more give, less take

Rural Commodities Wrap

February 2016

Photo: Mai Thai

Highlights

Most Australian agricultural markets started the year in broadly stable territory, with the lower Australian dollar supporting local prices. The NAB Rural Commodities Index was up 0.8% in AUD terms in January and our forecasts point to Australian agricultural prices trending generally higher in AUD terms in 2016, despite challenging international conditions.

January brought rain to many areas which saw a dry 2015. Rainfall was generally above average in southern Australia, although parts of western Queensland and much of the top end saw below average falls. The Bureau of Meteorology's latest three month outlook points to good autumn rainfall across most of the continent but more challenging conditions in the top end.

2016 got off to a bad start in global equity and commodity markets but despite these heightened global risks, our outlook for the Australian economy is essentially unchanged. We continue to anticipate further recovery across the non-mining economy. We have revised down our AUD forecasts for 2016 and we now see the AUD falling as low as USD 0.66 in Q2 2016.

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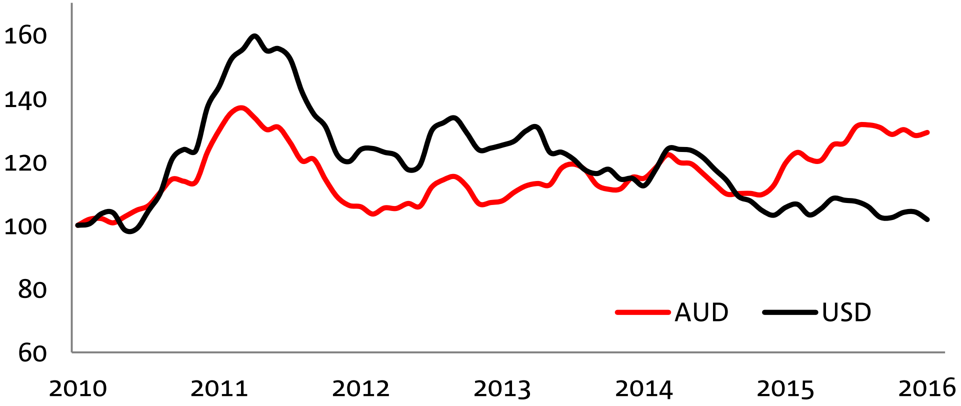
Photo: Carl Davies CSIRO

Rural commodity prices and production

NAB Rural Commodities Index

Index value, January 2010 = 100



Monthly price changes, production and price forecasts

	Month on month price change (AUD)	2015-16 annual production change	2015-16 annual price change (AUD)
Wheat	▲ 1.4%	▲ 5.0%	▲ 1.6%
Beef	▲ 0.1%	▼ 8.9%	▲ 45.4%
Dairy	▲ 3.3%	▲ 0.2%	▲ 3.0%
Lamb	▲ 1.8%	▼ 4.0%	▲ 3.9%
Wool	▲ 1.9%	▼ 2.6%	▲ 13.7%
Sugar	▼ 1.0%	▲ 5.0%	▲ 7.6%
Cotton	▲ 1.2%	▲ 10.9%	▲ 14.9%

Source: NAB Group Economics, ABARES, Meat and Livestock Australia, Australian Pork, Ausmarket Consultants, BNZ, Australian Bureau of Statistics, Bloomberg and Profarmer.

Our forecasts point to Australian agricultural prices trending higher in AUD terms in 2016, despite challenging international conditions. We forecast the NAB Rural Commodities Index to increase 12.5% (AUD) in 2015-16, supported by a lower AUD.

Beef prices have been hovering at record levels and the Eastern Young Cattle Indicator broke through the 600c/kg mark in mid-January. However, with volumes down after a prolonged period of elevated slaughter, export values are likely to contract in 2016-17. In the medium term, we expect increased competition from South American beef producers in the key US market. Wheat should find some support from the lower AUD amid plentiful global supply and low global prices. We forecast dairy prices to increase moderately despite tumult on global dairy markets last year and forecasts of slow growth in global prices.

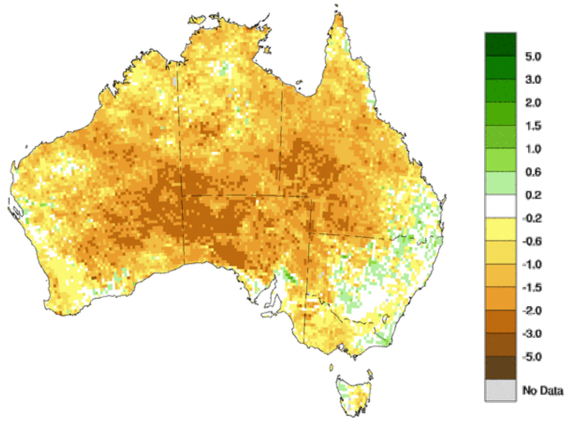
Overall, the NAB Rural Commodities Index was stable in January - up 0.8% in AUD terms but off 2.3% in USD terms.

NAB's Rural Commodities Index includes 28 commodities (wheat, barley, sorghum, rice, oats, canola, chick peas, field peas, lupins, wool, cotton, sugar, wine grapes, beef, lamb, pork, poultry, dairy, apples, bananas, oranges, mangoes, strawberries, broccoli, carrots, lettuce, potatoes and tomatoes). The index is weighted annually according to the gross value of production of each industry in Australia.

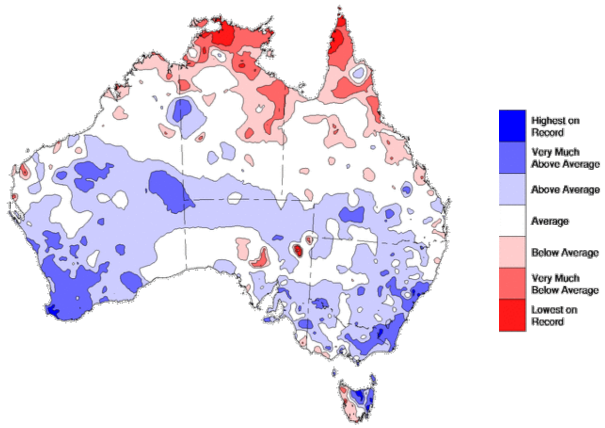
The outlook for production depends in part on how much rain we see coming into autumn. El Niño made conditions difficult in parts of Australia last year but the latest rainfall outlook points to a wetter than average autumn. This points to a potential upside in production for grains and dairy, although we continue to forecast a contraction in cattle slaughter for herd rebuilding.

Climatic conditions

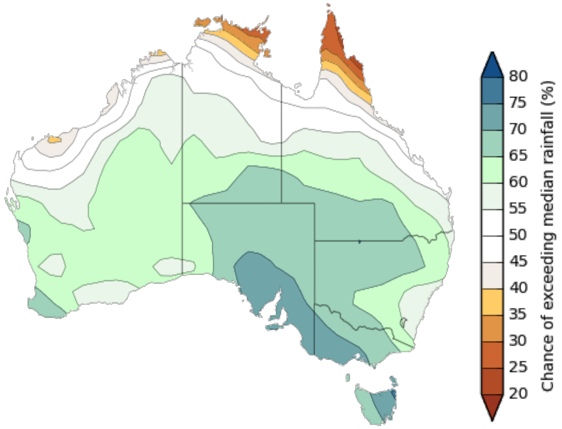
NDVI Anomaly
Six months to 30 December 2015



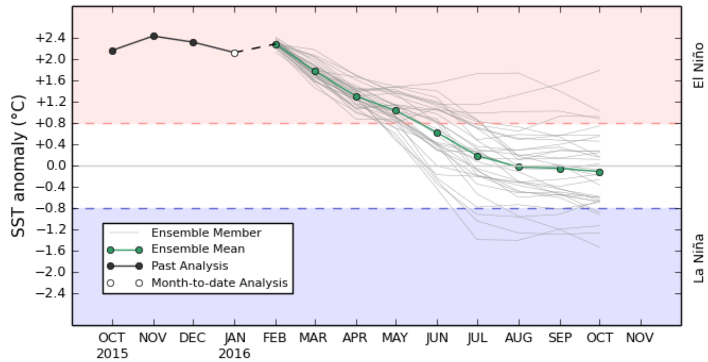
Australian rainfall deciles
January 2016



Three month rainfall outlook
February to April 2016



BoM POAMA El Niño outlook model
Monthly mean NINO34



Source: Bureau of Meteorology

The Bureau of Meteorology's three-month outlook to April projects above average rainfall across much of the continent, with the notable exception of the top end. Recent rainfall has followed this trend, with much of south-eastern Australia and south-western Western Australia enjoying above average falls, but Cape York and northern NT missing out.

Looking to next season, the Bureau of Meteorology's models suggest that El Niño will subside by late autumn this year and that conditions will tend closer to neutral in the spring. While earlier modelling had shown a move close to La Niña, this appears less likely in the latest results.

Rainfall was below to well below average across much of the continent in 2015, although most of New South Wales, the Northern Territory and parts of outback Western Australia experienced average to above average rainfall.

The Bureau of Meteorology's Normalised Difference Vegetation Index (NDVI) anomaly for the last six months of 2015 showed that throughout most of Australia, vegetation is less green than the long run average for the period.

Economic update

NAB Australian economic forecasts

Per cent change calendar year on year

	2015	2016	2017
GDP growth	2.3	2.7	3.0
Private consumption	2.6	3.0	2.4
Unemployment rate (year end)	5.8	5.6	5.5
Consumer Price Index (core)	2.0	2.6	2.6
RBA cash rate (year end)	2.0	2.0	3.0

NAB global economic forecasts

Per cent change calendar year on year

	2015	2016	2017
China	6.9	6.7	6.5
United States	2.4	2.3	2.3
Euro zone	1.4	1.7	1.9
Emerging East Asia	3.6	3.6	3.8
Japan	1.6	1.1	0.9
Advanced economies	1.9	2.0	2.1
Emerging economies	4.5	4.5	4.8
World GDP	2.9	3.0	3.3

Source: NAB Group Economics

For more detail, see our Global and Australian Forecasts.

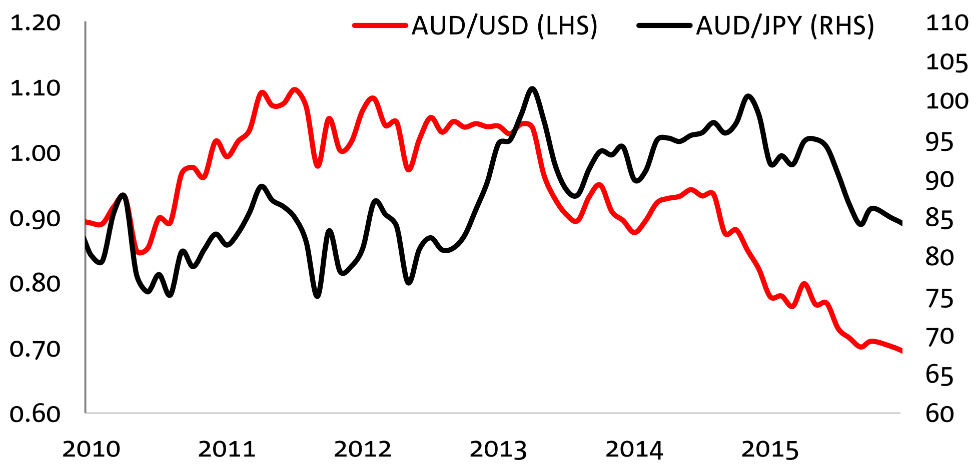
2016 got off to a bad start in global equity and commodity markets. Although the biggest falls since end 2015 have been in oil and Chinese equities, the price decline has been broad-based, while volatility has also increased across markets.

We have lowered our 2016 global forecasts to 3.0% (from a revised down 2.9% in 2015) in the face of a continuing sharp recession in Brazil, lower commodity prices, global equity market uncertainty and rising spreads – weakness in late 2015 in the USA has also not helped. Global growth remains sub-trend as the slowdown continues across many emerging market economies. Conditions remain mixed in the big advanced economies with solid upturns in the UK and the US alongside weakness in Europe and Japan, and this divergence is being reflected in monetary policies/ The latest bout of financial market volatility and sliding commodity prices further illustrate the risks, which have become more weighted to the downside. Nor do we see much sign of a pick up in 2017 (3.3% forecast). These numbers remain significantly lower than recent IMF revised (down) global forecasts.

Despite these global risks, the outlook for the Australian economy is essentially unchanged and we continue to anticipate further recovery across the non-mining economy. The AUD (now expected to depreciate to USD 0.66 by Q2 2016) will continue to act as a pressure valve, the tilt towards services activity will support employment, and lower petrol prices will support the cash flow position of most households and businesses. Resource export volumes will remain strong, although the associated income and government revenue will of course be challenged by low commodity prices. For the RBA, unless financial market volatility translates into substantive negative real economic outcomes offshore, the central bank is likely to remain on the sidelines and observe developments.

Exchange rates

Monthly exchange rate movements



We see the currency tracking lower in Q1 2016. We have revised down our AUD/USD forecasts to 0.67 in Q1 2016 (previously 0.68), climbing to 0.69 at the end of 2016 (previously 0.70). The AUD is now expected to reach as low 0.66 at the end of Q2 2016.

However, we note that the majority of the adjustment in the AUD occurred in 2014 and 2015 and we do not see the AUD providing the same level of support to local prices this year.

NAB FX strategy targets

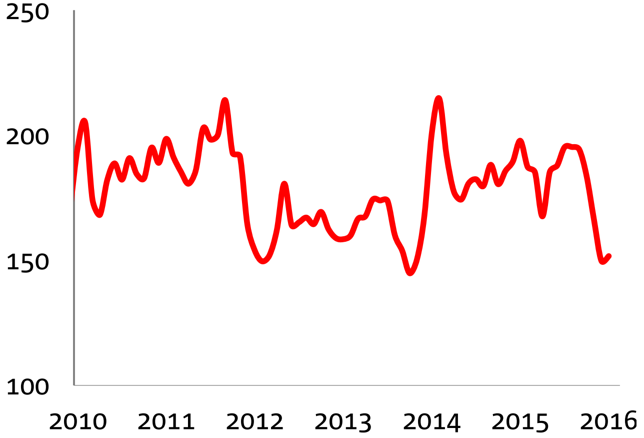
	2016Q1	2016Q2	2016Q3	2016Q4	2017Q1	2017Q2	2017Q3	2017Q4
AUD/USD	0.67	0.66	0.68	0.69	0.69	0.70	0.72	0.73
NZD/USD	0.62	0.60	0.61	0.61	0.61	0.62	0.63	0.65
USD/JPY	120	120	121	121	123	124	124	123
EUR/USD	1.09	1.07	1.06	1.07	1.07	1.08	1.09	1.10
USD/CNY	6.60	6.70	6.75	6.80	6.80	6.75	6.75	6.70

Source: NAB

Farm input prices

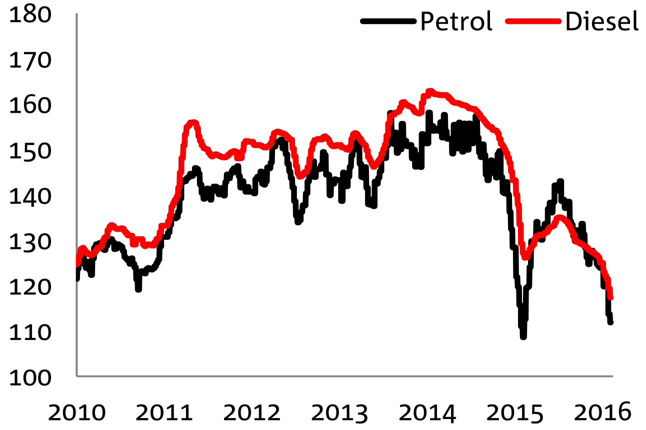
NAB Fertiliser Index

Index value



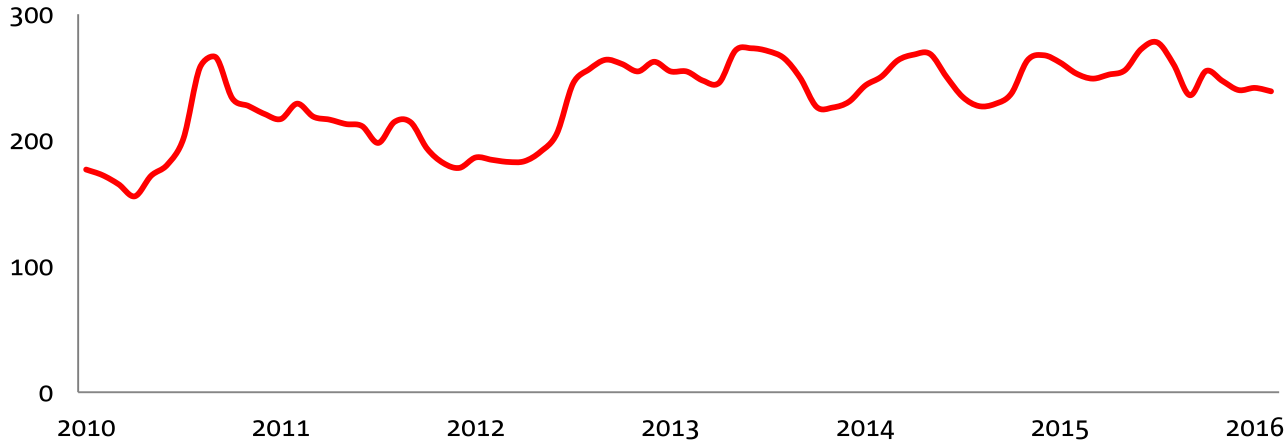
National average fuel prices

AUc/litre



NAB weighted feed grain price Index

AUD/tonne



Source: Bloomberg, Australian Institute of Petroleum, Profarmer and NAB Group Economics

Global fertiliser prices have continued to fall, although the lower AUD has blunted some of this impact in Australia. Overall, the NAB Fertiliser Index finished 2015 24.3% (AUD) lower than the start of the year. In January 2016, the index was up slightly (1.3%). The index is comprised of natural gas, urea and DAP.

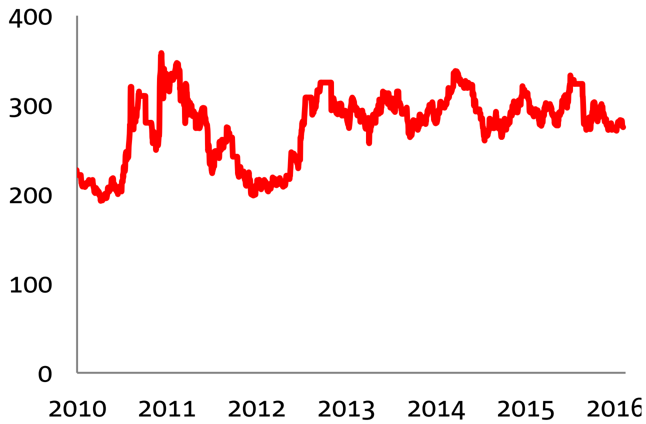
National average petrol prices also fell in response to a downturn in global crude oil prices in the new year but again the impact has been mitigated by a lower AUD. In January, national petrol prices averaged 118.95AUc/litre while diesel averaged 121.59AUc/litre. This is a 4.5% and 3.4% decline on December respectively.

Weighted feed grain prices were up slightly in January (up 0.7%), following falls in November and December. While major feed grains have continued to trade at subdued prices on global markets, the lower AUD has kept domestic feed prices higher.

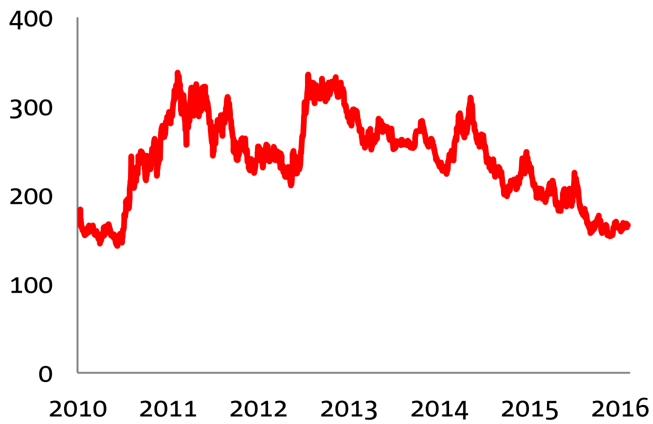
NAB's weighted feed grain price indicator includes feed wheat, barley, oats and sorghum. Three quarters of the indicator is made up of feed wheat and barley.

Wheat

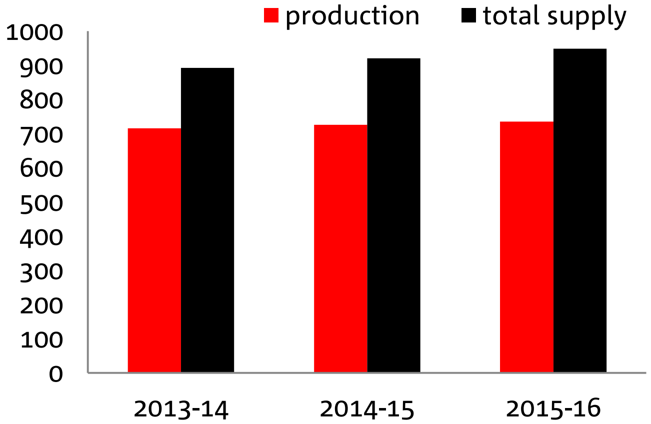
Generic 1st milling wheat
Eastern Australia, AUD/tonne



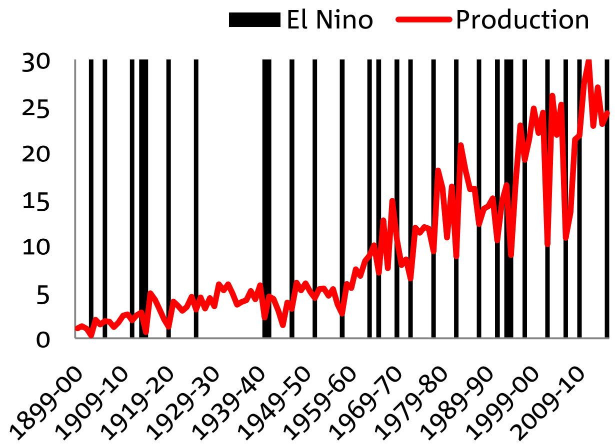
CBOT Hard Red Winter wheat
USD/tonne



USDA forecast world wheat supply
Million tonnes



Australian wheat production
Million tonnes



Source: Bloomberg, Profarmer, USDA, Australian Bureau of Statistics, ABARES and NAB Group Economics

Prices

Global wheat prices fell in 2015 in response to very strong global wheat supply. For 2016, we do not see a significant upside for wheat prices in USD terms as the USDA continues to forecast record supply this season.

However, AUD priced wheat has remained in a much narrower band since 2012 as the depreciation of the AUD continues to support prices. While prices are not exceptionally high by historic standards, the lower AUD has provided a buffer against a patchy Australian wheat season in 2015-16. Generic 1st Eastern Australian milling wheat was up 1.4% (AUD) in January.

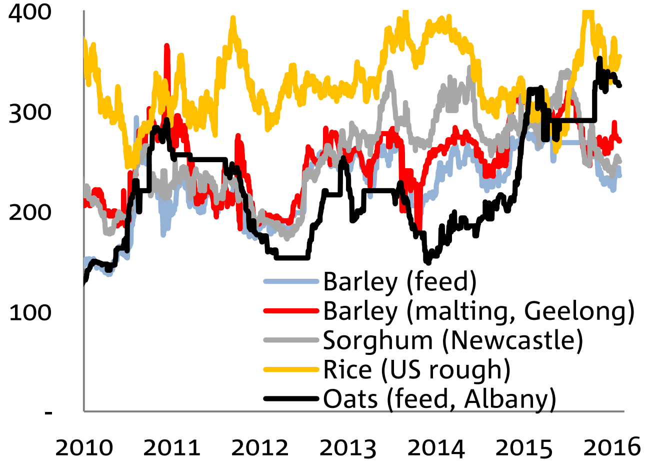
Production

ABARES reports that the 2015-16 wheat crop totalled 24.2 million tonnes. This was above our estimates last year, owing largely to strong production in NSW (up 16.3%) and QLD. Conditions were much patchier elsewhere.

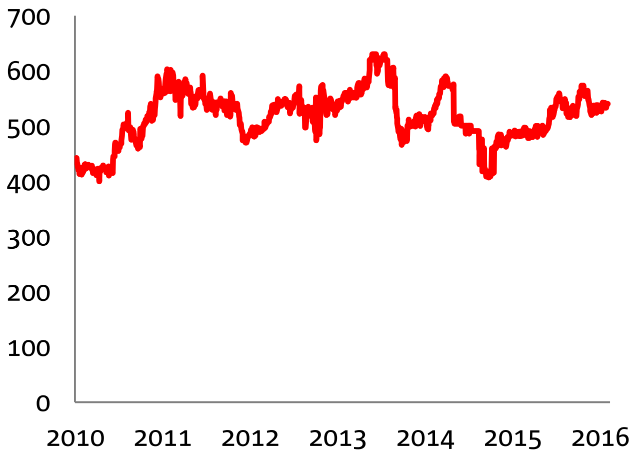
As we draw closer to autumn sowing, producers will be looking for soil moisture to give some confidence to plant larger areas. So far this year, major wheat regions have mostly enjoyed good rainfall. The latest three month climate outlook projects above average rainfall, pointing to decent plantings for the coming season.

Other broadacre crops

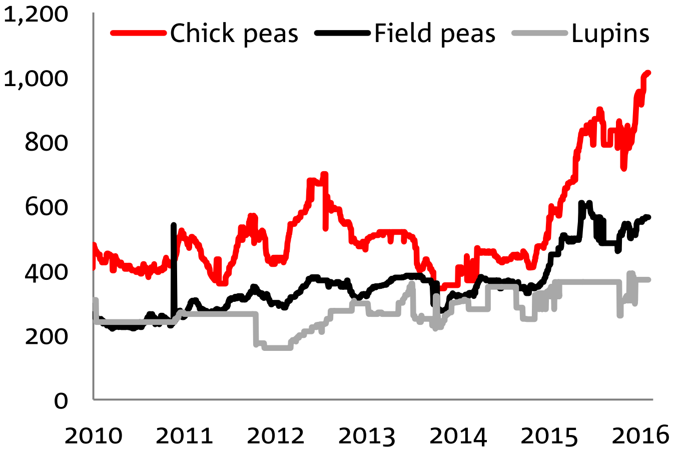
Selected coarse grains
AUD/tonne



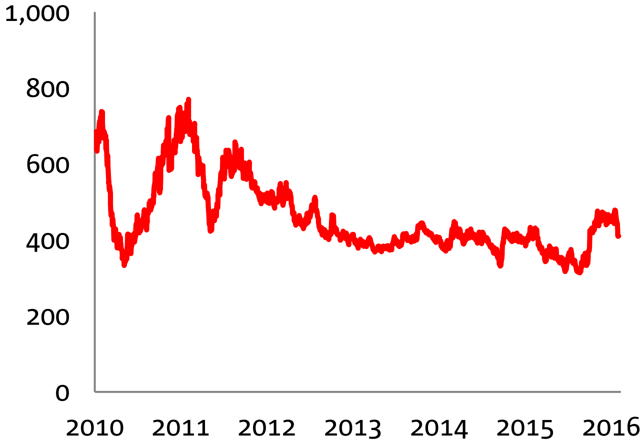
Canola, Newcastle NSW
AUD/tonne



Selected pulses
AUD/tonne



ICE no.11 sugar
AUD/tonne



Source: Bloomberg, Profarmer and NAB Group Economics

AUD coarse grain prices were mostly higher in January. Sorghum (Newcastle) was up 1.4% while barley (feed, generic) was up 1.9%. Rice was up strongly (5.0%). Meanwhile oats were almost unchanged at -0.2%.

Domestic canola was slightly higher (up 1.0% in AUD terms) in January. The 2015-16 Australian canola crop is likely to be lower this season based on lower plantings.

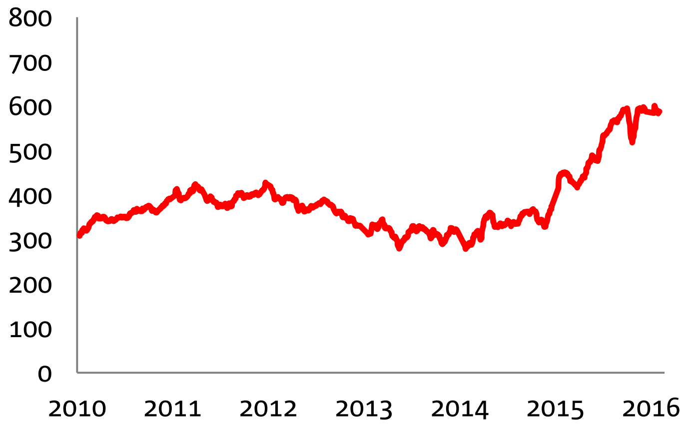
Chick peas' stellar run, which saw prices surge from less than AUD500/tonne at the end of 2014 to over AUD1,000/tonne this month, continues seemingly unabated amid difficult growing conditions in India. Chick pea prices surged 8.0% in January while field peas and lupins were also higher.

Global sugar prices fell in January (ICE no.11 sugar was down 1.0% (AUD) following strong momentum in the second half of 2015, when lower production, combined with domestic policy factors in Brazil, a major sugar producer, saw sugar prices rise almost 29% (AUD).

Beef

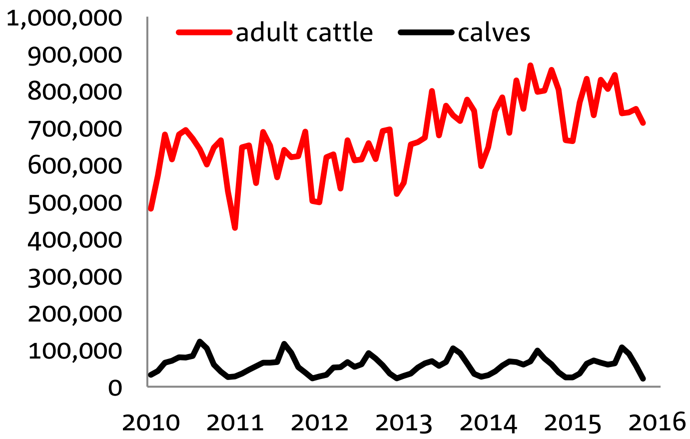
Eastern Young Cattle Indicator

AUc/kg



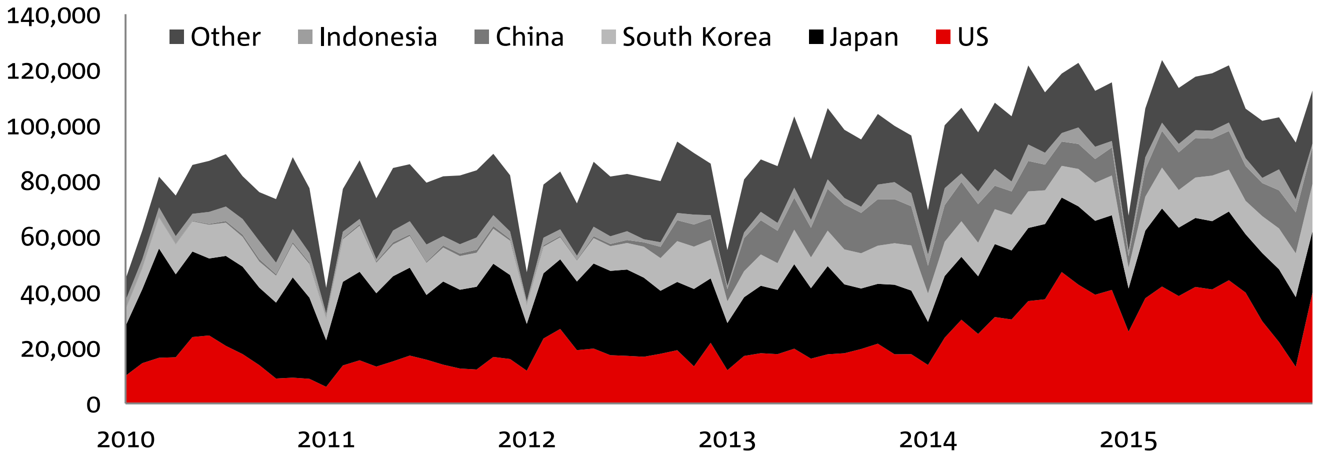
Monthly cattle slaughter

Head, Australia



Monthly Australian beef exports

Tonnes



Source: Meat and Livestock Australia and NAB Group Economics

Beef prices have been hovering at record levels and the Eastern Young Cattle Indicator broke through the 600c/kg mark in mid-January. However, with volumes down after a prolonged period of elevated slaughter, export values are likely to contract in 2016-17.

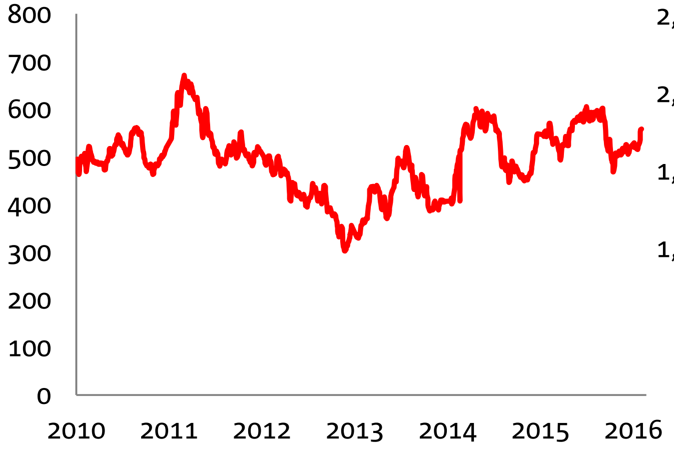
The Eastern Young Cattle Indicator (EYCI) was virtually unchanged in January – up 0.1% (AUD) in January. On a monthly basis, this is the third month that prices have risen.

In export volume terms, the second half of 2015 saw a pull-back from exports to the US (Australia's biggest beef export market), as cattle slaughter slowed from very elevated levels as stock became scarcer. This followed a significant expansion in exports to the US that began in early 2014 in response to the drought in the US.

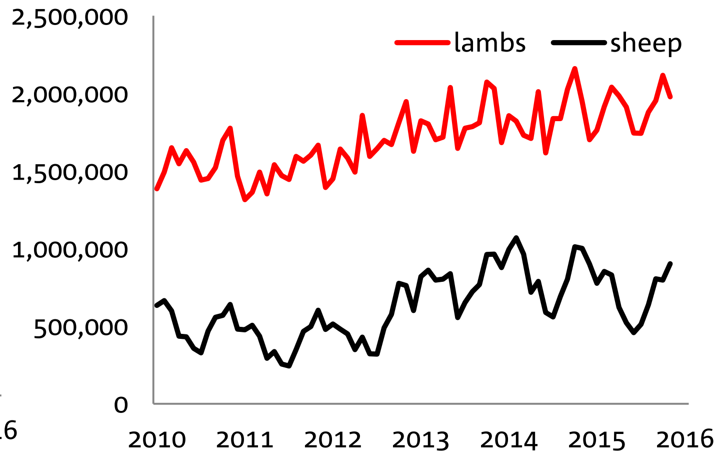
The US beef market has been volatile, reflected in lower 90cl beef prices even in AUD terms since late last year. US producers continue to rebuild their herds following the drought. Given recent rains in much of Australia, prices are likely to be kept high by producers looking to restock and rebuild herds depleted amid drought, rather than price growth in export markets. Beyond 2016, higher exports from Brazil and Argentina are likely to increase competition in the US market.

Lamb, pork and poultry

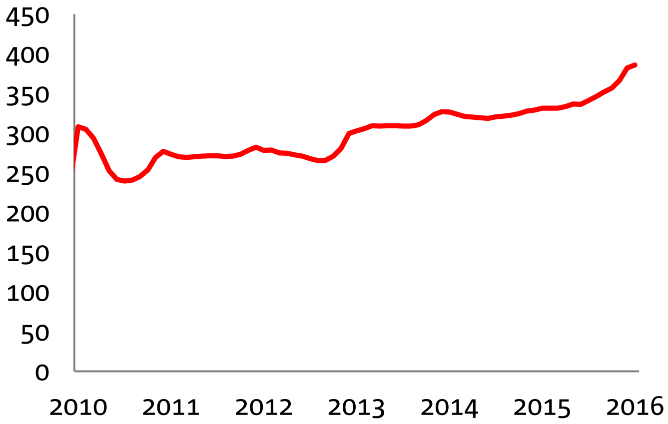
Eastern States Trade Lamb Indicator
AUc/kg



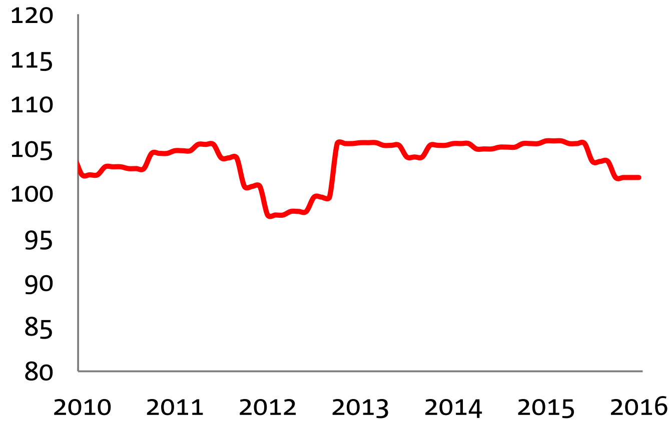
Monthly sheep and lamb slaughter
Head, Australia



Australian pork price indicator
AUc/kg



ABS poultry price index
Index points



Lamb prices have continued to edge back up (the Eastern States Trade Lamb Indicator was up 1.8% in AUD terms in January), broadly reflecting normal seasonal variation as well as good rains improving sentiment following concerns associated with a dry spring in some areas.

Australian wholesale pork prices (measured as an average of buyer and seller prices for eastern seaboard 60.1-75kg animals) continue to strengthen, up 1.0% in January to 385.67AUc/kg. While the industry generally sees relatively little volatility in prices, there has been a sustained upward trend which has strengthened since mid-2015. With Australia increasingly importing pig meat products, the lower AUD is a possible driver of this trend.

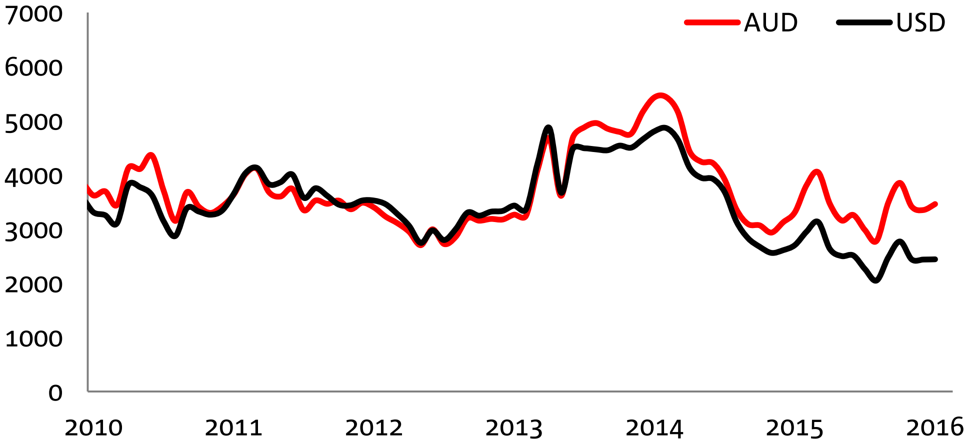
While we do not collect wholesale poultry price data, retail prices have remained reasonably stable since late 2012. However, national retail prices fell 1.7% in the December quarter 2015 (the most recent data available).

Source: Meat and Livestock Australia, Australian Pork, Australian Bureau of Statistics and NAB Group Economics

Dairy

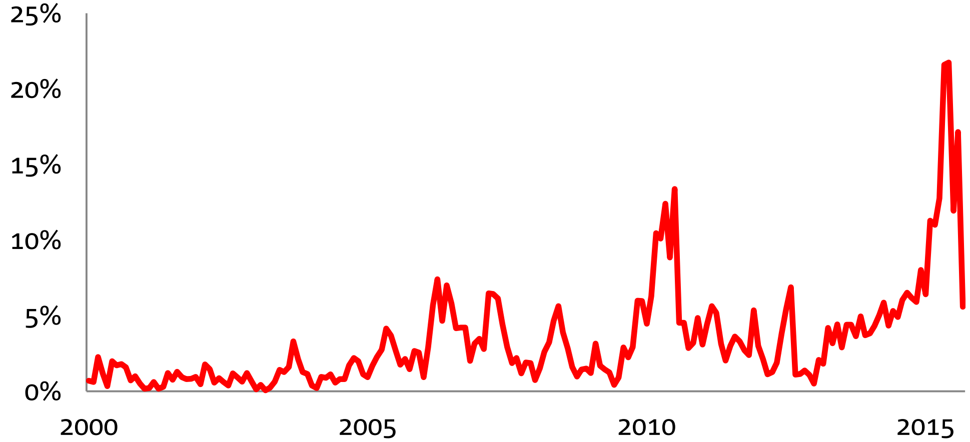
NAB weighted dairy export price indicator

$/tonne



Share of Australian feed exports destined for China

Per cent, excludes cereals



Source: Australian Bureau of Statistics, Global Dairy Trade and NAB Group Economics

For more detail, see our Dairy In Focus report, released last month.

International dairy markets saw a tumultuous 2015, with lacklustre demand, particularly from China, combined with adequate supply of most dairy products sending prices on a rollercoaster. However, Australian producers have been shielded from much of this tumult by a lower Australian dollar and a large and relatively stable domestic market.

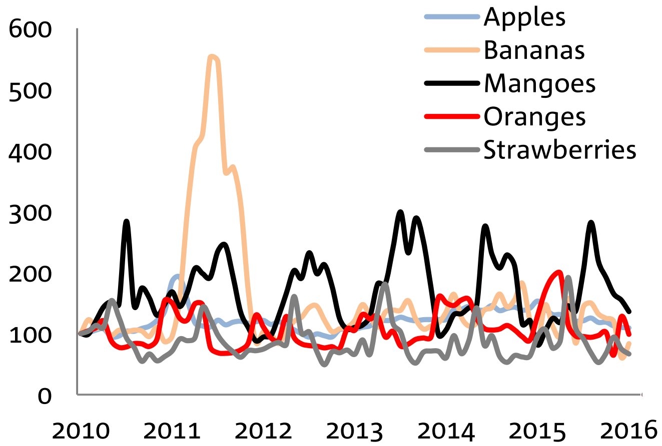
NAB's measure of dairy export prices, based on Global Dairy Trade (GDT) auction results, is weighted by the quantity of Australian exports for whole milk powder, skim milk powder, butter and cheese. The indicator rose 3.3% in January despite weakness in Global Dairy Trade auctions, supported by a lower AUD.

Looking to the coming year, we see a slow recovery in global prices, with moderately higher Chinese demand but continued strength in global supply. While weather was a challenge in many dairy regions in 2015 (especially Victoria, parts of South Australia and Tasmania), the outlook for 2016 points to a decent autumn break, which should see improved pasture growth and less need for supplementary feed.

Horticulture

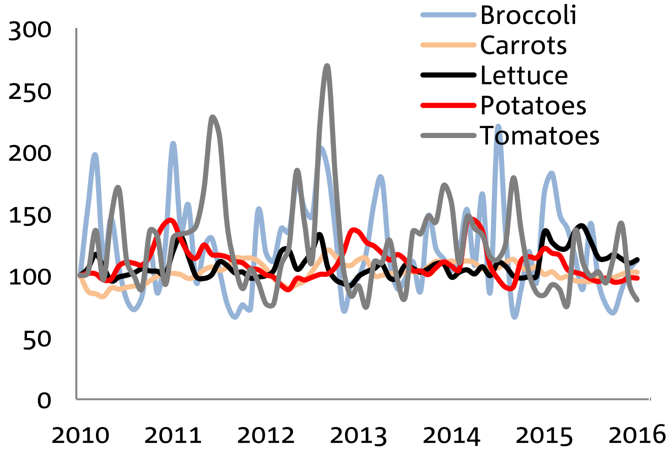
Wholesale fruit prices

Index value, Sydney and Melbourne



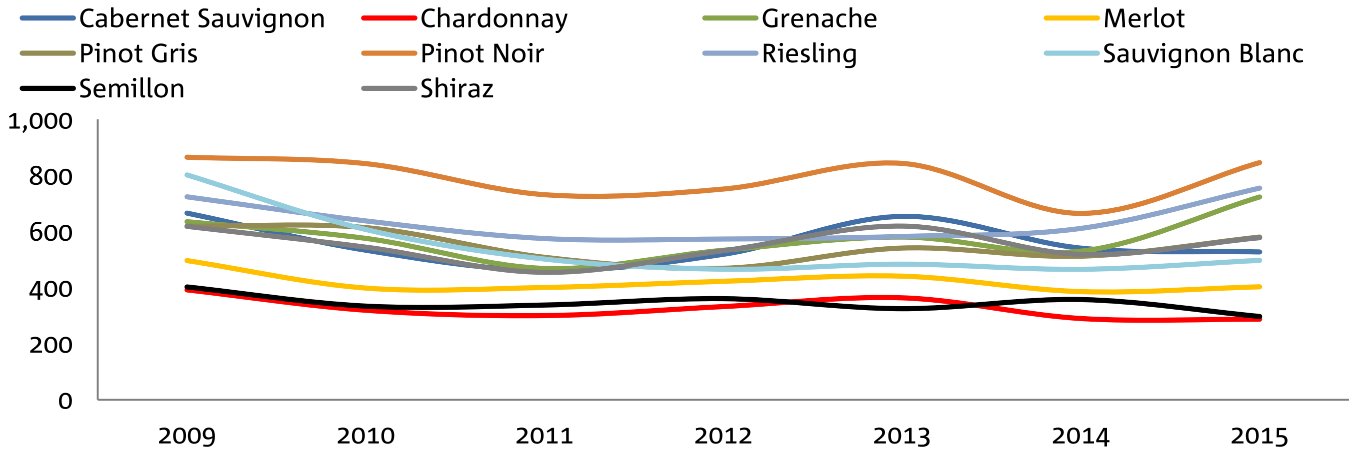
Wholesale vegetable prices

Index value, Sydney and Melbourne



NAB weighted wine grape prices

AUD/tonne



Source: Ausmarket Consultants, Wine Australia and NAB Group Economics

We produce wholesale price indices for fruit and vegetables, based on data from the Melbourne and Sydney wholesale markets.

Fruit prices fell 3.0% in January, led by lower orange mango and strawberry prices, although bananas were more expensive and apples were steady. The index stands at 100.0 for January 2016 (note January 2010 = 100), the lowest since early 2012.

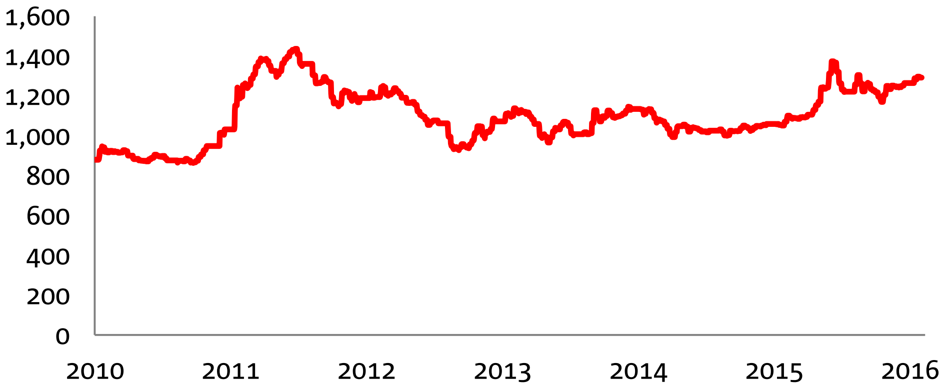
Vegetables were likewise lower, off 1.5% in January. The index stands at 100.0 for January 2016 (note January 2010 = 100), the lowest since September 2015.

Wine Australia's 2015 Price Dispersion Report, released in July 2015, shows a rebound in prices for several more expensive varieties. Grenache, Pinot Noir and Riesling all gained (36%, 13% and 24% respectively). However, lower priced varieties such as Chardonnay, Semillon and Merlot fared generally worse.

Fibres

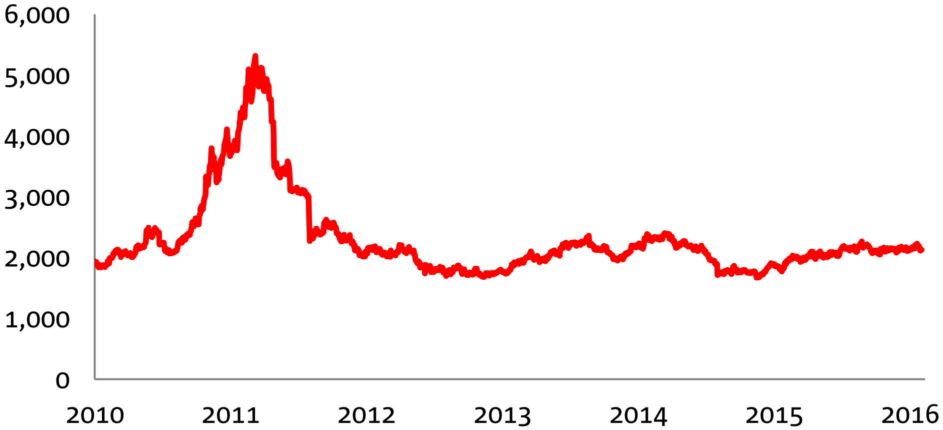
Wool – Eastern Market Indicator

AUc/kg



Cotlook A index

AUD/tonne



Source: Bloomberg and NAB Group Economics . Photo: CSIRO

Wool has started 2016 on a reasonably strong note. While the Eastern Market Indicator was up a moderate 1.9% in January, this is a continuation of an upward trend since October 2015 and is approaching the levels seen in mid-2015, which were the best in several years.

Global cotton prices were moderately higher in January, with Cotlook A up 1.2% (AUD).


Photo: CSIRO

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