13.6% (May 19)	-12.4%
NZ	2.2% (2018/19 season final)	

Source: Rabobank 2019



Prices to Firm as Supplies Slow

Rabobank expects farmgate prices to firm slightly over the next month, as domestic cattle supplies hit their seasonal low. Export returns remain solid as China continues to compete with the US for NZ product, supporting strong import prices for NZ beef from both markets.

Farmgate prices remained largely steady over the last month as processors began reducing killing capacity in an attempt to match the declining availability of cattle. As at the end of July, the North Island bull price is 2% higher MOM, averaging NZD 5.45/kg cwt, with the South Island bull price moving up 1% MOM to NZD 5.10/kg cwt. There was a notable drop off in supplies of prime cattle through July, well-below 2017/18 levels, which lead to some healthy price lifts for this class of cattle. Prime cattle prices in the South Island jumped 7% MOM, while North Island prices were up 4% MOM.

Chinese demand for NZ beef continues to outpace demand from the US. Of most significance to NZ is Chinese demand for manufacturing beef, a product that, traditionally, NZ has almost exclusively exported to the US. For the month of June, the total value of NZ beef exports to China went from NZD 78m in 2018 to NZD 183m in 2019. In contrast, exports to the US for the month of June fell from NZD 156m in 2018 to just NZD 91m in 2019. This competition has pushed US imported beef prices up 12%-14% YOY, as US importers struggle to source product for their summer, when beef consumption peaks.

NZ's overall cattle kill is sitting almost exactly where it was at this stage last year (+0.1% YOY as of 29 June). This is consistent with B+LNZ's forecast in their 'Mid-Season Update' that the 2018/19 cattle kill will only be marginally ahead (+0.7%) of last seasons kill.

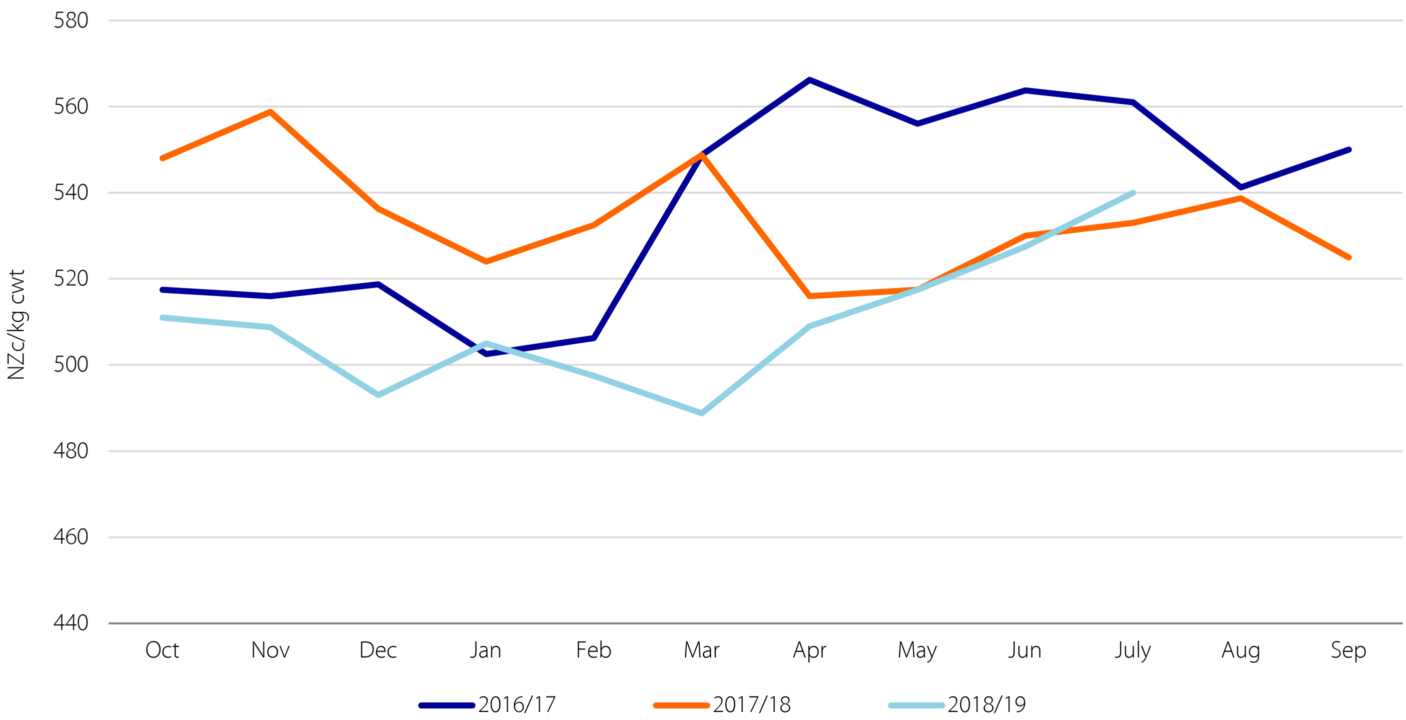
Blake Holgate
Analyst
Animal Protein and Sustainability
+64 3 955 4603
blake.holgate@rabobank.com

Beef

What to watch

- ***Introduction of M bovis levy –*** B+LNZ has approved a new biosecurity levy for Mycoplasma bovis response following consultation with farmers. With 59% of farmers who provided feedback supporting B+LNZ's proposals, the maximum rate for cattle under the new levy will be lifted from NZD 0.45/head to NZD 2/head. The initial levy rate will be set at NZD 1.80/head. The levy will be used to enable the beef sector to meet its 6% or NZD 17.4m share of the costs for the M bovis response. If approved by the Minister of Agriculture, B+LNZ expects the new levy to be in place by the end of the year.

North Island Bull Price



Source: NZX AgriHQ, Rabobank 2019

Highs of Last Year Within Sight

Rabobank expects farmgate prices to steadily climb between now and the end of the season, driven by strong market fundamentals, both locally and globally. Prices are on track to at least match last season's record highs with some upside potential.

Lamb supplies during June continued to fall behind last years kill numbers, increasing procurement pressure domestically while also contributing to scarcity on the global lamb market. As a result, prices in the North Island have broken the NZD 8/kg cwt mark, with South Island prices not far behind. As of the end of July, the slaughter price in the North Island averaged NZD 8.05/kg cwt (3% higher MOM), while South Island lamb averaged NZD 7.80/kg cwt (3% higher MOM). Prices are largely in line with pricing levels this stage last year.

Tight export supplies out of both NZ and Australia are severely limiting availability of lamb on the global export market, supporting strong export returns as international buyers compete over what product is available. Supplies from Australia have dropped off noticeably over recent months. Dry conditions forced many farmers to offload lambs earlier in the season than they would normally have. This has created a shortage of lambs available to kill between now and when Australia's new season lambs start to come online again in September. Consequently, farmgate prices in Australia have hit record levels, currently sitting above AUD 9/kg cwt.

China remains NZ's largest single-country export market, followed by the US, which continues to grow in importance for NZ exporters. NZ lamb exports for June totalled NZD 212m. China accounted for 34% of the month's export receipts, followed by the US (15%) and the UK (9%).

Blake Holgate
Analyst
Animal Protein and
Sustainability
+64 3 955 4603
blake.holgate@rabobank.com

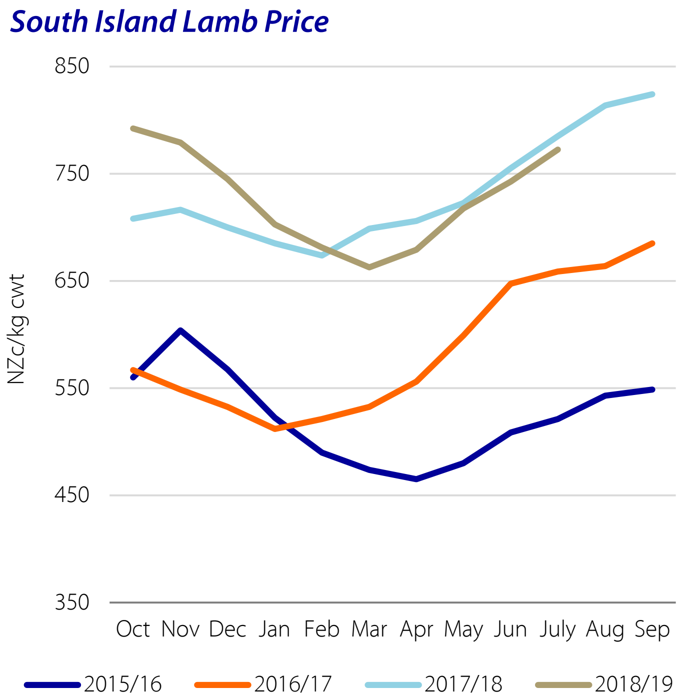
Sheepmeat

What to watch

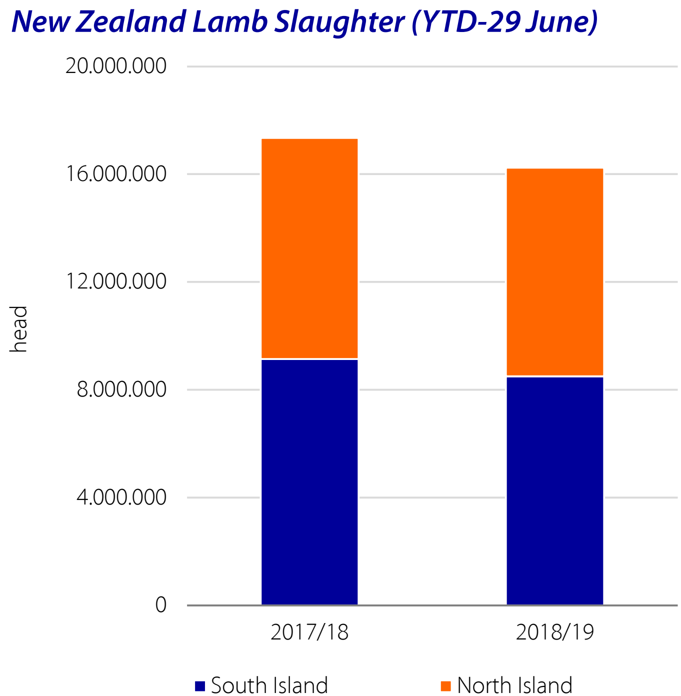
- ***Soaring mutton prices –*** the slaughter price for mutton in both islands has hit NZD 5.45/kg cwt. Prices have now surpassed last year's record highs, up 5% YOY and nearly 50% up on the five-year average. NZ's season-to-date mutton kill is down 16%, with many farmers opting to do a deeper-than-normal ewe cull last season to capitalise on the (then) record mutton prices. At the same time, demand from China for mutton continues to strengthen, as they look to import suitable proteins to replace lost domestic pork production as a result of African Swine Fever. These two factors have translated into very healthy mutton returns for NZ farmers.

South Island Lamb Price and NZ Lamb Slaughter

Rabobank



Source: NZX AgriHQ, Rabobank 2019



Source: NZ Meat Board, Rabobank 2019

Chinese Checkers or Chess?

New Zealand wine exports again pushed to new levels for the year end June 2019. Volume and value continued to rise overall, with strong United Kingdom exports driving the majority of revenue growth. Across the ditch, Australia continues to expand into China and takes the lead position from France for value.

Overall wine exports continued to rise in the year ended June 2019, with total volume increasing to all markets by around six percent and value by around 7 percent. This represents a good improvement on the previous year which was relatively flat compared to 2017.

The majority of the increase in export value was derived from exports to the United Kingdom, with an early rush of imports by the UK in the lead to up to the initial Brexit date. Q3 and Q4 2019 may again bring a similar profile for New Zealand's wine exporters in the lead up to the new Brexit date, especially with new Prime Minister Boris Johnson proposing to leave the EU with or without a deal. As we have noted previously, a no deal or hard Brexit will bring significant border disruption and economic implications for the UK. We will keep a watching brief on this over the coming months.

Australia continues to take advantage of a number of market dynamics to cement its position in the Chinese wine market. The rise in prominence of Australian wines in China continues, supported by Chinese wine drinkers continuing to follow the worldwide trend of premiumisation. Some of the success of Australian wines in favour of French wines in China can be partly attributed to Australia's FTA with China, which is a distinct advantage versus France. And secondly, the lower volumes of French wines in the market in 2018 from the poor 2017 vintage meant Australian wines have become even more price competitive in China. For further insights, check out the Rabobank Q3 Wine Quarterly.

Hayden Higgins
Senior Analyst
Horticulture & Wine

+64 6 974 9504
hayden.higgins@rabobank.com

Wine

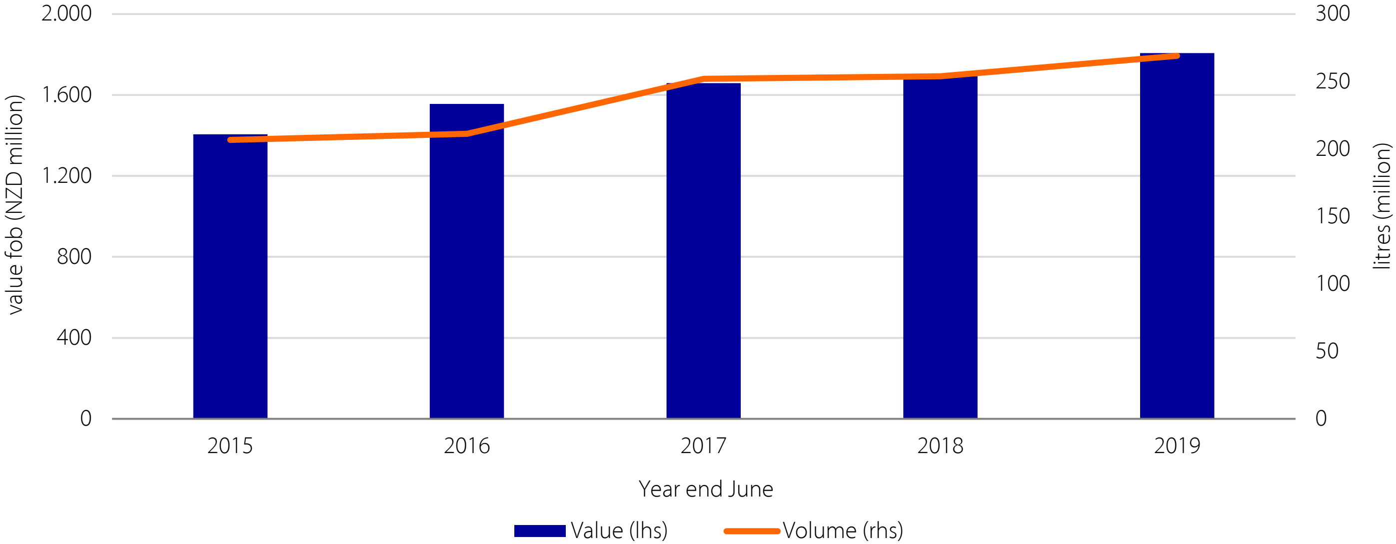
What to watch

- ***Sustainability characteristics a focus for the future consumer –*** Moving forward, sustainability should continue to be one of the focus points for brand owners looking for success in the US. The Wine Institute has recently highlighted results from a US survey showing 74% of respondents would consider buying sustainably-produced wine in the future with a particular focus on this topic from Millennials and Generation Z respondents.

Continued Moderate Value and Volume Growth

Rabobank

New Zealand Wine Exports



Source: Statistics NZ, Rabobank 2019

Total exports of New Zealand wine by both volume and value continued to rise YOY to 30 June 2019. The United Kingdom was the biggest driver of increased value.

It's All About Cycles

Both the cherry and avocado sectors domestically and internationally continue to undergo changes in supply amid an environment of rising demand. And, much like changes in strategy in the peloton combined with weather impacts on outcomes for the Tour de France, demand and supply cycles for horticultural products dictate outcomes and make forecasting a winner all the more complex.

The 2019 New Zealand cherry export season finished on a high note for New Zealand's exporters on a per kg fob value basis, but this was achieved on the back of a lower supply volume due to the smaller New Zealand crop. Resultantly, exports were down by around a third but continued rising demand in key markets supported prices. Across the Tasman, Australian fresh cherry exports achieved volume increases off the back of a good season and this was also reflected in strong pricing in fob export values. ***Australia continues to open up markets in Asia for cherries from the mainland, however, New Zealand retains a tariff advantage in key market Taiwan versus both Australia and Chile currently.***

What a difference a year can make – not only to the peloton, but to the European avocado market. Fresh avocado prices are spiking in Europe currently, due to a reduced volume coming from key South American suppliers. This is in stark contrast to 12 months ago when supply growth was exceeding demand, and prices decreased during the European summer (refer Rabobank' s Industry Note Last Summer's EU Avocado Price Dip Was Not a One-Off). ***This supply imbalance highlights seasonal dynamics at play,*** with US and Mexican production shortages in 2019 encouraging a shift of export focus from key South American countries to the US versus Europe. European avocado imports from both Chile and Peru are down by around a quarter, and by around a third from Mexico, to the end of May.

Hayden Higgins
Senior Analyst
Horticulture & Wine

+64 6 974 9504
hayden.higgins@rabobank.com

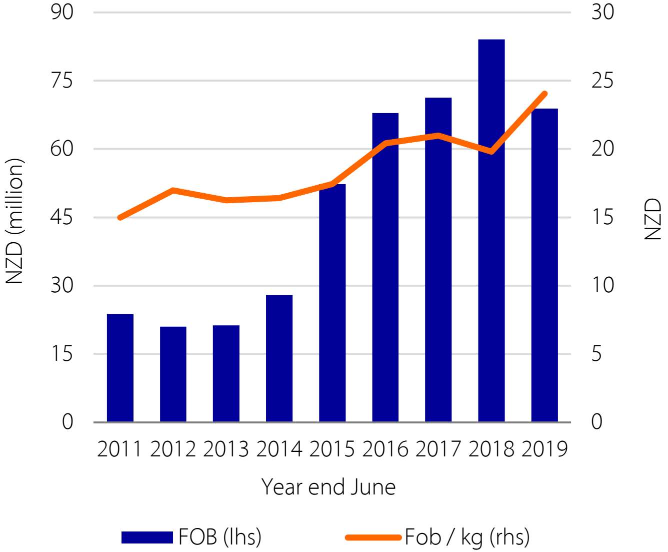
Horticulture

What to watch

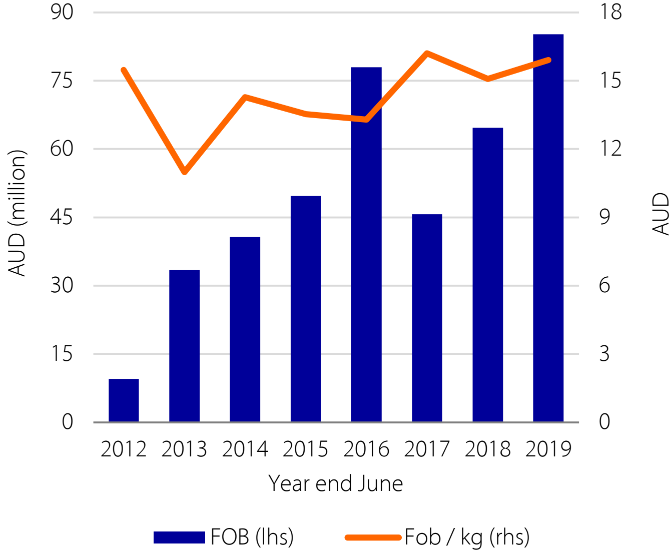
- ***Rise in Chilean fresh cherries in key export markets***– ongoing investment in productive assets over recent years, reportedly of around 12,000ha since 2015, will see significant increases in export volumes over the next four to five years from Chile. This is likely to coincide with further production increases out of New Zealand with ongoing industry expansion here.

Different Cherry Export Value Drivers In 2018/19

New Zealand Fresh Cherry Exports

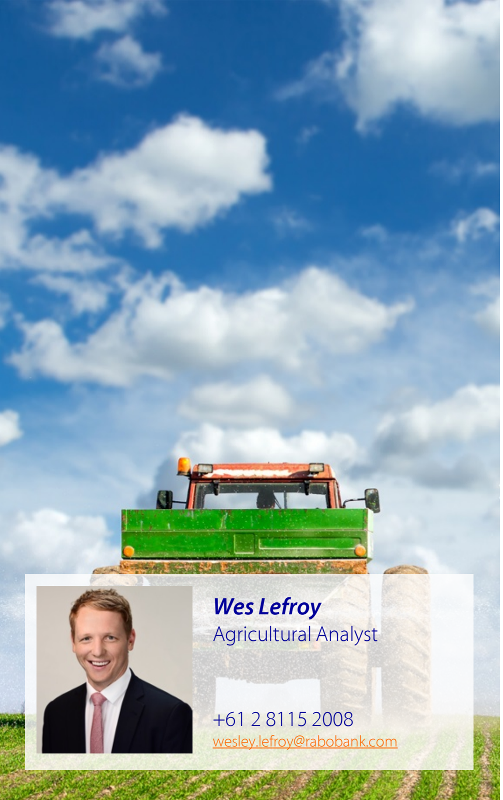


Australian Fresh Cherry Exports



Source: Infoshare, Trade Map, Rabobank 2019

Supported by rising demand, Australian fresh cherry fob export values per kg rose YOY alongside increased export volumes. The same demand signals also supported a rise in New Zealand fob value per kg against a backdrop of decreased export volumes related to weather impacts on the 2018/19 crop.



Wes Lefroy
Agricultural Analyst

+61 2 8115 2008
wesley.lefroy@rabobank.com

Farm Inputs

Global Phosphate Downside to Continue

We expect that global phosphate benchmarks will remain under pressure from low demand and over-supply until at least the end of Q3 2019.

Prices have fallen every month since DAP ex-US Gulf reached USD 439/tonne FOB in October 2018. As of late July, DAP ex-US Gulf was USD 340/tonne FOB. The fall in global prices was assisted in local terms by a slightly stronger currency over the period. The price decrease represents a 23 percent decrease in NZD terms.

Looking ahead, we expect global phosphate benchmarks to continue to slide toward the end of Q3 2019. We expect demand to remain stagnant, with the main demand season now over in Europe, the US and China. A group of DAP producers in China has announced a plan to cut 30%-40% of output during the third quarter, in response to over-supplied markets.

A period of stability may be about to end in the global urea market. The latest tender from India for 1.7m tonnes exceeded the previous tender by more than 1m tonnes. Given the significant size of this tender, this may keep India out of the market until early 2020. In this instance, we expect some downside for urea prices, even with extra demand expected from the Americas and Europe.

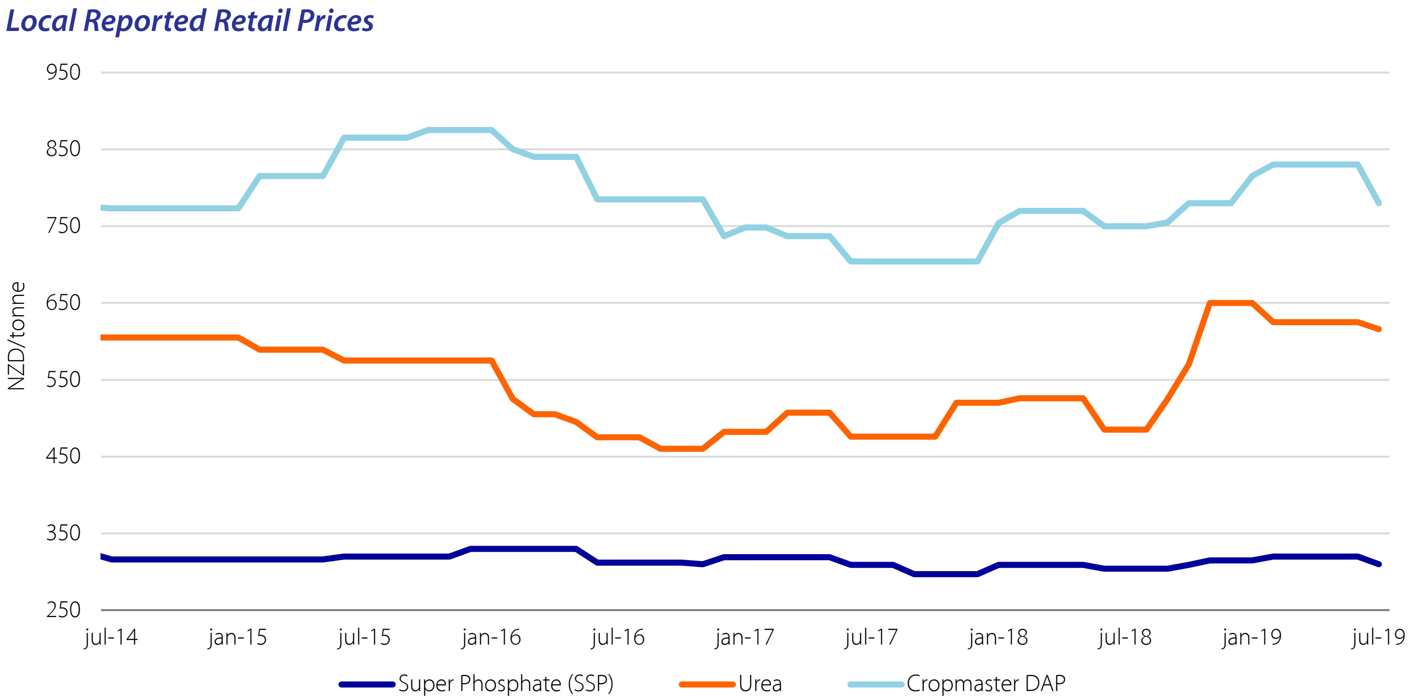
A majority of local reported retail prices were lower during July. Local urea fell 1.5 percent to 616 NZD/tonne, while Cropmaster DAP was down most significantly, lower 6 percent, to NZD 780/tonne.

What to Watch

- ***Ocean freight –*** During July, the Baltic Dry Index, the indicator of ocean freight prices, reached 2191, a five-year high. This was a result of the increased demand for capsize ships, following the re-commencement of mining at a Vale iron ore mine in Brazil. In the short term, we don't see more upside for freight prices, and expect prices will stabilise. If higher prices are sustained, this will add pressure to local fertiliser prices.

All Local Retail Prices down Month-on-Month

Rabobank



Source: Ravensdown, Rabobank 2019

NZD Resumes Its Slide

We hold our forecast for the NZ dollar to reach USc 63 within 12 months, as monetary policy loosening moves faster in NZ than the US.

In the US, the chances of a rate cut in 2019 are rising, although we still expect a full-blown cutting cycle to wait until 2020. One short-term risk to the economy was kicked down the road in July, as President Trump and congressional leaders reached an agreement to suspend the US debt ceiling for two years and allow hundreds of billions of dollars in new spending. But we expect the Fed to opt for a 25bps cut on 31 July. This would be an insurance cut rather than the beginning of an easing cycle. We think that one cut will not be enough to avoid a recession in 2020, with more cuts to follow next year as a result.

We expect more cuts from the Reserve Bank of New Zealand (RBNZ) in this cycle. The RBNZ cut rates by 25 bps in May, but left the OCR unchanged at 1.5 percent in June. It noted that the global economic outlook had weakened and that downside risk had intensified, meaning that further rate cuts may be required. In line with this, China posted its slowest growth rate in 27 years in the June quarter (at 6.2%). We expect rate cuts, with pressure on the NZD/USD to follow.

At USc 66.57on 26 July, the NZD was down around USc 0.7 on the start of July.

Rabobank forecasts the NZD to hit USc 63 by June 2020.

Tim Hunt
Head of Food & Agribusiness Research, Australia & New Zealand
+61 3 9940 8406
tim.hunt@rabobank.com

FX

What to watch

- ***Tensions in the straight of Hormuz.*** In July, Iran's Revolutionary Guard seized a 'foreign vessel' for smuggling fuel and the US shot down an Iranian drone in the Strait of Hormuz, after it allegedly threatened a US warship. About a fifth of global daily oil consumption (approx. 21m barrels) passes through the Strait each day. Moreover, tensions between the US and Iran are more likely to increase than not (don't forget Iran also shot down a US drone last month). Escalation of tensions will drive oil prices higher and negatively impact economic growth.

NZD Falls 0.7 US Cents in July

NZ/US dollar Cross Rate

Source: RBNZ, Rabobank 2019

Bullish Brent Outlook

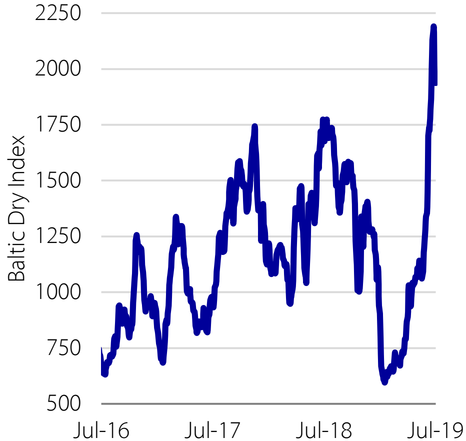
In our view, the fundamental outlook for Brent Crude is as bullish as it has been for quite some time. On the supply side, OPEC+ cuts have been extended through to the end of the year, while US sanctions on Iran and Venezuela, two of OPEC's largest producers, have forced both countries to reduce production. Alongside a sharp fall in ex-US oil supplies, demand is forecast to increase ahead of the IMO 2020 global shipping fuel specification change. Global refiners will be forced to run at high utilisation rates to produce enough post the specification change. We expect tight supplies, alongside expectations for increased demand, to lift Brent Crude to 75 USD/bbl during Q3 2019.

Ocean freight increased sharply during July. The Baltic Dry index peaked at 2191 points, the highest since January 2014. The increase was sparked by the partial resumption of iron ore mining at one of Vale's mines in Brazil, where a dam collapsed in January this year. Looking ahead, we see limited upside, and expect freight rates to stabilise in the short term.

Brent Crude Oil & Average Sydney Diesel July 2016 – July 2019

Source: AIP, Bloomberg, Rabobank 2019

Baltic Dry Index, July 2016-July 2019



Source: Bloomberg, Rabobank 2019

Agri Price Dashboard

As of 26/07/2019	Unit	MOM	Current	Last month	Last year
Grains & oilseeds					
CBOT wheat	USc/bushel	▼	496	544	537
CBOT soybean	USc/bushel	▼	883	894	861
CBOT corn	USc/bushel	▼	415	443	362
Australian ASX EC Wheat	AUD/tonne	▼	338	340	354
Non-GM Canola Newcastle	AUD/tonne	▼	586	605	566
Beef markets					
Eastern Young Cattle Indicator	AUc/kg cwt	▲	532	485	499
Feeder Steer	AUc/kg lwt	▲	300	278	292
North Island Bull 300kg	NZc/kg cwt	▲	545	535	535
South Island Bull 300kg	NZc/kg cwt	▲	510	505	525
Sheepmeat markets					
Eastern States Trade Lamb Indicator	AUc/kg cwt	▲	926	885	798
North Island Lamb 17.5kg YX	NZc/kg cwt	▲	805	780	805
South Island Lamb 17.5kg YX	NZc/kg cwt	▲	780	760	790
Venison markets					
North Island Stag	NZc/kg cwt	•	900	900	1,100
South Island Stag	NZc/kg cwt	▼	885	895	1,130
Dairy Markets					
Butter	USD/tonne FOB	▼	4,438	4,588	4,988
Skim Milk Powder	USD/tonne FOB	▲	2,588	2,363	2,050
Whole Milk Powder	USD/tonne FOB	▲	3,100	3,000	2,988
Cheddar	USD/tonne FOB	▲	3,888	3,838	3,613

Agri Price Dashboard

As of 26/07/2019	Unit	MOM	Current	Last month	Last year
Cotton markets					
Cotlook A Index	USc/lb	▼	75	76	98
ICE No.2 NY Futures (nearby contract)	USc/lb	▲	64	63	89
Sugar markets					
ICE Sugar No.11	USc/lb	▼	12.02	12.03	11.03
ICE Sugar No.11 (AUD)	AUD/tonne	▼	383	389	374
Wool markets					
Australian Eastern Market Indicator	AUc/kg	▲	1,754	1,740	1,981
Fertiliser					
Urea	USD/tonne FOB	▲	290	285	285
DAP	USD/tonne FOB	▼	340	353	434
Other					
Baltic Dry Index	1000=1985	▲	1,937	1,317	1,708
Brent Crude Oil	USD/bbl	▼	63	66	75
Economics/currency					
AUD	vs. USD	▼	0.691	0.699	0.738
NZD	vs. USD	▼	0.664	0.668	0.678
RBA Official Cash Rate	%	▼	1.00	1.25	1.50
NZRB Official Cash Rate	%	•	1.50	1.50	1.75

RaboResearch Food & Agribusiness Australia and New Zealand

Tim Hunt
Head of Food & Agribusiness Research and Advisory, Australia and New Zealand
+61 3 9940 8406
Tim.Hunt@Rabobank.com

Angus Gidley-Baird
Senior Analyst – Animal Protein
+ 61 2 8115 4058
Angus.Gidley-Baird@rabobank.com

Michael Harvey
Senior Analyst – Dairy
+61 3 9940 8407
Michael.Harvey@rabobank.com

Cheryl Kalisch Gordon
Senior Analyst – Grains & Oilseeds
+61 2 6363 5900
Cheryl.KalischGordon@rabobank.com

Hayden Higgins
Senior Analyst – Horticulture and Wine
+64 6 974 9504
Hayden.Higgins@rabobank.com

Wes Lefroy
Agricultural Analyst
+61 2 8115 2008
Wesley.Lefroy@rabobank.com

Emma Higgins
Analyst – Dairy
+64 3 961 2908
Emma.Higgins@rabobank.com

Blake Holgate
Analyst – Animal Protein and Sustainability
+64 3 955 4603
Blake.Holgate@rabobank.com

Charlie Clack
Commodity Analyst
+61 2 8115 2471
Charles.Clack01@rabobank.com

Dennis Voznesenski
Associate Analyst
+61 2 8115 3920
Dennis.Voznesenski@rabobank.com

Catherine Keo
Business Coordinator
+61 2 8115 4154
Catherine.Keo@rabobank.com

Rabobank New Zealand
Nearest branch call 0800 722 622
www.rabobank.co.nz