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Commodity outlook and financial performance of agriculture in northern Queensland

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This paper presents ABARE's current commodity outlook and the recent financial performance of some key agricultural industries in northern Queensland, highlighting the performance of beef, sugar and horticultural crop producers.

The northern Queensland region as covered in this paper is outlined in map 1. Major regional centres include Innisfail, Townsville, Charters Towers, Cooktown, Weipa and Normanton.

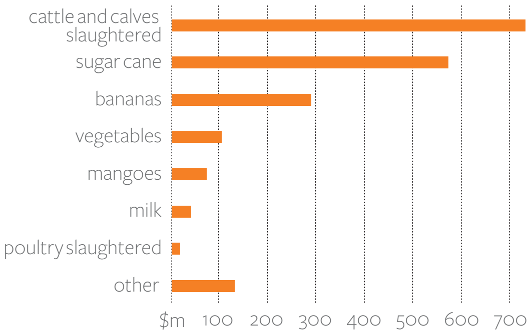
map 1 Northern Queensland region

Northern Queensland regional profile

Beef production makes a significant contribution to the value of agricultural production in northern Queensland (figure a). Australian Bureau of Statistics (ABS) data indicates beef cattle accounted for around 37 per cent ($734 million) of the region's $1.96 billion total value of agricultural production in 2004-05, while sugar cane contributed around 29 per cent ($574 million), making it the highest value crop.

Fruit production accounted for 21 per cent of the value of production, or $406 million, of which bananas contributed $289 million and mangoes almost $72 million. Vegetable production accounted for a further 5 per cent, or $103 million.

a Value of agricultural production northern Queensland

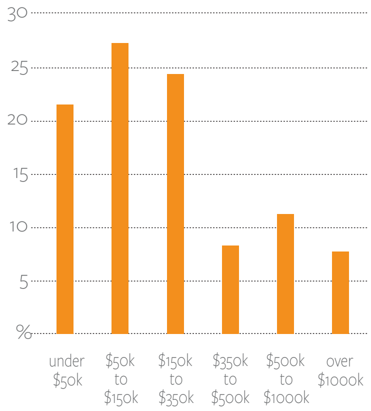


Number and type of farms

In 2004-05, there were 5059 farm businesses in the northern Queensland region with an estimated value of agricultural operations (EVAO) of $5000 or more (table 1). Sugar cane farms accounted for around 42 per cent of farms in northern Queensland, while beef cattle farms accounted for a further 28 per cent and fruit producing farms 16 per cent. Around 2 per cent of farms were classified as grain growers.

Farms are classified based on the activity generating the highest value of agricultural production for that farm.

b Distribution of farms by income, 2005-06 northern Queensland



Many farms in northern Queensland are small to medium in size. In 2005-06, slightly fewer than half of all farms had an estimated value of operations less than $150 000 as measured by the ABS (figure b). Around a quarter of farms had an EVAO between $150 000 and $350 000 and around 7 per cent or 390 farms had an EVAO of more than $1 million.

Employment

Recent ABS data indicates 256 000 people are currently employed in northern Queensland. The retail trade sector is the largest employer, accounting for around 14 per cent of the total work-force, or 35 900 people (figure c). Construction is the next largest employer, accounting for 12 per cent, or 31 000 people, followed by health and community services (10 per cent or 24 600), property and business services (9 per cent or 22 600) and manufacturing

1 Number of farms - Northern Queensland, 2004-05 a
by industry classification

	Northern Queensland		Queensland	
	no.	%	no.	%
Sugar Cane	2 127	42	4 054	15
Beef Cattle	1 402	28	12 136	45
Fruit	820	16	1 793	7
Vegetable	218	4	1 282	5
Dairy	136	3	956	4
Other crops	90	2	502	2
Grain	78	2	1 417	5
Other	188	4	4 816	18
All Industries	5 059	100	26 955	100

a Where the estimated value of agricultural operations is more than $5 000.

(8 per cent or 19 700). Agriculture, forestry and fishing accounted for 4 per cent of the workforce (10 600) and mining 3.5 per cent (9000).

C Employment profile, February, 2008
northern Queensland

Sugar Industry

In March 2007, ABARE conducted a survey of sugar cane growers across Australia on behalf of the Sugar Industry Oversight Group in collaboration with CANEGROWERS. Data from this survey provides a snapshot of sugar cane farm performance in 2005-06. A follow-up survey of sugar cane farm performance is currently being undertaken for 2006-07.

In 2005-06, there were 4824 sugar cane growers in Australia, of which 90 per cent were located in Queensland.

Nationally, cane production averaged 8250 tonnes a farm, with Queensland farms averaging 8560 tonnes. However, there was a wide dispersion of farm sizes and sugar cane production around this average. Nearly two-thirds of growers produced less than 7500 tonnes of sugar cane and in aggregate, these farms accounted for around a quarter of Australia's sugar cane production in 2005-06 (table 2). In contrast, 3 per cent of growers produced more than 30 000 tonnes, which in aggregate accounted for an estimated 22 per cent of national sugar cane production.

In 2005-06, the average area of Australian sugar cane farms was around 185 hectares, although half of all sugar cane farms operated less than 106 hectares (table 3).

2 Distribution of farms, by tonnage of sugar cane produced, 2005-06
Australian sugar cane industry

Quantity of sugar cane produced	sugar cane growers no.	share of growers %	share of production %
Less than 7500 tonnes	3 130	65	25
7500 to 15 000 tonnes	1 035	22	27
15 000 to 22 500 tonnes	349	7	16
22 500 to 30 000 tonnes	156	3	10
30 000 to 50 000 tonnes	105	2	10
More than 50 000 tonnes	49	1	12
Total	4 824	100	100

3 Distribution of farms, by selected estimates, by quartile, 2005-06
Australian sugar cane industry

		value below which specified percentage of farms lie			
		25%	50%	75%	average
Area operated	ha	55	106	200	184
Area of sugar cane harvested	ha	30	62	113	87
Quantity of sugar cane produced	tonnes	2800	6055	10650	8251

Sugar cane is normally grown on a four to five year rotation in Australia with producers harvesting up to 80 per cent of the crop area each year. The growing season required to reach harvest is around 12 months in Queensland but is between 18 and 24 months in New South Wales. The longer season in New South Wales means a lower proportion of the area under cane is harvested each year and results in higher cane yields per hectare.

Some of the largest sugar cane growers — in terms of area and quantity of sugar cane produced — were located in the Burdekin, Mackay and Herbert regions of Queensland. The use of irrigation water is also most widespread in these regions, with the majority of crops receiving at least one application of water in 2005-06. In contrast, producers in New South Wales and southern Queensland tend to have smaller farms and use little or no irrigation water.

In 2005-06, total cash receipts for sugar cane growers averaged around $281 000 per farm, of which almost 80 per cent was from the sale of sugar cane. Non-sugar related receipts were mainly from the sale of beef cattle and crops such as peanuts, oilseeds (principally soybeans), vegetables and fruit.

Farm cash income for sugar cane growers averaged around $66 580 per farm in 2005-06 (table 4). However, an estimated 27 per cent of producers reported negative farm cash incomes. Most farms reporting negative farm cash incomes were smaller sugar cane growers producing less than 7500 tonnes.

Box 1 Farm cash income and business profit definitions

Farm cash income is a measure of the cash funds available for farm investment and consumption after paying all cash costs incurred in production, including interest payments, but excluding capital payments and payments to family workers.

Farm business profit is a longer term measure of profitability that takes account of capital depreciation changes in on-farm inventories

Nearly two-thirds of sugar cane growers across all regions reported farm business losses in 2005-06. However, the 2005-06 survey results indicate that in all regions, financial performance improved as the scale of sugar cane production increased. For example, in the Burdekin, farms producing less than 15 000 tonnes of sugar cane reported a loss of $40 220 compared with a profit of $22 400 for farms producing 15 000 to 30 000 tonnes and around $357 600 for farms producing more than 30 000 tonnes (table 4).

In 2005-06, the average return on capital (excluding capital appreciation) for sugar cane growers is estimated to have been 1.4 per cent. When capital appreciation is taken into account,

4 Selected financial performance of sugar cane growers, by region and size group, 2005-06 Australian sugar cane industry average per farm

		under 15 kt	15–30 kt	over 30 kt	average
Farm cash income					
New South Wales	$	35 961	na	na	37 455
Far North Queensland	$	34 056	173 112	580 824	64 686
Herbert	$	57 070	247 050	429 208	87 947
Burdekin	$	12 850	94 856	580 374	68 462
Mackay	$	56 161	191 592	341 883	86 721
Bundaberg	$	25 450	233 382	na	44 312
Southern Queensland	$	31 568	na	na	31 568
Ord River	$	na	na	na	454 292
Australia	$	38 672	177 801	491 901	66 579
Farm business profit					
New South Wales	$	–11 638	na	na	–10 661
Far North Queensland	$	–3 665	64 375	444 422	16 377
Herbert	$	15 140	174 087	269 297	39 795
Burdekin	$	–40 220	22 402	357 579	–342
Mackay	$	4 430	82 265	186 166	22 813
Bundaberg	$	–22 859	142 057	na	–8 892
Southern Queensland	$	–33 613	na	na	–33 613
Ord River	$	na	na	na	366 405
Australia	$	–8 284	83 205	316 649	10 099
Rate of return excl. capital appreciation					
New South Wales	%	–0.4	na	na	–0.3
Far North Queensland	%	0.3	2.5	6.4	1.6
Herbert	%	2.6	7.0	4.9	4.0
Burdekin	%	–0.3	2.7	4.9	1.8
Mackay	%	0.9	3.2	3.8	1.8
Bundaberg	%	–0.8	3.4	na	0.3
Southern Queensland	%	–1.0	na	na	–1.0
Ord River	%	na	na	na	7.1
Australia	%	0.3	3.4	4.7	1.4
Rate of return incl. capital appreciation					
New South Wales	%	2.9	na	na	3.0
Far North Queensland	%	1.6	2.7	11.1	3.1
Herbert	%	9.3	13.9	11.2	10.7
Burdekin	%	7.8	8.0	6.3	7.4
Mackay	%	5.0	8.3	33.4	9.9
Bundaberg	%	4.2	3.6	na	4.8
Southern Queensland	%	21.1	na	na	21.1
Ord River	%	na	na	na	25.0
Australia	%	5.5	7.0	16.4	7.4

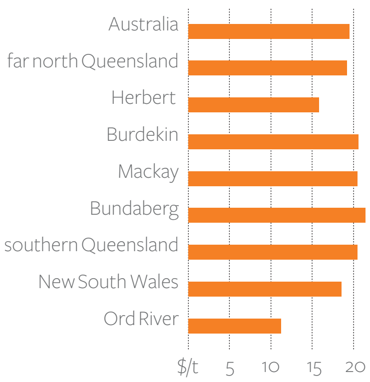
na Not available because of insufficient sample size.

primarily increases in land values, the average rate of return is estimated at around 7.4 per cent. Large growers (those producing more than 30 000 tonnes) had the highest average rate of return on capital (excluding capital appreciation) at 4.7 per cent, reflecting their ability to generate higher profits per dollar of capital invested than smaller farms.

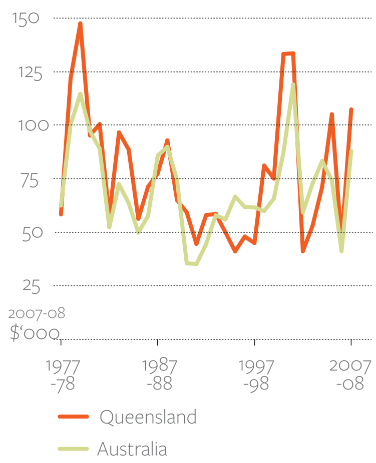
In 2005-06, the cash costs of sugar cane production averaged around $160 800 per farm, ranging from $67 660 for growers producing less than 7500 tonnes of cane to around $1.7 million per farm for growers producing more than 50 000 tonnes of cane.

Across all farms, harvesting costs and fertilisers were the largest cost items accounting for nearly half of total sugar cane related production costs in 2005-06. Other major cost items included fuel, repairs and maintenance, interest payments, and hired labour.

d Unit cash costs of production, by region, 2005-06



e Farm cash income, all broadacre industries



Overall, the average unit cost of producing sugar is estimated to have been $19 a tonne in 2005-06 (figure d). However, there was considerable variability in the estimated unit cost of production between sugar growing regions and size groups. On average, the lowest cost producers in 2005-06 were located in the Ord River region of Western Australia and the Herbert region of Queensland. Unit production costs are estimated to have been the highest in the Burdekin and Bundaberg regions, averaging around $21 a tonne in 2005-06.

The survey results suggest there may be some economies of size in the Australian sugar cane growing industry because estimated average unit costs of production were lower for farms producing higher quantities of sugar cane. The average unit cost of production for the smallest sugar cane growers is estimated to have been around $20 a tonne in 2005-06 (table 5) compared with around $18 a tonne for the largest growers. Data from future surveys will help to confirm these results.

Broadacre industry

Australia

Australian broadacre farm financial performance is projected to strengthen 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 $88 000 per farm (figure e). 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 more than the increase in farm cash income in 2007-08 (table 6). This largely reflects an increase in the value of trading stocks as producers increase livestock numbers and replenish on-farm inventories of fodder and grain.

5 Gross margin of sugar cane producers, by region and size group, 2005-06 Australian sugar cane industry average per farm

	under 15 kt	15–30 kt	over 30 kt	average
	$/t	$/t	$/t	$/t
Average sugar cane price				
New South Wales	24	na	na	24
Far North Queensland	26	26	28	26
Herbert	27	26	26	26
Burdekin	28	31	29	29
Mackay	29	29	29	29
Bundaberg	31	30	na	30
Southern Queensland	30	na	na	30
Ord River	na	na	na	34
Australia	27	28	29	28
Average sugar cane cash cost of production				
New South Wales	19	na	na	19
Far North Queensland	18	21	20	19
Herbert	16	15	16	16
Burdekin	25	21	17	21
Mackay	21	20	19	20
Bundaberg	25	15	na	21
Southern Queensland	20	na	na	20
Ord River	na	na	na	11
Australia	20	19	18	19
Sugar cane gross margin				
New South Wales	4.5	na	na	4.7
Far North Queensland	7.8	4.7	8.0	6.9
Herbert	10.0	10.8	9.7	10.2
Burdekin	2.5	9.0	12.2	8.1
Mackay	7.1	8.5	9.7	8.0
Bundaberg	5.2	13.6	na	7.6
Southern Queensland	8.3	na	na	8.3
Ord River	na	na	na	22.2
Australia	6.6	8.4	10.7	8.1

na Not available because of insufficient sample size.

Queensland

Broadacre farm incomes in Queensland improved modestly in 2003-04 and 2004-05 from the drought affected incomes of 2002-03. Increased beef cattle sales and higher beef prices contributed to a sharp increase in farm incomes in 2005-06. However, the widespread failure of crops across Queensland in 2006-07 and lower

6 Selected physical and financial performance indicators - all broadacre industries

average per farm

		Queensland				Australia			
		2005-06	2006-07		2007-08 p	2005-06	2006-07		2007-08 p
Physical									
Area operated at 30 June	ha	15 823	12 178	(8)	9 705	6 558	6 210	(5)	5 012
Area sown to crops	ha	171	161	(17)	209	359	357	(4)	309
Sheep on hand at 30 June	no.	454	386	(22)	474	1 445	1 318	(4)	1 359
Beef cattle on hand at 30 June	no.	988	996	(6)	1 037	370	356	(4)	358
Beef cattle sold	no.	330	293	(6)	289	141	139	(5)	129
Receipts									
Crops	$	46 840	43 500	(219)	98 000	130 400	87 400	(77)	125 000
Sheep and lamb sales	$	6 670	5 000	(30)	6 000	41 280	36 000	(5)	40 000
Wool sales	$	9 690	11 700	(24)	12 000	30 990	35 700	(5)	38 000
Beef cattle sales	$	276 490	228 900	(7)	210 000	111 210	98 200	(6)	90 000
Total cash receipts	$	410800	350400	(5)	360000	355610	302100	(3)	333000
Costs									
Sheep and lamb purchases	$	1 040	1 200	(33)	1 000	9 010	6 300	(10)	4 000
Beef cattle purchases	$	50 720	45 600	(15)	21 000	25 300	22 000	(10)	12 000
Seed	$	3 770	4 200	(13)	4 000	3 520	3 800	(7)	3 000
Fodder	$	29 410	32 700	(14)	18 000	11 680	18 500	(7)	9 000
Agistment	$	5 440	7 100	(30)	2 000	1 790	3 200	(27)	1 000
Fertiliser	$	3 640	5 500	(17)	6 000	26 500	23 400	(5)	25 000
Sprays	$	7 890	5 400	(11)	6 000	17 620	15 500	(5)	16 000
Fuel, oil and lubricants	$	25 100	20 300	(5)	22 000	24 060	20 600	(3)	21 000
Repairs and maintenance	$	30 120	27 300	(5)	31 000	24 990	23 700	(3)	25 000
Administration expenses	$	11 550	13 100	(12)	13 000	10 370	10 400	(5)	10 000
Rent and rates	$	10 440	10 700	(8)	10 000	13 600	13 700	(4)	13 000
Interest payments	$	33 610	41 600	(10)	48 000	25 320	32 400	(5)	35 000
Hired labour	$	15 150	15 100	(9)	15 000	11 100	10 000	(6)	10 000
Total cash costs	$	305730	303100	(6)	253000	281370	261000	(3)	245000
Financial performance									
Farm cash income	$	105 070	47 300	(23)	107 000	74 240	41 100	(12)	88 000
Farm business profit	$	- 6 250	- 7 700	(151)	134 000	- 8 190	- 52 600	(10)	23 000
Rate of return									
– excl. capital appreciation	%	0.9	0.9	(30)	4	0.8	-0.4	(39)	2
– incl. capital appreciation	%	10	14	(11)	na	7	8	(9)	na
Farm capital and debt									
Total capital value	$	4 589 260	5 347 900	(5)	na	3 466 940	3 713 400	(2)	na
Total farm debt at 30 June	$	494 010	596 300	(9)	483 000	360 540	450 600	(4)	362 000
Equity ratio at 30 June	%	89	88	(1)	na	90	88	1	na

p Projection based of information collected by telephone survey in November 2007.
Note: Figures in parentheses are standard errors expressed as per centages of the estimate provided.

saleyard prices for cattle resulted in average incomes falling by more than 50 per cent to around $47 000.

Farm income is projected to improve in 2007-08 as improved seasonal conditions result in increased receipts from both winter and summer crops, particularly sorghum, in combination with higher wool and sheep receipts and a reduction in fodder and agistment costs. In 2007-08, beef cattle receipts are forecast to fall as farms reduce cattle turnoff and rebuild beef cattle numbers.

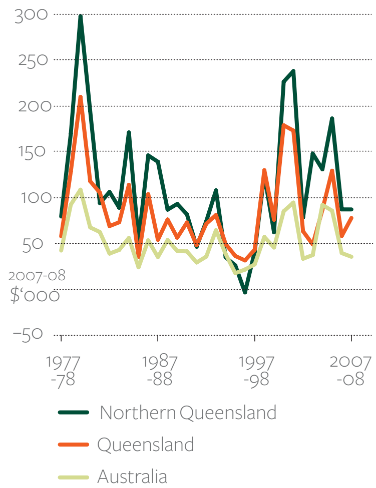
Reduced cattle turnoff and an increase in the number of calves is projected to result in higher numbers of beef cattle. In combination with increased grain stocks, this is projected to lead to higher values of on-farm inventories and improved farm business profit.

Beef industry

Queensland and northern Queensland

In 2006-07, farm cash incomes of beef specialist producers (defined as farms with the majority of their income derived from beef cattle sales) fell. Fewer beef cattle were sold in 2007 as producers began rebuilding herd numbers following high turnoff during 2006. In 2006-07, receipts from beef cattle fell by around 15 per cent while cash costs remained relatively high and farm cash income for Queensland beef industry farms halved, to average around $60 000 per farm (figure f).

f Farm cash income, beef farms



In 2007-08, farm cash income is forecast to improve by almost 30 per cent to around $78 000 per farm. Total cash receipts are projected to fall slightly as cattle turnoff is further reduced, but cash costs are projected to fall by more as beef cattle purchases slow. Beef cattle numbers are projected to rise again in 2007-08 reflecting improved seasonal conditions.

Northern Queensland experienced dry conditions early in 2006-07, but above average rainfall during the summer months boosted pasture growth and water availability. Producers began rebuilding herd numbers and the decline in cattle turnoff reduced farm cash income by more than $40 000 compared with 2005-06.

Improved seasonal conditions continued into 2007-08, however, cash receipts are forecast to be similar to those in 2006-07. Significant increases in cash costs are forecast to result in lower farm cash income.

Vegetable industry

There were around 2880 commercial vegetable farms with an EVAO greater than $40 000 in 2005-06. Around a quarter of these were in Queensland.

The majority of Australian vegetable growers are small in terms of the total area cropped. The average area sown to vegetable crops on Queensland vegetable farms in 2005-06 was 29ha, compared with an average 36ha for all Australian vegetable farms (table 7). However, the value of production of Queensland farms was higher on average. In 2005-06 cash receipts for Queensland vegetable farms averaged $843 000 compared to the Australian average of around $638 000 per farm (table 8).

Around 58 per cent of Queensland farms were estimated to produce only one type of vegetable, with the remaining 42 per cent producing two or more vegetable crops. For Australia, 64 per cent were estimated to produce one crop and 36 per cent two or more (table 9). Potatoes are the major vegetable crop in all states in

7 Distribution of vegetable growing farms, by area sown to vegetables Queensland and Australia, 2005-06

		value below which specified percentage of farms lie			
		25%	50%	75%	average
Queensland	ha	4	15	44	29
Australia	ha	4	14	46	36

8 Financial performance, vegetable growers, by state, 2005-06
average per farm

		Queensland		Australia	
Total cash receipts	$	843 280	(21)	638 170	(9)
Total cash costs	$	681 260	(22)	485 210	(10)
Farm cash income	$	162 020	(24)	152 960	(12)
Per cent of farms with negative cash income	%	25	(26)	24	(16)
Buildup in trading stocks	$	7 050	(95)	2 030	(84)
Farm business profit	$	71 140	(51)	66 410	(26)
Rate of return					
– excl. capital appreciation	%	3.2	(33)	3.2	(19)
– incl. capital appreciation	%	9.8	(32)	9.2	(16)
Total farm debt at 30 June a	$	310 880	(20)	224 100	(11)
Total farm capital at 30 June	$	3 567 920	(20)	3 084 000	(7)
Farm equity ratio a	%	88	(2)	92	(1)

a Average per farm responding to questions on debt.

9 Distribution of vegetable growing farms, by number of vegetable crops, Queensland and Australia, 2005-06

		1 crop	2 crops	3 crops	more than 3 crops
Queensland	%	58	21	12	9
Australia	%	64	9	15	12

terms of area sown, value of production, and volume of consumption. In northern Queensland, melon crops including watermelons, rockmelons and honeydew melons, are substantial contributors to the total value of vegetable operations.

In 2005-06, farm cash income for Queensland vegetable growers averaged $162 000, slightly more than the national average of $153 000.

Commodities summary

ABARE's assessment of the outlook for world economic growth is provided in ABARE's quarterly forecasting journal, Australian Commodities. Also included in Australian Commodities are market forecasts and detailed discussions for major Australian agricultural, mineral and energy commodities. The forecast summaries presented here for a number of the commodities important to this region are based on information in the March 2008 issue of Australian Commodities, which is included in delegate satchels.

Seasonal conditions update

The Australian Bureau of Meteorology in its seasonal rainfall outlook for the May to July period (23 April 2008), indicates there is a moderate to strong shift in the odds favouring a wetter than normal season through southern Queensland and northern New South Wales.

Over northwest and southern Queensland and far north New South Wales, the chances of exceeding median rainfall from May to July are between 60 and 70 per cent. In far north Queensland, the chance of exceeding median rainfall is around 50 to 55 per cent and over the rest of the country the chance is 45 to 60 per cent.

The Bureau also stated that the La Niña event in the Pacific Basin is weakening. Computer models indicate a return to neutral conditions over the May to July period. La Niña events typically bring wetter than normal conditions across much of the eastern half of Australia.

Sugar

The world indicator price for sugar (Intercontinental Commodities Exchange no. 11 spot, fob Caribbean) is estimated to average US12.1 cents a pound in 2008-09, a 7 per cent decrease on the average for 2007-08. In 2007-08 sugar prices have been buoyed by strong demand for sugar cane and molasses as feedstocks for ethanol production and the prospects of further cuts in sugar beet production in the European Union. The introduction of a range of market support policies in India, including export and storage subsidies, have the potential to depress world sugar prices, but do not appear to be having an effect so far.

Higher global prices for sugar will lead to improved returns for Australian producers. However, Australian producers will not receive the full benefits of the increase in world prices mainly because of an assumed appreciation of the Australian dollar in 2007-08.The average price received by Australian cane growers for 2007-08 sugar cane is forecast to be similar to that for 2006-07.

Heavy rains in the main sugar cane producing regions of Queensland in early 2008 have generally boosted prospects for Australian sugar cane production in 2007-08, despite some isolated flood damage to cane crops. Australian sugar production is forecast to recover to around 4.85 million tonnes (raw sugar terms) in 2007-08, 3 per cent higher than in 2006-07. Increased production is despite a reduction of 3 per cent in the area harvested. Heavy rain is also expected to lead to increased production in 2008-09 as irrigation dams are replenished and irrigation aquifers recharged.

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 second half of the year.

Reflecting 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 and 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. In 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.

Dairy

World prices for major dairy products rose sharply in 2007-08 and 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 increase at a relatively slow rate. Production in the major dairy exporting areas 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, particularly in developing countries in Asia. Demand is also expected to be strong in developed regions 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 a litre 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 relatively high forecast farm-gate milk prices reflect the ability of the dairy industry to benefit from strong world prices for dairy products.