Rural Bank
Insights Update
March 2020

Commodity updates

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Commodity Overview

- Tightening supply and strengthening restocker demand will be the dominant factors in Australian cattle markets in the short term.
- Australian cattle prices are expected to rise further into record territory as restocker demand strengthens in response to recent rainfall.
- Weaker Chinese demand is expected to remain as long as the Coronavirus outbreak continues, adding downwards pressure on finished cattle prices.

Australian cattle prices are expected to rise into record territory in coming weeks as supply tightens and restocker demand strengthens in response to long awaited rainfall, particularly in Queensland.

The eastern young cattle indicator increased by 50.2 per cent in the first two months of 2020, regaining all of the ground lost since previous record highs were recorded over three years ago. Rainfall in January and February helped to replenish soil moisture and invigorate pasture growth, fuelling restocker demand and stemming the flow of cattle turned off drought affected properties.

The supply of cattle in saleyards is expected to tighten as conditions allow more producers to retain stock, particularly females, reversing the trend of elevated turnoff of cows and heifers which accounted for a record 56 per cent of Australian cattle slaughter in 2019. Reduced yardings will result in a continued decline of weekly slaughter rates, which declined 15.1 per cent during February.

Demand for young cattle could strengthen further as more producers get a clearer idea of feed availability following rainfall.

Restocker demand will add competition to the already firm demand from feedlots and processors. Tightening supply and strengthening restocker demand will be the dominant factors in Australian cattle markets in the short-term.

These factors will more than offset downwards pressure on finished cattle prices resulting from softer international demand for beef. Chinese demand is expected to remain weaker as long as the Coronavirus outbreak continues, resulting in weaker economic sentiment and reduced red meat consumption.

Softer demand from China is expected to be temporary as the shortage in protein supply resulting from African Swine Fever is expected to see China import large volumes of beef throughout 2020.
**Commodity Overview**

- Recent rainfall has both brought some downward pressure to Australian grain prices.
- Offshore wheat futures have not been immune to the weakness that the Coronavirus outbreak has brought to financial and commodity markets.
- The Coronavirus outbreak has also seen the Australian dollar hit multi year lows against the US dollar. This has somewhat, but not fully, offset the impact of declining offshore grain futures in Australian dollar terms.

Much needed rain across many of Australia’s cropping areas, coupled with forecasts for a wetter than average autumn for many cropping regions has buoyed sentiment around this year’s winter crop.

Local values have responded lower and on the East Coast in particular, we expect prices will move closer to longer term averages if further rains deliver more certainty regarding the coming season crop.

In addition to boosting confidence, rain has assisted pasture growth and increased restocker activity in beef and sheep markets, if this continues, we expect to see reduced requirement for feed grains from this segment.

The combined prospect of improved supply in the coming season, and potential weakening of domestic demand is expected to see premiums to offshore values soften, particularly in East Coast markets.

As of the end of February, season to date Australian wheat exports were up 36 percent year-on-year, with key destinations including the Philippines, South Korea and Japan.

The more price sensitive market of Indonesia on the other hand has sourced lower cost wheat from alternative origins, hence wheat exports from Australia are running 75 per cent behind average.

 Interruption to global trade flows as a result of Coronavirus is likely to weaken global grain prices, however to the end of February Australia has already exported close to half of an estimated eight million tonnes of wheat exportable surplus.

In an average year the exportable surplus is typically around twice this year’s anticipated volume, however the smaller crop will limit our exposure to Coronavirus to an extent.

Global wheat production is expected to reach a new record high in 2020 on the back of a two per cent increase to area planted, which if realised, will place downward pressure on global wheat values. In Australian dollar terms however, a weaker Australian dollar has offset some of the weakness seen in offshore markets.
In response to the Coronavirus outbreak, the global dairy trade (GDT) price index fell 7.6 per cent across the two GDT events in February. The Coronavirus outbreak, and the subsequent impact on economic sentiment in China, and globally, has increased the level of volatility in global dairy markets as participants try to assess the impact. Like other agricultural markets, this uncertainty is likely to continue due to a short-term decline in demand from China and other countries that are seeing an impact on their supply chain.

Drought in New Zealand is expected to see milk supply flip from a story of growth to one of decline in 2020. Full year supply from New Zealand is now forecast to fall 0.5 per cent year-on-year as drought grips the North Island. Drought induced destocking is expected to result in a declining New Zealand dairy herd, however global demand uncertainties and increases in forecast for northern hemisphere production are likely to outweigh the global impact of decreased New Zealand production.

Australian milk production remains forecast to drop year-on-year, with the smaller national milk pool expected to lead to reduced volume of milk products exported, and maintaining competition between processors for domestic supply. Recent rainfall has improved pasture availability, particularly in Qld and NSW, combined with reduced feed lot throughput this has led to a decrease in the demand for hay from northern lot feeders and graziers. Rainfall across Victoria has also eased demand for supplementary feed. Should rainfall continue this will continue to support increased confidence from producers that they will have sufficient feed reserves to see through winter.

Sources: Dairy Australia, Global Dairy Trade
Commodity Overview

- A delayed table grape harvest could prove advantageous if it means the impact of Coronavirus on China’s logistics are able to resolve themselves or at least ease before export volumes pick up in earnest.
- Capsicum prices continue to rise to reflect a smaller crop in 2020.

Table grape season will be several weeks later than average this season as above average temperatures, particularly overnight, have slowed the ripening process.

There may be positives to a later season, especially this year, as Coronavirus has restricted China’s logistics industry and caused consumers to become more cautious when purchasing food. China is Australia’s largest export market for table grapes accounting for 38.7 per cent of export volume in 2019.

There will undoubtedly be some disruption to table grape exports, especially shipments that were in transit during the peak of the shutdown. However, inter-province logistics are expected to return to full capacity in the coming weeks restoring usual table grape supply chains.

Australia is expected to record a record table grape harvest of approximately 240,000 tonnes this year with exceptional fruit quality. Exports are forecast to reach 175,000 tonnes an increase of 19.8 per cent year-on-year. China will be a key market for this year’s extra supply.

Domestic prices have maintained similar levels to previous years despite increased supply. In the coming month prices are expected to soften as typical harvest pressure influences values. In the event Coronavirus continues to impact China’s logistics and table grape export volumes, the redirection of surplus volume onto the domestic market could see prices come under significant downward pressure.

Red and green capsicums are in short supply this season as drought conditions early in the season have resulted in a smaller crop in Queensland. Capsicums would normally be in high supply during the summer months however prices have increased to reflect a smaller crop.

In February, both red and green capsicum prices averaged almost double the price of this time last year. Historically March would be a high supply month however as it is unlikely supply will increase, prices are expected to remain elevated as the season tails off in April.

Sources: AusMarket.
* Table grape price index includes red and white grape varieties.
* Nightshade vegetable price index includes capsicums, tomatoes, chillies and eggplant.
Commodity Overview

- Lamb prices are expected to rise further and reach a record high peak in late winter when supply declines to a seasonal low.
- Coronavirus may see Chinese consumers reduce spending on premium proteins including lamb and mutton, however any impact on domestic values is expected to be offset by domestic factors.
- Sheep slaughter could decline as much as 40 to 45 per cent before the end of winter, as rains ease destocking pressure.

The eastern states trade lamb indicator has risen 24.7 per cent since the beginning of the year and is closing in on record highs. Rain-fuelled re-stocker and feeder demand could continue to strengthen in coming weeks, adding to strong processor demand.

While demand is likely to strengthen, the seasonality of lamb supply suggests weekly slaughter rates could decline by 20-25 per cent before August, or further if producers opt to retain more ewe lambs to rebuild breeding flocks. Prices are likely to respond positively and reach a record high peak in late winter when supply declines to a seasonal low.

The ongoing spread of Coronavirus could weaken spending by Chinese consumers on premium proteins, and in turn may bring downward pressure to prices, however this is unlikely to outweigh the domestic drivers of prices.

Prices in Western Australia will continue to track at a discount to eastern markets due to the relatively poorer season, however values are expected to trend higher in response to the trend in eastern markets.

Mutton prices are expected to push further into record territory in response to declining supply and continued strong export demand, despite current values being on par with trade lamb values from 12 months ago thanks to a year to date increase of 26.9 per cent.

The strength of export demand was such that prices have tracked at record levels for most of 2019 despite elevated sheep slaughter in response to dry conditions.

Sheep slaughter has slowed in response to rainfall in January and February which provided relief from destocking pressures for many producers and could decline by 40-45 per cent before the end of winter.

Export demand is expected to remain firm as mutton consumption is less susceptible to reduced discretionary spending which may result from any economic downturn and is contributing to filling the pork supply deficit resulting from African Swine Fever in China.

Sources: Meat & Livestock Australia
Wool
March 2020

Commodity Overview

- Australian wool prices are expected to take a positive tone over the next month as a sense of normality starts to return to the Chinese market.
- Further spread of Coronavirus into other unaffected countries or renewed restrictions within China would likely bring further weakness to local values.
- Despite recent rainfall on the east coast, wool production this season is expected to remain around nine per cent lower than last season.

Australian wool markets are expected to remain volatile following the spread of Coronavirus to Italy, which is the destination of approximately five per cent of Australian wool exports. Despite the economic uncertainty, sentiment in China is improving with reports through local factories is beginning to pick back up following the coronavirus induced shutdown.

The impending northern hemisphere winter is also supportive for sentiment in wool markets and is expected to contribute to a stabilisation of local wool values.

Improved sentiment is expected to result in renewed interest from Chinese buyers at Australian wool markets and an uptick in demand. Any drop off in demand from Italy in response to the Coronavirus outbreak there has the potential to temper some of this support.

In support of wool values has been the weakening of the Australian dollar relative to the US dollar in response to global economic uncertainty.

Currency moves alone are not expected to outweigh the impact of reduced Chinese buying activity.

Notwithstanding this, the Australian dollar is expected to remain under pressure in the coming months, and this should be supportive to wool values.

However, should we see the virus spread into other unaffected countries, worsening of the spread across Europe, or a return to increased restrictions across China, we would expect buyers to step back from the market again, bringing pressure to local prices.

Sources: Australian Wool Exchange, Australian Wool Testing Authority
About Rural Bank

Rural Bank is a division of Bendigo and Adelaide Bank Limited and provides exceptional financial services, knowledge and leadership for Australian farmers to grow.

About the research

Rural Bank provides a monthly analysis of production and pricing trends for Australian agriculture. Focusing on cattle, cropping, dairy, horticulture, sheep and wool, the Update provides producers with a timely overview of current trends and an outlook for the coming months.