JUNE 2020

Rural Price Index

Global meat price rise to offset lower world grain price

Recently, China introduced tariffs on barley imported from Australia. While this may reduce demand on a national basis, Western Australia will be disproportionately impacted as the vast majority of Australian barley exports to China come from Western Australia.

Construction of the Index

The BankSA *Rural Price Index* informs the state's farmers and farm industries how prices are faring for South Australia's farm products. The index aggregates price movements across 17 products which together account for more than 80% of South Australia's farm output.

There are three groups of products – grains (such as wheat and barley), livestock and related products (dominated by sheep, wool, and beef), and horticulture (dominated by grapes).

The index shows prices in Australian dollars (reflecting the prices received by South Australian farmers), as well as in terms of the currencies used by the typical customer for Australian exports (that is, prices paid by foreign buyers).

Weaker dollar provides some support while demand slumps

COVID-19 is having a significant impact right across the economy, including for the farm sector. This is occurring through changes in global supply chains as well as changes in the nature of demand. On the demand side, components of the sector have seen the reduction in consumption at restaurants and cafes offset to various extents by increased consumption at home. However, there are also supply side disruptions from social distancing restrictions affecting food production processing.

Additionally, exports will likely be affected by lower household incomes – particularly in the emerging middle classes of key Asian markets. As well as cutting into demand, this may cause export prices for certain products to fall. However, the lower Australian dollar (compared with 2019) will mitigate the impact on South Australia's farmers somewhat, as well as boosting their competitiveness.

Further factors that have influenced Australian agricultural exports in recent months include a boost in global meat prices

BankSA Rural Price Index

Index base : January 2000 = 100	Level	March 2020 % change since Sep 2019	Mar 2019	Mar 2018
AUSTRALIAN DOLLAR INDEX				
Grains	232.4	-1.9%	-2.7%	+30.6%
Livestock and Livestock Product	197.3	-1.7%	+1.8%	-0.1%
Livestock Only	*191.4*	*-2.2%*	*+2.1%*	*+1.8%*
Horticulture	159.6	+8.4%	+5.3%	+10.6%
TOTAL ($A Based)	**187.4**	**+0.0%**	**+0.8%**	**+4.0%**
SDR INDEX				
Grains	221.2	-11.2%	-14.6%	+10.9%
Livestock and Livestock Product	187.8	-10.9%	-10.6%	-15.2%
Horticulture	152.0	-1.8%	-7.6%	-6.1%
TOTAL (SDR Based)	**178.4**	**-9.4%**	**-11.5%**	**-11.7%**
TOTAL (TWI Based)	**183.0**	**-7.6%**	**-8.9%**	**-8.7%**

CHART R1
THE BANKSA RURAL PRICE INDEX - JANUARY 2000 = 100

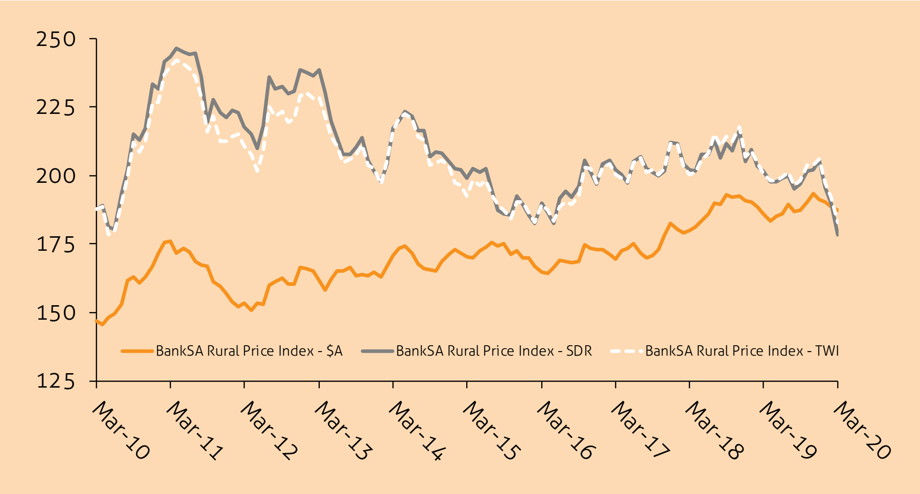
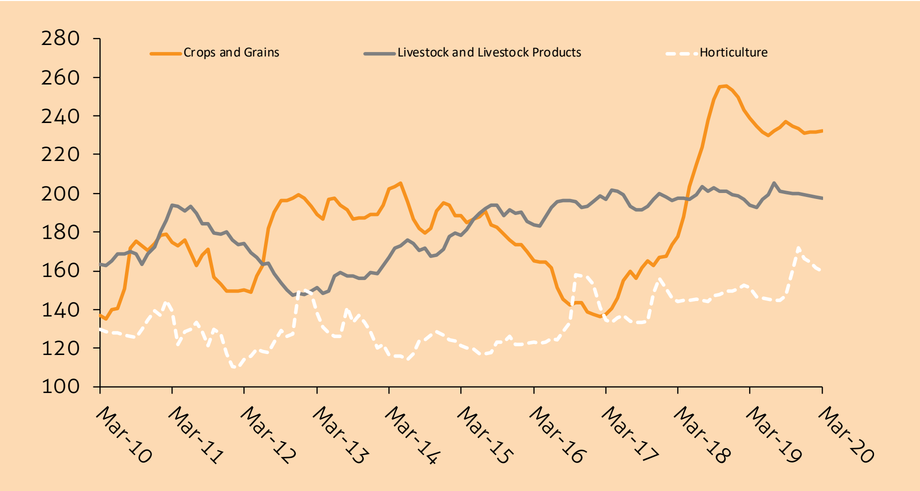


CHART R2
COMPONENTS OF THE BANKSA RURAL PRICE INDEX



(as a result of shortages driven by African swine fever) and a relatively low world grain price. Looking ahead, the world grain price may increase if countries introduce tariffs for staple grains in response to the pandemic. As a significant proportion of South Australia's wheat is exported, an increase in the world grain price would likely impact prices for South Australian farmers.

Recently, China introduced tariffs on barley imported from Australia. While this may reduce demand on a national basis, Western Australia will be disproportionately impacted as the vast majority of Australian barley exports to China come from Western Australia.

Domestically, upward pressure on the grain price resulting from drought-constrained supply is expected to ease.

The $A line in Chart R1 indicates the price that South Australian farmers receive, while the other two lines indicate what foreign buyers pay. So a larger gap between the two lines indicates a problem for the competitiveness of South Australian produce. As a result of the lower value of the $A in 2020, the gap has narrowed considerably since the start of this year. From January to March, the price received by South Australian farmers has decreased by 1.5%, while the price foreign buyers pay, as indicated by the SDR line, decreased by 8.9%. Overall, producers haven't seen a notable decline in the price they receive for exports even though prices on global markets have eased.

While this is something of a relief for exporters in the context of falling global prices, other key areas in the agricultural sector will also be affected by the current downturn in the domestic economy. In particular agricultural products that act as inputs into housing construction, clothing and other household items will be more susceptible to changes in economic activity. This is mainly applicable to forestry outputs and wool.

Rural Price Index varies across major categories

Chart R2 shows the performance of three key commodity groups within the broader South Australian agricultural industry. The price performance of the groups over the last year has been relatively unchanged as crops and grains and livestock have hovered near the same level as the start of 2019, and horticulture continued its upward trajectory over the year despite experiencing a recent downturn.

The overall grains price index continues to sit a little below the historical peak, which occurred in 2018. While the overall grains index has decreased since January, due to a fall in world grain prices, drought conditions have resulted in a greater proportion of Australian wheat being consumed domestically. The supply shortage has resulted in an increase in domestic prices and a reduction in exports. As production increases post drought, domestic grain prices are expected to fall to a more competitive rate, with a commensurate increase in exports. According to the ABARES February Crop Report, South Australian winter crop production for 2019-20 increased by 12% from 2018-19, seeing increases in wheat, barley and canola production of 8.5%, 21% and 15% respectively. Despite these welcome rises, production levels are still significantly below their 10-year average.

Livestock and livestock product prices have also eased of late, although they remain very close to the 2019 peak. The need to switch away from pork due to the ravages of African swine fever has pushed up beef prices in the global markets. And, as the vast majority of Australian beef is exported, the rise in export prices has a substantial flow-on impact on domestic prices too. The impacts of the supply shortage on pork prices have been even greater, although prices may ease from here as swine fever is contained.

The price level for horticultural products peaked in 2019 as a result of increased demand from China combined with a competitive Australian dollar. The impact of COVID-19 on the Chinese economy's demand for our products has seen that start to reverse.

The Barossa and Clare Valley, are expected to experience yield reductions of up to 80%. On the other hand, the Riverland area is expected to only experience a moderate 16% reduction in yield.

The wine industry – a testing vintage

Extreme heat, frost, wind, bushfires and smoke taint have seen a challenging vintage for South Australia's winemakers and wine grape growers. On top of this, the wine industry – as with many other industries – has been adversely impacted by COVID-19.

The industry has been tested through critical growth points, with early frosts, wind around flowering time and extreme heat. Bushfires over the summer destroyed many vines in the Adelaide Hills and across Kangaroo Island, and have left many vines smoke tainted. That has led the South Australian Wine Industry Association to estimate a 50% reduction in this year's yields, noting that some regions will fare even worse. Two of those regions, the Barossa and Clare Valley, are expected to experience yield reductions of up to 80%. On the other hand, the Riverland area is expected to only experience a moderate 16% reduction in yield. While production levels are set to be low, a spread out vintage has allowed for good ripening and will hopefully result in a good quality vintage.

COVID-19 has then created additional challenges for the South Australian wine industry. While social distancing has been enacted in production facilities, they have continued in many aspects with business as usual as restrictions have come into place post peak picking season. COVID-19 has had larger impacts on tourism levels, cellar door sales and sales to restaurants. All three factors mean that the pandemic is an even bigger negative for smaller boutique wineries.

As a result, Australian Grape and Wine Inc is estimating that approximately 30% of Australian wineries could go out of business. That impact is likely to be felt throughout the supply chain and distribution network – with both grape growers and the distributors who act on behalf of wineries to sell to restaurants, hotels and cafes likely to feel the effects.

A light at the end of the tunnel, at least for the Barossa Valley, could be a proposed 12-storey hotel and day spa at Seppeltsfield. The $50 million six-star hotel named "Oscar" could rival the d'Arenberg Cube in the McLaren Vale Wine Region. Construction on Oscar is expected to start in 2021, with completion expected in 2022. According to Seppeltsfield the direct tourism expenditure as a result of the hotel is expected to amount to $86 million over the first five years, with tourist visitor numbers expected to be close to 150,000 during that period. While this may ultimately be impacted by COVID-19 and the length for which restrictions remain in place, it remains a positive.

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