

Box D

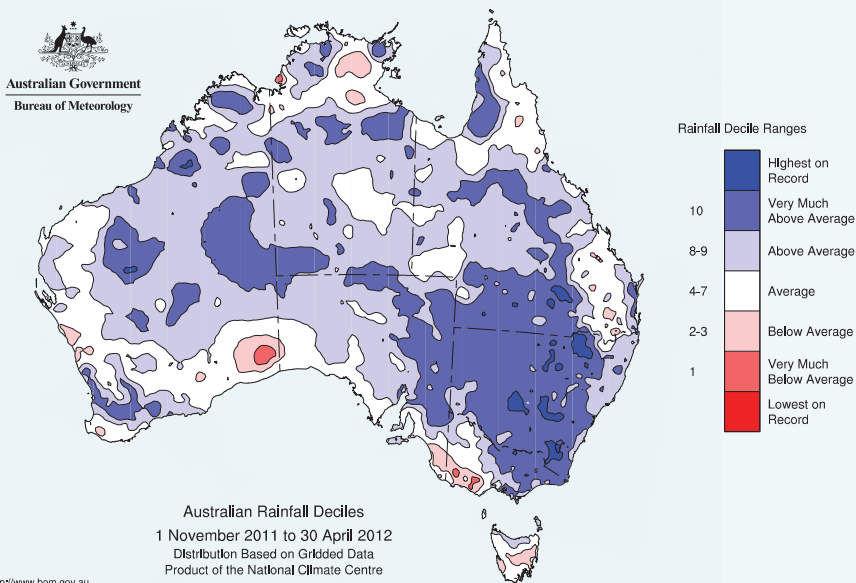
Conditions in the Farm Sector

Over the past six months, much of Australia has experienced above-average rainfall associated with the La Niña weather system (Graph D1). While this has resulted in flooding in some parts of eastern Australia, with associated damage to property, infrastructure and some summer crops, it has also provided more water for crops, increased subsoil moisture and replenished dams and irrigation supplies. This box outlines the effect that recent weather conditions have had on farm production and summarises current conditions in the farm sector.

Despite the damage to infrastructure and crops from flooding, the La Niña weather system has been associated with record crop production. The winter crop for 2011 is expected to be at a record level,

largely reflecting a bumper wheat harvest. This was driven by a substantial increase in Western Australia's wheat crop, as above-average rainfall in late 2011 boosted yields following a drought-affected 2010. However, while above-average rainfall tends to have a positive effect on wheat production, it has also resulted in some of the crop being downgraded to feed quality, reducing the prices received by farmers. The increase in subsoil moisture and increased availability of irrigation water should also support crop yields in the near-term. The Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) estimates that the summer crop (including cotton, sorghum and rice) is likely to be at a record level in 2011/12. In contrast, livestock

Graph D1
Australian Rainfall Deciles
1 November 2011 to 30 April 2012

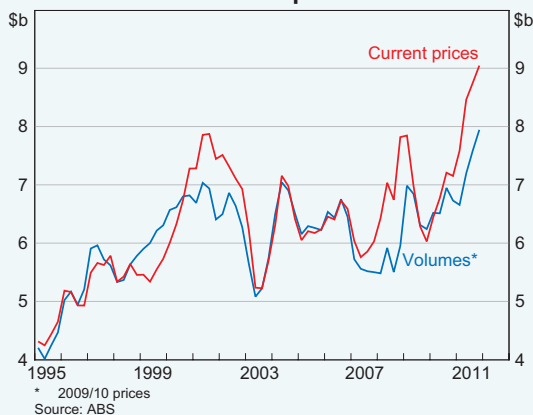


Source: Bureau of Meteorology

production, which accounts for a little less than half of farm production, is expected to remain largely unchanged in 2011/12 since favourable seasonal conditions will encourage farmers to rebuild herds at the expense of slaughtering.

The high levels of farm production over the past year have led to strong growth in rural exports, which accounted for around 10 per cent of the value of total exports in 2011. Rural export volumes grew by 18 per cent over 2011, with particularly large increases in grain exports (Graph D2). Despite the high level of farm production, there has been a reported 8 per cent fall in agricultural employment over 2011. Although the fall in employment was broad based, the largest falls were recorded in New South Wales and Western Australia, where the sector may be competing for labour with the mining industry.

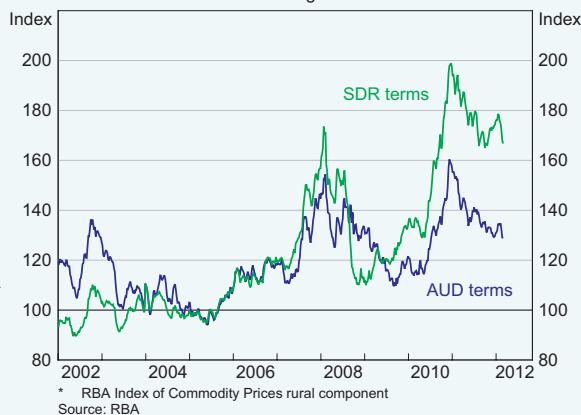
**Graph D2
Rural Exports**



Farm Prices and Incomes

Global prices for agricultural commodities have generally eased over the past year, but remain at high levels. Rural export prices are also relatively high in Australian dollar terms, although the increase over recent years has been less pronounced than in global prices reflecting the appreciation of the Australian dollar over this period (Graph D3).

**Graph D3
Rural Prices***
2005 average = 100



The longer-term increase in agricultural prices has been driven in large part by rising global demand; for example, food consumption per capita has increased strongly in developing countries such as China in response to rising incomes.¹ The demand for grains has also risen strongly because of their use in animal feed and biofuels.

Supply-side factors have also significantly influenced price movements in recent years, with adverse weather conditions in major cropping regions of the world having temporarily bolstered some rural prices. While the La Niña weather system increases rainfall in Australia, it tends to reduce rainfall in other major wheat-producing regions. Droughts in other parts of the world during 2010 and 2011 reduced wheat production putting upward pressure on prices. More recently, however, global supply has recovered and prices have eased.

Reflecting the strong level of both production and prices, real farm incomes in Australia increased strongly in 2010/11 and are expected to remain at a high level in 2011/12. ABARES forecasts that farm profits will be positive across all states and all farming industries in 2011/12, the first time this

¹ See Rayner V, E Laing and J Hall (2011), 'Developments in Global Food Prices', *RBA Bulletin*, March, pp 15–21.

will have occurred in over 30 years. The increase in farm incomes is being offset to some extent by the upward pressure on the cost of farming inputs such as fertiliser.

While the farm sector is a relatively small part of the Australian economy, the large swings in farm production mean that it remains an important source of variation in the aggregate economy. Annual output growth in the farm sector is on average over eight times more volatile than non-farm output growth. Farm GDP grew by over 7 per cent in year-average terms in 2010/11, contributing around $\frac{1}{4}$ percentage points to GDP growth of 2 per cent. Output in the farm sector is anticipated to remain at high levels over the next few years. ✎