

Post-farmgate Agribusiness Survey – June Quarter 2014

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Summary:

- Post-farmgate agribusiness conditions continued to fall in the June quarter, entering negative territory for the first time in 15 months. While this fall is partly explained by seasonal conditions, it comes despite welcome autumn rainfall in much of the country, which combined with above average late autumn temperatures has given many producers a decent break coming into winter.
- While total post-farmgate agribusiness confidence has fallen to -13, many sub-sectors report increasing confidence for the next three months and expected conditions for the next 12 months have risen to +24.
- The export sales index has fallen since the March quarter but remains squarely in positive territory. Export expectations have moderated considerably, reflecting expected results not being matched by actual results in the previous 4 quarters.
- Survey respondents continue to be overwhelmingly optimistic in their medium-term outlook for post-farmgate business conditions. This, combined with expectations of a prolonged period of low interest rates, has fuelled somewhat lower but nonetheless strong capital expenditure intentions for the year to come.

Key Survey Indicators

Index	Q4 2013	Q1 2014	Q2 2014
Business conditions	17	4	-4
Business confidence	6	0	-13
Trading	24	13	-2
Profitability	16	-2	-9
Employment	10	2	0
Expected conditions – 3 months	10	10	0
Expected conditions – 12 months	25	12	24
Forward orders	4	10	-2
Capacity utilisation (%)	78.4	77.2	77.3
Capex plans – next 12 months	22	29	22

Source: NAB Group Economics

Business conditions

- Post-farmgate business conditions continued to unwind in the June quarter and have now reached negative territory (-4), down from +4 in the March quarter and well below the 9 year high of +17 reached in the December quarter 2013.
- The move into negative territory for the index as a whole belies an increasing divergence among respondents. 23% of respondents described conditions as good or very good in the June quarter, up from 21% in the March quarter. The decline in conditions is driven by an increase in those who described conditions as poor or very poor, up from 17% to 26% in the June quarter.
- The decline in business conditions comes despite decent autumn rainfall across much of eastern and south-western Australia. Combined with above average temperatures, these conditions have given many producers a good break going into winter. However, with the Bureau of Meteorology forecasting a 70% chance of El Niño emerging in 2014, the prospect of poorer late winter and spring rains may be weighing on the minds of producers. Expected agribusiness conditions stand at zero for the September quarter, down from +10.
- In contrast to agribusiness conditions, total seasonally adjusted business conditions continued to grow in the June quarter, having edged above zero in the March quarter for the first time since the September quarter 2012.

Figure 1: Agribusiness business conditions

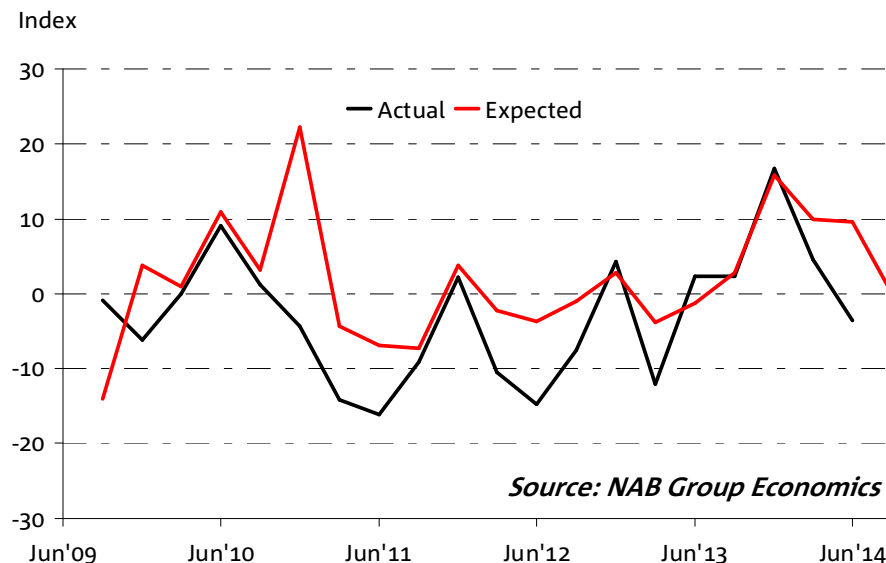
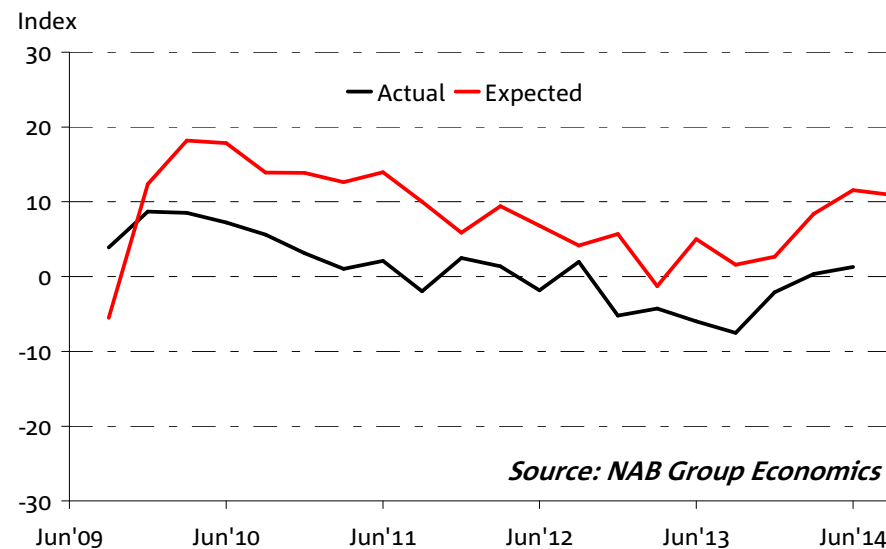


Figure 2: Total business conditions – seasonally adjusted



Trading

- Post-farmgate agribusiness trading conditions continued to cool in the June quarter, falling below zero after a historic high in the December quarter of 2013. While expectations of trading conditions for the September quarter have also eased, they remain positive at +5.
- The decline in trading conditions is driven in large part by falling customer confidence and “other” factors. Seasonality, company specific factors and exchange rates have not greatly affected the result.
- Recent international economic data has been mixed. The US economy is now thought to have gone backwards in the March quarter due to an estimated slowdown in inventory accumulation and an unusually harsh winter. Indicators point to a bounce back in the June quarter, with recovery expected to continue over the rest of 2014 and into 2015.
- Partial economic indicators point to a stabilisation in China’s economy in recent months, while moderate sub-trend growth continues across the emerging market economies of East Asia. Elsewhere, Eurozone manufacturing and service sector PMIs showed the European recovery stalling in June, with activity slowing rather than accelerating as expected.

Figure 3: Agribusiness trading conditions

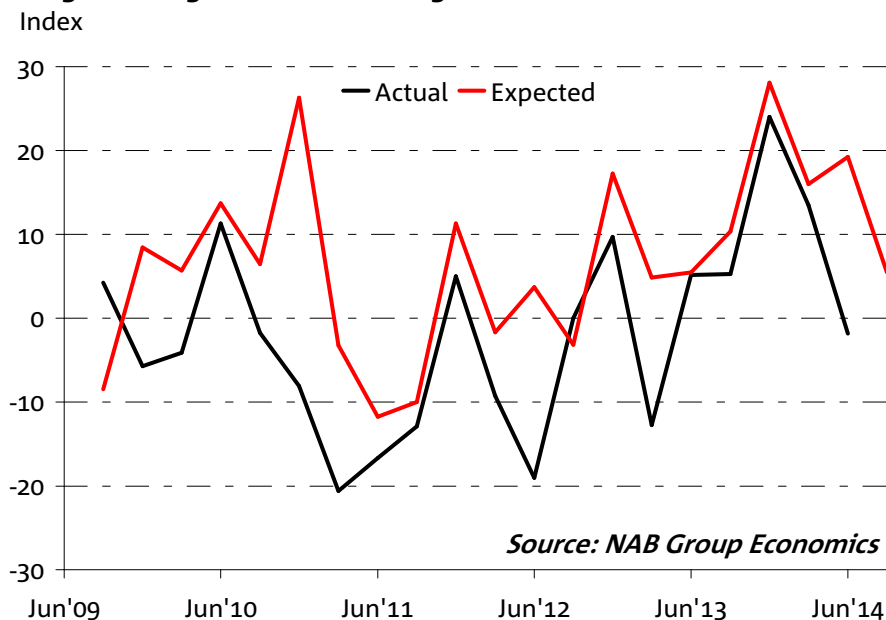
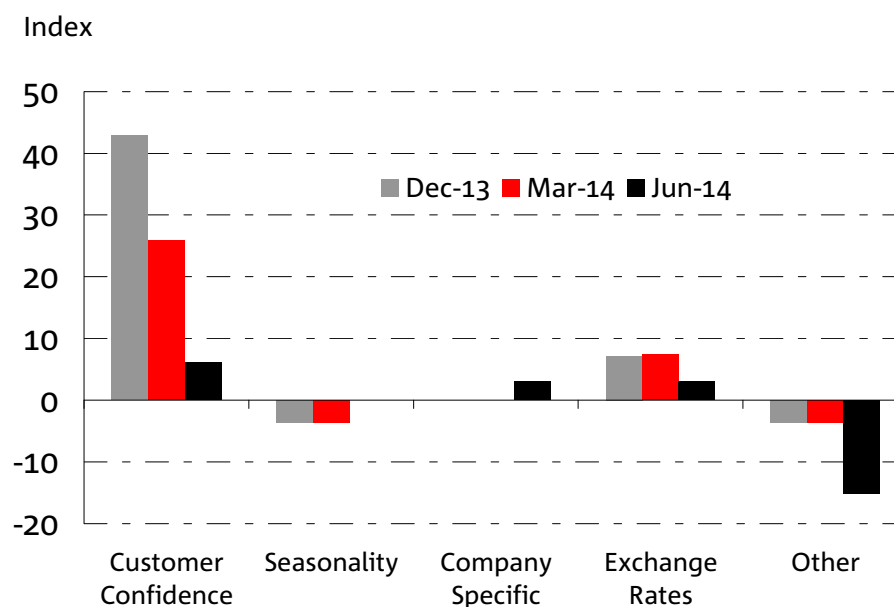


Figure 4: Drivers of trading conditions



Source: NAB Group Economics

Profitability

- Profitability continued to recede from its December quarter 2013 peak and now stands at -9 in the June quarter, but broadly in line with the 5-year June quarter average of -8. Behind the headline results there is an increasing divergence in profitability between respondents. While more respondents cite good or very good profitability compared to the March quarter (27% up from 23%), even more respondents cite poor or very poor profitability (36%, up from 25% in the March quarter).
- Respondents continue to cite a perceived lack of demand as the overarching constraint on post-farmgate agribusiness profitability, although somewhat less so than other businesses.
- While expected profitability has declined, it remains positive at +2 for the September quarter, albeit below the long term average of +4 for the September quarter.

Figure 5: Agribusiness profitability

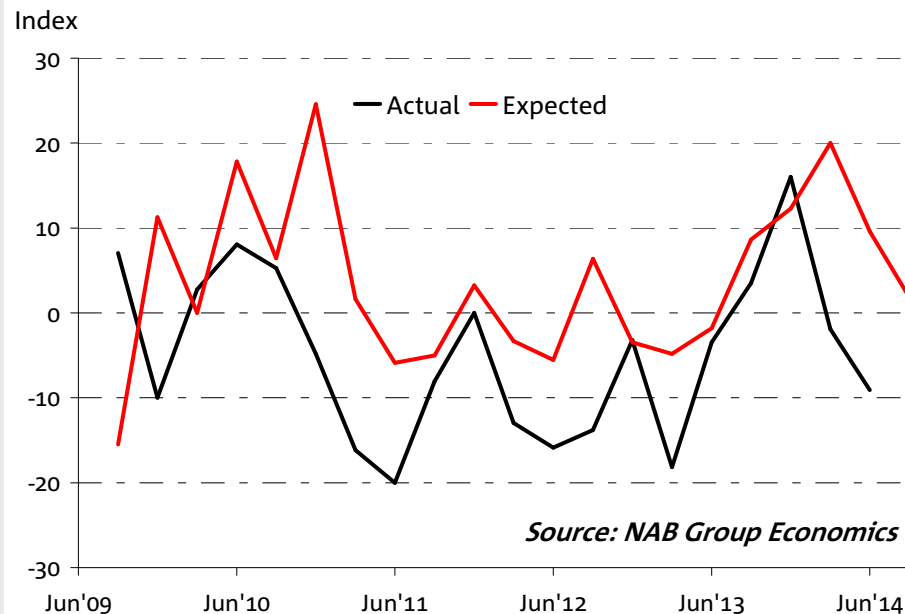
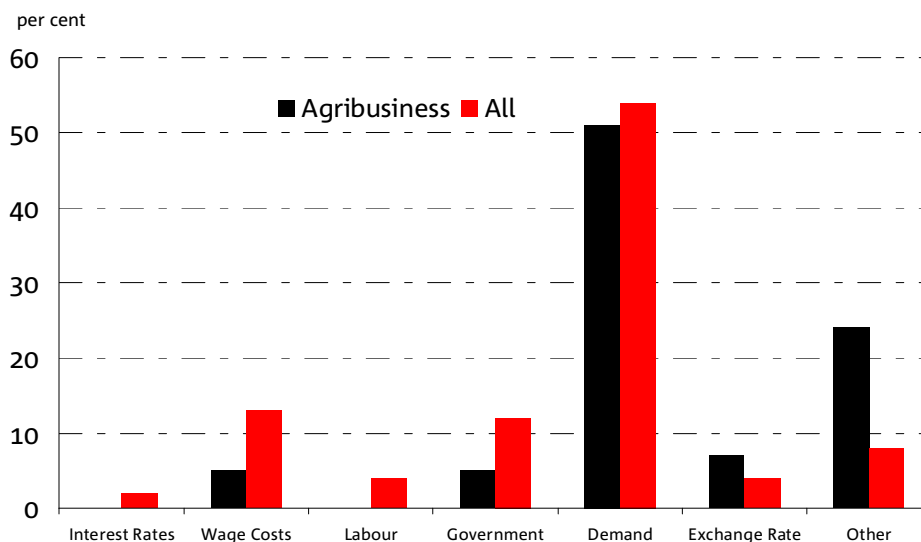


Figure 6: Constraints to profitability



Margins

- Sales margins slumped in the June quarter, falling from the highest level since the survey began in the March quarter (+10) to -15. The decline reflects an easing of beef, lamb and wheat prices after very strong gains in the first quarter as well as a continuing decline in dairy prices. Seasonal factors are also at play, with labour costs increasing ahead of their traditional September quarter peak. Margins tend to be generally higher in the summer and autumn than the winter and spring.
- Respondents expect a partial recovery in the September quarter to -2. Should El Niño emerge later this winter, margins will likely come under further pressure.

Figure 7: Agribusiness sales margins

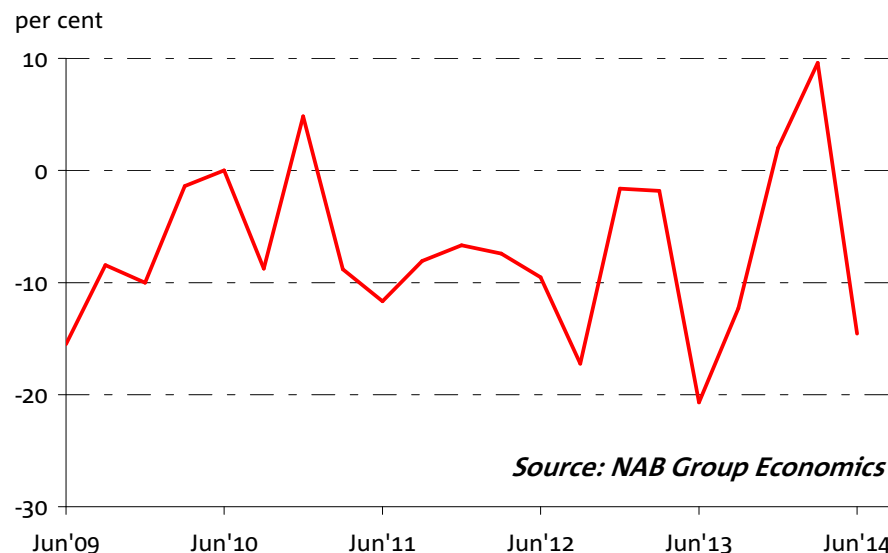
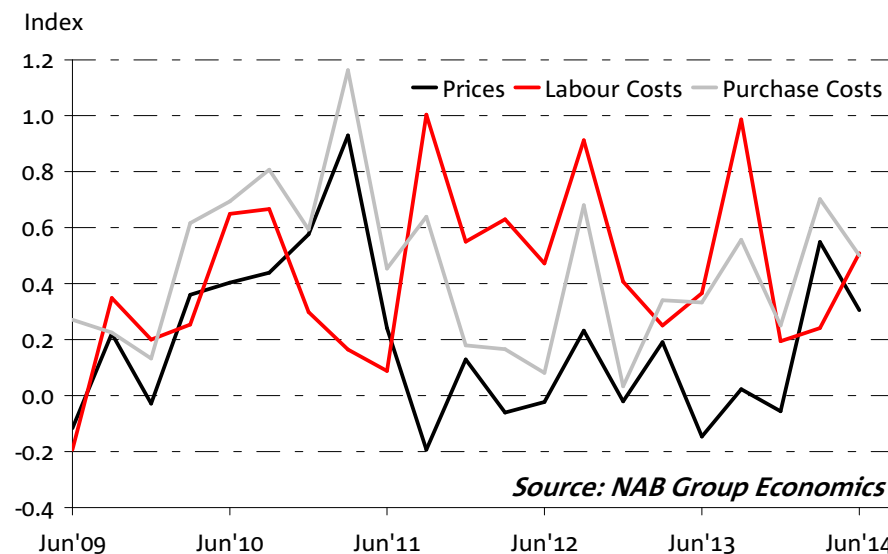


Photo: Mai Thai

Figure 8: Costs and prices



Employment

- Post-farmgate agribusiness employment conditions fell slightly in the June quarter to zero, in line with expectations reported by respondents in the March quarter and reflecting generally slower production during the winter months. Three quarters of respondents reported they had kept employment levels unchanged in the June quarter, with 13% reducing headcount.
- Employment expectations are -7 for the September quarter, with 16% of respondents planning to reduce their workforce. Nonetheless, three quarters of respondents still plan to keep employment levels unchanged in the quarter.
- Employers continue to benefit from largely placid labour market conditions with wage growth mostly constrained. Although post-farmgate agribusiness producers do not generally consider a lack of suitable labour to be a major impediment to profitability, almost half of the respondents reported that a lack of suitable labour is at least a minor constraint.

Figure 9: Agribusiness employment gains

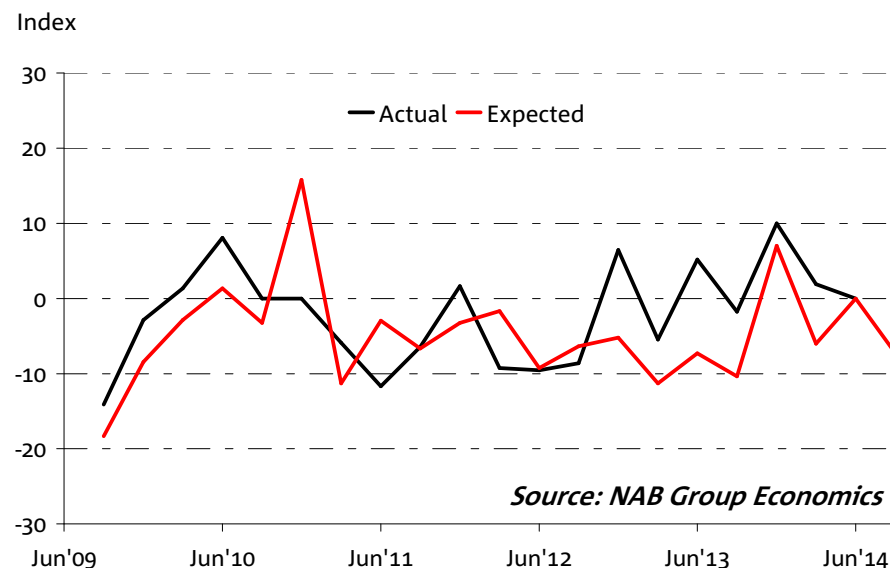
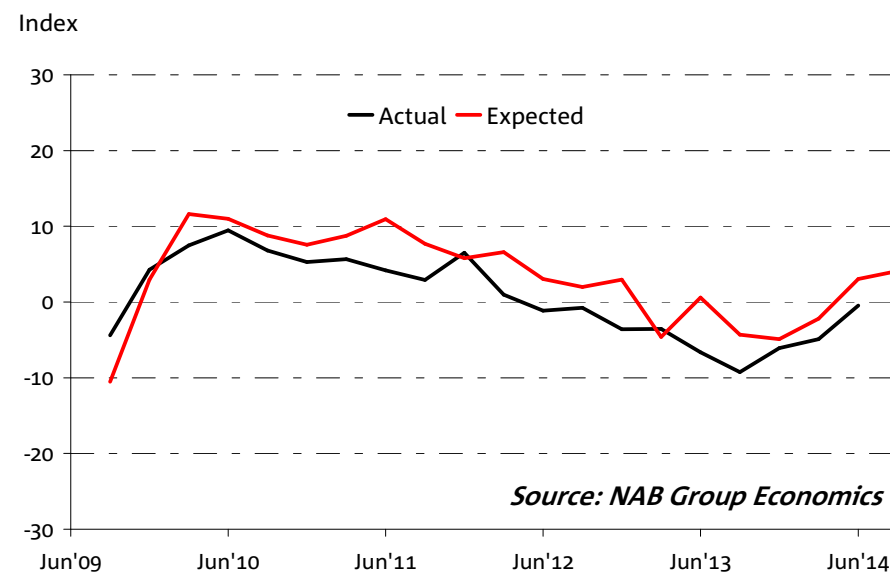


Figure 10: Total business employment gains



Expected conditions

- Respondents remain overwhelming confident about the future, despite generally declining post-farmgate agribusiness conditions over the June quarter. Expected business conditions for the next 12 months rebounded in the June quarter to +24.
- 34% of respondents expect their profitability to increase over the next year and just over half expect it to remain steady.
- Respondents continue to cite a lack of demand as the biggest single impediment to profitability. Post-farmgate agribusinesses are also generally confident about their growth – 60% predict that their output will increase and 17% plan to hire more staff in the next year.
- 12 month ahead capital expenditure intentions declined to a still optimistic +22 in the June quarter. With an upbeat industry outlook for the next 12 months and expectations that interest rates will remain low in the foreseeable future, 38% of respondents plan to increase capital expenditure in the coming year.

Figure 11: Expected business conditions – 12 months

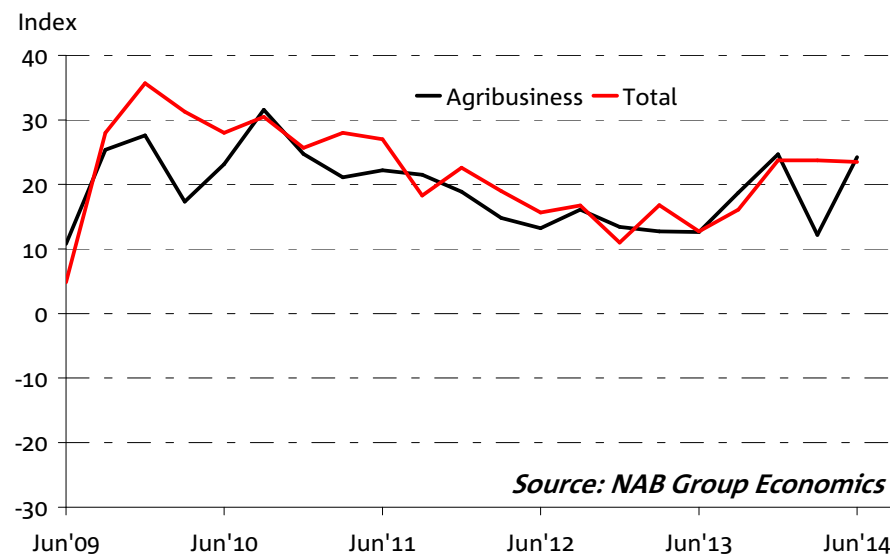
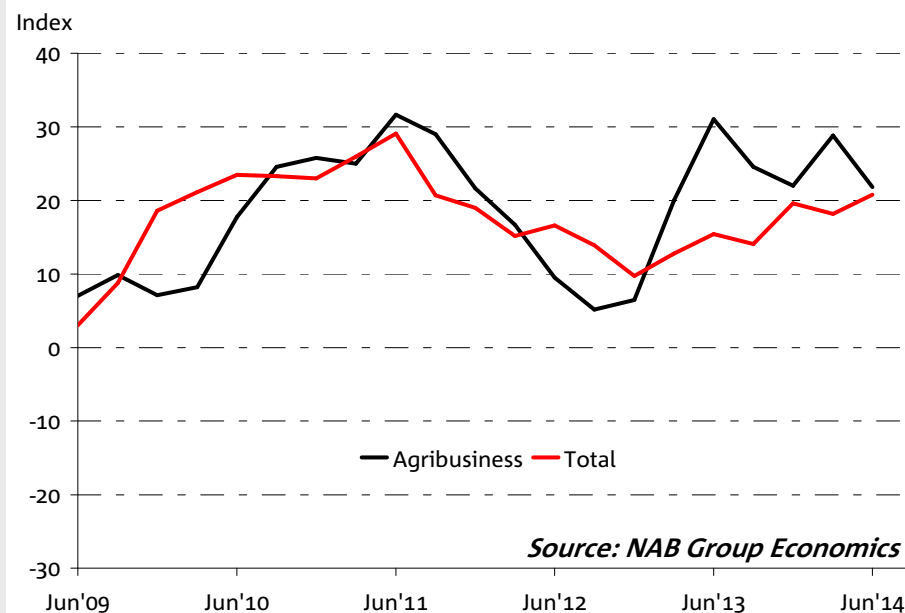


Figure 12: Capital expenditure conditions – 12 months



Forward orders

- Forward orders of post-farmgate agribusinesses fell in the June quarter from +10 to -2, just below their 5-year average level of -1. Only 9% of respondents reported an increase in forward orders in the June quarter, compared to 17% in the March quarter. The decline is consistent with moderating exports and generally weaker agribusiness conditions.
- The decline in forward orders comes as beef and lamb slaughter rates are expected to slow after high slaughter rates earlier in the year. A forecast smaller winter crop and the prospect of El Niño emerging later this winter, combined with soft world prices for several agricultural commodities, may also be weighing on the minds of producers.
- Total business forward orders were largely steady in the June quarter at +2, reflecting mostly unchanged domestic and foreign demand conditions.

Figure 13: Agribusiness forward orders

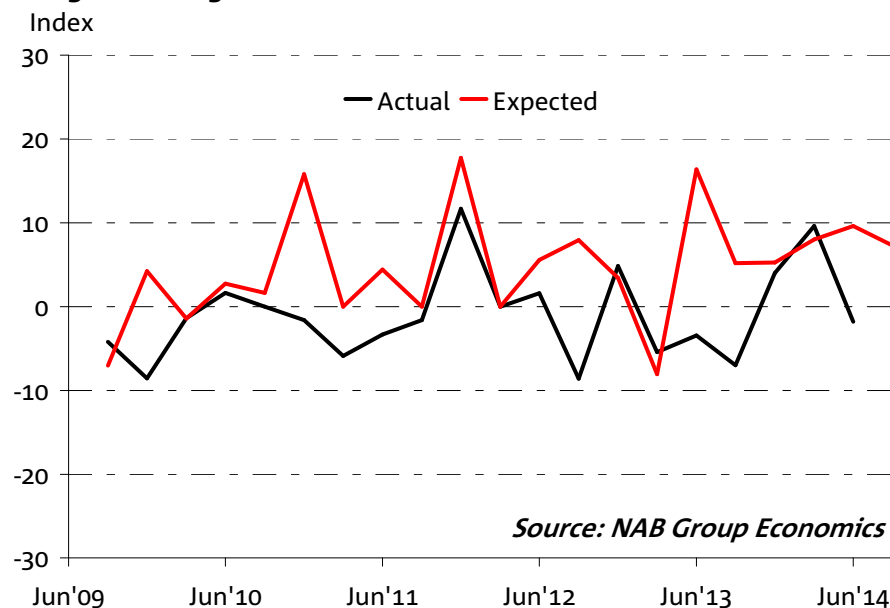
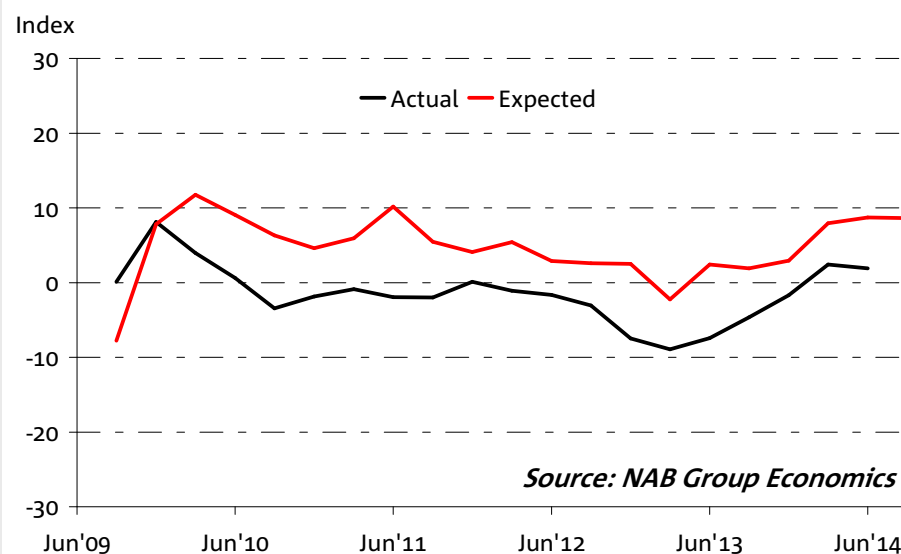


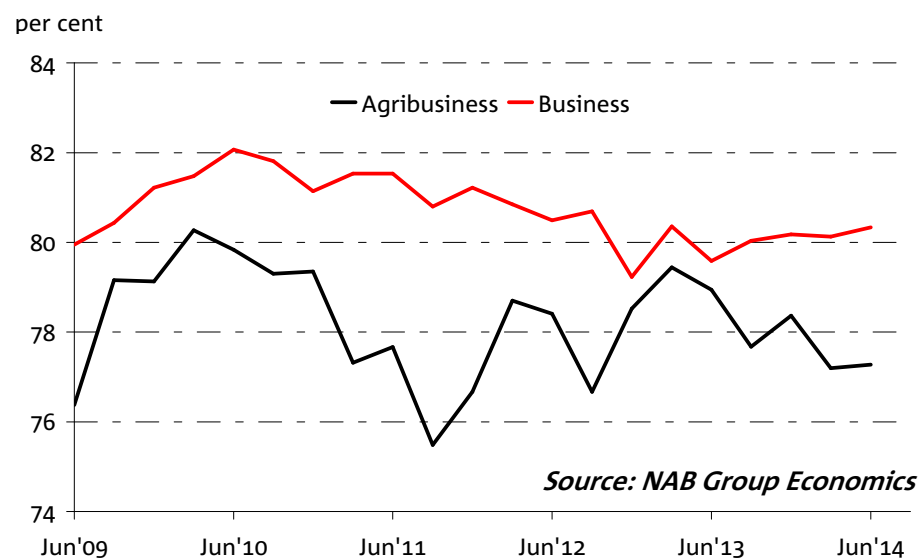
Figure 14: Total business forward orders



Capacity utilisation

- Post-farmgate agribusiness capacity utilisation was largely unchanged in the June quarter, up 0.1 percentage point to 77.3%. Capacity utilisation remains 1.2 percentage points below the 5-year seasonal average.
- Post-farmgate agribusinesses continue to report lower capacity than the total business average, reflecting a greater need by agribusinesses to maintain excess capacity to meet considerably more volatile agricultural production. Agribusiness sectors with output linked to climatic conditions, such as beef, grains and dairy tend to report lower capacity utilisation than sectors less exposed to climate, such as poultry production.

Figure 15: Capacity utilisation



Inventories

- Inventories continued to decline in the June quarter to +2, based on cyclical factors as agribusiness stocks are run down towards the winter months. Overall, inventories have been tending upwards over the past 5 years, with the June quarter result well above the 5-year seasonal average of -4.
- Respondents expect stocks to continue to decline in the coming quarter. A total of 55% expect stocks to remain unchanged and 20% expect a decline. These expectations are at odds with past experience, as agribusinesses have historically entered a stock rebuilding phase in the September and December quarters. However, given the weak correlation between stock expectations and actual results over the history of the survey, there is limited cause for concern at present.



Figure 16: Agribusiness stocks

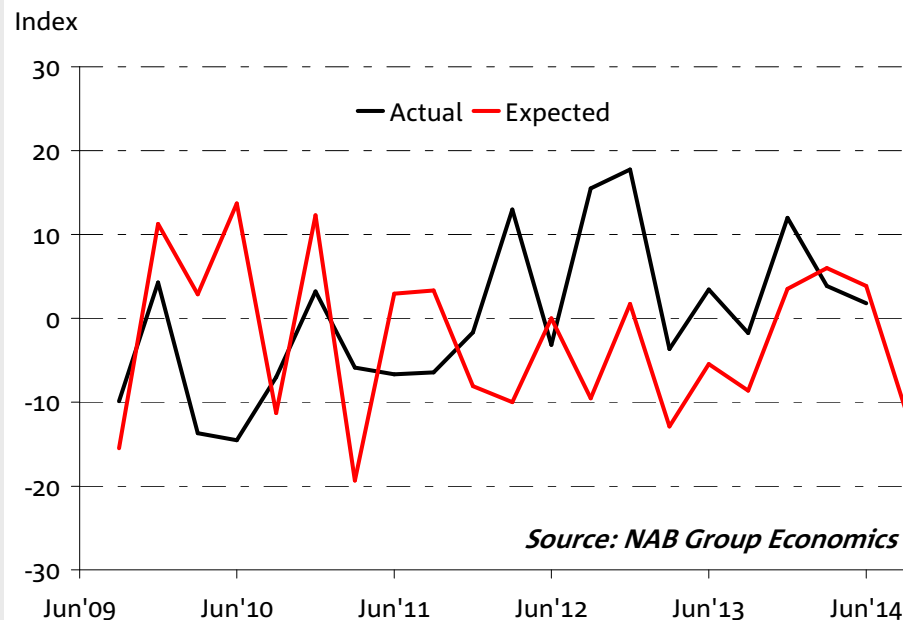
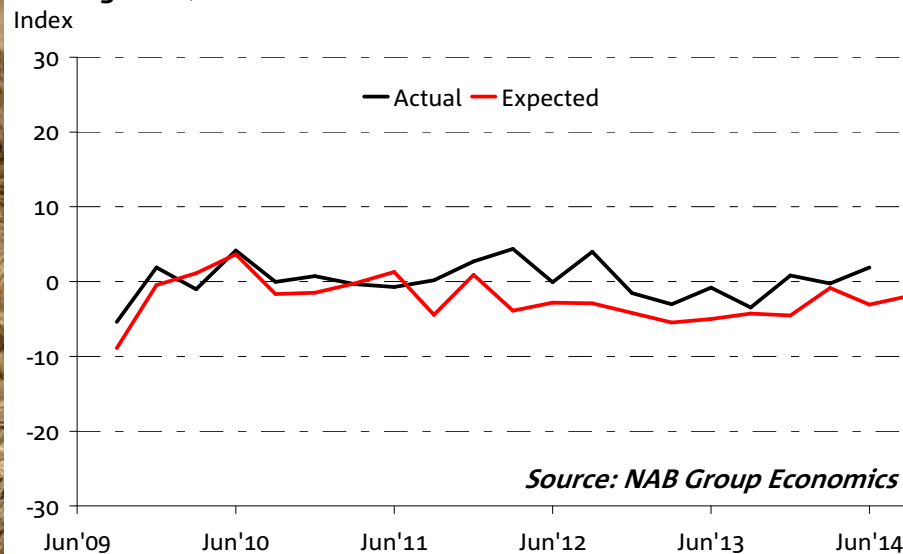


Figure 17: Total business stocks



Exports

- The export sales index has fallen since the March quarter but remains squarely in positive territory at +4, above the 5-year average of +2. The export sales index fell less than the trading index, reflecting the low reported influence of exchange rates on trading and profitability. However, the appreciation of the AUD in the June quarter may have influenced the result at the margin.
- Export expectations have fallen considerably since the March quarter, when respondents had the highest expectations in 7 years. With expectations in the previous 4 quarters well in excess of actual results, it is perhaps unsurprising that expectations for the quarter ahead declined. However, expected export sales continue to point to growth in the coming quarter.
- Post-farmgate agribusiness expectations of the AUD over the next 6 months average 90.5 US cents, slightly lower than the average business estimate of 91.5 US cents. These expectations are well above NAB's forecasts of AUD performance. We project that the AUD will fall to 85 US cents by the December quarter and to 83 US cents in the March quarter 2015.

Figure 18: Agribusiness export sales

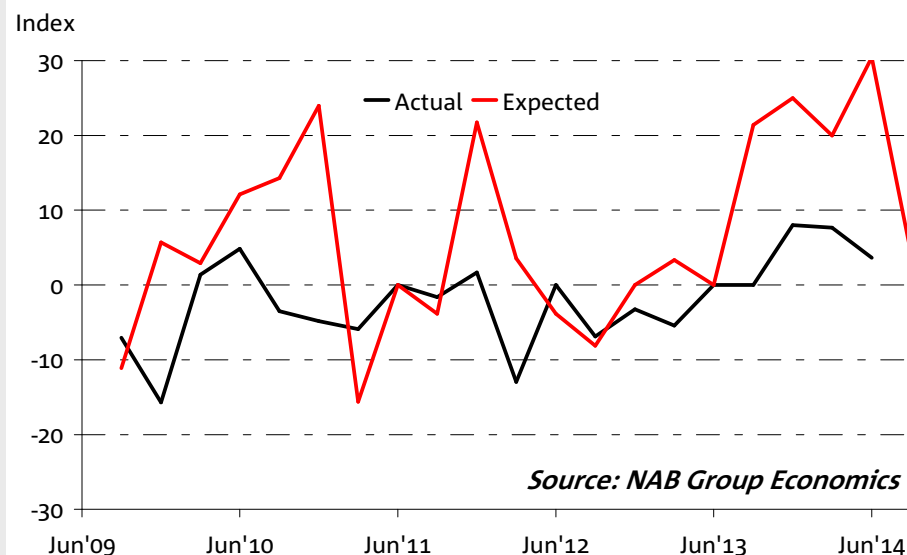
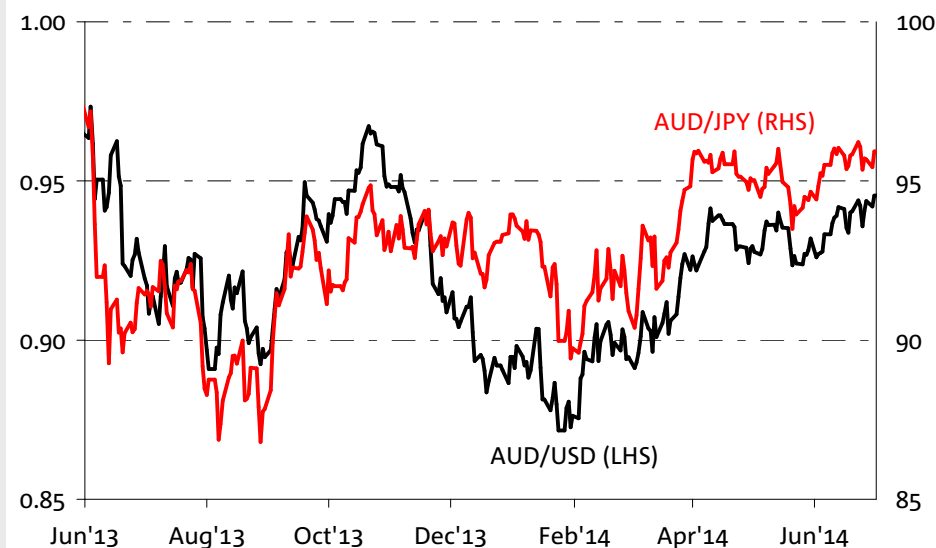


Figure 19: Currency movements



Source: NAB Group Economics

Agribusiness confidence

- While post-farmgate agribusiness conditions and confidence declined in the June quarter, sub-sector level confidence results point to increasing confidence over the next three months.
- Confidence in crops was up as producers look towards a winter harvest likely to perform reasonably well after a disappointing summer. Although ABARES expects winter crop production to fall 12% in 2014-15 after a bumper 2013-14 season, this heralds an improvement on the poor summer crop, which dropped 33%. Confidence in fibres also improved, with both cotton and wool recording gains.
- Confidence was also up for pasture reliant stock such as beef, lamb and dairy as pastures rebounded after decent autumn rainfall across key production regions and drought conditions eased in northern New South Wales and Queensland.
- Confidence in farm inputs, such as chemicals and equipment stayed in positive territory, although farm chemicals declined somewhat.

Figure 20: Agribusiness confidence in wheat and sugar

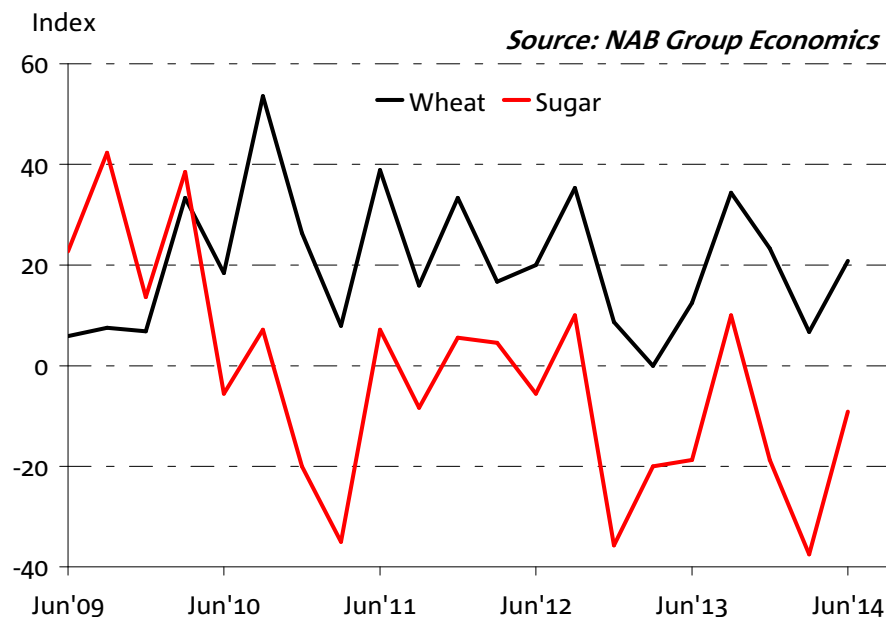


Figure 21: Agribusiness confidence in other crops and wine

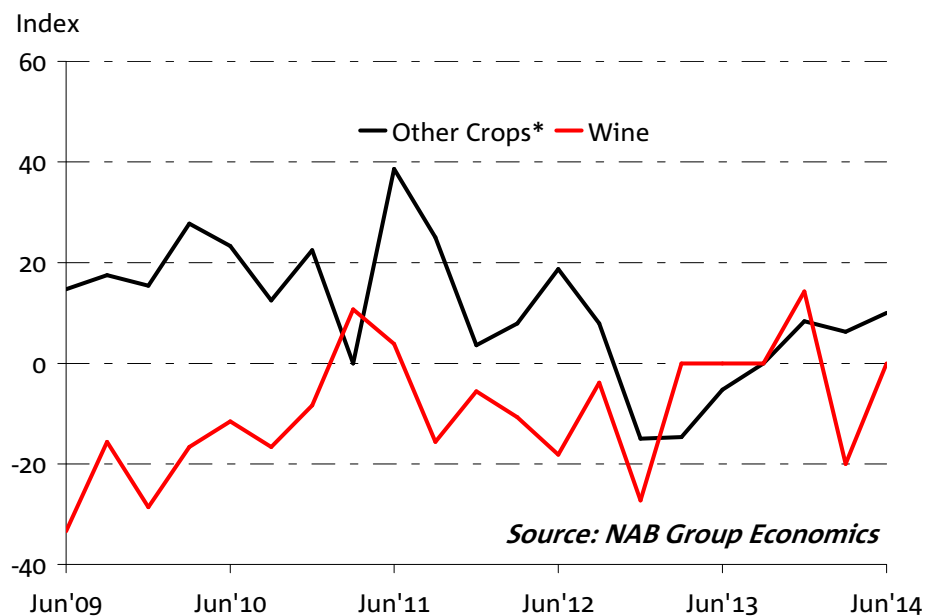


Figure 22: Agribusiness confidence in poultry and sheep meat

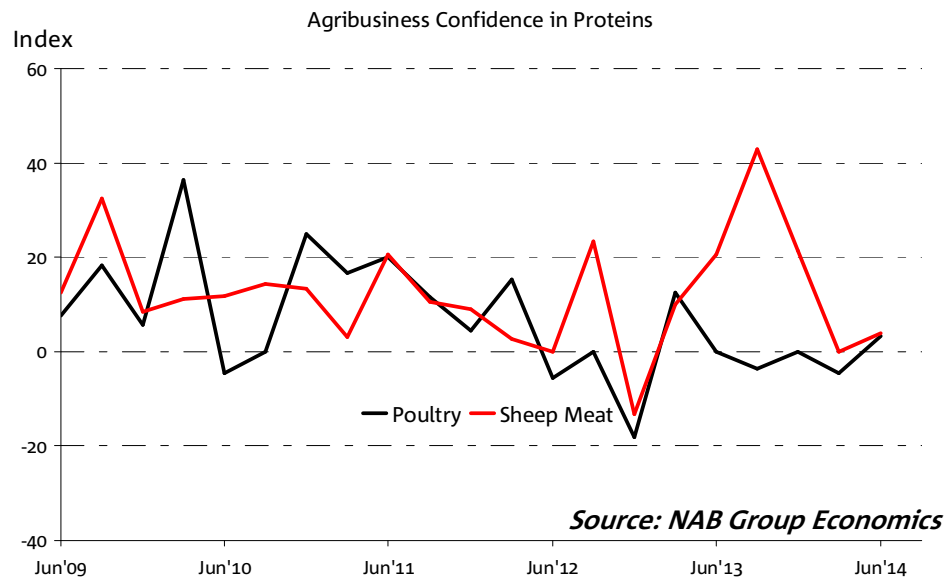


Figure 24: Agribusiness confidence in fibres

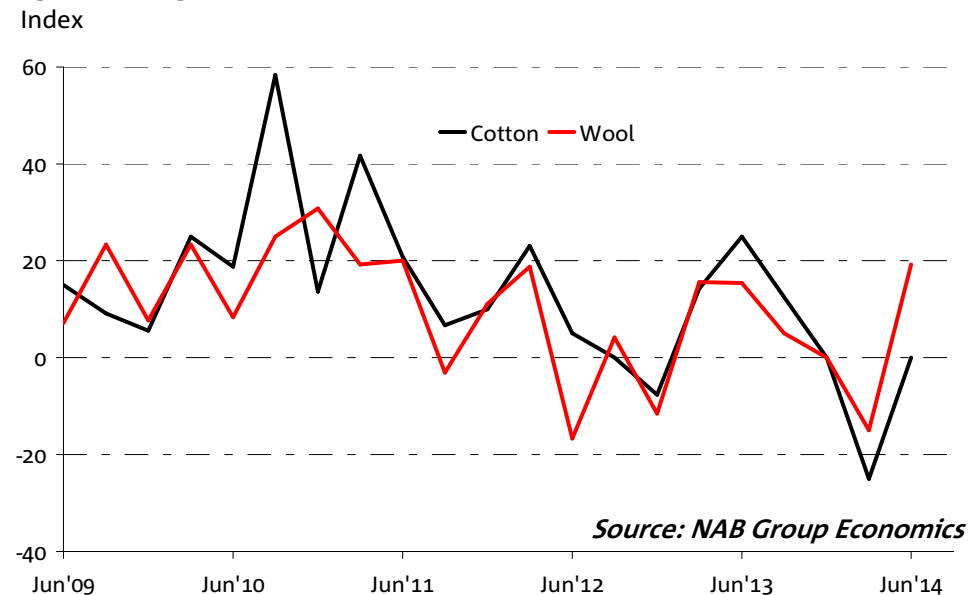


Figure 23: Agribusiness confidence in beef and dairy

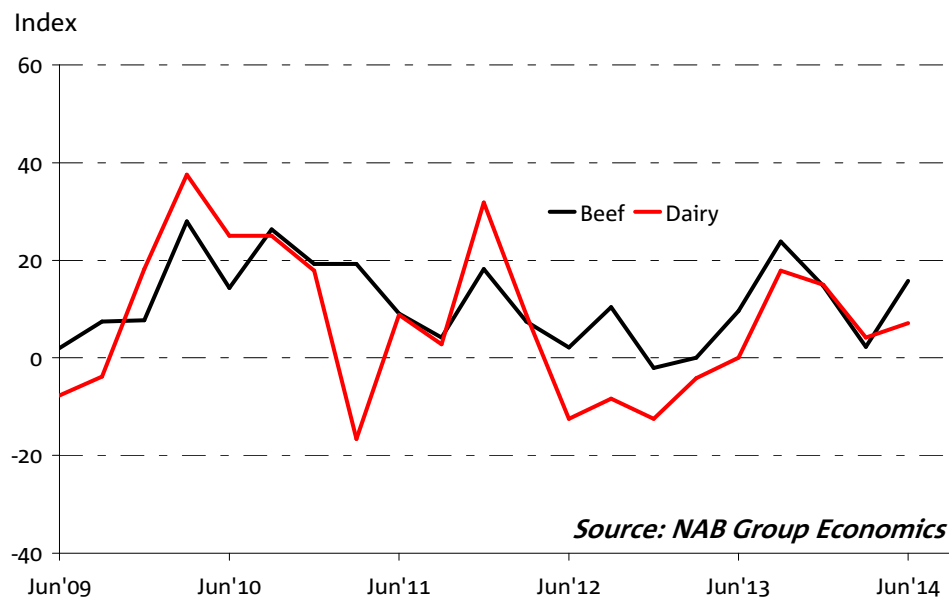
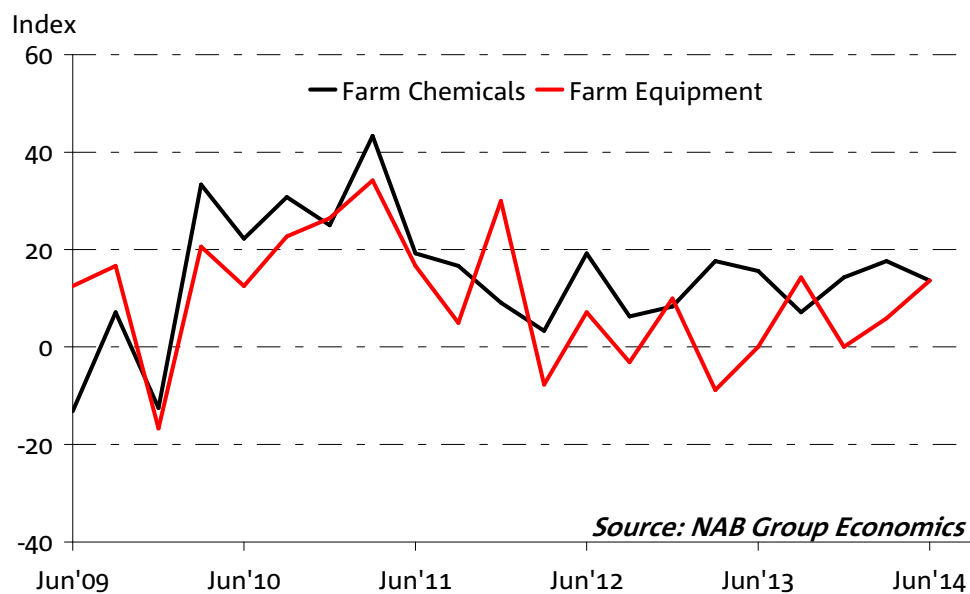


Figure 25: Agribusiness confidence in farm inputs



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