

Westpac-NFF

# Commodity Index

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

August 2008

## Analysis: limited global impact on domestic grocery prices

Recent analysis by the Australian Competition and Consumer Commission (ACCC) into grocery prices has highlighted that, despite there being a strong link between farm gate and world prices for tradable food products, the relationship between international food prices and domestic retail prices is limited.

The *Westpac-NFF Commodity Index* has highlighted the rise in global agricultural prices in recent years, particularly within the grain, oilseeds and dairy sectors.

The ACCC analysis notes that these commodity groups make up less than 20% of Australian food consumption.

Therefore, while the report notes that small, open economies such as Australia are more likely to be influenced by international price trends, this relationship can be difficult to identify when Australian retail prices are concerned.

Compounding this is the fact that the farm gate component generally makes up a very small part (between 5% and 40%) of the end retail price.

The August 2008 *Westpac-NFF Commodity Index* showed some moderation in July, with a 1.5% fall.

The index is now 7 per cent higher than last year's levels. Commodities experiencing

decreases were wheat (-4.5 per cent), dairy (-3.9 per cent), canola (-2.6 per cent), wool (-2.2 per cent) and cotton (-1.9 per cent).

This more than offsets rises in sugar (16.4 per cent), beef (4.2 per cent) and barley (2.2 per cent).

brought about an increase in production for Argentina and China.

### Beef

This month, Russia became Australia's second largest beef export location, overtaking the United States (US), Korea and

**“Compounding this, the farm gate component generally makes up a very small part of the end retail price.”**

- Andrew Hanlan  
Senior Agribusiness Economist, Westpac

### Barley

The amazing growth in the international market for barley eased this month in light of large supplies coming from the Black Sea and to a lesser degree Europe.

Yields have been good in Europe but most of that production will go towards meeting domestic demand. Large Black Sea and European Union supplies are therefore not expected to make a significant dent in long term global demand.

Improved weather conditions this month also

the European Union (EU).

This was due to strong consumer demand, low domestic production, a sharp fall in subsidized beef exports from the EU and higher disposable Russian income.

Beef exports to the US fell this month to their lowest volume in 10 years, reflecting the weaker US dollar. The EU is set to allow imported beef from Argentina, Brazil and Paraguay as they are now in a position to comply with EU quarantine regulations.

Despite Japanese buyers trying to source beef for the



Table 1. Component Indices.

Australian \$	Index				Percentage change over		
	Jul-08	Jun-08	Jan-08	Jul-07	1 month	6 months	12 months
Wheat (AU c/bu)	867	907	1024	718	-4.5	-15.4	20.7
Barley (AUD/t)	267	262	243	197	2.2	10.1	35.6
Canola (AU c/kg)	666	684	630	441	-2.6	5.8	51.1
Cotton (AU c/lb)	76.2	77.7	80.5	74.5	-1.9	-5.4	2.3
Sugar (AU c/lb)	14.8	12.7	13.6	11.7	16.4	8.8	26.3
Export beef index (AUD)	158	152	160	144	4.2	-1.2	10.3
Dairy price index (AUD)	153	159	180	200	-3.9	-14.8	-23.5
Wool (AU c/kg)	844	863	1067	925	-2.2	-20.9	-8.7
USD Index 97/98 = 100	198	198	196	166	-0.4	0.9	18.7
AUD/USD	0.962	0.952	0.882	0.868	1.1	9.1	10.9
AUD Index 97/98 = 100	140	142	151	131	-1.5	-7.5	7.0

a) The indexes are calculated as monthly averages

b) Data sources are Bloomberg, USDA FAS.

Japanese summer holiday season (late July to the end of August) leading to higher prices, Australian exports to Japan remain depressed due consumers turning to lower end beef products.

Prices for beef in South Korea plummeted as US beef re-enters South Korea.

### Canola

Consistent rain in Australia has boosted the hopes of growers for a larger than expected canola crop this season and global prices eased 2.6% as a result.

Harvests have begun in China and the Ukraine, with the latter expecting large yields which are expected to offset what is anticipated to be a disappointing European Union crop.

The demand for biodiesel will determine how much of Ukraine's surplus will be distributed to Europe.

### Cotton

Cotton plantings for the US are the smallest seen in 24 years, due to poor weather conditions and the pressure to move to grain crops for higher profits.

China's planting is almost complete, with crops reportedly progressing well, although severe storms in northern China have affected some areas.

Production will be down

in India due to the late arrival of the monsoon and the adoption of alternative crops that are less water dependant.

Central Asia (Uzbekistan, Tajikistan, and Kazakhstan) is suffering a heat wave, and lack of irrigation water is affecting plants maturity resulting in poor production and quality.

Rain in central Africa (Chad, Ivory Coast, Burkina Faso and the Central African Republic) has improved crop development in that region.

### Dairy

World inventories for milk and milk products remain at historical lows, while demand remains strong, particularly from Asia and the Middle East.

Production has increased in the EU and US to try and meet global demand and prices eased by 3.9% during the month as a result. EU dairy farmers were boosted this month by a subsidies program funded by the European Commission that provides free milk to EU schools.

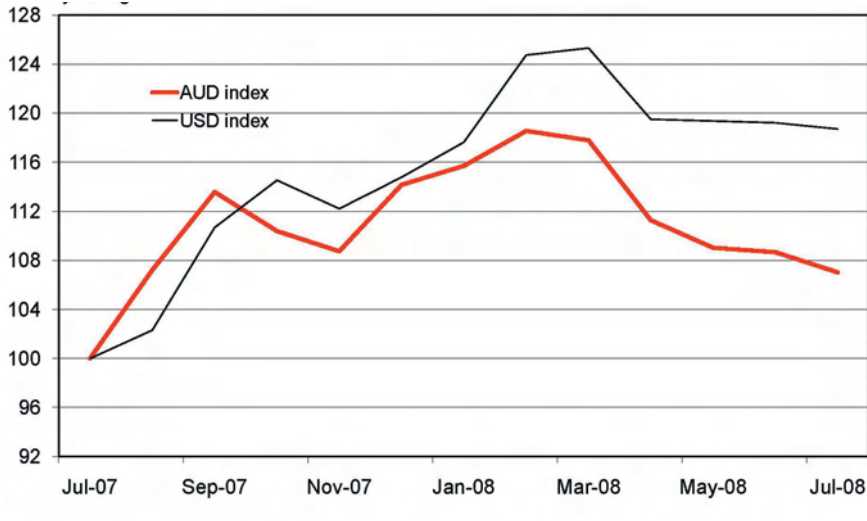
The program has been extended to include cheeses, yoghurt, buttermilk and other dairy products in a hope to get more schools involved.

### Sugar

Sugar prices lifted an amazing 16.4% during July, with Brazil in the middle of harvesting, and much of that production expected to be directed towards ethanol (62%).



Sweet dreams are made of this... Australian sugar cane growers received a major boost as the world market soared over 16% for the month of July 2008.

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

Greece's largest sugar producer is also looking to convert production to ethanol on the back of cuts to sugar subsidies in the EU, but cheap imports from Brazil look to make it unrealistic.

There is growing pressure for the US to lift its tariff on imported fuel ethanol to ease grain prices for animal feed and ingredients. US buyers currently account for less than 10% of Brazil's ethanol consumption.

### Wheat

Wheat saw declining prices this month due, primarily, to more favorable weather conditions in Australia which have meant crops are in better condition than this time last year.

Harvest is underway in the US and the EU and both expect good production volume.

Russian and Ukraine crops

are also progressing well and are in excellent condition.

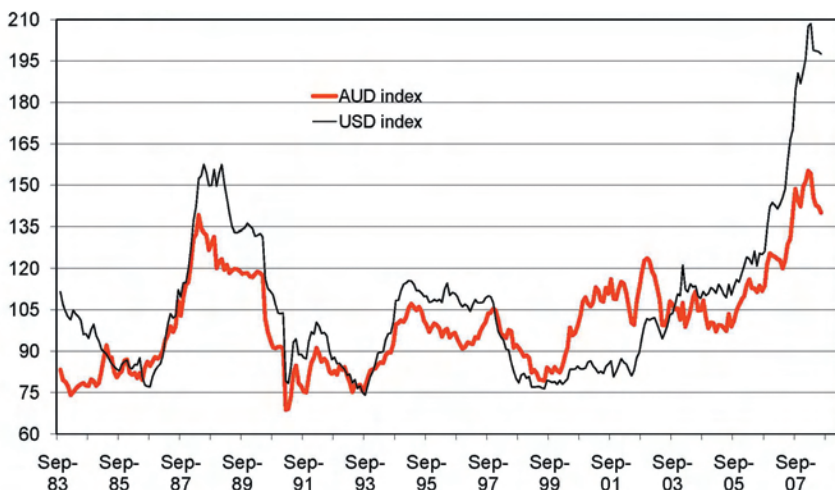
The Indian wheat harvest is mostly complete with higher production than recent years (due mostly to increased plantings).

Yet, in Argentina, wheat area planted is expected to be down 12-16% from last year's production due to drought and the Government export ban.

### Wool

Easing demand for wool was due to many Chinese mills waiting for price falls before committing to sales, and European buyers being on holidays.

Wool is expecting a boost. Synthetic cost hikes due to oil prices, and US cotton become more expensive, due to crop conversion. In Australia, too, farmers are abandoning sheep for more lucrative grain crops.#

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

Westpac-NFF

## Commodity Index

### Editor

Brett Heffernan

### Economists

Andrew Hanlan (Westpac)

Charlie McElhone (NFF)

The Westpac-NFF Commodity Index is published monthly as a joint undertaking between the Westpac Banking Corporation (ABN 33 007 457 141) and the National Farmers' Federation (ABN 77 097 140 166).

Westpac Banking Corporation Head Office:  
275 Kent St, Sydney NSW 2000.  
[T] 02 9293 9270, [F] 02 8253 4128,  
[W] www.westpac.com.au.

National Farmers' Federation Head Office:  
NFF House, 14-16 Brisbane Ave, Barton ACT  
2600. PO Box E10, Kingston ACT 2604.  
[T] 02 6273 3855, [F] 02 6273 2331,  
[E] nff@nff.org.au; [W] www.nff.org.au.

Material in the Westpac-NFF Commodity Index is protected under the Commonwealth Copyright Act 1968. No material may be reproduced in part, or in whole, without the written consent from the copyright holders (NFF).

The Westpac-NFF Commodity Index is weighted according to the value of Australian rural commodity exports only, dating back to June 1983. Therefore, unlike other commodity indices, rural export prices are not overshadowed by oil, mineral and energy prices.

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.

Westpac Banking Corporation and the National Farmers' Federation have taken all reasonable care to ensure the materials are correct and complete. However, since they are not the primary sources of the materials, they can give no warranty in relation thereto and disclaim liability for all claims against them, their employees, agents or any other person, which may arise from anyone acting or relying on the materials.

For more information, enquiries should be directed to either:

Jane Counsel  
Westpac Media  
Westpac Banking Corporation  
(02) 8253 3443

or

Brett Heffernan  
General Manager - Public Affairs  
National Farmers' Federation  
(02) 6273 3855.