Agribusiness Economics

FARM AGGREGATES – OUTLOOK FOR 2008-09

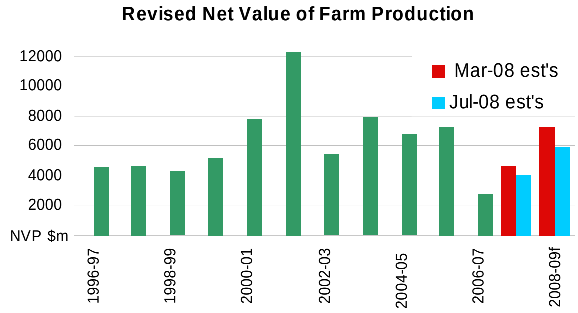
Thursday, 3 July 2008

Rising input costs constrain drought recovery

Increased winter crop production and strong global commodity prices are expected to underpin an increase in farm production and incomes in 2008-09.

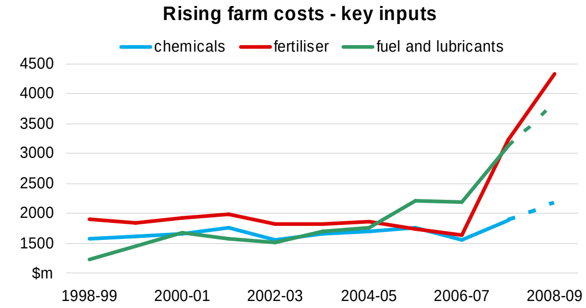
However, rising farm costs have resulted in a downward revision to 2008-09 farm incomes estimates (see chart opposite). NAB's key farm aggregates for 2008-09 are:

- Winter Crop Prod: 37 Mt, up 66 per cent
- Total Farm Prod: 88 Mt, up 20 per cent
- GVP: $44.5b, up 10 per cent
- Farm Costs: $38.5b, up 6 per cent
- Farm Prices: up 2 per cent
- NVP: $6 billion, up 48 per cent



Farm production, costs and incomes

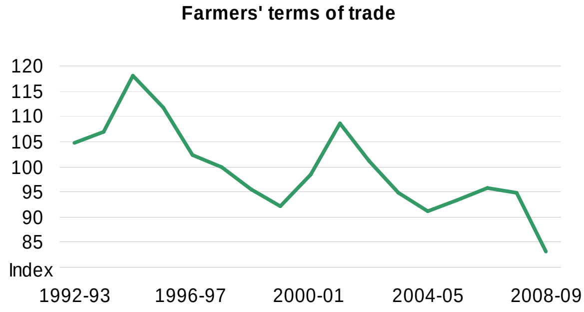
The net value of farm income (after costs have been deducted) is forecast to increase by 48 per cent in 2008-09 to around $6 billion — 18 per cent below NAB's previous estimate — due to a significant upward adjustment to farm cost estimates for 2008-09.



Reflecting this rapid increase in farm costs, relative to commodity prices, the farmers' terms of trade index (the ratio of prices received to prices paid) is forecast to fall to 83 in 2008-09, down from 95 in 2007-08.

Total farm costs are expected to increase by 6 per cent to $38.4 billion in 2008-09, as high global oil prices and rising global demand for chemicals and fertiliser places upward pressure on key agricultural input prices. Over the past five years, cash costs for fertiliser, fuel and chemicals accounted for 19 per cent of total farm costs; however, in 2008-09 this figure is forecast to jump to 27 per cent of total farm costs with:

- Fertiliser costs: up 34 per cent to $4.3 billion
- Fuel and Lubricant: up 26 per cent to $3.9 billion
- Chemicals: up 16 per cent to $2.2 billion



Oil Outlook

The fundamentals of the oil market have tightened considerably in the past five years, with a notable shift most recently. Net oil exports – effectively oil that is feely traded around the world – have fallen over the past two years. Importers such as the US and China have been competing for less traded oil, bidding prices higher.

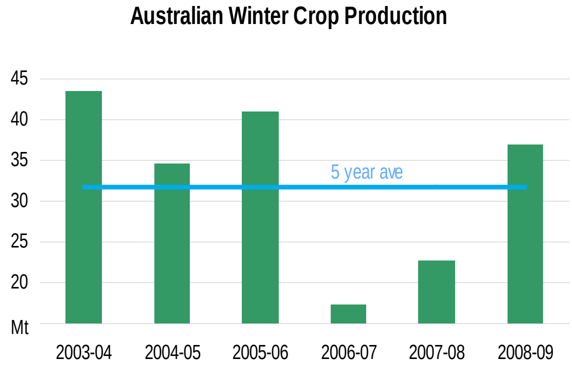
The key driver of this decline has been the rising consumption of crude oil in oil exporting nations – notably the Middle East OPEC nations. Oil consumption in this region has increased significantly, supported by subsidised petrol and diesel prices. Conscious of the social implications of a cut to these subsidies, there seems little motive to change policy. Reflecting the tight global oil market the price of petrol in Australia has continued to increase over the past five years and is estimated to average 135c/litre in 2007-08, 10 per cent above the previous year.

Looking forward, petrol prices in Australia are forecast to increase further in 2008-09 to average 150c/litre, reflecting our expectations for oil prices and exchange rates.

Winter crops forecast to drive recovery in farm production

Australian winter crop production is forecast to increase by 66 per cent in 2008-09 to 37 million tonnes — 5 per cent below NAB's previous forecast — after the driest May on record in Australia resulted in a downward revision to winter crop planting estimates. Reflecting this, current estimates for the major winter crops are:

- Wheat: 24.3 Mt, 86 per cent above 2007-08
- Barley: 7.8 Mt, 32 per cent above 2007-08
- Canola: 1.65 Mt, 55 per cent above 2007-08

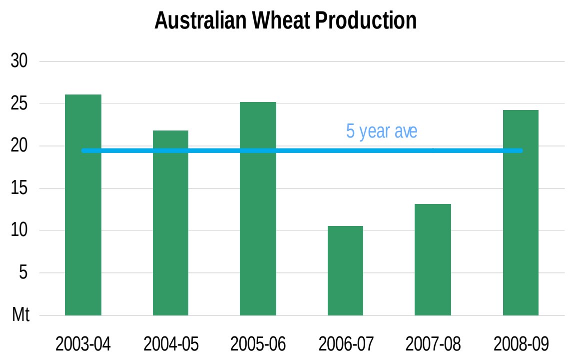


Regional Outlook

Southern NSW & south west WA

Production estimates have been revised down, in line with below average May rainfall. Solid falls in June have assisted early sown crops and allowed producers to complete planting. However, the poor rainfall outlook over the next three months raises concerns of another season of below average winter crop production in these areas.

Northern NSW & QLD



The outlook remains positive with many farms in the area receiving between 25 and 50mm of rain in June, connecting topsoil moisture with good subsoil moisture stored after above average summer rainfall.

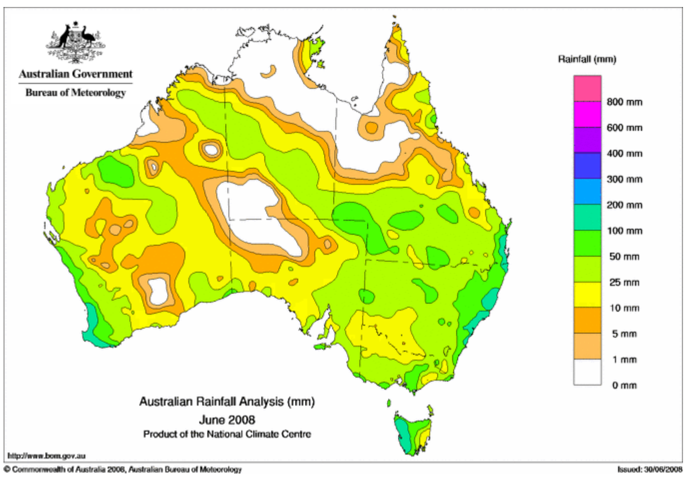
SA & Wimmera/Mallee

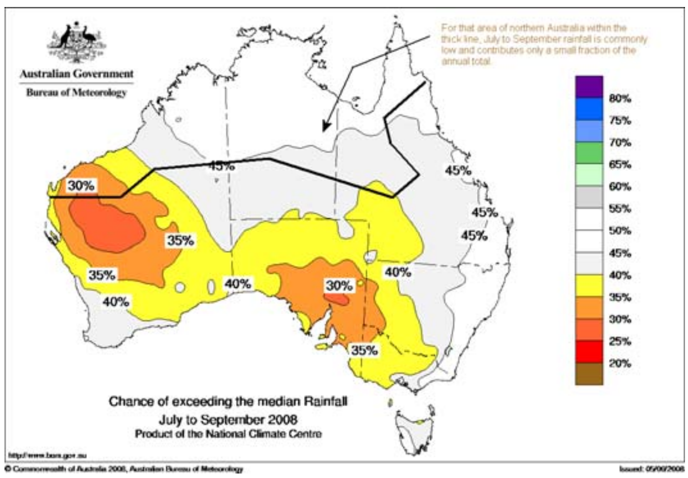
Projections have increased compared with previous forecasts, with good planting rainfall in late April and further follow up rainfall throughout May and early June lifting expectations of higher production in 2008-09.

Bureau of Meteorology Outlook

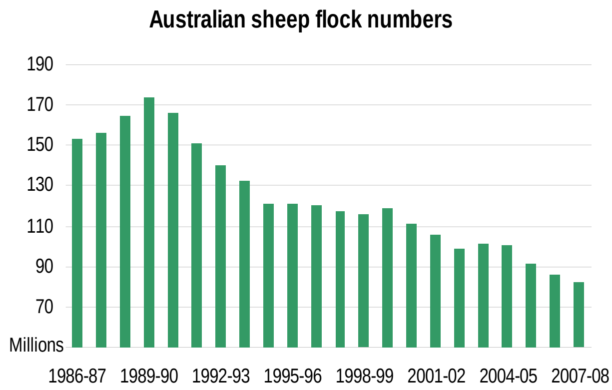
The latest Bureau of Meteorology seasonal outlook for July through to September shows a shift in the odds favouring drier than average conditions over a broad band from northwest WA to south eastern Australia. The chances of receiving above average rainfall from July to September are between 25 and 40 per cent, over a broad zone extending from northwest to southeast WA, across most of SA, parts of far southwest Queensland, far western NSW as well as western and northeast Victoria.

Rainfall totals:





Livestock



Livestock slaughter has remained high in the first half of 2008, as below average autumn rainfall in most states has constrained any significant pickup in restocker demand. In addition, a 9 per cent increase in winter crop plantings has assisted in maintaining high turnoff rates, as some producers switch into winter crop production to take advantage of the current high prices for cereal grains.

As a result, in 2008-09, lower opening livestock numbers and a reduction in the number of lambs and calves marked is expected to result in a decline in Australian lamb and beef production. In line with this, exports of both lamb and beef are forecast to fall.

Australian wool production is expected to fall in 2008-09, with a decline in the number of sheep shorn predicted to offset forecast higher fleece weights. According to the Australian Bureau of Statistics, flock numbers declined by 6 per cent in 2006-07 to 85.7 million in June 2007. In addition, reflecting the higher than anticipated mutton slaughter rates in the first half of 2008, current ABARE estimates suggest that numbers at June 2008 could be a further 4 per cent lower, at around 82 million head.

Australian milk production is expected to increase by 2 per cent in 2008-09 to 9.3 billion litres, in line with an assumed continual improvement in seasonal conditions and high farm gate milk prices.

USEFUL LINKS

National Australia Bank agribusiness reports

www.nab.com.au/agrireports

Bureau of Meteorology seasonal outlook

http://www.bom.gov.au/climate/ahead/rain_ahead.shtml

Murray Darling Basin Commission

http://www.mdbc.gov.au

Queensland Water Storage Information

http://www.sunwater.com.au/water.htm#

New South Water Storage Information

http://waterinfo.nsw.gov.au/copyright.shtml

Australian Bureau of Agricultural and Resource Economics latest outlook statistics

http://www.abareconomics.com/interactive/08ac_june/excel/Statistics.xls

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