Fortnightly Agri Update

7 March 2018

Trump and trade

Another week and another twitter tirade from US President Donald Trump. Last week Trump used his Twitter account to announce plans to slap a 25% tariff on steel and a 10% tariff on aluminium exports entering the US, justifying the move in the interests of "national security". It is expected that his plan will be confirmed in in the coming days (despite widespread lobbying to halt or soften the action).

As it's become increasingly likely to be implemented, financial markets have reacted nervously, and European leaders have threatened retaliation by taxing iconic imports from the US such as Levi's and bourbon. Officials from other countries such as Mexico, Brazil and China have also warned of the prospect of retaliatory action. The latest move is a continuation of the growing protectionist sentiment that has been bubbling since Trump was elected US president on his "America First" platform. He has already applied tariffs to solar panel and washing machine imports. The latest actions have ignited fears of an escalating tit for tat trade war. One that could potentially widen to include other sectors and countries and become a major drag on global economic growth.

Still, it's unlikely to be smooth sailing for Trump in his attempt to put "America First". He's faced criticism from within his own Republican party, and there's the prospect of legal challenges mounted at the WTO. What's more, as the higher input costs start to be passed through to domestic prices American consumers are likely to question how they are benefitting from increased protection for the US steel industry. Indeed, some point to Trump comments about the potential for exemptions of Canadian steel exporters if "new and fair NAFTA agreement is signed" as evidence of the announcements being a negotiation tactic rather than the launch of a trade war.

Trump isn't the first US president to use trade restrictions to try and support the US steel industry. However, in previous periods, the restrictions have been withdrawn sooner than expected in response to international pressure and trade disruptions. The current proposals are different in that they are being introduced under the threat to national security justification (which could give the President greater ability to maintain the barriers) but there's plenty of uncertainty about how long the proposed restrictions could remain in place.

At first blush, these developments might not be such a concern for New Zealand (or New Zealand farmers). We're not a major aluminium or steel exporter. But New Zealand, with its strong agricultural export base, is a nation reliant on trade. While retaliatory action could see some doors open and other doors close for New Zealand exporters, this would be hugely disruptive. What's more, New Zealand certainly doesn't have a lot of bargaining chips when it comes to retaliatory moves. We have a relatively small economy, with very few barriers to trade, and little incentive to put up walls. If the US were to impose similar tariffs on dairy imports or agricultural imports more broadly it would have a big impact on the agricultural sector.

In the near term, we think such a move to extend tariffs to agriculture looks unlikely. Yet there's no doubt that the growing protectionist sentiment evident not only in the US but also in other parts of the world (the UK's vote in favour of Brexit is another example), signal an uncertain and challenging environment for New Zealand exporters.

New Zealand exporters are going to have to work harder to differentiate themselves on the basis of quality and ability to match evolving consumer preferences, not price. It also highlights the importance of diversification amongst trading partners. With some countries all too willing to erect trade barriers, there are benefits to exporters of not having all their eggs (or in our case milk and meat) in one basket.

Anne Boniface
Senior Economist

GlobalDairyTrade Auction Results, 7 March 2018

	Change since last auction	Price index USD/Tonne
Anhydrous Milk Fat (AMF)	-3.2%	6,245
Butter	-1.0%	5,280
Butter Milk Power (BMP)	-4.3%	1,959
Cheddar	1.7%	3,759
Lactose	n.a.	n.a.
Rennet Casein	2.2%	5,128
Skim Milk Powder (SMP)	5.5%	2,051
Whole Milk Powder (WMP)	-0.8%	3,232
GDT Price Index	-0.6%	1,049

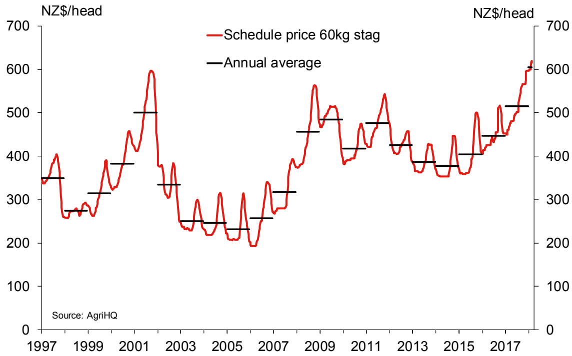
Farmgate milk price forecasts

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

Beyond the farm gate

Venison

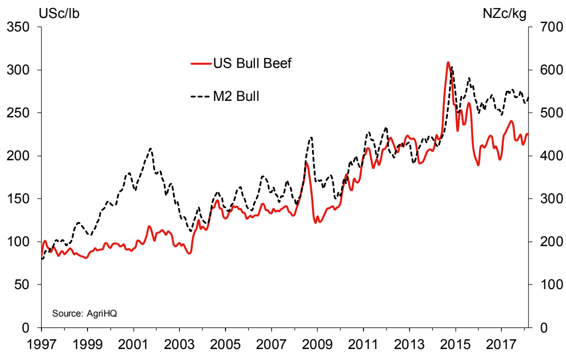
	Current price level compared to 10 year average	Next 6 months
Trend	High	➔



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.

Beef

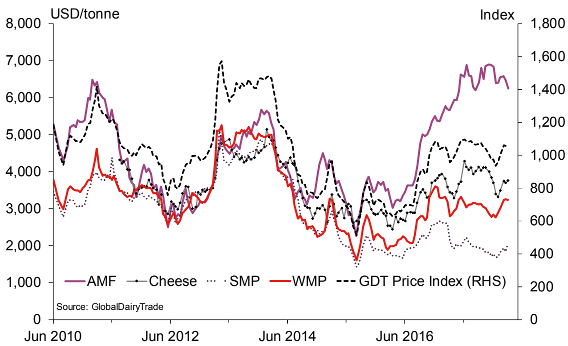
	Current price level compared to 10 year average	Next 6 months
Trend	Average	➘



For now, relatively tight local supplies and solid international demand are continuing to underpin beef prices. However, we still expect beef prices to come under some downward pressure over the course of this year as global supply increases. Australian cattle slaughter is expected to lift significantly this year (ABARES is forecasting 9% growth), while US beef production is also expected to grow strongly in 2018, encouraged by high beef prices and favourable feed costs.

Dairy

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



Dairy prices eased a touch further in last night's GlobalDairyTrade auction. In aggregate, the GDT index fell 0.6%, which included a 0.8% fall in whole milk powder prices. In contrast, skim milk powder prices (which have been under pressure over the last year or so because of the accumulation of large stockpiles in Europe) bounced 5.5% higher. Slightly softer prices followed Fonterra increasing the volume of WMP and SMP available through GDT auctions over the next few months. Back in December Fonterra said it expected a 4% drop in milk production this season and cut the volume of product available on the GDT platform. Nationwide, production in January was down almost 7% on a year earlier (on a milk solids basis) and down 1% for the season to January. However, since then on farm conditions have improved in many parts of the country and over the entire season, we expect nationwide domestic production to be down around 1%. We expect dairy prices to soften further in the coming months, as global supply continues to grow. With recent outturns in line with expectations, we remain comfortable forecasting a $6.50 milk price this season.

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

Contact the Westpac economics team

Dominick Stephens, Chief Economist +64 9 336 5671

Michael Gordon, Senior Economist +64 9 336 5670

Satish Ranchhod, Senior Economist +64 9 336 5668

Anne Boniface, Senior Economist +64 9 336 5669

Paul Clark, Industry Economist +64 9 336 5656

Any questions email: economics@westpac.co.nz

Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Disclaimer

Disclaimer continued

Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This communication is being made only to and is directed at (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (b) high net worth entities, and other persons to whom it may otherwise lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as "relevant persons"). Any person who is not a relevant person should not act or rely on this communication or any of its contents. The investments to which this communication relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this communication or any of its contents. In the same way, the information contained in this communication is intended for "eligible counterparties" and "professional clients" as defined by the rules of the Financial Conduct Authority and is not intended for "retail clients". With this in mind, Westpac expressly prohibits you from passing on the information in this communication to any third party. In particular this communication and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction. This communication is made in compliance with the Market Abuse Regulation (Regulation(EU) 596/2014).

Investment Recommendations Disclosure

The material may contain investment recommendations, including information recommending an investment strategy. Reasonable steps have been taken to ensure that the material is presented in a clear, accurate and objective manner. Investment Recommendations for Financial Instruments covered by MAR are made in compliance with Article 20 MAR. Westpac does not apply MAR Investment Recommendation requirements to Spot Foreign Exchange which is out of scope for MAR.

Unless otherwise indicated, there are no planned updates to this Investment Recommendation at the time of publication. Westpac has no obligation to update, modify or amend this Investment Recommendation or to notify the recipients of this Investment Recommendation should any information, including opinion, forecast or estimate set out in this Investment Recommendation change or subsequently become inaccurate.

Westpac will from time to time dispose of and acquire financial instruments of companies covered in this Investment Recommendation as principal and act as a market maker or liquidity provider in such financial instruments.

Westpac does not have any proprietary positions in equity shares of issuers that are the subject of an investment recommendation.

Westpac may have provided investment banking services to the issuer in the course of the past 12 months.

Westpac does not permit any issuer to see or comment on any investment recommendation prior to its completion and distribution.

Individuals who produce investment recommendations are not permitted to undertake any transactions in any financial instruments or derivatives in relation to the issuers covered by the investment recommendations they produce.

Westpac has implemented policies and procedures, which are designed to ensure conflicts of interests are managed consistently and appropriately, and to treat clients fairly.

The following arrangements have been adopted for the avoidance and prevention of conflicts in interests associated with the provision of investment recommendations.

(i) Chinese Wall/Cell arrangements;

(ii) physical separation of various Business/Support Units;

(iii) and well defined wall/cell crossing procedures;

(iv) a "need to know" policy;

(v) documented and well defined procedures for dealing with conflicts of interest;

(vi) steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission ("CFTC") as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC ('WCM'), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 ('the Exchange Act') and member of the Financial Industry Regulatory Authority ('FINRA'). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.