NAB Rural Commodities Wrap

June 2023

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Highlights

The NAB Rural Commodities Index has continued to fall over autumn and into winter, largely reflecting steep declines in cattle and lamb prices. Our NAB Rural Commodities Index dropped 0.7% in April and a further 3.4% in May. The index is now 25.2% below year-ago levels.

Cattle prices continue to drive the index lower. The benchmark EYCI now stands at around half its early 2022 peak. Lamb markets have also fallen, although somewhat less precipitously than cattle. Drier conditions in Queensland combined with constrained processor capacity have heaped pressure on the cattle market. Expectations of further dry weather to come have only added downside risk.

Climatic conditions have been mixed: while much of the continent is drying out, storm activity across Victoria, south-east South Australia and western NSW has seen above average soil moisture. The WA wheatbelt is also generally wetter than average.

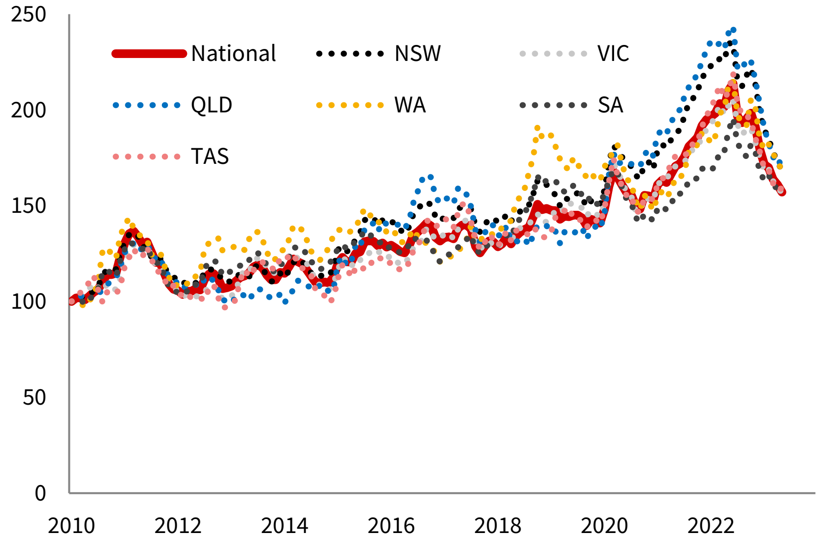
However, El Nino is approaching, if not already underway. NOAA has already declared an El Nino event, while the BoM remains on El Nino alert, indicating a 70% chance of an event forming in coming months. El Nino typically associated with hotter and drier spring-summer conditions across eastern and northern Australia.

We have again amended our rate call in response to RBA rate rises in May and June and now expect the cash rate to peak at 4.6% in coming months. The AUD has been higher recently, following lows last month. We see the AUD reaching 72 US cents at end-2023 and 73c at end-2024.

Contents

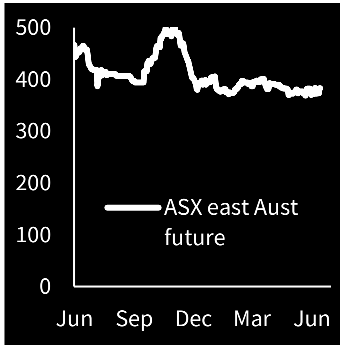
NAB Rural Commodities Index

National and state index, Jan 2010 = 100



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

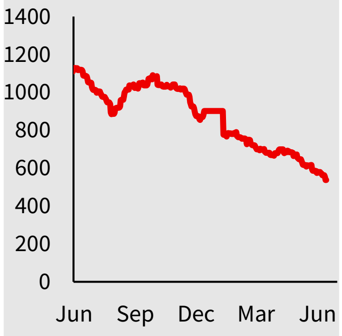
Outlook for major commodities



Wheat

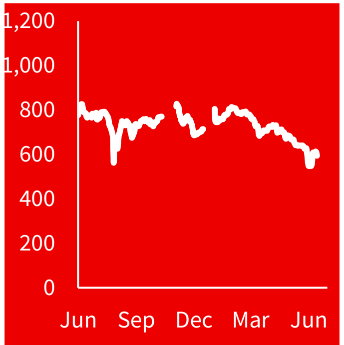
Australian wheat prices have seen little change recently, with east coast futures in the high $300s range. We see wheat closing out 2023 at around $350/t.

Yields are likely to be much lower than last season, with El Nino presenting a real downside risk.



Cattle

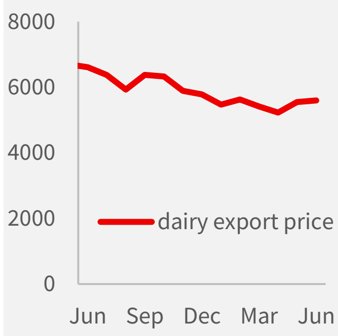
Australian cattle prices continue to fall, reflecting dry weather conditions, a very dry outlook and ample cattle supply combined with very constrained processor capacity. We see further downside if El Nino materialises – potentially with EYCI below 500c/kg.



Sheep

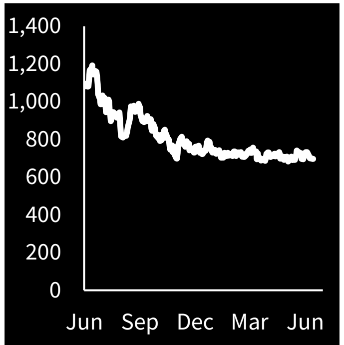
Lamb prices have fallen roughly 200c/kg since late January, reflecting similar themes to the cattle decline. As a premium niche product, the trajectory of the global economy will be key.

Wool prices continue to slowly weaken.



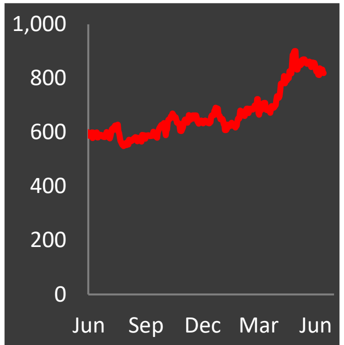
Dairy

Recent global dairy trade auctions have been somewhat more favourable in AUD terms and our export index rose 6% in May. Opening farmgate prices have been generally favourable given the global market – settling in the $9/kgms range.



Cotton

Cotton prices continue to offer little in the way of volatility. AUD Cotlook A is trading at around $700/bale. Dry conditions this year may affect dryland cotton yields but storage levels are excellent and likely to remain so for some time.

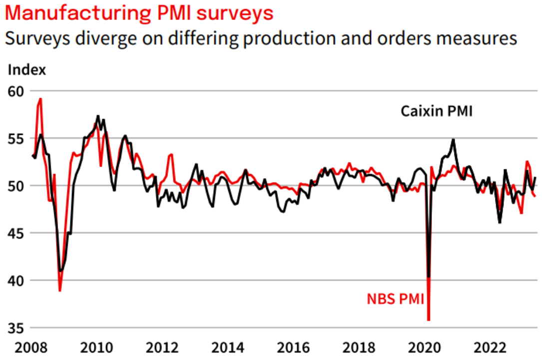


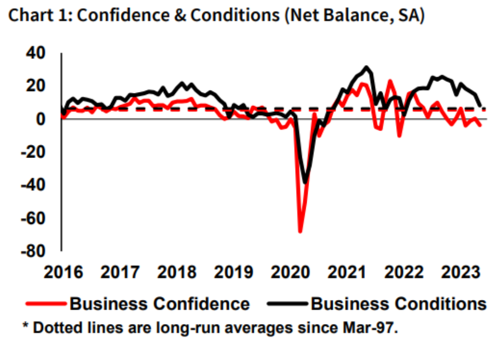
Sugar

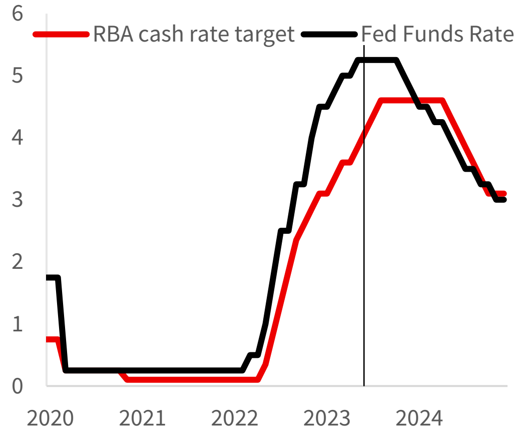
Sugar prices have eased a little following a surge earlier this year. But the conditions that underpinned higher prices (global supply concerns and strong demand) remain.

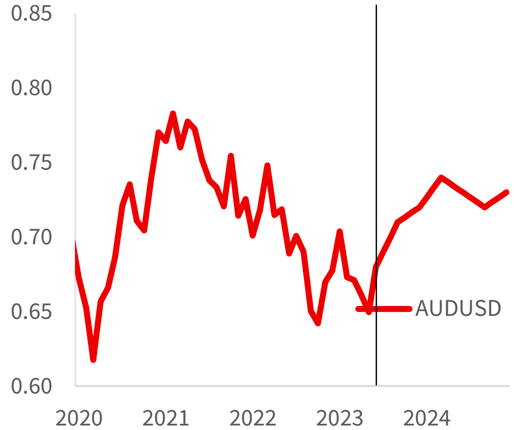
Source data: NAB Group Economics, Meat and Livestock Australia, Bloomberg, Global Dairy Trade, Refinitiv

Economic update









Global economy

Global economic activity has been mixed of late. While the US economy continues to outperform expectations, China has been much weaker.
Most of the key Chinese economic data fell short of market expectations in May – highlighting continued softness in China's economy. In particular, subdued retail sales (when looking though the volatility), and inflation data point to ongoing weakness in domestic demand.

Australian economy

Alongside the upgrade to our interest rate forecasts, we have pulled back our expectations for growth this year and next. We now see GDP growth of just 0.5% over 2023 and 0.9% over 2024.

While the economy remained resilient through 2022, there are increasing signs that interest rates are beginning to flow through with nominal (and real) spending growth slowing, an ongoing impact on housing construction and softening capex expectations.

Interest rates

Following the RBA's decision to lift rates to 4.1% at the June meeting, we upped our rate call to 4.35% by August. We are now tentatively adding an additional 25bp increase, taking the cash rate to 4.6%. Timing is less certain, and we pencil in 25bp increases for July and August.

We still see the RBA cutting interest rates back towards neutral in 2024 as a "forward-looking" central bank sees the slowing in growth and unemployment rising.

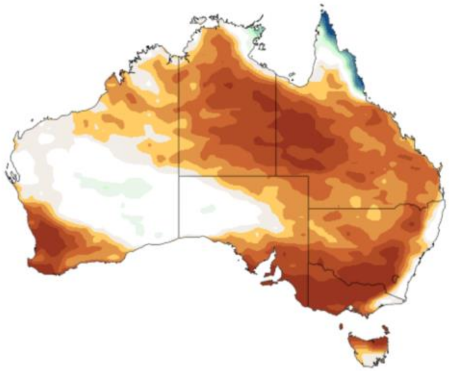
Currency

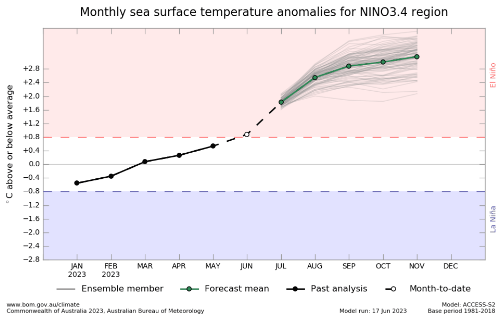
The AUD has been higher recently, following lows last month. Improved risk sentiment, a more hawkish RBA, slowing Australian economic growth, potential further Fed activity following their "hawkish pause" and lower Chinese growth are all likely to provide competing forces in coming months.

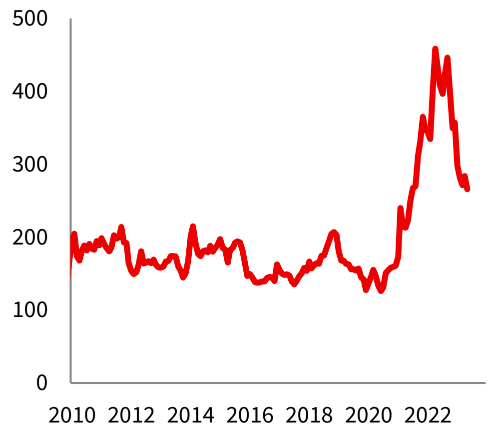
We see the AUD reaching 72 US cents at end-2023 and 73c at end-2024.

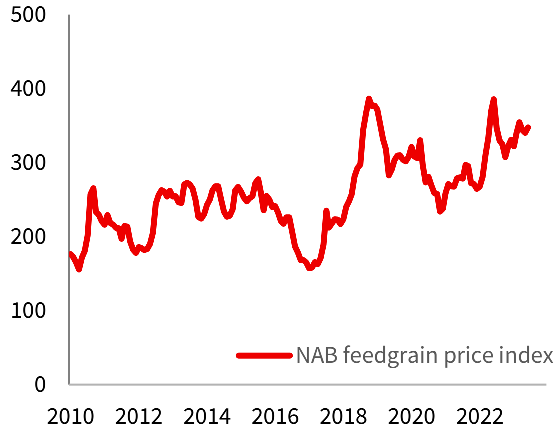
Source data: NAB Group Economics, S&P Global, Macrobond, Refinitiv, IMF, Australian Bureau of Statistics

Seasonal conditions and farm inputs









Parts of southern Australia wet, outlook dry

Climatic conditions have been mixed: while much of the continent is drying out, storm activity across Victoria, south-east South Australia and western NSW, has seen above average soil moisture. The WA wheatbelt is also generally wetter than average.

The three-month outlook to September is forecast to be drier than average across most agricultural regions, with particular risk in the south-east and south-west.

NOAA declares El Nino, BoM on alert

El Nino is approaching, if not already underway, with NOAA declaring an El Nino event earlier this month., While the BoM remains on El Nino alert, indicating a 70% chance of an event forming in coming months, its latest ENSO outlook, released on 20 June notes that some atmospheric thresholds have reached El Nino levels. El Nino typically associated with hotter and drier spring-summer conditions across eastern and northern Australia.

Fertiliser prices well down on year-ago levels

Fertiliser prices fell slightly last month, with big falls in previous months erasing well over half their covid/Ukraine war spike. While prices are still high by historic levels, they are now approaching 40% below year-ago levels.

That said, we remain cautious about further downside, given oil and LNG market uncertainty, and the the potential for European natural gas supply challenges next northern winter.

Feed grain prices flat since February

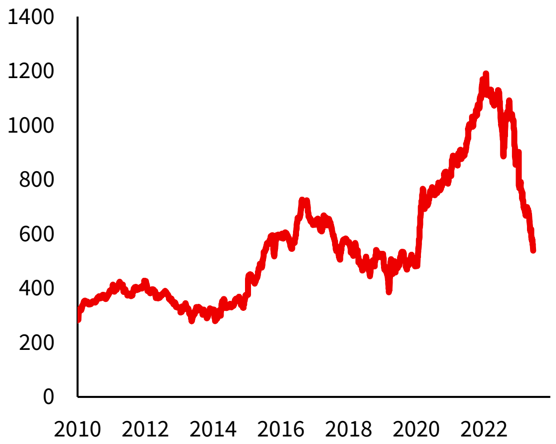
Our feed grain price index has been basically flat since February and is now down 8.1% on year-ago levels.

While last season saw a big (and quality downgraded) winter crop, 2023 is looking much drier and hay remains tight as producers scrambled to cash in planting grain last year.

We still don’t expect major upside this year, but a very dry season could test this.

Source data: Bureau of Meteorology. Bloomberg, World Bank, Refinitiv

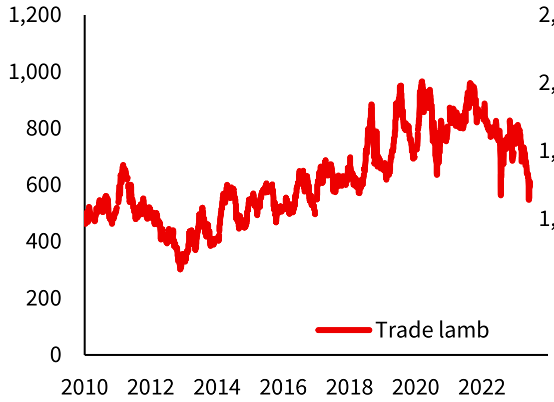
Livestock



Cattle

Australian cattle prices continue to fall, reflecting dry weather conditions, a very dry outlook and ample cattle supply combined with very constrained processor capacity. It is likely that processor capacity will remain constrained while the labour market continues to post historically low unemployment rates.

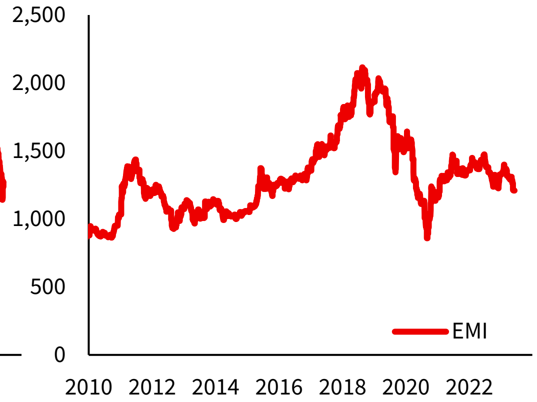
El Nino is the major downside risk and we see a typical El Nino event potentially pushing EYCI below 500c/kg in spring.



Lamb

Lamb prices have fallen roughly 200c/kg since late January, reflecting similar themes to the cattle decline. As a premium niche product, the trajectory of the global economy will be key.

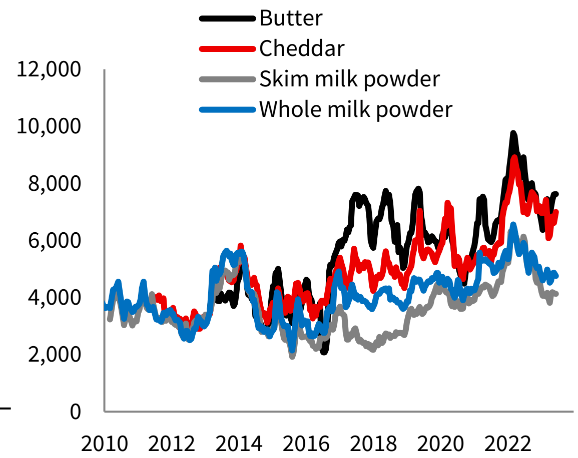
We remain optimistic about lamb's long-term prospects. The industry has innate risk-management advantages when paired with broadacre cropping and we have a strong position in the global market. But in the short-term, a dry season, rebuilt flock and economic jitters will continue to sap confidence.



Wool

Wool prices continue to slowly weaken, with EMI breaking below 1200c/kg last week. While recent FX moves may have dampened buyer interest of late, the fundamental problem is that demand is somewhat weaker amid a sluggish Chinese economy.

We see a risk of ongoing volatility in 2023 – we see global growth slowing and consumer goods spending is likely to weaken further.



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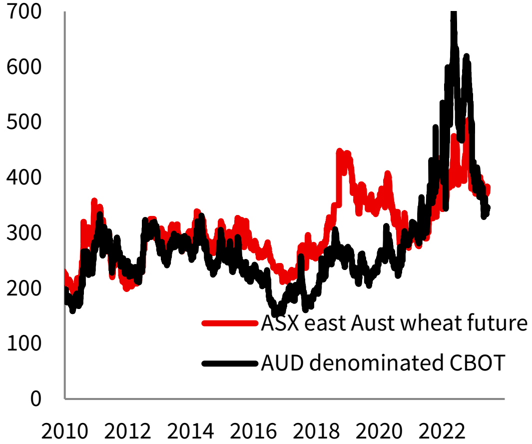
Opening farmgate prices have been generally favourable given the global market – settling in the $9/kgms range. While this has caused some disappointment, the reality is that these prices are very high by historic standards and reflect processor need for milkflow rather than global market fundamentals.

Source data: Meat and Livestock Australia. Bloomberg, Global Dairy Trade, Refinitiv

Crops



Winter crop prices

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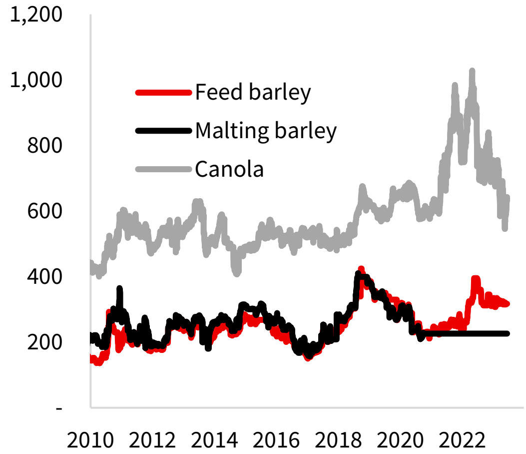
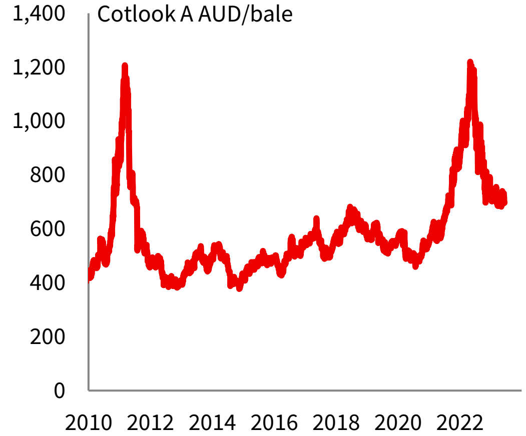
Canola prices have now stabilised, albeit substantially below their 2022 peaks.



Crop production

Yields are likely to be much lower than last season, with El Nino presenting a real downside risk.

ABARES' June crop forecasts have seen some downgrades, with wheat down from 28.2mmt in March to 26.2mmt in June, while barley is unchanged at 9.9mmt and canola down to 4.9mmt. While the March forecasts were speculative and predated planting, there are risks of further reductions from here if the season deteriorates amid an El Nino.



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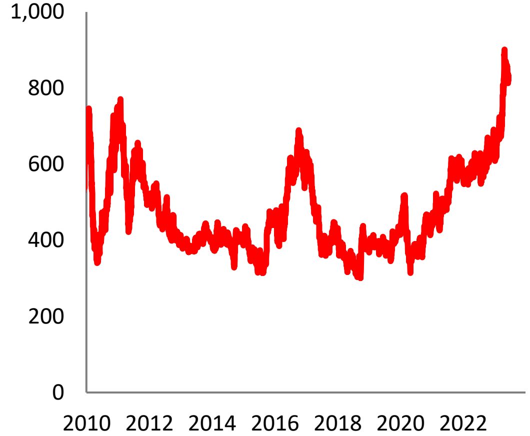

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Important Notice