The Merino Wool Market: What Has Gone Right and Can it Continue?

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and
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What Has Gone Right for Merino Wool?
Merino Wool Prices on a High: Australia and South Africa

Source: AWEX, NZ Wool Services, Capewools, BWMB
Data to 29th March 2018
## Merino Wool Price Supercycles

<table>
<thead>
<tr>
<th>Date</th>
<th>Peak Price*</th>
<th>Price change - start to peak*</th>
<th>Weeks - start to peak</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>UScents</td>
<td>Acents</td>
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<td>Acents</td>
</tr>
<tr>
<td>February 1986 to May 1988</td>
<td>1203</td>
<td>1582</td>
<td>+743 (+162%)</td>
<td>+925 (+140%)</td>
</tr>
<tr>
<td>April 1993 to March 1995</td>
<td>707</td>
<td>949</td>
<td>+379 (+116%)</td>
<td>+496 (+107%)</td>
</tr>
<tr>
<td>November 2001 to January 2003</td>
<td>709</td>
<td>1211</td>
<td>+350 (+97%)</td>
<td>+501 (+71%)</td>
</tr>
<tr>
<td>May 2010 to June 2011</td>
<td>1512</td>
<td>1434</td>
<td>+789 (+109%)</td>
<td>+564 (+65%)</td>
</tr>
<tr>
<td>April 2016 to March 2018</td>
<td>1439</td>
<td>1830</td>
<td>+540 (+60%)</td>
<td>+586 (+48%)</td>
</tr>
</tbody>
</table>

* Based on the Australian Eastern Market Indicator, 2017/18 basis
+ Peaked at 2nd March 2018
General Price Rise for Commodities
(US$ basis)

Index: Jan 2016=100

Source: The Economist metals and commodity prices US$ index; AWEX EMI in US$. Cotton Outlook for cotton and Mackenzie Wood PCI Fibres for polyester staple and acrylic
Data to 29th March 2018
Drivers of Demand for Merino Wool

• Economic conditions, consumer incomes and consumer confidence
• Retail sales of clothing
• Consumer tastes and preferences
  – Business vs casual or a blend?
  – Fast fashion
  – Sustainability
  – Luxury
• Prices for competing fibres
• Stocking and destocking of the wool textile pipeline
World Economic Events and Merino Wool Prices

Australian Eastern Market Indicator

US cents/kg


Strong global economy, USSR buying, China Wool Wars

World economic recovery, cotton prices to records, very strong A$

Double-faced woollen fabric mania

World economic growth grows solidly, low Merino supply

USSR implodes, Tiananmen Square. RPS collapses

Asian Financial Crisis

Global Financial Crisis

Euro debt crisis

Stockpile sold, supply squeeze

World economic ‘dead-cat’ bounce post-RPS

Source: AWEX – 2017/18 basis
Data to 29th March 2018
Improved economic growth forecasts in all key countries: China, Germany, Japan, France, Italy, US, UK and Korea

Driven by higher investment, trade, helpful economic and financial policies and improved confidence

Consumer confidence at near 20 year highs in US and EU

Clothing retail sales better in most major wool consuming countries

Source: World Bank, Global Economic Prospects, January 2018
China Drives the Increased Demand for Wool Calendar Year

Note: From the five major exporting countries (Australia, New Zealand, Argentina, Uruguay and South Africa)
Source: Australian Bureau of Statistics, FLA, SUL, Capewools, Beef + Lamb NZ
Apparel wool consumption is apparel NDA at retail average 2015-2017 as estimated by Poimenma Analysis. Income is US$ GDP per head in 2017 on a purchasing power parity basis.
World Trade in Wool Clothing in 2016 (% share)

- Knitwear: 35%
- Women's overcoats: 15%
- Men's trousers: 10%
- Men's jackets: 11%
- Men's suits: 11%
- Men's overcoats: 6%
- Other women's wear: 12%

Source: Foreign Trade Statistics, International Trade Centre, Poimena Analysis & Delta Consultants
Longer Term Outlook Positive

• Growing demand for fine Merino wool
• Long-term prospects for wool depend on global economic conditions and income growth, not relative production with other fibres
• Demand for **business-wear for men** will continue to be a mainstay for wool
• Knitwear a growth area, particularly with increased demand for **active leisurewear and casual garments**
• Coats the best performers in womenswear for wool
• Trade in other women’s wool clothing recovering a little
Product Segment Prospects:
Growth Opportunities For Merino Wool

Growth

Mainstay

Decline
Total and Merino Wool Production Stable At Lows

2016 total production
1,130.8 mkg clean

2017 total production
1,136.9 mkg clean

2018 total production
1,145.7 mkg clean

Near 70 year lows

Stocks:Use ratio
~8%

Source: IWTO, Country statistics, Poimena Analysis
Updated March 2018
But, Superfine Wool Production Remains High

Source: Poimena Analysis, AWTA, NZWTA, Cape Wools, FLA, Delta, American Sheep Industries, China Wool Textile Association.
Updated: March 2018
Australia Dominates Global Merino Wool Production share - 2017

Source: AWTA, AWEX, NZWTA, CapeWools, FLA, ASI, Delta Consultants, estimates by Poimena Analysis
Can It Continue for Merino Wool – What Are The Risks?
Risks to Global Economic Growth

- Rising interest rates
- Global financial imbalances
- Credit risks in China
- Potential for a trade war – Trump Administration’s unilateral action
Wool Garment Exports from China Falling Back
(12 month moving aggregate)

Source:  China Customs and China Wool Textile Association
Data to January 2018
Merino Wool’s Price Ratios With Other Fibres Rises to New Level

Price Ratio

Source: AWEX, Cotton Outlook, PCI Fibres, CIRFS, Poimena Analysis
Compared with 21 micron wool. Data to March 2018
Shift to Crossbred Wool in Australia

Crossbred wool share of total wool production has increased:
- 11% in 1991/92
- 12% in 2002/03
- 13.5% in 2008/09
- 17.2% in 2017/18

Has the Decline in Merino Breeding Ewes in Australia Come to an End?
“Sooner or later coarse crossbred values will sink to a low level… On the other hand, the world’s supply of merino wool is decreasing steadily… Is it not time to pause and consider well whether the outlook in regard to wool production is sound? If we are to preserve our wool supremacy in the future we must preserve our merino flocks.”

The Sydney Mail, 24th July 1918
Constraints on Merino Wool Production

• Available land in a suitable climate
• Competing land uses
  – Cropping
  – Forestry
  – Dairy
  – Beef
• Lamb and sheepmeat demand and prices
• Relative profitability
• Technology and productivity gains
Summary of Key Drivers

1. Higher economic growth leading to upturn in commodity prices (including Merino wool)
2. High consumer confidence and higher clothing retail sales growth
3. Increased raw wool demand, notably from China
4. Increased use of Merino wool in active and leisurewear?
5. Low production of Merino wool
6. Virtually no stocks left

BUT

1. Risks to global economy
2. High price relativity for Merino wool against competing fibres
3. Lower trade in wool clothing, including men’s suits
4. Increased Merino wool production constrained
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<td>March 1995 to May 1996</td>
<td>-232</td>
<td>-343</td>
<td>475</td>
<td>606</td>
</tr>
<tr>
<td>January 2003 to December 2005</td>
<td>-229</td>
<td>-562</td>
<td>480</td>
<td>649</td>
</tr>
<tr>
<td>June 2011 to September 2012</td>
<td>-549</td>
<td>-501</td>
<td>963</td>
<td>933</td>
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Thank You!