ANZ AGRI
INFOCUS
AUGUST
2021

COMMODITY INSIGHTS

FOREWORD

There are signs in Australian agriculture that not only is winter finishing and spring upon us, even if it is ahead of the official start on 1 September, but that the end of the year and the summer period are all not too far away.

Across all Agri landscapes, perhaps the most noticeable sign of spring is the early flowering of canola crops.

On other farms, new and growing lambs, looking healthy in fields of green. This year, however, there will be one aspect of spring which will be different in many country areas. The cancellation of field days, country shows, and other Agri events that would otherwise be filling dedicated sites across the country is a real disappointment for many.

While the range of events differ in their size and focus, they serve a range of really important functions for both their communities and the wider agriculture sector. The economic benefits to many country towns of a field day go without saying – the revenue generated by local hotels, restaurants, and a range of other service providers often peaks around their annual local event – and provides a major fundraising opportunity for vital local community groups.

These events also provide a chance for a welcome break, networking, connection for a community known for their hard work. In an era of increasing mental health awareness, all of this seems more valuable than ever, and is a notable miss.

Very importantly, field days also provide an opportunity for farmers, agricultural retailers, service providers, and other industry specialists, to get together to exchange ideas, discuss innovations and experience emerging technology.

One of the issues which would no doubt be thoroughly discussed at such events would be the state of the rural property market. With the industry as a whole continuing to perform strongly, good seasonal conditions, another strong production year, and global prices for major commodities remaining strong, land prices have been a major topic of conversion.

The stand out implication for the industry's strong performance has been the demand for rural land and booming rural land values.

While rural land values have been growing strongly for a number of years now, including throughout recent drought years, there is some growing nervousness in the industry over the sustained, stellar growth in land values.

The question preoccupying industry players is – how high is too high? Are the current increases justified? There are many factors in play which are well recognised including strong commodity prices, low number of farms on the market and low interest rates. The value of rural land as a stand-alone asset, however, is less often discussed and when rural land is considered next to commercial and residential property, it appears that rural land is in a 'catch-up' phase compared to growth in alternative property-based assets.

The implications for the industry are clear as growing rural property prices make it harder for new farmers to enter the industry, or for farmers to expand. It is also clear that the drive for the industry to reach $100 billion in output by 2030 will also continue to have an impact on property prices – and reaching that target could see an almost 30 per cent increase in rural land values by 2030.

People in agriculture and country communities pride themselves on being resilient, as well as planning for the many scenarios that this sector can throw up. Looking ahead, it is vital that we all consider what 2022 might look like – for farm values, commodity prices, season and community. It's hard to have confidence in planning ahead these days, there are risks, and the potential for challenges next year that might be different again. Despite the uncertainty, most farmers are looking forward with confidence at an industry and season that, to date, have weathered the COVID-19 storm.

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RURAL PROPERTY MARKET INSIGHTS

OVERVIEW

Rural land values are booming, and as Australian agricultural production reaches record levels to buck the COVID-19 downturn and provide a much needed boost to the economy as a whole, there doesn't seem to be an end in sight. But as the industry focusses on the goal of raising production value to $100 billion – what does this mean for land values?

While the world has been gripped by COVID-19 outbreaks, lockdowns and vaccinations, one industry which can only be said to be 'thriving' is the Australian agriculture industry. With livestock prices at or around the highest level ever, last season's record wheat harvest and record dairy prices, Australian farmers are in the midst of some of the best conditions since the wool boom. Given that – why are some in the industry starting to feel a sense of nervousness over the sharp climb in rural land values?

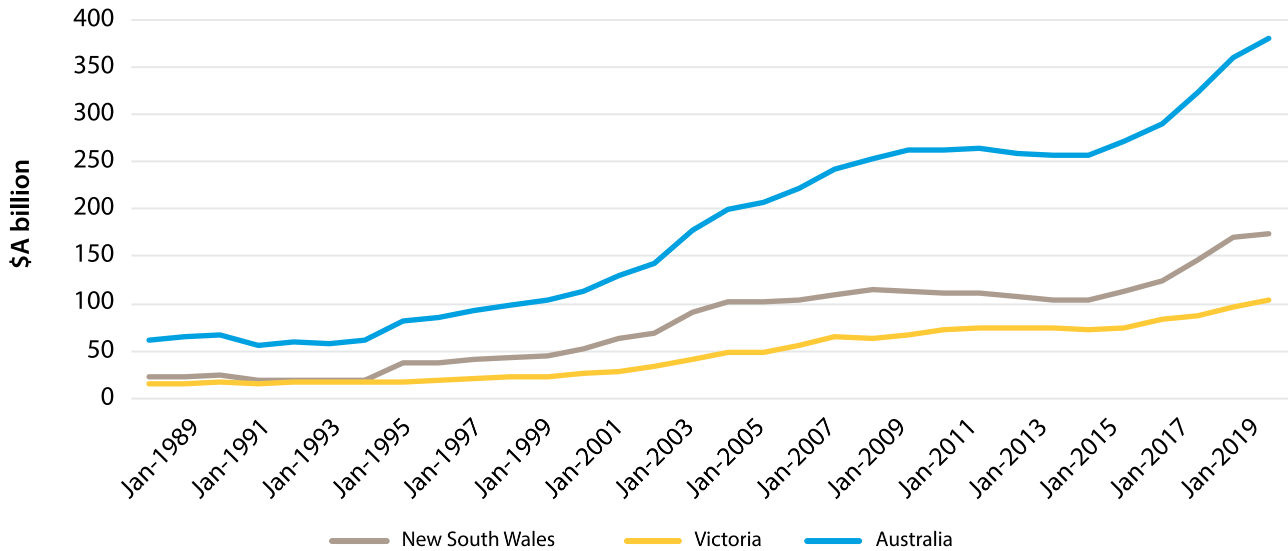
Low interest rates, strong commodities prices, farm consolidation, a low number of farms for sale and good season are the obvious answers to the current surge in land values. While over the long term rural land values have tracked commodity prices closely, up until this year there has been a notable divergence. So what's the x-factor?

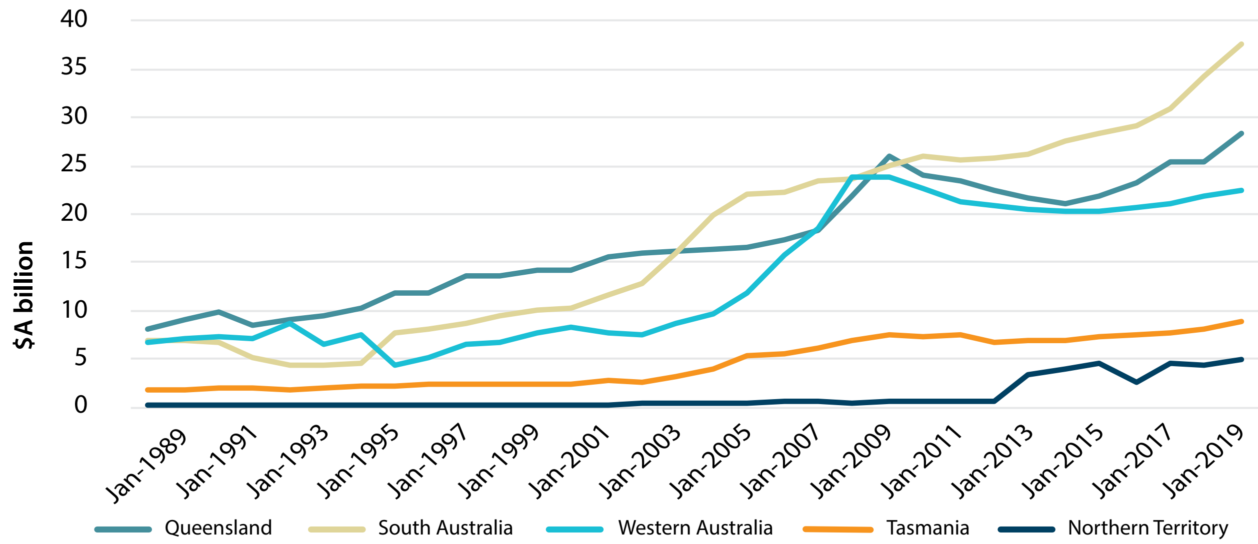
It may be that the driving force is less about the agriculture industry, and more about the comparison between rural land and other property-based assets. When we look at the growth in rural land values versus residential and commercial, it becomes clear that an element of the current growth spurt is 'catch-up' to alternative property-based assets, after years of relatively subdued growth.

RECENT, STRONG PRICE RISES

According to the official data from the Australian Bureau of Statistics (ABS), the value of Australia's rural land has appreciated by over 30 per cent in the three years to June 2020. This data is based on the information put together by each States' Valuer-General for government uses such as local council rates. But this can't be right, surely? We have all seen the headlines of large rural property sales and the ever increasing value of national agricultural land; or seen local properties sell at significantly higher sums than we expected – with many reports of localised growth over 20 per cent per hectare in a single year.

RURAL LAND VALUE BY STATE





Source: ABS, ANZ

THE FOMO FACTOR

So what else is factoring into higher rural land values, and is the growth as considerable as we're led to believe? In short, yes but there are other factors at play. There's no doubt that land value growth has been incredibly strong, which is well captured by the ABS data. But the ABS figures are inherently conservative and not necessarily done on the state of the land market at the time, rather they are based on the calculated 'underlying value' which market sentiment feeds into. The perception that land values are 'out of control' are being fed not only by strong demand but also by a reduction in supply.

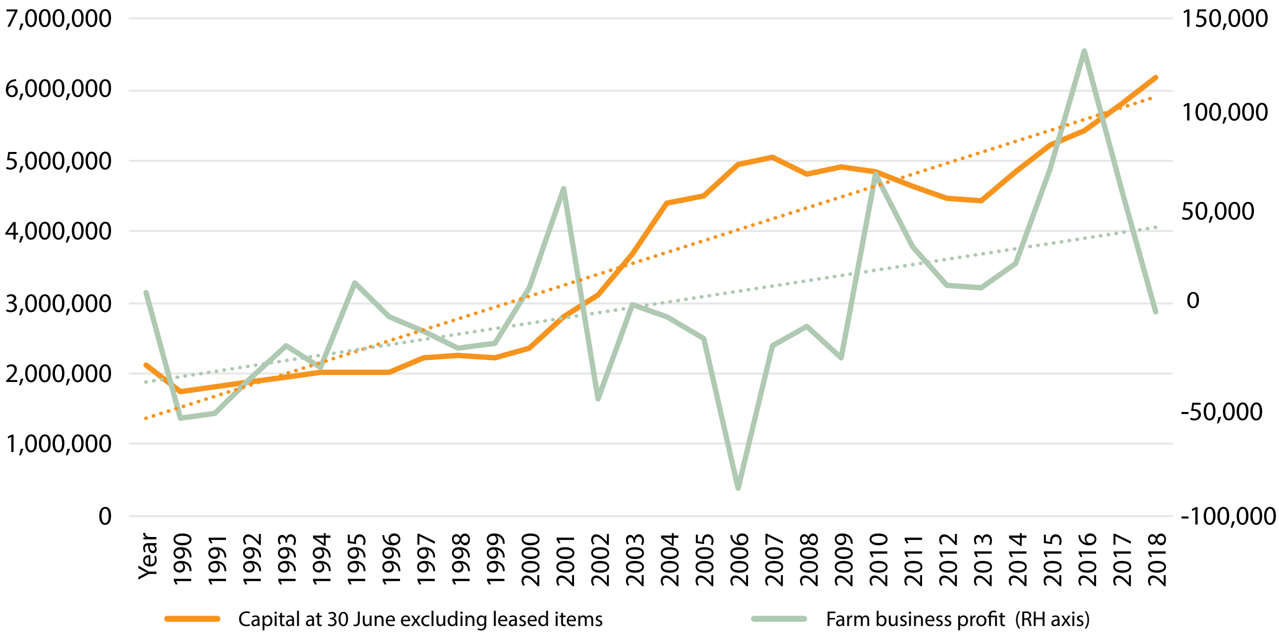
With commodity prices a very strong levels and good seasonal conditions over the past 12 months, not many farmers are selling – leading many in the industry to surmise that land values are being boosted by a lack of properties being offered. At a time when medium and large farmers are looking to grow their footprint and farm consolidation is driving change across the industry, the relatively small number of properties going to market is driving buying seen by many as 'over-priced'.

CHANGING VIEW OF RURAL LAND AS AN ASSET?

There is, of course, more to the story than just the 'fear of missing out'. Historically, rural land values have tracked commodity prices fairly closely, with drought years or commodity price slumps translating across to lower property values.

Since around 2016 however, land prices have continued to rise strongly despite drought years or stumbles in the commodity price such as the milk price drop. Clearly rural land values – and land values across all sectors - are strongly connected with historically low interest rates has provided a significant impetus for purchasers to buy now.

FARM CAPITAL V PROFIT

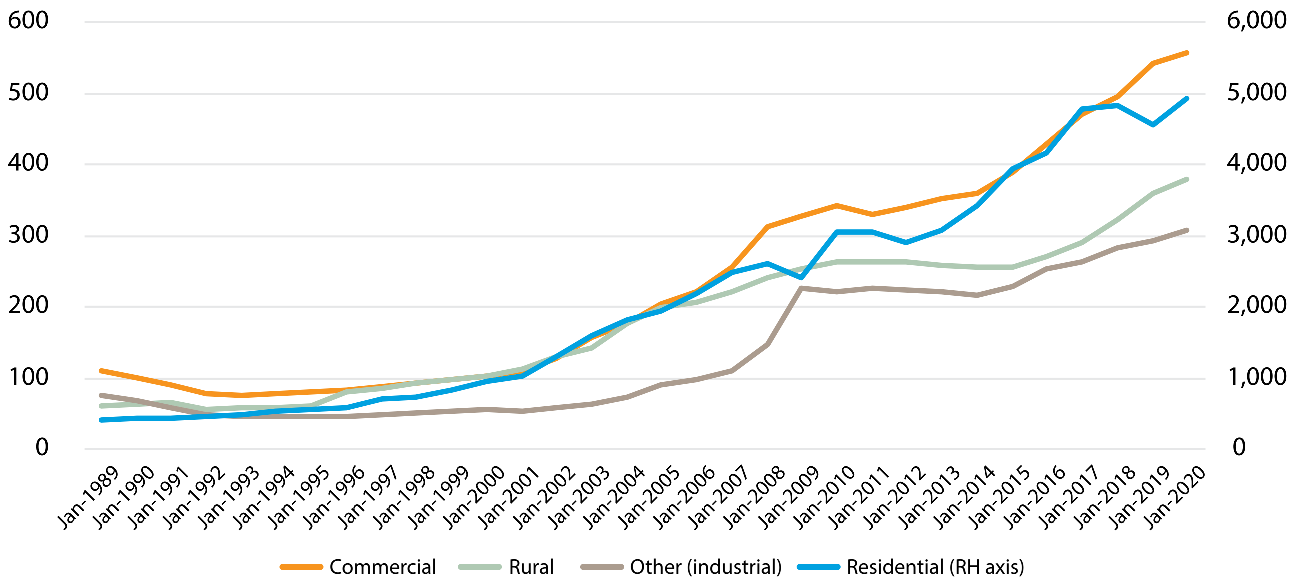


Source: AgSurf, ANZ

If this were the only real factor driving rural land prices then, we would expect to see rural land perform on par with both residential and commercial property. This has not been the case in recent years, however with rural land value growth outperforming the national residential property value growth by an average of 3 per cent each year (albeit from a low base) in the past 5 years – including drought years. Until the mid-2000s, residential, commercial and rural property had all shown relatively similar growth rates.

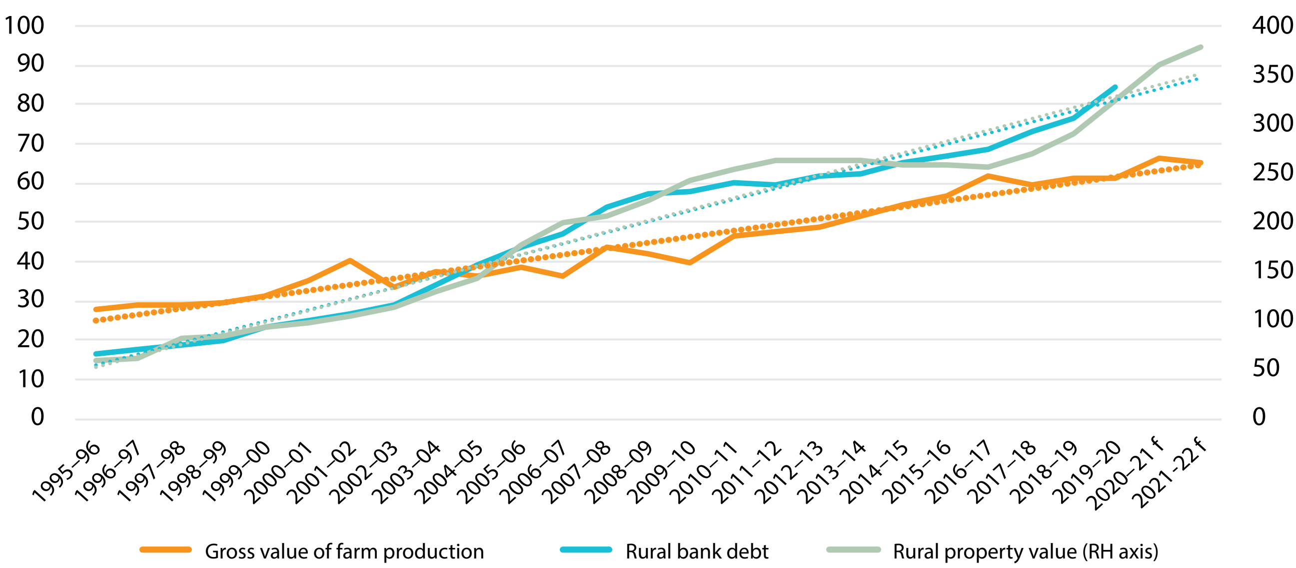
However during the 2010's, both residential and commercial property values have grown significantly stronger than rural properties. The recent growth in rural land may also be put down to investors seeking alternative property-based investments and playing catch-up to the residential and commercial sectors.

TOTAL AUSTRALIAN LAND VALUE BY INDUSTRY



Source: ABS, ANZ

NATIONAL GROSS FARM PRODUCTION, RURAL LAND VALUES AND RURAL BANK DEBT LEVEL



Source: ABARES, ANZ

LOOKING FORWARD TO $100 BILLION

With every boom comes the inevitable impact on asset prices. As Australian agricultural land values have climbed sharply in recent years, it has left many in the industry asking whether those prices can be justified based on the productive capacity and profitability. Rural land prices began to appreciate even before the end of the most recent drought, and before commodity prices had appreciated, raising the likelihood that the run on rural demand was more about consolidation, with medium-to-large farms buying and expanding their operations, than it was about pure profitability.

WHAT DOES THE INDUSTRY'S GOAL OF REACHING $100 BILLION IN OUTPUT BY 2030 MEAN FOR FARM VALUES? LOOKING AT THE LONG-TERM RELATIONSHIP BETWEEN AGRICULTURAL OUTPUT AND LAND VALUES, AN INDUSTRY OUTPUT OF $100 BILLION WOULD MEAN THAT THE TOTAL VALUE OF AUSTRALIAN AGRICULTURAL LAND COULD REACH $488 BILLION – AN ALMOST 29 PER CENT INCREASE ON TODAY IN VALUE BY 2030.

Rural debt levels were sitting at just over 26 per cent of rural land value in 2019-20 which has remained relatively stable in recent years despite drought. Since 1995, rural debt levels have fluctuated between just under 23 per cent and over 28 per cent. If this ratio is maintained to 2030 and $100 billion in output, then rural bank debt levels could be expected to rise to between $110 and $139 billion at the same time.

Demand for rural land isn't only coming from traditional farming, there are more investors seeing value in Australian property prices, international buyers continue to look for significant purchases, city dwellers looking to purchase their piece of regional lifestyle to escape lockdowns and even the recent trend of carbon farming and investors looking for offset opportunities. And while the strong demand for rural land must be considered a good thing for the industry – it does have ramifications for many, from new farmers looking to enter the industry and generational farmers looking to take advantage of high prices.

BEEF INSIGHTS

OVERVIEW

+ Records cattle prices provide a boon for all those producers selling stock
+ Demand for beef remains strong, especially in export markets with recovering economies
+ The Argentine suspension of beef exports has put Australia in an even more favourable global light

- High cattle prices will continue to provide challenges for many smaller restockers
- The tight supplies of Australian beef exports may push importers to continue looking to larger competitors
- The challenges to processors of the high cattle prices, including reduced capacity, could flow back up the supply chain

It seems appropriate that the past few weeks have been a time for records to be broken – both by Olympic athletes, but far more importantly to Australian beef producers, by cattle prices.

EYCI CONTINUING TO BREAK RECORDS

In late July, the benchmark Eastern Young Cattle Indicator (EYCI) broke through the once unthinkable 1,000 cent/kg mark. After months of the EYCI seemingly breaking record ground every few days, the ticking over to the new milestone was met with almost a sense of inevitability by many in the industry.

In some agri commodities, price rises to high levels are often followed by an equally sharp fall again, as the market rushes to take advantage of the price, and the resultant volumes on the market dampen the tightness of supply – the Australian lamb market is one example. For cattle however, prices have stayed high in the weeks since the 1,000 barrier was broken, and show little sign of any major reduction for at least the remainder of 2021.

While the reaction to the new peak in prices may have been somewhat muted, it is important to reflect on just how unforeseen, not that long ago, prices of this level were by many in the industry, and even more importantly, what this could mean for all stakeholders going forward.

One interesting indicator was that the National Livestock Reporting Service (NLRS), the body which collects and collates all the data essential for so much of the cattle industry's planning and analysis, was forced to call in IT experts to add a fourth digit to its online operating systems. If the experts at the core of the industry had not predicted that prices would ever reach this level when designing and building their systems, then the market is clearly in a whole new era.

It is also worth reflecting that this price level means that the EYCI has effectively doubled in around 18 months. It was in mid-January 2020 that prices pushed up through the 500 c/kg mark, having sat within a 400-600 c/kg band for around three years.

CORE INPUT PRICE DOUBLED

While it may seem basic, it is worth taking a moment to step back and look at what this means in context. The price of cattle, the central and fundamental commodity to the entire Australian beef supply chain, has doubled in a little over a year. Thinking about that in basic economic terms, the fact that both the prices received by the sellers in the market, but perhaps more importantly the price paid by those requiring this commodity have doubled in such a relatively short period, and far more quickly than so many of the other costs around them, must unavoidably create long term changes to the structure of the industry, especially if the high prices are maintained.

Major price changes this large and sharp are more commonly associated with the hard commodity sector – oil and iron ore prices are two of the major examples. Interestingly, the price rise of iron ore over the same period has been even more spectacular – up by around 146 percent – though the fact that the Australian iron ore market has a small number of concentrated suppliers, as well as one dominant trading partner (China, which is also relatively reliant on Australia), makes the market structure, and price implications, somewhat different.

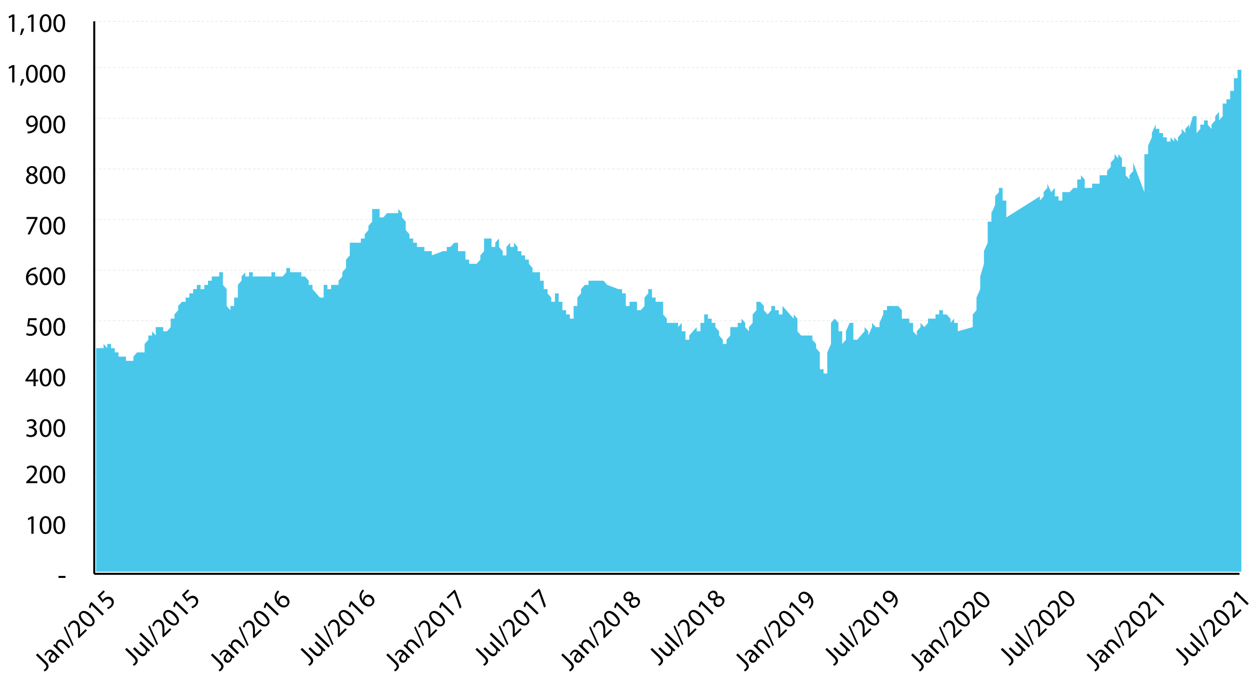
These unprecedented cattle price rises have come about through a combination of fundamentals, all interacting to generate than market activity.

EVERYTHING STILL RELIES ON SEASON

More important than anything is the rain. While no level of rainfall will ever be perfect – someone is always getting too much or too little – across most of Australia's cattle producing regions, the ongoing level of rainfall has been almost optimal, leading to excellent volumes of grass, which has provided growers with the capacity not only to rebuild their herds to pre-drought levels, but to potentially exceed those numbers. At the same time, their costs of supplementary feeding are negligible. As a result, if farmers don't need to destock, and if they can continue to build their herds internally, in combination with some restocking purchases, then it makes sense that the flow of cattle onto the market is going to be tighter than it has been for the past few years – a period which had possibly become accepted as the norm.

The fact that the good season is also likely to see larger cattle and carcass weights will also play into farmers not needing to sell cattle in the same numbers, to achieve the required returns for their operations.

EASTERN YOUNG CATTLE INDICATOR CONTINUES RECORD PRICE RISES



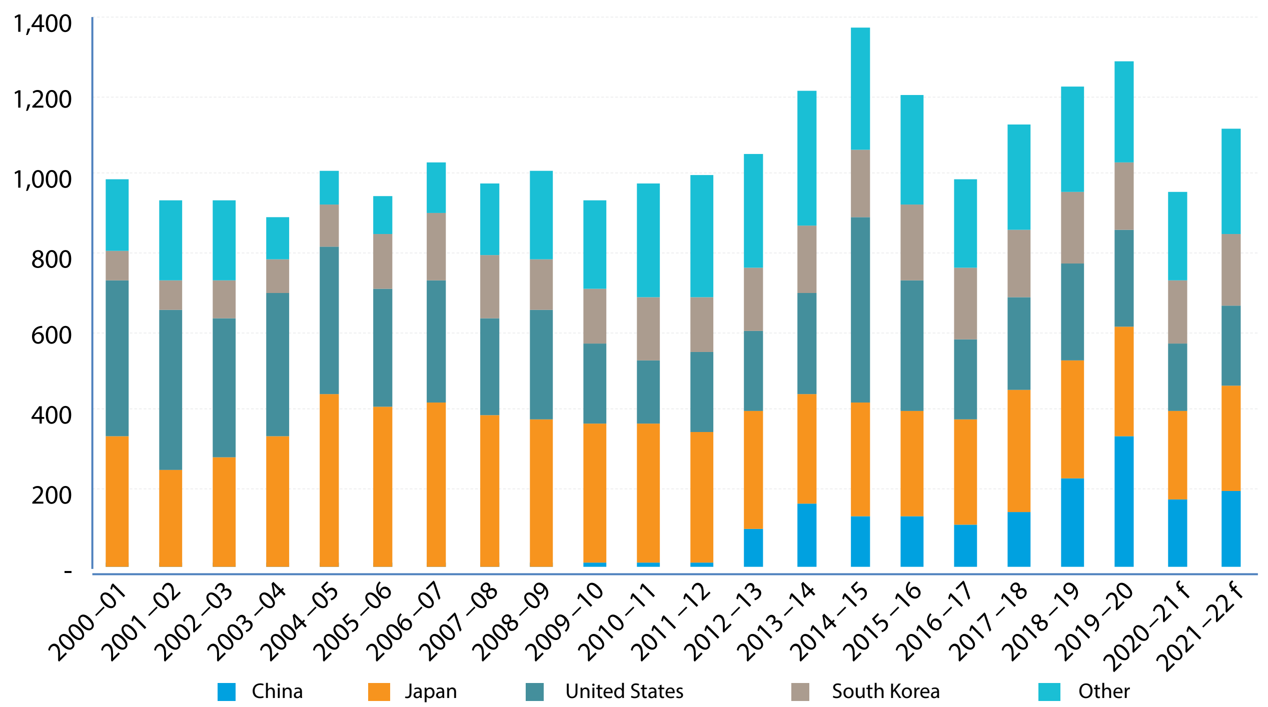
Source: MLA, ANZ

FALLING EXPORTS DRIVEN BY SUPPLY, NOT DEMAND

In terms of demand for beef, particularly exports, the market finds itself in an interesting position where the monthly numbers are well down, but the industry sentiment is increasingly positive. In July 2021, overall Australian beef exports reached just over 81 thousand tonnes, an eleven percent fall on the previous month, and almost seventeen percent down on the five year July average. Japan and South Korea took around half the total, while the United States and China were steady, but well down on last year's export figures. Despite these low numbers, the fact that they are driven almost entirely by Australia's tight supply, rather than dwindling demand or strong competition, continues to keep sentiment high. In terms of competition, the wariness in global beef markets of maintaining supply, particularly spurred by Argentina's recent temporary suspension of exports will continue for some time.

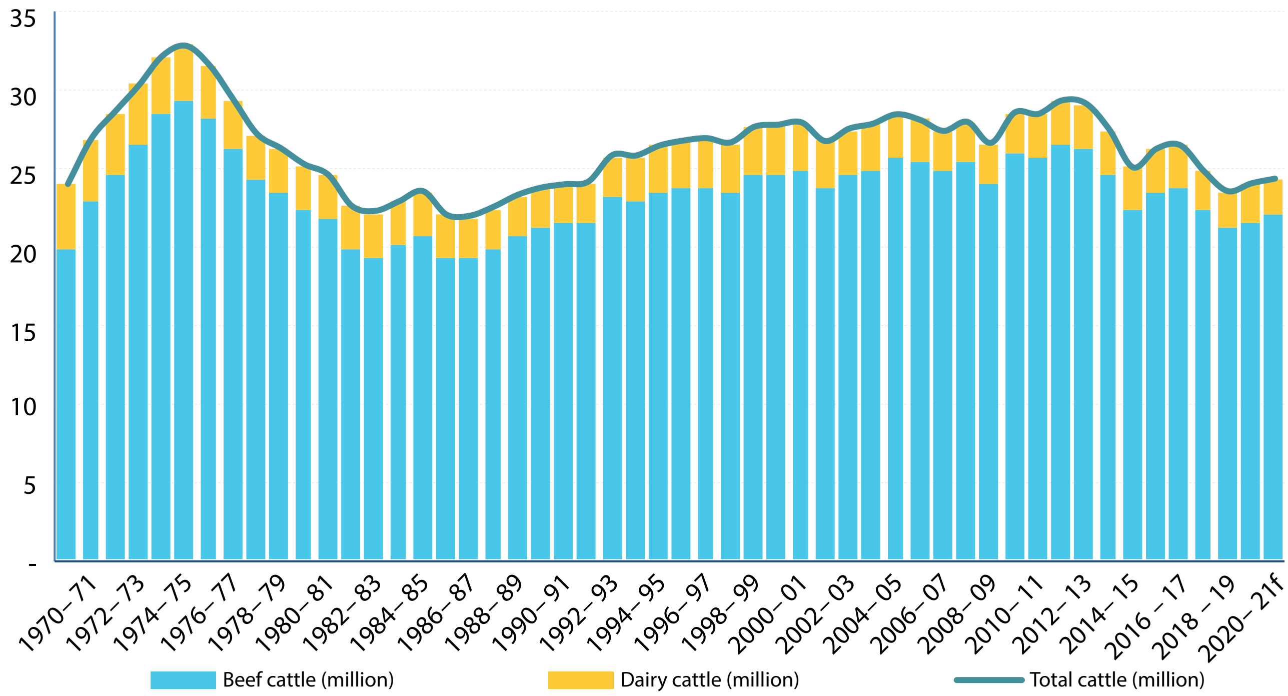
Finally, the combination of the tightness of supply, combined with high prices, may well see a speeding up of a fundamental change in the cattle selling process. Given that the three main buying categories – restockers, feed lotters and processors – all require ongoing supply for maintenance of their operations, the increasing competitiveness and uncertainty may stimulate greater offtake contracts and relationships, particularly between producers and processors. While this is unlikely to mean the decline of saleyards, especially as the herd recovers, the potential benefits for producers through processor relationships is something which may further work to their benefit in the long term.

BEEF EXPORTS SQUEEZED BY TIGHT SUPPLY



Source: ABARES, ANZ

HERD REBUILD CONTINUES, ALBEIT SLOWLY



Source: ABARES, ANZ

GRAINS INSIGHTS

OVERVIEW

+ Strong global and domestic grains prices continue being supported by drought conditions in Northern America
+ Good seasonal conditions in Australia's grain growing areas as resulted in early forecasts of strong, above-average harvest
+ Depreciation in the Australian dollar has also supported domestic prices

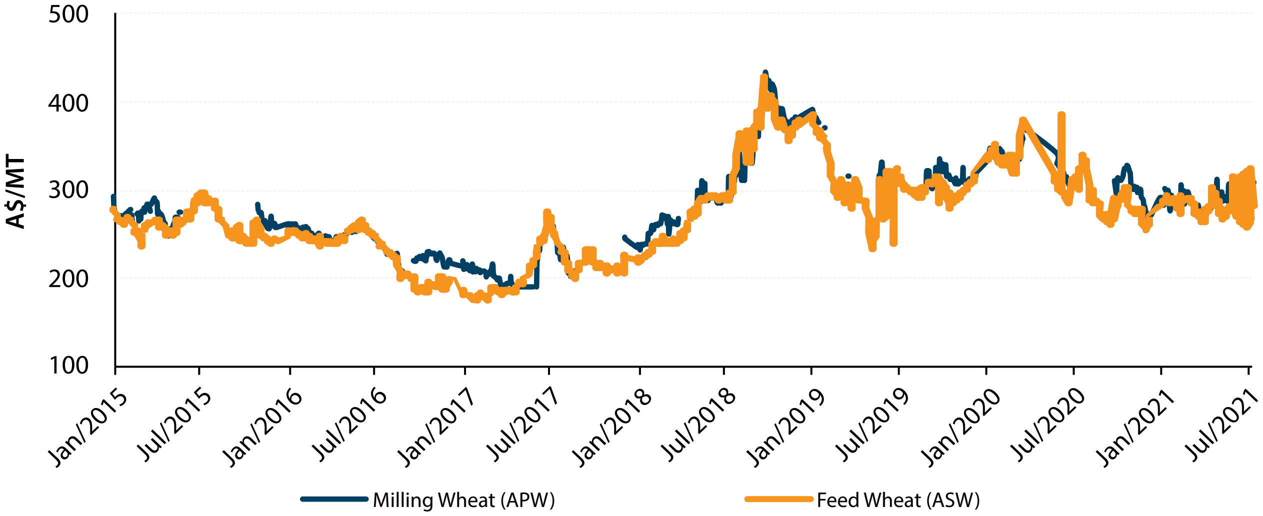
- Fertiliser prices have surged recently on the back of ammonia production shutdowns in Saudi Arabia
- Freight costs are also skyrocketing as a result of lack of capacity which is having mixed impacts for Australian producers
- Grains prices in Russia have been volatile in recent months indicating that there is some inherent instability in global prices

Continuing strong domestic and global wheat prices, a lower Australian dollar and forecast lower global production are all contributing to good conditions for local producers. However, a number of clouds are on the horizon which are tempering the global grains outlook, including soaring global freight costs, high fertiliser costs and volatile grains prices in the Black Sea region. While global production forecasts for both volume and quality have been shifting up and down from month to month, demand for Australian exports has been strengthening across south-east Asia – and most recently, in China.

STRONG GLOBAL WHEAT PRICES CONTINUE ON THE BACK OF CONCERNS OVER QUALITY

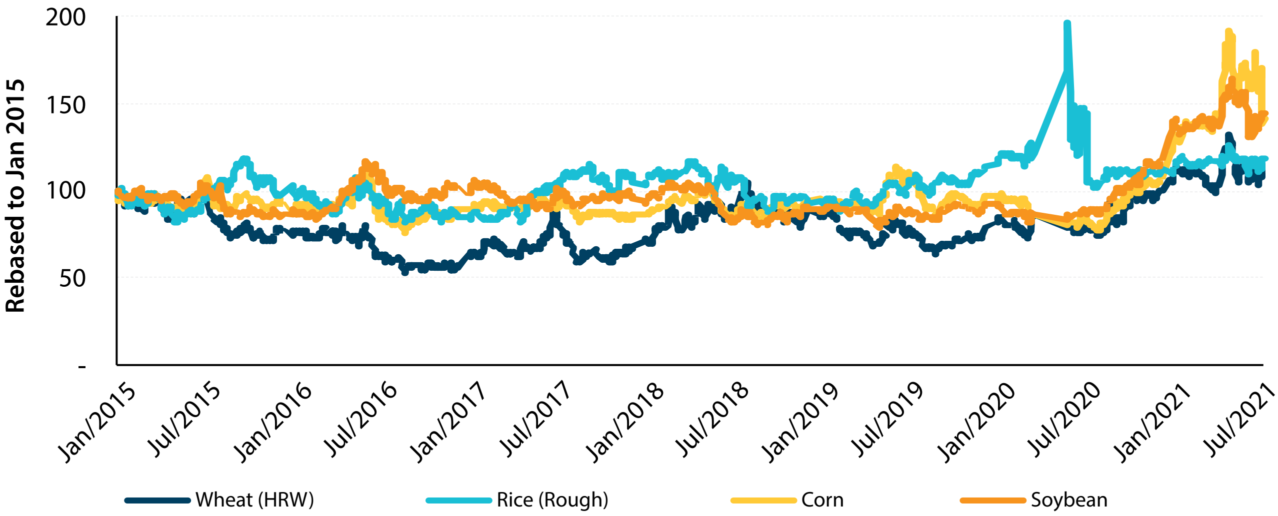
The global grains market is being dominated by the twin price pressures of surging global food prices, and soaring global shipping costs. Global wheat prices - which jumped in May coinciding with an increase in global food prices reaching their highest level since 2011 – were being primarily driven by maize prices. And while maize prices have come off, global wheat prices have remained relatively stable, being supported by recent downgrades in forecasts for global production.

DOMESTIC WHEAT PRICES STEADY



Source: Bloomberg, ANZ

GLOBAL GRAINS PRICES REMAIN STRONG



Source: Bloomberg, ANZ

The global production outlook has been mixed with drought in the United States and Canada, and a downgrade in Russia's expected bumper crop being offset by production levels in the European Union, Ukraine and the United Kingdom. The forecast Russian wheat crop is slowly being downgraded by a number of local and international analysts which are continuing to put upward pressure on global prices. Despite this, the United States Department of Agriculture (USDA) is forecasting a record global wheat harvest, based primarily on production in the EU, Ukraine and Australia. The driving factor behind strong prices is the ongoing concern around supply of high quality wheat following the drought and 'heat dome' impacts in Canada and the United States, and more recently, torrential rain and above-average temperatures in parts of Ukraine.

To offset record production, the USDA also is forecasting record wheat consumption, primarily as a result of higher feed and residual use by the EU and Russia. Trade in 2021-22 is also forecast at a record 203.2 million tonnes based on increased exports by Ukraine and India. Ending stocks are expected to increase slightly, however notably ending stocks are expected to fall for the first time in many years in China, while also remaining tight in major exporting countries which is considered a primary measure of supply.

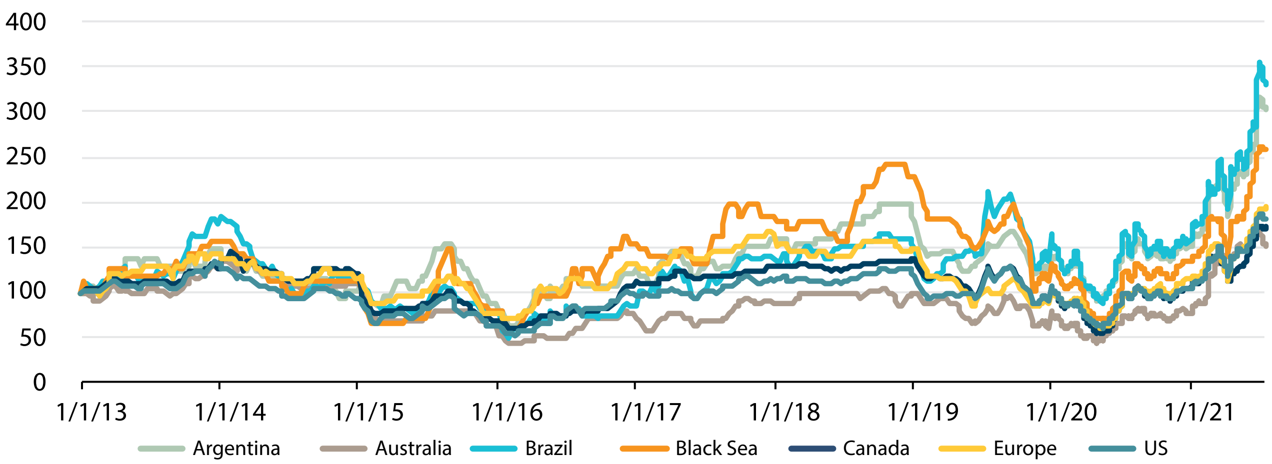
AUSTRALIAN WHEAT EXPORTS INCREASING TO CHINA

One of the major impacts of the drought in the US and Canada and the continuing downgrade in Russia's wheat crop has also created an opening in Asian export markets for Australian grain. Large increases in exports to Indonesia and Vietnam in 2021-21 have been followed by large shipments of Australian grain to South Korea, Indonesia and Thailand in the current year. As prices have increased in the US as a result of the season, there has been an increase in buying activity from China.

While Chinese buying is reported to be sporadic, it has marked a turn in the trading relationship.

Booming global freight rates which have come from a lack of capacity on major freight routes as a result of COVID-19 lockdowns are having mixed impact for Australian producers. While it has impacted margins for exports to European and Middle Eastern export markets, it has also resulted in Australian grains into Asia becoming more competitive with Black Sea region and European competitors.

GLOBAL FREIGHT RATES SOARING



Source: International Grains Council

2021-22 WHEAT CROP ESTIMATES APPROACHING 30 MILLION TONNES

The latest Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) crop estimate is for a solid domestic grains production season with the winter crop expected to be 13 per cent above the 10-year average. While harvest is expected to be down on last year's record harvest, good rains in many cropping regions in Western Australia, New South Wales and Queensland are expected to support a strong year. Mouse plague issues still remain across much of New South Wales, increased baiting will mitigate the major impact, however the additional costs will hit producers' bottom line. While total area sown to wheat is anticipated to reach a new record level, lower yields in New South Wales and patchy conditions in Victoria will impact the final harvest. Early USDA estimates of the Australian wheat crop are for a 28.5 milllion tonne harvest.

Booming canola prices as a result of the heat dome and drought in the United States and Canada have also resulted in a 25 per cent increase in canola plantings to 3 million hectares while barley plantings are expected to fall slightly. Chickpea plantings are also expected to increase area 20% to 607,000 hectares also as a result of high prices and good planting conditions in Queensland and New South Wales. On the down side, booming global fertiliser prices are also expected to hit producers' bottom line and curtail fertilising at a time when producers would normally be looking to invest heavily in soil condition. The boom in fertiliser prices is expected to be temporary however, as unanticipated shutdowns in ammonia production have flowed through to other classes of fertiliser.

EARLY ESTIMATES FOR AUSTRALIA'S WINTER CROP
ARE FOR A STRONG, ABOVE-AVERAGE HARVEST.

OVERVIEW

- + The ongoing strong prices for lambs and older sheep continue to be welcomed by producers
- + The good season, and ample grass, may well see some of the higher lambing percentages and heaviest lambs in some time
- + Demand remains strong, particularly into China, and especially for mutton exports

- - As with cattle, restockers could find high sheep prices challenging
- - Domestic consumption of both lamb and mutton remains lower than the industry would ideally prefer
- - COVID-19 disruptions have meant the cancellation of a number of major Australian sheep events for the second year in a row

With Spring just around the corner, the outlook for most sheep producers remains relatively bright. In most regions, conditions over the past few months have been largely good for lambing, with the majority of producers in Australia nearing the end of lambing and considering their farm strategies for coming months. Across the board for both livestock and meat, prices remain strong, driven by both restocking, as well as domestic and export meat demand.

GOOD SEASON LEADING TO STRONG LAMBING

For sheep producers, the rain and seasonal conditions at this time of year arguably provide a greater impact than on almost any other major agri sector. The relatively good conditions since the start of the year saw ewes come into lambing in better average condition than they had been for some time, leading to good initial lambing percentages. That said, the coming few months will be very important, in determining whether sucker lambs reach peak condition before sale, or whether they could potentially be impacted by colder conditions or above-average rainfall. While the season is far preferable to recent drought periods, recent strong rains across a number of regions have raised some concerns of a reduction in forecast percentages and lamb conditions.

Given the current high lamb prices, strategic sheep producers – and their stock agents – will be watching the market, and judging whether they will be better off selling lambs earlier, even if not in peak condition. While the normal scenario would see the volume of lambs from the spring flush pushing prices down, this year's high prices may see this volume hit the saleyards earlier than normal.

For heavy lambs, in the over 22 kg category, recent prices of around 957 c/kg have hit their highest levels since 2019, when prices peaked in the 900s. Importantly, as a portend for coming months, prices in 2019 subsequently fell steadily, dropping by 30 percent in the six months to the end of 2019, although subsequently regained most of this fall to climb to 956 c/kg by March 2020.

SEASONAL PRICE DROP EXPECTED IN COMING MONTHS

Looking ahead, assuming that market dynamics play out as forecast, lamb prices are likely to come off current highs over the coming month or two. One factor which may slow this trend down this year could be the potential for some producers to hold onto more of their lambs than usual, not just to continue restocking their properties, but to avoid paying high prices for ewes to build farm numbers.

The variation in seasonal conditions across different regions has seen different sale patterns in different areas. In Victoria's Wimmera Mallee region, tighter feed conditions earlier in the year saw a reasonable sell-off of ewes and lambs, which is likely to see a noticeably reduced volume of spring flush lambs. In these areas, some producers are likely to seek advantage of current high mutton prices, by selling cull ewes, or weaning early to sell older ewes.

COVID DISTRUPTIONS CONTINUE

The resurfacing of COVID-19 cases in a number of states over recent weeks, and the subsequent cross border restrictions between a number of states have created some disruptions for the sheep industry, though potentially likely to have minimal impact. Frustratingly, a number of major sheep events, including Hamilton's Sheepvention, Bendigo's Australian Sheep and Wool Show, and the Royal Melbourne Show have all been called off again in 2021, robbing a number of producers of the opportunity to take part in major industry competitions, and to increase the visibility of their rams. Similarly, recent border closures are likely to limit the ability of buyers to attend ram sales in different states, although the delay in the ability to deliver rams will hopefully be only short term.

Longer term, it will be interesting to see what the impact of the disruptions will be on not only major sheep related events, but on the traditional ram sale calendar. Many producers have now had around two years' experience of utilising online methods for buying and selling their rams, as well as other stock. While this may have lacked the social aspect of these events, many producers may well have taken note of the reduced costs and time commitment of being able to conduct everything online, until the rams or other sheep arrive at the purchaser's property.

CONFIDENCE IN MUTTON MARKET

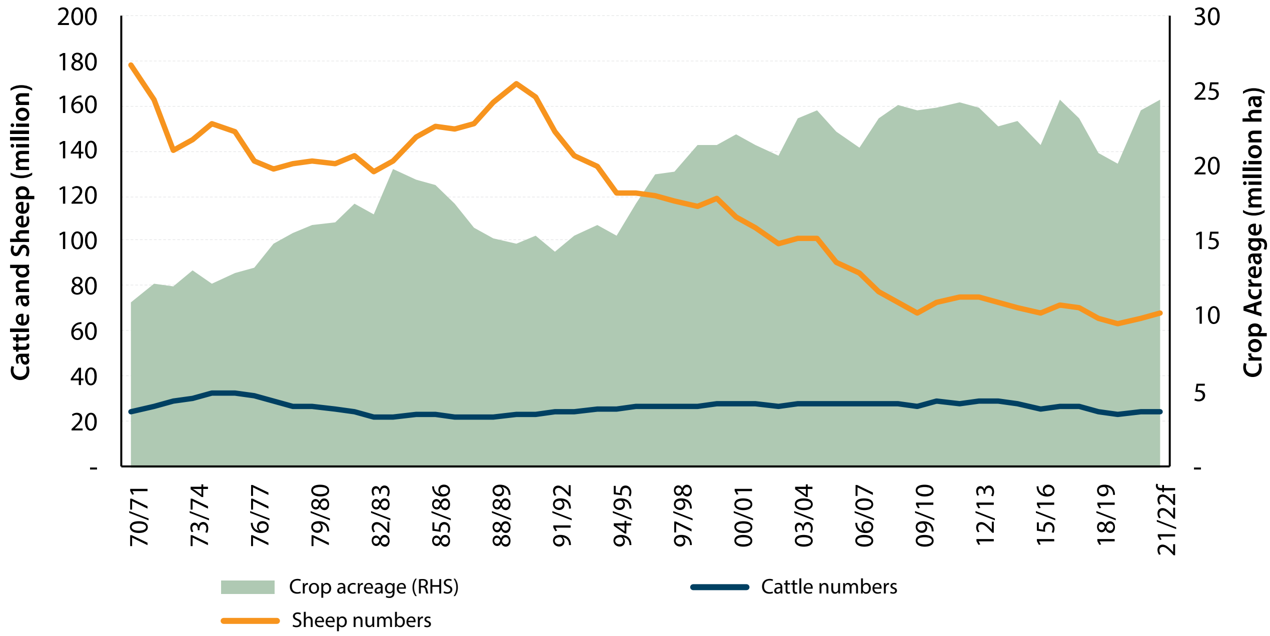
Away from the lamb price forecasts, the signs for mutton continue to be strong. Export demand remains high, largely from China, and a softening in the Australian dollar has only further increased the attractiveness of mutton exports. As a result, mutton export volumes are up around 30 percent on the same time last year. At the same time, mutton prices continue their steady growth, up around 26 percent from the price last September.

A sign of the confidence in the mutton market has been that recent larger yardings, particularly in NSW and Victoria, have had no downward impact on mutton prices.

A question which continues to be asked by many in the sheep sector, just as it has been with beef producers, is whether the pace of the restocking process may finally be slowing, or whether it is likely to remain strong. Given the forecast for a good spring, it may mean that many producers will be selling heavier lambs than they have for a few years, and that even if prices fall slightly based on supply, overall profitability may well be good.

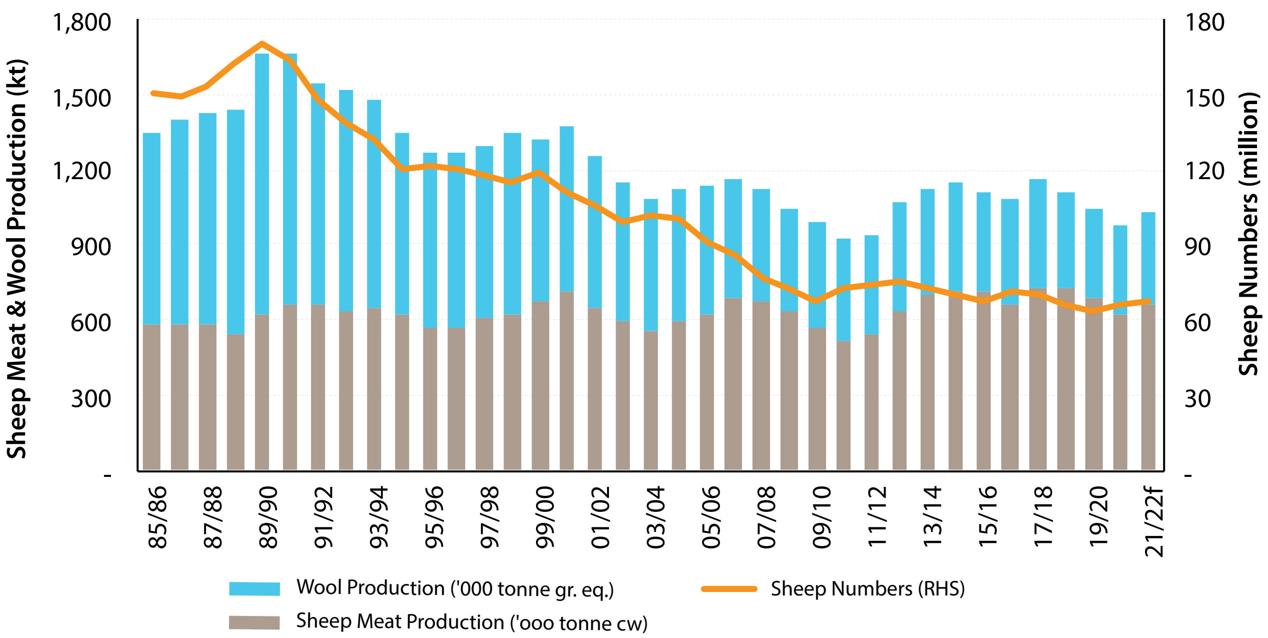
Given the combination of ongoing good feed, as well as industry confidence, it is likely that the restocking process will continue, potentially with a focus on replacement of ewes for the previous season's culls. In other times, if the returns on sheep were far more attractive than cattle or grain, then there may well be a move by some mixed producers to increase their flock considerably, while reducing the level of crops or other livestock. However, given the relative high prices of all major agri commodities this year, any rise in the flock numbers is likely to be muted.

AUSTRALIA'S SHEEP FLOCK REMAINS LOW BUT FLAT



Source: ABARES, ANZ

MEAT SHEEP CONTINUE TO DISPLACE WOOL SHEEP



Source: ABARES, ANZ

WOOL INSIGHTS

OVERVIEW

+ After the price dip of the last year, the ongoing wool price rises are welcomed by growers
+ High sheep prices are allowing many wool producers with the opportunity to hold their clip back to an auction time of their choosing
+ Recent wool prices stayed high, despite increased volumes on the market

- The wool market's renowned unpredictability is causing some nervousness after the mid-year auction break finishes
- With purchases for European winter garments largely already sold, there may be a reduction in demand
- Farmers selling sheep skins are seeing increased competition from synthetics, challenging historic high prices

While Australian wool sales were until recently paused for the mid-year auction recess, the medium term signs for the industry are looking relatively good. Prices are strong, despite higher volumes of wool hitting the market, and the most recent gains have been felt by some of the high microns, rather than just the fine wool.

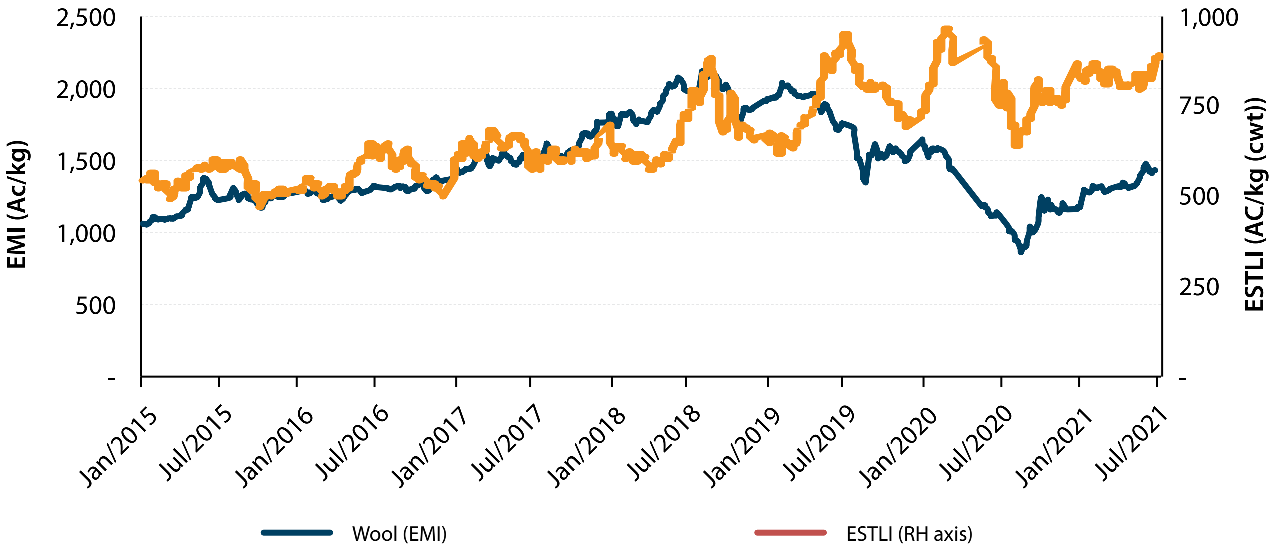
In the industry's final sale before the break, the benchmark Eastern Market Indicator (EMI) closed at 1428 c/kg, its highest price in sixteen months, and up over 60 percent on its low of September 2020. At the same time, wool sale volumes were also up considerably. For the first two sales of 2021/22, around 10,000 more bales were sold per week than the previous year.

From the increased volumes, it appeared that many growers who may have been holding their wool clips back, waiting for higher prices, finally took the opportunity to sell.

Another positive sign for many growers was the strong prices for the medium and coarse microns. For much of the recent rises in overall wool prices, the finer wools have accounted for almost all growth. However, in the weeks leading up to the mid-year recess, medium wools saw even stronger growth than fine wool.

Looking ahead, in particular with the auctions starting again mid-August, a number of industry observers are predicting that the market will follow its normal pattern for that time of the year, and slow or dip slightly. Prices are likely to be driven by several major variables. There is still likely to be a large volume of wool in the market, including stocks which had been held back for some time by producers whose high meat sheep returns meant they had no great necessity to sell, but who are now choosing to take advantage of the higher prices.

COMBINED HIGH WOOL AND LAMB PRICES BENEFITTING GROWERS



Source: MLA, Bloomberg, ANZ

In terms of buying activity, a lot of the wool required for garments for the coming Northern Hemisphere winter will have already been purchased, for processing and manufacture. In addition, the impact of COVID-19 may also play a role. On one hand, the recovery by major economies could see a resurgence in demand for woollen products, although the major social changes the disruptions have caused – such as the growth in working from home leading to a permanent shift in the demand for suits – may also indicate as easing in demand.

An interesting side effect of the recent rise on wool prices has been an increase in the value of sheep skin prices. While these are usually a small part of most sheep producers' operations, their price is often the subject of industry discussion, and can also be seen as one barometer of the industry's strength.

In recent months, the price of merino skins in particular has continued to strengthen. For merino skins with a 1.5 – 2 inch wool length, prices rose by 30 percent in one month to June 2021, to reach 1742 cents. For skins with a 3 inch wool length, prices reached 2633 cents. For each of these specifications, the prices are largely driven by the wool content of the skin.

Sheep skins have evolved in their uses, major markets, and their competition, all of which have impacted their prices. Traditionally, sheep skins were used for shoes and clothing, but are now increasingly competing with synthetics, which can have the advantage of being cheaper to produce. Lamb skins in particular were also popular for footwear or medical use, though are less in demand than in previous years.

While Turkey and Russia had been major buyers for sheep skins in the past, China is now the major customer.

Despite the long term fall in lamb skin prices, there has been some recent recovery. Lamb skins, which had once fetched around $25-30, had fallen to $2-3, but over the past year had risen strongly to $7-8.

DAIRY INSIGHTS

OVERVIEW

- + Consumers looking to connect more with where their food comes from, spending more on branded cheese
- + Opening prices increased as processors start bidding war for milk
- + Good seasonal conditions continue leading to high expectations for a profitable year for dairy farmers
- - Property prices being driven up by producers from other markets leading to farmers exiting dairy
- - Global Dairy Trade auction prices have declined following a strong start to the year

Dairy farms, like much of agriculture in Australia, are going one of two ways, consolidation for scale or boutique farm to table. During lockdowns the consumer demand for a link between farm and table is ever increasing. Consumers are looking to connect more with their food, hear the story behind the produce and farmers in a position to provide this are receiving premium for this offering.

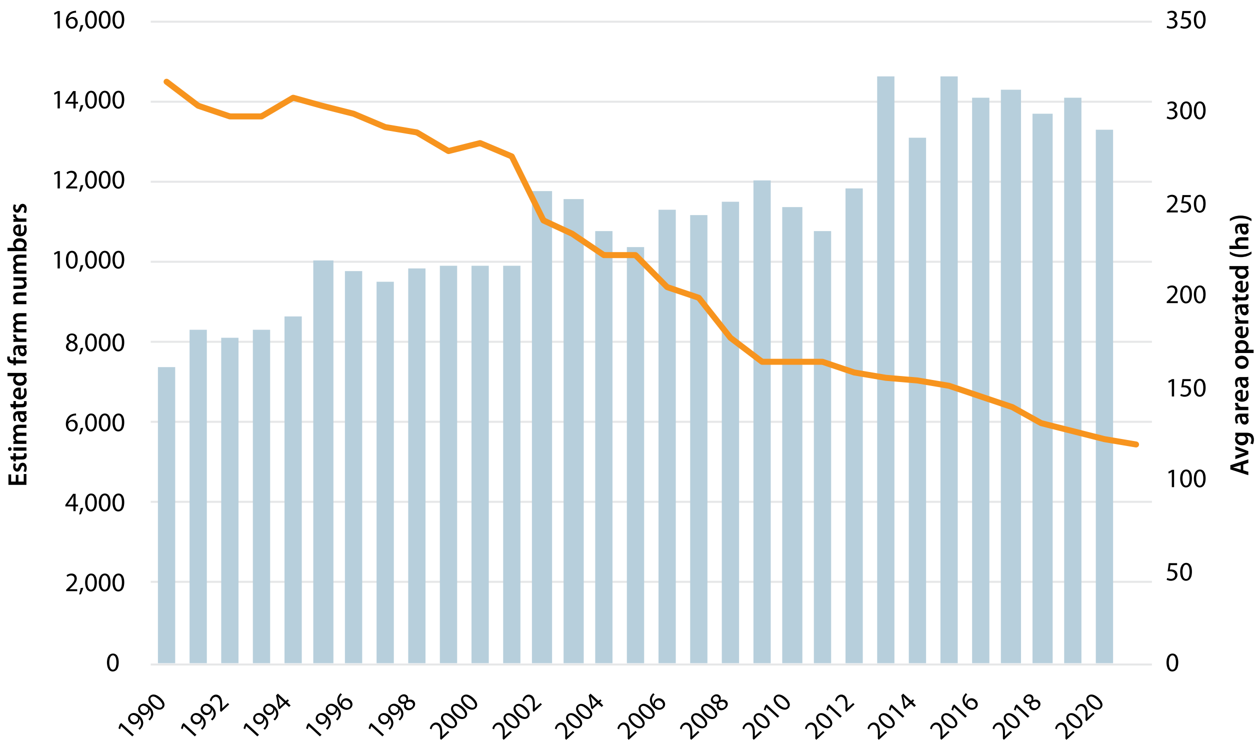
Major supermarket brands are also direct sourcing product for their home brands. Supermarkets are moving up the value chain in many fresh produce sectors and in dairy, they have already begun investing directly in farmers selling their milk through stores as a 'shed to shelf' offering.

It is likely supermarkets will be looking to take advantage of the increase in sales of everyday cheese ~4% which is currently being driven by increased consumer spending on higher end branded cheese as conscious consumers focus on quality produce. Or, stuck at home during lockdowns, are choosing to splurge on a nice cheese platter.

DAIRY FARM NUMBERS CONTINUE TO DECLINE

Unfortunately, while the outlook is good for dairy farmers there remain concerns in the industry that a series of difficult years has led to many dairy farmers leaving the industry and taking advantage of strong land prices. According to ABARES survey data, while the number of dairy businesses operating is at an all-time low so too is the amount of land under dairy as the average area operated also declines. The ongoing strong price for beef and other commodities is driving strong demand for dairy country with land owners taking advantage of high prices.

DAIRY FARM BUSINESS NUMBERS CONTINUE TO FALL



Source: ABARES, ANZ

DOMESTIC INDUSTRY EXPECTING IMPROVED PROFITABILITY

With good seasonal conditions continuing in much of the country, increased rainfall is improving soil conditions and filling ground water reserves. Improved grazing conditions has supported increased pasture grazing and this, along with lower feed costs, has greatly improved farmer confidence.

The lower cost of feed along with strong opening prices has improved profitability for dairy farmers with Dairy Australia Situation and Outlook Report indicating 88% of farmers are expecting a profit this financial year.

Farmgate prices are on the up since a strong start to the new season. A bidding war has put producers in the driver's seat with processor demand for milk driving up prices. The global position is looking good for domestic prices as well, as production growth remains relatively constrained despite increasing demand as the global economy recovers.

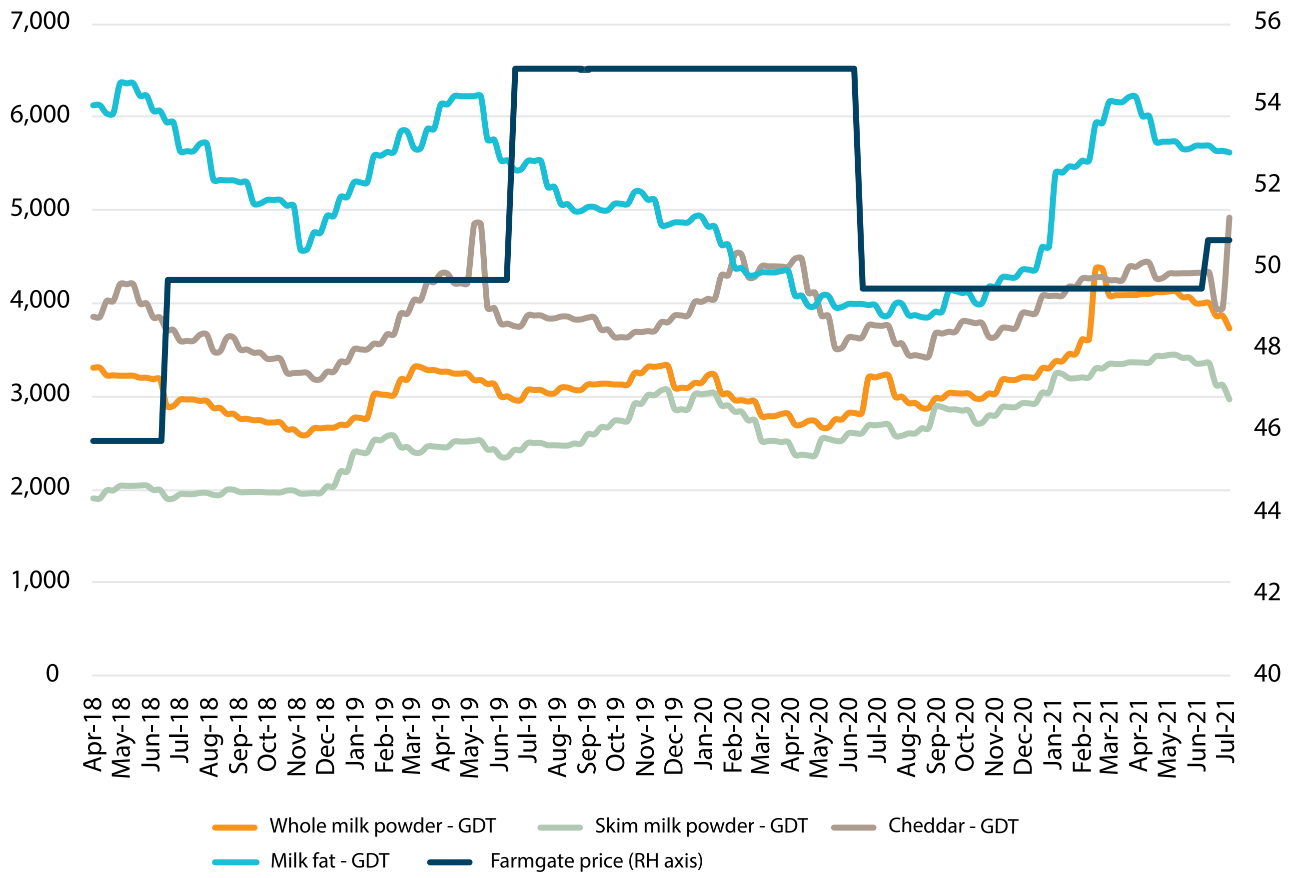
Opening prices were strong and have lifted with a price bidding war playing out in the market. Fonterra lifted their average farmgate milk price to $6.95/kg milk solids, up from the opening offer of $6.55/kg milk solids. Meanwhile Saputo revised their opening up 20cents to 6.85/kg milk solids just 3 days after the opening with Bega and Lactalis also announcing increases in their price offered by around 10 cents.

SOLID GLOBAL DAIRY DEMAND

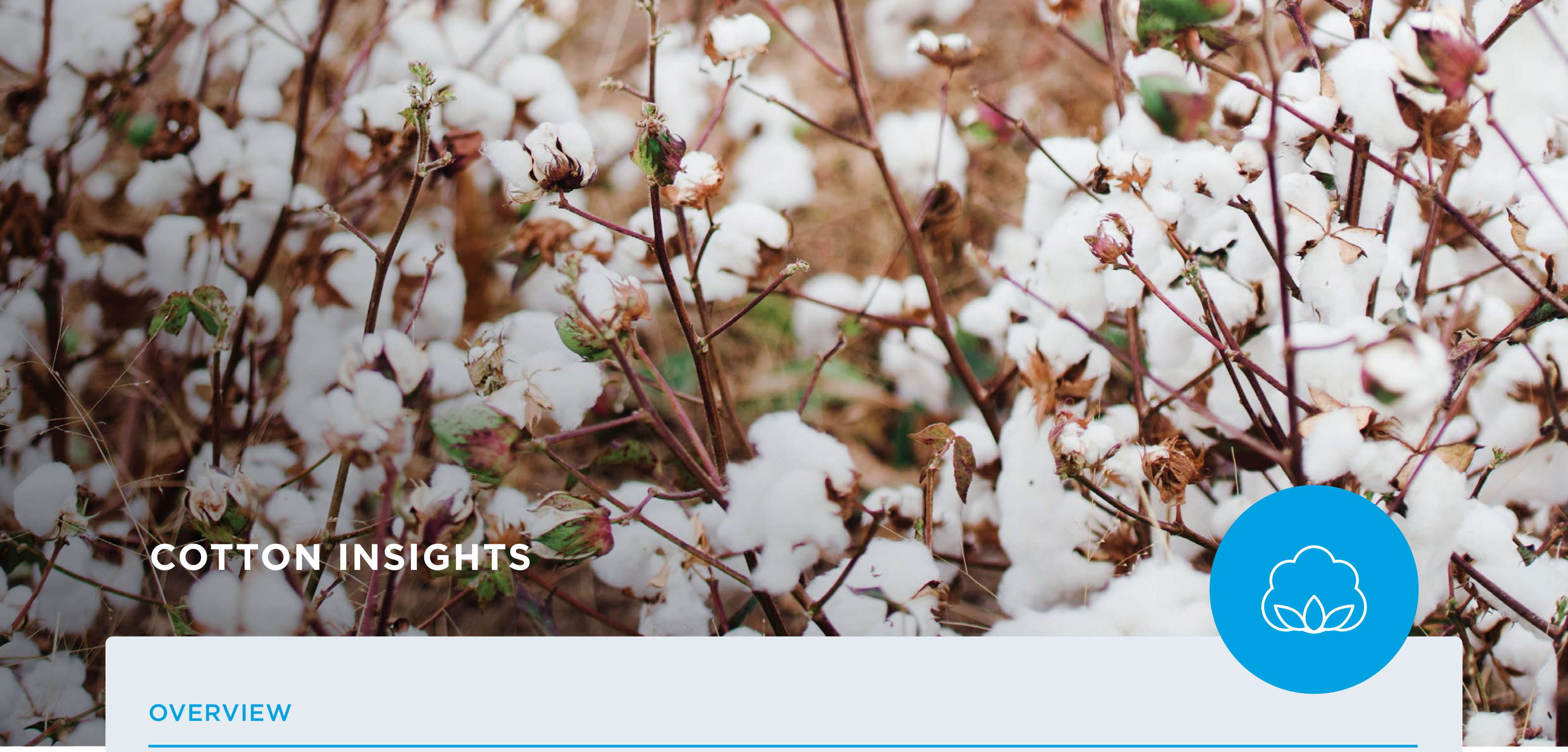
International demand, particularly from Asia, for dairy products, especially milk powder, is being driven both by an economic recovery, as well as a post-COVID-19 increased focus on healthier diets. Given these strong fundamentals, dairy assets are likely to remain attractive to investors.

Global dairy prices have been in decline since a very strong start to the year. This has, however, seen the solid gains from earlier in the years cemented at historically strong levels. The most recent GDT auction saw an overall fall in the average price of 2.9 per cent to $US3,839. This represents the 7th month of price index decline.

AUSTRALIAN FARMGATE PRICES LAG GLOBAL DAIRY TRADE AUCTIONS



Source: GDT, ABARES, ANZ



COTTON INSIGHTS

OVERVIEW

+ Cotton fibre as a sustainable plant-based option is becoming more popular
+ Cotton prices improving to above $600 per bale

- Unpredictable access to water impacting cotton farmers ability to plant consistently
- Limited infrastructure increasing costs for farmers moving to new regions

The unpredictable nature of cropping in the Murray Darling Basin is leading to some cotton farmers venturing north to seek out more secure rainfall in central and north Australia. Often considered desert, parts of north-west Queensland and the Northern Territory, Gulf country, receives huge volumes of water during the wet season. Harnessing this could change the landscape for Australian cotton.

Cotton Australia has named Katherine, Kununurra and Georgetown as emerging cotton growing areas. It's early days with many of these farmers in their first couple of years and limited infrastructure for cotton processing is forcing them to ship bails south to gins in central and southern Queensland. While this may appear an expensive exercise, local support has made this a worthwhile and valuable experiment. Time will tell if this bet will pay off for the early leaders.

While some producers seek to secure land with more secure water rights Cotton Australia is seeking buyers for what some are saying may be a record crop in 2022 just 2 years after the 40 year lows of 2020. The USDA is predicting Australia to reach 3.9 million bales in 2021/22.

AUSTRALIAN COTTON AS A SUSTAINABLE FIBRE OPTION

Cotton Australia will aim to promote Australian cotton fibre as sustainable, renewable and biodegradable. As traceability improves, buyers can ensure they are purchasing from farms using water sustainably and as a plant-based fibre there is also the possibility to market the product as Carbon Positive and environmentally sustainable, making it an excellent choice for environmentally conscious consumers concerned about the life cycle of their apparel.

INCREASED CONSUMER CONFIDENCE STRENGTHENING GLOBAL DEMAND FOR COTTON

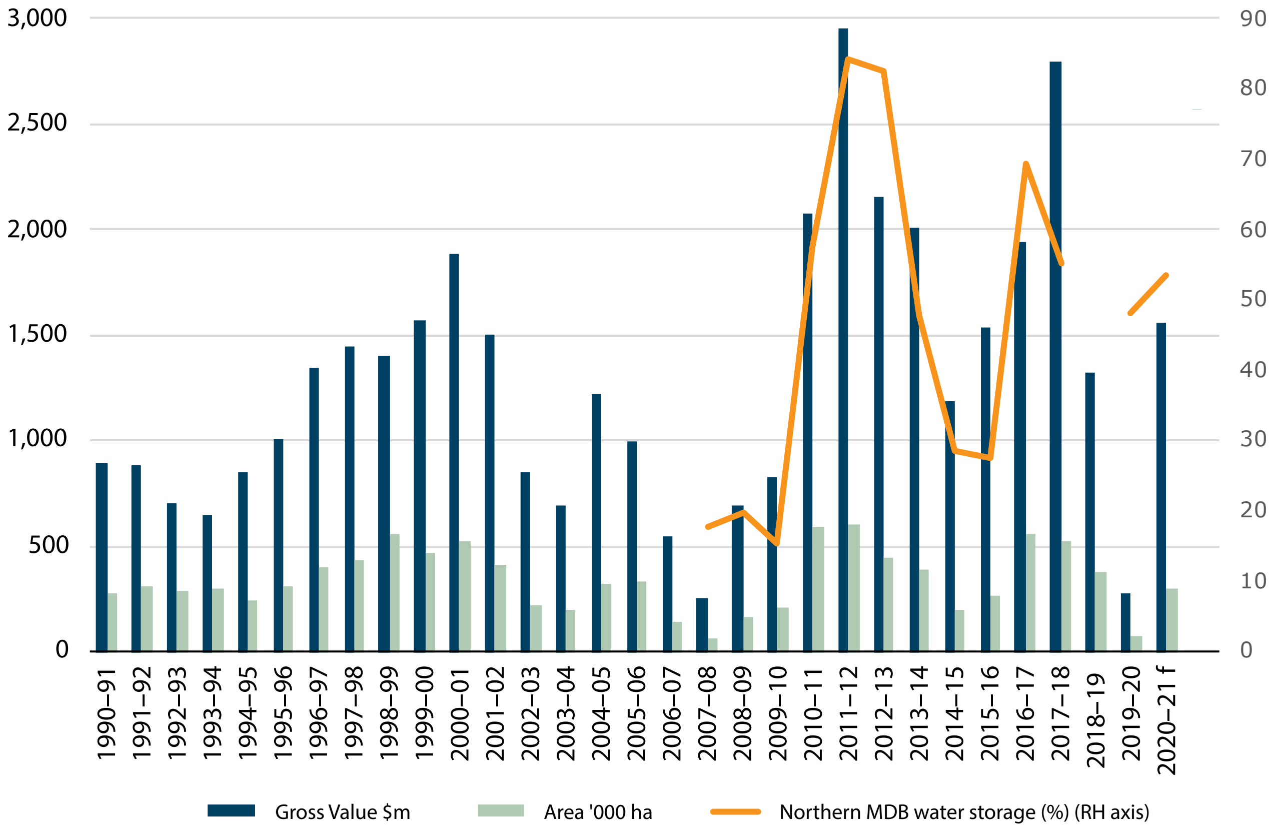
Not only has it been a better year for planting cotton but cotton prices have improved, edging above $600 per bale. This is due to increased demand from countries returning to post COVID-19 normal and projected cotton stocks dropping to the lowest level in 3 years. The predictions for stock to use ratio has also increased to around 71%.

The USDA global cotton projection indicates an expected increase of 6 percent in 2021/22 year to 119million bales.

The two largest producers are expected to be India at 24 percent, with China contributing 22 percent of cotton production. China's production is projected to fall 9 percent to 27 million bales with both a reduction in area and yield expected.

World mill use is improving, up around 4 percent on 2020/21 with increased global confidence in improving economies.

WATER STORAGE INCREASES IN THE NORTHERN MURRAY DARLING BASIN ARE LEADING TO INCREASES PLANTING AND PRODUCTION EXPECTATIONS



Source: BOM, ABARES, ANZ

ECONOMIC INSIGHTS

Delta to hit economic activity in the short term, but a strong rebound is likely

ECONOMY TO SHRINK IN Q3 DUE TO DELTA

Persistent lockdowns will remove any chance of growth in economic activity through Q3, as household consumption and businesses are limited by physical restrictions. While Melbourne is likely to see lockdown end by September or October, it is likely that the Sydney lockdown continues into Q4, slowing the recovery in economic activity. The much greater transmissibility of the Delta variant and the possibility of a longer lockdown in Sydney or further contagion into other states is a key element of uncertainty for the remainder of 2021 and into 2022.

BUSINESSES ARE MORE CONFIDENT THAN LAST YEAR DESPITE WIDESPREAD LOCKDOWNS

The latest business confidence and conditions data has been impacted by recent lockdowns, but they remain well above historical lows. Indeed, business conditions were at record highs before the recent Sydney and Melbourne lockdowns. While the Sydney outbreak and lockdown has removed the likelihood of positive economic growth in Q3, business balance sheets are in good shape and most will be able to recover quickly post-lockdown.

WE EXPECT THE UNEMPLOYMENT RATE TO INCREASE SOON BUT THEN FALL IN Q4

Employers are likely to hold onto their employees through lockdowns, particularly because of the current difficulty to find workers. This, combined with fiscal support including disaster payments, will mitigate the lockdowns' effects on employment and the unemployment rate. We expect the unemployment rate (4.6% as at the latest July data) to rise only modestly over the next couple of months, before resuming its downward trend.

While the rise in the unemployment rate will be quite modest, hours worked will fall sharply in Sydney as well as Melbourne, flowing through to lower household incomes.

HOUSEHOLDS HAVE MORE MONEY AND CONFIDENCE THAN LAST YEAR

National consumer confidence has now fallen to a similar extent as the decline during Victoria's second lockdown, but the level of confidence is much higher than last year. This is because the economy was in a stronger position at the start of the Sydney lockdown than it was when Victoria's began. The turn in confidence during Victoria's second lockdown came when daily case numbers started to fall, even though the lockdown extended well beyond that. We think this pattern will likely repeat.

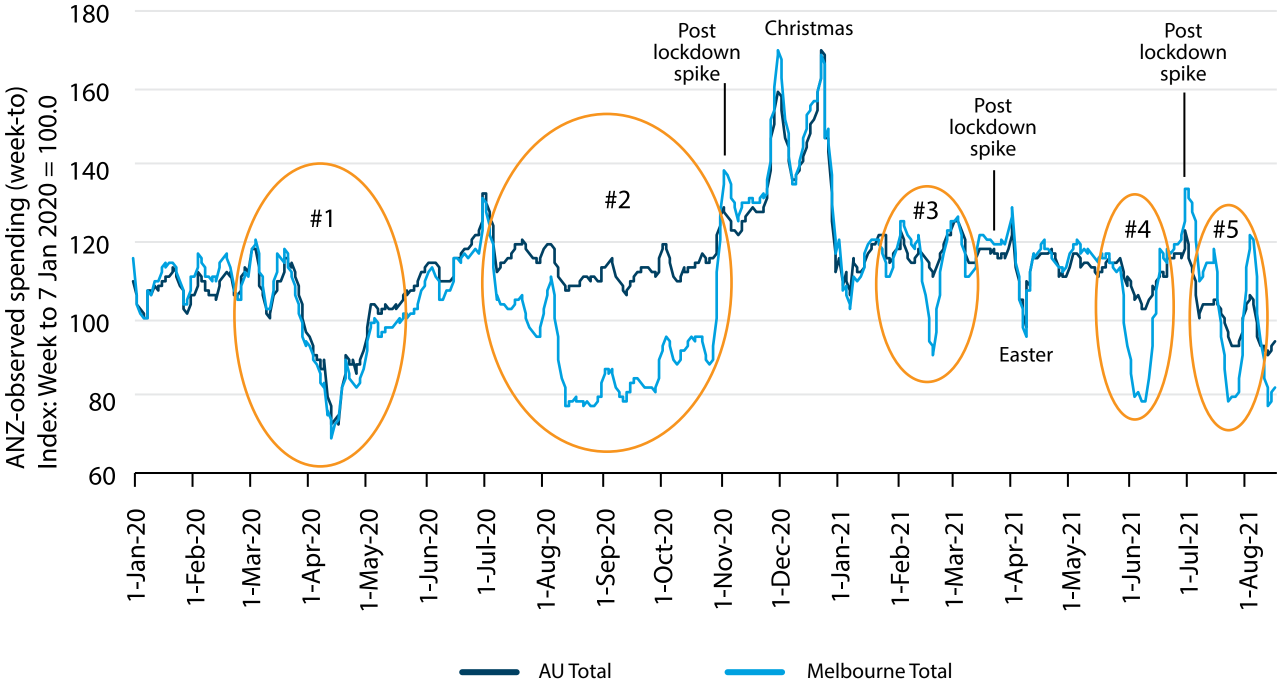
SPENDING USUALLY BOUNCES BACK RIGHT AFTER LOCKDOWNS

Ongoing fiscal support, strong housing price growth, resilient household incomes and low interest rates will support household spending outcomes once restrictions ease. The recoveries in ANZ-observed spending from Melbourne's fourth and fifth lockdowns were immediate, and we should see a swift rebound in Sydney and Melbourne spending once their respective lockdowns are over.

WE NO LONGER EXPECT THE AUD TO MOVE UP TO 0.80 USD

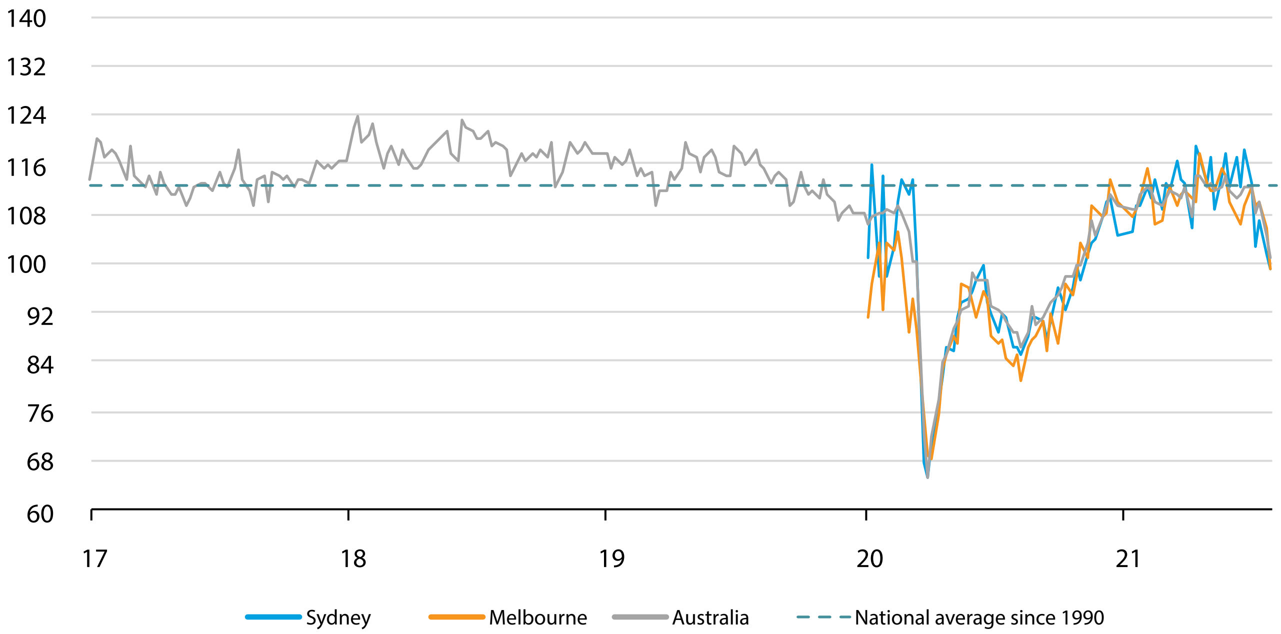
The AUD has continued to undershoot our forecasts as it remains untethered to the performance of commodity markets. We don't see this relationship normalising in the next 12 months. We expect that the AUD can re-test USD0.78 by year-end, but a move to USD0.80 looks like a stretch. The weaker outlook for the AUD will help the competitiveness of exports, including agricultural goods.

SPENDING TENDS TO SPIKE AFTER LOCKDOWNS, WHICH COULD SPEED UP AN ECONOMIC RECOVERY AS RESTRICTIONS EASE



Source: ANZ Research

CONSUMER CONFIDENCE IS DOWN ACROSS THE COUNTRY, BUT STILL FAR STRONGER THAN LAST YEAR



Source: ANZ-Roy Morgan

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