ANZ RESEARCH

AGRI FOCUS

DECEMBER 2022

A YEAR OF CHALLENGES

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INSIDE

CONTRIBUTORS

Susan Kilsby
Agriculture Economist
Telephone: +64 21 633 469
Susan.Kilsby@anz.com

Sharon Zollner
Chief Economist NZ
Telephone: +64 27 664 3554
Sharon.Zollner@anz.com

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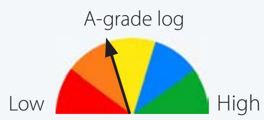
This year has delivered its share of challenges and tested the resilience of many of our primary producers. Market returns have generally softened, operating costs have increased, and the weather has caused plenty of challenges for farmers and growers. But as the year draws to a close signs of positivity are also emerging.

The excessively wet spring now means soil moisture levels are in good shape heading into summer, with some regions still actually battling with excess moisture.

Regulatory change is still occurring at pace, but the way forward is becoming clearer. Or at least, the destination is becoming apparent even though we may take various paths to get there and move at differing paces.

Global economic conditions are deteriorating, with activity forecast to slow further in 2023. This slower growth is impacting demand for many of the goods we export. At the same time, we are seeing upward pressure on the cost of producing food as high fertiliser prices push up feed costs and impact production, which in turn is helping to keep prices higher than otherwise would be the case.

Unfortunately, costs are also rising rapidly, and 2023 will therefore most likely favour those who have a sharp eye on costs and work to a budget. Imported goods are particularly pricey at present due to the low NZD so keep this in mind before asking Santa for a new tractor.

Prices at farm/orchard level relative to 10yr average		
Dairy	Dairy commodity prices have stabilised. We expect that returns next season will be at a similar level to this season. Our current season milk price remains at \$8.75/kg MS and we are forecasting \$9/kg MS for the 2023-24 season.	
Sheep	Lamb returns at the farmgate level are falling week to week due to challenging market conditions. This trend is expected to continue as lamb production lifts.	
Beef	Beef prices in our international markets continue to come under pressure, and this is now affecting farmgate prices.	
Forestry	Log returns at the wharfgate are under pressure due to weak demand from China, but lower shipping costs mean the decrease is not as large as it would otherwise be.	

ECONOMIC OVERVIEW

SLOWER GLOBAL ECONOMIC GROWTH

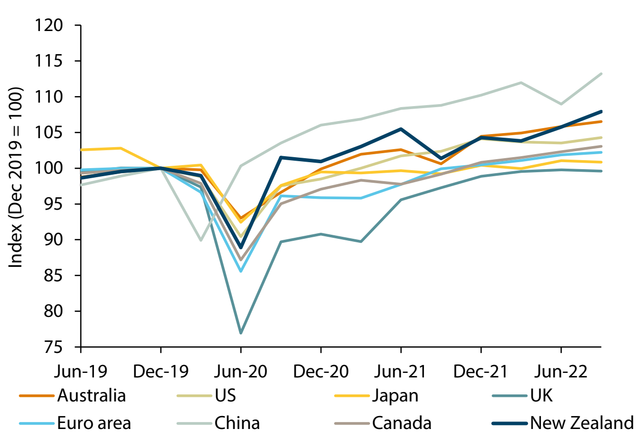
The global economy is at an inflection point. Tighter monetary policies amid high inflation are expected to slow economic growth in 2023. This is resulting in higher interest rates and downward pressure on many commodity prices. Operating costs continue to lift, squeezing operating margins for growers.

GLOBAL DEMAND SOFT

Global demand for the majority of the food products we export from New Zealand is relatively weak at present. Our high exposure to China for most sectors does mean demand for our exports has been directly impacted by the recent lockdowns.

China is stepping back from its aggressive zero-COVID policy, but no significant change in demand is expected in 2023 until beyond the Chinese New Year holiday period. Hopefully, this will signal a turning point in consumer confidence in China resulting in additional demand.

TRADING PARTNER GROWTH



Source: Macrobond, ANZ Research

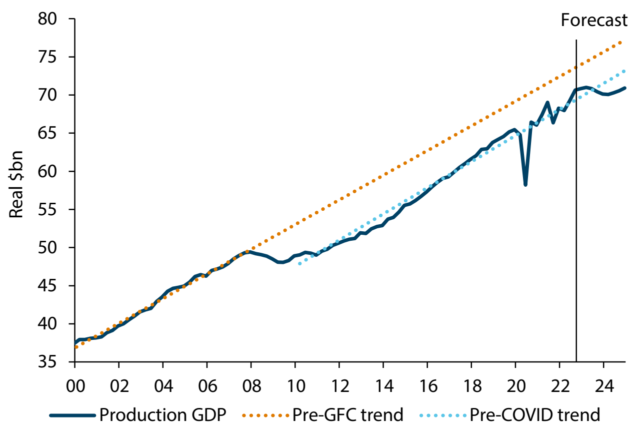
Demand is likely to face headwinds in other markets. Monetary conditions are tightening with the aim of reducing inflation, but that in itself requires a significant slowdown (or outright reduction) in consumer spending. This particularly impacts discretionary spend items. Protein exports from New Zealand do tend to fall into this category, although in some markets milk, cheese and meat are considered everyday items so are less price sensitive.

Despite the sharp slowdown in economic activity in China, its economic growth still outpaces that of any of our other main trading partners.

HIGHER INTEREST RATES

The Reserve Bank of New Zealand (RBNZ) lifted the Official Cash Rate (OCR) by 75bp in late November to 4.25%. The OCR has been lifted by 350bp over the past year – the fastest increase since it was introduced in 1999.

PRODUCTION GDP



Source: Stats NZ, ANZ Research

We expect the RBNZ will continue lifting rates at the next few meetings, taking the OCR to 5.75% by the middle of 2023. We anticipate another 75bp hike in February, a 50bp lift in April and finally a 25bp lift in May.

ECONOMIC OVERVIEW

The RBNZ's own forecast track has rates peaking at 5.5% by the end of 2023.

Markets expect further upward movements in interest rates, and the upward trend is already reflected in the interest rates currently available for fixed rate loans and deposits.

RECESSION LOOMING

Economic growth in New Zealand has been very solid in recent months, benefitting from the return of international tourists and students. But a recession is looming next year. We forecast the economy will enter recession in Q2 2023, with economic activity declining 1.3% between Q2 2023 and Q1 2024 as the RBNZ works to extinguish inflation.

During Q3 2022 the New Zealand economy expanded by a whopping 2.0% q/q, which was considerably stronger than expected. The weak spot in the economy is private consumption, which is contracting. It is clear the household sector is in belt-tightening mode as high inflation, falling house prices, and higher interest rates weigh. But the reduction in private consumption has been offset by a sharp increase in services exports (ie tourists and international students returning to New Zealand).

Some sectors are also being impeded by a lack of employees which means some service businesses such as restaurants and accommodation providers have had to scale back opening hours.

EMPLOYEE SHORTAGE IMPACTS OUTPUT

The employee shortage continues to particularly impact the primary sectors and the service sectors. This is particularly evident in seasonal jobs such as fruit picking and packing and meat processing.

Some meat processors have had to operate below capacity, which has resulted in processing delays occurring earlier than normal. Contracted supply is typically being prioritised, which provides a further incentive to lock in procurement terms in advance.

CURRENCY EXPECTATIONS

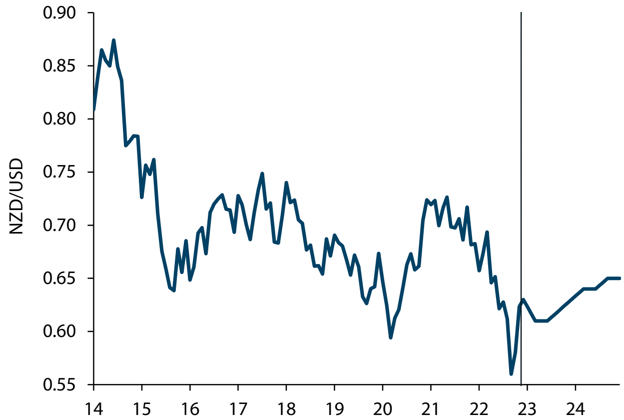
The NZD has firmed in the past couple of months which does put downward pressure on farmgate prices. Looking ahead, we expect to see ongoing volatility in the NZD as opposing forces impact its value.

If interest rates lift more in New Zealand than elsewhere that will put upward pressure on our currency. At present, the RBNZ is lifting rates a little quicker than some other countries are, but most central banks are committed to raising rates quite quickly as they battle inflationary pressures.

Global risk continues to be a dominant factor influencing the value of our currency. In times of uncertainty, investors tend to favour the USD which is considered a safe haven. Therefore, when global risks are high the NZD tends to be weaker.

At present we expect the NZD to generally appreciate a little through our forecast horizon although it is still at the low end of the ranges seen in the past decade.

NZD/USD



Source: Bloomberg, ANZ Research

Click here to access our latest forecasts.

DAIRY

ECONOMIC UNCERTAINTY IMPACTS DEMAND

Dairy prices have strengthened a little in recent months, but global demand looks fragile. Farmgate prices are supported by the lower NZD but market uncertainty remains extremely high. Global milk supplies are tight, which will support prices, but demand for dairy products is weakening. It is not yet clear whether the reduced availability of dairy products will be sufficient to offset lower demand.

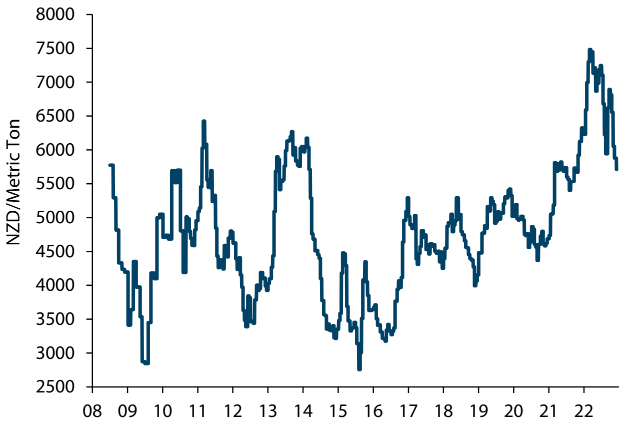
Dairy commodity prices have firmed a little over the past month, following a 30% decline in value during the previous seven months. Supply of dairy products and global demand remains delicately balanced. Both supply and demand are weaker than normal at the moment which is expected to keep prices near, or slightly above, current levels for the rest of this season. Looking further ahead, it is less clear whether deteriorating economic conditions in key markets will result in softer prices. Weakening demand is the largest risk at present to next season's farmgate milk price. Global milk production is expected to remain relatively subdued as profit margins at the farm level are tight due to elevated costs of production.

Our current milk price forecast for the 2022-23 season remains at $8.75/kg milksolid (MS), having barely changed since the beginning of the season. When this forecast was first released we allowed for some softening in commodity prices, which has now occurred. The upside and downside risks in this forecast are relatively balanced. Our forecast price is still slightly below the midpoint of Fonterra's latest forecast of $8.50-$9.50/kg MS (mid-point $9/kg MS).

The NZD has appreciated in recent weeks after languishing below USD0.60 for much of this season. The recent weakness in the NZD has helped to bolster returns at the farmgate level. Due to hedging policies, we expect the average effective exchange rate will be lower for the 2023-24 season than the current season.

The average price achieved at Global Dairy Trade events are still relatively high when considered in NZD terms, despite international dairy prices being relatively weak at present.

GLOBAL DAIRY TRADE PRICES IN NZD TERMS



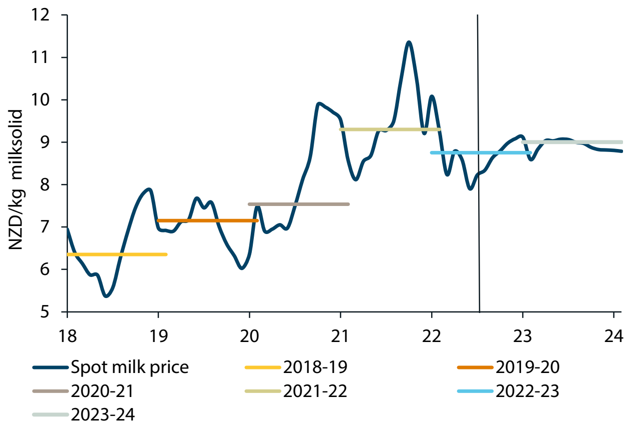
Source: RBNZ, Global Dairy Trade, Macrobond, ANZ Research

$9 FORECAST FOR NEXT SEASON

Looking ahead to the 2023-24 season, our initial milk price forecast for the season sits at $9/kg MS. This price assumes dairy commodity prices for the season will be at similar levels to current prices. No doubt we will see significant movement of prices through the season, but on average we are expecting the whole milk powder (WMP) price will be near USD3,450/t which is similar to the current level of pricing.

DAIRY

FARMGATE MILK PRICE HISTORIC AND FORECAST



Source: Fonterra, ANZ Research

SOFT DEMAND BIGGEST RISK

There is a lot of water to go under the bridge before the 2023-24 season is complete. Therefore, a high degree of caution should be applied to this longer-dated forecast. The biggest risk is soft demand for dairy commodities. Demand is already relatively weak, and if it deteriorates further it would put downward pressure on prices at the farmgate level. Global economic conditions are expected to worsen in 2023. Inflation continues to be a major problem in most parts of the world which means monetary conditions need to tighten further to get this under control.

If global economic conditions do worsen, we may also see a softer NZD which could offset some of the pain for exporters. When global risks are high, the NZD tends to depreciate, providing a natural hedge against softer commodity prices.

HIGH PRODUCTION COSTS

Locally, inflation is also having an obvious impact on the cost of production on our farms. The areas we have seen the largest increases are fertiliser, fuel, feed, labour and interest bills. The low NZD has pushed up the cost of imported goods such as fuel, fertiliser and some feed costs. Even locally produced feeds have risen sharply in price (see arable section) as the costs of growing grain have risen sharply too.

The large volume of debt repaid by dairy farmers in recent seasons has helped reduce the interest burden that would have otherwise been incurred. That being said, interest rates have risen very sharply, making a noticeable impact on costs.

The recent softening of the NZD and falling global energy prices are expected to result in some relief in fertiliser and fuel prices, but significantly lower prices are not expected to be realised until next season, at which time prices are still expected to be considerably higher than prior to the pandemic.

Labour supply remains well-short of demand in New Zealand, which is keeping the cost of labour high (although recent data suggests net migration may be returning to historically average levels). Providing favourable working conditions and other incentives, including loyalty incentives, are ways some farmers are looking to reward employees in a non-monetary manner.

Making informed decisions regarding spending will be a key challenge for this season and next (especially given the uncertainty around forecasting inflation at present).

Environmental performance on farm will be rewarded even more in the future in terms of price differentials for milk supplied, and the ability to attain the necessary consents to farm.

BUYERS HARD TO FIND

Global demand for both lamb and mutton is extremely weak and is expected to remain this way until well after Christmas.

Getting processing space for cull ewes is extremely difficult, and there are also wait times for lambs at most processors as not all chains are running at full capacity due to staffing issues.

Weak international demand, the appreciation of the NZD, and lack procurement pressure is resulting in farmgate prices dropping rapidly as we head towards Christmas.

The uncertainty of future market prices is also impacting demand for store stock. It is becoming harder to find buyers for smaller lambs being sold through the yards.

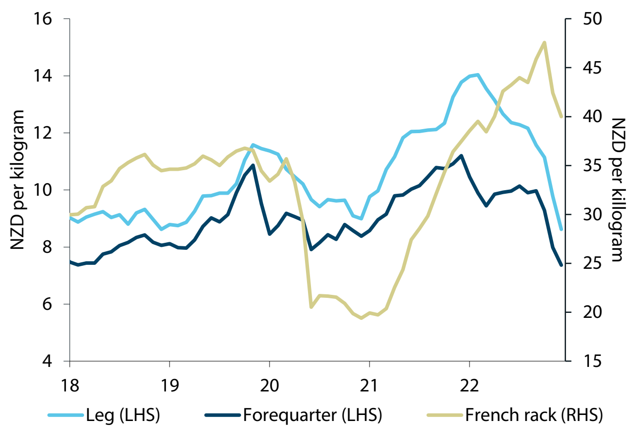
INTERNATIONAL MARKETS MIXED

In-market prices for all lamb cuts have dropped sharply in recent months and this trend is expected to continue during the early part of 2023. Buyers are reported to be well stocked for now, and therefore have the luxury of sitting out of the market and watching prices fall.

China is now pivoting away from its previous strict zero-COVID policy. Once businesses get back to a normal routine and consumers gain confidence that their jobs are secure, then - but only then - do we expect to see some uptick in consumer demand for sheep meat returning. This could take some months and demand will likely be lacklustre in the interim.

Demand from the UK and EU is also soft as the worsening economic situation, along with the financial impact of high energy-related costs, has impacted lamb consumption. Lamb is a costly form of protein, therefore customers tend to choose cheaper alternatives when under financial pressure. There also appears to be less discounting of lamb by UK supermarkets this Christmas, which is again negatively impacting demand.

LAMB CUT PRICES



Source: AgriHQ, ANZ Research

The recent appreciation of the NZD is also making it more difficult to sell lamb and reducing returns. When the NZD was weak, returns were higher in local currency terms, but now that the NZD is starting to rise again returns are falling.

It will be important to keep exports flowing, because if cold stores reach capacity early in the season, this could limit processing capacity later on. To do this exporters are likely to have to accept lower prices.

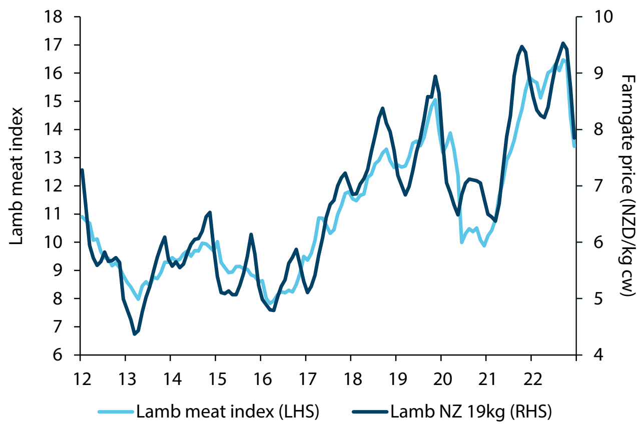
FAIR PRICES AT FARMGATE LEVEL

Based on current international prices and exchange rates, the prices being paid at the farmgate level for lamb are fair. The tight availability of space is not negatively impacting the prices being paid for lambs.

While schedule prices are falling rapidly at present, the average price expected to be paid this season is very closely aligned with the five-year average.

LAMB & WOOL

FARMGATE PRICE VS OVERSEAS MEAT PRICES



Source: AgriHQ, ANZ Research

Beef+Lamb New Zealand estimate there were 588,000 fewer lambs docked/tailed this spring, which equates to a 2.6% drop in lamb numbers with a larger fall recorded in the North Island. The lambing percentage (lambs per ewes mated) averaged 130.3%, slightly down on the previous season.

VERY LITTLE SPACE FOR EWES

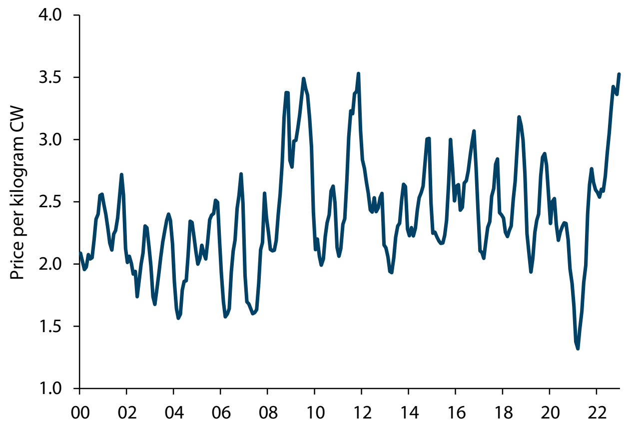
Meat processors tend to focus on lambs in the lead up to Christmas, but this year getting space for ewes is even harder than normal. Not all processors are running at full capacity, and they are having to select which lines of stock they will process. In some cases, there has been no space available for ewes for over a month.

There are also wait times for lambs, which vary from plant to plant. Some ewes have been processed recently, but this has tended to occur when there has been fewer lambs available due to not reaching the required finishing weights.

A lack of labour is the main reason why plants are not keeping up with demand. This situation will most likely get worse through the holiday season and the backlog is expected to increase as more lambs reach finishing weights after Christmas.

Our heavy reliance on China as a market for mutton explains the lack of demand for ewes for processing. In recent years, China has by far outperformed other markets in terms of the prices offered for mutton, which has resulted in virtually all of our mutton being exported to this market. At present, this demand is not there as the lockdowns in China have severely reduced demand for sheep meat.

FARMGATE DIFFERENTIAL BETWEEN LAMB AND MUTTON



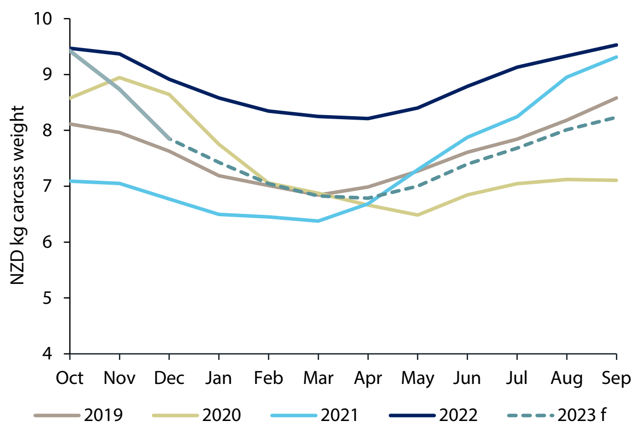
Source: AgriHQ, ANZ Research

The lack of demand for mutton is reflected in the premium paid for lamb compared with mutton, which is now at its highest level in over two decades. This clearly shows why processors really don't want cull ewes at the moment.

This does mean we are seeing more older ewes entering the sale yards. Offerings of store lambs have also been heavier than normal and this is putting downward pressure on prices.

This is particularly the case for lighter lambs, due to the uncertainty associated with pricing in a few months when these lambs will be ready for processing. The sharp reduction in returns for lamb this season has spooked the market.

FARMGATE LAMB PRICE TREND AND FORECAST



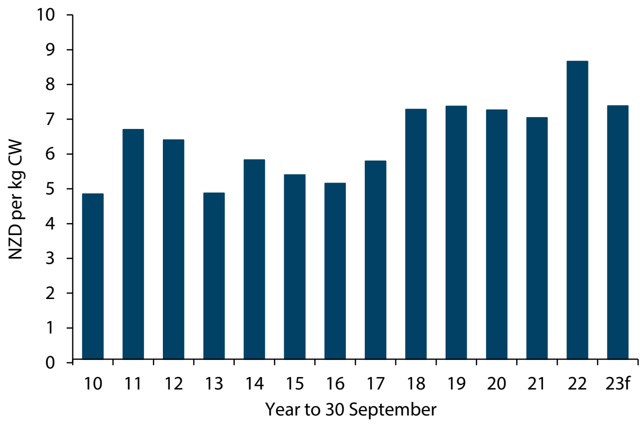
Source: AgriHQ, ANZ Research

We were anticipating a relatively sharp fall in pricing this season, but the drop has been even quicker than we had forecast. We now expect schedule prices to bottom out at about $6.80 per kg CW in March.

LAMB & WOOL

This will put the weighted average price of lamb for the 2022-23 season back in line with the prices achieved in recent seasons, excluding last season when returns were significantly higher.

WEIGHTED AVERAGE FARMGATE LAMB PRICES



Source: AgriHQ, ANZ Research

Supply contracts are particularly valuable this year as farmers holding these contracts generally find it easier to get space allocated at the processors. Even those with supply contracts are not always getting stock away when they want to.

MORE COMPETITION FROM AUSTRALIA

Stocks numbers in Australia have now rebuilt following the various devastating floods and droughts that resulted in sheep numbers plummeting a few years ago. Now that flocks are at stable levels the volume of stock available for processing is increasing.

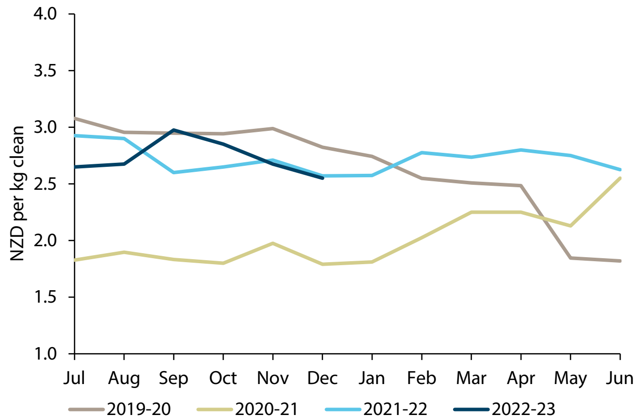
This is resulting in increased competition from the supply of lamb and mutton out of Australia. The United States is the largest market for Australian lamb, followed by China. New Zealand lamb and mutton compete with supply from Australia in China, but very little Australian lamb is exported to the EU and there is limited supply to the UK.

The European and UK markets are not as buoyant as usual due to the deteriorating economic situation which is making it hard for consumers to justify purchases of higher priced proteins. There also appears to be less promotion of lamb by retailers leading up to Christmas, which means less product is likely to be consumed over the holiday period. This is likely to result in higher in-market stocks and therefore dent demand for imports after the holiday period.

WOOL MARKETS FRAGILE

Wool prices continue to ease. With shearing in full swing around the country there is more wool flowing into the wool stores. However, it is becoming increasingly difficult to find buyers for this wool, hence coarse wool prices are falling.

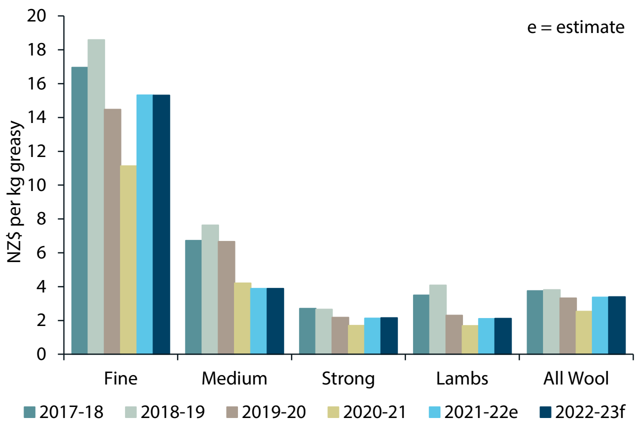
COARSE WOOL PRICES



Source: PGG Wrightson, ANZ Research

Fine wool prices continue to deliver better returns than the previous season. Beef+Lamb New Zealand estimates that the current season returns will be similar to the previous season's returns across most wool classes. However, since their outlook report was published, we have seen downward pressure on wool prices.

WOOL PRICE SEASON AVERAGES AND FORECASTS



Source: Beef+Lamb NZ

The lockdowns in China have impacted factory processing which is one of the reasons why demand for wool is weak at present.

GLOBAL SUPPLY LIFTS

Global beef demand has deteriorated in our major markets, but the low NZD means returns are still supporting farmgate prices at current levels. However, we do expect returns to ease as the season progresses.

Wet on-farm conditions are making it challenging to carry older cattle, but they will be needed to hoover up surplus pasture in the months ahead.

SUPPLIES BUILDING

The supply of beef entering global markets is currently expanding. Cattle numbers have now stabilised in Australia after a few years of herd rebuilding, meaning we will see more beef coming out of this market. An uptick in the number of cows culled this season will result in stronger competition in the lean manufacturing beef markets.

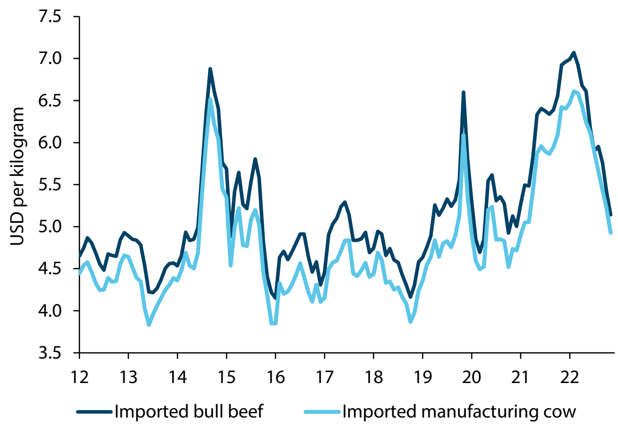
The US still has ample domestic supply as the ongoing drought means farmers continue to reduce the number of cattle they are farming. This is adding to already-high stocks of beef in this market.

Additionally, there is more beef than usual coming into the US from South America, particularly Brazil. This will keep downward pressure on prices in this market. Similarly, there is also plenty of beef from South America entering China. Brazil is by far the largest supplier of beef to China whereas New Zealand only supplies about 7%. China is also Brazil's largest market for beef accounting for about two-thirds of total exports by volume.

Demand from China remains subdued as lockdowns take their toll on domestic demand. There are also plentiful supplies of pork in China, relative to demand, which is resulting in cheaper prices.

We may see some improvement in demand from China in early 2023, which could help to move more New Zealand beef, but it is unlikely that any uptick in demand will be sufficient to push prices higher.

US IMPORTED BEEF PRICES



Source: AgriHQ, ANZ Research

Prices for imported bull and cow meat are now at their lowest level recorded in the past two years, when measured in USD terms.

As the demand for beef is relatively subdued in our two main markets (China and the US), we do expect to see further downward pressure on prices as we move through the summer months.

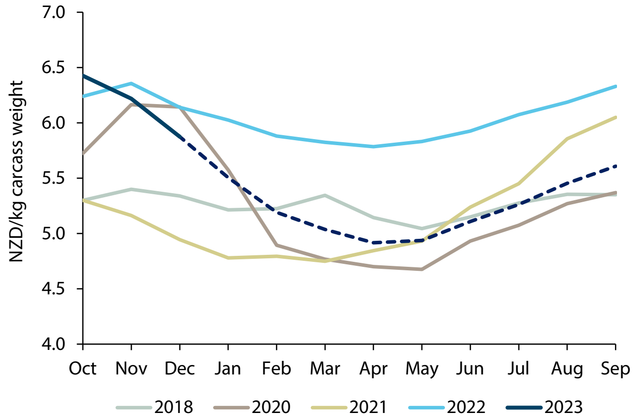
Inventories of cattle on feedlots in the US are smaller than normal, due to the drought. This will help support prices later on in the season as their domestic supply of beef will ease a little.

BEEF

DOWNWARD PRESSURE ON SCHEDULE PRICES

The drop in export prices, combined with a slightly stronger NZD, means we now expect schedule prices for bull beef to drop back to near $5 by autumn.

FARMGATE BULL BEEF PRICE TREND AND FORECAST

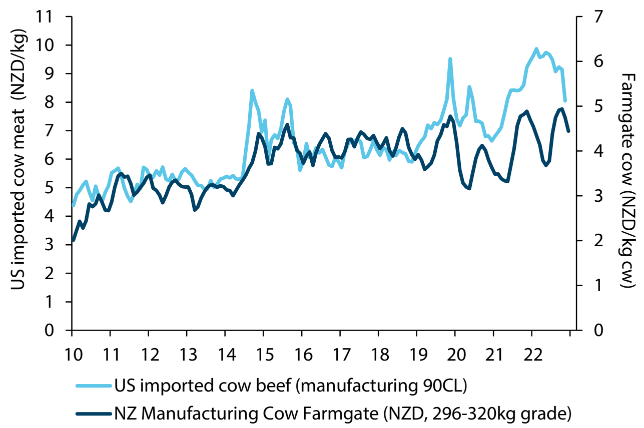


Source: AgriHQ, ANZ Research

Despite the sharp fall in prices, the weighted average price received for beef this year at the farmgate level is still expected to be slightly stronger than the 5-year average.

The margins that were evident earlier in the season between overseas and local pricing have now been squeezed out due to the rapid drop in overseas prices.

COW MEAT PRICES



Source: AgriHQ, ANZ Research

DEER

DIVERSIFICATION STRATEGY PAYS OFF

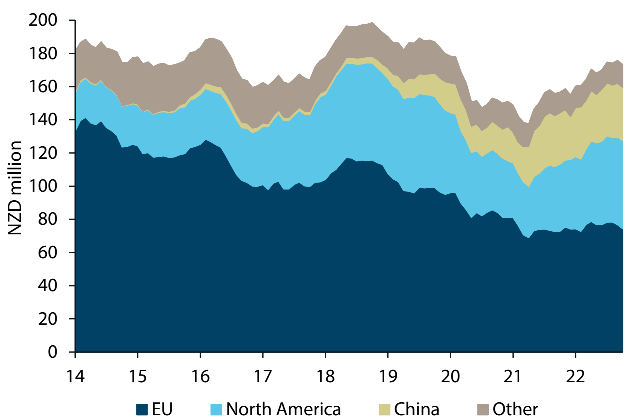
Farmgate pricing for venison is holding above the long-term average as more product is now being sold into alternative markets. This means we have not yet seen the typical drop in farmgate prices at the end of the processing season for chilled product.

The market for velvet remains very concentrated on China, despite South Korea been the larger end-user market.

Venison market risk has become less concentrated on the traditional European markets. More product is now being sold into North America – particularly the US but also Canada, and China.

The potential size of these markets is vast, and having a wider geographical spread, as well as increasing the amount of retail trade, is reducing the industry's reliance on European restaurants.

ANNUAL VALUE OF VENISON EXPORTS BY MARKET



Source: Stats NZ, ANZ Research

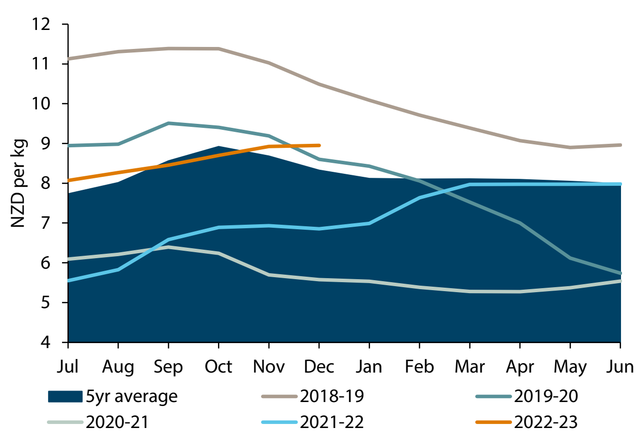
That said, international buyers are still cautious as venison is a high-end product and consumer demand is likely to be impacted by worsening economic conditions. But the economies of the US and China are expected to fare better than Europe, so increasing exposure to these markets relative to Europe makes sense.

The impact of market diversification is feeding through to farmer returns.

Supply of chilled venison to Europe for the 'game season' market has now finished. Demand during this time was reported to be steady with some product airfreighted to reach this market in time for Christmas.

Venison prices at the farmgate level have stabilised in recent months. Pricing is currently holding near $9/kg CW for young stags. Prices typically soften once the season for chilled processing ends, but this season's prices are still holding. This puts current price levels above the 5-year average.

FARMGATE VENISON (YOUNG 60KG STAG)



Source: AgriHQ

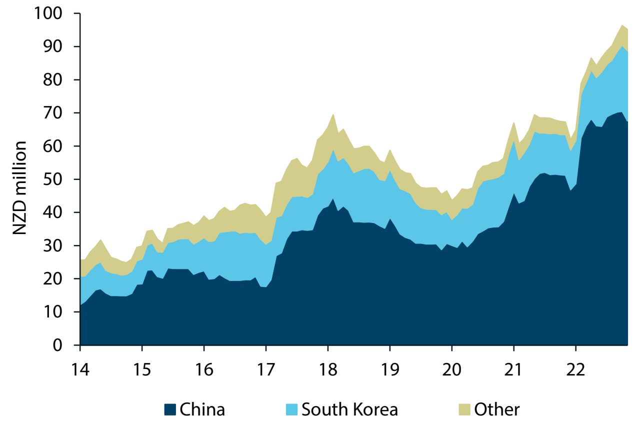
DEER

VELVET EXPORTS TO CHINA INCREASE

The total value of the velvet export market continues to grow. In volume terms, velvet exports have increased 12% y/y in the year to November, but there is now some nervousness in the market.

Virtually all of that growth has occurred in exports of velvet to China which now accounts for 86% of total velvet export returns. The main end-user market is South Korea, but much of the velvet exported from New Zealand is further processed in China before making its way to South Korea.

ANNUAL VALUE OF VELVET EXPORTS BY MARKET



Source: Stats NZ, ANZ Research

Farmgate returns for velvet appear to be in the range of $110 - $130/kg at present, although there is quite a lot of market uncertainty at the moment.

GRAIN

GRAIN PRICES ELEVATED

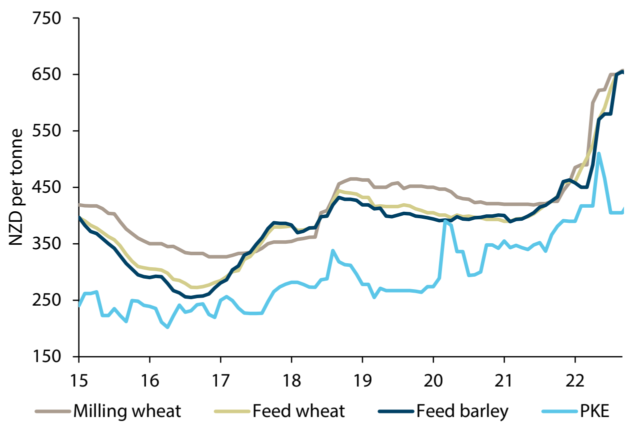
Grain prices remain firm. Soil moisture is at good levels in the South Island for arable crops, but excessive recent rains in the North Island have been problematic and are expected to impact maize production this season.

GRAIN PRICES REMAIN FIRM

Grain prices remain at elevated levels with milling wheat, feed wheat, and feed barley all priced at, or slightly above, $650/tonne. Slightly stronger prices are available in the North Island. There is virtually no premium for milling wheat over feed wheat due to the current strength of the feed wheat market.

New season maize plantings in the North Island have been hit by the recent heavy rains which flooded many paddocks. This has resulted in plantings being patchy, and replanting being required in the worst hit areas. The net impact is likely to be smaller yields than normal for both maize grain and maize silage.

NEW ZEALAND GRAIN PRICES



Source: NZX

The current market for maize grain is very tight which is keeping prices at elevated levels. This may well continue into next season if yields are smaller than normal, or feed firms may look to import more maize grain.

Grain prices may be high, but the price of palm kernel (PKE) is easing. The increase in the price differential is resulting in additional demand for PKE as farmers look to try and keep costs in check.

MARGINS STILL TIGHT FOR ARABLE FARMERS

Despite grain prices being firm arable farmers are struggling due to inflated costs. Arable farmers are highly exposed to the cost lines that have increased the most, particularly labour, fertiliser and fuel. Machinery purchases have also become costlier due to the NZD being relatively low in the past year.

Attracting skilled labour to drive tractors and harvesters has become more expensive during the pandemic due to the general labour shortage and the lack of skilled machinery operators who often alternate between hemispheres to work each harvest. This situation should start to improve as the flow of people into New Zealand continues to increase, but the labour market is expected to remain very tight for the next harvest.

STRONG HARVEST EXPECTED IN AUSTRALIA

Global grain production is relatively soft at present, with crop forecasts revised down for Argentina and Canada. More wheat is being produced in Australia and Brazil, but this is not enough to offset the reduced production elsewhere. Despite the expectation of lower crops, there is currently plenty of wheat being exported from Russia and Ukraine, which is keeping prices in check.

GRAINS

Australia's production is particularly strong this year. The Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) is forecasting a record wheat harvest, but its forecast estimate is still below that expected by many industry participants.

It will certainly be a big grain harvest this summer for most parts of Australia. Volumes are expected to be at or near record levels in Queensland, Western Australia and South Australia, which will help offset the impact of recent floods in New South Wales. However, the Australian harvest is expected to be later than normal and this may result in bottlenecks at key grain handling facilities. More grain than normal may also be downgraded from food grade which will increase the availability of feed grain.

The high volumes of grain in Australia, and strong prices in New Zealand, may result in more Australian grain heading to New Zealand in 2023.

FORESTRY

INTERNATIONAL DEMAND WEAKENS

Demand for logs from China has eased as a result of the recent lockdowns to stop the spread of COVID-19. Exporters expect demand for logs will gradually improve as lockdown restrictions ease, however it is clear China's property market won't recover anytime soon.

New Zealand continues to dominate the supply of logs to China. However, despite gains in market share, the quantity of logs being exported to China is less than normal. The lack of demand is flowing through to wharfgate prices. Lower freight rates are providing some relief.

Timber stocks in New Zealand have increased, which will allow sawmills to take a break through the holiday season.

CHINA DEMAND SLOWS

International prices for logs are soft at present due to the reduction in building activity in China in the wake of recent lockdowns.

This has resulted in lower than normal uptake of logs, from Chinese wharves.

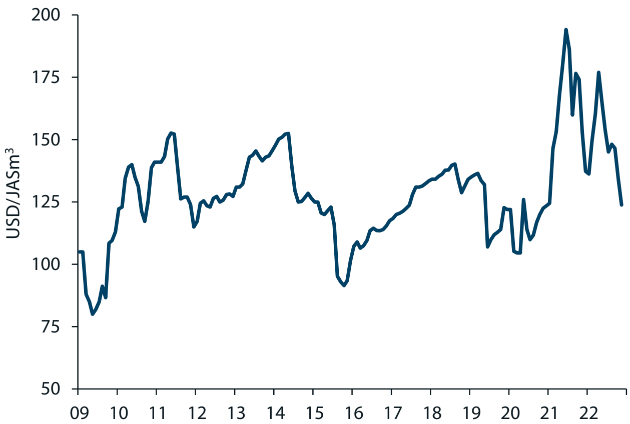
Sellers are hopeful that demand will pick up again soon, but at this stage it seems unlikely we will see significant changes in the market until after the Chinese New Year. This year the holiday period occurs relatively early as Chinese New Year falls on 22 January, with the extended holiday period running through to the Lantern Festival on 5 February.

Quarantine-free travel between mainland China and Hong Kong is expected to resume in late January in time for the New Year festivities. Exporters are hoping that demand from China improves once movement restrictions are relaxed and confidence resumes. However, this may take some time and therefore prices for logs may be weaker than normal for a while yet.

Total volumes of logs being imported by China have dropped drastically in the second half of this year, but this market still accounts for over 90% of the logs exported from New Zealand. New Zealand has gained market share at the expense of logs from both North and South America and Russia. Europe continues to supply the second largest volume of logs, after New Zealand, to China.

Prices for both pruned and unpruned logs are easing with the price of unpruned logs now about $10/JASm^3$ below the five-year average, at the wharfgate. Logs landed in China are currently worth approximately US$120/JASm^3$. In-market prices have fallen by 36% since the middle of 2021 and are now back to the levels seen two years ago.

UNPRUNED A-GRADE IN-MARKET PRICE



Source: AgriHQ

Shipping costs have continued to fall which has partially offset the weak in-market prices. Freight costs have fallen about 45% in the past six months and account for approximately a quarter of the value of the logs landed in China.

FORESTRY

Shipping costs for bulk freight are expected to stabilise near current levels in the coming months. The same degree of reduction in shipping costs is not being seen in the cost of freighting containers, but costs are easing.

DOMESTIC DEMAND WEAKER

Demand for timber for home renovations and new builds is easing which has resulted in local timber stocks increasing. This means some sawmills will shut down for extended periods over the Christmas break.

Summer tends to result in a surge of demand from the DIY home renovator, particularly timber for decks etc. Therefore, by the time the mills are back running at normal capacity the excess stocks of timber are likely to have cleared, so we may not see any significant change in pricing.

Home renovations are expected to slow as building costs rise. The sharp rise in interest rates, combined with falling home values has severely reduced the incentive to build or renovate.

We now anticipate that home values will decrease by 22% from peak to trough. However, the degree of the price correction is expected to vary from region to region.

PLAN TO ADD VALUE

In November, Te Uru Rākau (the New Zealand Forest Service) released the 'Forestry and Wood Processing Industry Transformation Plan'. Goals included in the plan include further processing of timber in New Zealand, providing sustainable fuels to replace fossil fuels, increase export earnings from timber, use of more timber in local construction, and plan more alternative species (other than pinus radiata).

The goal is to have alternative species account for 20% of plantings by 2030, up from the current level of 10%. Sawmilling capacity should also increase by 25% as should the use of wood products in mid-rise and commercial construction. At present 60% of the logs felled in New Zealand are exported, with just 40% processed onshore. Over the past 30 years the volume of timber processed in New Zealand has been very static while log exports have risen dramatically. Export volumes first exceeded onshore processing about 10 years ago and have continued to grow.

Te Uru Rākau's document outlines a number of priority areas for support for industry good initiatives, and also government support to reduce the risks associated with investment in wood processing. Exactly how this will work is not quite so obvious at this point.

HORTICULTURE

FOCUSING ON NEW SEASON

The quality issues relating to the fruit harvested last season have pulled late season prices down. But growers are now focused on the season ahead.

Late frosts did cause issues for some crops. There was some impact on kiwifruit, but other crops such as blueberries were impacted to a much greater degree.

KIWIFRUIT RETURNS SOFTEN

Orchard gate returns for the 2022 season have been revised down a little further due to the impact of quality issues associated with the latest harvest. However, looking further ahead Zespri is confident it will be able to continue to deliver strong returns across all commercial varieties.

Harvest volumes for the 2023 harvest have been compromised by early-season frosts. The impact may be in the vicinity of 10-15% of potential volume, but this will be somewhat offset by the ongoing growth in output.

Forecast prices for kiwifruit harvested in 2022 have been revised down from earlier estimates for most varieties. Zespri Green prices are unchanged, from the previous forecast of $6.13 per tray, which is slightly lower than the price achieved last season. The green varieties are starting to benefit from smaller harvest volumes as vines have been grafted over to other varieties or pulled out. Over the longer term, Zespri is forecasting stronger returns from Zespri Green ($6.50-$8.00) as further reductions in volume support prices.

SunGold prices have been revised down a further 21c per tray to $9.81 for this season. If this forecast price is achieved, then returns from this variety will be 15% lower than the previous season. The current season price is slightly lower than the mid-point of the forecast range. The current season price reflects the challenging conditions experienced this season, which resulted in greater volumes of inferior fruit. SunGold is expected to continue to deliver the highest per hectare returns to growers.

The forecast returns for RubyRed currently look low on a per hectare basis due to the large proportion of immature vines. Vines greater than two years old are forecast to return $122,882 per hectare this season, which puts the returns for this variety not too far behind SunGold. However, as greater volumes are grown Zespri does expect prices to fall on a per tray basis. The five-year forecast price for this variety is $10.50 - $16.50 which is a higher per tray price than any other commercial variety.

FORECAST ORCHARD GATE RETURNS

Fruit type	2022/23 per tray (forecast)	2021/22 per tray (Final)	2022/23 per ha (forecast)	5yr Forecast per tray
Green	$6.13	$6.35	$61,304	$6.50-$8.00
Organic Green	$8.83	$9.74	$62.075	$9.00-$11.00
Sungold	$9.81	$11.51	$135,377	$8.00-$12.00
Organic Sungold	$11.42	$12.61	$124,107	$10.00-$14.00
Sweet Green	$6.16	7.82	37,437	$54,609
Ruby Red	$20.38	$10.14	$38,501	$10.50-$16.50

Source: Zespri

Zespri is changing its process for allocated licenses to grow SunGold and RubyRed. From 2023, it will be moving to an ascending price open auction process. This will make the allocation process more transparent. Auction prices will commence at $340,000/ha (excluding GST) for SunGold. The same opening (reserve) price will apply to both the restricted pool for vines cutover from green varieties and the unrestricted pool. For RubyRed, an opening/reserve price of $33,000 will apply.

HORTICULTURE

APPLES RETURNS HIT BY QUALITY ISSUES

Late season apple export prices fell further as exporters grappled with quality issues. This means average returns to growers have dropped. The lower returns, combined with sharp rises in operating costs, mean some orchards will struggle to breakeven in 2022.

Looking ahead, the harvest for the new season will soon be under way. The labour market is still tight, but growers are a little more confident they will have sufficient workers for picking and packing fruit this season.

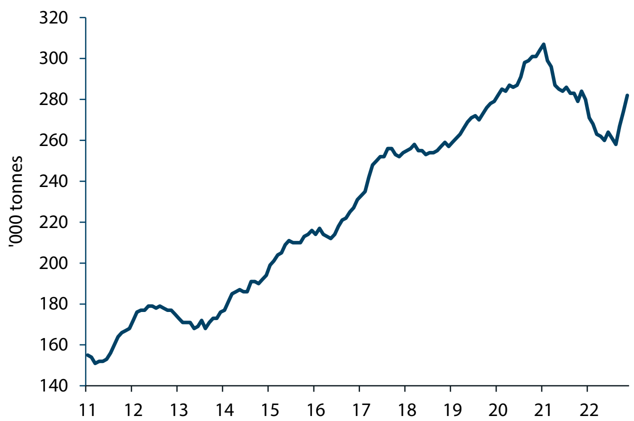
GRAPES

The 2022 season delivered improved financial returns for grape growers. Prices paid for grapes lifted, partially in response to tight volumes in the previous season. Yields were also stronger than normal as warm weather during flowering and the wet summer encouraged additional growth. This meant the 2022 vintage was significantly larger than 2021 where output was severely compromised. When compared to the 5-year average, grape yields in 2022 were about 20% larger.

Operating costs did lift for grape growers in 2022, which impacted financial returns. But overall it was a really good season from a financial perspective for growers. Like many other sectors, the costs that increased the most were labour and fuel.

Higher prices for grapes did increase costs for wine producers. The labour shortage also increased operating costs for wineries last year.

WINE EXPORT VARIETY VOLUMES



Source: StatsNZ

Higher prices for grapes did increase costs for wine producers. The labour shortage also increased operating costs for wineries last year.

Wine export volumes dropped away in late 2021 due to the small harvest that season. Exports are now rapidly rising again as wine from the big 2022 harvest makes its way to overseas markets. Export volumes are expected to continue to lift as wineries move product out before the 2023 harvest.

At this stage, the 2023 harvest is looking good. There were some frost scares earlier in the season, but most vineyards seem to have come through these relatively unscathed.

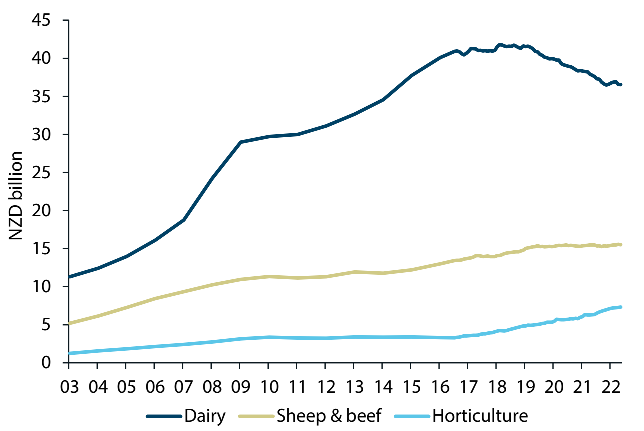
RURAL PROPERTY MARKET

PLENTY OF FARMS TO CHOOSE FROM

There has been an increase in the number of farms available for sale. This is particularly evident in the dairy sector, but also in other sectors as well. Whether there will be sufficient buyers for all these properties remains to be seen. The number of sales agreed is expected to pick up in the New Year after a relatively slow start to the season.

There is an abundance of farms on the market at present, with the trend evident across most farm types and most regions. To date, farms have been selling at similar prices to what was achieved last season, but there have only been a few sales so far.

AGRICULTURAL DEBT BY SECTOR



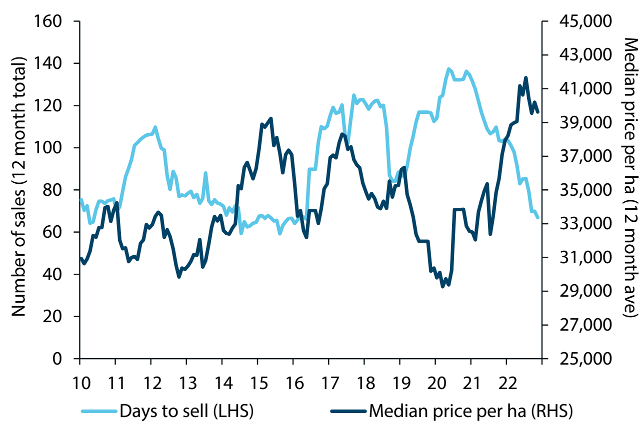
Source: RBNZ

The overall expectation is that prices will soften as the year progresses, as there doesn't appear to be sufficient demand at present to account for the supply of farms available. Alternatively, we may see a fair number of farms not actually selling if there is a significant gap between buyer and vendor expectations (a dynamic that's putting a floor on how quickly residential property prices are easing). At this point, most farms are not under undue financial pressure to sell. Instead, vendors are looking to exit the market now to avoid dealing with compliance, or they simply see this as a good time to exit the market.

DAIRY DEBT STILL A BURDEN

Debt levels across the dairy industry have fallen in recent years, but some individual farms are still highly indebted, which does affect their financial sustainability. It is clear that profits will be lower this season as elevated operating costs erode profit, despite farmgate milk prices still being relatively high (albeit not as high as some were expecting earlier in the season).

DAIRY FARM SALES (12 MONTH ROLLING AVERAGE)



Source: REINZ

It has also been a difficult spring for many dairy farms due to inclement weather, which may be why we haven't seen a lot of early season interest in dairy farms. It is hard to think about investing in a farm when you are putting in long hours during the calving/mating period. The labour shortage is another reason why we are seeing some reluctance from farmers to purchase, and a reason cited by some farmers for selling.

CARBON CREDITS STILL DRIVING PRICES

Sheep and beef farms are still in demand by carbon credit investors, who are generally offering higher prices for hill country farms than traditional farmers are able to offer. However, this is changing a little and in some regions it is getting more difficult to find these investors.

Regulations surrounding the carbon market are continually evolving. This uncertainty, combined with the relatively large amount of NZ units (NZUs) currently in circulation is potentially having an impact on this market. The price of NZUs has stabilised, with the quarterly auction of units held in December achieving a price of $79.00/NZU, which was slightly lower than market expectations.

Farmgate prices have fallen this year for meat producers as global demand for higher valued proteins comes under pressure. Tightening economic conditions have impacted consumers' confidence and ability to pay for higher priced foods. The lockdowns in China, in particular, have reduced demand and pushed prices down.

At the same time, costs are rapidly rising. The fear of dealing with increased regulation is also being cited as a reason to sell. As too are the financial implications associated with the methane emissions pricing which will take effect in 2025. While some details are yet to be agreed on, it is clear this environmental tax will impact sheep, beef and deer farmers the most.

The uncertainty relating to methane prices, along with many other legislative changes is making investing in land a more challenging proposition.

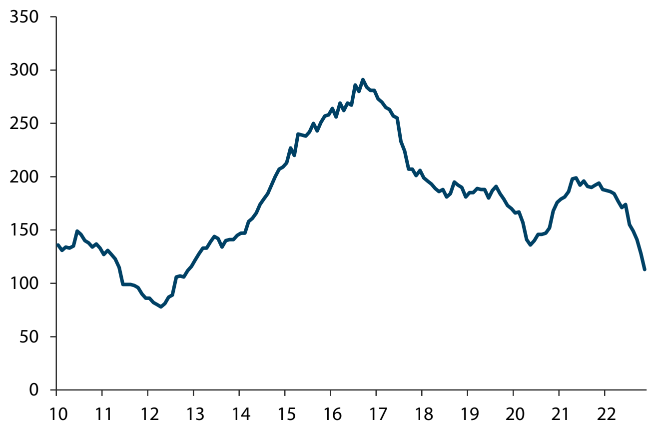
HORTICULTURAL HAS ITS OWN CHALLENGES

Demand for established kiwifruit orchards has waned a little recently. Returns for both gold and green varieties have fallen, and yields were lower than normal on many orchards last season. Inclement weather, including frosts at flowering and rain at harvest time, impacted yields and fruit quality. Staff shortages were another factor which resulted in some sub-optimal fruit making it to market, impacting market prices. Overall, it was a season that many growers will be pleased to put behind them. These challenges do mean investors are being a little more cautious about buying established orchards as future returns are less certain.

Rising costs of production, labour shortages, tighter environmental regulations and uncertainty as to future access to key inputs, such as water, is resulting in more caution being applied to the industry from potential investors. This is making it harder to sell properties, and there is some downward pressure on property prices.

The number of horticultural properties trading is starting to soften.

HORTICULTURE SALES VOLUME



Source: REINZ

The issues of securing water access and securing seasonal staff are prevalent for most horticultural businesses, as very little can be produced without these key inputs.

Fruit and vegetable production doesn't necessarily require vast quantities of water, but it is critical that sufficient water is available at key stages of production

RURAL PROPERTY MARKET

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	246	280	225	↓	↑
	Median Price ($ per ha)	39,618	37,117	34,785	↑	↑
Livestock	Number of Sales	791	951	995	↓	↓
	Median Price ($ per ha)	20,950	20,992	18,855	↓	↑
Horticulture	Number of Sales	113	194	194	↓	↓
	Median Price ($ per ha)	472,500	295,417	227,993	↑	↑
Arable	Number of Sales	45	50	94	↓	↓
	Median Price ($ per ha)	34,433	47,375	38,585	↓	↓
Forestry	Number of Sales	47	61	53	↓	↓
	Median Price ($ per ha)	14,850	10,796	8,554	↑	↑
All Farms	Number of Sales	1,320	1,628	1,592	↓	↓
	Median Price ($ per ha)	28,325	29,133	25,575	↓	↑

Source: REINZ

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Last updated: 1 September 2022

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