NEW ZEALAND ECONOMICS
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INSIDE

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SWEET & SOUR MIX

FEATURE ARTICLE: KIWIFRUIT REVIVAL

The New Zealand kiwifruit sector typifies many aspects of true 'value-add' leading the way in producing and selling a premium offering. Despite the challenges posed by Psa, the industry is in good heart appearing to have navigated the worst of its impacts. Confidence in the industry is reflected in current orchard prices and returns. Grower support for the single point of entry industry structure is also at historic highs. Green orchard prices have averaged $300,000-$350,000 per canopy hectare recently. With medium-term orchard-gate returns expected to be close to the $15,000-$18,000/ha mark this implies a rate of return close to 5-6.5%. The real potential is with the new Gold3 variety. Current Gold orchard prices have averaged $425,000-$500,000 per canopy hectare recently. Medium-term orchard gate returns are expected to be around $53,800/ha, which implies a rate of return of between 11.5-13.5%.

THE MONTH IN REVIEW

Parts of the East Coast of both Islands remain dry and feed positions are expected to be tight during the winter. Milk supply will register some small growth in 2014/15. Supply potential in 2015/16 looks lower due to high cull-cow turn-off through-out the season. The turn-off in breeding ewes through-out the 2014/15 year also implies a smaller flock and 2015 lamb crop. The kiwifruit crop rebounded to pre-Psa levels, while the 2015 vintage was 27% smaller.

RURAL PROPERTY MARKET

The rural property market continues to dance to its own tune. Total turnover has dropped back from the same period (Jan-Apr) last year, but prices over the last 6 months have continued to oscillate at what are historically high levels for many different land uses. Buyer confidence in the long-term food story is commonly being touted as a reason for buoyant prices, but this isn't the sole support factor.

KEY COMMODITIES AND FINANCIAL MARKET VARIABLES

New Zealand commodity prices continue to head lower and have aligned themselves with broader global moves for soft commodities. The NZD has started to react, easing the pressure, but OCR cuts will be required to get it to a more export friendly level.

BORROWING STRATEGY

The short end has been dragged lower by ramped up expectations for OCR cuts, and the long end slightly higher on the back of a lift in US interest rates. All else equal, the "steeper" yield curve discourages fixing for longer due to cost.

ECONOMIC BACKDROP

The outlook remains reasonably solid, supported by low interest rates, a strong construction pipeline, booming net migration and surging Auckland house prices. However, headwinds in the form of a high NZD relative to commodity prices and stresses on dairy cash-flow have clearly altered the risk profile.

EDUCATION CORNER: FOOD SAFETY ENVIRONMENT

This month we feature an article from Craig Armitage of PricewaterhouseCoopers on the food safety environment. It offer an insight in to why New Zealand food companies need to be global leaders in food safety and integrity. It also outlines the approaches leading food companies are adopting to improve food safety, trust and protect their brands.

FEATURE ARTICLE: KIWIFRUIT REVIVAL

SUMMARY

The New Zealand kiwifruit sector typifies many aspects of true 'value-add' and at is the forefront of producing and selling a premium food offering for the fresh fruit category. Despite the challenges posed by Psa the industry is in good heart appearing to have navigated the worst of its impacts.

The industry has a number of strategic features and focal points, but key ones include:

- Zespri controls all the intellectual property of the kiwifruit varieties it markets, bar Hayward green;
- New Zealand's product mix is to be more weighted toward golden varieties. Golden varieties face less competitive pressure versus Hayward at present and are preferred in Asian countries for their sweeter taste. Both factors help lift price premiums. This, combined with higher yields and a similar growing cost structure to green, delivers superior returns;
- the integrated and collaborative nature of the supply chain; which work together to consistently produce high-quality and high-taste products;
- growers receive market-based payments – reflecting the quality (taste, size, timing) of fruit;
- a dominant entity across the marketplace that has generally delivered results (the industry has contestable pockets, but has not fragmented and result delivery has been a key reason); and
- significant marketing and research/development investment over a long-period of time across all industry participants to create new innovations and drive efficiencies.

Of course such dynamics may not lead to good execution and optimal performance. There have been own goals (i.e. invoicing issues) and lessons learnt. But, ultimately it is 'runs on the board' that counts and this is illustrated by the industry being brought back from the brink when Psa first hit; a stronger run of grower returns; and a continued compelling offshore performance for Zespri's brand and margins. This sees the current industry structure delivering for the majority and was recently highlighted by growers voting overwhelmingly (97%) in favour of supporting the single point of entry structure. This level of support and engagement is almost unheralded across the other primary industries.

Current orchard prices also reflect confidence. Green orchard prices have averaged $300,000-$350,000 per canopy hectare recently (including the 2015 crop). With medium-term orchard-gate returns expected to be close to the $15,000-$18,000/ha mark (depending on yield & price assumptions), this implies a rate of return close to 5-6.5%.

The real potential lies with the new Gold3 variety, which is expected to account for 45-50% of the annual crop when re-grafted canopies reach full maturity in a few years. This will mark a significant transformation of the New Zealand industry into a genuine multi-crop industry – spreading market risk. The new Gold variety is expected to achieve a price premium over green, have a similar cost structure to grow, and yield more fruit per hectare.

Current Gold orchard prices have averaged $425,000-$500,000 per canopy hectare recently (including the 2015 crop and licences) and medium term net orchard gate returns are expected to be around $53,800/ha. This implies a rate of return of between 11.5-13.5%.

INTRODUCTION

This month we take a look at the New Zealand kiwifruit sector and the state of play. This includes an overview of the global kiwifruit market, the New Zealand industry structure and its unique points of difference, the road to recovery from Pseudomonas syringae pv. actinidiae (Psa), along with orchard-gate returns for Kiwifruit. Acknowledgement must go to Zespri, Belrose, Kiwifruit Vine Health (KVH), New Zealand Kiwifruit Grower Forum (NZKGF), and New Zealand Kiwifruit Journal for contributing a large amount of data and insight.

Despite the challenges posed by Psa, the industry is in good heart appearing to have navigated the worst of its impacts. While it has never been 'plain sailing' in the sector (they have had a few faux pas over time) the transition to a genuine multi-crop industry, with strong brand presence and many other competitive advantages in the production, grading, handling, packaging, transportation, marketing and channels to market (trade links and retail relationships) from many years of investment well outweigh many of the challenges faced when exporting fresh fruit. These strengths are reflected in grower returns and orchard prices at present. Grower engagement and support for the current industry structure is also at historic highs and unparalleled compared with many other primary sectors.

The industry plans to double export earnings from 2013 to $1.8 billion by 2020. If achieved, this will further lift the sector up the league table of New Zealand export earners and cap a remarkable turnaround from the ravages suffered when Psa appeared. It's one example of the growing diversity of agriculture based exports beyond dairying. Such sectors do not have the same scale as dairying, but have stronger growth credentials and are of sufficient critical mass that collectively they are having a growing impact on New Zealand's economic performance.

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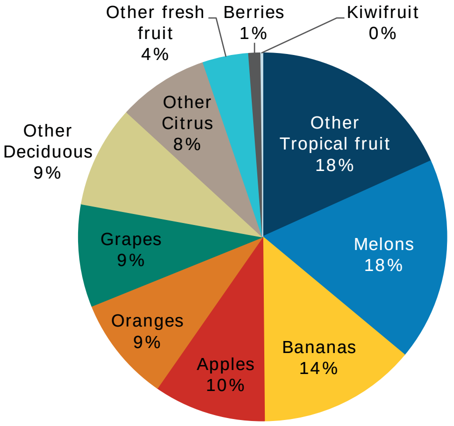
GLOBAL FRUIT CATEGORY AND KIWIFRUIT'S POSITION

Annual global per capita consumption (technically referred to as "disappearance") of all fruits and melons topped 108kg's in the 2010/12 period. Fruit specifically made up 89kg's and melons 19kg's. **Kiwifruit consumption was just 0.21kg's per capita and well behind the more commonly consumed apples, grapes, bananas, oranges and other tropical fruits.**

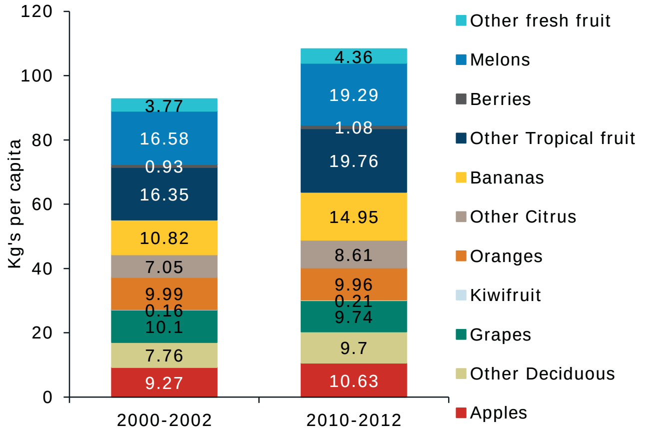
FIGURE 1. TOTAL GLOBAL FRUIT PRODUCTION BY FRUIT TYPE/GROUP (weight basis)



Source: ANZ, Belrose (World Kiwifruit Review)

There has been solid growth (1.6% per annum) in per capita consumption of most fruit categories over the last 10 years. The absolute volume produced per capita increased for all categories except two of the traditional favourites, grapes and oranges. Production of grapes has been hit by challenges in the wine category, including regulatory and tax changes for alcoholic beverages and competition from other alcoholic beverages. Oranges have faced heightened competition from rival, more novel, citrus fruits.

FIGURE 2. GLOBAL FRUIT CONSUMPTION PER CAPITA BY TYPE/GROUP



Source: ANZ, Belrose (World Kiwifruit Review)

The general fruit category is expected to continue to grow, but kiwifruit's relative share is not expected to grow in the near-term as it takes time to fully overcome the setbacks caused by Psa in many major producing countries.

The production (supply) of fruit is expected to expand. Larger scale operations have invested heavily in high-density plantings in recent years and they are increasingly able to generate higher production earlier in the life of new orchards or plantations, and achieve higher average production over the useful life of the plantings. Many development agencies have funded fruit production projects in emerging countries that follow similar principles, as they try to generate greater total revenue and jobs in rural areas by planting fruit crops, rather than cereals or oilseeds. There have also been many improvements in the harvesting, storing and transportation of many fruits (especially the more perishable tropical fruits), which is enabling greater availability of more exotic fruit in many different parts of the world and for longer periods throughout the year.

On the demand side, an increase in fruit consumption has been driven by the trend toward healthier diets across many different parts of society. Nutritionists, medical practitioners alongside other influencers (i.e. celebrity chefs) have encouraged dietary and regulatory change to highlight the important role fruit consumption can play in meeting personal and societal health goals. The globalisation of many different types of cuisines has brought new cooking styles and different types of fruits to a greater number of countries. Upper income consumers have taken the lead in incorporating more exotic fruits into their diets with higher prices not being an impediment to increased consumption. However, for many lower income consumers, the perception remains widespread that fruits are expensive relative to other processed/packaged food products.

As incomes increase further, demand is likely to shift from cheaper fruits, like apples and pears, to more expensive and exotic fruits like kiwifruit, cherries, stone fruits, exotic tropical fruits and berries.

That shift won't guarantee success though, with kiwifruit needing to:

1. **Continue to establish its credentials as a 'super health food' with substantial health benefits.**
2. **Overcome strong cultural and cuisine preferences in certain markets.**
3. **Adapt product offerings for convenience, busy lifestyles, changing retail formats and other new channels to market (i.e. internet).**

FEATURE ARTICLE: KIWIFRUIT REVIVAL

NEW ZEALAND'S PLACE IN THE GLOBAL KIWIFRUIT MARKET

The global production of kiwifruit has grown strongly over the last 10 years increasing by nearly 70% to 2.57 million metric tonnes. New Zealand has managed to hold on to its position as the third largest producer despite the ravages suffered by Psa.

China is by far the largest producer accounting for some 45% of global production, followed by Italy (16%), New Zealand (13%) and Chile (8%). From 2003 to 2011 global production increased by 40% to 2.83 million metric tonnes, with China growing 20% over this period and the rest of the world by 70%. Since 2011 to 2014 this has changed with China's production accelerating, but the rest of the world experiencing a decline of almost 17%, partly due to the damage from Psa. This is set to reverse over the next few years as a number of countries bounce back from the ravages of Psa and Chile from adverse weather conditions in 2014.

TABLE 1. TOP 10 KIWIFRUIT PRODUCING COUNTRIES (average 2012-2015)

Country	Annual Production (mt)	% Global Supply
China	1,150,000	45%
Italy	416,333	16%
New Zealand	323,667	13%
Chile	203,208	8%
Greece	121,677	5%
Iran	80,000	3%
France	61,833	2%
Japan	37,500	1%
United States	26,823	1%
Portugal	18,000	1%
Top 5	2,214,886	86%
Top 10	2,436,041	95%
World (total)	**2,573,298**	

Source: ANZ, Belrose (World Kiwifruit Review)

In total China's supply has grown by 670,000 mt (138%) over the last 10 years, well outpacing the other major producing areas. The three other major Asian kiwifruit producers, Japan, Iran and South Korea, saw a combined production increase of over 55,000 metric tons (+43%). The three major European suppliers (Italy, France and Greece) had combined production increases of almost 100,000 mt, (+19%), while the two major Southern Hemisphere suppliers (New Zealand and Chile) had combined production increases of over 129,000 mt (+32%).

INTERNATIONAL TRADE

All China's production is consumed domestically at the moment. But there is a lot of nervousness that with continued production growth from new plantings, new higher yielding varieties coming through, and some slowdown in the growth of domestic demand, **exports onto international markets could rise quickly over coming years.** At present China lacks the marketing and packaging expertise of modern retailing systems, as well as the high quality fruit to compete with the likes of New Zealand and Chile. **However, given the transition they have made for apples it would be prudent not to count them out.**

For the other top five global producers they are all predominantly export focused. New Zealand exports virtually all of its crop and the others (Italy, Chile and Greece) 90-80% of their crop depending on seasonal conditions.

Italian and Greek exports are predominately focused within Europe, but have begun to branch out a bit more in recent years – due to softer economic conditions within Europe. Italy is by far the largest European exporter, but some 75% of its exports are sent within Europe. A larger proportion (nearly 50%) of this heads to the higher returning western markets of Germany, Spain and France. Italian exports to North America and Asia have grown in recent years too. Conversely Greece has carved out niches in lower priced European markets. Russia had been their largest single market prior to last year's food ban. Other markets include new member states of Europe and Turkey.

TABLE 2. EXPORT MARKETS OF EUROPE'S THREE LARGEST PRODUCERS (metric tonnes, annual average last three years)

	Italy	Greece	France
Germany	56,541	-	3,154
Spain	40,457	-	3,513
France	21,945	-	-
Other EU	125,270	86,965	8,072
North America	28,372	717	-
South America	16,660	-	-
Middle East	9,644	4,257	-
Asia	15,490	1,623	7,102
Other	13,901	2,209	1,848
Total	**328,280**	**95,770**	**23,689**

Source: ANZ, Belrose (World Kiwifruit Review)

One of New Zealand's competitive advantages is that production is counter-seasonal to Northern Hemisphere competitors. This means there is still competition on the shoulders of the season from Northern Hemisphere supply, but less so during the main sales period. However, Chilean production is produced and sold at a similar time.

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TABLE 3. EXPORT MARKETS OF THE TWO LARGEST SOUTHERN HEMISPHERE PRODUCERS
(metric tonnes, annual average last three years)

	Chile	New Zealand
Italy	17,898	14,043
Spain	11,816	33,500
United Kingdom	7,283	-
Other EU	30,583	97,577
China	8,449	33,778
Japan	1,848	61,434
South Korea	6,035	16,481
Taiwan	1,330	24,267
Other Asia	1,967	24,871
North America	36,383	12,507
South America	29,343	-
Middle East	5,997	3,383
Other	17,815	20,705
Total	**176,747**	**342,546**

Source: ANZ, Belrose (World Kiwifruit Review)

Chilean exports of fresh kiwifruit fell by more than half between 2013 and 2014, largely due to severe weather damage during the growing season. The result was cuts across the board to all major Chilean markets. Prior to 2014, the fastest growth in Chilean fresh kiwifruit exports was to North and Central American countries, Asia and the Middle East. Notable gains to individual markets were reported for the United States, Mexico, China and South Korea.

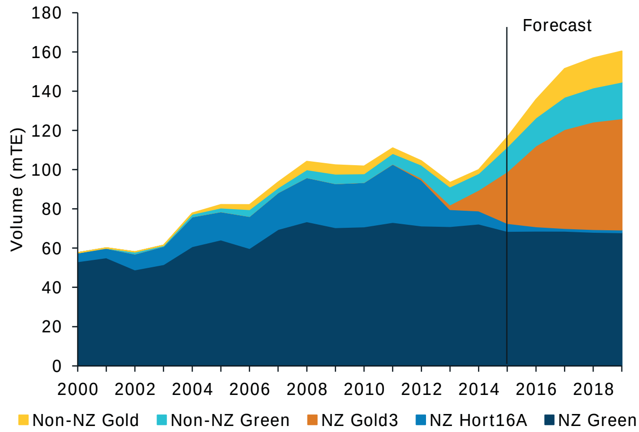
NEW ZEALAND'S PRODUCT MIX

Prior to the body blow the New Zealand industry took from the discovery and spread of Psa in 2010, the industry had ambitious plans to triple its export earnings by 2025. Most of this was to be driven by increases in orchard productivity and changes in the varietal mix. These plans have changed, but only slightly.

This year's crop is now back to pre-Psa levels after the significant re-grafting effort from Hort16A to Gold3[1] in 2012 begins to bear more fruit. The former gold variety was more susceptible to Psa. **Total export earnings are expected to hit $1.2 billion in 2015**, but more importantly there are **plans to grow this to around $1.8 billion by 2020.**

The bounce back from Psa is a remarkable story in itself (more on this later). But to now be on track to grow aggressively over the next 5 years is even more so. Even more importantly, all the growth is expected to be in Gold3, with volumes expected to hit 50-60 million trays in 2018. **This means 45-50% of the annual crop will be of the Golden variety marking a significant transformation of the New Zealand industry into a genuine multi-crop industry.**

FIGURE 3. ZESPRI'S VOLUMES BY VARIETY



Source: ANZ, Zespri

Zespri controls all the intellectual property of all the kiwifruit varieties it markets, except Hayward green. Globally the industry is heavily dependent on the green Hayward cultivar, which is generally viewed as a commodity. Many other producers lack the co-ordination of Zespri, and so damage the green category by oversupply, and low price offerings of often poor quality fruit. This puts pressure on New Zealand green returns despite better quality and taste standards.

Prior to the spread of Psa, the global industry was racing ahead to commercialise new variety's to reduce the dependence on the green Hayward. The race was enhanced by the success of Hort16A, which had achieved the twin goals of substantial price premiums and higher yields per hectare – a very potent combination for net returns.

[1] Gold3 is a large-fruited A. chinensis selection that received high taste scores in sensory trials in Japan and Europe from 2008-2011 and that develops yellow flesh colour approximately two weeks earlier than Hort16A. The Gold3 vine yields well, in fact better than Hort16A, and the fruit size is large. The fruit was able to be harvested and packed with ease because of the absence of a beak. On orchard:

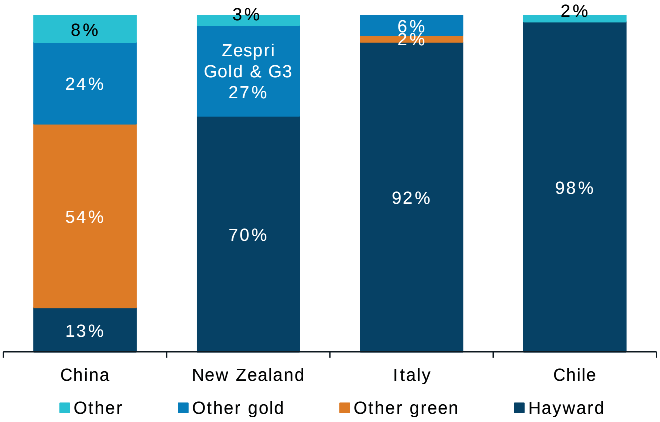
- Beakless;
- Naturally 120g on average;
- Canopy when brought down is less vigorous than Hort16A;
- Stringing of leaders and laterals showed good results and is recommended;
- Attractive to bees;
- Bird risk at budbreak similar to Hort16A; and
- Skins sensitive December to January but more robust at harvest than Hort16A.

Reports from picking contractors and growers and post-harvest suppliers indicate that Gold3 was significantly easier to harvest and pack than Hort16A, largely as a result of the low level of on-vine rejects, it's large size and the lack of a beak (meaning less picking damage).

FEATURE ARTICLE: KIWIFRUIT REVIVAL

Investment was ramped up with the goal to find cultivars that produce large fruit with a pleasant appearance, good colour, delicious flavour, high dry matter content, resistance to drought and disease, and a long shelf life. The race was enabled by the vast untapped resources of germplasm in the wild in China. Numerous cultivars with various permutations of skin surface (smooth or hairy), skin colour (green or golden), flesh colour (gradations of green, gold or red), shape, size, and maturity date have now been created and more are on the way.

FIGURE 4. SHARE OF KIWIFRUIT VOLUME BY VARIETY: NZ VS KEY COMPETITORS



Source: ANZ, Belrose, Zespri

Most of the new varieties are only sold in China at this stage, but a number of foreign entities, including Zespri and Enza, have made limited plantings of some of the golden and green varieties, as well as carried out tests of red-fleshed cultivars in other markets. **As yet, none of them have shown the potential to become a major commercial variety that performs consistently** under normal seasonal and packaging/transportation conditions. So their overall impact on the total kiwifruit market has been limited-to-date.

Golden cultivars appear to be the more susceptible to damage from Psa than green varieties. That said, the New Zealand industry is confident that the **new Gold3 cultivar will be sufficiently resistant** when complemented by good management and disease control practices. With most other countries still trying to find suitable commercial cultivars, still being challenged by Psa, and needing to address other production/quality issues, this potentially limits near-term competitive pressure.

The potential for major competitive pressure is likely to come from China, which has increased its investment and plantings in new cultivars. Particular cultivars showing promise are the likes of Jinyan and Jintao, with a significant proportion that were planted in recent years yet to bear fruit and the former being touted by some to possibly account for a significant proportion of the planted area in China in the not so distant future. So watch this space.

OFFSHORE SOURCING

Part of the industry's strategy has been to maintain a presence on the retail shelf all year round. The reason has been to keep the Zespri brand front and centre, as well as maintain the products shelf space and not be squeezed out by competitors during the off-season (i.e. by other kiwifruit, or another different type of fruit). Retailers generally like some category presence through-out the year too.

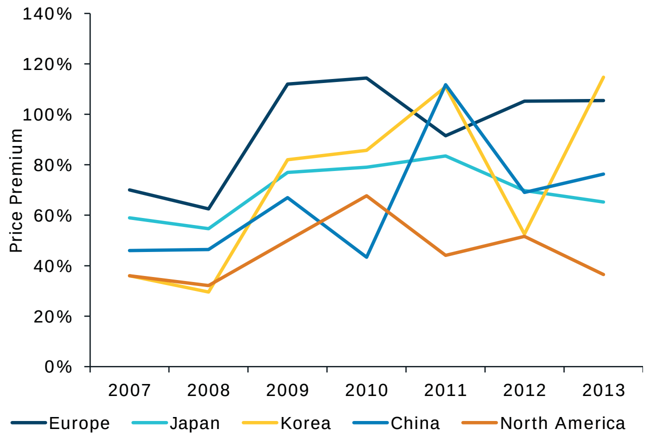
The majority of customers are very loyal to the Zespri brand for what it stands for and the quality of product. Across all markets the most important consumers are those who eat kiwifruit at least once a week. **Zespri estimate these loyal consumers account for 36% of New Zealand's consumers across core markets, but together they eat 86% of the total volume sold.** To keep them coming back for more, all year round supply is required.

To maintain a year round presence Zespri has partnered with Northern hemisphere growers to produce fruit during the New Zealand off-season. Fruit is now grown in orchards in Italy, France, Korea, and Japan. With the significant forecast growth in production of New Zealand fruit this is expected to be matched (not quite to the same extent) by growth in Gold from Italy and France over the next five years and incremental increases in Zespri Green volumes (see Figure 3).

NEW ZEALAND'S EXPORT FOCUS

New Zealand is estimated to account for around one third of the global trade in kiwifruit by volume, but captures a significantly high proportion of the value. This testament to the power of New Zealand's brand, better market access, strong supply chain relationships and intellectual property in producing and exporting quality fruit.

FIGURE 5. IN-MARKET PRICE PREMIUM BETWEEN NEW ZEALAND AND CHILEAN GREEN KIWIFRUIT



Source: ANZ, Zespri

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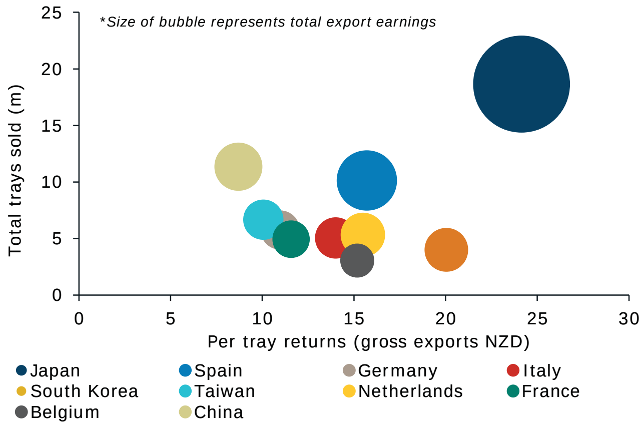
This is encapsulated in the consistently significant price premium New Zealand kiwifruit manages to extract versus its competitors, such as Chile. As an example, over the last five years the price premium of New Zealand green kiwifruit has been 50-100% better than that of Chilean fruit across the main export regions.

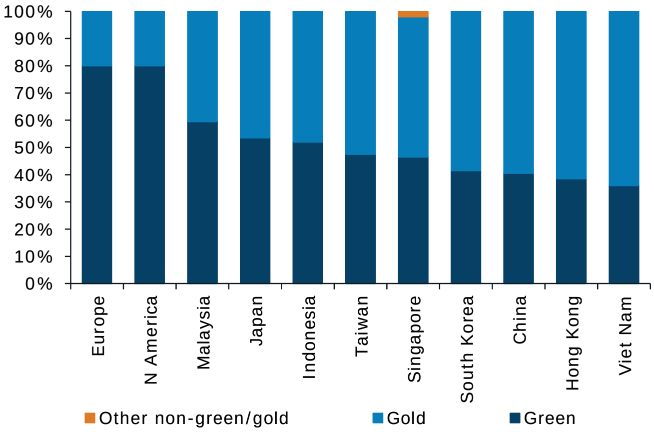
FIGURE 6. TOP 10 MARKET COMPARISON IN 2014



Source: ANZ, Zespri

New Zealand's top markets are Japan, Spain, China, Taiwan, South Korea and Western Europe. **There is a stronger cultural preference for Green kiwifruit in Europe; whereas Asian consumers tend to prefer the sweeter tasting Golden varieties.** This is reflected in the marketing mix with a much higher proportion of Green sold to Europe and Gold to Asia.

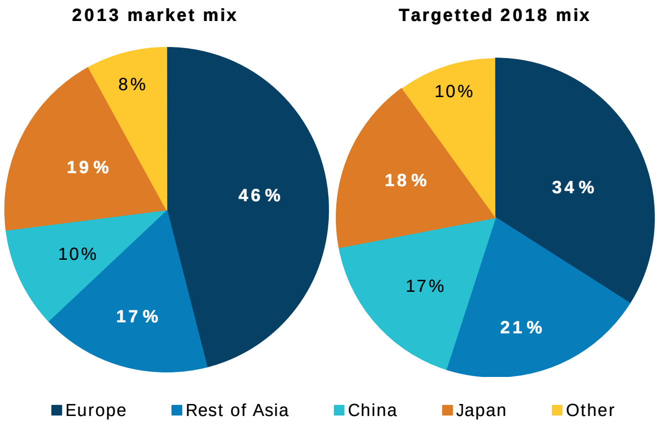
FIGURE 7. NEW ZEALAND'S KIWIFRUIT VALUE MIX BY CULTIVAR AND MARKET (PRE-PSA IMPACT)



Source: ANZ, Zespri

The highest returning markets on a per tray basis are Japan and South Korea, followed by Western Europe. Of course currency fluctuations can have a big impact too from year-to-year. The plan – with increasing volumes of Gold coming through – is to further develop new markets, such as China, the Middle East, South East Asia, India and Brazil, targeting the fast-growing middle-income earners who want tasty, safe, fresh, healthy produce. This will reduce the proportion of fruit sold to Europe over coming years.

FIGURE 8. CLASS 1 GLOBAL MARKET MIX



Source: ANZ, Zespri

Sales in China have increased at around 19% per annum from 1999 and Zespri are forecasting this rate of growth to continue until 2020, becoming New Zealand's largest market in a few years' time. There are also plans in place to continue to serve and exploit new opportunities in long-standing developed markets, such as Japan, Europe, Korea and Taiwan.

THE ZESPRI STORY AND INDUSTRY STRUCTURE

The person responsible for the start of Zespri Kiwifruit is Hayward Wright, and his exceptional green thumb. In 1928, with the Bay of Plenty's rich volcanic soils and mild climate, Hayward Wright developed a new variety of kiwifruit and ever since, the "Hayward" variety has been grown and exported all over the world. The first exports of kiwifruit from New Zealand were in 1952, to England.

In the years following, the industry expanded rapidly with entrepreneurial growers establishing orchards across the Bay of Plenty and in other regions. Growers banded together to pack and export their fruit overseas and competed against each other for markets. In the 1970's, the Kiwifruit Marketing Licensing Authority was formed to provide growers with control over their industry structure and regulate the activities of exporters. This structure enabled grade standards to be established and a coordinated approach to marketing be undertaken.

In the mid-to-late 1980's the New Zealand kiwifruit industry faced a crisis. The rapid expansion of orchards in New Zealand led to large crop volumes above and beyond that of global demand. The New Zealand dollar was rising and interest rates were high. As such, the price of kiwifruit dipped to an all-time low. Growers faced financial hardship and multiple exporters were competing against each other – driving prices, margins, and grower returns down further. It was at that point that New Zealand growers took the first steps toward establishing the current industry structure.

The current export regime for kiwifruit was established in 1999 through the Kiwifruit Export Regulations. The reform was driven by two concerns. First, that the old Kiwifruit Marketing Board was not an adequate commercial structure for the marketing of kiwifruit for export. And second, the Board was acting as both regulator and exporter, and was not subject to adequate controls. **The solution was to separate the regulatory and commercial functions of the Board, and convert the commercial functions into a company – Zespri – owned by growers.** The expectation was that the growers would then be able to control Zespri by exercising their shareholder rights.

Zespri was created and given the right to be sole exporter of New Zealand Kiwifruit outside of New Zealand and Australia. The reforms left future scope to revisit these facets in light of experience and changing commercial conditions. **But it also provided for collaborative marketing and export programmes between Zespri and other exporters.** This was implicit recognition that a single point of entry may not fully maximise overall economic opportunities and returns. Collaborative marketing programs are approved by the industry regulator Kiwifruit New Zealand (KNZ).

TABLE 4. KIWIFRUIT INDUSTRY ROLES

Growers	Producers	Grow fruit for export, respond to market signals
NZKGF	Grower representative body	Represents growers interests to industry and others
Kiwifruit New Zealand	Industry regulator	Authorises Zespri to export, approves collaborative marketing programmes, monitors and enforces regulations.
Zespri	Marketer/ exporter	Sole buyer of fruit for export to markets other than Australia, communicates market signals to growers.
Collaborative marketers	Marketer/ exporter	Run approved programmes to export fruit in collaboration with Zespri.
Post-harvest sector	Managing fruit between the orchard and wharf	Commercial relationship with both growers and Zespri packing and cool-storage of fruit and order fulfilment for export.

Source: ANZ

At first glance Zespri has unusual power. It could be argued there are **opportunities for largesse, inefficiencies and the ability to profit at growers expense.** A number of realities and certain checks and balances help prevent this though, including:

1. **The industry operates in a small category within the very large (650 million tonne) global fruit sector.** There is competitive pressure from a range of other high quality fruit offerings. A constant oversight in regard to those arguing against consolidation in key industries and dominance by a major player (i.e. they rather support a free market model to drive competition), is the reality that the real competition is offshore and not onshore, and competing offshore requires some scale.
2. Outside the regulatory functions performed by KNZ, **many industry decisions are made in consultation with input from Zespri, the growers represented by NZKGF and the post-harvest sector. Almost all major industry decisions are in consultation with the three parties.** Such decisions include the payment incentive structures for growers, through to initiatives to address and manage Psa.
3. **Only growers can buy shares in Zespri** – this restricts new investors to growers.
4. **Shareholders in Zespri can only vote to the extent of their production** – this ensures that non-supplying shareholders, such as growers who have sold orchards, have no control. It also ensures that although growers can acquire shareholdings, which exceed their proportion of industry production, their control in Zespri is limited to their production.
5. While there has been a build-up of non-supplying shareholders (i.e. ex-growers who are still allowed to retain shares) and those with more shares than their production in recent times. **Under the recent industry strategy review (yet to be past into law) there is to be a transition to cap the number of dry shares that can be held and the proportion that receive a dividend.** The proposed cap is a ratio of four shares to one tray of production. After three years, dividends will also stop for dry shareholders and for over-shared shareholders on the portion of their shares that exceed four times their production for three years. **This will reduce the financial incentive to retain shares for dry shareholders and above this cap.** Some believe the transition period is too long and cap is too high. But there seems room to move on both if shareholder support can be gathered.

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6. **A majority of Zespri's directors are grower directors and all are elected by shareholders, whose votes are tied to production.** There are eight directors in total – five growers and three independents. **This would seem to be a good mix to ensure growers' interests are well represented, but other expertise is brought in to fill any gaps.**
7. **Zespri's commission is now transitioning to be determined by a set formula that prevents it achieving abnormally high profits to the detriment of fruit payments to growers.** Historically Zespri's commission has been negotiated every three years by an industry committee that included elected grower representatives, this is set to change with the recent vote in the Kiwifruit Industry Strategy Project (KISP).
8. **The marketer of fruit takes possession at the wharf, which allows onshore competition right up to the wharf.** A very competitive post-harvest sector has developed, meaning that growers' costs are pushed down by competition and there is a commercial incentive for the post-harvest sector to continuously improve.
9. **Collaborative marketing opportunities, alongside Zespri for other exporters to increase overall grower returns.** However, there has been some recent challenges to its effectiveness with Turners & Growers applications being turned down (see more below).
10. **Active engagement of growers through the grower organisation NZKGF.** NZKGF exists separately from Zespri and this ensures that growers have an advocate without commercial conflicts.

All of these features of the industry structure work together to help growers retain industry control.

However, we would be amiss not to point out some of the shortcomings. Grower control can be far from ideal; witness the issues across a number of co-operatives in New Zealand. Some in the industry have sighted certain brokerage fees as to high reducing direct returns to growers. Transparency of Zespri's spending and the value of certain marketing activities have come under fire from time to time too. There has also been the well documented invoicing issue, with a distributor in China and subsequent fraud investigation.

The existence of substantial and on-going collaborative marketing programmes seems rare too and any are typically limited to specific markets, specific retailers, and specific fruit sizes. Some would say the effort to get a collaborative marketing programme approved is too onerous and this reduces product and marketing innovation, as well as diversification. **Of course there is the flipside argument too that appropriate due diligence should be done to ensure New Zealand's brand and associated product premiums aren't undermined.**

Turner's & Grower's challenge to the current industry structure in 2009-2011 seemed to have stemmed from a frustration in getting a collaborative marketing programme approved, as well as the potential terms, for the new kiwifruit varieties it had invested heavily in. It is now growing and marketing these new varieties offshore, which seems like a loss to New Zealand's industry. The company wanted a complete deregulation as they believed that this would promote more efficiencies and increased innovation, investment and diversification. It also suggested a halfway-house of an independent body, such as the Horticultural Export Authority to grant export licences, with an express provision for those who had new cultivars.

All these issues suggest there are some further efficiency and effectiveness gains to be had from the current industry structure, as well as transparency and alignment of incentives to deliver optimal outcomes for growers. **Ultimately it is performance that counts.** Any failure to address shortcomings, or delivery would result in industry fragmentation. **Bringing the industry back from the brink of Psa, a stronger run of grower returns, the continued compelling offshore performance for Zespri's brand and margins sees the current industry structure delivering for the majority.**

The confidence and support for the industry's current structure and performance was recently highlighted in the outcomes of the KISP. **Two-thirds of growers – representing 80% of production – voted 97% in favour of supporting the single point of entry structure (with a few tweaks). This level of support and engagement is almost unheralded** across the other primary industries where the average voter turn-out usually languishes at only around 40%.

THE ROAD TO RECOVERY FROM PSA

To recap, **Psa is a bacterium**, which when it infects kiwifruit vines can result in: leaf spotting, cane/leader dieback, and – in extreme cases – vine death accompanied by the production of exudates (a rusty red liquid discharge). Depending on the severity and management of an infection outbreak it can have anywhere from minimal impact on annual production right through to completely wiping out an orchard. It carries no risks to human or animal health and does not affect plants other than kiwifruit vines. This meant

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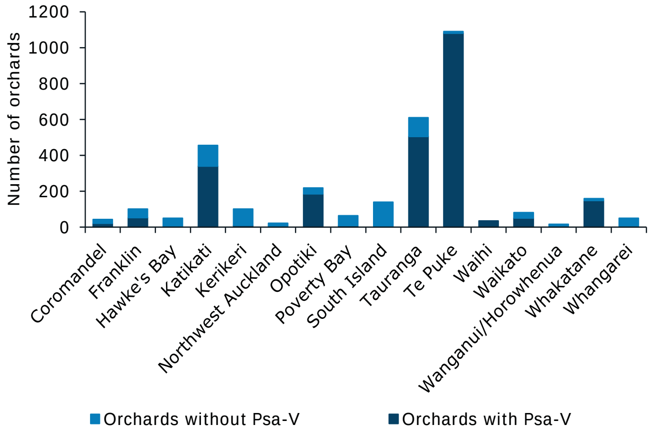
there weren't any major market access issues when Psa was discovered. It is difficult to contain though as it is spread via windborne pollen, strong winds, and heavy rainfall. It can also be spread by footwear, vehicles and orchard tools, animals and humans.

Since Psa was discovered, the destructive effect of the disease is obvious, both from the New Zealand industry experience, and from observing how the disease has rapidly spread in other countries, such as Italy and France. **In fact, Psa is a global kiwifruit problem, with much of the world looking to New Zealand to beat Psa. This is because the kiwifruit industry's integrated structure and long-standing commitment to research and development** makes it well placed to have a coordinated, well-funded response.

The industry was ill prepared when Psa was first found. This was despite the fact that Psa had been causing major damage to orchards in Italy – where some New Zealand industry members were involved – and there was no plan in place to respond for if it were to show up in New Zealand. **Today 87% of New Zealand's kiwifruit area has been identified as having Psa, and only Whangarei and the South Island haven't had a case detected yet.**

FIGURE 9. PSA STATUS OF ORCHARDS BY REGION



Source: ANZ, KVH

THE COST

There have been a few studies on the economic cost of Psa. The Agribusiness and Economics Research Unit of **Lincoln University estimated a cost of between $310 and $410 million in net present value terms between its discovery and 2016.** Over a longer time period (15 years) they estimated this could increase toward $740 and $855 million, but these future costs were largely dependent on the speed and extent of recovery. **The success of Gold3 over the next couple of harvests will determine the ultimate industry cost.**

The effect of Psa is at its most destructive in the individual orchard. Growers with infected orchards had to cut out some, or all, of their orchards and as a result lost part or all of their income for a period of time. The establishment of new vines and re-grafting to Gold3 since 2012 has come at a substantial capital cost too. **Even when growers have not lost vines as a result of Psa, the disease has caused increased costs and changes in orchard management practices.** This has added yet another variable into the mix of factors they must balance to ensure their orchard remains viable.

The impacts haven't solely been limited to orchards though, with a number of service providers suffering via cancelled orders and reduced turnover during the 2011 to 2014 period. Many had to downsize and restructure during this period to make it through.

PATHWAY TO RECOVERY

In reaction to Psa the kiwifruit industry immediately organised an industry wide response. Initially the intent was to contain and eradicate the disease. Once that was found to be impossible, the industry worked to minimise the damage to the industry and identify a pathway for recovery.

The unified nature of the industry meant that the response was quick and decisive. With support from the New Zealand government, KVH was set up to manage the response within a month. The industry had virtually no experience in dealing with any new serious pest, or diseases so it essentially started from scratch. **To meet the Psa challenge, KVH developed four main work streams for the disease that included control, management and finding appropriate solutions to enable recovery.**

The first work stream was biosecurity controls to contain and limit the spread of Psa as much as possible. The main part of this has ended up being the implementation of a national pest management strategy. This included different regional approaches to manage Psa based on the presence/ absence of infection in each region. In the recovery regions the focus is now on reducing Psa inoculum levels and supporting the successful establishment and recovery of the production of new varieties (specifically Gold3).

The second work stream was the establishment of a research and development program of work, alongside grower extension and technology transfer to help manage and minimise the effects of the disease. This has seen a number of new practices and sprays trialled and implemented on orchard, which are making a difference. A total of $20 million has been committed to Psa research and

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development so far with the Zespri's innovation team being responsible for managing the programme.

The third stream was the development of a pathway back to prosperity based on research and development and on orchard observations. A major part of this has been the re-grafting and successful transition away from Hort16A to Gold3, which started in 2012. **The last work stream was grower support and welfare** through all the difficult times that they have experienced since the disease was first discovered.

Other key facets alongside the quick decision to establish a dedicated body to manage the response included:

1. **Its integrated nature and close working relationships** between different entities within the industry.
2. **Existing governance systems**, which allowed united leadership.
3. **Extremely skilled leadership that operated effectively under enormous pressure.**
4. **Established relationships with Government and the banking sector.**
5. **Focus on managing the human impacts** of the bacteria, not just the bacteria itself.
6. **"Can do" attitude and ability to adapt.**
7. **Substantial (past and current) investment in the kiwifruit breeding programme.** This meant there were new cultivars, such as Gold3, which could be deployed at short notice as they had already been developed and commercially tested (i.e. commercially grown and some testing in-market for packaging, storage through to consumer feedback).

The industry is not entirely out of the woods yet as there are still both production and market risks associated with the recovery pathway. While considerable progress has been made towards understanding plant protection and management strategies, Psa is still relatively new to New Zealand and the last two seasons has delivered fairly favourable seasonal conditions (i.e. from a disease susceptibility perspective). From a markets perspective there are risks around acceptability of Gold3 and ability to find enough higher paying markets for the increasing volumes that will be delivered over the coming years. These are risks at present, but the industry is investing heavily in both areas to ensure they are appropriately managed.

The jointly run Psa research and development program highlights this investment. It pulls together the best scientific minds in New Zealand and offshore to understand Psa, and then develop and produce the tools needed to operate in a Psa environment.

KIWIFRUIT RETURNS

Kiwifruit returns are influenced by many factors right from the orchard through to end consumption. New Zealand is fundamentally considered a high cost producer given our distance to market and higher cost of labour, transport and handling, compared to our main Southern Hemisphere rivals in Chile.

In-market there are many demand and supply influences that can impact on returns (see feature article in April *Agri Focus* for more discussion), but to mitigate this, Zespri has established meaningful brand reputation and built up equity through long-term commitment and investment. **Zespri is now one of the top-five most recognised fruit brands in its key markets. It is seen to represent quality, great taste, sustainability and food safety.**

The Zespri brand, and the associated values and promises it delivers, **has generated meaningful price premiums** for the New Zealand grower and supports strong retail customer and trade relationships. These relationships enable Zespri to further develop the product categories and underpin product delivery to consumers.

The core factors sustaining the strength of the Zespri brand and system are:

1. **Consistency of supply of a high-quality and high-taste product supported by a world-leading supply chain** where growers receive market-based payments reflecting the quality of their fruit.
2. **An innovative portfolio of Zespri-exclusive product offerings**, including new and novel products.
3. **Significant investment and support of brand marketing and category growth.**
4. **A comprehensive understanding of the health benefits of kiwifruit.**
5. **Deep penetration of core markets.**
6. **Focused development of new high-growth markets.**
7. **Year round supply of Zespri branded fruit** with New Zealand supply augmented with product from the Northern Hemisphere. This enables Zespri to support its branded offering to consumers all year round, as well as offer a category management solution to large retailers. This is particularly important to support Zespri's category leadership position and the commercialisation of new varieties into a fruit that is consumed every day.

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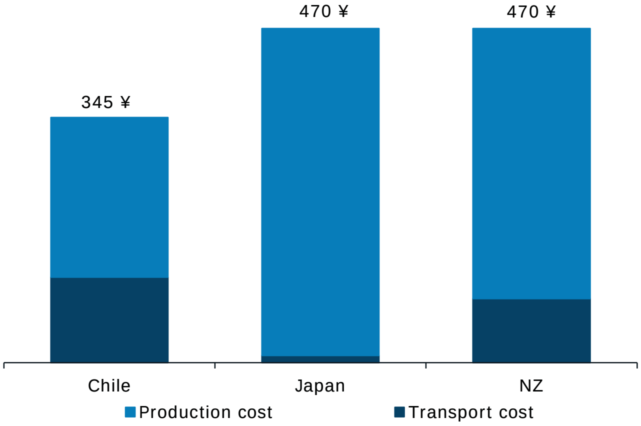
FIGURE 10. COST OF PRODUCTION TO DELIVER HAYWARD TO JAPAN

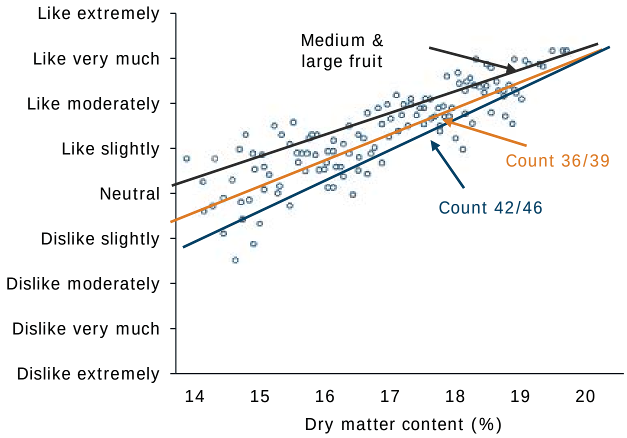


Source: ANZ, Zespri

These factors form the New Zealand kiwifruit industry's competitive advantage and are underpinned by the single point of entry.

On many levels the price incentives and direct feedback growers receive for their fruit is unparalleled across most primary sectors in New Zealand. Because off-shore marketing is co-ordinated, it means that markets have a single channel from which to deliver feedback to growers, helping them to grow the most marketable fruit. Zespri is able to feed these market signals back to growers via the payments system.

FIGURE 11. PREFERRED TASTE PROFILE OF GOLD3



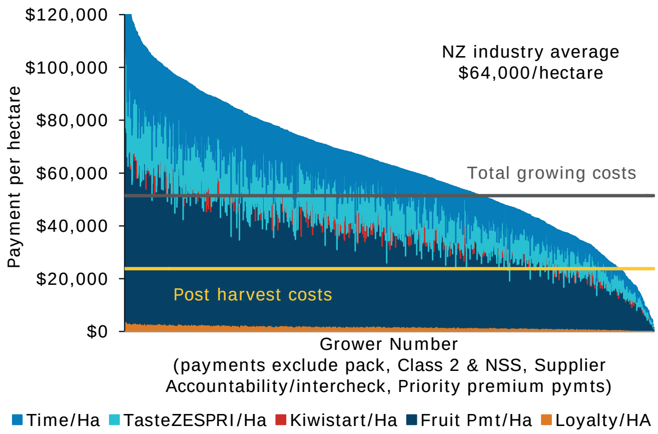
Source: ANZ, Zespri

A prime example of this sort of market signal is taste. **There is an accepted relationship between kiwifruit's dry matter content and good taste.** The markets pay more for good tasting fruit. Dry matter can be tested. **This allows Zespri to make a specific taste payment which incentivises growers to use orchard practices to increase dry matter. The result is growers provide better tasting fruit** because there is a clear market signal with a financial incentive attached.

This in turn allows Zespri to manage its inventory so that the best tasting fruit goes to markets that are prepared to pay top dollar. Similar market signals and financial incentives exist for the preferred fruit sizes (larger) and time of sale. **Without the co-ordinated approach it is unlikely such clear market signals would exist.** Price competition between multiple exporters would mean that the growers' main price signal would be at the exporter level. This could polarise the product offering between commoditisation and premium positioning impacting on the New Zealand brand.

The Holy Grail for orchard-gate returns is good price premiums, high yield, good sized fruit and good tasting fruit (high dry matter). Overall class 1 yield per hectare and fruit size are the most significant drivers of revenue and profitability for both major varieties (see distribution chart of revenue returns and make-up below). The taste grade is also a significant contributor too, but more so for Gold. In 2014/15 the taste grade payments are expected to make up 17% of total fruit and services payments for Green and 41% for Gold.

FIGURE 12. ZESPRI GREEN KIWIFRUIT- FRUIT & SERVICE PAYMENTS 2013/14 (based on final results)



Source: ANZ, Zespri

In 2014/15 orchard gate revenue after post-harvest costs averaged $53,884/ha for Green and $73,890/ha for Gold. For Green this was an all-time record driven by good in-market prices due to a shortage of Chilean product and low post-harvest costs (lower fruit loss & packaging efficiencies in recent years), as well as higher yields. **While average Gold orchard gate revenue was down for 2014/15, this did not represent a steady state** with a still heavy Psa impact and many Gold3 canopies yet to reach full maturity (meaning lower than potential yields).

Deducting average post-harvest and on orchard costs shows average net orchard-gate returns of $27,200/ha for Green in 2014/15, which is

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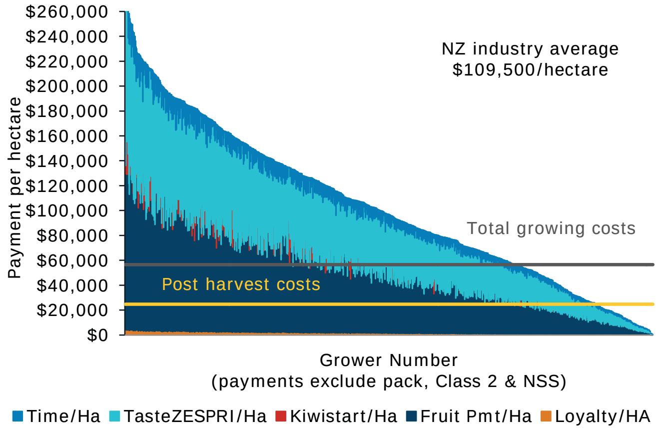
well up on the five-year average of $12,700/ha. Current orchard prices have averaged $300,000-$350,000 per canopy hectare recently (including the 2015 crop). After deducting the expected returns for the 2015 crop it implies a rate of return of between 7-8.5%. Of course this was a record year for returns and **medium-term prospects are generally expected to be closer to the $5/tray mark. This implies net orchard-gate returns closer to $15,000-$18,000/ha depending on yield assumptions, which implies a rate of return closer to 5-6.5%.**

The other aspect is these are average figures. **The top green growers (defined as top 20% for gross orchard revenue) have outperformed the average by nearly $36,000/ha over the last several years. This has generally been through higher yields, and better tasting and sized fruit.** Generally yield sets the top quartile apart, followed by orchard-gate return per tray. **Cost structures are generally higher to achieve outperformance, but even if you were to factor in an extra $15,000/ha of growing costs (we consider $40,000/ha to be the upper band for growing costs) the top green orchards could be delivering a rate of return that is up to 7% above the average.**

FIGURE 13. ZESPRI GOLD KIWIFRUIT- FRUIT & SERVICE PAYMENTS 2013/14 (based on final results)



Source: ANZ, Zespri

While the Golden varieties seem to be more susceptible to Psa, their advantages lie in the ability to be able to extract a price premium above Green, as well as to produce more fruit per hectare for a similar cost structure. The new Gold3 variety is expected to yield even more than Hort16A when the canopy is at full maturity. **Assuming a medium-term price of $6.5/tray for Gold3 and average yield of 13,000/tray/ha this equates to gross orchard-gate revenue of $84,500/ha. A similar cost structure to green (which is what Gold achieved anyway) implies net orchard gate returns of $53,800/ha.**

Current orchard prices have averaged $425,000-$500,000 per canopy hectare recently (including the 2015 crop and license rights). Assuming a similar cost structure to Green and after deducting the expected returns for the 2015 crop **it implies a rate of return of between 11.5-13.5%.**

Similar principles to Green are expected to apply for Gold3 top performance. Optimising yield and taste is probably expected to be of more equal importance in achieving extra revenue per hectare. In recent years the top grower returns have outperformed the average significantly, but it's difficult to disentangle Psa effects (price, yields and different re-grafting periods). So we will have to wait a few more years to get a read of the possible spread in performance, but it looks like it could be reasonably substantial.

While orchard prices might seem expensive to some at present and a far cry from just a few years ago, the returns look reasonable. Yes, there is "risk" in the product (i.e. Psa to manage) but the returns still look very good when benchmarked against other parts of the primary sector. Current investors are those who have an existing background in the industry and pack-houses looking to secure future through-put after substantial investment in packaging and storage facilities in recent times. There has also been the emergence of a few equity partnerships and syndicates in recent times. It will be interesting to see how they perform given a strong industry background seems to be required to deliver top on-orchard performance.

THE MONTH IN REVIEW

SUMMARY

Parts of the East Coast of both Islands remain dry, and feed positions are expected to be tight during the winter. While milk supply looks like it grew slightly in 2014/15, supply potential in 2015/16 looks lower due to high cull-cow turn-off throughout the season. The turn-off in breeding ewes throughout the 2014/15 year also implies a smaller flock and 2015 lamb crop. The kiwifruit crop rebounded to pre-Psa levels, while the 2015 vintage was 27% smaller.

MOTHER NATURE

While there has been plenty of rainfall through the autumn on the West Coast of both islands, it has been far patchier on the East Coast. In the South Island, rainfall for May was below average for Canterbury regions. This made for ideal planting conditions in Mid-to-South Canterbury. However, **North Canterbury remained extremely dry, having received less than 50% of its normal rainfall so far this year.** Feed positions will be very tight during the winter, with no autumn growth and not a lot of supplementary feed (crops, etc) left. On the East Coast of the North Island, coastal areas are dry too and feed positions are behind where they were at the same stage following the 2013 drought. More rain is required while soil temperatures are still favourable to provide early winter growth. North Canterbury has the highest soil moisture deficit in the country, while eastern coastal areas in the North Island also remain in soil moisture deficit. The rest of the country is sitting close to historic averages for soil moisture. Some parts of the West Coast of the North Island are particularly wet, such as the Manawatu.

DAIRY

Cows are now dried off, except for some that will be winter milking for domestic supply. The 2014/15 production season will be remembered as a game of two halves, with incremental growth (3%) the end result. We saw a stellar first seven months, with milk supply up 5.4% y/y, followed by a flat last five months as dry conditions bit during the summer months. There appears to have been a late autumn flush with supply bouncing back in the North Island, but not the South Island. North Island supply is likely to finish the season up 4%, whereas the South Island will only be up a touch.

The focus is now shifting to milk production potential in 2015/16. The offtake of cull cows and any new dairy start-ups will set the scene for 2015/16. Seasonal conditions, the milk price outlook, supplement availability/price, and cash-flow constraints will influence the yield outlook as the season evolves. **Cull cow slaughter has been elevated throughout the season** as farmers have turned off low-performing cows and excess heifers in response to the lower milk price and seasonal conditions. The final tally won't be known until the start of July, but **at the start of May cull cow turn-off was up 146,000 head (+24%) on the same period last year.** Not all of the increase will be dairy cows and there could be lower turn-off at the end of the season due to earlier culling. But it seems reasonable to expect that the **number of cows available to milk in 2015/16 could be more than 100,000 (2%) lower.** While there might be some offset from industry estimates of 30 new dairy conversions (21,000 cows), **when combined with cash-flow constraints and the likely use of lower-quality feed types, milk supply potential still looks lower.** As always, seasonal conditions will have a big say, but it seems New Zealand supply could be back 2-4%.

MEAT AND FIBRE

Lamb slaughter is running slightly ahead of the same period last year. There appears to have been a slight uptick over the last two months after a pull-back from mid-February to April. Lambs have been slow to finish in the South Island due to poor seasonal conditions. This is reflected in sluggish South Island production and lower average weights. **However, the focal point has been mutton turn-off, which has been higher than industry forecasts.** While production is likely to slow over coming months, it is still pointing toward a 200,000-300,000 decline in breeding ewe numbers in 2015/16. This, combined with challenging mating conditions in many eastern regions, points to a smaller lamb crop in 2015.

Year-to-date wool exports have been stronger than expected (+3%). This is despite a reduction in sheep numbers (-3%) and high sheepmeat turn-off earlier in the season. It suggests some inventory liquidation from wool that was held over from 2013/14.

HORTICULTURE AND VITICULTURE

This year's Kiwifruit Gold crop is expected to be around 30 million trays, with 25 million being the new Gold3 variety. Around 70 million trays of Green are expected. The 2015 Marlborough grape harvest was completed with very good quality being reported. **The 2015 vintage has been assessed as 326,000 tonnes, which is 27% smaller than last year.**

Other points to note: **the citrus industry is expecting a smaller harvest**, due to the crops bi-annual bearing nature. **The Manuka honey harvest has been reported to be reasonably strong. Forestry harvesting rates have dropped** on smaller wood-lots due to softer log export prices.

RURAL PROPERTY MARKET

SUMMARY

The rural property market continues to dance to its own tune. Total turnover has dropped back from the same period (Jan-Apr) last year, but prices over the last 6 months have continued to oscillate at what are historically high levels for many different land uses. Buyer confidence in the long-term food story is commonly being touted as a reason for buoyant prices, but this isn't the sole support factor. A split market appears to be starting to open up with turnover of dairy aligned property on the decline. The big challenge for any buyers of a dairy investment will be funding the cash-flow shortfall through to 2017. This will rule out some buyers, but will create opportunities for others. Opportunities are likely to first come from any distressed assets that come to market and less well located, lower quality properties. Higher quality properties are much less likely to face price pressure and vendors are likely to sit tight if they do.

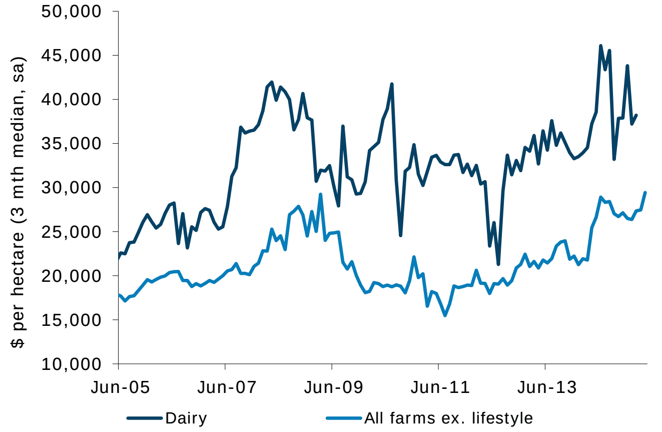
Total monthly turnover of rural properties in 2015 has dropped back to the 10-year average and is down by 10% on the same period last year. The all-farm price measure while it has eased from its peak in November last year it is still historically high and 28% above two years ago.

The drop in turnover in 2015 has centred on dairy aligned property. Total monthly dairy farm turnover in 2015 has dropped back to its 10-year average and is down 17% on the same period last year. Turnover for finishing properties was down 40% on the same period last year, but is still on par with 10-year averages. **Prices for both property types have remained remarkably resilient, with the likes of dairy farms up 16% in 2015 on the same period last year.** Outside of dairy aligned property turnover and prices remain more buoyant, especially for arable and horticultural properties. **The turnover of arable and horticultural properties remains well up on the same period last year. However, sales activity in recent months looks to have had an Auckland and kiwifruit centric bias this distorting average prices.**

FARM SALES BY FARM TYPE

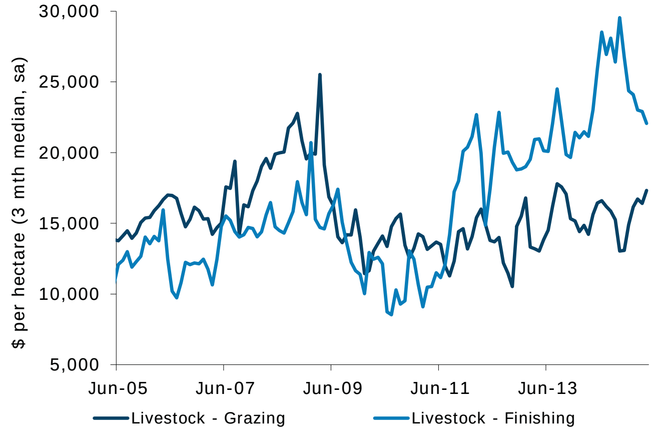
3-Month Seasonally Adjusted		Current Period	Previous Period	Last Year	10-Year Average	Chg. P/P	Chg. Y/Y	Chg. P/10yr
Dairy	Number of Sales	66	64	72	68	↑	↓	↓
	Median Price ($ per ha)	38,200	37,200	33,900	32,300	↑	↑	↑
Livestock – Finishing	Number of Sales	69	64	98	66	↑	↓	↑
	Median Price ($ per ha)	22,100	22,900	23,000	16,300	↓	↓	↑
Livestock – Grazing	Number of Sales	178	196	161	207	↓	↑	↓
	Median Price ($ per ha)	17,300	16,400	16,000	15,500	↑	↑	↑
Horticulture	Number of Sales	73	68	48	43	↑	↑	↑
	Median Price ($ per ha)	250,700	227,600	171,300	152,500	↑	↑	↑
Arable	Number of Sales	33	51	27	20	↓	↑	↑
	Median Price ($ per ha)	45,900	86,800	27,900	29,800	↓	↑	↑
All Farms ex. Lifestyle	Number of Sales	434	437	436	436	↓	↓	↓
	Median Price ($ per ha)	29,400	27,500	25,500	21,400	↑	↑	↑
Lifestyle	Number of Sales	1,824	1,785	1,628	1,520	↑	↑	↑
	Median Price	549,000	544,000	510,000	451,000	↑	↑	↑

FARM SALES, MEDIAN PRICE



Source: ANZ, REINZ

FARM SALES, MEDIAN PRICE



Source: ANZ, REINZ

RURAL PROPERTY MARKET

With the REINZ all-farm measure (which adjusts for compositional differences) continuing to oscillate at record levels, but farm-gate returns for many sectors looking softer than expected the common question is where to from here?

Buyer confidence in the long-term food story is commonly being touted as a reason for prices remaining buoyant, but this isn't the sole support factor. Other positive influences include:

1. **Historically low local and global interest rates.** The low cost of capital has pushed more investors and capital out the credit curve in the search for yield and into higher risk and "different" investments, such as farmland.
2. **A larger pool of buyers than pre-2008, which includes a wider range (country & type) of foreign investor interests and domestic equity investors from outside the sector.** There is also a bigger presence of larger sized corporate farmers that have balance sheet strength to allow them to make strategic purchases during downturns.
3. **Productivity and cost efficiency improvements.** We believe the gains many farmers and sectors have achieved in recent years have been under appreciated.
4. **Lower inflationary pressure in recent times placing less pressure on cost structures compared with the 2002-2011 period.**
5. **A competitive banking and lending environment.**

These five factors alongside the long-term food story suggest a substantial correction in farmland prices is unlikely to be around the corner.

That said there are still plenty of challenges for dairy aligned property, which has driven much of the property market activity in recent times. The current bout of price weakness is likely to shake some investors' confidence, any new buyers will need deep pockets to bridge any cash short fall through to 2017 and then there is still the other substantial challenges of more environmental regulation that is in train in many regions and other compliance related changes (such as health and safety law changes). **Less well located, lower quality properties always face the heat first in any downturn. Higher quality properties are much less likely to face price pressure and vendors that don't need to sell are likely to sit tight if they do.** Ultimately a more fundamental reassessment of medium-term farm-gate returns looks required to shake market confidence.

There will no doubt be some pockets of stress to emerge, and some businesses are already beginning to act with buoyant farmland prices making it an easier decision to move earlier rather than later. As the RBNZ identified in the financial stability review 11% of farm debt in 2014/15 had negative cash-flow and loan-to-value ratios above 70%. Cash-flow for a fully shared Fonterra farmer is forecast to tighten by a further $1.17/kg MS in 2015/16, which means some businesses will require restructuring to get through.

Examining the backward-looking indicators the REINZ dairy land price index (per hectare measure), which adjusts for compositional differences, has slipped (-10%) in recent months, but is elevated compared with the same period last year. Specifically **in the month of March, 38 dairy farms were sold, at a median sale value of $34,200/ha, or $37 per kg MS.** The median farm size was 111 hectares and the median production/ha was 932kg MS. **In the month of April, 26 dairy farms were sold with an average sale price of $37,900/ha, or $35 per kg MS.** The median farm size was 101 hectares and production/ha was 1,088kg MS.

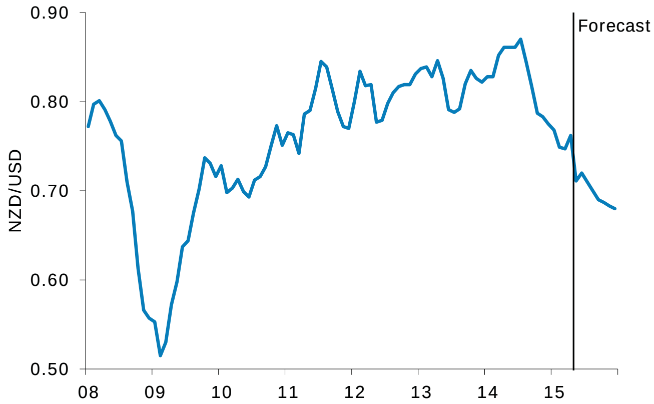
Turnover of finishing properties continues to hover around the 10-year average, but grazing property turnover has slipped slightly below its 10-year average in recent months. **Prices for finishing properties continue to trade at elevated levels despite coming off the peaks of mid-2014.** Finishing property prices have traded a US$22,000-24,000/ha range since the start of the year, which is nearly 40% above the 10-year average. **Grazing property prices have traded a $16,000-$17,000 range since the start of the year; this is a more modest 6% above the 10-year average. The turnover and prices for arable properties has taken off since the start of the year.** Examining the regional data shows an unusually amount of activity centred around Auckland, suggesting the land is being purchased with other future uses in mind.

In the horticulture sectors turnover and average prices have increased. There is no split by sector, but the large proportion of activity has focused on Auckland again and the Bay of Plenty. The Bay of Plenty activity is kiwifruit orchard sales. **Including this year's crop we have been seeing sale prices of $300,000-$350,000/caha for well located green kiwifruit orchards and $425,000-$500,000/caha for gold orchards.** Most of the buyers are those who are well established and have experience in the industry. Many are involved in the post-harvest industry and are looking to secure future supply.

ECONOMIC INDICATORS

EXCHANGE RATES					
	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
NZD/USD	0.711	0.753	0.861	↓	↓
NZD/EUR	0.647	0.676	0.627	↓	↑
NZD/GBP	0.465	0.493	0.511	↓	↓
NZD/AUD	0.930	0.962	0.926	↓	↑
NZD/JPY	88.23	89.85	87.72	↓	↑
NZD/TWI	75.70	79.64	78.99	↓	↓

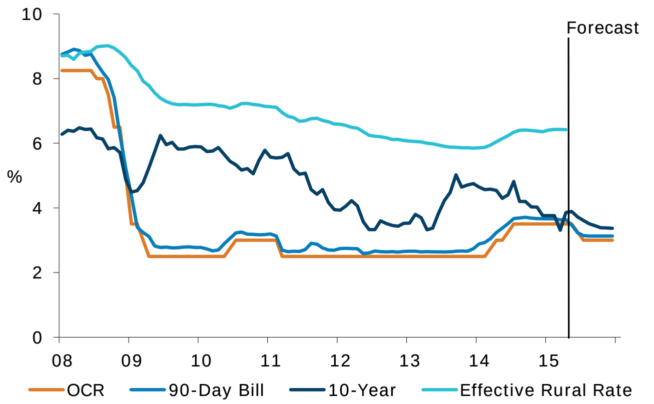
NZD BUYS USD



Source: ANZ, Bloomberg

NZ INTEREST RATES					
	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
Official Cash Rate	3.50	3.50	3.00	↔	↑
90 Day Bill Rate	3.47	3.65	3.38	↓	↑
1 yr	3.32	3.48	3.40	↓	↓
2 yr	3.34	3.43	3.59	↓	↓
3 yr	3.41	3.41	3.78	↓	↓
5 yr	3.59	3.49	4.03	↑	↓
10 yr	3.89	3.64	4.29	↑	↓
Effective Rural Rate	6.42	6.42	6.05	↑	↑
Agricultural Debt ($b)	55.41	54.58	51.89	↑	↑

KEY INTEREST RATES



Source: ANZ, RBNZ

We expect the NZD to continue to recede, but note that the trajectory is likely to be a volatile one. Catalysts for further sharp falls include additional declines in export commodity prices, a firmer USD – thanks to pending lifts in the Fed Fund Rate, global growth uncertainties, tougher economic conditions in China and Australia, and the RBNZ cutting the OCR. Volatility will be driven by the evolution of FOMC and RBNZ interest rate deliberations, market liquidity and positioning.

We expect there to be ongoing downward pressure on New Zealand short-term interest rates. The risk profile across the economy has clearly shifted. The dairy sector faces difficult times, other key export sectors have been facing more pressure in recent time, and the boost from the Canterbury rebuild is waning. Inflation is low and the RBNZ has an inflation target, not an Auckland housing one. With the risk profile across the economy shifting to the downside and inflation low, **we expect the OCR to be lowered by a cumulative 50bps before the end of the year.** The market is now expecting the same, which begs the question what will happen to the NZD if they don't move at all; hint: it'll move up.

The New Zealand economy needs a weaker NZD. Falls in the NZD have not aligned themselves to broader terms of trade and export commodity price trends. This has placed unnecessary stress on the exporting and import-competing sectors.

We see scope for a move down into the mid-60's to realign with export prices and boost tradable inflation. Beyond this there are some fairly key areas of support though:

1. **Even after an expected 50bps of OCR cuts, there is still a circa 300 point short-term interest rate differential with two-thirds of the global economy** (GDP wise). US rates are likely to move up in the second half of this year, but the Fed has signalled the pace of policy normalisation will be gradual and elongated. Printing presses at the BoJ and ECB remain in overdrive, with combined QE equivalent to the peak of the Fed's QE3.

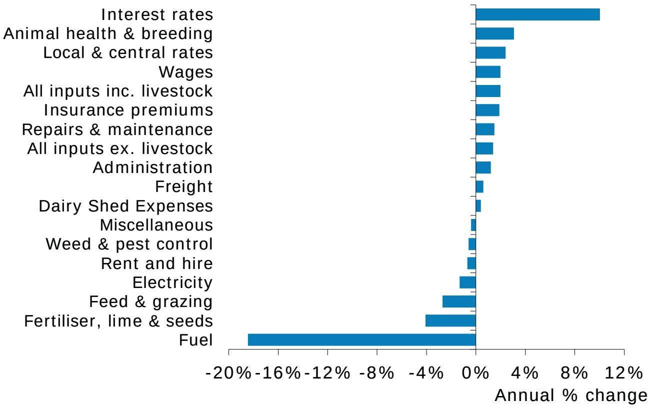
2. **While the New Zealand economy is slowing it remains relatively solid compared with many others.**

3. While international peers may notionally support stronger currencies, they implicitly want weaker ones to support growth; **we live in a world where competitive devaluation is the norm**, making it hard for NZD to continually devalue, unless the easing cycle becomes extended.

ECONOMIC INDICATORS

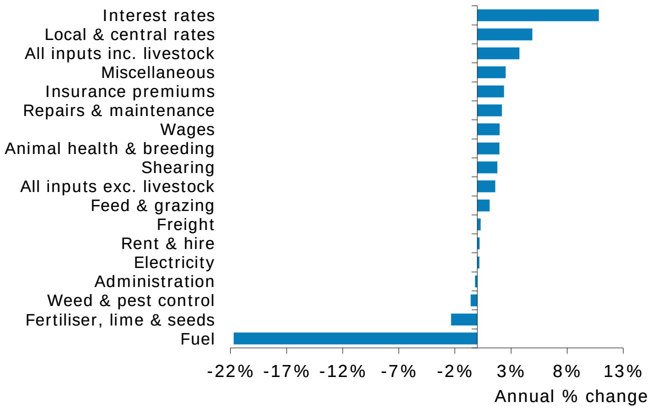
INFLATION GAUGES					
Annual % change	**Current Qtr**	**Last Qtr**	**Last Year**	**Chg. Q/Q**	**Chg. Y/Y**
Consumer Price Index	0.1	0.8	1.5	↓	↓
Farm Input	-0.2	1.9	0.6	↓	↓
Net Imp. Margins PPI	-17.1	-12.9	19.6	↓	↓

FARM EXPENSES MOVEMENT 2014/15 – DAIRY



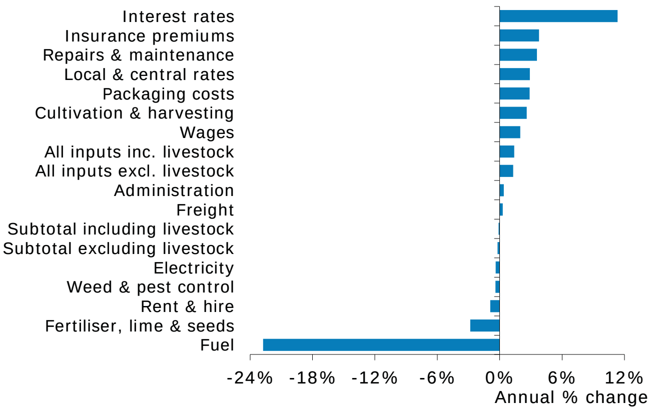
Source: ANZ, Statistics NZ

FARM EXPENSES MOVEMENT 2014/15 – SHEEP & BEEF



Source: ANZ, Statistics NZ

FARM EXPENSES MOVEMENT 2014/15 – HORTICULTURE & FRUIT GROWERS



Source: ANZ, Statistics NZ

Statistics NZ's **latest survey of on-farm cost movements for 2014/15 showed an annual increase of 1.4% for the "all farms" measure (excluding livestock).** This was above general inflation for the broader economy, but follows 3 years of benign farm costs movements. In fact **on-farm costs have only moved up by an average of 1.1% over the last three years. This is a far cry from the 2002-to-2012 period where they moved up by an average 3.2% per annum.**

Cost increases were similar across all farm categories in 2014/15. **Sheep and beef experienced the largest annual increase in farm costs of 1.6% y/y** (excluding livestock). **Dairying experienced a 1.4% y/y increase, and horticulture and fruit growers a 1.3% y/y increase.** For horticulture and fruit growers this annual increase follows a 0.4% decrease in 2013/14, implying little recent upward pressure on cost structures.

In the first time since pre the GFC the biggest upward lift across the main farming categories occurred for interest rates (10.0-11.3% of costs). This was due to the 100bps lift in the OCR that occurred and the majority of borrowing being on shorter-terms. **Local and government rates (2.4-4.9%), insurance premiums (1.9-2.4%) and repairs & maintenance (1.5-3.6%) were one of the biggest increases across all farm categories too.** Other upward movements of note in the dairy sector included animal health and breeding (3.1% y/y). For horticulturist other cost pressures included packaging (2.9% y/y) and cultivation & harvesting (2.6%). **Wages moved up by 2%** and there were generally small increases for administration, rent & hire, and administration costs.

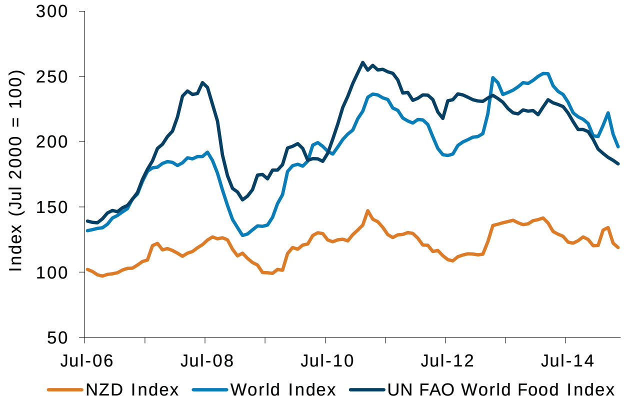
At the other end of the spectrum fuel costs fell on average by 20.5% y/y, while fertiliser, lime & seeds, and electricity cost were also down 3.3% on average. Fuel costs make up between 3.9% and 1.8% of on-farm costs, so the decline in fuel costs offset around half of the annual increase in on-farm costs. So it seems the farming community have at least gained some small benefit from a structurally high NZD and lower international oil prices.

For dairy farmers there was also a decline in dairy grazing costs (2.7% y/y) and electricity (-1.3% y/y). For horticulturist there were small declines in rent & hire costs, electricity and weed & pest control. Sheep & beef farmers benefited from a small decline in weed & pest control too.

KEY COMMODITIES: OVERALL INDEX AND DAIRY

SOFT COMMODITY PRICE INDICES					
	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
ANZ NZD Index	119	130	129	↓	↓
ANZ World Index	196	213	239	↓	↓
FAO World Food Index	183	188	229	↓	↓

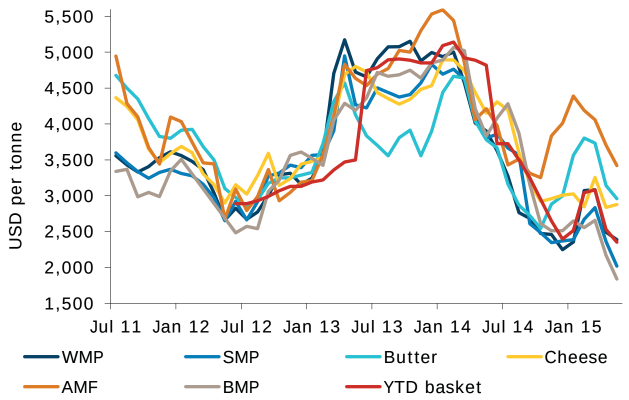
SOFT COMMODITY PRICE INDICES



Source: ANZ, FAO

OCEANIA DAIRY PRICE INDICATORS					
USD per tonne	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
Milk Price YTD ($ per MS)	4.45	4.47	8.40	↓	↓
Milk Price Forecast ($ per MS)	5.00-5.25	na	7.00	na	↓
Whole Milk Powder	2,388	2,655	3,903	↓	↓
Skim Milk Powder	2,020	2,405	3,803	↓	↓
Butter	2,958	3,278	3,779	↓	↓
Anhydrous Milk Fat	3,421	3,727	4,213	↓	↓
Butter Milk Powder	1,839	2,222	3,832	↓	↓
Cheese	2,879	2,990	4,152	↓	↓

DAIRY PRODUCTS – NZ EXPORT MARKET PRICES



Source: ANZ, GlobalDairyTrade

New Zealand's soft commodity basket continues to follow global food prices lower. An array of both supply and demand factors are buffeting New Zealand's key sectors at present. These include: sluggish economic conditions in many important market, including China and South-East Asia; the drop in other commodity prices affecting sentiment and price competitiveness; geopolitical ructions continuing to disrupt trade flows and import demand in some key import regions (mainly Europe and the Middle East); Russian sanctions and its economic woes continue to reverberate through many soft commodity markets; Farm support policy changes in Europe have taken export constraints off, but still provide certain domestic back-stops; Lower feed costs for the Northern Hemisphere has boosted the competitiveness of key competing exporters and products (early indications are of another good growing season in Europe and the US too); Competitors are opening up market access into China and other emerging markets; and finally the rise of the USD has made imported food products more expensive in some key emerging import markets. The flipside is a weaker NZD/USD and reduced US export competitiveness.

The dairy sector continues to be buffeted by many of these forces. The main pressure points in recent times has been the continued absence of China and increased competitive pressure in key secondary markets from European SMP.

Europe continues to produce and export more SMP into key New Zealand secondary markets, such as, Africa, the Middle East and Asia (ex. China). Near-term pressure is likely to persist while Europe tries to shift its seasonal peak in milk supply. However, we are now approaching intervention price levels for SMP in Europe, which is expected to provide a price floor. Beyond this **Russia is not expected to relent on its sanctions** and has announced it wants to be self-sufficient in milk supply in the next 7 to 10 years. Combined with the extra powder capacity that was added in Europe in anticipation of quota removal means increased competition looks here to stay.

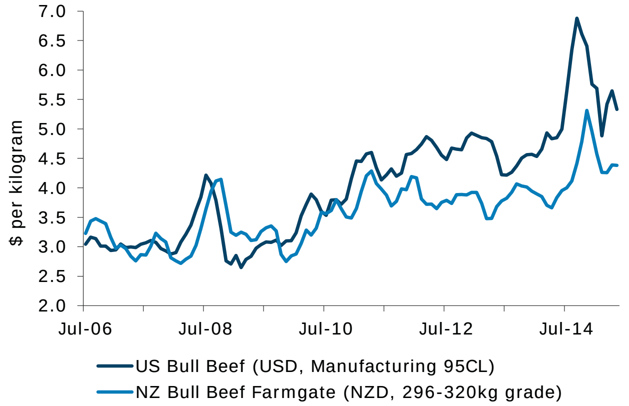
That leaves New Zealand reliant on Chinese demand to improve. Powder inventory levels are now being reported at more normal levels, but most are saying domestic milk supply as grown strongly. **Growth in larger-scale dairying operations appears to have filled much of the gap left by smaller producers exiting in 2013. Still it is currently cheaper for end-users to import milk powder than to purchase domestic raw milk.** On this basis we expect some increase in import demand during China's seasonal low milk supply period. **Globally milk supply growth continues to slow also, which when inventories are worked through should help rebalance the market over 2015/16. Budgeting on a milk price of $5.00-$5.25/kg MS seems appropriate for now given the timing and extent of recovery remains uncertain.**

KEY COMMODITIES: BEEF AND LAMB

BEEF PRICE INDICATORS					
$ per kg	**Current Month**	**3 Mth Trend**	**Last Year**	**Chg. M/3M**	**Chg. Y/Y**
NZ Bull Beef[1]	4.38	4.30	3.84	↑	↑
NZ Steer[1]	4.61	4.50	4.00	↑	↑
NZ Heifer[1]	4.04	3.94	3.42	↑	↑
NZ Cow[1]	3.06	3.07	2.62	↓	↑
US Bull Beef[2]	5.33	5.32	4.85	↑	↑
US Manu Cow[3]	4.85	4.92	4.50	↓	↑
Steer Primal Cuts	7.91	8.24	7.48	↓	↑
Hides[4]	66.1	65.9	75.8	↑	↓
By-Products[4]	51.7	52.9	53.5	↓	↓

[1] (NZD, 296-320kg Grade Bull & Steer), (NZD, 195-220kg Grade Heifer) (NZD, 160-195kg Grade Cow)
[2] USD, Manufacturing 95 CL [3] USD Manufacturing 90 CL [4] USD$ per Hide

BEEF INDICATOR PRICES

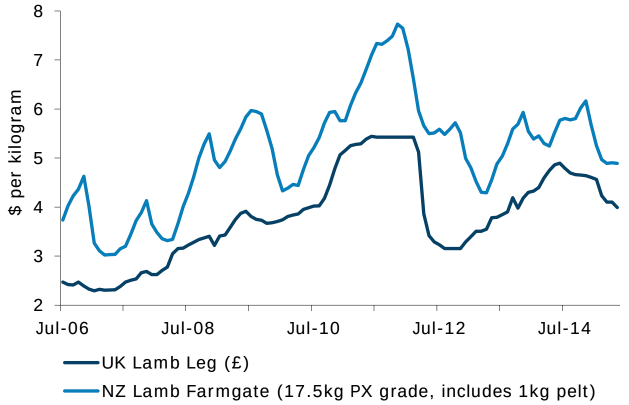


Source: ANZ, Agrifax

LAMB PRICE INDICATORS					
$ per kg	**Current Month**	**3 Mth Trend**	**Last Year**	**Chg. M/3M**	**Chg. Y/Y**
NZ Lamb[1] (NZD)	4.89	4.92	5.52	↓	↓
UK Lamb Leg (£)	3.99	4.15	4.86	↓	↓
Rack US (USD)	15.5	15.6	17.0	↓	↓
Flaps (USD)	4.55	5.07	5.81	↓	↓
Skins[2]	2.62	2.48	6.43	↑	↓

[1] 17.5kg PX grade, including 1kg pelt [2] USD per skin

LAMB INDICATOR PRICES



Source: ANZ, Agrifax

The beef market continues to be dominated by supply dynamics. The US remains structurally short of domestic manufacturing beef. Improved pasture conditions and high forecast returns for cow/calf operators (based on future calf prices and feed costs) should continue to fuel cow and heifer retention across the US. Cull cow supply is currently running 4-6% behind last year (which was a record low) and was 15% back on the four-year average in May. **This is being countered by high supply out of both Australia and New Zealand.** Australian supply has remained high with a poor wet season in Queensland and failed autumn in Victoria. Given the reduction in capital stock numbers in recent years improved weather conditions remain key for turn-off to slowdown. New Zealand supply will begin to normalise once the record cull cow slaughter passes. **Overall in-market prices look under more pressure, but the lower NZD/USD is helping relieve the pressure at the farm-gate.**

Lamb farm-gate prices are struggling to seasonally improve. Pricing pressure continues to be present in New Zealand's two largest markets China and the UK. **In-market prices appear to be stabilising, but exporters have been reporting sluggish sales, which implies an inventory build-up.** Both factors suggest s**chedule prices might struggle to get much above the mid-$5/kg MS mark this winter.**

All cuts have seen price declines. The biggest pressure point has been for the lower value cuts, with the likes of lamb flaps and forequarters prices back 20-25 y/y. This has been primarily due to a drop-off in Chinese import requirements. High import volumes during the first part of the year lead to an inventory build-up and higher earlier domestic production seems to have reduced import demand in recent months. This combined with additional uncertainty being created by the government clampdown on grey market channels for beef and lamb has made importers hesitate to forward commit. In the long-term NZ's better legitimate market access should provide an advantage if grey channel trade is reduced.

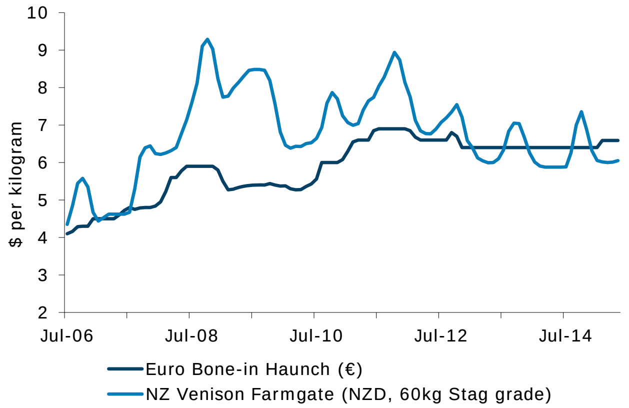
The other pressure point, especially for leg prices, has been higher domestic production in the UK. While New Zealand is counter seasonal to local supply, the largest UK lamb crop in eight years in 2014 saw a material carryover of local supply into 2015. This has provided plenty of competition for New Zealand's traditional marketing window. Prospects for the 2015 lamb crop are reported to be better than 2014 with a further 2% increase expected due to another rise in breeding ewe numbers. This means overall local supply is expected to remain high (+5.5% y/y) throughout the rest of 2015. Exporters have been trying to shift more product into Europe, but the strong NZD/EUR has reduced returns too.

KEY COMMODITIES: VENISON AND WOOL

VENISON PRICE INDICATORS					
$ per kg	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
NZ Stag[1]	6.05	6.01	5.88	↑	↑
NZ Hind[1]	5.95	5.91	5.77	↑	↑
Euro Bone-in Haunch (€)	6.59	6.59	6.40	←→	↑
Boneless Shoulder (€)	5.04	4.83	4.51	↑	↑
Loin (€)	16.5	15.8	13.0	↑	↑

[1] (60kg Stag AP grade), (50kg Hind AP grade)

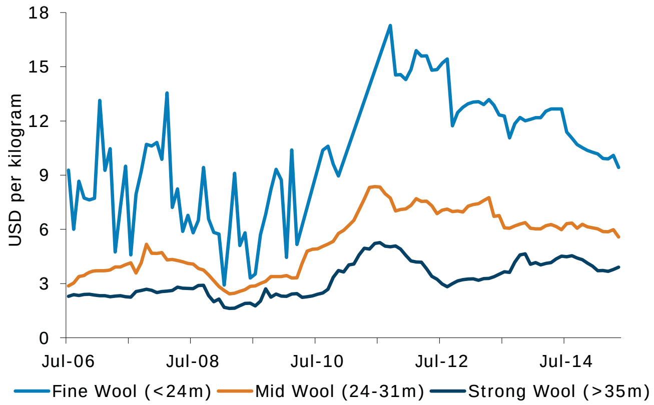
VENISON INDICATOR PRICES



Source: ANZ, Agrifax

CLEAN WOOL INDICATOR PRICES					
$ per kg	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
NZ Fine Wool (>24m)	13.25	13.25	14.71	←→	↓
NZ Mid Wool (24-31m)	7.85	7.85	7.15	←→	↑
NZ Strong Wool (>32m)	5.49	4.95	5.08	↑	↑
USD Fine Wool (>24m)	9.42	9.97	12.67	↓	↓
USD Mid Wool (24-31m)	5.58	5.91	6.16	↓	↓
USD Strong Wool (>32m)	3.90	3.73	4.37	↑	↓

WOOL INDICATOR PRICES (CLEAN)



Source: ANZ, Beef + Lamb NZ, Wool Services International

Farm-gate prices for venison have sat around the $6/kg mark in recent months. This is a little better than last year, but still $0.5/kg below the five-year average. The low farm-gate prices and dry summer conditions have continued to see high numbers of breeding hinds turned-off this season. **Year-to-date hind production is only 1% behind last year versus earlier industry expectations of a 15% decline on the expectation of a stabilisation in breeding hind numbers.** Things look to have eased up more recently with the improvement in seasonal conditions, but at present **the numbers point to another decline in the 2015 fawn crop. Stag slaughter has been softer, running 8% behind the same period last year.** This would seem to reflect the 7% decline seen in the number of weaners at the start of the 2014/15 season.

Most exporters sold forward the majority of the season's production out to June-July and managed to push overall prices slightly higher during this period. **The focus will now begin to shift to the chilled export window for September/October. Initial expectations are for some small improvement of in-market prices** due to lower inventory levels and reduced New Zealand supply. **With the NZD/EUR being back at more reasonable levels this should support schedule prices around the mid-$7/kg mark.**

Wool prices have recently spiked higher, with very larger increases for lamb and finer micron crossbred wool. The recent increase seems to reflect local supply and demand pressures more than in-market fundamentals. There was lower than expected auction supply at the end of April through to early May and exporters were reportedly short of product to fill specific contracts. Once this short-term covering need has been fulfilled it's difficult to see how sustainable the recent higher prices will be. Lower seasonal (winter) volumes might help extent current pricing depending on how short exporters are, but better in-market fundamentals are still needed to make them sustainable in 2015/16.

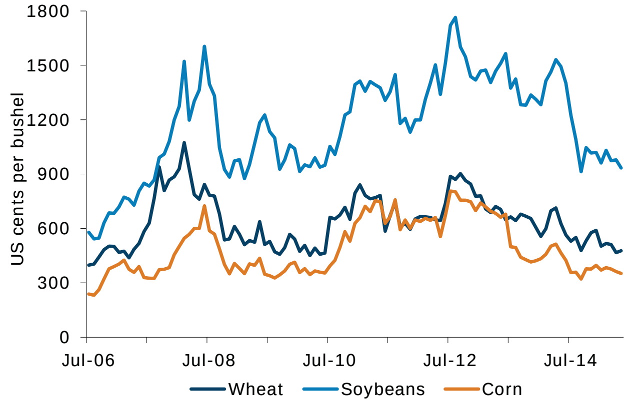
The flow of wool to China seems to have picked-up in recent months. Finer crossbreed and lamb's wool demand has reportedly been fairly steady as it has a wider range of uses compared with coarse crossbreed. Combined with less local supply this has supported prices to highs of $7.5/kg clean recently. **Stronger crossbreed wool still continues to lose market share to synthetic materials for carpets.** The US housing market has been a bit stop-start, but now appears to be emerging from its winter hiatus. This should support a general increase in end carpet demand, but woollen products will have to compete hard for their niche share of the market.

KEY COMMODITIES: GRAINS

GRAIN & OILSEED PRICE INDICATORS	Current Month	3 Mth Trend	Last Year	Chg. M / 3M	Chg. Y / Y
NZ Milling Wheat[1]	413	417	438	↓	↓
NZ Feed Wheat[1]	371	384	426	↓	↓
NZ Feed Barley[1]	360	374	429	↓	↓
Palm Kernel Expeller[1]	223	263	349	↓	↓
US Wheat[2]	4.8	5.0	6.3	↓	↓
US Soybeans[2]	9.3	9.9	14.9	↓	↓
US Corn[2]	3.5	3.7	4.7	↓	↓
Australian Hard Wheat[1]	369	386	427	↓	↓

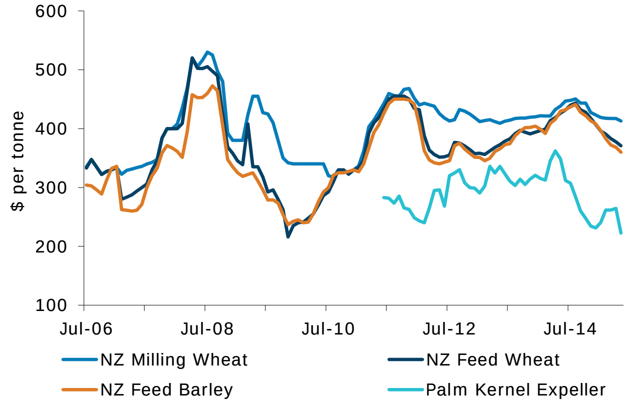
[1] NZD per tonne
[2] USD per bushel

CBOT FUTURE GRAIN & OILSEED INDICATOR PRICES



Source: ANZ, Bloomberg

KEY NZ GRAIN PRICES



Source: ANZ, Agrifax

Grain prices have been under pressure both domestically and offshore. Not a lot of non-contracted grain has reportedly changed hands at the lower prices in recent months as growers have sat tight though. Domestic feed wheat and barley prices have drifted toward the mid-$300/t mark in recent weeks. Price's for this seasons Maize crop is sitting between $380-$400/t.

Domestically the focal point is a lack of dairying demand. The price pressure is not expected to abate in the short-term given the cash-flow constraints in the sector and uncertainty on where the milk price might actually finish the season. One of the biggest operating costs is feed and this is where many are focusing to try and find any cost efficiencies they can for the new season. The management response does vary depending on a range of factors, such as farm system employed and locality. But ultimately marginal revenue needs to be better than marginal cost. At present this is points toward lower grain prices yet.

Palm Kernel is currently the supplement of choice for dairy farmers due to its lower price and the time of year. Palm Kernel is generally used more through winter as cows are not in milk, so do not need as high quality feed as they do during milking season. Average Palm Kernel prices are currently sitting between $200-$230/t. The lower NZD/USD and higher demand from Europe are preventing further declines for now.

Offshore things remain interesting as it appears there will be more bumper Northern Hemisphere harvests later this year. Combined with high carry-over stocks this is likely to lead to lower international prices for longer. It is expected that Europe's wheat harvest will only be just short of last year's record. The current forecast for **the 2015 EU soft wheat harvest is 142.6 million tonnes, which is 4% below last year's record.** France, which is the EU's largest wheat producer, in particular is expecting an exceptionally good crop. This is a result of France planting its largest wheat area in almost 80 years. However, EU exports are expected to be lower from increased Russian exports. **Russia is expected to export more due to changes in its export tax policy.** The fixed export tax has been replaced with a new tax that only kicks in if the domestic price is higher than 12,000 rubles/tonne.

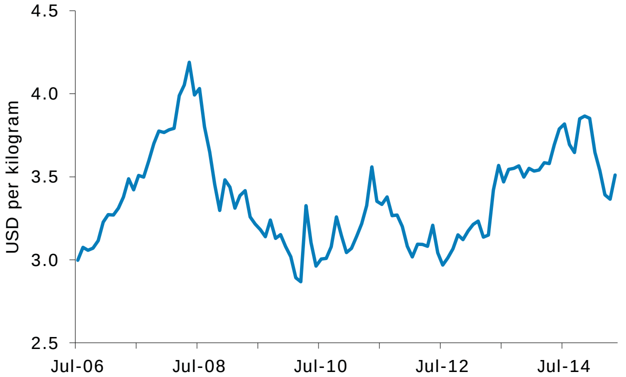
In the US planting progress of this year's corn crop has been early reducing some end of season weather risk. Summer rainfall and temperatures are key now for yields. The Renewable Fuel Standard which sets the ethanol mandate was recently released at 14 billion gallons, below the 15 billion envisioned by Congress. The mandate would imply a 4.8 billion bushel guaranteed demand for corn. Use in the past year has exceeded this level, in part due to exports, but also better domestic demand.

KEY COMMODITIES: HORTICULTURE

HORTICULTURE PRICE INDICATORS	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
Kiwifruit (USD per kg)	3.5	3.4	3.7	↑	↓
Apples (Weighted Index)	221	204	266	↑	↓
Average Wine Price[1]	5.53	4.84	6.25	↑	↓
Packaged White Wine[1]	5.71	5.93	6.52	↓	↓
Packaged Red Wine[1]	9.74	9.51	10.12	↑	↓
Bulk wine[1]	3.00	2.87	3.91	↑	↓

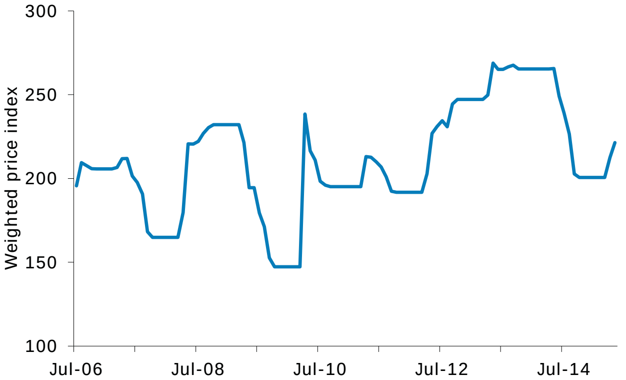
[1] USD per litre

KIWIFRUIT INDICATOR PRICE



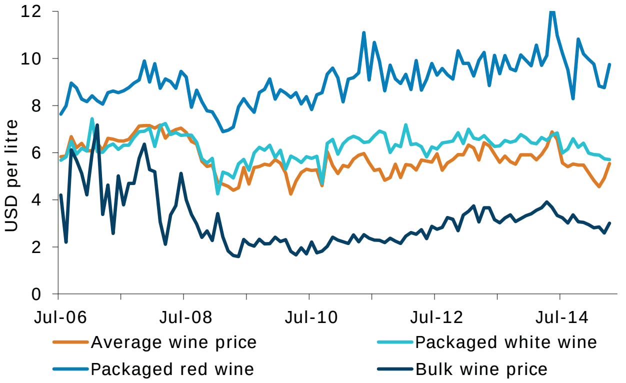
Source: ANZ, Zentrale Markt- und Preisberichtstelle

APPLE INDICATOR PRICE INDEX



Source: ANZ, Zentrale Markt- und Preisberichtstelle

WINE INDICATOR PRICES



Source: ANZ, NZ Winegrowers

The 2015 wine vintage has been confirmed at 336,000 tonnes, which is 27% smaller than the record crop last year. The slow run rate of the large 2014 vintage is expected to see a material carryover into 2015 though. Extrapolating year-to-date sales is expected to see nearly 40 million litres of the 2014 Sauvignon Blanc vintage carried over. We estimate the 2015 Sauvignon Blanc crop will be around 156 million litres, which implies carryover stock of 26%. The other implication of the smaller 2015 vintage is wine co-operatives are expected to blend some of the two vintages together. A maximum of 15% blend is permitted. Many have also been using the smaller and later release date of the 2015 vintage as leverage to negotiate the sale of leftover 2014 vintage. **These dynamics are expected to mainly benefit the bulk wine market rather than the packaged wine category.** Currently the bulk market for Sauvignon Blanc seems to be somewhere in range of $3.80-$4.00 for the 2014 vintage and $4.50 + for the 2015 vintage (both subject to quality of course).

In-market many of the themes remain the same. The UK and US remain the best-performing of the big three markets. The Australian market is proving tougher, with a slowdown in economic growth and high NZD/AUD. Premium wine sales are expected to continue to grow to both the UK and US over the coming 18 months. Competition from Chilean Sauvignon Blanc is likely to increase in both these markets following a better growing season. US domestic supply of Sauvignon Blanc has also increased in recent years.

Zespri have released their early season forecasts for the 2015 harvest. They expect a Green orchard-gate price of between $5.00-$5.50 per tray and for Gold varieties of $6.70-$7.20 per tray.

The drop in Green returns is primarily driven by increased competition from Chilean supply, which somewhat rebounds following a failure in 2014, and more competition within Europe on the shoulders of the season due to the Russian food import bans. **Combined with exchange rate challenges** in some of the main markets, such as Japan and Europe these dynamics are expected to account for the majority of the decline.

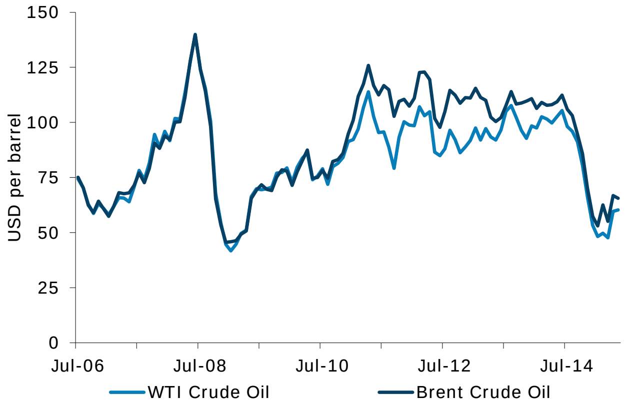
For Gold there will be a less favourable marketing mix, with higher crop volumes this year, increased promotional costs, and higher fruit loss. Scarce supply in recent years has seen Asia take 70-80% of the crop, but this is expected to decline with Europe's and North America's share growing once more.

KEY COMMODITIES: OIL, FREIGHT AND FERTILISER

OTHER COST INDICATORS	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
WTI Oil[1]	60	52	103	↑	↓
Brent Oil[1]	66	61	109	↑	↓
Ocean Freight[2]	589	578	934	↑	↓

[1] USD per barrel, grade WTI
[2] Baltic Dry Index

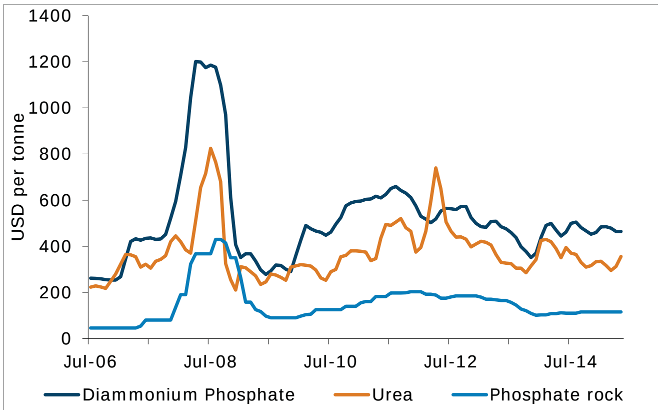
CRUDE OIL INDICATOR PRICES



Source: ANZ, Bloomberg

FERTILISER PRICE INDICATORS					
USD per tonne	Current Month	3 Mth Trend	Last Year	Chg. M/3M	Chg. Y/Y
DAP (USD)	464	476	445	↓	↑
Urea (USD)	356	308	350	↑	↑
Phosphate Rock (USD)	115	115	112	↔	↑
Farm-gate DAP (NZD)	818	816	797	↑	↑
Farm-gate Urea (NZD)	590	590	605	↔	↓
Farm-gate Super phosphate (NZD)	316	316	316	↔	↔

INDICATIVE INTERNATIONAL FERTILISER PRICES



Source: ANZ, Bloomberg

Oil prices will likely continue to be volatile over the coming months as the market grapples with conflicting reports of rising demand against the potential for recovering US shale production. A supportive macro-context could contribute to positive demand sentiment and prices near-term, but will likely be capped in the third quarter as the US dollar strengthens. After rallying 40% since mid-March, we expect WTI prices to remain around the top-end of our base case range of USD40-60/bbl while sentiment remains optimistic, but trend lower as the seasonally strong summer demand period comes to an end and markets refocus on stubbornly high US inventories. **Bearish sentiment will likely be driven by confirmations of US shale production ramping up. OPEC's strategy of capturing market share hasn't changed either** by keeping its target output at 30mbbls/day in the key semi-annual OPEC meeting in early June, which may additionally weigh on sentiment.

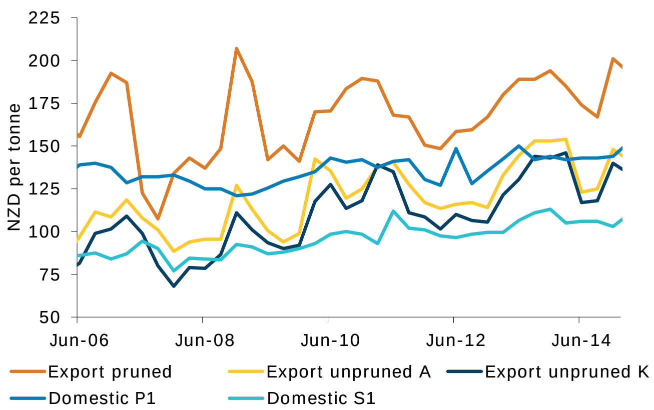
Although shale oil producers reacted quickly to the collapse in prices, the speed and magnitude of the recent price recovery should see cuts in shale oil drilling activity and production being reversed. The largest US shale producer (EOG Resources), hinted recently that it would increase drilling activity if WTI hit USD65/bbl. This has been followed by other key producers all raising full-year production outlooks. EIA data also showed US oil production climbed 30kbbls/day to 9.57mbbls/day at the end of May, the highest level in 30 years. Meanwhile, OPEC production is at the highest level in over two years. At the same time, Iraq plans to increase exports by about 25% to around 3.75Mb/d in June. **We think rising OPEC supplies could negate some of the supportive influence from unpredictable geopolitical flare-ups in the region. As a result, we believe the risk of global oil supplies picking up in H2 2015 is increasing.**

Fertiliser prices remain largely unchanged. Global urea prices are similar to same time last year. India recently announced changes to their urea subsidy policy, with a shift to more internally-sourced product instead of imports. Global potash prices are likely to start to increase as seasonal demand lifts from India and China. Phosphate prices remain steady awaiting demand signals from the Indian monsoon and North American planting season.

KEY COMMODITIES: FORESTRY

FORESTRY PRICE INDICATORS	Current Quarter	3 Period Trend	Last Year	Chg. P/3P	Chg. Y/Y
Export: (NZ$ per JAS m³ f.o.b.)					
Pruned	193	181	185	↑	↑
Unpruned A Grade	142	132	154	↑	↓
Unpruned K Grade	134	125	146	↑	↓
Pulp	119	113	133	↑	↓
Domestic: (NZ$ per tonne delivered at mill)					
P1	152	143	142	↑	↑
P2	126	126	126	↔	↔
S1	110	105	105	↑	↑
S2	103	106	105	↓	↓
Pulp	53	51	50	↑	↑

NZ FORESTRY INDICATOR PRICES



Source: ANZ, MPI

The downturn in the export log market gained momentum in May with NZ$ at-wharf-gate prices plunging $12-$17/JAS m³ for unpruned grades and pruned dropping on average $10. This is not reflected in our prices, which are up to April. In-market prices fell to multi-year lows, with the other drivers – exchange rate (marginally unfavourable) and ocean freight rates (marginally favourable) – offsetting one another. **The fall has seen many trucks and harvesting equipment parked up.**

The focal point is China who now takes nearly 80% of New Zealand's export logs (Korea about 13%; India about 5% and Japan only about 2%). Log demand in China has been steadily increasing since the Chinese New Year period in February and in response to government initiatives aimed at stimulating the soft housing market. However, the inflow of logs has exceeded demand and resulted in the accumulation of inventory to over 4.2 million m³ in early April representing over two months' supply. Historically at this level, in-market pricing has become vulnerable and volatile.

Most market participants feel the bottom has been reached now though. Inventories seem to be starting to recede and offtake is currently high at around the 65,000t/day mark. Other support factors are in-market prices have now reached a level that is a disincentive for most alternative supply sources (both domestic Chinese and import supply) to participant at. This is highlighted by a recent reduction in supply from North America. Russian supplies have been very competitive, but this could be about to slow too as the ruble has increased by 11% against the USD so far this year. Russia also faces supply chain issues (transportation & capacity) and the government increased tariffs in 2015 to raise revenue. The other support factor looks to be a softening NZD/USD too.

It has been a slightly different story on the New Zealand market with domestic pruned logs more strongly sought after. This is due to ongoing domestic demand and tight Central North Island supply. The Christchurch rebuild continues to create strong demand for structural timber in particular. The booming Auckland housing market is also stimulating additional demand. Auckland consents by floor area were up 10% y/y over the last quarter.

BORROWING STRATEGY

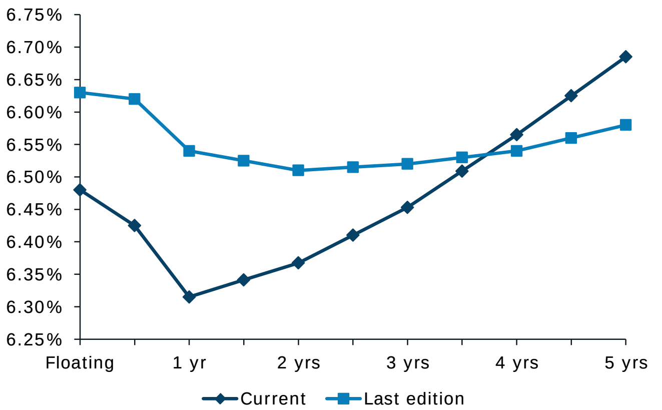
SUMMARY

Indicative rural lending rates are generally lower than they were when we published our last edition, with the short end dragged lower by ramped up expectations for OCR cuts, and the long end slightly higher on the back of a lift in US interest rates. All else equal, the "steeper" yield curve discourages fixing for longer because it costs more. We are also mindful that with the RBNZ's next move likely to be a cut, short end rates are likely to fall further, making the decision to hedge for longer even tougher. We do expect New Zealand and global long term interest rates to rise over time, but only gradually, and accordingly we remain cautious about fixing despite the fact that long term interest rates are still low by historic standards.

OUR VIEW

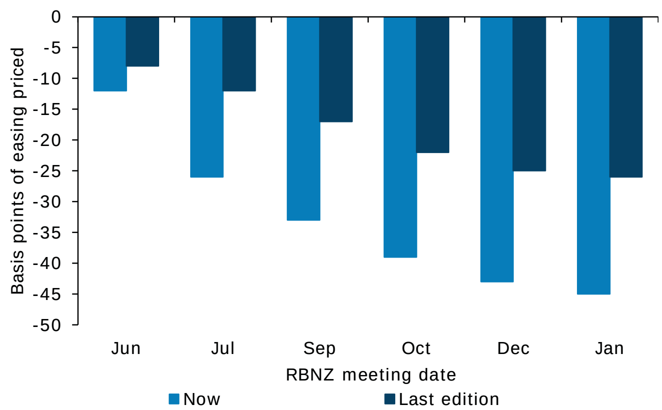
Indicative rural lending rates are generally lower than they were when we published the last edition of the *Agri Focus*, with the only rises being seen in the 4.5 and 5 year tenors (see chart below).

FIGURE 1. INDICATIVE RURAL LENDING RATES



Source: ANZ, Bloomberg

FIGURE 2. MONETARY POLICY EXPECTATIONS



Source: ANZ, Bloomberg

Shorter term rates (i.e. those for terms 2 years and less) are between 0.17% and 0.22% lower, thanks largely to the fact that **the market now expects the Reserve Bank to cut twice by the start of 2016.** The combination of ramped up expectations of OCR cuts (which tends to be the dominant driver of New Zealand short end rates) and higher US interest rates (which tend to be more dominant driver of New Zealand long end rates – see below) has seen the curve "steepen" dramatically.

FIGURE 3. NEW ZEALAND AND US INTEREST RATES

Source: ANZ, Bloomberg

From a cost comparison, a steeper curve clearly discourages fixing. Similarly, the prospect of rate cuts (that are not yet fully priced in) dragging short end rates even lower just adds further discouragement.

Of course, if one thought long end rates were set to move markedly higher, and had a desire to be fixed for the sake of certainty, it could be worth hedging now anyway. This is demonstrated by our breakeven analysis (see table), which shows that interest rates need to rise only gradually in order for fixing to be worthwhile. However recent speeches and comments by US Federal Reserve ("Fed") Chair Janet Yellen and other Fed officials point to a gradual and cautious lift in policy interest rates in the US. In our view, **the cautious approach that the Fed is taking is likely to temper the pace at which US long term interest rates rise. Given the strong correlation between New Zealand and US interest rates, we also expect the rise in long term interest here to be very gradual.**

Rural Lending Rates (incl. typical margin)		Breakeven rates			
Term	**Current**	**in 6mths**	**in 1yr**	**in 2 yrs**	**in 3 yrs**
Floating	6.46%				
6 months	6.43%	6.20%	6.34%	6.61%	6.72%
1 year	6.32%	6.27%	6.35%	6.67%	6.76%
2 years	6.34%	6.38%	6.51%	6.71%	6.89%
3 years	6.45%	6.49%	6.59%	6.82%	
4 years	6.53%	6.59%	6.70%		
5 years	6.63%				

ECONOMIC BACKDROP

SUMMARY

The economic outlook remains reasonably solid, supported by low interest rates, a strong construction pipeline, booming net migration and surging Auckland house prices. However, headwinds in the form of a high NZD relative to commodity prices and stresses on dairy cash-flow have clearly altered the risk profile. Inflation is being suppressed by structural as well as transitory factors. Policy-makers are taking a multi-pronged approach to tackling Auckland housing demand, with the speed and apparent coordination of measures notable. While uncertainty surrounds the precise impact, we suspect the effect will be stark. The OCR should be heading lower – and sooner rather than later to keep driving the NZD down.

SHIFTING RISK PROFILE

The economic outlook remains reasonably solid, with supports including low interest rates, the still-elevated (although admittedly falling) goods terms of trade, a long construction sector pipeline, infrastructure investment and the demand for more dwellings in Auckland. Net permanent and long-term migration is at a record high, equivalent to 1.2% of the resident population, benefiting both the demand and supply sides of the economy. Confidence remains elevated and employment growth has been significant, with the economy adding 75,000 jobs over the past 12 months.

The economy is slowing, but this does not solely reflect emerging headwinds; there are capacity constraints at work as well. Finding the right staff is now a major challenge for small-to-medium sized businesses (and pockets of the rural community). After growing solidly for the past few years, economies invariably level out at a more modest rate of expansion. Observers tend to overplay such a deceleration, forgetting that economies invariably perform more strongly early in an upswing (you bounce strongly off lows, partly because hitting lows tends to reflect a sharp contraction in activity, so there is a springboard effect), but level out once momentum hits cruising speed.

However, not all parts of the economy are firing, and the risk profile has shifted. Headwinds in the form of contractionary fiscal policy and a high NZD relative to the falls we're seeing in commodity prices are well known and have been around for a while. The global scene remains fractured and volatile despite historically low policy interest rates. The US economy is set to strengthen from its winter-induced lull, while growth in Europe is tepid despite very accommodative financial conditions. Growth in China is slowing more sharply than intended, with authorities employing further monetary and fiscal stimulus. Export commodity prices are copping the flak and are falling. Pressure is mounting on the dairy sector and anecdotes for the forestry sector have also weakened. The opening forecast of $5.25/kg MS for 2015/16 and a further downgrade to 2014/15 means cash-flow is going to be extremely tight for some time to come (until 2017!). The economic hit from reduced downstream activity will be substantial. The NZD is not aligning itself to broader terms of trade and export commodity price trends, placing additional stresses on exporting and import-competing sectors.

Policymakers on both sides of The Terrace in Wellington are taking a multi-pronged approach to tackling Auckland housing demand. The speed and apparent coordination of measures is notable. All of a sudden, there is much more coordination between officials across the Government and Reserve Bank. It is also telling that we have seen such a breadth of policy responses in such a short space of time. Auckland property prices have increased by two thirds over the last five years, and by a third in the last two – a stretched base off which to keep accelerating.

While uncertainty surrounds the precise impact, we suspect the effect of these measures could be stark given the extent of house price gains of late. Sentiment could turn quickly, and we will be paying particularly close attention to surveyed measures of house price expectations and to the number of property listings over the coming months, which could rise sharply as sellers try to beat the 1 October introduction of the new measures.

Readings from the wage and pricing side of the economy remain benign. There is certainty asset price inflation, but no broader inflation. Annual CPI inflation fell to 0.1%, a 15-year low. Core inflation at 1.3% was the equal-lowest on record and marked the 21st consecutive quarter it has been below the RBNZ target midpoint. We are watching our Monthly Inflation Gauge for further signs of subdued pricing pressure. **Strong growth has failed to bring about the anticipated rise in inflation.** Some are pointing to transitory factors such as the high NZD and lower petrol prices as reasons why inflation is low. These factors have certainly contributed. But core measures are subdued too and non-tradable (domestic inflation) has receded. There are structural forces at play as well.

We expect the RBNZ to lower the OCR on June 11. On some levels the RBNZ should be cautious. Low interest rates risk turbo-charging Auckland housing further. Inflation could pick up as the NZD falls. However, core inflation is low. The risk profile across the economy has clearly shifted; dairying faces tough times and Christchurch's stimulus is fading. And we now have risks surrounding how the property market will respond to recent steps. Cutting the OCR is a way to manage emerging risks and rebalance the mix of growth (i.e. more toward exports and the income-generating side of the economy). Moreover, it's required to get the NZD down and offset the impact of lower commodity prices on rural incomes and the broader economy.

EDUCATION CORNER: FOOD SAFETY ENVIRONMENT

SUMMARY

More and more, the success of food companies will come down to whether their brand is positively differentiated on safety and quality in the minds of consumers. Today's global supply chains demand a more strategic approach to protecting food integrity and the success of New Zealand Inc. A strategic approach will deliver on the customer promise, protect reputations, improve efficiency, reduce costs, limit disruptions and enable an effective response to a crisis. Leading food companies are adopting the following approaches to improve food safety, trust and protect their brands:

- install a positive culture of safety and quality from the farm to the shop floor;
- start at the top to ensure a risk-resilient business culture and best practice behaviours;
- regularly review supply chain risks, adopt a risk-focused approach, and benchmark against best practice;
- invest in technology-enabled solutions;
- approach crisis management in a transparent way;
- fully integrate food supply chains within organisations; and
- manage transactional risk.

INTRODUCTION

This month we feature a summary of an article from Craig Armitage of PricewaterhouseCoopers (PwC) on the need for New Zealand to be a global leader in food safety and integrity. PwC has set up a food supply and integrity service in New Zealand through a formalised alliance with the New Zealand Government-owned food safety and biosecurity company AsureQuality. For more information see 'Food trust: Giving customers confidence in your food', or get in touch with Craig Armitage at craig.armitage@nz.pwc.com.

What follows offers some insight on why New Zealand food companies need to be global leaders in food safety and integrity and the approaches leading food companies are adopting to improve food safety, build trust, and protect their brands.

PROTECTING NEW ZEALAND'S AGRICULTURAL ADVANTAGE

New Zealand is not immune to the threats facing the global food industry. Food crises are increasing and New Zealand's international reputation could be at risk.

For years we've dined well on our country's reputation for agricultural and food production excellence. Agriculture is New Zealand's biggest export earner, with the sector making a direct contribution of around 6% of total GDP, and much higher proportion when downstream industries are included. New Zealand food is globally recognised as being safe, nutritious and high quality. We export more dairy product than anyone else, our beef and lamb exports make up a significant share of global trade, and newer industries like wine are growing.

It's a competitive advantage we've worked hard to achieve over many years through continuous innovation and investment in creating 'best practice' processes. 'Made in New Zealand' and the sign of the kiwi and silver fern have become trusted brand marks that mean quality in the minds of consumers around the world. **New Zealand food is known to be safe and ethically produced.**

But in an environment where defending the integrity of food is becoming harder, growers and processors need to prepare for the new challenges testing food supply. **Basic fundamentals of trade are transforming the food industry as globalisation and complex supply chains create food safety risks on an industrial scale.** A daily search of the news show stories on food-borne illnesses and contamination, food fraud, and large-scale product recalls. Companies are losing money, customers are losing faith, and New Zealand risks losing trust in its food.

It's not just small or unsophisticated businesses that are feeling vulnerable to threats in the food value chain. These supply chain challenges are affecting the most reputable companies and developed economies. Forget about this being an emerging market or smallholder farming issue.

The recent 'nuts-for-spices' scandal, for example, in which peanut and almond shells were allegedly substituted for cumin seeds, saw dozens of food products pulled from supermarket shelves across the US and Europe. Across the Tasman, imported frozen berry products were recalled due to hepatitis A contamination fears. And in the past months spinach, ice-cream and hummus have been pulled from supermarket shelves in the US due to listeria contamination.

Closer to home, New Zealand had its own scare that placed its food industry in unfamiliar territory by putting a negative focus on the country's core export. When 'eco-terrorists' tried to blackmail the Government and dairy industry with a threat to poison infant milk formula, it showed New Zealand's vulnerability to the type of supply chain threats impacting companies everywhere. **Our view is the food industry needs to prepare for more of the same challenges.**

EDUCATION CORNER: FOOD SAFETY ENVIRONMENT

Clean, green, pure or otherwise; the nature of today's supply chains demand a more strategic approach to protecting food integrity and the success of New Zealand Inc. A strategic approach – what PwC calls food trust – will deliver on the customer promise, protect reputations, improve efficiency, reduce costs, limit disruptions and enable an effective response to a crisis.

FOOD TRUST – AN OPPORTUNITY OR A COSTLY CHALLENGE?

When it comes down to it, **there is ultimately nothing more important to people than what they feed their families and the food they put in their own bodies. It is imperative food is safe for all.**

More and more, the success of food companies will come down to whether your brand is positively differentiated on safety and quality in the minds of consumers. Food retailers have traditionally been faster than most to see the opportunity, with it becoming more common to see food sold on the basis of the quality of its ingredients, its health benefits, and ethical and sustainable considerations. Go to supermarkets in the UK, for example – especially at the upper end of the market – and you'll see these types of messages promoted strongly in-store and proudly labelled on food products.

Selling on quality is something that has the potential to disrupt the food market rapidly in this competitive consumer-driven environment. People don't just want food to taste good, but to feel good too. In response, retailers are becoming more demanding in the information they require around how food is farmed and processed and its journey to their shelves. New technology innovations in supply chain tracking and traceability will mean retailers can be more transparent in the information they share with consumers – information that will increasingly be available via the phone in people's pockets.

The risk for farmers and food processors is finding themselves behind the curve in terms of the information they can provide about their food. And for New Zealand's food industry, which is dependent on demand from international markets, this means it needs to be responsive and ahead of market changes by investing in the latest innovations that will increase consumer confidence.

New Zealand's farming industry faces stiff competition on the world stage. Competitors such as the Netherlands are leading the way with investments in efficient farming practices and the use of renewable energy and resources. Let's not let anyone take New Zealand's '100% pure' crown! Building trust in your food is more than an opportunity to defend your products from the expense of recalls, or import restrictions due to safety concerns. Yes, it is an investment and it is challenging to gather more information about your food, but it will become a more common requirement that will pay off for those that get it right. New Zealand must continue to sell on the strength and quality of its food brand. And to do it better and more easily, the food industry should come together in a collaborative effort to find a solution before it's a problem.

Food and agricultural companies naturally take safety and quality issues very seriously, but succeeding in tomorrow's market will require more to win consumers' trust and maintain a leading reputation.

GLOBAL AND LOCAL CHALLENGES

Over the past years we've seen the ongoing effects of global megatrends playing out across the food and agricultural sector. Globalisation, demographic changes, urbanisation, technological advances and climate change and resource scarcity are impacting the security, safety and quality of food.

Take the growth in food demand, for example. Food consumption is expected to increase 35% over the next 15 years as another billion people are added to the world's population by 2025. And by 2050, it is predicted agricultural production will need to increase by 70% to satisfy the demand. But extreme weather, rising temperatures, declining crop yield productivity, poor soil fertility, unsustainable farming practices and price volatility are some of the issues that will make growing this food mountain hard.

This is the type of problem we saw in India: drought affected the cumin crop and led to shortages, prices rose and, ultimately, resulted in the alleged passing off of ground peanut and almond shells as cumin seed. Widely used in spice mixes and as a key food ingredient, the alert posed a serious health risk to peanut allergy sufferers everywhere. Nowadays, we see problems turning up in more products, more quickly than ever before, causing food safety scandals that threaten large numbers of people.

You'd think that for New Zealand, a growing global population and its demand for food, combined with the rise of economies in Asia Pacific, would be an exciting prospect. And it is – if New Zealand's primary industry can continue harnessing its strong reputation while remaining vigilant to threats.

By 2050, 42% of the world's population growth will come from Asia: its people will continue consuming more dairy, meat, wine and other products that come out of New Zealand's food basket. Meat consumption alone is expected to increase by 128% by 2050 – a staggering figure, showing how New Zealand could benefit hugely from its close proximity and relationship with Asia. Let's remind ourselves that China is now New Zealand's largest export market and a significant investment partner.

EDUCATION CORNER: FOOD SAFETY ENVIRONMENT

But remaining competitive as developing economies become better at producing more food at lower prices will be challenging. And New Zealand will be tested by the impacts of megatrends too. Looking again at climate change, according to the United Nations, in 2011, New Zealand's carbon emissions per person were the fifth-highest in the industrialised world. The agricultural sector makes up at least half of all greenhouse gas emissions in New Zealand. Imagine a situation where people don't want to buy our food, or the global community demands a policy intervention that challenges business models and taxes carbon emissions. And of course, we know well the recurring debate around 'food miles' and the 'carbon cost' of transporting our food to overseas markets.

The whole food value chain is transforming. More food is being traded across borders as companies look for the best prices for their food. Companies are sourcing more from emerging markets where sustainability and supply chain risks are higher, and in response, consumers are growing anxious and regulation is increasing. Emerging markets are fast maturing, the customer base is changing, and expectations on safety and quality and new food demands, such as halal, are growing.

As more food is shipped offshore, some retailers and governments are worrying about having enough food to fill their shelves. Already, we're beginning to hear of 'at-risk foods', such as coffee, cocoa and some staple crops. **Another concern is that as food scarcity increases, so too will companies' vulnerability to fraud as the opportunity and motivation for financial gains increase.**

And what of technology? In PwC's recent survey of New Zealand CEOs 68% said they were worried about the speed of technology change. The time it takes to go from breakthrough technology to mass market is collapsing and disrupting industries. **New Zealand's agricultural sector will need to embrace technology to support farm development and meet the demand for greater traceability and oversight of food supply chains. The alternative is being left behind as the world moves on.**

THE FUTURE OF NEW ZEALAND FARMING – WHERE TO START TODAY?

Food companies that aspire to be market leaders can start by reviewing their food safety and quality management plans, training programs and supply chains. Greater traceability and oversight of supply chains should be a focus. External assessments can help. At a minimum, companies must ensure they are compliant with changing regulatory requirements – but I urge you to go further in winning your customers' trust and protecting the reputation of New Zealand's food.

In our experience, leading companies adopt the following approaches to improve food safety, trust and protect their brands.

Instilling a positive culture of safety and quality from the farm to the shop floor.
Organisations are adopting innovative practices that extend to staff awareness and training across the supply chain. Risks are identified and managed with ongoing hazard analysis and monitoring of leading indicators.

Starting at the top to ensure a risk-resilient business culture and best practice behaviours.
Business leaders must be fully engaged with food trust issues. Participation in industry bodies and thought leadership is essential to developing a culture that is relevant and responsive to current and emerging issues.

Regularly reviewing supply chain risks, adopting a risk-focused approach, and benchmarking against best practice.
Companies that have complete oversight over all stages of the supply chain, as well as risk management procedures tailored for multiple geographies, have a compelling competitive advantage. Proactive behaviour in supplier risk management leads to fewer compliance costs, fewer product recalls, and improved consumer confidence.

Investing in technology-enabled solutions.
The best companies continuously invest in new technology to enhance controls, monitoring, hazard detection, traceability and data analysis to manage risk and provide more information about their food.

Approaching crisis management in a transparent way.
Trusted companies approach issues and crisis events with swift remedial action and open, honest communication. They prepare for events with scenario analyses, planning and rehearsal, and have robust product recall and crisis management procedures.

Fully integrating food supply chains within organisations.
Vertical integration offers maximum control and traceability throughout the entire supply chain, and enables a more structured approach to risk management and crisis planning.

Managing transactional risk.
Operational and food trust due diligence is fundamental to managing transactional risk. This includes the systems and processes at production sites, as well as culture, governance, supplier risk and support functions, such as HR and IT.

KEY TABLES AND FORECASTS

FX RATES	ACTUAL			FORECAST (END MONTH)						
	Apr-15	May-15	9-Jun	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16
NZD/USD	0.762	0.711	0.713	0.72	0.69	0.68	0.67	0.67	0.66	0.66
NZD/AUD	0.962	0.930	0.928	0.95	0.93	0.93	0.93	0.94	0.94	0.94
NZD/EUR	0.681	0.647	0.632	0.67	0.67	0.69	0.67	0.64	0.60	0.60
NZD/JPY	90.62	88.23	88.85	86.4	83.5	83.0	82.4	83.1	82.5	82.5
NZD/GBP	0.494	0.465	0.465	0.47	0.45	0.45	0.44	0.43	0.43	0.43
NZ TWI	79.6	75.7	74.7	76.8	75.1	75.4	74.2	73.3	71.6	71.6

INTEREST RATES	ACTUAL			FORECAST (END MONTH)						
	Apr-15	May-15	9-Jun	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16
NZ OCR	3.50	3.50	3.50	3.25	3.00	3.00	3.00	3.00	3.00	3.25
NZ 90 day bill	3.64	3.47	3.46	3.20	3.10	3.10	3.10	3.10	3.20	3.60
NZ 10-yr bond	3.37	3.51	3.89	3.30	3.10	3.00	3.10	3.20	3.40	3.50
US Fed Funds	0.25	0.25	0.25	0.25	0.50	0.75	0.75	1.00	1.25	1.50
US 3-mth	0.28	0.28	0.28	0.70	0.70	0.95	1.20	1.45	1.70	1.80
AU Cash Rate	2.25	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
AU 3-mth	2.25	2.15	2.14	2.20	2.30	2.30	2.30	2.30	2.30	2.30

ECONOMIC INDICATORS	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
GDP (% q/q)	**0.6**	**0.7**	**0.8**	**0.8**	**0.7**	**0.6**	**0.6**	**0.6**	**0.6**	**0.6**
GDP (% y/y)	**3.1**	**3.2**	**3.1**	**3.0**	**3.1**	**3.0**	**2.8**	**2.6**	**2.6**	**2.6**
CPI (% q/q)	-0.3	**0.3**	**0.5**	**0.0**	**0.4**	**0.5**	**0.6**	**0.2**	**0.2**	**0.2**
CPI (% y/y)	0.1	**0.2**	**0.3**	**0.5**	**1.3**	**1.4**	**1.6**	**1.8**	**1.8**	**1.8**
Employment (% q/q)	0.7	**0.6**	**0.5**	**0.4**	**0.3**	**0.3**	**0.3**	**0.3**	**0.3**	**0.3**
Employment (% y/y)	3.2	**3.5**	**3.0**	**2.2**	**1.8**	**1.6**	**1.4**	**1.3**	**1.3**	**1.3**
Unemployment Rate (% sa)	5.8	**5.8**	**5.7**	**5.6**	**5.6**	**5.5**	**5.5**	**5.5**	**5.5**	**5.5**
Current Account (% GDP)	**-4.1**	**-4.4**	**-4.6**	**-4.8**	**-4.8**	**-4.9**	**-4.9**	**-5.0**	**-5.0**	**-5.0**
Terms of Trade (% q/q)	1.5	**-3.7**	**-3.5**	**-2.1**	**0.1**	**-0.3**	**-0.3**	**-0.2**	**-0.2**	**-0.2**
Terms of Trade (% y/y)	-5.3	**-9.0**	**-8.0**	**-7.7**	**-9.0**	**-5.7**	**-2.7**	**-0.8**	**-0.8**	**-0.8**

Figures in bold are forecasts. q/q: Quarter-on-Quarter, y/y: Year-on-Year

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