RESEARCH
ECONOMY WATCH

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Macroeconomic Risks From NZ Cattle Disease

- **Government, industry, plan to eradicate Mycoplasma bovis**
- **152,000 cows to be culled; circa 1.5% of NZ total**
- **Production will be affected**
- **Likely higher costs, loss of efficiency, elevated uncertainty, add to downside risks**
- **RBNZ to assess this risk in Wednesday's FSR?**

The economic risks associated with cow-disease Mycoplasma bovis are rising. Over recent months more farms have come under scrutiny. The disease was first detected in NZ in July last year, with further subsequent findings.

Mycoplasma bovis presents no human food safety risks and is prevalent in many countries. For infected cows, it can cause untreatable mastitis, severe pneumonia, ear infections, abortions, and swollen joints and lameness.

Today, the Government, in consultation with industry, announced plans to try and eradicate the disease over time. The plan estimates 126,000 cattle will be culled. This is in addition to the 26,000 cull already in progress. This would take the total cattle to be culled to 152,000. The Government estimates that 192 properties will be depopulated.

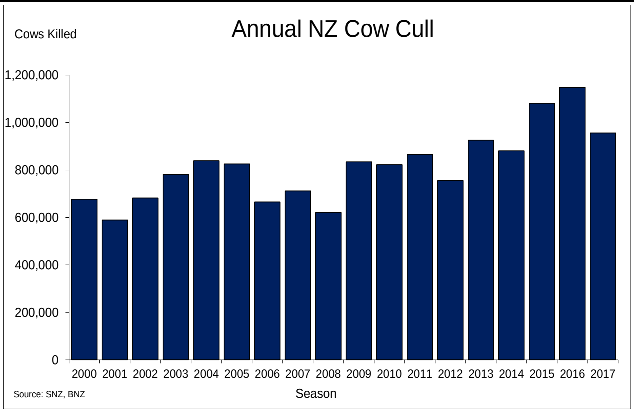
The planned 152,000 cow cull represents a significant step up from the 26,000 cull already underway and the 60,000 cows previously under scrutiny, although it is still a relatively small 1.5% share of NZ's total beef (3.6m) and dairy (6.5m) cattle. It will have a direct impact on production.

The planned 152,000 cow cull is a bigger share of the usual annual average cow cull of around 1m. So some upward pressure on the meat production profile can be expected ahead, but the actual cull will also be heavily influenced by the weather and pricing through the season. So, from a production point of view, there is potential for more meat at least initially, but less milk.

There is much more to it than the initial impact on production from culling cows.

Costs are increasing. Farmer confidence is low (watch for the latest reading in Thursday's business survey). Elevated uncertainty and risk threaten to curb investment.

Facing Some Upward Pressure



Moreover, restricted cattle movement, either as a result of enforcement by authorities or by choice, would reduce efficiency across the dairy and beef sectors. Restricted movement of stock threatens to alter current farm practices that may see a reduction in stocking rates, on net, across the industry. This is something to watch for as it would negatively affect future production over and above any cow culling. Animal welfare and grazing costs are likely to lift. All up, productivity will be lower than it would be absent the disease. In the least, it all adds up to a lot of disruption and angst.

The Government estimates the full cost of eradication at $886m over 10 years, including farmer compensation, with the Government meeting 68% of this and industry bodies, DairyNZ and Beef and Lamb NZ, meeting the remainder. Most of the eradication work is expected to be done over the first two years. Government analysis saw the eradication option as superior to long term management (at a projected cost of $1.2b) or doing nothing (with an estimated cost of $1.3b in lost production over 10 years with ongoing productivity losses).

Farmers have been all too aware of the disease and the massive disruption it is causing to those with affected cows and flow on effects to others. It is causing considerable angst across the dairy and beef sectors. We have previously noted that the disease was one reason behind very low farmer confidence, despite generally strong primary product prices. It is a headwind to overall economic activity. However, the financial markets have been seemingly sanguine (and again today, with the NZD pushing marginally higher after today's announcement). We just wonder if the market is too sanguine given the risks circulating. We will certainly keep a close eye on this risk, including for any significant impacts it might have on our macroeconomic views.

Much uncertainty remains. Indeed, if, for example, it is found that the disease is more widespread than anticipated the plan to eradicate would be re-evaluated. Spring test results due in February will help inform that decision.

From an RBNZ perspective, it is interesting that Mycoplasma bovis and any associated economic risks stemming from it did not get any mention in the May Monetary Policy Statement. From this starting point, any inclusion of the risk by the RBNZ would be a downside development. In the least, it reinforces the idea that the RBNZ will not be hiking the OCR this year. We'll be interested to see if the RBNZ includes an assessment of this disease risk in its Financial Stability Report due Wednesday.

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