



Fortnightly Agri Update

22 January 2014

Spotlight on Beef

The dairy sector was the undoubted headline act of 2013. And like Meryl Streep or Daniel Day Lewis we suspect it will keep the star billing for some time yet. But in 2014, it may be worth keeping an eye out for the beef sector to put in a solid supporting performance.

One reason we are relatively upbeat on prospects for beef prices in 2014 are fairly tight global supplies. Nowhere is this more acute than in the US – a major market for New Zealand beef exports. There, an extended drought saw widespread culling of stock, pushing cattle numbers to multi-decade lows. More recently, growers have been looking to rebuild herds, encouraged by improved pasture conditions in key regions, and lower feed costs. In addition, favourable conditions for dairy producers should reduce culling of dairy cattle (a source of supply for the grinding beef market). This has meant a sharp reduction in cattle available for slaughter and sent cattle prices sharply higher.

New Zealand beef producers should also benefit from growing demand for their products from emerging markets as beef consumption increases as incomes grow. This is illustrated in dramatic fashion by the surge in New Zealand beef exports to China. From less than 1% in early 2012, 9% of New Zealand beef exports (by value) over the year to November 2013 were destined for China. While China is one of the largest beef producers in the world, domestic production has struggled to keep pace with growth in demand, meaning increased demand for imports. The Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) reports that New Zealand was the third largest supplier of imported beef to China in over the past year, accounting for 15% of imports (this was behind Australia and Uruguay with which account for 50% and 25% respectively).

Of course it is never all one way traffic. With household incomes remaining under pressure in developed economies such as the US and Europe, it will be difficult to push higher prices through to budget sensitive consumers who may well choose to substitute other meats in favour of relatively expensive beef. And the supply situation in some key countries is better than in the US. For example in Australia ABARES is forecasting slaughter numbers in the current season to rise by 6% on the back of adverse weather conditions.

Over a longer horizon, New Zealand producers should benefit from international efforts to remove tariff and trade barriers. Initiatives such as the Trans Pacific Partnership agreement as well as bilateral trade agreements (such as the one with Taiwan which came into effect on the 1st of December) have the potential to benefit NZ producers. Our disease free status is also a major trading advantage. It means New Zealand producers don't face the import restrictions that countries with Foot and Mouth Disease or BSE face. China, clearly the biggest growth market for Australasian producers, doesn't allow beef imports from the US. The stance of countries towards imports from different areas can

change, which can in turn impact trade flows. Recent changes include Japan relaxing its restrictions to US beef imports and potential changes to US restrictions on beef imports from Brazil.

Yet while there are opportunities on the horizon for the industry, there remain challenges, including the structure of the red meat industry locally. The debate, fuelled by tight margins, volatility in prices and conditions, and the grass looking greener on the dairying side of the fence remains some way off a conclusion.

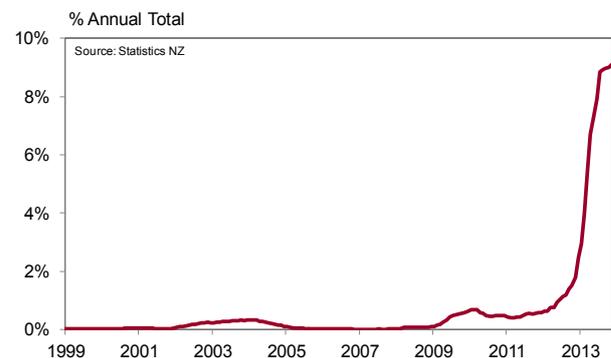
Global Dairy Trade Auction Results, 22 January

	Change since last auction	Price USD/Tonne
Anhydrous Milk Fat (AMF)	2.2%	\$5,641
Butter Milk Power (BMP)	3.0%	\$5,244
Butter	10.8%	\$4,657
Skim Milk Powder (SMP)	-0.5%	\$4,698
Whole Milk Powder (WMP)	0.1%	\$4,943
Cheddar	10.40%	\$5,133
GDT Price Index	1.4%	

Payout Forecast Table

	2013/14		2014/15
	Fonterra	Westpac	Westpac
Milk Price	\$8.30	\$8.40	\$6.70

Total Beef Exports to China (by value)



Anne Boniface
Senior Economist

See overleaf for sector outlooks.

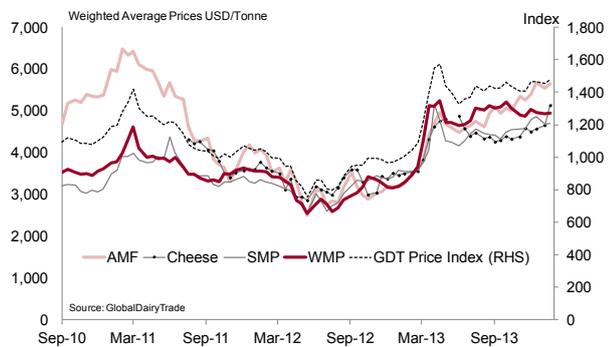
Beyond the farm gate



Dairy

	Current price level compared to 10 year average	Next 6 months
Trend	High	↘

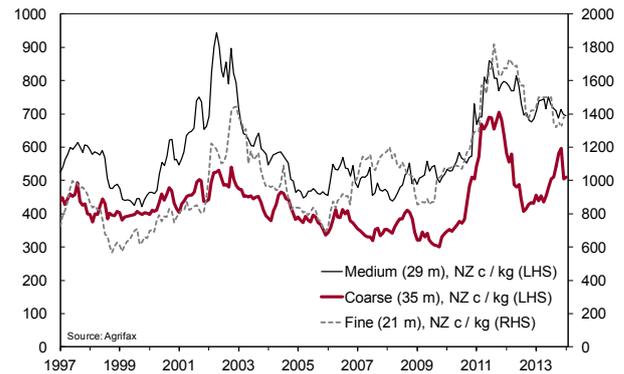
There was another solid global dairy trade auction last night. On a trade weighted basis prices rose 1.4%. Whole milk powder and skim milk powder prices continued to drift sideways (up 0.1% and down 0.5% on the last auction) while there was a big jump in cheddar prices. This further closed the gap between the two product streams which has been evident this season. Strong prices suggest demand from China for dairy products continues to hold up. We continue to expect to see dairy prices moderate in 2014 as global supply ramps up but it is starting to look as though this won't happen until closer to the middle of the year. Domestically production continues to run well ahead of last season, and the comparisons will only get more favourable as we move into the period where drought hit production hard in 2013. Nationwide production was 5.5% ahead of last year for the 6 months to November and we expect it to be up around 8.5% by the end of the season.



Wool

	Current price level compared to 10 year average	Next 6 months
Trend	Above Average	→

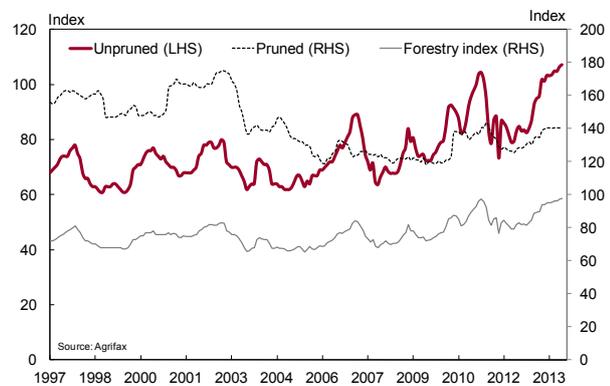
Local wool prices have started to climb again in recent weeks on the back of tight supplies. And there is a similar theme internationally. While Eurozone demand for high end wool products is likely to remain subdued, China is increasingly importing wool to manufacture products to meet its own demand for woollen apparel. ABARES reports that while China's exports of wool products to the US and EU are falling, this is being partially offset by increasing demand domestically and from South East Asia.



Forestry

	Current price level compared to 10 year average	Next 6 months
Trend	High	↘

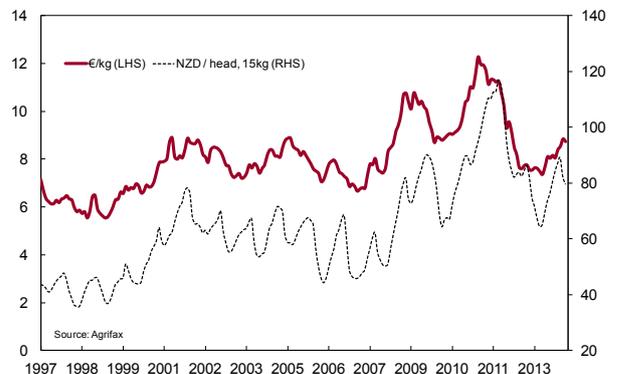
Strong demand from China for NZ logs pushed log prices up over 20% during 2013. Stats NZ reports that New Zealand is now the third largest exporter of logs in the world, after Russia and the United States. They report that in 2012 New Zealand supplied 8% of the total value of the world's log exports. Strong demand from offshore and increased building activity locally (as the Canterbury rebuild gathers steam) is putting upward pressure on log prices. While it is difficult to see prices taking a further step up from these already high levels, prices may drift sideways over the next few months.



Lamb

	Current price level compared to 10 year average	Next 6 months
Trend	Average	↑

International lamb prices have continued to edge higher in recent months. Domestically tight supplies, a remnant of last summer's drought and good pasture conditions encouraging farmers to add more weight to stock, should underpin prices during the seasonal decline over the next few months. While the Eurozone remains unambiguously weak, the UK economy has shown some positive signs in recent months, which may support consumer demand for lamb. Tight supplies in NZ and Australia should also help underpin prices. Locally many farmers are looking to take advantage of good pasture growth to improve finishing weights.



NB: Trend arrows indicate direction of change in world prices.

Westpac economics team contact details

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Felix Delbrück, Senior Economist
+64 9 336 5668

Anne Boniface, Senior Economist
+64 9 336 5669

Any questions email:
economics@westpac.co.nz

For email address changes contact:
WNZResearch@westpac.co.nz

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