

RURAL COMMODITIES WRAP

AUGUST 2017



KEY POINTS

This month, the NAB Rural Commodities Index fell 1.2% as generally higher grain prices were offset by weakness across livestock, dairy, cotton and mixed performance in horticulture. Wheat has been on a rollercoaster of late, with eastern Australian futures surging 23% between the start of June and mid-July, before falling 13% by the end of the month. Meanwhile, dry conditions have seen further falls in cattle and lamb prices.

Over the coming months, we will be closely watching two areas, the performance of which will be key for the agricultural sector:

- The first of these is the progress of the season which has been very patchy so far this winter. This is particularly an issue for Western Australian, South Australian and New South Wales grain growers as well as Queensland graziers. Rainfall will be a major driver of grain yields and livestock slaughter (and therefore livestock prices) over the coming months. The latest Bureau three month outlook points to below average rainfall for much of the country, although most of Queensland and Tasmania are forecast to see closer to average conditions.
- The Australian dollar is also major consideration. The AUD started July at around 76 US cents but ended it at 80 US cents. While our forecasts remain that the AUD will fall to 70 US cents by the end of 2017, there are clearly risks to this outlook and any upside will adversely affect many local agricultural commodity prices.

PRICE UPDATE



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The NAB Rural Commodities Index fell 1.2% in July, reflecting weak livestock prices offsetting some big gains across some grains (wheat and barley in particular). Dairy and cotton were also lower in AUD terms, while horticulture was volatile and very mixed with fruit up 21.5% but vegetables down 24.2% (as tomatoes fell back to normal levels). While the monthly average for wheat shows a large gain, it is important to note that prices have been falling heavily since the second half of the month.

MONTHLY AUD PRICE CHANGES

Monthly average price change

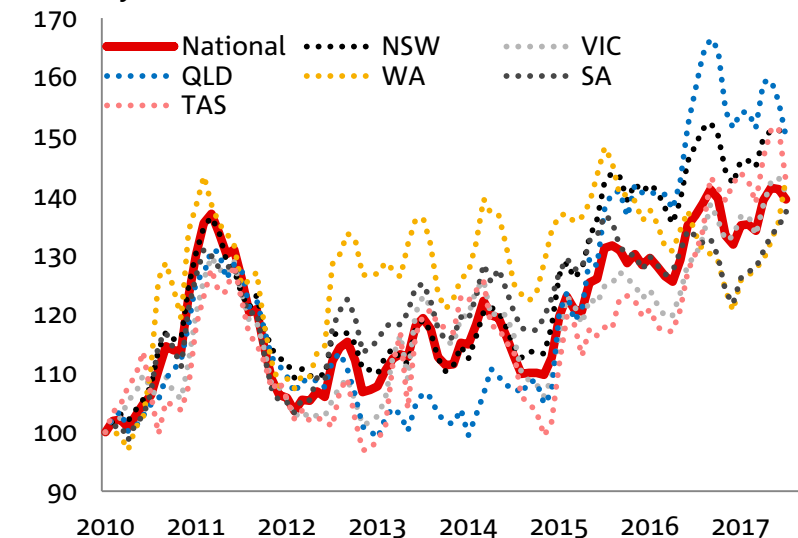
	May	June	July
Wheat	▲ 2.6%	▲ 8.2%	▲ 10.8%
Beef	▼ 2.0%	▼ 1.1%	▼ 6.2%
Dairy	▲ 9.1%	▲ 5.5%	▼ 4.2%
Lamb	▼ 2.4%	▲ 2.5%	▼ 9.0%
Wool	▲ 1.6%	▼ 1.5%	▲ 1.5%
Sugar	▼ 2.8%	▼ 15.0%	▲ 0.9%
Cotton	▲ 3.2%	▼ 5.8%	▼ 3.8%

On a state basis, previous outperformer Queensland (with its large cattle industry) fell 4.0%, while New South Wales was off 1.0%. Dairy heavy Victoria and Tasmania fell 1.9% and 6.2% respectively, while grain dependent Western Australia gained 5.6% (its biggest monthly gain in over three years) and South Australia rose 1.9%.

The index tracks 28 commodities weighted by the relative size of each commodity in the Australian agricultural sector.

NAB RURAL COMMODITIES INDEX

January 2010 = 100



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

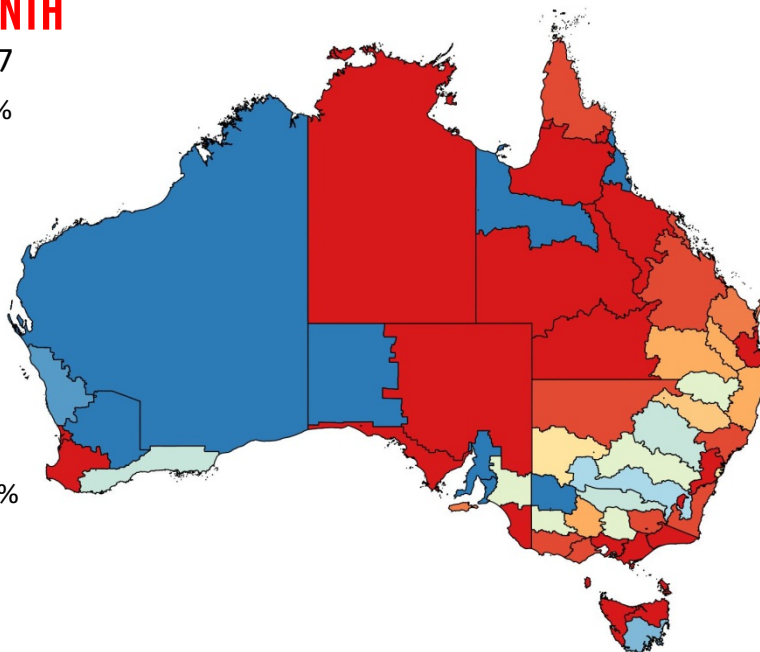
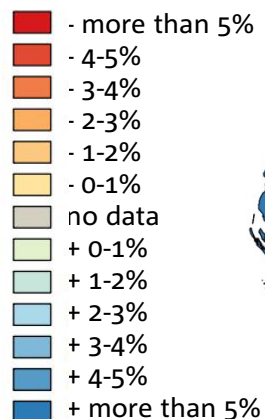


REGIONAL PRICE INDICATORS



MONTH ON MONTH

June to July 2017

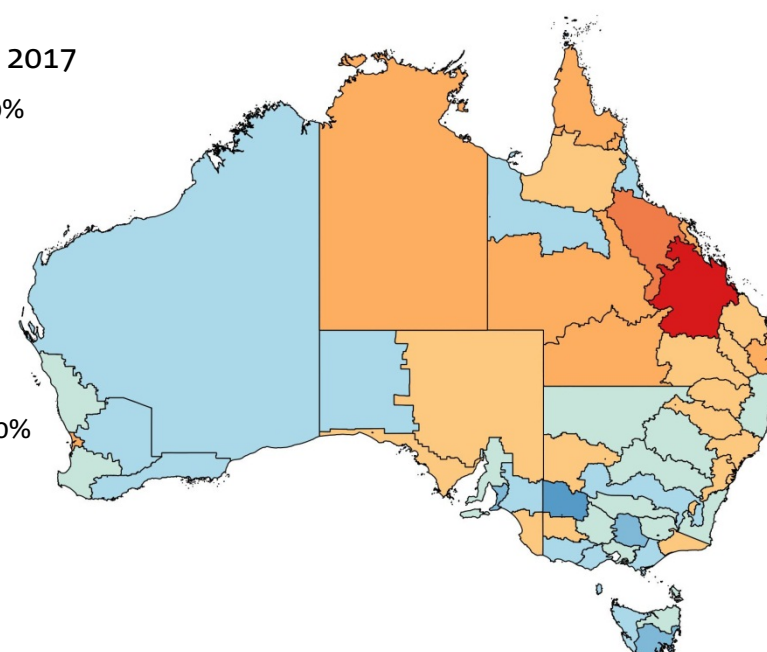
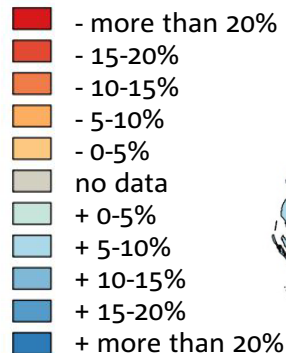


Monthly regional price indicator data shows a very volatile picture emerging behind the small national fall of 1.2%. Cattle and sheep heavy regions have seen substantial declines (many in excess of 5%), while cropping districts have seen generally very good results. Western Australia's wheatbelt, the Mallee, Mid-north and Yorke Peninsula, were among the best performers.

Dairy export prices fell, although this should be read with some caution as July saw only positive moves in farmgate prices. Farmgate opening prices have been released and both Murray Goulburn and Fonterra have issued upward revisions. For more information on dairy see page 13.

YEAR ON YEAR

July 2016 to July 2017



On a year on year basis, the index has seen less change, although cropping districts still outperform.

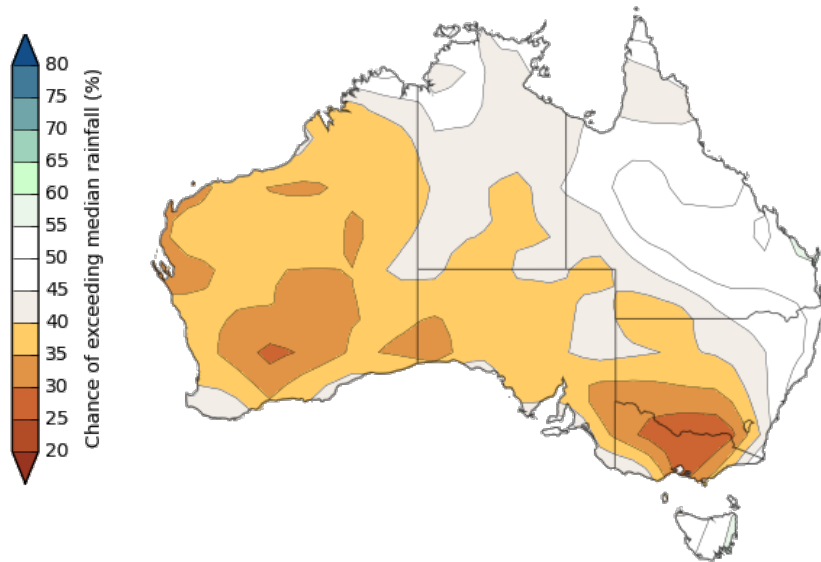
This is the fourth month of NAB's new regional price indicators – in effect a separate NAB Rural Commodities Index for every region in Australia. The data is based on state natural resource management regions (rather than ABS SA4 regions) to match agricultural regions as well as possible. Our maps are based on 2011 region boundaries. When the ABS releases production data based on updated boundaries, these boundaries will change.

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

SEASONAL CONDITIONS

THREE MONTH RAINFALL OUTLOOK

August to October 2017



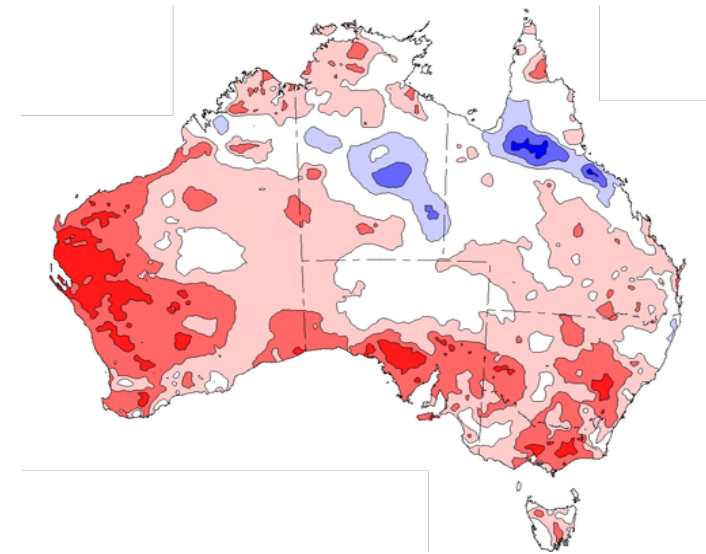
The Bureau of Meteorology's latest three month climate outlook for August to October shows below average rainfall across all of Western Australia, South Australia and Victoria, as well as most of New South Wales and the Northern Territory. Queensland and Tasmania are expected to see more mixed conditions.

The Bureau of Meteorology's three month outlooks have been forecasting well below average rainfall for most of southern Australia for most of 2017. While the actuals outperformed the forecasts in many areas across autumn, winter has been much closer to the outlook as poor seasonal conditions bite.

Source: Bureau of Meteorology

RAINFALL DECILES – LAST THREE MONTHS

May to July 2017



Rainfall was generally below average in July, although much of the Northern Territory, northern Queensland, south west Victoria and a small part of south west Western Australia enjoyed above average rainfall.

Data for the last three months shows very serious deficiencies across most of Australia's agricultural regions. The northern wheatbelt of Western Australia, the Eyre Peninsula, Gippsland and parts of New South Wales have seen the worst deficiencies.

OUTLOOK FOR PRICES AND PRODUCTION



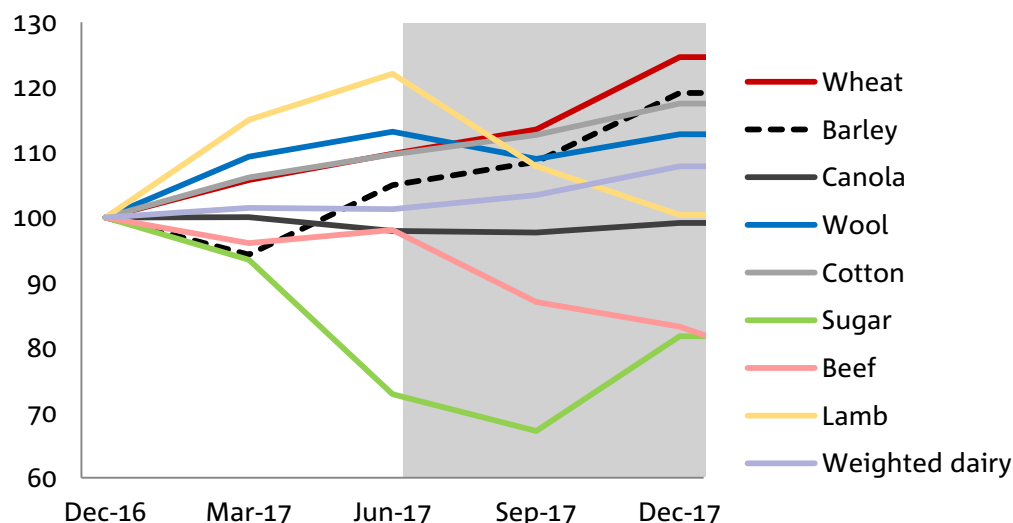
Prices

The outlook for the coming year is highly dependent on the course of the Australian dollar, which has surprised on the upside of late. Although we still expect the AUD to fall to 70 US cents at the end of 2017, providing some upside towards the end of the year, the outlook is fraught with risks.

Weather will continue to be a major driver of livestock prices. Drier weather has already had a major impact on cattle and sheep prices. If these conditions continue we expect to see further downside for livestock, but conversely increased support for grains as local feed becomes scarce. The Bureau of Meteorology forecasts dry conditions to continue in south eastern and south western Australia.

INDEX OF PRICE FORECASTS FOR RURAL COMMODITIES

AUD index value, December quarter 2016 = 100



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

Production

Rainfall (or more accurately the distinct lack of it), is the major issue for production this year. Concerns about the state of the winter crop are growing in many parts of the country, with parts of Western Australia, South Australia and New South Wales the worst affected. Our latest estimate for national wheat production is 22.7 million tonnes, although a dry finish could see production drop into the very low 20s or even high teens in a worst case scenario.

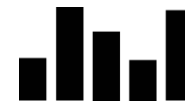
Conversely, dry conditions have already seen an uptick in cattle slaughter. If it remains dry, production is likely to be higher for some months before declining again.

PRODUCTION OUTLOOK (ABARES JUNE 2017 EXCEPT WHEAT)

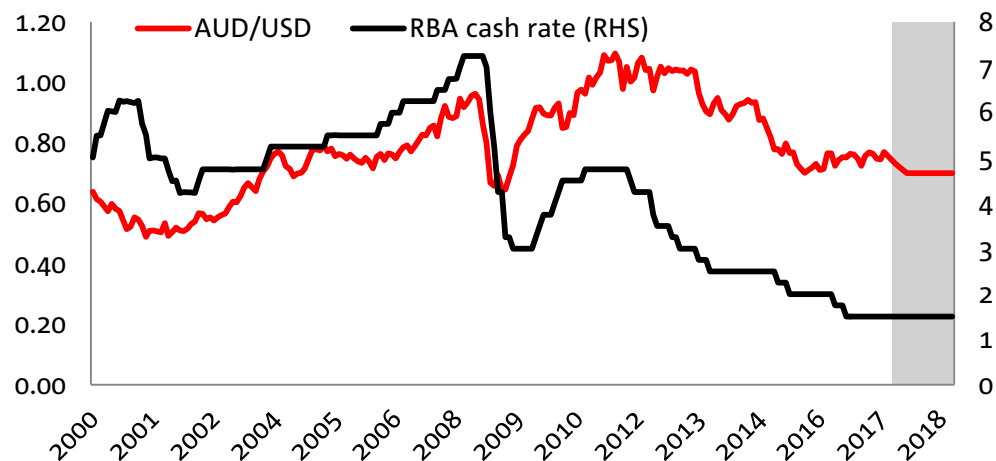
Financial year production estimates, Australia

	2016-17	2017-18	% change
Wheat (million tonnes)	35.1	22.7	▼ 35.4%
Beef (kt)	2,035	2,114	▲ 3.9%
Dairy (milk, ML)	8,910	9,250	▲ 3.8%
Lamb and mutton (kt)	669	668	▼ 0.1%
Wool	431	442	▲ 2.6%
Sugar (kt)	4,804	4,821	▲ 0.4%
Cotton (lint, kt)	960	1,083	▲ 12.8%

EXCHANGE RATES AND INTEREST RATES



EXCHANGE AND INTEREST RATES INC. QUARTERLY FORECASTS



NAB FX STRATEGY TARGETS

	2017Q3	2017Q4	2018Q1	2018Q2
AUD/USD	0.73	.070	0.70	0.70
NZD/USD	0.71	0.68	0.68	0.68
USD/JPY	114	118	120	120
EUR/USD	1.17	1.15	1.17	1.18
USD/CNY	6.81	6.82	6.81	6.81
AUD TWI	62.7	61.0	61.0	60.8

Source: NAB

AUD gained over 4% against the USD in July with over half of these gains explained by broad USD weakness. Political turmoil, disappointing US data releases and a seemingly wavering Fed, weighed on the USD. Meanwhile solid gains in commodities and a benign risk environment were additional factors supporting the AUD. In July the currency pair traded in 4.9 cent range with the monthly low recorded early in the month (0.7573, 6th July) and the high late in the month (0.8066, 27th July). The AUD/USD traded above the 80c mark for the first time in 26 months, ending the month at 0.8003.

Our forecasts point to the AUD falling to 70 US cents by the end of the year, although clearly the forecast (particularly for Q3) has substantial upside risks.

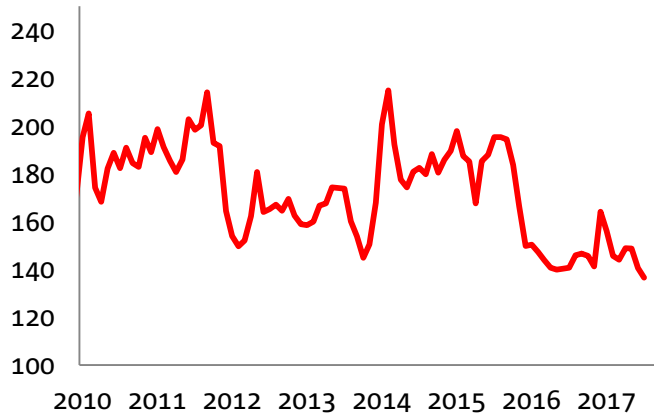
The RBA caused a bit of AUD volatility when Board minutes revealed a discussion on the neutral rate, but the importance of those remarks were later downplayed at the highest level. Ultimately we see the RBA keeping the cash rate on hold until 2019, noting significant slack remaining in the labour market and wages and inflation data looking subdued. The higher than desirable level of the AUD will likely also weigh on the RBA. There appears to be no urgency for the RBA to hike – although there will be some near-term inflation shocks that need to be monitored (such as the recent hikes in retail energy prices). The RBA should be content with keeping interest rates on hold for an extended period (a hike is not expected until mid-2019).

FARM INPUT PRICES



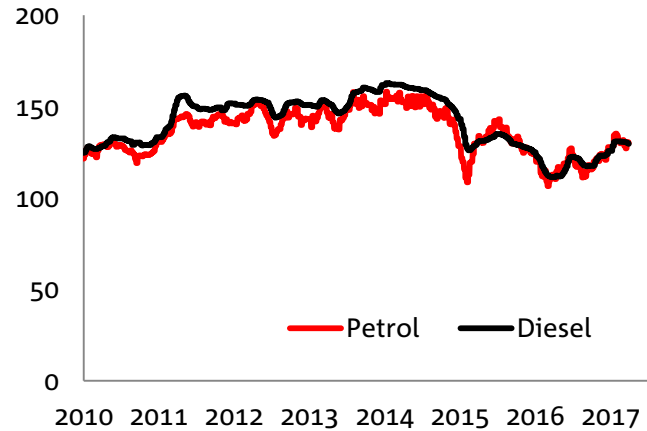
NAB FERTILISER INDEX

AUD index



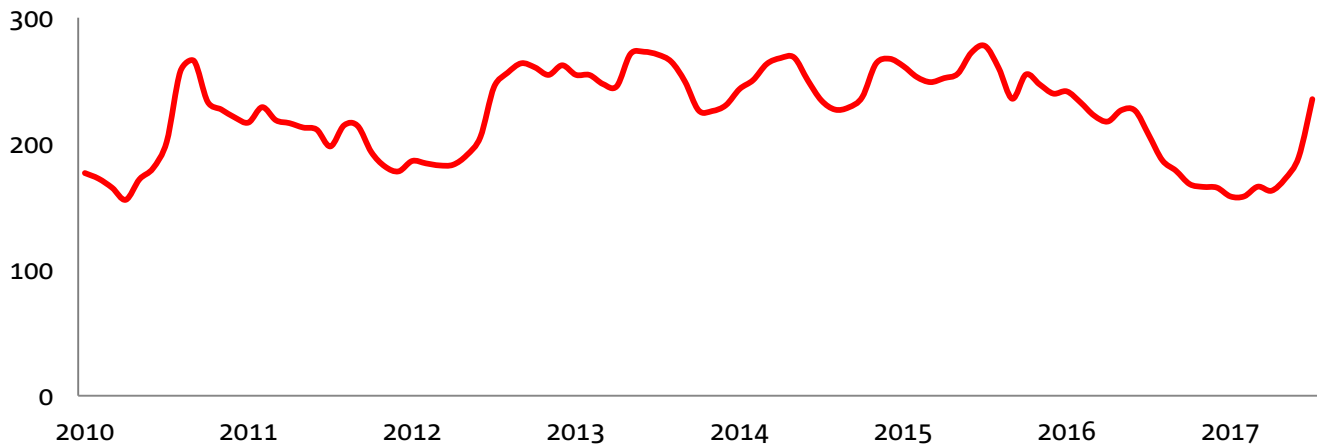
NATIONAL AVERAGE FUEL PRICES

AUc/litre



NAB WEIGHTED FEED GRAIN PRICE INDEX

AUD/tonne



Source: Bloomberg, Profarmer and NAB Group Economics

Feed prices jumped 24.3% to \$235/tonne in July, reflecting higher wheat and barley prices amid an international rally, combined with very dry seasonal conditions. There have been numerous reports of livestock producers scrambling to secure old season crop for stock feed as dry weather bites.

Although the earlier rally in global grain prices has well and truly retreated (see page 9 for more detail), the combination of i) the risk of below average grain yields this season and ii) great uncertainty around the level of old season crop remaining on farm, could see domestic feed prices attract a premium over coming months.

Fertiliser prices were down again in July, largely as a result of a higher AUD. Overall, the index was down 2.9% for the month. If the AUD falls back to 70 US cents we expect fertiliser prices to rise in AUD terms.

With oil still mired in the low 50s and the AUD back up to the high 70s range, Australian drivers have been enjoying somewhat lower fuel prices. Latest national data shows petrol prices at 122.6 cents/litre and diesel at 126.6 cents/litre. However, any depreciation in the AUD from here would see some upward pressure on fuel prices.

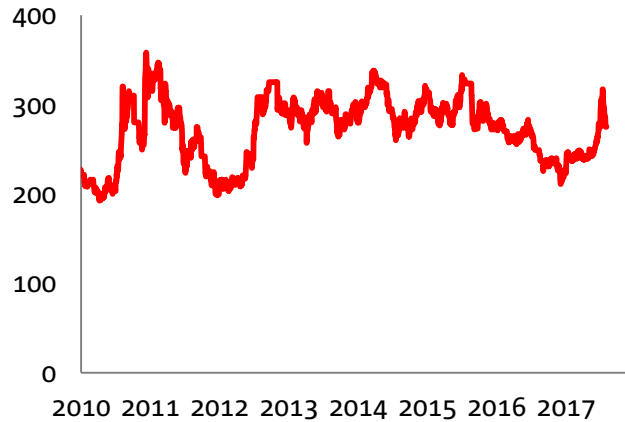


WHEAT



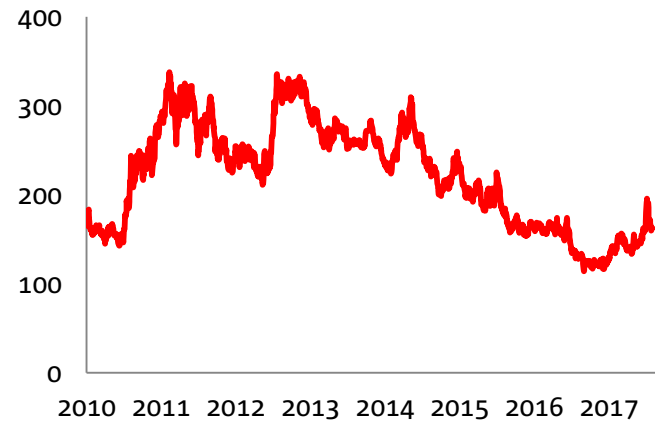
ASX MILLING WHEAT FUTURE

Eastern Australia, AUD/tonne



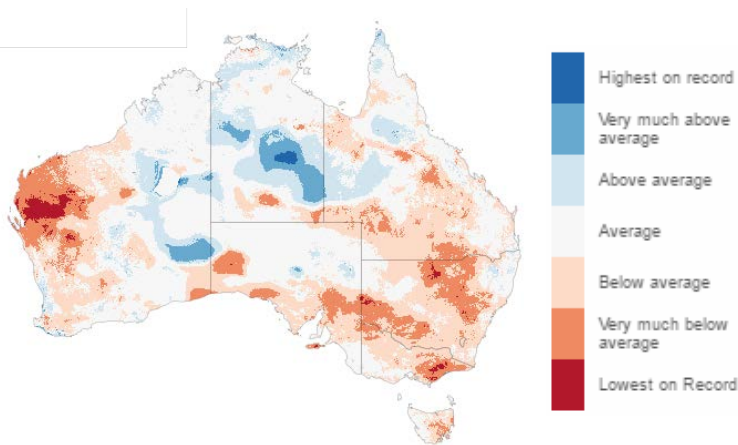
CBOT SOFT RED WINTER WHEAT

USD/tonne



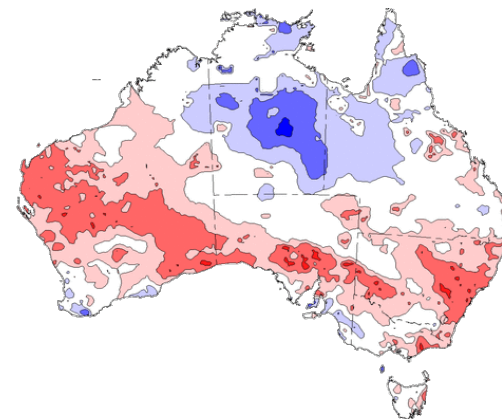
ROOT ZONE SOIL MOISTURE

Relative to average, 3 August 2017



RAINFALL – JULY 2017

Deciles



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

Prices

The last two months has seen substantial volatility in wheat prices, with eastern Australian futures surging 23% between the start of June and mid-July, before falling 13% by the end of the month. Futures topped out at \$317/tonne, an extraordinary result given prices had been mired in the mid-240s range for months. This spike was driven by a forecast 15 year low in the US spring wheat crop. However, with spring wheat such a small part of global production, prices have since retreated to lower levels. There is likely to be a premium for domestic wheat in the coming months as livestock producers scramble for feed.

Production

July did not bring good news for our wheat production model, with below average rainfall in many areas. However, the last week has seen some decent falls across WA, SA, VIC and southern NSW.

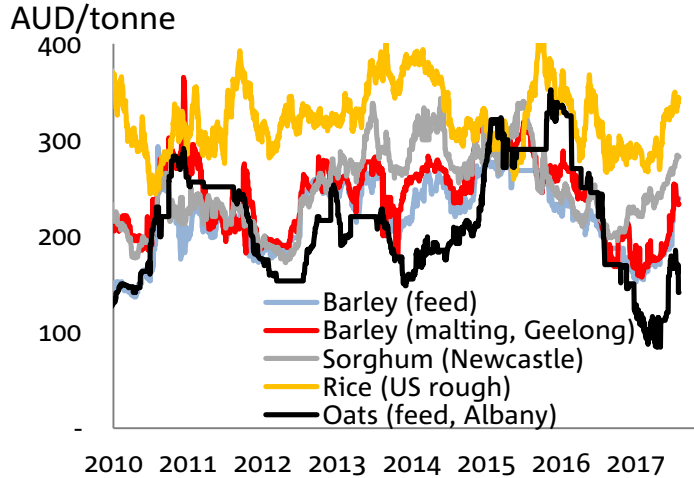
Our central case estimate for the 2017-18 Australian wheat crop is now 22.7 million tonnes, based on rainfall to date and assumed average rainfall in major cropping areas for the rest of the season. If rainfall continues to be below average a much smaller crop, potentially in the very low 20s or high teens, is well within the realms of possibility.



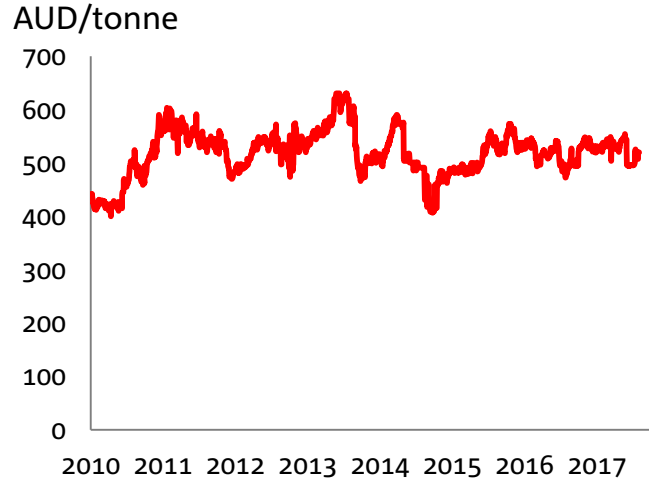
OTHER BROADACRE CROPS



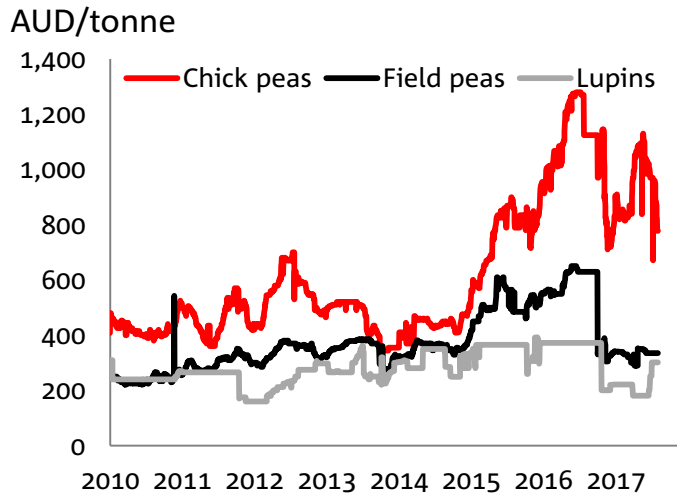
SELECTED COARSE GRAINS



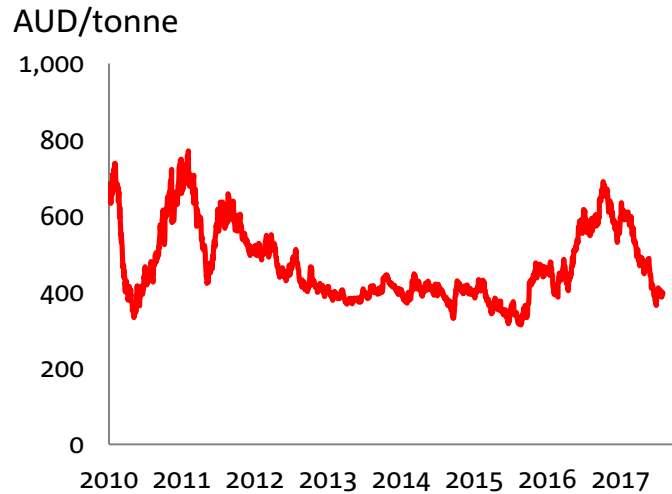
CANOLA, NEWCASTLE NSW



SELECTED PULSES



ICE NO.11 SUGAR



Prices for most coarse grains have seen a strong jump, in line with wheat, amid global concerns combined with domestic supply uncertainty. Our outlook is broadly similar to wheat for the coming year, with the AUD (and global growing conditions) to be key. Canola remains a stand-out, with prices holding up much better, although obtaining seed was a major challenge for planting.

We have been cautious around the trajectory of chick pea prices for some time, so the ongoing roller-coaster is something of a surprise. Prices exceeded AUD1,200/tonne last year following two poor Indian monsoon seasons, before falling into the 700s late last year, recovering to AUD900-1,000/tonne of late, but now falling again. Prices are hovering in the high 700s. If the Indian monsoon is stronger this year prices are likely to see sharp falls. Nonetheless, chick peas are likely to remain more expensive than alternative crops this season, although Australian plantings are likely to be lower on disease concerns after two big seasons.

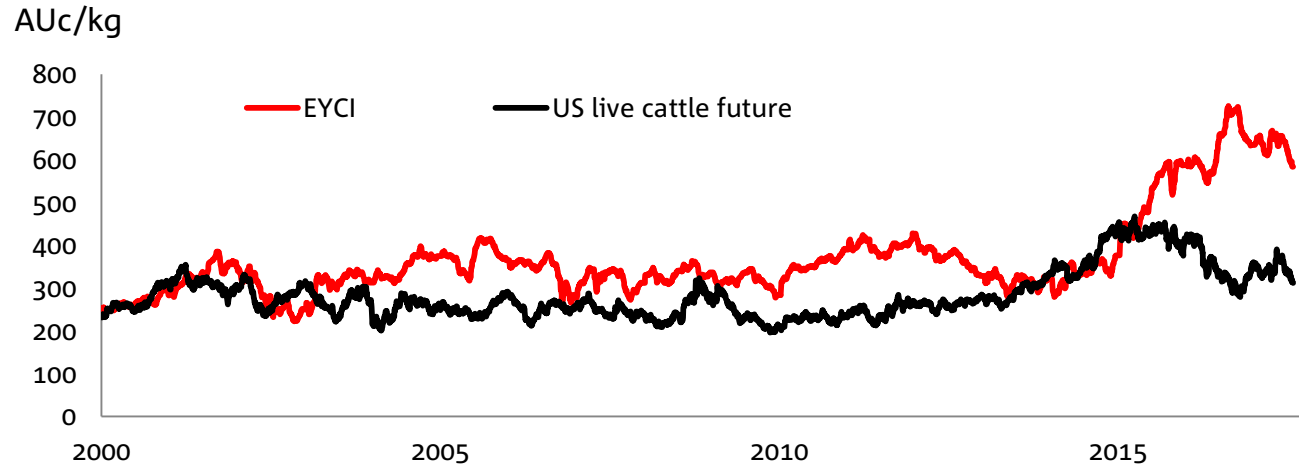
Sugar prices show some tentative signs of stabilisation after a big tumble this year which wiped off all of the previous rally and fell close to 2015 lows in AUD terms.

Source: Bloomberg, Profarmer and NAB Group Economics

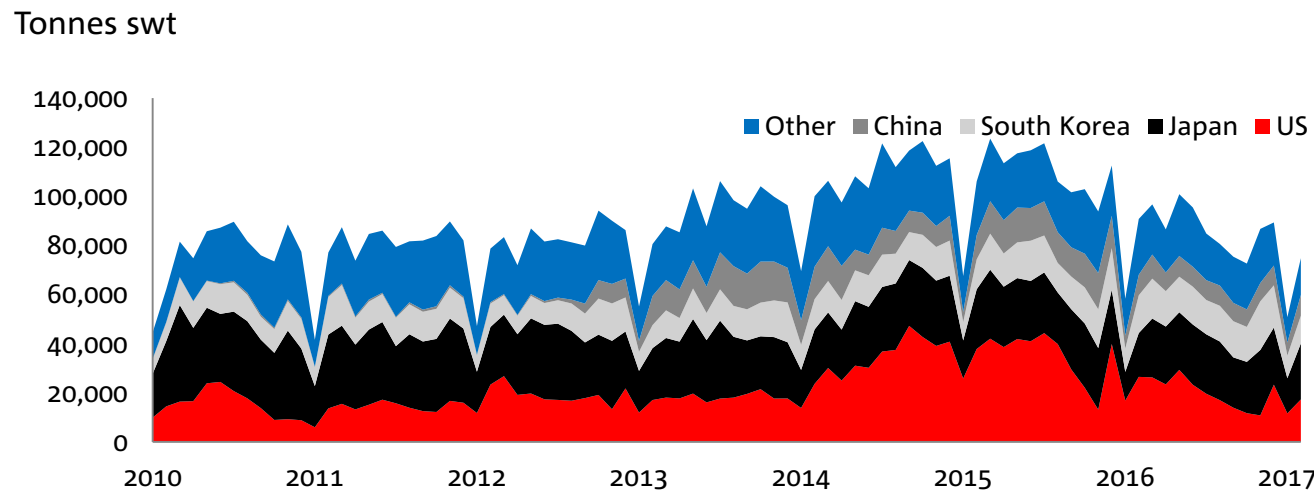




EASTERN YOUNG CATTLE INDICATOR AND US CATTLE FUTURES



MONTHLY AUSTRALIAN BEEF EXPORTS



Source: Meat and Livestock Australia and NAB Group Economics

There has been a great deal of news in the cattle industry of late, although little of it is good. Young cattle prices continue to fall amid dry weather and poor export market prices. The EYCI is not only below its level at the same time in 2016, it is fast closing on 2015 levels.

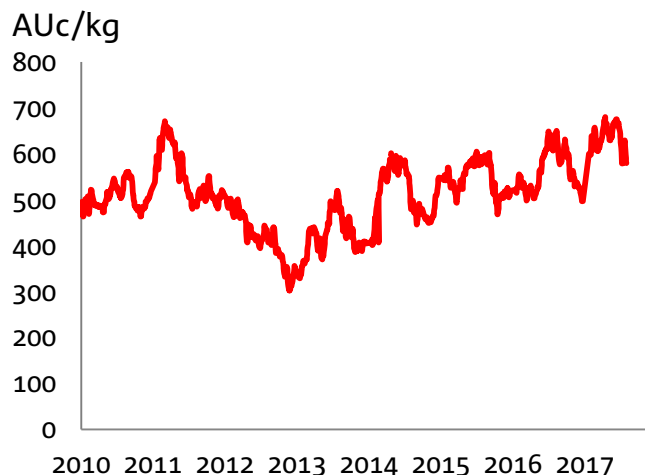
Dry conditions have seen slaughter increase rapidly – Queensland slaughter is up 20% and New South Wales is up 12% year on year based on data from Meat and Livestock Australia. MLA reports that this follows slaughter levels below 2016 figures for most of 2017. With winter dryness looking likely to persist into spring in many areas, it is likely that there will be further turnoff and increased pressure on saleyard prices. Elevated feed prices will be a concern for some producers, pointing to higher input costs for feedlots.

Current conditions come against a background of a near unprecedented boom in Australian cattle prices. The EYCI reached an all time high of almost 725c/kg in September 2016, a level which was always unsustainable when based largely on restocker demand rather than any fundamentals in export markets. We see the EYCI falling to 500c/kg either late this year or early next. While this represents a sharp fall, prices should remain well above pre-boom levels.

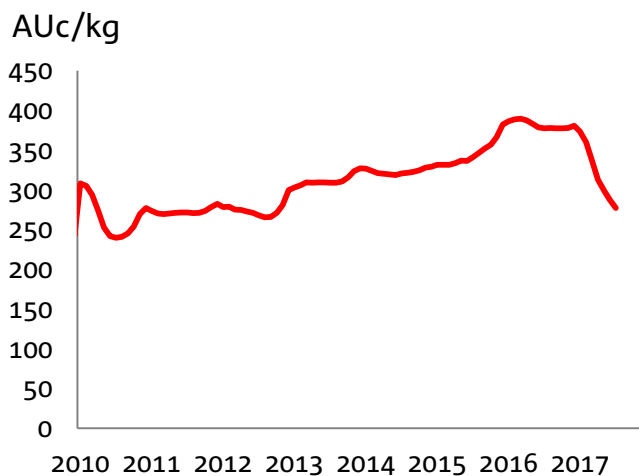
LAMB, PORK AND POULTRY



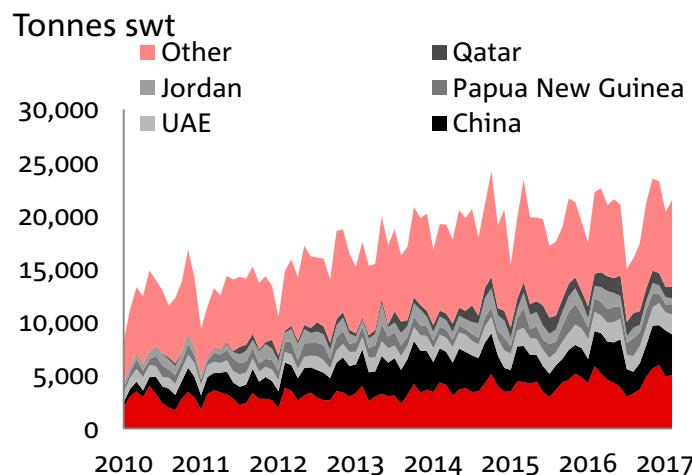
NATIONAL TRADE LAMB INDICATOR



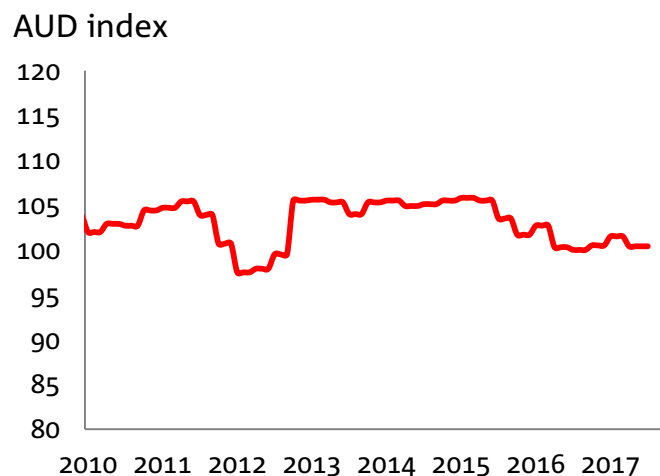
AUSTRALIAN PORK PRICE INDICATOR



MONTHLY LAMB EXPORTS BY DESTINATION



ABS POULTRY PRICE INDEX



Lamb prices have likewise felt the pressure of a dry July across the much of the country. The National Trade Lamb Indicator was down 9.0% on a monthly average basis and recent data show prices hovering around 2015 levels. Further price falls are likely in line with the usual spring flush, but should not in themselves be a major concern as prices in the first half of the year were elevated compared to 2015 and 2016.

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.

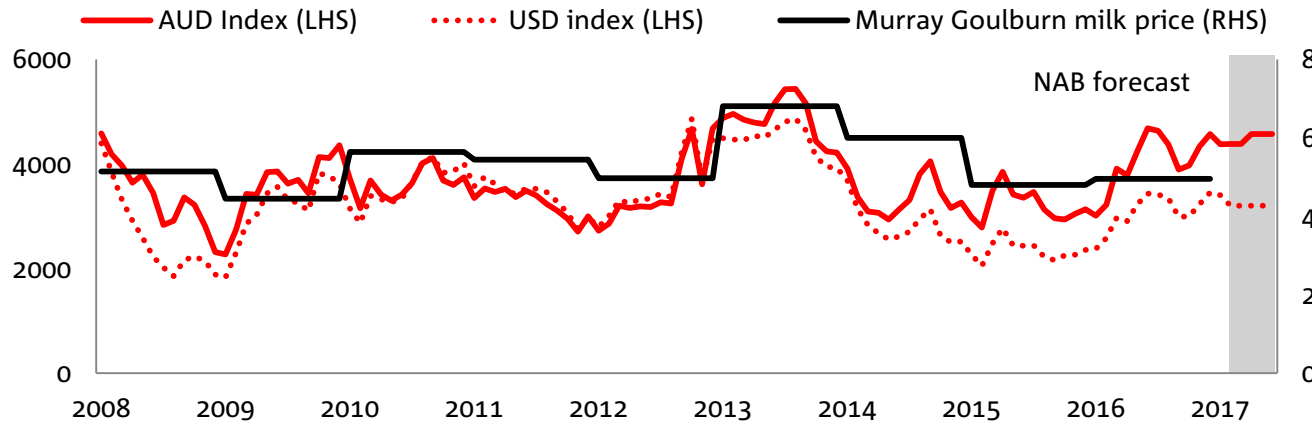
The quagmire in the Australian pork industry continues unabated. Wholesale pork prices (measured as an average of buyer and seller prices for eastern seaboard 60.1-75kg animals) continue their poor run that began late in 2016. Prices were off another 3.6% in July (to date) and are now approaching 27% lower than the same time last year. The pork industry is grain intensive, and producers may come under further pressure from elevated grain prices combined with competition from cheap imports (particularly with the AUD having risen).

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)

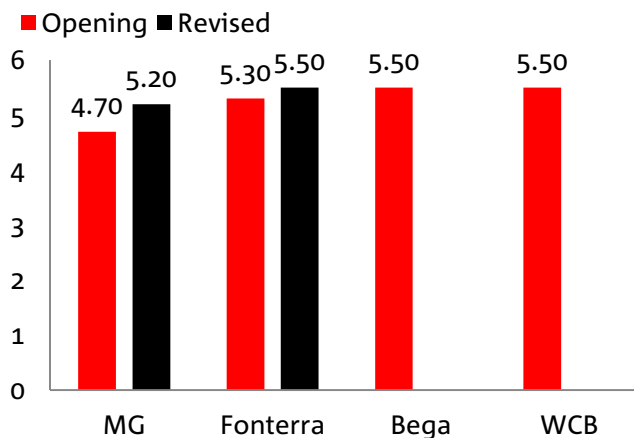


Global Dairy Trade auction results in July were mixed to lower and the NAB weighted dairy export price indicator fell 4.2% for the month in AUD terms after rising 5.5% in June.

While recent auctions have perhaps underperformed expectations, there is a good deal of interest around farmgate prices for the 2017-18 season. Murray Goulburn opened at \$4.70/kgms, well below Bega and Warrnambool Cheese and Butter (both on \$5.50/kgms) and Fonterra (\$5.30/kgms). Seeking to maintain milk flow, Murray Goulburn revised its opening price substantially higher to \$5.20/kgms. Fonterra has now announced a step-up to \$5.50/kgms, leaving Murray Goulburn somewhat off the pace.

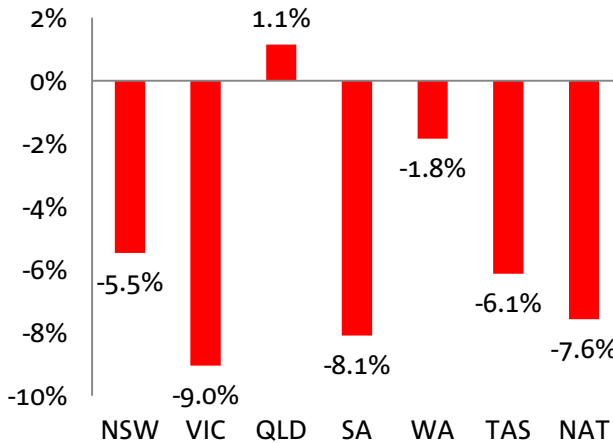
FARMGATE PRICES

2017-18 season



SEASONAL MILK PRODUCTION CHANGE

2016-17, YTD to May



Milk flow remains well down on last season. Season to date production to May is down 7.6% nationally. An emerging concern is how dry conditions will affect spring milk flow. While south west and northern Victoria and south east South Australia have enjoyed some of the better conditions nationally, Gippsland is extremely dry, underlined by very early irrigation activity in the Macalister Irrigation District.

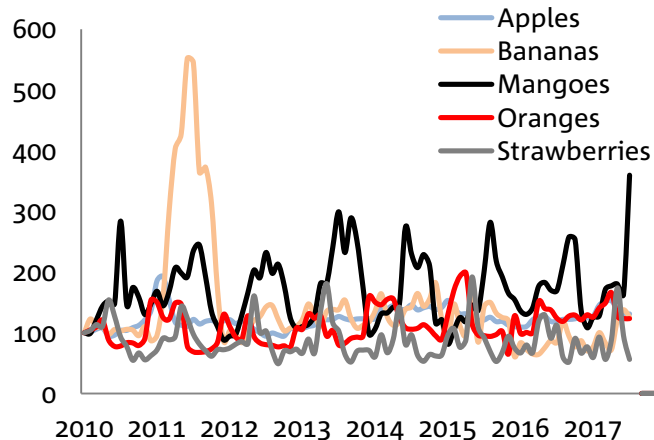
Source: Australian Bureau of Statistics, Global Dairy Trade, Dairy Australia, processors, ABC and NAB Group Economics

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



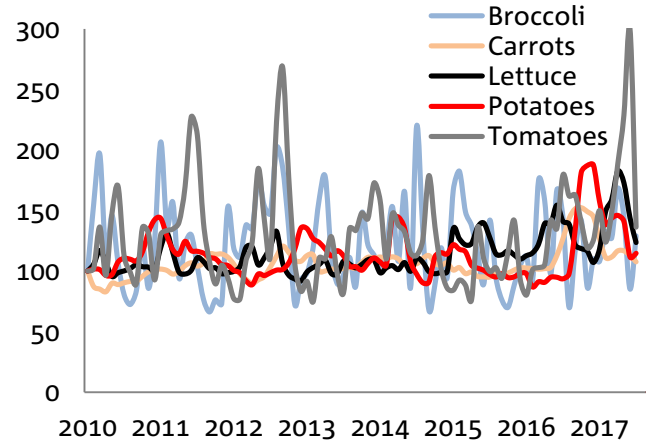
WHOLESALE FRUIT PRICES

AUD index, Sydney and Melbourne



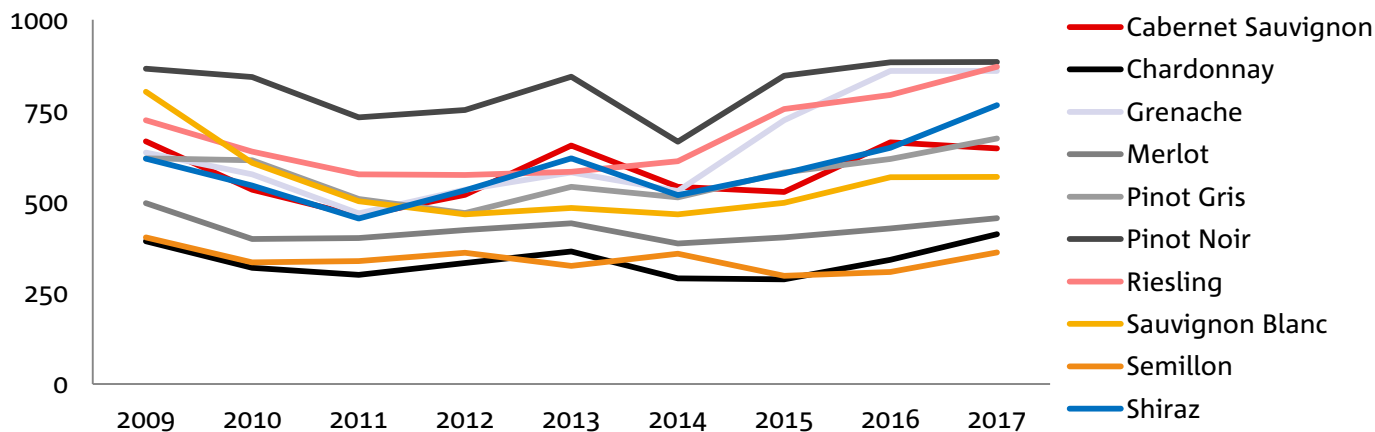
WHOLESALE VEGETABLE PRICES

AUD index, Sydney and Melbourne



WINE AUSTRALIA 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.

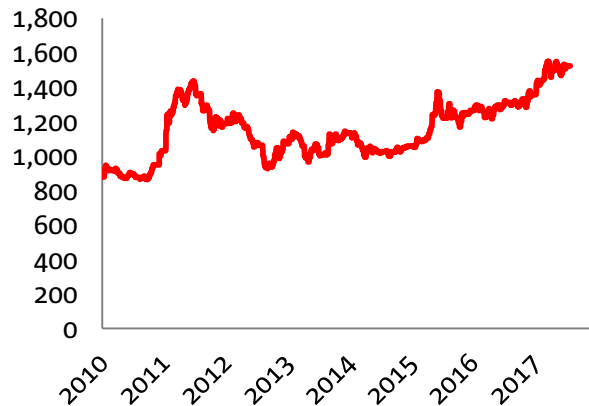
Wholesale fruit and vegetable prices were very volatile in July. Fruit was up 21.5%, largely reflecting a big and partly seasonal jump in mango prices. In July the index stood at 160.8 index points (January 2010 = 100). Vegetables fell sharply, down 24.2% to 122.3 index points. This drop reflects the end of an extraordinary rally in tomato prices brought on partly by the effects of Cyclone Debbie this year.

Wine Australia's 2017 National Vintage Report shows prices rose once again this year, with the average of all wine grapes up 7% on a volume weighted basis. An AUD at more sustainable levels likely explains some of the increase, but overall the industry looks to be on a more sustainable footing following years of glut and poor export conditions. Among the best performers were Riesling (up 13%), Shiraz (up 12%), and Pinot Gris (up 9%).



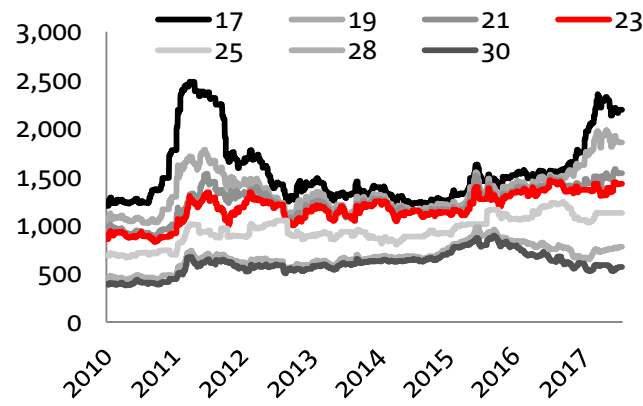
WOOL – EASTERN MARKET INDICATOR

AUc/kg



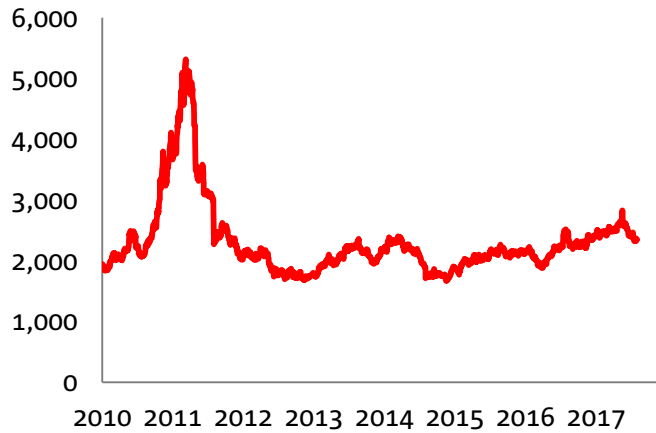
WOOL PRICES BY MICRON

Southern Region



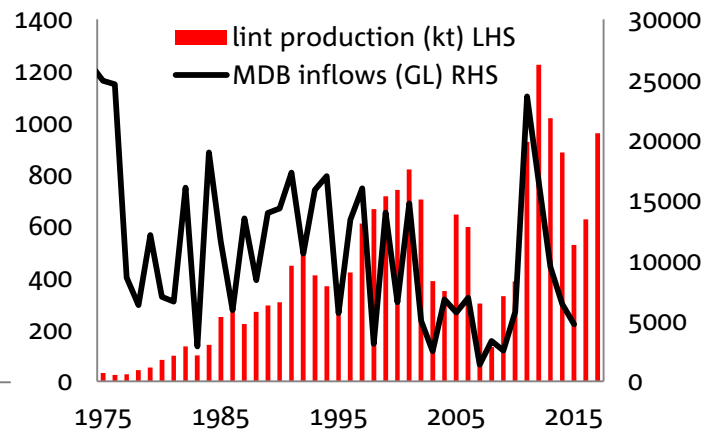
COTLOOK A INDEX

AUD/tonne



AUSTRALIAN COTTON AND BASIN INFLOW

Production and MDB system inflows



The wool market continues to see good prices, despite the sharp rally in the Australian dollar towards the end of the month. This follows a return of confidence to the industry last year after several years of unfavourable prices. If our forecast of the AUD at 70 cents transpires, there may be further upside but this outlook contains a number of risks. The best performance continues to be in been in fine and super-fine wool – below 20 microns. Coarser wools at the 28 and 30 micron level have generally seen lower prices. However, there are some emerging signs that prices for super-fine wool have peaked..

The Eastern Market Indicator rose 1.5% in July. With prices at these levels, ABARES projects that wool production will increase in the coming year, arresting (at least temporarily) a long decline in production.

Cotton prices fell 3.8% in AUD terms in July. While the Australian cotton industry has expanded rapidly over the past three decades, it remains dependent on irrigation water, with around three-quarters of Australian cotton acreage irrigated. With low inflows amid dry conditions, there is an emerging risk to production for the coming season.

Source: Bloomberg, ABARES, Murray Darling Basin Authority and NAB Group Economics

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