

Westpac-NFF

# Commodity Index

Barley • Beef • Canola • Cotton • Dairy • Sugar • Wheat • Wool

March 2008

## Good reason for optimism, but high prices bring risks

Recording a new 20-year high in February, the *Westpac-NFF Commodity Index* surged a further 2.5% on the back of strong underlying global demand fundamentals.

While the rural sector remains optimistic, mounting input costs, and rising volatility in output prices, illustrates it is vital that Australian farmers exercise caution and apply solid risk management practices.

As demonstrated with the 2007 winter crop, when many producers failed to meet contract targets after poorer than expected yields, farmers must make realistic production estimates, rather than getting carried away by the potential offerings of strong commodity prices.

Farmers have access to a wide variety of modern risk management tools that can assist them in achieving more competitive, sustainable and profitable farming businesses despite the hazards that beset the sector from time to time.

These include a combination of tools under the Australian Government's Advancing Australian Agriculture (AAA) package, commercial risk management tools such as price hedging and farm management deposits, and new on-farm technology adoption such as GM crop varieties and improved water reticulation systems.

As usual, farmers are encouraged to seek advice from trusted sources such as their accountants, bank managers, financial planners and others within the farming community on the range of options that are available.

Compared with January 2008 levels, global prices in

easing demand growth. Chinese interest in Australian stocks has subdued, due to the Chinese New Year holiday, with demand expected to rise in March.

Saudi market demand for feed barley eased following the arrival of Australian shipments, which bolstered the region's stock levels.

## "Australian farmers face a delicate balancing act."

- NFF Vice-President, Charles Burke

February increased for Barley (0.7%), Beef (1.2%), Sugar (8.6%), Wheat (10.1%) and Canola (13.1). Cotton (-0.9%), Dairy (-2.8%) and Wool (-4.4%), all experienced a decrease in price from previous month levels.

The overall weighted index increased by 2.5% during February, taking it to 25.7% above year-ago levels.

### Barley

While world barley prices lifted marginally during February, the market showed signs of

### Beef

Prices for imported beef in the United States (US) market were driven even higher by steady demand on tight supplies from Australia, New Zealand (NZ) and Uruguay. With imported supplies difficult to source, prices for US domestic product have also been forced higher by end-users.

Preparations for the Lunar New Year celebrations were well underway in Korea ahead of the holiday break in early February.



Table 1. Component Indices.

Australian \$	Index				Percentage change over		
	Feb-08	Jan-08	Aug-07	Feb-07	1 month	6 months	12 months
Wheat (AU c/bu)	1128	1024	850	610	10.1	32.6	84.7
Barley (AUD/t)	245	243	198	203	0.7	23.2	20.6
Canola (AU c/kg)	712	630	473	413	13.1	50.5	72.3
Cotton (AU c/lb)	79.8	80.5	73.1	68.9	-0.9	9.2	15.9
Sugar (AU c/lb)	14.8	13.6	11.8	13.6	8.6	25.1	8.7
Export beef index (AUD)	162	160	150	157	1.2	8.0	3.4
Dairy price index (AUD)	175	180	215	136	-2.8	-18.9	28.7
Wool (AU c/kg)	1020	1067	944	994	-4.4	8.1	2.7
USD Index 97/98 = 100	208	196	170	141	6.0	21.9	46.8
AUD/USD	0.913	0.882	0.829	0.782	3.5	10.2	16.8
USD Index 97/98 = 100	155	151	140	123	2.5	10.6	25.7

a) The indexes are calculated as monthly averages

b) Data sources are Bloomberg, USDA, FAS.

A peak period for beef consumption, importers and retailers have been building supplies for popular beef gift sets over the past three months.

The market was seasonally quieter for the latter half of the month, but low stocks of NZ, Australian and US beef put significant pressure on prices.

The tight supply of Australian chilled items on the Japanese market helped strengthen importer demand, although the strong Australian dollar (AUD) deterred buyer willingness to match current market prices.

### Canola

Global canola prices saw a further 13.1.0% rise in February due to unrelenting demand on a market with already limited stocks. Buying of old crop canola was, again, strong, reflecting sustained demand for the oilseed complex.

Canola futures were also driven by poor seasonal conditions. Severe flooding in South America adversely affected crops in that region and China's harsh winter has raised concern about the extent of damage to their stock.

### Cotton

Cotton prices decreased over February due to widespread speculation on what is considered one of the remaining

underperforming agricultural markets.

Australian short-term export demand to China has been subdued throughout February as Chinese New Year celebrations and wild snowstorms forced Chinese mill closures.

Increasingly, reports have noted spinning mills - in countries including India, Pakistan and Turkey - have opted to limit yarn production rather than produce stock at a loss.

Rainfall at home bolstered a positive outlook for the 2008-09 crop as water storage levels in many areas were replenished.

### Dairy

Despite the depreciating US dollar and rising global



'Bringing in the sheaves'... wheat farmers rejoice as global prices soar.

demand across all major dairy categories, world prices fell 2.8% during February.

Global dairy sales lifted in both volume and value as drought limited supplies from traditional exporters, such as Australia and NZ.

Milk production in NZ was again limited as drought conditions affected their largest dairying region, Waikato. The resultant downturn in NZ dairy supplies and increased milk production in other dairy markets around the world led to a slight softening of dairy prices.

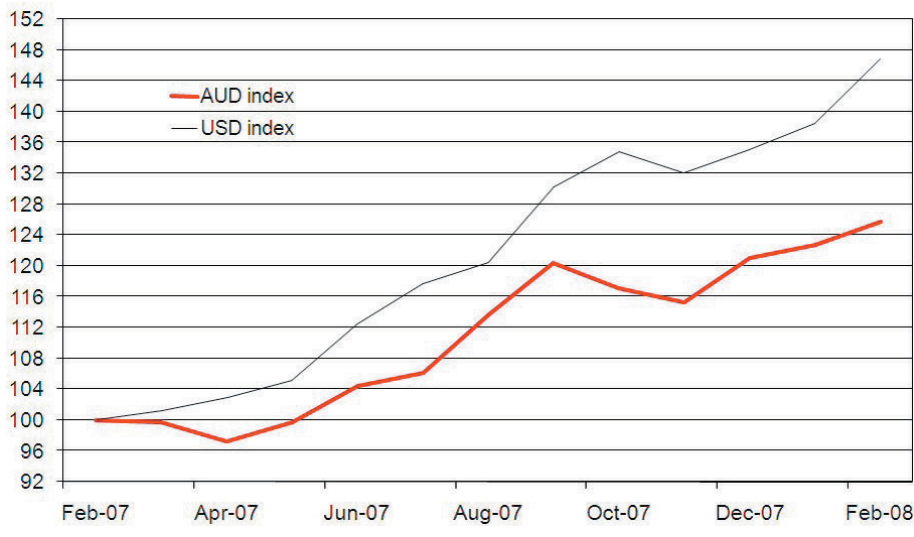
Kenya, east Africa's leading milk producer and exporter, has been working towards re-empowering its dairy industry following post-election violence, which disrupted processing and export supplies.

The sector was critically hurt as the main milk production area, the Rift Valley province, was hardest hit by skirmishes that resulted in displaced farmers, transport disruptions and destruction of processing equipment and plant property.

The Kenyan dairy sector has moved to prioritise milk exports to their major Middle East market ahead of their domestic market in order to protect exports from the country's main competitor, South Africa.

### Sugar

Biofuel production, again, drove global demand as prices

**Graph 1. Index Over 1 Year: Average Of First Month = 100.**

strengthened 12.4%, despite production increases, largely from Brazil and India.

Recent rains in Australia topped-up water reserves and better seasonal conditions have had a positive impact as the raw sugar harvest is expected to rise.

### Wheat

The global wheat price soared 10.1% this month to new record highs. The spike was largely driven by a weak US dollar and a lack of product availability.

World wheat holdings are severely depleted with US stocks at their lowest since 1947/48.

Dry weather in the US and Canada, and speculation of dry conditions across the north China wheat-belt, also affected prices.

While global prices continued to be supported by

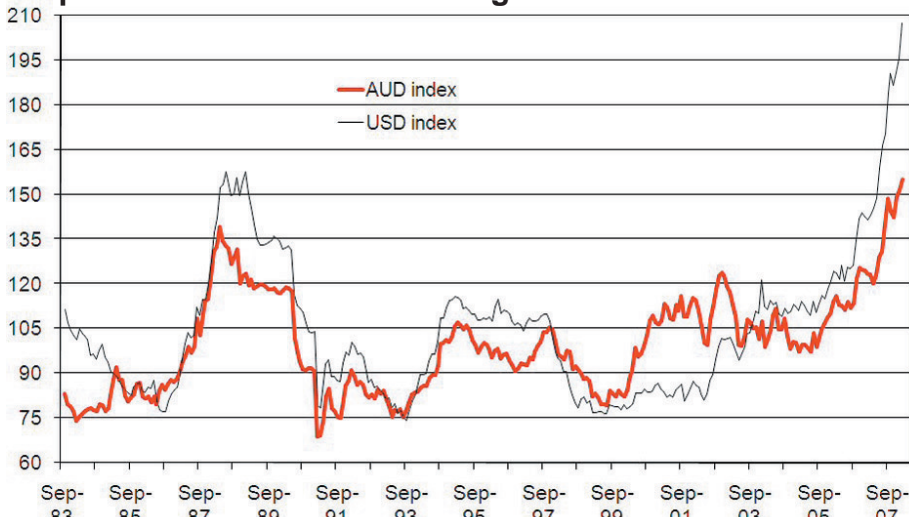
Asian demand, Egypt cancelled a tender in mid-February highlighting that there are still many importers reluctant to commit to large volumes of wheat at current market prices.

### Wool

After a month of solid gains, the Australian wool market traded 4.4% weaker during February as volatility in both the currency and equity markets finally took its toll.

Demand for Australian and NZ wool continued to be subdued due to the Chinese New Year and snowstorms closing a number of domestic wool mills. The renewed strength of the AUD further dampened demand for wool.

However, demand for quality wools remained strong from all trade sectors.#

**Graph 2. Historical Index: Average Of 1997/98 = 100.**

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## Commodity Index

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This index is updated on a daily basis and calculated in both SA and \$US so the effects of exchange rate differentials can be determined. The Westpac-NFF Commodity Index benefits all levels of Australian agribusiness by providing a relevant and timely indicator of commodity price movements.

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