

# Fortnightly Agri Update

16 August 2017



## Viticulture – Fermenting

Presently, wine is a \$1.6 billion export industry for New Zealand, with a substantial scope for growth. That success will rest on continuing to identify the sources of demand growth, areas for productivity improvements and changing tastes around the world.

The wine industry is gearing up for boosting their global presence, on the back of firming global demand and strategies supporting productivity growth locally. Although technically classified as viticulture, the wine industry forms a vital part of the overall horticultural industry across New Zealand. Part of the 2020 growth strategy across the horticultural industry is the New Zealand wine industry's target of \$2 billion in exports by 2020.

The future of viticulture in New Zealand will largely rely on how we respond to developments on the globalisation front. As we have noted in the past, trade plays a vital role in the success of New Zealand's agricultural markets. The upward trend in the global environment – see more in our August 2017 *Economic Overview* – is opening up opportunities for our key export destinations.

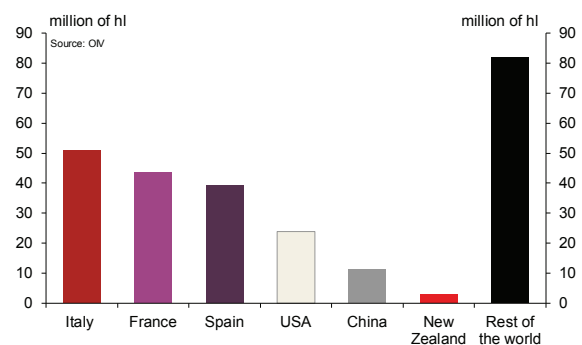
### Global Wine Market

The size of the global vineyard in 2016 was around 7.5 million hectares of area under vines. Area under vines refers to the land used for the production of wine grapes, table grapes or dried grapes that are in production or available for production. Accordingly, five countries (Spain, China, France, Italy and Turkey) represent approximately 50% of the global vineyard. In contrast, New Zealand vineyards represent around 0.5% of the global vineyard.

The wine market is a truly global market, with the greatest concentration of producers coming out of Europe. Italy

dominates as the world's largest producer of wine, with the France as a close second. It is not surprising that Europe dominates the market. However, demand side shifts are becoming central to the supply side responses by producers.

### Global wine production (Top 5 producers incl. NZ)



New Zealand ranks as 15th on the global production scale, specialising mainly in white wines. On an area basis, 79% of New Zealand vineyards support the production of white wines, with Marlborough and the Hawke's Bay contributing around 80% of the total producing area. In particular, Sauvignon Blanc represents around 76% of the white wines produced. Global supply metrics show that white wines tend to be the most widely consumed and thus more heavily produced.

However, observable food consumption trends suggest room for growth in red wine production. Red wine accounts for 21% of the total producing area, with Pinot

Noir representing 72% of the output. In general supply developments, especially in New Zealand, the industry is calling for greater diversification across the product mix. Demand for wine will largely shape this mix; however, given current industry structure, there is room for greater growth in red wine production.

The US remains the world's largest consumer of wine. Recent data details that on a per capita basis, US consumers drank around 11 litres of wine in 2016, with 3.6 billion litres consumed in total. The interesting development on the demand side is the growing demand for wine in Asia, most importantly China. The growing middle class and general consistency in the outlook for the Chinese economy has shown an exponential rise in the demand for premium goods, especially in terms of agricultural products.

Wine industry reports strongly suggest that given the current Chinese wine consumption trends, China will become the second largest consumer of wine by 2020. On a per capita basis, Chinese wine consumption is relatively low to the US and other consumers. However, the sheer size of the market suggests that the total value of sales could exceed US\$21 billion by 2020.

This surpasses the value of both France and the UK, which are in the top 10 of global wine consumers. Furthermore, industry experts are forecasting China to become the world's largest consumer of still wines, i.e. non-sparkling wines by 2020.

Wine has a significant global presence. The consumption of finer foods has a higher income elasticity, which means that under firm economic conditions, the consumption of these goods tends to rise. With a notable firmness in the global economy, there is an upside to the market for wine. Moreover, with a generally firm outlook for the New Zealand economy – see more in our August 2017 *Economic Overview* – there is scope for further investment across vineyards to productivity growth.

This growth potential supports the case for pushing for better trade arrangements for the Asia region and potentially for the US as well, which will be a key destination for New Zealand soft commodity exports going forward. In general, given the current path of expansion, there is strong potential for the wine industry to play a larger role in New Zealand's rural economy over time.

**Shyamal Maharaj**  
Economist

#### GlobalDairyTrade Auction Results, 16 August 2017

	Change since last auction	Price index USD/Tonne
Anhydrous Milk Fat (AMF)	-1.2%	\$6,199
Butter	-1.3%	\$5,735
Butter Milk Power (BMP)	n.a.	n.a.
Cheddar	1.4%	\$4,005
Lactose	-4.9%	\$747
Rennet Casein	2.9%	\$6,255
Skim Milk Powder (SMP)	0.3%	\$1,968
Whole Milk Powder (WMP)	-0.6%	\$3,143
GDT Price Index	-0.4%	

#### Payout Forecast Table

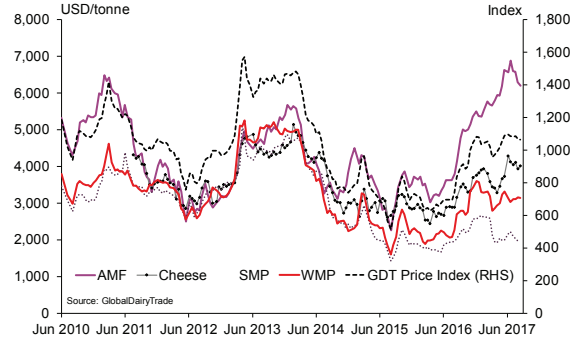
	2016/17	2017/18	
	Fonterra	Fonterra	Westpac
Milk Price	\$6.15	\$6.75	\$6.50

# Beyond the farm gate

## Dairy

	Current price level compared to 10 year average	Next 6 months
Trend	Average	↘

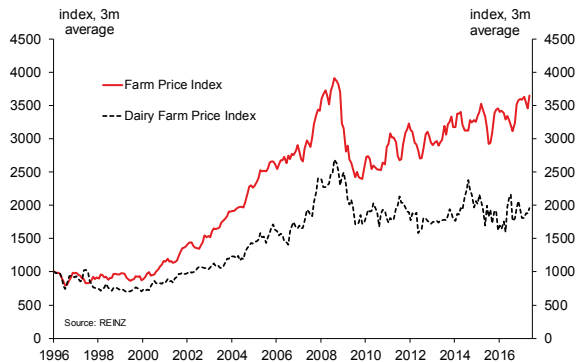
Last night's GlobalDairyTrade auction saw a mild 0.4% decline in the overall price index, with lower prices across most products. The result went against some of the recent optimism in the market (for instance the NZX dairy futures implied a 4% rise in prices), but was in line with our outlook for the rest of this season. Milk production has picked up among the major exporters (including New Zealand) and has scope to rise further, which could put some downward pressure on prices in coming auctions. Our farmgate milk price forecast for this season remains at \$6.50/kg.



## Land prices

	Current price level compared to 10 year average	Next 6 months
Trend	Above Average	→

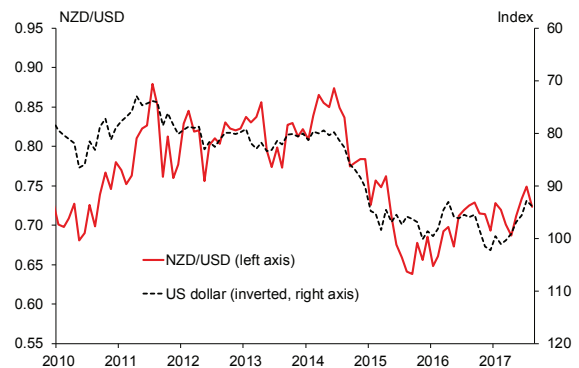
The REINZ farm price index rose in July, to be up 9% on the same time last year. However, price estimates are being drawn from a dwindling number of farm sales. Prices for arable land and finishing farms have been picking up in recent months, but declining for orchards. Dairy farm prices have been relatively static, despite improving conditions for the industry. The improved milk price forecast for this season will give buyers some confidence, although sales between existing farmers may be limited as they focus on debt reduction.



## NZ dollar

	Current price level compared to 10 year average	Next 6 months
Trend	Above Average	↘

The New Zealand dollar has sustained its recent strength against the US dollar, although this strength has been primarily a US story. Uncertainties on the Trump administration's policies and the spate of softer US economic data have halted the gains in the USD. On the domestic front, we see the OCR staying on hold until the end of 2019, while the US is likely to raise interest rates further in this time. This will help to narrow New Zealand's interest rate spread over the US and reduce the appeal of the NZD.



**Note:** Trend arrows indicate direction of change in world prices.

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