episode3

COMMODITY UPDATE

QUARTER 1 - 2024

CATTLE

The Australian Bureau of Statistics (ABS) have released their livestock slaughter and meat production volumes for the third quarter of 2023 and with this updated information we can measure the female slaughter ratio (FSR) for cattle to see how the Australian cattle herd cycle is faring in terms of herd liquidation or rebuild. Historically an annual FSR above 47% implies that we are liquidating the herd and an FSR under 47% is the herd in rebuild mode. The quarterly measure of FSR came in at 49% for September (Q3 2023), up from the June quarter's 48% calculation. This brings the annual average FSR to 46.7% for 2023, just 0.3% away from signalling a herd liquidation phase has begun.

A comparison of the annual herd change to the FSR shows that Meat & Livestock Australia (MLA) has been forecasting a 4% increase to the herd over 2023. However, historically an annual average FSR nearer to 47% would be more consistent with only marginal herd growth (circa 1%, or less). As the year progresses if the FSR continues to trend higher we may see MLA shave off some of the growth projections on the herd for the 2023 season.

The Beef Processor Profitability Index (BPPI) for 2023 averages at 0.64, below the 2014 peak of 0.82 but above the long-term average of 0.14 from 2000 to 2023. The last decade has been challenging for beef processors with an average BPPI of just 0.04, and even a negative average of -0.05 since 2018, indicating that the current season offers a chance for processors to recover from recent losses. According to ABARES data, the profit balance has swung towards processors in 2023, with the expectation that beef farm profitability will decline from its 2022 peak, continuing the historical trend where farm profitability and processor profitability are inversely related, reflecting the cyclical nature of boom and bust in the beef industry, with farmers and processors experiencing opposite ends of the price cycle.

The BPPI serves as an indicator of the Australian beef processing sector's trading environment, with a negative BPPI pointing to tougher conditions and a positive BPPI indicating a more favourable situation. However, it does not accurately reflect the financial status of individual processors. Recent increases in labour costs, including the application of the Pacific Australia Labour Mobility (PALM) scheme and higher general labour costs due to limited workforce and increased overtime, are not accounted for in the current BPPI model. Furthermore, the rise in the Temporary Skilled Migration Income Threshold (TSMIT) in July 2023 has inflated wage costs, suggesting that recent profitability levels indicated by the BPPI may be somewhat elevated.

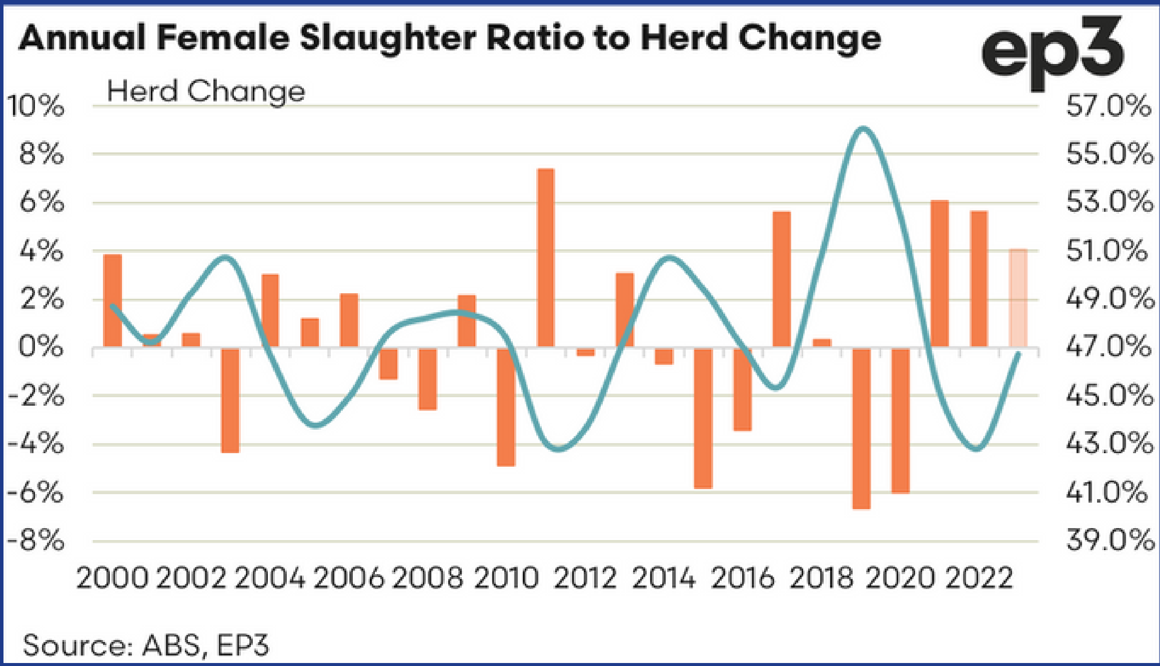


FIGURE 1.

The annual female cattle slaughter ratio (FSR) for 2023 has nearly moved into herd liquidation territory

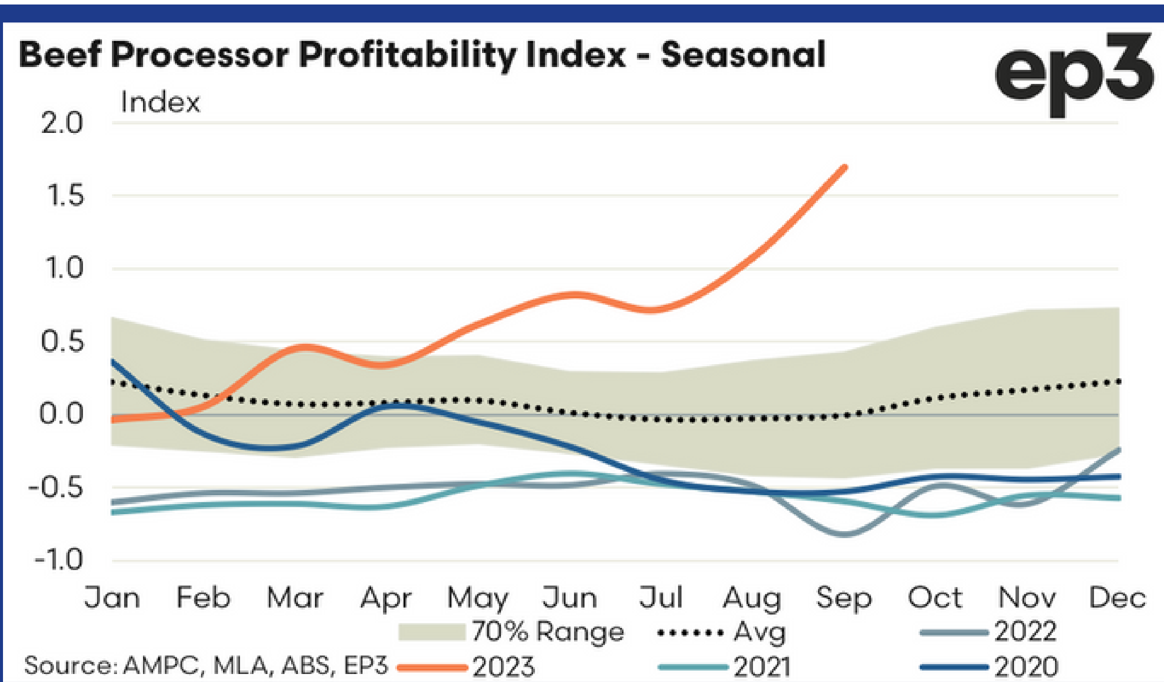


FIGURE 2.

The beef processor profitability index displayed steady improvement during the first three quarters of 2023 as falling cattle prices favoured the processor bottom line

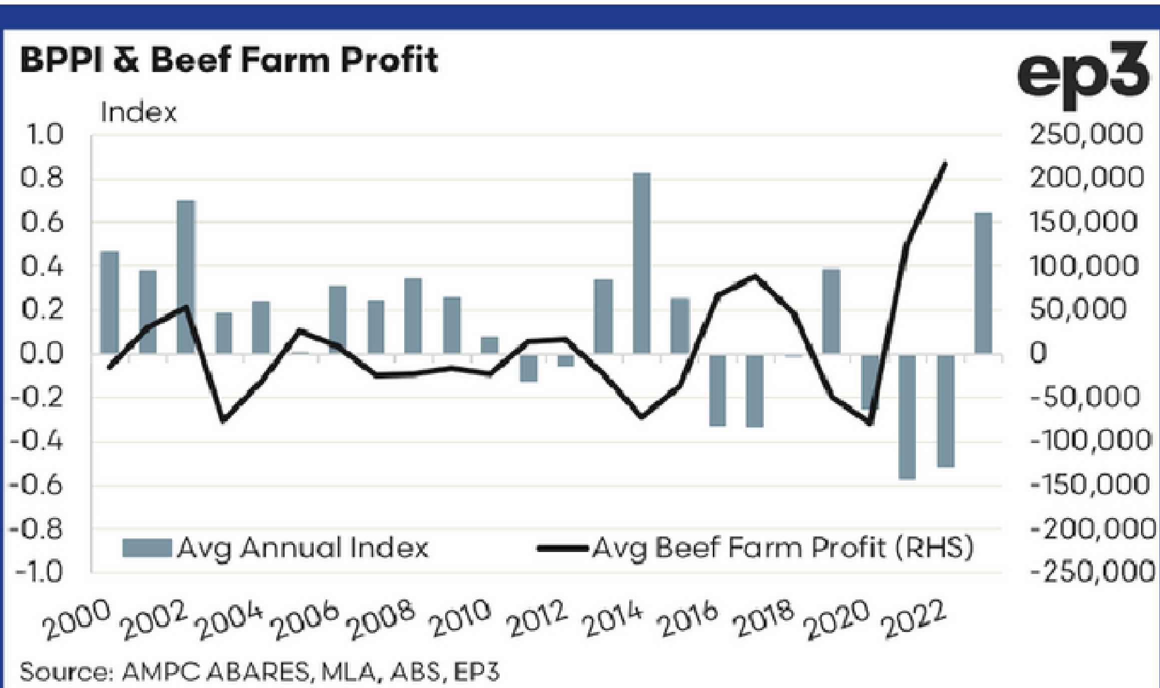


FIGURE 3.

Annual beef processor profitability usually tends to runs in a counter cyclical trend to beef farm profitability

CATTLE

In total there was 1,082,405 tonnes of Aussie beef exported during 2023 which is the best annual volumes seen since 2019. In terms of market share the USA accounted for the largest proportion of Aussie beef exports during 2023 at 22.7% of the trade. Japan squeezed out China for second top destination on 19.1% of the trade versus China's 19.0% of total beef export flows. South Korea, ended up in fourth place on 17.5% of total Aussie beef export volumes.

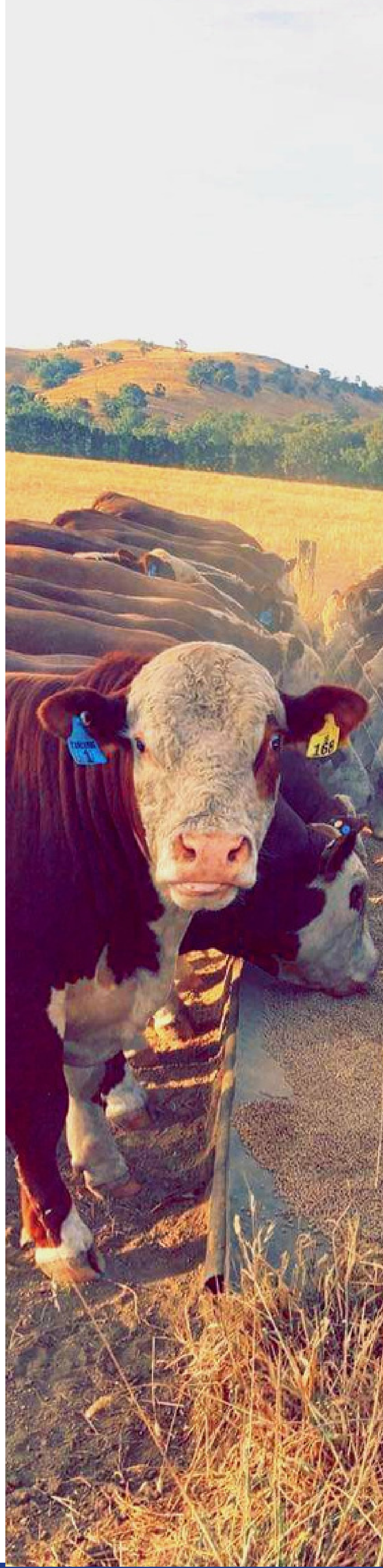
A summary for the top four beef export destinations for 2023 is outlined below.

USA – Increasingly tight cattle and beef supplies in the USA, on account of their fourth consecutive year of herd liquidation, has seen imported beef from Australia make a resurgence as record high US cattle price levels and a declining Australian cattle market increase the competitiveness of Australian beef exports. During the 2023 season USA shipped in a total of 245,849 tonnes of Aussie beef, which is the best result seen since 2019 when they took 251,822 tonnes.

Japan – The 2023 season has been the weakest annual beef trade between Japan and Australia since 1991. High levels of beef in Japanese cold storage saw relatively lacklustre demand for Australian beef from Japan over much of 2023. However, toward the final quarter of the year there was an increase in Japanese demand to see December 2023 trade volumes reach within 7% of the 5-year December average volumes. This lift in demand was enough to pip China for second top spot as a trade destination for 2023. For the 2023 season Japan took a total of 206,802 tonnes of Aussie beef exports versus China's 206,191 tonnes.

China – Despite ongoing trade and diplomatic tensions between Australia and China during 2023 the trade in beef ran at above average monthly levels for nine months of the year. On an annual basis China took 206,191 tonnes of Aussie beef exports for 2023, which was the strongest annual result since the 300,133 tonnes seen traded during 2019.

South Korea – Although the 2023 season ended a little weaker there was still a total of 188,923 tonnes of Australian beef shipped to South Korea over the year representing a new annual record volume. The 2023 season has beaten the previous record year in 2016 by around 5%.



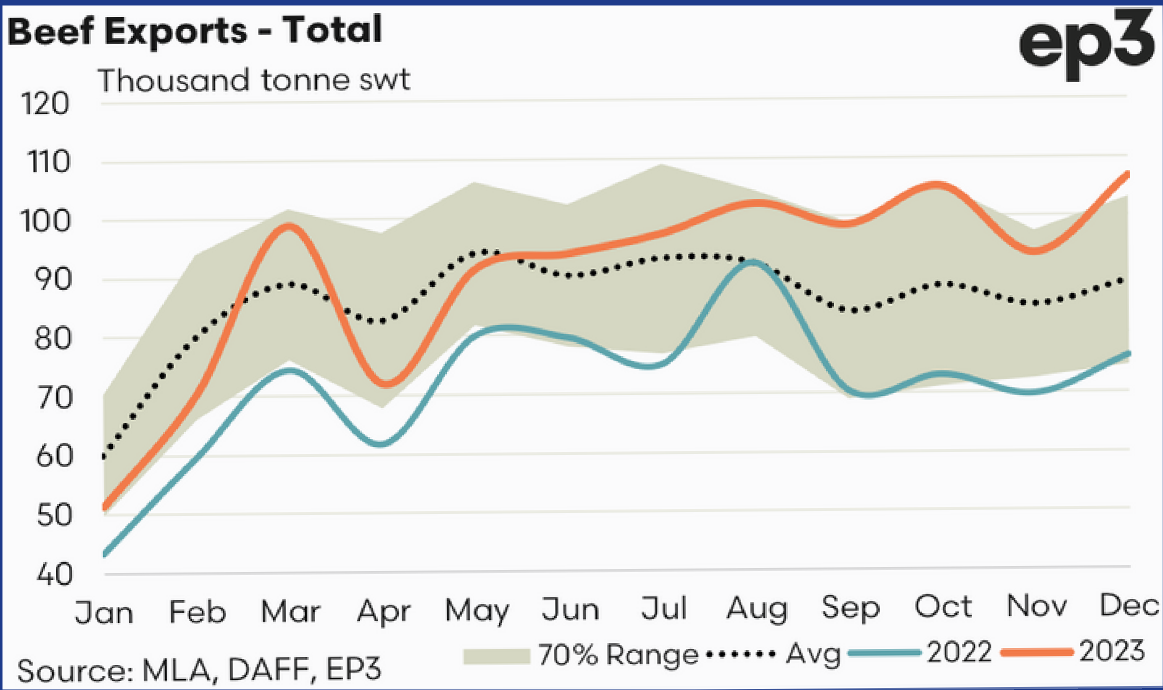


FIGURE 4.

Total Australian beef export volumes per month saw trade flows run above the 5-year average monthly volumes for much of the second half of 2023

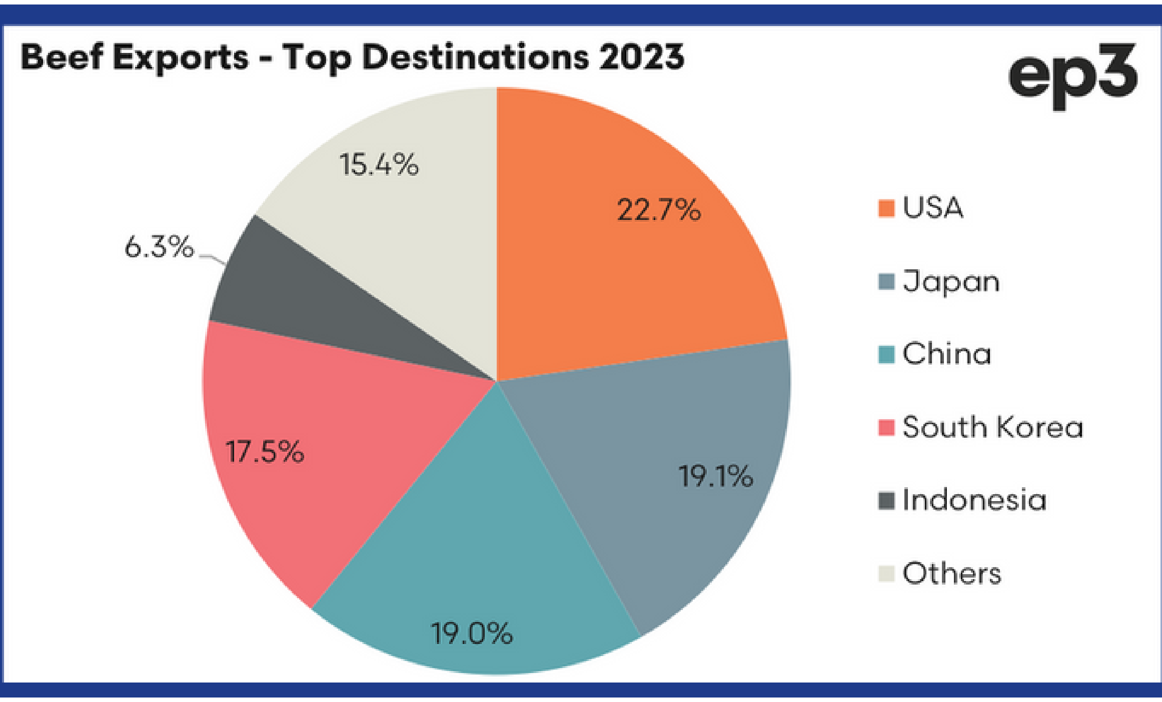


FIGURE 5.

During 2023 the USA moved into top position for market share of Australian beef exports, a significant lift from finishing in fourth place in 2022

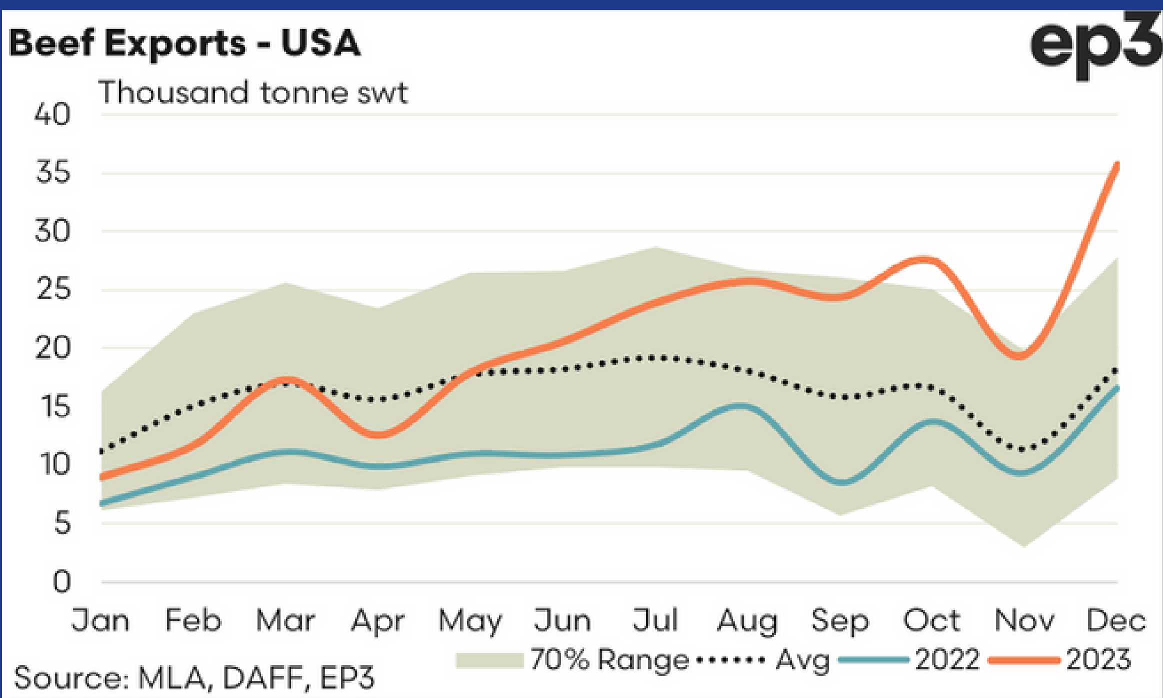


FIGURE 6.

Four consecutive years of herd liquidation in the USA saw domestic beef supply constrict in the second half of 2023, lifting cattle & beef prices and making beef imports from Australia more competitive

SHEEP

The latest Australian Bureau of Statistics (ABS) release on livestock slaughter indicates that the Australian sheep flock is still in the rebuilding phase rather than liquidation, with the sheep turnoff ratio (STR) for September 2023 at 12.6%, up slightly from 11.9% in June but still below the 14% threshold that signals liquidation. Despite the increase, the trend is moving towards liquidation, but with the annual average STR for 2023 at 11.3%, an increase in the flock size is anticipated, roughly around 4%. This aligns with Meat & Livestock Australia's (MLA) July 2023 projection of a 3.6% flock growth for the year, corroborating the statistics from the ABS data.

In total there was 326,013 tonnes swt of Aussie lamb exported offshore in 2023, a new annual record volume and nearly 15% higher than the previous record year seen during 2022 when there was 284,256 tonnes of lamb exported.

China managed to sneak past the USA for top trade destination with 20.8% of the trade compared to the 20.3% that the USA accounted for during 2023. The United Arab Emirates (UAE) held onto third top destination with 7.3% and Papua New Guinea (PNG) was placed fourth accounting for 6.9% of total lamb export volumes from Australia.

A summary of the top four Aussie lamb export destinations is as follows.

China – In total China took 67,763 tonnes of Australian lamb during 2023 which is the second highest annual volumes on record, around 5% below the 71,223 tonnes reported shipped during 2019.

USA – During the entire 2023 season there was 66,320 tonnes of Aussie lamb exported to the USA, which equates to the third highest annual volumes on record.

UAE – For the 2023 year the UAE took a total of 23,764 tonnes of Australian lamb exports which is a new annual record volume. Compared to the previous record of 20,904 tonnes set in 2016 the current trade levels are 14% higher.

PNG – In total during 2023 PNG shipped in 22,340 tonnes of Australian lamb product making the 2023 season a new annual record for lamb exports, with flows 2% higher than the previous record year of 21,900 tonnes set in 2022.

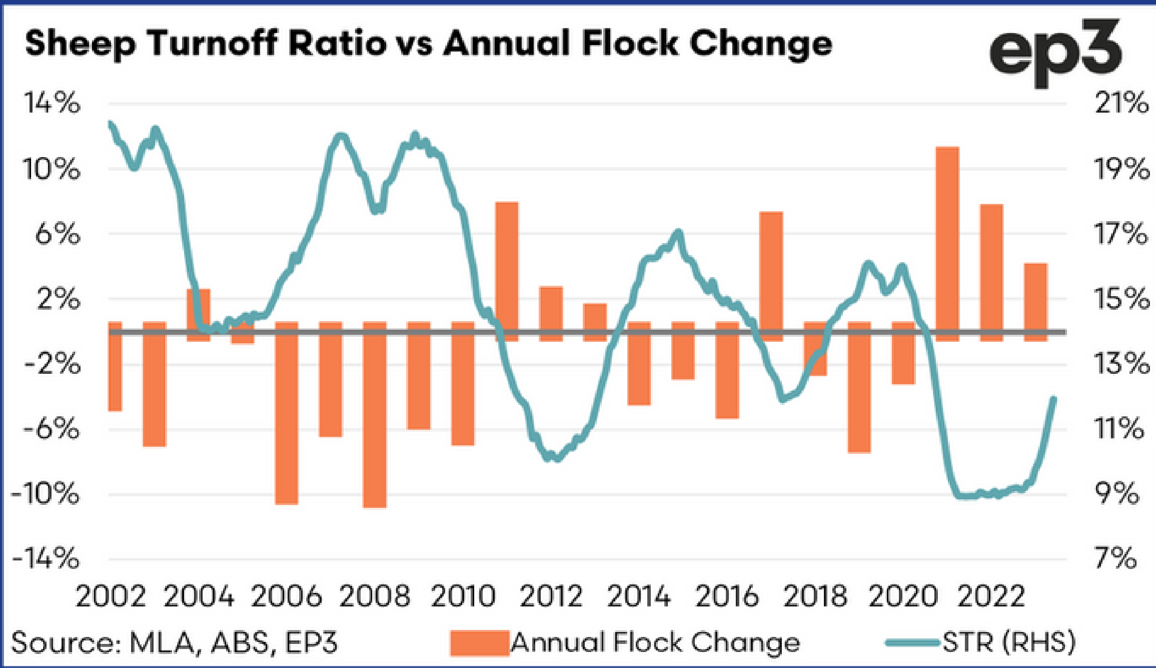


FIGURE 7.

The annual sheep turnoff ratio (STR) for 2023 shows that the Australian flock remains in rebuild mode

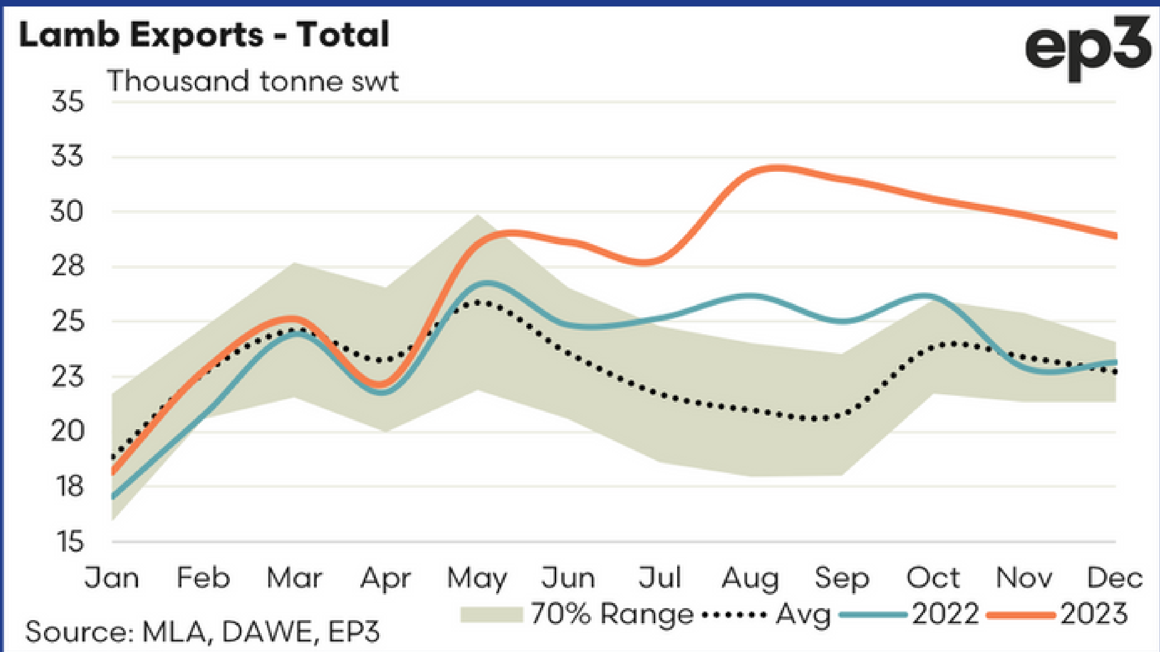


FIGURE 8.

Total Australian monthly lamb export volumes for 2023 saw unusually strong flows during winter and a very solid finish to the year leading to record annual export flows, 15% higher than the previous record year

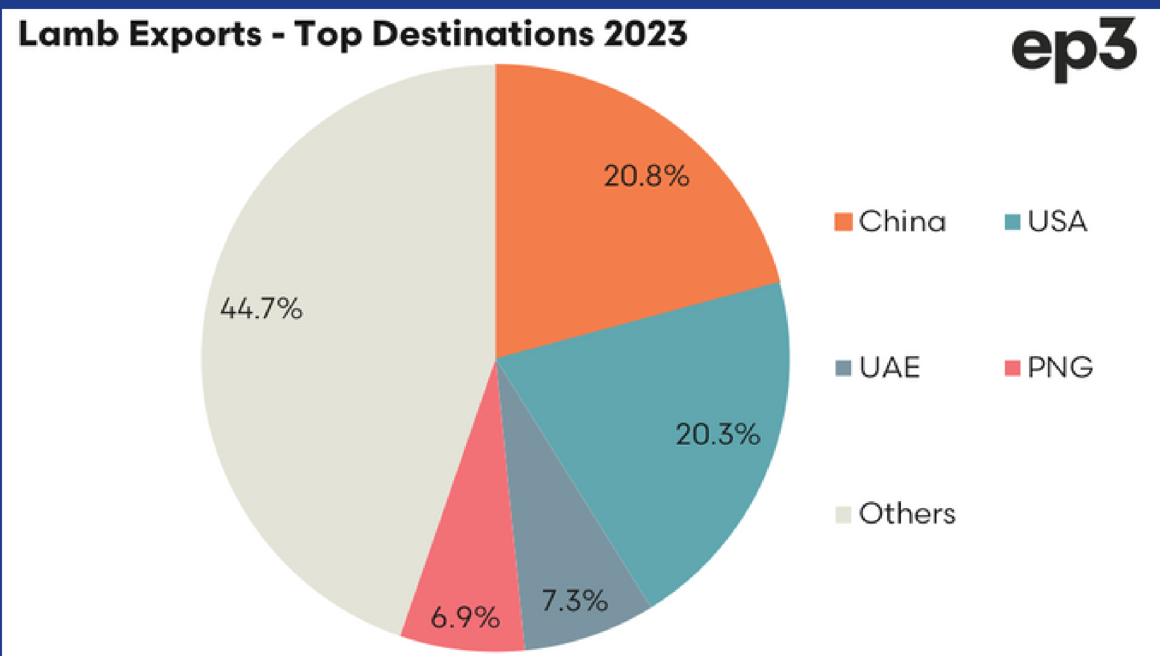


FIGURE 9.

China and the USA remain the top two destinations for Australian lamb exports in 2023, combined accounting for over 41% of the total trade

SHEEP

December 2023 saw total Australian mutton export volumes lift by nearly 5% from the levels shipped during November with 20,799 tonnes swt reported exported from Australia, making a new December record export total for mutton exports after topping the 20,309 tonnes exported in December 2014.

Compared to the five-year average for December the 2023 flows were 24% higher and nearly 37% above the export volumes reported for December 2022. The strong finish topped off a stellar year for Aussie mutton exports with 209,580 tonnes of mutton exported over the 2023 season which is a new record for annual Australian mutton exports. Mutton export flows for 2023 were nearly 13% higher then the previous best year, which was seen in 2014 when 185,992 tonnes of mutton were reported shipped offshore.

China dominated the market share of Australian mutton exports in 2023 accounting for 46.5% of the trade, a big lift from the 39.8% seen in 2022. Malaysia took out second top spot with 10.2% of the trade in 2023, down from 12.5% in 2022. Third top destination for 2023 was secured by the USA on 6.6%, down from a 12.2% share in 2022. Meanwhile, Saudi Arabia placed fourth with an increased share from 4.2% in 2022 to 5.7% in 2023.

A summary of the trade flows to the top four mutton destinations is as follows.

China – In total China took 97,481 tonnes of Australian mutton during 2023, nearly 20% above the previous record year in 2019 when 81,460 tonnes of mutton was shipped from Australia.

Malaysia – Over the 2023 season Malaysia took a total of 21,414 tonnes of mutton from Australia which makes 2023 the strongest year on record, beating the previous best year (2022 with 18,046 tonnes) by nearly 19%.

USA – In total the USA accounted for 13,749 tonnes of Australian mutton exports for 2023, which is around 27% softer than the average annual flows seen over the last five years.

Saudi Arabia – For the entire 2023 season Saudi Arabia took 11,851 tonnes of Aussie mutton, which is the strongest annual trade volumes seen since 2018 when they took 12,070 tonnes.

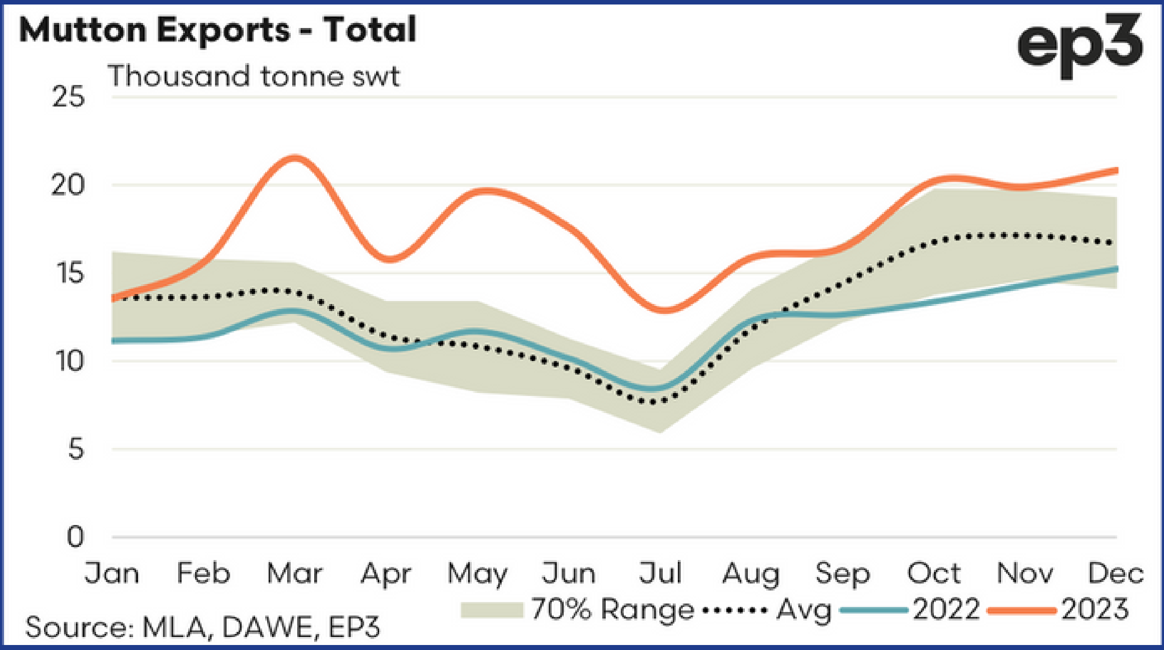


FIGURE 10.

Total Australian mutton export flows spent the entire 2023 season well above the 5-year average trend and annual export volumes exceeding the previous record year by 13%

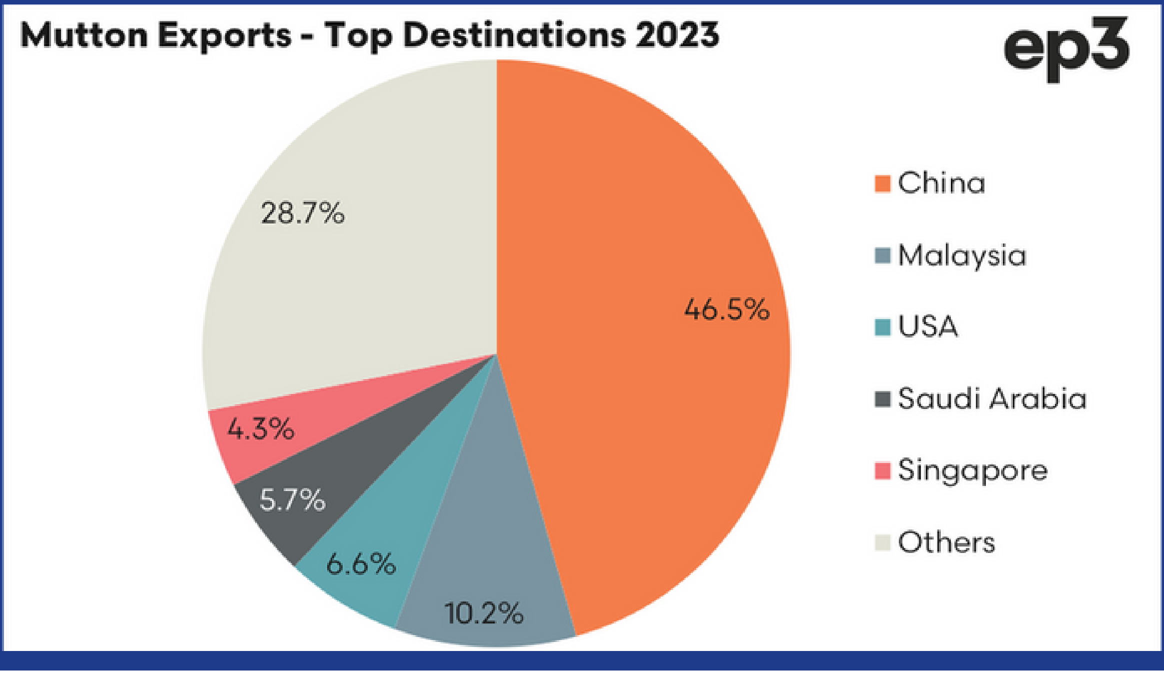


FIGURE 11.

China retained a clear dominance in the market share of Australian mutton exports, meanwhile Malaysia outperformed the USA for the second consecutive season

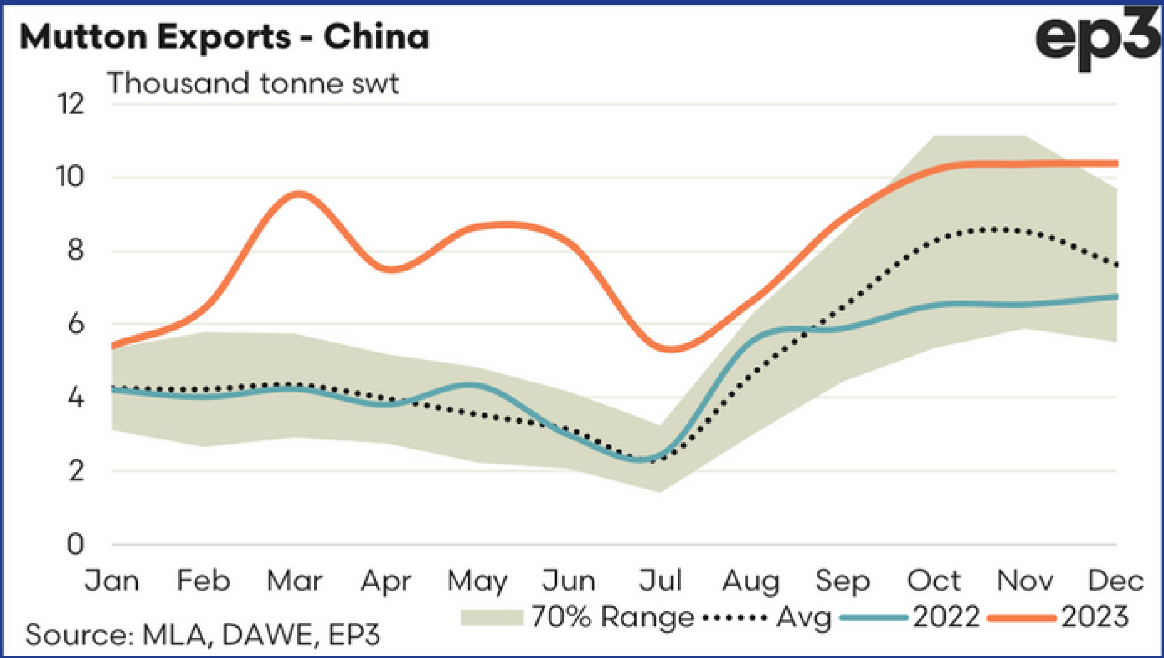


FIGURE 12.

2023 proved to be an exceptionally strong year for Chinese demand for Australian mutton with very cheap Australian pricing during the season assisting export competitiveness

WHEAT

The Australian winter wheat harvest was completed in Mid-January. The expectation prior to harvest was of a dry period due to the declaration of an active El Nino phase, it is important to note that there is confusion about El Nino and La Nina.

An El Nino phase increases the chance of dry conditions, and a La Nina phase increases the chance of wet conditions. It does, however, not guarantee either result. The harvest in Australia was mired in many places by wet conditions despite the declared El Nino. This has resulted in harvest being longer than expected, by around a fortnight.

The Australian wheat crop estimates were increased between September and December as wet weather increased yields. The current estimate for the Australian wheat crop is 25.45mmt, which places it 946kmt lower than the ten-year average.

It must be noted that the ten-year average is now potentially skewed higher due to the extreme production of 2020 to 2022.

New South Wales suffered through a slow harvest, which has ultimately resulted in a reduction in higher protein wheat. Production was pegged at 6.6mmt, down 3.66mmt year on year.

Western Australia had a drier finish than eastern states, allowing harvest to progress with minimal delays. Western Australia produced 8.15mmt, down 5.85mmt year on year.

South Australia had patchy storms throughout the growing period, which resulted in some areas performing significantly higher than others. South Australian production was 4.9mmt, down 2.45mmt year on year.

Victoria experienced variable weather conditions throughout harvest, which resulted in significant delays, and harvest only completed in mid-January. Victoria produced 4.6mmt, down 774mmt year on year.

The Australian average wheat yield in 2023 was 2.04mt/ha, which was lower than the ten-year average of 2.2mt/ha. Victoria was the only state that produced a yield in 2023, higher than the ten-year average.

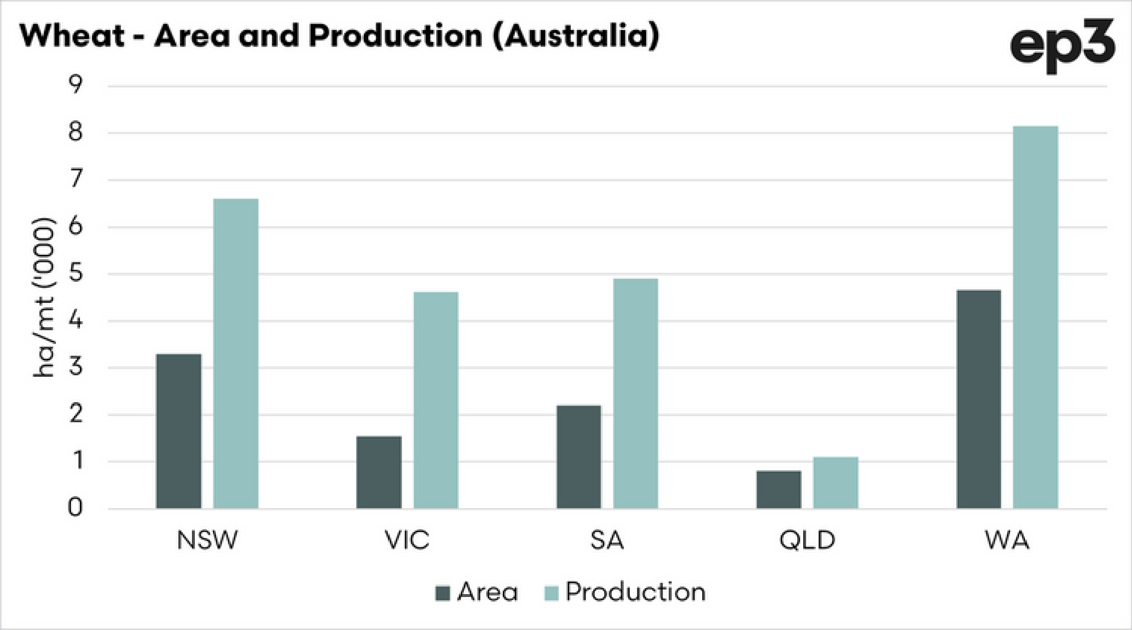


FIGURE 1.

Area planted in 2023 was reduced slightly, but yields were substantially down year on year

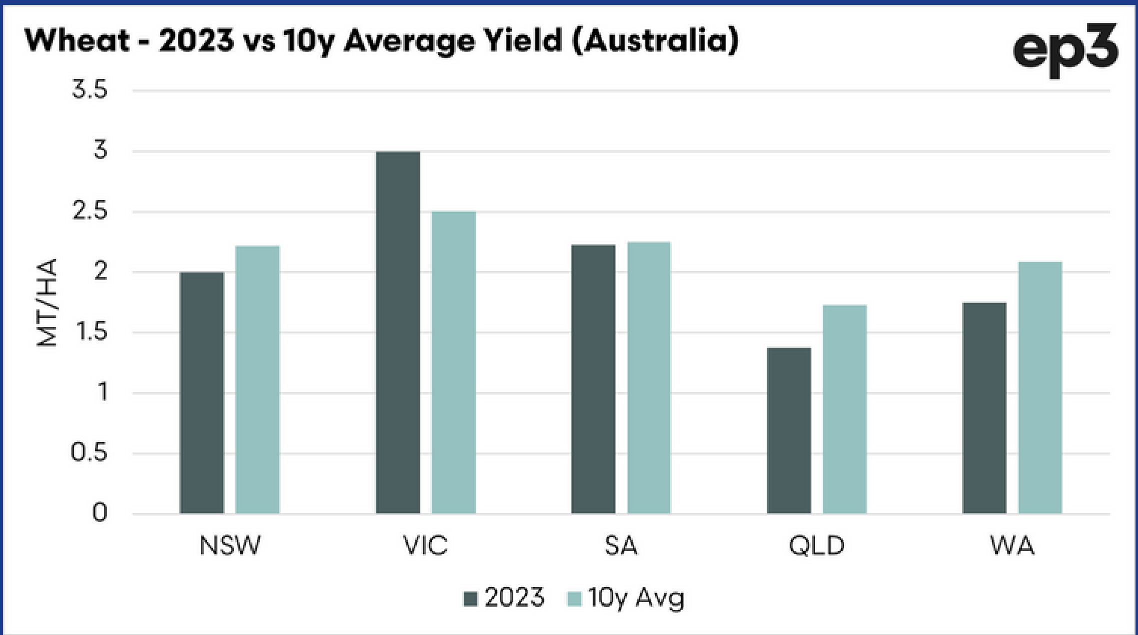


FIGURE 2.

Victoria was the only state to record a higher wheat yield in 2023 than the ten year average

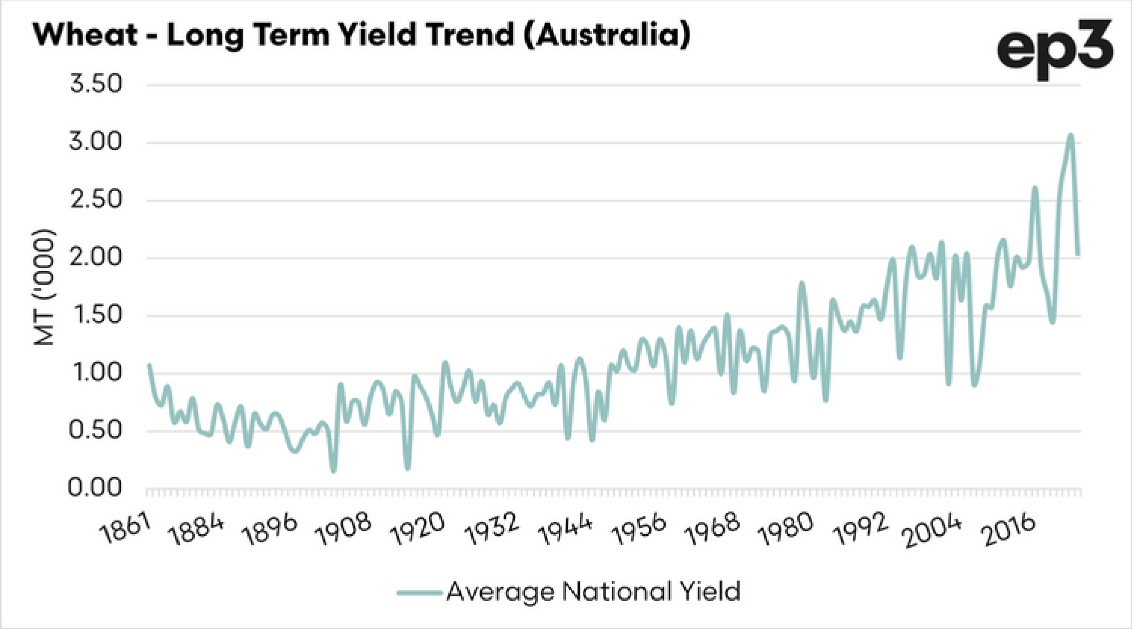


FIGURE 3.

Wheat yields have been trending higher. It is important to note that almost perfect conditions were experienced in the period 2020 to 2022

WHEAT

The Australian wheat market is influenced by both local and international factors. In recent years, Australian wheat has been trading at a significant discount to overseas values, due largely to the large crops the country has been producing. In 2023, the Australian wheat price increased from a discount to a premium.

The premium was at its strongest for this season in the run to harvest, as buyers and sellers were anticipating reduced yields due to poor weather forecasts. As harvest developed and production above domestic demand was realised, the premium declined to the expected range.

The inclement weather reduced the risk of further falls in yields. However, wet weather reduced the quality through lower protein levels. The wet finish causes a dilution effect, where increased moisture content can result in a lower proportion of protein relative to the total weight of the grain.

This reduced availability of higher-protein wheat can be seen in the spread between APW1 (Mid protein) and H2 (High protein). The spread has increased this season to the highest since 2017, a season that experienced wet conditions in the lead-up to harvest.

The spread will likely remain high until local domestic consumers have achieved their required volumes, after which prices may taper downward. At an international level, markets were relatively quiet during the past quarter. The largest story in markets (other than the continuation of the war in Ukraine) has been the high production and stocks of corn.

As of the end of December, US corn stocks are at the highest level since 2018, and the third largest on record. These large stocks have a bearish influence on wheat pricing, as corn and wheat are fungible. In the coming months, from March to May, there will be more visibility of the global wheat and corn production for 2024.

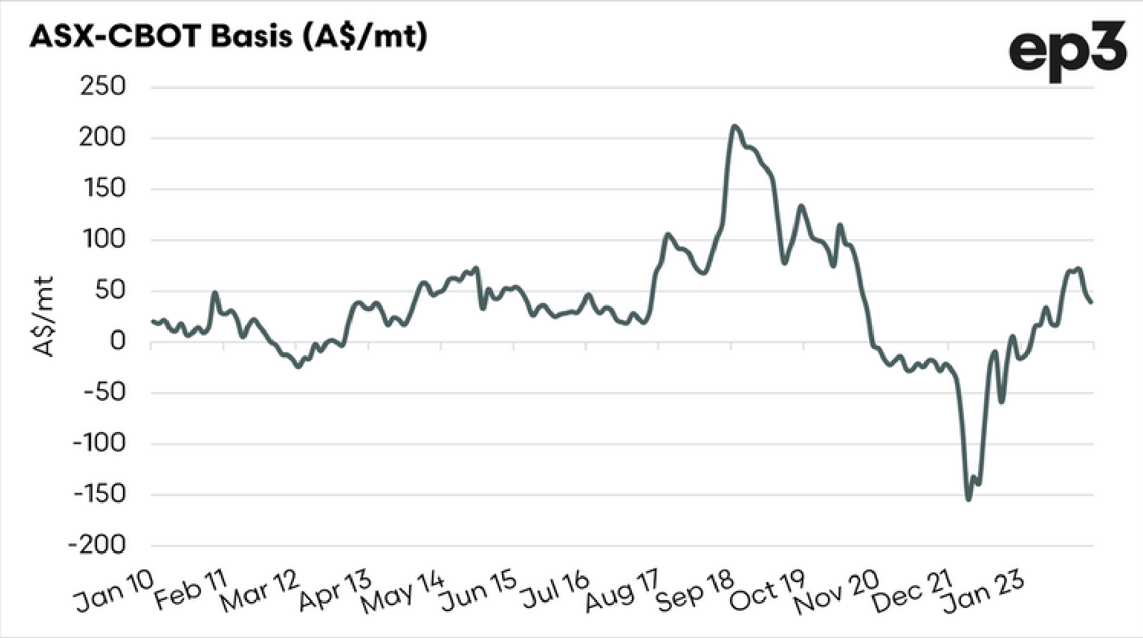


FIGURE 4.

Australian wheat tends to trade at a premium when supplies are locally low, and at a discount when large

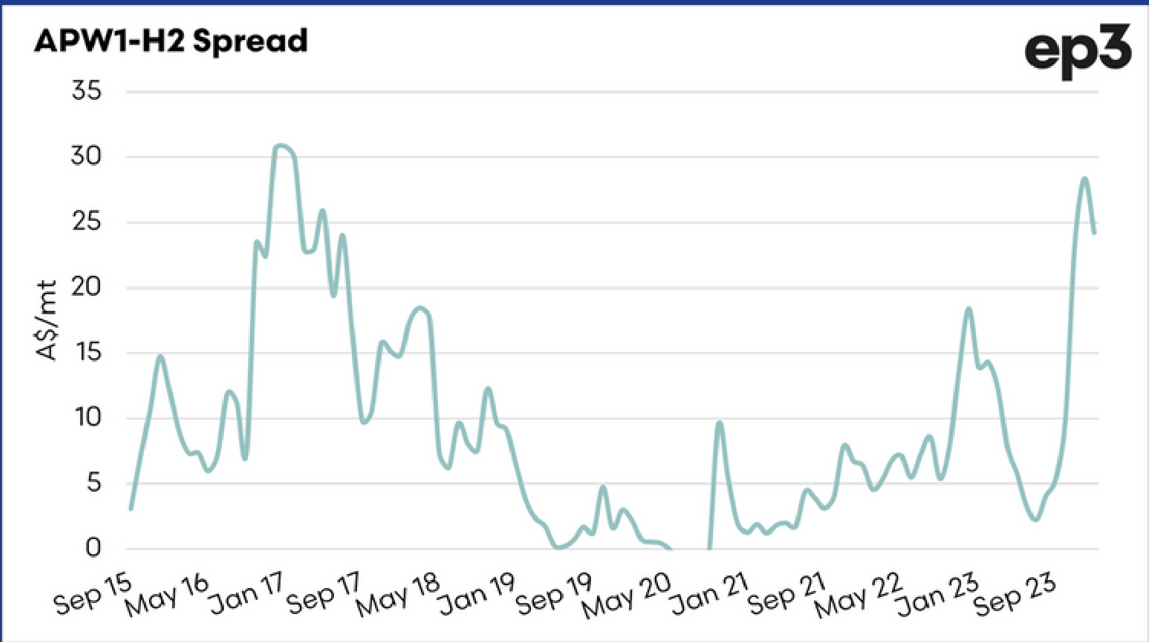


FIGURE 5.

The spread between APW1 and H2 is indicative of the availability of higher protein wheat. During seasons with a wet finish (2016 and 2023) the premium increases

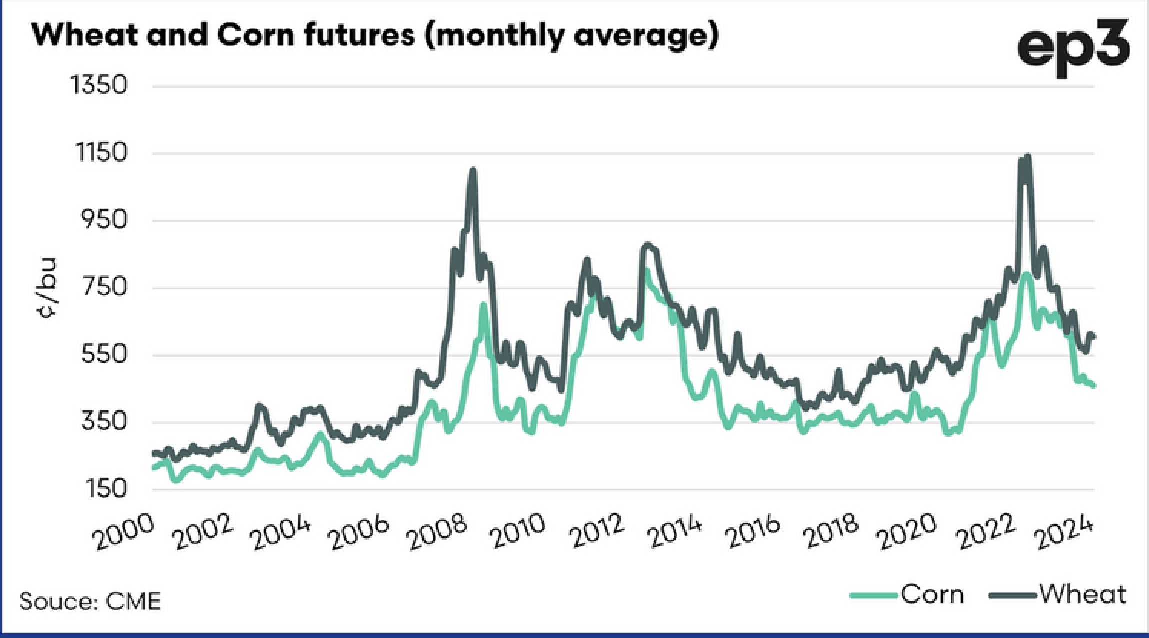


FIGURE 6.

Corn and wheat have similar uses (feed), and their prices tend to follow one another with a relatively strong correlation

As global corn supplies increase, it will create downward pressure on wheat

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