

POTS
2nd INTERNATIONAL PALM OIL
TRADE FAIR &
SEMINAR *2008*

Changing Marketing Landscape - Challenges for Business Sustainability

24 - 26 August 2008

**TARGETTING OPPORTUNITIES & MANAGING
CHANGES IN THE COMMODITIES MARKETS**

John C. Baize

John C. Baize and Associates, USA

PLENARY SESSION

Targetting Opportunities & Managing Changes in the Commodities Markets

John Baize
John C. Baize and Associates

Email: jbaize@attglobal.net

Abstract

The last two years have seen the most profound changes in global commodity markets in modern history. Driven by explosive energy process and increased global demand for better diets, particularly in Asia, the prices of vegetable oils, oilseeds, wheat, corn, and rice have reached record levels. Ocean shipping rates also have reached record levels because of the same forces. High petroleum prices and concerns about global warming also have created a new market for the world's vegetable oil producers in the form of biodiesel. No longer is food demand the main driver of vegetable oil demand. Now the food market must compete with the biodiesel sector which has the capacity to use a much larger share of vegetable oil supplies than it currently is consuming. However, the use of vegetable oil for fuel also has led to major concerns about the world running short of food, pricing the poor out of the market, and accelerating the destruction of tropical forests. The challenge for commodity producers, traders, processors, and consumers is how to profitably navigate the new and evolving marketplace while managing risks and avoiding political minefields. Companies will have to find the right mix of the aggressiveness to capitalize on new markets and the caution to avoid chasing markets that may disappear overnight.

Targeting Opportunities & Managing Changes in the Commodities Markets

John C. Baize
John C. Baize and Associates

Global Markets Changing Faster Than Ever

- Rapid globalization and information flows
- Increased containerized shipment of agricultural commodities
- Emergence of new producers and producing countries
- Increased government regulations pertaining to quality, safety, and country-of-origin labeling
- More market segmentation
- Increased influences by NGOs

World Market of The Past

- Relatively stable commodity prices
- Domination of production, marketing, and processing by established industry participants
- Low and relatively stable ocean freight rates
- Relatively slow technological change

World Market of The Past

- Energy prices had minimal impact on agricultural commodity prices and demand
- Little interest in agricultural markets by investment banks, speculative funds, and others
- Relatively few consumer demands
- Relatively few societal demands
- Few market segments

Today's Global Market

- Energy prices driving commodity prices and shipping rates
- Rapid development of new biotech crops focused on improved agronomics as well as consumer traits
- Major investments in agriculture, food, and biofuel sectors by non-traditional investors and by speculative funds
- Greater price volatility
- Greater interference of governments in exports

Today's Global Market

- Growing demand by governments for “sustainable” food and bio-energy supplies
- Growing demand by consumers for foods that meet perceived social objectives (e.g. animal welfare, labor rights, protection of rainforests, less or no pesticides, fair trade, non-biotech, carbon-neutral, less “food miles”, etc.)
- Greater power by large retailers to control food product standards
- Tightened food safety standards

What palm oil industry and hungry people see



What environmentalists see



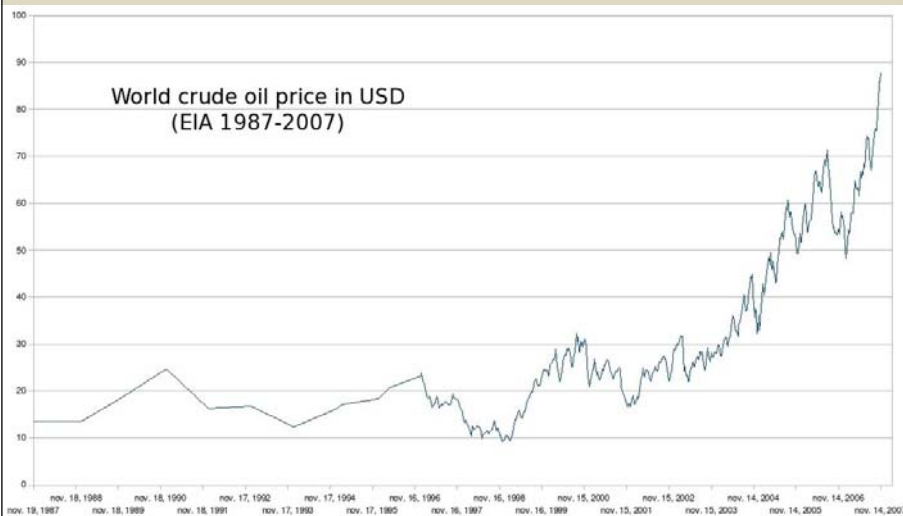
Among the Things Environmental and Animal Rights Groups want to Protect



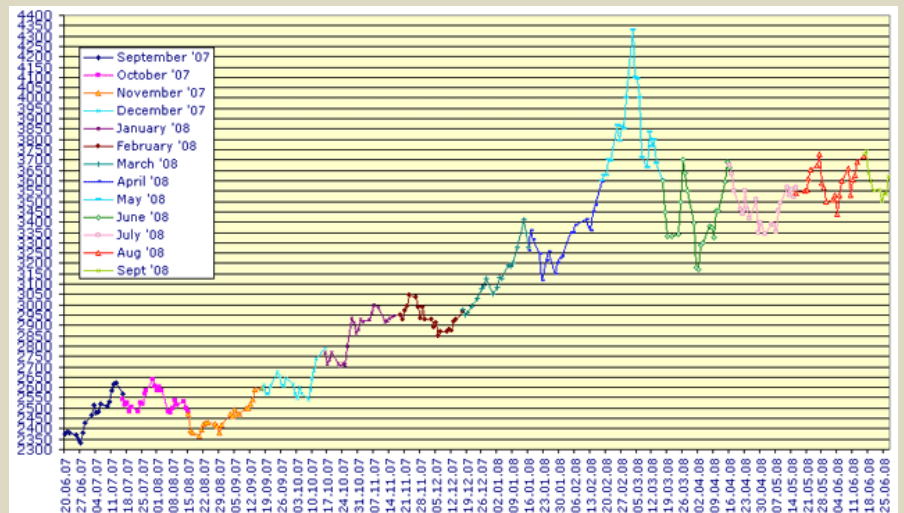
Non-Governmental Organizations Have Increasing Impact on Markets Require Counter Efforts by Producers



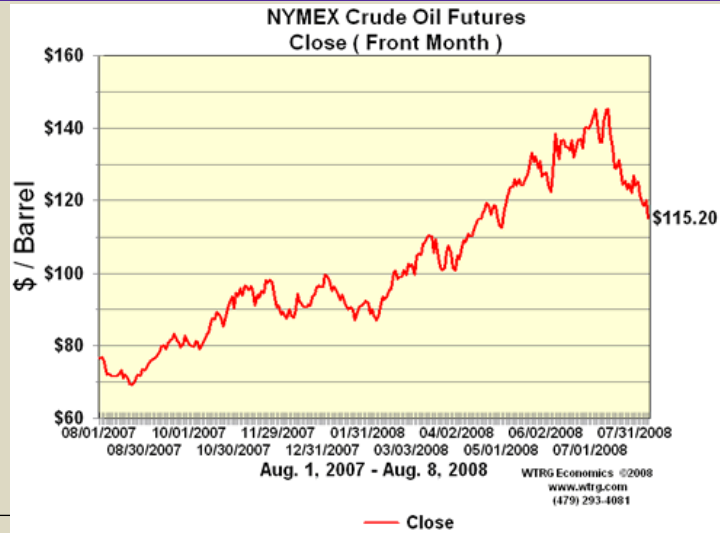
Relatively Stable Petroleum Price 1987 - 2004 and Then Increases Began



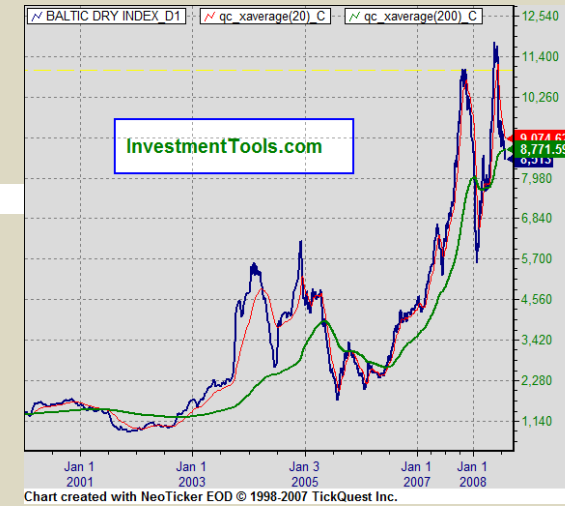
Volatile Crude Palm Oil Futures Price



Oil Prices Exploded and Retreated in 2008



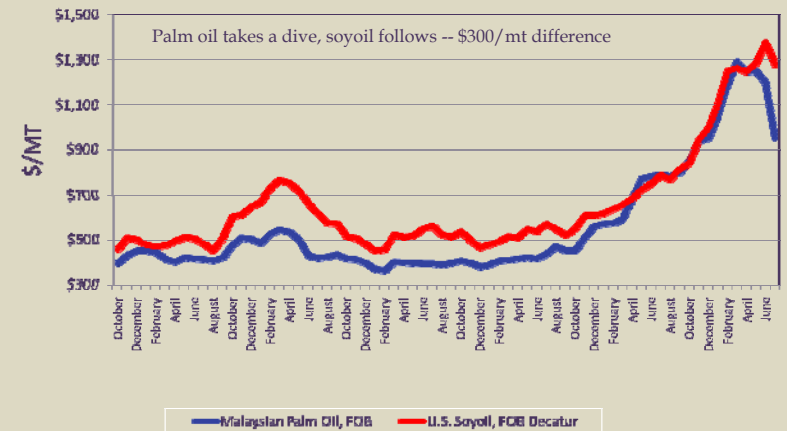
Major Surge in Ocean Freight Rates



Impact of Changing Petroleum Values On Energy Value of Agricultural Commodities

Crude Oil (\$/Barrel)	\$80	\$100	\$120	\$140	\$160
Corn (\$/MT)	\$211.98	\$264.97	\$317.96	\$370.96	\$423.95
Wheat (\$/MT)	\$232.81	\$291.01	\$349.21	\$407.41	\$465.61
Soybeans (\$/MT)	\$220.13	\$275.16	\$330.19	\$385.22	\$440.25
Vegoil (\$/MT)	\$527.08	\$658.85	\$790.62	\$922.38	\$1,054.15

Prices of U.S. Soyoil and Malaysian Palm Oil October 2002 – July 2008



Clearing Land in the Amazon for Soybeans



High Commodity Prices Have Created Wealth But Will Bring Major Challenges

- High commodity prices in last 2 years have brought great profits to agriculture
- They also have brought strong demand and very high prices for fertilizer and agrichemicals
- Major new investments in agricultural production will bring burdensome supplies and lower prices
- Land prices have greatly increased
- High food prices have lessened public and government support for agriculture
- Agriculture faces much higher risk in the future

Navigating the Minefields of Public Perception

- Until recent years agriculture was generally admired by the public and strongly supported by governments
- Now the situation is much different
- Many groups and governments now see agriculture as being destructive of wildlife and the environment, cruel to animals, and damaging to endemic populations
- Agriculture is seen as overusing pesticides and artificial fertilizers
- No longer does the public see agriculture as small farmers, but as large agribusinesses
- Even biofuels once advocated by environment groups are now seen as a contributor to global warming and climate change.

Navigating the Minefields of Public Perception

- In the current environment products like palm oil or palm biodiesel may have a market one year, but be fenced out of key wealthy markets by government regulations or public boycotts in a short period of time.
- A good example is the EU's sustainability standards for biofuels which would exclude biodiesel from newly-cleared land
- To prevent this from happening companies and industry associations must seek to mollify opponents by developing sustainability and other standards which are acceptable to consumers and governments
- Sitting on the sidelines and doing nothing is not an alternative

Navigating the Minefields of Public Perception

- The establishment and the enforced preservation of large tropical forest and wildlife reserves will be a necessity in the future
- Companies and industries will have to establish and enforce stronger worker rights
- The rights of endemic populations will have to be protected.
- Greater care will have to be given to the application of pesticides and fertilizers
- More research will have to be funded to improve the environmental protection by agricultural sectors
- Public education campaigns will need to be financed to show the positive side of agricultural industries.

Greater Risks Which Are Hard to Mitigate

- High price volatility has brought in speculators who have driven up price.
- Hedgers using futures to mitigate risks are impacted by high margin calls
- Options become very expensive
- Banks and other lenders are sometimes unwilling to loan money to cover margin calls.
- Buyers may renege on contracts if prices fall sharply

The Threat of Inflation and High Borrowing Costs

- High energy prices have driven up costs of food, transportation, and almost all other traded items.
- Higher prices have rationed demand, particularly in developing countries
- Lower demand occurring as supplies are growing in response to higher production profits
- High prices brings inflation which governments attempt to constrain with higher interest rates and tighter credit
- The result is higher borrowing costs

Substantial Global Political Risk

- What would be the fallout of attacks on Iran's nuclear facilities?
- What if Iran's current government falls because of revolution and is replaced by pro-western government?
- Will some government's fall because of high food prices?
- What if India and China or Pakistan get into armed conflict?
- What would be the impact of another Arab war with Israel?
- What if there is a revolution in Saudi Arabia?

Impact of Changing Exchange Rates

- Global prices have benefitted greatly from decline in U.S. dollar from \$1.20 Euros to only \$0.63 Euros
- Brazilian soybean production has been greatly limited by increase in value of Brazilian real versus dollar
- U.S. dollar's value likely to strengthen substantially over next 2 years. Rising dollar value will bring lower dollar-denominated prices and less U.S. agricultural competitiveness
- Will Malaysian ringgit's value increase versus dollar?

Impact of Demographic Changes

- Population growth is the slowest in rich, developed countries and fastest in poor, underdeveloped countries.
- This may bring slowing demand
- Greater imports by poorer countries increases risks of defaults, slow payments, vulnerable demand in difficult economic periods
- Very important to know your foreign buyers and their financial soundness

Population of Major Markets 2008 Estimate and Forecast for 2040

Country	2008	2040	Change
China	1,330.0	1,454.6	124.6
India	1,148.0	1,684.3	536.3
Pakistan	172.8	272.0	99.2
Iran	65.9	80.6	14.7
Bangladesh	153.5	250.6	97.1
Egypt	81.7	119.5	37.8
Russia	140.7	116.6	-24.1
Japan	127.3	103.9	-23.4
Australia	21.0	27.7	6.7
USA	303.8	392.2	88.4
Europe	727.0	677.2	-49.8

Source: U.S. Census Department, United Nations

Anticipate the Unexpected

- Now and then a new technology is developed which changes global market place (e.g. internet)
- New types of engines will greatly reduce fuel use
- New scientific findings will change the types of foods we eat (e.g. trans fats, omega 3)
- Biotechnology will change the competitiveness of different crops
- What if soybean and/or rapeseed yields increase by 75% because of biotech breakthrough?

Anticipate the Unexpected

- Odds are a new energy technology will be developed which changes the global energy market. One major possibility is biodiesel from algae. What if cold nuclear fusion is developed?
 - What if there is a global epidemic which kills hundreds of millions of people?
 - The key is to closely watch global events, be aggressive in research, and be prepared as much as possible for major events that may change market, and your companies' future.
-

Questions?

John C. Baize
John C. Baize and Associates
7319 Brad Street
Falls Church, Virginia, USA
Tel: 703-698-5908
Email: jbaize@attglobal.net
