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Your quick guide to

Agricultural Swap Contracts

What is a Swap?

A Swap lets you exchange, or swap, a floating price for a fixed price for a specified commodity at an agreed future date. This gives you the security of a fixed commodity reference price, which lets you budget and plan with more certainty. Swaps are especially useful for primary producers looking to protect their revenue against declining commodity prices.

Why Westpac Agribusiness?

- Enjoy the support and guidance of dedicated local agribusiness bankers who get to know your business and the challenges you face.
- Get access to agribusiness products and solutions tailored for your needs.
- As Australia's first bank, we've backed the agribusiness sector for almost 200 years – weathering floods, droughts and recessions together with our customers.

Benefits

Price protection[1]
You receive a guaranteed price for a pre-agreed quantity of a commodity on an agreed future date.

Flexibility
You choose the quantity of the commodity you want to cover, the timeframe and the price protection level that best suits your situation.

Simplicity
You can make swap transactions in Australian or US dollars. By choosing Australian dollars, you eliminate the need to hedge the associated foreign currency exposures.

Risks

- You can't take advantage of favourable price movements during the period of the contract.
- If you terminate the contract early there may be a cost to you.
- You're not covered for total risk, so you still carry 'basis risk' (see overleaf for details).

Quick facts

Costs	There are no direct fees associated with a Swap Contract.
Minimum Transaction Amount	Wheat – 100 metric tonnes Canola – 20 metric tonnes Sugar – 50 metric tonnes (smaller amounts and other commodities may be available on request).
Term	1 week to 3 years (longer terms may be available on request).
Settlement	A Swap Contract is cash settled at maturity. On the Settlement Date, which must be agreed upfront, amounts owing or due must be paid. Once the Settlement Date is agreed it cannot be varied. No physical delivery of the underlying commodity occurs.
Early Termination	You can terminate a Swap Contract early, but there may be a cost to you if you do.

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Case study

Commodity Producer (Seller of Wheat – USD Swap)

You're a wheat producer looking for protection from falling wheat prices in November, and you decide to hedge the price on 250 metric tonnes of wheat for this period. You decide to only protect the USD value of your production, choosing to manage your AUD/USD exchange rate risk separately.

Without a Swap Contract

If you do nothing, the amount of USD you'll receive in November when you sell your wheat will depend on the market price for wheat at the time as specified in your sales contract.

If the wheat price falls you'll receive less USD when you sell your wheat in the physical market. Alternatively, if the wheat price rises you'll receive more USD when you sell your wheat.

With a Swap Contract

You enter into a Swap Contract with a notional volume of 250 metric tonnes and a maturity date of 28 November, and specify the floating reference price to be the December Chicago Board of Trade (CBOT) Wheat Futures contract. Based on these details Westpac determines the fixed Swap Price to be USD 200 per tonne.[2]

There are two possible scenarios on the maturity date of 28 November:

(a) If the floating reference price is less than the USD 200 per tonne fixed Swap Price, Westpac will pay you the difference in USD on the Settlement Date (30 November). This amount will compensate you for the lower price you'll receive when you sell your physical wheat.

(b) If the floating reference price is greater than the USD 200 per tonne fixed swap price, you will pay Westpac the difference in USD on the Settlement Date (30 November). This amount will be offset by the higher price you receive when you sell your physical wheat.

By entering into a Swap Contract you've removed the uncertainty of commodity price fluctuations between now and November. Provided you can sell your physical wheat at the floating reference price, you've effectively fixed the sale price of your wheat at the fixed swap price of the Swap Contract.

What isn't covered with a Swap Contract?

You need to remember that the price you receive under the contract for the physical sale of your wheat may not be an exact reflection of the floating reference price under your Swap Contract. This could occur, for example, because the price that you receive for the physical sale of your wheat takes into account matters such as transport costs, the quality of the wheat and other factors.

These fluctuations in the price that you receive are referred to as the 'basis risk' and are not covered by a Swap Contract. Any adverse slippage between the price you receive in the physical market and the floating reference price effectively reduces the fixed price you actually achieve.

This example is indicative only and uses rates and figures that we have selected to demonstrate how the product works. In order to assess the merits of any particular Swap Contract, you would need to use the actual rates and figures quoted to you at the time.

For more information, speak with your local Westpac Agribusiness Banker or call 1300 134 979.

Things you should know: 1. Provided there is no basis risk between the underlying price you achieve in the physical market and the floating reference price. 2. The scenarios and prices are indicative only. Westpac Banking Corporation (ABN 33 007 457 141 AFSL 233714) is the issuer of the Agricultural Swap Contract. You can obtain a copy of the Product Disclosure Statement (PDS), or contact Westpac, by calling your local Westpac Agribusiness Banker or visiting westpac.com.au/agribusiness. You should consider the PDS before making any decisions about the product. You can also obtain a Financial Services Guide (FSG) by calling 132 032 or visiting westpac.com.au. This information has been prepared without taking into account your objectives, financial situation or needs. Because of this you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation and needs. Information current as at 30 January 2010.

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