Commodity outlook and financial performance for Gippsland farms

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This paper presents the current commodity outlook and the recent financial performance of some key agricultural industries in Victoria, highlighting the performance of beef and dairy farms within the state as well as at the regional level.

The Gippsland region covered in this paper is outlined in map 1. The major regional centres include Leongatha and Traralgon.

**map 1: Gippsland**

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**Agricultural sector profile**

Milk is Gippsland’s most important agricultural product in value terms. In 2004-05, milk accounted for 53 per cent or nearly $405 million of the $770 million total value of agricultural production in the region (figure A).

Cattle slaughter accounted 25 per cent of total value of production while hay production accounted for 6 per cent and vegetables 4 per cent of the total value. Other products contributing a small proportion of the total value of agricultural production included poultry, eggs, sheep and lambs and fruit.
Number and type of farms

Australian Bureau of Statistics data indicate that there were 3347 farms in Gippsland with an estimated value of agricultural operations of more than $5,000 in 2004-05 (table 1).

<table>
<thead>
<tr>
<th>Industry Classification</th>
<th>Gippsland</th>
<th>Victoria</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beef Cattle Farming</td>
<td>1419</td>
<td>7924</td>
</tr>
<tr>
<td>Dairy Cattle Farming</td>
<td>1415</td>
<td>6199</td>
</tr>
<tr>
<td>Sheep-Beef Cattle Farming</td>
<td>179</td>
<td>2255</td>
</tr>
<tr>
<td>Sheep Farming</td>
<td>108</td>
<td>3790</td>
</tr>
<tr>
<td>Vegetable Growing</td>
<td>76</td>
<td>793</td>
</tr>
<tr>
<td>Livestock Farming n.e.c.</td>
<td>56</td>
<td>112</td>
</tr>
<tr>
<td>Horse Farming</td>
<td>20</td>
<td>366</td>
</tr>
<tr>
<td>Other</td>
<td>74</td>
<td>10611</td>
</tr>
<tr>
<td><strong>All Industries</strong></td>
<td>3347</td>
<td>32050</td>
</tr>
</tbody>
</table>

*Where the estimated value of agricultural operations is more than $5000

source ABS

Beef cattle and dairy farms each accounted for 42 per cent of farms in the region. A further 5 per cent of farms were sheep-beef farms, 3 per cent were sheep farms, 2 per cent vegetable farms and there were a small number of farms running other types of livestock.

Farms are classed in table 1 according to the activities that generate most of their value of agricultural production. Around 25 per cent of the total number of dairy cattle in Victoria is located in this region.
Most farm businesses in Gippsland are small in size with around 60 per cent of farms producing less than $150,000 in agricultural outputs in 2004-05 (figure B). Almost 35 per cent of farms produced less than $50,000 and there were only 2 per cent of farms that produced more than $1 million of agricultural production in 2004-05.

**Employment**

Australian Bureau of Statistics data from 2007 indicate that 125,000 people were employed in Gippsland. The retail sector is the largest employer employing almost 16 per cent (19,600 people) of the total workforce. However, agriculture forestry and fishing was the second largest employer accounting for 16,700 people or 13 per cent of the workforce. Manufacturing, including food processing industries accounted for around 10 per cent of the workforce and the construction industry also employed around 10 per cent of the workforce - a relatively high proportion of the workforce, particularly for a rural area.

**figure C: Gippsland employment profile, 2007**

Dairy farm performance — Victoria and Australia
During 2006-07, dairy producers in Victoria and nationally recorded large reductions in farm cash incomes resulting from increases in farm expenditure and reduced production (figure D). The effect of dry seasonal conditions was more pronounced for Victorian producers during 2006-07, with income falling by more than 70 per cent compared to a decline of 39 per cent nationally (table 2).

**figure D: Farm cash income, dairy farms in Victoria**

In 2007-08, farm cash income is projected to improve significantly for dairy producers in both Victoria and across Australia. Milk prices, on average, are forecast to increase by around 30 per cent to result in one of the largest one year increases in farm cash incomes in the past 20 years for both Australia and Victoria (figure D). Despite some further reduction in milk production in 2007-08 due to reductions in cow numbers, total cash receipts for Victorian dairy farms are projected to increase by over 25 per cent, on average. Farm cash costs are forecast to decline by around 10 per cent as improved seasonal conditions allow for some reduction in fodder expenditure.

**Dairy farm performance — Gippsland**

Farm cash income for Gippsland dairy farms fell sharply in 2006-07 as sustained drought reduced milk yields and increasing fodder costs although reductions in milk yields were partially offset by an increase in the number of cows milked within the region (figure E). An increase in the number of dairy cows milked led to a lesser reduction in milk receipts in Gippsland compared to northern Victorian dairying regions.

In 2007-08, farm cash incomes in the Gippsland are forecast to recover markedly on the back of higher milk prices, combined with improved seasonal conditions during 2007 and reduced fodder expenditure. Farm cash income is projected to rise by slightly more in this region than the state average due to a lesser reduction in milk production in this region compared to irrigation regions in the north of the state (figure E).
Financial performance, Australia and Victoria

Dairy industry

<table>
<thead>
<tr>
<th></th>
<th>Australia</th>
<th>Victoria</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total cash receipts</td>
<td>$416,899</td>
<td>$394,449</td>
</tr>
<tr>
<td>Total cash costs</td>
<td>$331,458</td>
<td>$360,811</td>
</tr>
<tr>
<td>Farm cash income</td>
<td>$85,440</td>
<td>$33,638</td>
</tr>
<tr>
<td></td>
<td></td>
<td>p(10)</td>
</tr>
<tr>
<td>Farms with negative farm cash income</td>
<td>% 15</td>
<td>% 36</td>
</tr>
<tr>
<td>Farm business profit</td>
<td>$18,970</td>
<td>$39,509</td>
</tr>
<tr>
<td></td>
<td>(46)</td>
<td>(168)</td>
</tr>
<tr>
<td>Farms with negative farm business profit</td>
<td>% 49</td>
<td>% 76</td>
</tr>
<tr>
<td>Farm capital at 30 June a</td>
<td>$2,835,420</td>
<td>$3,206,041</td>
</tr>
<tr>
<td>Farm debt at 30 June bd</td>
<td>$442,927</td>
<td>$493,759</td>
</tr>
<tr>
<td>Equity ratio be</td>
<td>% 84.3</td>
<td>% 84.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(13)</td>
</tr>
<tr>
<td>Rate of return e</td>
<td></td>
<td>- excl. cap. appreciation</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- incl. cap. appreciation</td>
</tr>
</tbody>
</table>

- Excludes leased plant and equipment.
- Average per responding farm.
- Equity expressed as a percentage of farm capital.
- Harvest loans are not included in farm debt.
- Rate of return to farm capital at 1 July calculated as farm business profit plus interest paid expressed as a percentage of total farm capital.
- Preliminary estimates.  a Provisional estimates. na Not Available.

figure E: Farm cash income, dairy farms in Gippsland

Broadacre farm performance — Victoria and Australia

Australian broadacre farm financial performance is projected to strengthen markedly in 2007-08, after recording the lowest incomes since 1992-93 in 2006-07. Increased grain and livestock production, combined with higher grain and wool prices and strong prices for beef cattle, sheep and lambs are projected to result in farm cash incomes on broadacre farms nearly doubling in 2007-08, to average around $78 200 per farm (figure F). In addition, total cash costs are projected to be slightly lower for livestock farms as improved seasonal conditions enable reduced expenditure on fodder and agistment.

Average farm business profit across Australia is projected to recover by even more than the increase in farm cash income in 2007-08 (table 3). This largely reflects a build up in the value of trading stocks as producers increase livestock numbers and replenish on-farm inventories of fodder and grain.

Average farm cash income for Victorian broadacre farms is projected to rise by around 70 per cent to $69 000 in 2007-08. Further, positive farm business profit is forecast for Victoria following two losses in 2005-06 and 2006-07 (figure G).
### 3. Financial performance, Australia and Victoria

#### All broadacre industries

<table>
<thead>
<tr>
<th></th>
<th>Australia</th>
<th>Victoria</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farm cash income</td>
<td>$70,182</td>
<td>41,180 (24)</td>
</tr>
<tr>
<td>Farms with negative farm cash income</td>
<td>%24</td>
<td>42 (12)</td>
</tr>
<tr>
<td>Farm business profit</td>
<td>$-7,745</td>
<td>-49,610 (19)</td>
</tr>
<tr>
<td>Farms with negative farm business profit</td>
<td>%65</td>
<td>79 (5)</td>
</tr>
<tr>
<td>Farm capital at 30 June $a</td>
<td>3,277,465</td>
<td>3,612,180 (5)</td>
</tr>
<tr>
<td>Farm debt at 30 June $bc</td>
<td>340,835</td>
<td>436,520 (10)</td>
</tr>
<tr>
<td>Equity ratio bd</td>
<td>%90</td>
<td>87 (1)</td>
</tr>
<tr>
<td>Rate of return $e</td>
<td>- excl. cap. appreciation</td>
<td>%0.8</td>
</tr>
<tr>
<td></td>
<td>- incl. cap. appreciation</td>
<td>%7.0</td>
</tr>
</tbody>
</table>

*Excludes leased plant and equipment. Average per responding farm. Harvest loans are not included in farm debt. Equity expressed as a percentage of farm capital. Rate of return to farm capital at 1 July calculated as farm business profit plus interest paid expressed as a percentage of total farm capital. Preliminary estimates. Provisional estimates. na Not Available.

### figure F: Farm cash income, broadacre farms in Victoria

![Graph showing farm cash income for Victoria and Australia from 1977-78 to 2005-06]
Over the past four years the demand for rural land has remained strong. Rising land values have increased average farm capital values underpinning farm equity and offsetting the impact of higher farm debt. This has enabled producers to borrow more both for working capital to meet the reduced cash flow during the drought and for new investment in land, plant, machinery, vehicles and improvements. Increases in farm capital values have resulted in rising rates of return including capital appreciation in recent years despite average rates of return excluding capital appreciation remaining very low. Rates of return are calculated on a full equity basis (farm business profit plus interest paid), as if the farm were fully owned by the operators (table 3).

**Broadacre farm performance — Gippsland**

Farm cash income for Gippsland broadacre farms fell in 2006-07, reflecting prolonged drought conditions within the region (figure H). Broadacre farms are farms that run beef cattle or sheep or grow grain crops.

In 2007-08, little change is forecast in farm cash income for Gippsland broadacre farms. Little change is expected in receipts for beef cattle with turnoff expected to be slightly lower than in 2006-07. Some herd rebuilding commenced in 2007 as seasonal conditions improved but turnoff is expected to increase in 2008 in the face of drier seasonal conditions. Higher wool, sheep and lamb prices are forecast to boost receipts for sheep producers. Overall, reductions in farm costs are expected to be relatively small with reductions in fodder expenditure largely offset by increased livestock purchase in late 2007.
Farm cash income in the region is typically below the state average due to the relatively small size of farms (figure H). Only in some years of particularly high beef cattle prices and dry seasonal conditions, such as 2006-07 when beef cattle turnoff increases markedly, do average farm cash incomes approach the Victorian average.

Over 60 per cent of farms in this region have operators that work off-farm for wages. Average farm cash incomes are, on average low and even negative in some years. Off-farm income is a major contributor to household incomes in this region.

**Beef farm performance — Victoria and Australia**

In 2006-07, farm cash incomes for Victorian beef specialist producers (defined as farms with the majority of their income derived from beef cattle sales) deteriorated markedly as drought conditions reduced farm production and contributed to increased production costs (figure I). The impact of reduced sale numbers on farm receipts was exacerbated by lower prices, caused by increased turnoff of more unfinished and younger stock.

Farm cash income for Victorian beef specialists is projected to rise only slightly in 2007-08. Beef receipts are estimated to be constrained by reduced turnoff as farms rebuild beef cattle numbers. Improved seasonal conditions have allowed producers to reduce outlays on fodder expenditure and consequently total cash costs are projected to fall slightly. Farm cash income is projected to remain similar to 2006-07 at around $35 000. However, increases in beef cattle numbers are projected to boost the value of trading stocks raising farm business profit to around $30 000 in 2007-08 following an estimated average business loss of $40 000 in 2006-07.
Outlook for selected commodities

Seasonal conditions update
The Australian Bureau of Meteorology in its latest seasonal rainfall outlook (26 March 2008) for the April to June period, shows a moderate to strong shift in the odds favouring a wetter than normal season over the eastern half of Queensland and New South Wales.

The chances of exceeding median rainfall over April to June are between 60 and 70 per cent over most of the eastern half of Queensland and New South Wales, approaching 75 per cent around the boarder of the two states. Over the rest of the country the chances of exceeding median rainfall are between 44 and 55 per cent.

The Bureau also announced that a La Niña event in the Pacific Basin is showing signs of weakening, although computer models indicate it is likely to persist until the end of autumn. La Niña events typically bring wetter than normal conditions across much of the eastern half of Australia.

Livestock
Dairy
World prices for the major dairy products rose sharply in 2007-08 and have remained relatively high in the first two months of 2008. In 2007-08, world prices for cheese are forecast to be up by 70 per cent, skim milk powder prices up by 40 per cent and butter prices up by 95 per cent. In 2008-09 world prices for most dairy products are forecast to decline as production and exports rise in response to recent higher world prices.

In 2008-09 and 2009-10, world dairy production is forecast to grow at a relatively slow rate. Production in the major dairy exporting countries of the European Union, New Zealand and Australia is forecast to grow relatively slowly. This is a result of changes to production incentives under the Common Agricultural Policy (CAP) in the European Union, higher feed prices and lead times in herd-building in New Zealand and recovery from recent drought conditions and associated irrigation water supply constraints in Australia.

Global demand for dairy products remains relatively strong in a world market influenced by strong economic growth, particularly in developing countries in Asia. Demand is also expected to be strong in developed countries such as the European Union.

The ability of Australian dairy farmers to recover quickly from drought will depend largely on the financial situation of individual farmers, the availability of irrigation water and the ability of farmers to rebuild milking cow numbers. While good
rains in late 2007 and early 2008 have been helpful, uncertainty remains about the possibility and timing of increased allocations of irrigation water in the southern Murray Darling Basin, and the availability and price of fodder. Australian milk production is estimated to have fallen by more than 5 per cent in 2007-08, to around 9.1 billion litres. In 2008-09, Australian milk production is forecast to begin to recover, rising by almost 2 per cent to around 9.25 billion litres.

After averaging around 45c in 2007-08, Australian farm-gate milk prices are forecast to rise by a further 20 per cent to 54c a litre in 2008-09. The forecast of relatively high farm gate milk prices reflects both the prices needed by dairy farmers to cover the high cost of feed and other inputs (such as purchased irrigation water entitlements) and the ability of the dairy industry to benefit from strong world prices for dairy products.

**Beef**

The Australian weighted saleyard price of beef is forecast to increase by 7 per cent in 2008-09 to average 315 cents a kilogram. Underpinning the rise in prices will be a decline in numbers of cattle turned off for slaughter as producers move to rebuild herds. The extent of the price increase is expected to be moderated by weaker demand for Australian beef in Japan and Korea as competition from the United States increases, particularly toward the latter half of the year.

Reflecting an increased retention of female cattle for breeding, total slaughterings are forecast to fall by 2 per cent to 8.6 million in 2008-09. As a result, beef production is also forecast to decline by 2 per cent in 2008-09, to 2.1 million tonnes.

Total beef exports are forecast to fall to 880 000 tonnes in 2008-09 as a result of lower production, as well as an expected increase in competition from US beef in Japan and Korea. Exports to Japan in 2008-09 are forecast to fall by 6 per cent, while exports to Korea are forecast to fall by 19 per cent.

Exports of live cattle are forecast to increase in 2008-09, to 700 000 head, despite a forecast rise in prices, reflecting an expected increase in demand. Over the medium term the number of cattle exported live is projected to rise, driven by solid demand in South East Asian markets, a projected fall in cattle prices and an assumed weaker Australian dollar.

**Sheep meat**

Lamb production is forecast to rise by 2 per cent to 412 000 tonnes in 2008-09, as a result of higher slaughterings and a slight increase in slaughter weights. Reflecting an expected increase in export and domestic demand, the Australian weighted saleyard price for lambs is forecast to rise by 7 per cent in 2008-09, despite the higher production, to 355 cents a kilogram (dressed weight).

High wool prices over the past year, combined with strong saleyard prices for lambs and sheep, are expected to provide an incentive for producers to begin rebuilding flocks in 2008-09, and beyond. With producers likely to hold on to additional ewes for flock rebuilding in 2008-09, slaughterings of sheep are forecast to fall by 17 per cent to 8.5 million, but then to increase gradually as flock numbers grow over the medium term. Reflecting lower supply of sheep and increased demand as producers begin to restock, the Australian weighted saleyard price of mutton is forecast to rise by 9 per cent in 2008-09 to average 180 cents a kilogram.

Total Australian lamb exports are projected to increase by around 2 per cent, to 163 000 tonnes in 2008-09. In 2008-09, Mutton exports are forecast to fall by 24 per cent to 108 000 tonnes (shipped weight), as a result of lower production. Live sheep exports are forecast to fall to 3.7 million in 2008-09, constrained by a limited supply of sheep suitable for live export.

**Wool**

Strong prices for both sheep meat and wool, in addition to the encouragement provided by the recent good rains in many areas, can be expected to result in wool producers moving to expand flock sizes. Australian shorn wool production in 2007-08 is forecast to be 395 000 tonnes, down 7 per cent from the previous year. Australian shorn wool production is forecast to rise slightly in 2008-09 to 404 000 tonnes, largely as a result of a slightly higher number of sheep shorn and increasing fleece weights.

In the face of strong export demand, the lower production of shorn wool contributed to continued increases in the eastern market indicator price in 2007-08. Reflecting these further upward movements in wool prices, the eastern market indicator price in 2007-08 is forecast to average 970 cents a kilogram clean, 12 per cent higher than in 2006-07.
China is by far the largest consumer of Australian raw wool, which it processes and manufactures into a range of commodities from textiles to clothing. Substantial quantities of these products are exported to developed country markets. Since the largest export market for wool products is the United States, changes in US demand will have repercussions along the supply chain. Chinese imports of raw wool from Australia will be affected by expectations of Chinese processors about next year’s US orders for wool products. Any perceptions on the part of Chinese buyers of a softening in US demand for wool apparel and textiles could translate into lower Chinese imports of raw wool, thereby putting downward pressure on Australian wool prices.

Assuming uncertainty about US economic growth and its effect on demand for finished wool products is reflected in Chinese buying activity, the eastern market indicator price is forecast to fall by 1 per cent in 2008-09, to average of 960 cents a kilogram clean.

Grains

Wheat
The world wheat indicator price (US hard red winter, fob Gulf ports) has been at record highs in both nominal and real terms, in 2007-08. In 2008-09, world wheat supplies are forecast to increase by 12 million tonnes as global wheat production is forecast to increase by 19 million tonnes. This increase in wheat supplies is forecast to outweigh an increase in wheat demand and result in the world wheat indicator price falling by around 15 per cent in 2008-09. However, low wheat stocks will provide support to prices, maintaining them at historical high levels.

Global wheat production in 2008-09 is forecast to increase to 622 million tonnes, an increase of 3 per cent on the previous year. High wheat prices in 2007 and early 2008 are expected to encourage a larger area to be sown to wheat in many northern hemisphere countries, and are also likely to result in an increased area sown to wheat in southern hemisphere countries later in the year.

World wheat consumption is forecast to increase to 616 million tonnes in 2008-09, 5 million tonnes above the previous season. The major use of wheat is for human consumption, which accounts for around 70 per cent of global consumption. However, the increase in wheat consumption forecast for 2008-09 is largely the result of a forecast increase in demand for wheat for livestock feeding purposes.

Assuming average seasonal conditions in Australia, it is reasonable to expect a sharp increase in the area sown to wheat in 2008-09. The area sown to wheat is forecast to be a record 13.4 million hectares in 2008-09. Wheat production is forecast to increase to nearly 26 million tonnes in 2008-09.

Increased Australian wheat production in 2008-09 means that wheat exports will rise by a forecast 9 million tonnes. The value of Australian wheat exports is forecast to increase to $4.7 billion - more than double the value in 2007-08. The pool return for Australian premium white wheat (APW 10) is forecast to decline by around A$80 a tonne to average A$359 a tonne in 2008-09.

Coarse grains

World coarse grain prices are forecast to remain high through 2008-09 as production and consumption remain firmly balanced for a second year. The world indicator price for coarse grains (US corn, fob Gulf) is forecast to average around US$198 a tonne in 2008-09, around US$5 a tonne higher than the previous year.

World coarse grain production is forecast to reach 1.1 billion tonnes in 2008-09 – 16 million tonnes higher than the record output of the previous year, and reflects the expectation of continuing strong grain prices. A recovery in coarse grain production in the European Union, Ukraine and Australia will more than offset a forecast decline in US corn production.

World coarse grain consumption is forecast to rise by 1 per cent to 1.1 billion tonnes in 2008-09, reflecting the continuing growth of the worldwide ethanol industry and the use of corn as a major feedstock. In the United States, the amount of corn used in ethanol production increased by 50 per cent to an estimated 81 million tonnes in 2007-08 – representing around a quarter of US corn production. Adding to the tight coarse grain market in the United States has been the strong growth in corn exports. US corn exports are estimated to have increased by 15 per cent to 62 million tonnes in 2007-08, reflecting to a large extent the effect of a weaker US dollar on price in importing country currencies and stronger demand from the European Union.
In Australia the area planted to barley is forecast to increase by 4 per cent in 2008-09, while production is forecast to increase by 51 per cent. The expected larger harvest means total coarse grain exports are forecast to increase by 83 per cent in 2008-09, with the bulk of the increase comprising shipments of barley which are forecast to increase by 80 per cent to around 5 million tonnes. The value of coarse grains exports is forecast to rise 72 per cent to around $1.8 billion, reflecting the larger volumes shipped and continued relatively high prices in the global market. In response to a forecast dramatic improvement in production, Australian grain prices are likely to fall in 2008-09, however, prices are expected to remain at relatively high levels.

Oilseeds
The world oilseed indicator price (soybeans, cif, Rotterdam), has been at record highs during 2007-08. In 2008-09 prices are forecast to increase further as increased demand (particularly for biodiesel) provides support to prices. The world oilseed indicator price is forecast to increase from an average of US$503 a tonne in 2007-08 to an average US$513 a tonne in 2008-09.

World oilseed production is forecast to increase to 405 million tonnes in 2008-09, a 4 per cent increase compared with the previous year. Production of soybeans and canola/rapeseed (two of the major oilseeds) are both forecast to increase in 2008-09. In the United States – the world’s largest soybean producer – the area sown to soybeans is forecast to increase in 2008-09. In 2008-09 the area sown in Brazil is forecast to increase once again. However, the strong appreciation of the Brazilian real against the US dollar may to some extent limit the price incentives for expanded plantings. In Canada in 2008-09 yields are forecast to return closer to historical averages and production is forecast to increase. In 2008-09 the total area sown to canola/rapeseed in the European Union is likely to fall slightly. Despite record canola prices and the policy changes to ‘set-aside’ land (reduced to zero) in the European Union, it is expected that more area will be sown to wheat.

World oilseed consumption is forecast to increase by 2 per cent to 414 million tonnes in 2008-09 compared with the previous year, as demand for oilseed products increases. Vegetable oil consumption is forecast to increase to 130 million tonnes in 2008-09, and oilseed meal consumption is forecast to rise by 9 million tonnes. The growth of biodiesel is leading to increased demand for vegetable oil, a product derived from oilseeds. Industrial use of vegetable oil has more than doubled since 2000-01, from 8.7 million tonnes in 2000-01 to 22.8 million tonnes in 2007-08. With rising investment in biodiesel plants across the world, industrial use of vegetable oils is expected to continue to increase in 2008-09.

With grains prices remaining high and early seasonal indications looking reasonably favourable, it is forecast that there will be a record area sown to winter crops in 2008-09. The area sown to canola is forecast to increase by 10 per cent in 2008-09. Australian canola prices are forecast to fall by 10 per cent in 2008-09 to average A$568 a tonne. The decrease in price can be attributed to forecast increases in production. However prices are still expected to remain high in both the short and medium term.