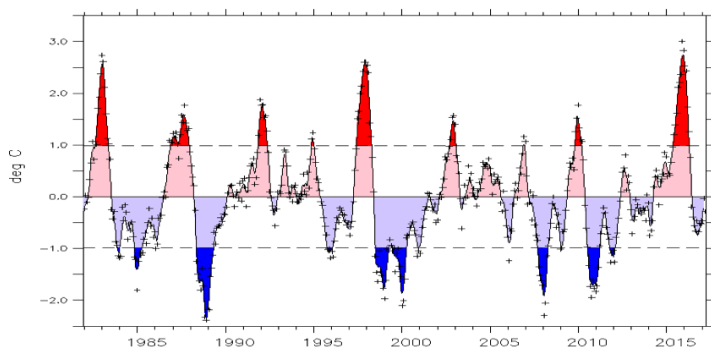


2016/17 – The Season of Records

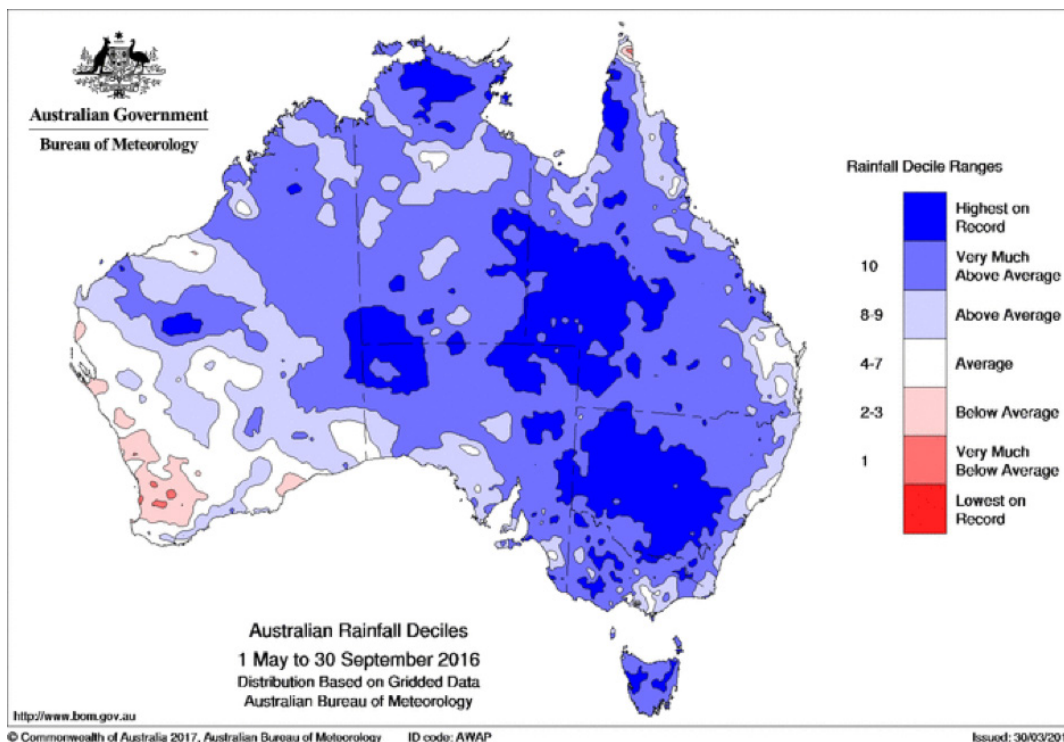
The 2016/17 season started on the back of a record strong El Nino Sea Surface temperature event in the Pacific Ocean. This weather pattern eventually broke down and led to a La Nina, which served Australian growers well, with above average rainfall for the majority of growing regions. As a consequence, records were set for both wheat and barley production. As the marketing portion of the 2016/17 season progresses, we now see a record export pace across Australia.

Figure 1: Pacific Ocean Sea Surface Temperatures



Fears of the 2015 El Nino impact evaporated almost as quickly as the weather pattern itself. A mild La Nina formed in 2016 which proved to be highly supportive for Australian winter crop production. For example, South Australia recorded its fourth wettest year on record. All growing regions notched double digit percentage gains on the average rainfall. The final culmination was the wettest May – September on record.

Figure 2: 2016 Australian rainfall decile map



Rain makes grain

The February 2017 ABARES update stated “total Australian winter crop production is estimated to have increased by 49 percent in 2016/17 to 58.9 million tonnes.” The report goes on to state yields “reached unprecedented levels in most growing regions.” Wheat achieved a record high production of 35.1 million metric tonnes (MMT), barley set a record of 13.4MMT, chickpea production set a record of 1.4MMT and canola matched the previous record of 4.1MMT.

The big yielding season saw a significant increase in canola oil content with reports of up to 50% oil. Unfortunately, cereal quality didn't fare as well, with the the normal APW1 quality being reduced to ASW1 in many cases. In South Australia, ASW1 deliveries made up over 40% of Viterro receivals.

Pricing reacts to large southern hemisphere wheat production

Australia and Argentina both experienced a 40 percent (plus) increases in production. As a consequence, pricing continued to fall over the harvest months of October through January. Off shore markets also reacted to the pricing of these large crops, with the benchmark CME futures markets seeing season lows through the month of December.

Figure 3: CME Wheat Future for May 2017 Delivery



Australian exports for wheat and barley surge

The high yielding and lower priced 2016/17 season created the perfect scenario for a strong year on year increase in exports for most winter crops. After a late harvest for most regions, exports really fired in January. Wheat exports totalled a record 2.53MMT for the month. Barley also set a record at 1.04MMT. In February, barley exports increased yet again to 1.12MMT. Wheat decreased to a still very strong 2.37MMT. At the time of writing, barley is on track to set a new season total for exports at 7–7.5MMT. If wheat can maintain the current pace we should see 23–25MMT exported.

The dramatic pace of Australian cereal exports is largely a function of price. In particular, price against our competitors in regions such as the Black Sea, North America and to a lesser extent Europe. For the last three years, Black Sea wheat has been the lowest cost wheat origin, a result of three banner seasons in a row. Since 2012/13 to now, Russia has increased wheat production from 38MMT to 73MMT. The increase of 35MMT over this period led to Russia being the world's largest exporter for 2016/17.

Can the Russian production streak continue?

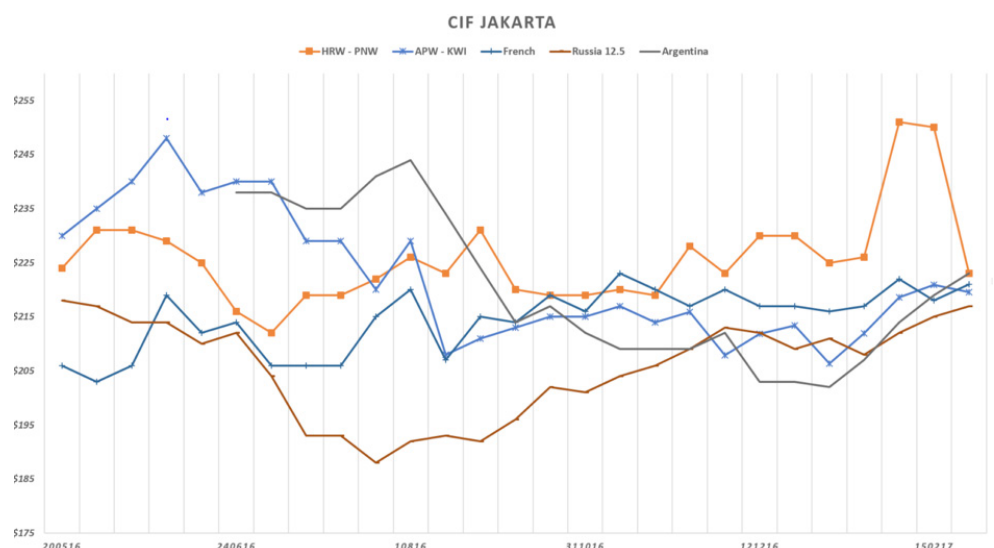
The marketplace expects a slight increase in the acreage planted in Russia this season. However, the critical factor to watch over the next two months as wheat exits dormancy and looks for benign conditions to mature, is the weather. At the time of writing, Russian rainfall has been relatively normal. The outlier is March, where they saw a decline in rainfall deciles and a sharp increase in temperatures.

It is worth noting other Black Sea and European producers have experienced a dryer and warmer than usual season. France is currently at approximately 75% of their annual rainfall for the season, Italy at approximately 77% and Spain at 66%. If these weather trends continue, there is no doubt yield penalties in production will be faced.

Impact on Australian exports and pricing

The below chart shows the relative pricing of major wheat exporters into Indonesia, a major wheat importer. The chart follows pricing between May of 2016 and March of 2017. HRW is representative of the United States. Argentinian values are tracked and we will use the APW ex Kwinana in WA for simplicity sake. The noteworthy item is the impact of last season's big Russian harvest on pricing. Over July – August, a large Russian crop acted as an anchor on world values into key destination markets. As a consequence, Australian and Argentinian values dropped to remain price competitive.

Figure 4: Matrix of multiple origin wheat values



Another big Black Sea crop having a similar impact when it comes to market for pricing, is a risk for the second half of this marketing season.

How does the season of records end?

As we have seen, 2016/17 showed us weather can take a positive turn and reward with yield in a low priced environment. However, just as easily it can turn against. Over the next three months, we look to the northern hemisphere for guidance on where supply will be produced and sourced. From there, the function of the marketplace will be to price grain correctly in each region, either for consumption or carry out.