

# Fortnightly Agri Update

22 March 2017



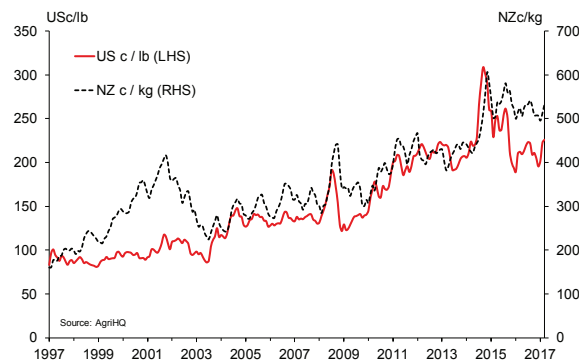
## Where's the beef?

In this Fortnightly Agri Update, we take a closer look at developments in beef markets. It's been a positive start to the year for local beef farmers. NZ dollar prices are lingering above year-ago levels, and are over 25% above their 10-year average. With a recovery in global beef supply now well underway, prices are expected to come under a bit of downward pressure over the coming year. However, rising demand from a growing Asian middle class and increasing resource constraints should support prices at much higher levels than in the 2000s. Of course, there is significant uncertainty about the broader global trade environment, and a swing back towards more protectionist policies would have negative implications for the beef outlook.

Over the past few years, global beef prices have been propped up by tight supply, as farmers in the United States and Australia rebuilt their herds following severe droughts. But we have now passed the turning point in global cattle production, with production stabilising in 2016 and set to record a decent gain this year. Against a backdrop where input costs like grains and fertiliser have remained relatively subdued, it's not surprising to see a supply response now coming through.

Supply in the United States – the world's largest beef producer – is well on its way to recovery with the cattle herd growing for the past three years. Beef production rose a solid 6% in 2016 with even stronger gains in exports. The United States Department of Agriculture (USDA) is forecasting a further 4% rise in production in 2017. The recovery in domestic production has reduced the reliance on imported beef, and after 3 years of being a net importer of beef, US beef export and import volumes are expected to be broadly balanced in 2017.

### Beef prices



The US manufactured beef market is a key export market for New Zealand's bull and cow meat, and decreasing demand for imported product has seen the US dollar price fall nearly 30% from 2014's highs. That said, the imported beef market has been surprisingly resilient this year, with prices rising over the past couple of months to be a bit higher than a year ago. In part, this reflects New Zealand supply being slow coming to market, as good summer growing conditions in most regions have encouraged farmers to keep cattle on farm, and the improved outlook for dairy sector incomes has reduced the supply of dairy cull cows.

At the same time, supply from Australia – New Zealand's biggest competitor in the US market – has continued to tighten. Australia's total beef exports declined 21% in 2016 and Meat and Livestock Australia are forecasting a further

# Where's the beef? continued

5% fall this year. While dry conditions in Queensland could see more cattle processed in the near term, Australia's supply to the US will remain constrained by the broader herd rebuilding dynamic.

Turning to prime beef (i.e. not manufacturing), Asia is the main destination for New Zealand's exports. And here, China is by far the fastest growing market. China's total beef imports rose a whopping 22% in 2016, seeing it become the world's second largest beef importer. Strong growth in imports is expected to persist in 2017. But despite this rapid rise in demand for foreign beef, in-market prices have been coming under pressure due to increased competition as more countries are granted market access.

The re-entry of Brazil into the Chinese market in 2015 has been significant, with Brazil capturing the lion's share of China's growth in imports last year. However, a developing scandal about Brazilian suppliers selling tainted meat has resulted in China and other countries suspending imports from Brazil. While much will depend on how long the suspensions last, tighter supply, especially in China where Brazil is now such a big player, will create opportunities for other beef exporters, including New Zealand. With a ban on some US beef products removed last year (that had been implemented over mad cow concerns back in 2003), US suppliers could benefit from the potential supply gap in the Chinese market.

Despite steady growth in demand, other large import markets including South Korea and Japan have also been feeling the pressure of rising supply. In these markets, it's been US beef suppliers seeing particularly strong growth and increasing their foothold.

While rising beef supply is expected to place prices under some pressure over the coming year, solid fundamentals remain in place to support prices at higher levels than those seen in the 2000s. On the demand side, the growing middle class in China and elsewhere in Asia, and continued

liberalisation in trade access will bolster global demand, although there is a risk of a swing back to more protectionist policies which would cloud the demand outlook. In China, per-capita beef consumption is low, urbanisation and rising incomes are expected to underpin growing demand for premium beef. For New Zealand, the prospect of chilled beef access in China presents a key opportunity for our exporters to gain a foothold in the higher-value segment of the market. And on the supply side, the volatile global climate and growing resource and environment constraints will hold back the response in global supply, which should help to avoid the over-correction in prices that we've seen in the past.

**Sarah Drought**  
Economist

## GlobalDairyTrade Auction Results, 22 March 2017

	Change since last auction	Price index USD/Tonne
Anhydrous Milk Fat (AMF)	3.0%	\$5,799
Butter	4.9%	\$4,910
Cheddar	-1.0%	\$3,406
Lactose	-2.7%	\$913
Rennet Casein	3.6%	\$5,927
Skim Milk Powder (SMP)	-10.1%	\$1,948
Whole Milk Powder (WMP)	2.9%	\$2,855
GDT Price Index	1.7%	

## Payout Forecast Table

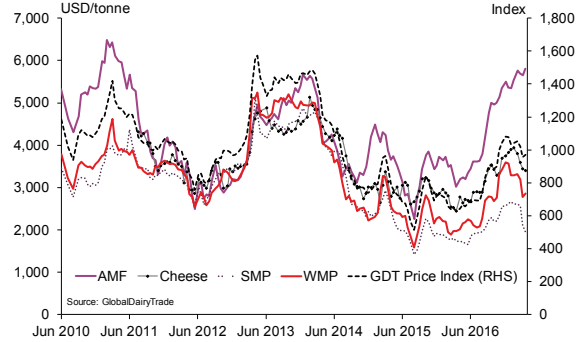
	2016/17		2017/18
	Fonterra	Westpac	Westpac
Milk Price	\$6.00	\$5.90	\$6.10

# Beyond the farm gate

## Dairy

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

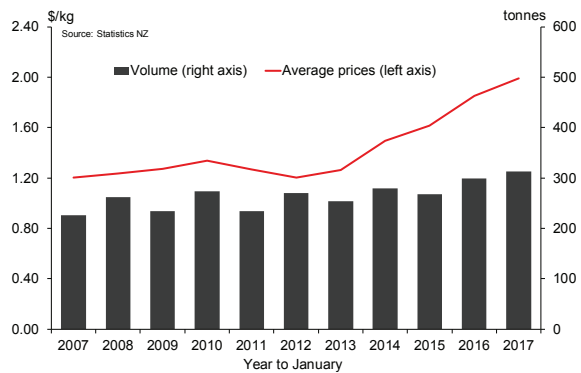
Dairy prices stabilised in last night's GlobalDairyTrade auction, rising 1.7% after a 9% fall over the previous two auctions. Within last night's move, whole milk powder prices rose 2.9% to US\$2,855/tonne. With a number of contracts hitting the lower price limit in the previous auction, last night's result was encouraging. Skim milk powder, weighed down by high stockpiles in Europe and rising US supply, continued its poor run falling 10% last night to US\$1,948/tonne. With milk production in both New Zealand and Europe gradually trending higher, the dairy market will continue to be challenged by rising supply in coming months. Our forecast of \$5.90/kgMS for this season's farmgate milk price had incorporated some more near-term softness in prices. As a result, last night's stabilisation in prices creates a bit of upside risk to our forecast.



## Apples

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

Harvesting of the 2017 apple crop is now in full swing. Pipfruit New Zealand are expecting this year's crop to eclipse the previous record held since 2004 as an "on year" crop coincides with growth in tree numbers. The crop is expected to be of high quality in both colour and taste, with conditions described as "pitch perfect" as recent rain followed a combination of hot days and cool mornings. The sector is benefitting from greater use of technology and product innovation that have allowed them to be successful in meeting preferences in Asian markets in particular. Demand from Asia (including China) reportedly remains strong, helping to underpin local returns. However, conditions in Europe have been and are likely to remain more challenging, with local returns under pressure from unfavourable exchange rates.

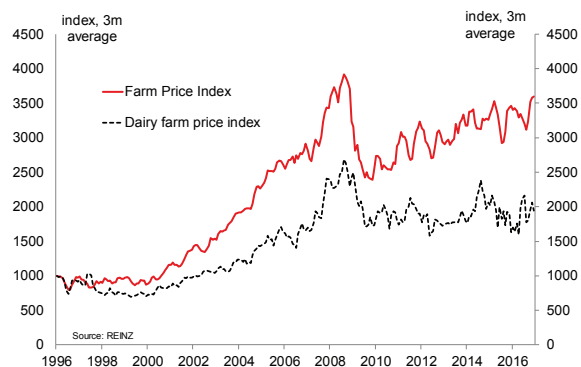


## Land prices

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

The REINZ farm price index edged higher in February, with prices 4% higher than a year earlier. Contributing to the improvement has been a recovery in dairy farm prices from a soft patch in early 2016, as the improved outlook for the farmgate milk price has shored up sentiment within the industry. While dairy farm prices edged back in February, they were still up nearly 20% from a year earlier. Turnover has also improved. That said, recent sharp declines in global dairy prices will serve as a fresh reminder how volatile income can be, and will likely weigh on sentiment somewhat. Outside of this, demand for horticulture properties remains high, with kiwifruit orchards in particular continuing to sell strongly.

## REINZ farm price index



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

# Contact the Westpac economics team

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**Michael Gordon**, Acting Chief Economist +64 9 336 5670

**Satish Ranchhod**, Senior Economist +64 9 336 5668

**Sarah Drought**, Economist +64 9 336 5696

**Any questions email:** [economics@westpac.co.nz](mailto:economics@westpac.co.nz)

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