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February has been wet and wild for many parts of the country. In particular, the top of the South Island has had to deal with record rainfall and the floods and slips that have gone with that. Meanwhile, other parts of the country have welcomed the rain, following the very dry early summer and accompanying drought.

However, the wet weather hasn't translated into better dairy production just yet. Indeed with January production weak, we have revised our 2017/18 production forecast to equal with last season, from +1% previously.

The flipside to weaker production is higher prices. We now expect dairy prices to remain stronger for longer than we had anticipated previously, meaning some upside risk to our 2017/18 milk price forecast of \$6.50/kg. Also with current prices firm and the fact that global dairy markets are largely balanced, it augurs well for another \$6.00/kg+ milk price in 2018/19.

There is plenty of love to go around in the meat sector. Average prices over February 2018 were the highest ever on record for a February month for both benchmark lamb and beef prices. Indeed, we expect prices remain healthy over the remainder of the season and most likely start 2018/19 strong as well.

Coarse wool prices, however, remain stuck in a rut. February prices remained stuck at under \$3.00/kg. Meanwhile, the outlook is slightly better, although high wool stocks may temper any price recovery.

On the interest rate front, we expect NZ interest rates to remain relatively low. Although, long-term interest rates may drift modestly higher over the next six months.

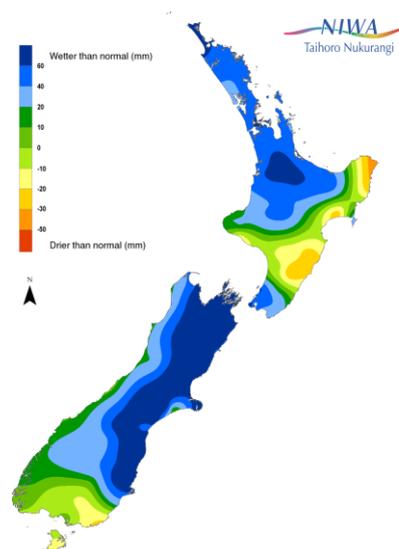
Lastly, the NZD gave back some of its January gains against the USD over February. On balance though, we expect the NZD to drift higher against most currencies over the next six months. With that in mind, the NZD may cap further gains in commodity prices in NZD terms over the next six months.

Key Rural Data:

Chart of the Month:

As at 23 February 2018	Current	4 wks ago	Year ago	Outlook*
Rural Commodity Prices:				
ASB Dairy Price Index (USD)	95.1	93.0	90.0	➔
Lamb Price Index (NZD)	116.0	114.4	88.7	➔
Beef Price Index (NZD)	112.7	108.6	108.9	➔
Wool Price Index (NZD)	63.3	60.6	70.4	➔
Interest Rates:				
90-day bank bills	1.92	1.88	1.99	➔
2-year swap	2.18	2.18	2.32	↗
5-year swap	2.72	2.70	2.95	↗
Exchange Rates:				
NZD/USD	0.7291	0.7356	0.7204	↗
NZD/CNY	4.62	4.65	4.95	↗
NZD/GBP	0.5219	0.5191	0.5778	➔
Milk solids production (ytd % chg]**	-0.9	0.4	-2.9	↗
Fonterra Shareholders' Fund	6.11	6.40	6.36	↘

Soil moisture anomaly (mm) at 9am on 26/02/2018



*Direction of change over the next 6 months. **As at January 2018.



Rural Fact or Fiction?

Cyclones, of which Gita was one, are very different to hurricanes.

Answer on page 3

Rural Commodities Outlook

Dairy – Production forecast trim

January nationwide dairy production was weak. January production fell 7.4% compared to January 2017, marking the second weak month in a row.

Moreover, January production was weaker than we had anticipated. While December was very dry, January saw rain in many areas. However, the rain hasn't translated into better production just yet.

As a result, we have revised our 2017/18 production forecast to equal with last season, from +1% previously. Recent rain means that production will still recover some lost ground in coming months. However, this recovery is likely to come too late to prevent lower overall production.

The flipside to weaker production is higher prices. We now expect dairy prices to remain stronger for longer than we had anticipated previously. In turn, this points to some upside risk to our 2017/18 milk price forecast of \$6.50/kg. That said, most of the milk for 2017/18 has already been sold, so there is limited scope for further movements in this season's milk price.

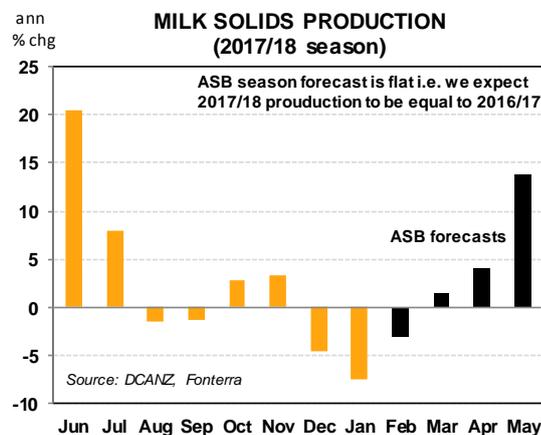
At this juncture, the 2018/19 season is likely to off start on the right foot. Using the most recent auction prices, the spot milk price is sitting at around \$6.70/kg. With that in mind and the fact that global dairy markets are largely balanced, it augurs well for another \$6.00/kg+ milk price.

Dairy Index (USD), 23 Feb: 95.1 ↑2.3% (mpc)

Season End Milk Price Forecasts:

	2017/18		2018/19	Long Run
	Fonterra	ASB	ASB	ASB
Milk Price*	\$6.40	\$6.50	\$6.50	\$6.50-\$7.00

* per kg of milk solids (excluding dividend).



Lamb – It keeps getting better

It keeps getting better for lamb prices. Average prices over February 2018 were the highest ever on record for a February month.

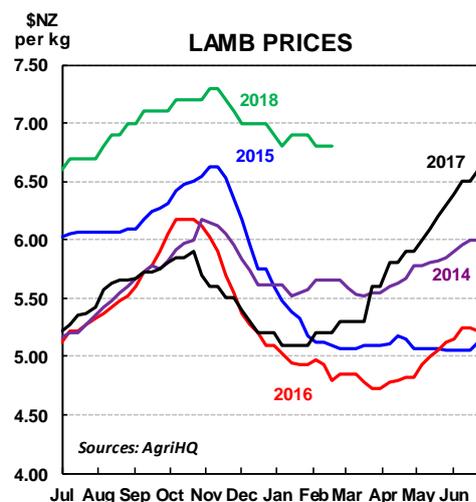
Moreover, the seasonal decline through late summer has been modest to date. Per kg lamb prices only fell 20c/kg over January February 2018.

With this in mind, our previous view that we expect lamb prices to remain over \$6.00/kg for the remainder of the season looks a done deal. In fact, we are increasingly confident may hold above \$6.50/kg for the remainder of the season.

Moreover, the majority of factors underpinning prices are likely to remain in play. Also, we are unlikely to see a major pick up in supply either side of the Tasman.

The demand side of the equation also looks healthy as the global economy improves. As a result, we expect that prices are likely to remain healthy at the start of the 2018/19 season.

Lamb Index (NZD), 23 Feb: 116.0 ↑1.5% (mpc)



Beef – Sharing the love

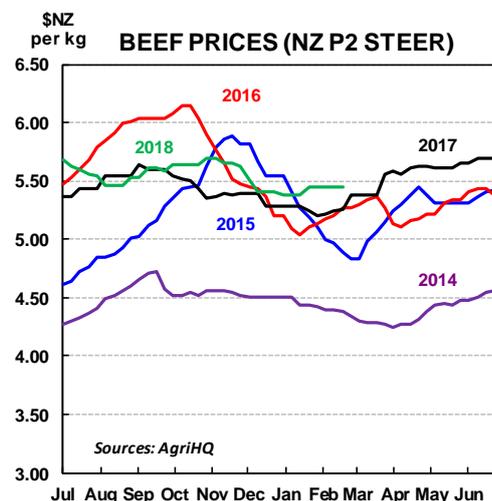
There is plenty of love to go around in the meat sector currently. Like lamb, beef prices have also averaged over February the highest ever on record for a February month.

Moreover, the seasonal dip in prices has been very minor. After falling 31 cents per kg from their November peak at one stage, P2 steer prices since have consolidated. Indeed, per kg prices look set to remain comfortably above \$5.00/kg for the remainder of the season.

NZ supply remains tight, helping keep prices firm. Supply remains similarly tight across the Tasman as Australian farmers rebuild their herds. On the other hand, Brazilian exports are strong particularly into the Chinese market.

Meanwhile, demand from key markets remains solid. All up, we don't expect to change in this respect over coming months. So like lamb, beef prices are shaping up for 2018/19 as well.

Beef Index (NZD), 23 Feb: 112.7 ↑2.3% (mpc)



Rural Commodities Outlook (continued)

Wool – Coarse wool stuck in a rut

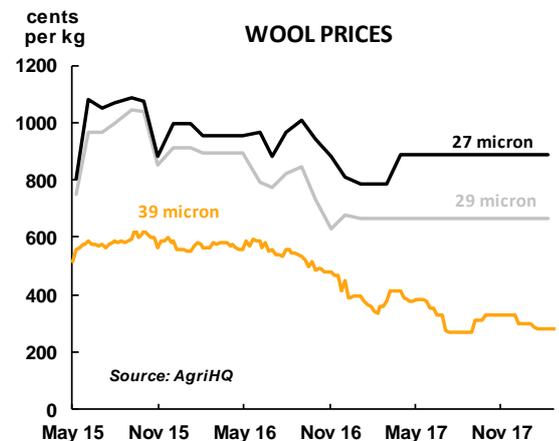
Wool Index (NZD), 23 Feb: 63.3 ↑4.4% (mpc)

Coarse wool prices remain stuck in a rut. February prices have continued where January left off and are stuck at under \$3.00/kg.

Back in the spring of 2017, coarse wool prices had hinted at recovery. However, prices have since then have given back most of the 25% gain over the summer.

That said, this time of the year represents peak wool supply, so some price relief may be due as supply recedes over coming months. While we are confident that prices may lift off their current lows, we are not so confident that prices will lift materially. In particular, wool stocks are still high so it will take a rundown of stocks before prices can lift in earnest.

Meanwhile, mid-micron prices remain stable at a moderate level. In addition, fine (merino) wool prices are healthy. We expect these prices to remain around current levels over coming months. In particular, we expect the improving global economy and subsequent lift in consumer demand to underpin these prices.



Financial Markets Outlook

Interest Rates – Lower for longer

90-day bank bills, 23 Feb: 1.92% ↑ 0.04 (mc)

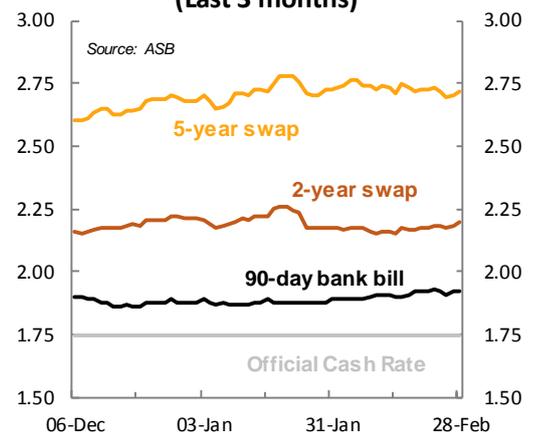
On 8 February, the Reserve Bank (RBNZ) kept the Official Cash Rate (OCR) on hold at 1.75%. Moreover, its Monetary Policy Statement contained little change from the last statement back in November.

The RBNZ doesn't expect to lift the OCR until late 2019. And in the press conference following the Statement, the RBNZ also raised the possibility of the next OCR move being a cut.

We agree that OCR hikes are long way off. On this basis, we have pushed out our view for the timing of the next OCR hike to August 2019, from February 2019 previously.

The RBNZ's stance should help keep NZ short-term interest rates around current low levels. In contrast, long-term interest rates may drift higher in line with rising global rates. In particular, we expect three US Federal Reserve interest rate hikes this year. All up, we expect interest rates to continue to remain low by historical standards.

BENCHMARK INTEREST RATES (Last 3 months)



NZ Dollar – Back, but still solid

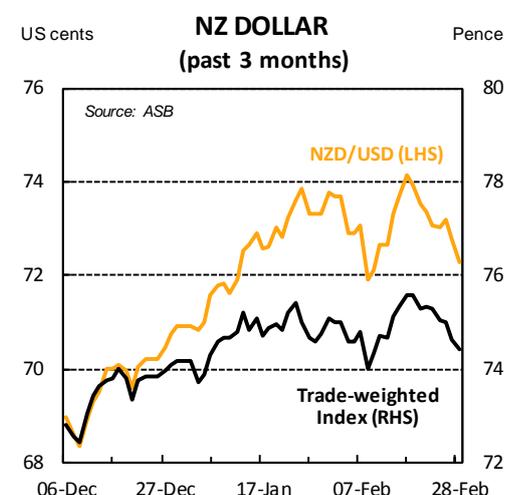
NZD/USD, 23 Feb: 0.7291 ↓ -0.0065 (mc)

The NZD gave back some of its January gains over February. This fall was mostly the consequence of a broad-based USD rebound. Specifically, the NZD has receded around 1% since the last edition of Farmshed Economics.

Against other currencies, the NZD was more mixed over February. Indeed, against the euro the NZD was largely unchanged, while it lifted modestly against the pound. Meanwhile, the NZD gained nearly two cents against the AUD.

On balance, we expect the NZD to drift higher against most of the major currencies over the next six months. In particular the NZD remains underpinned by the solid NZ economic outlook and strong NZ commodity prices.

With that in mind, the high NZD may cap further gains in farmgate prices (i.e. commodity prices in NZD terms) over the next six months.



Rural Fact or Fiction?

? **Answer: Fiction!** Cyclones and hurricanes are the same thing. The different in names only indicates where the storm took place. Those formed in the Atlantic or Northeast Pacific (near the US) are called hurricanes, while those formed in the South Pacific or Indian oceans are called cyclones.

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