

RURAL COMMODITIES WRAP

SEPTEMBER 2016

Author Phin Ziebell, Agribusiness Economist

Crop progress in the Clare Valley, South Australia, September 2016 | Photo Meredith Gould

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CONTACTS

Phin Ziebell
Agribusiness Economist
+61 (0) 475 940 662

Alan Oster
Chief Economist
+61 3 8634 2927

Riki Polygenis
H-O Australian Economics
+61 3 8697 9534

Khan Horne
General Manager
NAB Agribusiness

Kristin Kenny
Senior Consultant
+61 (0) 439 255 981

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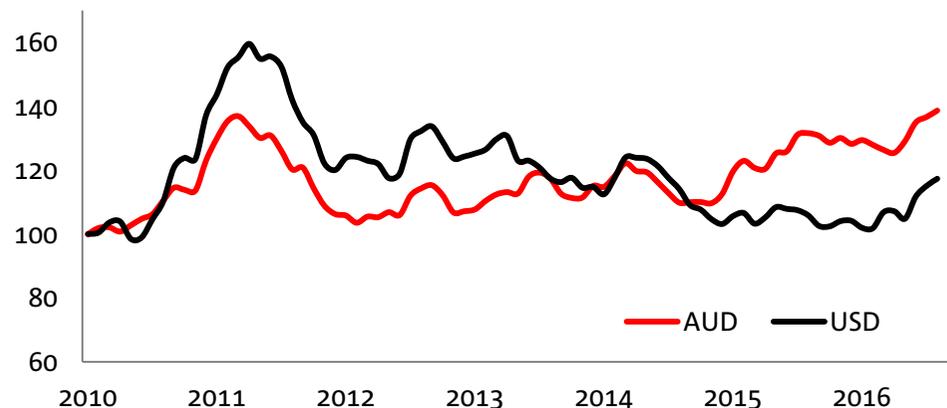
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RECENT RURAL COMMODITY PRICE MOVEMENTS

NAB RURAL COMMODITIES INDEX

Index value, January 2010 = 100



MONTHLY AUD PRICE CHANGES – SELECTED COMMODITIES

	July 2016	August 2016	September 2016 (partial)
Wheat	▼ 6.3%	▼ 5.4%	▼ 3.5%
Beef	▲ 6.4%	▲ 7.1%	▲ 0.5%
Dairy	▼ 2.0%	▲ 6.8%	▲ 21.5%
Lamb	▲ 1.8%	▼ 2.0%	▼ 1.4%
Wool	▲ 2.1%	▼ 0.4%	▲ 0.5%
Sugar	▲ 0.3%	▲ 0.1%	▲ 4.2%
Cotton	▲ 7.5%	▼ 2.4%	▼ 3.1%
Index	▲ 1.3%	▲ 1.5%	NA

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

Spring has brought not only considerable rain to parts of the country but also a further uptick in the NAB Rural Commodities Index. The index was up 1.5% in August and is on track for a moderate increase in September. This steady increase masks discrepancies across commodities, with weakness in major grain markets offset by strength in red meat and a rebound in dairy prices. Dairy has been standout performer following considerable weakness over the last two years – the NAB weighted dairy export indicator gained 6.8% in August and 21.5% in September.

Rain across eastern Australia has put winter crops on track for a bumper season, although flooding and waterlogging in some areas is a real concern, as is frost damage in Western Australia. The Bureau of Meteorology's outlook is for a neutral to wetter than average finish to spring, which could pose some risk of quality downgrades depending on how late the rain persists. Good rainfall has continued to drive restocker interest in red meat, with cattle prices remaining at record levels and lamb defying the usual spring price drop as producers retain more lambs.

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.

PRICE, PRODUCTION AND EXPORT FORECASTS

Our expectations for prices in the coming year have been revised in line with the AUD tracking higher at the end of 2016 than we previously forecast. This presents less support to local prices, exposing increased risks from challenging global grain markets.

Cattle prices are likely to come under pressure in 2017 in response to higher US supply and improved South American access, although we note that good rainfall in Australia is pushing restocker demand higher (and prices with it). Dairy has seen quite a rebound of late, although risks to the outlook remain.

Our outlook for agricultural production is highly reliant on the climate outlook. The Bureau of Meteorology is still on La Niña watch, but recent data show the likelihood of La Niña lessening and a move to neutral conditions and even slightly towards to El Niño in mid-2017. Nonetheless, the season has been generally very favourable so far and the three month outlook continues to forecast almost ideal conditions.

The table below outlines our latest outlook for production, prices and the value of exports. These estimates are contingent on estimates for production and export volumes, prevailing global prices and NAB's foreign exchange outlook.

PRODUCTION, PRICE AND EXPORT FORECASTS (AUD)

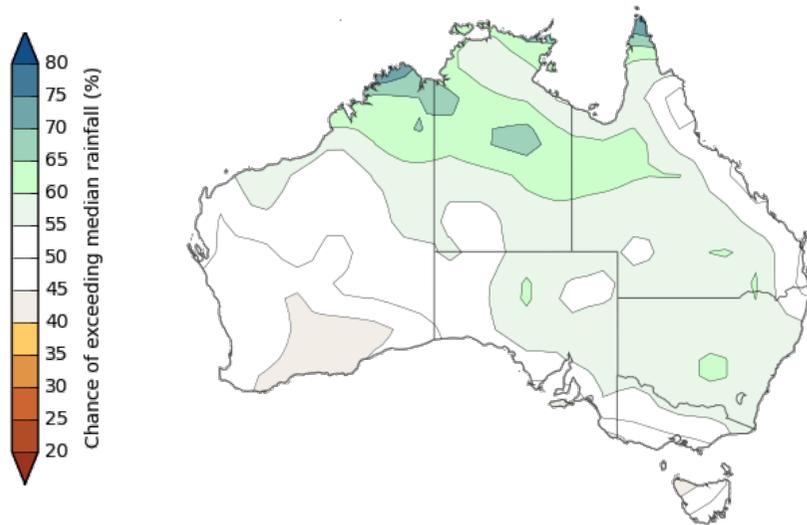
	Production change		Price change		Export value change	
	2015-16	2016-17	2015-16	2016-17	2015-16	2016-17
Wheat	▲ 1.9%	▲ 13.9%	▼ 2.7%	▼ 14.5%	▼ 7.8%	▼ 1.6%
Beef	▼ 12.0%	▼ 9.5%	▲ 43.7%	▲ 14.3%	▼ 6.5%	▼ 9.5%
Dairy	▼ 2.0%	▼ 2.3%	▼ 5.0%	▲ 12.0%	▲ 4.5%	▲ 9.4%
Lamb and mutton	▼ 1.2%	▼ 6.4%	▲ 4.7%	▲ 2.1%	▼ 6.9%	▼ 5.8%
Wool	▼ 5.4%	▼ 1.0%	▲ 14.4%	▲ 7.0%	▲ 4.1%	▲ 6.0%
Sugar	▲ 7.6%	▲ 3.7%	▲ 13.1%	▲ 25.1%	▲ 15.2%	▲ 28.4%
Cotton	▲ 12.1%	▲ 51.2%	▲ 11.2%	▲ 10.3%	▼ 18.7%	▲ 43.6%

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

CLIMATE OUTLOOK

THREE MONTH RAINFALL OUTLOOK

September to November 2016



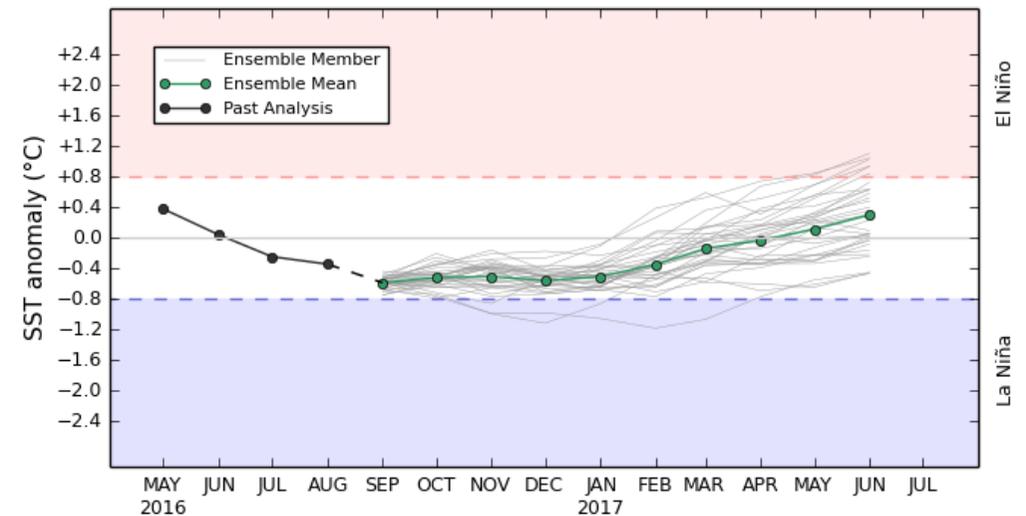
The Bureau of Meteorology (BoM) three month rainfall outlook to November points to generally average to well above average rainfall across northern and much of eastern Australia. However, Western Australia, Tasmania, much of Victoria, southern South Australia and coastal Queensland are expected to see more neutral conditions.

This outlook points to good grain growing conditions towards harvest, although the strong rainfall outlook across New South Wales presents the risk of crop downgrades if the rain persists into summer. Rainfall has also boosted sentiment in livestock industries, with cattle and lamb restocker interest continuing to be very strong.

Source: Bureau of Meteorology

BOM POAMA MODEL LONG-RANGE EL NINO OUTLOOK

Monthly mean NINO 3.4 – 11 September 2016



The Bureau of Meteorology's long range outlook for El Niño points to a return to neutral conditions, moving in the direction of El Niño by winter 2017. The BoM ENSO tracker remains on La Niña watch (placing the chance of a La Niña event at around 50%).

ECONOMIC UPDATE

NAB AUSTRALIAN ECONOMIC FORECASTS

Per cent change calendar year on year

	2016	2017	2018
Real GDP	3.0	2.8	2.6
Terms of trade	-2.4	-5.9	-7.4
Unemployment rate (year end)	5.6	5.7	5.6
Consumer Price Index (core)	1.6	1.8	2.0
RBA cash rate (year end)	1.5	1.0	1.0

NAB GLOBAL ECONOMIC FORECASTS

Per cent change calendar year on year

	2016	2017	2018
United States	1.5	2.1	1.9
Euro-zone	1.6	1.5	1.6
Japan	0.5	0.6	0.6
China	6.6	6.5	6.3
Emerging East Asia	3.5	3.6	3.5
World GDP	2.9	3.1	3.2

Source: NAB Group Economics

For more detail, see our [Global](#) and [Australian](#) Forecasts

How one assesses Australia's economic performance at present depends in large part on which industry / geography one looks at and whether the benchmark is in real or nominal terms.

The Australian economy grew at a year-ended rate of 3.3% in Q2, the fastest pace since mid-2012, thanks to a surge in government spending. In future, real GDP growth is expected to ease, most clearly in 2018 after the dwelling cycle has turned and resource exports no longer contribute to growth. Our forecasts are for real GDP growth of 3.0% on average in calendar year 2016, followed by 2.8% in 2017 and 2.6% in 2018. The unemployment rate is expected to hold steady through the forecast horizon at around 5.6-5.7%, a rate which indicates ongoing spare capacity in the labour market.

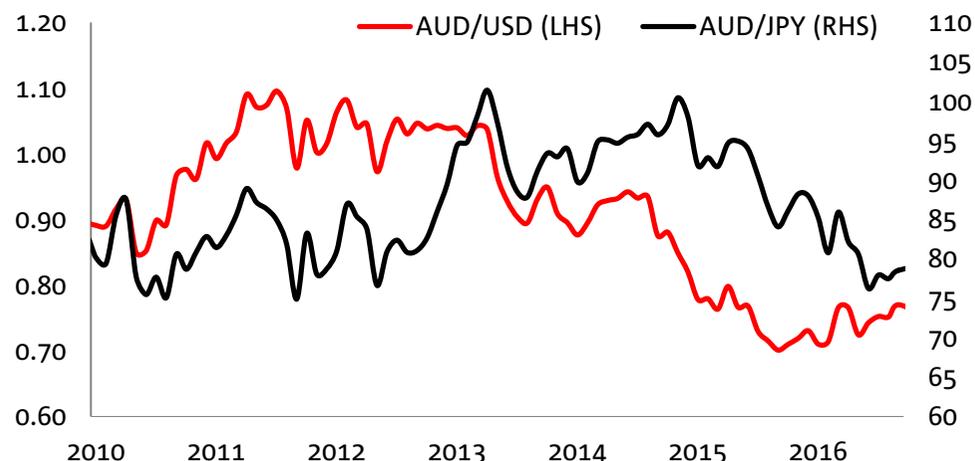
There is some downside risk to our near-term forecasts given the recent loss of momentum in indicators of household spending in particular, but also business conditions. These bear close watching.

Sluggish global growth was the focus of the latest G20 meeting, particularly protectionist trade measures, rising support for "populist" anti-globalisation political parties and the difficulty in persuading voters to support reforms needed to lift productivity and growth.

Despite signs of stabilisation in areas of the world where economic activity has been weak, there is little evidence of new growth engines appearing that could pull economic growth out of the doldrums. Consequently, we do not expect much improvement in global growth which should remain below trend.

EXCHANGE RATES AND INTEREST RATES

MONTHLY EXCHANGE RATE MOVEMENTS



September Fed inaction has re-enforced the AUD/USD range (0.7450 - 0.7750 on the wide). While the AUD remains overvalued on most metrics (including NAB's short term value model estimate) we see it likely to remain so for the time being.

Looking into 2017, our forecasts show the AUD falling to 0.72 by mid-year and 0.70 by end-2017. We see the AUD falling into the high 60s in 2018.

We expect two 25bp cuts to the cash rate in May and August 2017 (to a new low of 1%). Monetary policy deliberations may then turn to the possible use of nonconventional policy measures if the outlook deteriorates further, although that is not in our forecast. Additionally, persistent weakness in CPI inflation could potentially trigger a rate cut even sooner than expected.

NAB FX STRATEGY TARGETS

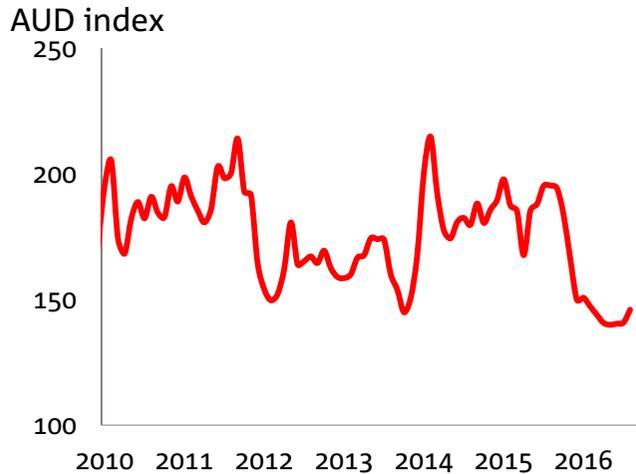
	2016Q4	2017Q1	2017Q2	2017Q3	2017Q4	2018Q1	2018Q2	2018Q3
AUD/USD	0.75	0.73	0.72	0.70	0.70	0.69	0.68	0.68
NZD/USD	0.72	0.70	0.68	0.67	0.67	0.68	0.68	0.69
USD/JPY	102	103	103	102	101	100	99	97
EUR/USD	1.12	1.10	1.09	1.07	1.06	1.06	1.07	1.08
USD/CNY	6.70	6.70	6.68	6.65	6.65	6.65	6.63	6.60
AUD TWI	63.6	62.7	62.0	60.4	60.2	59.9	58.0	57.5

Source: NAB

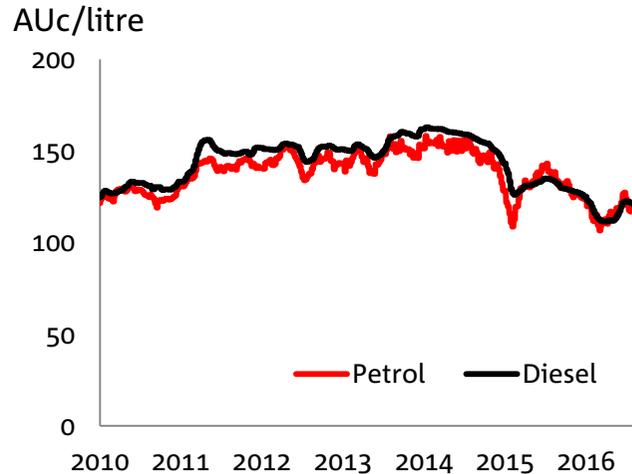
FARM INPUT PRICES



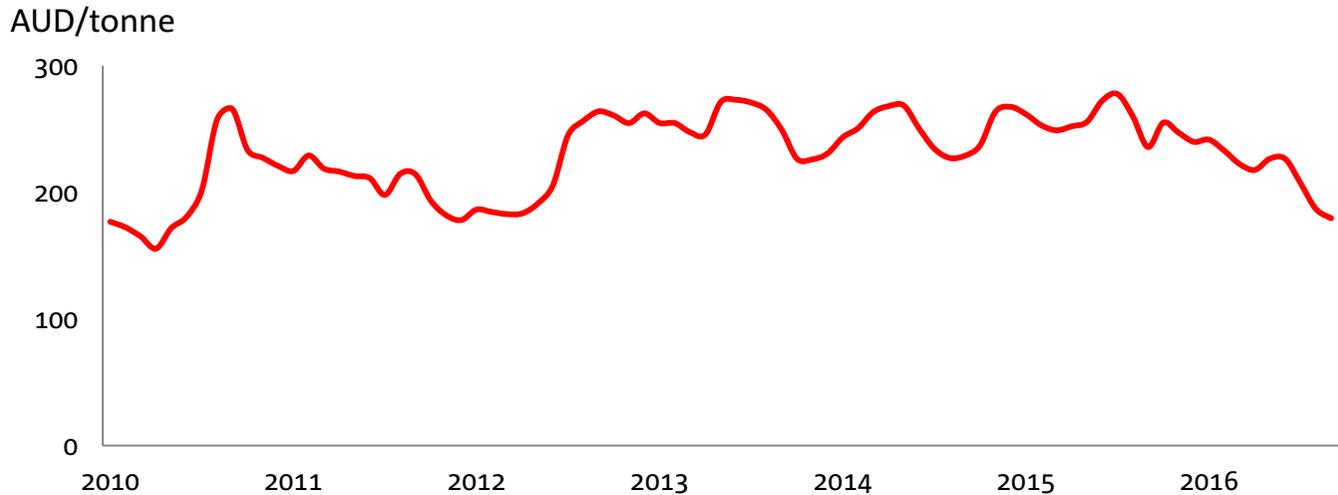
NAB FERTILISER INDEX



NATIONAL AVERAGE FUEL PRICES



NAB WEIGHTED FEED GRAIN PRICE INDEX



The drop in global fertiliser prices that began in earnest in September last year looks to have been arrested. August saw the NAB fertiliser index up 3.7% on higher DAP and urea prices. In September, DAP and natural gas have continued to strengthen, while urea is somewhat lower. This points to further upside in the coming months, although we note that prices remain at very low levels.

National average petrol prices were generally lower in August, but have strengthened somewhat in September. In August, petrol was off 4.2% to 113.8c/l while diesel fell 2.6% to 118.1c/l. The latest data show petrol at 117.3c/l and diesel at 117.6c/l.

Weighted feed grain prices continue to fall, in line with continued weakness on global grain markets. The NAB feed grain price index fell 9.8% in August and is off another 3.9% so far in September. We see strong signs that Australia is on track for a bumper winter crop. Combined with good pasture availability and global weakness, we expect further downside pressure in domestic feed grain markets into 2017. NAB's index includes feed wheat, barley, oats and sorghum. Three quarters of the indicator is made up of feed wheat and barley.

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

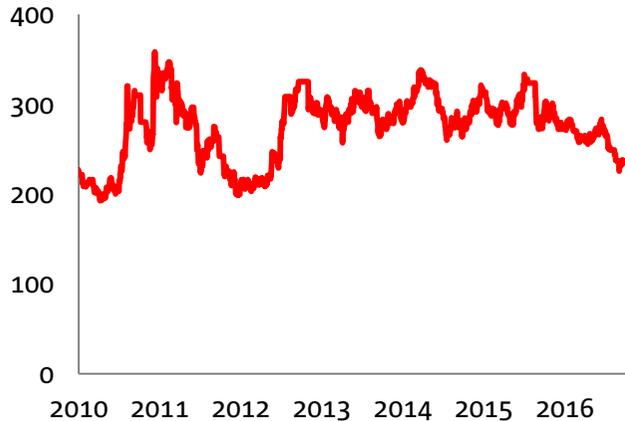


WHEAT



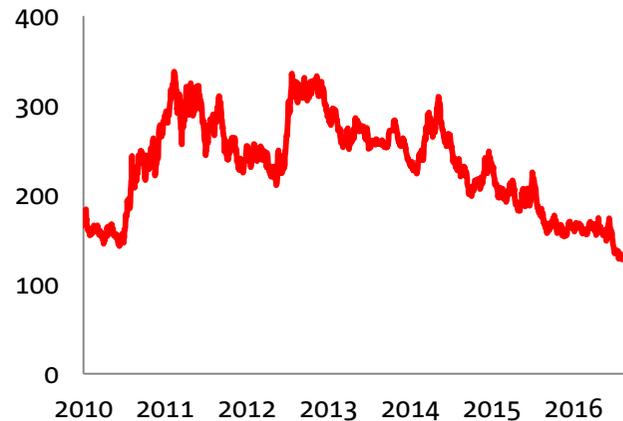
GENERIC 1ST MILLING WHEAT

Eastern Australia, AUD/tonne



CBOT SOFT RED WINTER WHEAT

USD/tonne



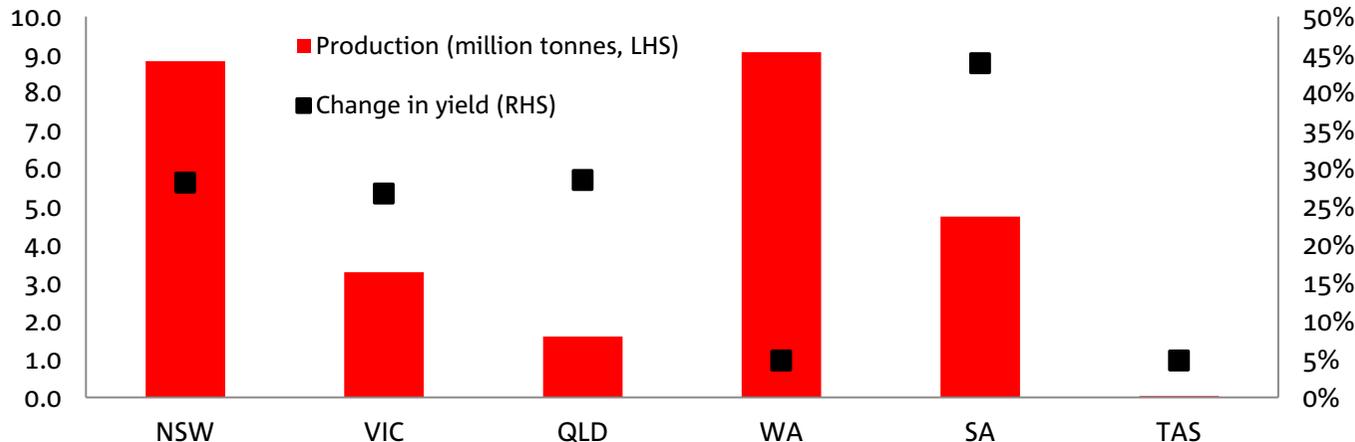
Prices

The steady downward trend in USD denominated global wheat prices over the last four years continues unabated. Global wheat supply remains plentiful. Combined with favourable shipping costs and low production costs in the Black Sea region, Australian competitiveness is coming under substantial pressure.

We have again downgraded our outlook for wheat prices, noting that the USDA continues to forecast strong global supply. Generic 1st Eastern Australian milling wheat was off 5.4% (AUD) in August and another 3.5% so far in September.

NAB CENTRAL CASE AUSTRALIAN WHEAT PRODUCTION OUTLOOK

Production and change in yield



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

Production

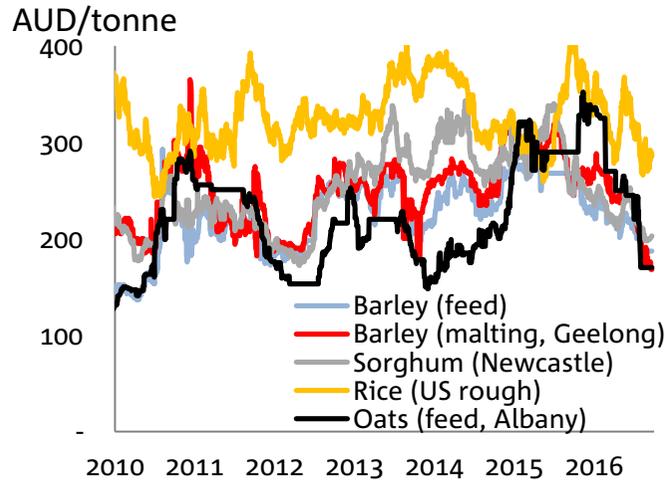
Spring has been generally wet to very wet in many areas, particularly in the south east. With this additional rain, our wheat forecasting indicator points to production of 27.6 million tonnes this season. However, there is every reason to suggest that production will be higher than this figure., A harvest in excess of 29 million tonnes is a real possibility, although water logging and rain damage on the east coast, combined with frost damage in the west present a risk to the upside.



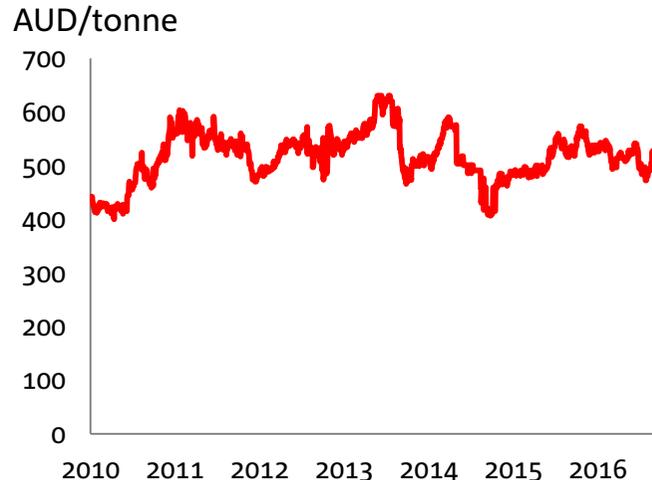
OTHER BROADACRE CROPS



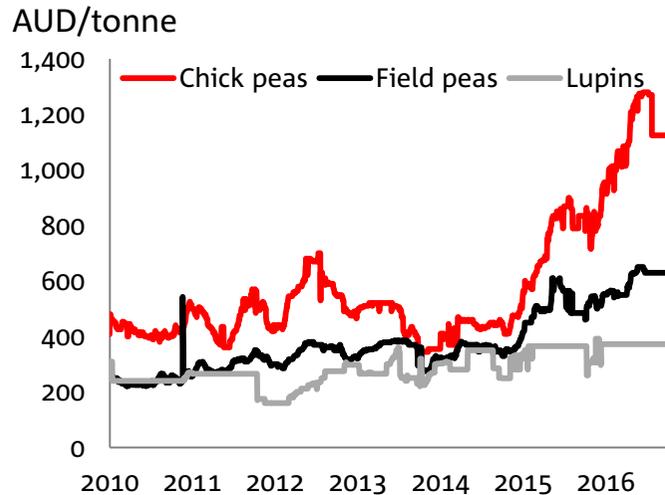
SELECTED COARSE GRAINS



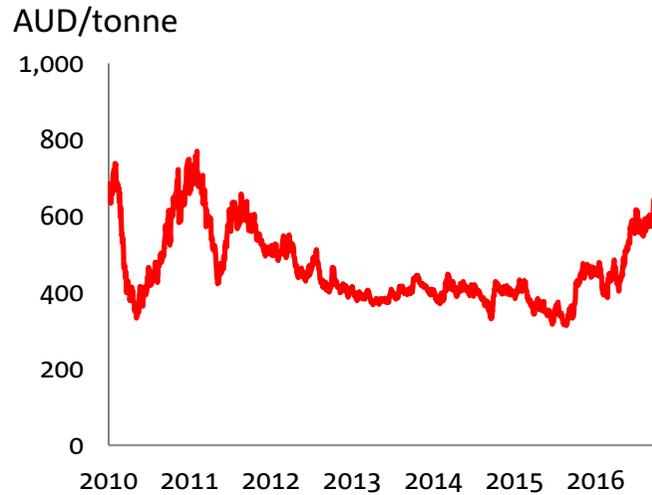
CANOLA, NEWCASTLE NSW



SELECTED PULSES



ICE NO.11 SUGAR



Source: Bloomberg, Profarmer and NAB Group Economics

Australian coarse grain prices have mostly followed broad trends set by wheat this year, reflecting a dependence on movements in the AUD. Recent data point to light trading of old season crop. Sorghum (Newcastle) was off 6.2% in August while barley (feed, generic) fell 7.7%. Rice and oats were 7.7% and 24.8% lower in AUD terms.

Domestic canola was up 1.7% in AUD terms in August. With canola remaining in the high AUD400s to low 500s over the last several months, those who planted canola should see a strong premium compared to wheat this season.

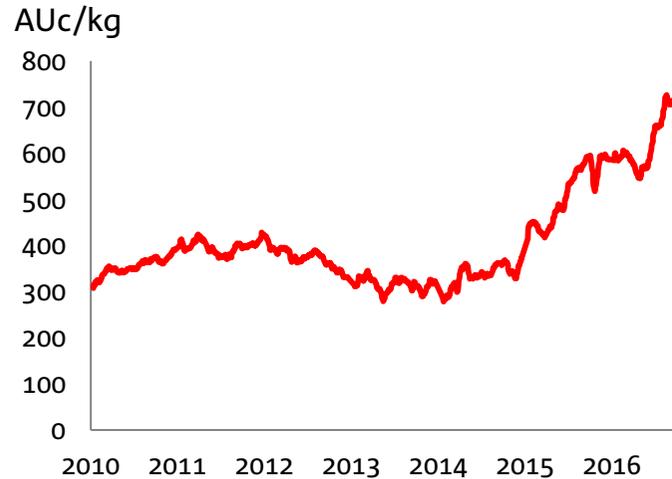
We continue to expect very favourable Australian pulses production this season, based on very good weather conditions and elevated planting. We remain circumspect when it comes to the outlook for prices. This is particularly the case for pulses predominantly destined for India, such as chick peas and lentils.

Global sugar prices have continued to surge amid global supply shortfall concerns. ICE no.11 sugar was steady in August, but is up 4.2% (AUD) so far this month. While prices have been volatile this year, we continue to expect higher prices, noting supply issues and improving global demand.

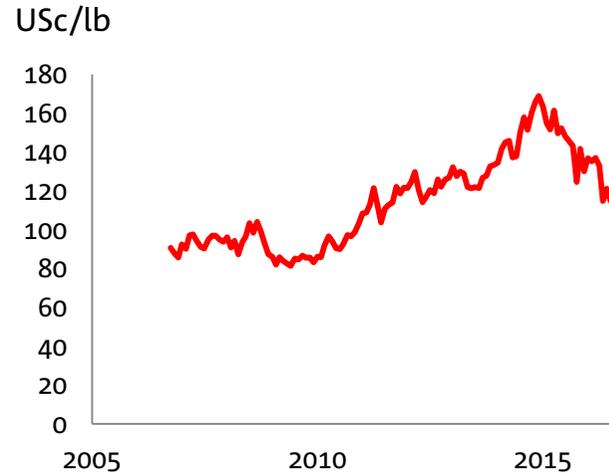




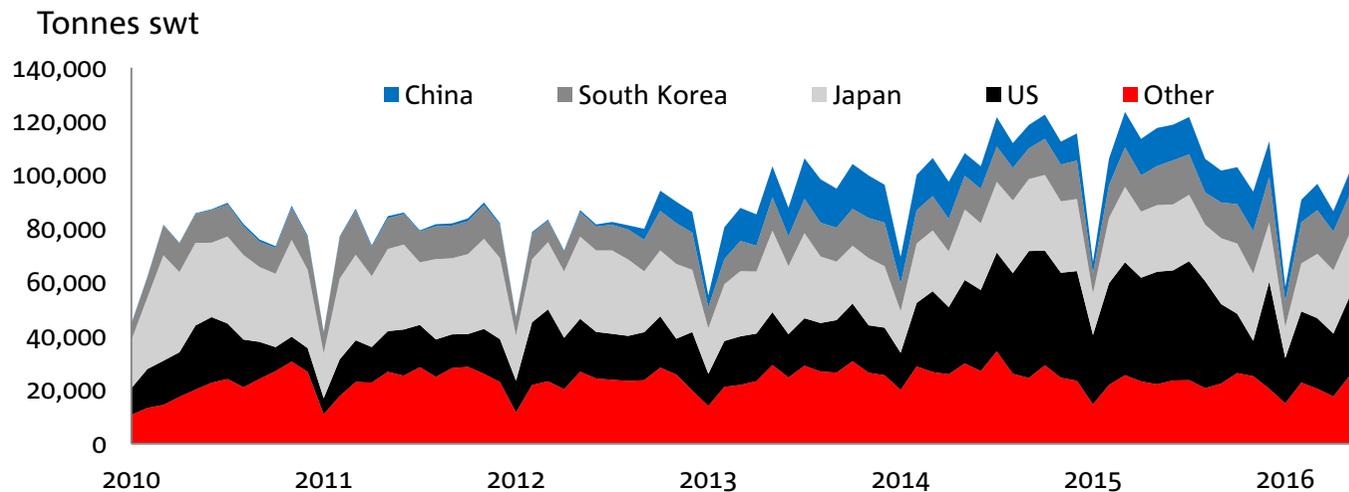
EASTERN YOUNG CATTLE INDICATOR



CME LIVE CATTLE FUTURE



MONTHLY AUSTRALIAN BEEF EXPORTS



Source: Meat and Livestock Australia and NAB Group Economics

Restocker demand is pushing cattle prices further and further into the stratosphere. The Eastern Young Cattle indicator rose 7.1% in August before stabilising in September. The indicator now stands at a scarcely fathomable 714.75AUc/kg.

While cattle prices are likely to stay high for the remainder of the year (especially if it keeps raining), the risks to the outlook into 2017 and beyond are increasing.

The US market in particular presents a sobering picture for the industry. Australian 90cl cow meat into the US averaged 555.71AUc/kg last week, in September last year it peaked at 739.54AUc/kg.

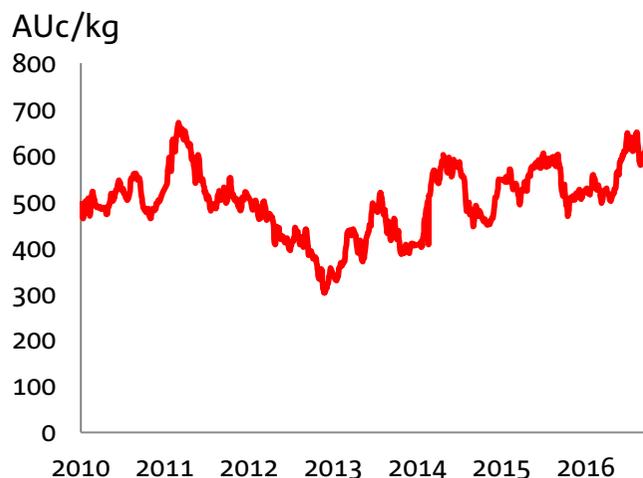
Meanwhile, US cattle futures on the Chicago Mercantile Exchange have fallen to five year lows.

The USDA forecasts that US beef production will increase 5.2% in 2016 and 3.4% in 2017. Low feed grain prices, especially for corn, have substantially improved input costs for US cattle producers. This will keep export prices under pressure, further compounded by increasing competitiveness from South America in key east and south-east Asian markets.

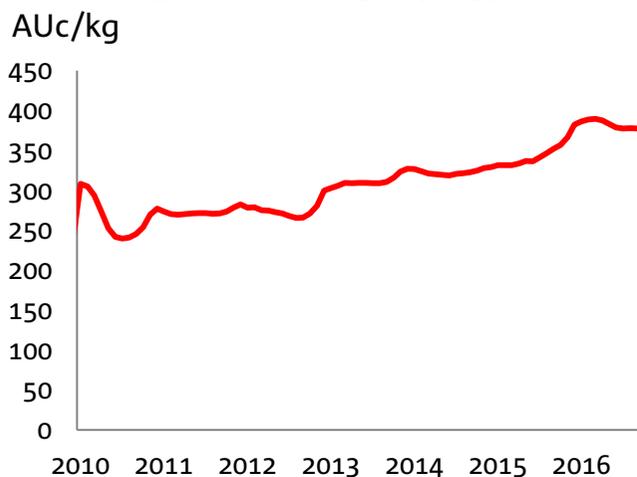
LAMB, PORK AND POULTRY



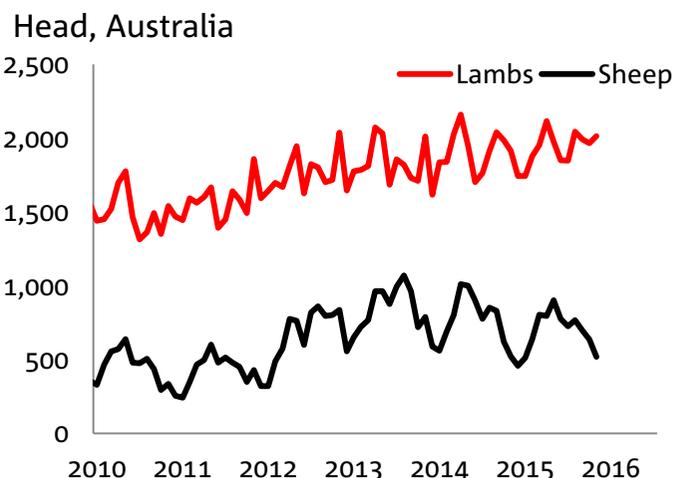
NATIONAL TRADE LAMB INDICATOR



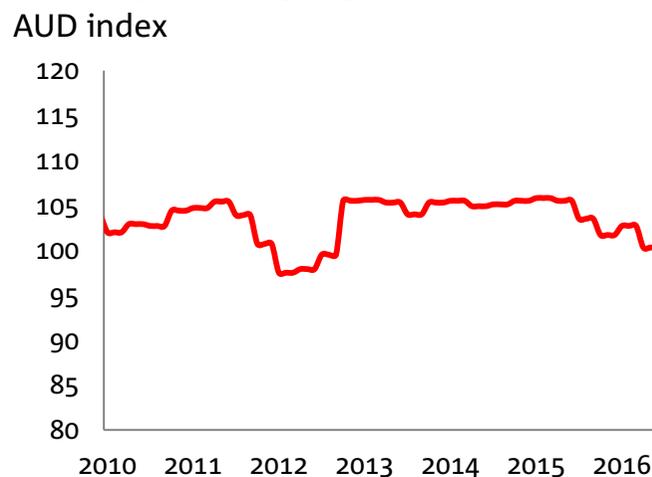
AUSTRALIAN PORK PRICE INDICATOR



MONTHLY SHEEP AND LAMB SLAUGHTER



ABS POULTRY PRICE INDEX



The Australian lamb industry has enjoyed broadly favourable conditions of late, and we remain upbeat in our assessment of the industry. Restocker demand has seen spring prices surprise on the upside and we continue to expect stable to moderately higher prices into next year, continuing a good run since 2013. We place lamb prices at 2.1% higher in 2016-17. Overall, we expect the value of lamb and mutton exports to fall 5.8% in 2016-17, reflecting lower volume.

Export markets for lamb are reasonably diversified, with the US and China accounting for a substantial volume. However, the Middle East remains a very important market, particularly for mutton and live sheep.

Australian wholesale pork prices (measured as an average of buyer and seller prices for eastern seaboard 60.1-75kg animals) look to have stabilised following some movement earlier in the year (albeit in an industry that generally sees relatively little volatility). Prices were up 0.1% in August but are down 0.1% for September to date.

While we do not collect wholesale poultry price data, retail prices have remained reasonably stable since late 2012. However, national retail prices fell 2.3% in the June quarter 2016.

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



NAB WEIGHTED DAIRY EXPORT PRICE INDICATOR

\$/tonne (export price, LHS)

AUD/kg milk solids (farm gate price RHS)

— AUD Index (LHS)

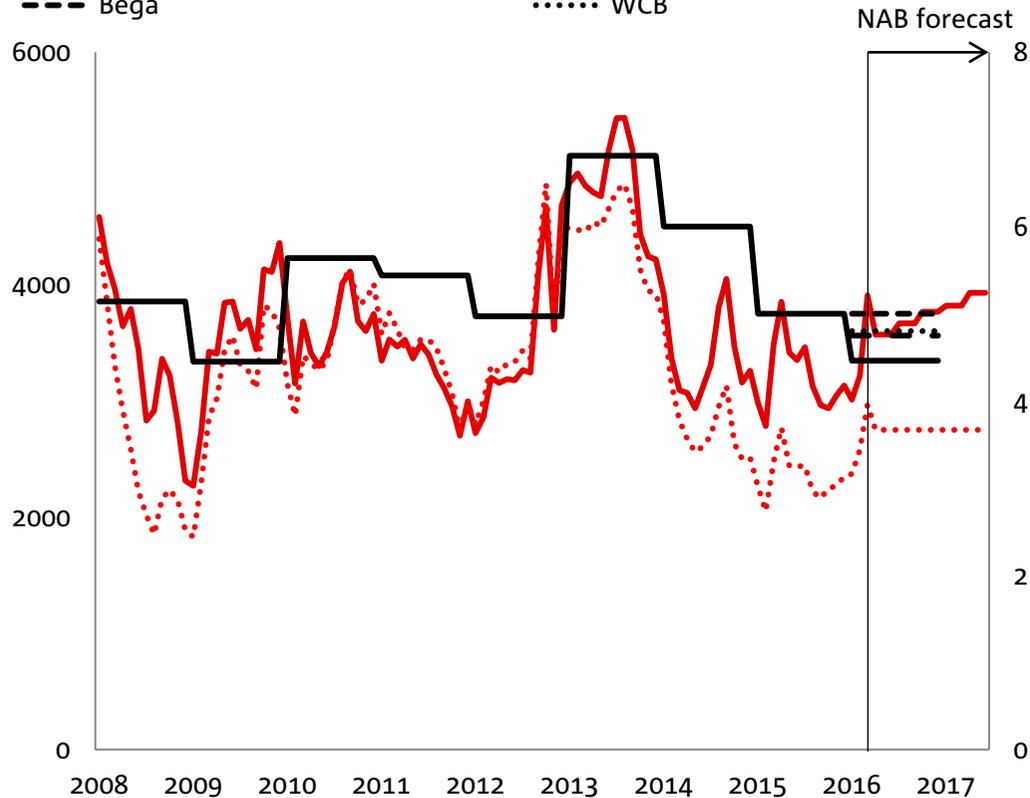
..... USD index (LHS)

— Murray Goulburn milk price (RHS)

— Fonterra

- - - Bega

..... WCB



While the dairy industry has come under sustained price pressure this year, recent Global Dairy Trade auction results have provided significant upside. The NAB weighted dairy export price indicator rose 6.8% in August and 21.5% in September, reflecting lower than anticipated supply from key exports New Zealand and the European Union. Our export indicator now stands at AUD3908.70/tonne – five months ago it was below AUD3000/tonne.

While we still see some concern in China, a key export market, recent developments are clearly of benefit to the industry and we have raised our forecasts accordingly. Even if prices remain at current levels in USD terms, our forecasts for a lower AUD should provide support locally.

Improved auction results are already having some impact at farmgate. This month, Murray Goulburn announced a step-up to \$4.46/kg milk solids. While competitors' farmgate prices are generally higher (such as Fonterra at \$4.75 and Warrnambool Cheese and Butter at \$4.80), it offers some scope for any further upside on global markets to be passed on to producers.

The progress of the season offers further comfort to producers – a wet start to spring in Victoria (which accounts for around two-thirds of national production) should see pastures in much better shape than last season coming into summer.

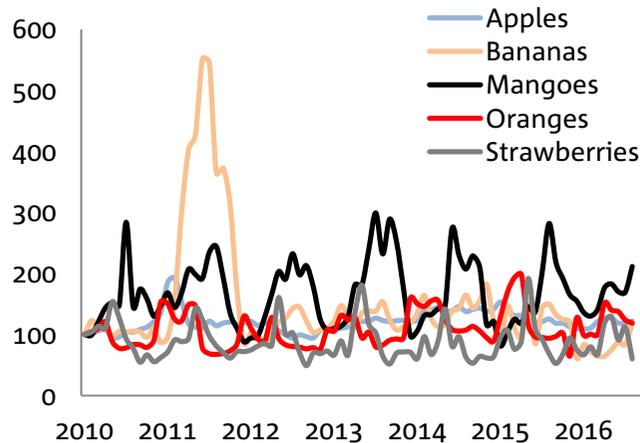
Source: Australian Bureau of Statistics, Global Dairy Trade, Dairy Australia, Fonterra, Murray Goulburn, ABC and NAB Group Economics

Note: chart shows Murray Goulburn farmgate prices (upper range for revised 2015-16 price) except 2008-09 which shows Dairy Australia's reported Victorian average value



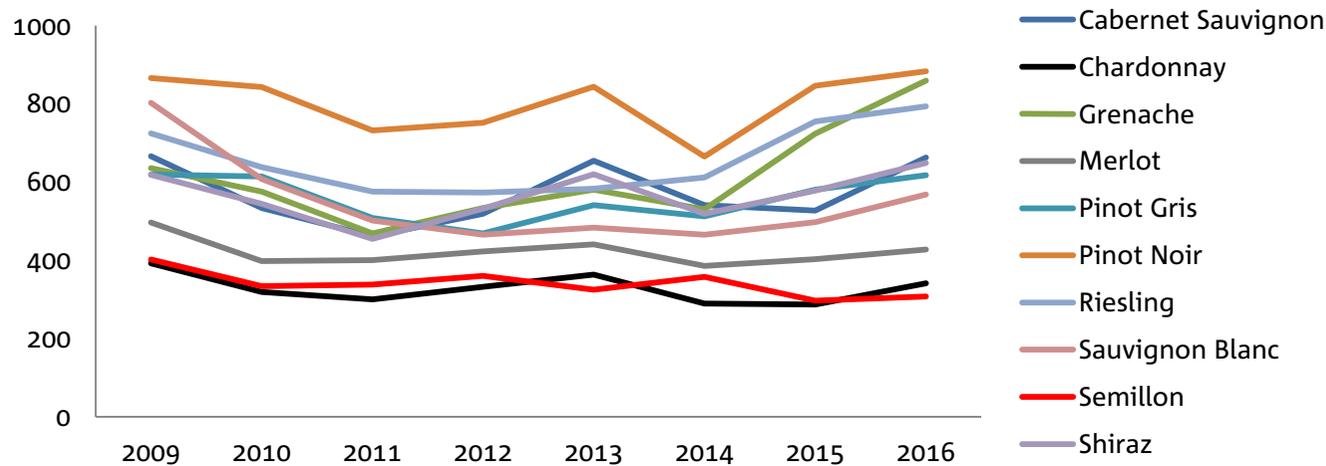
WHOLESALE FRUIT PRICES

AUD index, Sydney and Melbourne



NAB WEIGHTED WINE GRAPE PRICES

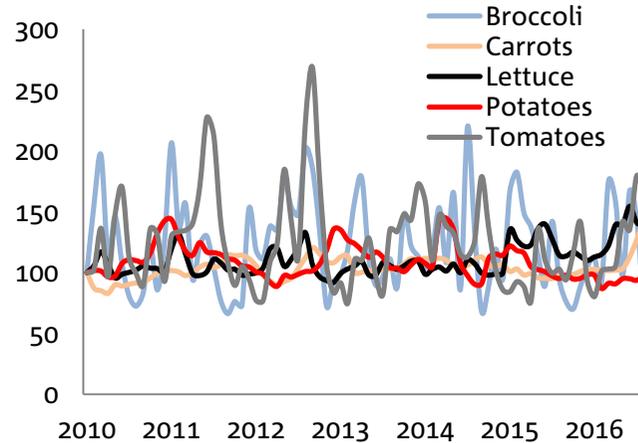
AUD/tonne



Source: Ausmarket Consultants, Wine Australia and NAB Group Economics

WHOLESALE VEGETABLE PRICES

AUD index, Sydney and Melbourne



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

Wholesale fruit and vegetable prices were again divergent in August, with fruit gaining but vegetables falling. Fruit prices rose 8.6% in August to an index value of 128.9 (January 2010 =100). Vegetables fell 6.3% in August to an index value of 119.0 (January 2010 =100).

Wine Australia's 2016 Price Dispersion Report, shows further strengthening in wine grape prices in the 2016 vintage, reflecting the rewards of a lower AUD. Overall, wine grape prices for major varieties were higher to much higher. Cabernet Sauvignon was a standout performer, up 26% from last season. Chardonnay and Grenache also grew strongly, both up 19% in volume weighted terms.



WOOL – EASTERN MARKET INDICATOR



COTLOOK A INDEX



Source: Bloomberg and NAB Group Economics

After several years of unfavourable prices, wool producers continue to enjoy a moderate upturn since last year. The Eastern Market Indicator gave up 0.4% in August but has gained 0.5% so far in September. Continued AUD strength has been something of a brake on price upside (wool is quite sensitive to movements in the dollar) any move downward in the AUD provides an upside to price. We forecast that prices will increase 7.0% in 2016-17.

The higher prices are forecast to offset lower production in 2015-16 and provide some production incentive to wool growers in 2016-17. We forecast the value of Australian wool exports to increase 6.0% 2016-17.

Global cotton prices have given up some of their earlier gains. Cotlook A was off 2.4% (AUD) in August and a further 3.1% in September (to date).