



# Economic Report

## Rural Commodities Wrap – September 2015

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## Key points

- Agricultural prices diverged in August and into September – protein and fibres generally rose while crops trended lower. Overall, the NAB Rural Commodities Index was flat in AUD terms in August (down 0.1%) and moderately lower in USD terms (down 2.0%).
- The AUD continued its downward trajectory in August, before sinking below 70 US cents in early September. The AUD sustained something of a recovery in mid-September but has subsequently faced renewed downward pressure. Our AUD/USD forecast reflects the likelihood of continued terms of trade weakness, ongoing risks to the growth outlook globally and in China in particular as well as USD appreciation as the Fed commences tightening late this year (or early next).
- Rainfall continued to be patchy in August and into September although good rains in Western Australia and New South Wales have led us to boost our outlook for the 2015-16 wheat harvest. With the impact of El Niño now likely to appear later in spring and into summer, the major climatic risk is for graziers and summer crops.

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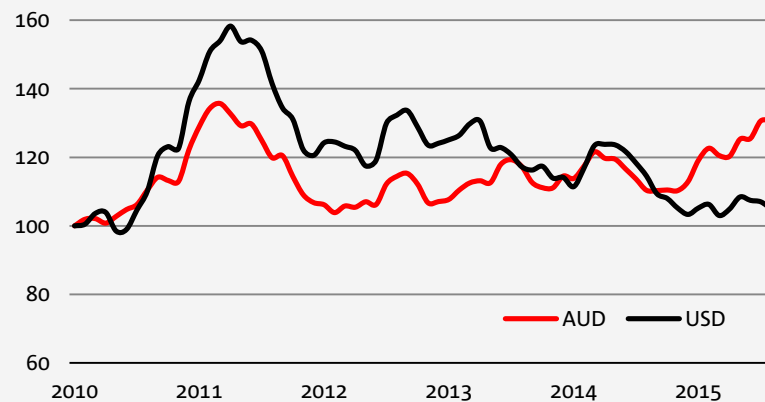


## NAB Rural Commodities Index

The NAB Rural Commodities Index was flat in AUD terms in August (down 0.1%) and moderately lower in USD terms (down 2.0%). The flat overall result masks price divergence in August and into September – protein and fibres generally rose while crops trended generally lower on favourable grain supply and expectations of a strong global harvest.

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.

Figure 1: NAB Rural Commodities Index



Source: NAB Group Economics, ABARES, Meat and Livestock Australia, Australian Pork, Ausmarket Consultants, BNZ, Australian Bureau of Statistics, Bloomberg and Profarmer. January 2010 = 100

## Production and Price Outlook

The Bureau of Meteorology’s declaration of El Niño earlier this year clouds the production outlook, particularly coming into summer. While we have previously highlighted the risk of El Niño to Australia’s wheat crop, solid rainfall in Western Australia and New South Wales has led us to boost our outlook for the 2015-16 harvest. With the impact of El Niño now likely to appear later in spring and into summer, the major climatic risk is for graziers and summer crops.

We have also adjusted our price forecasts in line with market conditions. With signs that declining beef slaughter is likely to continue owing to a shortage of stock, we see continuing upside for prices. Furthermore, a striking reversal in Global Dairy Trade auction results, reflecting likely lower New Zealand supply, has seen an upgrade to our dairy forecast. Price and production forecasts for major commodities are shown in *Table 1*.

Table 1: June 2015 price movements, production and price forecasts for major agricultural sectors

	Month on month price change (AUD)	2015-16 annual production change	2015-16 annual price change (AUD)
Wheat	▼ 5.0%	▲ 1.4%	▲ 8.6%
Beef	▲ 4.6%	▼ 8.2%	▲ 43.0%
Dairy	▼ 6.6%	▲ 0.7%	▲ 1.1%
Lamb	▲ 0.3%	▼ 1.0%	▲ 1.2%
Wool	▲ 2.8%	▼ 12.0%	▲ 9.6%
Sugar	▼ 8.8%	▲ 6.4%	▲ 1.1%
Cotton	▲ 0.8%	▲ 4.4%	▲ 14.9%

Source: NAB Group Economics, ABARES, Meat and Livestock Australia, Bloomberg, BNZ and Profarmer. Forecasts represent year-on-year average changes.

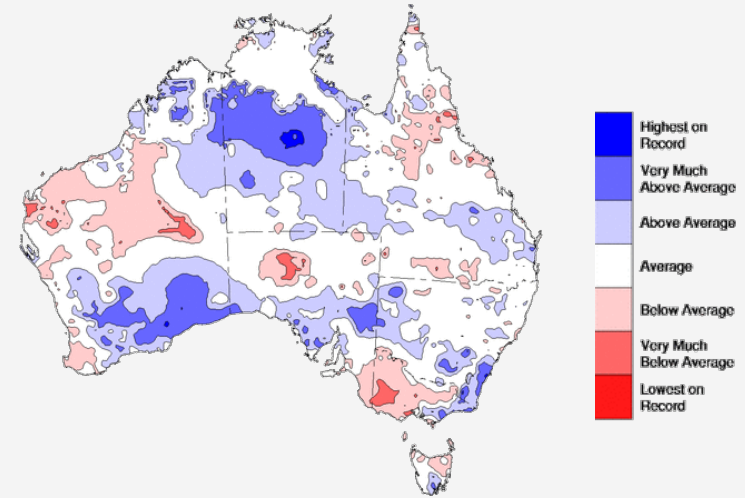
## Climatic Conditions

Rainfall continued to be mixed in August, with above average falls in much of New South Wales, southern and central Queensland, the Northern Territory, parts of the Western Australian wheatbelt and goldfields and South Australia's Eyre Peninsula. However, parts of northern Queensland, the Gascoyne, and much of Victoria and northern Tasmania received below average to well below average rainfall. Western Victoria in particular suffered difficult conditions.

Challenges remain approaching summer, compounded by the presence of El Niño since May this year. El Niño causes generally lower winter and spring rainfall in northern and eastern Australia and can continue well into summer.

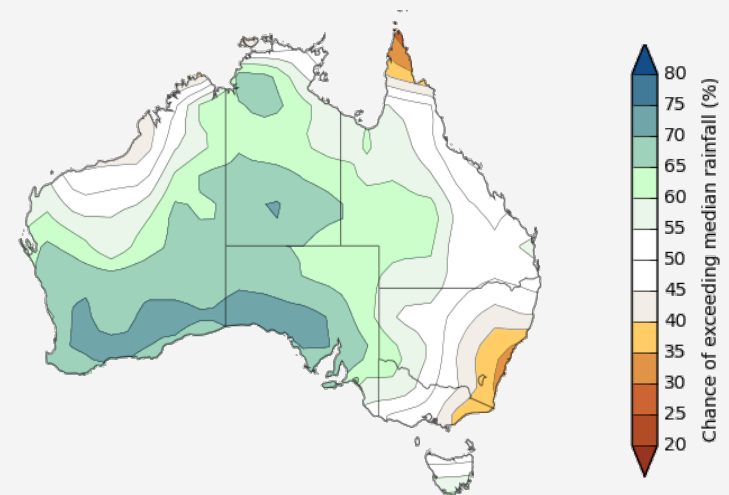
*Figure 3* shows the three-month rainfall outlook to November, which forecasts below average rainfall from Gippsland to the New South Wales central coast as well as in parts of Cape York.

Figure 2: Australian rainfall deciles – August 2015



Source: Bureau of Meteorology

Figure 3: Rainfall outlook – September to November 2015



Source: Bureau of Meteorology



## Economic Update

For detailed analysis of Australian and global economic trends see our [Global and Australian Forecasts](#). Below is a précis of this report.

### Global Economy

Growth in global GDP has disappointed by staying around 3¼% yoy since mid-2014 rather than picking up. The latest data for industrial output and world trade still show weak growth (only 0.1% in the June quarter). World trade is faring even worse with volumes falling by 0.5% in the June quarter after a 1½% drop in the March quarter. Partial data for industrial activity does not show any pick-up in global activity since June. At the same time, falling commodity prices are eroding export earnings in key primary producers. However, limited data available shows service sector growth easily outpacing industry.

### Domestic Economy

Australian real GDP is struggling to regain momentum, against a weak income backdrop and significant structural change at the industry and geographic level. The economy expanded by just 0.2% in the June quarter and 2.0% over the year. Australian income growth is weak as the terms of trade declines further. On the other hand, there is some evidence that momentum in the non-mining sector (beyond dwelling construction) is taking place and responding to lower rates and the weaker AUD. Gross value added in services industries such as ITC, finance & insurance and hospitality was solid in Q2. Net tourism exports continue to expand and business conditions and capacity utilisation are trending up, despite the understandable dip in confidence amidst global volatility.

### Interest Rates

Global financial market ructions and a slower China suggest the risks to the Australian economic forecasts and the RBA cash rate are tilted to the downside near term. At this stage, however, the RBA is likely to sit back and wait for a clearer global picture to emerge, and will at least be comforted by the “natural hedge” being provided by the lower AUD. The case for further easing on purely domestic grounds is limited in our view amidst a trend improvement in business conditions and capacity utilisation and a stronger than expected labour market.

**Table 2: NAB Global Economic Forecasts**

% change year on year	2015	2016	2017
China	7.1	6.9	6.5
United States	2.5	2.5	2.4
Euro zone	1.3	1.7	1.9
Emerging East Asia	3.7	3.8	4.1
Japan	0.7	1.2	1.0
Advanced economies	2.0	2.1	2.1
Emerging economies	4.8	4.9	4.9
World GDP	3.1	3.2	3.4

Source: NAB Group Economics

**Table 3: NAB Australian Economic Forecasts**

% change year on year	2015	2016	2017
GDP growth	2.3	2.7	3.3
Private consumption	2.5	2.5	2.7
Unemployment rate (year end)	6.1	5.8	5.8
Consumer Price Index (core)	2.5	2.6	2.4

Source: NAB Group Economics

**Table 4: NAB Interest Rate Forecast (end of quarter)**

	2015 Q1	2015 Q2	2015 Q3	2015 Q4
RBA Cash Rate	2.25	2.0	2.0	2.0

Source: NAB Group Economics

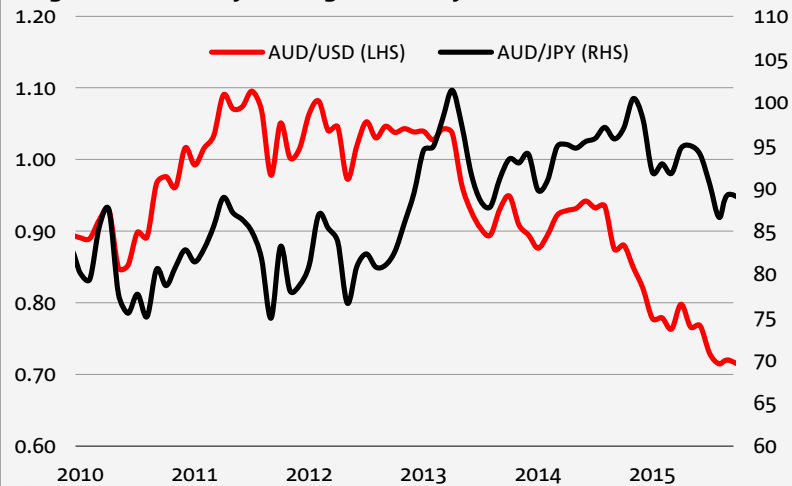
## Exchange Rates

The AUD continued its downward trajectory in August, before sinking below 70 US cents in early September. The AUD sustained something of a recovery in mid-September but has subsequently faced renewed downward pressure.

Our AUD/USD forecast reflects the likelihood of continued terms of trade weakness (although the drop on a TWI basis is not as pronounced), ongoing risks to the growth outlook globally and in China in particular as well as USD appreciation as the Fed commences tightening late this year (or early next).

We forecast the AUD to reach 70 US cents by the end of year before bottoming out in Q1 2016 at 68 US cents. This represents an upside for local prices and is good news for Australian agricultural producers and the expectation for the AUD to drop to 70 US cents by year end has materialised a little earlier than predicted, suggesting further scope for downside risk.

Figure 4: Monthly average currency movements



Source: DXdata, NAB

Table 5: NAB FX Strategy Targets

		2015 Q4	2016 Q1	2016 Q2	2016 Q3
Australian Dollar	AUD/USD	0.70	0.68	0.69	0.70
New Zealand Dollar	NZD/USD	0.62	0.60	0.60	0.61
Japanese yen	USD/JPY	125	126	126	127
Euro	EUR/USD	1.05	1.03	1.03	1.04
British Pound	GBP/USD	1.52	1.51	1.51	1.53
Swiss Franc	USD/CHF	1.01	1.04	1.04	1.04
Chinese New Yuan	USD/CNY	6.55	6.60	6.62	6.65
Canadian Dollar	USD/CAD	1.35	1.37	1.36	1.34

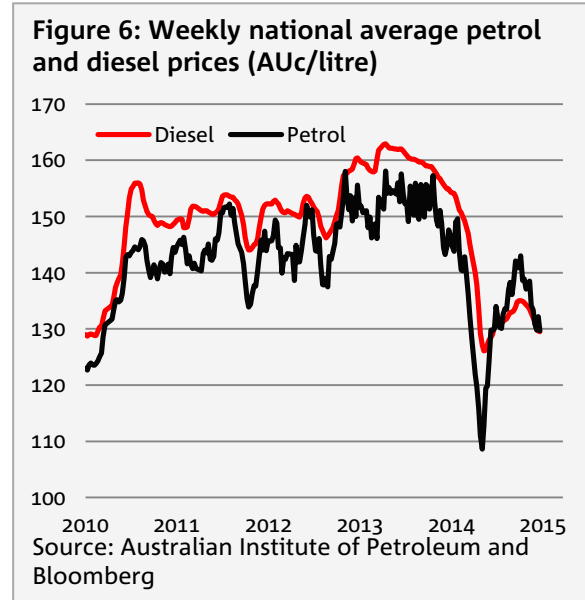
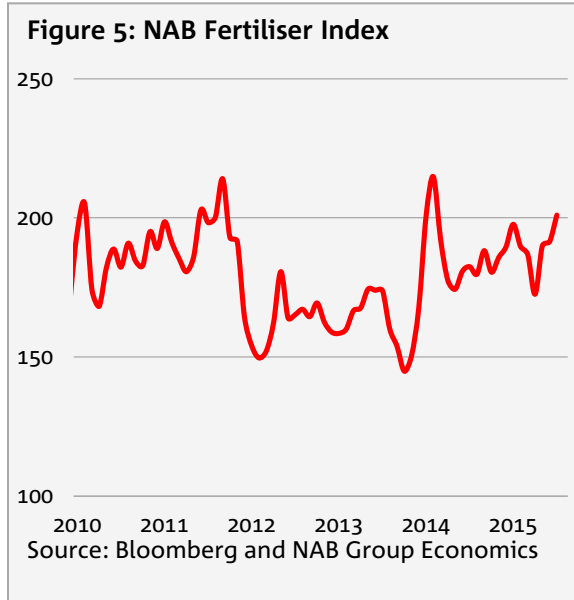
Source: NAB



## NAB Farm Input Prices

The NAB Fertiliser Index was up 1.0% in AUD terms in July as the lower AUD offset lower international urea prices.

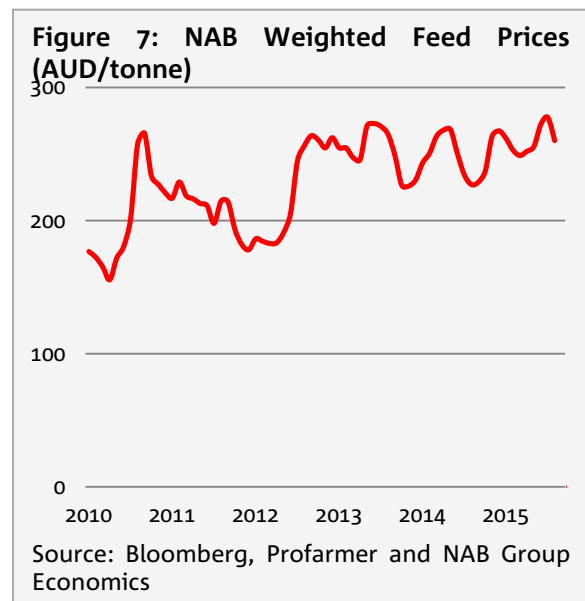
National average petrol prices fell 3.2% in August, while diesel prices were 1.5% lower for the month. This came as global oil prices resumed their downward slide. The AUD is forecast to fall further in the coming months, presenting a moderate upside risk for fuel prices.



## Weighted Feed Grain Prices

Weighted feed grain prices fell in August (down 6.3%), the first monthly price drop since March 2015. This reflects generally lower prices among major feed grains in domestic markets as a result of buoyant international supply. The prospect of strong El Niño conditions coming into summer could see elevated domestic feed grain demand as graziers look for additional supplementary feed.

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.



## Crops

### Wheat

Generic 1<sup>st</sup> Australian milling wheat prices fell in August and into September – down 5.0% to average AUD309.67/tonne for August on higher expected supply. Global wheat supply remains generally favourable and the USDA has revised up its global 2015-16 wheat production forecast by 6.7 million tonnes, reflecting good crops in the European and Black Sea growing regions.

### Coarse grains

Coarse grains generally followed wheat lower through August and into September, with the exception of rice, which was up 7.4% in AUD terms for August.

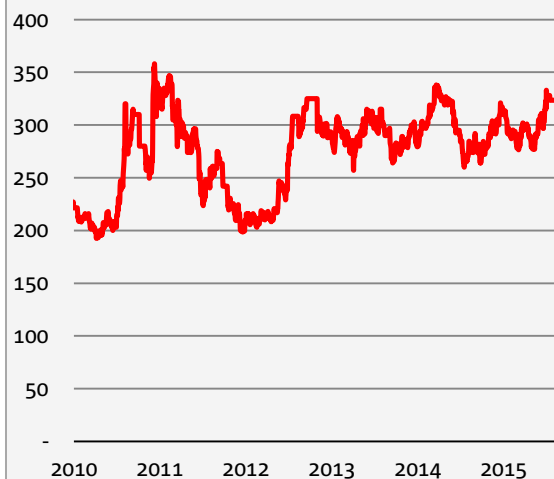
### Oilseeds

Domestic canola was also down, but somewhat less than wheat and coarse grains. Overall, canola (Newcastle NSW) was down 3.3% (AUD) in August.

### Pulses

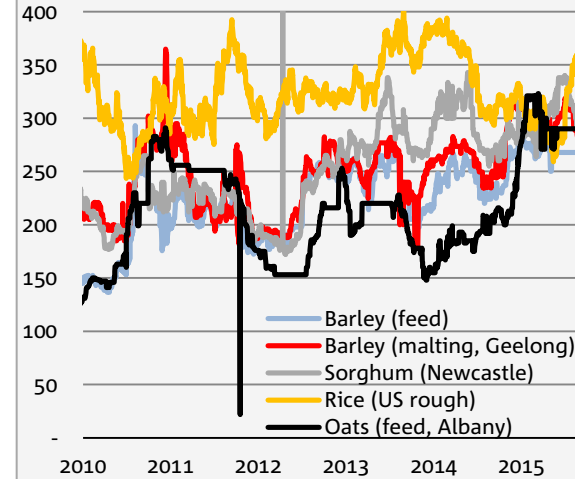
Chick peas' stellar run, which saw prices surge from less than AUD500/tonne at the end of 2014 to almost AUD900/tonne in late July this year, appears to have abated. Chick peas (Brisbane) were off 8.9% in AUD terms to average AUD800.48 in August. Field peas were similarly lower, off 7.1% (AUD) in August.

**Figure 8: Generic 1<sup>st</sup> Australian milling wheat (AUD/tonne)**



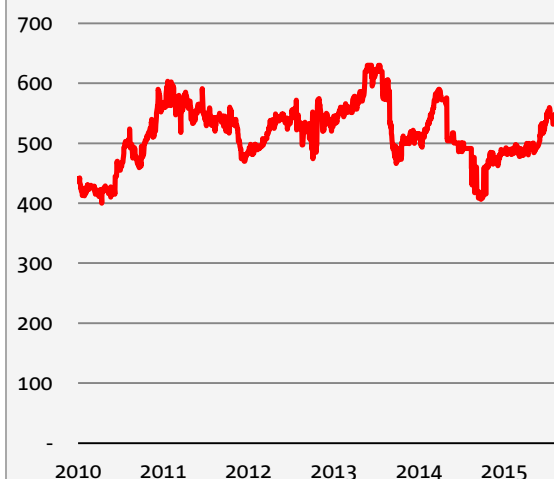
Source: Bloomberg

**Figure 9: Selected coarse grains (AUD/tonne)**



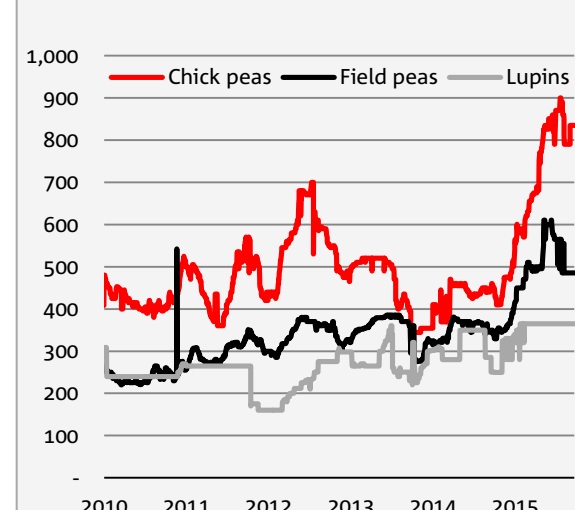
Source: Bloomberg, Profarmer

**Figure 10: Canola, Newcastle NSW (AUD/tonne)**



Source: Bloomberg, Profarmer

**Figure 11: Selected pulses (AUD/tonne)**



Source: Bloomberg, Profarmer



## Protein

### Beef

The Eastern Young Cattle Indicator continues its run well record territory and is approaching 600AUc/kg. Overall, the indicator was up 4.6% in August.

The downward trend in slaughter that began mid-year is continuing and exports have now begun to slow. August exports were down 10.0% to the US, 15.1% to Japan and 20.1% to Korea. While Australia-US 90cl export prices remain elevated, there are signs that US domestic beef prices are beginning to moderate.

### Lamb

Lamb prices were steady in August (up 0.3% AUD), with the Eastern States Trade Lamb Indicator averaging 588 AUc/kg. With the arrival of the spring lamb flush, prices have since moderated but remain higher than the same time last year.

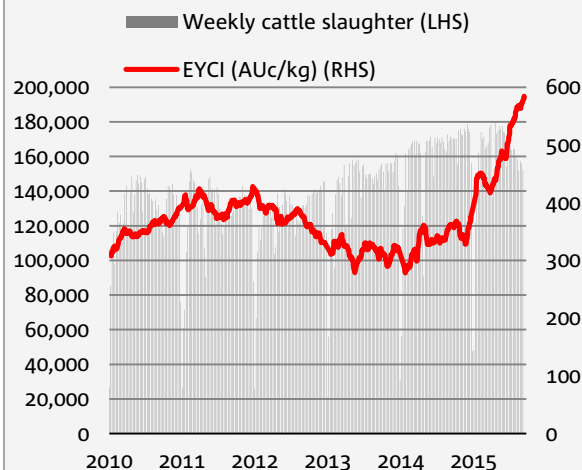
### Pork

Australian wholesale pork prices (measured as an average of buyer and seller prices for eastern seaboard 60.1-75kg animals) were up 1.6% (AUD) in August, reflecting continued stability in prices in the industry.

### Poultry

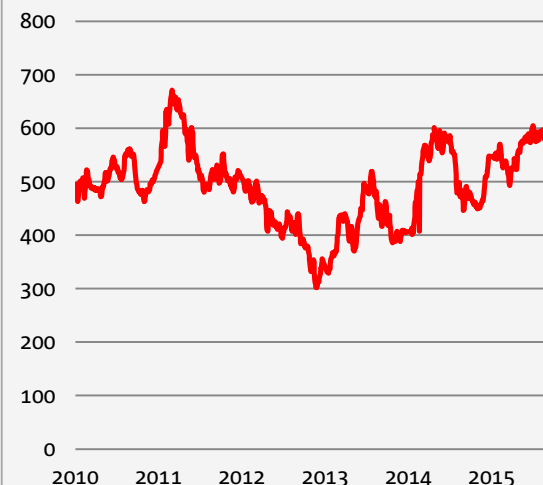
While we do not collect wholesale poultry price data, retail prices have remained stable since late 2012, gaining falling 0.3% in the June quarter (the most recent data available).

**Figure 12: Eastern Young Cattle Indicator (AUc/kg)**



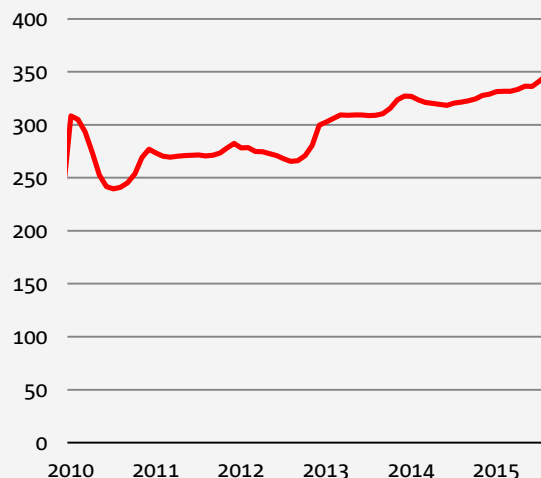
Source: Meat and Livestock Australia

**Figure 13: Eastern States Trade Lamb Indicator (AUc/kg)**



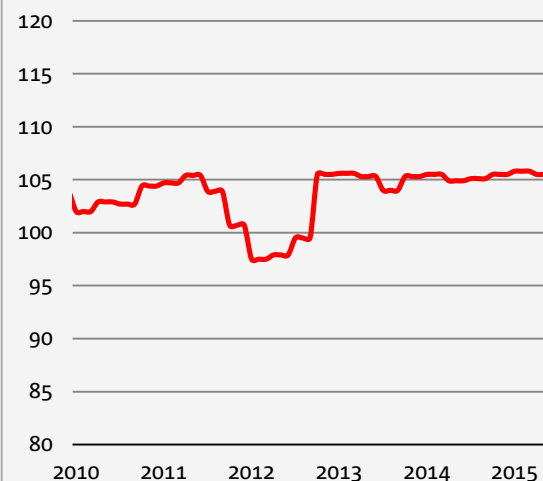
Source: Meat and Livestock Australia

**Figure 14: Pork – 60.1-75kg (AUc/kg)**



Source: Australian Pork. Average of buyer and seller price for the eastern seaboard.

**Figure 15: Poultry – Australia (ABS index)**



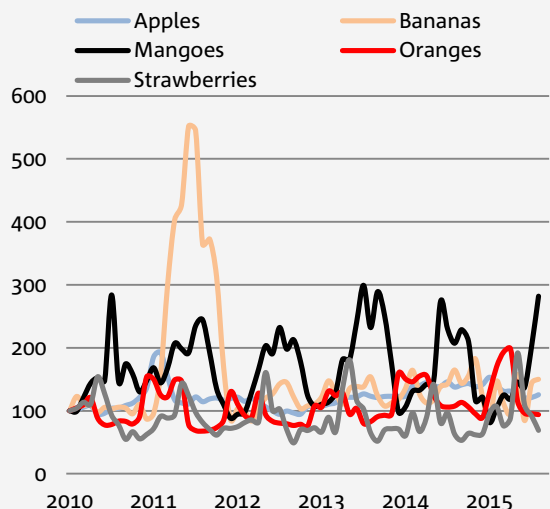
Source: Australian Bureau of Statistics

## Fruit

The NAB Fruit Price Index, based on data from the Melbourne and Sydney wholesale markets, continued to gain in August and was up 10.9% for the month. The rise was led by mangos at Sydney wholesale market.

The index stands at 148.8 for August 2015 (note January 2010 = 100), 3.8% higher than the same time in 2014.

**Figure 16: Wholesale market price index, selected fruit – Sydney and Melbourne**



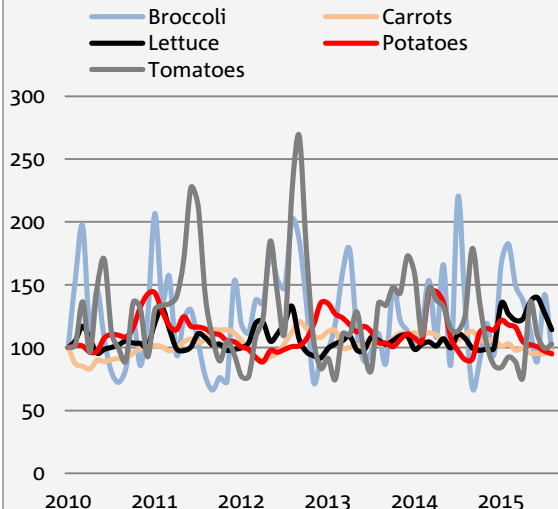
Source: Ausmarket Consultants and NAB Group Economics

## Vegetables

The NAB Vegetable Price Index, based on data from the Melbourne and Sydney wholesale markets, fell again in August, down 7.0% (AUD).

The index stands at 102.3 for August 2015 (note January 2010 = 100), 8.2% lower than the same time in 2014.

**Figure 17: Wholesale price index, selected vegetables – Sydney and Melbourne**



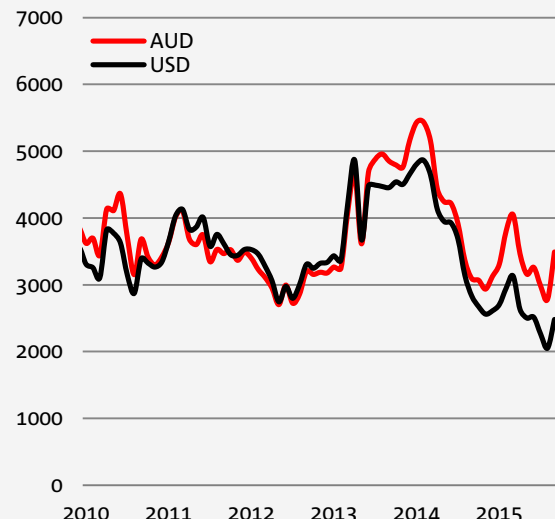
Source: Ausmarket Consultants and NAB Group Economics

## Dairy

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.

There have been sharply higher prices at the last three GDT auctions, beginning from 16 August. However, due to the weighting of NAB's indicator, we report lower prices for August, down 6.6% (AUD). Nonetheless, September results have rebounded over 25% from their August level.

**Figure 18: NAB monthly weighted dairy price indicator (\$/tonne)**



Source: Global Dairy Trade and NAB Group Economics

## Fibres

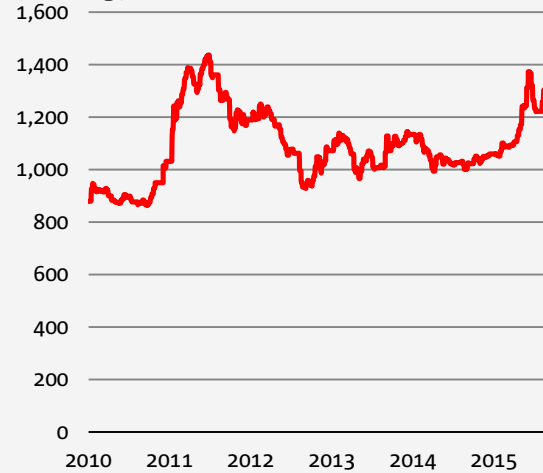
### Wool

Wool's rally peaked in mid-June with the Eastern Market Indicator approaching 1400 AUc/kg. Since then, there has been some pressure but prices remain elevated. The index was up 2.8% (AUD) in August.

### Cotton

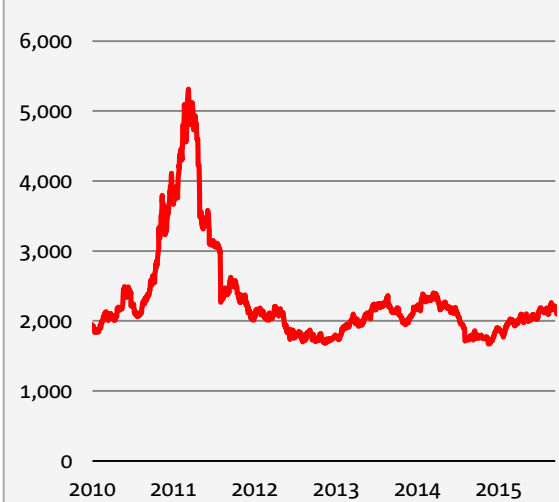
Global cotton prices were steady in August in AUD terms, with Cotlook A up 0.8% (AUD). Although cotton is now trading above the same time last year and AUD prices have recovered from late 2014 lows.

**Figure 19: Wool - Eastern Market Indicator (AUc/kg)**



Source: Bloomberg

**Figure 20: Cotlook A cotton (AUD/tonne)**



Source: Bloomberg

## Industrial crops

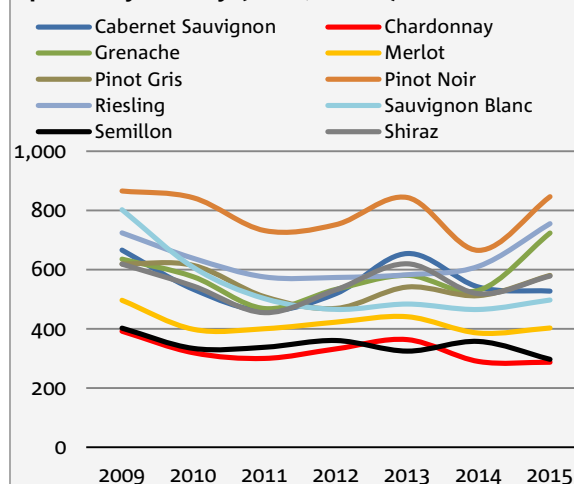
### Wine grapes

Wine Australia's 2015 Price Dispersion Report, released in July, 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.

### Sugar

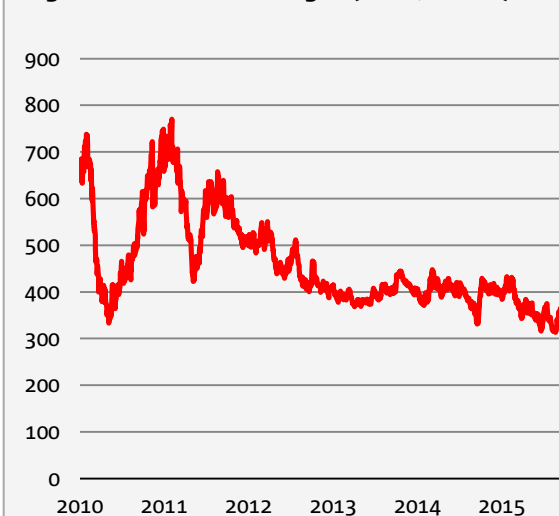
Global sugar prices fell in AUD terms in August, with ICE no.11 sugar down 8.8% (AUD). The depreciation of the Brazilian Real (Brazil being a major sugar producer) continues to affect global prices.

**Figure 21: Volume weighted wine grape prices by variety (AUD/tonne)**



Source: Wine Australia, NAB Group Economics

**Figure 22: ICE no.11 sugar (AUD/tonne)**



Source: Bloomberg

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