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Economic Report

Rural Commodities Wrap

Vyanne Lai, NAB Agribusiness Economist

September 2013

- **Global financial markets rallied strongly when US Federal Open Market Committee (FOMC) defied market expectations of a modest tapering and decided to leave retain the status quo on the pace of asset purchases.**
- **The long-awaited rotation of global growth towards a greater contribution from big advanced economies is currently underway, while some key emerging economies have shown notable signs of slowing.**
- **In Australia, domestic demand continues to struggle, with retail trade remaining weak into July, although sentiment in the housing market has improved.**

Throughout August and early September, global financial markets remained focussed on the likely policy actions of the big central banks, with the US Federal Open Market Committee (FOMC) on 18 and 19 September at the centre stage of attention. Global markets rallied strongly when FOMC defied market expectations of a modest tapering of $10bn to retain the status quo of asset purchases of $85bn a month, citing concerns on the rapidly tightening financial conditions in recent months and the need to see more improvements in the labour market. In saying there was now “no fixed calendar schedule” for when the US Federal Reserve will begin tapering its asset purchases, the Fed signalled that any tapering decision will be contingent on economic data and has effectively left markets today with no guidance on when and what will drive the start of a slowdown in asset purchases. Meanwhile, other central banks in the UK, Euro-zone and Japan have signalled that they are likely to keep their policy running along current lines for quite some time yet. Prior to the FOMC meeting, markets’ expectations of some form of Fed tapering have resulted in large capital flows out of emerging economies such as India, SE Asia and Latin America, which served to dampen their share markets and currencies significantly.

The last few months have finally brought some early evidence that things could be getting better and a rotation of global economic expansion towards a greater contribution from the big advanced economies has begun. This has been driven by a number of factors: ongoing advanced economy policy stimulus measures like Abenomics in Japan or incentives supporting the UK housing market, the ending of recessions in Western Europe, the impact of previous interest rate increases in emerging markets and recent financial market instability in big emerging economies like India and Indonesia. Several of the key emerging market economies have been experiencing difficulties in recent months. Financial market pressure and political difficulties have either seen policy tightened or likely interest rate cuts postponed in India (3rd biggest global economy), Brazil (7th biggest) and Indonesia (15th biggest). Fortunately, Chinese growth has held up and its economy is 1½ times the size of India, Brazil and Indonesia combined.

2013/14 Estimates, Rural Prices & Production

Commodity	Production	Price
Wheat	21.0%	-22.5%
Beef	3.0%	4.0%
Dairy	1.6%	22.5%
Lamb	-7.1%	10.8%
Wool	-3.3%	3.2%
Sugar	4.7%	-1.8%
Cotton	3.0%	23.3%
Oil	-	-3%

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

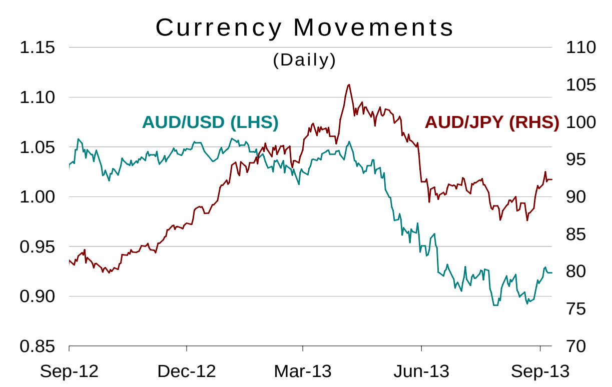
Within Australia, national accounts for Q2 showed no sign of GDP growth picking up from sub-trend rates. Domestic demand continues to struggle, with retail trade remaining weak into July, although sentiment in the housing market has improved. Underlying business investment declined with Q2 capex giving no hint of a pick-up outside the mining sector. Business conditions remained weak into August, especially employment, with soft orders and low capacity utilisation. However, confidence recovered strongly, especially in mining, construction and finance. We now see growth softening to 2.3% in 2013, before rising to a still below-trend rate of 2.5% in 2014. We still expect the RBA to cut again before the year ends, likely in November on the back of continuing low inflation and a weaker labour market.

In August, the prices of livestock moderated slightly on continued high slaughter rates in response to price increases in the past two months. Wool prices retraced slightly from the height reached before the annual three-week trading recess as auction sales and supplies resumed. Dairy prices have stabilised from the recent Fonterra crisis but maintained at high levels from global supply shortage. Global wheat prices were pressured by weak corn complex in the month but derived some support from expectations of strong Chinese demand. Meanwhile, sugar prices received a boost from purchases by the US government, while cotton prices stayed largely unchanged in monthly average terms. This month, sugar is our commodity in focus.

Currency Movements

Since early August, the AUD has rallied by around 4%, whether measured just against the USD or in broader trade-weighted terms. Upon FOMC's announcement on 19 September that tapering will not start this month and any future decision to slow its asset purchases will be guided by emerging economic data, the AUD shot past 95 US cents to be the highest since mid-June. Given the overall more dovish slant of the FOMC (in terms of not starting tapering, and possibly not starting it this year– the USD is going to be softer for longer and in itself this means AUD is likely to now spend some time above 95 cents. Almost half of AUD's fall to date has now been retraced. While there is in no sense of a mechanical link between the currency and RBA policy, further currency strength will surely add some pressure for the RBA to cut again and sooner than the market discounts (the Overnight Indexed Swaps (OIS) curve is currently pricing 26% chance of cut in November, 54% chance of cut by March and 36% chance of rate hike by December 2014). Also note the comments from the RBA's Assistant Governor Malcolm Edey recently which suggest the RBA does not share the bubble view of housing. As such housing issues – at the moment at least - look to be less of a constraint to further easing than many assume. In any event, shifting expectations for RBA policy are at best a minor influence on where the AUD now trades. USD considerations should till overwhelm in the short-run, and in the continuation of a loose monetary setting in the US, the realisation our AUD forecast of 86 US cents by the end of the year is now looking highly improbable. As such, our analysts are leaning towards lowering our USD forecast profile and lifting our AUD forecast profile in the coming week.

The AUD regained some momentum in August

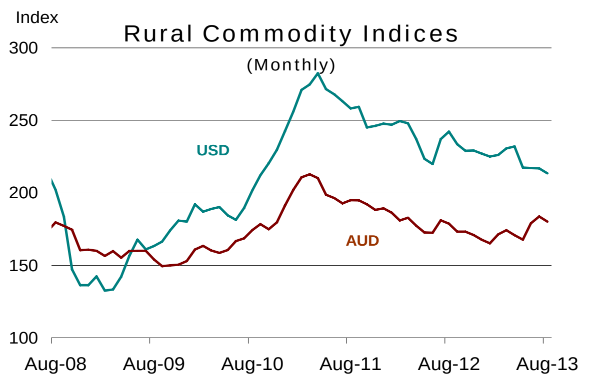


Source: Datastream

NAB Rural Commodity Index

In August, the loss of steam in the price growth trajectory for livestock after two months of solid gains and an appreciation of the AUD saw a 1.9% fall in the NAB Rural Commodity Index in AUD terms in the month and a corresponding marginal decline of 1.6% in USD terms. Lamb led the pack in losses denominated in AUD by falling by 7%, followed by wool (-4%), dairy (-3%) and beef (-1%). These were partly offset by moderate rises in sugar (+2%) and barley (+1%) while wheat and cotton remained largely unchanged. In the near-term, there are some upside risks to the index in AUD terms from a likely easing in the AUD should the Fed's tapering commence after the FOMC meeting this week, but the dampening effects of the Fed's tapering on the AUD is likely to be relatively minor as most of the downside risks to the exchange rate have already been captured in its depreciation against the greenback to-date. Moreover, any tapering by the Fed is expected to be gradual and unlikely to cause sharp moves in the exchange rate.

Rural Commodity Index fell in AUD terms

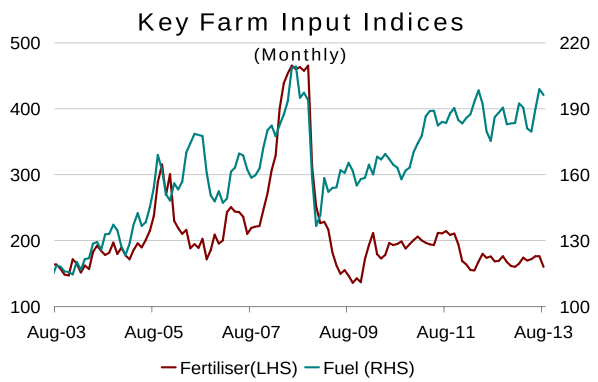


Source: Bloomberg, NAB Economics

NAB Farm Input Indices

Over the past month, the global fertiliser market retreated moderately to still track at subdued levels, with broad-based falls recorded in the global prices (denominated in USD) of urea (-13%), Diammonium Phosphate (-9%) and natural gas (-5%). The appreciation in the AUD in the month suggests that the overall price impact on the fertiliser index in AUD terms is less, with the index recording an overall decline of 9% in the month. Sluggish global demand and an overhang of global inventories have kept a lid on fertiliser prices. China's low export tax window for Diammonium Phosphate and urea, which are currently in effect and will run through to mid to late October, have also ensured a consistent stream of nutrient exports from the country, keeping upward price potentials in check. The oil price index fell marginally in August but remained at elevated levels on heightened geopolitical tensions in Syria.

Fertiliser prices remained subdued but oil prices stayed elevated on Syrian crisis



Source: Bloomberg, NAB Economics

NAB Weighted Feed Grains Price

Feed grain prices were generally lower in August, with the domestic futures market increasingly geared towards new crop prospects, which suggest improved production on more favourable weather conditions relative to last year. Barley production is forecast to increase by 10% in 2013–14 to 7.4 million tonnes. Similarly, production of sorghum, Australia's major summer coarse grain, is forecast to increase by 22% to 2.1 million tonnes on larger plantings and improved yields.

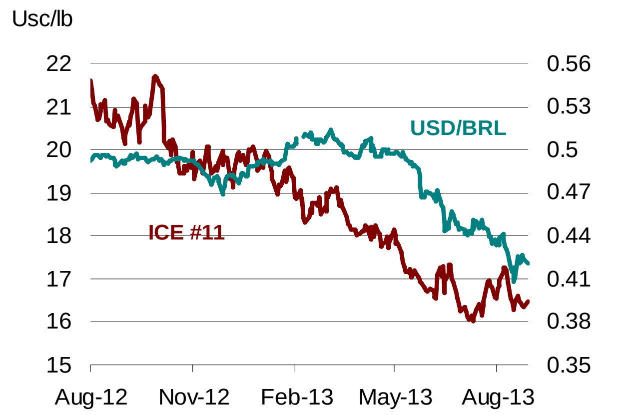
In Focus – Sugar

- **Sugar prices have stabilised somewhat in August after a prolonged period of steady declines, as rising demand for ethanol in Brazil competes for sugarcane supply and the US government intervened in the market to boost prices and stave off risks of federal loans defaults.**
- **Sugar market fundamentals suggest that global surplus in 2013/14 might be smaller than expected, with solid production outlook in Brazil, Thailand and China likely to be counteracted to a large extent by robust demand by emerging economies, although sharply depreciating Indian rupee and Brazilian real pose some downside risks to prices.**
- **Australian sugarcane crushing season is more than half way through with industry bodies reporting mixed conditions across regions. Overall production and exports expected to tick up on increased plantings and improved yields.**

Sugar prices have stabilised lately but remain at low levels

Since reaching a three-decade high in October 2011, sugar prices have plunged 40% as global production recovers from drought conditions in many major producers in the 2011-12 marketing year (from October to September). Output from Brazil, the largest producer in the world, is estimated by the US Department of Agriculture (USDA) in its May report on sugar to have risen solidly by 7% in 2012/13, aiding an overall growth of 1% in world supply and global surplus of around 11mt. Furthermore, sharp depreciations experienced by currencies of major exporters of Brazil and India this year have also played a significant role in driving the prices of sugar contracts traded in global futures exchanges, denominated in US dollars, lower. Brazil is the key global exporter with almost a 50% share of the global market and any depreciation in the real has a sizeable market-moving impact, as a weaker real has meant Brazilian exports are now much more competitive, even though domestic prices denominated in real may stay the same.

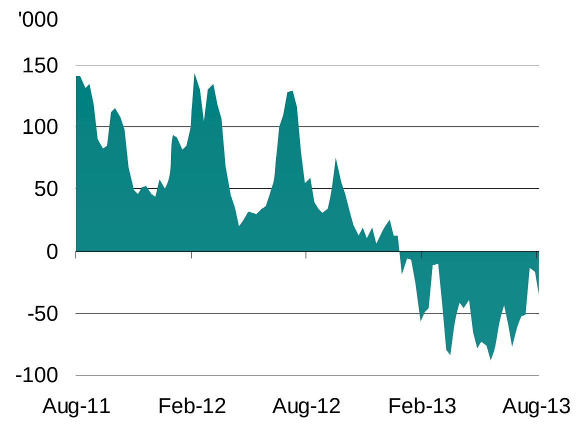
Sharp depreciation in Brazilian Real has weighed on sugar prices



Source: Bloomberg, NAB

Having said that, the price level of sugar is unlikely to fall that much further, given that it has reached a level where it's already below the cost of production for some refiners in Brazil, with a larger proportion of sugar canes being diverted to the production of ethanol, serving as a floor to prices. Reflecting this, net short managed money positions have declined since mid-June and retraced notably in July. The global index for sugar, ICE #11, got a significant boost mid-July from China importing 504,000 metric tonnes of sugar, raw value, in July 2013, up 25% from the same month last year and the highest amount imported in any month of the 2012/13 (Oct/Sep) season so far, said the National Development and Reform Commission (NDRC), citing customs data. A prolonged period of depressed sugar prices has also prompted concerns by the USDA that producers might not earn enough income to repay their federal loans. This has resulted in the USDA recently buying sugar from a domestic processor and selling it to an ethanol producer at a loss of $2.7 million, the latest move by the agency to encourage price growth and stave off defaults on federal loans. During the fiscal year ending October, the US government lent $1.1 billion to sugar processors, secured with 2.6 mt of the sweetener. As of late August, 27% of those loans remained outstanding. Market participants estimated that the government will need to remove additionally 0.3 to 0.5 mt of the sweetener by the end of the season in October to avoid any forfeiture whereby processors will pay the government back with tonnes of the sweetener instead of cash. As such, it's likely to be the case that sugar prices are likely to stay reasonably stable in the short-term as they have reached levels deemed to be unsustainable in the long-term by industry authorities. In the medium term, volatility in sugar prices are likely to reduce as most of the expected global surplus for 2013/14 is already priced in, but downside risks stemming from the likely continued weakness in the Brazilian real and Indian rupee remain.

Net Managed Money Positions in ICE #11 Sugar



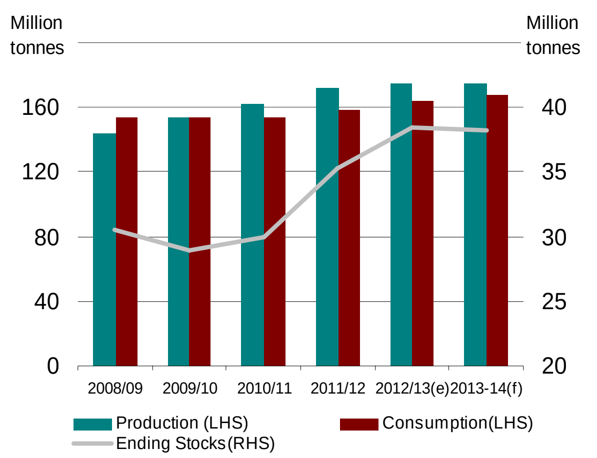
Source: Bloomberg, CFTC

Global production to exceed consumption for the fourth consecutive year

As previously alluded to, global production is expected to exceed demand this 2012/13 marketing year, largely reflecting the favourable planting conditions and an acreage response to the high prices in 2010/11. However, the low prices of 2012/13 are likely to provide some offsetting effects by discouraging the cultivation of sugar crops for the upcoming marketing year of 2013/14 (October to September). An indication of this has been the report of significantly reduced sowings of beet in Russia and Ukraine and increasing diversion of sugar crops into biofuel production. Echoing this trend, the International Sugar Organisation (ISO) has forecast in its latest monthly report that global production will fall 1.2% to 180.8mt in 2013/14, the first drop since 2008/09, while demand to expand by 2.1% to 176.3mt. Meanwhile, the USDA is forecasting global production and consumption for 2013/14 to be around 175mt and 167mt respectively. Despite the differences in the levels of forecasts by the ISO and USDA, both agencies came to a similar conclusion that the world will enter into its fourth consecutive of year of statistical sugar surplus in 2013/14.

In Brazil, production this year was affected somewhat by persistent wet weather and a surprise frost in July. This has prompted the official crop bureau of Brazil, Conab, to revise its forecast for Brazillian sugar output downwards by 2.6mt to 40.97m tonnes, representing an annual growth of 7.1% which is broadly consistent with USDA's forecast.

USDA Global Sugar Balance Sheet



Source: USDA, NAB Economics

Apart from unfavourable weather, an increasing trend of diverting sugar cane supply into ethanol production instead is also exerting downward pressure on Brazilian sugar output, thanks to the more favourable returns to mills from producing the biofuel than the sweetener. According to ABARES' September quarter report, the proportion of sugar cane to be used to produce sugar, rather than ethanol, in Brazil is forecast to decline by 5 percentage points in 2013/14 to 45%. This decline is based on a recent increase in the mandatory blending ratio of anhydrous ethanol (which is produced in a smaller quantity than hydrous ethanol in Brazil) with gasoline from 20% to 25%, effective from 1 May 2013. Many vehicles in Brazil can run on either pure, hydrous ethanol or the gasoline-anhydrous combination, but more drivers have opted for the blend this year, which raises concerns of a potential shortfall as the sugar cane industry goes into the inter-harvest season, especially when the current level of inventory remains low. The higher domestic prices of ethanol relative to sugar have encouraged mills in the South Central region of Brazil to continue to prioritise ethanol production during the first half of July. The share of processed cane directed to sugar production was just 45%, compared to 50% in the same period a year ago. The resilient demand outlook for ethanol is likely to have positive spillover effects onto sugar prices as well, which suggest sugar prices in the domestic currency are likely to stay buoyant.

Sugar production in China, the second largest global producer, is forecast by ABARES to be largely unchanged at 14.2 million tonnes in 2013/14, with an increase in average sugar yields largely offsetting the adverse effect of smaller plantings. This is a result of Chinese farmers responding to lower world sugar prices by moving away from sugar cane cultivation to alternative crops. On the other hand, production outlook in Thailand, the third largest producer, is rosier by comparison. ABARES is predicting that the country's production of the sweetener will grow by 7% in 2013/14 to 10.7mt, with a return of more favourable seasonal conditions from drought conditions in 2012/13 is likely to improve yields with similar areas planted.

As with many other food commodities, growth in sugar consumption in 2013/14 will be predominantly driven by large emerging economies, such as China, India and Brazil. With a rapidly rising middle class in these countries, dietary patterns have shown a significant shift from "staples" of grains to the discretionary items of proteins, fats and sugar. Higher household incomes are also associated with relatively more copious amounts of processed foods consumption which typically contains higher sucrose content. Imports of raw sugar in Indonesia, the world's largest importer, is expected to double to 5.4mt in 2013/14, after heavy rains caused extensive damage to the country's cane crops. Apart from seasonal factors, other regulatory and market-related issues such as land license red-tape, competition for land and under-investment have also frustrated the government's efforts to boost sugar output, inadvertently led to the abandonment of its goal of being self-sufficient in white sugar production by 2014. As such, it needs to import sugar from Brazil, Thailand and Australia to satisfy its domestic needs. In China, low global prices are enabling sugar to gain market share over high-fructose corn syrup, an alternative sweetener. Chinese import demand maintains a strong pace on the back of a government policy to stockpile local sweetener which helped push domestic prices above the international market, prompting more buying. Similarly, significantly reduced plantings of sugar beet in Russia are also likely to prompt it to increase sugar imports significantly.

Australia's prominence in global sugar trade is gaining traction

As a result of the acceleration in demand from these emerging economies and strong production outlook in Brazil and Thailand, global trade in sugar is expected to pick up pace in 2013/14, by around 2.5% according to ABARES' latest September quarter report. While production in India is expected to be lower in 2013/14 at around 24mt, record weakness in the rupee against the USD is likely to spur demand for Indian exports quite markedly, with the country's largest refiner, Shree Renuka Sugars Ltd expecting a threefold increase in the country's exports in the year.

While Australia is not a major global producer of sugar, its status as the third largest exporter in the world is more relevant, with around 80% of sugar production destined for foreign countries at a value of around $1.3bn. ABARES pegs Australia's exports in 2013/14 to be at 2.9mt, largely unchanged from 2012/13, while production is forecast to be 4.25 million tonnes, down slightly from 4.3 million tonnes in 2012/13. The forecast decline reflects flood damage to new plantings in early 2013 and lower average sugar yields, due in part to canopy syndrome disease in the Bundaberg and Isis regions. Australian sugar cane crushing season is now more than halfway through, with industry bodies citing inconsistent crop conditions across regions. According to them, old crop standover canes are yielding more poorly than expected, meanwhile some regions in northern Queensland, such as Burdekin, are enjoying optimal crushing conditions from improved mill performance, favourably dry and mild weather and record sucrose content. On balance, they are relatively more pessimistic than ABARES in their forecast production volume, to be around 3.8 to 3.9 mt.

Despite a more competitive exchange rate relative to a year ago, overall earnings for Australian exporters are expected to be marginally lower in 2013/14, with largely similar export volumes expected to be more than offset by weaker world prices.

Comments from the field

The crush for the Mackay/Proserpine district has experienced some recent ideal harvesting conditions over the past few weeks. Approximately 50% of the crop has been cut to date and the sugar content is quite acceptable around the 14 mark. The tonnes cut remain in line with estimates or above expectations. A few farmers are now looking to the skies for rain with a view of establishing their plant cane and ratoons for next years crop.
Arthur Douglas, Agribusiness Manager 2, Mackay, QLD

Good weather for the first 9 weeks of the crush in the Bundaberg Sugar and Isis regions has seen good throughput for all three mills. Bundaberg Sugar has processed nearly 40% of its estimated 1.5 million tonnes and Isis has processed half of its estimated 1.2 million tonnes. Dry weather is a concern as tonnages are starting to slip below estimates. However, Commercial Cane Sugar (CCS), which represents the sugar content of cane as it is purchased by sugar mill, is good averaging above 14.5 for the year at all three mills. Isis is projecting that the crush will be completed in early November a couple of weeks before Bundaberg, weather permitting.
Ian Frankland, Agribusiness Manager, Bundaberg, QLD

We saw Burdekin pass 5 million tonne cane crushed or 72% at average CCS 14.28. Ideal harvesting conditions and well performing mills have resulted in revised completion date for harvest of 19/10/2013. Estimate at the beginning of the season was originally for total 7.44 mill crushed with a finish date of 09/11/13. Whilst tonnage has been revised down, CCS continues to remain steady on last year's result with steady increases seen over recent weeks.
Tanya Atkinson, Agribusiness Manager, Ayr, Qld

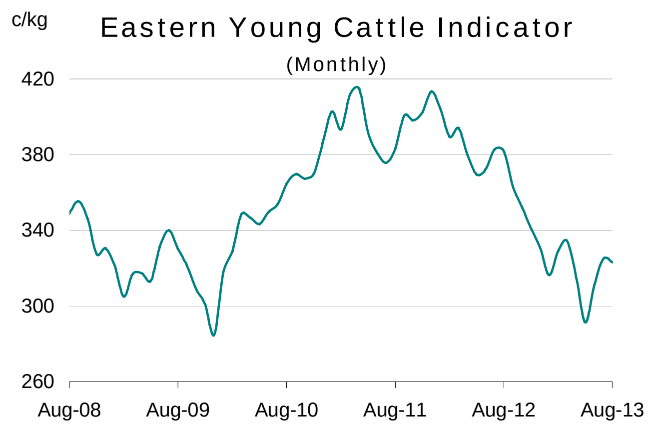
The Herbert district has emphatically demonstrated its two climate zones this year being on the transition between the wet and dry tropics. The wet zone to the north of Ingham and west of the Stone experienced wet conditions through June and July, which disrupted the harvest and delayed planting. Meanwhile, the dry areas to the south of Toobanna and Cattle Creek and also the Upper Stone are exhibiting very dry, moisture-stressed conditions and will need rain to hold the condition of the crop at its current estimate. Harvesting equity consideration has helped the groups in the wet areas to catch up.

The crop is now more than 63% harvested and in the absence of major rain or mechanical issues the crop will be harvested by late October to early November. The crop is now cutting at 99.6% of original estimate indicating we are likely to harvest very near 4 million tonnes. The mill estimate has been downgraded to 3.95 million tonnes from an original figure of 4.04 million. A major part of the former Managed Investment Forest Plantations has now returned to sugar cane use with plantings this year.

Yellow Canopy Syndrome remains a mystery as to its root cause. It is being expressed in differing degrees throughout the Herbert but most significantly in moisture stressed soils south of Ingham. Members of the Science advisory panel have visited and are reporting with recommendations for further investigation. CCS results for severely affected cane have shown substantial losses. The district is very concerned about this latest threat to the crop.
Tony Duggan, Manager, Ingham, Qld

Key Commodity Prices

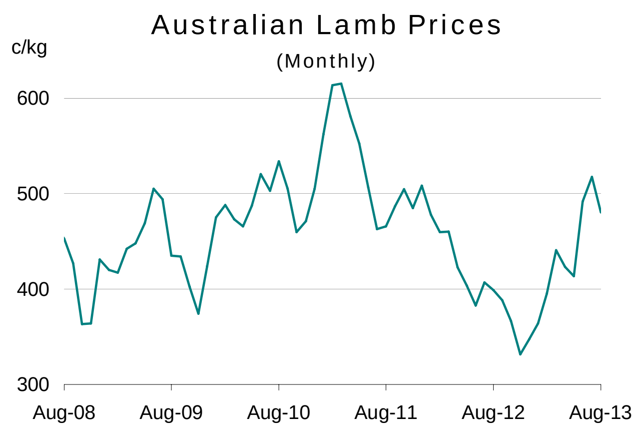
Cattle prices fell marginally from persistent dry conditions in the northern regions



Source: MLA

After some improvements in June and July, cattle prices moderated in August as seasonal conditions in the northern part of NSW and Queensland deteriorated further during winter time on prevailing dryness, while Southern states enjoyed decent amount of rain coverage. A lacklustre finish to winter and a warm start to spring continue to underscore a dire need for a decent spring break for the northern states, as continued dryness in these areas threatens a recurrence of a similar situation during spring last year when the lack of feed availability drove a sharp uptick in slaughter rate and corresponding decline in prices. Despite the Bureau of Meteorology's forecast of 55-60% chance of above median falls for spring, so far rain occurrences across the country have been patchy at best. After a sustained period of high throughputs (since the end of last year), there have been some signs of supply slowing in recent months, especially in Queensland, with producers preferring to retain breeding stock for when the drought breaks. This suggests some upside potential to prices in the near term.

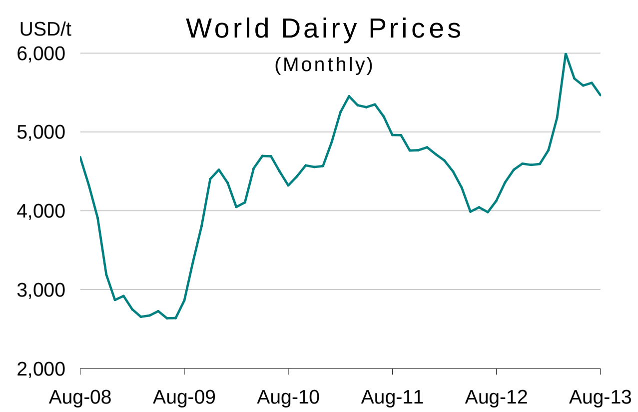
Lamb prices fell in August on increased supply, contributing to the highest August export volume on record



Source: MLA

Similar to the trend in beef prices, heavy lamb prices fell in August on a positive supply response associated with the firming of prices in the months of June and July, at a time when supply was expected to tighten. While the pick-up in prices served as an incentive to lift production, the main driver of elevated throughput is still the unrelenting dryness in the northern regions. Particularly in NSW, dry conditions saw saleyard throughput reach levels not seen since 2009. This in turn contributed to the highest August export volume on record in the last month to 16,286 tonnes swt. Leading August exports were shipments to the Middle East totalling 5,388 tonnes swt, up 9% on year-on-year and the third largest monthly volume on record, only exceeded by those in July and May 2013. Encouragingly, most of the shipments consisted of chilled beef, which commands a higher premium than frozen beef. As a result of high slaughter rates combined with low prices, total lamb exports from the start of the calendar year through to August have lifted by 12% relative to the same period in 2012, the highest year-to-date lamb export volume on record. Looking forward, lamb supply is expected to tighten as herd rebuilding by farmers resumes, providing an underlying layer of support to prices.

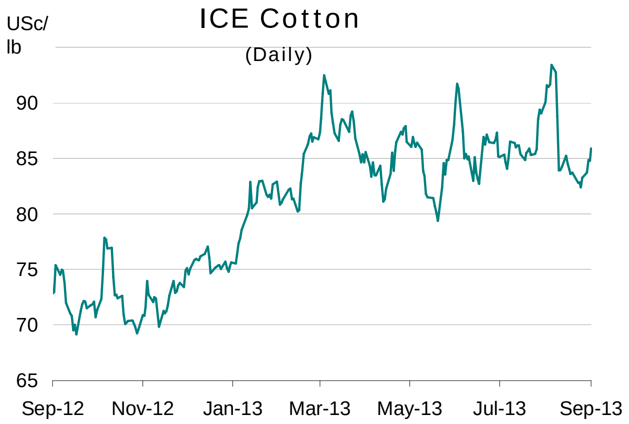
Global dairy prices stayed elevated in August on global supply shortage



Source: NZX

Global dairy prices fell marginally but still tracked at elevated levels from a tight global supply. The market furore caused by the alleged discovery of botulism-causing bacteria in a sample of whey protein concentrate from Fonterra has ended well as the New Zealand Ministry for Primary Industries Ministry concluded from their own extensive testing that no such bacteria was present. Nonetheless, Fonterra, the largest dairy company in th world, has reduced its offerings of products to be sold on GlobalDairyTrade (GDT), citing a move into higher value products as the reason for this. This is likely to exacerbate the supply tightness situation in the short term and keep prices high. However, it is not clear how quickly the market will be able to respond to these price signals. Production in New Zealand and Australia is having a good start to the new dairy season, but is unlikely to be able to fully supply the market in the immediate future. In the Northern Hemisphere, production has passed its seasonal peak but remains relatively stronger during the same time last season for both the US and European Union. Nonetheless, most of the production in these regions will be directed at domestic consumption rather than exports.

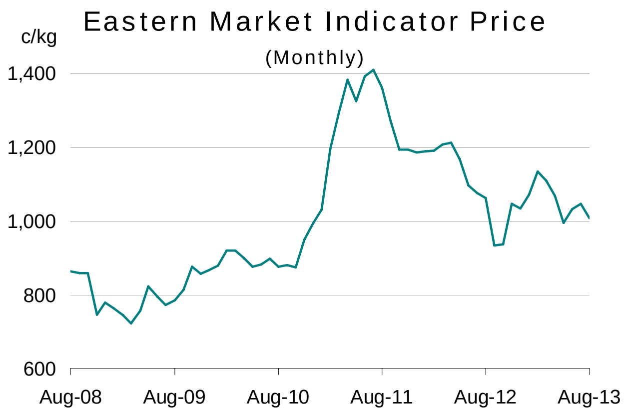
Cotton prices volatile in August on speculations of poor crop conditions in the US



Source: Bloomberg

Cotton prices were relatively volatile in August compared to recent months. Early to mid-month, speculations of poorer crop conditions due to wet weather delaying crop development helped to build upward price momentum ahead of the release of World Agricultural Supply and Demand Estimates (WASDE) report by the US Department of Agriculture. It then peaked at US93.4 cents, the highest since early 2012, when the report revealed a downgrade to the world cotton supply forecast and predicted a higher level of world consumption. However, prices quickly turned southwards to record the biggest three-day slump since 2011 when dry weather was forecast to return in Southeast of the US, the world's largest exporter. Despite short-term price volatility, the underlying fundamentals suggest that global supply is going to exceed demand this 2013/14 marketing year, even as production is expected to fall. The latest September WASDE report pegged world production at 117.4 million bales while consumption to 109.5 million bales, with global ending stocks rising to record high of 94.7 million bales. Adding to the downside risks to prices are favourable growing conditions in India and a sharply depreciated rupee, which suggest that exports from the country are likely to be very strong this year.

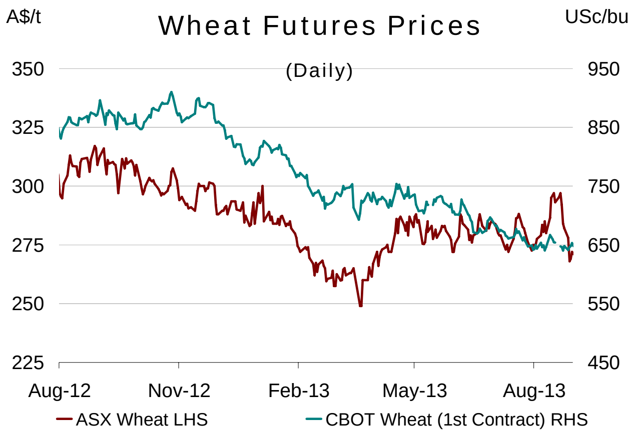
Wool prices stayed resilient as auction sales resumed from winter recess



Source: Bloomberg

Wool prices fell marginally in August but remained at relatively resilient levels as the resumption of auction sales after a three-week winter recess was greeted positively by buyers. Volumes were thin to start with, but picked up pace towards the last week of the month, accompanied by substantial price gains being recorded across the entire selection from medium to superfine types. This trend continued into the first week of September, supported by strong demand from China whereby large forward orders have been placed with traders and exporters for shipments up to November, although very little speculative purchasing for the 2014 calendar year has been witnessed. More recently, the strengthening of the AUD to around US 92 cents and a supply response to the two consecutive weeks of robust price increases have taken some wind out of the sail of auction sales, but sellers are hoping that some positive sentiments and demand impetus would arise from the attendees of the annual Nanjing Wool Market Conference held from 14th to 16th September in China. In the short-term, prices are likely to be range-bound as spring supplies gain pace.

Domestic wheat basis resilient on weaker new crop prospects in New South Wales and Queensland



Source: Bloomberg

Global wheat price is largely unchanged (+0.6% for red hard winter wheat) in August in monthly average terms, with robust Chinese demand overcoming the weight of a weak corn complex. Wheat and corn prices are highly correlated given their high degree of substitutability in animal feed, and the currently looming global corn bumper crop is offering no reprieve to wheat prices. Corn output in the US, the largest producer in the world, is expected to hit record high at around 13.8 billion bushels this year, sending global inventories jumping by 24% to the highest in 12 years. However, demand for wheat continues to be relatively resilient from sustained demand from emerging economies and should provide a floor to wheat prices in the near term. In contrast, domestic wheat prices have held up relatively better due to speculations of worsening crop prospects in NSW and Queensland, although production in WA, Victoria and SA are now expected to be stronger than previously thought in light of some decent rain outcomes recently. This has prompted us to revise our earlier production forecast for Australia for 2013/14 upwards, from 24.1mmt to 25.0mmt.

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