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agribusiness

Economic Report

Rural Commodities Wrap

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- **Global equity and commodity markets exhibited increased volatility in the past month, caused by heightened geopolitical tensions in Ukraine, adverse weather events in the US and news of a slowing Chinese economy.**
- **December quarter GDP result for Australia was close to trend, but capital expenditure expectations portend a sharp fall in mining investments by 2014-15.**
- **As such, jobless growth is expected to continue through 2014 in Australia, with unemployment rate still to reach 6½% by end-2014 when a final rate cut is predicted (possibly November).**

The directions of commodity markets over the past month have been mixed, and have generally prevented any clear price signals from emerging. Extreme weather conditions in the US and Canada, signs of slowing in China and emerging markets, as well as escalating geopolitical tensions in the Black Sea region have introduced heightened volatility in financial and commodity markets, with agricultural, energy and safe haven assets such as gold generally benefiting, while the outlook for bulk commodities was dampened. Interest rates look set to remain very low in the big advanced economies for some time yet. The US Federal Reserve looks likely to keep interest rates low even after the jobless rate falls below 6½%, provided inflationary pressures are under control. We expect the Fed to begin lifting its funds rate in the latter half of next year. Ahead of that, the Fed should continue to gradually wind back new asset purchases ("tapering") through the rest of 2014.

The early 2014 dip in business survey readings across several advanced economies points to the impact of bad weather on business. Nevertheless, their underlying strength remains and activity growth should get back to its previous trend. Financial markets are not pointing to a sustained slowing in growth and forward-looking questions in business surveys show confidence that the upturn remains solid. Looking at individual economies, February growth in service sector activity slowed noticeably in the US (possibly weather affected) and Japan (unexpected, given the impending lift in indirect taxes – but early readings for March rebounded). The UK service sector was strong and essentially unchanged while the Euro-zone improved.

Meanwhile, emerging economic growth has flat-lined as expected and looks set to continue. Official Chinese data is held up by the usual start of year delay, but the monthly industrial business surveys for early 2014 are consistent with the slowing manufacturing trend. Elsewhere in East Asia, slow growth continued into early 2014 for exports and industrial output and the December quarter figures for the region showed little momentum toward faster growth in consumer spending or fixed investment.

2013/14 Estimates, Rural Prices & Production

Commodity	Production	Price
Wheat	17.0%	-16.1%
Beef	3.1%	-7.3%
Dairy	-2.7%	38.7%
Lamb	-1.1%	20.2%
Wool	-2.0%	5.5%
Sugar	-1.2%	2.5%
Cotton	-2.7%	21.0%
Oil	-	1.0%

Source: NAB Group Economics
These forecasts represent year-on-year average changes in Australian production and corresponding AUD prices between 2012/13 and 2013/14 financial years

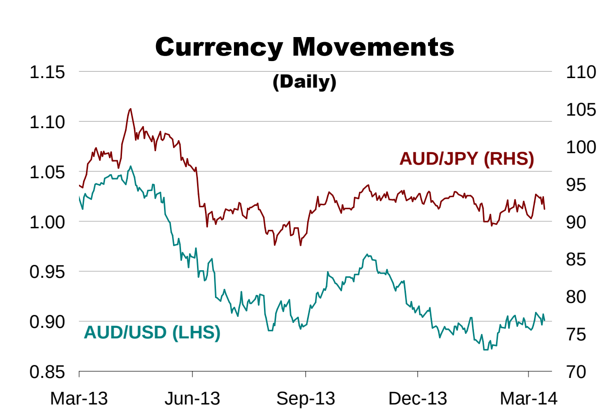
Domestically, the recently released National Accounts data suggest that Australian Q4 growth of 0.8% was close to trend, but obscured weak domestic demand growth of 0.1% that will not be enough to stop further rises in unemployment (6.0% in January). Capital expenditure expectations point to a two-year decline of 21% in labour-intensive mining investment by 2014/15 with little offset from other industries. Australian forward indicators are largely in retreat as NAB business conditions and orders fell in February, implying GDP growth of 2¾% in Q1. Jobless growth is expected to continue through 2014 with unemployment rate still to reach 6½% by end-2014 when a final rate cut is predicted (possibly November). Our GDP forecasts are broadly unchanged: in through-the-year terms, we expect growth to be broadly constant at 2.8% from Q4 to mid-2014 (was 2.6%) and 2.9% to mid-2015.

In February, most major rural commodity prices in Australia rose. Average to above average rainfalls across most parts of Australia have stoked restockers' confidence in cattle and sheep, propping saleyard prices upwards. Wool prices fell in the month on large auction supplies and subdued trading activity from major Chinese buyers, presumably due to the seasonal effects of Lunar New Year. Meanwhile, domestic grain markets continued to trend upwards in conjunction with a global rally on concerns of supply delays from Canada and Argentina, drought in Brazil and the Ukraine crisis. Global dairy prices reached unprecedented levels in the month but appear to be at a turning point with price losses recorded in two consecutive Global Dairy Trade auctions. For softs, cotton has held up on constrained production in the US, while sugar gained ground from record lows as worsening drought conditions in Brazil threaten crop yields from the largest global producer and exporter.

Currency Movements

Movements in AUD/USD have been largely range-bound in February and the first half of March, further consolidating the gains seen in the aftermath of the Reserve Bank of Australia's 4th February post-board meeting statement in which the central bank dropped its 'easing bias' and chose to no longer refer to the currency as uncomfortably high (or even just 'high'). Despite the recent sharp falls in iron ore prices and escalating geopolitical tensions in Ukraine, AUD/USD has held its ground to be around the USD$0.90 mark, presumably due to the expected idiosyncratic and temporary nature of such factors. To trigger larger sell-offs of the AUD, we would probably need to see: a) big capital outflows from EM, b) a sharp spike in VIX (or other risk measures) and c) further declines in commodity prices. However, these conditions are not being met currently. The VIX, a measure of broad market risk sentiment, remains somewhat well-behaved. It may be trending higher but remains at levels well below those seen in critical periods previously. Similarly, the gold price is rising, not falling. The index of Asian currencies (ADXY) is in a mid-range after an early March bounce, which is AUD supportive and is not showing signs of stress. Mixed domestic economic data also prevented any clear directions from emerging, with Australia's Q4 GDP result proving satisfactory despite more definite signs of slowdown in mining investment pointing towards more downside risks. NAB's forecasts of the AUD/USD remain unchanged, with the currency expected to moderate gradually to around USD$0.84 by December quarter this year.

Lack of adverse economic news sees AUD movements range-bound

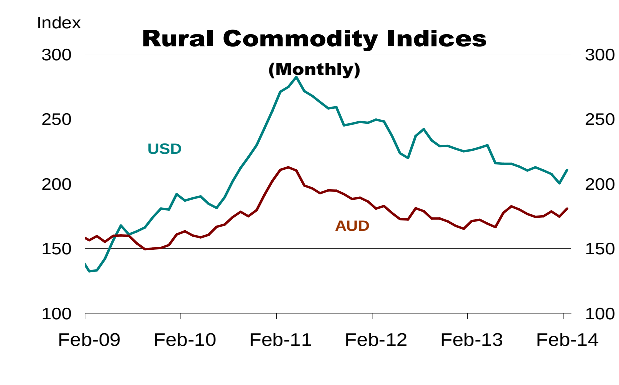


Source: Datastream

NAB Rural Commodity Index

In February, broad-based rises in commodity prices have supported the NAB Rural Commodity Index, with the index in AUD terms rising by a notable 3.5%, supported by rises in lamb (+19%), wheat (5.5%), sugar (+5.1%), beef (+3.8%), cotton (+3.5%), dairy (+2.5%) and barley (+2.2%), only offset by a fall in wool prices of 3.5%. This month prices have generally deviated from what fundamentals would suggest, thanks to idiosyncratic factors such as news of drought developments in South America, grain supply delays due to transportation problems in Canada and Argentina and heightened geopolitical tensions in the Black Sea region. Meanwhile, domestic livestock prices have benefited from average rainfall in the month. The trajectories of some of these events remain largely uncertain, and are likely to create some volatility in local domestic prices in the short-term.

Broad-based rises in commodities propped NAB Rural Commodity Indices higher in the month

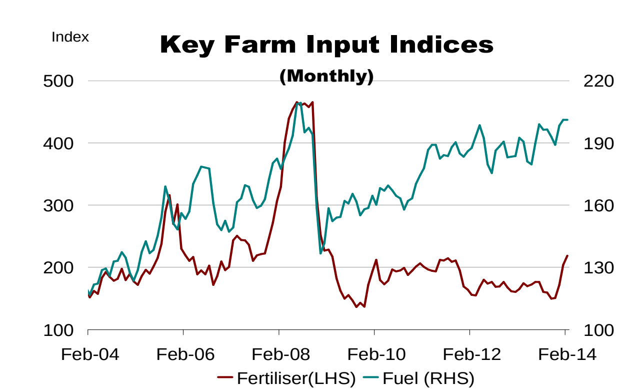


Source: Bloomberg, NAB Economics

NAB Farm Input Indices

In February, the global fertiliser market continued its strong pace, underpinned by significant rises in the prices of energy and Diammonium Phosphates (DAP). An unusually frigid winter in the US, the largest global producer of DAP, has fuelled surges in energy prices in the month in the country. Meanwhile, mounting geopolitical uncertainty in Ukraine also sparked supply disruption concerns for energy and grains more widely in global financial and commodity markets, thereby fuelling prices of commodities relying heavily on them as inputs. Urea prices remain subdued from an overhang of supply from low-cost manufacturing regions in the Middle East and North Africa. Overall, fertiliser prices continue to trade at discounted levels relative to a year ago and should not pose a significant cost constraint to upcoming winter crop production.

Spikes in energy prices fuelled input indices higher



Source: NAB Economics

NAB Weighted Feed Grains Price

Domestic feed grain prices rose for the fourth consecutive month in February, led by sustained price growth of feed barley which was in turn underpinned by robust export demand. Barley prices rose to the highest level in a year and are already pricing some domestic end users out of the market. Meanwhile, poor sorghum production prospects at the start of its harvest season was also price supportive, with lingering potential for further weather damage in drought-hit southern Queensland. There were also some spill-over effects in the month from firming global prices stemming from concerns on the Ukraine crisis but these appear to have eased somewhat for now.

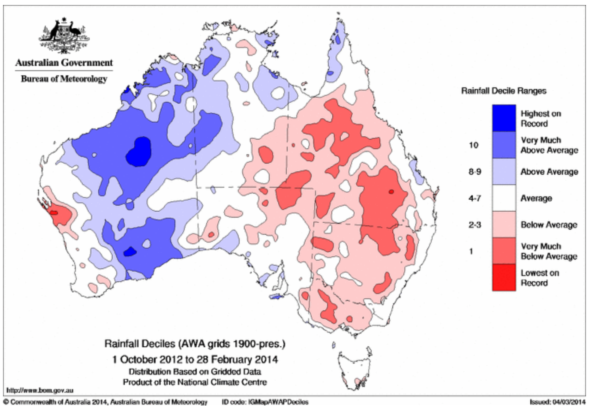
In Focus – Implications of drought on the agricultural sector

- **After two very wet years in 2010 and 2011, extensive drought conditions returned to a significant inland area of eastern Australia since late 2012. The dryness worsened over the course of 2013, with 80% of Queensland now declared drought-affected, the most widespread in history.**
- **Severe and prolonged drought conditions have forced livestock farmers to offload their stocks for slaughter and crop farmers to reduce their summer crop, and potentially winter crop plantings.**
- **Average farm cash income disparity has widened sharply in 2013-14, with grain-intensive farms in WA earning around 8 times more than cattle-intensive farms in Queensland.**

Recent drought developments in Australia

After two very wet years in 2010 and 2011, extensive drought conditions returned to a significant inland area in eastern Australia in late 2012. The dryness worsened over the course of 2013 with inland Queensland most affected, peaking in early 2014 until normal to above normal rainfall across major areas of Australia in February halted a further deterioration in conditions. The severity of the drought in Queensland was recently reaffirmed by the state's Agriculture Minister, John McVeigh, who declared 15 additional shires to the list of drought-affected areas on 1 March, bringing the total to 38. The list constitutes about 80% of Queensland's land area and is the most widespread drought-declared area on the state's record, which also includes, for the first time, large sections of the state's coastal strip. Meanwhile in NSW, the areas most affected by rain deficiencies are in the central north and the north-west which are mainly involved in sheep and wheat farming. In Victoria, dry conditions are centred on the Mallee region, while in SA rainfall deficiencies have been most severe in the south-east and north of the state.

National Rainfall Deciles from October 2012 to February 2014



Source: BOM

According to the Bureau of Meteorology (BOM), February's average to above average rainfall through northern Australia and most parts of the mainland have helped ease the extreme rainfall deficiencies in western Queensland. This helped to lift much of the area out of the lowest 10% of rainfall records for 17-month period ending February. That said, the recent scattered rain events have merely soothed the wound rather than healed it. Much more rain is needed for any major turnaround in conditions.

Soil moisture in the upper layer soil of eastern Australia has improved from recent rainfalls to some extent, but remains very much below average for the current drought-affected northeastern NSW and southeastern Queensland. As a result, water supply shortages have become extremely acute in certain communities of Queensland as residents are faced with increasingly harsh water restrictions. For example, the town of Cloncurry in northwest Queensland, which has not received decent rain in two years, moved to level six water restrictions in February.

Effects of drought

In Australia, drought has become largely synonymous with the predicament of farmers. While agriculture tends to suffer first and most severely in a drought event, implications of a drought can reach beyond simply the physical, and also have social, environmental, economic and standard of living impacts. The focus of this article will be limited to the direct effects of drought conditions on the agricultural sector, and mainly its implications on farm production, prices, exports and farmer incomes.

1. Agricultural production, prices and exports

Crops

In a typical drought, the immediate casualty tends to be a fall in crop and pasture production. In Australia's case, this is demonstrated by the clear divide in the 2013-14 winter cropping outcomes across states, with less-affected WA and SA reporting bumper crop harvests, while production in NSW and Queensland showed significant declines. According to the latest ABARES' crop report, winter crop production in WA hit a record of 17.2 million tonnes in this year's season, a 55% increase on the previous year.

The disparity in the balance of grain demand and supply situations across the northern and southern states was further exacerbated by the compounded effects of drought-induced fodder shortages amongst the cattle-intensive farms in Queensland and NSW. This increasingly forces farmers to liquidate their stocks by fattening cattle up in feedlots on grains before slaughtering. Fodder and hay shortages are relatively contained in the southern states. While grains supply in these regions is more bountiful, high transportation costs have prevented the efficient flow of grains northward from these states. As a result of these differences, two distinctive feed markets emerged: the northern Australian feed market characterised by sustained strong basis trends which are likely to persist for the coming months, unless a major autumn break materialises, while the grain prices in the southern market have eased from the historically elevated levels over the harvest period as new supplies became available. More downward pressures on prices are likely to stem from soft domestic purchases as many buyers appear reluctant to lock in orders at current price levels. Reflecting the fragmented nature of the domestic grains supply chains, exports of grains from the southern states are influenced more by demand conditions from a waning Chinese import appetite and stiffening competition from major grain producers of the US, Black Sea region and EU. Currently it doesn't appear that the crisis in Ukraine would have any immediate impact on exports stemming from the region, which continue to pose competition for Australian exports.

While some regions have reported below average winter crop outcomes, the overall national winter crops production has performed well despite the dry conditions. That said, the outlook for the prospective summer cropping season doesn't appear to be as rosy. ABARES has forecast the area planted to summer crops will fall by 15% in 2013–14 to 1.15 million hectares, while total production is forecast to fall by 25% to 4 million tonnes, largely driven by reduced plantings by most summer cropping regions in northern NSW and Queensland as a response to the persistent dry conditions, as well as expected falls in the yields of dryland crops. Falls in production have been forecast for all major summer crops: sorghum, cotton and cotton seed, rice and sunflower, with the estimates of greatly reduced sorghum production in 2013-14 (ABARES predicts a decline of 36%) having flowed through to higher prices on the east coast, ranging from around a 15% year-on-year increase in Sydney and Newcastle in the first 7 months of 2013-14 to reach $315 and $292 a tonne respectively, to a 22% year-on-year rise in Brisbane to $306 a tonne.

Cattle and sheep

Relative to the cropping sector, the livestock sector appears to be the bigger victim of the drought to date. Cattle and sheep herds were rebuilt over the wet years of 2010 and 2011, with the latest peaks in 2012 at 29 million head of cattle and 74.7 million head of sheep/lamb respectively. However, the lack of pasture regrowth from recent drought conditions, and thus feed availability, has forced many livestock owners to liquidate their stocks in increasing numbers.

The 2013 calendar year saw the largest turnoff of cattle since 1978 at 8.36 million head nationally, while lamb slaughterings hit a new record at 21.9 million head. Sheep slaughterings also recorded a five-year high of 9.5 million head. The strong pace of slaughter gained further momentum in the first two months of 2014 to reach record rates, as dry conditions worsened over a warmer than average summer. By states, cattle and calf slaughter increased sharply in Queensland, NSW, Victoria and South Australia compared with the same period in the previous year.

Cattle and calf slaughter from July to December 2013

Source: ABARES

The increase in supply of lower quality livestock for slaughter and reduced demand for younger cattle/sheep for restocking purposes have weighed on saleyard prices. In contrast, a stronger demand for Australian protein exports, led by emerging economies of China and the Middle East, further aided by a more favourable AUD, has buoyed average unit export returns for beef and lamb/mutton, thereby widening the gap in the payments received by farmers and exporters.

For cattle, the average saleyard price, as indicated by Eastern Young Cattle Indicator (EYCI), fell 15% in 2013, to around 315AUc/kg cwt. According to data from the Meat and Livestock Australia, the largest price falls were recorded in Queensland, followed by NSW, SA and Victoria. Generally, the lighter weight trade steers and medium cows have experienced the largest declines in prices across states, while prices of heavy steers (400-600kg) have been more resilient due to relatively limited supply offerings.

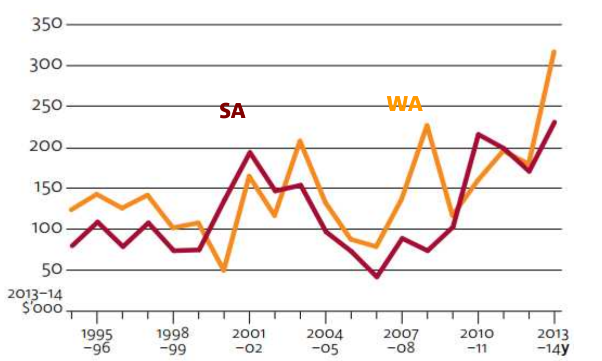
In contrast to lower cattle prices, average unit export returns for beef for the calendar year were 5% higher. Lamb prices also held up much better over 2013, with the Eastern States Trade Lamb Indicator averaging 423AUc/kg cwt, up 1.4% year-on-year but still well below the 551AUc/kg average recorded for 2011. More recently, lamb prices have surged dramatically on the arrival of more concentrated rain patterns in NSW, which helped to reinvigorate restockers' interests. Similar to the trend in beef imports, average lamb export unit values also rose by 5%.

As a by-product of the drought-induced high slaughter rates, Australian red meat production and exports reached unprecedented levels in 2013, with old records sent tumbling. The surge in Australian exportable supplies in the year were absorbed readily by our trading partners, underpinned by a number of favourable factors in the global market: a 6% fall in the AUD; the clamping down of grey channels of meat imports by the Chinese government, and certain trade bans in importing countries favouring Australian exports, such as a ban on Brazilian beef by Saudi Arabia; as well as a change in import protocols aimed at controlling rising beef prices in Indonesia. In 2013, beef and veal production rose to a new high of 2.4 million tonnes cwt, with around half of this exported, which in itself constituted a new record as well. Live exports are also recovering with the relaxation of the live cattle imports ban by Indonesia last year, as total exports are forecast by ABARES to hit 750,000 head in 2013-14, the highest since 2009-10. Meanwhile, lamb exports in 2013 also successfully toppled the previous record and hit 214,000 tonnes swt, accounted mostly by the Middle East, Greater China (including Hong Kong) and the USA markets.

2. Farm Incomes

As a result of the varied effects of drought conditions across different commodities and regions, farm incomes in 2013 have suffered widely varying fates as well, with the disparity between top performers and the bottom performers widening to what is possibly the largest gap in the history of ABARES collecting financial performance survey data.

Average Broadacre Farm Income of WA and SA



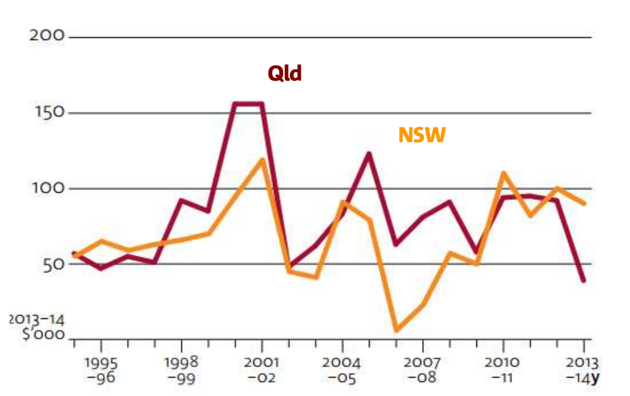
Source: ABARES

Reflecting the exceptional winter crop harvests this financial year, farm cash incomes for WA and SA broadacre farms are projected by ABARES to be the highest recorded in more than 30 years to reach an of average $317,000 and $231,000 per farm respectively, which amount to a staggering 70% and 85% above their decade averages ending 2012–13.

NSW, Tasmania and Victoria fall into a middle band. Average farm income in NSW is expected to hold up reasonably well despite being impacted by drought conditions in the north, to decline only marginally to $90,000, as stronger grains output, combined with higher lamb and wool prices, have acted as a partial cushion to higher fodder costs and subdued prices received for livestock sales despite more livestock being sold.

Meanwhile, average farm income in Tasmania is expected to rise by 12% to $71,000 while Victoria is expected to record a marginal fall to $82,000. Given their relatively more diversified farming industry base and favourable weather conditions, coupled with higher prices received for dairy, wool, sheep and lamb, the performances of these states are expected to be above long-term average this year.

Average Broadacre Farm Income of New South Wales and Queensland



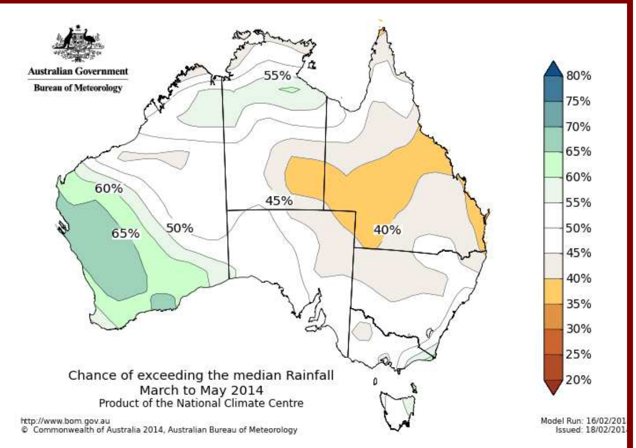
Source: ABARES

Expectedly, Queensland broadacre farms are likely to fare the worst this year from the most widespread drought conditions of all states. Average farm cash incomes are projected to decline everywhere except coastal regions, with the state average expected to fall by 35% to $39,000, largely attributable to severely reduced winter and summer crops, as well as lower cash receipts from livestock sales from battered saleyard prices despite higher turnoffs. About one-third of farms in Queensland are expected to earn negative cash income in 2013-14, up from 14%, which implies a notable deterioration in financial liquidity for some farm owners.

In acknowledgment of the financial hardship some farmers are going through, the Federal Government has recently announced a $320 million drought assistance package which would allow farmers easier access to income support and larger concessional loans.

Outlook

National Rainfall Outlook from March to May



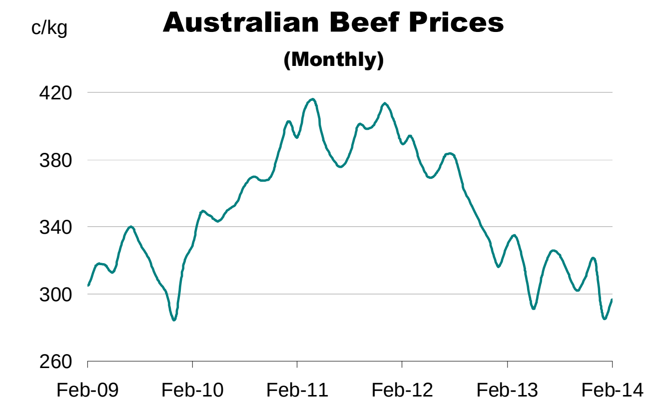
Source: BOM

In the months ahead, the prospects of Queensland and northern NSW returning to more normal weather conditions appear subdued. BOM's autumn rainfall outlook suggests that parts of central and western Queensland and the southeast corner of the NT are likely to receive below average rainfall during the season, dampening hopes of a major autumn break occurrence. This implies that high cattle turnoffs are likely to persist for some time to come, weighing on saleyard prices and fuelling exports further. The more positive rainfall outlook for NSW and Western Australia will continue to benefit the sheep re-stockers' interests to a larger extent, thereby reducing slaughter rates and seeing sheep prices outperforming that of beef for the foreseeable future.

The drier than normal outlook is also threatening the growth outlook for 2013-14 summer crops and winter crops next financial year. As outlined earlier, the effects of drought are already factored into ABARES' forecasts for this year's summer crops, but their effects on winter crops could be more severe than currently anticipated should soil moisture remain at low levels into the winter months; with a likely casualty in canola which is more sensitive to soil moisture compared to other major winter crops such as wheat and barley.

Key Commodity Prices

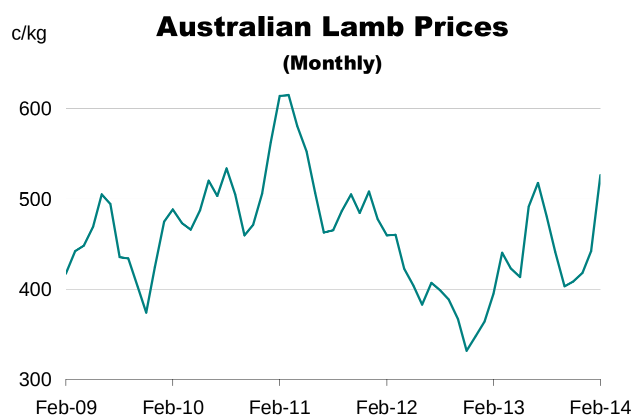
Cattle prices showed a mini rebound on scattered rain events



Source: MLA

Cattle saleyard prices, indicated by the Eastern Young Cattle Index (EYCI) rose consistently over February, to be 4% higher than the January average, as parts of the major cattle rearing areas received average to above average rainfall in the month. This trend persisted into the first week of March which offered further relief to restocking pressure. By state and territory, NSW and NT received relatively more rain to date, while Queensland's falls were concentrated in the north and west, with eastern producing areas missing out almost completely, offering limited prospects from breaking away from drought conditions anytime soon. Also, little rain was recorded in both SA and WA, while showers in Victoria were patchy. That said, the amount of rain received was far from sufficient to encourage a turnaround in feed regrowth and hence restocking intentions. The sustained strong pace of cattle slaughterings helped to contribute to another monthly record of beef and veal exports exceeding 100,000 tonnes swt, easily the highest volume for February. In particular, the firming of the EU economy has seen a rising demand for Australian red meat exports, with beef and veal shipments during February up 76% year-on-year, to 1,974 tonnes swt – the highest February volume since 1998, according to data from Meat and Livestock Australia (MLA).

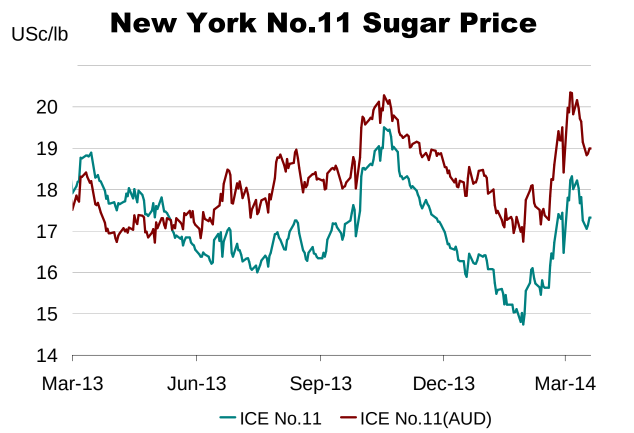
Lamb prices surged in February on promising rain events in NSW



Source: MLA

Heavy lamb prices continued to outperform cattle price growth in February, to jump by 19% to a monthly average of 525 AUc/kg, the highest since June 2011. Major rain events in producing regions of NSW during the month have offered a disproportionate boost to sheep restockers' confidence, as evident in a stabilising supply trend. Heavy lamb prices continued to benefit from wet weather in the first week of March, to rise by 29 AUc to 574AUc/kg cwt, a level not seen since Q2 of 2011. That said, the recent rain patterns in NSW are an exception, with many sheep rearing regions still under the cast of a sustained dry spell which has persisted for 18 months. Similar to the trends in beef and veal exports, lamb exports hit a new February record volume to exceed 19,000 tonnes swt, while mutton exports, which tend to be significantly less than lamb exports usually, also neared 19,000 tonnes swt. In the month, eastern states lamb slaughter reached the highest level in over two years despite notable rain events, according to MLA's National Livestock Reporting Service. Exports to the Middle East, Australia's biggest market, remained robust to rise by 3% year-on-year.

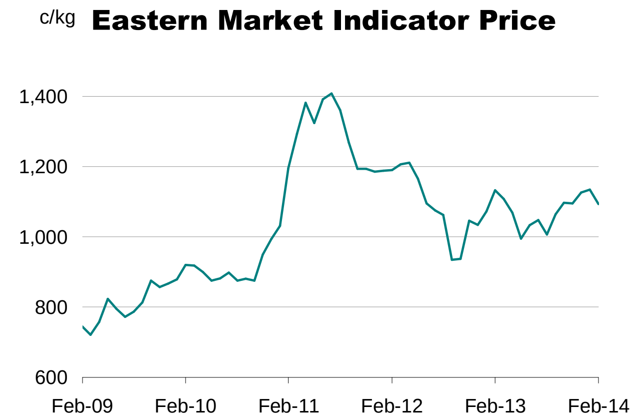
Sugar prices rose on production worries in drought-hit Brazil



Source: Bloomberg

Since the recent low in January, raw sugar futures have risen by more than 20% to be currently around 15 USc, as the worsening drought conditions in Brazil threaten crop yields from the largest producer and exporter in the world. Copersucar SA, a Brazilian producer cooperative with 47 associate factories, now expects millers to crush around 570mt of canes in 2013-14, 40mt lower than previously expected. This still represents a historically large crush figure and the associated sugar production loss (approximately around 2.9 mt) will serve little to dent the underlying global oversupply situation. Meanwhile, higher sugar prices may also encourage the production of more sugar instead of ethanol by sugar processors. The recent rally peaked on 6 March before easing on weak demand impetus for crystal sugar at the spot markets in Brazil. Four consecutive years of global surpluses are likely to culminate in a record sugar global ending stock of around 40 mt in 2013-14, and together with subsidised Indian sugar exports up to 4mt, are likely to weigh on international prices this year. More recently, some patchy rains in Brazil have improved soil moisture slightly.

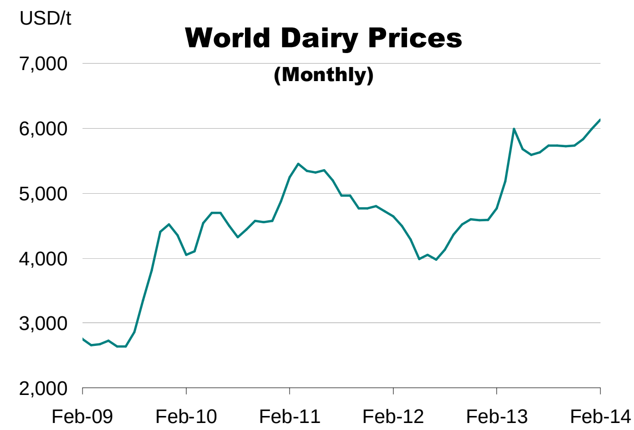
Wool prices retreated slightly from Chinese buyer activity and large auction offerings



Source: Datastream

In February, wool prices eased modestly by 4% in monthly average terms, with quieter activity from Chinese and Italian buyers largely reflecting some pulling forward of purchases in January, as well as wool offerings of increasingly poorer quality and lighter weight as drought conditions drag on. The easing in Chinese buyer activity also coincided with large volumes offered for auctions, as an increasing number of cash-strapped sheep farmers turn to income streams from wool sales to finance the basic requirements of feed and water for their core stocks. Meanwhile there were signs of some pick-up in activity from buyers from India and other destinations in the month, albeit still at ordinary levels. As the average quality of wool offerings drops, the demand for Superfine wool of superior quality became more acute, reflected in stiffer competition arising from Chinese, central Europe and Indian activity on the usual Italian operators at the top end of the market. High quality Superfine and Ultrafine wool were able to widen their premiums to the broader styles. Within the same micron bands, the same trends continue, demonstrated by the price disparity ranging from 40AUc to 80AUc/kg between the best and worst quality wool.

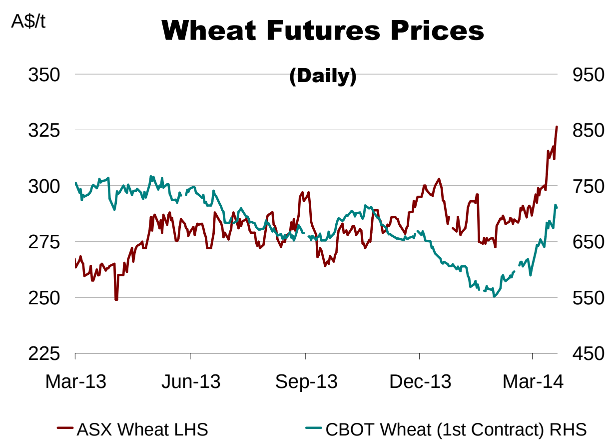
Consecutive declines in global dairy commodity auction prices possibly signalling a turning point



Source: BNZ

Global weighted dairy prices in monthly terms reached a record high in February, breaching USD6000/tonne for the first time in history. This has been largely driven by sustained robust Asian import demand, especially those stemming from China. Chinese dairy imports from NZ kicked off the year at a historic pace in January to be up 70% from same time last year, amounting to around USD1.3 billion. While this year's early celebration of the Lunar New Year would have had some pull-forward effects, underlying demand fundamentals remain solid. Optimistic about the current trends, Fonterra, the world's largest exporter based in NZ, raised its forecast farmgate milk price by 35 NZ cents to NZD 8.65/kgMS, which is 48% higher than last season's milk price. Correspondingly, Fonterra has also offered greater volumes at the recent GlobalDairyTrade (GDT) auctions which it holds twice a month, but demand conditions at the last two auctions had fallen short of expectations, which resulted in the index price falling on both occasions. The decline of 4% in the GDT Index on the auction on 4 March was the largest since June last year, possibly heralding the start of the long-anticipated correction from the current historically elevated levels.

A confluence of timely supply and geopolitical issues supported a sustained rally in global wheat prices



Source: Bloomberg

Global wheat prices have reversed their downward trend since the start February, to have risen by more than 20% from its recent low on 31 January. Wheat futures first rose on news of brisk demand for US wheat exports, as Canadian shipments faced rail transportation delays. Canadian production of wheat, canola and corn hit record highs in 2013, and the simultaneous surges of different types of crops have pushed the capacity of rail lines that handle 95% of Canada's output beyond their limits, which were further exacerbated by extreme winter conditions. Meanwhile, rising concerns about potential supply disruptions from the Black Sea, an important grain exporting region, as Ukraine remains highly volatile have also lent support to prices. So far there are no indications of any disruptions, with grain export patterns normal and the spring planting programs actually progressing at a quicker than average pace. More recently, news on drought conditions in Brazil and the closure of the largest grain exporting port in Rosario, Argentina after a ship ran aground in the main channel of the Parana River were also bullish on the market, but an overall loose grain balance sheet globally will serve to anchor prices in the medium term.

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