AGRICULTURE

Monthly roundup.

August 2024

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SUMMARY

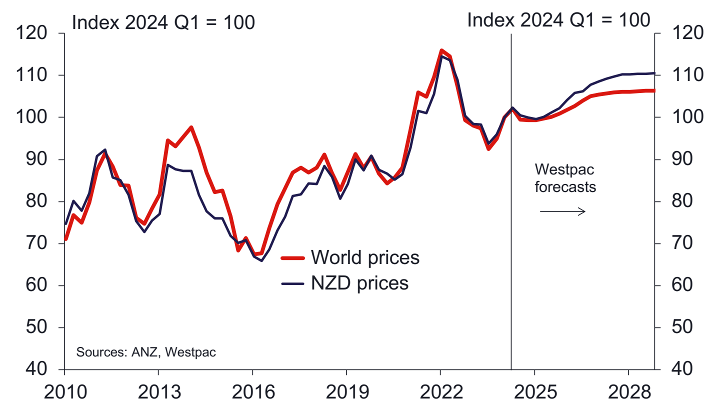
Better prices ahead, but margins to remain under pressure.

- Prices to lift slightly over the coming year reflecting better demand outside of China.
- Farm profitability will improve because input cost inflation will moderate, debt servicing costs will fall and prices will lift, But on farm profitability will remain challenged by high-cost structures.
- Hence some farmers will still look to economise on key factor inputs, such as fertiliser to protect margins.

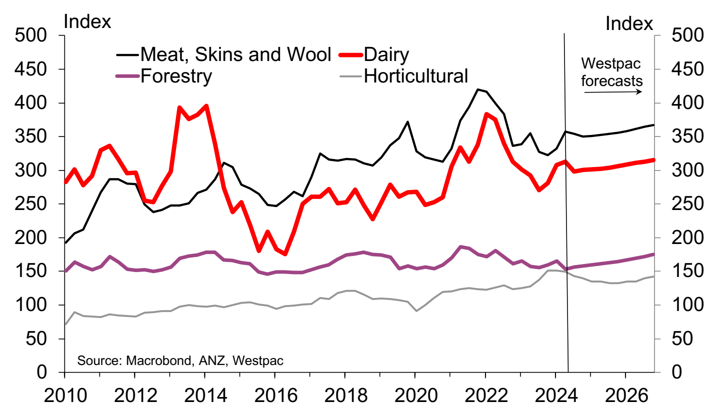
China is the big swing factor across all commodities.

- Dairy prices are expected to track modestly higher. We see balanced risks around our milk payout of $8.40 per kg MS for 2024/25, with the trajectory of Chinese demand being key.
- Beef prices will continue to be supported by solid US demand and reduced US supply. A firmer medium-term uptrend in prices will require stronger Chinese demand which we don't expect to see for a while.
- A recent pick up in export lamb prices reflects strength of demand in traditional export markets, notably the UK, but also the US. That said, we don't expect a more sustained increase in export prices until Chinese demand recovers.
- Orchardists should see higher export volumes, which is likely to offset lower kiwifruit and slightly weaker apple prices. Meanwhile, export log prices should move sideways and are only likely to lift once building activity in China begins to recover.

Commodity prices – World and NZ$ denominated



Commodity prices by category



GLOBAL BACKDROP

Trading partner growth to remain subpar.

- New Zealand's trading partners are forecast to grow 3.3%. Growth in most advanced economies should lift as monetary policy settings normalise.
- The near-term growth outlook in China has been lowered. Chinese growth should continue to slow as consumers are constrained by a weak property market and unfavourable demographics.

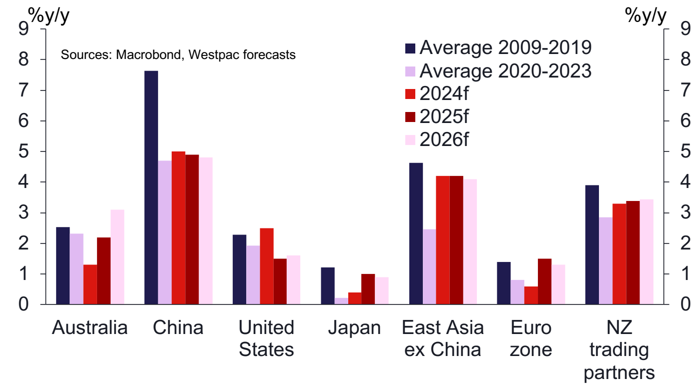
Monetary policy easing is drawing closer in many jurisdictions.

- Encouraging US inflation data should prompt the Fed to commence policy easing in September.
- The ECB and BOE have already cut rates, with further reductions likely. The RBA is not expected to start easing until February 2025.

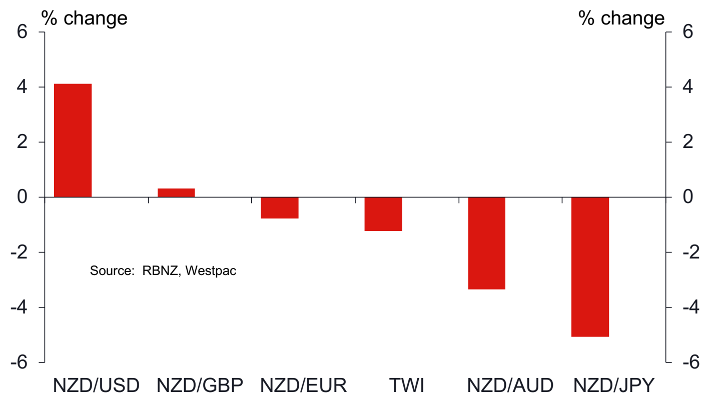
The NZD is likely to underperform.

- A declining yield advantage, weak growth outlook and significant fiscal and current account deficits likely imply a weaker NZD against most currencies in the next year.
- Trends in the USD more generally will drive the NZD/USD. The USD is expected to be supported by risk aversion around the upcoming US election and eventual policy easing.

Growth forecasts, major trading partners



Forecast change in NZD to December 2025



DAIRY

China is lifting its own production of dairy products.

- The recovery in dairy prices that started almost a year ago seems to have lost momentum with prices at the recent GDT auctions being generally mixed.
- That partially reflects fluctuating Chinese imports of whole and skim milk powder. Demand remains intermittent and there has been a drive for greater self-sufficiency in domestic production, supported by policy measures to boost genetics and reduce animal feed costs.

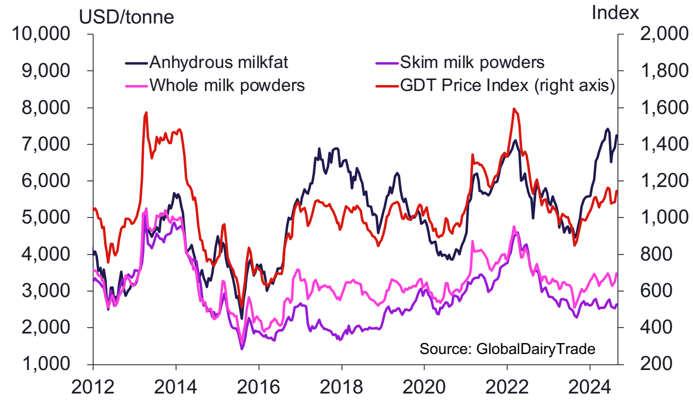
Demand from other markets is helping to lift prices.

- Strengthening South-East Asian and Middle Eastern demand has been an offset that's supported whole and skim milk prices, and milk fats.
- Butter and anhydrous milk fat prices are near record levels reflecting non-Chinese demand.

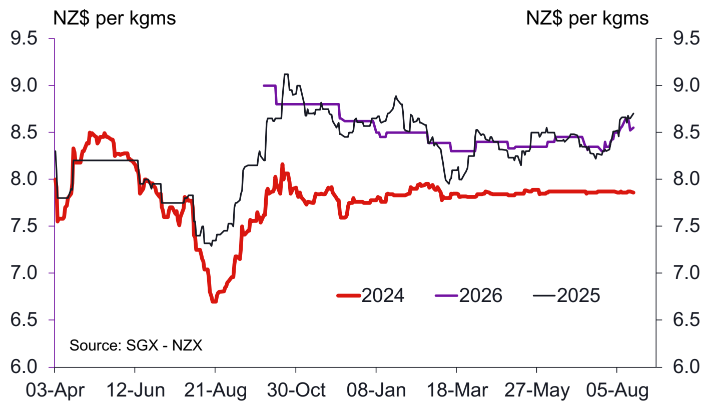
But all roads lead back to China.

- Looking forward, a partial recovery in Chinese demand and ongoing strength in other markets (particularly South-East Asia) should offset modest production gains in key export regions and lift dairy prices over the coming year. While a slightly stronger NZ$ will weigh on returns, we still expect higher farmgate milk prices.
- The futures market is currently pointing to a milk payout of around $8.65, but it is still early in the season. We think the risks are evenly balanced and remain comfortable predicting a payout of $8.40/kg MS for 2024/25.

Dairy product prices on the GDT auction



Milk futures prices



BEEF

US demand is helping to support export prices.

- Slaughter prices reflect strength in demand from processors and a shortage of cattle. Competition is intensifying between processors that focus on the domestic market and those selling into the export market.
- Meanwhile beef export prices are being underpinned by favourable supply and demand dynamics, particularly in the big US market.
- Supportive economic conditions in the US continue to underpin the consumption of beef products with a high import component. That together with falling US beef production has helped to support US import demand as well as export prices.

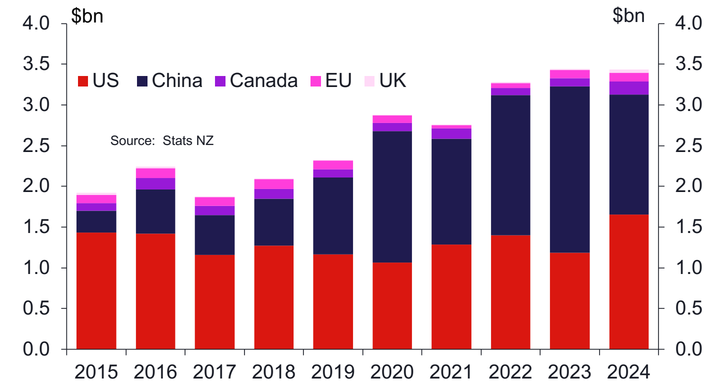
Weak Chinese demand is keeping a lid on prices.

- Lower Chinese import demand provides a partial offset to the more positive US picture. That reflects two dynamics - an increase in domestic production in China, and weak consumer demand in that country. Beef is also seen as a premium product and so faces strong competition from cheaper alternative proteins like pork and chicken. A switch to less expensive cuts is also evident.

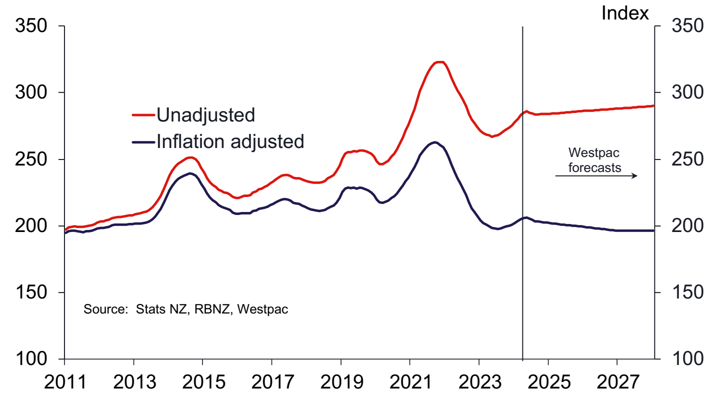
Roles to begin reversing over the next few years.

- Looking forward, the rebuild of the herd in the US and slightly lower economic growth should provide less support to beef prices over coming years. By contrast, a recovery in Chinese demand should be supportive, although that support could be undermined by higher domestic production.

Value of beef exports to key markets – March year end



Beef export prices – US$ price index



SHEEP MEAT

Shortages pushing up domestic slaughter prices.

- Sheep meat prices have recently ratchetted higher from multi-year lows. Rising slaughter prices reflect the strength of competition between domestic processors for finished lambs, which are in short supply.
- Kill rates are close to record lows and that is increasing demand for domestic store lambs. Farmers are holding stock back to increase weights.

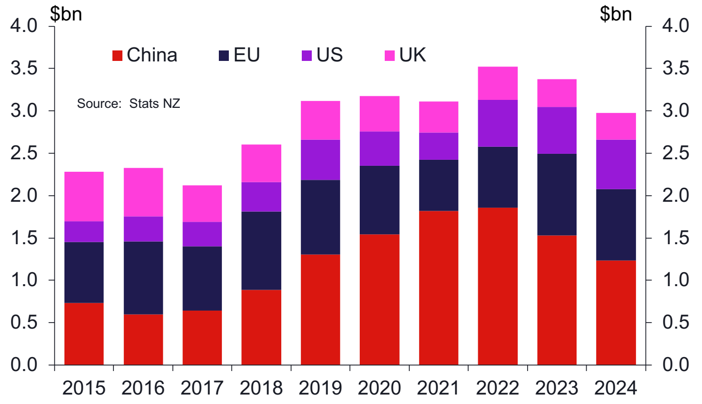
Exports shifting focus towards more traditional markets.

- Lamb export prices have also picked up recently. That reflects strength in demand in traditional markets, especially in the UK where price competitive New Zealand lamb has continued to make inroads. Initially that was because of production issues in UK. Recent further gains have been under an FTA.
- New Zealand lamb has also made gains in the small but still relevant US market. Exports to the EU have also lifted, despite New Zealand lamb having to compete with cheap Australian lamb in that market.

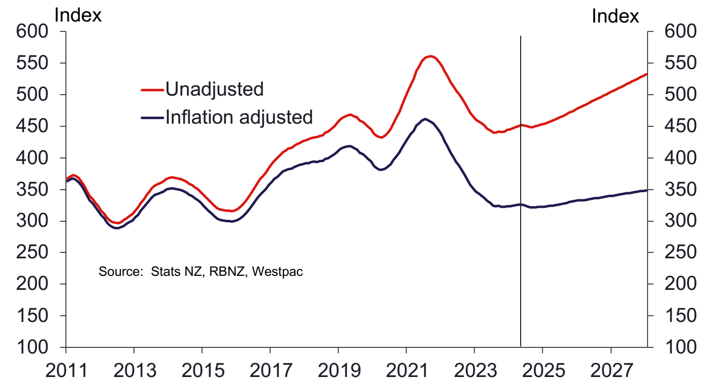
Focus will revert to China in coming years.

- Even so, prices remain relatively low compared to history. Much of that is due to sluggish Chinese demand, with consumers in China opting for cheaper lamb cuts or alternative proteins like pork and chicken. Competition from cheap Australian lamb is also a factor.
- Looking forward, we think that Chinese consumer demand for lamb will recover, and that will translate into higher prices over next couple of years.

Value of sheep meat exports to key markets – March year end



Sheep export prices – world price index



HORTICULTURE

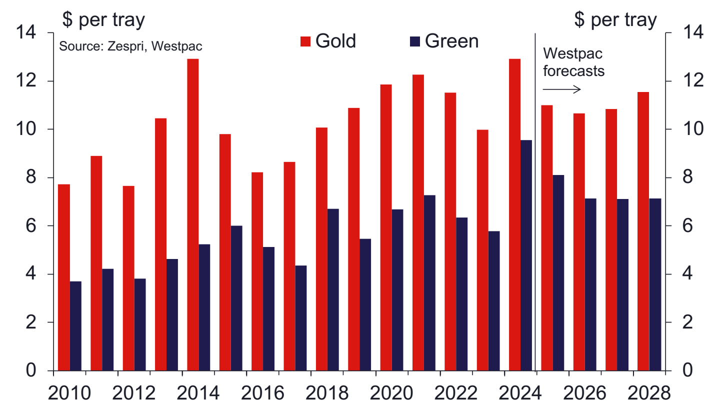
Increased production to boost Kiwifruit growers.

- The 2024 kiwifruit crop of just over 190m trays is larger than the 133m trays exported in 2023. Last year's production was affected by adverse weather events, including cyclone Gabrielle.
- Demand for kiwifruit is set to remain strong. Prices though should dip slightly as supply from New Zealand, China, Greece and Italy, increases. Competition from seasonal summer fruits in coming months is also likely to dampen prices.
- That said, volume effects should outweigh prices effects, and that should mean better orchard gate returns on a per hectare basis.

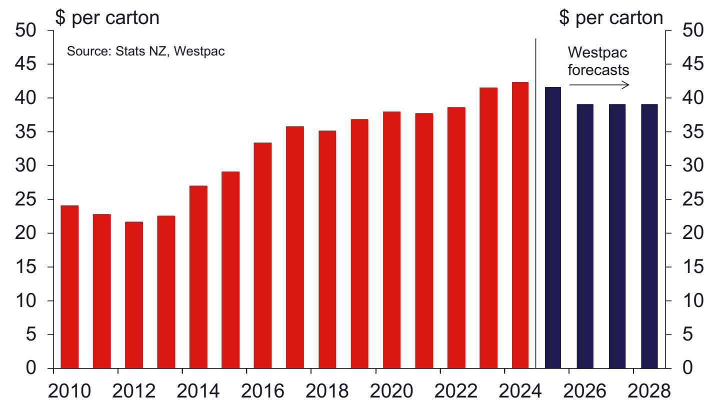
Apple growers also to benefit from gains in production.

- Conducive growing conditions last summer have resulted in an improved harvest for 2023/24. Although still down on past levels, this latest harvest represents a partial recovery from cyclone Gabrielle.
- Nevertheless, the lingering impacts of cyclone Gabrielle have been reflected in smaller fruit size, which has meant a lower than anticipated export crop.
- New Zealand's production runs countercyclical, which means that demand for its apples is likely to remain strong in key export markets. That should support prices.
- That said, we still expect prices to tilt lower over the coming year, as growing capacity recovers further, production rises and size of fruit increases. Over time, increased volumes are likely to translate into better orchard gate returns for growers.

Kiwifruit – Orchard gate returns per tray



Apple prices



FORESTRY

Export market for logs to remain soft in 2025, stronger in 2026.

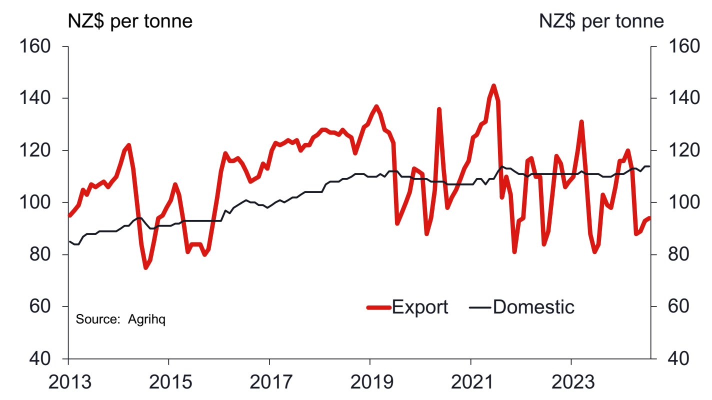
- Soft export log prices reflect ongoing difficulties facing China's residential and non-residential building sector.
- A seasonal decline in building activity in China is also helping to keep a lid on export prices. Wet weather conditions in some areas have also reduced activity.
- That said, there has been a small tick up in export prices recently as log buyers in China have sought to rebuild port level inventories. Stronger manufacturing activity may be providing some limited support.
- Chinese usage has slowed to about 55k cubic metres per day. That has meant fewer log carrying ships making the trip from New Zealand.
- We expect export log prices to move largely sideways well into 2025 and will only really pick up in 2026 when Chinese demand recovers.

Domestic market for logs is set to weaken further.

- Reduced harvesting rates because of weakness in the export market and poor weather conditions are helping to largely maintain log prices in the domestic market.
- Domestic demand for logs is weakening. That reflects a slowdown in building activity. With consent issuance having fallen substantially, further weakness is likely.
- That is likely to mean less logs going into the domestic market over the coming year, and less revenue for forestry owners.

Export log prices – world price index

Export log prices – world price index



INPUT COSTS

Pace of input cost increases continues to ease.

- Looking across all farm types, rural costs rose 1.6% over the year to June 2024. That compares to 2.2% increase for the year ending March 2024. That's well down from the peak of 15.6% in the year to September 2022.
- Costs on sheep and beef farms rose 2.2% over the year to June 2024, while those on dairy farms nudged 0.8% higher. Orchardists saw costs rise by 3.2%.

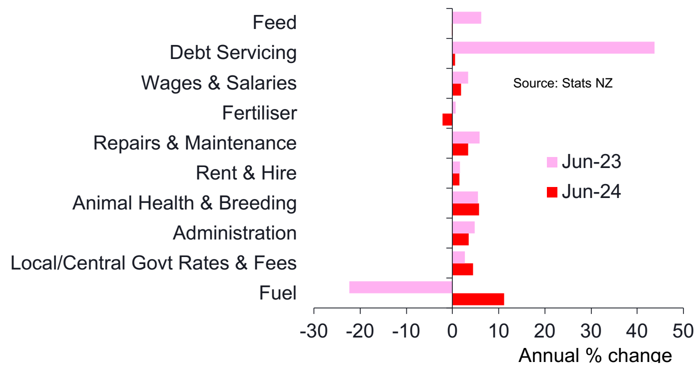
Debt servicing costs are set to dampen further input cost increases.

- Lower input cost inflation in large part reflects a much smaller rise in debt servicing costs. With monetary policy in an easing cycle, debt servicing costs are likely to contract further over coming quarters.
- Categories with a large weighting, such as feed, fertiliser as well as wages and salaries have either started to contract or are posting smaller increases. By contrast, fuel prices rose by 11% over the year to June 2024, although they still remain below levels seen in the latter part of 2023.

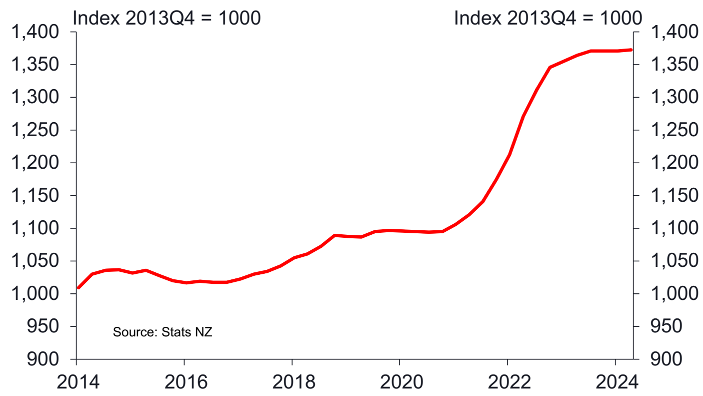
On-farm profitability remains under pressure.

- While input cost increases have moderated, costs are now 28% higher than they were pre-Covid and have easily outpaced growth in prices received by farmers.
- As a result, farmers and growers continue to experience pressure on margins, with some – especially those with high debt loads – likely to be facing losses.
- Looking ahead, an expected pickup in prices, particularly for dairy, beef and sheep meat, should deliver some relief, as will lower interest rates.

Change in level of farm input costs



Change in level of farm input costs



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