Ministry for Primary Industries
Manatū Ahu Matua

SITUATION AND OUTLOOK FOR PRIMARY INDUSTRIES UPDATE DECEMBER 2012

HIGHLIGHTS

- Global economic conditions have deteriorated since the release of the Ministry for Primary Industries June forecasts[1] of commodity markets – this has dampened prospects for New Zealand's primary sector exports.
- Short-term prospects have also been adversely impacted by the exchange rate, which has appreciated against most major trading currencies since June 2012.
- As a result, total primary sector export revenue is forecast to decline around 3 percent to $27.5 bilion in 2012/13, compared with our June 2012 forecast.
- International dairy prices are expected to recover over the remainder of the 2012/13 dairy season and beyond.
- Lower lamb prices are expected to reduce export earnings in the year to 30 June 2013, whereas beef prices are expected to remain firm over the next two years.
- The forestry sector will remain squeezed over the next few years, due to subdued demand from major export markets – export volumes are expected to hold up, but some product prices will not.
- Horticultural exports are on track to reach $3.5 billion in the year to March 2013, with higher in-market prices expected to offset lower volumes of kiwifruit and wine.
- The bacterial vine-killing disease 'Psa' has spread to nearly all kiwifruit growing regions, and will adversely impact gold kiwifruit exports in the year to March 2014.

1 *Situation and Outlook for Primary Industries 2012*, available at http://www.mpi.govt.nz/news-resources/publications.aspx?title=Situation%20and%20Outlook%20for%20Primary%20Industries%20(SOPI)%202012.

MACRO-ECONOMIC SITUATION

Global economic conditions have weakened since the release of our forecasts in June 2012, due to a further deterioration of the EU economy and a slow-down in China and other emerging markets. As illustrated in Figure 1, the International Monetary Fund (IMF) recently revised down its 2013 growth forecasts for at least 80 percent of New Zealand's export markets, compared with six months ago.

The structural and fiscal adjustments necessitated by the ongoing European debt crisis and imminent US fiscal 'cliff' create further downside risk to New Zealand's commodity exports in the short-to-medium term. Such adjustments are likely to underpin a strong New Zealand dollar (NZD) – refer below.

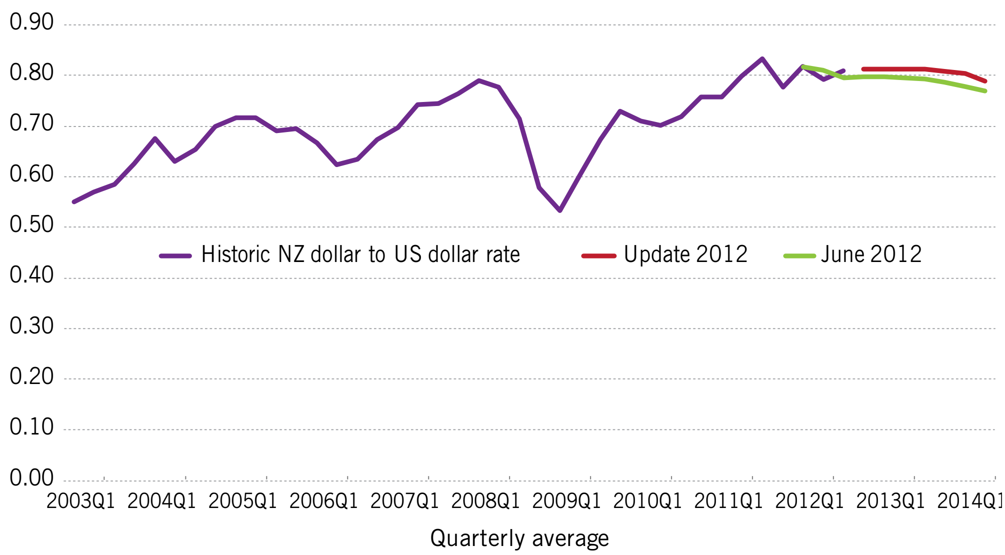
By contrast, the US drought has had a positive influence on international agricultural prices, and despite relatively weaker growth in China and other emerging markets, they are still expected to grow strongly in absolute terms, as is their demand for safe and nutritious food.

EXCHANGE RATES

The NZD has appreciated against the United States dollar (USD), the Euro and the United Kingdom pound (UKP) over the past two years. This has mainly reflected expansionist monetary policies in the US and the UK and fears regarding the future of the Euro.

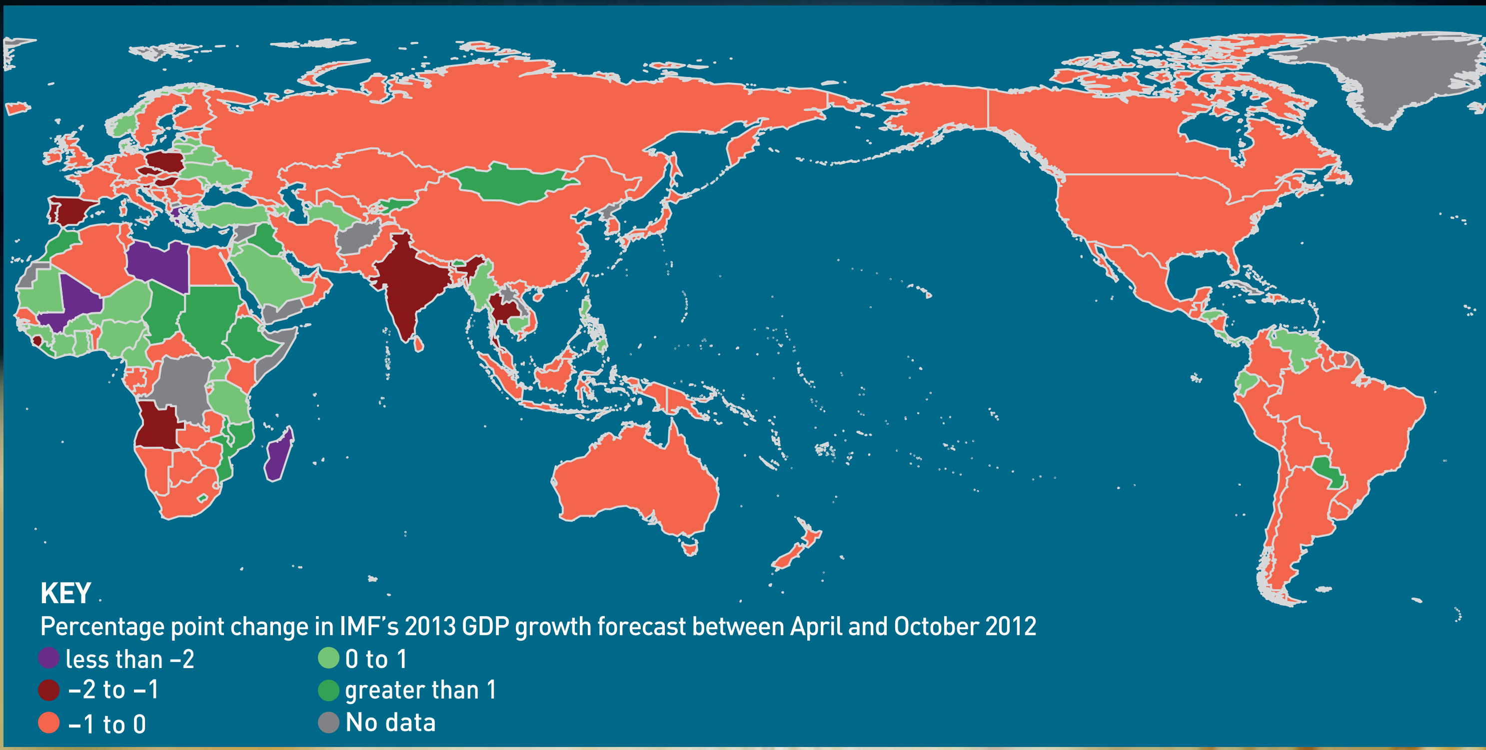
The Treasury exchange rate assumptions used for our updated forecasts is an average NZD/USD cross rate of 0.807 over the period December 2012 quarter to June 2014 quarter. This compares with 0.788 used in the June 2012 forecasts – refer to Figure 2.

Figure 2: New Zealand dollar exchange rate



SOURCE: Reserve Bank of New Zealand and The Treasury.

Figure 1: 2013 Economic Growth Forecasts



Source: World Economic Outlook Database (April 2012 and October 2012 Edition), International Monetary Fund.

DAIRY

This update slightly revises down the short-term forecast farm gate milk price and dairy export revenues, compared with the June forecast.

New Zealand experienced superb climatic conditions in 2011/12, boosting milk production by 11.4 percent. Assuming a return to average climatic conditions, milk production is expected to remain at 2011/12 levels in the current season. While this equates to zero growth relative to the previous season, it nonetheless reflects high milk production relative to historic levels. It is forecast to remain at these relatively high levels as a result of an increase in cow numbers which offsets an expected decrease in milk yield per cow relative to 2011/12.

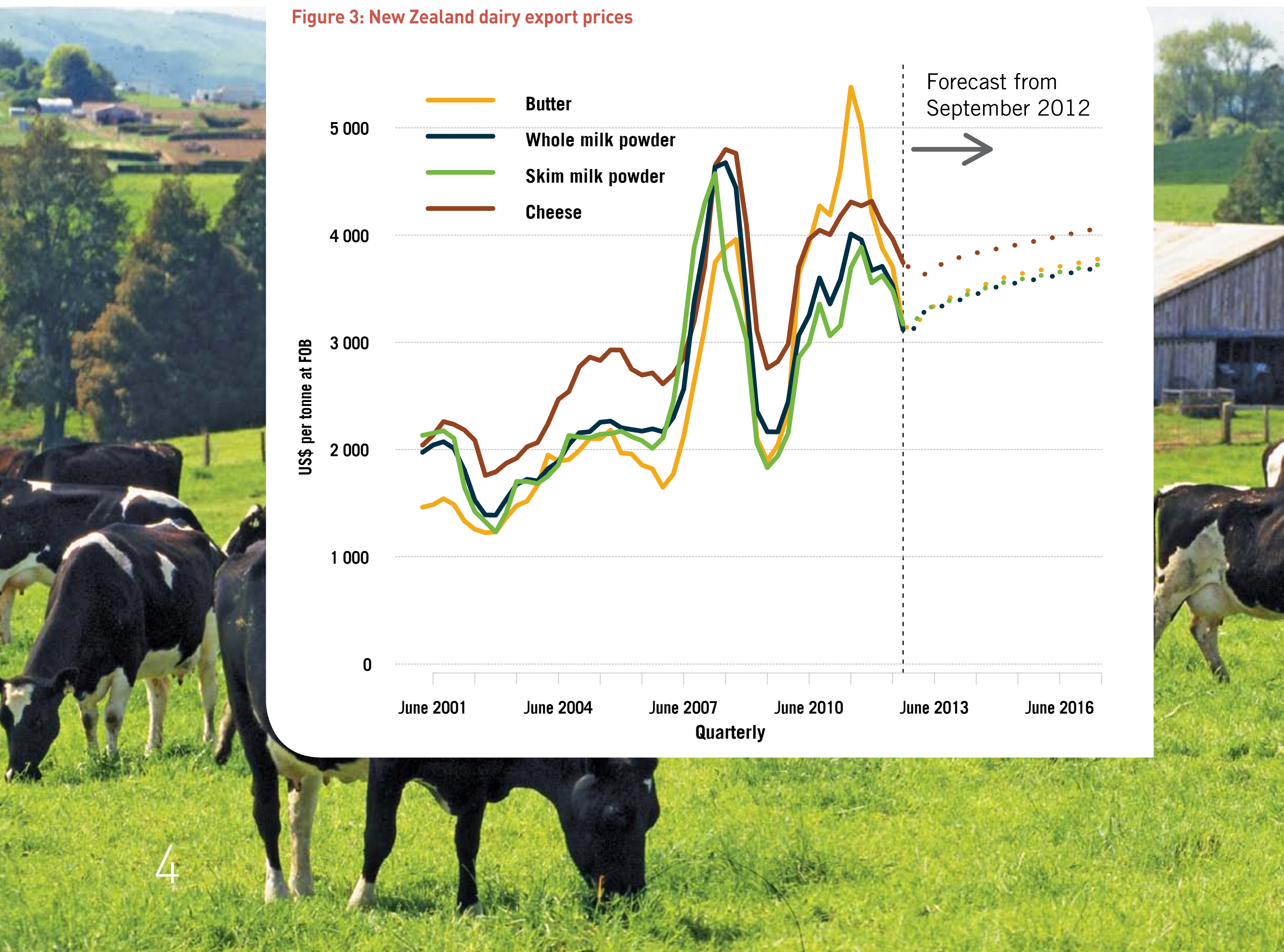
EXPORTS

New Zealand's dairy export revenue is expected to fall by 8.1 percent to $12.6 billion in the year to 30 June 2013 (compared with the previous year); this is slightly below the June forecast.

PRICES

International dairy prices have recovered 24 percent from their recent low in May 2012. This rapid recovery was due to market expectations of a reduction in milk supply from the EU and US. A slow-down in the growth of international milk production is expected to support the continued recovery of international dairy prices in the 2012/13 dairy season and beyond (refer to Figure 3).

Figure 3: New Zealand dairy export prices



In particular, international milk production is forecast to expand at a much slower rate in 2012/13 than in the previous year. High feed costs caused by the US drought have already had a negative impact on milk production in the US, where production fell 0.5 percent in September 2012 compared to the same month in 2011. High feed costs also impacted on milk production in the EU, where production was down 2.5 percent in July 2012 relative to July 2011.

However, economic uncertainty in the developed world and weaker demand growth from emerging markets are likely to constrain future increases in international dairy prices. Demand growth for dairy products slowed during 2011/12 and a rebound is unlikely to happen in 2012/13 due to the subdued global economic outlook.

The domestic farm gate milk price for year ending 31 May 2013 is expected to average $5.54 per kilogram of milksolids, down 42 cents on last season's price, due to the stronger NZD eroding the expected gain in international prices.

MEAT AND WOOL

Meat and wool export revenue is forecast at $6.05 billion in the year to 30 June 2013, 7.7 percent less than forecast in June 2012. This is mainly due to lower prices for lamb and wool.

BEEF

Beef export revenue in the year ending 30 June 2013 is expected to increase marginally, to $2.03 billion, due to a slight increase in both export prices and volumes.

US droughts are keeping beef prices reasonably strong. US cattle numbers at July 2012 were the lowest since 1972 as a consequence of drought conditions in 2011. A more severe drought started in June 2012, but subdued US consumer demand and increased imports (particularly from Australia) meant that a significant price increase was not fully borne out in New Zealand export beef prices.

It will be a year before rebuilding of the US cattle herd can resume and, as a consequence, beef prices are expected to remain firm over the next two years.

After favourable pasture conditions in New Zealand since autumn 2011 and increased beef schedule prices over the previous two years, beef cattle numbers are estimated to increase slightly to 3.87 million as at 30 June 2012. Over the next two years, normal climatic conditions and increased demand for dairy land use are expected to cause beef cattle numbers to fall.

LAMB

New Zealand lamb export revenue is expected to decrease 17 percent to $1.91 billion in the year ending 30 June 2013. This is mainly due to lower export prices compared with the previous year.

Weakening demand in the EU saw lamb export prices in the September 2012 quarter fall 27 percent from their peak in the December 2011quarter. This resulted in a build-up of frozen lamb cuts in New Zealand and overseas, which is now starting to clear with lower in-market prices.

China became New Zealand's largest market for frozen lamb cuts during the six months to 30 June 2012 (accounting for 33,200 tonnes, or 31 percent of export volume). A high proportion of these were lower value cuts; the average price of lamb sold to China is about half that obtained in the EU.

Increased lamb exports from Australia and weak economic conditions in global lamb markets are expected to keep prices subdued over the next two years.

Favourable climatic conditions since autumn mating contributed to an estimated 1.6 million more lambs born in late winter to early spring 2012, compared with last year. Total sheep numbers are estimated to be up 1.7 percent to 31.7 million as at June 2012.

WOOL

Wool export revenue is expected to decrease 23 percent to $580 million in the year ending June 2013, due to lower export prices.

Weaker demand for finished wool products in developed countries saw wool export prices in the September 2012 quarter decline 41 percent from their peak in the December 2011 quarter, when prices were high due to limited global supply.

Most of New Zealand's wool exports are now being sent to China for scouring, manufacturing and/or for sale to end consumers in its domestic market. The proportion of New Zealand wool exports going to China has increased from 33 percent to 53 percent over the last five years. Prices are expected to remain static over the next two years due to weaker growth in China and the EU.

FORESTRY

The value of forest product exports[2] for the year to June 2013 is forecast to fall slightly to $4.1 billion, from $4.4 billion forecast in June. This is due to a combination of lower prices for major products and a stronger NZD. Export volumes are forecast to remain stable.

Over the short-to-medium term, tree harvesting may increase slightly. The longer-term outlook for wood availability is a potential increase of 40 percent (equal to an additional 10 million cubic metres) late this decade. This increase is due to the afforestation that took place during the 1990s. Further analysis is required to better understand the economics of harvesting and utilisation of this new forest resource.

LOGS

The total value of log exports is expected to fall slightly in the year to June 2013, to $1.4 billion. Export volumes are expected to remain stable, but prices are forecast to be slightly lower due to lower international log prices and short-term strengthening of the NZD.

A combination of historically low shipping costs and reduced imports from alternative suppliers, has allowed New Zealand to continue growing its market share in China over recent years – refer to Figure 4 below. New Zealand's exports to China increased in the year to September 2012 despite total coniferous log imports to China declining eight percent. Prices for New Zealand logs in China are sufficiently lower than competitors' logs to sustain their appeal to Chinese buyers.

These conditions are expected to continue into 2013, providing a ready alternative for logs that cannot be absorbed by domestic wood processors.

2 This excludes the value of newsprint exports which are suppressed by Statistics New Zealand in the breakdown of trade data available to MPI due to confidentiality.

SAWN TIMBER

Forecast sawn timber exports for the year to June 2013 have declined to $763 million since June (from $817 million). Export volumes to the US and Australia have decreased due to weak housing markets, but this has been offset by larger than expected volumes of timber going to Asia. However, Asian markets yield lower prices than Australia and the US.

Sustained growth in US home building has been recorded through 2012. But activity remains at less than 40 percent of the levels experienced prior to the global financial crisis. Further sustained growth in activity in this market will gradually divert global supply back into the US.

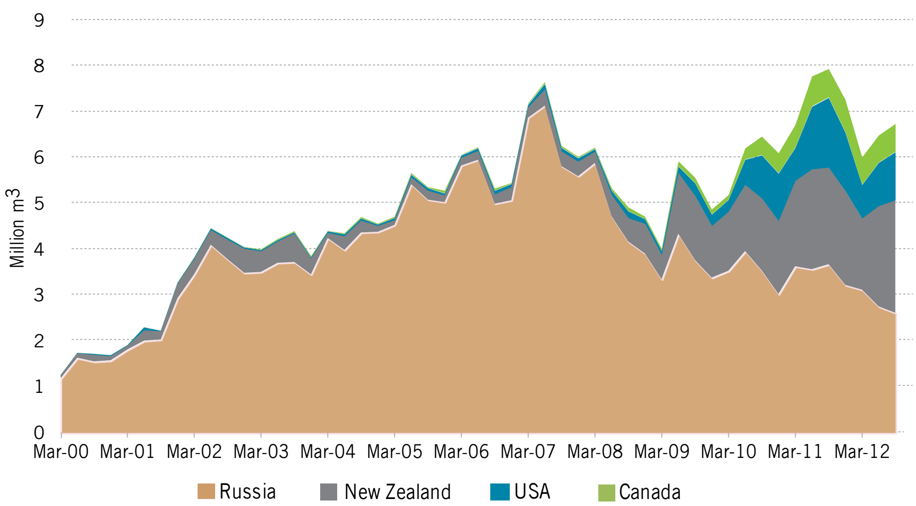
PANELS

Forecast export returns for panel products have increased to $505 million in 2012/13, from $462 million in June. Global panel prices have been relatively high since the Japanese earthquake and tsunami in March 2011. However weaker construction activity in Australia is now having a negative impact on returns for exporters of plywood to this market.

PULP, PAPER AND WOODCHIPS

Forecast returns from pulp, paper and woodchips have decreased from the June 2012 forecasts. International prices are currently depressed due to an accumulation of wood fibre globally, as paper manufacturers seek to consolidate operations in key markets. With the announced rationalisation of Norske Skog's newsprint manufacturing in Australasia, the company is due to close one of its two newsprint lines at its Kawerau mill in the first quarter of 2013. This is expected to reduce annual pulp and paper exports by around $100 million from next year.

Figure 4: Coniferous log imports to China (top four suppliers)



HORTICULTURE

Export revenue from all horticultural products is on track to reach $3.5 billion in the year to March 2013, with higher in-market prices expected to offset lower kiwifruit and wine exports and the stronger NZD.

WINE

Forecast export volume in the year ending June 2013 remains at 155 million litres. This represents a 13 percent drop on the previous year, due to the smaller grape harvest in 2012. The decreased export volume is forecast to raise the average price per litre by 15 percent to $7.60, resulting in export revenue of $1.18 billion, similar to that achieved in the year to June 2012.

Wine exports in the year ending June 2014 are forecast to be slightly higher than the June 2012 forecast, reaching 180 million litres and an average $7.80 per litre, with export revenue of $1.4 billion. The 2013 vintage is expected to bounce back, due to more benign climatic conditions. Efforts to develop markets in the US, China and Northern Europe since the supply demand imbalance of 2008, should result in increased sales of premium bottled wine, and the proportion of bulk wine dropping to less than 30 percent.

APPLES AND PEARS

Apple and pear export revenue is expected to reach $386 million for the year to 31 December 2012, 3.8 percent higher than the June 2012 forecast. This is due to small increases in both export volumes and prices as a result of higher-than-forecast demand in international markets.

Despite some hail and late frosts in spring 2012, apple and pear exports are still expected to reach the forecast 16.5 million cartons in the year ending December 2013. Export production is expected to stabilise in the short-term, with new plantings replacing tree pulls and recent plantings reaching maturity.

Demand for New Zealand fruit in international markets is expected to be strong during 2013, due to below-average apple crops in Western Europe, Canada and parts of the US. This should result in a lift in market prices buffering the high value of the NZD. Export prices are expected to improve beyond 2013 from further expansion of markets outside of Europe and changes in the variety mix.

FRESH AND PROCESSED VEGETABLES

Total fresh and processed vegetable export revenue is estimated at $545 million for the year to 31 December 2012, down from $560 million forecast in June 2012.

Export volumes of fresh vegetables for the year to 31 December 2012 will be higher than forecast in June 2012, due to generally good growing conditions increasing onion and squash yields.

Exports of processed vegetables in the year to 31 December 2012 are expected to fall by 5 percent compared with the previous year, despite expanded processing capacity in the Hawke's Bay. Contributing factors include land use competition in the main growing regions and the high NZD reducing competitiveness in international markets. Accordingly, forecast export volumes for 2013 and beyond have been revised downwards.

KIWIFRUIT

Kiwifruit export revenue is expected to reach $1.0 billion for the year to 31 March 2013, 14 percent higher than the $880 million forecast in June 2012, due to higher-than-expected export volumes and prices for gold kiwifruit.

Impact of Psa

The bacterial vine-killing disease Psa (*Pseudomonas syringae* pv. *actinidiae*), confirmed in New Zealand in November 2010, has devastated many kiwifruit orchards. The Te Puke District in the Bay of Plenty remains the hardest hit. Despite measures to slow its spread, over the past 12 months Psa has spread throughout the Bay of Plenty and to the Waikato, the Coromandel, Auckland, Northland, Hawke's Bay and Poverty Bay. The only kiwifruit growing region without Psa confirmed is Nelson.

As of 28 November 2012, 68 percent of kiwifruit orchards are known to have the bacterium present, up from 26 percent a year ago.

A lower export kiwifruit crop is expected in the year to 31 March 2014, due to the ongoing impacts of Psa. Gold kiwifruit exports are forecast to fall significantly to between 10 and 16 million trays in 2013/14, depending on how many of the remaining Hort16A gold kiwifruit orchards will successfully harvest a crop.

Existing gold kiwifruit growers have purchased over 1700 hectares of the new Gold3 more Psa-tolerant cultivar license. This will transition the equivalent of two-thirds of the orchard area of the Hort16A cultivar. The majority was grafted in winter 2012. Some growers have used the notch grafting technique to establish the Gold3 cultivar on the existing rootstock in an attempt to grow another crop of Hort16A in 2013 before they cut it out.

Green kiwifruit exports are expected to range from 70 to 80 million trays in the year to 31 March 2014. Psa has started to impact some green orchards, particularly male cultivars and orchards in frost prone and wet areas. While there is some concern about pollination, there is optimism that there is enough pollen available for the 2013 crop (at least), to compensate for the death of male vines. Flower numbers on green orchards are reported to be above average.

Overall, export volumes for the year ending 31 March 2014 are expected to fall 3 to 18 percent compared with the previous year, to between 81 and 96 million trays. Export returns are expected to fall 12 to 28 percent, to between $724 and $887 million – refer to Table 1.

The Minister for Primary Industries declared Psa a medium-scale biosecurity event on 5 December and announced a package of support measures to assist North Island kiwifruit growers to recover from the incursion.

Table 1: Kiwifruit export volumes, prices and values 2011 to 2014

		2011	2012	2013	2014	
Year to 31 March					Upper-bound	Lower-bound
Export volume	Green	78	83	75	80	70
(million trays[1])	Gold	21	27	24	16	10
	Total[3]	**100**	**111**	**99**	**96**	**81**
FOB[2] price ($/tray)	Green	7.9	7.7	8.0	7.5	7.6
	Gold	15.3	14.2	16.9	17.6	18.4
	Total[3]	**9.5**	**9.3**	**10.1**	**9.2**	**9.0**
Export value	Green	622	639	600	601	535
($ million)	Gold	315	389	401	282	184
	Total[3]	**944**	**1034**	**1007**	**887**	**724**

Notes

1. One tray equals 3.6kg.
2. Free on board is the value of the goods delivered to the port of export and loaded onto a vessel for transportation out of the country of origin.
3. Totals include other kiwifruit varieties.

SOURCE: Statistics New Zealand and MPI.

SEAFOOD

Seafood exports declined slightly in the year to 30 June 2012, to $1.54 billion, due to a 6.5 percent fall in volume, coupled with a 5.7 percent rise in price.

New Zealand's largest seafood export market, China, continued to grow in terms of volume and value. This was more than offset by lower export earnings from most other markets, notably the US and Europe.

The economic downturn in the EU is likely to have contributed to reduced demand for New Zealand seafood. Uncertainty around market access requirements associated with the EU's Illegal, Unreported and Unregulated (IUU) fisheries regulations may also have had an adverse impact on export volumes. The high exchange rate has continued to depress export returns to New Zealand producers; they have responded by holding catch and reducing export volumes.

A further decline in export earnings in 2012/13 is expected, due to the strong NZD and static international prices. Short-term prospects are further exacerbated by significant groundfish stock recovery in the Northern Hemisphere, leading to increased supply in international markets.

WILD CAPTURE

Wild capture fisheries' export volumes declined 6.6 percent to 250 000 tonnes in 2011/12, while value decreased by 0.8 percent to $1.25 billion.

Export earnings from hoki increased by 31 percent in the year to June 2012. An increase in hoki export volumes as a result of the recent increases in the Total Allowable Commercial Catch (TACC) was forecast. However, total wild capture exports were lower than forecast, due to significant declines in the volumes and prices received for other species, particularly orange roughy and squid.

AQUACULTURE

Aquaculture export volumes declined by 5.9 percent to 42 400 tonnes in the year to 30 June 2012, while earnings decreased by 2.8 percent to $292.3 million.

The fall in aquaculture export earnings was most pronounced in salmon. A significant increase in Atlantic salmon production – as a result of the recovery of the Chilean salmon farming sector – caused downward pressure on international prices. Opportunities for New Zealand salmon exporters arising out of supply chain disruption caused by the 2011 Icelandic volcanic eruption have also dissipated.

Our top aquaculture earner, greenshell™ mussels, experienced a slight increase in value and decrease in volume. Oyster export volumes decreased significantly as a result of juvenile oyster mortality caused by the Ostreid Herpes Virus. Reduced production has been partially offset by significantly increasing prices, as global supply remains low.

Table 2: Key statistics and forecasts

Year to 30 June		2010	2011	2012	2013	2014
Opening livestock numbers[1]						
Dairy cows and heifers in calf	Mil hd	4.61	4.68	4.82	4.97	5.10
Ewe and ewe hoggets mated	Mil hd	24.0	23.9	22.5	22.8	22.0
Total beef cattle	**Mil hd**	**4.10**	**3.95**	**3.85**	**3.86**	**3.80**
Prices						
Milk price[2]	c/kg MS	610	760	596	554	602
Lamb schedule[3]	c/kg cw	467	623	637	488	495
Prime beef schedule[4]	c/kg cw	335	408	406	405	400
Production volumes						
Milk solids	000 tonnes	1 437	1 513	1 685	1 685	1 751
Lamb	000 tonnes	379	344	364	368	364
Beef and veal	000 tonnes	638	618	607	610	616
Wool	000 tonnes	138	131	122	128	126
Export values						
Dairy	$ bil	10.6	13.2	13.7	12.6	13.7
Meat, pelts and wool	$ bil	6.13	6.77	6.61	6.05	5.97
Seafood	$ bil	1.40	1.56	1.54	1.52	1.56
Selected horticulture[5]	$ bil	2.98	2.99	3.11	3.15	3.10
Forestry	$ bil	3.86	4.52	4.27	4.15	4.25

Notes

1. Opening refers to 30 June of the preceding year.
2. Year to 31 May. The milk price excludes distributable profit.
3. All grades average cents per kg of carcass weight.
4. P2 steer and beef cents per kg of carcass weight.
5. Year to 31 March for wine; kiwifruit; apples and pears; fresh, dried and frozen vegetables; vegetable preparations.

SOURCES: Statistics New Zealand, Beef + Lamb New Zealand Economic Service, Seafood Industry Council and MPI.

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