ANZ RESEARCH

AGRI FOCUS

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WINTER CHILL

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INSIDE

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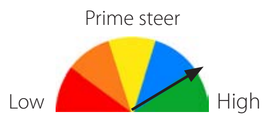
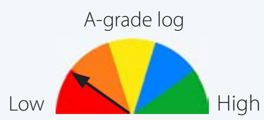
Global demand for most of our export commodities has softened recently. China's economy has not recovered as quickly as expected, putting downward pressure on prices.

Farmgate returns for most industries are at or above a five-year average, but cost increases mean, in many cases, returns are barely covering costs. The rapid rise in interest rates is a major cost that is taking a toll on heavily indebted businesses.

Autumn's warm wet conditions mean most farms are entering winter with plenty of feed.

Farmgate prices for milk and meat have softened, although procurement pressures have kept movements in meat schedule prices in check.

For the horticultural sector autumn harvests are now almost in. The sector's overriding theme is smaller harvests and slightly stronger prices, but overall returns are well down for many growers.

Prices at farm/orchard level relative to 10yr average[1]		
Dairy	Dairy commodity prices have continued to weaken. We have revised down our milk price forecasts to \$8.20/kg milk solids (MS) for the 2022-23 season and \$8.25/kg MS for the 2023-24 season.	
Sheep	Lamb returns at the farmgate level have stabilised. Processors are still keen to source lambs, as the supply available for processing remains tight.	
Beef	Beef prices have dropped, as volumes from local processing and competing markets have lifted.	
Forestry	Log returns have dropped sharply in-market due to softer demand from China. The lower New Zealand dollar (NZD) has slightly offset the impact of that at the wharf level.	

[1] All prices are in New Zealand dollars, except where otherwise indicated.

ECONOMIC OVERVIEW

THE MACROECONOMIC BACKDROP

Tighter global economic conditions are taking a toll on demand for New Zealand's export products. China's economic outlook has softened, and consumer confidence has not rebounded as strongly as expected.

Inflation is still an issue for New Zealand and most of the developed world. The Reserve Bank of New Zealand (RBNZ) has signalled a plan to pause rate rises, but we think it has more work to do and expect rates will rise further later this year.

LESS MONEY TO SPEND

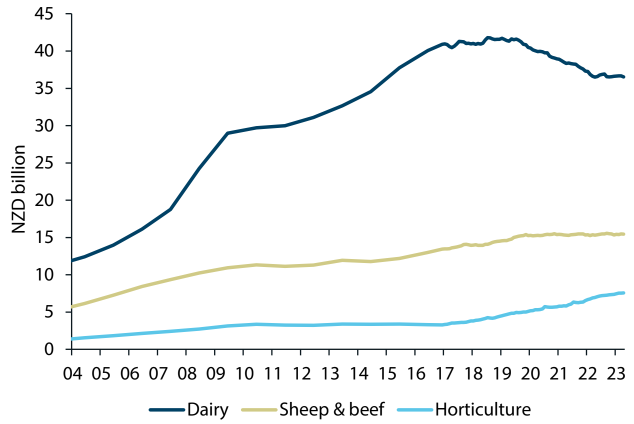
Global economic conditions are tightening, reducing consumer spending in many regions. This is making it more challenging to extract higher returns for export products, particularly those that are relatively generic.

Monetary conditions are also tightening across the developed world. There are signs that many economies are nearing the top of the tightening cycle but still have a little further to go. In other areas inflation isn't abating and central banks have more work to do.

The RBNZ has signalled it will "watch, worry, and wait" with the OCR on hold at 5.5% over coming months. However, we think domestic inflation will prove stickier than the central bank expects and have pencilled in a 25bp hike for November (with risks skewed towards that figure being higher).

Most parts of the productive economy are feeling the pain caused by rising interest rates. In the primary sector, cost inflation is high across many items, but it is the cost of borrowing that has increased the most for many agri-businesses. Those with high debt levels are particularly exposed to interest rate rises.

AGRICULTURE DEBT BY SECTOR



Source: RBNZ

Consumer spending and inflation are slowing, but New Zealand's tight labour market is allowing consumers to keep spending, for now. Immigration is increasing, which will alleviate some labour shortages, but will also put pressure on resources, particularly housing, so won't necessarily 'cure' inflation.

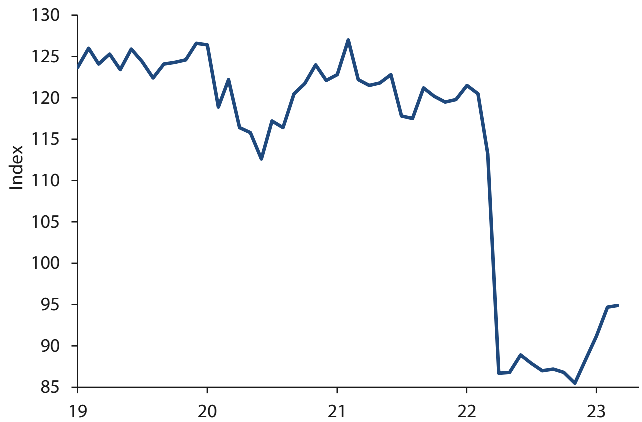
We are already seeing a change in the mood of the housing market, with prices poised to lift again. Most parts of New Zealand's economy are growing, albeit at a lacklustre pace, but the primary and manufacturing sectors remain under pressure.

Export market demand has faded alongside expectations of Chinese demand. Chinese consumer confidence has fallen markedly, which is a concern as it is the largest market for most of NZ's export goods.

China presently has very high youth unemployment. The jobless rate of urban 16–24-year-olds has hit 20.4%, far above the national urban unemployment rate of 5.2%. Many young people are employed in service industries, so the figures indicate that demand for services such as restaurants is not strong.

ECONOMIC OVERVIEW

CHINESE CONSUMER SENTIMENT INDEX

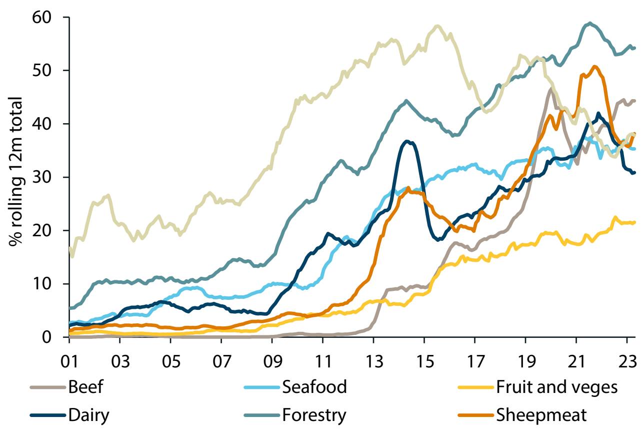


Source: CEMAC, CFLP, ANZ Research

New Zealand exporters are reporting a slowdown in China's demand. It was hoped that demand would lift once COVID-19 restrictions ended earlier in the year. There was an initial surge in activity, but it was short-lived. Consumers are still feeling the impacts of lockdowns and don't yet have the means or confidence to spend more.

China's economic growth is now expected to slow to 4.9% in 2023. That rate will exceed most developed economies but is lower than China's pre-COVID pace. This has widespread implications for NZ, which is highly exposed to this market.

SHARE OF NZ EXPORTS SENT TO CHINA



Source: RBNZ

Click here to access our latest forecasts.

DAIRY

DAIRY PRICES REVISED LOWER

Dairy commodity prices have, against expectations, weakened over the past few months. Global milk supplies have grown modestly, but it is weak demand that is keeping prices in check.

Farmgate prices have been revised down as the much-anticipated recovery in dairy commodity prices proves elusive.

The market expected demand from China to lift dramatically in the wake of strict lockdowns, but it hasn't. Product is moving through the supply chain, but demand is insufficient to bolster prices. Prices for milk powder have continued to soften.

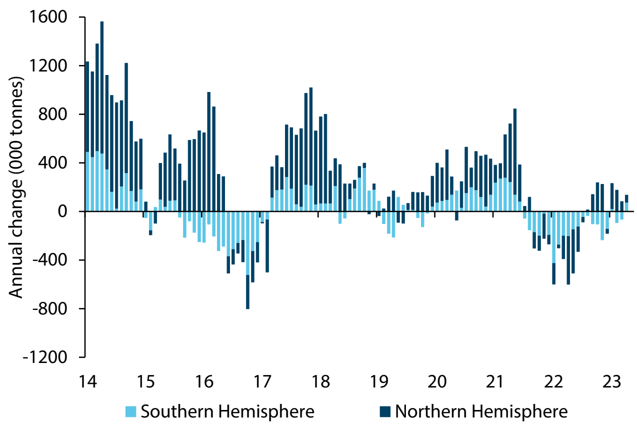
The cost of holding inventories is also rising due to interest rates lifting across the globe. Importers are keeping stocks at minimal levels and are wary of building stocks when there is uncertainty around the demand outlook. If prices keep falling, they risk holding expensive stock, but when prices eventually lift we are likely to see a flurry of restocking to get ahead of rises. Exactly when that will happen is the question.

MILK SUPPLY GROWTH STEADY

Global milk supplies are growing only mildly, but in the current environment any growth is putting downward pressure on prices.

Milk output from both the US and Europe is increasing at about 0.5% per year, an amount that the market would normally easily absorb. And there is no expectation that supply from these regions will grow excessively in the coming months because feed costs are high compared to milk prices. Farmers have no incentive to expand production.

MILK PRODUCTION GROWTH FOR MAJOR EXPORTERS



Source: DCANZ, Dairy Australia, EuroStat, USDA, CLAL

Output from the major southern dairy exporters – New Zealand, Australia and Argentina – is stagnant, at best. Australia is going backwards, New Zealand is expected to gradually trend down and Argentina will fluctuate based on politics but is stable after last year's solid growth.

In Australia, the milk intake this season is 5% behind the previous season. Processors recently announced opening prices for the 2023-24 season, with many quickly revising up price forecasts to secure a higher share of the market. Australia's dairy industry is shrinking, so the volume available for export is rapidly dropping.

CHINA: MORE MILK, LESS DEMAND

India and China are both massive producers of milk, but what is not clear is whether these countries are increasing their production or not.

What India produces it tends to consume. Most milk doesn't make it to a processing plant and what does is soaked up by growing city populations.

DAIRY

China is a different story as its population is shrinking and it plans to become self-sufficient in milk. But it lacks the water and land to produce enough feed for its dairy herd. China must import either feed for its cows or dairy products. At present, it does both, but the economics favour importing milk powder over lucerne hay, particularly when dairy commodity prices are relatively low.

It is hard to know exactly how much milk China produces and there is a risk its supply is rapidly growing; but while ever it can import milk powder more cheaply than it can produce it locally, this will limit growth.

Global milk supply growth is not particularly strong; but, when demand is weak, any growth in supply puts downward pressure on prices.

The seasonal peak in production in the Northern Hemisphere is now over, so supply will tighten from here. We should see some tightening in the volume of product offered into global markets from the Northern Hemisphere. But as this will coincide with New Zealand exporters starting to forward sell next season's product, buyers won't be short of options.

CONSUMER DEMAND IS SOFT

Demand for dairy products is currently weaker than was expected. Rising inflation has restricted consumer spending and impacted demand for dairy products.

In countries where dairy products are commonly consumed, demand for liquid milk is relatively inelastic, so price movements don't have much impact on consumption. This is not the case for higher-priced products such as cheese.

In nations where dairy is not a common part of the daily diet, demand for dairy products can be very price sensitive.

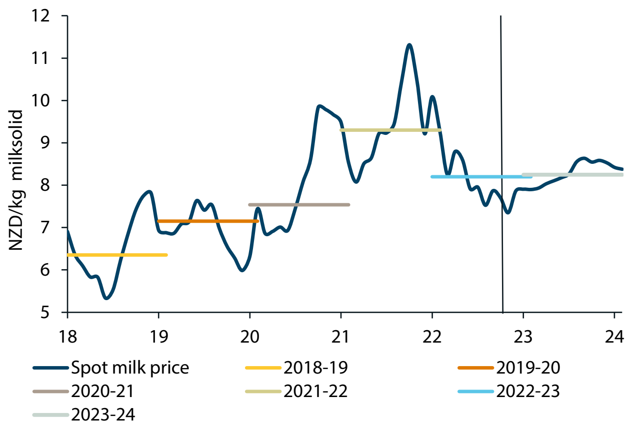
China's market for infant formula is shrinking due to a slowing in the birth rate and tighter economic conditions making it relatively expensive. Local brands are gaining market share as their reputations improve. All processors and exporters are also subject to strict registration requirements, including the auditing of production facilities, which have disrupted supply for some brands and pushed others out of the market.

At recent Global Dairy Trade events, demand for whole milk powder was weaker than normal. Prices were relatively soft right across the supply curve indicating buyers are not in a hurry to secure purchases. The price of whole milk powder is particularly relevant in the farmgate milk-price calculation.

IMPLICATIONS AT THE FARMGATE LEVEL

We have recently revised down our local milk price forecast for the 2023-24 season by 25c to $8.25/kg for milk solids (MS). The new forecast is still above the $8.00 mid-point of Fonterra's forecast range of $7.25–8.75/kg MS.

FARMGATE MILK PRICE HISTORIC AND FORECAST



Source: Fonterra, ANZ Research

We are confident dairy commodity prices will lift as the season progresses, but it is not clear exactly when this will occur.

We have also tweaked our 2022-23 season forecast 5c lower to $8.20/kg MS, as the end of season product has not reached the price we anticipated. Fonterra is forecasting a range of $8.10–$8.30/kg MS for the 2022-23 season.

LAMB & WOOL

SLOWING ECONOMICS HITS LAMB MARKETS

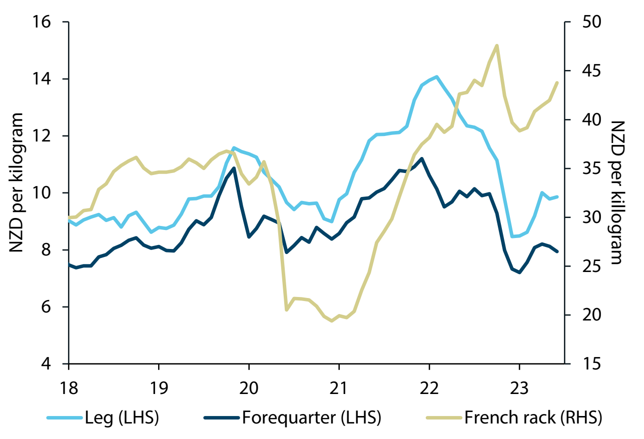
International markets for lamb and mutton have deteriorated after a brief lift earlier in the year.

Farmgate prices for lamb and mutton are holding, as limited throughput of stock is bolstering prices. Store prices have been strong, but buyers are backing off on prices paid for store stock as global markets lose their gloss.

CHINA DEMAND DRIES UP

A surge in demand for lamb products that followed China's post lock-down reopening was short-lived. Chinese importers were initially positive, pushing up the price of lower-priced lamb cuts and mutton, but they are finding it challenging to move goods on. Consumption has not lifted as quickly as expected, because consumers remain financially constrained and don't yet have the confidence to spend as much as they once did on relatively expensive products.

LAMB CUT PRICES



Source: AgriHQ, ANZ Research

Demand from importers has since waned, and prices have quickly retreated to lockdown levels.

On top of that, a surge in supply from Australia has contributed to the current market imbalance. Also hoping to take advantage of the expected pick-up in Chinese demand, Australian producers increased exports over recent months.

The downward trend in pricing now means buyers are holding off in the hope of even lower prices. Added to which, China's demand for lamb generally weakens over the northern summer. So we could be waiting some time for any significant improvement.

EUROPEAN DEMAND MEDIOCRE AND UK WEAK

Tightening economic conditions across Europe are supressing demand generally, particularly for higher end products such as lamb. Although, once the European summer arrives, we expect a lift in demand for cuts suitable for grilling.

Demand from the UK is very weak. New Zealand exporters are less and less focused on this market. The UK-NZ free trade agreement came into effect at the end of May this year, but it will be 15-years before NZ has free access for sheep meat products. During the transition period, exporters will first have to fill 90% of the existing World Trade Organisation quota before gaining additional access. Sheep meat quotas will increase by 35,000t per year in the first four years, then 50,000 per year up to 15 years when tariffs will be fully abolished. In recent years NZ has only used about half of the WTO quota, so the new agreement will have little impact in terms of access to the UK market.

LAMB & WOOL

US DEMAND THE BRIGHT SPOT

Demand from US importers is robust, particularly for middle cuts like Frenched racks. This is the only major cut for which prices have firmed in the past month. Demand for other cuts is not as strong, but the US is the strongest export market at present.

LOCAL PRICES STILL STRONG

Lamb prices are still rising, despite the weakness in global markets.

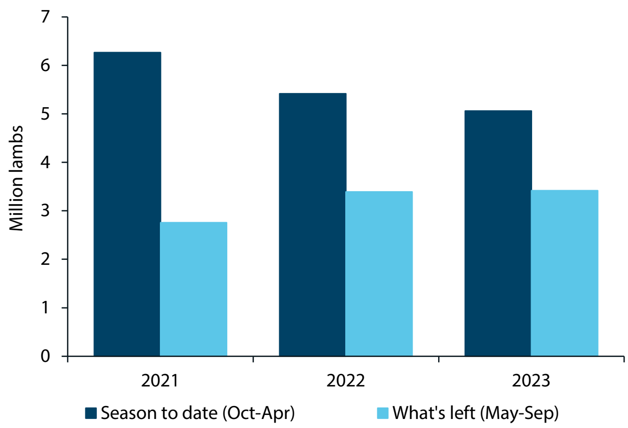
The store market for lamb domestically is relatively strong. The emergence of some winter supply contracts are supporting farmers in some regions. Lambs are generally fetching about $4/kg loin weight (LW) in the South Island, with per-kilogram pricing a little stronger for the lighter lambs. In the North Island, while some lambs have hit the $4 mark most have been selling around $3.70/kg LW.

PROCESSORS CUT CAPACITY

The overall supply of lamb through processing plants is lower than normal for this time of year. Good autumn pastures in parts of New Zealand mean farmers are letting lambs grow out to maximum weight. Processors are unsure how many lambs are still on farms, but report that demand for processing space is lower than normal. Many plants have cut back on lamb processing shifts to adjust to dwindling supply. It won't be long before some start to switch chains over to bobby calf processing, which will reduce lamb processing capacity going forward.

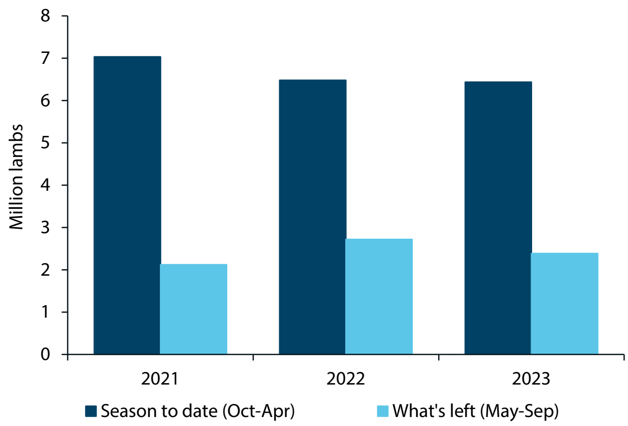
Improved road access to regions hit by flooding earlier in the year has allowed a flurry of lambs to reached processing yards, putting some downward pressure on pricing. Some regions are still experiencing very wet conditions, which has increased the supply of available lambs as farmers look to reduce stocking rates and the wet conditions have also reduced demand.

LAMB PROCESSING NORTH ISLAND



Source: NZ Meat Board, AgriHQ, ANZ Research

LAMB PROCESSING SOUTH ISLAND



Source: NZ Meat Board, AgriHQ, ANZ Research

The number of lambs processed this season (October to April) is down on the previous season by about 3.5%. There will be about 300,000 fewer lambs available for processing between May to September than in 2022 based on Beef & Lamb NZ estimates of this seasons lamb crop. In the North Island numbers left are similar to last season, while in the South Island estimates suggest there are 12% fewer lambs left than last year but more than in 2021.

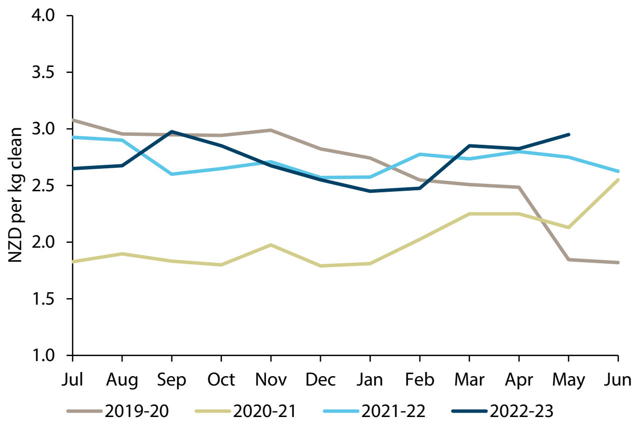
COARSE WOOL PRICES LIFT

Coarse wool prices are improving, albeit off a low base. Prices have lifted about 25c/kg over the past month and are about 20c/kg ahead of pricing at this time last year. While prices are trending up they are not yet meaningfully lifting farm incomes. Shearing costs are still outstripping returns.

LAMB & WOOL

Winter shearing is proving challenging in some regions due to the wet and muddy conditions, which are impacting wool quality. But good quality fleeces are still sought after. As is typically the case, better quality wool is proving easier to sell than poorer quality bales. At recent sales, the range of pricing across fleece quality widened.

COARSE WOOL PRICES



Source: PGG Wrightson, ANZ Research

BEEF

SUPPLY LIFTS, DEMAND SOFTENS

Beef prices eased, mostly because global demand softened, but a recent surge in cattle processing in New Zealand added to the problem. Farmgate prices are now recovering, as processing volumes are starting to slow.

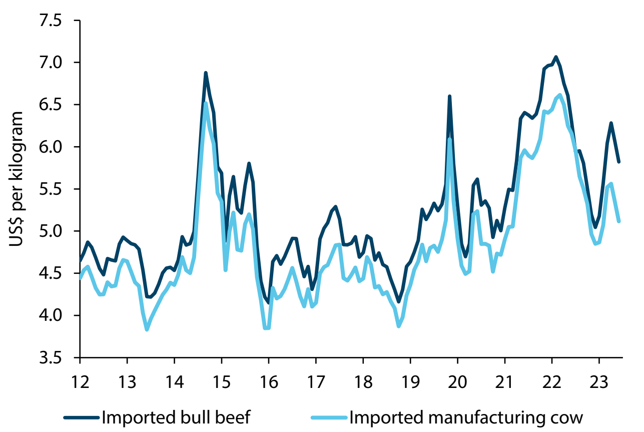
In the store market, there is good demand for lighter cattle but the wet conditions mean heavier cattle are less favoured.

GLOBAL BEEF PRICES EASE

Global prices for beef softened recently, as demand eased in both the US and China. At the same time, the supply of meat from NZ and Australia lifted. The US is also processing higher volumes of cattle again which is contributing to price pressure.

These market dynamics have pulled down the price of meat going into the US market. Prices of meat from both bulls and cows are lower, but cow meat prices are weaker due to the higher supplies available at present.

US IMPORTED BEEF PRICES



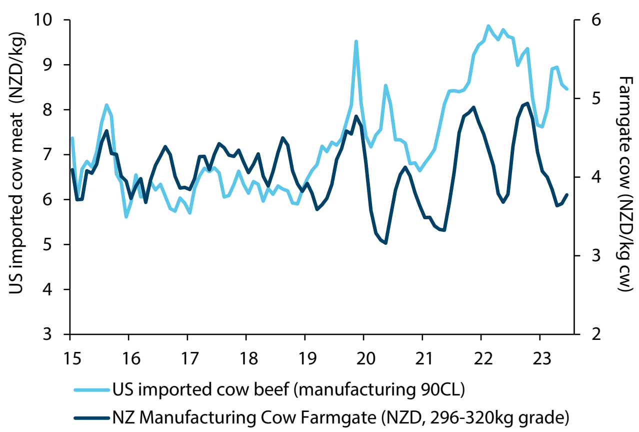
Source: USDA, AgriHQ

As the dairy season ends, NZ processors have concentrated on cows, limiting the amount of bull meat going onto the market, in turn supporting the latter's price. We are seeing a wider than normal difference in US pricing for these two grades of beef.

Farmgate prices paid for cull cows trended down in the North Island but, during May and June, lifted in the South Island. Overall, prices are similar to this time of year for the past couple of years.

Recent years have seen strong seasonality in farmgate prices for manufacturing grade cows, and this year is no exception. So, although international meat prices are trending down, we expect to see local farmgate prices lift, as supply volumes continue to ease as we move further into winter.

COW MEAT PRICES



Source: AgriHQ, ANZ Research

Cow processing in the South Island is running well ahead of last season, which was limited by COVID-19 restrictions, but is also ahead of the previous season. In the North Island, numbers are similar to last season but well down on the season before.

BEEF

What isn't clear is how many cows are still available for processing. Dairy and beef herds across New Zealand are declining, but by how much is not known. Processing plants are busy, but it looks like most available cows have been processed and plants are now catching up on the backlog of bulls and steers.

WET CONDITIONS UNDERFOOT

While paddock conditions vary across the country, most farms are wetter than normal for this time of year. Farmers are offloading heavier cattle, causing prices for this grade of beef to drop a little. Buyers are also cautious about global market conditions, but it's the wet conditions keeping demand for heavier cattle subdued.

CHINA DEMAND WEAKENS

China's beef imports have eased, which is particularly impacting Brazil, which is the world's largest beef exporter and China's main supplier. China typically buys about half of Brazil's beef exports.

Recently China is buying more beef from Argentina due to more favourable currency terms. Beef slaughter figures have been higher than normal for Brazil and Argentina but lower than normal for Uruguay. Overall, the supply of beef from South America has been higher this year.

Demand from China for NZ beef is steady but certainly not exceptional. Until Chinese consumers gain confidence in the economic outlook, we are unlikely to see a rise in demand for imported foods. Beef is not as expensive as some meats but is costlier than pork and chicken, so demand does tend to ease during tougher economic times.

DEER

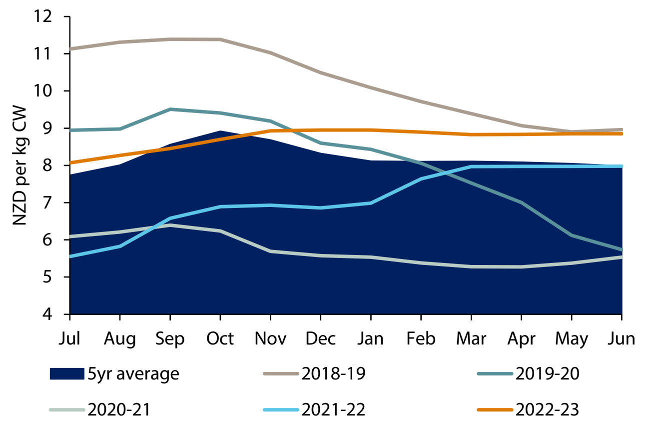
VENISON RETURNS PLATEAU

Farmgate prices for venison have barely changed in the past six months, providing a stable return, albeit a little lower than venison producers would like.

Exporters are focusing on getting more product into the US and China to reduce their reliance on the European market.

Farmgate prices for venison haven't changed much in the past six months. That stability will hopefully boost confidence in the industry, even if prices are a bit lower than producers would like.

VENISON FARMGATE PRICES (BASED ON 60KG STAG)



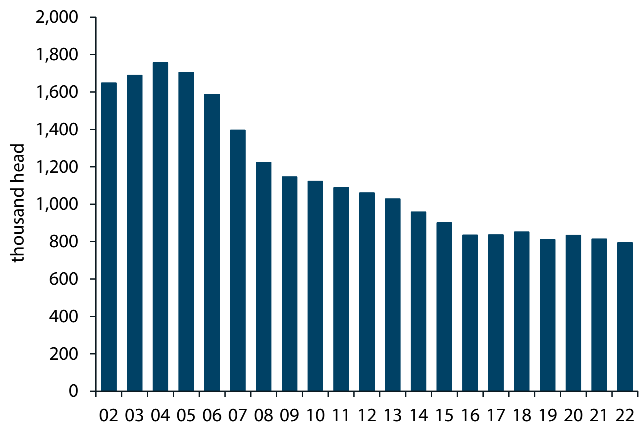
Source: AgriHQ

The number of deer processed at this time of year tends to be relatively low. There is typically a spike in both processing and farmgate returns in the spring, when young stags are killed for the European chilled market. Traditionally, this has been a lucrative market, but exporters are now looking to diversify into other markets.

The target export markets are the US and China. For the US market, NZ's five major venison exporters are collaborating in various initiatives, including targeting consumers who are affluent and fond of game meat.

By increasing supply into these markets, exporters hope to deliver stronger returns to the farmgate and stop the decline in the number of farmed deer in NZ.

DEER FARMED IN NZ (NUMBERS IN YEAR TO JUNE)



Source: Stats NZ

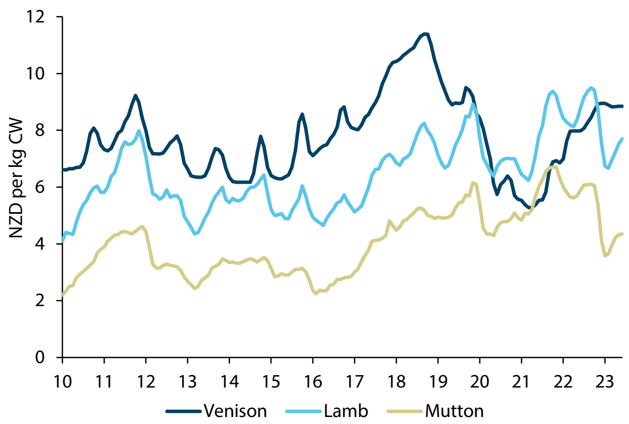
In recent years, the returns from deer farming have not stacked up well against other stock, such as sheep and cattle. Many farms run a mixture of species, and we have seen a decrease in deer numbers in favour of other species.

That said, returns for venison have improved, but for lamb have deteriorated. So the balance is tipping back in favour of farming deer.

In terms of price, the graph below compares prices only and doesn't factor in production costs. Some industry analysts believe a farmgate price of at least $9.50/kg carcass weight (CW) is required for venison to stack up against other stock classes. The question is whether the industry can push returns above the current level, where they seem to have plateaued.

DEER

FARMGATE PRICES BY SPECIES



Source: AgriHQ

At present, the number of deer being processed is seasonally low. Exporters are reporting steady demand for frozen meat, which is a positive sign. The question remains whether a lift in farmgate returns would stimulate supply.

GRAIN

GLOBAL GRAIN SUPPLIES TO EXPAND

Grain prices are soft in both local and global markets. Global supplies are expected to increase in the year ahead, but output from Australia is expected to fall.

China may soon lift its heavy tariff on Australian barley, which could divert supply away from the Southern Hemisphere market, putting upward pressure on prices.

GRAIN PRICES DROP AS SUPPLY WOES EASE

Global grain prices have softened as supply issues have dissipated.

In early 2022, Russia's invasion of Ukraine raised fears of a global grain shortage, causing prices to peak. However, Ukrainian grain has been making it to global markets, and shortages have not been as bad as originally feared. That said, the obstruction and destruction of Ukraine's farming land and infrastructure are ongoing. The recent devastation of a hydropower dam has flooded areas where grain is stored and will disrupt the logistics of exporting via the Black Sea. So, supply from Ukraine is likely to remain constrained.

Overall, though, global grain production is expected to exceed demand for the 2023-24 season, as other sources of supply are forecast to rise.

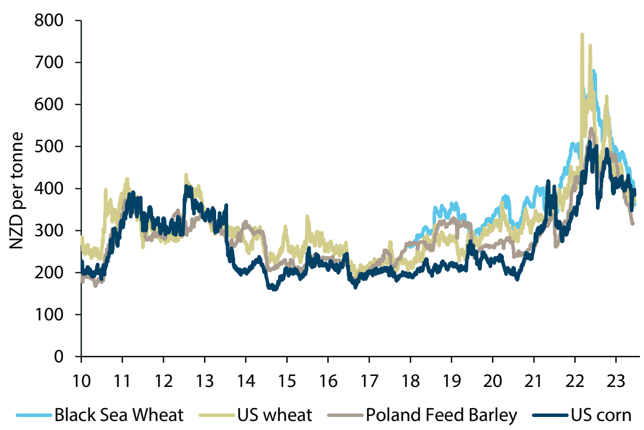
Corn production and exports are expected to increase in the US, Brazil and Argentina.

Wheat production is forecast to increase in the European Union (EU), Argentina, Canada, China, India and Turkey, which will offset declining production in Australia, India, Ukraine and the US. However, less wheat is expected to be traded globally resulting in lower stocks. Of particular note, the US Department of Agriculture is forecasting a 26% fall in wheat production in Australia, following several record crops, while a recent forecast from the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) indicates a 33% drop in Australia's wheat production as drier weather impacts yields.

Barley production globally is expected to be lower this year, with smaller crops forecast for Australia (-30%), Russia and Algeria, more than offsetting increased production in the EU, India and Turkey. While Australia may have less barley to export, its market options are expected to open.

In 2020, China placed an 80.5% tariff on Australian barley imports, which effectively blocked trade. Recent talks have reopened trade in products such as coal and logs, and barley could be next. Prior to that disruption, China accounted for half of Australia's barley exports. Australia is the world's third largest producer of barley but only accounts for 6.5% of global production. The EU grows most of the world's barley. Australia exports other grains, such as wheat, to China, but barley makes up most of the Australia-China grain trade.

WORLD GRAIN PRICES



Source: CME Group, Polish Ministry of Agriculture & Rural Development, ANZ Research

GRAINS

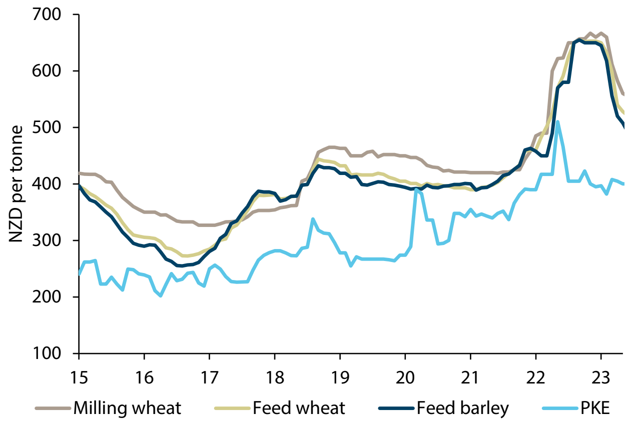
If Australia resumes exporting barley to China, that will limit what's available for other Asian buyers, which could add upward pressure on prices in the short term. Likewise, the smaller wheat crop forecast for the new season could lift grain prices in Australia, which may have flow-on effects for NZ.

Planting conditions for new season crops in Australia have been less than ideal. Drier soil is likely to limit yields. Australian Crop Forecasters estimated 13.7 million hectares will be planted in wheat, while 4.4mha will be dedicated to barley; and more recent forecasts from ABARES have seen these figures revised down to 12.8mha of wheat and 4.3million ha of barley. The change in acreage is not nearly as dramatic as the drop in expected yields as dry conditions limit production.

LOCAL PRICES RETREATING

Prices for locally grown grains have generally retreated but may be starting to find their feet as more contracts for new season production are signed.

NEW ZEALAND GRAIN PRICES



Source: NZX

Generally, grain growers are not happy with current prices, but the rapid fall in global prices it is making it challenging for them to command anything higher. The situation may change if Australia exports less, which would tighten the market.

FORESTRY

DEMAND FOR LOGS PLUMMETS

Global demand for logs dropped sharply in recent months, after a surge in activity in China ended. International and local prices for logs have dropped sharply.

Meanwhile New Zealand carbon prices languish, as we await the outcome of a government review of the Emissions Trading Scheme.

GLOBAL DEMAND SUBSIDES

China's demand for NZ's logs has waned, taking prices back to late 2020 levels.

The property sector in China remains weak and is unlikely to recover soon. Chinese investors remain wary after many lost savings on failed property investments during the pandemic. In previous downturns, the Chinese government encouraged investment in this sector to unleash private savings, but this is not currently occurring. Most of the recovery in China's economy is expected to come from the service industry rather than demand for goods or property investment. So demand for raw logs to support housing remains relatively weak.

Demand for logs lifted briefly after the government relaxed zero-COVID policies. Then a sudden slowdown resulted in some shipments heading to China without a purchase agreement in place.

While China's demand for logs has weakened, New Zealand's share of the existing supply has grown. This year that reached approximately 40%, which is about double the volume being supplied by Europe, the next largest supply region.

China's ban on Australian logs, since 2020, has now lifted, but prices are too weak to attract Australian logs, so they're not expected to make up a large share of supply.

The volume of logs being exported by Australia is now a fraction of what is used to be. The Chinese ban had a significant impact, but the strength of Australia's housing industry means more logs are now being milled for the domestic use than for export.

Most of the logs Australia exports are going to India, significantly reducing New Zealand's share of that market. South Korea and Japan are also significant markets for Australian logs.

LOWER FREIGHT RATES AND NZD HELP

One factor moving in favour of New Zealand exporters is a lower cost of shipping. At the peak of the pandemic induced supply-chain disruptions it was costing over USD75 per Japanese Agricultural Standard cubic metre (JASm^3) to ship logs. Prices are now under USD35/JASm^3. These lower shipping prices helped offset some of the weakness of in-market prices.

WHARFGATE PRICES DROP SHARPLY

Wharfgate prices for unpruned NZ logs are trading around \$100/JASm^3 depending on location and quality. Prices have dropped about 45% in the past couple of months.

The drop in returns is prompting foresters to slow down harvesting, although other factors have contributed such as crews being relocated to clean up cyclone damage and obstructed roads. At current prices, those that have discretion as to the timing of their harvest are likely to hold out until higher pricing resumes. Larger firms, though, are likely to keep up the pace of harvesting regardless of price cycles.

Issues with road access are expected to limit harvesting in the Gisborne and Hawke's Bay regions. Soil moisture levels are extremely high in many regions, which is also making it difficult to harvest timber during the winter months.

FORESTRY

Overall, the volume of logs available for export in coming months is likely to be well down.

DOMESTIC DEMAND MAY IMPROVE

The other factor that impacts the availability of timber for export is domestic demand. NZ mills generally use higher quality timber and have often in recent years had to compete with the export market to secure supply. Our local no longer facing sharp competition from the export market but their own appetite for logs has diminished due to the recent downturn in domestic construction. However, that may soon change.

Just as the supply of new homes is waning, demand is starting to lift. The damage done by recent cyclones and flooding and the uptick in immigration are together stimulating demand. This is likely to put upward pressure on house prices in coming months (see our latest Property Focus for details). As house prices start to rise, we are likely to see new housing projects kick off.

CARBON MARKET STALLED

Carbon markets are awaiting the results of the government's review of the Emissions Trading Scheme (ETS). The review has caused considerable uncertainty in the carbon market.

The ETS review is examining how to encourage a greater reduction in gross emissions, rather than companies simply offsetting emissions by purchasing carbon credits.

The supply of carbon credits is rising, as investors plant more exotic trees and these plantations mature and sequester more carbon.

NZ CARBON PRICE

Source: Bloomberg, ANZ Research

The review may have significant implications for owners of Pinus radiata forests (and/or future investments of this type), which are currently earning carbon credits.

While uncertainty continues, trading in secondary markets for carbon has slowed considerably. Prices have stabilised at near $57 per New Zealand Unit (NZU).

The government's latest quarterly auction of NZUs that took place on 14 June resulted in no units trading as the prices bid did not reach the confidential reserve price (CRP).

The CRP calculation uses a formula that takes into account the price at which NZUs are currently trading in the secondary market. Its purpose is to provide price stability across the various carbon markets.

HORTICULTURE

FOCUS ON EXPORTS

The fruit harvest is in for most growers, and the focus has shifted to exporting.

The harvest of green kiwifruit is ongoing, but for the red and gold fruit it's over. This year the kiwifruit harvest, like the apple harvest, was considerably lower than normal.

In-market prices have improved a little for early season fruit, but it is unclear whether these prices are sustainable.

APPLES: HARVEST VOLUMES FALL

Apple export prices recovered this season, mostly due to lower volumes. Early season export returns have increased to levels seen a couple of years ago, but reduced yields will limit the sector's total returns.

While yields are down, the industry has worked hard to ensure fruit quality.

Exporters have reported an improvement in the reliability of shipping this season compared to previous seasons, which is not unexpected given the global supply chain challenges associated with the pandemic. Getting space on ships when and where needed can be a challenge, and tends to be a bigger problem for smaller companies.

There is a small window of opportunity this year for apple exporters to benefit from the NZ-UK free trade agreement. The agreement which came into force on 31 May allows NZ apples to enter the UK at zero duty from January to July each year, during the offseason for UK apple production. Apples exported from August to December will be subjected to a quota, which will diminish progressively over three years.

Apple production is forecast to be 20–30% down this season, because of the Hawke's Bay floods. Production will be impacted for years as some regions have been deemed unsuitable for permanent crops. Not all growers have the appetite or finances to rebuild businesses, whilst others will opt to keep operating but on a smaller scale.

KIWIFRUIT: GROWER RETURNS REVISED UP

The harvest of red and gold kiwifruit is now complete. Packhouses are currently processing green fruit. By late May about 15% of fruit had been delivered to market.

This year's harvest has been smaller than previous years. Zespri now expects to export 136m trays of fruit, which is about 20% less than the 171m exported last season. Recent hailstorms, wet weather at harvest, and frost earlier in the season have all taken a toll on volumes.

This season, the industry has focussed heavily on quality, to avoid the issues that plagued last season's produce. To secure premium prices, the market needs to be able to rely on consistently high quality. Consumers are willing to pay for and repurchase products they know to be good.

Looking ahead to 2024, the kiwifruit harvest is likely to be significantly higher. Growers expect next season's gold fruit harvest to be about 50% larger than this season, as existing gold plantings mature and growers switch from green to gold varieties.

Growers are increasing their exposure to the Zespri SunGold™ variety. At the latest licence release, prices remained high.

Just prior to that auction, additional information about recent yields from Zespri RubyRed® was released showing that in 2023 the fruit was smaller than anticipated. There is uncertainty around what this new variety will sustainably yield, but it tends to perform better in warmer sites. Under the new auction process, a RubyRed licence fetched $38,000/ha, (inc. GST). For 125.8ha of RubyRed, 65 bidders successfully attained a licence, leaving 24.2ha of licences unsubscribed.

HORTICULTURE

Demand for SunGold remained very strong. A restricted pool of 200ha was offered for those growers switching from green fruit. This auction preceded the 150ha of SunGold offered in the unrestricted pool. The two SunGold auctions were heavily oversubscribed, which resulted in pricing for the restricted pool reaching $678,000/ha (including GST), while the licence price of the unrestricted pool pushed up to $700,000/ha (inc. GST).

Prior to this season a tender process was used to allocate licences, causing a wide variance in licence prices. In 2022 the median price paid for a licence was $921,150/ha, while the minimum price was $519,740/ha (inc. GST).

Overall, the new licences allocation process was successful, and there is an aim to speed up the process at future auctions.

Zespri has finalised financial results and grower payments for the 2022-23 season. Growers will be pleased to see prices revised up for all categories after forecast orchard returns dropped sharply in February. However, returns are still considerably lower than the previous season with most fruit categories returning 9–14% less than last year.

The drop in returns also coincides with smaller yields and increased operating costs. This has particularly impacted growers who only have exposure to green varieties of kiwifruit which tend to be generating much smaller margins than SunGold.

Zespri's profits also dropped, mainly because it released fewer licences in 2022 than in 2021.

FORECAST ORCHARD GATE RETURNS

Kiwifruit variety	2023-24 per tray (March forecast)	2022-23 per tray (Final)	2022-23 per tray (Feb forecast)	2021-22 per tray (Final)
Green	$6.50 - $8.50	$5.78	$5.55	$6.35
Organic Green	$9.00 - $11.00	$8.68	$8.04	$9.74
SunGold	$10.50 - $12.50	$9.97	$9.79	$11.51
Organic SunGold	$11.00 - $13.50	$12.28	$11.58	$12.61
Sweet Green	$7.50 - $10.00	$6.87	$6.31	$7.82
RubyRed	$17.00 - $20.00	$22.27	$21.99	

Source: Zespri

Source: Zespri

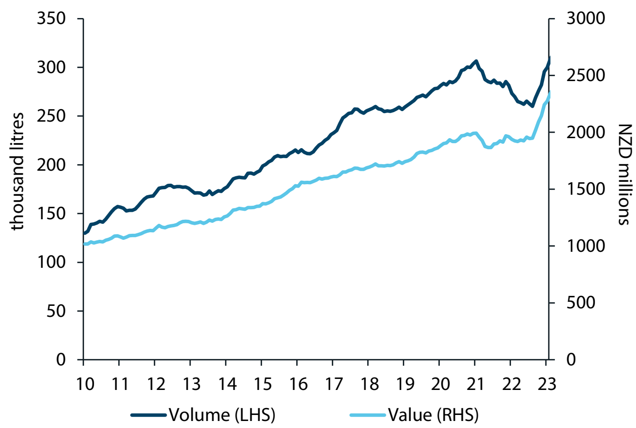
Forecast prices for the current season are considerably higher than last season when quality issues knocked $2.56/tray off grower returns for green and $3.44 for SunGold. Forecast ranges are still relatively wide at present but will tighten up as the season progresses and fruit sales and deliveries are completed. If quality issues can be successfully managed then the grower returns should be nearer the upper end of the forecast range.

WINE HARVEST COMPLETE

New Zealand's wine harvest is over for the year. Labour shortages, which have troubled the industry in recent years, abated somewhat.

Weather was not particularly favourable during the harvest, causing quality issues. Weather issues earlier in the season meant some vineyards had lower than normal yields. Production in the Hawke's Bay and Gisborne regions is significantly down. In 2022 these two regions accounted for 11.6% of wine produced in NZ.

NZ WINE EXPORTS (12 MONTH ROLLING)



Source: Stats NZ

Wine exports took off again this year, following a couple of poor seasons. Both export volumes and prices rose, as the 2022 harvest was exported to international markets.

Wine will benefit from May's NZ-UK free trade agreement. All tariffs on NZ wine have been removed, and an alignment of standards will help reduce technical barriers to trade. At present the UK is the second largest market for NZ wine behind the US. Much of the wine exported to the UK is shipped in bulk and botted in-market.

RURAL PROPERTY MARKET

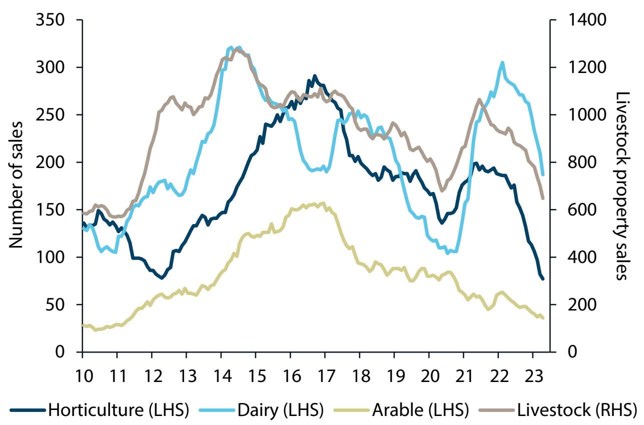
FEWER PROPERTIES TRADED

The number of rural properties traded has fallen across all main property types. This meant it was quieter than usual on 1 June, the date when dairy properties typically change hands.

Rising interest rates, uncertainty surrounding future returns and a higher regulatory burden are reducing demand for rural properties.

Rural property sales are trending down across almost all land classes. This is particularly true for horticultural properties, but a similar trend is evident for dairy and livestock properties.

SALES VOLUMES (12 MONTH ROLLING AVERAGE)



Source: REINZ

In the past year, the number of rural properties that changed hands fell by 35%. Dairy properties traded fell 41%, livestock properties 31% and horticultural properties 57%.

Falling sales numbers tend to pre-empt lower prices. There is now evidence that pricing is starting to retreat for both livestock and horticultural properties, but we are yet to see a fall in dairy property prices.

Only median price data are available, and these don't tell the full story. This is particularly the case for an industry such as horticulture which has a wide range of property types and therefore sale prices. However, for industries such as dairy, those data are a reasonable indicator.

Anecdotal evidence suggests that dairy property prices are holding, because higher quality farms are trading well while lower quality farms are harder to move.

Time will tell where farm prices head, but evidence points to prices trending lower.

Farm margins are being squeezed across all industries as operating costs have increased. In the past year, the cost that has risen most is interest on debt. Businesses carrying high levels of debt are disproportionately exposed to the sharp rise in interest rates. And, in addition to existing costs, new regulatory requirements are expected to add new costs and complexity to many farming operations.

Regulations to protect freshwater are being progressively rolled out. The first regions that will be required to provide Freshwater Farm Plans are the Waipa River catchment in Waikato and Aparima and Fiordland in Southland. Those farming 20ha or more or with horticultural operations of 5ha or greater in these regions will need to deliver a Freshwater Farm Plan by August 2023. Farm planning requirements will be progressively rolled out to the remaining parts of Waikato and Southland from early 2024 to mid-2025.

The timing of the rollout of Freshwater Farm Plans in other regions will be announced later in 2023, although some regional councils already have regulations in place that require consents or farm plans. Farmers have 18 months from the time the new regulations come into play in their area to get their plans certified. The industry is concerned there won't be enough accredited certifiers, and if farm plans are not done well there is a risk they won't improve environmental outcomes. If done well they will provide valuable information to potential farm buyers.

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	167	283	226	↓	↓
	Median price ($ per ha)	42,418	39,050	35,324	↑	↑
Livestock	Number of sales	648	944	984	↓	↓
	Median price ($ per ha)	19,725	22,225	19,083	↓	↑
Horticulture	Number of sales	77	179	193	↓	↓
	Median price ($ per ha)	428,625	375,083	242,223	↑	↑
Arable	Number of sales	36	57	93	↓	↓
	Median price ($ per ha)	42,200	46,317	39,084	↓	↑
Forestry	Number of sales	37	71	54	↓	↓
	Median price ($ per ha)	10,763	12,604	8,977	↓	↑
All farms	Number of sales	1,043	1,616	1,582	↓	↓
	Median price ($ per ha)	27,775	30,658	25,944	↓	↑

Source: REINZ

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Last updated: 18 April 2023

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