agribusiness

Economic Report

Rural Commodities Wrap

Vyanne Lai, NAB Agribusiness Economist

April 2013

- **Global financial markets are digesting latest Euro-zone crisis (Cyprus) where bank depositors are being forced to take losses. Pre-crisis global financial markets had been on a strong rally, especially against the background of still sluggish economic performance in the big advanced economies. Commodity prices are less buoyant.**
- **There are some "green shoots" in the domestic economy but overall conditions and confidence as indicated by the latest NAB Monthly Business Survey are still subdued.**
- **The domestic poultry industry is gaining traction but pig industry continues to face stiff import competition.**

2012-13 Outlook, Rural Prices & Production		
Commodity	**Production**	**Price**
Wheat	-25%	16%
Beef	2%	-13%
Dairy	-2%	1%
Lamb	2%	-17%
Wool	0%	-13%
Sugar	15%	-23%
Cotton	-11%	-15%
Oil	–	-2.3%

Source: NAB Group Economics

These forecasts represent year-on-year average changes in Australian production and corresponding AUD prices between 2011-12 and 2012-13 financial years

The protracted and confusing process of dealing with Cyprus's banks eroded financial market confidence in late March and the decision to "bail-in" depositors has only added to the confusion. Is this a "one off" tax on deposits or is it a new template for Euro-zone handling of crises? Global equity markets had been rallying strongly since last November and measures of volatility in mid-March were back at levels that had not been seen since the first half of 2007, before the first rumblings of what became the global financial crisis. Having said that, the extent of the damage done to global equity prices from this Euro-zone crisis has been quite limited. The previous upward market trend was arrested as several big equity markets levelled off, but they did not fall as had been seen in similar episodes before.

Growth in global industrial output and trade picked up through late 2012/early 2013 after poor performance for most of last year. Business surveys in big advanced economies also improved as sentiment on future output turned more optimistic. Even after accounting for better economic fundamentals, financial markets appear to have got ahead of improvements in the real economy, partly reflecting lowered risk aversion, as the tail risks of Euro-zone break-up, Chinese hard landing and excessive fiscal tightening in the US have receded.

Revised national accounts numbers show that the level of economic activity in the US and Japan in late 2012 was not as weak as initially feared. Real GDP fell in the UK and the Euro-zone but it increased very slightly in the US and Japan. The emerging market economies also experienced a slowdown in the pace of growth through 2012. India and Brazil experienced a marked softening and their situation was further complicated by high inflation. Indian CPI inflation reached double digit rates at the end of 2012 and into early 2013 while the Brazilian CPI was up by around 6½% yoy in early 2013, well above the central bank's target rate. Chinese growth was slowing until it started picking up in late 2012, with the latest March quarter national accounts showing annualised growth of 7.7%, an outcome that is deemed to be "stable" by the Chinese authorities. Chinese industrial output began growing faster towards the end of last year but sentiment has suffered recently as tighter policy on housing is again being announced.

While there are some signs of improved atmospherics in the Australian economy, including from the latest national accounts, the outlook is still subdued. The latest NAB survey points to continuing weakness in conditions, confidence and forward orders. Given the GDP outcome for Q4 and an upward revision to Q3, we have strengthened our forecast for 2013 moderately since our last report, with growth expected to be 2.4% (up from 2.0%) and unemployment rising to around 5¾% by late 2013 (unchanged). That said, we have removed one of our forecast rate cuts and delayed the timing. We now expect the RBA to cut rates by 50 points in 2013, with the most likely scenario being a cut in June in response to a deteriorating labour market, and November.

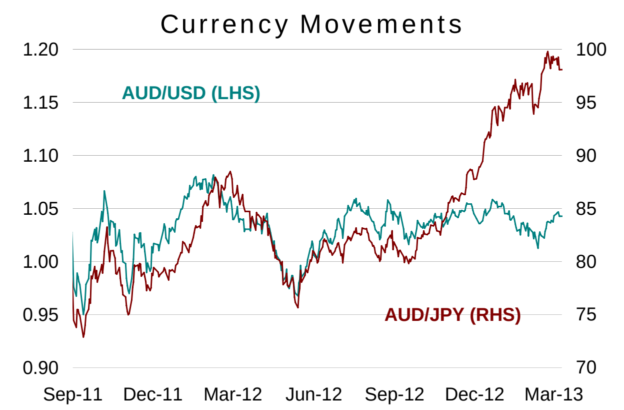
For the farm sector, most agricultural commodity prices have had a solid run over February and March. Global grains prices, except for wheat, have ticked higher in recent months due to strong demand for animal feed and tight global supplies, while wheat has suffered an opposite fate from recovering production in Europe. Livestock prices at saleyards have recorded moderate growth to return to more normal levels despite higher slaughtering numbers. Global dairy prices are approaching the historical high in March 2011 from critical supply shortage in New Zealand from drought conditions. On the contrary, excess surplus is weighing on sugar prices but cotton continued to inch higher from China driven speculative demand. This month, poultry and pork are our commodities in focus.

Currency Movements

February proved to be a weak month for the AUD/USD as the currency slipped steadily throughout the month and the first few days of March. The parity benchmark was tested when the AUD/USD fell to 1.01 on 5 March, followed a succession of weak Chinese purchasing managers' surveys covering both manufacturing and services and news of the Chinese government tightening lending standards and introducing new property taxes aimed at curbing the re-emergence of a house price boom. Since then, the exchange rate has recovered some ground to be around the 1.05 mark, owing to decent local data of retail sales and Q4 GDP, as well as RBA's decisions to keep the cash rate on hold in March and April.

The speed at which the AUD/USD rebounded from its early March trough and its subsequent resilience in the face of a strengthening USD has prompted our currency strategists to lift their forecasts slightly through 2013. They now expect the exchange rate to be at 1.03 by mid-year (previously 1.01) and 1.01 at the end 2013 (previously 0.99). A sustained drop through parity is deemed to be likely only in the event of a much stronger USD, which to some extent is limited by the current flow of the US Federal Reserve's quantitative easing program. On the domestic side, downside risks on the exchange rate will stem from further poor economic news from China and other parts of emerging Asia.

AUD weaker as global risk appetite rises



Source: Datastream

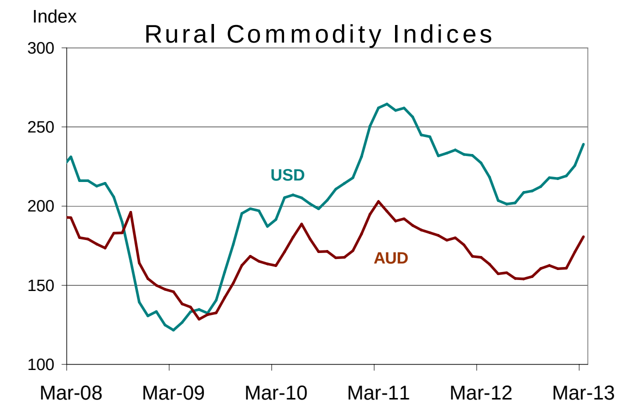
NAB Rural Commodity Index

Global commodity prices continued to track higher in February and March, with the NAB Rural Commodity Index in USD terms in the month growing by 3.0% and 6.0% in February and March respectively. The index in AUD terms grew even more strongly over the same period, by 6.3% in February followed by 5.6% in March, with a number of main Australian exported commodities recording sharp price growth. Driving the AUD index price higher over the two months were price gains in beef, dairy, wool, lamb and cotton, partly offset by price falls in sugar and wheat while the price of barley remains unchanged. In the near term, the rising trend of the commodity index is likely to slowdown, with support coming mainly from the skyrocketing dairy prices, and some extent, cotton, which will be offset by falling prices of beef, lamb, grains and the softs of wool and sugar.

NAB Farm Input Indices

Input prices rose in February and March, with the NAB Weighted Fertiliser Index tracking higher by 3.0% and 5.4% in the two months respectively. Underlying the rise were

Input prices range-bound, look to rise in 2013 Q2 onwards



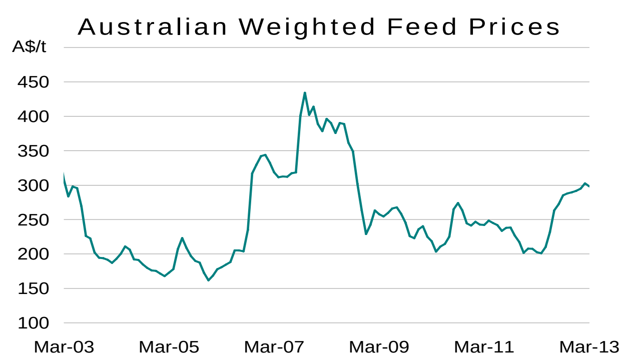
Source: Bloomberg, NAB Economics

cumulative growth of 18% in the price of natural gas and 9.0% in Diammonium Phosphate (DAP), while urea was 4% lower over last two months. The short-term price movements are range-bound by elevated inventories in key markets, but beyond 2013 Q2, prices are likely to trend up corresponding to greater usage intensity from the commencement of the planting season in the Northern Hemisphere. Similarly, fuel prices were cumulatively 4% higher over the last two months as well, partly attributable to the strengthening of USD from a slew of positive economic news from the US.

NAB Weighted Feed Grains Price

Low global stocks of corn and soybean continue to provide some support to domestic feed grains prices, resulting in the NAB weighted feed grains price to be cumulatively 1.1% higher in March compared to the last reported result on the month of January. The monthly movements suggested that grains prices rose sharply in February but were detracted partly by a fall in March, the first monthly fall in 10 months. This potentially signals a turning point in the recent bullish trends of grains prices, as the production of grains and oilseeds around the world are forecast to be notably higher in 2013-14. Relative to their individual price levels in January, feed wheat and barley were 2% higher in March. Maize and triticale, accounting for a smaller weight of the index, rose modestly as well. On the other hand, the prices of sorghum and oats were 2% and 1% lower respectively.

Feed grain prices reaching a possible plateau



Source: ABARES, NAB Economics

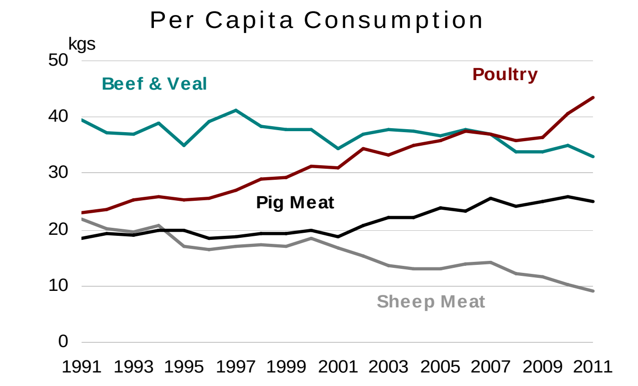
In Focus – Poultry and Pork

- **Consumption of poultry continues to climb on favourable prices, consumer preference**
- **The current high levels of feed prices might flow into higher chicken meat prices in the short term, but its price is still competitive relative to substitute meats of beef and lamb.**
- **Australian pork industry still faces strong competitive headwinds from imports with the shift to fresh meat production inevitable. However, the outlook for high-end exports looks positive in the longer term.**

The last year or so has been a challenging year for poultry and pig meat, with high feed costs and falling prices of beef and lamb creating a double blow to the pork industry, and to a lesser extent, the poultry industry. Given that chicken meat production accounts for around 95% of total poultry production, with the remainder comprising duck and turkey meat production, our analysis will focus predominantly on the chicken meat industry.

The chicken meat industry has proven to be more resilient in the face of these challenges, supported by its competitive pricing and some of its inherent appeal to consumers - ease of preparation in meals and perceived nutrition propositions. On the contrary, the pig meat industry has to contend with additional sources of pressure of rising import competition from processed meat and more stringent regulatory requirements to ensure that its farming practices are environmentally sustainable. Hence, there is a strong impetus for local pig meat industry to explore new production technologies and methods which will enhance the value propositions of its products to customers, such as by offering a higher-end product that is ethically produced.

Per Capita Consumption



Source: ABARES, NAB Economics

Australian chicken meat industry continues to gain traction

The Australian chicken industry has been a success story within protein farming since its inception in the 1950s with the release of Australia's first scientifically bred meat chicken strain in 1959.

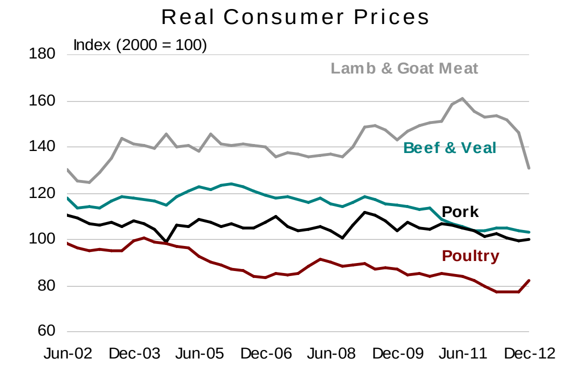
The chicken meat industry has expanded rapidly in the first three decades from its humble beginning, with production expanding average by around 4% a year over the past 10 years. Compared to other livestock industries, the chicken meat industry is highly concentrated and more vertically integrated. There are currently two major processors: Baiada Poultry and Inghams Enterprises, which supply about three quarters of the domestic chicken meat market. The predominant business model at present is still very similar to its earliest predecessor in the 1960s, based on a highly successful US meat chicken company model. Under this model, processors own chicken breeding and hatching operations, feed mills and chicken processing plants and either owned or contracted the growing of chickens from day-old to slaughter weight, which currently takes around 5 weeks.

The Australian chicken meat industry has managed to, over the years, improve the quality and efficiency of production starkly which has in turn raised the price competitiveness of chicken meat relative to other proteins. Most of the genetic stock for Australia's chicken meat is imported from specialist breeding companies in the USA and Europe with the objective of improving certain traits such as robustness, disease resistance, growth, meat yield and more efficient feed conversion. According to ABARES, the average meat yield per bird increased by an average of 1% a year to 1.9 kilograms in the 20 years to 2011–12. This trend is expected to continue over the medium term.

The number of chickens slaughtered has increased steadily over time to meet increasing demand. The percentage increase in chicken meat produced over the same period is even greater, as changing consumer preferences for different cuts such as raw chicken breast fillets or chicken drumsticks, as well as processed chicken products, has led to demand for larger birds on average at the time of slaughter. Since 2008, chicken and other poultry have surpassed beef and veal as the most consumed protein in Australia at approximately 44 kilos per capita in 2012-13, and fast gaining upon total red meat (beef, veal, lamb, mutton) consumption. According to the Australian Chicken Meat Federation (ACMF), 90% of all Australian households consume chicken at least once a week, with around 30% consuming chicken three or more times a week, amounting to about a conservatively estimated $5.6 billion in total spending per annum.

Chicken meat enjoys a number of advantages over other sources of protein. It appeals to consumers due to its ease of preparation in meals and low fat content for the health conscious. More importantly its relative price has stayed reasonably flat over other meats, with its real price falling steadily for some time. According to an unpublished survey by the ACMF, some 58% of Australians consider chicken to be the best value for money meat option. More recently, chicken meat prices have ticked up along with high feed prices, but that is likely to unwind once global production of corn and soybeans recover.

Real Consumer Meat Prices



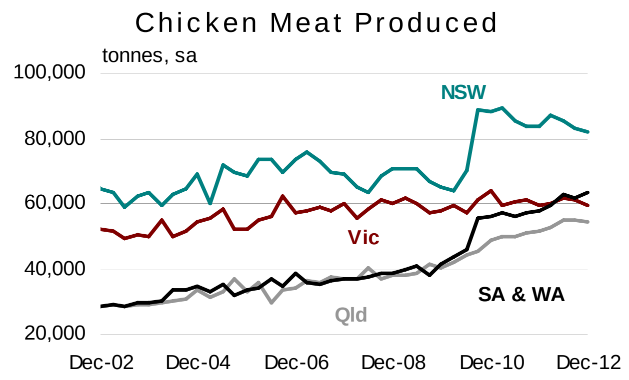
Source: ABS, NAB Economics

Going forward, we expect chicken meat to have a growing place in the Australian diet, underpinned by a strong value proposition and better perceived health benefits from consumption compared to other meat alternatives. The current high levels of feed prices might flow into higher chicken meat prices in the short term, but its relative price is still competitive in the context of rapidly rising beef and lamb prices in the last few months.

Australian Chicken Meat Industry Consolidates 2010-11 Growth Spurt

After showing a tremendous lift in production growth of 22% in 2010-11, the chicken meat industry appears to have largely consolidated the growth spurt to grow by 1% in 2012-13. New South Wales, which contributed the most to growth in 2010-11 saw its production contract slightly by 3% in 2012-13. Similarly, South Australia and Western Australia combined was unable to match its startling growth of 33% in 2010-11 to come in at only 6% the year after. Meanwhile Queensland has exhibited the characteristics of a marathon runner of showing consistent growth, to be at 6% in 2012-13. In contrast, Victoria's chicken meat industry has shown signs of stagnation since 2006, fluctuating around the 238,000 tonnes mark in the last five financial years.

Quarterly Poultry Production



Source: ABS, NAB Economics

According to the ACMC, a combination of factors has contributed to the success of the chicken meat industry of sustaining growth in production and maintaining competitive prices. Thankfully, the 'recipe' is hardly as mysterious as the secret blend of 11 herbs and spices that go into the popular chicken dish of KFC Fried Chicken:

- Selective breeding – chickens have been selectively bred to more efficiently convert feed into meat. In 1975, it took 64.1 days and 4.66kg of feed to grow a chicken to 2kg. In 2011, it takes just 35 days and as little as 3.4kg of feed.

- Animal husbandry and feeding – a strong research focus on ensuring an ideal growing environment and finding the right mix of nutrients to optimise the health and growth of chickens, as well as the efficiency of feed conversion into meat.

- Processing automation – to readily adopt technology that helps process, cut and pack chicken meat more economically and efficiently.

Looking ahead, ABARES forecasts poultry production in 2012-13 to grow by 1.9 % to 1,050 kilo tonnes, and rising to 1,210 kilo tonnes by 2017-18. After falling in 2012-13, exports are expected to resume growing in 2013-14, predicated on the withdrawal of the temporary bans currently imposed due to the discovery of a case of avian influenza virus (H7N7) that had been detected at an egg farm near Maitland, New South Wales December last year. Having said that, the bulk of increased production is expected to be absorbed by rising domestic consumption, as exports only account for a mere 3% of total production volume.

Domestic pork industry continues to face stiff competition from imports and rising environmental concerns

In 2012-13 the Australian pork industry continues to be weighed down by growing competition from imports, exacerbated further by the recent spate of rising feed costs and a high exchange rate. In its latest quarterly report, ABARES found that pig meat imports increased by 11% in the first half of 2012-13, compared with the same period a year ago.

Since the relaxation of import restrictions in the 1990s and the subsequent establishment of free trade agreements between Australia and a number of countries, the Australian pork industry has had to stand up to fierce competition from imports from countries such as Canada, the US and Denmark which benefit from greater economies of scale. As a result, a high degree of structural consolidation progressively took place in the last decade within the industry.

Reflecting this, Australian pork production experienced a notable decline between 2003 and 2008, after which production started to recover slowly again to a point where the 2012 level was close to the 1997 level. This appears to suggest that the earlier tectonic shift in the industry playing field appears to have stabilised, reflected in the slowing pace of decline in the number of pig farming enterprises in recent years.

Increasingly, pig producers are gripped by issues of a different nature: how to ensure that their operations are ecologically sustainable. According to Australia Pork Limited, agriculture accounts for approximately 16% of greenhouse gas emissions in Australia. Most of the emissions associated with pork production relate to on farm emission of methane (CH_4) from effluent lagoons and nitrous oxide (N_2O) following the land application of effluent and manures. Disposal of this waste is causing increasing concern for modern intensive livestock industries. Hence Australian pig producers are under mounting pressure to demonstrate that they take every practical step to minimise the impact of their operations on the environment, evident from the increasingly stringent regulatory requirements imposed on piggeries. In response to these pressures, some piggeries have adopted the technology to convert methane 'digested' from piggery waste into methane gas which can then be converted into electricity that can be used to power the farm, or sold to the local electricity network, generating on-farm revenue.

Flat pork prices and high production costs continue to squeeze profit margins

Rising feed costs since the mid last year, accompanied by relatively flat prices, have squeezed the profitability of pig producers. Expenses needed to meet the regulatory requirement to phase out sow stall pork production acts as a further constraint on profitability. According to the latest ABARES quarterly report, weighted average over-the-hooks price of pigs is forecast to average around 280 cents a kilogram in 2012–13, largely unchanged from the average in the previous year. Combined with high feed costs pig-to-wheat and pig-to-barley price ratios averaged 25% and 22% lower respectively in the first half of 2012-13.

While feed costs are expected to moderate in 2013-14 from their current levels as grain prices return to more normal levels, slaughterings are likely to fall due to a decline in breeding sow numbers, which will help to prop up prices to a certain extent. The Australian pig herd fell by 6% over the 12 months to June 2012 to 2.2 million head, the lowest in 40 years. In turn this is likely to flow into a contraction in pig meat production of 2% in 2013-14 to 340 000 tonnes.

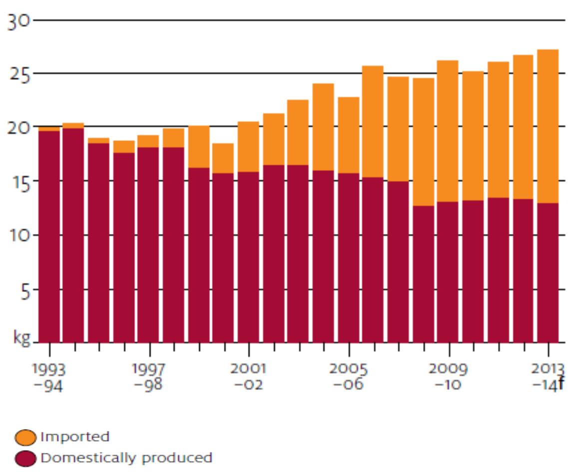
Over the medium term, ABARES forecast pig prices to decline gradually to 246 cents a kilogram by 2017–18 (in 2012–13 dollars) as more production is expected be directed from processed meat to fresh meat which fetch a lower premium. This shift was inevitable given the nature of import restrictions in Australia. Imports of fresh pig meat for domestic consumption are restricted, whereas imports of processed pig meat are permitted under current regulations. Meanwhile, with the Australian dollar assumed to remain relatively strong over the medium term, demand for imported processed pig meat is projected to rise.

For those producers remaining within the processed segment, conditions are expected to remain fairly challenging. Imports of pig meat increased from only 23% of total pork consumption in 2002–03 to an estimated 49% in 2012–13, and are projected to rise further in 2013-14 by a further 9%, totalling 165,000 tonnes. Over the medium term, imports of pig meat are expected to increase to 180,100 tonnes by 2017-18.

Pig meat consumption to trend up gradually, outlook for exports positive

In 2011-12, Australian per capita pig meat consumption increased to 25.4 kgs from 24.5 kgs recorded in 2010-11. Over the medium term average per person consumption of pig meat is projected to rise to 27 kilograms by 2017–18. A significant proportion of this projected increase in consumption is expected to be met by imports.

Average Australian per capita pig meat consumption



Source: ABARES

The key to the outlook for pig meat consumption in Australia will be the favourable relative prices when compared to other red meats. However, poultry is much more competitive on the price front, so a decent marketing effort will be required to further boost domestic pig meat consumption. Having said that, the export market provides more scope for local pig meat exporters to be optimistic in the longer term, despite facing strong competitive headwinds from the world's largest three meat exporters: Denmark, the US and Canada in the near term. Around the world, there has been an unprecedented increase on issues such as food security, climate change and the way food is produced, offering Australia the opportunity to set the benchmark of high integrity yet affordable pork exports. To assist the advancement of scientific research in pig farming, the Australian Federal Government established the Pork Cooperative Research Centre (Pork CRC) in 2005 which has a vision to enhance the international competitiveness of the Australian pork industry by providing and adopting new and novel technologies that reduce feed costs, improve herd feed conversion efficiency and increase the range and functionality of pork products.

Further complementing the pork exports outlook is the strong forecast growth in imported pork in the two major Asian importing countries of Korea and China in the foreseeable future.

Comments from the Field

It's always hard to get anything definitive out of pork industry due to the sensitive nature of the individual relationships with buyers / suppliers. The impact and timing of moving to sow stall free systems has added to this. Normally prices dip during this period but the indication is that prices may remain stable for longer, driven more from an anticipated reduction in supply than an increase in demand for product. From a cost position, there is upward price pressure on some of the feed ingredients (pulses etc) in the short term however the longer outlook is more favourable for feed prices.

Peter Read – Senior Agribusiness Manager, Adelaide

Poultry remains a strong point in agriculture, with moderate consumption increase, driving sound business fundamentals. This is due to poultry's price competition against substitute meats. Area of concern rests with coming grain crops and feed grain prices.

Stephen Richards - Senior Partner Agribusiness, Canberra

The demand for chicken meat is still strong. There are not as many farm sales in this area as there was several years ago. In fact sales have dropped by nearly half in the last 12 month period to 7 or 8. This is mainly due to the price. Prices of farms are quite high, especially on the Mornington Peninsula due to the high land value. Prices are also high due to the fact that it is difficult to build new farms or expand old farms in this area. What this means is that anticipated rationalisation of smaller farms is not occurring and they are continuing to operate.

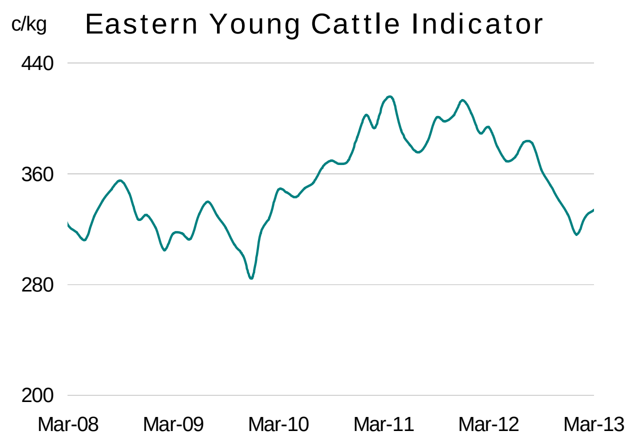
Michael Young – Agribusiness Manager, Hastings, Victoria

Pig producers continue to see strong prices with bacon around $3-/kg which is above historical levels at this time of the year. These prices are expected to hold over the coming months as a result of the disruption to production in Southern Queensland from the floods in January along with some smaller producers continuing to leave the industry. Finished feed prices have increased circa $80-/t over the past 12 months and given the weakness in global grain prices over the past 6 weeks these feed prices could trend lower later this year after the wheat harvest. Producers are waiting for the grain markets to soften before looking to lock in forward purchases. Imports are still benefiting from the high AUD and have this market saturated with domestic producers covering the fresh pork market.

John Stenzel – Senior Agribusiness Manager, Toowoomba, Queensland

Key Commodity Prices

High cattle slaughterings continue to weigh on prices



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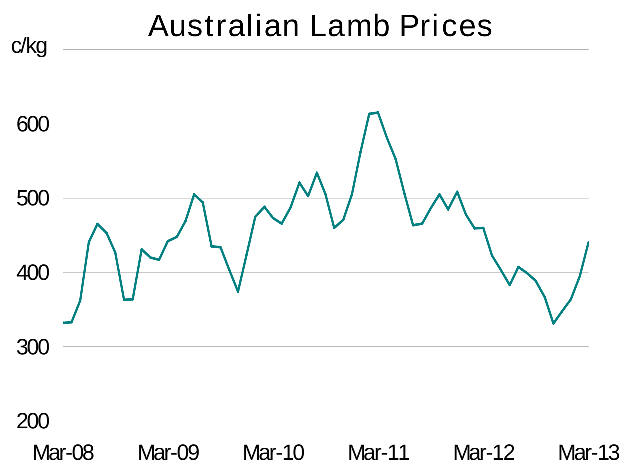
ource: MLA

Australian beef and veal production surged in February and March relative to the same period last year, with slaughterings up by 6% and 9% in February and March respectively as a continuous flow of cattle from the western regions kept supply ample. According to MLA, the majority of processing plants are booked well in advance as the dry conditions continue to pressure producers to offload suitable slaughter lines as soon as possible. Despite the high slaughtering numbers, prices ticked marginally higher in the two months as decent rainfalls in the east coast stoked confidence and some restocker demand. However, the EYCI has demonstrated a more bearish trend since then, having eased since the start of April from oversupply. The current poor seasonal conditions are a stark contrast to those the same time last year, as sufficient rain helped to encourage plentiful pasture growth which eventually fuelled fierce competition between the restockers and feeders for suitable lines. In this situation, beef prices are likely to remain subdued for some time to come.

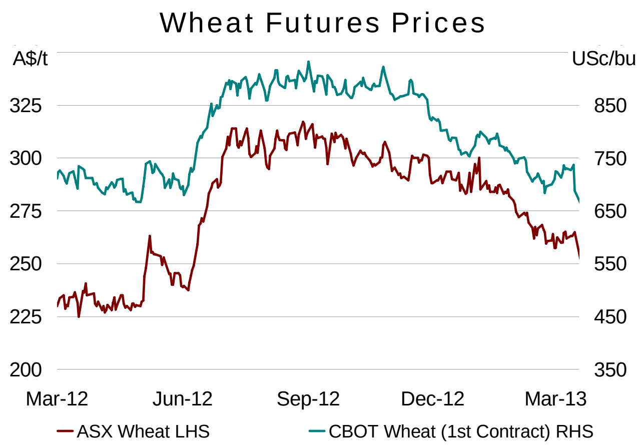
Lamb prices surged despite high slaughtering numbers



Source: MLA

Lamb prices rose markedly in February and March despite high slaughtering numbers keeping supply comfortable. Late February rain across New South Wales and Victoria was a welcome relief for lamb farmers, bolstering confidence and pulling prices further upwards. As a result, the Heavy Lamb Indicator rose 9% in February and 12% in March, but prices remain subdued compared to levels a year ago. Average weekly slaughter continues to be above that of the same period last year, with expectations for the high turnoff to start to slow as more normal conditions return in autumn. The increase in supply has mostly been absorbed by exports to Middle East, China and the US, although export volumes in March are showing signs of moderation from the earlier trailblazing pace in the three months earlier. In the next month or so, lamb prices are likely to ease from its current levels as the effect of oversupply from the persistently dry conditions kicks in.

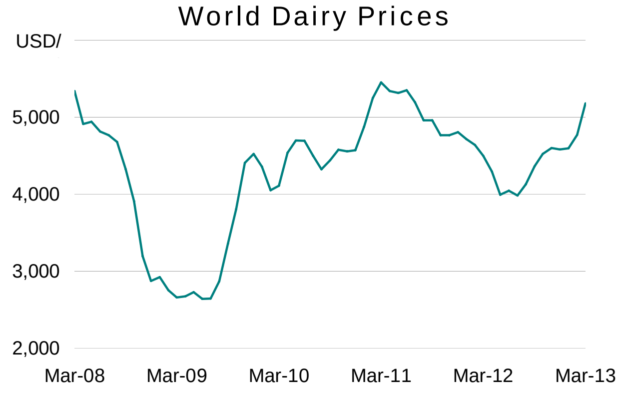
Wheat prices tracked lower from unexpected rise in stockpiles



Source: Bloomberg

Wheat prices have broadly pulled back over February and March, on the back of an expected increase in world production and ending stocks, as well as rising number of speculative net short positions in the market. The latest USDA's World Agricultural Supply and Demand Estiamtes (WASDE) report on 10 April has revised up its forecast of world's ending stock for 2012-13 to 182 metric tonnes. The revision primarily reflects weaker demand for wheat feed from the US and around the world, now that coarse grain prices are lower. Strong coarse grain feed demand and a moderate planting pace have supported corn prices for the month of March but a USDA crop report on the 28 March announcing a surprisingly large corn surplus has sent corn futures into a tailspin, correcting sharply by 5.4%, the maximum daily change allowed by the Chicago Board of Trade exchange . Since then, corn prices have tracked lower. Soybean prices have also been dampened by an upward revision in its ending stock by the USDA, and the news of a bird-flu outbreak in China potentially slowing export demand dragged prices lower further, to its lowest point in 10 months.

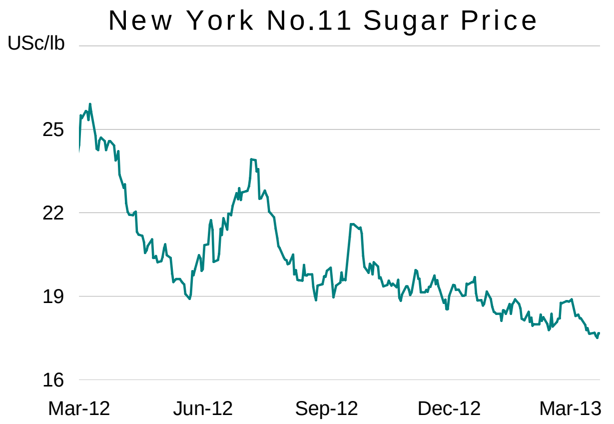
Dairy prices gaining strength on constrained supply



Source: NZX

World dairy prices accelerated in the last two months on tight global supply, having lifted by 4% in February and a further 9% in March to reach the highest level since July 2011. Adverse climatic conditions in Australia and New Zealand have reduced milk flow significantly compared to last season, while the Northern Hemisphere season is not yet fully underway. In New Zealand, the largest dairy exporter in the world, the persistence of dry conditions into March and earlier commencement of cow slaughters suggest that dairy production is likely to remain constrained till the end of the Southern Hemisphere season. While higher dairy prices may suggest stronger cash flow for farmers, nonetheless high feed costs and lower milk prices from supermarket price wars continue to squeeze margins at the farmgate level. In the upcoming months, the commencement of Oceanic spring flush may serve to limit the extent of further price increases but the current tightness in global feed supply could potentially delay the maturing of the season.

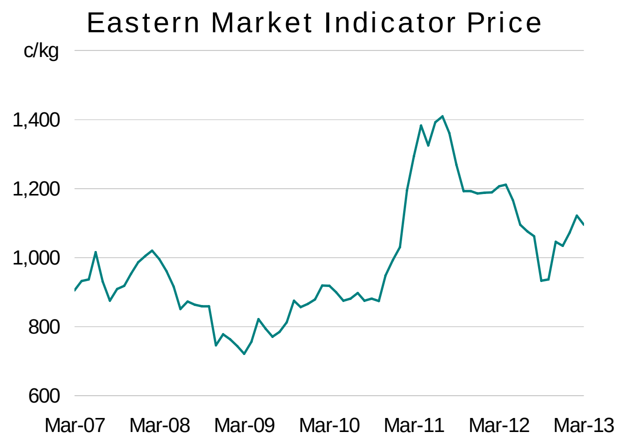
Sugar prices subdued on stronger-than-expected global surplus



Source: Bloomberg

The slide in raw sugar prices continued in February and March from the overhang of global surplus, with the ICE No.11 futures easing to below 18USc/lb by the end of March, the lowest since November 2010. ABARES forecast world sugar production to increase by 2.3% in 2012–13 to a record 179 million tonnes, slightly lower than the 180.4 million tonnes forecast by the International Sugar Organisation in its February quarterly report. Larger sugar production is forecast in 2012–13 for Brazil, Australia, China, the United States and Mexico. However adverse seasonal conditions are expected to result in lower sugar production in India and Thailand. This, combined with higher margins expected from ethanol in Brazil may divert some production away from sugar this year, creating a layer of resistance to further downward pressure on prices.

Wool fell on renewed Euro-zone concerns



Source: Bloomberg

After two months of strong growth, the Eastern Market Indicator (EMI) weakened slightly in March, as demand from large consuming countries such as China and India softened. The sustained strength of the AUD against the USD, accompanied by the surfacing of the sovereign crisis in Cyprus which has rocked investors' confidence, has cast a negative sentiment over the market. The European Union is the largest export destination for China's textile goods, hence China's demand for raw Australian wool is highly contingent on the economic outlook of the EU. The superfine Merino fleece types of 18.5 micron and finer fared the worst, while the 19.0 to 23.0 micron fine and medium Merino fleece were relatively more resilient. Earlier concerns over potential supply shortages in some areas of the industry have not been realised so far, with the volumes offered at auctions this financial year likely to be quite similar to those of last year. In the short-term, the EMI might fall further as a larger supply comes online after the Easter break, but overall prices are likely to remain relatively firm in the last months of 2012-13.

Contact details

Agribusiness

Khan Horne	**David Brett**	**Neil Findlay**	**Brenton Sellers**
General Manager – Agribusiness	Head of Agribusiness – Northern Australia	Head of Agribusiness – Southern &Western Australia	Head of Business Development & Projects
+61 2 9237 9963	+61 7 3234 5664	+61 3 8634 1762	+61 3 8634 0606

Risk Management Services

Rod Fraser	**Mick Pitts**	**Tim Glass**
Head of Agribusiness Wholesale Banking	Global Head of Institute Commodity Sales	Director - Commodities
+61 2 9295 1141	+61 2 9237 1925	0419 389 721

Economic Research

Alan Oster	**Rob Brooker**	**Vyanne Lai**
Chief Economist	Head of Australian Economics & Commodities	Economist Agribusiness
+61 3 8634 2927	+61 3 8634 1663	+61 3 8634 0198