

Farmshed Economics

Winners and losers

November 2020



ASB

Inside this edition:	Pg.
Rural Commodities	
Dairy	2
• Hotting up	
Lamb	2
• Not out of the woods	
Beef	2
• Ditto	
Fruit	3
• Resilient	
Financial Markets	
Interest Rates	3
• Low, low, low, low, low	
NZ Dollar	3
• Still bouncing	

It is around eight months since the World Health Organisation declared COVID-19 a public health emergency, and since then its been a wild ride for commodity markets. After steep falls earlier in the year, prices for many agricultural commodities have lifted off their lows and some are even touching year-ago levels. Still, the gains have not been evenly distributed, and the unique export mix and supply factors of each commodity have played a big part in where things have landed. In this edition, we look at the (relative) winners and (relative) losers.

The forestry and horticulture sectors have been the big winners over recent months. Forestry prices have lifted above year-ago levels and face further upside with construction activity holding up and the Chinese recovery continuing. Similarly, kiwifruit export values have remained resilient as the season has gone on, thanks to strong demand.

The dairy sector is broadly in the middle of the pack. The sector has proved much more resilient than many had anticipated and has been another beneficiary of still-sturdy Chinese demand. Since our last report, we've revised our farmgate milk price up to \$6.75 per kg of milk solids for the season. That's lower than the \$7.14 farmers enjoyed for the past season, but a far cry from earlier in the year when many felt there was a risk the price could fall below \$6. Things haven't been so flash for meat. Prices have stabilised since their crash earlier in the year but remain down on a year-ago by double digits.

Unfortunately, the outlook for the sector is still uncertain, with new lockdown measures in Europe shutting restaurants in key markets.

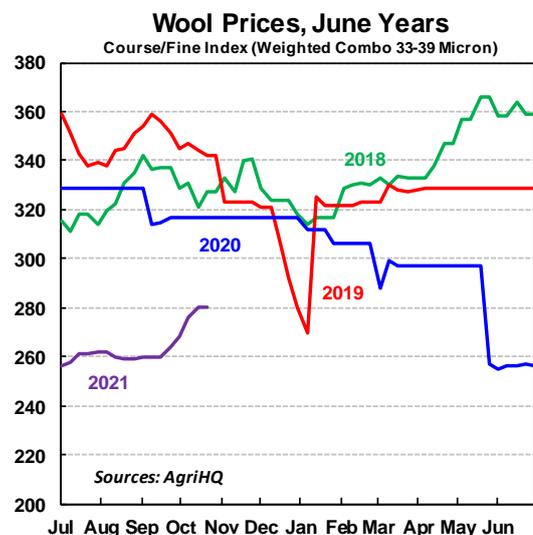
Wool prices have also been a big laggard and, at times, have been down by more than 20% on a year-ago levels. Still, there has been a little bit of positive news recently, with prices lifting decently off the back of stronger demand. It's very early yet, but the events this year show how quickly fortunes can change. Remember, as that great poet of times of upheaval Bob Dylan once sung, "the loser now will be later to win."

Key Rural Data:

Key Rural Data:	As at 30 October 2020	Current	3 mths ago	Year ago	Outlook*
Rural Commodity Prices:					
ASB Dairy Price Index (USD)		98.4	98.6	99.9	➔
Lamb Price Index (NZD)		111.3	111.8	136.6	➘
Beef Price Index (NZD)		95.3	94.7	109.7	➘
Fruit Price Index (NZD)		106.5	101.4	124.4	➔
Interest Rates:					
90-day bank bills		0.28	0.30	1.080	➘
2-year swap		0.01	0.20	0.99	➘
5-year swap		0.11	0.31	1.08	➘
Exchange Rates:					
NZD/USD		0.6610	0.6639	0.6349	➔
NZD/CNY		4.42	4.66	4.49	➔
NZD/GBP		0.5111	0.5191	0.4951	➘
Milk solids production (ytd % chg)**		2.9	2.0	2.0	➔
Fonterra Shareholders' Fund		4.61	3.82	4.24	➔

*Direction of change over the next 6 months. **As at September 2020.

Chart of the Month:



Rural (and Presidential Election) Fact or Fiction?

Prior to being elected US President, Jimmy Carter was a walnut farmer.

Answer on page 3

Author: Nat Keall – Economist – nathaniel.keall@asb.co.nz

Nick Tuffley – Chief Economist – nick.tuffley@asb.co.nz

Please refer to the important disclosures at the end of this document

Rural Commodities Outlook

Dairy – Hotting up

Dairy Index (USD), 30 Oct: 98.4 ↑ 0.8% (qpc)

Fonterra has tentatively lifted its farmgate milk price range since the start of the season, though it has retained a reasonably wide range of \$1.00/kg given lingering uncertainties. We've also nudged up our forecast since the season began and are now sitting at \$6.75 – not far off the \$6.80 mid-point of Fonterra's estimate.

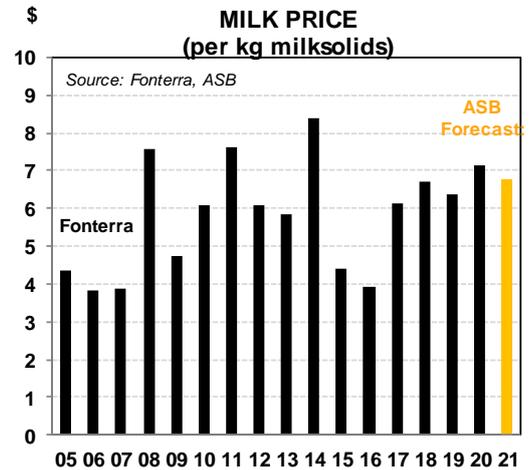
This season's forecast has been unusually difficult given the current environment, even as we've adapted to the new normal. Indeed, we've seen some dramatic – and occasionally counterintuitive – moves at some dairy auctions. Amid fears of a slowdown in international trade and widescale logistics disruption as buyers bid heavily to secure supply in July, before prices fell away markedly at subsequent auctions. Demand in China still looks to be holding up well, but there are reports that the country has now built up a good stockpile, raising questions around how far that trend can continue.

By contrast, the other key area of uncertainty is around New Zealand production. After some superb grass growing conditions, domestic production is already running about 3% ahead of last season. However, with a 'La Niña' weather event hitting NZ's shores there is a risk that things could really dry off over the summer, tightening supply and putting some upward pressure on prices.

Season End Milk Price* Forecasts:

2020/21		
	Fonterra	ASB
Milk Price *	\$6.30 - \$7.30	\$6.75

*per kg of milk solids (excluding dividend)



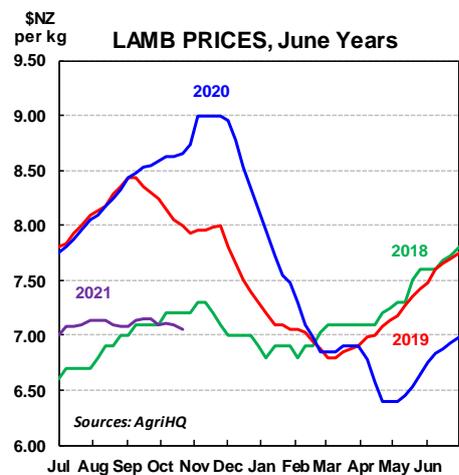
Lamb – Not out of the woods

Lamb Index (NZD), 30 Oct: 111.3 ↓ 0.7 (qpc)

In our last update, we suggested that lamb prices might be 'turning a corner.' Unfortunately, things have simply tracked sideways. Prices are tracking even further behind 2019 than they once were, and, as of the end of October, they are down about 19% on an annual basis.

Unfortunately, the outlook for lamb still looks far from certain. At the time of writing, new lockdown measures have just been announced in France, Germany and the UK, shutting restaurants in one of the sector's most important markets. The looming Brexit deadline adds another layer of uncertainty to the mix too, and our friends at AgriHQ note lamb exporters face tariffs of up to 14% in the British market if a free-trade deal can't be arranged or the UK and EU can't agree on a quota split.

One other thing to watch is that other ongoing viral outbreak – African Swine Fever – which continues to spread around the world, disrupting the global supply of protein. Heavy flooding in China earlier in the year has also affected several of the key pork production regions.



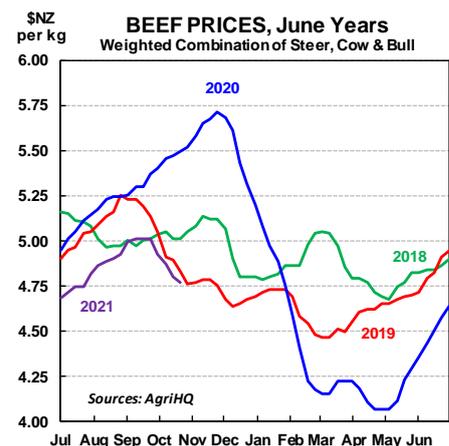
Beef – Ditto

Beef Index (NZD), 30 Oct: 95.3 ↑ 0.6 (qpc)

At the time of our last update, we also suggested that beef prices might be on the up. However, in reality, prices have struggled to consolidate their gains. Beef prices have performed a bit better than lamb but are still down about 14% on an annual basis and have been losing further ground over recent weeks.

Like the outlook for lamb, beef prices face further downside risks. As above, new lockdown measures have just been announced in parts of Europe, though we expect beef prices will be a bit more resilient than those for lamb, given the greater utilisation of beef carcasses.

As with lamb, the spread of swine fever and flooding in China (which heavily impacted the country's pork supplies) is something to watch, and should provide some support for global protein prices. Tightening beef supply out of Australia is another emerging factor, though it is too early to gauge the impact just yet.



Rural Commodities Outlook (continued)

Fruit – Resilient

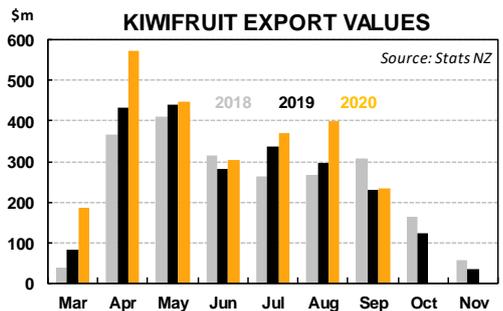
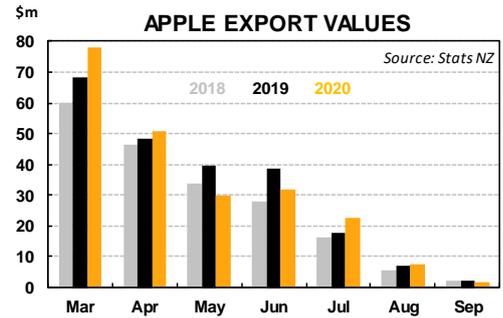
Earlier this year, there were predictions the pandemic could send globalisation into reverse, triggering a broad slowdown in international trade amid border closures, softer global demand and logistics disruption.

That hasn't transpired, and last month the World Trade Organisation revised its forecast for international goods trade over 2020. It now projects a fall of 9.2% in 2020 – less than the 12.9% drop originally feared. NZ exports too are proving resilient – particularly in the primary sector.

Fruit exports are a good example of the resilience in international trade. Apple export values held their ground over the six-months to September versus the same period last year, a respectable performance. Kiwifruit exports are even more robust, with volumes up a whopping 19.5% on a season-to-date basis after a bumper crop. Global demand for both fruits seems to be holding up and may be benefitting from the greater focus on healthy eating as COVID stays at the top of the agenda.

Still, it's not all good for the sector. Thus far orchards have weathered the reported seasonal worker shortage well, but it remains a real challenge, with the border set to stay shut for a very long time.

Kiwifruit Export Values, Aug & Sep: \$634m ↑ 20% apc



Financial Markets Outlook

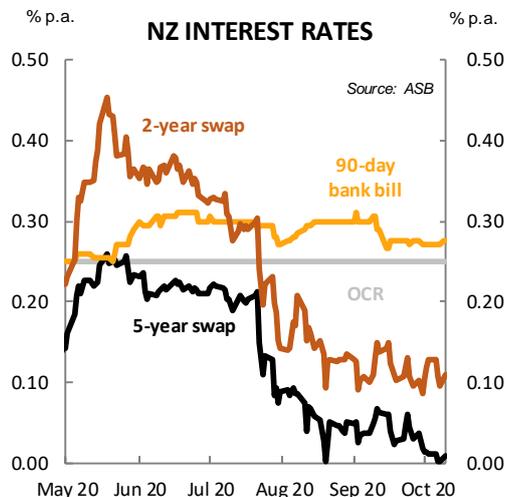
Interest Rates – Low, low, low, low, low

The outlook for interest rates remains much the same as it has been since the crisis began: very low for a very long time.

Central banks globally have continued to take strong action to avert disaster, and consequently, we've seen interest rates remain at historically low levels over the past three months or so. In New Zealand, the Official Cash Rate (OCR) remains at 0.25%, whilst the cap on the Reserve Bank's massive asset-purchase programme has expanded to \$100bn since our last report.

Strong action by the RBNZ has been broadly successful in lowering rates, with both deposit and lending rates plumbing record lows. Nevertheless, despite improving economic data of late, there is still the possibility the bank could take the cash rate negative next year if it feels more stimulus is prudent, pushing rates even lower. Interest rates should start to drift higher when the pandemic ultimately recedes, but the timing and speed of any shift is highly uncertain – and probably quite some time away.

90-day bank bills, 30 Oct: 0.28% ↓ 0.02 (qc)



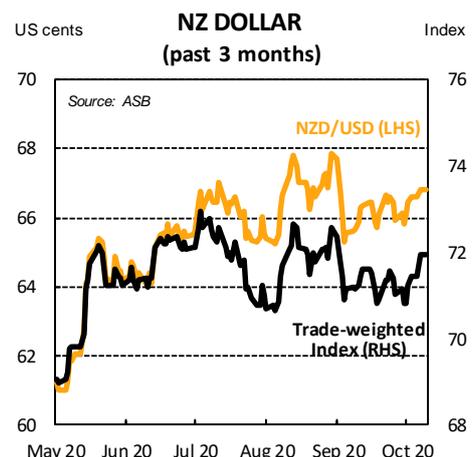
NZ Dollar – Still bouncing

As we noted in our last update, the NZD had a rollercoaster ride earlier in the year when COVID-19 ramped up, crashing as low as 55 US cents.

In the months since, the kiwi has staged a comeback to trade at higher range. Having spent most of April and May shy of 0.62, the NZD/USD has been broadly higher in the months since, even managing to creep up to 0.68 when conditions have been accommodative.

Still, there remains a fair degree of volatility around. Markets have digested a litany of US election and COVID-19 related headlines over recent months and the NZD has been characteristically vulnerable to swings in sentiment. At the time of writing, positive risk sentiment had helped the NZD sweep higher in the aftermath of the US elections and the positive COVID-19 vaccine news.

NZD/USD, 30 Oct: 0.6683 ↓ 0.2040 (qc)



**Rural Fact or Fiction?***Answer: False. He was a peanut farmer.***ASB Economics & Research**

Chief Economist

Senior Economist

Senior Economist

Senior Economist, Wealth

Senior Economist

Economist

Data & Publication Manager

Nick Tuffley

Mark Smith

Jane Turner

Chris Tennent-Brown

Mike Jones

Nat Keall

Judith Pinto

nick.tuffley@asb.co.nz

mark.smith4@asb.co.nz

jane.turner@asb.co.nz

chris.tennent-brown@asb.co.nz

mike.jones@asb.co.nz

nathaniel.keall@asb.co.nz

judith.pinto@asb.co.nz

Phone

(649) 301 5659

(649) 301 5657

(649) 301 5853

(649) 301 5915

(649) 301 5661

(649) 301 5720

(649) 301 5660

asb.co.nz/economics

@ASBMarkets

Disclaimer

This document is published solely for informational purposes. It has been prepared without taking account of your objectives, financial situation, or needs. Before acting on the information in this document, you should consider the appropriateness and suitability of the information, having regard to your objectives, financial situation and needs, and, if necessary seek appropriate professional or financial advice.

We believe that the information in this document is correct and any opinions, conclusions or recommendations are reasonably held or made, based on the information available at the time of its compilation, but no representation or warranty, either expressed or implied, is made or provided as to accuracy, reliability or completeness of any statement made in this document. Any opinions, conclusions or recommendations set forth in this document are subject to change without notice and may differ or be contrary to the opinions, conclusions or recommendations expressed elsewhere by ASB Bank Limited. We are under no obligation to, and do not, update or keep current the information contained in this document. Neither ASB nor any person involved in the preparation of this document accepts any liability for any loss or damage arising out of the use of all or any part of this document.

Any valuations, projections and forecasts contained in this document are based on a number of assumptions and estimates and are subject to contingencies and uncertainties. Different assumptions and estimates could result in materially different results. ASB does not represent or warrant that any of these valuations, projections or forecasts, or any of the underlying assumptions or estimates, will be met.