ANZ RESEARCH

AGRI FOCUS

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IT'S RAINING, IT'S POURING

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INSIDE

Economic overview 1

Dairy 3

Lamb & wool 5

Beef 7

Deer 9

Grain 11

Forestry 13

Horticulture 16

Rural property market 18

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Wet conditions prevail across most of New Zealand, which has made it very difficult for wintering stock as soils are saturated. Some regions have received more rain in the past month than they have all year.

Delays getting stock to processors also mean some farms are carrying more stock than normal for this time of the season. The labour shortages that meat processors have been faced with mean we may need to reconsider our heavy reliance on being able to get space at processors when desired with little notice. More forward planning, including supply contracts, could be beneficial for all parts of the supply chain.

The upside of the recent heavy rains is that irrigation dams have filled up nicely, which will be beneficial later in the year.

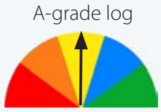
Commodity prices remain elevated, but the heat has come out of some markets recently as demand continues to be disrupted. Lockdowns in China have had an impact, as have tightening economic conditions in most markets.

Within New Zealand, the flood of regulatory change shows no sign of letting up. While there is widespread support for the intent of many of these rules, the practicality of implementing rules and unintended consequences remain a key concern for many.

Recently the Climate Change Commission has recommended sharp upward changes in pricing guidelines for carbon credits released in the quarterly government auctions, and have advised they don't support including sequestration within the He Waka Eke Noa framework.

What is very clear is that we still have some way to go in terms of regulatory change, and consents will be something most landowners will need to get used to.

Prices at farm/orchard level relative to 10yr average

Dairy	Dairy commodity prices are trending down but we continue to hold our milk price forecast at $8.50/ kg MS for the current season.	Milk price Low  High
Sheep	Lamb returns at the farmgate level have trended up a little but the number of lambs currently being processed is extremely low.	19kg lamb Low  High
Beef	Demand from the US market for our beef is currently weak but demand from China has improved, so most of the beef being exported is heading to Asian markets.	Prime steer Low  High
Forestry	Log returns have been buoyed by lower shipping costs while in-market prices hold steady. Meanwhile carbon prices continue to firm as emissions rules evolve.	A-grade log Low  High

ECONOMIC OVERVIEW

GLOBAL ECONOMIC CONDITIONS TIGHTEN

Global economic growth is slowing. China is battling high unemployment levels and ongoing challenges as it tries to control COVID. In many western nations economic growth is being negatively affected by efforts from their respective central banks to rein in inflation. Energy and food prices are both very high at present, although the price of many of the foods we export is starting to ease. The lower prices are largely driven by lower demand as supply remains tight for most foods we export.

There are still major challenges getting goods to market due to ongoing issues in the container shipping industry. Prices for goods shipped in bulk have eased a little, which is benefitting our forestry industry.

OCR EXPECTED TO REACH 4%

We expect the Reserve Bank of New Zealand (RBNZ) will lift the Official Cash Rate (OCR) to 4% by the end of the year. At present the OCR sits at 3%; we are expecting two further 50bp lifts.

A year ago the OCR was at just 0.25%. This increase over the past 12 months to 3% has been the quickest monetary policy tightening experienced in New Zealand. The battle against inflation is not an easy one, but one that the RBNZ must face head-on.

New Zealand is not alone in facing inflationary challenges; in fact prices have been rising at a similar pace in most developed economies. A common story is that supply chains have not been able to keep up with demand throughout the pandemic and therefore prices have risen sharply. Demand for goods received a massive boost from the fiscal and monetary policy stimulus packages delivered to offset the economic impact of COVID. But in many cases the economic impact was not as bad as was first feared and therefore the stimulus simply caused excess demand at a time when supply chains were limited in their ability to respond.

DAMPENING DOWN DEMAND

The purpose of tightening monetary policy is to subdue demand, and there are now signs that this is starting to happen.

Unfortunately this does mean that demand for our export products is not likely to be quite as robust as it has been recently, and this means we are likely to see prices ease somewhat. However, at this point we are not seeing any significant recovery in supply growth globally within any of our major export sectors. This will limit how far prices will deteriorate.

Costs of production are rising rapidly, which means on-farm profits will be squeezed as incomes fall and costs rise.

BIOSECURITY POSES RISK TO TRADE

Foot and Mouth Disease (FMD) has always been a risk to our agricultural sector. Recently the awareness of the risk of an outbreak of FMD has heightened due to the presence of the outbreak in Indonesia and the recent detection of disease fragments in Australia. While this is certainly not a new risk to our agricultural sector, the appearance of the disease uncomfortably 'close to home' is not good news.

The Government is well positioned to respond to this risk as they have plans in place and have good knowledge of how to try to control the disease. Should there be an outbreak in New Zealand, we could expect to see a much quicker response from authorities than we did with the M.Bovis outbreak.

ECONOMIC OVERVIEW

One major risk we have is that most of our trade agreements are conditional on New Zealand being free of FMD. That means in the event of an outbreak, exports would be severely disrupted and trade agreements would need to be renegotiated before exports could resume. This would cause considerable logistical and financial challenges for our agricultural sector.

While movement restrictions for livestock may be limited to just the region where an outbreak occurs, the trade challenges would impact our entire meat and dairy supply chains.

Biosecurity risks are a major threat to our agricultural sector, so we need to be vigilant in mitigating these risks by implementing good on-farm practices to protect our own businesses.

Click here to access our latest forecasts.

DAIRY

DOWN BUT NOT OUT

Global dairy prices have softened considerably in the past couple of months. This has clearly been driven by weaker demand, as we are not seeing growth in global milk supply.

Deteriorating economic conditions, combined with subdued demand from China, has led to softer prices for dairy products. It is not unusual to see some weakening in prices at this time of the season as the volume of product available from New Zealand starts to lift.

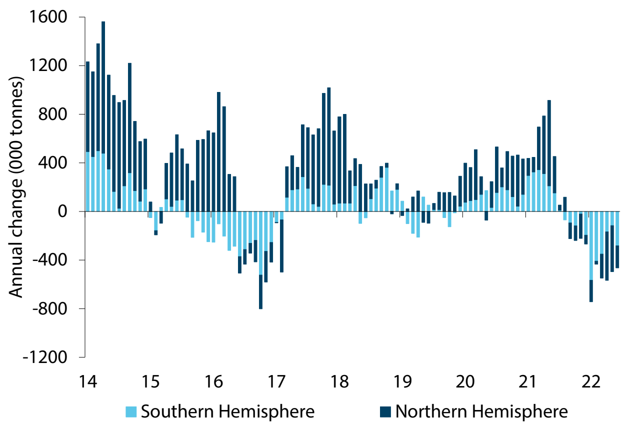
At this time of the season, New Zealand exporters are forward selling for the season ahead. Milk production in New Zealand increases sharply from August to October as cows come back into milk following calving. This places pressure on exporters to secure forward sales, which can be challenging when demand is subdued.

At present there are plenty of buyers for New Zealand dairy ingredients, but not all can pay the extremely high prices that have recently prevailed. As prices ease, the pool of buyers will potentially increase further, which will help to offset reduced demand from China.

China's demand for dairy is a little subdued at present as the lockdowns have taken their toll on opportunities to dine out (including visiting bakeries), and – in some cases – has severely impacted the financial position and confidence of consumers.

The main factor that will stop dairy commodity prices slipping too far is the lack of growth in global milk supply. The data available for the main dairy-exporting countries certainly backs this up (see figure below).

MILK PRODUCTION IN THE MAJOR DAIRY EXPORTING COUNTRIES



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

Demand for imported dairy products is also impacted by the amount of milk produced within some of the large dairy-importing countries. China, for instance, produces about 1.5x as much milk as New Zealand does, so any change in their domestic milk supply has the potential to alter their demand for imported product.

Recently there has been talk about China increasing its milk production quite dramatically, but it is difficult to rely on the data as it tends to focus on the large-scale milk producers and there is little information available on the small-scale producers.

For many years we have seen small-scale dairy farmers in China (often milking fewer than 10 cows) give up dairying, while the number of large-scale farms (who milk 5,000 cows or more) increases. Milk production data is typically only measured for the large-scale operators, so may overstate growth in production.

DAIRY

MODEST GROWTH IN THE US

Milk production in the US is expected to expand modestly over the next 12 months. The number of dairy cows in the US has dropped by 50,000 per head (or 1%) over the past year, and replacement stock has fallen by a similar amount. The lack of stock combined with high prices for feed will limit the growth of milk production in the US over the next 12 months.

Milk supply in the US in 2023 is currently expected to expand by 1.5%, following a year in which growth came to a standstill. The expected growth next season is relatively modest, and high feed prices could make even this amount of growth difficult to achieve.

In Europe, milk supplies during the first five months of 2022 fell by 0.8% across the EU, with output in most of the major dairy-producing nations contracting. Poland was one of the exceptions, recording growth of 1.9%.

Exports of virtually all dairy products from the EU have decreased this year. This is particularly the case for whole milk powder. When milk production is low there tends to be less milk available for milk powder production, and the high cost of drying milk (due to the high energy costs in Europe) is increasingly also a limiting factor.

FARMGATE MILK PRICE

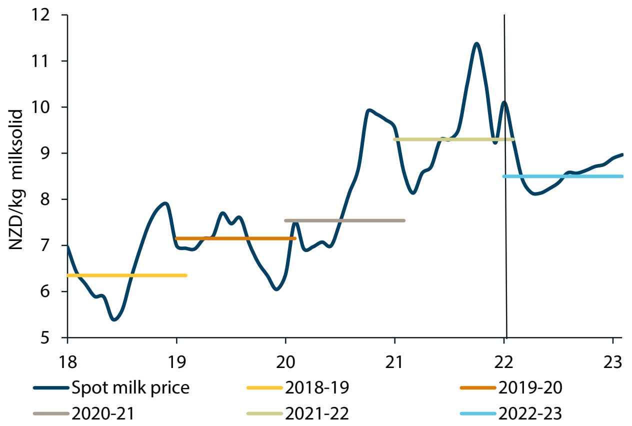
There has been a notable rise in farm operating costs, particularly fertiliser, labour, feed and fuel. Finance costs have also lifted sharply, meaning those dairy farms who have made extra debt repayments over the past couple of years are unlikely to be regretting that decision. It is likely that the quantity of debt repaid in the season ahead will be considerably lower than last season, but this will depend on where the milk price ends up, and it is still very early in the season.

Global dairy markets have eased over the past couple of months, but this has not impacted our forecast farmgate milk price as a fall in global commodity prices was anticipated.

Our milk production forecast for the 2022-23 season remains at $8.50/kg milksolid (MS). While this figure still looks relatively high in an historic sense, the cost of production is fast approaching this level.

The latest survey of dairy farmers in the Waikato/Bay of Plenty region by consultancy firm Ag First puts the breakeven price for dairy farms at $8.44 (allowing for drawings and debt repayments).

FARMGATE MILK PRICE HISTORIC AND FORECAST

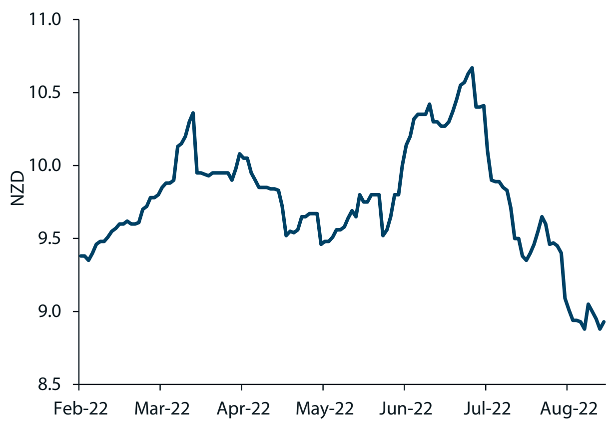


Source: Fonterra, ANZ Research

Our $8.50/kg MS forecast assumes dairy commodity prices will be, on average, just slightly below current prices across the season. This forecast is currently below the lower end of the forecast range of $8.75 - $10.25/kg MS provided by Fonterra at the end of June.

Milk price futures for the 2022-23 season peaked at $10.67 at the beginning of July but have recently been trading below $9.

MILK PRICE FUTURES 2023 CONTRACT



Source: NZX, Bloomberg

LAMB & WOOL

PROCESSING BACKLOG

Lamb processing is running well behind normal due to labour issues curbing meat-processing capacity. This means there are still more old-season lambs on farm as the new lambing season gets underway.

Lambing is well underway (at least in the warmer regions) and the extremely wet conditions are proving challenging in many regions. Snowfalls have also been heavy, but most of the farms at higher altitude won't have commenced lambing just yet.

Also proving challenging is trying to get killing space for last season's lambs. Capacity at the processors has been severely curtailed throughout the season by labour shortages. Now many processing lines have switched over to bobby calves, which means there is even less space available for lambs.

The bobby kill has been elevated this season as there is limited interest from rearers (see Beef section for more details). This means even less space available for lambs as processors concentrate on calves.

Many farms are now having to cope with still having some of last season's lambs on farm as the new lambing season commences. Muddy paddocks are making it very difficult to deliver lambs to processors in clean condition, which has also kept some lambs on farm.

Available feed tends to tighten up at this time of the year and the recent flooding has further impacted feed availability. This will be a bigger problem on farms that have not been able to get lambs to processors in a timely manner.

CAPTURING MORE VALUE

Farmers have become used to being able to easily get space for processing stock without a great deal of notice. But this flexibility is a luxury that simply wasn't available this season. It may mean both farmers and processors start to place more value on having supply contracts that are mutually beneficial. There will always need to be a spot market for processing stock, but this should probably be the exception rather than the norm.

Looking to the future, supply contracts will become even more important as we try to match on-farm practices and consumer preferences. At the moment, a small portion of our lamb is supplied on these types of contracts, but this should grow in the future if we want to capture the additional value relating to 'how we farm'.

SOME PRESSURE ON INTERNATIONAL MARKETS

Export markets for lamb are starting to feel the pressures of policy designed to dampen down inflation. To reduce inflation, demand needs to ease, and this does mean we expect to see some reduction in demand for our export products – particularly more high-end products such as meat destined for the restaurant trade.

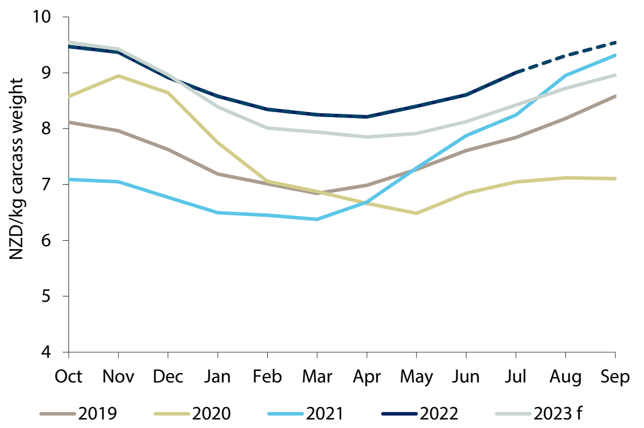
At this time of the season there isn't that much product to sell, but even with low volumes we are starting to see a little bit of pressure on international prices. Prices are expected to come under more pressure later in the season when our export volumes lift.

RETURNS STILL STRONG AT FARMGATE LEVEL

Despite in-market prices starting to ease, schedule prices for lamb and mutton continue to creep up. But these prices are only relevant if you can actually get processing space for your lambs. The range of prices being offered by various companies is also opening up a little, but overall throughput is very low so current prices don't have a significant impact for most farmers.

LAMB & WOOL

FARMGATE LAMB PRICE TREND AND FORECAST



Source: AgriHQ, ANZ Research

Returns are expected to remain firm until a significant volume of new-season lambs become available. Last season schedule prices were very flat, but this year we would expect to see prices drop by a greater amount after Christmas, and a more typical price curve prevail.

At this point, it looks like the lamb schedule should be about $8/kg CW during the peak of the season, but this will be very dependent on how market demand reacts to the deteriorating economic conditions. There are definite downside risks to this forecast.

WOOL RETURNS REMAIN LOW

Wool prices have slipped a little at the auctions held over the past couple of months. Prices are currently just below where they were this time last year.

Prices did firm slightly at the latest North Island sales where returns were supported by lower offer volumes.

Demand from China for wool has been disrupted by the recent lockdowns, which have impacted port throughput. China is the largest market for New Zealand wool and it is a particularly significant market for our lower-grade wools.

Sales of fine wool are non-existent at this time of the season as high country farms don't shear in winter.

Demand for high-end wools may also be negatively impacted by economic conditions deteriorating in some of our major end-user markets such as Europe.

URGENCY TO MOVE HEAVY CATTLE OFF FARM

Global beef demand is steady, but the lack of demand from US importers is resulting in more New Zealand beef being sold into Asian markets.

Pricing has softened a little due to the reduced competitive pressures from US buyers, but there is sufficient demand to absorb the relatively low volumes of beef being exported from New Zealand at present.

Processing backlogs are starting to clear, but many farmers have had to winter more heavy cattle than they would have preferred, given the wet conditions underfoot.

MORE CATTLE CULLED DUE TO DROUGHT IN US

Demand from the US for imported beef remains subdued due to the abundance of local beef. The cow kill (beef cattle) is elevated as US farmers offload stock due to the severe drought.

This has resulted in the quantity of beef in US cold storage lifting 29% y/y to record levels. The quantity of pork and lamb in storage is also elevated, meaning there is limited demand for importing more beef.

Luckily this drop in demand from the US has coincided with the seasonal drop in beef production in New Zealand. The additional supply within the US is expected to drop away before the end of the year, which is good timing, as supply from New Zealand will remain relatively light until summer.

The quantity of beef being processed in New Zealand is a little higher than normal as the tail end of the backlog that built up during the autumn is really only being cleared now. The extremely wet conditions are also encouraging farmers to move some stock, as they are likely to be in a feed deficit situation for some time yet and heavy cattle can do some serious damage to pastures when soil is as wet as it is currently.

COMPETITION STRONG IN ASIAN MARKETS

Brazil continues to dominate exports of beef into China, with volumes continuing to grow year-on-year. Meanwhile the US is exporting more beef to Korea and Japan. Exports from Australia have started to lift in recent months but are still well below the 5-year average. Beef exports from Australia have been subdued for the past few years as farms restock following the damage caused by the droughts, fires and floods that occurred a couple of years ago.

Demand from Korea and Japan remains steady for prime beef cuts as well as trimmings.

CHINA DEMAND HOLDING UP

Demand from China for New Zealand beef remains robust despite the recent lockdowns. Chinese importers will continue to build up stocks leading up to Chinese New Year, which should keep demand from this market steady for the next few months. This market is certainly providing greater returns than the US market at present. however, the pricing is not quite as strong as it was earlier in the season.

Having two large markets for beef has been very favourable for exporters, as when demand has dropped off in either the US or China, demand from the other market has tended to be pretty robust. This means we have enjoyed relatively stable returns for our export beef for the past few years.

FOOT AND MOUTH DISEASE RISK RISES

The number of stock being culled in Australia is expected to rise as some risk-adverse farmers opt to cull cattle now.

BEEF

An outbreak of Foot and Mouth Disease (FMD) would cause severe disruptions to stock movements and market access. Therefore, some farmers are opting to cull stock early to lower their exposure to an outbreak of FMD.

The chance of a FMD outbreak occurring in Australia is assessed at 10%, which is a reasonably high risk. Now that FMD is rampant in Indonesia (including in the popular tourist island of Bali), it's feared it will spread to Australia via tourists. Border biosecurity measures have been tightened, but they aren't 100% effective.

In New Zealand the risk of a FMD outbreak is considerably lower than in Australia as we have no direct flights to Indonesia. If an outbreak occurred in Australia then there would be a heightened risk of an outbreak occurring in New Zealand.

FMD OUTBREAK WOULD SEVERELY DISRUPT TRADE

Should an outbreak of FMD occur in New Zealand, then trade of meat and dairy products from New Zealand would come to a standstill. Our Free Trade Agreements (FTAs) are dependent on New Zealand being free of FMD, and therefore these would have to be renegotiated should an outbreak occur here.

Australia would be in a similar position regarding international trade as New Zealand, but it does have a larger domestic market, so is not quite as exposed to the trade channel as New Zealand is.

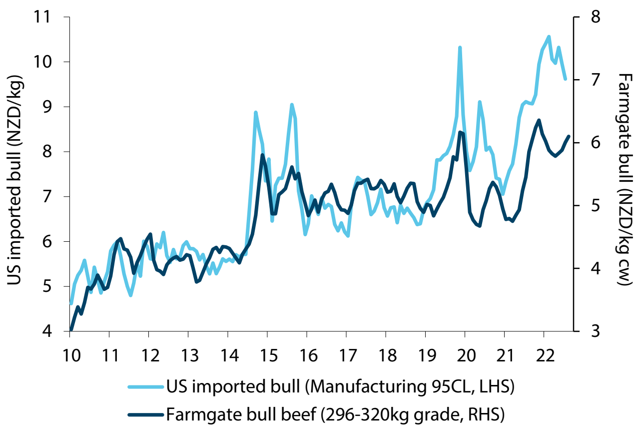
Authorities in New Zealand have emergency response plans ready to roll out and therefore may be able to contain an outbreak within a specific region. However, even if the disease is able to be quickly contained it would still disrupt the export of product from all regions in New Zealand, until trade deals are able to be renegotiated.

The processing of livestock would therefore likely be severely disrupted as space for storing meat will be limited by cold storage capacity and how much extra meat our domestic population is willing to consume or store in their freezers.

INTERNATIONAL PRICES SOFTENING

In-market prices for beef have softened in recent months but still remain relatively high in a historic sense. The low NZD has helped elevate returns at the farmgate level.

BULL MEAT PRICES



Source: AgriHQ, ANZ Research

In recent months, schedule prices have not fully reflected the underlying strength of the international markets, as can be seen in the figure above. One of the reasons why this long-term relationships may no longer hold true is the increased costs of processing meat (labour etc), and storing and shipping. However, it is also clear that profit margins for meat processors have improved recently.

This does mean that although international beef prices have softened a little lately we have not yet seen this reflected in schedule prices.

SUPPLY CONCERNS AHEAD

The beef finishing industry in New Zealand is becoming increasingly reliant on sourcing stock from the dairy industry. This trend is expected to increase in coming years as some of the steeper land that typically carried beef breeding cows is converted to forestry.

This season dairy farmers are reporting it is difficult to find calf rearers, and there is currently an oversupply of 4-day old calves. Calf rearer profit margins are typically relatively low and many are worried that with milk powder prices high, increases in meal costs and higher fuel prices they may end up out of pocket if they can't achieve good prices for weaner calves. The lack of contracts between calf rearers and finishers has a major impact on the viability of this industry.

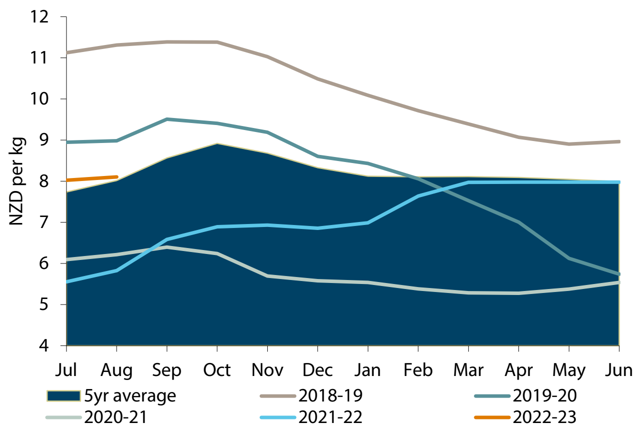
If fewer calves are reared than normal then there is likely to be less stock available for processing in a couple of years' time.

RETURNS IMPROVING BUT CHALLENGES AHEAD

Venison returns at the farmgate level are increasing again in line with the typical seasonal pattern.

Farmgate prices for venison are on the rise, which is typical for this time of the season. Prices during August were slightly above the 5-year average but well off the lofty levels reached prior to the pandemic.

FARMGATE VENISON (YOUNG 60KG STAG)



Source: AgriHQ

Demand is reported to be firm for chilled product to be supplied into European markets to meet the increase in seasonal demand that occurs leading into the Northern Hemisphere winter months. Demand for game meats, including venison, lifts at this time of the season, with peak consumption occurring during the Christmas festive season. Product needs to be on the water by October to supply this market.

The backlog of frozen venison that built up during the pandemic has now cleared, which puts exporters in a much stronger negotiating position.

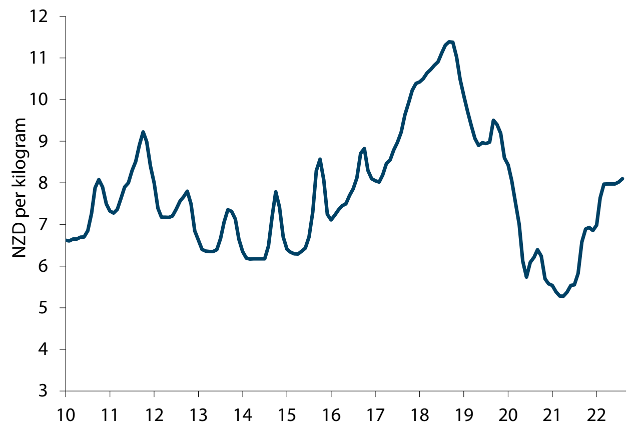
There has been a strong push to diversify away from the heavy reliance the industry has previously had on the European restaurant trade. Whilst this will always be an important market, the pandemic-induced lockdowns highlighted the value of alternative supply chains. The industry has worked hard to increase its retail trade and also geographical diversity with a focus on the US and China.

Consumers in the US are attracted to venison due to its free-range and grass-fed attributes. Also working in its favour amongst health conscious, affluent consumers is its lean attributes and its positioning as a high-quality protein.

Venison is not a typical cuisine for Chinese consumers, but demand is being steadily built up through the high-end restaurant trade.

Having diverse markets will be important as global economic conditions are expected to deteriorate over the next year, which may well affect the demand for dining at high-end restaurants.

FARMGATE VENISON (60KG STAG GRADE)



Source: AgriHQ

DEER

Returns for velvet continue to grow. This season, export returns for velvet are expected to be at an all-time high. A combination of increased production and higher prices has bolstered returns.

VELVET DEMAND ROBUST

Velvet demand has remained robust throughout the pandemic. As travel restrictions ease it will be easier for marketers to get face-to-face with consumers again to promote this product.

South Korea remains the main end-user market for this product but demand amongst Chinese consumers is also growing. There is currently a focus on positioning velvet as an ideal gift for the various upcoming festivals such as the Chuseok festival (which occurs between 9-12 September this year) and China's National Day Golden Week (1-7 October).

GRAIN

GRAIN PRICES STRONG

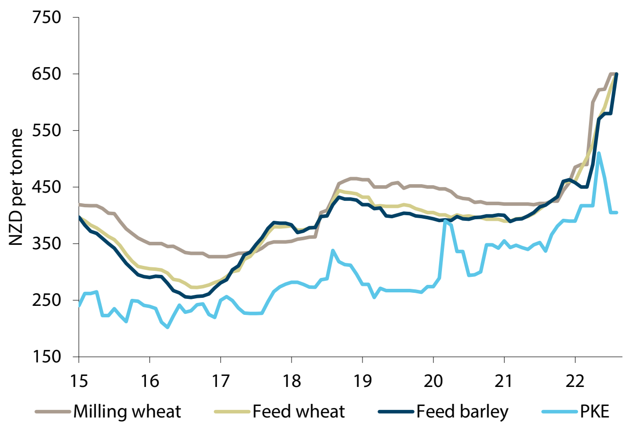
Grain prices have continued to trend up over the past month, but contracts for next season's grain are priced below the level being achieved in the current spot market. The recent wet weather has impacted the planting schedule and some paddocks will need to be re-drilled due to flood damage.

TIGHT GRAIN MARKET BOLSTERS SPOT PRICES

Grain is trading at exceptionally high prices in the local spot market. Pricing for the 2023 harvest contracts are not as elevated as the spot market but are still considerably higher than usual.

The increase we have seen for grain prices is not extraordinary when considered in the global context. Global grain prices have lifted sharply due to reduced supply, which has been accentuated by the shortage of grain from the Black Sea region since the invasion of Ukraine.

NEW ZEALAND GRAIN PRICES



Source: NZX

Ships are now carrying grain out of Ukraine, which is desperately needed to create room for storing the new season's harvest. But the quantity of grain that is currently available is much less than normal, and future production of grain within Ukraine is expected to be severely impacted for years to come.

Milling wheat is currently priced at about $650/t, although there is little wheat being traded since there is not much available. A lot less milling wheat was produced than last year. Uncertainty surrounding last season's contracts resulted in planted areas dropping sharply, as many growers weren't prepared to take the chance of producing milling wheat without a contract in place. Instead they opted to produce wheat for the feed market, which is easier to grow and has lower costs of production. Yields were also down 3% on the previous season. All up, 37% less milling wheat was harvested. Interestingly, some growers ended up selling some wheat to flour mills that was initially intended for the feed market.

The latest AIMI survey indicates that the area of land allocated to milling wheat this season will increase again, but remain 10% lower than it was two seasons ago.

STRONG DEMAND FOR FEED GRAIN

Feed grains have been in strong demand. Demand from the dairy industry has been bolstered by the high milk prices, and more recently, feed shortages. These feed shortages were brought about by the recent wet weather, reduced availability of winter grazing, and some farms milking cows longer than normal last season as they looked to take advantage of the high milk prices, compromising winter feed reserves.

This season profit margins on dairy farms are tightening. This may negatively affect demand for grain in the autumn, but for now, demand for feed grain remains firm.

GRAINS

Spot prices for feed wheat and feed barley are considerably stronger than the contract prices available for the 2023 harvest. In the spot market feed wheat is priced at about $625 per tonne, but it does vary across the country, with higher prices on offer in the North Island. Feed barley is priced at about $580 to $600 per tonne at present.

Contracts for feed wheat for the 2023 harvest are priced at about $570 per tonne, while contracts for feed barley are closer to $550 per tonne.

WET WEATHER DELAYS PLANTINGS

Spring planting is currently difficult as the recent extremely heavy rainfall is likely to keep heavy machinery off the sodden paddocks for some time.

Also, some paddocks that were planted in the autumn and earlier in the winter have recently been flooded and may need to be replanted.

LOG PRICES STABLE, CARBON PRICES LIFT

In-market prices for logs have stabilised, and some relief in terms of shipping prices is helping returns at the wharfgate level.

Meanwhile, demand for land for planting trees remains strong as carbon returns lift. Returns from forests planted either solely for carbon or for a combination of carbon and harvesting remain favourable relative to other land uses.

Regulatory changes continue at pace, but it is clear further changes are required for rules to become more closely aligned with the desired outcomes of more trees being planted, but in ways that also supports the viability of rural communities.

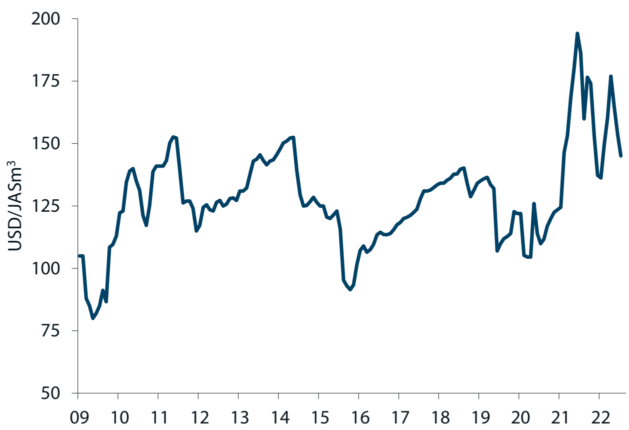
IN-MARKET PRICES STABLE

Demand for logs is increasing again and prices remain stable in this market, which is positive.

Stockpiles of logs on wharfs are not building further despite off-take levels being low at this time of the season. It is normal for demand to be low during the hot summer months, as it is simply too hot to work outdoors for long periods of time. This summer has been especially hot in China, and indeed throughout much of the Northern Hemisphere.

Also having some impact on demand are the ongoing issues in China's property development sector. Many developers have left projects unfinished. This has seen some home buyers who purchased apartments off plans refuse to make mortgage payments, further imperilling the financial situations of developers.

UNPRUNED A-GRADE IN-MARKET PRICE



Source: AgriHQ

Despite these issues, demand for New Zealand logs is steady, as there is still strong demand for pine for infrastructure projects. The Chinese Government is focusing on boosting its economy through building additional infrastructure, including roading and other construction where New Zealand pine is used for concrete boxing and the like.

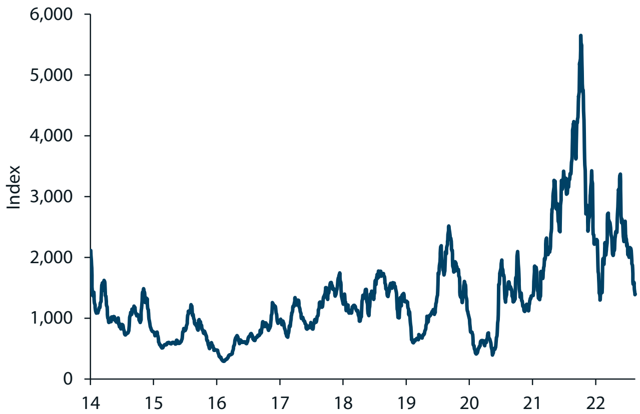
SHIPPING COSTS EASE

Returns at the wharfgate level in New Zealand have lifted as shipping costs have eased a little. The relatively weak NZ dollar has also had a positive impact on wharfgate prices, although our currency is now starting to appreciate a little.

Shipping costs have been especially high throughout the pandemic but prices are now starting to ease a little for bulk freighters. This is partially due to weaker demand to move other goods such as fertiliser and coal. The Ukraine situation has limited the supply of some goods such as fertiliser and grains, which has also reduced demand for ship capacity. This has put downward pressure on shipping prices, which is beneficial for log exporters.

FORESTRY

BALTIC DRY INDEX



Source: Baltic Exchange, Bloomberg, ANZ Research

NZ CARBON PRICE

Source: Bloomberg, ANZ Research

DOMESTIC DEMAND EXPECTED TO EASE

Demand for timber for housing projects in New Zealand is expected to ease as construction slows in line with the broader housing market. Housing prices are steadily trending down and we expect a 15% decline in house prices from peak to trough.

Housing consents indicate there should be a steady stream of demand for timber but some of these projects may not go ahead. There are plenty of homes in the construction phase and the completion of these homes will result in steady demand for timber through to about the end of the year, but demand may then drop away.

The wet winter conditions have impacted the immediate demand for timber as it has simply been too wet underfoot to get some housing projects underway. There also tends to be reduced demand from the DIY sector during the winter months.

WET CONDITIONS MAKE HARVESTING DIFFICULT

The wet weather has also impacted the supply of logs as severe flooding, slips and sodden soil have reduced access into many forests. It may be several months before harvesting can resume in some regions.

CARBON PRICE LIFTS

Demand for land for planting trees for carbon sequestration remains very strong. This has been buoyed further by the recent lift in the carbon price to over $80/NZU (or t of CO_2e).

Recent advice from the Climate Change Commission (CCC) to increase the guidance prices for units released to the ETS via the government quarterly auctions has resulted in the carbon price jumping about $10/NZU.

At present the floor price for the auction system is set at $30 for 2022. The CCC has proposed this be increased to $70 in 2023. But having a more direct impact on the market is the proposal to significantly increase the price at which units from the cost containment reserve are released. In the past two years all of the units in the CCR reserve have been released to the market. But it has been proposed to lift this trigger price to $171 next year (from the current price of $70), which means the additional units are much less likely to be released. The CCC has also recommended a two-tiered approach to the cost containment reserve so only some of the units would be released should the price reach $171, with the price needing to hit $214 before the remainder of the units would be released.

Additionally, the CCC has advised that the number of units available for auction should be reduced. The combined impacts of these proposals has seen upward pressure on the spot price for carbon. At this stage the proposals are only recommendations, but it is expected that the Government will largely accept this advice. There are, however, some technical considerations, as the auction system would need to be adjusted to allow for a two-tiered approach and at this stage it is not clear if this could be easily implemented by EEX, who runs the auctions in conjunction with the NZX.

FORESTRY

REGULATORY CHANGE AFOOT

The other areas where regulatory changes to the ETS are being considered is whether pinus radiata forests will be able to be registered in the permanent forest category. This is a new category which is due to be introduced to the ETS in 2023.

Initially pines were to be excluded from this category as there is a fear that too much land will be planted with trees, which will limit alternative land uses in the future. But it is clear that in some areas permanent pine forests may be the most viable long-term land use, so the Government is now reconsidering its stance.

At present the combination of regulations and the current carbon price mean, from a financial point of view, that there is a clear incentive to plant farming land in pines. It will take much more than just a tweak to the permanent forestry category in the ETS to get the desired outcome of additional tree planting occurring in areas that will have a limited impact on profitable sheep and beef farming operations and the viability of rural communities.

SEQUESTRATION WITHIN HE WAKA EKE NOA

A few months ago, He Waka Eke Noa – the joint industry/government initiative to price agricultural emissions – released its proposal, which currently awaits a government decision regarding its implementation.

The proposal includes providing offsets for sequestration, and implementing farming practices that will reduce agricultural emissions. However, the CCC has recommended that offsets for sequestration are not included within He Waka Eke Noa. If the Government takes this advice this will jeopardise the whole implementation of the scheme, as the industry-led agreement was based around this package deal, so pulling part of it out would most likely mean heading back to the negotiating table.

At present the impact of the pricing of methane emissions has a larger impact on the sheep and beef sector than the dairy sector. This is because the dairy sector is more efficient at producing milk relative to methane emissions, and is more likely to be able to implement farming practices that reduce methane emissions. Additionally, the profit margins in dairy are generally higher than the sheep and beef sector, so paying for methane emissions will have a smaller impact on the viability of the farm business.

Sheep and beef farmers have more opportunities to sequester carbon on their properties. The sequestration rules within He Waka Eke Noa were designed to encourage and reward plantings that are not currently recognised in the ETS. This includes smaller-scale plantings, riparian plantings, regenerating native bush etc. It is recognised that it will be challenging to accurately measure this on-farm sequestration, and the level of scrutiny will not be as great as required by the ETS. Therefore this sequestration will be recognised at a proportionally lower price than the prevailing carbon price.

HORTICULTURE

LABOUR STILL THE NUMBER ONE ISSUE

Labour shortages continue to plague our horticultural industries, limiting output. This has particularly been the case for the apple industry, which was not able to harvest all the fruit grown. The kiwifruit industry has managed to achieve a record harvest despite the huge labour challenges.

WINE: EXPORT VOLUMES LIFTING AGAIN

Wine export returns are gradually improving again. Export returns were hit hard in 2021 due to a 19% fall in the volume of grapes harvested that year. The 2022 harvest increased 44% due to an exceptionally strong rebound in the volume of grapes harvested in Marlborough, which is by far New Zealand's largest wine-producing region.

The new season's harvest is now being exported and this has helped to bolster returns, but export income has not yet returned to the levels achieved in 2020. A record volume of wine was exported in June for that particular month, but on a calendar year-to-date basis export volumes are well below normal levels. In June more wine than normal was exported to Australia and US, while exports to the UK fell.

APPLES: LABOUR WOES LIMIT HARVEST

It has been a challenging season for apple exporters due to labour shortages and the lack of ships calling at the smaller ports.

The labour shortage meant not all apples grown were able to be harvested, with earlier estimates from New Zealand Apple and Pear indicating the 2022 harvest would be down by 12%.

Getting apples to market has been particularly challenging this season. The Nelson region has been particularly impacted by the lack of available containers and limited sailings.

Work is underway to try to improve coastal shipping within New Zealand. Earlier this year the Government allocated $30 million towards coastal shipping initiatives. A new direct shipping route has been established between Tasmania and three New Zealand ports: Nelson, Lyttleton and Bluff. This new service is particularly targeted at aquaculture exports, but other sectors will also benefit from more ships calling at our local ports.

KIWIFRUIT: EXPORT RETURNS AT RECORD LEVELS

The record kiwifruit harvest is now finished for the season and orchardists are focusing on winter pruning. Meanwhile, exporters are still busy with the logistics of getting produce to our international consumers.

Exports of SunGold now exceed Green varieties in volume terms, and account for about 70% of export revenue.

Despite the challenging season with labour shortages impacting both orchards and packhouses, and inclement weather impacting fruit quality, export volumes and export returns are currently at record levels. However, the total volume of kiwifruit exported in 2022 is expected to be slightly down on last season.

Returns will be negatively impacted by the higher than normal fruit losses. Forecast orchard gate prices are due to be updated by Zespri on 23 August.

Market conditions have been very challenging this year, but export volumes are marginally ahead of the same time last year, with approximately two-thirds of the harvest exported by the end of July.

HORTICULTURE

Demand is steady but tougher economic conditions are affecting the ability of consumers to pay for high-value produce such as kiwifruit.

Kiwifruit exports to China have been particularly strong this season. Demand from Japan has not been quite as exceptional as last season, but this remains a very important market. Japan, China and South Korea tend to consistently pay the highest prices for kiwifruit exported from New Zealand.

Zespri is looking to expand the quantity of kiwifruit grown outside of New Zealand in order to help supply markets with fruit all year round. It is currently asking its members to vote on a proposal to increase the area of SunGold kiwifruit grown outside of New Zealand by a further 10,000 hectares (ha). At present there is just 5,000ha officially planted. The mandate for increasing plantings excludes plantings in China or Chile.

RURAL PROPERTY MARKET

PRICES RISING

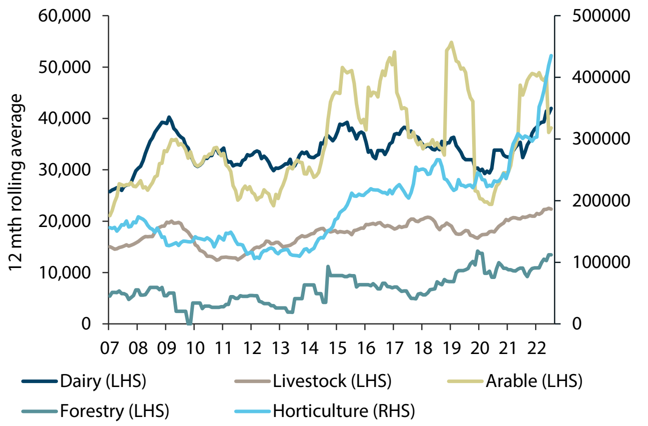
The total number of farms traded in the past year remains low relative to the previous year, but prices being paid are increasing again. Returns from agricultural sectors have outperformed many other forms of investment in recent years, which has renewed interest in the sector amongst corporate investors.

The number of rural properties that changed hands in the year to June 2022 is down 14% on the previous year. However, the median price paid has lifted by 18%.

Median prices have lifted for all sectors except arable. But median prices are also influenced by the quality of properties on offer and therefore don't necessarily reflect the total market trend.

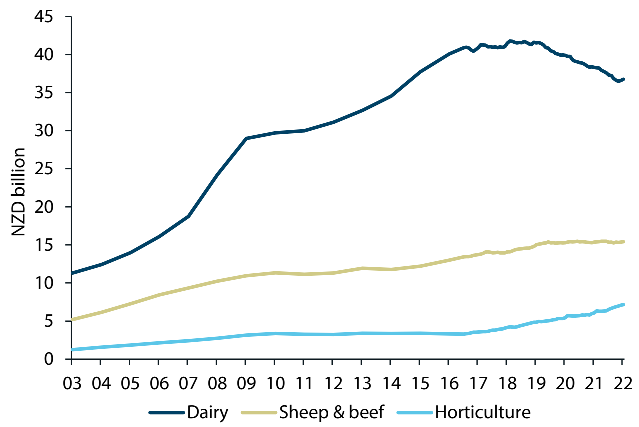
Interestingly, the Farm Price Index for all categories of farms has increased on a median price basis, but when this is considered on a per hectare basis, the median price has actually declined slightly. The same trend was evident in the Farm Price Index for dairy farms.

MEDIAN PRICE PER HECTARE BY SECTOR



Source: REINZ

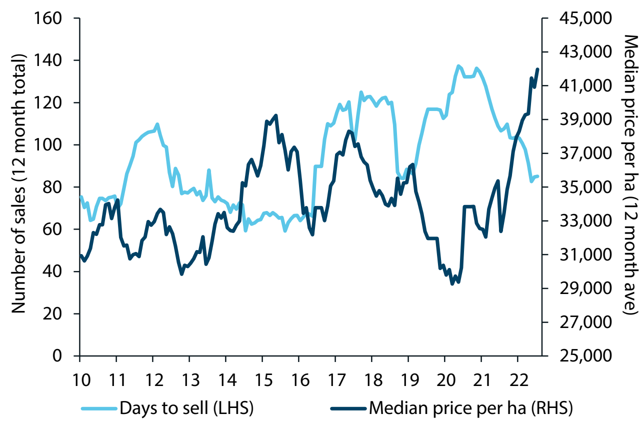
AGRICULTURE DEBT BY SECTOR



Source: RBNZ

Rural properties are generally selling more quickly than previously. This trend is prevalent across all sectors, but it does vary considerably from region to region. It is taking much longer to sell farms in Taranaki, West Coast, and the Auckland region than elsewhere. The regions where farms are changing hands the quickest are Marlborough, Bay of Plenty, and Manawatu-Wanganui.

DAIRY FARM SALES (12 MONTH ROLLING AVERAGE)



Source: REINZ

RURAL PROPERTY MARKET

Horticultural properties are selling the quickest. Dairy farms are the slowest to sell, but the median sale time has sped up considerably in recent months.

Interestingly, a similar trend is evident in the total lending to the various sectors.

Demand for dairy properties has increased recently, which is reflected in both the reduction in the days to sell and the increase in the median price.

In particular, dairy support blocks have been in strong demand. This is partially in response to tighter winter grazing regulations. These have reduced the number of farms offering winter grazing, while other farms reducing the number of cows they are wintering in order to meet the stricter regulations.

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	266	259	222	↑	↑
	Median Price ($ per ha)	41,973	32,380	34,486	↑	↑
Livestock	Number of Sales	858	1,037	1,002	↓	↓
	Median Price ($ per ha)	22,367	20,800	18,681	↑	↑
Horticulture	Number of Sales	150	196	193	↓	↓
	Median Price ($ per ha)	435,455	300,917	216,766	↑	↑
Arable	Number of Sales	47	55	95	↓	↓
	Median Price ($ per ha)	38,167	44,550	38,373	↓	↓
Forestry	Number of Sales	60	62	53	↓	↑
	Median Price ($ per ha)	13,481	10,860	8,172	↑	↑
All Farms	Number of Sales	1,464	1,721	1,591	↓	↓
	Median Price ($ per ha)	30,100	27,200	25,251	↑	↑

Source: REINZ

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Last updated: 22 June 2022

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