

# Agricultural outlook for 2001-02 and farm performance estimates for Gippsland

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*With 60–70 per cent of Australian agricultural production exported each year, developments in world markets, and progress in negotiating expanded market access and reductions to policy induced distortions to production and consumption in major markets, will be crucial to the future prosperity of the farm sector.*

*Slower economic growth in the United States, Japan and east and south east Asia is expected to dampen demand for Australia's commodities in the near term. However, improved economic growth in 2002 and a weak Australian dollar are expected to underpin returns to Australian farmers.*

*Forecast further improvements in prices for beef, sheep meats, dairy products, wheat and canola indicate another strong financial performance from the Australian farm sector in 2001-02.*

*Farm cash incomes of Victorian broadacre (grains, sheep and beef) farmers are estimated to have averaged 26 per cent higher in 2000-01. However, in the Gippsland region of Victoria, increased livestock purchase costs offset the gains from higher cash receipts, resulting in little change to farm cash incomes. Dairy farmer incomes in the Gippsland region are estimated to have increased in 2000-01, but rose by less than the average for all Victorian dairy farms.*

ABARE project 1193

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## World economic outlook

Over the past nine months, world economic growth has eased significantly from the high achieved in 2000. Following the global economic slowdown, weaker demand for commodities and a subdued outlook for world economic growth have resulted in a significant reduction in prices for many commodities on world markets, particularly prices for mineral and energy commodities. However, prices of many agricultural products, such as grains, beef, wool and dairy products, remain firm.

A major factor underlying the strength of agricultural prices is a tightening of supply in major world markets. Despite a modest weakening in demand, world production, as well as stocks, of many agricultural commodities have declined significantly over the past few years. While a tightening of supply has so far provided support for many agricultural prices, a prolonged weakening of world economic growth could lead to significantly lower prices on world markets. In such an event, and in the absence of a marked increase in demand, there could be considerable downward pressure on prices.

In the short term, the prospects for world economic growth remain dependent on developments in the United States, the world's largest economy. Over the past year, significantly weaker economic growth in the United States has adversely affected economic activity in other parts of the world, leading to a marked slowing of global economic growth in 2001. In addition, following the terrorist attacks on New York and Washington in September, indications point to some short term instability in the US economy.

In Asia the economic outlook has weakened significantly. The United States is a major export destination for Asian countries, taking around 20–30 per cent of the region's exports. Since early 2001, significantly weaker economic growth in the United States has sharply reduced its demand for imports from Asia. Similarly, economic performance in Latin America has also weakened as the recent financial problems in Argentina have influenced activity in a number of neighboring economies, including Brazil and Chile.

It appears likely that world economic growth will strengthen in 2002, supported by an expected partial recovery of US economic growth. World economic growth is assumed to be 2.4 per cent in 2001, before strengthening to 3.3 per cent in 2002. This compares with growth of 4.4 per cent in 2000.

However, there is considerable uncertainty about the economic outlook. The key risks stem from the US economy where, despite recent sharp reductions in interest rates, there remains a possibility that economic weakness could persist longer than currently assumed.

## Australian economy

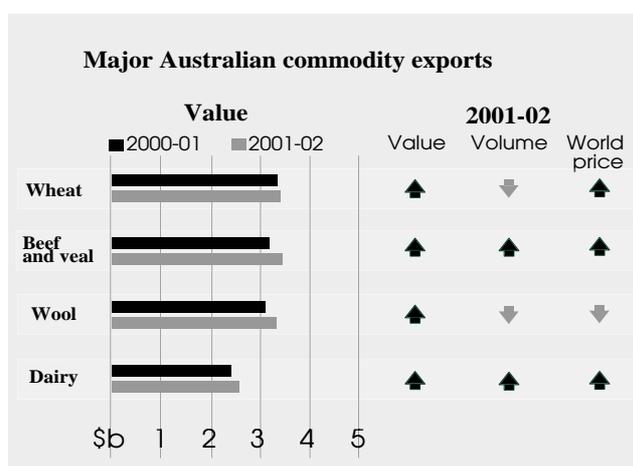
Despite the weakening global economic environment, the economic outlook for Australia remains favorable. Partial indicators, such as growth in retail sales and building approvals, suggest that economic growth in Australia is likely to remain strong in the short term. There has also been a remarkable improvement in Australia's trade performance, assisted by the relatively low Australian dollar.

In preparing this set of commodity forecasts, economic growth in Australia was assumed to strengthen from an estimated 2.5 per cent in 2000-01 to around 3.5 per cent in 2001-02. This assumed Australian growth rate in the short term is higher than the rates assumed for the major world economies, including the United States, Japan and western European countries. Australia's inflation rate is assumed to average around 2.5 per cent in 2001-02, compared with an estimated 6.0 per cent in 2000-01 (including the effects of the new tax system).

The outlook for the Australian dollar is particularly uncertain. In the short term, movements in the Australian dollar are likely to be influenced by the prospects for economic growth in the major world economies, especially in the United States and Japan, and hence by the outlook for Australia's export performance. If, for example, there is a further weakening in the world economic outlook (and hence the outlook for world commodity prices), this could be interpreted unfavorably by financial markets and result in significant downward pressure on the Australian exchange rate. The Australian dollar is assumed remain weak, averaging around US54c and TWI 51 in 2001-02, compared with an average of US54c and TWI 50 in 2000-01.

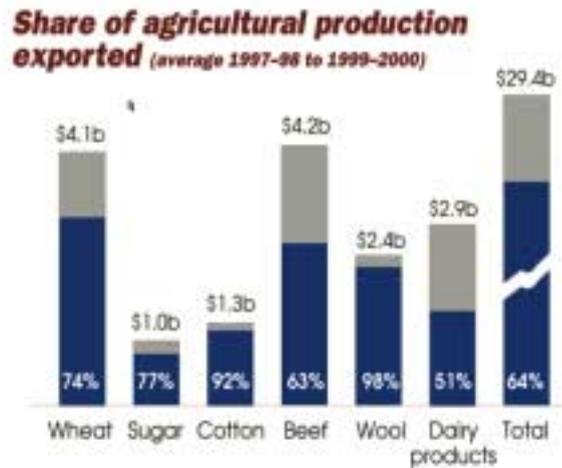
## Prospects for agriculture

Forecasts of further improvements in prices for beef, sheep meats, dairy products, wheat and canola indicate another strong financial performance from the Australian farm sector in 2001-02. The net value of farm production is forecast to rise by 19 per cent to \$8.0 billion in 2001-02, following a 32 per cent increase in 2000-01. The brighter outlook for farm incomes is being driven by a big lift in farm export earnings, the result of generally favorable export prices for most farm commodities. After rising an estimated 21 per cent last financial year, the value of farm exports is forecast to rise by a further 4 per cent to \$30.4 billion in 2001-02.



**Trade reforms vital**

International markets are crucial to Australian agriculture. In the three years to 1999-2000, around 64 per cent of agricultural production (in value terms) was exported. In the case of wool the figure was 98 per cent. The dairy industry currently exports a little over half of its output, but this can be expected to grow as the industry expands to take advantage of opportunities in the world market.



In view of the importance of exports to Australian agriculture, future prospects will be determined in large part by how much extra market access can be achieved through trade negotiations, and by how competitive Australian suppliers are in those new markets. There can be little doubt that most of the growth in Australian agriculture will come from the export market, not from the small domestic market.

Recent ABARE work on world dairy trade highlights the potential gains from reducing some of the market distorting measures that currently exist. If, for example, there was a concurrent doubling of import quotas and a halving of all applied tariff rates, world prices for cheese would rise by an estimated 25 per cent. Increased world prices would flow back directly to Australian exporters, to dairy farmers and to the rural communities that contribute to cheese production. Of course if Australian dairy farmers are not competitive on world markets they would fail to capture these opportunities.

In the past eighteen months or so there has been a significant rise in antiglobalisation sentiment in many parts of the world. In light of this development, it is worth reflecting on what would happen if Australia ceased further economic reform. For example, what would it mean if there was a tightening of restrictions on overseas investment in Australia, a reinstatement of protection in agriculture and manufacturing to pre-Uruguay Round levels, and a cessation of immigration. It is estimated that such a policy would cost the Australian economy a full percentage point in economic growth forever. It would take Australia's current long term sustainable growth rate from 3.5 per cent a year down to 2.5 per cent. The consequence of that would be the loss of around 400 000 new jobs over the next ten years.

**Grains**

Firm demand for grains, especially in Asia, is forecast to result in world consumption exceeding production for cereals and oilseeds in 2001-02. Reduced stocks of wheat, coarse

grains and oilseeds are forecast to lead to increased world prices. Returns to Australian growers will be assisted by a relatively low Australian dollar.

Australian winter crop production in 2001-02 is estimated to be 1 per cent lower, mainly as a result of the late start to the season and subsequent dry conditions in Western Australia and Queensland. Australian winter crop area is estimated to have fallen by 5 per cent because of a lack of planting rain. Wheat and canola areas are estimated to be lower, but barley area higher. Australian wheat production is forecast to fall by 5 per cent to just under 20.1 million tonnes, canola production to fall by 3 per cent to 1.6 million tonnes, and barley production to be up by 7 per cent to 5.9 million tonnes.

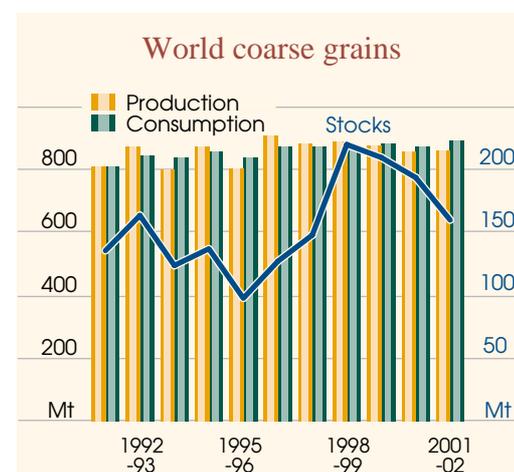
### Wheat

The world indicator price for wheat (US hard red winter, fob Gulf) is forecast to average US\$135 a tonne in 2001-02, up from US\$129 a tonne in 2000-01, in response to reduced world supplies and continued firm demand. World wheat production in 2001-02 is forecast to fall by 11 million tonnes to 569 million tonnes, the smallest crop since 1995-96, reflecting reduced production in key producing countries. Substantial production falls forecast for four of the five major exporting regions (the United States, the European Union, Canada and Australia) will reduce the availability of wheat on the export market, adding further upward pressure to world prices. Global consumption of wheat is forecast to exceed production for the fourth consecutive year. In Australia, the average pool return for Australian premium white wheat is forecast to be \$249 a tonne, up A\$21 a tonne on the 2000-01 return, reflecting higher world prices and a continued weak Australian dollar.



### Coarse grains

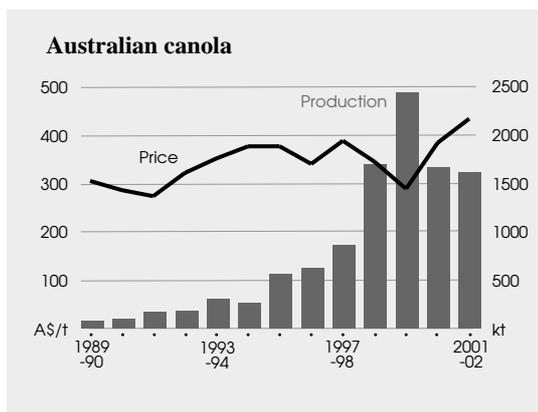
World coarse grains prices are forecast to strengthen in 2001-02 in response to lower world stocks and continuing firm demand for feed grains. In the case of corn, the world indicator price (US corn, fob Gulf basis) is forecast to increase by 9 per cent to average around US\$98 a tonne in 2001-02. Despite an easing in import demand for feed barley, world barley prices are expected to remain firm as supplies of barley are reduced in some of the major



exporting countries. Australian barley prices are forecast to remain relatively buoyant in 2001-02. Continuing strong domestic demand for feed grains is expected to result in barley prices falling only marginally, despite forecast higher production. Australian prices for malting and feed barley are forecast to decline by around \$3 a tonne to average \$220 a tonne and \$175 a tonne respectively in 2001-02.

**Oilseeds**

World production of canola in 2001-02 is forecast to decline. Dry conditions in Australia and the European Union have reduced both plantings and yield potential of canola crops. Reduced plantings in Canada, because of dry weather and relatively poor price prospects at the time of planting, are likely to result in a fall in Canadian production. The expected decreases in production in Australia, Canada and the European Union, combined with strong EU demand for canola oil, are likely to sustain high prices. Given these developments, Australian canola prices are forecast to average \$433 a tonne in the 2001-02 marketing year, a rise of 30 per cent from the previous year.

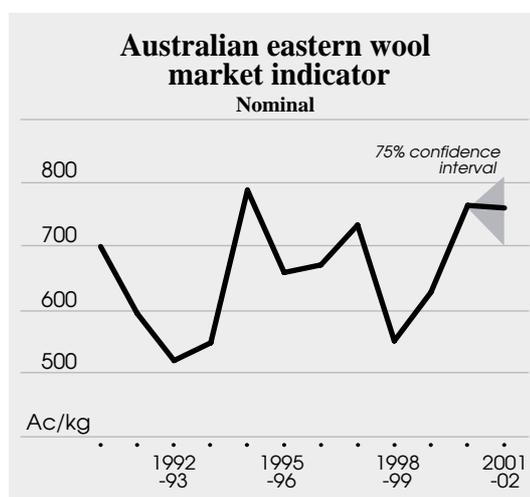


**Wool**

After reaching a peak of 840 cents a kilogram clean in April 2001, Australian wool prices have since averaged around 800 cents a kilogram. Although wool supply is at a historic low, the major risk facing wool prices at the moment is the potential for the downturn in world economic growth to be greater than expected. In particular, slow growth in the United States and Asian economies in 2001-02 is expected to result in some easing in demand for wool. As a result, the Australian wool eastern market indicator is forecast to fall slightly to 760 cents a kilogram in 2001-02.

Strong demand in 2000-01 resulted in an increase of over 5 per cent in Australian exports of raw and semiprocessed wool, to 845 000 tonnes (greasy equivalent). However, exports are forecast to fall by a little over 1 per cent in 2001-02 because of reduced supplies.

In recent years, the United States has developed into a major final consumer of Australian



wool. Most of this consumption has been through imports of finished and semiprocessed textiles and apparel from Asian countries such as China, the Republic of Korea and Chinese Taipei. In the short term, however, slower growth in the United States in 2001-02 is expected to result in weaker US demand for wool.

China is a major processor and reexporter of Australian wool. Exports to China accounted for a major part of the increase in total Australian shipments of wool in 2000-01. Exports to China rose by 30 per cent to 323 000 tonnes (greasy equivalent), but have slowed in recent months. With weaker demand expected in key wool consuming markets such as Japan and the United States, Australian exports of raw wool to China are expected to decline in 2001-02.

With lower sheep numbers and reduced fleece weights because of dry seasonal conditions in many wool growing areas, shorn wool production is estimated to have been 602 000 tonnes in 2000-01. With sheep numbers expected to fall further in 2001-02, shorn wool production is forecast to fall by 1 per cent to 596 000 tonnes. Australian wool stocks are also minimal. The WoolStock Australia wool stockpile has now been completely dispersed and stocks of wool held on farms were substantially reduced during 2000-01.

## Meat

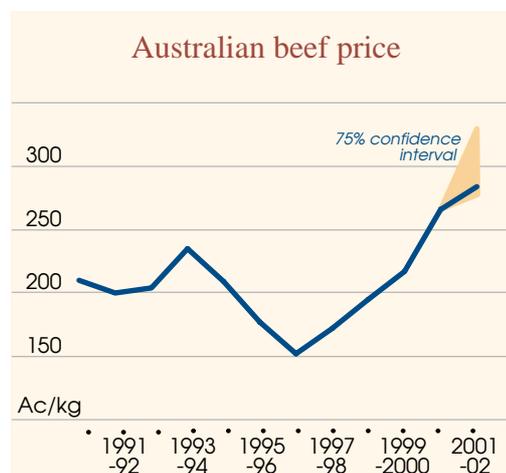
### *Beef and veal*

Australian saleyard cattle prices are forecast to average nearly 7 per cent higher in 2001-02, at 284 cents a kilogram (dressed weight). Continuing weakness in the Australian dollar, combined with strong export demand, is forecast to underpin higher beef saleyard prices.

As a result of a slowing US economy, and a stagnant economy in Japan, demand for competitively priced imported meat in those markets is forecast to remain largely unchanged in 2001-02. There is the risk, however, that Japanese consumer demand for beef may be affected by the discovery of a case of BSE (bovine spongiform encephalopathy or 'mad cow' disease) in Japan last month.

On the upside, market liberalisation in the Republic of Korea is expected to result in greater opportunities for Australian exporters, while in Canada, lower beef production and reduced imports from south America (banned because of foot and mouth disease) are forecast to result in continuing strong demand for Australian beef.

Australian beef and veal production is forecast to rise by 3 per cent in 2001-02 as high cattle



prices continue to encourage producers to offload greater numbers of stock. Slaughter weights are forecast to rise, particularly as the production of grain fed cattle continues to expand and a larger proportion of the total slaughter consists of heavier weight male cattle.

Australian beef and veal exports are forecast to rise by almost 2 per cent to 975 000 tonnes in 2001-02 as domestic beef production increases, and export demand remains strong. After exceeding \$4 billion in 2000-01, Australian export returns are forecast to rise by a further 8 per cent to over \$4.3 billion. Continuing weakness in the Australian dollar, combined with higher Pacific beef prices as US production declines, are forecast to support higher beef export returns.

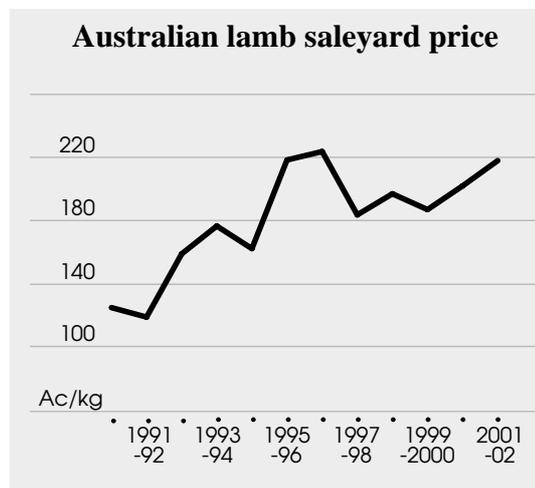
During 2000-01, live cattle exports to Indonesia, Australia's largest export market for live cattle, increased by 23 per cent. However, offsetting that rise were lower exports to both the Philippines and Egypt. Exports to Indonesia and the Philippines have been affected by currency devaluations making imported cattle more expensive in local currency terms. In the Philippines, consumer fears about BSE also contributed to the decline in exports to that market. Overall, live cattle exports in 2000-01 were unchanged from the previous year. Live cattle exports are forecast to rise by 5 per cent in 2001-02 as demand in these key importing markets improves.

**Lamb and mutton**

Saleyard lamb prices are forecast to rise by 8 per cent in 2001-02, to average 218 cents a kilogram. Lower lamb supplies and strong export demand are the main factors influencing forecast higher saleyard lamb prices. Lamb slaughter is forecast to fall by 4 per cent to 18.1 million in 2001-02, as improved wool prices prompt sheep producers to join a larger proportion of ewes to merino rams for wool production.

As a consequence of lower Australian lamb production, lamb exports are forecast to fall by around 3 per cent in 2001-02 to 112 000 tonnes. However, lamb exports to the United States are forecast to rise by a further 7 per cent in 2001-02 as US demand for imported lamb continues to strengthen. After increasing by 27 per cent last year, despite quota restrictions, lower growth in lamb exports to the United States is forecast as Australian lamb supplies tighten and growth in the US economy eases.

Mutton production is forecast to fall by 6 per cent to 329 000 tonnes in 2001-02. With reduced sheep available for slaughter and increased demand for store sheep, saleyard

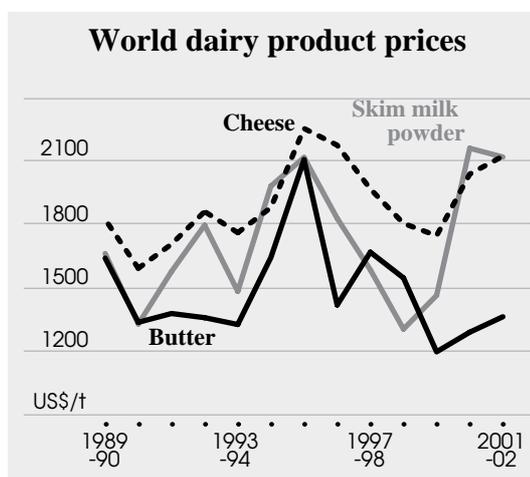


mutton prices are forecast to increase by 9 per cent to 110 cents a kilogram (dressed weight).

Demand for live sheep from Saudi Arabia and other Middle East nations has been strong following a ban on imports of live sheep from north African markets due to rift valley fever, and bans on imported meat from Europe in response to BSE and FMD concerns. Given that these bans are expected to remain for some time, demand for live sheep from the Middle East is forecast to remain firm during 2001-02. However, with lower overall sheep numbers, live sheep exports are forecast to fall by 4 per cent in 2001-02, to around 5.7 million.

## Dairy

Higher world prices for dairy products, combined with the low value of the Australian dollar and strong export demand have resulted in increased farm gate returns for Australian dairy farmers. Australian farm gate milk prices are forecast to rise by nearly 10 per cent in 2001-02 to around 31 cents a litre. Manufacturers are continuing to pass on the benefits of improvements in world prices over the past year, while some manufacturers supplying 'home brand' milk to supermarkets have renegotiated higher contract prices.



Australian milk production fell by 2.7 per cent in 2000-01, the first decline in annual production since the drought affected year of 1989-90. This recent decline was the result of dry seasonal conditions in some dairying regions, such as Gippsland, and the exit of some dairy farmers from the industry following deregulation. Improving farm gate returns are expected to encourage a turnaround in 2001-02, with cow numbers forecast to rise marginally to close to 2.2 million by June 2002. Total milk production in 2001-02 is forecast to rise by 1.6 per cent to 10.7 billion litres.

## Farm performance

The Australian farm sector continues to demonstrate considerable flexibility as it adjusts to pressures associated with fluctuating commodity prices, rising costs and the vagaries of the weather. In response to market signals, farmers have altered the range of activities on farms and the intensity of these activities. At the same time farmers have increased productivity to maintain their profitability and international competitiveness. For example,

over the 22 year period to 1998-99 total factor productivity growth in the broadacre sector was around 2.6 per cent a year.

Forecasts of further improvements in prices for beef, sheep meats, dairy products, wheat and canola indicate another strong financial performance from the Australian farm sector in 2001-02. The gross value of farm production is forecast to rise by 5 per cent to \$35.3 billion in 2001-02, reflecting increases in prices received and a 1.3 per cent increase in the volume of farm production.

Total farm costs are forecast to increase by just under 2 per cent to \$27.2 billion in 2001-02, following a 5.2 per cent rise in 2000-01. The expected increase in farm costs during 2001-02 reflects a forecast rise of 1.3 per cent in prices paid for farm inputs and some increase in total inputs used. Some easing in fuel prices is forecast, in line with expected modest falls in international crude oil prices. Australian farmers can also expect some falls in fertiliser prices in 2001-02, following recent declines in international prices for ammonia based fertilisers. Interest costs will also be lower in 2001-02, reflecting recent falls in official rates.

## Financial performance

Results from ABARE's annual farm survey provide a basis for evaluating the financial performance of the rural sector. Higher farm production combined with increased commodity prices is estimated to have resulted in increased profitability in 2000-01 for broadacre farms (grains, beef and sheep) in Victoria generally. Farm cash income (total cash receipts minus total cash costs) for Victoria's broadacre industries as a group is estimated to have risen by 26 per cent to average \$46 400 per farm in 2000-01 (table 1).

By comparison, farm cash income for Gippsland's broadacre industries is estimated to have remained similar in 2000-01 to that recorded in 1999-2000. The majority of the broadacre farms surveyed in the region are located in east Gippsland. Average total cash receipts for Gippsland broadacre farms rose by 8 per cent to \$90 100 in 2000-01, which was largely offset by an 11 per cent increase in farm cash costs. A substantial portion of the increase in costs is due to the higher level of beef cattle purchases in 2000-01. This follows the rundown in beef herds over the previous two years as a consequence of dry seasonal conditions.

While average beef cattle receipts rose in the region in 2000-01, many cattle producers in the process of rebuilding herds had reduced turnoff and were therefore not able to take full advantage of higher beef prices. At 30 June 2001 the average beef herd in the Gippsland is estimated to have risen by 12 per cent to average 212 per farm.

## ABARE CONFERENCE PAPER 2001.26

Table 1: **Broadacre industries farm performance** Average per farm

		High rainfall zone east of Melbourne (including Gippsland)			Victoria		
		1998-99	1999-2000 <sup>p</sup>	2000-01 <sup>s</sup>	1998-99	1999-2000 <sup>p</sup>	2000-01 <sup>s</sup>
Sheep at 30 June	no.	323	704	758	1 462	1 433	1 383
Beef cattle at 30 June	no.	192	189	212	115	92	99
Beef cattle sold	no.	104	91	82	64	45	42
<b>Receipts</b>							
Beef cattle	\$	45 589	49 072	53 013	27 642	23 285	26 967
Crops	\$	6 055	1 836	2 819	47 485	63 610	69 059
Sheep	\$	7 126	9 785	10 079	19 958	18 307	18 741
Wool	\$	6 887	15 605	16 146	23 423	28 564	31 782
Total cash receipts	\$	76 272	82 822	90 136	133 928	147 634	161 440
Total cash costs	\$	61 970	65 873	73 488	112 334	110 712	115 080
Farm cash income	\$	14 302	16 949	16 648	21 595	36 922	46 361

<sup>p</sup> Preliminary. <sup>s</sup> Provisional estimate.

Sheep flocks in the Gippsland region increased on average in 2000-01, leading to a small rise in receipts from sheep and lamb sales. Despite lower wool production, wool receipts increased by a relatively small amount, as prices rose.

Gippsland dairy farm cash incomes are estimated to have increased by 20 per cent on average in 2000-01, compared with a 74 per cent rise in dairy farm cash incomes for Victoria as a whole (table 2). With milk prices increasing in 2000-01, Gippsland dairy farmers

Table 2: **Dairy industry farm performance** Average per farm

		Gippsland <sup>a</sup>			Victoria		
		1998-99	1999-2000 <sup>p</sup>	2000-01 <sup>s</sup>	1998-99	1999-2000 <sup>p</sup>	2000-01 <sup>s</sup>
Dairy cows at 30 June	no.	165	165	174	173	179	188
Dairy cattle at 30 June	no.	240	234	240	252	265	274
Total milk production	L	697 684	693 380	660 679	754 436	847 750	862 494
Beef cattle 30 June	no.	15	24	11	24	26	20
<b>Receipts</b>							
Milk (excl. freight)	\$	189 487	171 832	194 193	206 866	204 727	249 535
Dairy cattle	\$	12 811	16 792	27 880	13 034	17 970	25 751
Beef cattle	\$	3 345	847	1 910	5 826	4 713	3 489
Crops	\$	4 552	346	0	1 333	521	504
Total cash receipts	\$	216 081	193 119	225 528	236 322	234 841	284 297
Total cash costs	\$	151 739	135 810	156 674	166 681	181 624	191 544
Farm cash income	\$	64 342	57 309	68 854	69 641	53 217	92 753

<sup>a</sup> Excludes the MacAlister Irrigation Area. <sup>p</sup> Preliminary. <sup>s</sup> Provisional estimate. Estimates do not yet fully reflect changes in the distribution of milk production across farms arising in 2000-01. <sup>na</sup> Not available.

received, on average, an additional \$22 600 in receipts despite a fall in milk production per farm. Farm costs increased by 15 per cent, reflecting greater expenditure on dairy cattle and fodder. The slightly poorer performance of Gippsland dairy farms, relative to the state as a whole, partly reflected drier seasonal conditions in Gippsland.