Russia-Ukraine Impact on Australia

Australia Agribusiness Monthly

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RaboResearch
Food & Agribusiness

Rabobank

Commodity Outlook

Commodities	Russia and Ukraine have taken centre stage and fear of global supply shortages drive prices of grain, energy and fertilisers. Length of conflict and effectiveness of sanctions will determine regions exports.
Grains & Oilseeds	Conflict in the Black Sea to raise export demand and prices, but Australian basis is moving heavily negative offsetting some of the international price gains for Australian farmers.
Dairy	Milk prices have moved higher locally with more upside to follow. Supply in New Zealand and the US recently fell short of Rabobank's expectations, driven by poor weather in New Zealand and feed pressures in the US.
Beef	Upward momentum taken out of cattle market as cattle supplies start to lift. Russia and Ukraine are minor beef trading regions, but cost increases from feed and energy will likely be also felt in Australia's beef sector.
Sheepmeat	A flush of lambs could hit the market in the coming months, which would see prices ease despite so far healthy US demand for heavy lambs.
Cotton	Cotton price fell from decade highs despite rising energy prices due to the war in Ukraine and sanctions on Russia. China's role in the conflict needs to be watched as it is the world's major cotton importer.
Wool	woolen suit import recovery to support EMI between AUc 1350-1500/kg over the next 12 months. China needs to be monitored, also in regard to its role in the Russia-Ukraine war.
Downstream Markets	Local food markets returning to normal post Omicron-peak, with labour and supply chain issues still to watch. Higher packaged food and meat prices flowing through but offset by falling fresh produce (particularly fruit).
Farm Inputs	We now expect global urea prices will increase again to levels just below the November peak for the next couple of months, before tapering once again by mid-year.
FX	We have retained our year-end forecast of USc 74. Rising commodity prices add even more inflationary pressure to the economy.
Oil	Local diesel prices are now at the highest levels they have been since 2008. Looking forward, we think prices will move higher, primarily driven by a rising price for Brent crude oil.

Ukraine Conflict

Russia-Ukraine crisis the impact outlook for agri

- The region is a massive export powerhouse for grains, oilseeds, fertilisers and energy.
- Price volatility is expected to remain high in the coming weeks and months.
- Ukraine export disruptions are largely priced in for the exports over the next three months, however the impact on 2022 crop production is unknown.
- A further escalation and recent heavy sanctions on Russia, which will disrupt Russian exports of grains, energy and fertilisers, is only to a limited extent priced in and could still drive prices up.
- A direct ban of Russian grains and oilseeds exports is unlikely due to humanitarian reasons, but indirect disruptions are occurring. Price increase likely for input costs due to energy and fertiliser price as their exports could also face direct sanctions.

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Ukraine in the Global F&A Context

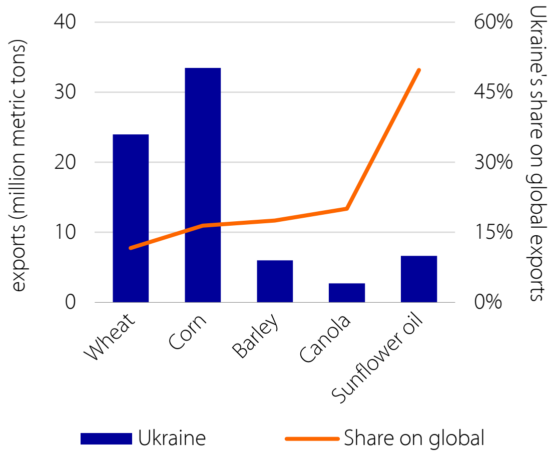
Ukraine is a major exporter of grain and oilseeds, while trade of meat, dairy and of farm input cost drivers like energy and fertilisers is minor.

- Ukraine ships per year almost 25mmt of wheat (12% of global trade), 35mmt of corn (16%), 6mmt of barley (18%), 3mmt of canola (20%), 7mmt of sunflower oil (50%), and 10% of the global walnut trade, and with it heavily impacts those global markets and global pricing.

Status Quo of Export sector:

- Exports are heavily disrupted or completely halted due to ongoing war also in the southern regions along the Black Sea coast where all the export terminals have closed.
- Unknown when exports will resume.
- Unknown if 2022 crop will be impacted. Wheat, canola and over half of barley are winter crops and are in the fields. Corn, sunflower and pulses planting will start as from April.
- The length of the war and the extend of the disruptions will be crucial to monitor.

Ukraine's G&O exports in a regular season



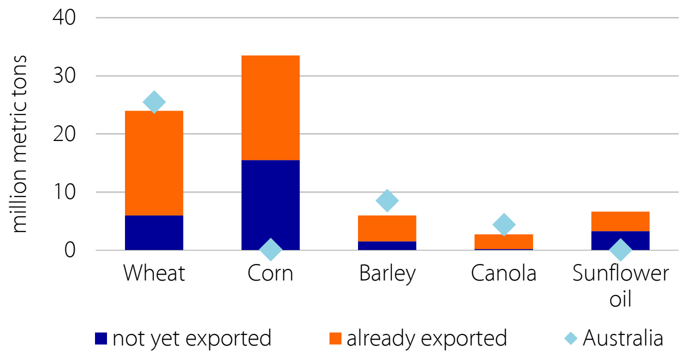
Key Black Sea G&O Ports

Ukraine Export Halt Priced In, Russian Sanctions Not Fully

Ukraine is a major exporter of grains and the conflict has driven prices higher, but the prices of inputs, including energy and fertilisers, are also volatile.

Ukraine is a heavyweight in grain and oilseed exports, but on its own not for fertilisers, dairy, meat or energy. It's share of global annual exports is 12% for wheat, 16% for corn, 18% for barley, 20% for canola and 50% for sunflower oil. It outranks Australia's current record crop and export volumes as it would have usually exported almost a similar amount of wheat this season compared to Australia, slightly less barley and corn, but also ships massive corn and sunflower volumes. However, as the country harvests its crops in the July-November period, large volumes have already been exported, leaving about 50% of the corn (~7mmt), 25% of wheat (~6mmt) and 50% of sunflower oil (~3mmt) still left in the country, which currently cannot reach the importers in the world. With a continued export stop out of Ukraine for the remainder of this season until their next harvest in the July to October period, we modelled a global wheat price increase compared to pre-crisis escalation period (i.e. late January 2022) of 30% (of which most has already materialised) and corn +20%

Ukraine: Exports in 2021/22 would have exceeded Australian



Source: USDA, Rabobank 2022

Impact on Australia of Ukraine export disruptions

- This scenario has already materialised as Ukraine exports have halted and heavy sanctions on Russia drive us to scenario B (next page).
- Ukrainian exports are expected to continue to be disrupted due to ongoing war, port closures and vessels avoiding the region. This will increase demand for Australian grains and those of other regions.
- Input costs (energy and fertiliser) are volatile due to risk premiums introduced as a result of our scenario B (see next page).
- Markets have already priced in a significant risk premium for grains and with it a further upside in prices is only to be expected if:
  - ***Sanctions on Russia,*** which effectively reduce exports of grains, fertilizer, and energy (see next page for more details) cut into Russian exports.
  - ***War in Ukraine continues for several more months and impacts the 2022 production.*** Winter crops (i.e. almost all of the wheat and canola and over half of barley) are in the fields and would need fertiliser/plant protection treatments only as from April before their harvest in July/August. Spring planting in April and May for corn, sunseed, spring barley and pulses is at risk.

Source: USDA, Rabobank 2022

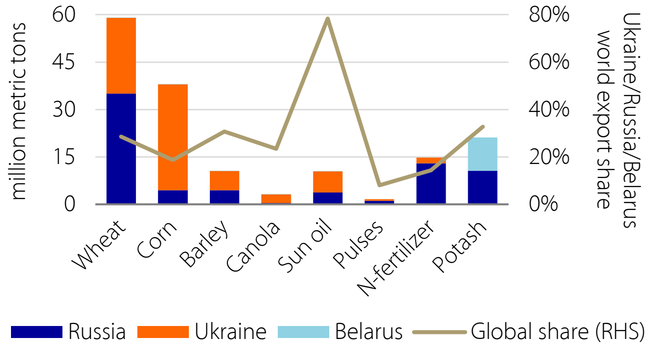
Heavy Sanctions on Russia Under Way and Drive Prices

So far Russian and Belarussian exports are not significantly disrupted. However, heavy sanctions could change this. While an outright ban of key staples like wheat and vegetable oil is for humanitarian reasons unlikely, recently introduced SWIFT sanctions are expected to have a severe impact on exports.

Countries around the world are imposing sanctions on Russia and potentially its ally Belarus. While it remains unlikely that a direct export sanction would be imposed on food staples, they can still get caught up heavily indirectly through two measures:

- SWIFT sanctions recently introduced by the EU and the US will cut deeply into the ability of Russia to receive international payments for its exports and could significantly limit the capability to pay for all exported goods including food, fertiliser and energy.
- Similar sanctions on Iran over its nuclear activities in 2012 limited Iran's crude oil exports by two-thirds and forced it three years later back to the negotiation table.
- Russia exports even more wheat than Ukraine. The combined Russian and Ukrainian wheat export volumes reach 60mmt per year, well over twice the volume Australia will ship in the current record season. Also, fertiliser exports are significant.
- Russia also exports 13% of the world's crude oil and 9% of natural gas, and disrupted exports will drive input prices, including, for example, urea and diesel.

Russia, Ukraine, and Belarus global export market share



Source: USDA, FAO, Rabobank 2022

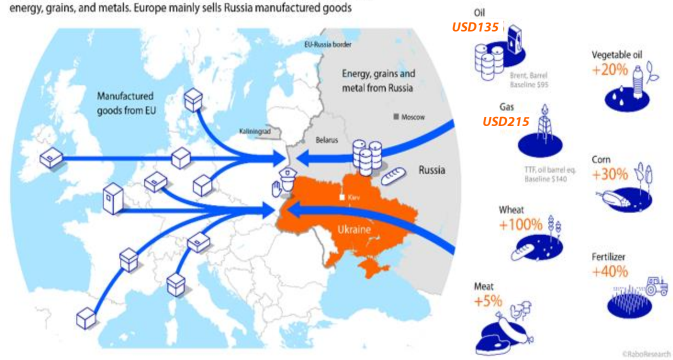
Impact on Australia of Russia/Belarus/Ukraine disruption

- This scenario has not yet materialized, but sanctions on Russia have significantly tightened. As a direct or indirect result, the trade from Russia, and potentially Belarus in the future, will be heavily slowed, in addition to the existing export stop in Ukraine.
- SWIFT sanctions might already have enough indirect impact on the grain, fertilizer, and energy trade to drive a disruption of exports from the region. A lasting disruption of trade flows from all three countries would trigger a massive price increase for grains as well as for inputs like fertiliser and diesel.
- So far introduced sanctions still allow for some Russian exports, but at much lower levels.
- Direct export restrictions on food staples are highly unlikely due to humanitarian reasons, while a restriction on energy and fertiliser might be a next measure. With it the risk for Australian farmers is that their output prices might not rise as dramatically, but input prices might face another strong upward push.
- A significant production impact of the 2022 crops to be harvested in Q3 2022 in Russia and Belarus is for now unlikely, while a production impact for Ukraine cannot be excluded as spring works including planting for corn, sunseed and pulses starts in April.

Price projection absolute or % change over Jan 2022 base:

Scenario B

Trade is disrupted between EU and Russia due to sanctions. Russia sells Europe energy, grains, and metals. Europe mainly sells Russia manufactured goods



La Niña May Have Peaked, Influence to Continue

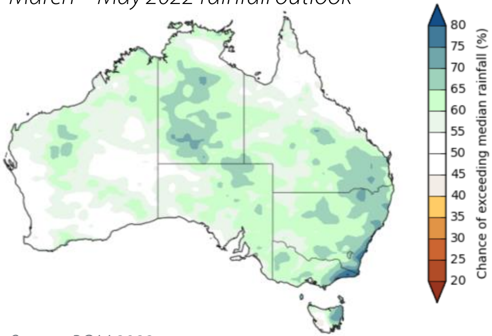
The Bureau of Meteorology (BOM) expects that a wet March is likely for large parts of Australia.

BOM expects the El Niño–Southern Oscillation (ENSO), will return to neutral during the autumn. Three of seven international climate models expect La Niña thresholds will be exceded during April and only two in May.

On the other side of the continent early indicators are that the Indian Ocean Dipole (IOD) is expected to stay neutral for the foreseeable future. One of five International forecasting models expect negative thresholds to be reached during July.

Chance of exceeding median rainfall is better than 50%

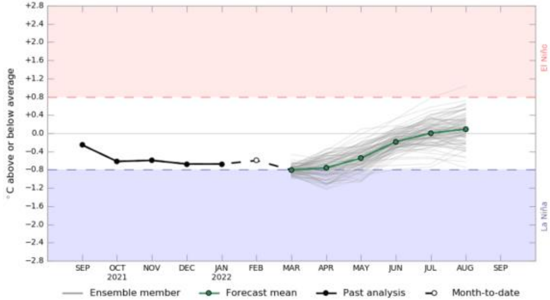
March – May 2022 rainfall outlook



Source: BOM 2022

La Niña event is coming to an end

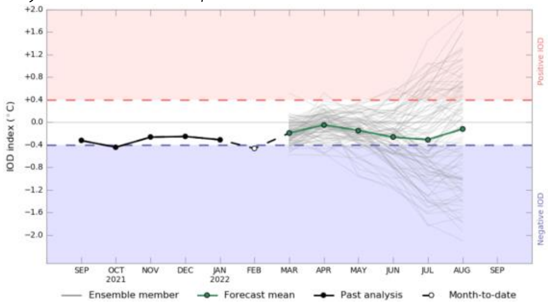
Monthly sea surface temperature anomalies for the central Pacific Ocean



Source: BOM 2022

IOD neutral

Monthly sea surface temperature anomalies for the Indian Ocean



Source: BOM 2022

Extreme Weather Galore

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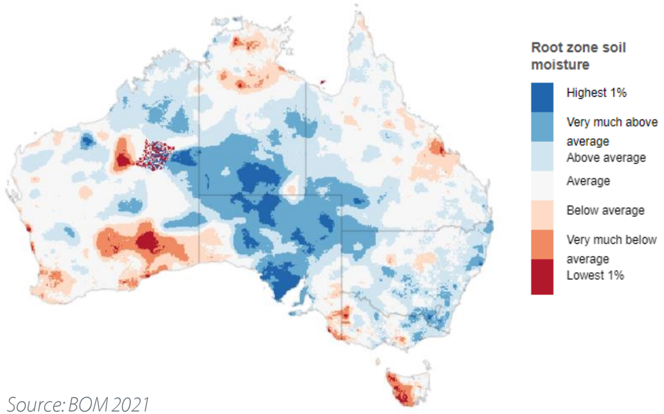
While La Niña may have peaked, heavy rain continued for parts of the east coast of Australia during February.

Flash flooding and heavy falls were prevalent across Northern New South Wales and Southeastern Queensland. Early in the month, heavy flooding was recorded in central south Australia which damaged some critical infrastructure.

On the contrary, it has been an extremely dry and hot start to the year on the west coast. Large fires destroyed a large amount of farming infrastructure, livestock and some homes. One fire burnt 45,000 ha of agricultural land.

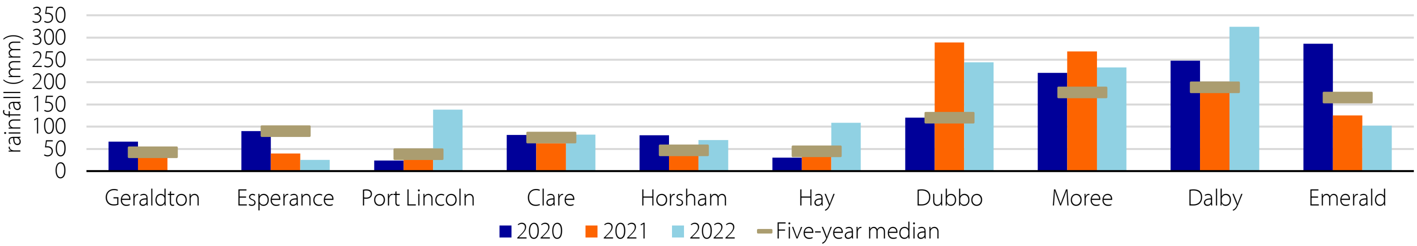
As we start to turn focus toward the winter production season, soil moisture is above average for most of the east coast of Australia.

Relative Soil Moisture, February 2022



Source: BOM 2021

Aug-Oct rainfall



Source: BOM 2021

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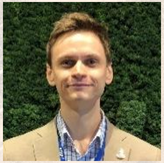

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Grains & Oilseeds

'What to Watch' Becomes Reality

Factors that were considered 'what to watch' in our Annual Outlook have materialised, and prices have rocketed, with CBOT wheat, corn, and soybeans up 33% MOM, 19% MOM and 9% respectively as of 2 March 2022. Uncertainty over trade and sanctions associated with the Russia-Ukraine crisis has come at the exact time when global markets are short of supplies and crop prospects are declining in some regions.

Rabobank's 12-month CBOT wheat price forecast has been increased to trade above at least USc 800/bu for the balance of the year, following the initial, and likely prolonged, disruption to Black Sea supply. The conflict has added to a world wheat market that already has tight stocks, where 70% of the US is experiencing some level of drought and where crops in South America are deteriorating. The world was counting on Ukraine for another 6mmt of wheat this season and demand will need to shift to alternate suppliers now that shipping from Ukrainian ports is suspended and Russian exports face sanctions.

Rabobank's 12-month CBOT corn forecast has also been increased, to trade above USc 600/bu for the balance of the year. La Niña is causing crop downgrades for a second year in a row for South America. Argentina is particularly at risk where soy and corn yields are in their most vulnerable growth stage. High inputs costs and yield declines will squeeze corn farmer profits and make corn farmers more restrained sellers. The Russia-Ukraine crisis is also adding to corn price upside, with 15mmt of Ukrainian corn (7% of world trade) still not exported this season. Volatility is to remain high.

Locally, we forecast for APW2 wheat in KWI to move above AUD 400/tonne in 1H 2022. Due to our large local crop, export constraints and positive prospects for 2022/23 crop, prices will not rise one-to-one with global levels at least in 1H, but still see upside, especially if the war continues to mid-year and sanctions or conflict prevents the world accessing the it's 'breadbasket'. The war will also see upside for barley, especially if China cannot access Ukrainian corn, and Canola given that Ukraine is the third largest canola exporter.

What to Watch

- ***Conflict length and how sanctions disrupt Russian grain exports:*** Due to near-term export disruptions, global prices are expected to escalate 30% from a CBOT base of Usc 750/bu, and possibly add much more price upside if both the conflict continues into the July Black Sea harvest window, and also if wheat out of Russia is not reaching the global markets anymore due to sanctions. The upside impact on Australian pricing is expected be more tame than global, and more details can be found in a just released report on the impact for Australian prices: 'When Black Sea Wheat is Caught in Conflict'.

Black Sea disruption expected to increase AU prices and demand

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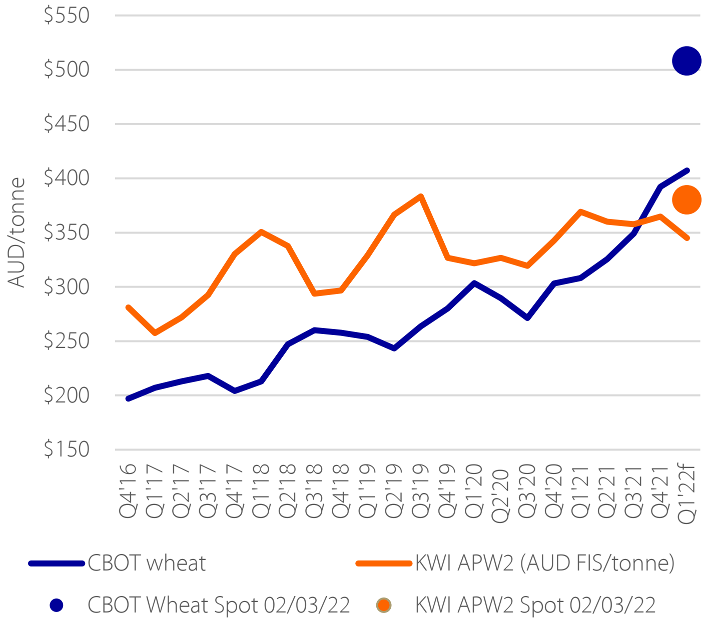
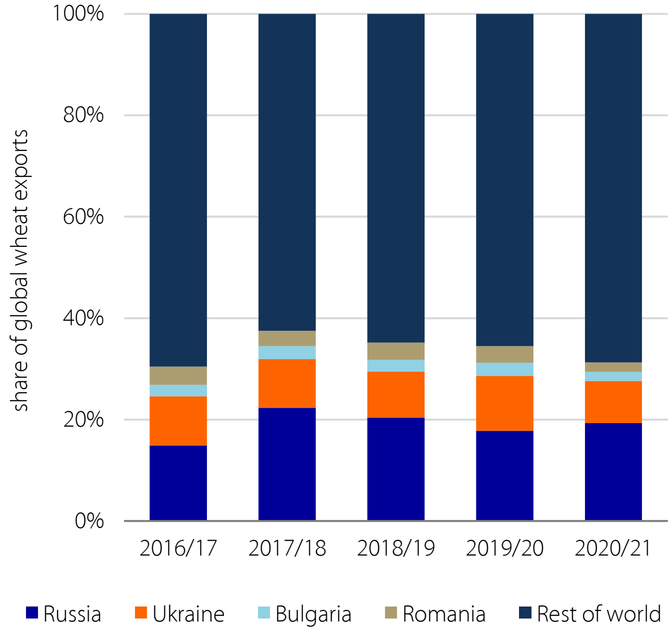
Russia-Ukraine crisis sees prices rocketing higher, with upside above base case likely



Source: Bloomberg, Rabobank 2022 – Quarterly prices except for spot price circles 02/03/22

High global dependence on Black Sea wheat exports means large impacts as access is limited



Source: USDA, Trade Map, Rabobank 2022

Commodity Basket to Boost Milk Prices

The milk supply situation in several key export regions continues to deteriorate. The latest milk production data releases in the US and New Zealand have been below Rabobank expectations. New Zealand milk production was down 6.1% in January. The worsening supply is driven by poor weather in New Zealand and feed pressures in the US.

As a result, Oceania commodity prices continued firm in February. All commodity prices posted gains in the month, with butterfat the best performing. Spot prices for Oceania butter and cheese are now in unchartered territory trading at record levels. The underlying dairy fundamentals will support the commodity basket in the short term

The firm commodity basket is helping lift farmgate milk prices in Australia's export region. In February, Fonterra Australia increased its average farmgate milk price for the 2021/22 season by AUc 20/kgMS (comprising AUc 17/kgMS of butterfat and AUc 24/kgMS of protein). This takes their weighted farmgate milk price to AUD 7.30/kgMS (backdated to July 1). Rabobank is anticipating more upside in milk pricing to come.

The profit pool of the Australian dairy industry is being squeezed. The latest earnings updates from some of the dairy companies provided a glimpse at the processing sector's performance. Higher milk prices were a drag on processing margins, but significant pandemic-related costs were also reported due to the Omicron wave early.

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Dairy

What to Watch

- ***Clouds from conflict in Europe.*** Russia is no longer a major importer of dairy. Following the sanctions introduced back in 2014, Russia has invested in local milk production capabilities. However, the impacts of conflict in Europe on the global dairy markets are multi-layered. Higher feed and fertiliser prices will only serve to limit milk supply growth in an already tight market. Higher energy costs pose further inflationary risks, which could impact discretionary dairy purchases in emerging markets.

New Zealand Milk Supply At Risk of Falling off a Cliff

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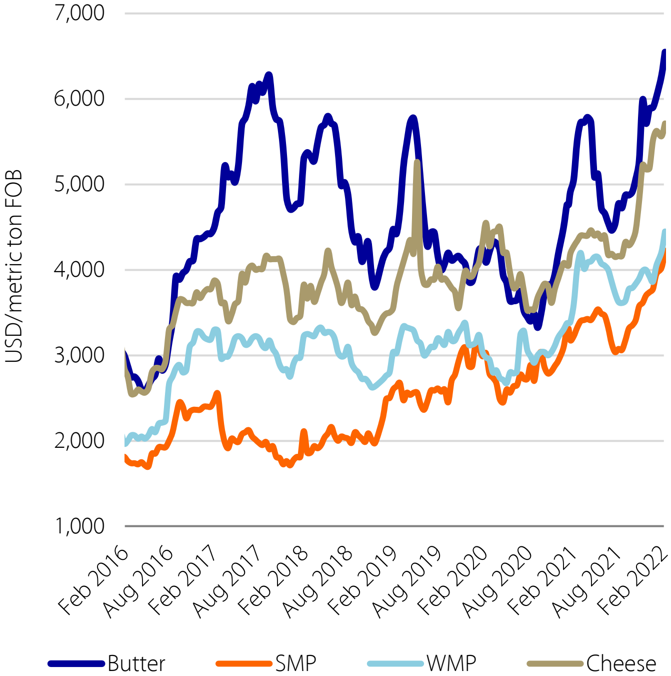
Global dairy prices, 2016-2022

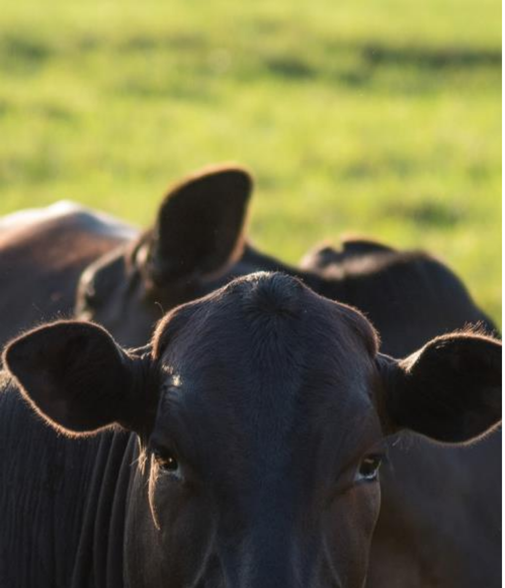


Source: USDA, Rabobank 2022

Production growth key exporting regions

	Latest month	Last three months
EU	-0.7% (Dec 21)	-0.6%
US	-1.6% (Jan 22)	-1.1%
Australia	-2.1% (Dec 21)	-1.3%
NZ	-3.6% season-to-date (January 2022)	

Source: Rabobank 2022



Volumes Pick Up, Prices Steady

Cattle prices have tacked sideways for much of late January through into February. The EYCI was sitting at AUD 11.23/kg on 24 February, after trading between AUD 11.15/kg and AUD 11.34/kg for the month of February. We did see saleyard cow prices jump in early February, but they have stabilised since. Likewise heavy cattle rose slightly, indicating there remains a shortage of these finished cattle. However, the feeder and restocker markets were more stable, suggesting there are more of these cattle flowing into the system and producer appetite is waning. ***Despite ongoing favourable seasons, the increase in young cattle numbers may well mean this is the top of the market.***

Slaughter numbers for 2021 (released in February) showed total cattle volumes (5.95m head) were down 17% on 2020 volumes and the lowest in 37 years. Encouragingly, male slaughter numbers in Q4 showed a 1% increase YOY following a 7% increase in Q3 – an indicator that the herd is rebuilding. The female slaughter proportion dropped to 43% – the lowest since Q4 2016 – also indicating the rebuild is in progress. East Coast weekly cattle slaughter numbers have started to pick up after a slow start to the year, but they still sit behind 2021 volumes. ***We expect numbers to slowly increase as more supplies become available.***

January beef exports (43,362mt swt) were down 13% YOY and were the lowest volume since January 2011. Volumes to Japan have been on a downward trend in the last couple of months as Japanese buyers contend with high prices and lower consumer purchasing activity. Australian live feeder/slaughter cattle exports were down 66% YOY and reached their lowest volume in over five years, reflecting the low availability of cattle and seasonal wet season transport difficulties.

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What to Watch

- ***Russia-Ukraine conflict***. Russia plays a much smaller role in global beef trade than they did six years ago – in 2013 Russia accounted for 13% of global beef imports, in 2020 it accounted for 2%. As such we are expecting minimal direct impact on global beef trade as a result of the conflict. However, there are likely to be indirect impacts in the form of higher costs (feed and energy) and any imposition of secondary sanctions may have wider implications.

Upward Momentum from Cattle Prices May Have Reached a Peak

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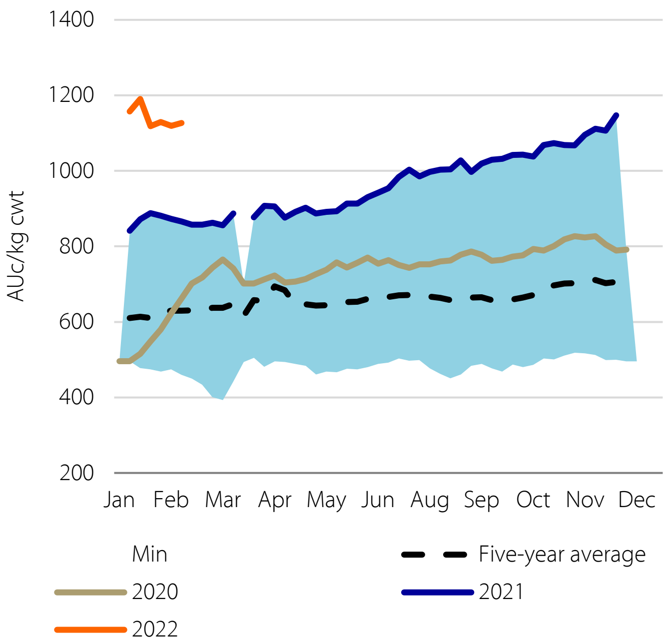
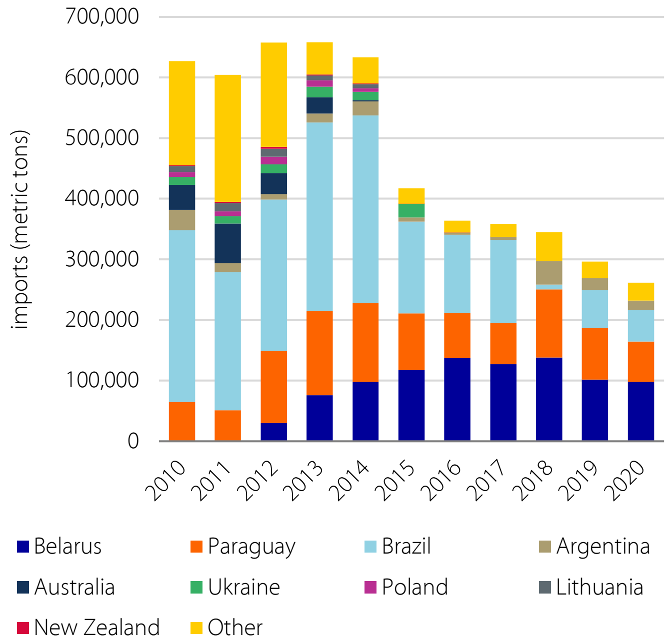
EYCI steady, this could be the top of the market



Source: MLA, Rabobank 2022

Russia is a much smaller player in the global beef market than a decade ago



Source: ITC Trade Map, Rabobank 2022

Sheepmeat

Increased Volumes, Prices Easing

For lambs held over from late last year, higher volumes through early 2022 and a bit of a dip in prices can be expected. The ESTLI has seen a general easing from the peak in late January and was at AUD 8.29/kg on 17 February. Despite favourable seasonal conditions through 2021, slaughter numbers in late 2021 and through January 2022 were some of the lowest in the last ten years. Coupled with the very strong US demand at the moment, which is supporting prices of heavier lambs, ***we may find a number of lambs carried through to heavier weights and a lift in volumes over the coming months with a corresponding dip in prices.***

Lamb slaughter (20.6m head) for 2021 (released February) showed a 3.9% increase on 2020 numbers. Average carcase weights were unchanged at 24.4kg, which are the heaviest lambs we have produced in history. Sheep slaughter declined a further 8% in 2021 reflecting the ongoing rebuild of the sheep flock. east coast weekly slaughter numbers have picked up in February after starting 2022 slowly, although they remain below the five-year average. Victorian lamb slaughter numbers were up 17% for weeks six and seven of 2022 compared to the same period in 2021.

Lamb exports in January (17,057mt swt) saw a big lift (25%) compared to January 2021. This increase was driven by YOY lifts to China (up 29%) and the US (up 35%). US import prices remain very strong although they have plateaued recently, suggesting there may be limited upside as the US heads into their big lamb consumption months around Easter.

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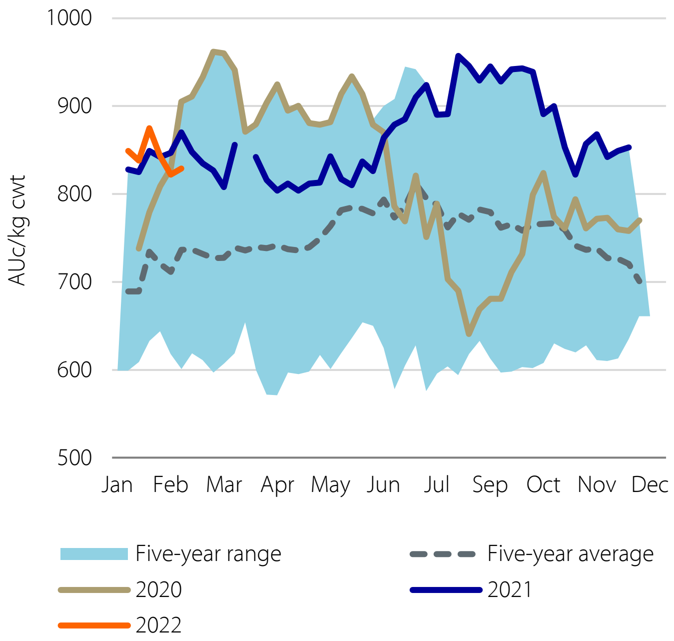
What to Watch

- ***Russia-Ukraine conflict***. Russia plays a much smaller role in global sheepmeat trade than they did six years ago. Australia exported 118mt of sheepmeat to the Commonwealth of Independent States in 2021, down from the 5,669mt in 2013. As such we are expecting minimal direct impact on global sheepmeat trade as a result of the conflict. However, there are likely to be indirect impacts if economic growth were to contract and any imposition of secondary sanctions may have wider implications.

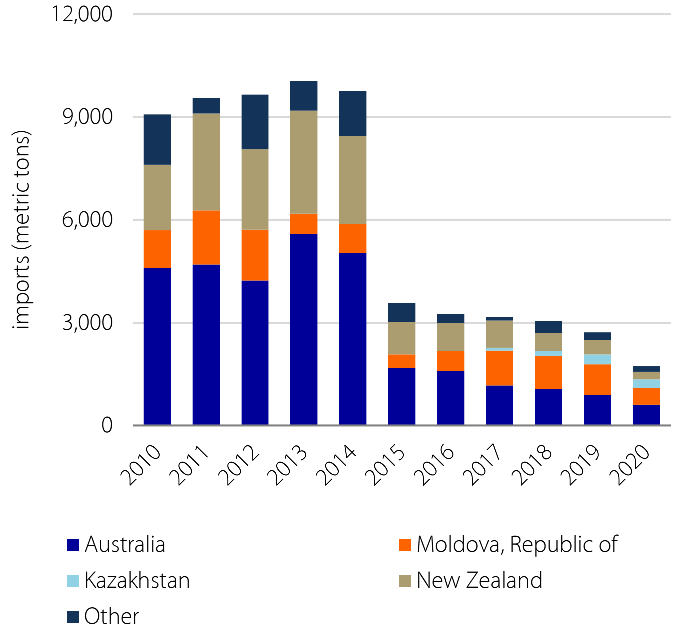
Some Carry Over Lambs May See Volumes Increase and Prices Ease

Lamb prices easing into the new year



Source: MLA, Rabobank 2022

Russian sheepmeat imports now much smaller than they were seven years ago



Source: ITC Trade Map, Rabobank 2022

Cotton Going Against the Grains

While the Russia-Ukraine conflict has moved energy and grains markets higher, cotton found its way lower in February on uncertainty and some closing of long positions. From 11-year highs in early February, ICE #2 lost 3% this month to finish around USc120/lb, but this move down keeps it still in territory not seen for 11 years, and 62% above the five-year average.

Russia and Ukraine, and the Black Sea region more broadly, do not figure highly in global cotton trade patterns. However, ***the sector remains prone to flow on impacts from already factored in, and potentially stronger, price increases for fertiliser and energy. Moreover, long-term impacts on demand through higher inflation*** will also be weighing into market positions.

If sanctions already in place broaden to include those who remain on trading terms with Russia, which could include China, then we will see considerable downside risk for cotton markets. If the world's largest importer is not able to source cotton from the US and Australia, this will put huge anticipation on how Brazil would move and open up holes in China's import program during the year.

Meanwhile there are questions on US production – the USDA has put out its first forecast for potential production in 2022 – 18.2m bales up 3.2% YOY. However, continuing La Niña conditions in the southern US, is delivering extreme dryness into the important cotton-growing regions of northwest Texas and into Oklahoma ahead of April planting, so that a YOY production lift would seem unlikely.

The Australian production prospects remain very positive. Flooding in northern NSW and southern Qld is a factor to watch as we open March, and it will be the period of inundation that is key to watch for potential losses. Locally, pricing around AUD 800/bale is still on offer for 2022, and 2023 still around AUD 650/bale. We continue to see ***2022 Australian cash prices trading lower over 2022 but remaining above AUD 700/bale in 1H and above AUD 600/bale in 2H.***

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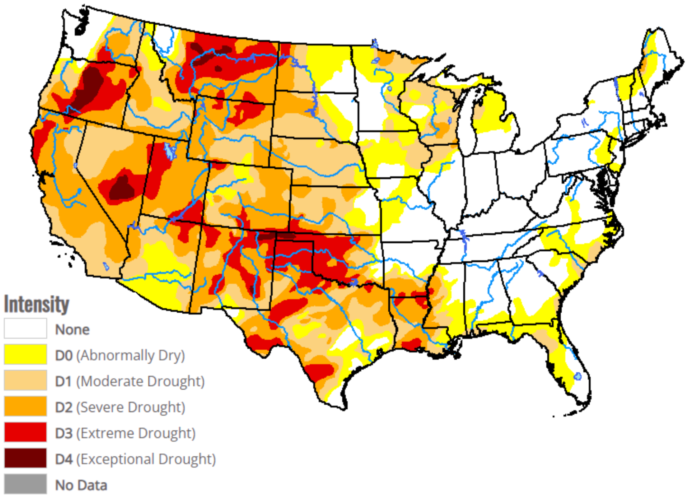
Cotton

What to Watch

- ***Sanctions*** – Should US sanctions be expanded to countries that choose to still trade with Russia, the US, and other allies, including Australia, would no longer be able to export cotton to China. This would cause a severe drop in ICE#2. However, ongoing access to cotton imports would be a key in China's considerations of how to play its cards under in the current circumstances, given how important the cotton milling and textiles sector is to China.

Question Marks on Cotton Supply

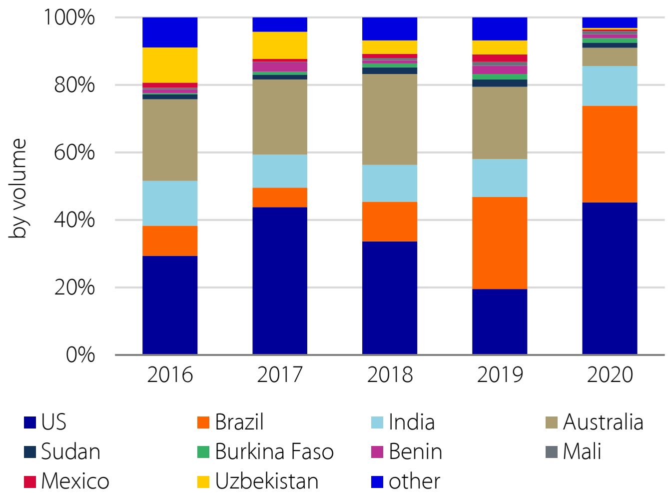
Dry south ahead of US cotton planting puts question marks on USDA's recently released Outlook Forum prediction of 18.2m bales for 2022



Source: US Drought Monitor, 24 February 2022

There are question marks on Chinese import supply if US sanctions are extended to those supporting Russia

China's cotton imports by origin



Source: TradeMap, Rabobank 2022

We continue to see 2022 Australian cash prices trading lower over 2022 but remaining above AUD 700/bale in 1H and above AUD 600/bale in 2H.

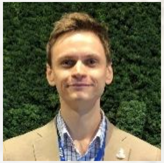
Positive Price Outlook for 2022

Rabobank continues to see upside for fine and mid micron wool prices through this year as demand for woolen apparel, particularly suits, picks up. The Eastern Market Indicator increased 2% MOM as of the 24 February at 1421c/kg, 17 micron rose an entire 6% MOM while coarser wool remained mostly unchanged. Rabobank still expects the EMI to trade between AUc 1350-1500/kg through 2022.

The big demand side story is US woolen suit import volumes in December rising to only 11% below pre-pandemic December 2019 levels. The closest we've seen to pre-pandemic levels since Covid-19 started. Retail apparel sales in the US also continued at very strong levels, recording 17.3% and 16% growth in excess of 2019 levels across December 2021 and January 2022 respectively. January retail apparel sales in the UK were lower than December 2021, when compared to 2019 equivalent months: -12.4% in January 2022 versus -5.7% in December 2021. With looming interest rate rises and further withdrawal of economic stimulus, consumer confidence in key markets continues to soften. The Langer US Consumer Comfort Index shows end of January results already 33% below it's August 2021 pandemic recovery highs.

December 2021 Australia wool exports volumes (29.98m kg) were up 8.6% on December 2020 levels. Trade concentration with China increased to almost 80% in December, up from 76.7% in November, with the share of wool exported to India and Czech Republic declining MOM.

National wool tested data for January shows the weight of wool tested down 6.5% MOM and down 13% YOY. Higher costs of freight continues to create challenges for buyers from foreign markets, and the issue is expected to continue through the rest of 2022, particularly 1H 2022.



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Wool

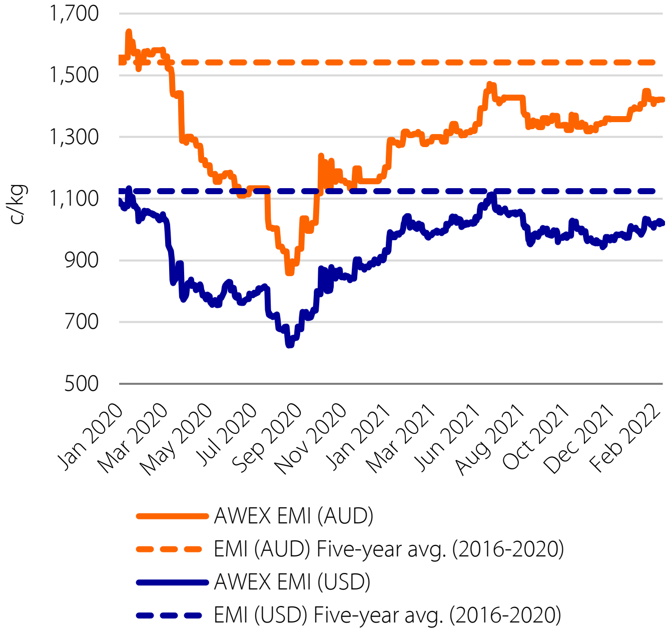
What to Watch – Interest rates and secondary sanctions

- ***US Interest rates:*** central banks are starting to ready markets for rising interest rates. If rates rise too quickly, consumer spending will drop and weigh on wool. We still believe the recovery in woolen suits demand will be the larger positive factor, but it is still a very big 'what to watch' factor.
- ***Trade Sanctions***: Rabobank's latest report 'How We Would Pay for the War' outlines the possibility of secondary sanctions on countries who do not follow western sanctions on Russia. If China falls into this basket, we will have to watch for trade developments and any impact on wool.

EMI Looks for Higher Ground as US Woolen Suit Imports Head Higher

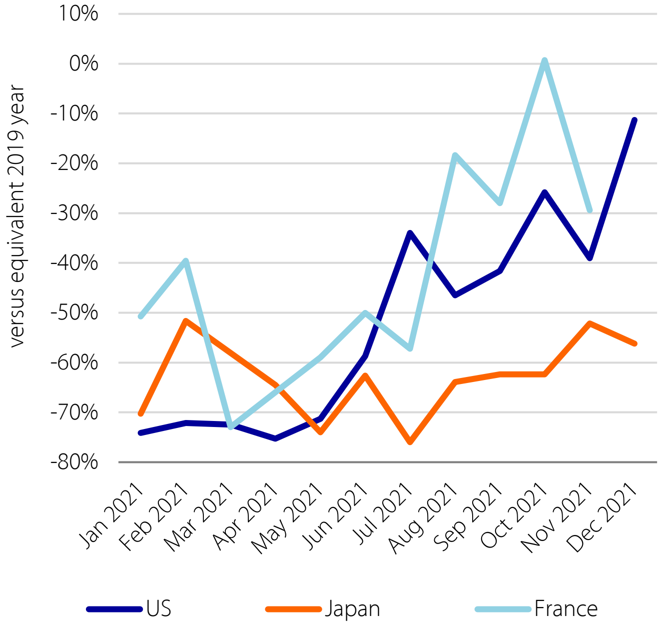
Rabobank

Most major apparel markets see an improvement moving in September



Source: Bloomberg, Rabobank 2022

US woolen suit imports to the rescue! December 2021 Imports only 11% below pre-pandemic levels



Source: TradeMap, Rabobank 2022

Downstream Markets

Record-setting Omicron Wave Hits

The Australian food supply chain started 2022 with unprecedented disruptions. A significant Omicron wave placed the food system under pressure. Workforce shortages led to inefficiencies in retail stores, distribution, and transportation (as well as manufacturing). During the wave, there was a spike in Covid-related costs, which continue to linger.

Locally daily cases numbers have fallen, and restrictions are easing. As a result, the local operating environment for the food supply chain is on the way to normalisation as the wave now subsides and restrictions ease.

Globally, there is a keen eye on inflation with headline numbers surging. Food and beverage companies are witnessing inflationary pressures across all aspects of their businesses. Some of this is being passed through to consumers. Inflationary pressures are expected to intensify in the months ahead, particularly due to rising energy markets.

Closer to home, the latest updates from Australia's major food retailers highlighted higher packaged food and meat prices flowing through but offset by a fall in the price of fresh produce (particularly fruit).

Key export markets still face headwinds. Across Southeast Asia, Omicron is still impacting a number of economies. As a result, some countries have reinstated strict containment measures in the face of Omicron waves, which will be a drag on food and beverage markets in the short term.

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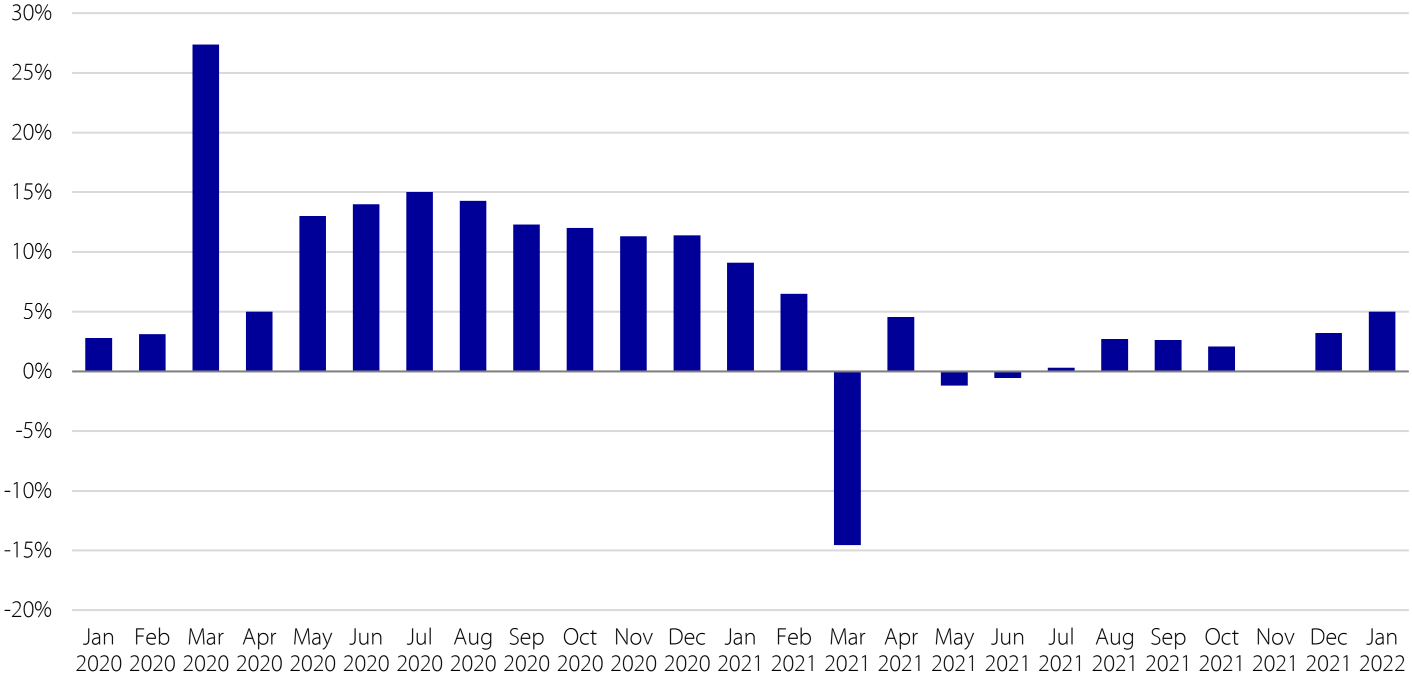
What to Watch

- **Thrifty consumers.** The purchasing decision and discretionary spending from consumers will be a fascinating watch in the months ahead in all economies. All households are facing cost-of-living pressures and waning confidence. The global economy is losing some steam, meaning income growth potentially slows. How households react with their food purchases will vary greatly, but many will likely be a little more thrifty in their spending.

Grocery Sales Elevated by Omicron Wave

YOY change in Australian food retail and foodservice sales



Sources: Australian Bureau of Statistics, Rabobank 2022

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Farm Inputs

About to Get Uglier

Russia's invasion of Ukraine has put a major dent in the likelihood of local urea prices significantly declining ahead of the winter and spring application period. We now expect global urea prices will increase again to levels just below the November peak for the next couple of months, before tapering once again by mid-year.

Fertiliser markets are likely to be impacted by the crisis in three ways:

1. ***Export capacity:*** Russia itself is a major exporter of fertilisers, especially of ammonium nitrate (46% of global exports), ammonia (23%), urea (15%) and mono-ammonium phosphate (MAP) (14%). With the addition of Belarus, a total of 40% of global Muriate of Potash exports come from the region.

   Although we are yet to see any official sanctions on fertilisers, the impact of other sanctions, such as the removal of Russian Banks from the SWIFT payments system, is highly likely to reduce the ability of importers to purchase products, even if they could get it out of the region (see 2).

2. ***Port Access:*** Many ports across the Black Sea region are now closed. Shipping lines are also avoiding Baltic ports due to the high war insurance premiums and the risk ships may get stuck in the region.

3. ***Gas Supply:*** The Nord Stream 2 pipeline has been halted and EU gas prices again have escalated. Russia typically supplies about one third of the EU's natural gas. Given natural gas is the main feedstock for urea, high natural gas prices may elevate urea prices once again.

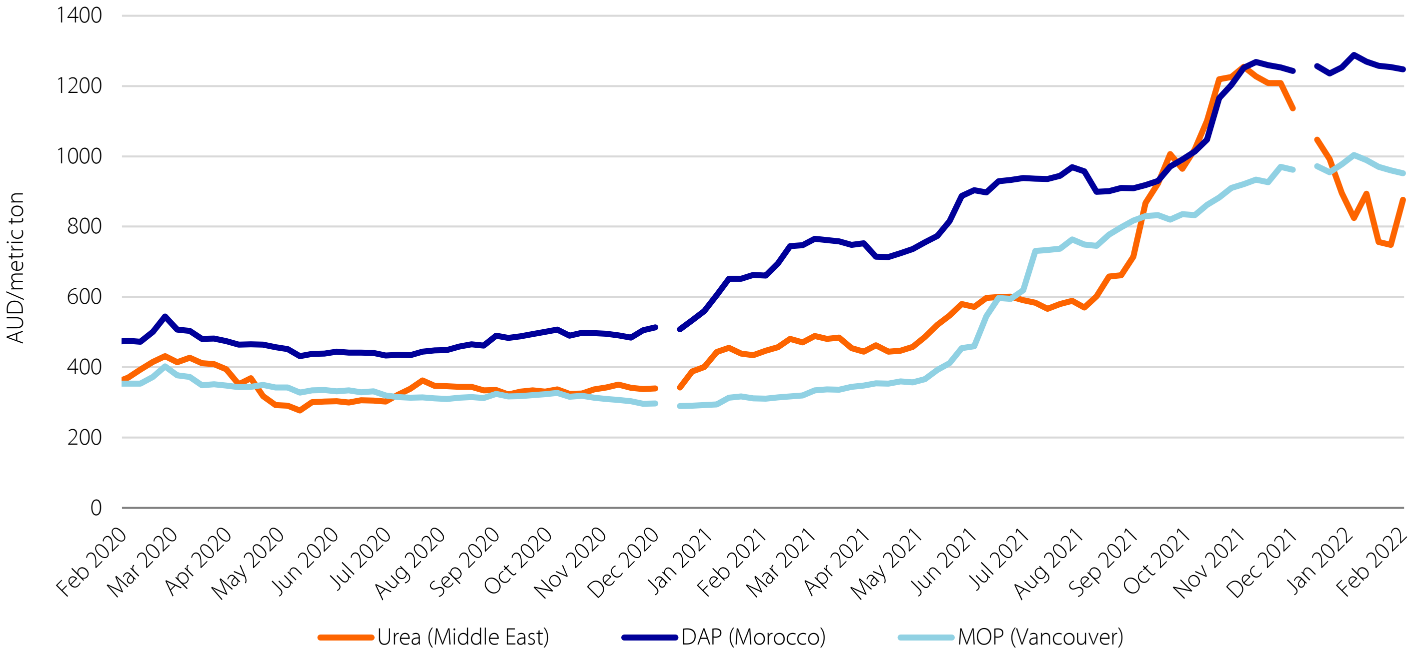
What to Watch

- ***Prices versus Supply Risk.*** It is clear there is much uncertainly regarding the full extent of this war on fertiliser prices. Between 22 and 24 February, offers for single urea cargoes from the Middle East increased from USD 600mt FOB to USD 730mt FOB. Depending on the outcome of peace talks taking place this week (week of 28 February), prices may keep going on a similar trajectory. For local farmers, price risk must be assessed against the increasing supply risk for the upcoming application season.

Global Urea Prices Have Begun to U-turn Upwards

Rabobank

AUD-adjusted global fertiliser prices



Source: CRU, Rabobank 2022

AUD: Patience

The AUD is above early February levels, currently trading at USc 73. In view of the buoyancy of the Australian economy in addition to commodity price strength, we have retained our year-end forecast of USc 74.

- The impact from escalations in Ukraine and sanctions on Russia on the local economy will be relatively mild. Bilateral trade between Australia and Russia is limited. Exports to Russia are ranked 29th in terms of export value and 56th in terms of imports, both less than 0.2% of total exports/imports.
- The largest impact will be from the rise of commodity prices, which add even more inflationary pressure to the economy. December inflation figures came in at 3.5%, with underlying inflation creeping up towards 2.7%, inching closer towards the upper tolerance band of the RBA.
- Much of the inflation is cost driven, and the RBA is poorly equipped to fight 'cost-push inflation'. In case the RBA pulls the trigger on raising interest rates too soon to temper inflation, it would be counterproductive. It would only contribute to already eroding demand, providing a 'double whammy' to the economy. Hence, the RBA would be wise to focus on the developments of fundamentals in the Australian economy.
- One of the fundamentals that currently draws much attention is wage growth. Governor Lowe continues to express his ambition that wage growth needs to be significant (around 3%) before inflation can sustainably stay within the 2 % to 3% target. And the RBA is ready to be 'patient'.
- Looking ahead we expect the economy to accelerate from the second quarter onwards. The absence of government-imposed restrictions and propped up savings will contribute to higher demand, especially in the service sector as people are making up for lost experiences post-pandemic. Moreover, we expect further tightening of the labour market over the course of 2022, setting new historic lows, further fuelling wage growth towards RBA's desired level.

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FX

What to watch:

- Historically, the AUD has been the 'higher risk' currency within the G10 basket. More recently, the spread between Australian bond yields and those in 'core' G10 markets has fallen. Additionally, Australia runs a current account surplus. The AUD's sensitivity to current risk events would appear diminished as Australia is a commodity exporter.
- Traditionally, commodity exports would come under pressure when a 'risk event' is sparked. This logic is currently in turmoil. Supply chain disruption and strong rebounds in demand following the pandemic had already underpinned commodity prices. Given that Australia is a large exporter of coal (a substitute for oil) and a producer of LNG suggests that the AUD should find additional insulation if energy prices remain elevated.

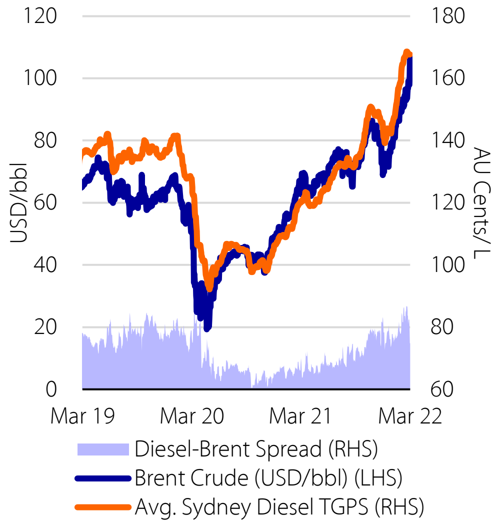
Room for Diesel to Move Higher

Local diesel prices are now at their highest levels since 2008. Looking forward, we still think prices will move higher, primarily driven by a rising price for Brent crude oil, which we expect to reach USD 118/bbl by mid-year.

The crisis in Ukraine is one predominant factor driving oil prices higher, driven by concerns of Russia's ability to export. Furthermore, market volatility and inflationary concerns have continued to attract investors toward commodities, which has further supported Brent crude.

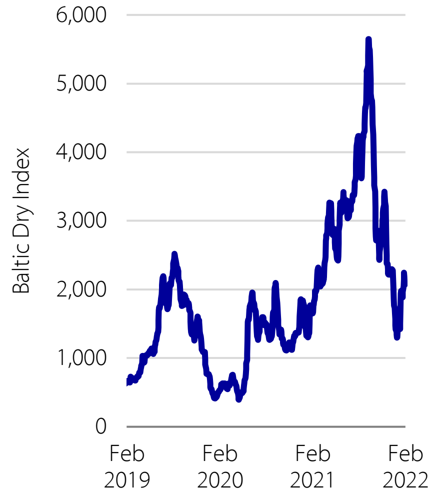
Aside to all the major headlines on the Ukraine crisis, there is one potential downside factor looming. There are reports that a new US-Iran nuclear deal is forthcoming, which may bring short-term negative sentiment to prices, if announced.

Brent crude oil & Average Sydney Diesel, Mar 2019-Mar 2022



Source: AIP, Bloomberg, Rabobank 2022

Baltic Dry Index, Feb 2019-Feb 2022



Source: Bloomberg, Rabobank 2022

Agri Price Dashboard

28/02/2022	Unit	MOM	Current	Last month	Last year
Grains & oilseeds					
CBOT wheat	USc/bushel	▲	843	786	655
CBOT soybean	USc/bushel	▲	1,590	1,470	1,405
CBOT corn	USc/bushel	▲	660	636	556
Australian ASX EC Wheat Track	AUD/metric ton	▲	382	370	296
Non-GM Canola Newcastle Track	AUD/metric ton	▲	893	766	600
Feed Barley F1 Geelong Track	AUD/metric ton	▲	302	293	240
Beef markets					
Eastern Young Cattle Indicator	AUc/kg cwt	▲	1,127	1,119	858
Feeder Steer	AUc/kg lwt	▲	609	602	445
North Island Bull 300kg	NZc/kg cwt	▼	590	605	500
South Island Bull 300kg	NZc/kg cwt	▼	575	590	460
Sheepmeat markets					
Eastern States Trade Lamb Indicator	AUc/kg cwt	▼	829	875	848
North Island Lamb 17.5kg YX	NZc/kg cwt	▼	835	860	650
South Island Lamb 17.5kg YX	NZc/kg cwt	▼	825	840	635
Venison markets					
North Island Stag	NZc/kg cwt	▲	795	715	530
South Island Stag	NZc/kg cwt	▲	785	715	545
Oceanic Dairy Markets					
Butter	USD/metric ton FOB	▲	6,550	6,025	5,063
Skim Milk Powder	USD/metric ton FOB	▲	4,225	3,950	3,225
Whole Milk Powder	USD/metric ton FOB	▲	4,450	4,050	3,600
Cheddar	USD/metric ton FOB	▲	5,713	5,625	4,275

Agri Price Dashboard

28/02/2022	Unit	MOM	Current	Last month	Last year
Cotton markets					
Cotlook A Index	USc/lb	▼	135.2	135.9	95
ICE No.2 NY Futures (nearby contract)	USc/lb	▼	122.1	123.8	88
Sugar markets					
ICE Sugar No.11	USc/lb	▼	18.0	18.2	17.53
ICE Sugar No.11 (AUD)	AUD/metric ton	▼	541	563	426
Wool markets					
Australian Eastern Market Indicator	AUc/kg	▲	1,421	1,407	1,306
Fertiliser					
Urea	USD/metric ton FOB	▼	580	869	375
DAP	USD/metric ton FOB	▲	858	810	580
Other					
Baltic Dry Index	1000=1985	▲	2,076	1,381	1,675
Brent Crude Oil	USD/bbl	▲	98	90	66
Economics/currency					
AUD	vs. USD	▲	0.718	0.699	0.771
NZD	vs. USD	▲	0.669	0.655	0.723
RBA Official Cash Rate	%	•	0.10	0.10	0.10
NZRB Official Cash Rate	%	▲	1.00	0.75	0.25

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