



USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Voluntary Report - Public distribution

Date: 2/12/2009

GAIN Report Number: AS9005

Australia

Agricultural Situation

Financial Turmoil Impacts Australian Agriculture

2009

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Report Highlights:

Recent global financial turmoil has gained widespread media attention in Australia and has driven significant (if not profound) changes in expectations for key economic indicators. Falling commodity prices will likely be offset (at least partially) by falling input costs. A depreciated Australian dollar will also greatly assist returns for exports and improved export competitiveness. Disparity in depreciation of these prices will likely provide major challenges for agriculture producers. Another challenge for Australian agricultural industries is the declining demand in key export markets. Australia exports around two thirds of total agricultural production and thus remains highly reliant upon export market factors.

Includes PSD Changes: No
Includes Trade Matrix: No
Trade Report
Canberra [AS1]
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Executive Summary

Recent global financial turmoil has gained widespread media attention in Australia and has driven significant (if not profound) changes in expectations for key economic indicators. Parallel to this, prices received for key agricultural commodities have diminished as have prices for key inputs. Many prices, despite sharp falls, have not yet fallen below the ten-year-historical average.

Shifts in interest rates, gross domestic product and unemployment will likely affect the performance of the agricultural sector. However, the most profound change will likely flow from changes in currency values and import demand.

The most recent ABARE quarterly report (December Quarter) revised key 2008/09 macro economic assumptions due to recent changes in the economic outlook. ABARE has also revised its 2008/09 forecast price index data downwards for 2008/09. However, more recent indicators have surpassed these figures suggesting another downward revision in the future.

Falling commodity prices will likely be offset (at least partially) by falling input costs. A depreciated Australian dollar will also greatly assist returns for exports and improve competitiveness. Post's investigations have revealed that input and output prices for 2008/09 are returning to levels more reflective of the long-term average.

The challenge for Australian agriculture depends on input and output prices moving downwards together. Disparity in depreciation of these prices will likely provide major challenges for agriculture producers. For example, already a sharp downwards movement in cash prices for wheat remains at odds with historically high fertilizer prices and will likely constrain returns for producers.

Another challenge for Australian agricultural industries is the declining demand in key export markets. In recent months, beef, wine and dairy exports have already experienced poorer demand and this has been reflected in domestic prices generally. Australia exports around two thirds of total agricultural production and thus remains highly reliant upon export market performance.

For the Australian dairy industry, a downward shift in milk prices will likely be offset (at least partially) by decreased fodder and fuel costs. The falling Australian dollar will also likely buffer this industry somewhat from falling global prices as will a decline in interest rates. However, other input costs such labor and fertilizer may not shift downwards at the same rate.

Beef, poultry and pork production will also benefit from reduced prices of fuel and fodder. Beef is the most export-reliant of these industries and so has already experienced price falls below current forecasts. Cotton and sugar are expected to remain relatively stable following price corrections prior to 2008/09.

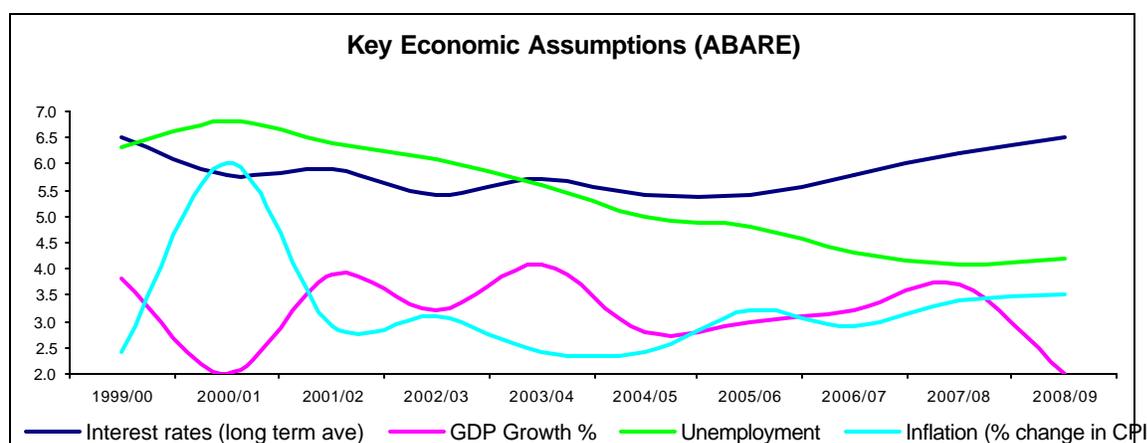
Key Economic Indicators

Interest rates rose steadily in Australia since 2002/03 amid concerns of inflation. ABARE for example, had assumed an interest rate of 6.5 percent for 2008/09, up on the 6.2 percent for the previous year and significantly higher than the ten-year-average of 5.9 percent established using historic data.

Interest rates in 2008/09 had been expected to remain relatively unchanged, due to continued inflation concerns. However, official interest rates have since experienced consecutive cuts and remain lower at time of writing this report compared to year previous. This fall will likely see current estimates for full-year 2008/09 interest rates lowered.

Inflation had also been estimated to remain at historically high levels in 2008/09 at around 3.5 percent. Across-the-board increases in the cost of goods and services in Australia since 2004/05 brought upward pressure on inflation. The ten-year average for inflation is 3.2 percent. Inflation reached a record level of 13.9 percent in Australia in 1976/77 and reached 11.5 percent in 1982/83.

More recent data suggests that poorer demand combined with a radically different global financial situation will see inflation levels fall in the second half of 2008/09. Recent Australian Bureau of Statistics data shows a slight fall in consumer prices for the December 2008 quarter.

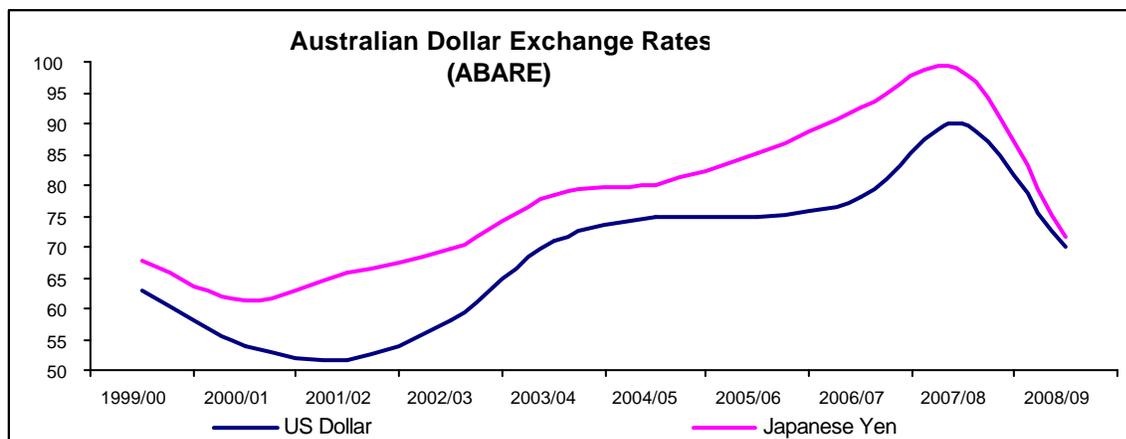


Growth in GDP is estimated to have slowed to 2.0 percent in 2008/09, down on the 3.7 percent growth in the previous year and the ten-year-average of 3.2 percent. Despite this fall, this level of growth (if achieved) would make Australia one of the fastest growing economies in the developed world and one of the few developed countries not currently experiencing "negative growth". Recent ABS data shows growth in GDP growth falling on a monthly basis.

Unemployment is estimated to rise slightly to 4.2 percent in 2008/09, up from the record low of 4.1 percent. Media reports unemployment will likely surpass the 4.2 forecast.

The Australian dollar has depreciated markedly in recent months. Currently ABARE, estimates the full-year dollar value at US\$0.70 for 2008/09, down on the US\$0.90 estimated for the previous year but up slightly on the ten-year-average of US\$0.69.

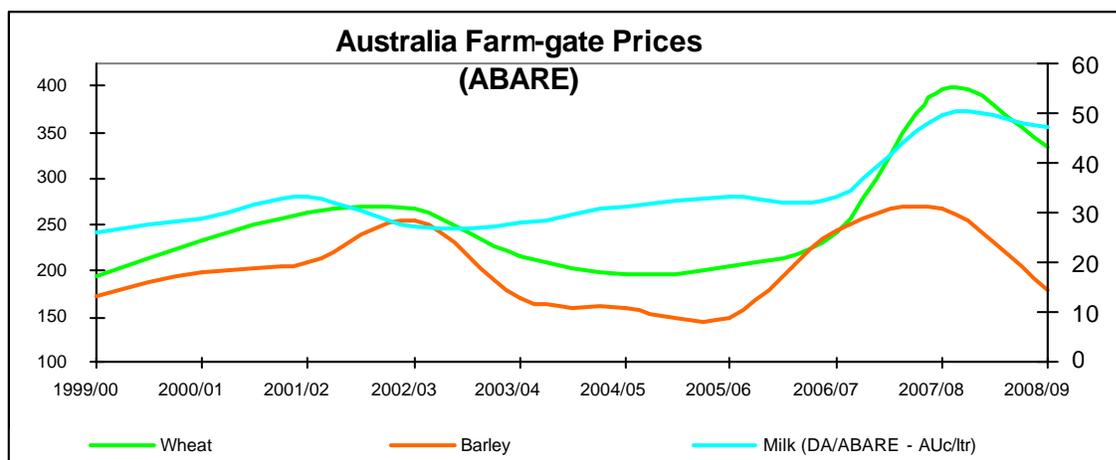
At time of writing this report the Australian dollar is valued at around US\$0.67. A continuation of this level for the remainder of the year would reinforce Australia's global export competitiveness.



Farm-gate Prices

Australian farm-gate prices for wheat, barley and milk are forecast by ABARE to decline in 2008/09. Wheat and milk are forecast to remain above the ten-year-average despite the drop in prices while barley prices are expected to fall to below average levels.

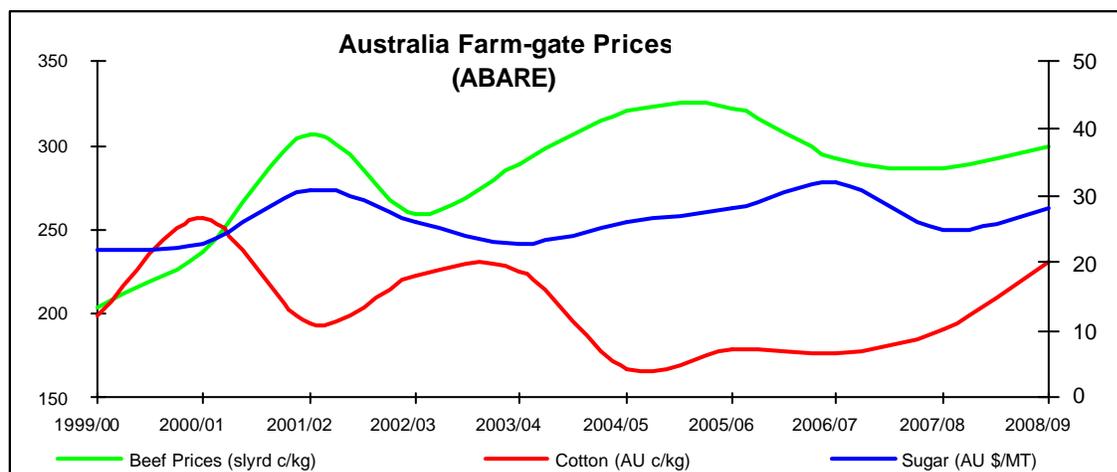
The fall in global dairy prices has gained much media attention, falling from all-time record high levels. These declines have already filtered through to lower farm-gate prices for milk. Wheat prices have also declined sharply in recent times, however in the case of wheat, industry sources are confident of a modest price increase going forward. This outlook is supported by anecdotal evidence that suggests sizable quantities of wheat are currently being withheld from sale as farmers respond to sufficient storage and market uncertainties.



ABARE forecasts prices for beef, sugar and cotton to increase slightly over the 12 months in 2008/09 despite the poor economic outlook. These commodities already experienced significant price declines prior to 2008/09 and therefore arguably have less downside potential in terms of pricing.

Nonetheless farm-gate prices for beef at time of writing this report have fallen somewhat. The market for feeder cattle has been remarkably weak considering the recent sharp decline in feed and fuel prices and the decline in the value of the Australia dollar. Industry sources suggest poor demand for Australian beef in export markets is the primary driver for these

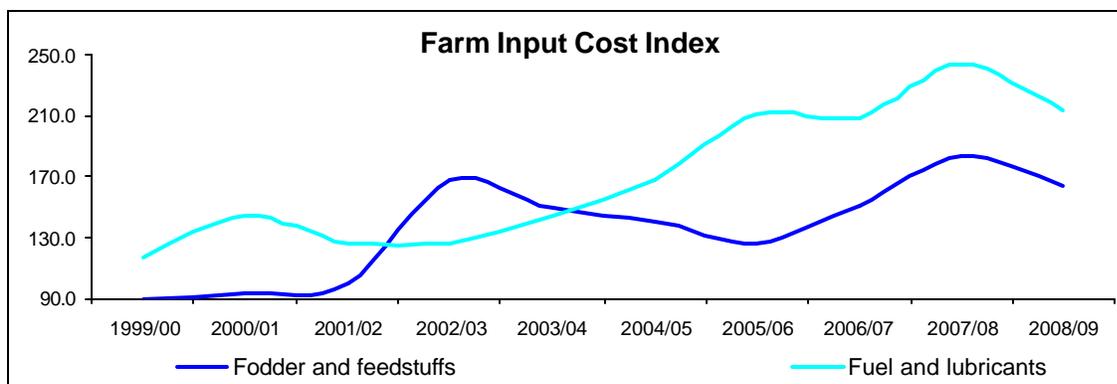
declines. Australia exports around two thirds of beef production so that beef prices fall in line with export demand despite relatively strong domestic demand. High beef stocks combined with reduced consumption in export markets has depressed prices for Australian beef exports.



Farm Inputs

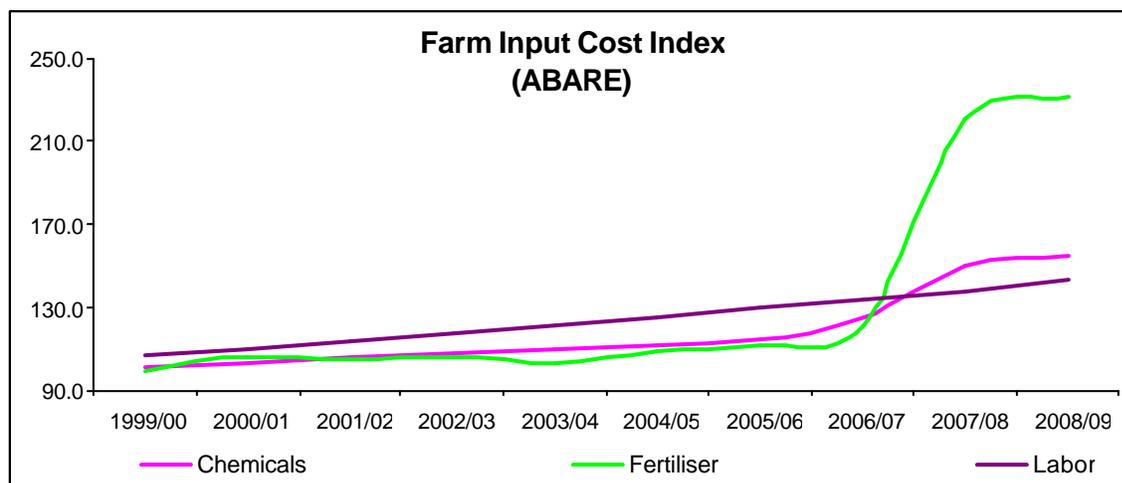
Total farm input costs are forecast to decline slightly in 2008/09. Fuel is expected to decline 12 percent and fodder is expected to decline around ten percent. However, indicative prices for fuel and fodder suggest these will fall much further than this in 2008/09 and will likely reflect levels closer to the ten-year-average.

Declines in fuel prices are expected to benefit the entire agriculture sector while falls in fodder prices are expected to greatly benefit intensive animal enterprises such as lot-fed beef, pork, poultry and dairy. Fuel and fodder have both fallen from record levels.



Farm chemicals and labor costs in 2008/09 are expected to increase slightly, in line with the long term trend. However, fertilizer is expected to also increase slightly over the 12 months of 2008/09. Industry sources were anticipating sharp declines in fertilizer prices given the decline globally. Post's inquiries suggest that the fertilizer industry has been unable to resolve the issue of overpriced stocks throughout the supply chain and that this issue may be constraining price corrections at the retail level. A high level of fertilizer import means that the lower Australian dollar has also constrained falls in retail fertilizer prices.

The disparity between global fertilizer prices and retail prices within Australia has been subject to government scrutiny which found that Australia's Trade Practices Act had not been breached. An Australian Senate Committee has also undertaken a similar investigation.



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