

1 December 2023

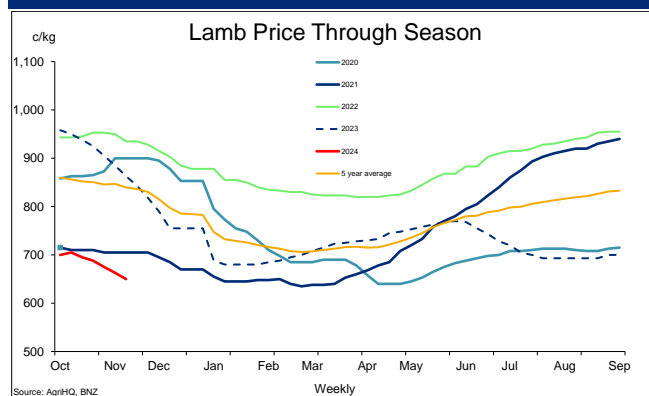
## Lamb Chop

- **Lamb prices under pressure**
- **As more Australian supply enters markets**
- **El Nino not helpful**
- **Neither are difficult global economic conditions**
- **Prices at risk of being lower for longer**

Lamb prices remain under downward pressure. Falling prices at this time of year isn't particularly unusual, but following a very uncharacteristic drop through winter it sees prices pushing further below average. Lower prices will put pressure on budgets across the sector.

Lamb prices through mid-November are tracking around 25% below year ago levels.

### Lamb Price Low



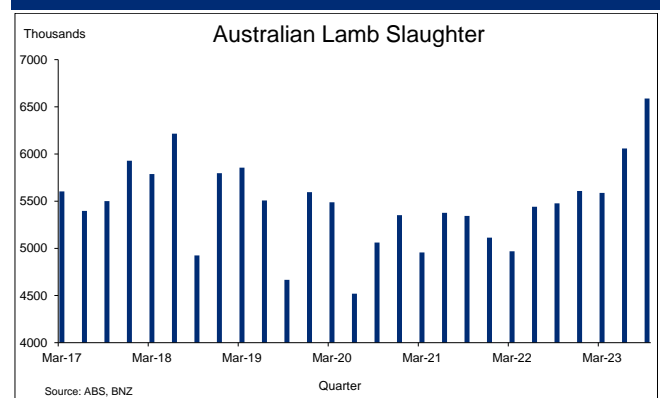
Multiple factors remain in play, including:

- A significant increase in Australian lamb supply
- Increased competition in the UK market following the AU-UK FTA
- Slower economic growth in key trading partners, including China

We have long talked about the headwind of a significant increase in Australian lamb supply. This follows an aggressive multi-year flock rebuilding during previous La Nina weather conditions. Estimates of Australian sheep numbers are at their highest level since 2007. This – and recent below average rainfall – has seen a substantial lift in both lamb and sheep product now coming to market. Australian lamb slaughter numbers were more than 20% higher in Q3 this year compared to last year. In addition, Australian adult sheep slaughter numbers were up nearly

35% over the same period. Hefty increases on any measure. Moreover, timely indicators suggest slaughter numbers over the ditch have continued to track well above year earlier levels through October and into November.

### More Australian Lamb

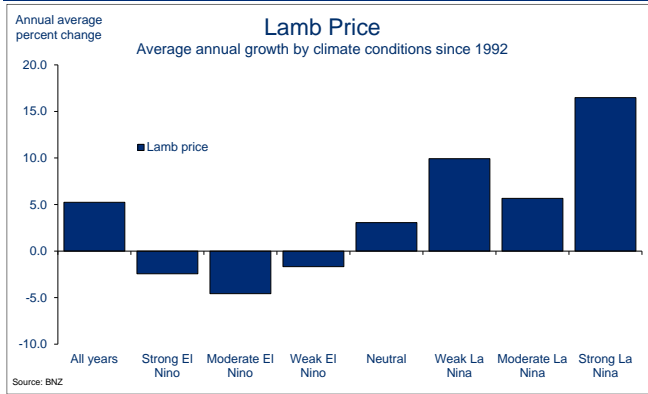


A substantial amount of this product has entered world markets. Australian lamb export volumes have been averaging around 18% higher than a year earlier, over recent months. Australian mutton export volumes have been even stronger, averaging around 50% above that of a year ago. The significant increase in Australian export volumes has increased competition across many markets. This includes in the UK, especially following the AU-UK FTA coming into force earlier this year.

More Australian product is expected ahead, especially with El Nino weather conditions seemingly locked and loaded for summer and into autumn according to weather agencies. Such conditions also risk more NZ lamb supply through the season than would otherwise be the case. We have previously discussed that NZ lamb prices have tended to be lower during El Nino weather patterns. This (El Nino) season is unfortunately shaping up in that direction. It all suggests headwinds to lamb prices will persist for some time.

Slower economic growth in key trading partners, including China, has not helped on the demand side. The value of NZ sheepmeat exports to China has declined. In the year to October, these exports are down 12% on year earlier levels, to be back to levels last seen in the (pre-covid) 2018/19 season. The most recent months have averaged around 28% lower than the equivalent year ago levels.

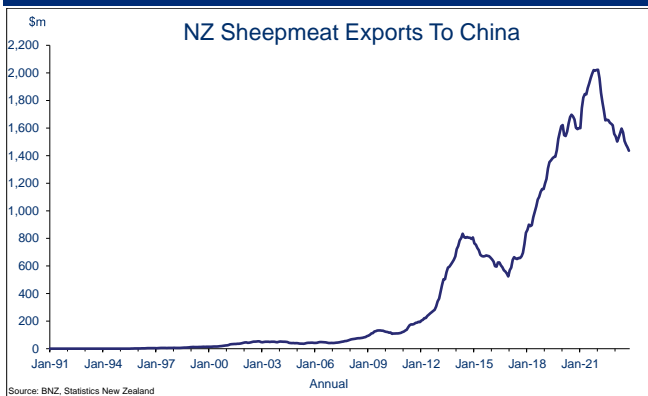
**Lamb Prices Typically Lower During El Nino**



Disentangling the influence of more competition on the supply side as distinct from genuine changes in overall market demand on export price and values is difficult. For instance, export lamb volumes, including to China, have been generally holding up.

In any case, any sign of better economic indicators out of China would be welcomed, especially those regards consumer demand. There have been some hints of improvement, such as the recent lift in retail sales growth. The evolution of lamb demand from China, as well as elsewhere, will play an important role in determining price levels ahead. Without a substantial lift in demand, the current supply dynamics present a material risk of lamb prices being lower, for longer, than some are forecasting.

**Markedly Lower**



Of course, lower prices themselves tends to encourage more buying. While that channel will not be the catalyst for a turnaround in prices in the first instance, to the extent that lower prices introduce or reintroduce new customers to lamb products it can alter preferences that can have price benefits in the longer term. Let’s hope so, such that something good can come out of the current weakness.

We remain cautious on the outlook for lamb prices. There looks to be an increasing risk that prices dip below the \$6/kg mark at some point during this season, even if prices can manage to average a bit above that mark for the season overall.

Our current season forecast sees average lamb prices around 18% lower than the previous season (which itself was down 15% on the season before that). It would see lamb prices average at their lowest level since 2017. That is on a dollar basis. But farmers will know more than anyone that the lamb price declines have been occurring in the face of stiff cost escalating over recent seasons. On an inflation adjusted basis, the 2024 lamb price average is shaping up to be the lowest since 2008.

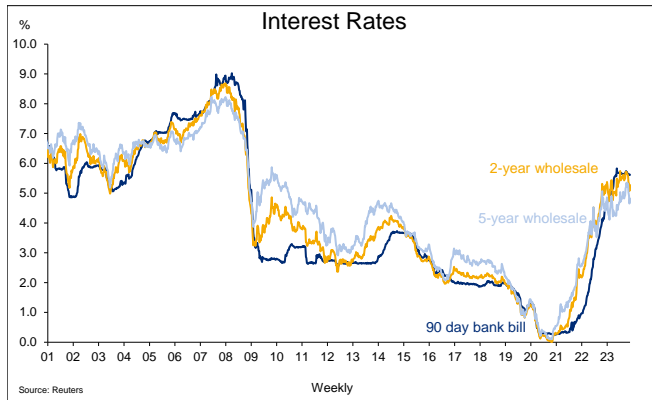
Like we noted in the previous *Rural Wrap*, ‘even if prices stabilise offshore from here, we expect lamb prices this season to average below the season just ended and be well below average on an inflation-adjusted basis.’ It represents a tough period ahead for lamb producers first and foremost. But with accompanying influence on associated industries as the lack of export earnings makes its presence felt through supply chains, regional areas, and the national economy at large.

It is worth noting that above normal supply stemming from identified weather patterns will eventually end, as has been the case in previous cycles. If it is a cycle we are in, and a lot of it looks that way, we can expect price improvement at some stage even if that looks some way off at this point.

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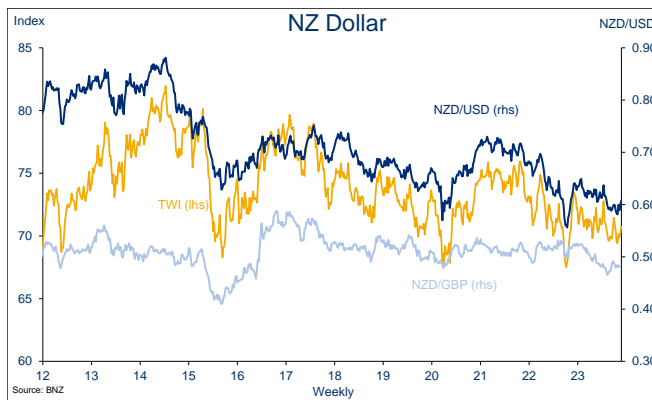
# Key Macro Drivers for Commodity Producers

## Interest Rates



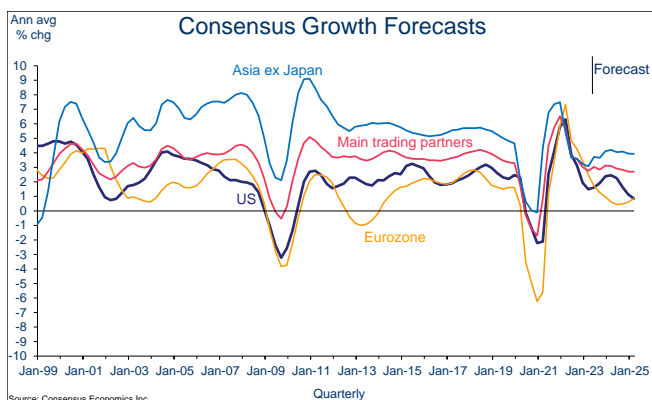
The Reserve Bank held the Official Cash Rate at 5.50% at its late-November meeting, as expected. But the accompanying statement and forecasts were outrightly hawkish – with the RBNZ upping the chance of another hike and suggesting the OCR will stay high for quite some time. If the RBNZ means what it says, and we have no reason to doubt this, then we also must accept the chance of a further rate hike is very real. Inflation is still forecast to fall, but the RBNZ has suggested it has little tolerance for upside inflationary surprises. Meanwhile, the market continues to price rate cuts next year. We can't help but feel one of the reasons the RBNZ adopted a hawkish stance is that it was concerned financial markets were pricing in three rate cuts for 2024. Our forecasts show the OCR being on hold until into the second half of 2024, before some easing starts.

## Foreign Exchange



It increasingly looks like the Fed tightening cycle is over. We have long seen this as a key precondition for a softening in the US dollar, which now seems underway. A weaker US dollar projection is critical to our forecasts for a higher NZD in 2024, with an expected move into the mid-60s. That said, a soft global economic growth backdrop isn't naturally the sort of time that the NZD outperforms and, indeed, our NZD cross rate forecasts are flat to weaker. A lot can still throw a weaker US dollar view of course. It assumes that the US economic downturn isn't hard enough to trigger a major global risk-off event that would be detrimental to the NZD. It also assumes pessimism around China's outlook is effectively already in the price. We see more influence on FX markets from an expected Fed easing next year than from RBNZ/OCR projections.

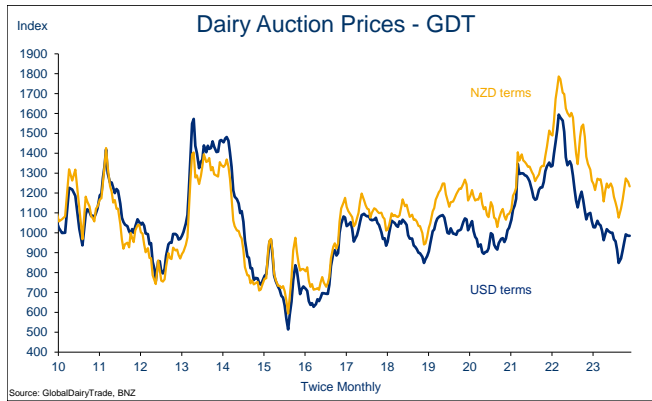
## Global Growth



Recent growth offshore has been mixed: declining in the EU, UK, and Japan, but strong in the US. Growth indicators for emerging markets have generally softened. Stimulus measures should ensure that China (at least) meets its growth target for the year, although focus remains on weakness in its property sector. Consensus forecasts for growth in New Zealand's major trading partner economies remain below average at 3.1% in 2023 and 2.7% for 2024. This remains a generally soft backdrop for primary product prices. A bit more hope comes from more signs that inflation in advanced economies has eased further, raising the chances that most major central banks are at the end of their tightening cycle (even if some upside risk remains). Markets have been focussing on possible Fed rate cuts next year, lifting risk sentiment and with it some chance of improvement in product prices from generally low levels.

# Key Commodities

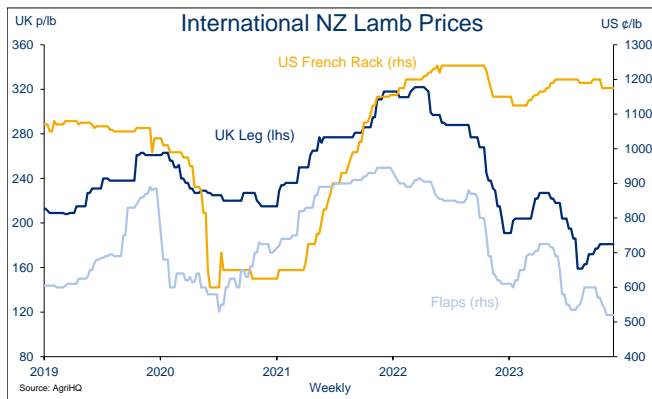
## Dairy



Global dairy prices have stalled after bouncing from their mid-August low. Prices are well above their low but still about 10% lower than a year ago. NZ milk production has been tracking above year earlier levels, perhaps stronger than some feared earlier in the season. Meanwhile, US milk production continues to trail year earlier levels. Our 2023/24 milk price forecast remains at \$7.25. A lift in global risk appetite and a lower US dollar of late suggests some upside risk to this, although an associated higher NZD would be a local price headwind (over time).

	Current	Month ago	Year ago	Next 12 months
Whole milk powder (US \$/t)	3070	3090	3400	↑

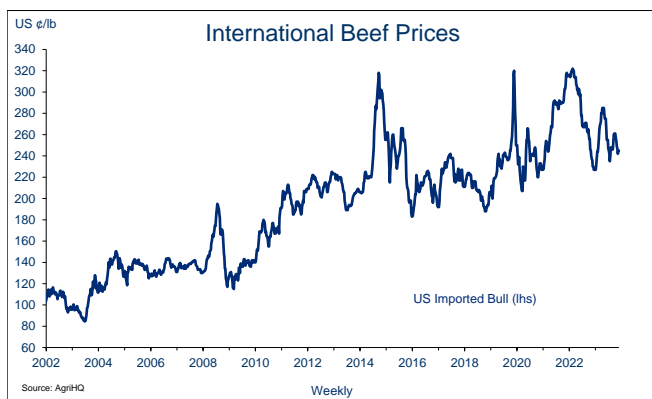
## Lamb



International lamb pricing remains weak. Very large volumes of Australian product, amplified by El Nino conditions, has lifted competition across many markets. Meanwhile, below average economic growth in several key markets is not helping on the demand side. Domestic lamb prices have been under material downward pressure. Even if prices stabilise offshore from here, we expect lamb prices this season to be well below average on an inflation-adjusted basis. Prices are at risk of being lower for longer as elevated global supply persists.

	Current	Month ago	Year ago	Next 12 months
Lamb leg (UK p/lb)	181	181	215	→

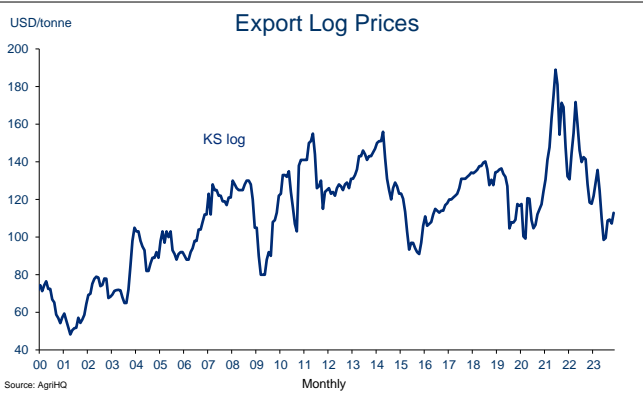
## Beef



US beef prices have eased over the past two months, as US supply has remained relatively elevated. Beef supply, more generally, is likely to remain a headwind for markets, including from South America and Australia (as El Nino driven production continues). Demand continues to be variable across markets. Economic conditions in Europe remain challenging, but there is expansion opportunity for NZ beef via free trade agreements. There are some hints of improvement in China, albeit from markedly lower export levels compared to a year ago. We expect the coming season's prices to average close to or a touch below the prior season's average.

	Current	Month ago	Year ago	Next 12 months
Imported bull (US ¢/lb)	245	249	230	→

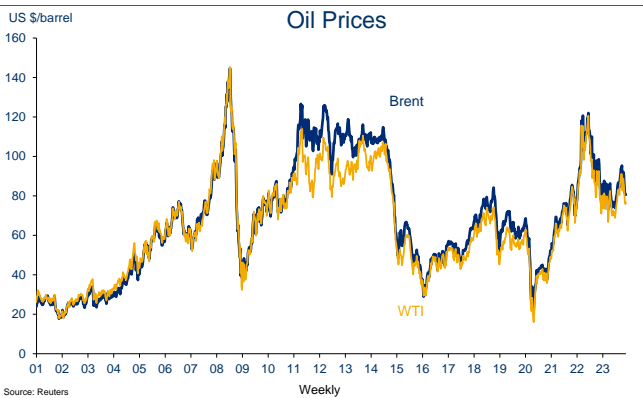
**Forestry**



There has been some further incremental improvement in export log prices into November, but they remain around 5% below year ago level and 13% under their 5-year average. Prices remain weak, even if off their recent low. AgriHQ reports buyers reacting to decreasing log inventories at Chinese ports. Weakness in China’s property market remains in focus, with more discussion of official support and stimulus helping sentiment. Domestic construction activity is forecast to decline in the near term, putting some downward pressure on domestic prices, although some support may filter through from offshore.

	Current	Month ago	Year ago	Next 12 months
S1/S2 log price (NZ \$/t)	126	126	132	➔

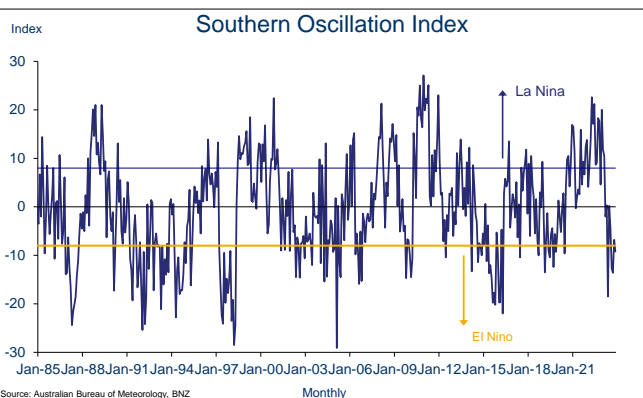
**Oil**



Oil prices always seem to be volatile and so they have been of late. From circulating around \$US75/bbl mid-year, Brent crude prices surged up toward \$US100/bbl during September before returning to around \$US80/bbl by late November. Some volatility has reflected uncertainty around the possible extension of OPEC+ oil production cuts, while weak global economy activity is likely curbing demand. The supply-demand balance has been weighing on prices, while early details from the late November OPEC+ meeting seemed to disappoint those looking for more decisive restraint on production.

	Current	Month ago	Year ago	Next 12 months
Brent Crude (US \$/b)	81	90	84	➔

**Weather**



Climate indicators remain in El Nino territory. And there is a very high chance El Nino will persist through summer and into autumn. NIWA recently noted that, from an oceanic perspective, this El Nino continues to rank with the most significant events in recent decades. But NIWA also observed that El Nino is displaying some unusual atmospheric tendencies (considering its oceanic strength). The Southern Oscillation Index hasn’t been decisively at El Nino levels as it has been in the past. Soil moisture deficits maps around the country for this time of year certainly look unusual given El Nino. It is another reminder that every El Nino is different. Yes, there are pockets of relatively dry conditions around, but there are also large areas of the opposite – including in the North and East – which is counter to what would typically be observed during El Nino conditions. But things can change quickly, and we remain alert to elevated dry risk this summer and autumn.

# Quarterly Forecasts

Forecasts as at 1 December 2023

## Key Economic Forecasts

Quarterly % change unless otherwise specified

	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24
GDP (production s.a.)	1.3	1.5	-0.5	0.0	0.9	0.0	-0.2	-0.4	0.2	0.6
Retail trade (real s.a.)	-2.0	-0.5	-0.8	-1.3	-0.9	0.0	-0.5	0.2	0.6	0.8
Current account (ytd, % GDP)	-7.9	-8.3	-8.8	-8.2	-7.5	-7.2	-6.7	-6.3	-6.3	-6.2
CPI (q/q)	1.7	2.2	1.4	1.2	1.1	1.8	0.5	0.6	0.6	1.3
Employment	-0.2	1.4	0.6	1.0	1.0	-0.2	0.3	-0.1	0.0	0.1
Unemployment rate %	3.3	3.2	3.4	3.4	3.6	3.9	4.3	4.5	5.0	5.4
Avg hourly earnings (ann %)	7.0	8.6	8.1	8.2	7.7	7.1	7.0	6.2	5.5	4.4
Trading partner GDP (ann %)	2.2	3.7	2.1	2.8	3.4	3.0	3.2	2.8	2.7	2.7
CPI (y/y)	7.3	7.2	7.2	6.7	6.0	5.6	4.7	4.0	3.5	3.0
GDP (production s.a., y/y)	0.7	6.6	2.4	2.2	1.8	0.3	0.6	0.3	-0.4	0.2

## Interest Rates

Historical data - qtr average

Forecast data - end quarter

	Cash	Government Stock			Swaps			US Rates		Spread
		90 Day	5 Year	10 Year	2 Year	5 Year	10 Year	Libor	US 10 yr	NZ-US
		Bank Bills						3 month		Ten year
2022 Jun	1.83	2.24	3.55	3.68	3.83	3.92	3.95	1.50	2.90	0.76
Sep	2.83	3.33	3.65	3.77	4.12	3.95	3.95	3.00	3.10	0.67
Dec	4.00	4.27	4.34	4.31	5.10	4.67	4.55	4.50	3.80	0.49
2023 Mar	4.58	4.99	4.27	4.26	5.11	4.51	4.40	4.90	3.65	0.61
Jun	5.42	5.62	4.23	4.27	5.19	4.44	4.30	5.40	3.60	0.68
Sep	5.50	5.66	4.87	4.87	5.54	4.90	4.75	5.65	4.15	0.73
Forecasts										
Dec	5.50	5.60	5.30	5.30	5.50	5.45	5.40	5.85	4.60	0.70
2024 Mar	5.50	5.60	5.00	5.05	5.20	5.20	5.20	5.85	4.40	0.65
Jun	5.50	5.50	4.70	4.80	4.85	4.90	4.95	5.60	4.20	0.60
Sep	5.25	5.00	4.45	4.60	4.45	4.70	4.80	5.35	4.00	0.60
Dec	4.75	4.75	4.10	4.30	4.00	4.35	4.50	4.85	3.75	0.55
2025 Mar	4.50	4.25	3.75	4.00	3.55	4.00	4.20	4.35	3.50	0.50
Jun	4.00	3.75	3.65	4.00	3.20	3.90	4.20	3.85	3.50	0.50
Sep	3.50	3.15	3.55	3.95	3.00	3.80	4.15	3.35	3.50	0.45

## Exchange Rates (End Period)

### USD Forecasts

	NZD/USD	AUD/USD	EUR/USD	GBP/USD	USD/JPY
Current	0.62	0.66	1.09	1.26	148
Dec-23	0.60	0.66	1.10	1.27	148
Mar-24	0.62	0.69	1.13	1.31	145
Jun-24	0.64	0.71	1.16	1.35	138
Sep-24	0.64	0.72	1.17	1.34	135
Dec-24	0.65	0.73	1.18	1.35	130
Mar-25	0.67	0.75	1.19	1.35	125
Jun-25	0.69	0.77	1.21	1.37	120
Sep-25	0.71	0.78	1.22	1.37	118
Dec-25	0.71	0.78	1.23	1.38	116
Mar-26	0.69	0.76	1.23	1.38	115

### NZD Forecasts

	NZD/USD	NZD/AUD	NZD/EUR	NZD/GBP	NZD/JPY	TWI-17
Current	0.62	0.93	0.57	0.49	91.3	71.6
Dec-23	0.60	0.91	0.55	0.47	88.8	69.8
Mar-24	0.62	0.90	0.55	0.47	89.9	71.0
Jun-24	0.64	0.90	0.55	0.47	88.3	72.1
Sep-24	0.64	0.89	0.55	0.48	86.4	71.3
Dec-24	0.65	0.89	0.55	0.48	84.5	71.3
Mar-25	0.67	0.89	0.56	0.50	83.8	72.5
Jun-25	0.69	0.90	0.57	0.50	82.8	73.8
Sep-25	0.71	0.91	0.58	0.52	83.8	75.4
Dec-25	0.71	0.91	0.58	0.51	82.4	75.2
Mar-26	0.69	0.91	0.56	0.50	79.4	73.6

### TWI Weights

13.8% 16.5% 9.8% 3.1% 6.1%

Source for all tables: Statistics NZ, Bloomberg, Reuters, RBNZ, BNZ

# Annual Forecasts

Forecasts as at 1 December 2023	March Years					December Years				
	Actuals		Forecasts			Actuals		Forecasts		
	2022	2023	2024	2025	2026	2021	2022	2023	2024	2025
<b>GDP - annual average % change</b>										
Private Consumption	6.0	2.7	1.2	0.5	2.5	7.4	3.2	1.4	0.0	2.3
Government Consumption	8.0	2.0	-0.3	-2.9	1.4	8.2	4.6	-0.7	-3.1	0.9
Total Investment	10.4	3.5	-0.1	-2.6	4.2	12.3	4.1	1.0	-3.5	3.1
Stocks - ppts cont'n to growth	0.5	-0.1	-1.1	1.0	0.0	1.4	-0.3	-1.3	1.1	0.1
GNE	8.0	2.6	-0.4	0.1	2.7	10.2	3.4	-0.2	-0.6	2.4
Exports	2.5	6.0	5.6	3.1	5.2	-2.7	-0.2	9.1	3.2	5.2
Imports	17.3	4.7	-1.0	0.3	3.8	14.8	4.7	0.7	-0.6	3.2
Real Expenditure GDP	4.8	2.9	1.2	0.8	3.0	6.1	2.3	1.5	0.5	2.8
<b>GDP (production)</b>	<b>5.2</b>	<b>2.9</b>	<b>0.8</b>	<b>0.8</b>	<b>3.0</b>	<b>6.0</b>	<b>2.7</b>	<b>1.2</b>	<b>0.3</b>	<b>2.8</b>
<i>GDP - annual % change (q/q)</i>	1.1	2.2	0.3	2.2	3.1	3.3	2.4	0.6	1.1	3.1
Output Gap (ann avg, % dev)	1.3	1.6	-0.5	-1.0	-0.1	1.4	1.8	0.1	-1.1	-0.3
Nominal Expenditure GDP - \$bn	358	388	412	425	449	353	381	408	420	443
<b>Prices and Employment - annual % change</b>										
CPI	6.9	6.7	4.0	2.8	2.1	5.9	7.2	4.7	2.9	2.1
Employment	2.5	2.9	1.0	0.9	2.4	3.3	1.7	2.1	0.3	2.3
Unemployment Rate %	3.2	3.4	4.5	5.8	5.7	3.2	3.4	4.3	5.7	5.8
Wages - ahote (private sector)	5.3	8.2	6.2	3.9	3.0	4.1	8.1	7.0	4.3	3.0
Productivity (ann av %)	2.3	0.8	-1.2	0.4	0.9	3.9	0.5	-1.3	0.0	1.1
Unit Labour Costs (ann av %)	4.0	6.2	7.0	4.0	2.2	2.0	6.2	7.4	4.9	2.3
House Prices	13.8	-12.1	2.6	8.6	10.9	27.2	-11.1	-1.6	6.7	12.5
<b>External Balance</b>										
Current Account - \$bn	-23.6	-31.8	-26.2	-23.3	-16.1	-20.6	-33.4	-27.1	-24.8	-18.1
Current Account - % of GDP	-6.6	-8.2	-6.3	-5.5	-3.6	-5.8	-8.8	-6.7	-5.9	-4.1
<b>Government Accounts - June Yr, % of GDP</b>										
OBEGAL (core operating balance)	-2.7	-2.4	-2.8	-1.7	-0.8					
Net Core Crown Debt (excl NZS Fund Assets)	17.0	18.0	22.4	23.2	23.3					
Bond Programme - \$bn (Treasury forecasts)	20.0	28.0	36.0	35.0	30.0					
Bond Programme - % of GDP	5.6	7.2	8.7	8.2	6.7					
<b>Financial Variables <sup>(1)</sup></b>										
NZD/USD	0.69	0.62	0.62	0.67	0.69	0.68	0.63	0.60	0.65	0.71
USD/JPY	119	134	145	125	115	114	135	148	130	116
EUR/USD	1.10	1.07	1.13	1.19	1.23	1.13	1.06	1.10	1.18	1.23
NZD/AUD	0.93	0.93	0.90	0.89	0.91	0.95	0.94	0.91	0.89	0.91
NZD/GBP	0.52	0.51	0.47	0.50	0.50	0.51	0.52	0.47	0.48	0.51
NZD/EUR	0.62	0.58	0.55	0.56	0.56	0.60	0.60	0.55	0.55	0.58
NZD/YEN	81.5	83.0	89.9	83.8	79.4	77.4	85.6	88.8	84.5	82.4
TWI	73.9	71.0	71.0	72.5	73.6	73.0	72.9	69.8	71.3	75.2
Overnight Cash Rate (end qtr)	1.00	4.75	5.50	4.50	2.75	0.75	4.25	5.50	4.75	2.75
90-day Bank Bill Rate	1.45	5.16	5.60	4.25	2.90	0.92	4.55	5.60	4.75	2.90
5-year Govt Bond	2.90	4.40	5.00	3.75	3.50	2.20	4.30	5.30	4.10	3.50
10-year Govt Bond	3.20	4.35	5.05	4.00	3.90	2.35	4.25	5.30	4.30	3.90
2-year Swap	3.00	5.15	5.20	3.55	3.00	2.22	5.21	5.50	4.00	3.00
5-year Swap	3.20	4.50	5.20	4.00	3.75	2.56	4.62	5.45	4.35	3.75
US 10-year Bonds	2.10	3.65	4.40	3.50	3.50	1.45	3.60	4.60	3.75	3.50
NZ-US 10-year Spread	1.10	0.70	0.65	0.50	0.40	0.90	0.65	0.70	0.55	0.40

<sup>(1)</sup> Average for the last month in the quarter

Source: Statistics NZ, BNZ, NZ Treasury

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