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Macroeconomic and geopolitical risks play on Australian agri markets in 2012 – Rabobank

Heightened macroeconomic and geopolitical risks are likely to exert a strong influence on the food and agribusiness sector in 2012 resulting in considerable uncertainty in agricultural markets, according to a new report released by Rabobank.

In its keynote annual report **Australian Agriculture in Focus 2012**, Rabobank says that given the elevated level of uncertainty associated with the general global economic outlook, the world's financial, industrial and agricultural markets have all begun to exhibit greater risk aversion, price volatility and a deterioration in demand.

Rabobank general manager for the bank's Food and Agribusiness Research & Advisory division Luke Chandler says there is a real trend developing that shows a closer alignment between the agri commodity complex and the global macroeconomy where the drivers of global economic conditions and financial markets are increasingly influencing global trade in agriculture.

"We're seeing this relationship develop in terms of real demand – the scale and distribution of global growth which flows through to real incomes and impacts the demand for agri commodities," Mr Chandler says.

"This trend is also apparent in investor activity where market speculators shift funds into and out of agri commodities in keeping with broader risk sentiment, therefore influencing agri commodity price movements."

In addition, Mr Chandler says: "Geopolitical factors are also becoming a greater challenge for those operating in global agricultural markets which are being increasingly politicised, impacting international agricultural trade, contributing to heightened uncertainty and price volatility".

The Rabobank report forecasts a slow year for the global economy dictated by uncertainty over exactly when and how the Eurozone sovereign debt crisis will be resolved.

'Soft Landing'

Rabobank expects that agri commodity markets will face a "soft landing" in 2012 after prices for many commodities hit record levels in early 2011. While the outlook for the global economy has soured, growth in the emerging economies remains supportive of demand, and supply remains tight for many agri commodities with global inventories resting at modest levels.

Mr Chandler says prices in 2012 are expected to mostly remain above their average levels set over the past decade, but exhibit heightened volatility due to delicately posed



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global inventories and financial market instability arising from uncertainty surrounding global economic growth.

Australia in focus

Despite the generally positive outlook for prices, the year ahead is expected to present a unique set of issues affecting the competitiveness for those operating in Australia's food and agribusiness sector, Mr Chandler says.

"A historically high dollar will continue to challenge export competitiveness and earnings, while the risk of further downward revisions to global growth cannot be ruled out," he says.

"The slim yet real prospect of a third consecutive La Nina weather pattern re-emerging this year and preventing a return to more normal weather conditions is also at play here.

"The introduction of a carbon price into the Australian economy, the finalisation of the Murray-Darling Basin Plan, and the increasing crossover of mining and energy producers into Australian agricultural communities are also key factors of focus for farmers."

On the balance, Mr Chandler says Rabobank sees a positive year ahead for Australia's food agribusiness sector.

"In the background, an ongoing shift in the organisation of food and agribusiness supply chains is taking place, with downstream companies looking to increase control over agri commodity supply, and in the process, better manage their price risk," he says.

"These developments could offer both opportunities and risks to Australian producers who remain key suppliers of products to global markets."

Sector summaries

Looking at the main agricultural sectors, the Rabobank **Australian Agriculture in Focus** report found:

Grains -

- Grain markets will remain uncertain until the northern hemisphere crop emerges from its winter dormancy.
- Wheat markets are likely to trade sideways in the Q1-Q3 period.
- Domestic wheat values will have difficulty rallying given ample global supply and the low quality of wheat produced.



Beef -

- Australian cattle prices are expected to rise modestly in 2012.
- Global beef production is expected to fall, largely due to a major decline in the United States herd.
- Any easing in the Australian dollar will support finished cattle prices.

Sheepmeat -

- Sheep and lamb prices are likely to decline in 2012 yet remain elevated assuming there is not a return to drought conditions.
- Australian supply will increase, as will production in New Zealand, Australia's main competitor in export markets.

Wool -

- Macroeconomic uncertainty in the main wool-consuming countries poses a downside risk for the Australian wool market risk this year.
- Prices are expected to find support above five-year averages.

Dairy -

- Fundamentals across the global market should continue to support high farmgate prices. The outlook is positive for producers' profitability; also being helped by a good supply of inexpensive feed, high water allocation and pasture growth.
- For farmers in the fresh milk sector the outlook remains subdued. Ongoing retailer discounting of fresh milk and a need to balance local market requirements is weighing on price signals and overall sentiment.

Sugar -

- Rabobank expects sugar prices to remain firm in 2012, at an average of USD 23.5c/lb or AUD 510/tonne.
- The Australian industry is poised for a recovery this year, following strong cane plantings in 2011.

Cotton -

- The global macroeconomic slowdown continues to pressure cotton prices, adding to the complexity and uncertainty faced by growers.
- Rabobank forecasts Australian cotton production to reach 4.73 million bales in 2011/12.

Food retail -

- Global economic uncertainty and a bifurcated household economy are having a defining influence on the Australian food retail sector.
- Grocery retail dynamics are driving suppliers to refocus on product positioning and cost rationalisation.
- Harnessing advances in information technology will increasingly become a determinant of success as a retailer or supplier.



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Wine -

- Tighter supply fundamentals are encouraging and the market for significant increases in production will remain soft in 2012.

Farm inputs -

- A boost in demand for farm inputs underpinned prices throughout 2011 and will continue to do so throughout 2012.
- Future price direction will be driven largely by the Chinese government's export policy and seasonal demand conditions in key regions.

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Rabobank Australia & New Zealand is a part of the international Rabobank Group, the world's leading specialist in food and agribusiness banking. Rabobank has more than 110 years' experience providing customised banking and finance solutions to businesses involved in all aspects of food and agribusiness. Rabobank is structured as a cooperative and operates in 48 countries, servicing the needs of more than nine million clients worldwide through a network of more than 1600 offices and branches. Rabobank Australia & New Zealand is one of Australasia's leading rural lenders and a significant provider of business and corporate banking and financial services to the region's food and agribusiness sector. The bank has 93 branches throughout Australia and New Zealand.

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