

# Fortnightly Agri Update

21 February 2018



## Down in the dumps

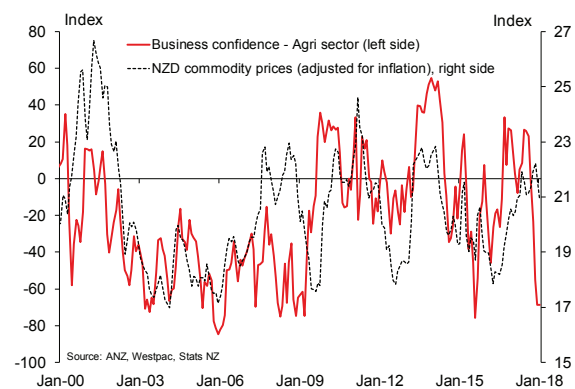
Prices for New Zealand's key agricultural commodity exports remain reasonably firm, with robust global demand providing a supportive backdrop. Looking ahead, we expect key commodity prices to come under pressure, as growth in China slows, and global supply increases in some markets. Yet despite relatively buoyant prices, confidence in the rural sector is weak; with apparent nervousness about the impact of impending regulatory changes probably a key concern.

As we outlined in our last Fortnightly Agri Update, most of New Zealand's key rural exports have started 2018 on the front foot. Dairy prices have improved noticeably since the start of the year – although this has partly been due to concerns that poor weather may curtail NZ production. Some of these concerns have eased following recent wet weather, and in last night's GlobalDairyTrade auction prices stalled. The overall GDT index was down 0.5%, and Whole Milk Powder prices edged up a smidgeon (up 0.3% to US\$3,246). Higher prices over the last couple of months have prompted us to lift our milk price forecast to \$6.50 this season earlier this month. However, we still expect prices to moderate in 2018 as growth in China slows and global production increases (particularly in Europe).

Solid farm gate prices for most export commodities, however, have done little to bolster confidence in the rural sector. Confidence is lingering well below what we would expect given the current level of commodity prices (see chart). Undoubtedly, this reflects a number of developments. Weather conditions have been adverse in

some regions with parts of the country suffering drought conditions in late 2017/early 2018, the dairy sector has watched with concern the spread of mycoplasma bovis, while the tighter labour market nationwide is also probably influencing the sector. But we suspect the plunge in confidence also has plenty to do with the change in government. The latest Federated Farmers confidence survey released earlier this month reported increased concerns around climate change and the ETS, while regulation and compliance costs was the top concern amongst survey respondents.

New Zealand commodity prices and rural confidence



Changes signalled by the new Government that are likely to effect the rural sector include:

- commitment to a legally binding carbon emissions target
- no new taxpayer funding for irrigation

- support for less intensive land use (such as forestry)
- no new mines on conservation land, and
- tighter restrictions on foreign ownership of land.

The details around some of these policies are still to be confirmed, but evidently farmers are fearful that ultimately they will increase their cost of doing business. This may mean farmers are reluctant to undertake significant investment on farm while uncertainty around how government policies will be implemented persists.

Weak confidence in the sector is also affecting the rural property market, most noticeably via soft sales volumes. To date, there has been little downward pressure on prices, with the combination of low interest rates and relatively healthy farm gate prices meaning sellers aren't being rushed into accepting lower prices. However, this combination won't last forever. And the increasing focus on the environmental costs of farming is likely to see some land prices to come under pressure. In particular, the price of land used for dairying (which is likely to face the most significant cost increases as new environmental regulations are introduced) is expected to fall. In contrast, prices for less carbon intensive uses of land such as horticulture and forestry could get a relative boost.

**Anne Boniface**  
Senior Economist

#### GlobalDairyTrade Auction Results, 21 February 2018

	Change since last auction	Price index USD/Tonne
Anhydrous Milk Fat (AMF)	-1.9%	6,458
Butter	1.1%	5,334
Butter Milk Power (BMP)	n.a.	n.a.
Cheddar	-1.3%	3,686
Lactose	n.a.	n.a.
Rennet Casein	0.7%	4,980
Skim Milk Powder (SMP)	-3.0%	1,832
Whole Milk Powder (WMP)	0.3%	3,246
GDT Price Index	-0.5%	1,055

#### Farmgate milk price forecasts

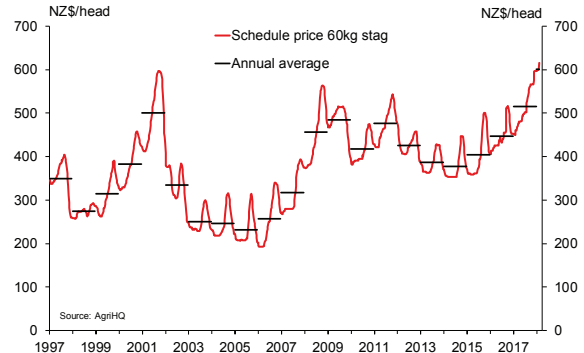
	2017/18		2018/19
	Westpac	Fonterra	Westpac
Milk Price	\$6.50	\$6.40	\$6.50

# Beyond the farm gate

## Venison

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

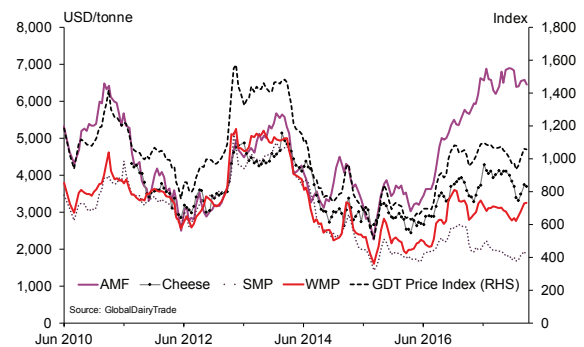
Venison prices have risen strongly over the last year. The US is an increasingly important market for venison exports, and consumer demand there has strengthened on the back of a stronger backdrop for the household sector, falling unemployment and stronger wage growth. In addition, supply from New Zealand has been falling, in part due to herd rebuilding. Stats NZ reports deer numbers grew 1.7% in the year to June 2017 (although fawn numbers still fell 1.5% over the same period), the first time it has recorded an annual increase in deer numbers since 2004. Looking ahead, we expect the NZD to weaken, especially against the USD over the course of 2018. This, combined with a solid consumer demand backdrop in key export markets, is likely to continue to support farm gate prices.



## Dairy

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

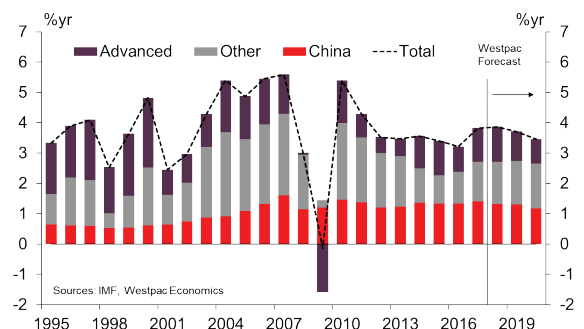
Dairy prices stalled in the latest fortnightly GlobalDairyTrade auction, with headline prices falling 0.5%. This was in line with our expectations and leaves us comfortable with our \$6.50 payout forecast for this season. Within this, there was a small lift in whole milk powder prices while skim milk powder prices came under greater pressure, falling 3%. Prior to last night's auction, Fonterra announced an increase in its expected offer volumes over the next 12 months, due to more WMP on offer. However, the volume on offer is still significantly less than a year ago. We expect dairy prices to come under further downward pressure in the coming months, as local supply concerns dissipate and European production continues to expand.



## Global Growth

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

We've revised up our global growth forecasts in recent months, largely on the back of a stronger outlook for the US economy, and modestly higher forecasts for Chinese GDP growth. But while the picture for global growth as a whole looks more promising, the outlook is more mixed when it comes to New Zealand's major trading partners. Growth in China is set to slow from 6.9% last year to 6.3% this year and 6.1% next as Chinese policymakers step up efforts to rebalance their economy. Expectations of growth in the Australian economy have also been downgraded on the back of soft wage growth and dwindling construction activity.



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

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