ANZ AGRI
INFOCUS
NOVEMBER
2019

COMMODITY INSIGHTS

ANZ

FOREWORD

As we enter the summer months and find the new year rapidly approaching, we may start to reflect on the year that has been for Australian agriculture.

Looking back, we have experienced a challenging but unique period, where tough climatic conditions have been met with reasonable to very strong commodity prices across our major agri industries. With some welcome yet patchy rainfall falling over the past few weeks in the east, there is yet to be a widespread break in drought conditions. For many, the commencement of summer will mean the start of another summer of feeding livestock and a second (or greater) summer cropping season without the sowing gear even leaving the shed. As these conditions play out, there is increased attention on the industry and its response to drought, and the role of various stakeholders in attempting to smooth the volatility for our producers through these difficult times. As a bank, we continue to see and support the benefits of forward planning for drought events, but of course there are some events that even the best-laid plans cannot foresee.

A learning for many from this current drought has been the importance of timely decisions. For cropping operations, this may have been a decision to cut crops for hay when grain yield and quality were questionable. For livestock producers, the decision has more likely been based upon a 'feed or sell' equation that can be complex when feed sources may be limited or unknown. The ability to make these decisions in a timely manner, and follow them through with support from business partners and advisors, has resulted in many producers still achieving good returns as domestic and international demand for our products continues to forge ahead.

Early in 2019, our sheep and wool producers were in the enviable position of lamb, mutton and wool prices combining to achieve exceptional returns, even under dry conditions. The good news story for lamb and mutton continues, however, the wool market has seen far more significant volatility throughout the year and experienced a price correction that places current indicator prices back in line with 2017 levels. With supplies of Australian greasy wool forecast to be well down due to the sell-down of the national flock, the 12 months ahead promises to be an interesting period as the impact of international trade tensions plays out and softens demand for woollen products.

For cattle producers, the Eastern Young Cattle Indicator (EYCI) and Western Young Cattle Indicator (WYCI) have been relatively flat this year, awaiting a much-needed and widespread rainfall event to kick start the market. The industry as a whole has, perhaps, gained a new appreciation for the presence of an adequately invested feedlot sector throughout 2019, as numbers of cattle on feed continue to be at all-time highs. The strong international demand for quality beef that sits behind feedlot growth has played a major role in sustaining saleyard prices throughout a dry year where many producers have been forced into offloading lighter than average stock into the market.

For our dairy producers, an uncertain start to the year was met with favourable opening milk prices from processors. Continuation of the dry, low water supply and allocations, and high fodder costs continue as major challenges for many dairy producers and contribute to a rising cost base for each kilogram of milk solids produced. From a global perspective, the low Australian supply of milk has recently coupled with lower than anticipated production from the United States, lifting global prices for manufactured milk products and assisting local processor/exporter margins.

Looking ahead, we certainly hope that 2020 brings with it a much kinder rainfall pattern, that enables the process of recovery from drought. We also hope that the Christmas and New Year period allows our producers some time to rest and recharge. Importantly, the fundamentals behind all of our major agri commodities remain sound, and we look forward to continuing our support of the sector through 2020 and beyond.

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WHEAT & GRAIN INSIGHTS

OVERVIEW

- The Australian cropping sector continues to be impacted by the drought, with the average forecast for this season's wheat crop at around 17 million tonnes
- Globally, while high-end stocks had previously limited price rises, recent weather impacts on the North American and Argentine crops, combined with Australia, are pushing prices upwards
- Recent rains, particularly in Victoria, have delayed the harvest, leading to a tightening of grain supplies
- Australia's share of global grain exports will fall to a multi-year low

Only three months ago, global wheat prices were feeling downward pressure in the wake of a record global harvest. However, as we head toward the end of 2019, a series of global factors are now pushing wheat prices up, a trend which is also being seen in Australia.

On the bearish side, global wheat stocks remain high and continue to climb in updated United States Department of Agriculture (USDA) estimates. At just under 290 million tonnes, this equates to a stocks-to-use ratio of around 38 percent. While this is roughly equivalent to the past two years, it is almost 50 percent up on the 2012/13 levels, and over 80 percent up on the 2007/08 figure.

However, a number of other global events are now combining to push prices up. While the Australian drought-impacted crop is perhaps the largest event, cold weather in the US and Canada is casting concern over the potential size of the North American spring crop and what this could mean for global supplies. For a number of cold-hit cropping areas in the northern US, there is speculation that the wheat crop may simply be ploughed into the ground to take advantage of that country's crop insurance program.

At the same time, the latest developments in the China-US trade disagreements may be positive for wheat. World markets reacted to rumours that China may be looking to purchase around 2 million tonnes of US wheat, a move which would bring a lot of confidence to global trade.

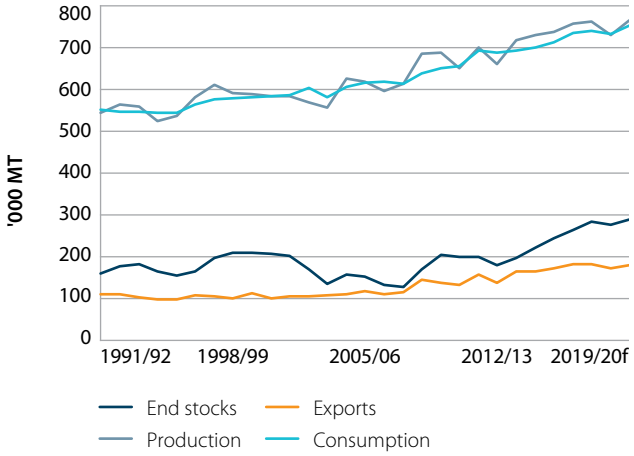
In terms of price, the bullish pressure is coming as a result of when the rain doesn't come, and when it does. In northern regions, including Queensland and northern NSW, grain buyers, particularly feedlots, are increasingly paying strong prices for Victorian and West Australian grain, with local supplies increasingly difficult to access.

In contrast, in much of Victoria and some parts of NSW, the recent rain has delayed the start of harvest, making available grain supplies even tighter and pushing prices up for local buyers.

In overall figures, the production outlook for the 2019/20 winter harvest continues to slide. On latest industry forecasts, which are, on average, suggesting a 17-million-tonne wheat crop, the conditions experienced through October and November could push the actual result even lower. Should this eventuate, Australia would experience its lowest wheat crop since 2007/08.

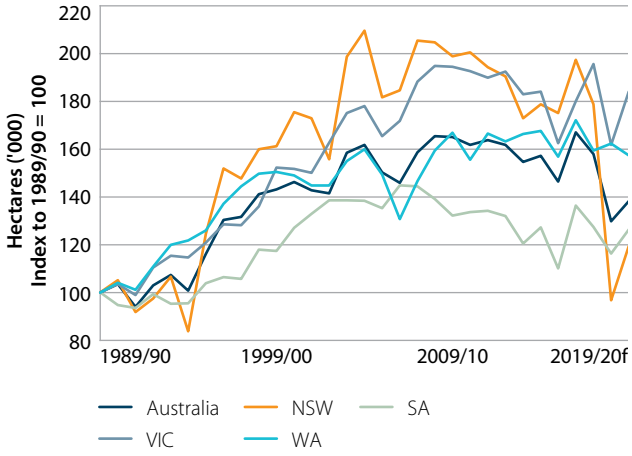
Notably, the forecast production level varies markedly by state. While NSW will see a recovery from the 2018/19 production levels, it remains heavily impacted by the drought. Wheat production may lift by around 50 percent on the previous year to just under 3 million tonnes, but is still likely to be below the 10-year average. In particular, the northern cropping regions of NSW are forecast to see the lowest rainfall on record. In Queensland, the central region around Emerald has seen average rainfall, in contrast to southern areas. Queensland's wheat production is likely to be up marginally this year to just under 0.5 million tonnes, but again well down on average.

GLOBAL WHEAT PRODUCTION, CONSUMPTION, EXPORTS AND END STOCKS



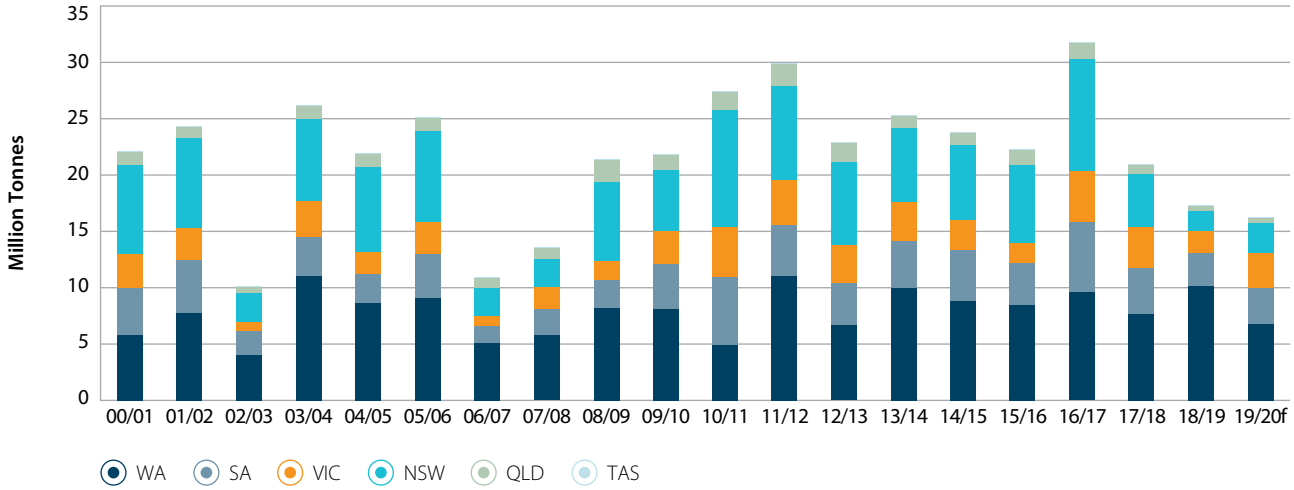
Source: USDA, ANZ

CHANGE IN WINTER CROPPING ACREAGE BY STATE



Source: ABARES, ANZ

AUSTRALIAN WHEAT PRODUCTION



Source: ABARES, ANZ

The state which is likely to see the least drought impact on cropping is Victoria. Most of Victoria's grain regions have experienced good conditions, apart from the Northern Mallee. With Victoria currently forecast to see a wheat crop of around 3.6 million tonnes, reasonably above the five-year average, the state is likely to be the focus for a great deal of national feed requirements.

In South Australia, similarly to Victoria, cropping fortunes are likely to vary over the north-south divide, with the state forecast to harvest a wheat crop of around 3.8 million tonnes, slightly below the five-year average. The winter rains brought relief to most cropping areas, apart from the northern regions. In Western Australia, the biggest grain producing state, most cropping areas were impacted.

Despite brief good rains in June, the subsequent return to below-average rain pushed the state's wheat production forecasts down again to around 8 million tonnes, slightly below average.

One interesting observation is that 2019/20 looks to be the year in all cropping states apart from WA that overall winter crop acreage has reversed its trending plateauing and decline. If reasonable rains return next year, it could be likely that cropping acreage could return to the high levels seen from around 2008–2013. However, with the long-term fundamentals for high sheep prices looking strong, many crop farmers may choose to retain a more diversified operation.

BEEF INSIGHTS

OVERVIEW

- Low volatility in cattle prices has been experienced throughout the east coast and in WA over the past few months
- Live export prices steady on the back of strong demand from Vietnam and Indonesia
- The liquidation of the Australian beef herd continues with female slaughter rates maintained at well over 50 per cent of total slaughter
- Production throughout 2020 expected to be subdued on the back of the poor seasons and a retain strategy once conditions improve
- Global beef demand being driven by a burgeoning need for protein in China as a direct consequence of African Swine Fever
- Australia's export market share will continue to feel pressure from competitors with growing supplies expected from Brazil and Argentina and others

Cattle prices have remained on a steady path over the past few months as poor weather conditions continue to dictate on farm management and sale strategies. The EYCI has traded between 468 and 520 cents per kilogram carcase weight (c/kg cwt) since the end of August, with November prices almost on par with prices from the same time last year. In the west, the WYCI has traded within a similar low level of volatility, although trading at a slight premium to the EYCI, on average, around 50 c/kg cwt higher over the past three months.

The grainfed beef industry continues to buffer the market as record cattle numbers enter feedlots. Latest available data from the June quarter suggests that over 1.147 million cattle were on feed for the April to June period this year, up around 27,000 head year-on-year. The increases in cattle on feed have been made possible via investment in the sector which has seen total feedlot capacity increase by around 6 per cent or 81,000 head year on year. The majority of this capacity building has occurred in Queensland, followed by South Australia and New South Wales.

In the live cattle trade, exports were up 21 per cent on the 12 months to September 2019, driven by increased demand for feeder cattle in Vietnam and Indonesia, and strong demand for slaughter weight cattle in Vietnam. The dry conditions throughout large parts of Australia's northern cattle production zones has led to plentiful supply, which fortunately has been met with sustained reasonable prices from a historical perspective.

Once conditions improve and local prices increase, these rising costs may put pressure on live exports particularly to markets where cheaper Indian buffalo meat is a viable alternative.

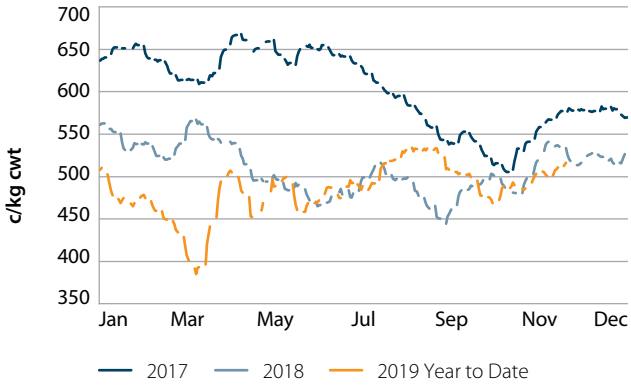
National cattle slaughter is up 7 per cent year on year to the end of August, with around 5.6 million head being processed. The lack of spring rain has bought some cattle to market sooner than they may have been presented in an average year, with Victoria claiming the highest year on year increase in slaughter compared to 2018 of 14 per cent. The national calf slaughter rate is also significantly up, presumably as a result of decisions to sell versus feed, with a national year on year increase of 27 per cent. Queensland has seen a stark 67 per cent increase in calf slaughter from 2018 levels.

The female proportion of slaughter cattle varies by state, however, a national average of 55 per cent for August is only slightly back on the 58 per cent record set earlier this year, and at this level, it continues to signal a state of rapid herd liquidation across the nation. Although slaughter rates are high on last year, the quality of stock in terms of carcase weights has seen a gradual decline, and hovered around the 280-kilogram mark this year, representing a 4 per cent decrease on carcase weights for the same period last year.

For beef production, assuming a return to average seasonal conditions, the consensus across the industry is that as restocker buyers enter the market, their purchasing activity will combine with a retain strategy from cattle breeders and traders, therefore limiting market supply and causing beef production to be subdued into 2020. Likewise, if poor conditions continue, the tight supply and lower production remains forecast, as a lower number of finished stock are expected to be coming through the system. Meat and Livestock Australia have forecast Australian beef production for 2020 at a little over 2 million tonnes cwt, which would be the lowest national production since 2000.

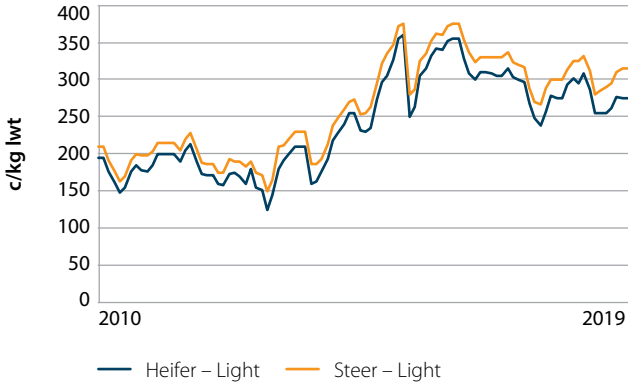
Globally, export demand for beef is forecast to be up to 4 per cent higher due to a reduced availability of protein following the consequences of African Swine Fever on pork production and supply throughout Asia. The United States Department of Agriculture (USDA) predicts a 3 per cent increase in beef consumption in China, which would generate a 21 per cent increase in China's beef imports in 2020. With Australian production down on the back of the reduced herd, the additional world beef demand is expected to be filled by Brazil, Argentina, the United States and India. Collectively however, global beef production is only forecast to be up by 0.9 per cent, creating a situation where demand could outstrip supply, therefore supporting strong global beef prices. Australian exports, which are up 7 per cent year on year to October, are increasingly driven by the China market, where exports are up a staggering 75 per cent for the same period. USDA forecasts that China will be responsible for 25 per cent of the global beef trade in 2020, from just 4 per cent five years ago in 2014. Looking ahead to 2020 however, Australia's ability to supply will be limited by production, with exports tipped to be below 1 million tonnes shipped weight.

EASTERN YOUNG CATTLE INDICATOR



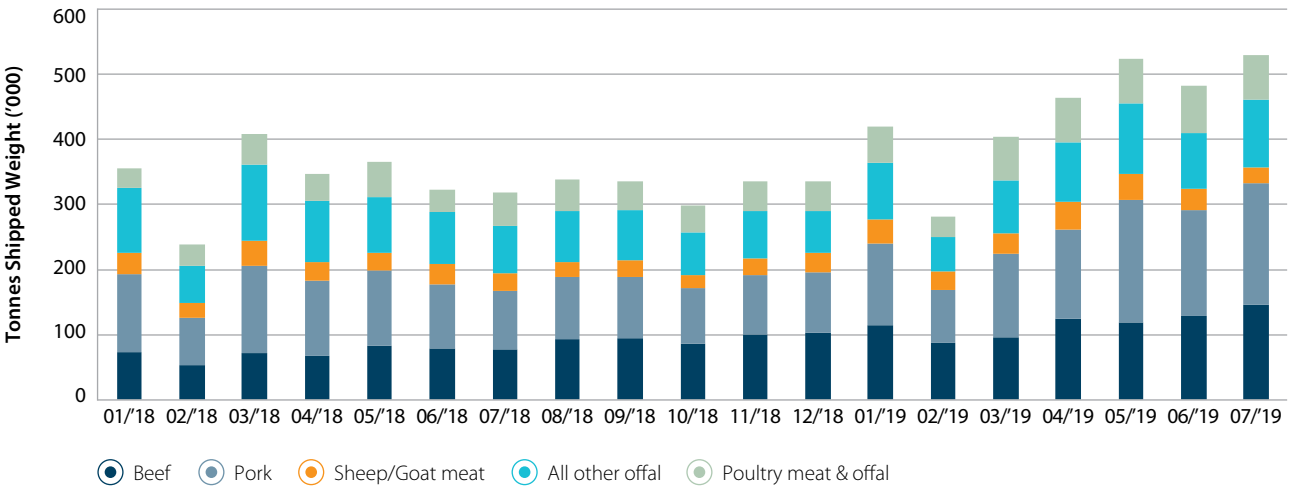
Source: Meat and Livestock Australia

LIVE EXPORT CATTLE PRICES, INDONESIA, EX DARWIN



Source: Meat and Livestock Australia

CHINA MONTHLY MEAT IMPORTS



Source: USDA

SHEEP INSIGHTS

OVERVIEW

- Lamb prices continue to ease despite rains in the north boosting prices in select saleyards
- Increased yardings and slaughterings have put downward pressure on prices
- Flock rebuilding is supporting prices as the spread between restocker and light lambs increases
- Exports continue to provide support to prices
- The New Zealand flock has posted an increase in numbers as dairy farming wanes

The Eastern States Trade Lamb Indicator (ESTLI) continues to ease back from the highs experienced in July as yardings and slaughter rates increase. However there are some indications that the northern market prices are set to jump ahead of southern saleyard prices, as low supply and recent rains have increased demand. While prices have come back to be sitting at or near 2018 prices, the drop in prices at this time of year is not unusual as spring lambs hit the market before Christmas, and the ESTLI still sits over 130c higher than 2017 and around 100c higher than at the beginning of the year.

Yardings have boomed in southern states, particularly Victoria and South Australia, and the lamb slaughter rate which lagged previous years throughout July and August has now jumped to be on par with 2018 levels. Lamb slaughter rates are relatively stable across the states, although Queensland lamb slaughter has jumped very strongly on this time last year, albeit from a low base. Sheep slaughter rates have been increasing strongly since July – although sheep slaughter rates are split across states with South Australia and Victoria showing signs of focusing on flock rebuilding, while the drought-impacted States of Queensland and New South Wales are currently slaughtering sheep at a higher rate than this time last year.

The ESTLI has continued to ease, now sitting just over 750c/kg however saleyard prices are mixed across categories. Since the peak in mid-July, the heaviest hit categories in the saleyards have been heavy lambs which have fallen in the region of 25 per cent, trade lambs which have fallen nearly 20 per cent and merino lambs.

LAMB SLAUGHTER RATES ARE RELATIVELY STABLE ACROSS THE STATES, ALTHOUGH QUEENSLAND LAMB SLAUGHTER HAS JUMPED VERY STRONGLY ON THIS TIME LAST YEAR, ALBEIT FROM A LOW BASE

At the other end of the spectrum, restocker lambs have only fallen 3 per cent while mutton and light lambs have suffered declines of just over 10 per cent. As better quality lambs continue to enter the market in increasing numbers in the lead-up to Christmas, we are likely to see the margin between restocker lambs and other categories continue to grow.

Saleyard prices have gained a strong premium on over-the-hook prices across the country, as producers are increasingly selling through saleyards instead of to processors. This has been the case for much of 2019 with many processors feeling the pressure of higher than anticipated saleyard prices.

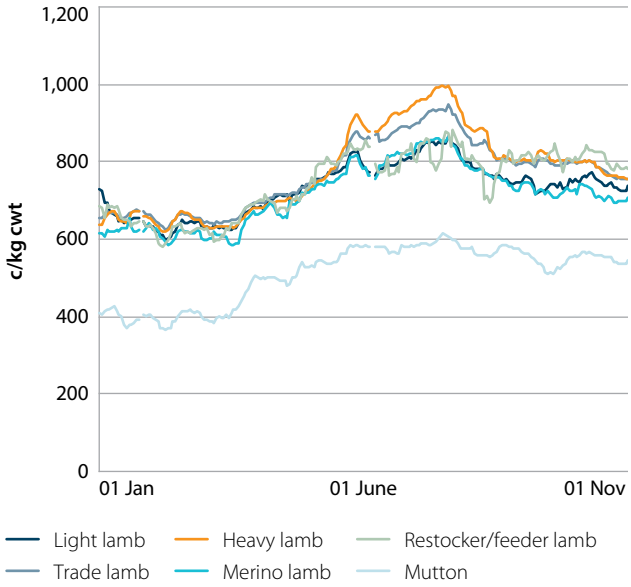
Flock rebuilding, the impact of drought and relatively good prices will continue to play a significant role in the outlook in the industry, with the Meat and Livestock Agency forecasting the national flock falling to a record low of 66 million in 2019 before rebuilding slowly.

Making the task of flock rebuilding harder is the relatively low number of breeding ewes in the national flock which, while not at record lows, is sitting at almost 6 per cent lower than in 2010.

Exports continue to support demand and prices with the most recent figures are showing that 233,332 tonnes of lamb has been exported year-to-date, up from 220,808 tonnes last year. African Swine Fever continues to drive demand in China with demand for both mutton and lamb jumping very strongly, with some in the industry describing China's demand as 'insatiable'. In the month to October, lamb exports to China hit a new record high of 7,745 tonnes, with the previous high being reached as recently as May this year.

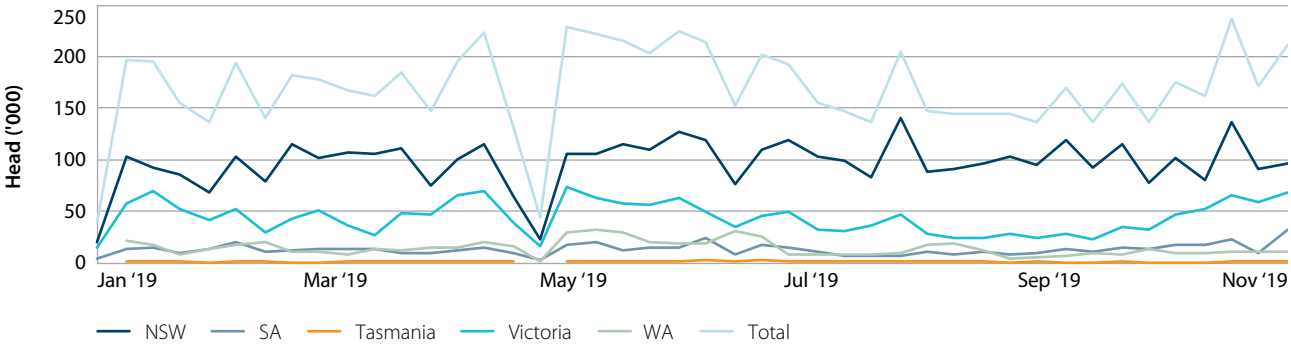
Australia's position in global lamb and mutton exports has been particularly strong now for a number of years as sheep flocks have declined across a number of major competitor markets. However, as increased environmental and government regulations hit the New Zealand dairy industry, it appears that many NZ farmers are returning to sheep farming with the national flock estimated to increase by 0.4 per cent in 2019 – the first increase in numbers since 2012 and down from the 1992 peak of 70 million.

SALEYARD SHEEP PRICES 2019



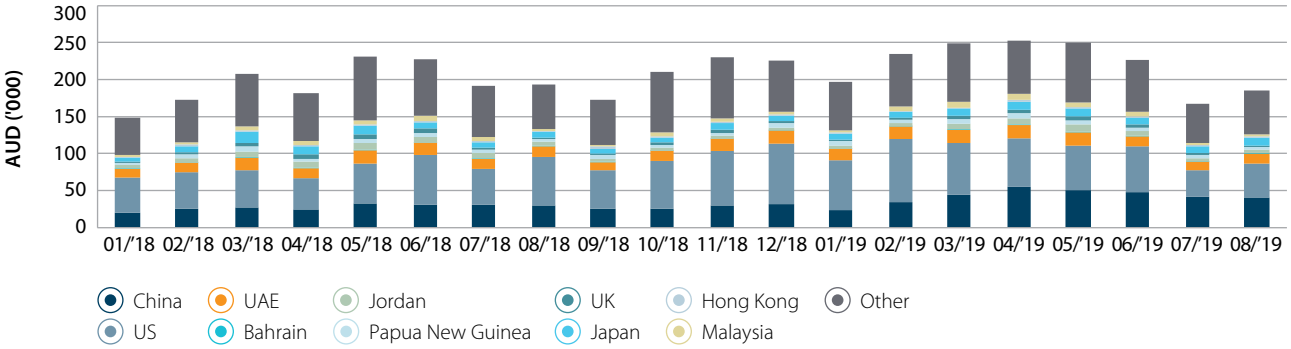
Source: Meat and Livestock Australia

YARDINGS BY STATE



Source: Meat and Livestock Australia

EXPORTS



Source: Meat and Livestock Australia

WOOL INSIGHTS

OVERVIEW

- Wool prices have stabilised somewhat in October–November however variances have been large since the winter recess
- Producers are holding back on sales in terms of the bales offered and pass-in rates when the market falls, while buyers appear to be holding back when prices rally
- Australian wool production is forecast to be down to under 300 mkg for the 2019/20 season
- Subdued demand for woollen products caused by instability in the major wool consuming markets of Europe and China are said to be the main cause of both the falling market experienced this year and the recent volatility

Wool prices have experienced a volatile period since the winter recess, with the Eastern Market Indicator (EMI) fluctuating between 1365 cents per kilogram (c/kg) and 1609 c/kg from early August through mid-November. The Western Market Indicator (WMI) has also traded within a similar range, however, more quickly found stability when compared to eastern markets.

Following what had been a downward trend over the months prior to the recess, August prices dipping to the mid-1300 cent mark came as a shock to some producers, considering pricing had started out the 2019/20 season in July at around 1750 c/kg. More recently, throughout October and November, the market has stabilised in comparison and has experienced short-lived, modest price rises followed by small corrections.

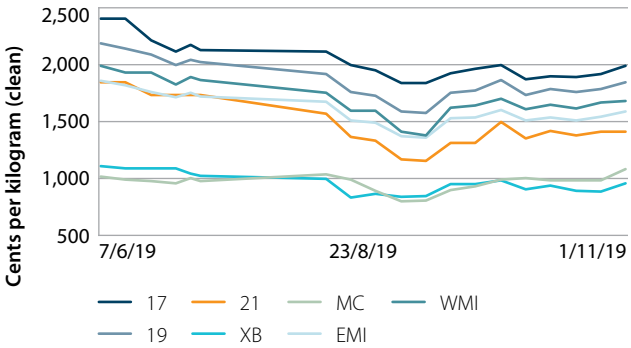
Such market conditions are making selling decisions difficult for producers who are hoping to extract whatever premium they can under the pressure of continuing dry conditions. Large fluctuations in bales on offer are occurring weekly as a direct result of the previous weeks sale results. Likewise, buyers are unlikely to be enjoying the instability, dealing with both large fluctuations in supply between weekly auctions, coupled with high pass in rates, which peaked at over 33 per cent at one sale this season.

Globally, industry sources are quoting subdued demand for woollen products as the major cause of market instability. Unstable economic conditions, particularly through the two major woollen garment markets of Europe and China, are reportedly impacting on discretionary spending on high value products like wool. Not unlike many of Australia's other major Agri commodities, the Chinese domestic market is becoming of increasing importance to wool producers. China imports around 75 per cent of Australian wool, and Australian Wool Innovation (AWI) estimate that up to 60 per cent of this is now remaining in China for the Chinese consumer. AWI quote that in 2009, China imported the same percentage of Australian wool, however almost 100 per cent of the processed and finished garments were then exported to other nations.

In regards to wool production, the most recent forecast available from the Australian wool production forecasting committee suggests that 2019/20 will see a 5 per cent decline in production nationally. A clip of around 285 million kilograms (mkg greasy) is forecast, which would represent Australia's lowest clip on available records, commencing with in 1992. The largest reductions in wool clip will come from NSW, where production is forecast to drop from 99 mkg greasy in 2018/19 to around 88 mkg greasy in 2019/20.

Looking forward, limited supply may favour Australian producers, perhaps providing a floor in market pricing given Australia is the world's dominant supplier of fine merino wool. Trade tensions and resultant tariffs have led to uncertainty in the wool supply chain that appears to have reached the consumer and therefore impacted on demand for raw product. Market sources suggest that wool prices could remain unstable for some time, as demand wavers due to global political uncertainty.

AUSTRALIAN WOOL INDICATOR PRICES (NORTHERN REGION)



Source: Australian Wool Network

COTTON INSIGHTS

OVERVIEW

- 2019/20 Australian harvest likely to be lowest since 2007/08 at around 750,000 bales
- Further dry conditions and low water allocations driving reduced plantings and yield
- Global production and storage at record highs
- China relying more on Australian cotton as tensions with US continue
- Strong basis keeping prices in Australia buoyant

There is unlikely to be much respite for cotton growers in New South Wales and Queensland. An extended dry period across typical cotton producing areas has left producers cautious about the summer ahead, with plantings expected to be down. Dryland growers do not have access to sub-soil moisture, and the majority of irrigators are dealing with allocations below 100 per cent and depleted water storage levels.

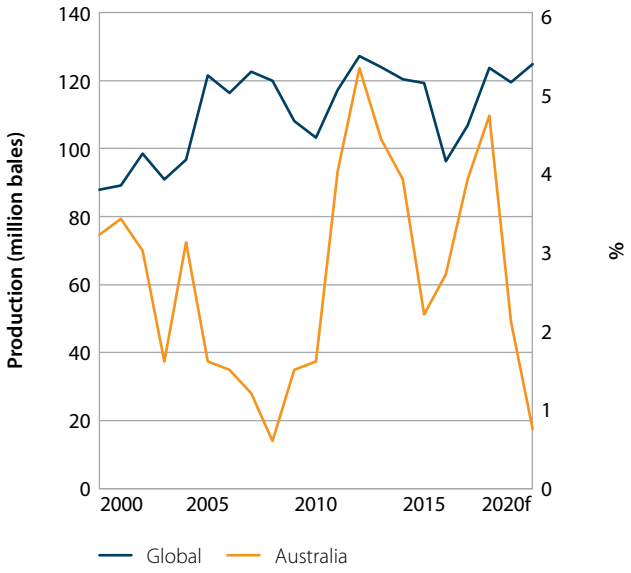
According to ABARES and Cotton Australia, unless substantial rain is received between now and mid-December to refill soil moisture profiles and boost dryland plantings, Australia's total production for 2019/20 is likely to be around 750,000 bales. This represents less than one-fifth of the record crop grown in 2011/12 of over 5 million bales and less than a third of the ten- year average of 3 million bales. The Bureau of Meteorology has also indicated that spring and summer rainfall in key cotton production areas is likely to be below average, pointing to a reduced yield for the growers that are able to plant.

Current dam levels and subsequent irrigation allocations are also having a detrimental impact on Australia's production forecasts and driving water prices higher. The Namoi River system's current level is 3.1 per cent, Macquarie system 10.5 per cent and the Lachlan system 19.2 per cent. Temporary water prices in some areas are such that growing cotton is looking unviablein the current season.

On the global front, the USDA is forecasting record 2019/20 production of 124.8m bales which is 5 per cent higher than last year. This is driven by favourable conditions in India, China and Pakistan and is despite production levels decreasing in Brazil, Pakistan and Australia due to dry conditions, and Hurricane Nestor impacting the US harvest.

Additionally, the trade war between the US and China is providing negative macroeconomic sentiment and global uncertainty, which is impacting consumption. World ending stocks are projected to be 3 million bales, higher than last year at 83.7m bales which will likely have a negative impact on prices.

COTTON PRODUCTION



Source: ABARES, USDA, Cotton Australia

Recently, thoughts of a trade deal between the US and China have seen a US market rally, however analysts believe this could be speculators off-setting their positions. Global prices have been on a steady downward spiral, however, a strong Australian basis has predominantly sheltered Australian producers from this market decline. The trade war has resulted in Chinese mills turning to Australian cotton instead of purchasing heavily tariffed US cotton, while domestically the prolonged period of drought has meant that Australia's cotton merchants are having to compete for bales. Given the export-orientated nature of the industry, the falling Australian dollar has helped strengthen the basis even further.

SUGAR INSIGHTS

OVERVIEW

- The drought continues to hit Australia's sugar production sector, impacting both acreage and production levels
- Australian sugar exports are increasingly challenged in key markets by South American sugar
- Australia continues to challenge Indian domestic sugar subsidies in the World Trade Organisation
- While global sugar production may decline slightly this year, high sugar reserves are likely to keep prices flat

As with most other agri sectors in Australia, the drought has resulted in 2019 being a challenging year. According to some observers, the sugarcane harvest for this year will end up being just under 30 million tonnes, a fall of around 3.5 per cent on 2018 and around 7 per cent down on 2017. This is roughly in line with national sugar acreage, which fell around 3 per cent this year to around 380,000 hectares, with the likelihood of a similar decline in 2020.

While overall sugar production is forecast to be down around 6 per cent in 2019 to around 4.4 million tonnes, sugar exports could be even further reduced, dropping by over 13 per cent to 3.6 million tonnes. In terms of value, this could see this year's sugar exports drop by 9 per cent to just over $1.5 billion.

Looking ahead, the outlook for the industry in 2020 remains at the mercy of the weather, with the potential for production figures to vary widely depending on the rain.

However, the structure of Australia's sugar industry makes it relatively more vulnerable to regulatory changes in other countries than many of its competitors. In comparison, however, the domestic sugar industries of countries such as Thailand and Brazil have a greater diversification of revenue, including a far larger share of domestic production going into areas such as ethanol, molasses and co-generated power.

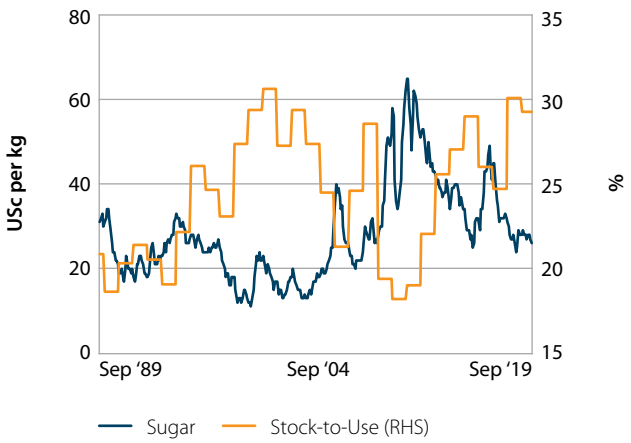
In terms of exports, Australian sugar remains primarily destined for Japan and South Korea, well ahead of Indonesia in third place. Looking ahead, however, competition in these markets is likely to grow from an increased presence of South American sugar.

Outside of the drought, one of the major challenges highlighted by the domestic sugar industry has been the impact of Indian production levels on world markets and prices. Over the past year, Australia has taken action against in the World Trade Organisation (WTO), alleging that India's domestic sugar subsidies were leading to a global glut of sugar and downward pressure on prices, and were against WTO regulations.

In response, India has argued that the subsidies are necessary to maintain the livelihoods of around 60 million small-scale sugar cane farmers. Due to the fact that the grower subsidies have led to mills having difficulty in paying farmers for the large production volume, the Indian Government has also raised the minimum selling price of sugar, provided support to exports, and instructed banks to provide soft loans to sugar millers.

In terms of global sugar production, strong declines in India and Thailand, respectively driven by flooding and a shift to alternative crops, is likely to see a global decline of around 2 per cent, which may start to put upward pressure on prices. However, with current global sugar stocks remaining at a relatively high stock to use ratio of 30 per cent, prices may foreseeably change little for the next 2–3 years, until these stocks are cleared from the pipeline.

WORLD SUGAR PRICE VS STOCKS TO USE RATIO



Source: USDA, Index mundi

DAIRY INSIGHTS

OVERVIEW

- Dairy prices have shown strong growth as lower than anticipated production hits the market
- Developing nations continue to drive the strongest demand for dairy, although much of that demand is likely to be met by local production
- Australian production continues to fall with total number of dairy farms decreasing by 46 per cent since 2002

The global dairy market has started to firm in recent weeks, as lower than anticipated production in Australia, the European Union and the United States has finally filtered through to prices. The most recent Global Dairy Trade auction saw the average price put in a strong performance, rising 3.7 per cent – with the strongest gains being shown in skim milk powder (6.7 per cent) and whole milk powder (3.6 per cent). In the longer term, despite showing some weakness earlier in 2019, dairy prices are holding their ground despite global trade tensions.

A poorer than anticipated production season across the United States and European Union, as well as Australia's decline in production, has meant that supply has tightened and is expected to continue to tighten for the remainder of the year. While slow production growth bodes well for prices for the remainder of the year, ongoing international trade tensions had, until recently, kept a lid on those prices.

Across the mix of products, cheese prices have remained relatively steady across the year, however, US cheese prices have jumped recently to over $US4,300/MT while Australian and New Zealand cheese prices have dropped to almost on par with the cheaper European cheese. In contrast, butter prices have come back significantly following the surge the 2017 and 2018 with butter prices now sitting over $US4,110/MT in the EU and Oceania, down from the heights of over $US8,000/MT in 2017 after a strong production response to high prices. Whole milk powder production has fallen from last year and while prices have remained relatively stable throughout the year in the EU and Oceania, the US has exhibited strong and consistent growth in Whole Milk Powder (WMP) prices. Skim Milk Powder (SMP) prices have also recovered strongly as the EU continues to run down the last of its stockpile with Oceania SMP prices now sitting almost 35 per cent higher than the same time last year. While global SMP demand has remained relatively flat for a number of years, the global stocks-to-use ratio has now fallen to 12.7 per cent down from highs of 26.5 per cent in 2016.

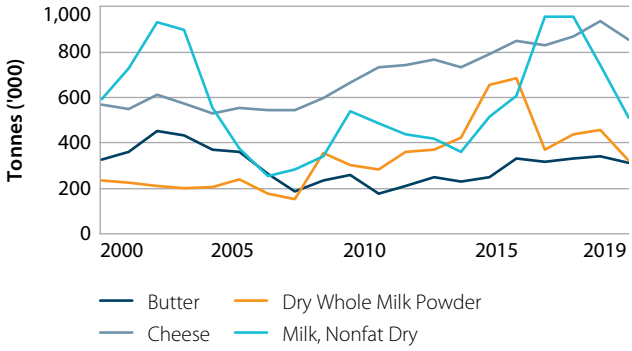
Global consumption of dairy products continues to exhibit stable and strong growth, particularly for butter and skim milk powder. Fluid milk, cheese and whole milk powder are showing consistent growth and low volatility in demand. Developing nations continue to drive the strongest growth in demand, particularly in relation to fluid milk. In response, the OECD is forecasting 80 per cent of the increase in production is anticipated to come from developing countries, in particular Pakistan and India, which are expected to jointly account for 32 per cent of total milk production by 2027. However, of that increase in production, most of this additional production will be consumed domestically as fresh dairy products. As a result, the major markets for Australian exports, particularly cheese, are likely to remain to China, Japan and the rest of the Asia market. On the positive side, the depreciation of the Australian dollar compared to the US dollar has improved affordability of Australian exports despite the relatively high Australian farm-gate milk price.

In the year to August, milk production in Australian fell 6.9 per cent due to drought conditions, high fodder costs and soaring water prices. Dairy Australia is currently forecasting a decrease of 3–5 per cent in national milk production to 8.3–8.5 billion litres for the season.

This decline in production has been accompanied by the reduction in total number of farms of 46 per cent since 2002. Those losses have been most concentrated in Queensland, South Australia and New South Wales, where declines of up to 67 per cent have been felt. In contrast, the southern states of Victoria and Tasmania have seen less dramatic declines of 39 per cent and 24 per cent of farms respectively.

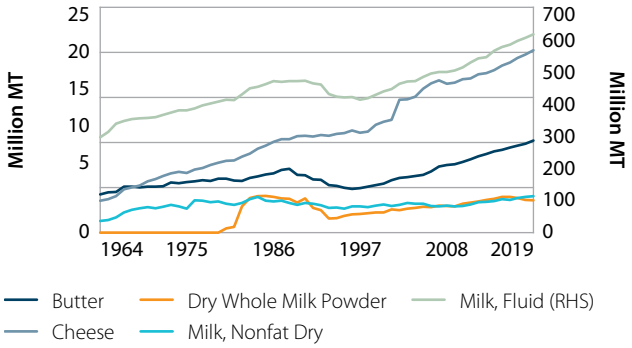
THE GLOBAL DAIRY MARKET HAS STARTED TO FIRM IN RECENT WEEKS, AS LOWER THAN ANTICIPATED PRODUCTION IN AUSTRALIA, THE EUROPEAN UNION AND THE UNITED STATES HAS FINALLY FILTERED THROUGH TO PRICES

GLOBAL ENDING STOCKS



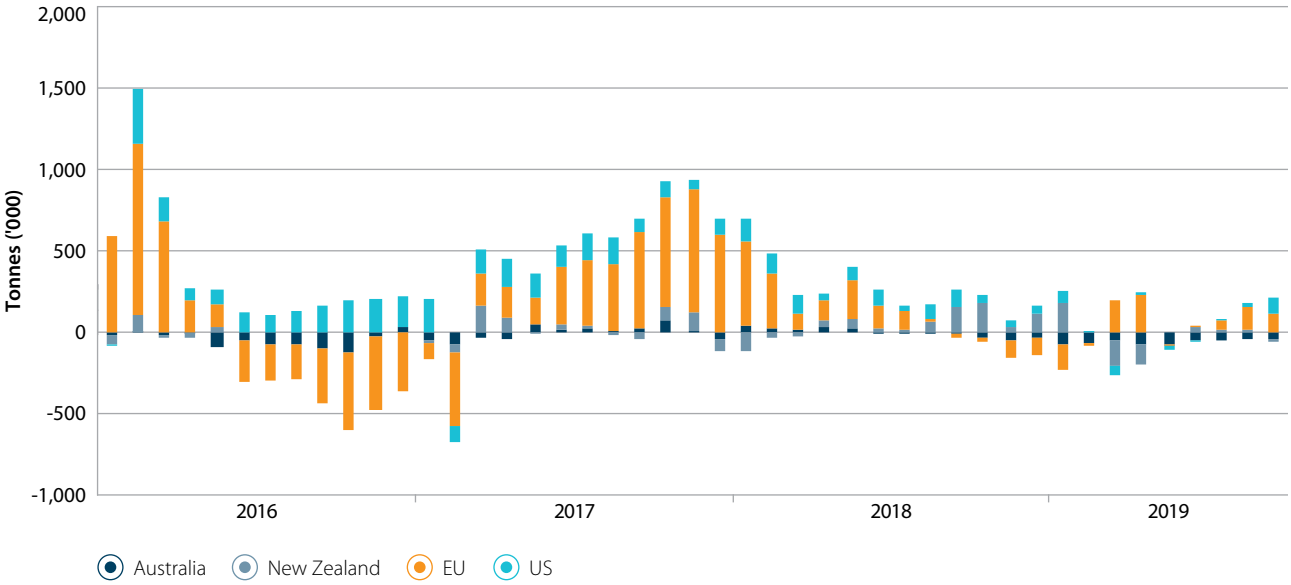
Source: USDA PSD

GLOBAL CONSUMPTION OF DAIRY PRODUCTS



Source: USDA PSD

CHANGES IN GLOBAL PRODUCTION



Source: USDEC

CITRUS INSIGHTS

OVERVIEW

- Australia's citrus industry has gone through a period of very strong growth on the back of strong export demand
- Increasing water prices have put significant pressure on many citrus growers
- Strong export demand from China has driven industry growth, however, competitors such as Chile are increasingly looking to enter the China market

The Australian citrus industry was worth $476 million in 2017–18, up from $345 million five years earlier. Growth in the industry is due, in large part, to strong growth in export markets where Australia's reputation for high-quality produce and competitive advantage – due to its harvesting periods compared to Northern Hemisphere competitors – have provided very strong demand. Today, there are over 20,000 hectares of citrus planted and around 900 growers operating. Major production regions are in the Riverland, South Australia; Murray Valley, Victoria and New South Wales; Riverina, New South Wales and the Central Burnett region in Queensland.

While the industry has grown significantly in value, a large part of that growth in value has been through a growth in prices rather than in production. Today there 6.6 million citrus trees planted – which has remained relatively stable over the past 5 years. Expansion and new plantings are a relatively slow process as biosecurity rules prevent importation of trees, and local supply is limited. The greater change in the industry has been the increase in plantings of navel oranges at the expense of Valencia. According to the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES), total production of oranges in Australia has fallen 15 per cent in the five years to 2016–17.

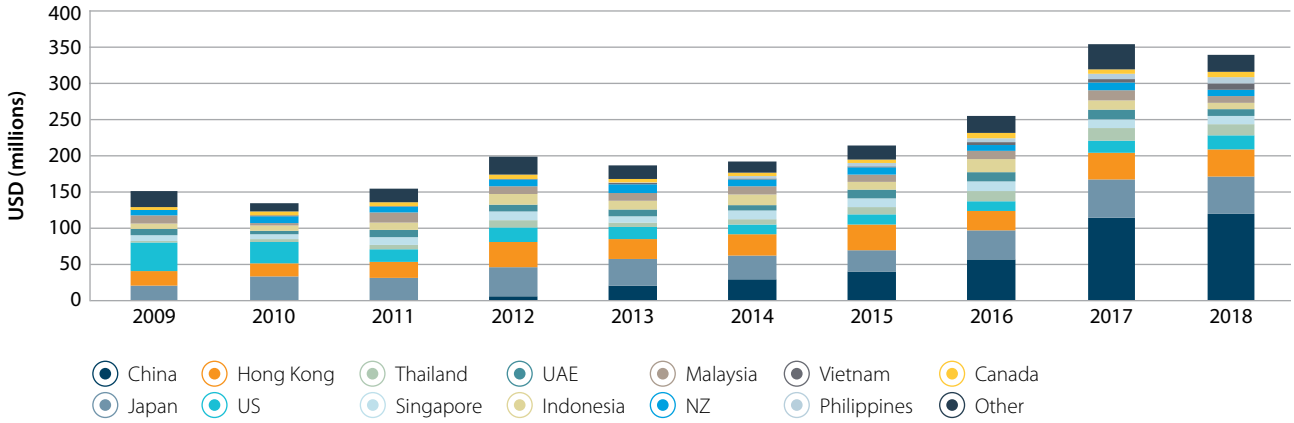
The USDA is forecasting that fresh orange production in 2018/19 will fall to 520,000 metric tons in 2018/19. However, this forecast was made assuming average seasonal conditions and the continued availability of irrigation water.

WHILE THE INDUSTRY HAS GROWN SIGNIFICANTLY IN VALUE, A LARGE PART OF THAT GROWTH IN VALUE HAS BEEN THROUGH A GROWTH IN PRICES RATHER THAN IN PRODUCTION

Around 21,000 hectares of orange orchards have been planted in Australia, of which an estimated 12,000 hectares are navels and the balance are Valencia trees. Valencia oranges are mainly grown for juice production while navels are an eating variety, which is in strong demand internationally. Three-quarters of Valencia oranges are processed into fruit juice for the domestic market.

As the majority of Australian orange production occurs in the Murray-Darling Basin, production levels and producers' margins are highly reliant on water allocations and prices. The recent drought conditions and lower than average water available for irrigation has seen many orange producers have their margins impacted severely. Lack of water availability have also led to some producers in the Lower Darling turning off the water to their permanent plantings and exiting citrus production.

AUSTRALIAN CITRUS EXPORTS (VALUE)



Source: TradeMap

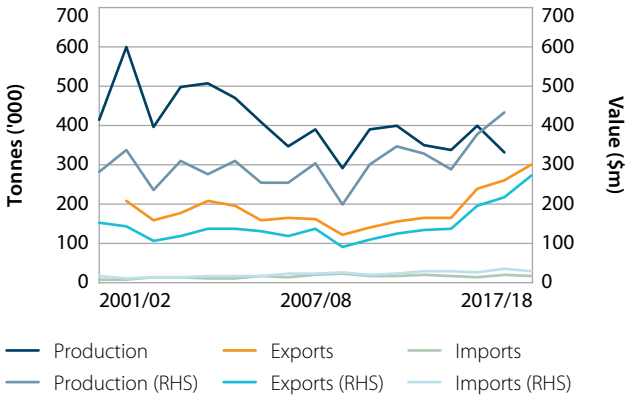
Australian exports of oranges have boomed in recent years, primarily off the back of the China-Australia Free Trade Agreement and opening of the Chinese market to Australian oranges as well as the recognition of the South Australian Riverland region as fruit fly-free. Recently however, the USDA forecast Australian orange exports for 2018/19 to have fallen 6.5 percent on 2017/18 due to lower production. The per tonne value of Australian orange exports has grown substantially in recent years, with the average export price rising an average of 20 per cent in the past five years. Of that, average per tonne export prices to China rose 9 per cent while export prices to Japan rose 27 per cent.

Globally, the USDA is forecasting global orange production for 2018/19 to increase 6.3 million metric tons (tons) to 54.3 million. This is the largest harvest in eight years and comes primarily from the United States and Brazil due to good weather conditions. However, fresh orange exports are expected to be down slightly as Brazil and Florida primarily produce oranges for processing. The large increase in production in the United States comes as production in Florida returns to normal following the losses suffered in 2017/18 due to Hurricane Irma.

However, in the longer term, the USDA is forecasting that US citrus production will decline from 16.07 billion pounds in 2019 to 14.7 billion pounds in 2028. The declines are expected to result from and the loss of bearing acreage in Florida and the continued spread of citrus greening, a citrus disease spread by insects.

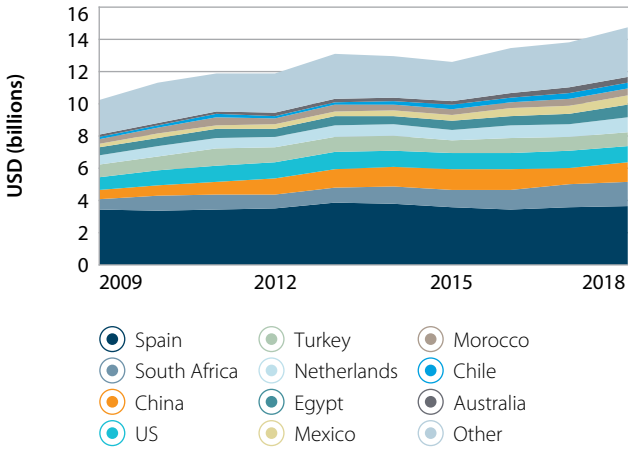
For Australian producers, however, there are some threats on the horizon as analysts expect increased competition from Southern Hemisphere orange producers, particularly Chile, who is looking to diversify away from their reliance on the US export market.

AUSTRALIAN CITRUS PRODUCTION AND SUPPLY



Source: ABARES

GLOBAL CITRUS EXPORTS (VALUE)



Source: TradeMap

AQUACULTURE INSIGHTS

OVERVIEW

- The Australian fisheries sector continues to grow strongly in production value, primarily driven by export demand
- While wild catch still makes up the majority of production, the output from farmed aquaculture is gaining rapidly
- Despite global seafood consumption rising steadily, per capita consumption in Australia is actually declining
- Export of rock lobsters into China continues to grow strongly, in both direct trade, and through Hong Kong and Vietnam

Australia's fisheries sector is one of our largest agribusiness sectors, with its productive value forecast to rise 4 per cent to $3.3 billion. The fisheries sector is made up of two parts: wild-caught products and aquaculture. Proportionally, wild catch still makes up the majority of the industry, but the gap is closing fast. In terms of volume, wild-caught fisheries produced 166,000 tonnes (or 64 per cent of overall volume) in 2016/17, compared to 94,000 tonnes (or 36 per cent) for aquaculture. In terms of value, however, the wild-catch sector produced $1.7 billion (or 56 per cent), while the aquaculture sector was valued at $1.3 billion or 44 per cent.

For the wild catch sector, a number of factors have impacted its growth, including changes to the number of allowable catches of some species, high input costs, and the impact of the AUD.

Aquaculture production volume increased 53 per cent in 10 years to 2016–17 and can be largely attributed to rise of salmonid production.

Overall, salmonids make up the largest share of overall fisheries production value, worth around $830 million in 2018/19, followed by rock lobster on $678 million, other fish on $438 million and prawns at $375 million.

In terms of demand, fish consumption has continued to trend upwards, both globally and within Australia. Across the world, fish and seafood provide the largest source of animal protein (178 million tonnes), poultry (125 million tonnes), pork (118 million tonnes) and beef (70 million tonnes).

A comparison of seafood consumption trends between the Australian and global figures present an interesting contrast. Globally, annual seafood consumption per capita sits at around 20.5kg, up considerably from 4kg in 1961.

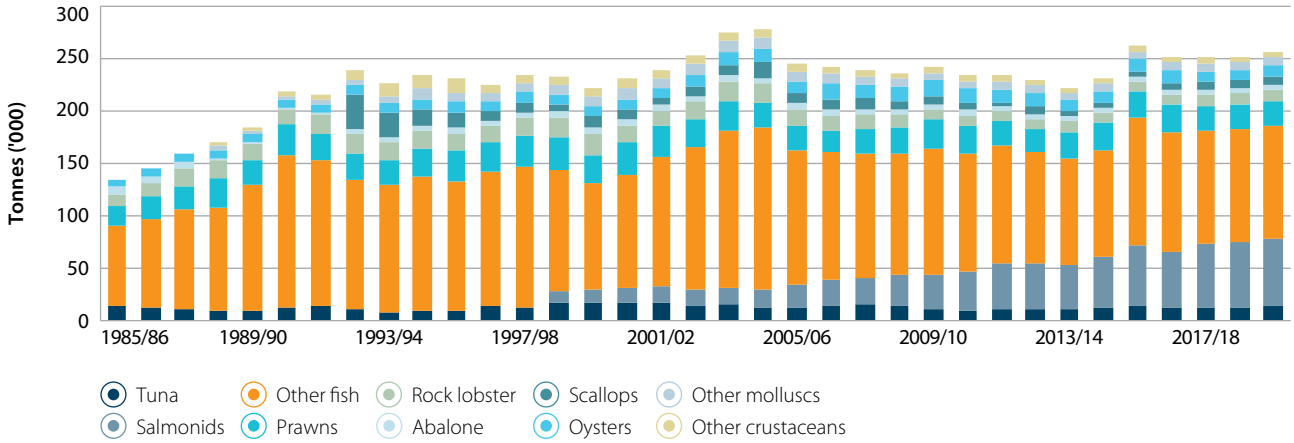
For Australia, overall seafood consumption has grown relatively slowly, at just over 1 per cent per year, to 360,000 tonnes. Interestingly, on a per capita basis, seafood consumption in Australia has actually declined marginally, from 15kg in 2006/07 to 14.5kg in 2016/17.

It is interesting to speculate why per capita fish consumption in Australia may be falling. This includes limited promotion compared to other meats, limited availability in Quick Service Restaurants, the fact that consumers are more likely to seek an Australian-sourced product, and the fact that other meats are easier to cook.

In terms of trade, Australia remains a net importer of fisheries products both in value and volume terms, largely comprising of finfish and prawns. Thailand is the biggest source of imports for Australia – it represent 27 per cent share of imports, followed by China (19 per cent), Vietnam (15 per cent) and New Zealand (12 per cent).

In terms of exports, China/HK and Vietnam are important trade partners for Australia, with an increasing share of total exports. Exports to China/HK continue to account for over 50 per cent of total exports, while Vietnam now accounts for 21 per cent, followed by Japan at 12 per cent in 2017–18.

AUSTRALIAN FISHERIES PRODUCTION



Source: ABARES

Most seafood exports to HK and Vietnam had ultimately been destined for China. With the signing of the China-Australia Free Trade Agreement (ChAFTA) seeing reduced tariffs on seafood products, this has subsequently seen a sharp rise in exports to China and a subsequent decline in exports to Vietnam.

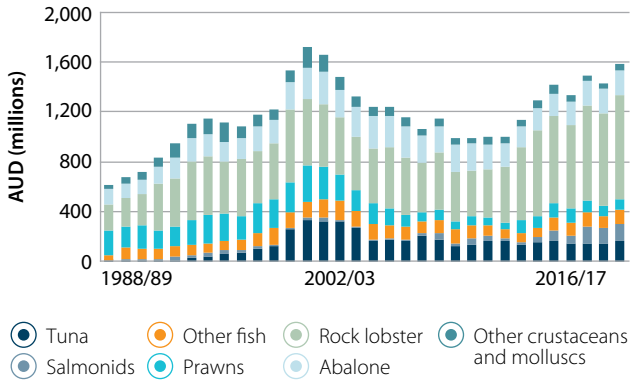
Globally, while China is currently a net exporter of seafood, it is also the world's third largest importer. On the back of depleted coastal waters and environmental pressures, China is likely to become a net importer of seafood in the 2020s.

One of the strongest opportunities the Chinese market provides for Australia is in the ongoing growth in imports of rock lobsters. The fluctuation in imports between official and unofficial channels provides an explanation for the staggering 94 per cent increase in direct imports of live rock lobsters in 2018 to US$912 million. For Australia, the fall in tariffs on rock lobster imports under the ChAFTA saw 2018 live rock lobster trade to China jump to US$466.

On the most recent UN figures, Australia is the world's fourth largest producer of lobsters. Canada and the US alone account for over half of all lobsters landed, while Australia accounts for around 5 per cent of the world's catch.

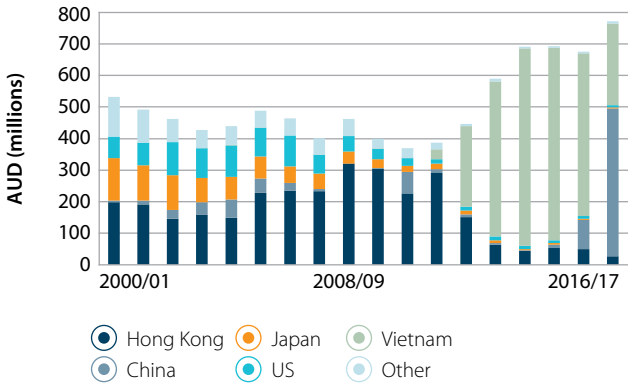
Rock lobsters are sourced from a number of states, with Western Australia providing the greatest share, and with the state actively seeking to grow the rock lobster industry, both in terms of exports and domestic consumption. Earlier this year, after lengthy debate between government and industry, both parties agreed to increase the annual catch by 315 tonnes, rather than the 1,700 tonnes originally proposed by the government, of which it would have held 1,385 tonnes. The majority of the new catch would be allocated for local consumption, rather than for export, the destination for 98 per cent of WA's lobster catch.

AUSTRALIAN FISHERIES EXPORT VALUE BY SPECIES



Source: ABARES

AUSTRALIA ROCK LOBSTER EXPORT VALUE BY DESTINATION



Source: ABARES

ANZ ECONOMIC UPDATE

FOREIGN EXCHANGE

The last few months have been volatile for rates markets as sentiment surrounding the China-US trade conflict continued to swing around. Our central case now is for the Fed to hold rates and observe the impact of three consecutive rate cuts. This means we think most of the rally in the front-end is done and as the US economy holds up, the UST curve will start to steepen mid to late next year. With the Australian economy expected to pick up next year, combined with the anticipated steepening in US rates, we think the ACGB curve will also steepen late next year but not to the same degree. However, we don't think the RBA is done easing and expect them to cut the cash rate twice more, taking the cash rate down to 0.25 per cent by May next year. In our view these additional cuts will be necessary to make further inroads in reducing spare capacity in the labour market and driving the unemployment rate lower.

THE LAST FEW MONTHS HAVE BEEN VOLATILE FOR RATES MARKETS AS SENTIMENT SURROUNDING THE CHINA-US TRADE CONFLICT CONTINUED TO SWING AROUND

FX AND CENTRAL BANK POLICY RATE FORECASTS

FX Forecasts	Current	Dec '19	Mar '20	Jun '20	Sep '20	Dec '20	Mar '21	Jun '21
AUD/USD	0.69	0.67	0.65	0.66	0.68	0.69	0.70	0.70
NZD/USD	0.64	0.62	0.59	0.61	0.61	0.63	0.63	0.63
AUD/NZD	1.08	1.08	1.10	1.08	1.11	1.10	1.11	1.08
USD/JPY	109	108	105	105	105	105	105	105
EUR/USD	1.11	1.10	1.06	1.05	1.05	1.08	1.10	1.10
USD/CNY	7.03	7.2	7.24	7.28	7.32	7.35	7.35	7.35

Rate Forecast	Current	Dec '19	Mar '20	Jun '20	Sep '20	Dec '20	Mar '21	Jun '21
RBA cash rate	0.75	0.75	0.5	0.25	0.25	0.25	0.25	0.25
Feds fund rate	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75
RBNZ OCR	1.00	0.75	0.5	0.25	0.25	0.25	0.25	0.25

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