

agribusiness



RURAL COMMODITIES WRAP

OCTOBER 2017



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Cover photo | Carl Davies CSIRO

KEY POINTS

In September, the NAB Rural Commodities Index fell 2.2%, largely reflecting weak cattle prices. On the other hand, domestic grain prices strengthened, reflecting a premium in a season where conditions are wildly varied between regions. Parts of New South Wales and Queensland have seen record breaking temperatures in close proximity to frosts, while southern Western Australia, and more recently south-east Queensland, have seen soaking rains. This month we have again cut our wheat production forecast, this time to 18.7 million tonnes – the lowest in a decade.

The outlook for the remainder of the year and into next is somewhat more positive. The latest outlook from the Bureau of Meteorology points to average to above average rainfall for most of the continent for the rest of 2017, although temperatures are likely to be above average. Recent rains in Queensland have already seen a partial recovery in cattle prices. While the Australian dollar remains higher than most agricultural producers would like, recent pressure has been downward and we see the currency falling to 75 US cents at the end of this year and spending most of next year at the 73 US cent mark.

PRICE UPDATE



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The NAB Rural Commodities Index fell 2.2% in September, following a 7.6% plunge in August, the biggest monthly drop for the expanded index (with data going back to 2010). While the August drop was broad based, September's fall was mostly driven by lower cattle and horticultural prices, as well as moderately lower wool results. The Australian dollar has receded somewhat from its recent highs, although remains at an uncomfortable level for many agricultural producers.

MONTHLY PRICE CHANGES

AUD prices

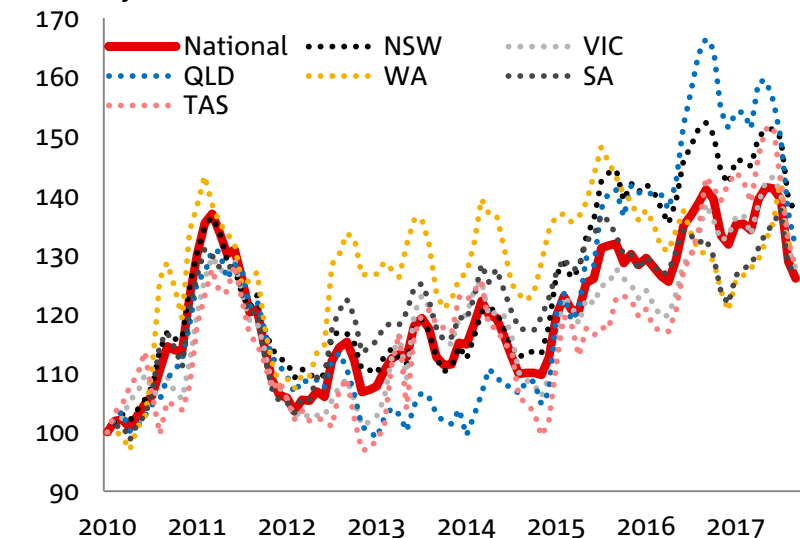
	July	Aug.	Sept.
Wheat	▲ 10.8%	▼ 13.0%	▲ 6.4%
Beef	▼ 6.3%	▼ 7.3%	▼ 5.3%
Dairy	▼ 4.2%	▼ 3.8%	▲ 0.2%
Lamb	▼ 9.1%	▲ 1.6%	▼ 0.8%
Wool	▲ 1.5%	▲ 2.5%	▼ 1.5%
Sugar	▲ 1.1%	▼ 3.7%	▲ 0.1%
Cotton	▼ 3.8%	▼ 7.1%	▲ 0.8%

On a state basis, cattle-heavy Queensland once again saw the sharpest falls, off 4.6% for the month, while New South Wales was down 2.0%. Victoria and Tasmania fell 2.9% and 3.7% respectively, while grain dependent Western Australia gained 1.0% on higher grain prices and South Australia was moderately lower, losing 0.7%.

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.

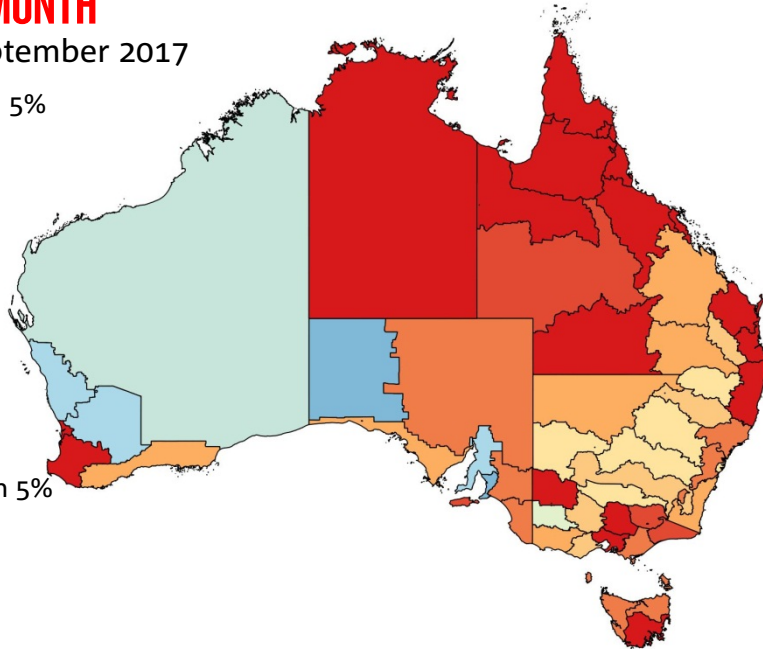
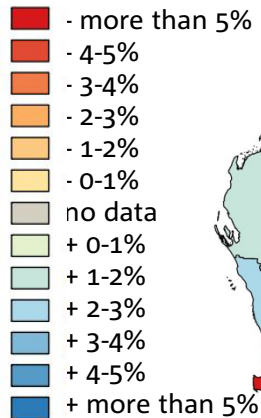


REGIONAL PRICE INDICATORS



MONTH ON MONTH

August to September 2017

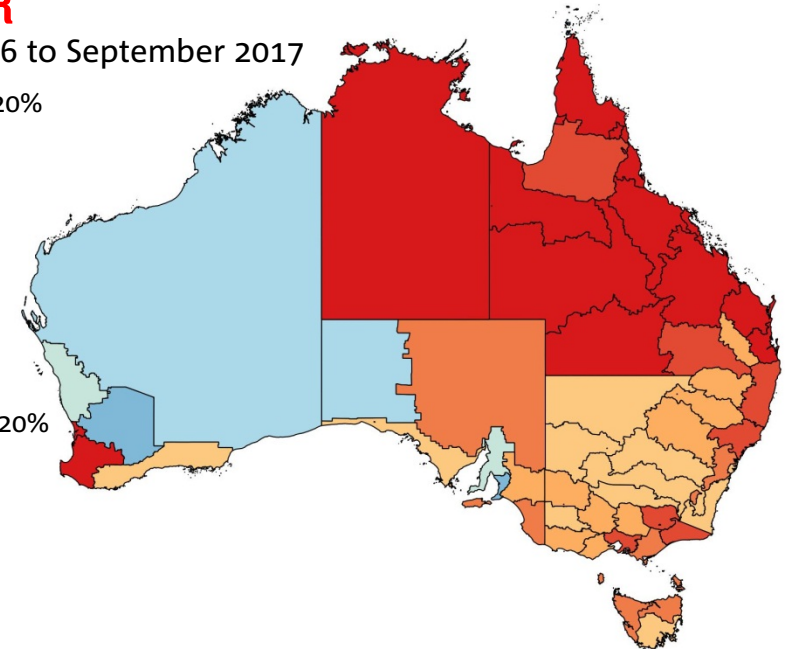
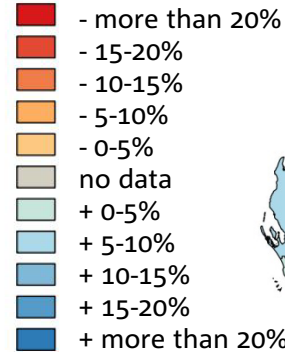


Monthly regional price indicator data shows a negative picture continuing across most of the country in September, although far less so than in August. Areas with large cattle industries, such as much of Queensland, have fared among the worst.

On a year on year basis, the best performing regions are those with a cropping focus, particularly in Western Australia and South Australia. On the other hand, cattle country across Queensland and the Northern Territory in particular has seen steep falls with prices well below their level at the same time in 2016.

YEAR ON YEAR

September 2016 to September 2017



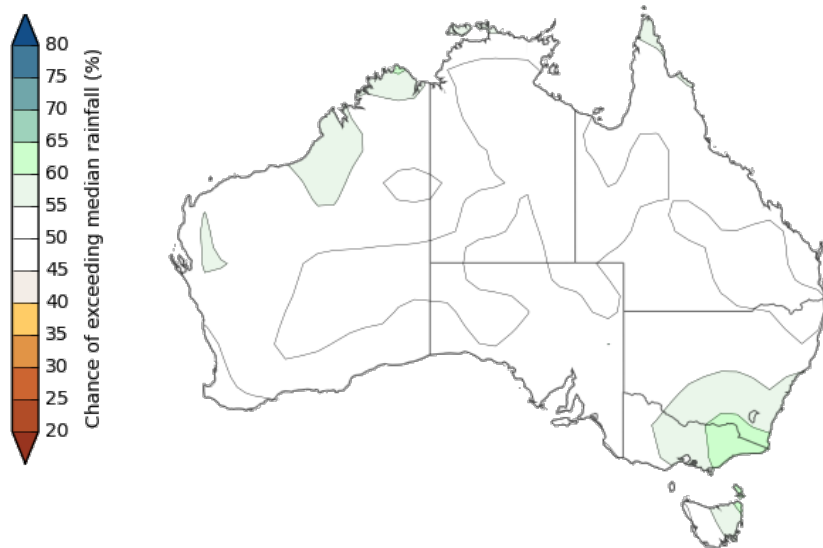
This is the sixth month of NAB's new regional price indicators – in effect a separate NAB Rural Commodities Index for every region in Australia. The product still remains in a trial stage and is calculated on a different basis to our national and regional data, without annual chain-weighting. We will continue to develop this series throughout 2018, making further improvements where possible.

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

November 2017 to January 2018

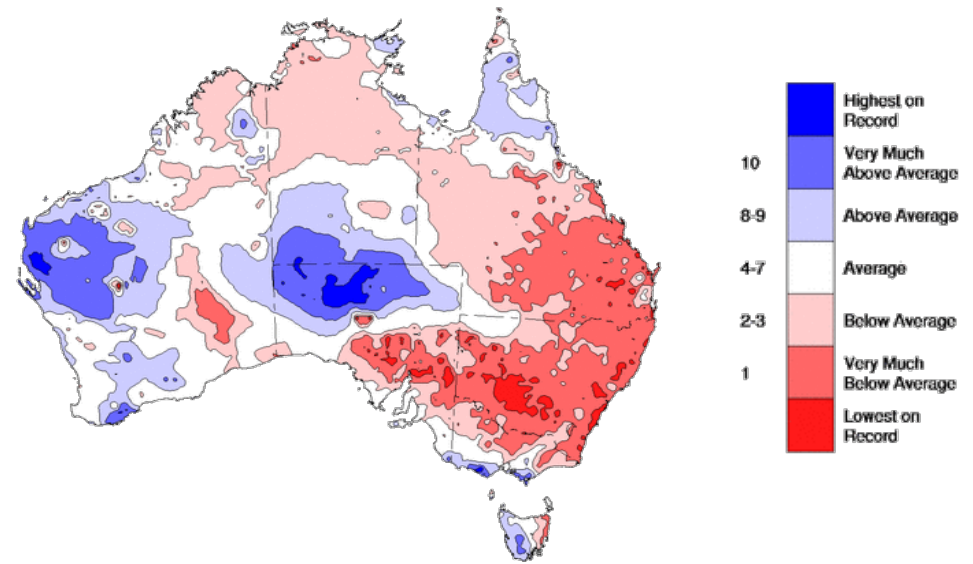


The Bureau of Meteorology's latest three month climate outlook to January 2018 points to neutral conditions for most of the country. Southern New South Wales, most of Victoria, eastern Tasmania and parts of the Pilbara and Kimberley are more likely to receive above average falls.

Improved rainfall is certainly welcome in the south east. The likely beneficiaries will be primarily livestock industries and potentially cotton growers in the New South Wales Riverina (although they already have good access to irrigation allocations).

RAINFALL DECILES – SEPTEMBER

Deciles based on long run average data



September rainfall was generally well below average across the country, although Cape York, the red centre, most of Western Australia, southern Victoria and western Tasmania were the exceptions. The first two weeks of October brought soaking rains to parts of Queensland, New South Wales and Victoria, which was very welcome news for cattle producers.

Seasonal conditions overall have been weakest in New South Wales. Much of the state is experiencing severe rainfall deficiencies. While Western Australia started the year with very tough conditions, recent rains have boosted prospects.

Source: Bureau of Meteorology

OUTLOOK FOR PRICES AND PRODUCTION



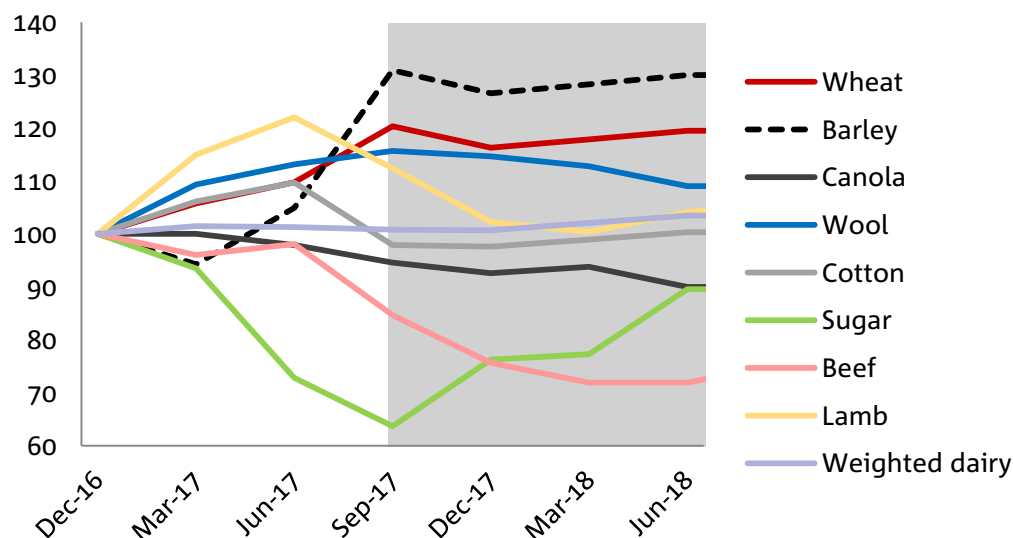
Prices

Weather has been a major driver of local prices and we expect this to continue. Drier weather has seen cattle prices slide and we expect this trend to continue (although recent rains in Queensland have seen something of an uptick). Domestic grain prices are at a premium as domestic suppliers scramble to source sufficient grain, although we expect this to retreat a little in the new year.

As always, the dollar will be a major driver. The AUD is off its recent highs but remains at an uncomfortable level for many producers. We see the AUD at 75 cents at the end of 2017 and 73 cents for much of next year.

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

The season has been, in the parlance of our times, all over the shop. New South Wales in particular has suffered badly from below average rain. This month we have revised our wheat production forecast down to 18.7 million tonnes – the lowest for a decade.

Conversely, dry conditions are likely to keep slaughter at elevated levels. Recent rains in Queensland may see some pullback however. ABARES forecasts point to beef production rising 8.5% in 2017-18.

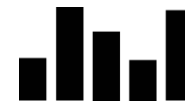
Expectations of cotton production have seen some pullback with dry conditions in northern New South Wales, although southern New South Wales is likely to see much higher planting.

PRODUCTION OUTLOOK (ABARES SEPT 2017 EXCEPT WHEAT)

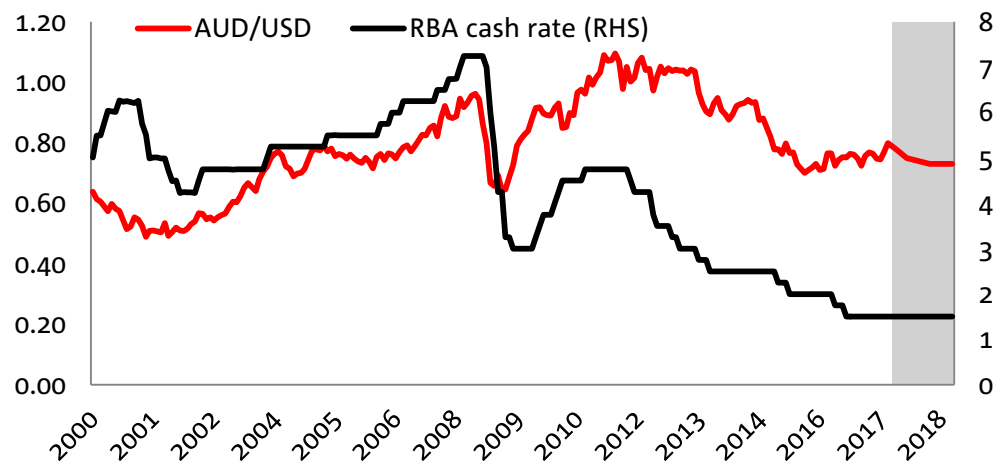
Financial year production estimates, Australia

	2016-17	2017-18	% change
Wheat (million tonnes)	35.0	18.7	▼ 46.6%
Beef (kt)	2,069	2,244	▲ 8.5%
Dairy (milk, ML)	9,015	9,250	▲ 2.6%
Lamb and mutton (kt)	670	673	▲ 0.5%
Wool	414	428	▲ 3.4%
Sugar (kt)	4,804	4,800	▼ 0.1%
Cotton (lint, kt)	935	956	▲ 2.2%

EXCHANGE RATES AND INTEREST RATES



EXCHANGE AND INTEREST RATES INC. QUARTERLY FORECASTS



NAB FX STRATEGY TARGETS

	2017Q4	2018Q1	2018Q2	2018Q3
AUD/USD	0.75	0.74	0.73	0.73
NZD/USD	0.70	0.69	0.69	0.70
USD/JPY	116	118	118	118
EUR/USD	1.17	1.18	1.20	1.22
USD/CNY	6.67	6.64	6.64	6.62
AUD TWI	64.1	63.4	62.3	62.1

Source: NAB

On balance, we remain comfortable with our view that the easing cycle for monetary policy has come to an end, but that tightening won't commence until mid-2018. Our forecasts published last month, for 2 sets of 25bp increases to the RBA's cash rate in August and November 2018, remain intact. Two further hikes also anticipated for 2019. This would take the cash rate back to 2.5%, a level well below the RBA's current estimate of "neutral" (3.5% nominal, 1% real), suggesting monetary policy will remain stimulatory at that point.

The RBA kept the cash rate on hold in October as expected. The bank noted the improved outlook for non-mining business investment and current strength in employment (key reasons for our change of view last month). Wages growth, however, is likely to remain low for a while yet. A new set of forecasts from the RBA is due on 10 November.

The Aussie dollar has depreciated by ~2 cents over the past month vis-à-vis the USD to 0.78 at the time of writing. While this has partly reflected USD strength, the AUD has underperformed relative to the size of the USD move, and has also fallen against every other major currency with the exception of the Japanese yen. This has largely reflected weakness in industrial metals and bulk commodity prices, while risk appetite measures have actually improved and been a source of support for the AUD.

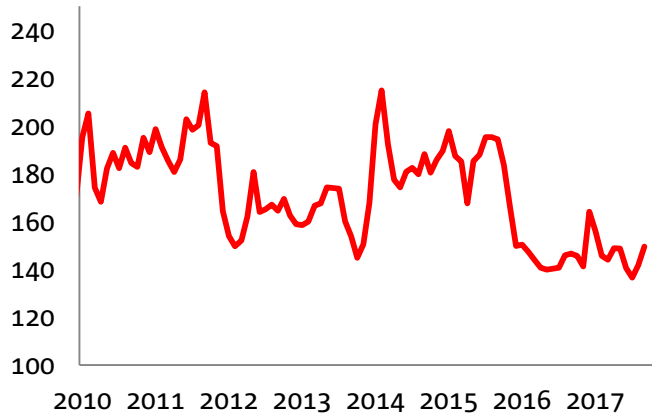
We expect to see further progress towards our AUD/USD year end target of 0.75 in coming weeks - assuming no quick reversal of the downward move in commodity prices, no major set-back to the December Fed hike odds, and/or tax reform optimism in the US. Donald Trump's decision about the next Fed Chair to take over from Janet Yellen could also lead to some volatility near term.

FARM INPUT PRICES



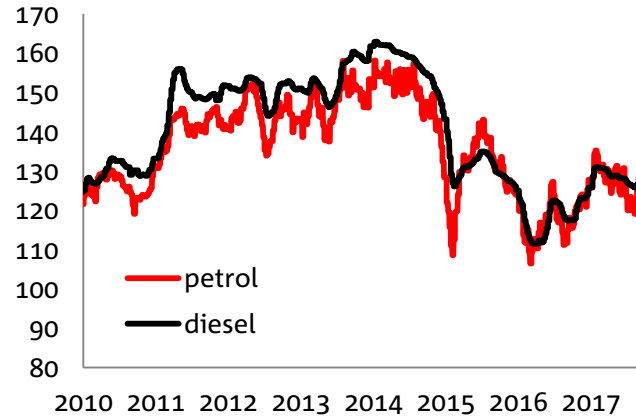
NAB FERTILISER INDEX

AUD index



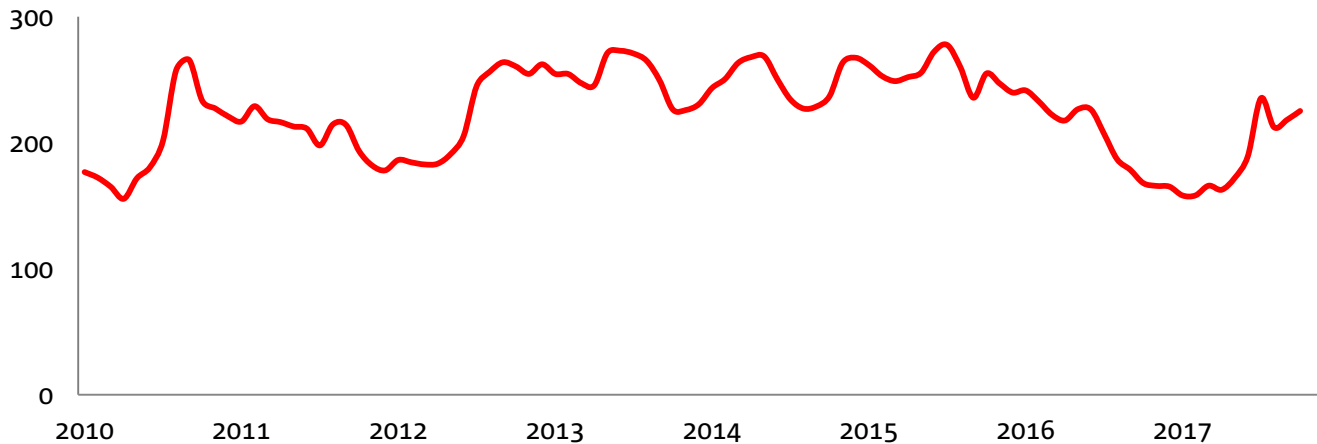
NATIONAL AVERAGE FUEL PRICES

AUc/litre



NAB WEIGHTED FEED GRAIN PRICE INDEX

AUD/tonne



Source: Bloomberg, Profarmer and NAB Group Economics

Feed prices rose 4.4% to \$228/tonne in September, as the reality of a sharply lower grain harvest came into view. With most old season crop now gone, demand for stock feed has been elevated. Hay supply remains perhaps higher, but mostly in southern regions and transport costs will add a premium further north.

While we expect little upturn in grain global prices over the coming months a possible shortage of domestic grain over the next few months will likely keep prices above world benchmarks. As we move into December and the new year, it is likely that prices will adjust back closer to global levels.

Fertiliser prices were up again in September, reflecting further gains in DAP and urea prices. Overall, the index was up 5.5% for the month.

Global oil prices have been on the rise since mid-year, with Brent now sitting above USD56/bbl. However, combined with a somewhat stronger AUD, domestic fuel prices have risen gradually. The latest national average data shows petrol prices at 130.5c/litre and diesel at 127.7c/litre. We see oil prices increasing gradually. Combined with an expected lower AUD, domestic fuel prices are likely to rise rather than fall.

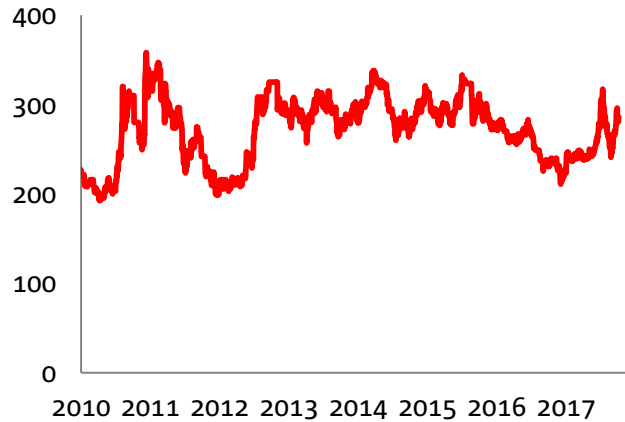


WHEAT



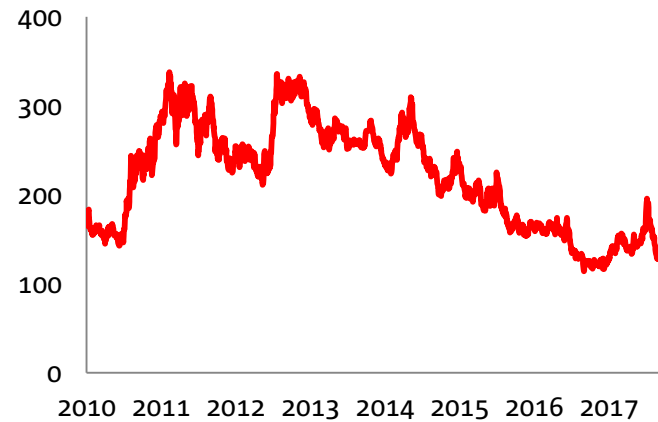
ASX MILLING WHEAT FUTURE

Eastern Australia, AUD/tonne



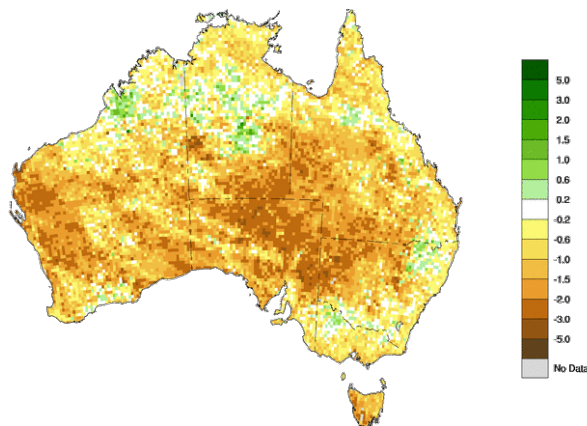
CBOT SOFT RED WINTER WHEAT

USD/tonne



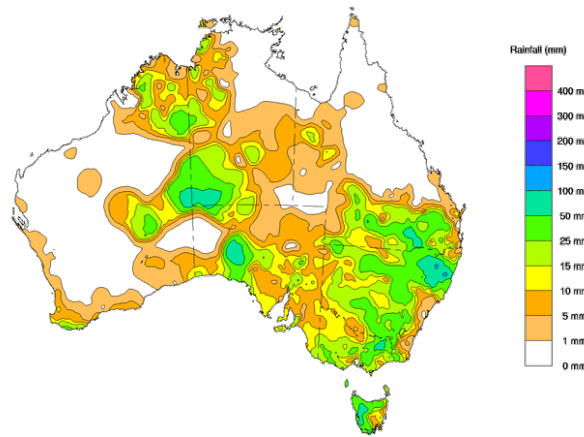
VEGETATION GREENNESS

NDVI anomaly July to September 2017



RAINFALL – WEEKLY

MM to 7 days to 12 October



Prices

Global grain prices remain very subdued, and with global growing conditions broadly very favourable. While concerns have been raised about inventory levels outside of China, it would still take a reasonable hit to global production to cause a sustained upward movement in prices. We do not see these conditions being met at present. Domestic grain is trading at a large premium amid a lack of supply, although this is likely to abate for export grain, which will need to meet the world market.

Production

Seasonal conditions have been extremely mixed across the country. While rains in Western Australia, and more recently Queensland, New South Wales and Victoria, are a boost to prospects, overall the picture is very patchy. New South Wales in particular looks set for a very poor season.

This month we cut our wheat production outlook to 18.7 million tonnes – the lowest wheat production in a decade. The biggest cuts have come from New South Wales, which has suffered from very low rainfall, frosts and heatwaves in the space of a single season. Grain region rainfall data is available on page 10.

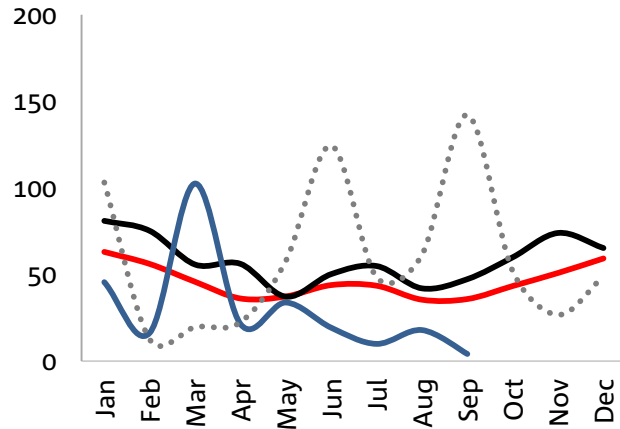
Source: Bloomberg, Profarmer, USDA, Bureau of Meteorology, ABARES, Australian Bureau of Statistics and NAB Group Economics



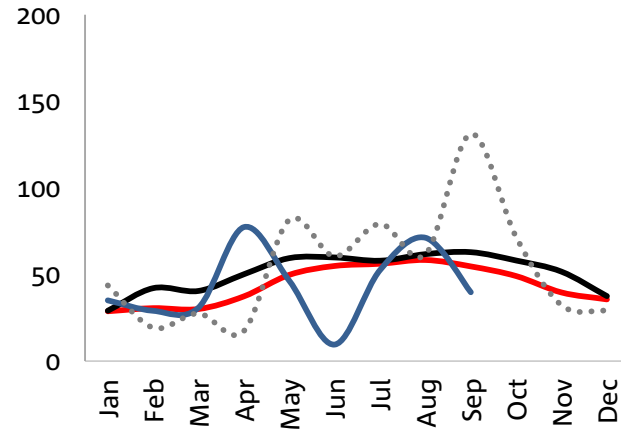
MONTHLY AVERAGE RAINFALL IN WHEAT REGIONS (MM)

— Long run average 1900-01 to 2013-14 — La Nina years — 2017 YTD 2016

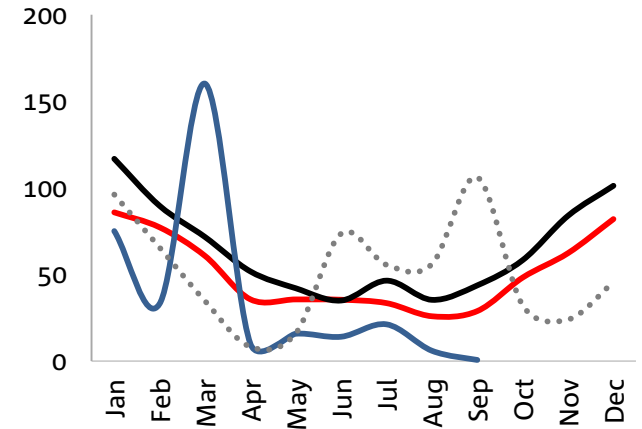
NEW SOUTH WALES



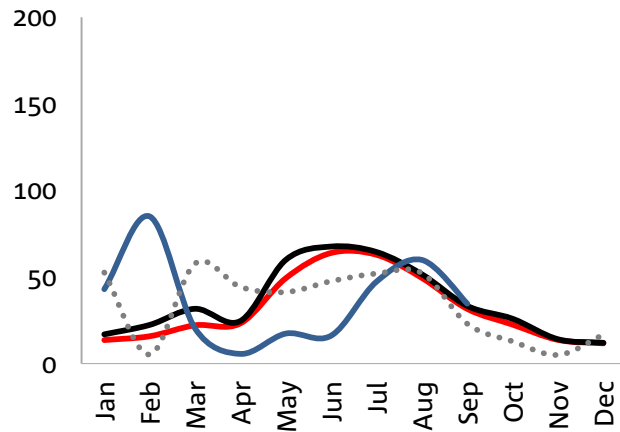
VICTORIA



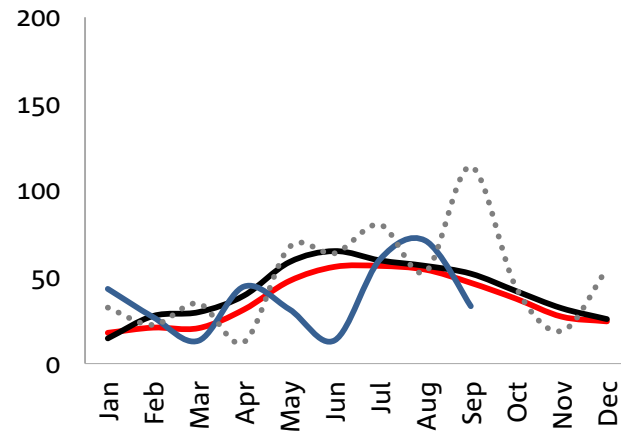
QUEENSLAND



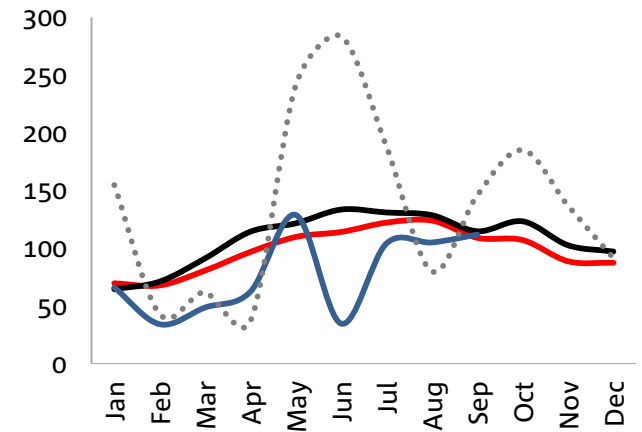
WESTERN AUSTRALIA



SOUTH AUSTRALIA



TASMANIA

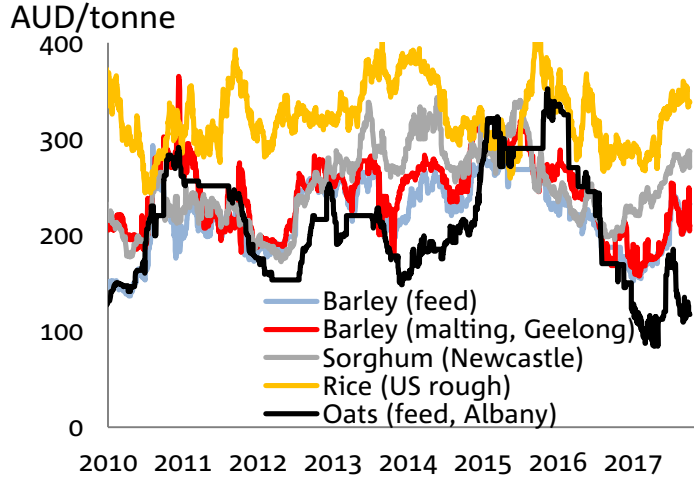


Source: Bureau of Meteorology and NAB Group Economics

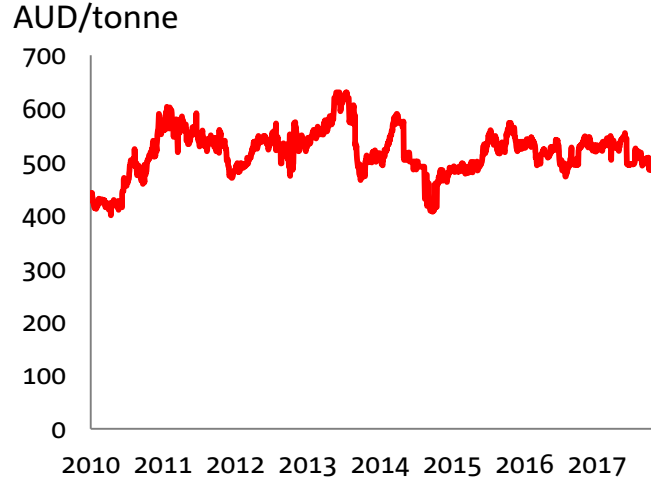
OTHER BROADACRE CROPS



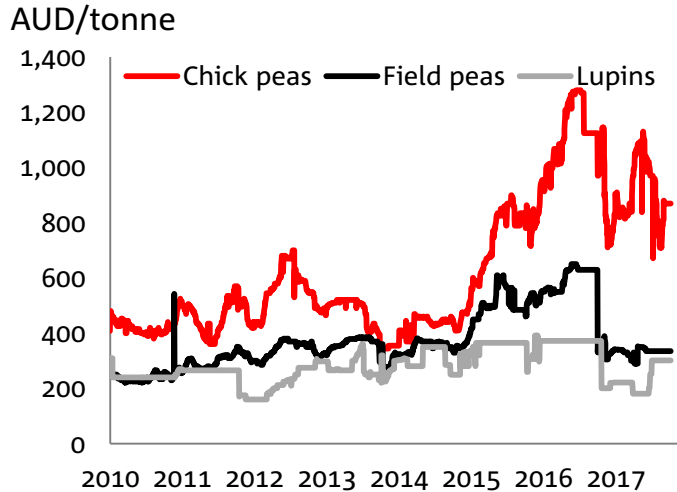
SELECTED COARSE GRAINS



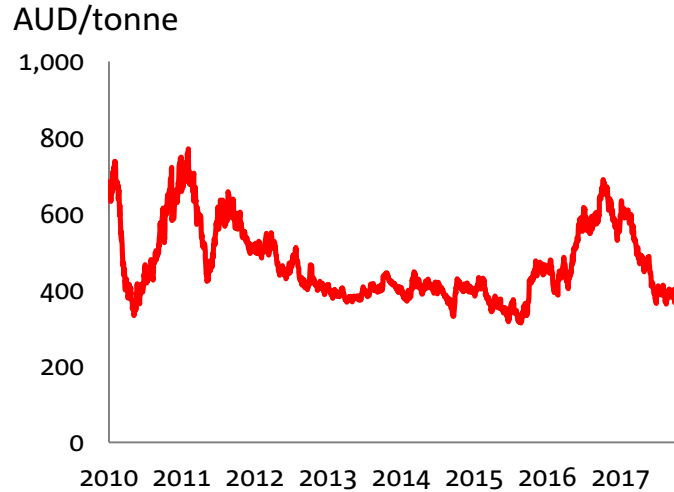
CANOLA, NEWCASTLE NSW



SELECTED PULSES



ICE NO.11 SUGAR



Prices for most coarse grains have been higher over the month. Rice and sorghum (with their different production systems – rice being irrigated and sorghum a summer crop) have both performed well, although rice looks to be relegated to second best in the New South Wales Riverina this season in favour of more profitable (and generally less water intensive) cotton. Canola prices have trended downwards, although not drastically. Frost damage is likely to be above average in Australia this season.

Chick pea prices are back in the mid-high 800s range in AUD terms, reflecting a likely shortage of domestic crop this season amid very challenging growing conditions in Queensland and northern New South Wales. The humble chick pea still attracts a substantial premium compared to alternative crops

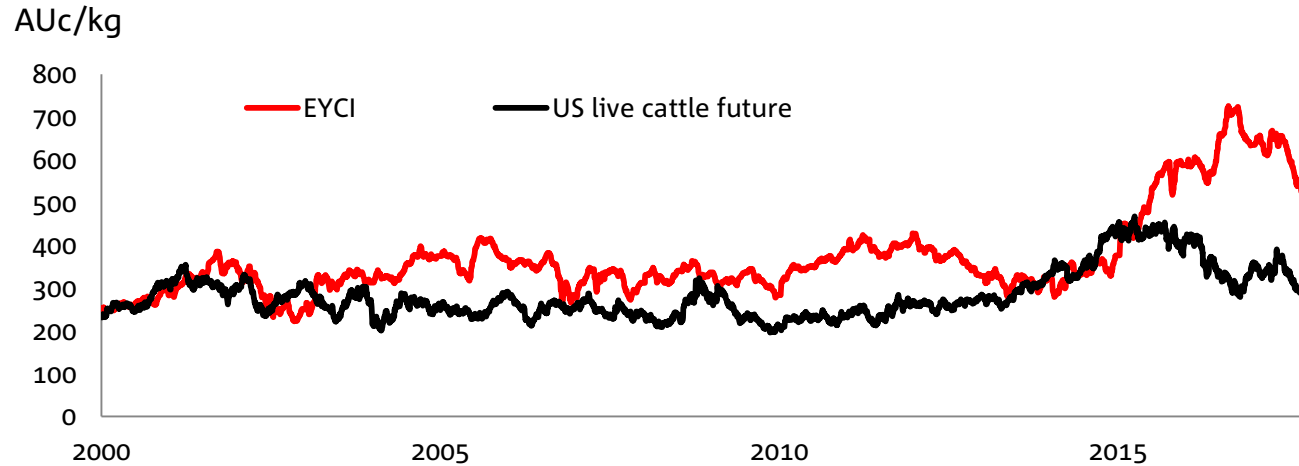
Sugar prices continue to show signs of stabilisation after a big tumble this year which wiped off all of the previous rally and fell close to 2015 lows in AUD terms. Prices were steady (up 0.1%) in AUD terms in September. The strength of the AUD has not helped the industry.

Source: Bloomberg, Profarmer and NAB Group Economics

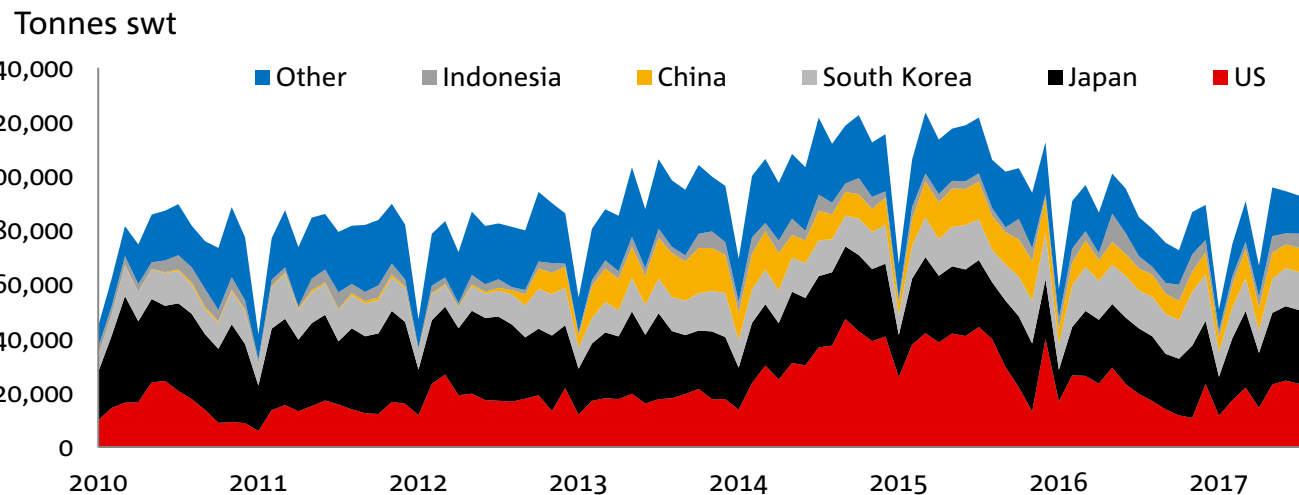




EASTERN YOUNG CATTLE INDICATOR AND US CATTLE FUTURES



MONTHLY AUSTRALIAN BEEF EXPORTS



Source: Meat and Livestock Australia and NAB Group Economics

The September slide in cattle prices looks to have been arrested in October, as rains across much of eastern Australia have seen cattle producers reassess turnoff plans. Nonetheless, much of the country remains very dry and pasture availability ahead of summer is by no means guaranteed. After nudging 500c at the end of last month, the EYCI is now back above 540c/kg.

However, even if seasonal conditions recover – which is far from certain – key export markets remain a challenge. Export prices to the key US market have gained slightly recently, although Australian prices still remain detached from US fundamentals in many ways. If Australia is to reflect the US market, the EYCI will likely need to fall further.

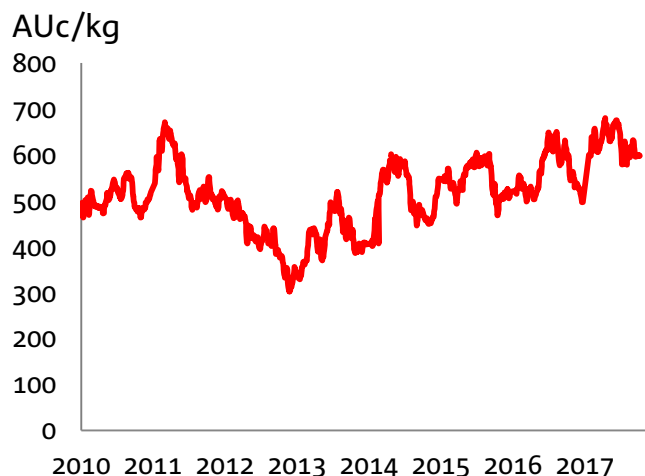
Beef export data reflects the uptick in slaughter in Queensland in particular this year. MLA and ABS data show adult cattle slaughter to be up 10% y/y in August. Elevated feed prices has been a concern for some producers (feedlots especially), and it is likely that domestic grain will be at a premium against global benchmarks until the new year.

We see the EYCI falling to 500c/kg either late this year. A price with a 4 in front of it is more likely than not in 2018.

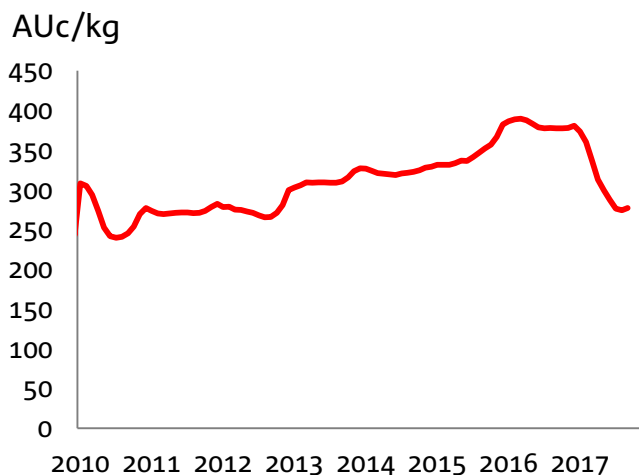
LAMB, PORK AND POULTRY



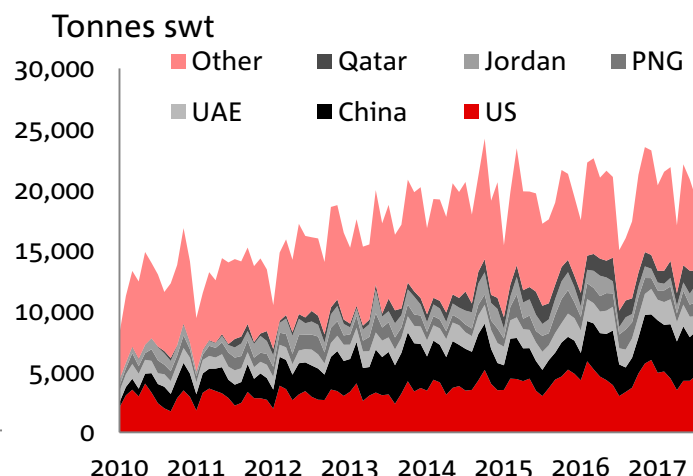
NATIONAL TRADE LAMB INDICATOR



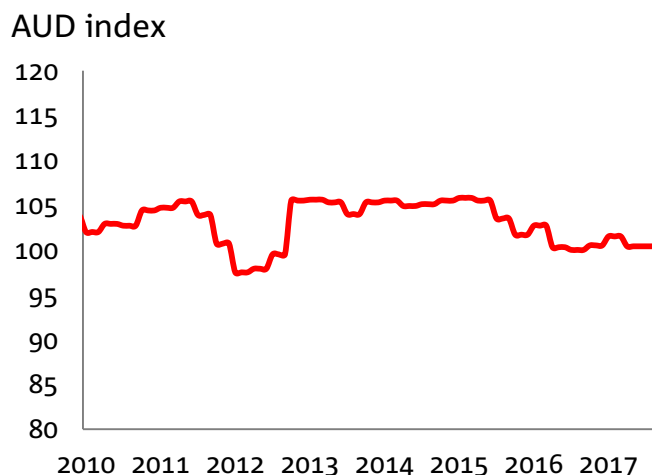
AUSTRALIAN PORK PRICE INDICATOR



MONTHLY LAMB EXPORTS BY DESTINATION



ABS POULTRY PRICE INDEX



Lamb prices have displayed incredible resilience in the face of dry seasonal conditions and the usual spring flush. The National Trade Lamb Indicator remains just over 600 cents and is slightly higher than the same time last year. While price falls are likely in line with the usual spring flush, the trajectory for the industry remains very positive.

Export markets for lamb are reasonably diversified, with the US and China accounting for a substantial volume (around 41% by weight 2017 YTD). This compares to almost 54% for the top two markets for Australian beef. The Middle East also remains a very important market, particularly for mutton and live sheep.

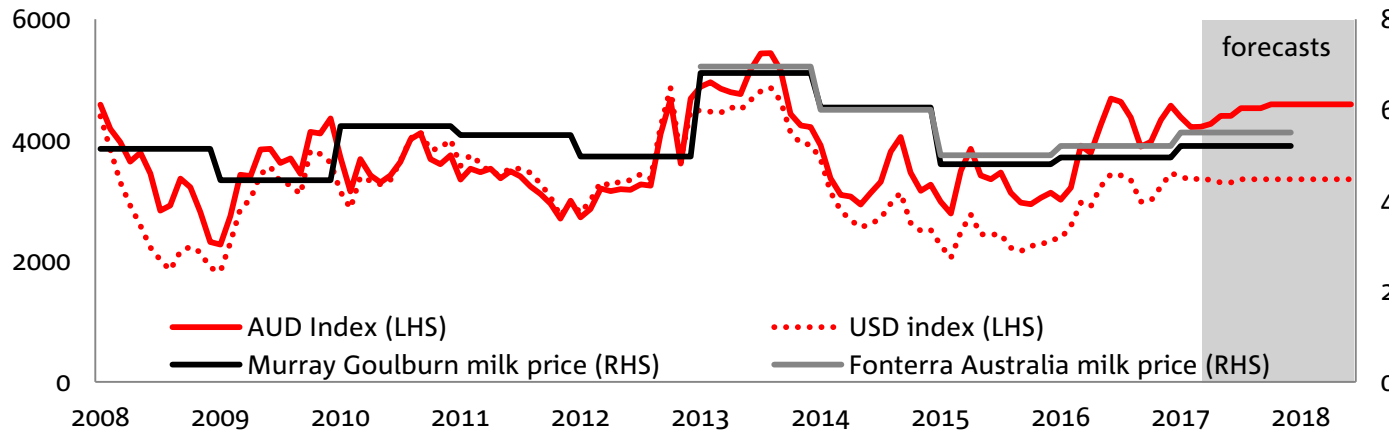
The severe drop in Australian pork prices looks to have stalled and indeed our Australian pork price indicator (based on data provided by Australian Pork and based on an average of buyer and seller prices for eastern seaboard 60.1-75kg animals) was up 1.0% in September – the first monthly rise since December 2016. Nonetheless, pork is off more than 25% year on year. Competition from cheap imports will remain a major challenge for the industry.

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)

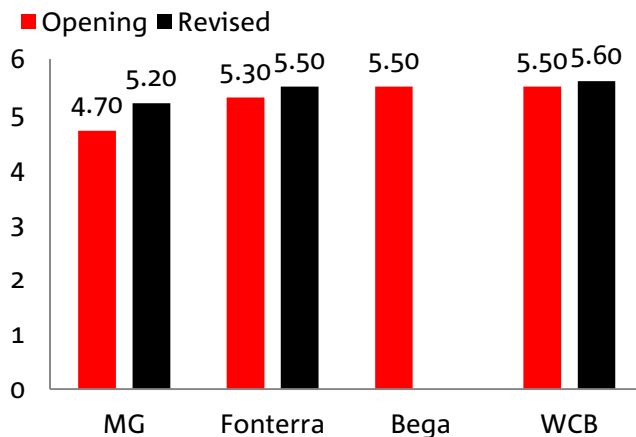


Global Dairy Trade auction results were up slightly in September, although these gains were essentially wiped out at the 3 October auction. NAB weighted dairy export price indicator rose 0.2% in September in AUD terms.

Farmgate prices continue to be the major focus in the domestic market. Warrnambool Cheese and Butter has stepped up to \$5.60 and all major players have been keen to take supply from Murray Goulburn, which may not even be the biggest supplier this season at an expected 2 billion litres. There has been considerable speculation that Murray Goulburn will be sold, potentially to Fonterra or Bega or indeed elsewhere.

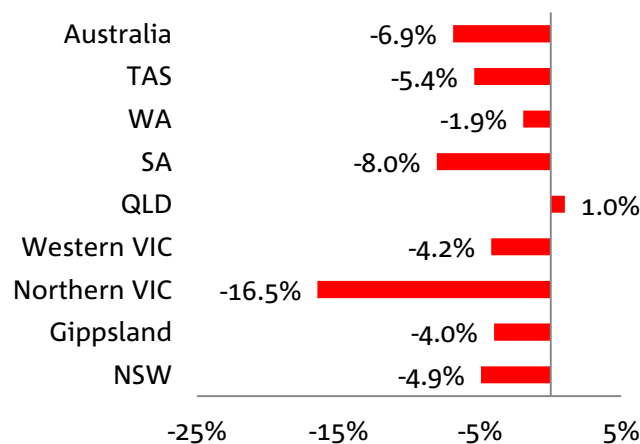
FARMGATE PRICES

AUD/kg milk solids, 2017-18 season



SEASONAL MILK PRODUCTION CHANGE

2015-16 to 2016-17



Milk flow was well down last season – off 6.9% nationally. The worst falls were in the major export states of Victoria, South Australia and Tasmania. Northern Victoria saw particularly steep declines, reflecting poor prices combined with a very wet 2016 spring. Expectations are stronger for this season, although market uncertainty and herd thinning last season are impediments to a speedy recovery. Dry conditions in Gippsland also warrant observation.

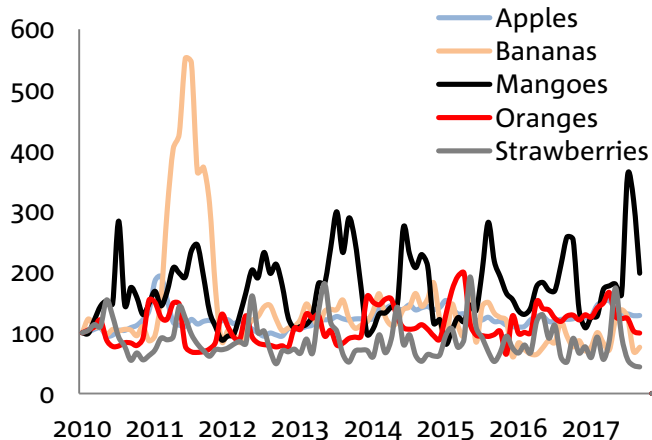
Source: Australian Bureau of Statistics, Global Dairy Trade, Dairy Australia, processors, ABC and NAB Group Economics
 Note: chart shows Murray Goulburn farmgate prices except 2008-09 which shows Dairy Australia's reported Victorian average value





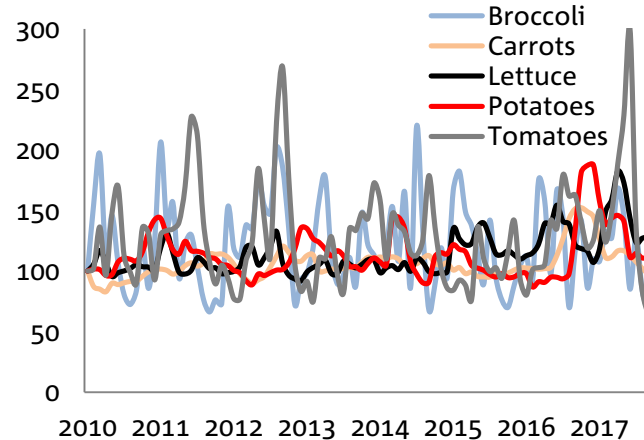
WHOLESALE FRUIT PRICES

AUD index, Syd+Melb, Jan 2010=100



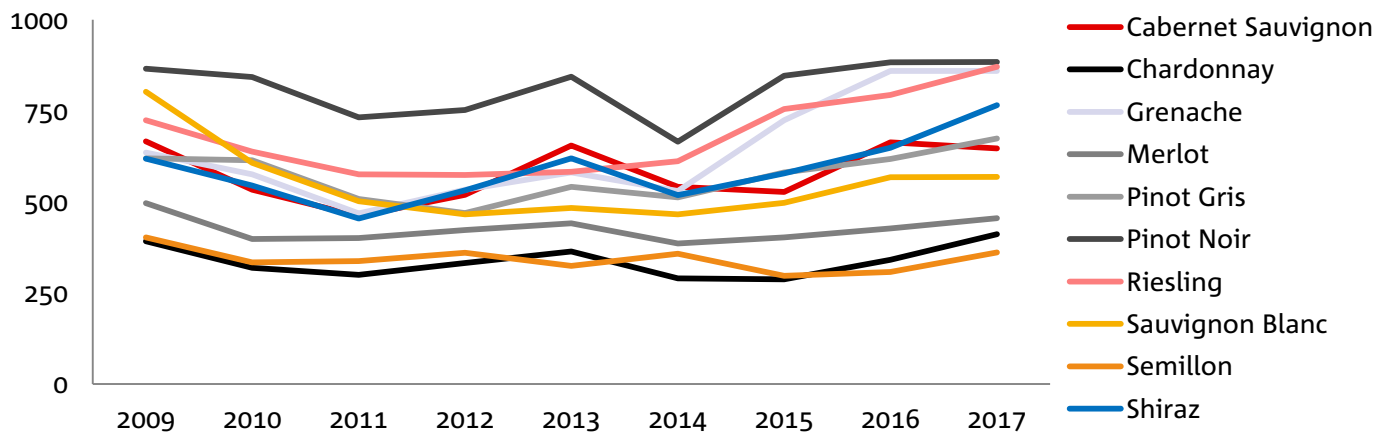
WHOLESALE VEGETABLE PRICES

AUD index, Syd+Melb, Jan 2010=100



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.

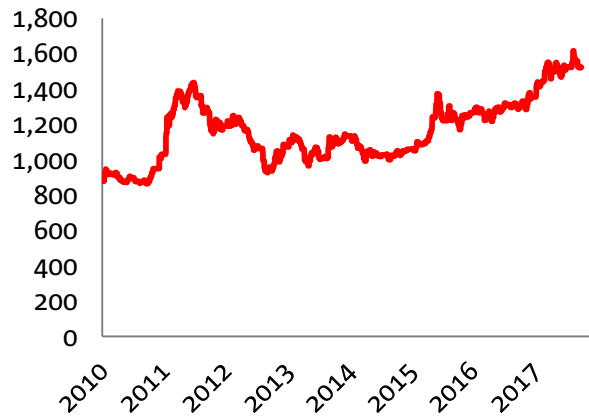
Wholesale fruit and vegetable prices again displayed characteristic volatility in September, although both were lower. Fruit was down 15.8%, largely reflecting seasonal factors, led by lower prices for delicious mangoes. In August the index stood at 111.5 index points (January 2010 = 100). Vegetables were down 7.0% to 97.0 index points. This means that our basket of vegetables used in our index are now on average cheaper at a wholesale level than at the beginning of the decade.

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 in 2016 likely explains some of the increase, although the higher currency more recently is some concern. 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%).



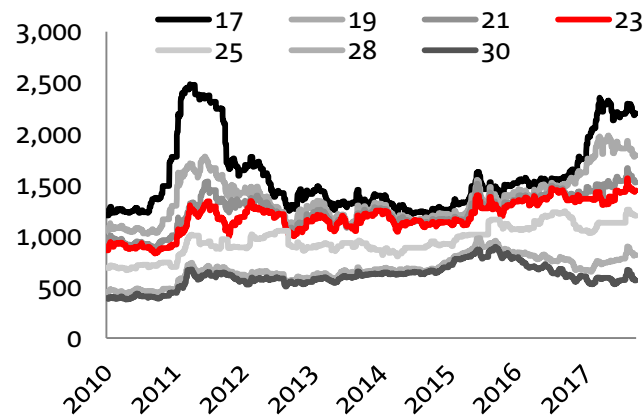
WOOL – EASTERN MARKET INDICATOR

AUc/kg



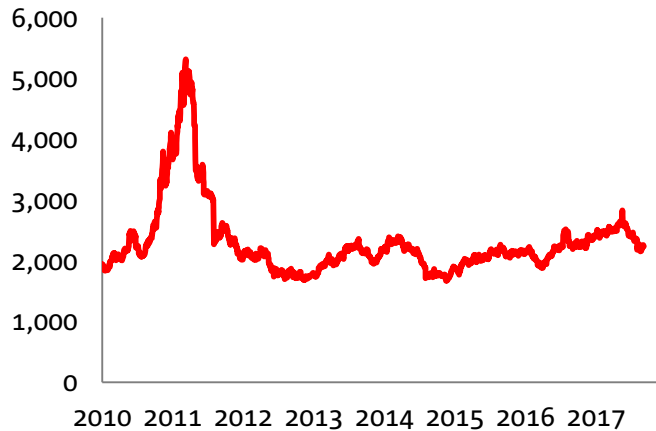
WOOL PRICES BY MICRON

AUc/kg, Southern Region



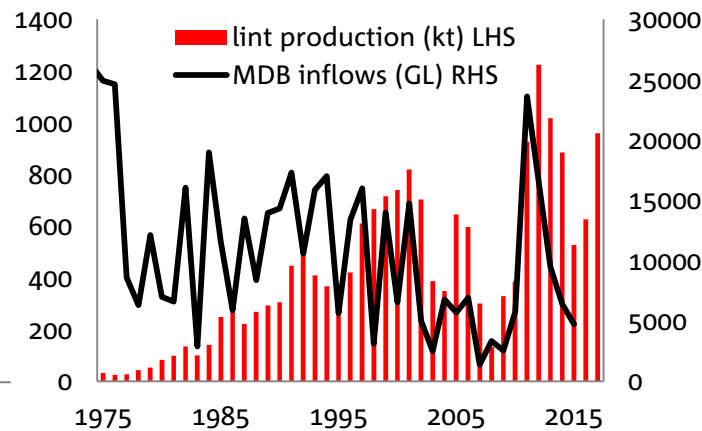
COTLOOK A INDEX

AUD/tonne



AUSTRALIAN COTTON AND BASIN INFLOW

Production and MDB system inflows



The wool market has retreated slightly from its record breaking highs, but remains buoyant overall. Wool prices declined 1.5% in September, with declines across the micron range. The market remains strong, despite an elevated Australian dollar, to which the wool industry is usually very sensitive. It is unclear whether prices are sustainable at their current levels. While we see good signs in the form of very strong Chinese demand, this is not inherently sustainable. It is likely that prices will come back somewhat over coming months.

With prices at these levels, ABARES projects that wool production will increase 3.4% in 2017-18, arresting (at least temporarily) a long decline in production.

Cotton prices were up slightly in September. 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 northern basin inflows amid dry conditions, ABARES has cut back production forecasts for the coming season. On the other hand, Southern New South Wales looks set up for a strong season as cotton continues to push south.

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

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