ANZ RESEARCH

AGRI FOCUS

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SPRINGING INTO ACTION

INSIDE

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Warm winter days make it feel like spring is already here. The improved conditions for pasture growth are certainly welcome, particularly in the regions that were hit hard by drought in the autumn.

Also running hotter than expected is New Zealand's economy. Very strong measures for both inflation and employment mean it is time for the Reserve Bank to spring into action with tighter monetary policy.

We are now forecasting the first increase in the Official Cash Rate (OCR) will occur in August (+25 bps) with two further lifts in October and November bringing the OCR to 1% by the end of the year. We also expect two further 25bp hikes in H1 2022.

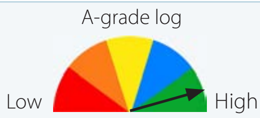
Global commodity prices remain high, but we are starting to see some prices start to recede from lofty levels. Prices for whole milk powder and logs are currently trending down. Meanwhile, returns for meat and wool are lifting.

Food security continues to feature and it is difficult to judge how this is impacting demand. Trade tensions, combined with the disarray in the shipping industry, are prompting buyers to build buffer stocks to mitigate risks of not being able to source goods when required. This has created additional demand that won't be sustained once sufficient stocks are to hand.

The rate of change in government regulatory policy is difficult to keep up with. By the end of this year we should have a clearer idea of how agriculture will account for its greenhouse gas emissions and whether pricing will be linked to the existing emissions trading scheme. Carbon prices have recently lifted, prompting further concerns that this will entice more land conversion to forestry than is desirable long-term. Expect further policy change in this area as the Government tries to rebalance incentives.

The Government has also had a crack at revising its contentious low-slope map that is part of its freshwater policy.

While it is easy to focus on the negative consequences of regulatory change, we are seeing some industries focusing more on the positive attributes our farming systems are already delivering. This is particularly visible in venison marketing – an industry that is desperate to create new channels to market following the demise of the restaurant trade.

Prices at farm/orchard level relative to 10yr average		
Dairy	Dairy prices have eased but our milk price forecast of $7.70/kg MS remains intact for the current season.	
Sheep	Lamb returns have rapidly firmed, but some of this strength is being driven by strong procurement demand.	
Beef	Beef prices are benefiting from very strong international demand from a number of countries – particularly China.	
Forestry	Log prices have eased from record levels as Chinese demand has dissipated during their hot summer months, but prices are still very high.	

ECONOMIC OVERVIEW

MONETARY POLICY TIGHTENING TO COMMENCE

New Zealand's economy is recovering quickly, but the rate of recovery for many of our trading partners is considerably slower. Supply chain disruptions continue to create challenges moving goods around the world. Monetary policy tightening is expected to get underway this month in New Zealand, whilst other major economies are still some way off. This situation may well put upward pressure on the NZ dollar.

New Zealand's economy continues to outperform, particularly on the indicators most closely monitored by the Reserve Bank (RBNZ).

Our central bank is now expected to be the first off the blocks in terms of unwinding the emergency monetary stimulus that was delivered to stave off the negative economic consequences of COVID-19.

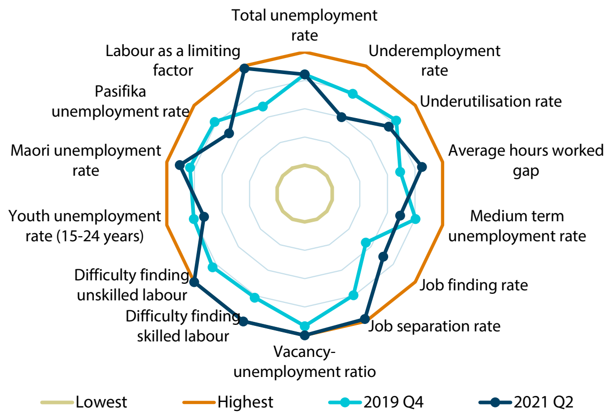
Fortunately, the economic downturn was not nearly as bad as first feared, and the stimulus measures dished out by the Government and central bank have helped send the economy into overdrive. But it's now time to bring things back onto a more even keel in the interests of longer-term stability.

NOT ENOUGH PEOPLE TO FILL JOBS

Employment measures are now above what is considered a sustainable level, which will not come as any surprise to those of you in the primary sector who have been struggling to find workers.

The unemployment rate in the June quarter fell to 4.0%, despite a small increase in the participation rate. The tight labour market is also flowing into wage pressure, with labour costs up 2.2% y/y and average hourly earnings up 4.5%.

RBNZ LABOUR MARKET INDICATORS



Source: Stats NZ, MBIE, NZIER, Macrobond, ANZ Research

Many of the labour market indicators monitored by the RBNZ (to track progress towards "maximum sustainable employment" as required by their mandate) are at their highest levels in the past 20 years. It's currently incredibly difficult to find either skilled or unskilled labour. The labour market is now tighter than it was prior to the pandemic.

The New Zealand economy is also outperforming on the RBNZ's other mandate: inflation. Inflation pressure is evident right across the economy and it can't be all attributed to short-term pandemic-related factors.

Headline inflation is expected to lift to 4.2% y/y in Q3, having already achieved 3.3% y/y in Q2. Inflation is also evident in farm operating costs. Local council rates is one area where costs are creeping up. Another is insurance. Compliance is also a new cost category for many farms as consultancy firms are often required to help provide the data required to obtain a consent, and then there are ongoing costs associated with auditing these consents. As more aspects of land use become regulated, consenting costs will only rise further.

ECONOMIC OVERVIEW

Food inflation is evident in many parts of the world. A survey by global research company Ipsos showed that 63% of respondents said they were facing higher costs for food, groceries and household supplies.

TIME TO ACT

The RBNZ can't rely on transitory factors dropping out to get inflation back down to its 1-3% target range. They need to act, and they need to act promptly in terms of reducing monetary stimulus from its extreme settings.

We now expect the RBNZ will raise the OCR in 25 basis point increments at the August, October, and November meetings this year. That will deliver 75 basis points of tightening to take the OCR back to 1.0% by year-end reversing the emergency stimulus provided when COVID hit last year. Two more hikes are also expected in H1 2022, but it's possible these won't be needed, depending on how things unfold.

GLOBAL RECOVERY SLOWER

The economic recovery in many other parts of the world is happening at a slower pace than in New Zealand. This is primarily due to the higher number of COVID cases in these countries and the responses required to limit the spread of the disease.

Hopes are currently pinned on a sharp reduction in cases as vaccination rates lift, but these new variants appear to be more infectious, and some cases are still occurring amongst those who are vaccinated. Therefore, it could be well into 2022 before the pandemic is under control.

China's economic growth remains strong but it is battling a widely seeded outbreak of COVID currently as well. Trade relationships between China and Australia remain tense and this has disrupted the flow of agricultural goods from Australia to China. Bans, or partial restrictions, have occurred for a range of products including wine, grains, meat, logs and hay.

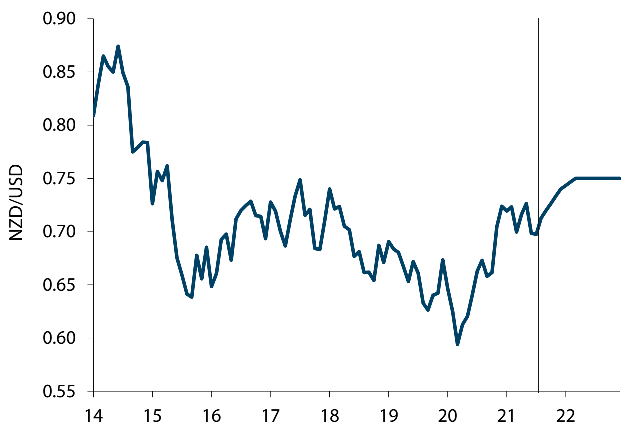
Demand from China for commodities has been extremely strong, but is now showing signs of easing for some key products. Demand for logs has slowed, although this is not unusual for this time of the year. And the recent reduction in the volume of milk powder available via the GDT platform did little to inspire buyers to act now. But if you look at the quantity of milk powder imported this year to date, it is probably a fair assumption that some of this is yet to be consumed. See the Dairy section for more details.

UPWARDS PRESSURE ON NZD

With interest rates set to lift in New Zealand well ahead of most other countries, this is likely to encourage more overseas investors to invest in funds here. This will, in turn, put upwards pressure on our exchange rate.

We expect the NZD will continue to firm, trading up to USD 0.75 by early next year. The higher NZD will curb returns at the farmgate level. That said, exchange rate forecasting is a highly uncertain business and the NZD will also be influenced by commodity prices and not least the global risk mood, which is all but impossible to predict.

NZD BUYS USD



Source: Bloomberg, ANZ Research

High shipping costs are also limiting returns back to our growers and producers. Shipping capacity is expected to remain stretched for some months yet. The quantity of goods shipped globally tends to peak in the third quarter of the year as buyers stock up for Q4 holiday spending.

Many shipping lines are trying to take a proactive approach to sorting the congestion, which means they are dropping ports from their schedules to reduce the amount of time vessels are idle. While this will help, it will also cause some short-term challenges as goods will not be able to delivered or picked up from some ports as frequently as they previously have.

But there is no doubt the shipping industry needs to try to do anything it can as it will be a long wait for more capacity to be built. It takes a long time to build a ship, and companies are wary that some of the demand is likely to be temporary.

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GLOBAL MILK SUPPLY GROWTH SLOWS

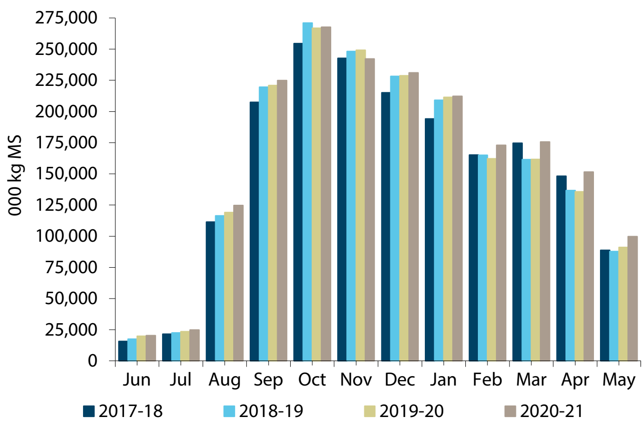
Milk supplies are still growing across the major dairy-exporting countries, but the rate of growth has slowed. Demand for dairy products has been very strong this year, but some of this is potentially related to importers building stocks to mitigate shipping delays.

Dairy commodity prices have eased but our farmgate milk price forecast of $7.70 per kg milksolid (MS) remains intact. In fact, our forecast still has room for dairy commodity prices to ease a little further, as the NZD has not lifted quite as quickly as we expected.

NZ STRONG AUTUMN PRODUCTION

New Zealand has had a strong finish to the 2020-21 milk production season, with much stronger than usual milk intakes from February to May. This resulted in 2.7% growth in milksolid production across the full season.

NZ MILK PRODUCTION



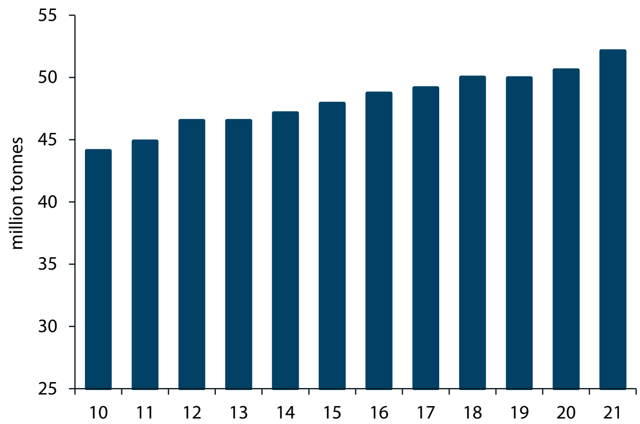
Source: Fonterra, ANZ Research

We anticipate similar production levels this season, but actual levels will depend on the weather. Over the longer term, output is expected to steadily reduce as externalities start to be priced in or limited by regulations.

US milk production is strong with 2.5% y/y growth recorded in H1 2021. In recent months this growth has been even stronger, with output up 3.2% in June and 4.7% in May. However, these figures were distorted by comparing to a lower base, as last year's milk intakes were constrained due to the COVID-19 outbreak.

US milk production for the 2021 calendar year is projected to grow at 2.2% y/y, indicating slightly slower growth in the second half of the year.

US MILK PRODUCTION JANUARY TO JUNE



Source: USDA, ANZ Research

The number of dairy cows in milk in the US is elevated, with an extra 153,000 head in milk, or 1.6% more than the same time last year. The higher stock numbers could support stronger growth, but growth in production per cow is not particularly strong at present, indicating margins between feed costs and the milk price are not supportive of increased feed rations. In fact, the milk-feed

DAIRY

ratio has trended down from 2.56 in November 2020 to 1.69 in May 2021. When returns are low US dairy farmers tend to reduce the quantity or quality of the feed.

Milk price forecasts for the remainder of 2021 have recently been revised down, which will restrict output per cow and continue to restrict growth in milk production.

Drought is also impacting the availability and cost of feed in many of the larger dairy-producing states.

Slightly more dairy product is expected to be exported from the US this year as domestic consumption eases. US dairy products are typically exported to Mexico, China and Southeast Asia. Exports to China mainly consist of whey-based products used to feed pigs.

MODEST GROWTH IN EUROPE

Europe's milk output is growing, but only modestly. Output in the first half of 2021 is up about 1% but production is back on last year in several of the major milk-producing countries, including Germany and France. The European Commissions is forecasting growth of 0.8% y/y for 2021.

More European milk is being directed into butter, skim milk powder (SMP) and cheese production, which is constraining production of whole milk powder (WMP).

Exports of dairy products from both the US and EU to China have increased this year.

AUSTRALIA'S DAIRY CONFIDENCE GROWS

Steady growth in milk production in Australia is expected this season as farmer confidence has improved. The higher milk prices over the past few seasons have improved farm profits and farmer confidence. At this stage Australian dairy farmers are not facing the environmental constraints that NZ farmers are. Dairy Australia anticipate 2% growth in the 2021-22 season, which follows growth of about 1.2% last season.

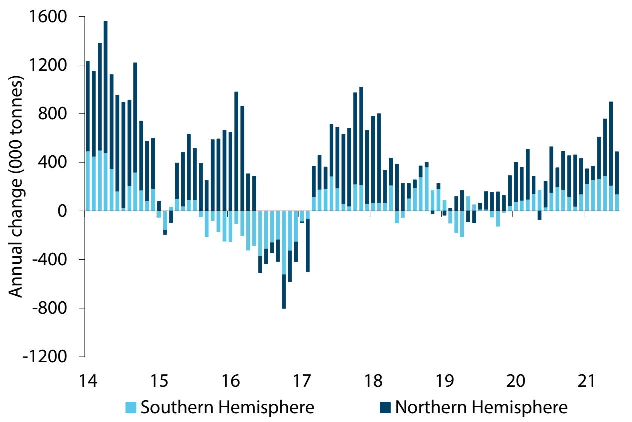
Feed prices are relatively cheap compared with milk prices, which is important given Australian dairy farmers rely more heavily on supplementary feed than NZ farmers do. There is also a surplus of hay available, as much less hay is now being exported from Australia to China following the revocation of licenses for 25 Australian hay exporters. About 10-15% of the hay produced in Australia is exported – with oaten hay being the main variety and China being the largest market for this hay. The revocation of the licenses is associated with the wider trade and political issues between Australia and China.

STRONG GROWTH IN SOUTH AMERICA

The main dairy-producing countries in South America are producing more milk. Output in the first half of 2021 increased by between 4.5% and 6% in Argentina, Uruguay and Brazil but was more constrained in Chile, where growth was under 1%.

Modest growth has also been reported for Russia. While production in the Ukraine has fallen, output from Belarus has increased. For these three countries combined, output in the first half of this year is very similar to last year.

MILK PRODUCTION – MAJOR DAIRY EXPORTING COUNTRIES



Source: DCANZ, Dairy Australia, Eurostat, USDA, CLAL, ANZ Research

FOOD SECURITY ISSUES PROMPT HOARDING

Overall we continue to expect modest growth in milk output for the remainder of 2021. This should help underpin commodity prices at or near current levels. However, one unknown is how much stock is held in the major dairy-importing countries.

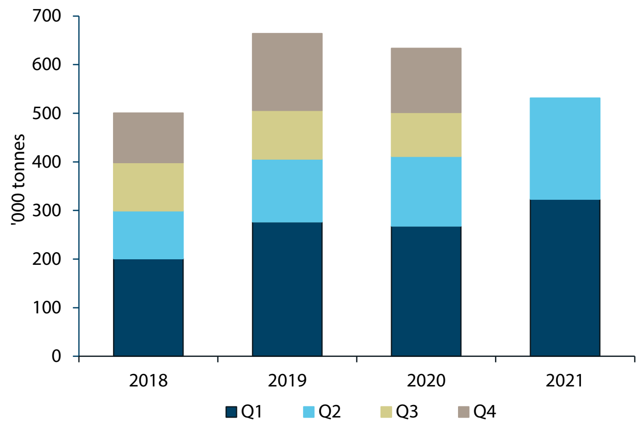
Food security issues associated with the current delays to international shipping mean importers are looking to hold additional stock. Therefore, some of the recent strength in demand may be related to the build of buffer stocks, rather than being driven by consumption.

At some point any additional buying associated with increasing stock levels will cease, and when supply chain confidence improves again we may even see a reduction in buffer stocks. These changes will be difficult to forecast so pose a potential risk to demand and therefore commodity prices.

DAIRY

China has imported 29% more whole milk powder (WMP) in the first half of 2021 than during the same time period the previous year. Imports do tend to be weighted heavily to the first few months of the year due to the lower tariffs available under the NZ-China FTA, which applies to a specific quantity of milk powder imported from NZ each year.

CHINA WHOLE MILK POWDER IMPORTS



Source: China Customs

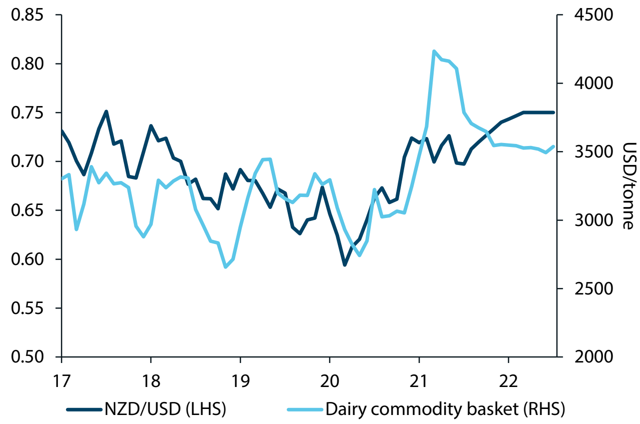
By the end of June this year China had imported more WMP than it did in the first nine months of last year. Consequently, there is a high possibility that we will see slower-than-usual demand later in the year. However, Fonterra recently announced they are seeing stronger demand than normal for contracted supply (of milk powders) and therefore have reduced the volume of milk powder that will be offered on the GlobalDairyTrade (GDT) platform.

Reducing the volume that is available on GDT is yet to prove supportive to prices, but this may change later as buyers find it difficult to source product elsewhere.

MILK PRICE FORECAST HOLDS

At this stage we are holding our milk price forecast for the 2021/22 season at $7.70/kg MS. Since we first posted this forecast there has been both a reduction in dairy commodity prices and also a reduction in the NZD/USD rate we use in our milk price forecast calculation. These two changes have basically cancelled each other out.

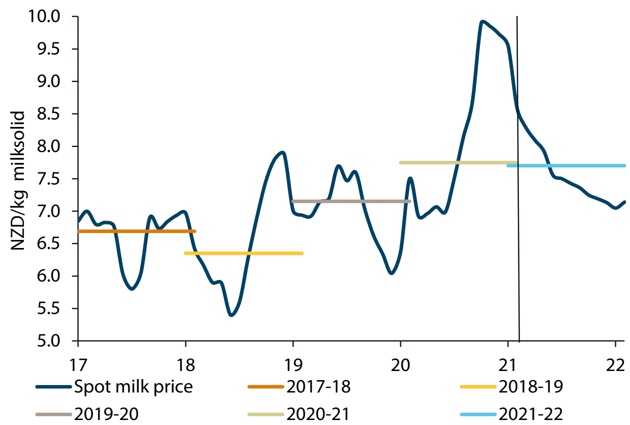
NZD VS DAIRY PRICES



Source: GDT, Bloomberg

We anticipated dairy commodity prices would ease from the elevated levels of a couple of months ago, and we built a buffer into our forecast to account for this. Prices have reduced but are still about USD200/t above the USD3600/t (weighted average) used in our forecast.

MILK PRICE – HISTORIC AND FORECAST



Source: Fonterra, NZX, ANZ Research

LAMB & WOOL

PRICES FIRMING

Lamb returns at the farmgate level are now trending up, supported by improvements in international markets and tight supply. International markets are expected to continue to improve as vaccines are rolled out.

LAMB RETURNS LIFTING

Lamb products are lifting in price in international markets, with prices of all cuts now substantially higher than they were a year ago, and well above long-run levels for most cuts.

The price of leg cuts (destined for the UK/EU markets) is about 30% above the 5-yr average, and similar increases have been seen in the price of cuts being sold to China. The exception is the price of French rack destined for European markets.

European markets remain subdued, with confidence only just starting to rebuild after the Delta variant of COVID-19 swept through the region. Vaccination rates are lifting quickly and movement restrictions are easing. But it will be some time before this region gets fully back on its feet as its economy was not in particularly good shape prior to the pandemic.

The outlook for the US, on the other hand, is looking considerably brighter with confidence levels bouncing back and restaurants starting to reopen. This has boosted demand for lamb products. That said, states with lower vaccination rates are facing the possibility of further restrictions.

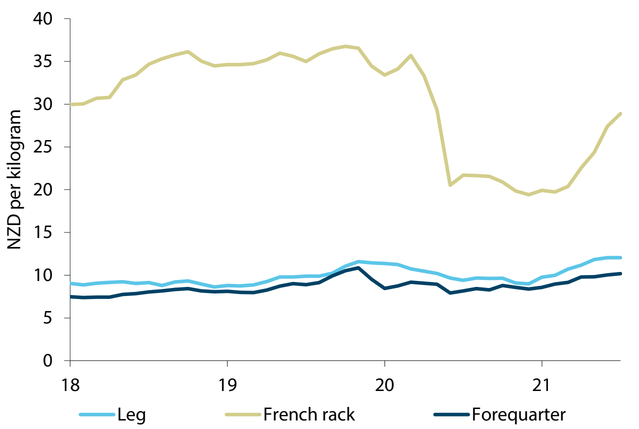
During the pandemic, marketing campaigns were directed to consumers purchasing lamb to cook at home. These messages may be responsible for the overall increase in consumer demand for lamb that we are now seeing.

The quantity of lamb being imported by the US has lifted and prices for their domestically produced lamb have also lifted. This suggests US consumers are wanting to include more lamb in their diets.

The biggest challenge with the US market is actually getting product to market, due to the ongoing shipping congestion, particularly delays in unloading ships in West Coast ports. The shipping situation is unlikely to get better any time soon given volumes going through ports typically lift in August as wholesalers start stocking up with goods for holiday season demand.

The UK market for lamb is mainly focused on domestic production at this time of the year. Prices for their new-season lambs fell sharply in June as more lamb became available, but is now starting to pick up again.

LAMB CUT PRICES

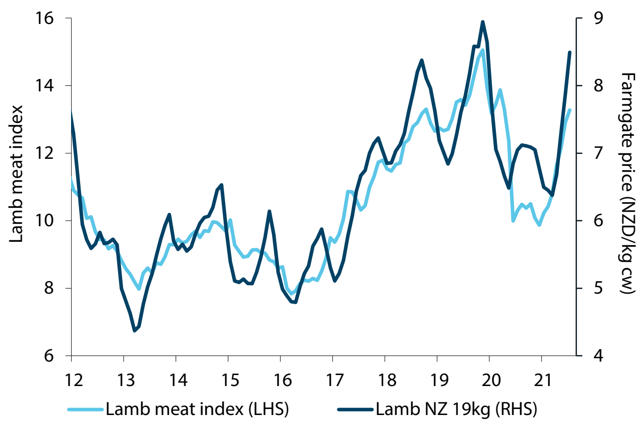


Source: AgriHQ

Strong international prices combined with strong procurement pressure have bolstered the price being paid for lambs this winter. While international prices are very strong, they don't fully justify the prices meat processors are currently paying for lambs. The procurement factor is certainly coming into play – not unusual for this time of the season.

LAMB & WOOL

FARMGATE PRICES VS INTERNATIONAL MARKET PRICES



Source: AgriHQ, ANZ Research

Schedule prices are now above $9/kg CW in the North Island and very close to this level in the South Island. The rate of increase in prices paid this winter has been extremely rapid.

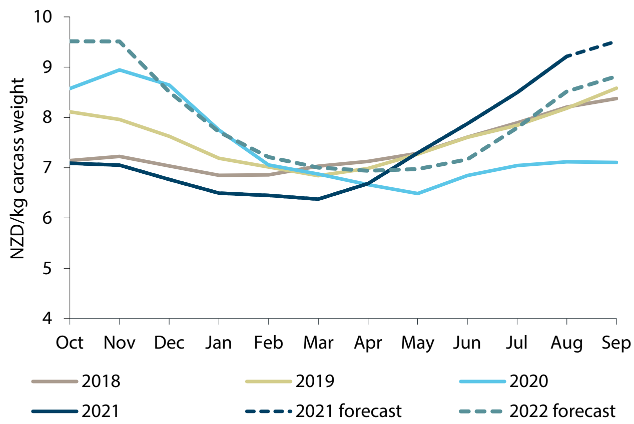
The high prices on offer for current supply mean farmers who signed supply contracts earlier in the season may not be rewarded as much as those who didn't. This does little to encourage farmers to contract supply. Minimum price contracts would certainly help alleviate this risk but then may put the processor at risk if the farmer contracts were backed by contracts with international or local buyers.

NEW SEASON LAMB UNDERPINNED BY INTERNATIONAL PRICES

Whilst we previously anticipated schedule prices would lift sharply this winter, they have moved up more rapidly than expected. We do think prices are now near peak levels and will hold near these levels. We may see a little further upside (15-20 cents) but unless we see a sharp lift in international prices then this will be purely driven by procurement pressure.

The fact that the international market is expected to gradually improve in the coming months does bode well for prices for new-season lamb. We expect prices to remain above $8/kg CW until Christmas and then ease towards $7/kg CW as higher numbers of lambs become available in the New Year.

FARMGATE LAMB PRICE TREND AND FORECAST



Source: AgriHQ, ANZ Research

STORE MARKET DEMAND EASING

While demand for finished lambs may be extremely high, there is limited appetite amongst farmers to purchase store lambs. Prices for store lambs have softened slightly in recent months, with prices now ranging from about $4.10-$4.50/kg LW in the North Island and $3.80-$4.10/kg LW in the South Island.

The feed situation has become tight in many regions, which has eroded demand for lambs. It has resulted in an increase in the supply of in-lamb ewes being offered for sale.

MUTTON AT RECORD PRICES

The price processors are paying for cull mutton grade stock, ie cull ewes, is at eye-watering levels. Pricing is around the $6.50/kg CW level. The high prices being paid by processors can be justified by the ongoing strength of Chinese demand for mutton. Virtually all of our mutton now heads to this market, which is not surprising given the price this market is prepared to pay relative to other markets.

WOOL PRICES TRENDING UP

Coarse wool prices are now trending higher after a long period languishing at extremely low levels. While the current prices are not yet high enough to really get excited about, what is exciting is the direction of travel.

At recent auctions coarse wool has traded at about $2.80/kg in the North Island, whilst prices have exceeded $3.00/kg at the recent South Island sales. Coarse wool is now worth about $1/kg more than it was a year ago and prices are now at their highest level in more than two years.

LAMB & WOOL

There has been strong demand for wool at the recent auctions with excellent clearance rates. There is nothing like rising prices, and limited supply, to get buyers engaged! We have also seen more interest from buyers from Europe and India, following a lengthy hiatus, which is providing more competition for Chinese buyers.

There won't be a lot of wool offered in the next few months as pre-lambing shearing will not be complete. The next lot of wool coming off the ewes will be from those farms that shear with lambs at foot – which tends to be the farms operating an eight month shearing regime.

We are starting to see a little more of the finer grade wools coming to the market.

STRONG WOOL (>35MM)

Source: NZWSI, PGG Wrightson, ANZ Research

BEEF

TIGHT GLOBAL SUPPLY SUPPORTS PRICES

Farmgate prices for beef are lifting sharply, supported by strong international markets and limited global supply. Farmgate prices are expected to remain supportive in the shorter term. Global supplies of beef are limited whereas global demand remains strong in a number of markets.

The quantity of beef being traded globally is relatively tight, which is helping support the markets. Strong demand for beef from a number of markets is assisting prices.

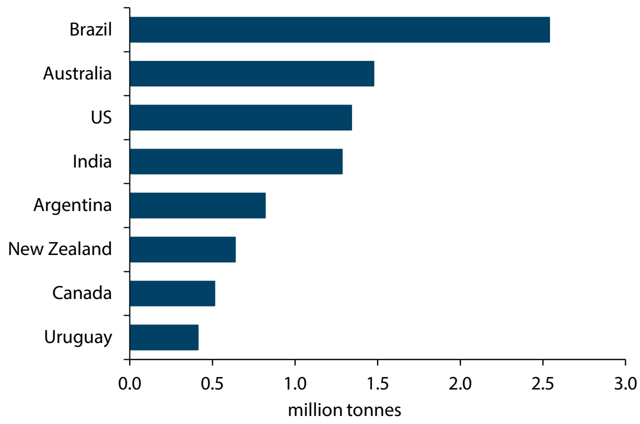
These market conditions have helped drive up the price of beef imported into the US to levels not seen since late 2019. While prices haven't gotten quite as heady as they were at that time, they are still at very healthy levels.

In recent weeks the volume of beef available in the US market has lifted substantially as widespread drought has resulted in more of their own stock being culled than normal – particularly breeding cows. This type of meat can potentially displace some of the product imported from NZ, but differing end uses means it typically just puts downward pressure on prices rather than eliminating the underlying demand.

Prices for NZ meat entering the US have eased a tad, but as our exporters don't have a lot of meat to offload at present they are not under pressure to accept low offers. There is also strong demand from other markets such as China and Canada, which will limit any potential downside in prices.

Global supply of beef is relatively limited at present. The quantity of meat being offered by Australia continues to be much less than normal as farmers look to rebuild the number of stock being run on their properties. The quantity of Australian beef entering the US is only about half of normal levels.

WORLD'S LARGEST BEEF EXPORTING COUNTRIES



Source: USDA, ANZ Research

Argentina temporarily banned exports, or at least some exports, for about a month, which also tightened up supply. A little more beef seems to be coming out of Brazil now, but overall the quantity of product available is barely keeping up with demand.

There is also less beef being exported from India, with many processing plants being closed due to COVID-19. India primarily exports buffalo meat so doesn't directly compete with offerings from NZ.

CHINA'S INSATIABLE DEMAND FOR BEEF

China's demand for beef doesn't appear to be letting up. They are gradually rebuilding their pork industry but are having ongoing challenges with further outbreaks of African Swine Fever and the measures they have put in place to manage diseases is pushing up the cost of producing pork. High feed costs are also contributing to lower returns, which may actually result in less pork being produced in the future.

BEEF

MORE US BEEF HEADING TO ASIA

Demand from Asian markets for US beef has been particularly strong recently. US exports are gradually establishing entry routes to China and this is now the third-largest market for US beef behind South Korea and Japan.

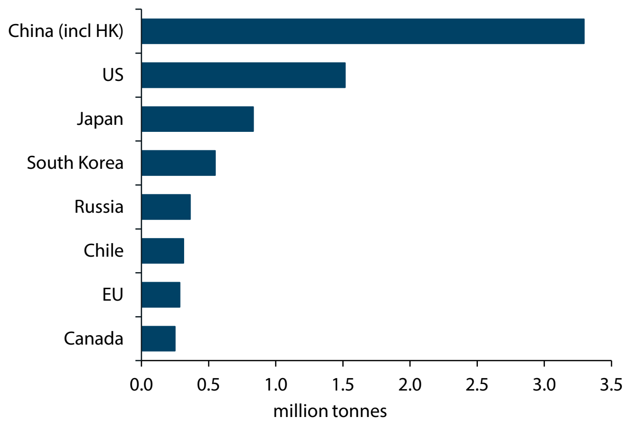
It is forecast that the US will export record volumes of beef this year. A 16% lift in volume terms is expected, following a relatively subdued year for exports in 2020. This would put exports of US beef 8% above 2018 levels – the previous record export year.

The US exports two to three times as much beef as NZ does. The US is the only country that is both a major exporter of beef and a major importer. The US imports lean manufacturing grade beef, which it blends with locally produced fatty cuts to produce hamburgers, and it exports grain-fed prime beef to the Asian markets.

New Zealand is a relatively small player in the global beef export market compared to the likes of Brazil, US and Australia. Global demand for beef is now dominated by China.

At present China is sourcing about 75% of its beef from South America. Supply from the US is rapidly ramping up, while supply from Australia remains limited due to ongoing trade tensions.

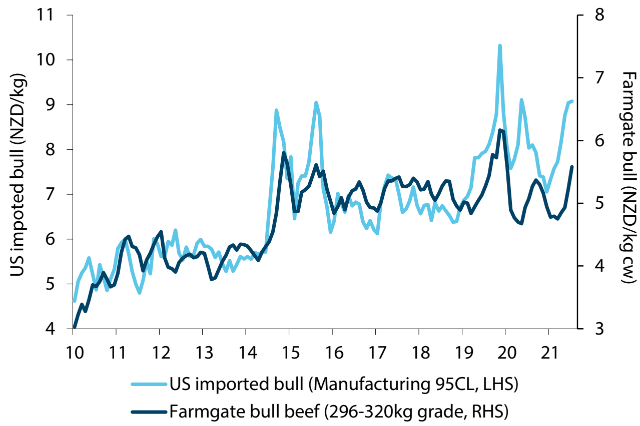
WORLD'S LARGEST BEEF IMPORTING COUNTRIES



Source: USDA, ANZ Research

NZ's beef exports are spread across a number of countries, but the lion's share goes to China and the US.

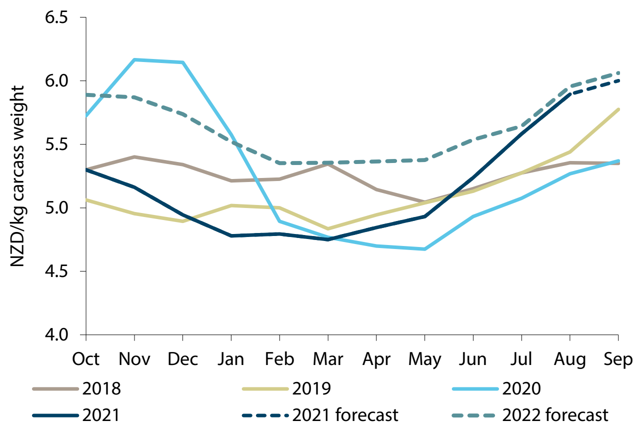
FARMGATE BULL BEEF PRICE VS OVERSEAS MARKET PRICE



Source: AgriHQ, ANZ Research

The recent strength in the international market means the latest lift in the schedule price for bull and steers to over $6 (in the North Island) is justified. Steer is actually commanding a small premium over bull at the farmgate level, which we haven't seen for some time.

FARMGATE BULL BEEF PRICE TREND AND FORECAST



Source: AgriHQ, ANZ Research

We anticipate the current strength in farmgate prices will remain intact for the next few months whilst supply is low, before easing later in the year.

DEER

TELLING THE SUSTAINABILITY STORY

Venison returns remain low, but should improve from here. Farmgate prices will lift as we move into the chilled supply season, and we are already seeing evidence of this. But returns certainly need to lift considerably further than we are likely to see this season to make farming deer for venison financially viable.

Marketers are continuing to push the environmental attributes of deer products and the traceability aspects in order to deliver more sustainable financial returns to growers. Whilst velvet returns are still strong, venison markets still have some way to go.

Venison returns have been about 30% lower in the past year than the previous 12 months. This sharp drop in revenue was due to the fact that virtually all of the end markets for venison were closed, or partially closed, due to the movement restrictions put in place to combat the spread of COVID-19.

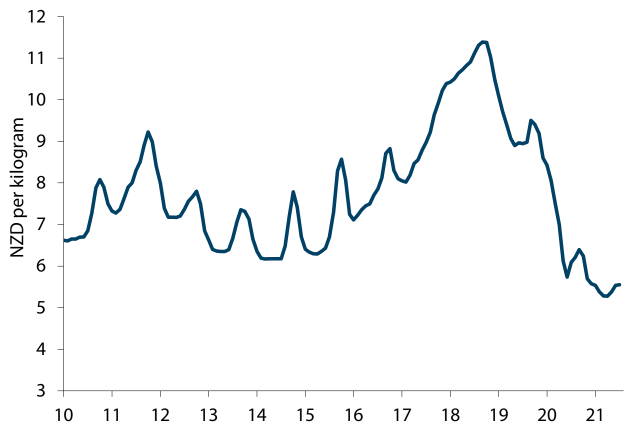
None of our other food exports are as reliant on the restaurant trade as venison. But the industry has become more innovative and has developed its direct-to-consumer and supermarket offerings.

The deer industry is probably leading the charge in terms of marketing itself as a sustainable industry. Some of our exporters have teamed up with brands that consumers buy from because they are considered sustainable, or 'regenerative' – the new buzz word.

Other exporters have developed direct-to-consumer sales channels to supply both domestic and export markets. The NZ Venison International BBQ day happens on 7th August. While the date may be more suited to Northern Hemisphere customers, no doubt some kiwis will also drag out their barbeques to support our venison farmers.

Whilst these new markets are not yet sufficiently developed to deliver strong returns at the farmgate, they are a very proactive step in the right direction to attaining higher and more stable returns.

FARMGATE VENISON PRICE (60KG STAG)



Source: AgriHQ

Unfortunately weathering a couple of years of very low returns is not easy and we are seeing some farmers reduce deer numbers in favour of other livestock classes such as sheep, particularly where they are already running a mixed operation.

This has resulted in more deer being culled, which in turn creates more pressure on markets to absorb this additional volume. Despite farmgate returns falling to their lowest level in 15 years, farmers are generally confident about the long-term future of the industry.

The number of hinds culled in the past year is a little higher than normal but industry leaders expect this trend will be relatively short-lived.

That said, the contracts on offer for the chilled season ahead certainly aren't high enough to inspire confidence just yet. Contracts are generally in the vicinity of $7 to $7.50/kg CW. That is better than the $5.50 - $5.60/kg CW currently being offered.

DEER

TRACKING PRODUCT TO MARKET

Global demand for velvet is still strong. The most challenging aspect for our exporters has been getting the product to market. Hopefully this aspect will have improved somewhat by the time export volumes lift again in the New Year.

The industry continues to work on developing end markets within China, as this is considered a massive growth opportunity. China is the largest buyer of velvet but much of this is then further processed for export to Korea. But China is not a market that can be developed overnight. It takes years of building relationships to develop a market.

The deer industry is also working hard on product traceability and recently launched the VelTrak system. Velvet is tagged on farm and then is traceable throughout the supply chain. Most, but not all, growers are registered for the new system.

Only velvet from registered farms will be able to be used in products destined for human consumption. The product from non-registered farms will be worth considerably less than product that is traceable, which will provide a real incentive for farmers to get on board with the new system.

GRAIN

FEED GRAINS LIFT

Prices for feed wheat and feed barley have firmed a little in recent months. But the price of milling wheat has eased.

Global grain supplies are expected to be relatively tight due to inclement weather in many of the major supply regions. Meanwhile global demand for grains remains robust.

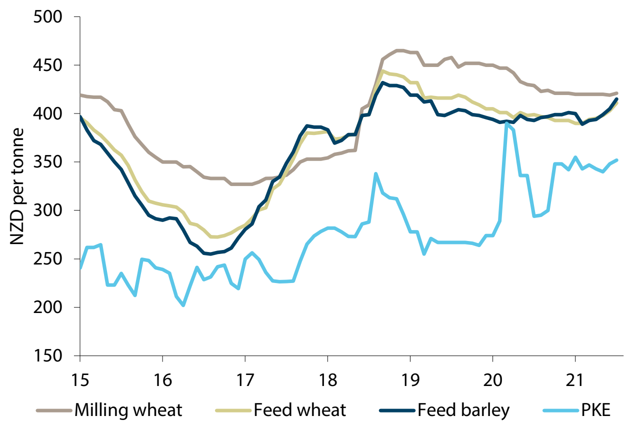
Prices for locally produced feed grains have lifted a little in recent months, but the price of milling wheat remains flat. The margin being paid for milling wheat this year is much lower than normal and also the price is less transparent due to recent changes to the procurement process.

The new procurement process has left many growers feeling disillusioned due to the lack of certainty surrounding supply contracts. This has resulted in some wheat growers opting to simply grow for the feed market as the late availability of contracts meant there wasn't sufficient certainty to take on the risk of growing a higher-value, but lower-yielding variety.

Data from the latest Arable Industry Marketing Initiative (AIMI) survey indicated a 27% reduction in the area of milling wheat sown (for harvest in 2022). The report also indicated strong demand for both feed wheat and feed barley. Unsold stocks of these grains are low, and growers are planning on dedicating more land to their crops this spring.

Feed barley continues to trade at a small premium to feed wheat. The price of imported palm kernel expeller (PKE) continues to lift, meaning it is no longer the cheap feed source it once was. This provides local grain growers with a larger opportunity to provide feed for local dairy farmers.

NZ GRAIN PRICES



Source: NZX

LOCAL MAIZE MARKET

At the beginning of June, the AIMI reported on the maize harvest at for the previous season.

Fractionally less ground is expected be planted in maize this season, with the areas planned to be planted for both maize grain and maize silage each falling by 1%.

The 2021 maize harvest produced good yields, particularly for maize silage, which lifted 4%. This partially offset the 8% reduction in area harvested, resulting in 4% lower volumes harvested. Maize grain yields were marginally lower at 11.7t/ha but more grain was produced. The total tonnage harvested was 13% higher than the previous year as 14% more land was dedicated to growing maize grain.

GRAINS

INTERNATIONAL MARKETS

Global demand for grain remains robust, but excess supplies are relatively tight this year, meaning the volume available for export is lower than normal. The volume of wheat exported from the US, Canada, Russia, and Kazakhstan is expected to be considerably lower than normal. A little more wheat is expected to be supplied by the EU and Australia, but this will not make up for the shortfall from those other major supply regions.

Wheat prices have diverged considerably depending on the supply situation in the various regions. Canadian wheat is very expensive at present while wheat from the US, Australia and Argentina is in the next price band, and product from Russia and the EU is considerably cheaper. Demand from major importing regions such as North Africa and China is expected to remain strong.

Buying from China has been driving the global barley feed market, which has firmed as they look for more supply to supplement their growing herd of pigs. This demand is also responsible for the lift in the volume of soy being imported by China. Low-grade soybeans are imported and then crushed to feed to pigs. In June, China imported more than 10 million tonnes of soybeans, having imported nearly this much in May. However, this strong demand may melt away in the second half of the year, as the price pig farmers are willing to pay for feed is not high enough to cover the cost of importing and crushing the soy. So there may be some downward pressure on soybean prices in the second half of the year.

China is also responsible for lowering the price of malting barley by banning imports from Australia late last year. This has effectively reduced the spread between Australia's malting and feed barley. At the time of the ban Australia was exporting more barley to China than the rest of the world put together.

FORESTRY

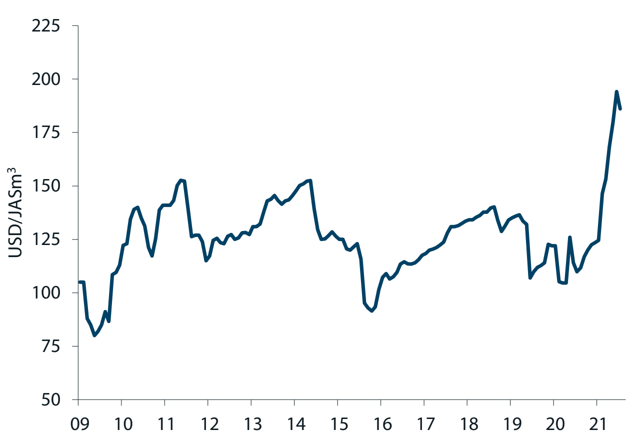
LOCAL PRICES LIFT, EXPORT PRICES FALL

The premium for exporting logs rather than selling them locally is rapidly eroding. Domestic demand for timber is strong and mills are finding they are able to pass on their higher costs. Meanwhile, after a long run of elevated prices Chinese demand for logs has waned. This is not unusual at this time of the year, but the closure of some of China's mills has further eroded short-term demand for logs. The strength of the domestic market, combined with the challenges and cost of getting product to export markets, may mean more of our home-grown timber stays on our shores.

EXPORT PRICES UNDER PRESSURE

In-market prices have eased after peaking at about USD194 per JASm^3 last month. The value of a log delivered to China is now about USD10 lower than this, and further downwards price pressure is expected.

UNPRUNED A-GRADE IN-MARKET PRICE



Source: AgriHQ

This follows nine months of elevated prices that have favoured our growers and exporters. Chinese buyers are finally pushing back on the prices being asked for by NZ exporters.

A number of factors have reduced the immediate demand for logs in China. Firstly, the quantity of logs being utilised in China tends to fall away at this time of the year as construction activity slows during the very hot summer months. This typically results in stocks of logs building on the wharves of Chinese ports. This season the quantity of logs being utilised is even lower than normal.

In Taicang (just north of Shanghai) there has been a government crackdown on the operation of timber mills. Whilst this has generally occurred under the guise of improving environmental outcomes, there is also pressure to develop some of the land currently used for mills into higher-value uses.

It has been estimated that maybe half of the milling capacity in Taicang has been shut down, and given about 20% of NZ's logs head to this port, that equates to significant reduction in overall demand.

It is not unusual in China to see Government regulatory changes result in factories being quickly shut down, but over the longer term this capacity tends to be rebuilt in other regions. At this stage it appears that the current slowdown in demand is primarily seasonal.

This explains the recent pushback from Chinese importers on the prices they are prepared to pay for logs. Whilst buyers may be pulling the shots now, the lack of global supply of export logs means the balance of power may swing back to our exporters relatively quickly. Despite the recent fall, returns for logs are still exceptionally high.

China's main suppliers of logs are NZ, Russia, and Europe but it also buys smaller volumes of logs from North America (Pacific North-West region) and South America (mainly Uruguay). Supply from most of these regions is expected to be constrained.

FORESTRY

Russia announced some time back that it was banning the export of raw logs to China but these regulations are yet to take effect. Russia wants to support its own domestic milling industry and would rather export sawn timber than logs. Its lumber exports to China have been falling in recent years as China has been importing more logs and less lumber. Russia has also been supplying a smaller portion of China's lumber imports.

Similarly, there are growing concerns from European mills that the large quantity of logs being exported to China will undermine their ability to secure supply. The export of logs from Eastern Europe to China really cranked up when vast tracts of forest were being felled to stop the spread of bark beetle. There was insufficient local demand, meaning if the logs weren't exported to China they would simply have rotted where they lay.

China's relationship with Australia remains strained, meaning we are unlikely to see any significant lift in logs being sourced from Australia. At present, Australia is exporting logs to alternative markets such as Korea and India. Likewise, logs from Uruguay are helping fill demand from India, but the prices on offer from the market in recent months have not matched those of China.

Meanwhile supplies of logs from North America have been very tight in the past six months due to strong demand within the US for timber to build, expand, and remodel homes. Spending additional time at home during lockdowns has prompted this demand. However, that demand is now easing as funds are being directed into other uses, and the supply of lumber has improved. This has resulted in a dramatic plunge in US lumber prices, which had risen at an exorbitant rate in the past year.

US LUMBER FUTURES

Source: NRCan. Macrobond

Whether we will see a significant lift in the volume of logs available for export from the North America remains unclear.

So overall there is not a lot of additional supply that China can call on when its demand for logs lifts again later in the year. Therefore, the lack of supply is likely to limit the fall in market prices. But it is unlikely the prices received recently will prove to be sustainable over the longer term.

WHARF-GATE RETURNS FALLING

Returns at the wharf-gate in NZ are also under pressure from increased shipping costs. Delays getting ships loaded and unloaded at ports are pushing up the cost of transporting logs as the time they are idle needs to be paid for by someone. Up to now, strong demand and rising prices were somewhat masking the additional shipping costs as wharf-gate returns were still rising.

Even at many of our smaller ports, like Gisborne, there have been reports of ships waiting a month to get loaded. Until the shipping industry can operate in a more efficient manner these costs are going to continue to be absorbed by both sellers and buyers of logs. The forestry industry has been lucky enough to have been selling products into a firm market, so importers have borne a large portion of the cost. But exporters have also been faced with higher costs.

LOCAL PRICES LIFTING

Domestic supply of logs to mills tends to be done on a contract basis, so when prices move sharply it can be a few months before domestic contract prices are adjusted. Recently, we have seen an upward adjustment in the prices being paid for logs by local mills. This upward adjustment, combined with the recent weakening of the export market and the shipping challenges, will make it more attractive to supply local mills.

Local mills are finding they have been able to pass on the higher costs to timber buyers. Unfortunately, this is making building and renovating houses more expensive, but so far consumers seem willing to pay these higher costs. Many projects would have already been underway before the cost of materials lifted, and therefore would have found it difficult to stop their build part-way through.

NZ has a severe shortage of houses – an issue which consecutive governments have acknowledged but failed to fix. Whether it be the Government or the private sector that funds the homes that are required it will be a costly exercise.

HORTICULTURE

EXPORT RETURNS SLIP ON LOWER VOLUMES

Export earnings from the horticultural sector have generally slipped this year, primarily due to lower export volumes. This is due to inclement weather impacting yields, and labour shortages further reducing harvest volumes. As yet there is little evidence that the lower export volumes will be offset by higher prices.

Horticultural businesses that employ RSE workers will be relieved by the recent Government announcement that workers from Vanuatu, Samoa, and Tonga will not be required to quarantine when entering NZ.

How exactly this will work is yet to be figured out, but it will reduce one of the complications of sourcing RSE labourers. Approximately 75% of RSE workers come from Vanuatu, Samoa and Tonga. These islands have had minimal (or nil) cases of COVID-19, so this is logical decision. Why it has taken so long for this decision to be made is still not clear.

This policy change certainly won't fix the labour shortage but it will alleviate some of the complications of getting workers into New Zealand.

KIWIFRUIT: CHARTER SHIPS PAY OFF

Zespri has reported strong market demand for kiwifruit this year. This will be welcome news to growers who have faced a challenging season – particularly on the labour front. The lack of available workers has put both physical and mental strain on growers this season – particularly during harvest. The industry from the orchard to the pack-houses has been very constrained by labour shortages.

The focus for growers will now be on winter pruning.

Zespri are well through exporting the current season crop. Smaller count-size fruit has again been rejected so that the fruit exported is best matched with buyer expectations.

There was a slower start to the export season than last year but export returns for SunGold are now ahead of last season. China and Europe have been the standout markets thus far with returns from Japan not matching the strong level attained last year.

June was a record month for the volume of kiwifruit exported from NZ. As at mid-July about 55% of SunGold fruit had reached market and 34% of the Green fruit harvested has been delivered.

Zespri has experienced fewer challenges getting product to market than many other industries due to chartering ships to carry a large proportion of produce to market. However, it does still rely on moving some of its fruit via container ships, particularly when servicing its smaller markets. Therefore it is still experiencing some issues with deliveries but not to the extent that other exporters have.

Demand for land for greenfield development and demand for existing kiwifruit orchards is still really strong despite some uncertainty surrounding future returns. It remains to be seen if Zespri can retain the premiums it is currently achieving for Zespri SunGold fruit as more gold fruit becomes available, including that from the unlicensed plantings of Zespri Gold in China.

Zespri is paying its shareholders a final dividend for the 2020-21 season of 27c per share on 13 August, which brings the total dividend for the 2020-21 season to 133c per share. It will also pay an interim dividend for the 2021-22 season of 144c per share, also on 13 August. This dividend payment will distribute most of the funds generated from the recent sale of Gold3 and Red19 licenses. Further dividends are expected to be paid in December 2021 and August 2022 relating to the 2021-22 season.

HORTICULTURE

WINE: INDUSTRY CONSOLIDATION

With the harvest now well in the rear-mirror, vineyard owners are busy preparing vineyards for the new season.

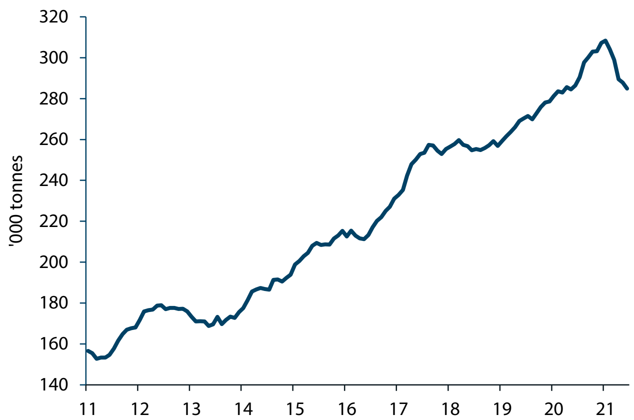
Meanwhile wine sellers are working hard to maximise returns from the latest harvest. The 2021 harvest may have lacked in quantity but has made up for this in quality terms.

Wine export returns have been weak so far this year with export revenue generated thus far related primarily to last season's harvest. Up until this year export returns for wine have continuously grown over the past decade as a result of both higher volumes and improved returns. Export returns typically lift from July onwards as sales from the new vintage start to flow through.

The volume of wine exported during the first half of 2021 is considerably lower than normal. Exports volumes this year are aligned with the levels of 2018 and are about 20% lower than last year.

Prices being attained for wine have eased in some of our higher-priced markets such as the United States and Canada but have lifted in some other markets, meaning there has been little change in overall prices. The lower export returns are primarily been driven by smaller quantities of wine being exported.

WINE EXPORT VARIETY ITEMS (12 MONTH ROLLING AVERAGE)



Source: Statistics NZ

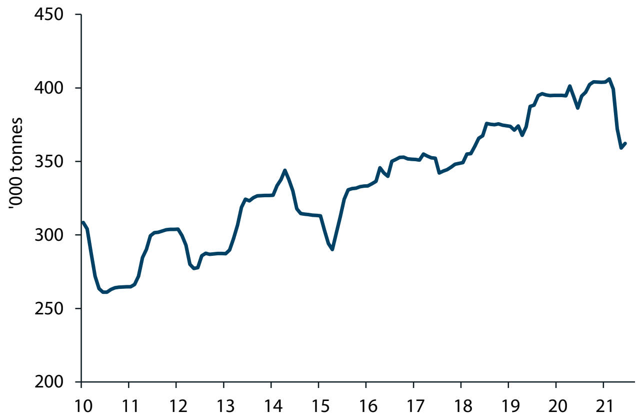
We have seen some consolidation in the NZ wine industry. A conditional agreement has recently been signed by Indevin, NZ's largest contact winemaker, to buy Villa Maria. The sale is expected to be completed by the end of August. Villa Maria has been looking for ways to raise capital since last year before its parent company was placed in receivership in May.

APPLES: ILLEGAL APPLE PLANTINGS IN CHINA

Apple exports have suffered this year, and like wine, export returns are back down to 2018 levels. Again this is primarily a volume story as considerably fewer apples were harvested this year due to both lower yields and labour constraints.

The focus on only harvesting the higher-value varieties of apples should, in theory, result in higher average export prices, but we are yet to see evidence of this.

APPLE EXPORT VOLUMES (12 MONTH ROLLING AVERAGE)



Source: Statistics NZ

It also appears the kiwifruit industry is not alone in its challenges with illegal plantings of licensed varieties. Significant plantings of the PremA280 variety of apple have been found in China. A license was previously granted for a Chinese company to grow this variety in China, but that company has discovered that many Chinese orchards are already producing this variety of apple. Action is being taken to try to control this issue but it won't be easy to achieve given how widespread plantings are already thought to be.

RURAL PROPERTY MARKET

HEATING UP

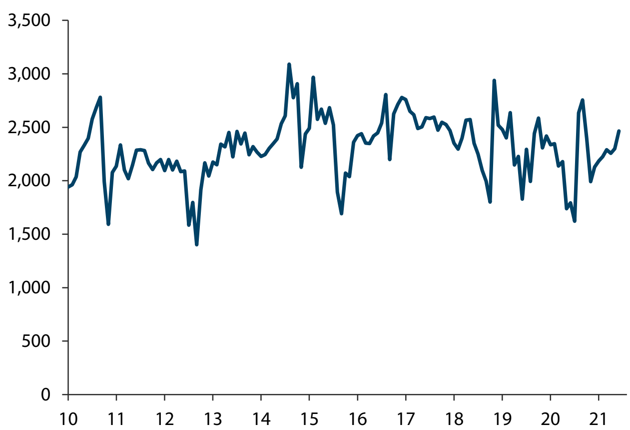
The rural property market is starting to heat up with an increased number of farms changing hands. This is being prompted by improved returns in some sectors and some land-use change opportunities. There are also a number of vendors looking to exit the market ahead of impeding regulatory changes.

MORE FARMS SELLING

The number of farms sold in the past year is well above the 10-year average. This trend is present in all of the major sectors, with arable being the only exception. Median sales prices have also lifted in all sectors when measured on a per hectare basis.

In June the Farm Price Indices compiled by the REINZ lifted for both dairy farms and all farms.

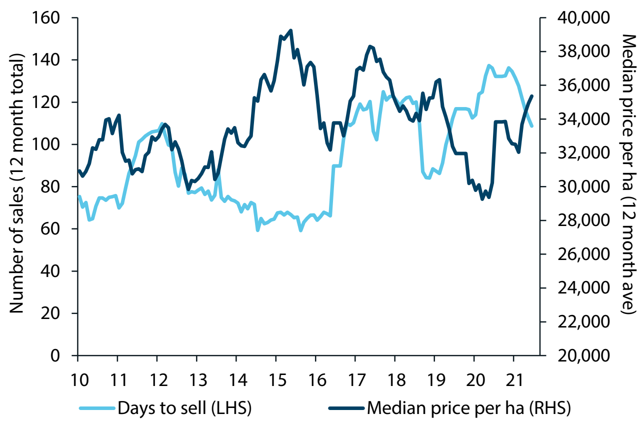
DAIRY PRICE INDEX



Source: REINZ

The renewed enthusiasm for investing in dairy farms is evident in the reduction in the number of days it is taking to sell a dairy farm. This has been consistently above 100 days for the past couple of years but is now easing.

DAIRY FARM SALES (12 MONTH ROLLING AVERAGE)



Source: Statistics NZ

LAND FOR CARBON FARMING IN DEMAND

Land continues to be sought after to plant in pine trees in order to provide carbon returns. Returns from this land use are looking even more attractive as the carbon price trends towards $50 per New Zealand Unit (NZU). Where carbon prices head from here will be highly dependent on any future regulatory changes.

There is a fear, amongst both farmers and regulators, that a high carbon price will entice too much land-use change towards forestry. Whilst this would provide a strong return for land owners in the medium term, and help the Government meet its climate change obligations, it could be detrimental in the longer term. For more details please refer to NZ Insight: Carbon markets 101.

REINZ data shows forestry land changed hands at an average median price of $10,751 per hectare in the past year. Data from other sources shows a large variety in prices being paid for farmland on the East Cost of the North Island to plant in trees. Prices are ranging from as little as $3,500/ha up to about $15,000/ha.

RURAL PROPERTY MARKET

LIVESTOCK PROPERTIES

Over 1,000 livestock properties have changed hands over the past year. The median sales price lifted to $20,450/ha in the past 12 months, compared to $18,050/ha in the prior year.

Favourable returns for lamb and cattle have bolstered confidence in the industry. There has also been some land-use change from dairy farming to grazing properties in the past year, as farmers look for less-intensive land uses ahead of regulations intensifying.

HORTICULTURAL LAND

Demand for land already used for horticulture, as well as suitable for converting to horticultural use, remains high.

In the past 12 months 191 horticultural properties have changed hands at a median price of $307,883/ha. That is 60% higher than the 10-year average. The large lift is influenced by the type of properties being sold, with highly priced kiwifruit orchards pushing up median values.

FARM SALES BY FARM TYPE

Annual average/total		Past 12 months	Previous 12 months	10-Year Avg.	Chg. Y/Y	Chg. P/10yr
Dairy	Number of Sales	252	104	210	↑	↑
	Median Price ($ per ha)	35,360	30,229	33,907	↑	↑
Livestock	Number of Sales	1,049	692	995	↑	↑
	Median Price ($ per ha)	20,450	18,050	17,893	↑	↑
Horticulture	Number of Sales	191	140	183	↑	↑
	Median Price ($ per ha)	307,833	223,364	192,324	↑	↑
Arable	Number of Sales	57	82	95	↓	↓
	Median Price ($ per ha)	36,929	23,333	35,543	↑	↑
Forestry	Number of Sales	57	52	51	↑	↑
	Median Price ($ per ha)	10,751	9,076	7,485	↑	↑
All Farms	Number of Sales	1,726	1,152	1,551	↑	↑
	Median Price ($ per ha)	26,292	23,117	24,023	↑	↑

Source: REINZ

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Last updated: 9 April 2021

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