

Fortnightly Agri Update

5 March 2014

Cherry on top

The current dairy season is shaping up as a record breaker on a couple of fronts. Firstly, there's the payout. With last week's upgrade by Fonterra, the forecast milk price payout for the 2013/14 season is now \$8.65. That's a whopping 48% above last season's level of \$5.84. This is easily a record in current dollar terms (with the 2011 farmgate milk price a distant second at \$7.60). New Zealand's other dairy companies are also capitalising on high international dairy prices. Westland has also been revising up its payout forecast. It's most recent forecast in December was \$7.90-8.30 (including retentions) and Synlait expects to pay its farmers \$8.30-\$8.40 KgMs.

Last season, Fonterra collected 1,463 million Kg of milk solids. Consequently, the jump in milk price means an extra \$4.1 billion in revenue for Fonterra farmers (assuming no growth in production).

But it doesn't end there. The real cherry on the top this season is the bounce in production. Here too, the 2013/14 season looks set to go down in the record books. At times in the past, high dairy prices have been driven by tight supplies locally. But that's certainly not the case this season. Dairy NZ reports that nationwide milk flows are running 6% ahead of last year (for the season to the end of February). And we think production could finish the season close up 10% to set a new high.

However, conditions have become much more challenging in some parts of the country as pastures have dried out. Waikato, parts of Northland, Wairarapa, Wanganui-Rangitikei and Marlborough are amongst the worst affected regions. In the Waikato milk production is up just 4% for the season to date according to Dairy NZ figures. That's well below the Bay of Plenty which is 9% ahead. Improved cash flow will help farmers in these parts of the country mitigate the impact of the dry conditions (e.g. by purchasing supplementary feed) to eke out as much milk as possible in the remaining few months of the current season.

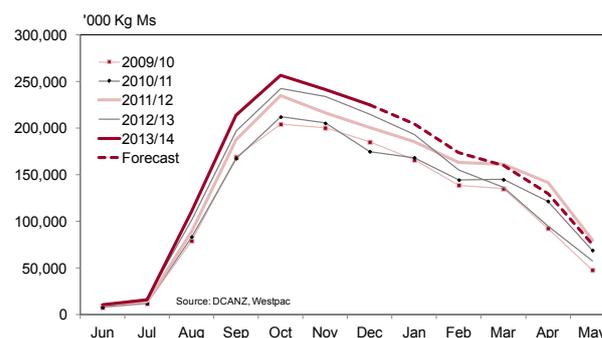
Overall high prices plus a bounce in production means \$5.4bn extra revenue for Fonterra farmers (and close to a \$6bn boost if incomes for non-Fonterra farmers are taken into account). That's equivalent to around 2.4% of GDP. So where will all this extra revenue end up? We think it will be a combination of saving/paying down debt, investment and spending on farm, with at least a portion flowing through to spending on consumer goods.

But while 2013/14 season will go down in the record books, we don't think such a sweet spot can persist indefinitely. We expect to see international dairy prices soften this year under the weight of increasing global supply. Indeed, we saw the biggest fall since mid-2013 in last night's GlobalDairyTrade auction. Prices fell 4% on a trade weighted basis, with lower prices for a range of products on offer including WMP (down 5.7%), SMP (down 3.9%) and AMF (down 3.5%).

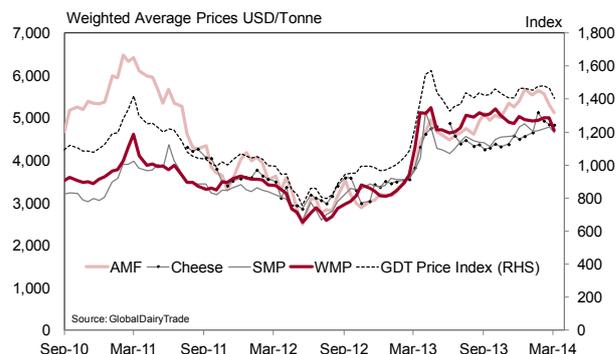
We are cautious about reading too much into a single GDT auction outcome (as these can be volatile from fortnight to fortnight). Indeed, the increased volume of WMP and SMP on offer in last night's auction may have been one factor weighing on prices.

However, we will be watching closely to see if last night's move signals the start of a move lower in prices.

NZ Milk Production



GDT auction prices



GlobalDairyTrade Auction Results, 5 March

	Change since last auction	Price USD/Tonne
Anhydrous Milk Fat (AMF)	-3.5%	\$5,126
Butter Milk Power (BMP)	3.9%	\$4,746
Butter	3.9%	\$4,746
Skim Milk Powder (SMP)	-3.9%	\$4,658
Whole Milk Powder (WMP)	-5.7%	\$4,703
Cheddar	0.70%	\$4,837
GDT Price Index	-4.0%	

Payout Forecast Table

	2013/14		2014/15
	Fonterra	Westpac	Westpac
Milk Price	\$8.65	\$8.65	\$7.10

Anne Boniface, Senior Economist.

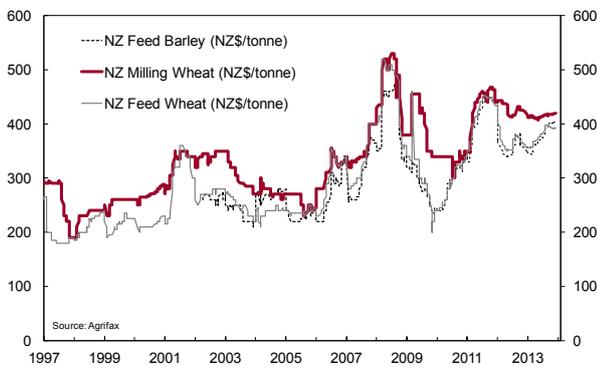


Grains

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

International grain prices have been among those commodities affected by tensions between Russia and Ukraine. Ukraine is expected to be the third-biggest corn exporter and the sixth biggest wheat shipper this season, and prices surged on fears that this supply would be disrupted by Russian troops moving into the Crimea region. Closer to home, ABARE's latest estimates are for Australian wheat production for the 2014/15 season to be 24.8m tonnes, down from 27m tonnes last season which should help support prices there.

NZ Feed grain prices rose over the course of 2013 and have broadly consolidated at these levels at the start of this year. Looking ahead, local prices may be supported by tight supplies, with the ongoing conversion of arable land into dairying (particularly in Canterbury) coinciding with high demand for feed grain in the region. Agrifax reports strong demand for maize grain in the North Island as dry conditions for dairy farmers and the high payout on offer underpin demand for supplementary feed.

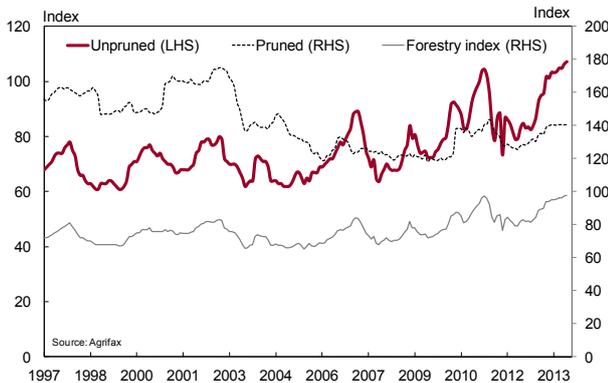


Forestry

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

Log prices continued to trek higher in February as demand from China remained strong and inventories at ports there remained tight. NZ is now the biggest softwood exporter to China, and limited supply from alternative sources is supporting demand for NZ product.

In January, the Ministry of Primary Industries upgraded their forecasts of forestry exports. Export revenues from the industry are now expected to be around 20% higher in both 2013/14 and 2014/15 than they thought 6 months ago. NZ log producers are responding to very high prices on offer by increasing their harvest rates.

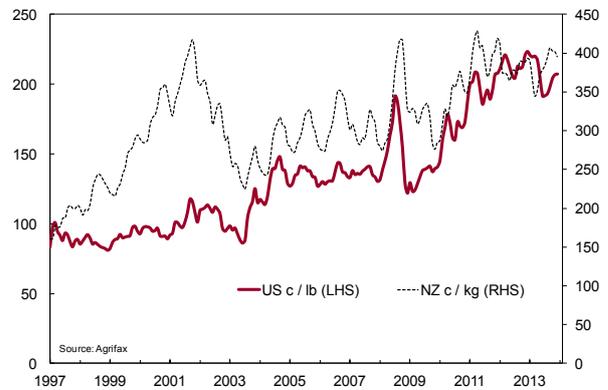


Beef

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

US domestic beef supplies remain very tight, with cattle numbers starting 2014 1% lower than levels a year ago, which is flowing through to reduced slaughter numbers. This was the 16th year of decline in beef cow inventories since 1996, which will continue to weigh on US beef production over the next couple of years as producers gradually rebuild herds.

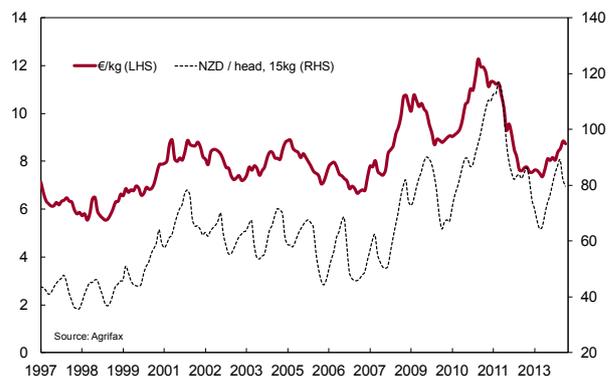
In contrast to tight US supplies, Australian beef exports were very strong in January, as drought conditions persist across much of Queensland. Australian producers are also optimistic about increased trade with South Korea on the back of an FTA due to be signed shortly by the two countries. While this is not great news for New Zealand producers, it could potentially provide opportunities in other regions if an increased proportion of Australian beef exports are diverted to Korea.



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

Disclaimer

Things you should know: Each time someone visits our site, data is captured so that we can accurately evaluate the quality of our content and make improvements for you. We may at times use technology to capture data about you to help us to better understand you and your needs, including potentially for the purposes of assessing your individual reading habits and interests to allow us to provide suggestions regarding other reading material which may be suitable for you.

If you are located in Australia, this material and access to this website is provided to you solely for your own use and in your own capacity as a wholesale client of Westpac Institutional Bank being a division of Westpac Banking Corporation ABN 33 007 457 141 AFSL 233714 ('Westpac'). If you are located outside of Australia, this material and access to this website is provided to you as outlined below.

This material and this website contain general commentary only and does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material and this website may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material and this website does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. The forecasts given in this material and this website are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Transactions involving carbon give rise to substantial risk (including regulatory risk) and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. Statements setting out a concise description of the characteristics of carbon units, Australian carbon credit units and eligible international emissions units (respectively) are available at www.cleanenergyregulator.gov.au as mentioned in section 202 of the Clean Energy Act 2011, section 162 of the Carbon Credits (Carbon Farming Initiative) Act 2011 and section 61 of the Australian National Registry of Emissions Units Act 2011. You should consider each such statement in deciding whether to acquire, or to continue to hold, any carbon unit, Australian carbon credit unit or eligible international emissions unit.

Additional information if you are located outside of Australia

New Zealand: The current disclosure statement for the New Zealand division of Westpac Banking Corporation ABN 33 007 457 141 or Westpac New Zealand Limited can be obtained at the internet address www.westpac.co.nz. Westpac Institutional Bank products and services are provided by either Westpac Banking Corporation ABN 33 007 457 141 incorporated in Australia (New Zealand division) or Westpac New Zealand Limited. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QFE Group Financial Advisers Act 2008 Disclosure Statement at www.westpac.co.nz.

China, Hong Kong, Singapore and India: Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking license and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activity.

Disclaimer continued overleaf.

Disclaimer continued

Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking Regulatory Commission (CBRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

U.K.: Westpac Banking Corporation is registered in England as a branch (branch number BR000106), and is authorised and regulated by the Australian Prudential Regulatory Authority in Australia. WBC is authorised in the United Kingdom by the Prudential Regulation Authority. WBC is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority in the United Kingdom. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. This material and this website and any information contained therein is directed at a) persons who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services Act 2000 (Financial Promotion) Order 2005 or (b) high net worth entities, and other persons to whom it may otherwise be lawfully communicated, falling within Article 49(1) of the Order (all such persons together being referred to as “relevant persons”). The investments to which this material and this website relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this material and this website or any of its contents. In the same way, the information contained in this material and this website is intended for “eligible counterparties” and “professional clients” as defined by the rules of the Financial Services Authority and is not intended for “retail clients”. With this in mind, Westpac expressly prohibits you from passing on the information in this material and this website to any third party. In particular this material and this website, website content and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission (“CFTC”) as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC (“WCM”), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 (‘the Exchange Act’) and member of the Financial Industry Regulatory Authority (‘FINRA’). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.

For the purposes of Regulation AC only: Each analyst whose name appears in this report certifies that (1) the views expressed in this report accurately reflect the personal views of the analyst about any and all of the subject companies and their securities and (2) no part of the compensation of the analyst was, is, or will be, directly or indirectly related to the specific views or recommendations in this report.