



ANZ AGRI  
**INFOCUS**

APRIL  
2021

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# COMMODITY INSIGHTS

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# FOREWORD

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With 2021 now around a third of the way through, the Australian agri sector has emerged from the disruption of COVID-19 in excellent shape.

Obviously, this is partly due to a good season and an agri cycle which have resulted in both high production levels and prices for most soft commodities. However, the industry's relative strength is also due to the way that Australia's agri and food supply chains managed to adapt quickly and pragmatically through the COVID-19 disruption.

Looking ahead, the Australian agri sector currently faces a new kind of challenge – one which is arguably good, but still vital to the growth and sustainability of many agribusinesses.

Farmers across all major agri sectors need to carefully evaluate their medium- to long-term business strategies. Investors outside of agri might consider three, five or 10 years as long horizons, and in this sense there is some comfort to be gained from short- and medium-term economic forecasts. But when you invest for a generation and beyond, it's critical to have a view of where you are in a cycle at any point in time. If, for example, you believe the industry is near the peak of a cycle, not just in terms of prices and production, but in terms of favourable interest rates, it might indicate whether growth or consolidation is the imperative.

As the latest ABARES outlook reinforces, most agri commodities are likely to see a gradual decline in price over the coming years, as they return to more 'normal' levels – in the years heading out to 2025/26, prices for most agri commodities are forecast to soften by between 5 per cent and 30 per cent.


In particular, assuming a return to average seasonal conditions, the decline in wheat yields and acreage from the coming year is forecast to see Australian wheat production levels fall by around one-third over the next five years. Based on this outlook, and with their experience of volatile seasons, grain producers will need to think carefully about their strategies in everything from grain storage to planting to equipment purchasing. And all farmers will continue to balance their own strategies of building wealth through capital gains and profits driven by operating margins, an issue especially top of mind given the recent and current strength of the rural property market. Good farmers are long-term investors, so maximise their long-term agri memories and experience.

Times are definitely good and will continue to be good for many. The best agri businesses will be those that take opportunities appropriate for them and their business model while carrying a healthy degree of caution, realism – and an escape plan – for when something goes wrong.



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## WHEAT & GRAIN INSIGHTS



### OVERVIEW

- + Forecasts of strong global production have been outstripped by forecast consumption growth on the back of feed grain demand in China
- + A record Australian wheat crop combined with good soil moisture has put crop producers in a very strong position.
- + The Russian government's export tax has restricted global grain availability putting upward pressure on prices
- + Strong prices for feed barley, corn and other feed grains was pushed higher by USDA plantings survey
- Futures prices have begun to moderate as medium-term forecasts are for global production to outstrip consumption growth
- The recent blockage of the Suez Canal saw freight costs jump, the impacts of which could take many months to clear
- Price support as a result of Russian export taxes is uncertain as the medium-term imposition of taxes by the Russian Government remains unclear
- Ending stocks of wheat continue to sit at very high levels, despite a slight moderation in 2020/21

The Australian wheat crop is set to come in at record levels and international events coalesce to maintain solid prices both in the international and domestic markets, Australian producers are in the midst of some of the best conditions in recent memory. Despite the spike in freight rates for Australian exporters due to the blockage in the Suez Canal provide, Australian wheat is globally competitive. While the short-term prospects for Australian croppers remain exceptionally strong on the basis of both volume and price, the outlook for the medium-term is slightly more moderate.

As both international and Australian futures slide and export prices moderate from early March highs, the Australian Bureau of Agricultural and Resource Economics (ABARES) has forecast wheat prices to drop on the back of strong global production.

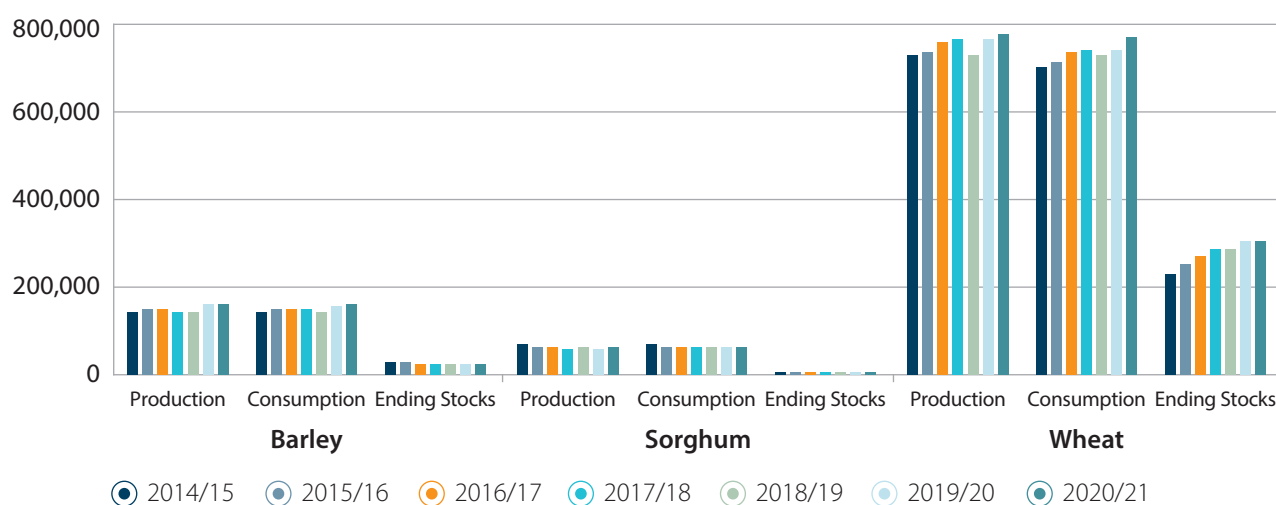
### GLOBAL CONSUMPTION GROWTH TO OUTSTRIP PRODUCTION IN THE SHORT TERM

United States Department of Agriculture (USDA) estimates are for a strong showing in both global wheat production and consumption for 2020/21 with global production increasing 1.7 per cent, based on strong production growth in Russia, Australia and Canada offsetting a decline in the European Union. To offset production growth, consumption is forecast to increase by 3.9 per cent, driven primarily by strong feed wheat demand in China and India.

Demand is also driven by countries such as Egypt and Indonesia seeking to build supplies of milling wheat as COVID-19 lockdowns continue. As a result, wheat ending stocks are forecast to rise only very slightly by 0.3 per cent. Given recent years' sharp growth in stocks, being driven by China, the slight moderation in stocks-to-use should be some support for prices.

Global growth in production of barley at 2.9 per cent is forecast to outstrip growth in demand of 1.8 per cent resulting in a smaller increase in stocks of 1.6 per cent – however with production expected to still remain ahead of consumption, most in the industry are anticipating a drop in the price through the year.

## WHEAT STOCKS REMAIN HISTORICALLY HIGH



Source: USDA

While international barley prices are anticipated to fall, a reduction in domestic production is also expected to help drive domestic prices higher.

The imposition of new tariffs on Australia by China last year was feared to have a significant impact on Australian exports, however, it has resulted in Australian barley becoming more competitive in alternative markets, and malting grade barley entering new markets such as Mexico.

Much of the outlook for Australian feed barley is also closely connected with the global price of corn and soybean, which are currently sitting at exceptionally strong levels, although slightly off early March highs. There has been increasing demand for feed grain from China as they rebuild their domestic pig herd, although this is likely to be offset by lower demand for corn as a biofuel due to higher corn prices. While ABARES is predicting a global drop in both corn and barley prices, this has been placed under a question mark by the most recent USDA plantings survey.

The latest USDA update came complete with a survey of US planting intentions which showed a strong increase in wheat planting intentions, but a drop in soybean and corn plantings in the US despite consistently high prices for both. The report's release threw futures markets into some disarray, forcing both soybean and corn prices even higher while taking the shine off wheat futures. This report has been met with some scepticism however, with many awaiting the second survey in June.

## RUSSIA MOVES TO KEEP A LID ON DOMESTIC FOOD PRICE INFLATION

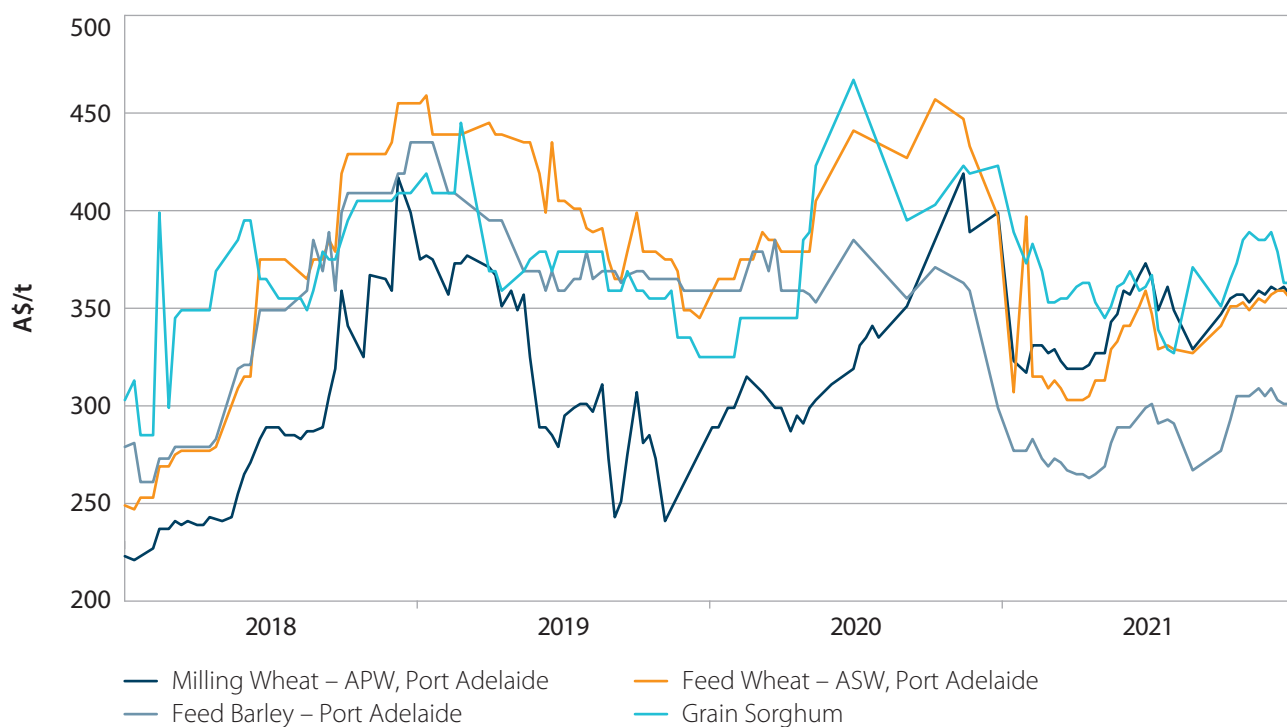
The Russian Government's announcement of an export tax of 25 euros per tonne, commencing in mid-February, was announced as a policy directed towards limiting food price inflation in the domestic Russian market.

This announcement was made despite forecasts of a record Russian wheat crop and is set to continue at 50 euros per tonne until June 30. The Russian export tax is not limited to wheat either, with barley and corn exports also being taxed. As one of the world's largest wheat exporters, the export tax is likely to not only redirect export demand to lower cost exporters but also restrict total grain availability on the global market. To date, this has provided strong support for global prices, although ongoing uncertainty about any future moves by the Russian Government may mean price support is relatively short-lived.

## IMPACTS FROM THE SUEZ CANAL BLOCKAGE MAY TAKE MONTHS TO CLEAR

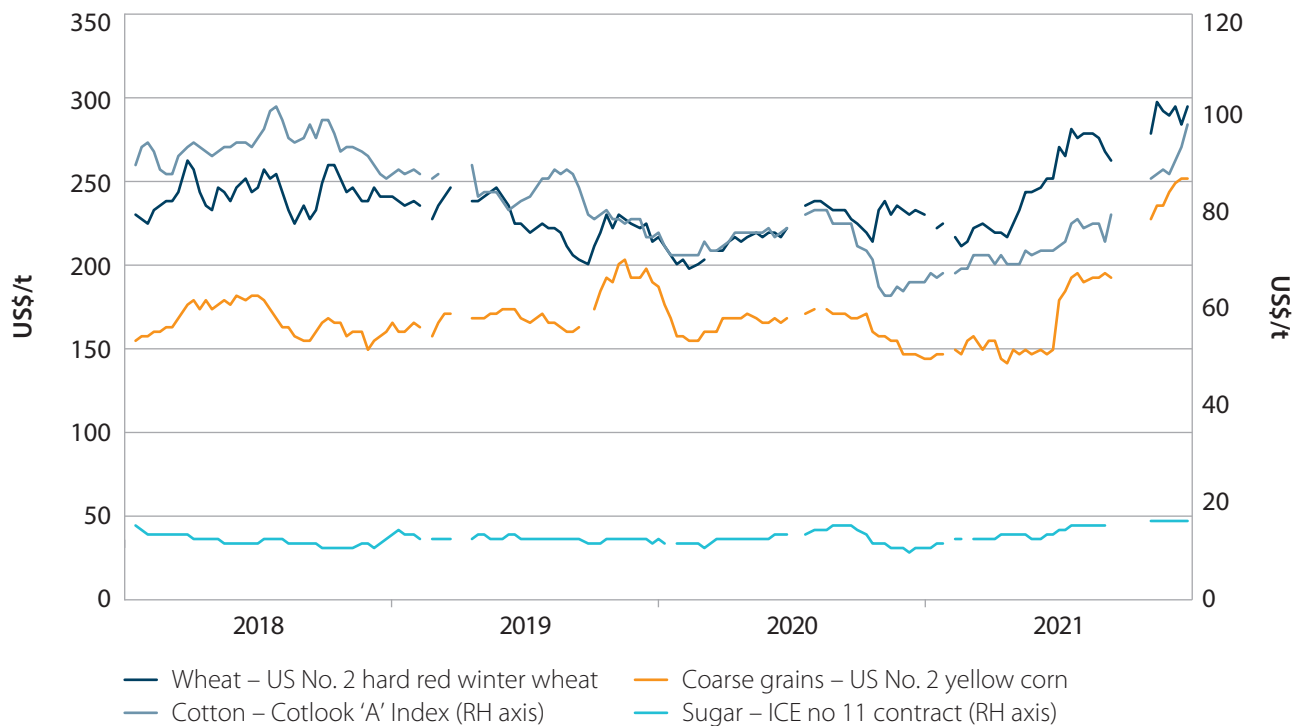
The recent blockage of the Suez Canal is likely to have some flow-on effects, as the delayed ships, including 60 dry-bulk container ships, are cleared. While officials said that the backlog of vessels waiting to transit the Suez Canal were cleared in a matter of days, the longer-term impact for global trade will be felt for weeks, or even months. The Suez blockage saw grains freight rates jump across the globe before moderating in early April, however, it also appears to have had the longer-term impact on Australian freight rates, which increased more substantially than other exporters – and for now, have yet to return to normal.

## AUSTRALIAN GRAIN PRICES REMAIN STRONG, BUT DOWN SLIGHTLY ON DROUGHT YEAR PRICES



Source: ABARES, ANZ

## INTERNATIONAL GRAINS PRICES ARE AT VERY STRONG LEVELS



Source: ABARES, ANZ





## BEEF INSIGHTS



### OVERVIEW

- + Recovery in global beef consumption in 2021 to support growth in trade volumes. Fall in global demand was not as big as anticipated
- + Australian cattle herd on path of recovery after years of liquidation
- + Demand for Australian beef to remain strong in international markets despite tight supplies and high cattle prices
- Domestic processors face tough conditions with high input prices, which may stay at elevated levels throughout 2021
- Australian retail consumers may see high prices through 2021 due to tight domestic supplies
- Strong South American beef production and exports to increase competition in price-sensitive Asian markets

In some ways, the current trajectory of the Australian beef industry could be compared to the running of an Olympic marathon. Right at the start of the event, the initial burst away from the line captures the attention, with a blistering pace to get things underway. But before too long, the early surge soon becomes a long, steady slog, with the finish line a long way ahead, and the knowledge that different dips and rises are going to present interesting challenges to the participants along the way.

While an Olympic marathon usually takes just over two hours, the Australian cattle industry is now around 16 months into its current race. Arguably, the starter's gun went off at the start of 2020, when Australian cattle prices began the rise which they continue to see today. While the preceding two years had been an extremely tough one for many cattle producers having to manage through drought conditions, overall cattle prices had been relatively flat over that period.

The benchmark Eastern Young Cattle Indicator (EYCI) had largely moved with a band of around 450–550 c/kg, as farmers continued to unload a steady stream of cattle onto the market, as lack of feed necessitated ongoing herd reductions.

As all beef supply chain stakeholders are well aware, the EYCI has risen by around 70 per cent since the start of 2020, climbing from the low 500s c/kg to finally breaking through the once unheard of 900 c/kg. However, in terms of price volatility, apart from reasonable price surges at the start of 2020 and 2021, overall monthly price volatility has been reasonably consistent with historical trends.

### SELLERS' MARKET WITH DEMAND FOR CATTLE AT A HIGH

Undoubtedly, the record prices for cattle have meant great news for those in a position to be selling. Cattle producers in the right place at the right time will have managed their calving, their pastures, their feed usage and other inputs, to be in a position where they are gaining a windfall rarely seen in the sector, and one which is well deserved.

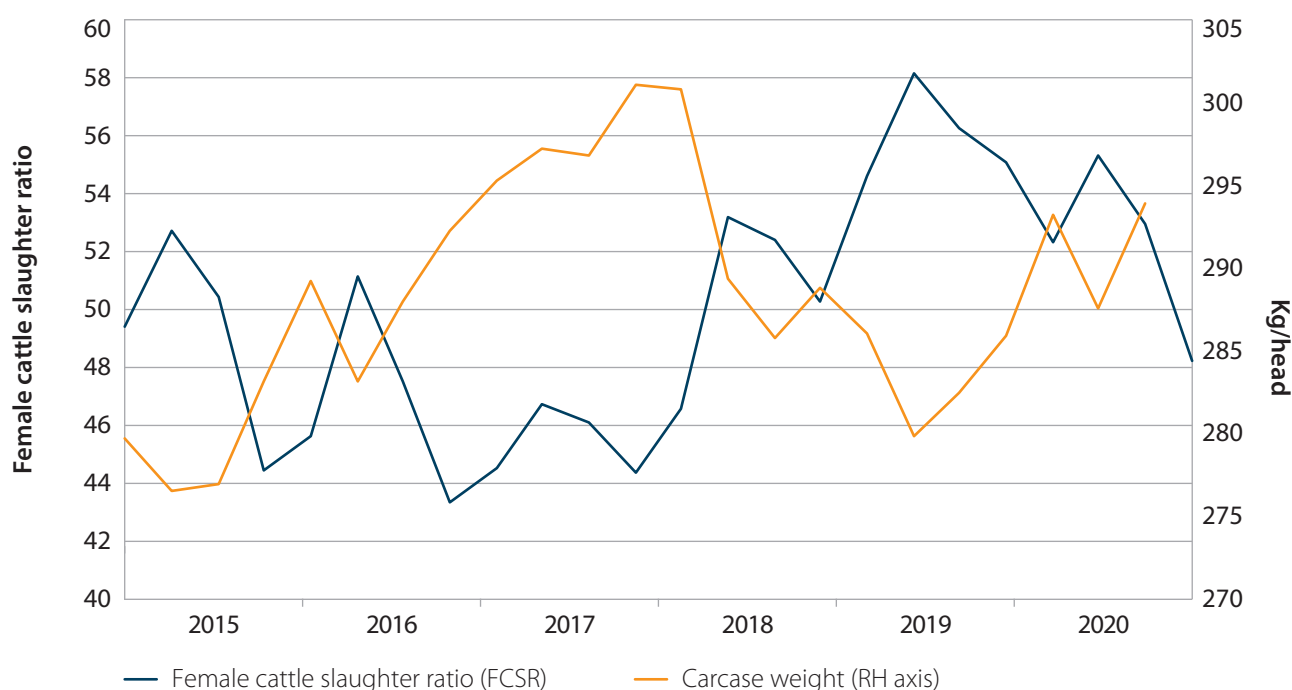
Month on month change in c/kg of EYCI

— Eastern Young Cattle Indicator (EYCI)

Year	Month on month change in c/kg of EYCI (Approximate)
2015	-20, 18, 35, 15, 45, 20, -40, 38, 5, 5, -10, -30, 10, 50, 45, 10, -40, -15, 10, -10, -35
2016	-30, 10, 50, 45, 10, 5, 5, -10, -30, 10, 50, 45, 10, -40, -15, 10, -10, -35
2017	-40, -10, 10, -15, -10, -45, -40, -10, 38, -10, -10, -45, -40, -10, 20, 30, -10, -25, -10, -40, -45
2018	-10, 20, 30, -10, -25, -10, 20, -40, -30, 20, -40, -30, 20, 10, 10, -40, -30, 20, 10, 10, -40, -30
2019	-30, -20, 10, 58, -10, 10, 28, 10, 10, -40, -25, -30, 58, -10, 10, 28, 10, 10, -40, -25, -30
2020	-20, 15, 15, -20, 135, 60, 20, -25, 20, 28, 10, 10, 15, 15, -20, 135, 60, 20, -25
2021	20, 28, -5, 18, 25, 25, -30, 70, 10, 10, -10



## CARCASE WEIGHT CONTINUE TO RISE WITH FEMALE CATTLE HERD RETENTION



Source: MLA, ANZ

The improved pasture conditions are also likely to see relatively slower growth than normal in the numbers of cattle on feed. While numbers have remained over 1 million since 2018, a 15 per cent fall in feedlot numbers in the last quarter of 2020, at a time which would normally see a rise, would potentially signal that feedlot growth in 2021 may remain slow.

### DEMAND FOR AUSTRALIAN BEEF ON THE EXPORT MARKET REMAINS HIGH

In terms of beef exports, the tight squeeze on domestic supply has continued to ripple through to export numbers. The fall in beef exports in 2020 of around 15 per cent can largely be attributed to Chinese imports declining from the 2019 record shipments, as demand created by the pork deficit from African Swine Fever (ASF) declined. In addition, the lockdown disruptions to the US domestic food service sector also saw that market fall by around 15 per cent last year, although the gradual recovery in that sector may stimulate greater import demand for Australian beef.

Overall Australian beef exports may see a marginal rise of around 2 per cent over the course of 2021, as domestic supplies remain tight. Exports to Japan and South Korea are likely to remain stable at current levels as their food service sectors recover.

China will potentially remain the most price sensitive market, with rising South American supply providing increasing competition on a price basis. For the US, recovering domestic beef supplies, high cattle prices in Australia, and currency movements will be the key factors driving Australian exports to that market.

Globally, overall beef production is forecast to remain relatively flat in 2021, at around 61 million tonnes, with slight increases forecast in Brazil and India. These two increases, as well as a lift in the US domestic herd, should see global export growth return to a level slightly below that of the 2019 'normal' trading year – after the disrupted 2020 – to around 10.8 million tonnes.

In terms of imports, China looks set to continue as the world's largest importer, rising almost 3 per cent from 2020 to just under 3 million tonnes. While the gradual recovery in China's pork sector from ASF may slightly reduce beef demand, this will be countered by an increase in beef demand from the food service sector, as the recovering economy sees Chinese consumers increasingly eating beef away from their homes.



## SHEEP INSIGHTS



### OVERVIEW

- + Favourable weather conditions and feed availability support flock rebuild through 2021
- + Global demand for Australian sheepmeat produce remains strong despite COVID-19 disruption
- + Australian exports to be stable in 2021, particularly to US, with tight domestic supplies
- Exports to Middle East markets may fall in the short term due to COVID-19-led economic impact on these economies
- Divergence between east coast and west coast sheep sectors will create regional imbalances
- High sheep prices could eventually flow through retail channels and could deter domestic consumption

If the Australian sheep industry was a football team, then the pundits may be well describing them not only as being at a good point of a rebuilding cycle but on the verge of a potentially strong era. In particular, if the most recent ABARES quarterly forecasts are to be believed, the growth prospects for the Australian sheep flock over the next five years are stronger than any of the other of Australia's main agricultural sectors.

Australia's sheep producers are heading toward the winter months in a strong position on a number of fronts. Prices remain strong across most categories, seasonal conditions continue to be favourable and while exports may be challenging, their fundamentals in the medium to longer term provide cause for optimism.

In terms of prices, different categories have been impacted by a range of factors, although nothing which has created too many surprises. After having seen record high prices in the first half of 2020 followed by a period of correction in the second half of the year, 2021 has so far seen trade lamb prices strengthen, sitting largely just over 800 c/kg for the past three months.

### CONCERNS OF LONGER-TERM FEED LEVELS SEES MORE LAMBS ON THE MARKET

Yet while the relatively wet summer meant many farmers had held sheep back from the saleyards to restock on ample feed, the warmer weather in late March and early April appears to have had the opposite effect. With farmers concerned that feed quality may not remain as strong as it has been, and faced with the prospect of buying in feed to maintain their high stocking levels, many producers took the opportunity to sell lambs in their current good condition while the market remained strong. As a result, prices eased off over recent weeks.

Looking ahead, there is every likelihood that the supply of lambs on the market may remain stronger than it has been in the earlier part of the year, with the potential to limit the likelihood of prices rising strongly again for some time.

On top of this, the good growing season through 2020 resulted in not just an increase in the number of ewes, but in an overall enhanced sheep condition, which is likely to see increased lambing percentages across most sheep-producing regions this year.

Given these factors, the tight supply of sheep into the saleyards seen earlier this year may not be seen again for some time.

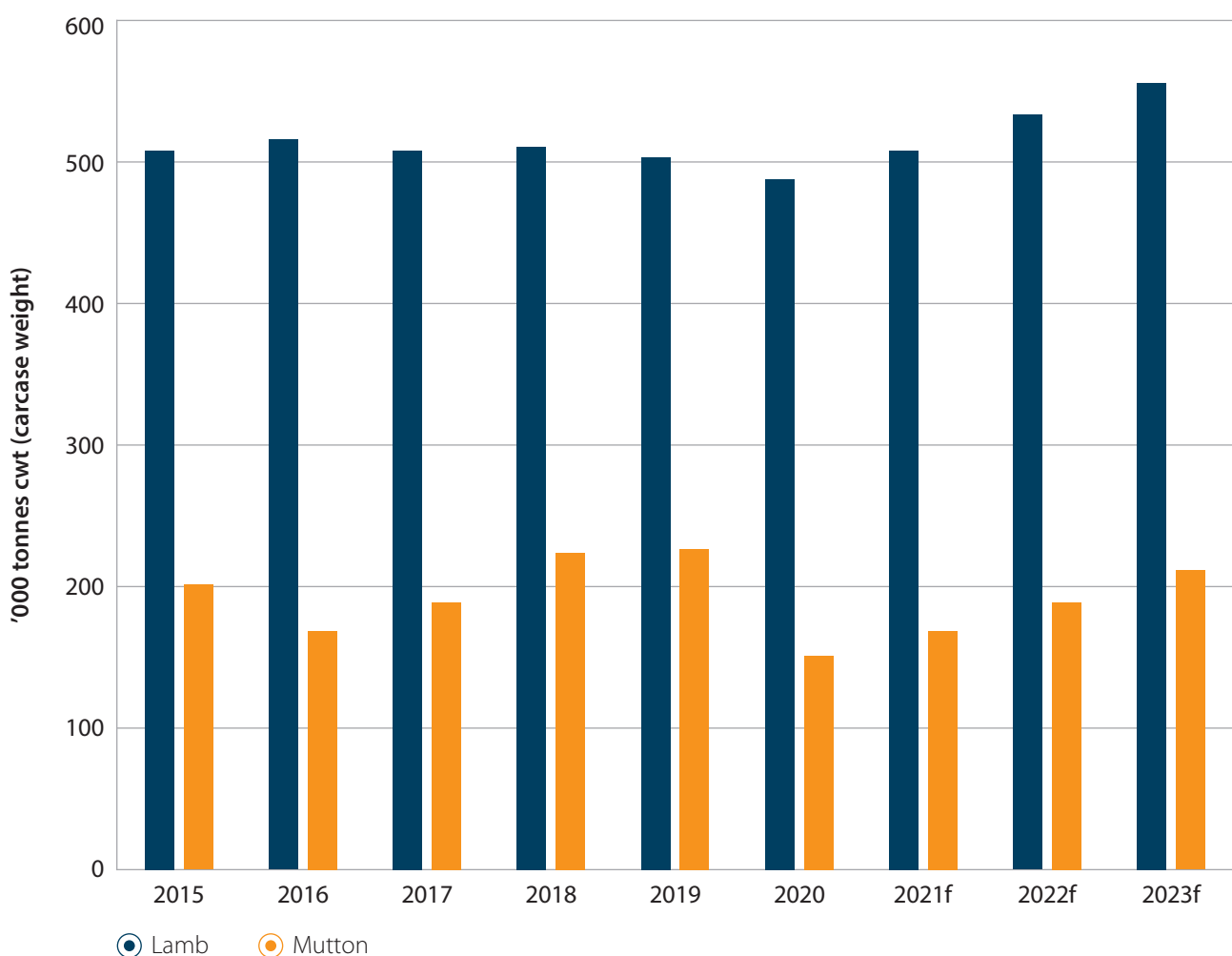
Notably, the market results would also indicate that while many producers are selling increased numbers of stock, they are also continuing to strategically rebuild their flocks, with an eye on the longer term. This is particularly illustrated by the growing gap between trade lamb and restocker lamb prices.

In terms of the price differential, restocker lambs have now traded the highest premiums to trade lambs in years – an indication of ongoing confidence in the market by producers.

Importantly, one exception to this trend has been in Western Australia where poor weather conditions have seen producers seeking offload stock at a far greater rate than in the east.

The ongoing rebuilding process has also been a major factor in the decline in mutton production. As many farmers chose to retain their old ewes in 2020 to help rebuild their flocks, the gap in the market saw mutton production fall by 33 per cent year-on-year to around 152,000 tonnes. In contrast, lamb production stayed relatively flat, falling by less than 3 per cent in 2020, to just under 490,000 tonnes.

#### MONTHLY VOLATILITY OF THE EASTERN YOUNG CATTLE INDICATOR 2015-2021



Source: MLA



Looking ahead, and assuming that conditions remain complementary to production, supply may well remain relatively tight until at least 2022, particularly in comparison with saleyard supplies over the past five years, as producers continue their flock rebuilding process.

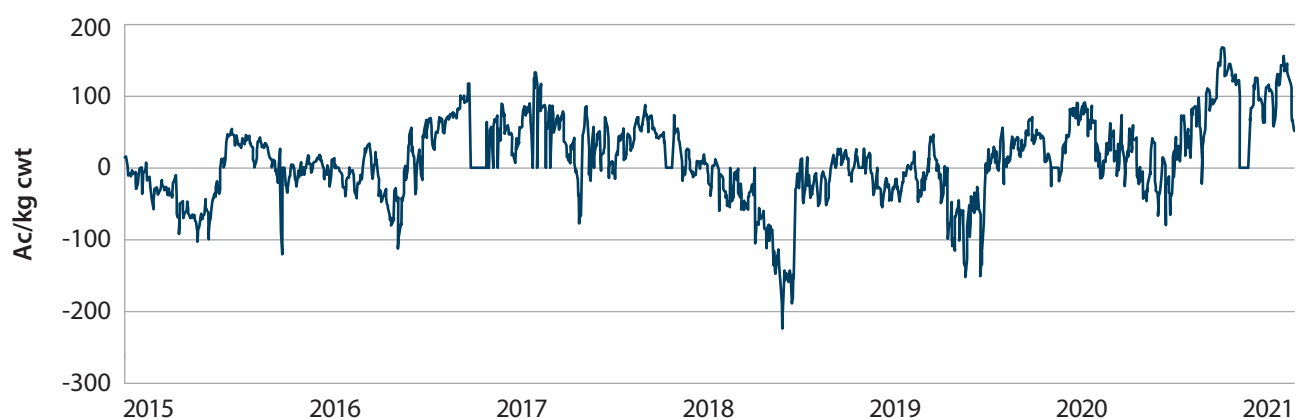
In terms of exports, the tight supply also saw both lamb and mutton numbers fall, though neither to alarming levels. While lamb exports fell by just over 6 per cent last year, it still remained the third-highest figure on record.

The one major growth market for Australian lamb was the US, where demand remained strong, particularly from retail channels, as well as from restaurants. In contrast, lamb exports fell in other major markets, especially China, as well as the Middle East, where the COVID-19 impact was particularly disruptive.

Looking ahead, while the combination of restocking and disrupted demand saw sheepmeat exports fall, a change in both of these factors may well provide a more promising outlook, particularly from the second half of 2021 onwards.

With more supply coming onto the market, a plateauing or correction in prices may see Australian lamb and mutton become more attractive to global buyers, at the same time as many economies are continuing to rebuild. In addition, the recent speculation that the impact of African Swine Fever has remained stronger than first thought may also keep Chinese demand at reasonable levels.

#### FLOCK RE-BUILD TO DRIVE RE-STOCKER LAMB PRICES THROUGH 2021



Source: Meat and Livestock Australia

#### RESTOCKER LAMBS TRADING AT HIGHEST PREMIUMS OVER TRADE LAMBS IN YEARS



Source: Meat and Livestock Australia

## WOOL INSIGHTS



### OVERVIEW

- + Domestic flock recovery to support wool production recovery in medium term through 2023–24
- + Wool prices stabilised with consistent offerings and improved demand from buyers
- + Favourable climate conditions to improve fleece weight despite fall in number of sheep shorn
- Shipping challenges may create short-term disruptions to buyers' finance and order booking
- Short to medium-term wool demand to be dependent on global economic conditions
- Wool has relatively low share of global textile market and alternative cheaper fibres continue to create demand uncertainties and price volatility

Winter may have been a time of discontent according to the quote by Shakespeare, but it can be an excellent time for a wool-exporting nation looking to keep millions of people warm in the cold Northern Hemisphere. And while the next Northern Hemisphere winter won't be rolling around until the end of this year, the world's woollen mills and clothing manufacturers will already be doing their sums on the volumes of wool required to provide for that time when it comes.

Australian wool producers, as with every farmer to some degree, are impacted by two fundamental factors: The conditions impacting the production of their product and the circumstances surrounding the sale of it, and the price they receive. While a reasonable amount of the former is within their control, apart from the obvious factor of the weather, most of the sale is up to many circumstances beyond their control, mostly well away from Australia.

The first quarter of 2021 has largely seen wool price indicators climbing back to a level last seen a year ago, before prices fell around 50 per cent between January–September 2020. With the benchmark Eastern Market Indicator having hit a low of around 850 cents last September, prices have now risen solidly again, to reach around 1,300 Ac/kg in April 2021.

While some agri sectors would look at similar price movements as part of an annual cycle, the wool price movements are being driven by other fundamentals. Undeniably, the momentum of buyers will increase, as mills and manufacturers look to provide for growing demand as COVID-19 restrictions ease. While some large European markets for woollen garments, such as France and Italy, are clearly continuing to feel the impact of COVID-19 lockdowns, the suppliers need to look longer term, hypothetically to a time when national vaccination programs have reinvigorated economies and consumer behaviour, and start planning their supply chain processes accordingly.

For some wool exporters, the challenge of accessing available shipping freight space has continued to create issues, which may impact the market in coming months. If importers, not just in China, but in markets such as Europe and India, become increasingly uncertain that their wool purchases will reach them, it may cause some softening in the market until greater certainty of delivery is achieved.

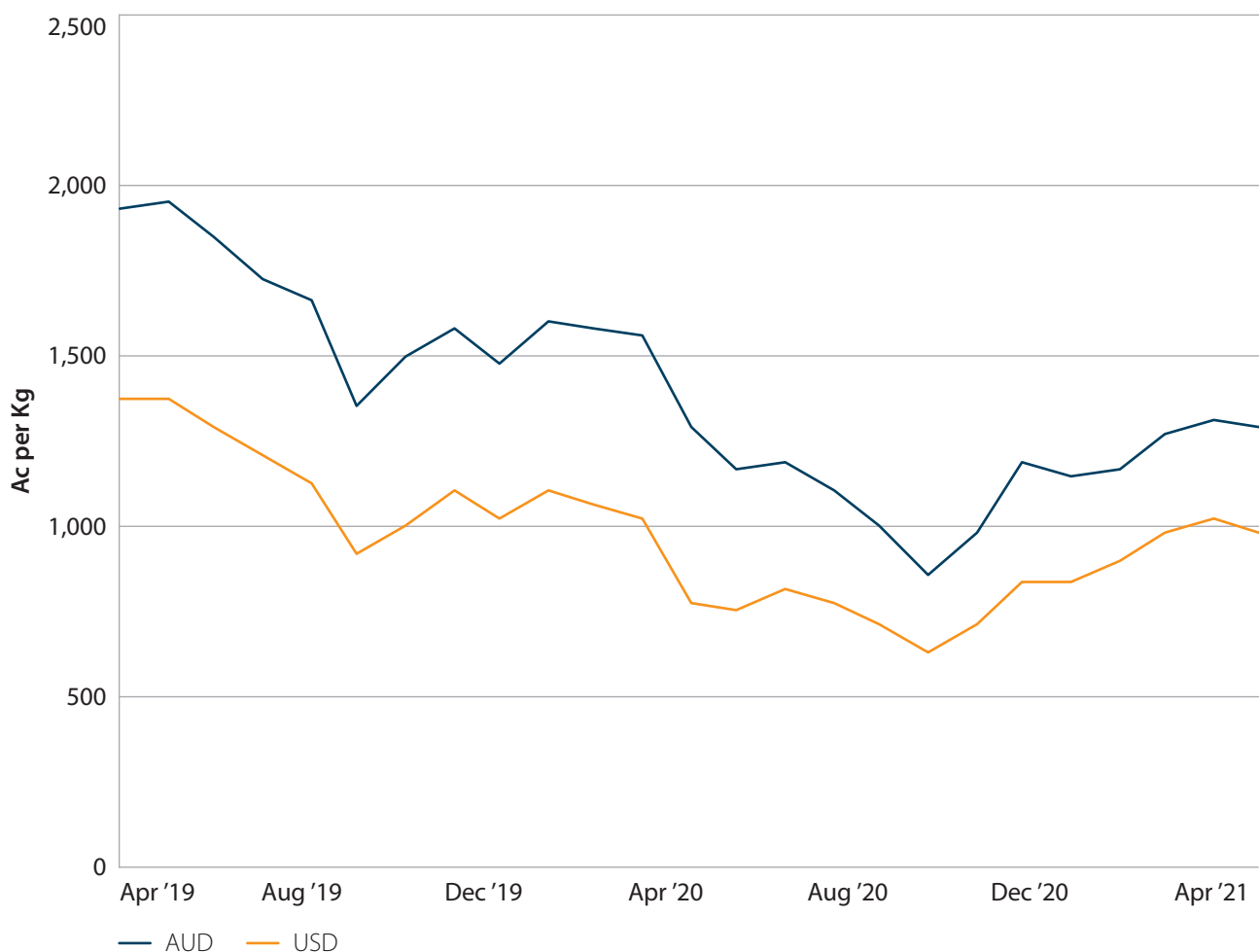
One concern which may impact the market are the continuing challenges with shipping, which have affected a wide range of Australian imports and exports.

#### ON FARM STOCK LEVELS MAY INCREASE

Importantly, it has also been noted by market observers that the recent high wool auction prices have also been partly maintained by many growers withdrawing their supply from sale. This could be driven by a range of factors, including the hope by producers that prices will continue to rise.

In addition, many producers will be running mixed farming operations and may find themselves in such a good financial position from the sale of their sheep and cattle this year that they can afford to hold onto their wool clip for longer than normal.

#### WOOL PRICES TO FIND SUPPORT WITH GLOBAL ECONOMIC RECOVERY



Source: AWI

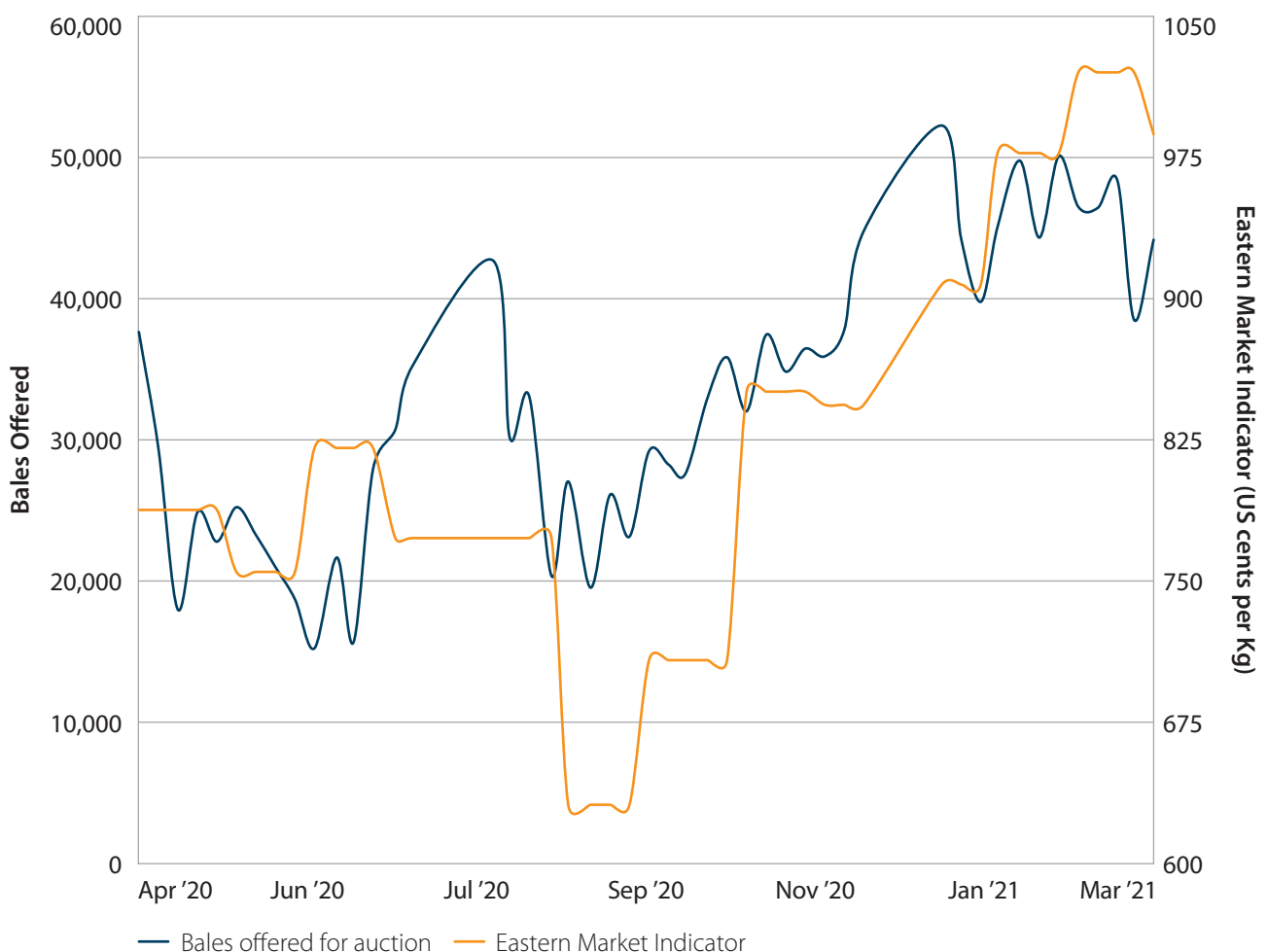


Looking ahead, the current ABARES forecast is that prices are likely to plateau at around the 1,300 AC/kg level. While the likely increase in demand from buyers will serve to push prices up, the uncertainty around freight, combined with the possibility of wool being stored on farm coming back onto the market could, at the same time, provide a dampener to any strong upward price movement.

In the medium term, the overall supply of Australian wool onto the market is forecast to grow for at least the next five years. In a further sign of the positive impacts of the ongoing relatively good season, the Australian wool clip is forecast to climb by a marginal 1.7 per cent in 2020/21 to 288,000 tonnes, despite a 5 per cent fall in the number of sheep shorn. This reflects the positive impacts of the good season on sheep condition and wool yields.

As the overall levels of wool production grow, with a forecast rise in overall production of over 20 per cent by 2025/26, concerns may arise that this could lead to a build-up of supply in the system, increasing domestic stockpiles to the levels where they could cause a structural correction in the market, where falling prices cause many producers to move away from wool sheep. Optimistically, however, the current forecasts also indicate that wool exports are likely to continue to grow at the same strong rate as production, limiting the levels of end stocks.

#### FALL IN BALES OFFERED AT AUCTION LED TO SHARP RISE IN PRICES



Source: AWI, ANZ



## COTTON INSIGHTS



### OVERVIEW

- + The start to 2021 has been exceptionally strong for the Australian cotton industry on the basis of both prices and volume, although prices have come down in recent weeks
- + Rain events across much of the eastern seaboard have boosted dam storages, carryovers and soil moisture, raising the prospect of an even bigger crop next year
- + Low global production has come at the same time as a rebound in consumption following COVID-19 lockdowns, leading to very strong prices
- The hangover from the COVID-related drop in global economic growth remains, however, with stocks still remaining markedly higher than two years ago
- The prospect of a ‘third wave’ of lockdowns in Europe is also adding a note of caution of currently strong prices
- Trade tensions between China and the US, UK and Europe have some potential to distort cotton trade flows into the future.

While the Australian and global cotton industries have started the year in fine form, recent weeks have seen some shine come off both the domestic and global prices. The reasons range from tensions with China, the US crop and exports, and ongoing COVID-19 lockdowns in Europe. This is not to say that it has been anything but an exceptional start to the year for the domestic industry with the 2020/21 crop looking at hitting 2.4 million bales or higher and prices at above \$530 per bale. Behind that, a reduction in global production combined with increased water carryover in domestic production areas are also boding well for 2021/22. There are challenges on the horizon, however, as global economic growth is still recovering and remaining stocks from 2020 still needing to be used, weighing on the outlook.

Strong cotton prices have been supported by lower production, and rebounding consumption in 2020/21. Global cotton production in 2020/21 saw a fall of 6.5 per cent from the previous year to 114.1 million bales, across almost all producing nations except China and Australia.

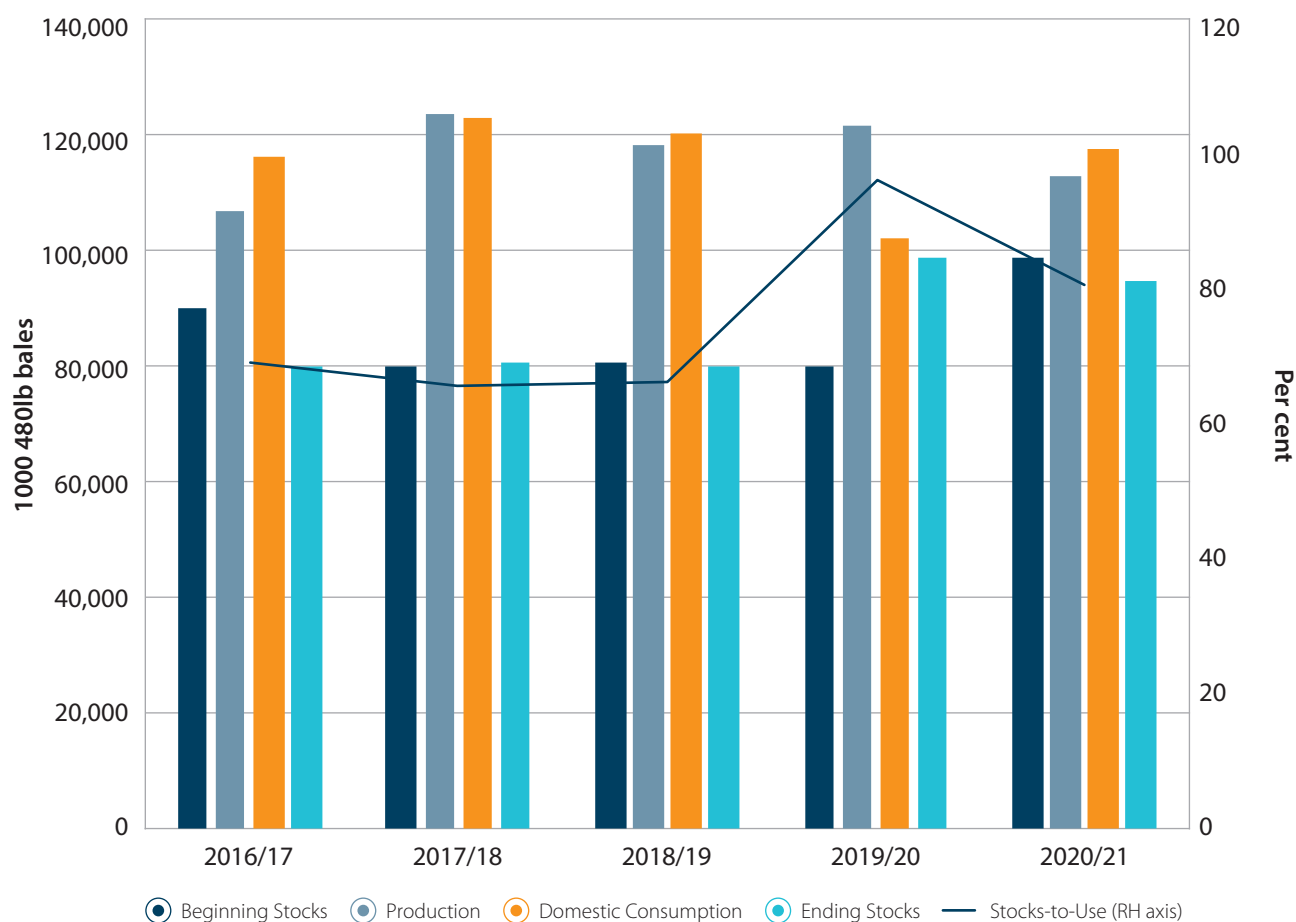
Production in the US fell almost 25 per cent with production in Texas falling strongly and Pakistan production fell to historic lows. Yields fell across many nations including Pakistan, India and Brazil.

### GLOBAL CONSUMPTION SET TO NORMALISE

Consumption is expected to grow more than 14 per cent to 117 million bales. This comes after consumption fell by over 15 per cent in the previous year, meaning that this year’s growth is a correction rather than the start of a trend. Consumption growth has been strongest in China and India which make up for over 75 per cent in consumption growth. Growth has also been strong in Pakistan and Turkey. The most recent *USDA Prospective Plantings Report* also shows a potential decrease in supply in 2021/22 of US cotton with planned cotton acreage just under 1 per cent from the 2020 acreage figure, to about 12 million acres despite strong prices.

Australian cotton production is forecast by ABARES to reach 2.4 million bales in 2020/21, however other industry sources are more optimistic, putting production at up to 2.8 million bales.

## GLOBAL COTTON CONSUMPTION TO NORMALISE



Source: USDA PSD, ANZ

While this is a massive recovery from the previous year, it is still significantly below the 10-year average according to ABARES. However, large rainfall events across the cotton-producing areas have increased dam storage levels and soil moisture and are likely to result in even further increases in production in 2021/22.

The hangover from COVID-19 shutdowns is still impacting global cotton prices and the global textile industry in general, with both processing throughput and final consumer demand impacted by lockdowns. While the global economy is recovering, albeit slowly, the slowdown in manufacturing has left a significant amount of stocks which still need to be processed. In 2019/20, the global cotton stocks jumped to a record high of 96 per cent – and while that will normalise slightly in 2020/21 returning to just over 80 per cent, there is still a long way to go before it returns to the 2018/19 levels of around 66 per cent.

Added to this, the possibility of a 'third wave' of lockdowns around Europe and the hangover from COVID-19 continues to impact cotton's outlook.

Relations between China and some western nations, including the US and EU, have re-emerged as some western clothing brands have raised concerns over allegations that members of the mostly Muslim Uighur minority group are being used as forced labour for garment manufacturing. As a result, sanctions were introduced by the EU, UK, US and Canada against China. China has now responded with its own sanctions on European officials and a number of western brands. While the trade tensions over Xinjiang cotton have yet to make a major impact of textile trade flows, they have highlighted ongoing concerns held by many brands over some Chinese textile exports.





## DAIRY INSIGHTS



### OVERVIEW

- + Global dairy prices continue with strong rises into 2021
- + Global consumption is currently keeping in line with strong global production, particularly in the US and EU
- + Major milk processors have announced increases in farmgate prices
- Dairy cattle herd rebound taking longer than expected with yields impacted
- Australia losing market share of export market with significant growth in US production
- Dairy producers continue to leave the industry with demand for land from beef and sheep producers driving up land prices

The last six months have provided ideal weather conditions for many of Australia's dairy farms. As a result, milk production grew strongly through spring and summer, resulting in high pasture growth and lower grain and hay prices. The improved conditions and cheaper feed resulted in producers focusing on rebuilding herd numbers. Recent floods in parts of NSW impacted some producer supply chains, however, this was fairly localised with limited broad impact on herds. La Niña is expected to come to an end with Winter and a return to neutral Southern Oscillation Index.

While some producers found new income streams in shipping dairy heifers in to China during the 2019 drought, this has driven up the price of cows. As a result of the higher demand for cows, producers are focusing on retaining calves and older cows. This is likely to result in a slight drop in yield due to the retention of older cows and first-time heifers producing less milk. The continuing trend of declining number of dairy farms has also slowed the rebuild.

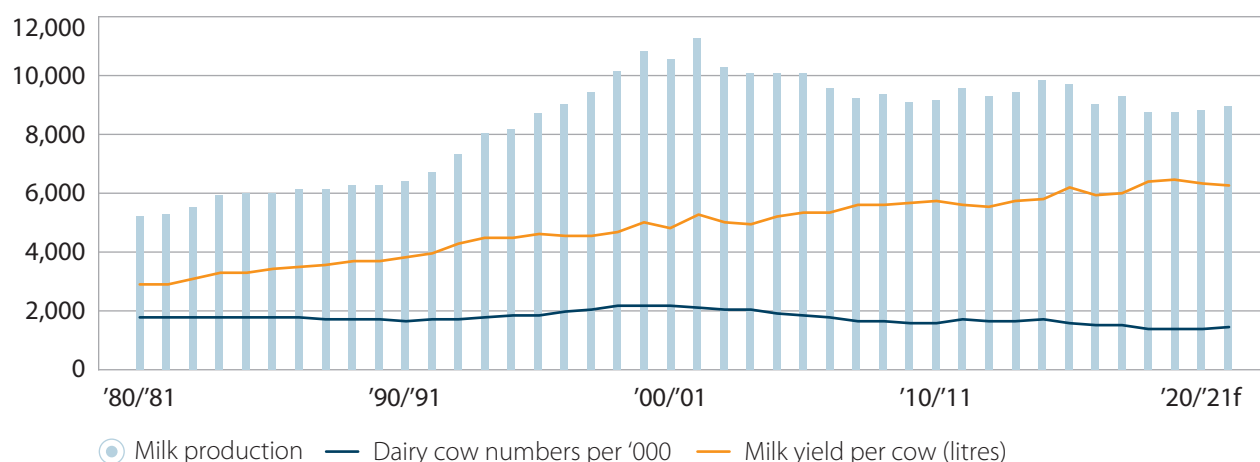
There are many drivers to the declining dairy farm numbers, however, recent limited access to international workers due to travel restrictions along with increasing demand for property from beef and sheep producers may increase the attractiveness of selling up.

### DEMAND STILL STRONG FOR AUSSIE MILK

Strong international demand is driving up Australian farmgate milk prices with ABARES expectations of a 2 per cent increase to 48.8 cents per litre. While butter, cheese and whole milk powder prices are forecast to remain relatively unchanged, the price of skim milk powder is expected to rise by 10 per cent.

Below average rainfall in New Zealand limited pasture growth at the start of the season, resulting in lower than expected milk production. The reduced supply from New Zealand and recovery from COVID-19 has seen China, Australia's largest export market for dairy products, increase demand for Australian dairy, specifically, butter. With the International Monetary Fund forecasting growth in the Chinese economy of 8.1 per cent in 2021 this is expected to support ongoing increases in import demand.

## THE LONG-TERM TREND OF INCREASING YIELD EXPECTED TO PLATEAU IN THE SHORT TERM



Source: ABARES, ANZ

On the whole, Australian exports of dairy products have declined fairly consistently, leading to shrinking global market share. This leads to the question of where Australia sits in terms of producing milk for the domestic market or the export market.

After five months of solid growth the Global Dairy Trade (GDT) Price Index dropped of 3.8 per cent in mid-March as a result of a 6.2 per cent drop in whole milk powder. This was on the back of a particularly high start to March which saw prices rise to US\$4,364 per tonne with the reference price dropping back down to around US\$4,000 per tonne at the start of April.

The strong GDT auction results have seen the major milk processors including Saputo Dairy, Bega Cheese, Burra Foods and Bulla Dairy Foods lift their forecast farmgate milk prices by around \$0.10 per kg this year. Fonterra Australia was the last to follow suit with announcements of farmgate price increases of \$0.13/kg of milk solids for the 2020/21 season.

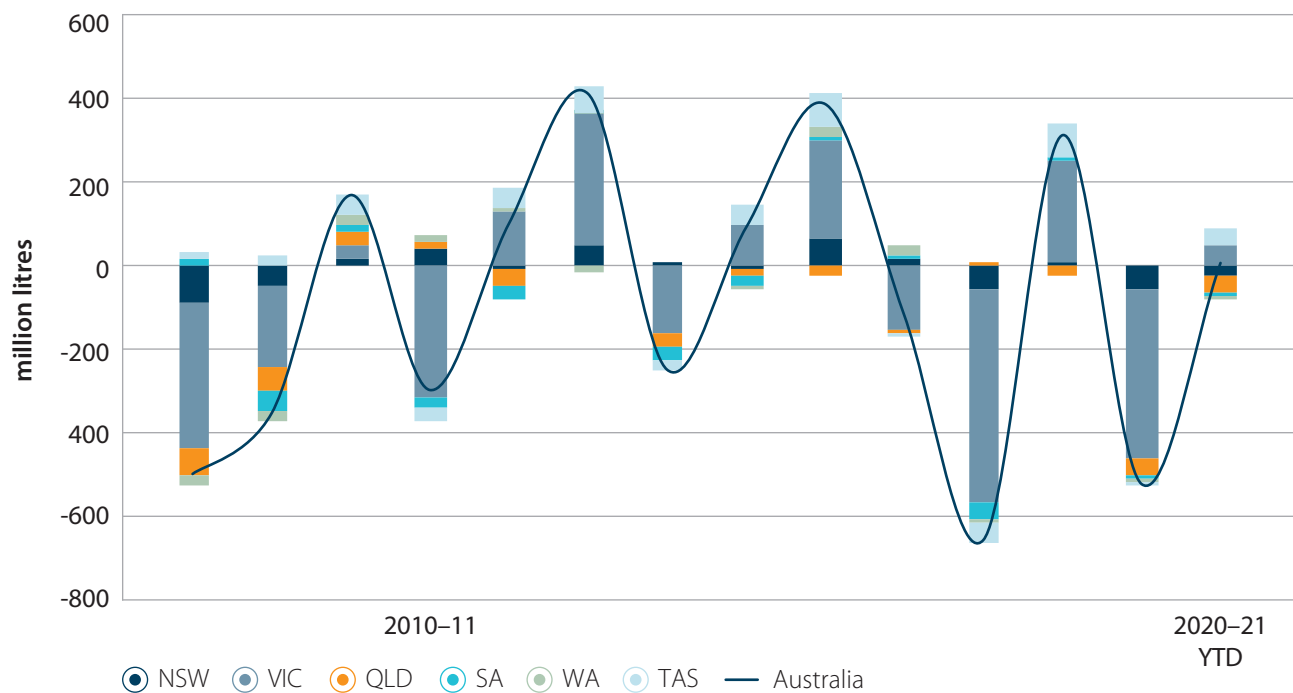
Domestic consumption of dairy products has changed over the years, with Australians drinking higher volumes of milk compared to other developed countries, although per capita, this has declined in recent years. This is driven by changing consumer lifestyle choices including the entry of milk alternatives. The return to post COVID-19 normal in Australia is seeing food service industries return to relatively normal and increasing restaurant and cafe dairy sales.

The trends post-COVID-19 of consumers seeking a connection to their food has seen new opportunities for producers and processors. Recently, Australian Competition and Consumer Commission authorised the 'Fair Go Dairy' label for Queensland brands who pay their farmers at least the agreed 'Sustainable and Fair Farmgate Price'.

In New Zealand, recent months have seen additional changes announced to the National Freshwater Regulations. The high levels of nitrogen run-off from intensive dairy farming practices has led to the regulator bringing in additional wintering requirements to those already brought in last year. The new regulations should allay concerns from Environmental groups that the run-off may cause algae blooms impacting fresh water sources as they flow through to the sea. While the issue of nitrogen-rich run-off is not an issue specific to New Zealand, the high rainfall, farm intensity and soil content is likely to increase the risk.

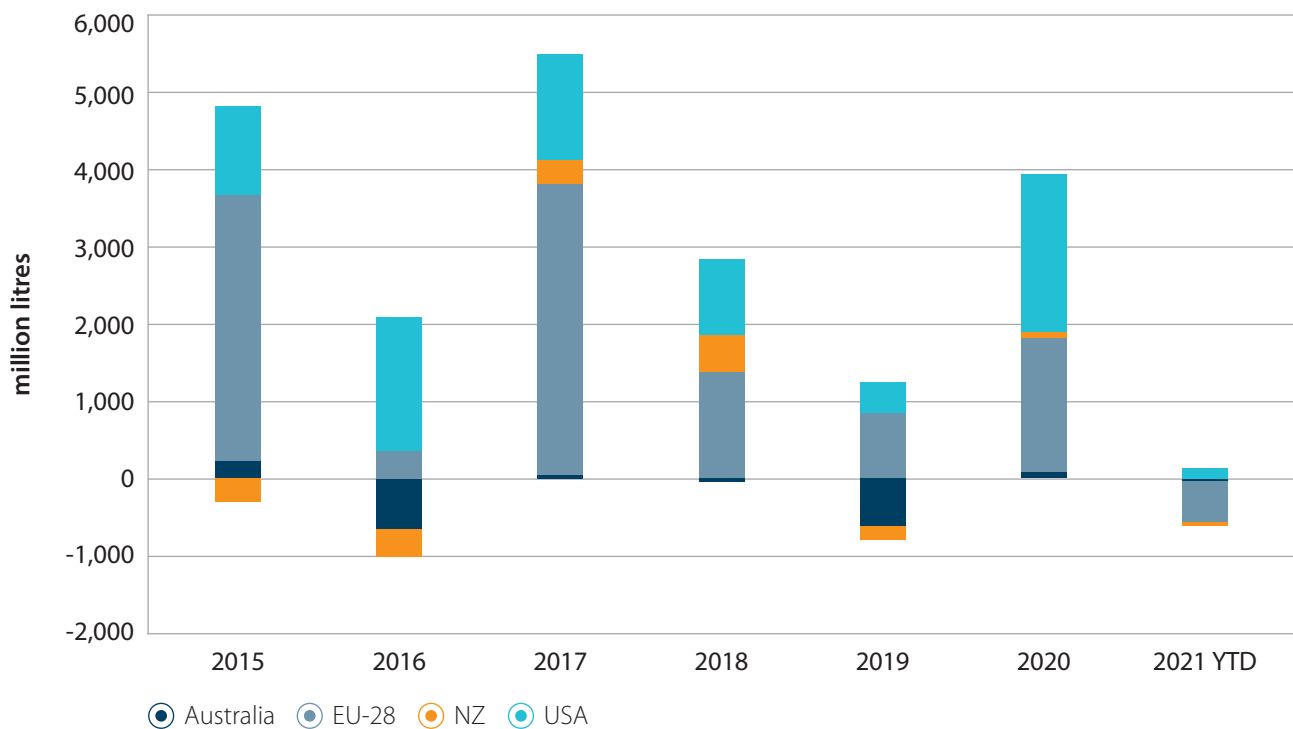
In March, Dairy Australia launched a Climate Change Strategy to support farmers in adapting to climate change. Dairy Australia modelling indicates there has been a loss of dairy farm business productivity of up to 0.9 per cent per year since 2000 as a result of climate change. The strategy includes research and development into Green House Gas (GHG) emissions and accelerating technologies being developed to reduce methane emissions. A survey completed by Dairy Australia in 2020 found that almost all farm respondents have implemented at least one practice that reduces GHG emissions reflecting the investment farmers are making toward on-farm sustainability measures.

## AUSTRALIAN PRODUCTION GROWTH DRIVEN BY VICTORIA AND TASMANIA



Source: Dairy Australia

## AUSTRALIA LOSING GLOBAL MARKET SHARE WITH EU-28 AND USA GROWING PRODUCTION



Source: USDEC





## CITRUS INSIGHTS



### OVERVIEW

- + The ongoing recovery from the drought will continue to lift production levels
- + Demand from China and Asia for nutritious quality fruit set to continue to grow
- + New Zealand travel bubble may help provide much-needed workers
- Labour shortages continue to be a concern with border restrictions to remain in place for most of 2021
- The lack of international travel is increasing the cost of freight and impacting supply chains up the supply chain
- The demand from other industries for land is driving up property prices

### AUSTRALIANS ATE LESS BUT PAID MORE

Domestically, Australians ate less citrus during the COVID-19 lockdowns, with the overall local fresh wholesale market volume declining 3 per cent while the value of spend in retail increased 7 per cent. This more than made up for the closure of Food Service industries due to COVID-19 with 18 per cent of citrus sold through food service in 2019, this dropped by 11 per cent in 2020.

According to Horticulture Innovation Australia (HIA), Australians ate on average 12kg of citrus varieties in 2020, down 5 per cent from 2019. In 2020, over 92 per cent of that supply was sourced from Australian fruit producers with the remainder coming from the US and Egypt.

### LABOUR SHORTAGES IMPACTING PRODUCTION

Concerns over labour shortages in the horticultural industry are set to continue with ABARES a reduction in overall volume of production by around 1 per cent in the 2021/22 season.

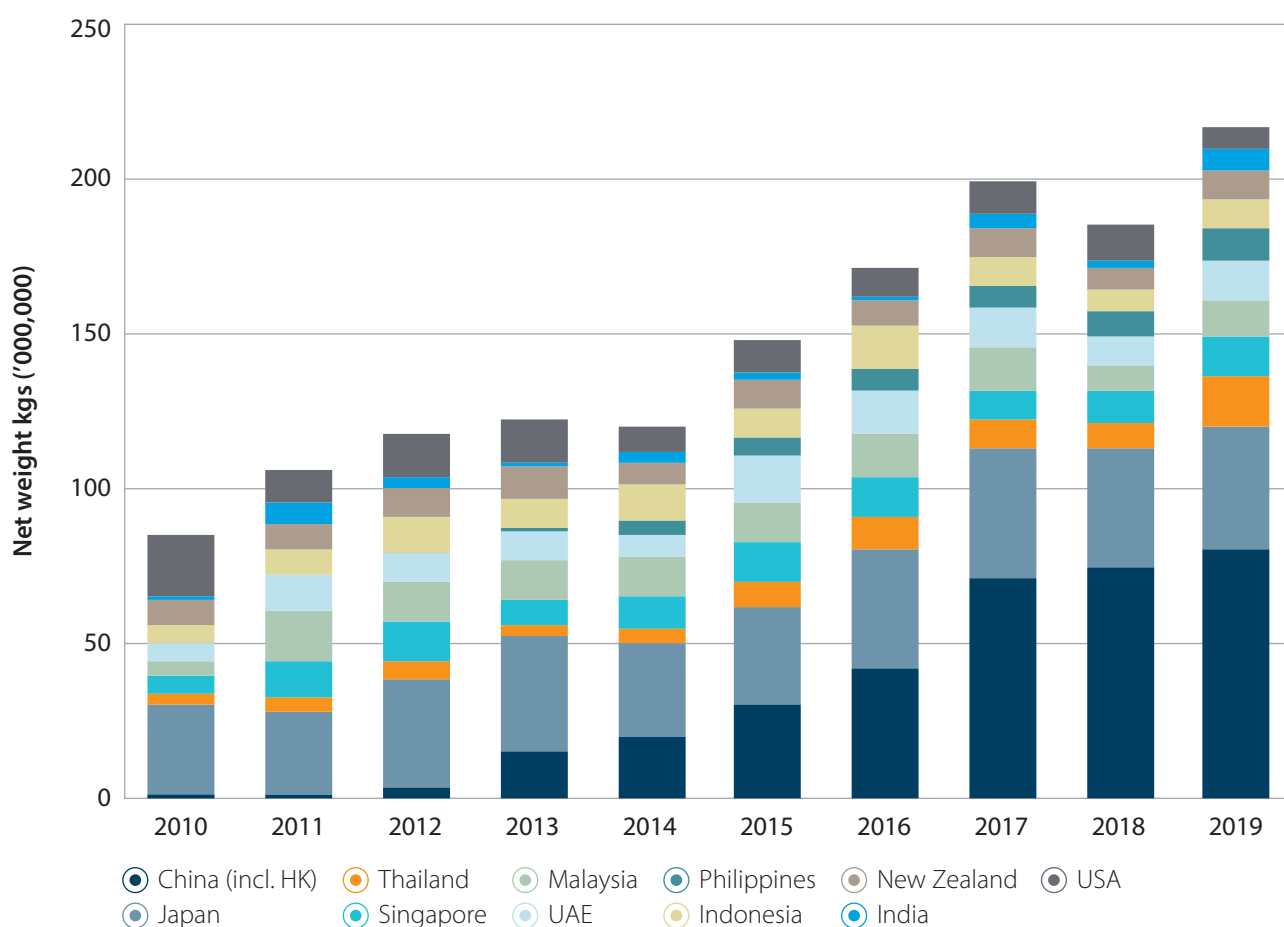
Fruit is forecast to fall by around 17 per cent, with producers concerned about limited worker availability for harvest, having reduced production expectations where possible.

Others have invested in automation where this is a viable option. As a result, there has been a focus on innovation and technologies which will likely improve efficiencies in the long term.

The impact to labour was mostly due to the significant decline in the number of working holidaymakers as a result of border closures. Without new arrivals, visa holder numbers fell by 64 per cent to about 40,000 since COVID-19 emerged last year. There has been some success in programs implemented to bring in workers from Pacific Island nations. However, with hotel quarantine caps and part of the cost burden being incurred by farmers, this has had limited take up.

Unfortunately, efforts to encourage Australians to travel to regional areas for fruit-picking jobs have mostly been unsuccessful. However, recent confirmation of the Trans-Pacific bubble may go some way to alleviating the gap, with New Zealanders able to travel back and forth without quarantine.

## EXPORT GROWTH OF AUSTRALIAN CITRUS TO GREATER CHINA EXPECTED SLOW IN 2020



Source: UNComtrade

Most recent available export figures are for the 2019 year which do not show the significant fall experienced in 2020

### SUPPLY CHAIN ISSUES CAUSE TROUBLE FOR EXPORTERS IN 2020

The grounding of international airlines significantly impacted the airfreight industry, leading to delays in deliveries and extended transit times. This impacted the fresh fruit market due to the short shelf life and requirement for end-to-end cold storage.

China is by far the largest export market for Australian fruit including citrus. As of 2019, 35 per cent of Australia's citrus export went to China. However, this appears to have dropped off significantly during 2020 with final figures not yet available.

The decline is partly as a result of the impacts of reduced freight but also in recent years there has been a significant uplift in imports to China from Egypt. It's possible a deal between Australia and China for lower import tariffs on citrus in 2021 will see this turn around.

### DEMAND FOR LAND DRIVING UP PROPERTY PRICES

Almonds are increasingly moving into areas that were previously focused on citrus growing, particularly along the Murray River, due to their high export value. Many plantations are now just reaching maturity, leading to record production volumes. The high value of these crops have made them attractive through many areas despite forecast irregular rainfall, as it remains profitable to purchase water allocations from other lower returning crops. The demand for almonds is set to continue to grow both domestically and internationally, with exports to China forecast to continue to grow. This will only increase the demand for land to be converted to almond farming, pushing out lower return crops such as citrus.



## VERTICULTURE INSIGHTS



### OVERVIEW

- + Urbanisation, deterioration of cropping conditions and food security concerns drive rising interest in vertical farming
- + Global vertical farming market size to grow rapidly in the next five years, driven by the US and European markets
- + Potential to unlock significant gains in horticulture produce yields
- Industry remains in a nascent stage with a majority of vertical-farm related business models to be commercially viable
- Expensive urban real estate may act as a deterrent for large scale expansion
- Consumer preference will be influenced by price, which will drive decisions made by supermarkets, grocers and others, to agree to buy vertical produce

For a long time, it has been easy for Australians to take for granted this country's abundant quantities of growing lands and great soils, and the ability to grow all kinds of healthy and affordable produce in volumes to easily feed our own population, as well as exporting the surplus.

For many countries, the challenge in achieving this has been far greater – a factor which has admittedly been of benefit to Australian exporters. Importantly, these hurdles are not just in developing countries, but in heavily urbanised locations including in Europe and North America.

Factors which can impede the widespread growing of food are many, but can include:

- Rapid growth of urbanisation
- Poor soils, due to climate or neglect
- Poor food safety, often due to water and soil contamination
- Difficulty in getting food quickly and freshly to points of sale
- Lack of cold storage networks and facilities

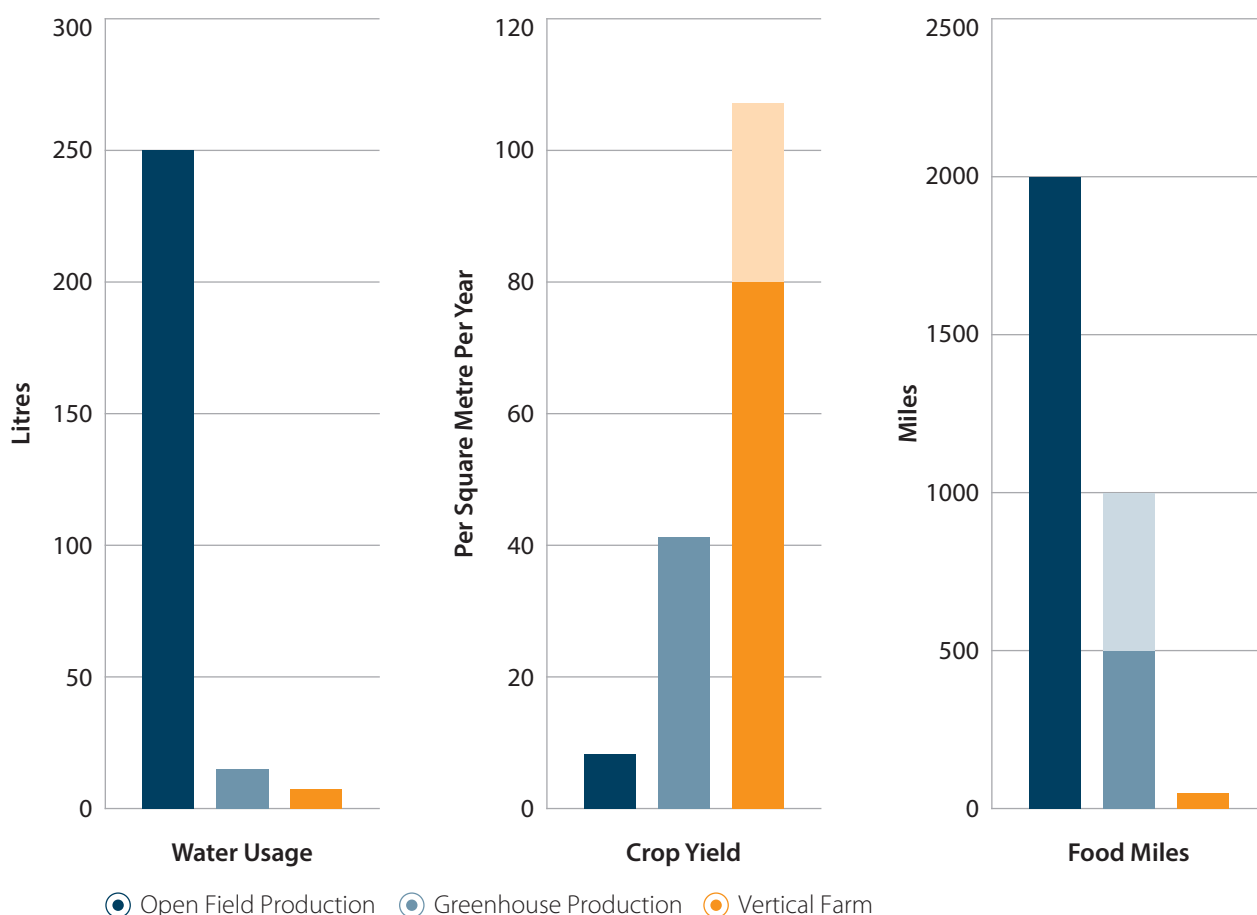
It was from these challenges that the concept of vertical farming – verticulture – first arose. Vertical farming is essentially aimed at being able to provide freshly-grown horticultural products in areas of limited space and soils, particularly urban environments.

Vertical agriculture takes a number of forms. It encompasses:

- Crops grown indoors in vertically stacked layers
- Relying on artificial light
- Grown without soil

While both vertical farming and greenhouses use indoor farming technologies, greenhouses predominantly use sunlight with almost translucent roofs and wall structures. One study on lettuce production indicated vertical farming could be far more efficient in water usage, and crop yield, while also being conveniently located closer to urban areas, significantly reducing transportation and food handling wastage.

## COMPARISON OF 1KG LETTUCE PRODUCTION UNDER DIFFERENT PRODUCTION SYSTEMS



Source: EIT Food – 'Is Vertical Farming really Sustainable?'

Vertical farms come in three main types – hydroponics, aeroponics and aquaponics.

### HYDROPONIC

- The most popular
- The plants are grown in either liquid or soil substitutes
- Hydroponic operations are usually high yielding, and use less water

### AQUAPONICS

- These combine fish farming with plant growth
- The operations utilise fish water for plant nutrition
- The plants also consume carbon dioxide created by the fish
- This style of vertical farm is not widely used

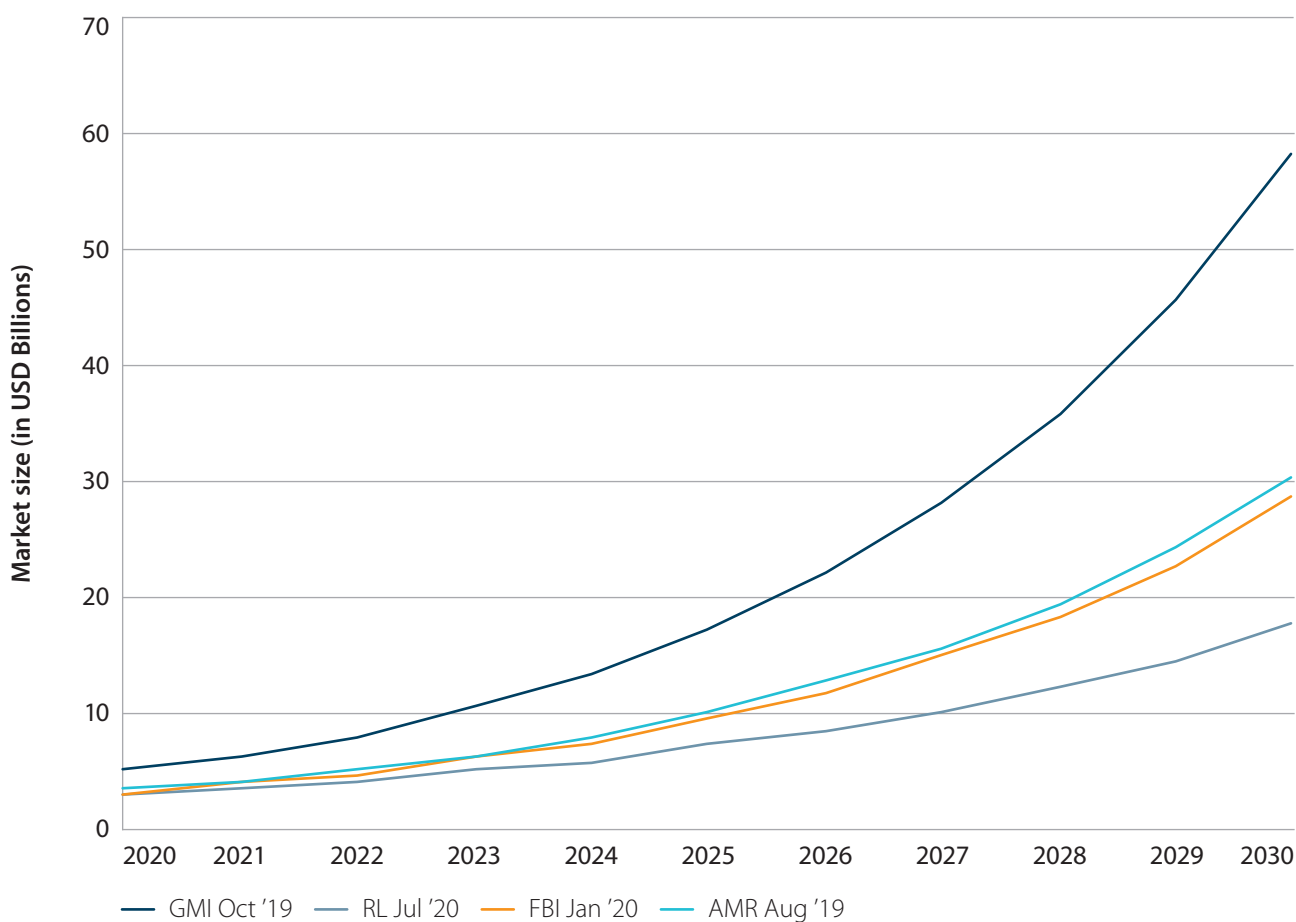
### AEROPONICS

- This kind of vertical agriculture does not use liquids or solids as a base to grow plants
- Instead, it utilises liquid with nutrients, sprayed as a mist, with the plants suspended
- This method, which uses less water than the others, is not widely used but growing in popularity

While much has been written about the concept, the actual scale of vertical farms globally is still very small. It is estimated globally that vertical farms currently cover just 50 hectares of land in total. This is in contrast to an estimated 500,000 hectares currently occupied by greenhouses, or 50 million hectares of land currently being used for outdoor cultivation. Forecasts for the size of the market vary widely – different analysts have predicted anywhere between below \$20b and around \$60b by 2030.



## ESTIMATES OF THE GLOBAL VERTICAL FARMING MARKET (USD BILLION)



Source: GMI Insights (GMI), Report Linker (RL), Fortune business insights (FBI), Allied Market Research (AMR)

Despite some of its challenges, activity in the vertical farming space continues to grow. Europe's largest vertical farm is currently being constructed in Denmark (73,000 square feet). In addition, there are plans to build the world's largest vertical farm in Abu Dhabi, a country which spends nearly US\$3.3bn every year on fruit, nuts and vegetables. For countries such as this, which import 90 per cent of its food supply, and where the sandy soil, harsh climatic conditions and limited water availability create food security issues and challenges, vertical farming is seen as one potential long-term solution.

### BENEFITS

Vertical farming offers a number of other benefits, many of which have become more pronounced globally through the COVID-19 period. Theoretically, it can provide greater levels of food security to countries or communities which could otherwise be impacted by supply chain disruptions. By growing vegetables in the midst of communities, it provides the ability to deliver fresher products to a population, enhancing overall health levels.

Vertical farming also gained further attention in the COVID-19 period due to its minimal requirement of labour. While agricultural operations in many countries were disrupted when farm labourers were unavailable due to travel bans, vertical farms can be operated almost labour free, optimally right up until the produce leaves the facility. In addition, the lack of human interaction reduces any food safety concerns which may arise from human handling of the plants.

## CHALLENGES

Vertical farming does come with a number of challenges. At this point in time, with a lot of the technology still in a developmental stage, set-up costs for operations remain very high. In addition, given the reliance by vertical farms on artificial lighting, as well as for the internal climate control, the ongoing power costs can also be a major cost – as well as necessitating a reliable source of electricity.

The issue of power costs could be seen as negative by some, due to the high levels of fossil fuels indirectly required to grow the food. While research is continuing on how to provide adequate power from other sources, such as solar, a viable alternative has yet to be developed.

With the need to generate strong revenue and margins to cover the relatively high production costs, vertical farming does not make sense for standard crops, such as wheat, rice or oilseeds, where broad acre farming is still the most profitable option. At this time, vertical farming is most suited to salads, leafy greens or herbs.

In addition, while labour requirements may be low, the personnel required are still normally highly specialised. And while full automation may be the aim of vertical farming, it is still some way off.

## INVESTMENT POTENTIAL

One factor which has kept vertical farming in the headlines has been its investment potential. As with all parts of the food supply chain, investors continue to look for opportunities which combine the surety of the fundamentals (i.e. people will always need to eat) with an opportunity which has the potential to deliver the returns to match their risk profiles.

At the same time, many investors will always be keen to find emerging categories which may combine newer IP with an ability to take a leading position in a less crowded marketplace – in a way, not dissimilar from the current activity in the plant-based protein or ‘fake meat’ space.

Vertical farming in Australia is still at a nascent stage but with rising interests across the supply chain, it is likely to play greater role in future. For example, Coles Nurture Fund (A\$50m fund to support small and medium business focused on innovation) funded a herb greenhouse in 2015, partnering with Australian Fresh Leaf Herbs and product to be supplied through Coles supermarket chains. Queensland-based Stacked Farms, with its fully automated vertical indoor farm, produces salad greens, tomatoes and strawberries and distributes them through traditional supply chains. In addition, the Victorian-based Roto-Gro ag-tech company has developed specialised cultivation and patented technology which could be used for perishable food production through its urban vertical farms.

## IS THERE CONSUMER DEMAND?

Ultimately, vertical farming will not prove profitable unless consumers are happy to pay what is required for its output. As with many food products, the issues of consumer reaction and perception will play a strong role in its uptake. That said, while new kinds of foods or growing technologies may sometimes arouse loud public comment, this doesn't necessarily impact on sales – a lot of consumers will quite happily eat GM foods, despite the headlines.

For vertical farming crops, it is possible that there may be one vocal group of consumers happy to pay a price for the ‘local food’ concept, while another group may potentially object to eating items not grown in natural sunlight and soil. At the end of the day, however, consumers are likely to buy based on price, and it is this factor which will most impact the decisions by supermarkets, grocers and others to agree to buy vertical produce, and ultimately, their viability.

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# ECONOMIC MOMENTUM TO CONTINUE AS STIMULUS WINDS BACK

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Our activity levels are back,  
but we are still leaning on stimulus

Economic activity in Australia is likely to be above pre-pandemic levels after a rapid recovery from the COVID-19 downturn. The total number of workers in the economy, as at February, also made a full recovery. We expect strong economic growth this year, of 4.2 per cent year-on-year to December. This is much higher than what we've seen in previous years, especially when we take into account very weak population growth due to our closed international borders.

But while total activity has come back, Australia is still leaning on more fiscal spending and lower borrowing costs than before the pandemic. ANZ forecasts that the rest of the year will include less fiscal spending than the March quarter, but similar levels of support from the RBA to keep borrowing costs low.

It's likely that Australia will adjust to the reduction in fiscal spending with growth in the private sector. But some key economic goals, like stronger wage growth and the RBA's inflation target, are at least a couple of years away.

## AUSTRALIA'S LABOUR MARKET WILL KEEP IMPROVING DESPITE THE END OF JOBKEEPER

Treasury estimated that 1.1 million workers were receiving JobKeeper in the March quarter, and ANZ estimates that 100,000–150,000 people will lose employment as a result of JobKeeper's expiry at the end of March 2021 (0.8–1.2 per cent of total workers).

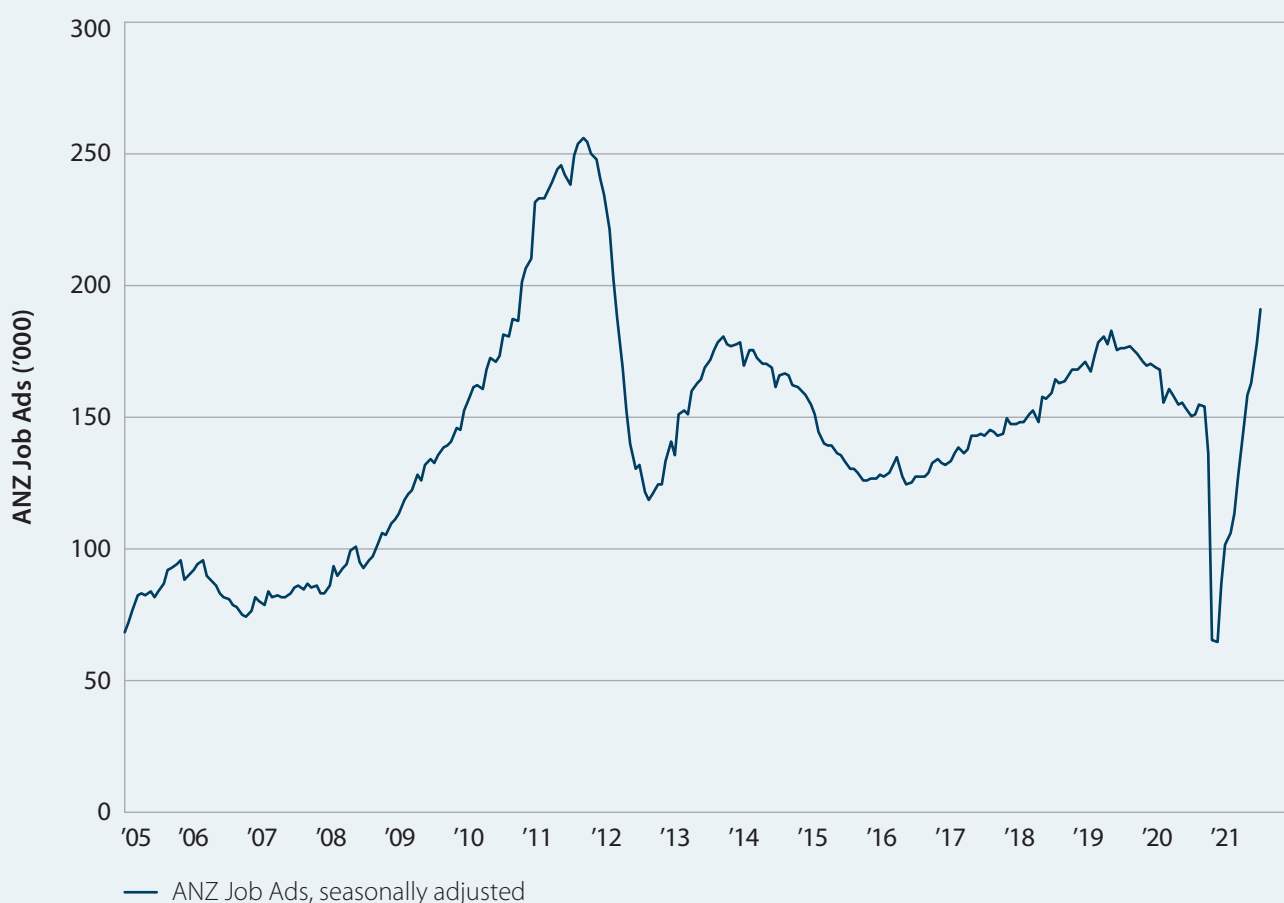
But that doesn't mean there will be 100,000–150,000 fewer employed workers in the country. Many of these workers will find new jobs quickly, as recent labour market data points to a rapid absorption of excess workers in the economy. The unemployment rate dropped from 6.3 per cent in January to 5.8 per cent in February, and ANZ Job Advertisements data indicate that there are 27 per cent more job ads in Australia compared to before the pandemic. Indeed, there were actually more job ads around in March than there were in any single month since November 2008. It's also important to note that while JobKeeper was shrinking in the December and March quarters, the unemployment rate was going down at the same time.

ANZ expects to see slightly higher unemployment during the June quarter, while the economy adjusts to the end of JobKeeper, after which we expect the unemployment rate to resume its downward trend. We also expect the recent drop in consumer confidence to be temporary, as households adjust to the end of JobKeeper and JobSeeker supplements as well.

## RBA RHETORIC HAS HELPED EASE UPWARD PRESSURE ON THE AUD

In his speech on 10 March, RBA Governor Lowe noted that 'over the past couple of weeks, market pricing has implied an expectation of possible increases in the cash rate as early as late next year and then again in 2023.' He went on to say, 'this is not an expectation that we share.'

## ANZ JOB ADS ROSE 7.4% MONTH ON MONTH IN MARCH



Sources: SEEK, Dept of Education Skills and Employment, Macrobond, ANZ Research

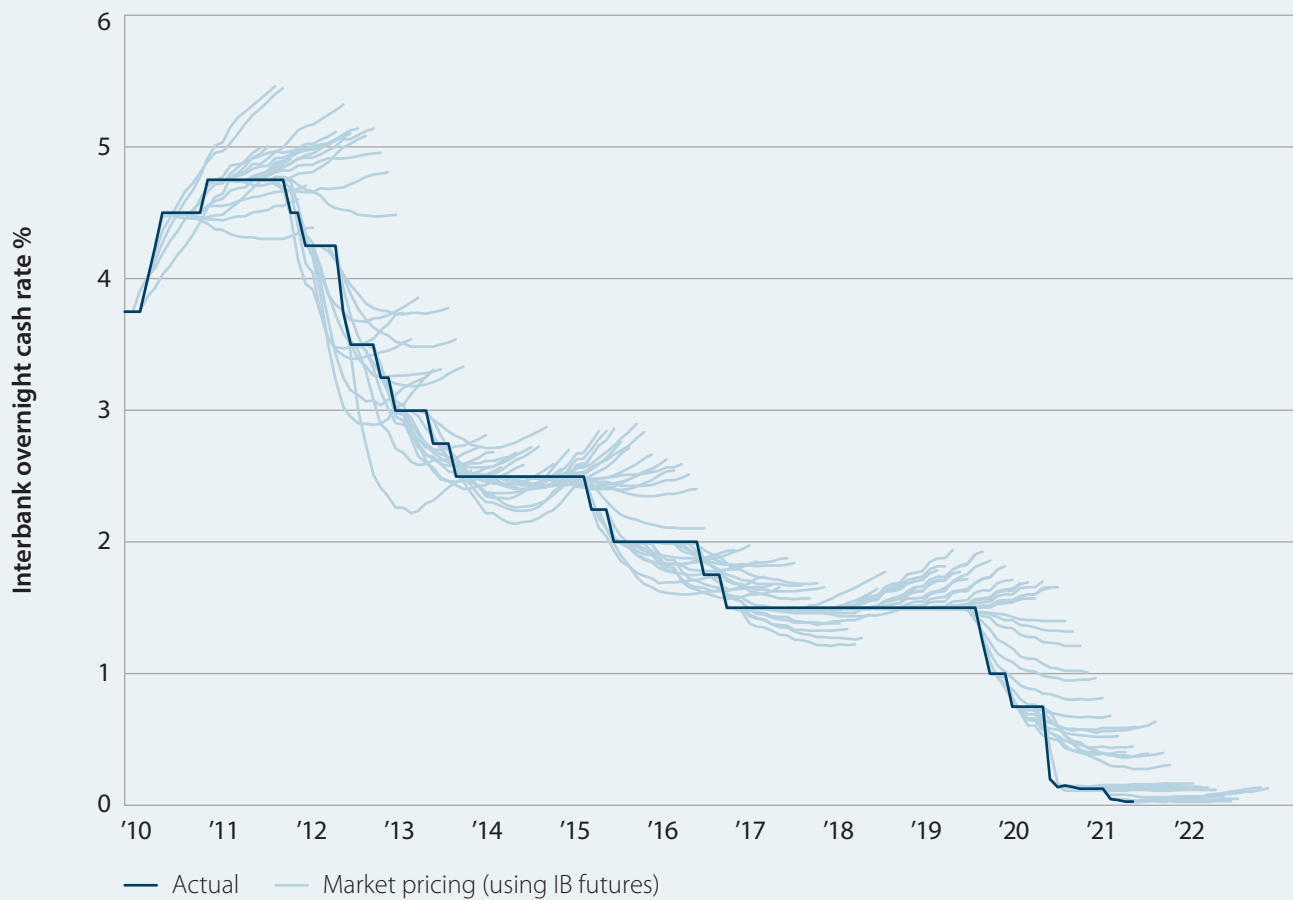
We believe this message and the actions the RBA has taken on its bond purchases has contributed to the pullback in the AUD from close to 0.80 in late February to close to 0.76 in late March/early April.

Recent stimulatory policy and rhetoric by the RBA have been important in bringing the strong upward trend in the currency to at least a temporary halt. The slightly lower currency value may have helped the growth of rural exports, which were up 11.6 per cent year-on-year to February 2021 in value terms.

While markets are still pricing an early lift in the RBA cash rate, there is some reason to be sceptical. The chart on p.27 shows that markets often expect a lift in the cash rate, and that it doesn't necessarily happen when it's priced. Indeed, there have been many occurrences of cash rate increase expectations over the last 10 years, even though the last cash rate hike occurred in 2011.

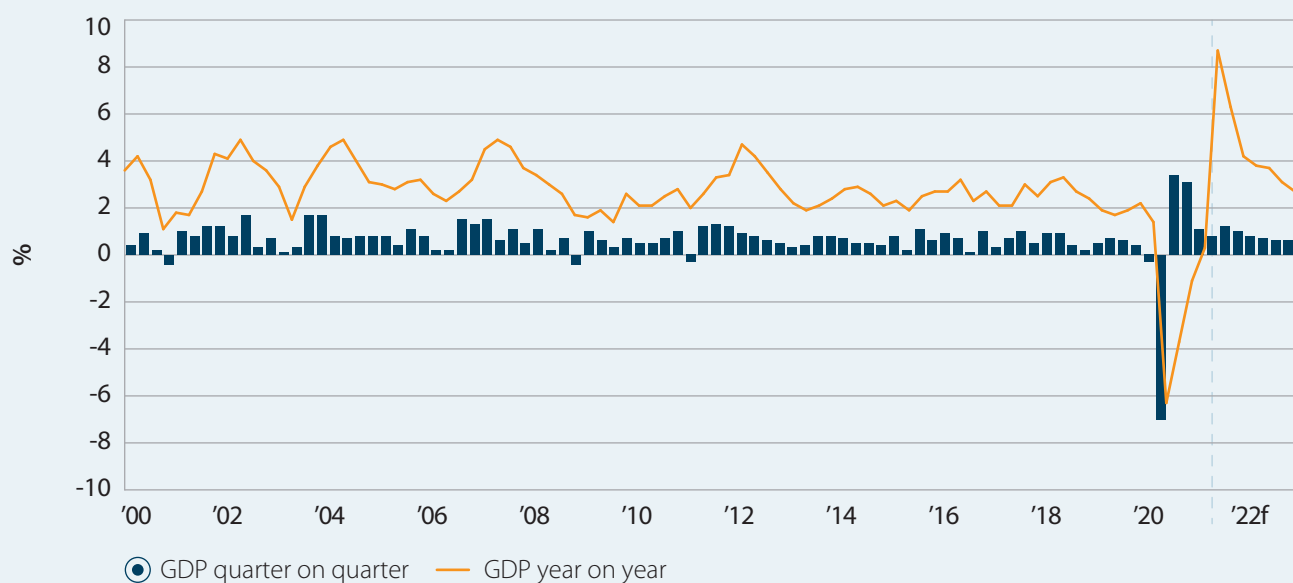


## MARKET EXPECTATIONS FOR CASH RATE INCREASES DON'T ALWAYS COME TRUE



Source: RBA, Bloomberg, ANZ Research

## WE EXPECT GDP GROWTH IN EXCESS OF 4% THROUGH 2021



Source: RBA, Bloomberg, ANZ Research

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