Rabobank

March 2009

Rabobank Soft Commodities Monthly

Wheat, Corn, Soybeans, Palm Oil and Sugar

Rabobank International

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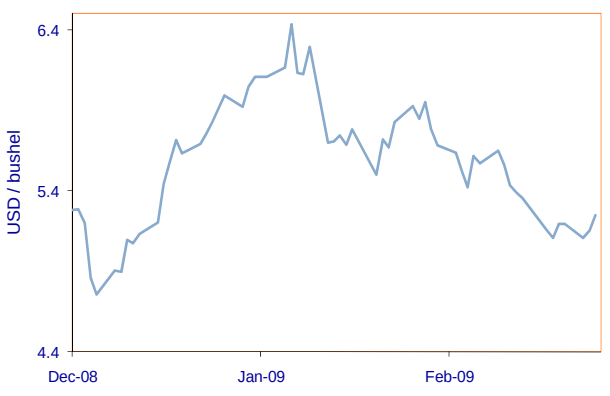
Wheat

- Significantly lower world production in 2009/10
- Early conditions in the US HRW belt and parts of China are dry
- Stock levels forecast to tighten in 2009/10—increasing the potential for weather induced shortages
- Ample supplies of low priced wheat available in BSR

Figure 1: Wheat Prices (CBOT) Dec 2008 – Feb 2009

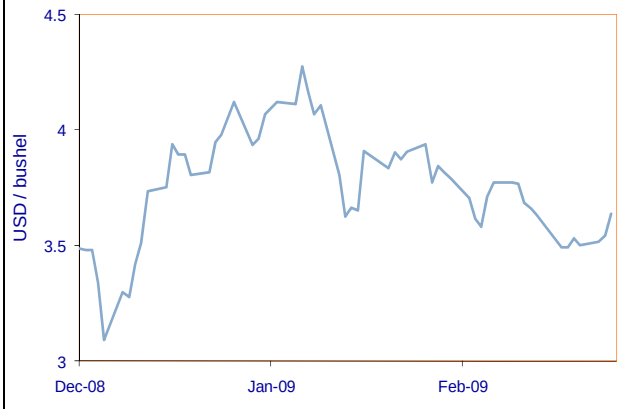


Source: Rabobank, Bloomberg

Corn

- New crop fundamentals—US and world—more supportive for prices
- Slight improvement in ethanol profitability
- Increased US ethanol mandates in 2009/10
- Feed demand sharply lower due to global economic weakness
- Higher carry-in stocks from 2008/09

Figure 3: Corn Prices (CBOT) Dec 2008 – Feb 2009

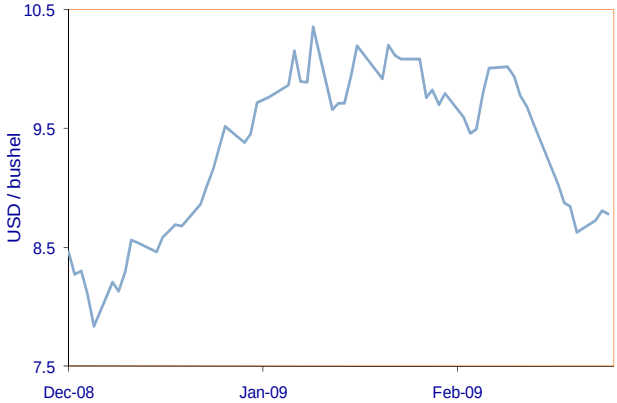


Source: Rabobank, Bloomberg

Soybeans

- South American supply concerns
- US exports remain robust, supported by China
- New crop plantings in US
- Weaker feed demand for soymeal

Figure 2: Soybean Prices (CBOT) Dec 2008 – Feb 2009

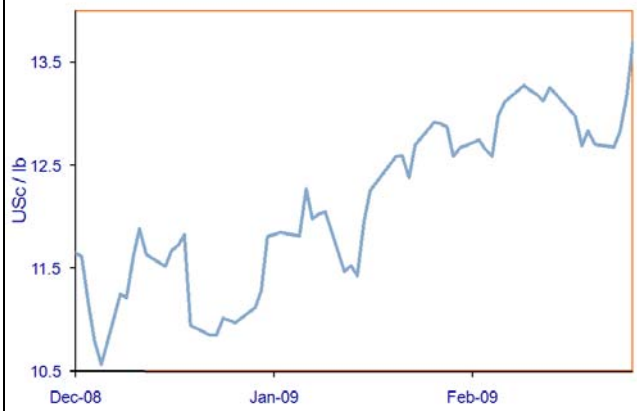


Source: Rabobank, Bloomberg

Sugar

- Deficit of 5 or more million tonnes expected for 2008/09 international crop year
- Downward revision of Indian production
- Low Brazilian ethanol prices

Figure 4: Sugar Prices (ICE - NYBOT) Dec 2008 – Feb 2009



Source: Rabobank, Bloomberg

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Wheat

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Key Market Drivers	
▲	Significantly lower world production in 2009/10
▲	Early conditions in the US HRW belt and parts of China are dry
▲	Stock levels forecast to tighten in 2009/10—increasing the potential for weather induced shortages
▼	Record world wheat production in 2008/09
▼	Ample supplies of low priced wheat available in BSR
▼	Feed demand to weaken in 2009/10 season

Prices

What a difference a year makes. Twelve months ago the global wheat market was in a situation of panic, world wheat prices reached record levels in February 2008 as consumers and governments, concerned about global food shortages, scrambled for supplies.

In February 2009, prices have fallen to their lowest levels in two months and are around 60% lower than year-earlier levels as world stock levels have rebounded to comfortable levels due to record world wheat production. Apart from the drought in Argentina, almost all producing regions experienced idyllic conditions over the past 12 months.

US futures and cash prices continue to trade at a premium to competitor exporter markets such as the Black Sea region (BSR) and the European Union (EU). Despite logistical constraints in both Canada and Australia in recent months, United States (US) exports are significantly lagging year-earlier levels and will need to become more price competitive in coming months in order to reach the United States Department of Agriculture (USDA) forecast estimate of 1 billion bushels for the 2008/09 season.

Figure 5: Wheat Price Forecasts (CBOT)

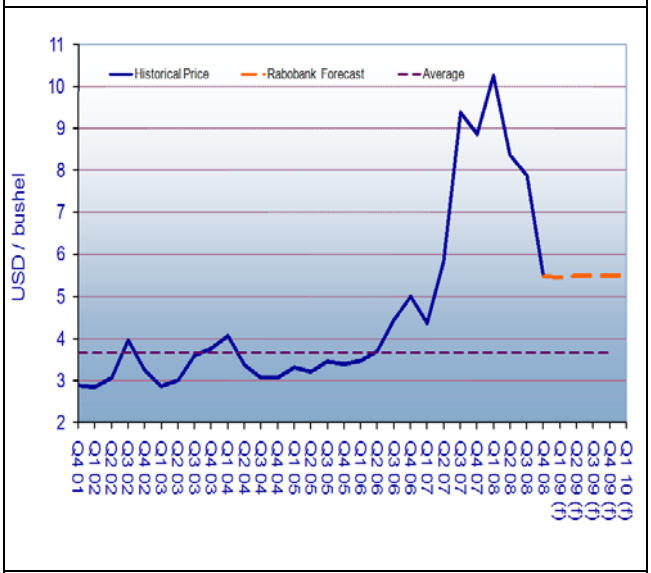
	2008			2009				2010
USD/bu	Q2	Q3	Q4	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
prices	8.4	7.9	5.5	5.5	5.5	5.5	5.5	5.5

*All forecasts are period averages. Source: Rabobank, Bloomberg

US exporters have also been disadvantaged by rising freight costs throughout January and February, the Baltic Dry Index is up over 200% from mid-December—although it remains well below last year's highs. In addition the USD has continued to benefit from the perceived 'flight to safety' and is around 23% higher than mid-2008 levels on an index basis.

US futures prices have continued to ease from early January, and it appears will need to fall further in coming weeks in order to draw additional export business away from the BSR. This may prove difficult if conditions in the central plains region of the US continue to deteriorate in coming weeks. At this early stage, crop conditions and soil moisture levels are at below-average levels, although there remains time to prevent significant production losses.

Figure 6: Wheat Price Quarterly Forecasts (CBOT)
Q4 2001 – Q1 2010



Source: Rabobank, Bloomberg

Likewise, Paris milling-wheat futures have shed almost all their gains from early 2009 and, as of end-February, were back below EUR 140/tonne. Time will tell if this will be enough to increase EU competitiveness and garner increased export business this season. Certainly the threat of the Russian government distributing 6 to 7 million tonnes of intervention stocks will ensure that Black Sea origin prices will remain competitive in March/April.

Rabobank's outlook for global wheat prices remains largely unchanged from our outlook in late 2008. Based on the benign old crop (2008/09 season) fundamental situation and uncertain economic environment, there appears to be limited upside for wheat prices in 2009. That said, the large net short of approximately 35,000 contracts held by hedge funds may provide some upside for CBOT prices, particularly if seasonal conditions in the

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US continue to deteriorate and funds are forced to liquidate these positions.

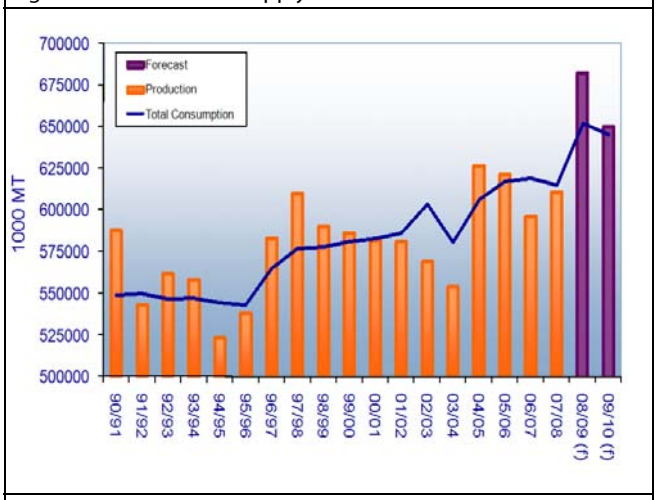
Rabobank expects CBOT nearby wheat prices to continue trading in the USD 5 to 6/bushel range throughout 2009. The upside of this range appears safe unless there is a rapid deterioration in Northern Hemisphere seasonal conditions or a collapse in the USD. Currently the low of this range appears more at risk in mid 2009 given the current weakening demand scenario and absence of any real production issues. Certainly the price records set in 2008 appear safe without a production disaster.

New crop (2009/10 season) fundamental risks that will need to be monitored include dry conditions in the Hard Red Winter (HRW) plains of the US and of China's major producing province, Henan. The risk of winter kill in the BSR will also be monitored closely by the market in March and April.

World Wheat Fundamentals

While it remains early days for new season fundamentals in the wheat market, the carryover of stocks from 2008/09 is expected to provide sufficient cushioning for the market in 2009/10. World wheat production is expected to fall substantially from the record level of 683 million tonnes reached in 2008/09 due to a combination of fewer plantings, reduced fertiliser and chemical applications, and an assumption of normal seasonal conditions. It would be a very unusual occurrence for another season of favourable seasonal conditions in almost all major producing regions of the world. As alluded to earlier, there are already some areas of concern in the Northern Hemisphere at this early stage.

Figure 7: World Wheat Supply and Demand



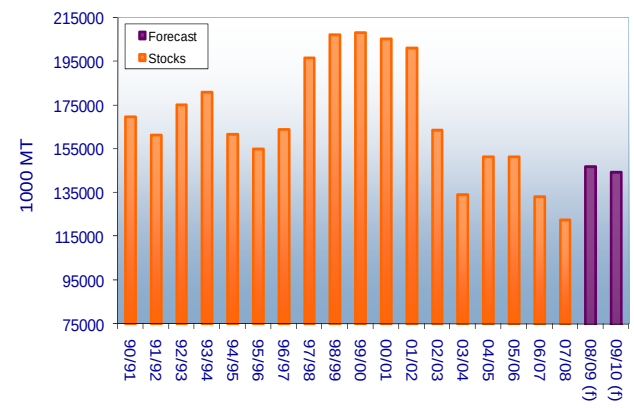
Source: Rabobank, USDA

Rabobank is currently forecasting world production of 640 million tonnes in 2009/10, a 6% decline year-on-year (YOY), but still the second largest production on record.

Consumption of wheat as a feed product is expected to decline in the 2009/10 season. This is based on falling animal numbers and a subsequent slowdown in feed demand largely driven by weak global macroeconomic conditions together with an ample supply situation of coarse feed grains. Depending on the extent of competition from other grains, world wheat consumption may actually fall by as much as 6% in 2009/10, largely offsetting the contraction in world production.

Without a major production issue, world wheat stock levels are expected to remain at comfortable levels in 2009/10, although they are expected to fall by around 3% from year-earlier levels. The world wheat stocks-to-use ratio is expected to fall by 1% to a level of 22%, remaining well above the thirty-year lows reached in 2007/08 of only 19%.

Figure 8: World Wheat Stock Levels



Source: Rabobank, USDA

US

Although beginning stocks were historically low (8.2 million tonnes), higher production and lower exports for 2008/09 are projected to promote an ending stocks recovery to 16.2 million tonnes by year end. US feed and seed usage is reportedly lower than expected, and the total wheat exports are tracking 19% lower to mid-February YOY. US exports have suffered due to a stronger USD and intense competition from the BSR, EU and Canada. As a result, the US stocks-to-use ratio is expected to jump from a historical low of around 13% in 2007/08 to close to 26% in 2008/09.

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New crop 2009/10 dynamics are shaping up completely differently with USDA planting estimates indicating US farmers responded to the sharp price decline in H2 2008 by significantly lowering their area allocation to Winter Wheat. Estimates released by the National Agricultural Statistics Service (NASS) section of the USDA in January suggest a 9% YOY decline in US winter wheat plantings to 42.1 million acres in 2009/10. The bulk of the decline is expected in the soft red winter (SRW) area which is down 26% from last year, with the late row crop harvest and lower prices both contributing to a sharp contraction in SRW area. Planted area for HRW is estimated to be 4% lower with the largest falls in Kansas and Colorado. Production of HRW is also at risk at this early stage of the season with over half the crop in Texas rated poor to very poor.

Despite the expectation of a significant decline in US wheat production in 2009/10, the combination of high carry-in stocks, a sharply lower export pace and a rapidly deteriorating demand scenario, is likely to result in the US wheat supply-demand balance remaining at relatively comfortable levels over the coming year.

EU27

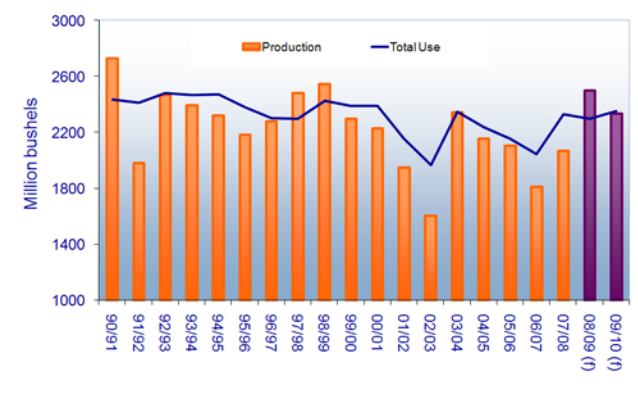
The 2008/09 EU27 wheat balance sheet has a large exportable surplus following a favourable growing season last year. Exports are estimated to increase from 11 million tonnes in 2007/08 to 18 million tonnes in 2008/09, although growers remain reluctant to sell at current price levels which are being pressured from intense competition from BSR origins.

EU milling-wheat price movements of late have largely been in line with US futures price falls since late January. Prices for EU milling-wheat are currently around EUR 140/tonne basis the nearby Euronext Paris contract.

The EU27 wheat production in 2009/10 is expected to be 5% below the record level of 140 million tonnes in 2008/09. The main reason for the reduction is a decrease in yields after last year's good harvest in several member states and a reduction in planted area.

The EU27 demand for wheat in 2009/10 is expected to be around the 2008/09 level. The increasing demand for ethanol will be offset by a decline in demand for feed wheat by the animal feed industry. The latter is facing stable livestock numbers and has more alternative feedstuffs available, like co-products from the biofuel industry. As the carryover stock will be substantial, the EU27 appears likely to also have a large export potential in 2009/10.

Figure 9: US Production and Total Use



Source: Rabobank, Bloomberg

Canada

Large production increases, low carry-in stocks and strong demand set the stage for lower prices but strong exports for Canadian wheat in 2008/09. In January, the Canadian Wheat Board (CWB) posted a Pool Return Outlook (PRO) 30% lower than 2007/08 for durum and 17% lower for nondurum. Total wheat ending stocks are expected to improve slightly from the beginning of 2007/08, but, with lower prices overall, a slowdown in production may be expected going forward.

The CWB announced an export target for 2008/09 of 16 million tonnes, up 1.4 million tonnes from last year. The high quality crop and benefits of increased rail and lake freight capacity are expected to offset exchange rate volatility and competition from a record global crop. Food and industrial use in 2008/09 is forecast higher by over 10% at 3.6 million tonnes, and feed use is forecast to double in 2008/09 from the previous year.

Large production increases in both durum (+50% YOY) and nondurum wheat (+41% YOY) are partially off-set by low carry-in stocks. Total durum supply is +29% YOY and nondurum wheat is +23% YOY, but total wheat supplies are still 4% lower than two years earlier in 2006/07.

The Canadian dollar has fluctuated dramatically this past year, but capacity on rail and barge has been helpful to grain exports.

Black Sea Region

Wheat production reached historic highs in 2008/09, especially in the Ukraine and Russia. Russian production reached a level of 63 million tonnes (nearly 28% higher compared to last year), and Ukraine produced nearly 26

million tonnes in 2008/09. This was more than 83% higher than 2007/08.

With a total production of 12.5 million tonnes, the wheat crop in Kazakhstan was nearly 25% lower due to unfavourable weather circumstances.

Wheat exports out of the BSR have been running at record pace so far in the 2008/09 season. Milling-wheat price levels in the main BSR ports (Russian and Ukrainian origin) are currently around the USD 170 to 180/tonne range, due to the devaluation of the Russian rouble versus the US dollar and the effect of supportive pricing through the Russian intervention programme.

Ending stocks for 2008/09 in the BSR are expected to be substantially higher than the last crop year. Looking ahead, the combination of a large carry-in stock, weaker prices and a less favourable environment to finance farm inputs is expected to result in lower wheat production. Rabobank expects Black Sea wheat production may fall as much as 10% to 15% in 2009/10 due to a combination of lower plantings and reduced fertiliser rates limiting yield potential.

Australia

Australia's wheat production estimate for the 2008/09 season was increased to 21.4 million tonnes in mid-February by the Australian Bureau of Resource Economics (ABARE), the Australian government's official forecaster. This was a 64% increase on the 2007/08 season due to record plantings and a recovery from drought conditions in a number of cropping regions. That said, conditions throughout Australia in H2 2008 were far from ideal, with dry conditions persisting in the southern parts of the wheat belt and heavy rain at harvest in Northern New South Wales resulting in quality downgrades.

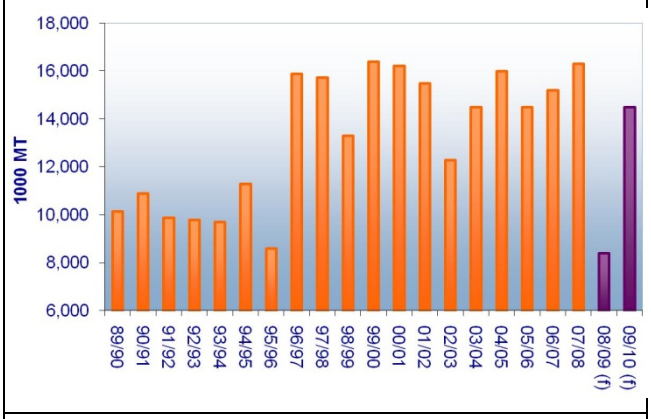
Export pace has been relatively slow in the first year of deregulation for bulk wheat exports, following the abandonment of the Australian Wheat Board (AWB) monopoly. Growers have been cautious to sell into a declining market and rail and port logistical capacity has been challenged. Australian wheat exports for 2008/09 are expected to reach 12.5 million tonnes, just below the five-year average.

Argentina

Argentina's wheat production is estimated to have fallen by as much as 48% in 2008/09. In February, the USDA lowered their Argentinean wheat production estimate for 2008/09 to 8.4 million tonnes, in contrast to 16.3 million last year. Given a relatively stable local consumption level of 4 to 5 million tonnes, it is likely that exports will be limited to 3 to 4 million tonnes, substantially below the 11.2 million tonnes that were exported last year. The dramatic reduction in wheat production this year is the result of both lower area planted and reduced yields due to unseasonal dry conditions.

Total planted wheat area this season was 4.5 million hectares (ha), a 20% reduction from the 5.9 million ha planted during the 2007/08 crop year and the lowest planted area in more than 30 years. The major reasons for the sharp drop in wheat planting were the drought that affected the main growing areas at planting time, the sharp increases in input costs and government interventions in the sector which acted as a disincentive for local producers.

Figure 10: Argentina Wheat Production



Source: Rabobank, USDA

Over 90% of the wheat has been harvested and average yields were disappointing at 1.8 tonne/ha, 30% lower than last year. Parts of the main growing areas in the province of Santa Fe had yields as low as 1.6 tonne/ha. Lack of rain and lower use of fertiliser were the main causes of the below average results.

India

India has targeted a national wheat production of 78.4 million tonnes in 2009, although recent hot and dry weather is threatening this season's crop. Rabobank currently expects Indian wheat production to reach 75 million tonnes in 2009/10.

At the beginning of January 2009, the area planted under wheat was 26.26 million ha, marginally higher than the 26.21 million ha in the 2008/09 season and below the record plantings of 28.15 million ha in the 2007/08 season. The area under wheat has not increased to 29 million ha this year as targeted by the government as farmers in

Madhya Pradesh and Rajasthan have diversified to other crops.

There are reports that the farmers in 4 to 5 districts of Madhya Pradesh have increased the area under gram (legume) hoping for better comparative returns, while farmers in Rajasthan have shown an inclination towards mustard. Uttar Pradesh (UP), the largest wheat-producing state, may see more areas under the wheat this year as at least half of the 10 lakh ha of rice area in UP will go to wheat. Wheat acreage in Punjab stood at 34.95 lakh ha so far, while those in Haryana touched 24.80 lakh ha.

China

Chinese wheat production estimates for the current 2009/10 crop have been revised lower in recent months, due to on-going dry conditions in some of the major wheat-producing regions.

Rabobank is currently forecasting Chinese wheat production of 108.5 million tonnes in the 20009/10 season.

Due to the high level of domestic inventory, the Chinese wheat spot price is still quite stable, around 1,770 in second half February, 2009

Outlook

The world wheat market is slowly starting to shift its focus away from the bearish old crop fundamentals, following a record harvest in 2008/09 and looking to 2009/10. Given the sharply higher carry-in stocks, the focus is shifting to Northern Hemisphere plantings and weather conditions. Unless there is a significant production issue in at least one major producing region, Rabobank is forecasting a 6% decline in world production in 2009/10, although stock levels are expected to remain at comfortable levels.

Rabobank's price outlook indicates wheat prices remaining range bound—USD 5 to 6 throughout the remainder of 2009—unless there are significant production issues or the recent strength in the USD subsides and US wheat exports are able to become more competitive versus the Black Sea and EU origins.

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Corn

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Key Market Drivers	
▲	New crop fundamentals—US and world—more supportive for prices
▲	Slight improvement in ethanol profitability
▲	Increased US ethanol mandates in 2009/10
▼	Feed demand sharply lower due to global economic weakness
▼	Higher carry-in stocks from 2008/09

Prices

Corn prices have been pressured lower in the first two months of 2009 weighed down by bearish fundamentals. Old crop (2008/09) production estimates have been ratcheted higher while demand numbers have been slowly unwound as the impact of the global economic slowdown and weaker energy prices have reduced corn consumption.

Despite nearby corn prices benefitting from challenging weather in South America in recent months, the upward revision in carry-in stocks for the 2009/10 season together with an increasingly bleak demand picture have largely eroded early 2009 price gains. Nearby CBOT corn prices (March 2009 contract) have remained above the 25-month lows reached in December 2008, which now look likely to set the low for the season.

The 'battle for acres' between corn and soybeans in the US has been a major focus for the market at this stage of the season in recent years. Tight stock levels for both crops have resulted in a need to encourage plantings in the upcoming spring. However, this season the competition does not appear as critical given the increased inventory levels and weaker demand scenarios for both corn and soybeans.

Current price levels indicate US farmers will favour soybeans over corn in 2009/10, given the relative price ratios and higher per acre production costs associated with corn. In 2008/09 the price ratio in the nearby contract between CBOT soybeans and corn was around 2.7:1, resulting in an 8% YOY decline in corn plantings.

Figure 11: Corn Price Forecasts (CBOT)

	2008			2009				2010
USD/bu	Q2	Q3	Q4	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
prices	6.3	5.8	3.8	3.8	3.8	3.9	3.8	3.8

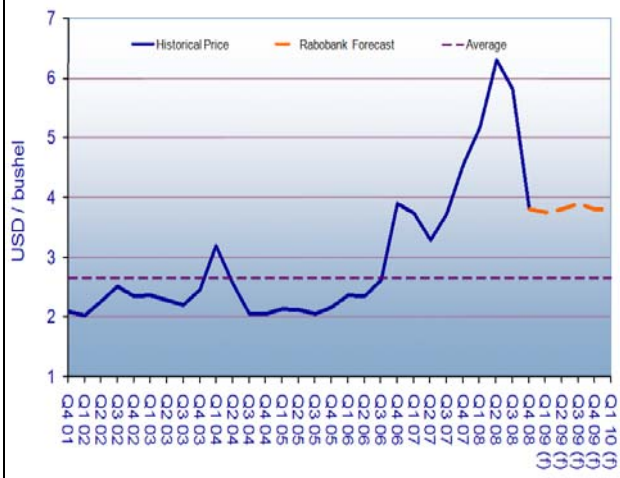
*All forecasts are period averages. Source: Rabobank, Bloomberg

Figure 12: Soybean to Corn Ratio (Nearby contract CBOT)

Source: Rabobank, Bloomberg

While the planting decision window remains open, the current nearby ratio is around 2.5:1, and, together with the carryover of high-cost fertiliser from last season, of which corn requires a higher intensity than soybeans, there is little to suggest that there will not be a further swing this season, unless this ratio changes throughout March.

Figure 13: Corn Price Quarterly Forecasts (CBOT)
Q4 2001 – Q1 2010



Source: Rabobank, Bloomberg

That said, the US corn balance sheet cannot afford another 8% YOY decline in plantings this season and corn

prices will need to remain competitive relative to soybeans over coming weeks. Improved South American soybean weather forecasts together with a turnaround in US gasoline consumption trends and an improvement, albeit modest in ethanol profitability, have started to help improve corns competitiveness.

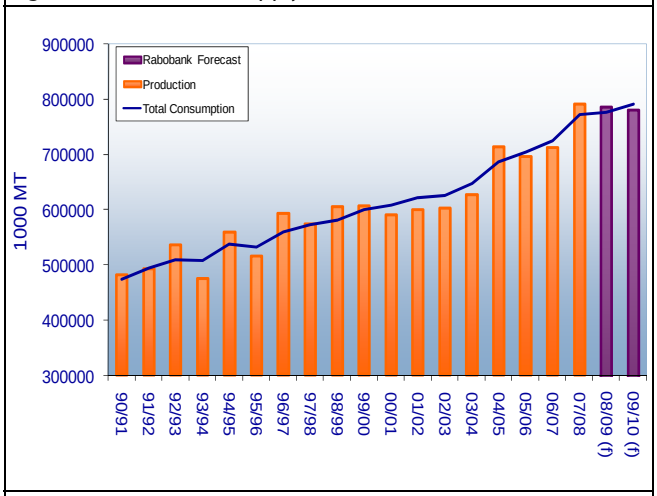
Rabobank is forecasting CBOT corn prices to remain range bound between USD 3.50 to 4.50/bushel over coming months and during the US growing season. Although there remain many variables with USDA plantings announcements, ethanol usage and profitability together with seasonal conditions and USD direction all continuing to be highly important to price over coming months.

Corn Fundamentals

Better-than-expected crop production in the US and China and a deteriorating demand complex is expected to outweigh drought affected production in South America and push corn carry-out levels to 139 million tonnes in 2008/09, 9% higher than year earlier levels.

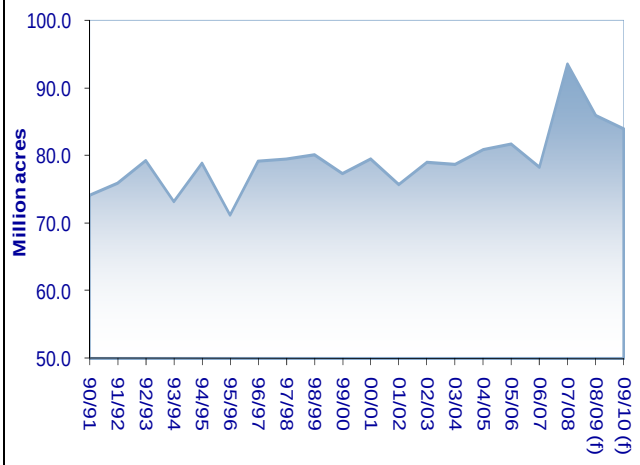
Based on current price relativities and the limitations on financing for many of the worlds farmers, world corn production is expected to fall slightly in 2009/10, although weather will remain a key determinant. Consumption is forecast to be relatively flat, with weaker feed demand being offset by higher ethanol mandates in the US.

Figure 14: World Corn Supply and Demand



Source: Rabobank, USDA

Figure 15: US Corn Planted Area



Source: Rabobank, USDA

US

US-corn ending stocks are estimated to reach 48.5 million tonnes in the 2008/09 season, up from 41 million tonnes in the 2007/08 season.

Ethanol usage in 2008/09 was lowered by 100 million bushels to 3,600 million bushels due to weaker margins at current prices, and projections for feed and residual use also declined by 50 million bushels due to lower livestock numbers in the US.

Clearly the 'battle for acres' between corn and soybeans holds less importance in 2009/10 than it has in recent seasons with stock levels for corn at more comfortable levels than the 2006/07 and 2007/08 seasons and with ample supplies of feed grains available globally. That said, given the increased ethanol mandates which will push minimum corn usage higher in 2009/10, despite the weaker feed demand scenario, the market is likely to remain highly responsive to any production issues in the summer months.

Brazil

Mainly as a result of the expected reduction in the summer corn planted area (down 3% from the 2007/08 crop) and the drought that has been affecting most of the major growing regions (basically the south of Brazil), the 2008/09 summer corn production was revised downwards in Conab's (National Food Supply Agency) February report. Brazil's summer corn crop is estimated to be 32.9 million tonnes, 17.7% lower than the 2007/08 crop.

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Despite the expectation of lower summer crop production, a total output (summer and winter crop together) of more than 50 million tonnes for the 2008/09 crop is still projected. Adding up 12 million tonnes of current stockpile, Brazil is likely to face its largest corn supply in history (around 62.5 million tonnes). This high stocks level has pressured prices in Brazil since the end of 2008, and a significant recovery in local prices is not expected until March. Local demand, however, is likely to increase in 2009, offsetting the over-supply in the medium term. The winter crop area (planting has just started in Brazil) and the pace of domestic corn exports are the two main drivers that will determine the speed with which domestic prices recover.

Argentina

Area planted to corn this year will be 3.5 million ha (including forage), 14% lower than 2007/08. This reduction has occurred in all regions of the country and represents the lowest area of corn in over a decade.

As in the case of wheat, reduced planting was due to dry weather and increased production costs at a time of decreasing international prices. In addition, export permits for both wheat and corn are severely restricted, reducing farmers' interest in planting corn.

The USDA reduced its Argentinean corn production estimate from 16.5 million tonnes to 13.5 million tonnes in its February report, due to the hot and extremely dry weather conditions affecting the corn crop at an important pollination period. Local estimates indicate production may fall as low as 12.5 million tones, with the harvest percentage likely to fall as low as 75% of plantings due to the poor crop conditions. Major producing areas have received 40% to 60% below average precipitation in 2008/09.

Argentina was the world's second largest corn exporter last year. This year, corn exports are projected at only 5 million tonnes, 67% lower than last year's 15 million tonnes. Export taxes on corn have been reduced from 25% to 20%, but restrictions in the granting of export rights imply that export markets are practically closed for these two crops at present.

EU27 and Black Sea Region

The EU corn price is in line with feed-wheat market price movements and is currently trading at a level of EUR 138/tonne. As there is abundant feed wheat in the market, the price of corn will follow feed wheat levels because of the possibility to substitute between the two crops. There is still a substantial price difference between French and Hungarian corn of more than EUR 35/tonne because of the abundant corn crop in the eastern part of the EU27. Hungarian corn is currently trading at a level of EUR 103/tonne. The feed industry uses more corn because it has gained competiveness against wheat. The 2008/09 corn crop in both the EU27 and the BSR remains close to earlier figures.

The corn markets in the EU27, Russia and Ukraine are expected to be largely driven by international market developments in 2009/10.

China

The area planted to corn in China was 28.8 million ha in 2008, 0.68 million ha lower than the previous year. The main reason for the 2.3% decrease in acreage was some farmers' choosing to switch to planting soybeans at the beginning of crop season as they believed soybeans could have higher returns over corn. The output of corn in 2008 was 165.5 million tonnes, up 8.7% from 2007.

In 2008, China exported roughly 270,000 metric tonnes of corn, with a decrease of 94.5% over 2007. Many former protective trade policy measures, such as eliminating the export tariff rebate and imposing a 5% export tax, contributed significantly to such a sharp decline in corn export.

Despite the bumper harvest of corn, feed-corn demand—which accounts for two-thirds of total corn consumption—is relatively stagnant at present due to the negative effect of the melamine scandal and low returns on hog raising. Facing a possible corn oversupply in the coming year, the Ministry of Finance decided to eliminate the former 5% export tax to zero, starting December 2008.

Outlook

World corn stocks are set to increase in 2008/09, despite drought-affected South American production, as demand expectations are wound back due to the flow on effect of the weak global economic conditions.

New crop fundamentals do appear more supportive, with higher US ethanol mandates and recently improved blending margins expected to partially negate weaker feed demand. Market focus is increasingly shifting to new crop plantings in the US with the soybean/corn ratios and grower returns continue to favour soybeans. Corn competitiveness will need to improve over the next month to ensure sufficient acreage in 2009. Weather during US plantings and the growing season will remain critical for price direction.

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Soybeans

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Key Market Drivers	
▲	South American supply concerns
▲	US exports remain robust, supported by China
▲	New crop plantings in US
▼	USD strength
▼	Weaker feed demand for soymeal

Prices

Soybean nearby futures prices as represented by the Chicago Board of Trade (CBOT) reached a 20-month low in early December 2008 of USD 7.84/bushel. A fall of 53% in only five months from its record peak of USD 16.49/bushel. Supply concerns in the drought-impacted regions of South America, ongoing support from government biofuel policies, continuing import demand especially from China has seen nearby soybean futures prices perform strongly in January and first half February before easing in line with improved weather in Argentina.

In early 2009, the key focus in the market has centred on supply, particularly in Argentina and Brazil as the third and second largest soybean exporters, respectively. Since July 2008, the drought—mainly in Argentina—has intensified and soybean plantings will need substantial rain to improve yield an production expectations. Rain in mid-February has improved crop conditions although more rain will be needed prior to harvest.

Figure 16: Soybean Price Forecasts (CBOT)

	2008			2009				2010
USD/bu	Q2	Q3	Q4	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
prices	13.8	13.2	9.0	9.2	8.8	8.8	9.0	9.0

*All forecasts are period averages. Source: Rabobank, Bloomberg

Adding to the South American weather concerns are production risks as generally lower amounts of fertiliser have been applied to the 2008/09 crop due to the market uncertainty at planting and credit constraints for crop funding. The potential of Argentine soybean production falling short is pushing export demand towards the US and, subsequently, supporting soybean futures prices.

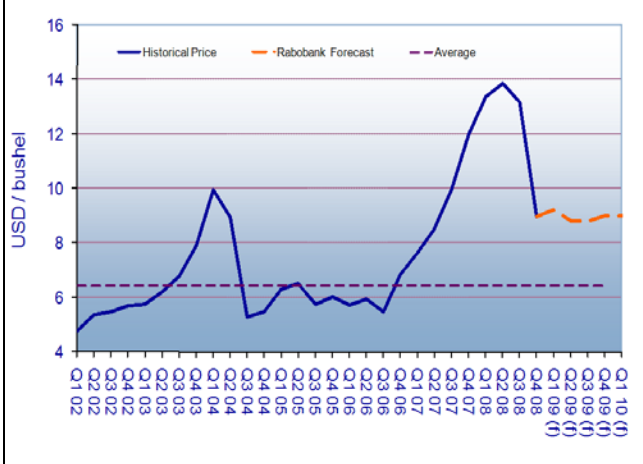
Following early season production issues in South America, Rabobank is forecasting a slight easing of soybean prices throughout 2009. Already this trend has developed in second half February with CBOT soybeans trading at USD 8.70/bushel, down from a 2009 high of USD 10.36/bushel. Looking ahead prices may test USD 8.00/bushel downside, particularly if Chinese demand eases and South American weather continues to turn favourable. Further out US weather during plantings and the growing season will be critical for price direction.

Global fundamentals

The January USDA forecasts for Argentina and Brazil show production at 49.5 million tonnes and 59 million tonnes, respectively. The potential impact of continuing drought and lower use of fertiliser could see these numbers significantly lowered in the coming weeks. As an example, Argentina's Buenos Aires Cereal Exchange has already placed a production range of 34.5 million tonnes to 38.2 million tonnes of soybeans in 2008/09 season, well below the USDA forecast.

If rains eventuate and production is maintained in South America, it is likely that large carry-out stocks of corn and soybeans, 14% and 6% above the previous five-year average respectively, could place downward pressure on prices. With the lure of lower production costs, more flexible planting windows and higher margins for soybeans, the trend of higher plantings to soybeans may increase further in 2009/10 and may also see the market push soybean prices lower, encouraging farmers to rethink their planting options.

Figure 17: Soybean Price Quarterly Forecasts (CBOT)
Q4 2001 – Q1 2010

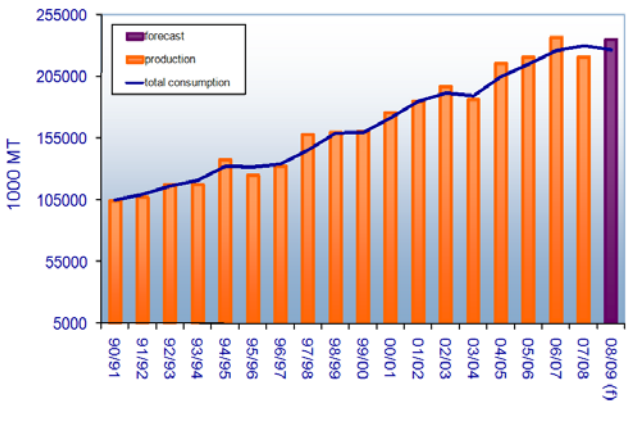


Source: Rabobank, Bloomberg

On the demand side, Chinese imports that have been holding strong have been a saviour for the soybean market, especially in the US. China's portion of US exports so far in the 2008/09 season is at 58%. The continued

demand in the latter part of the first half of the season has placed upward pressure on soybean prices. However, the full-year forecast for Chinese imports of soybeans in 2008/09 is still very uncertain with initial expectations suggesting global imports will be down 5% compared to 2007/08.

Figure 18: World Soybean Supply and Demand



Source: Rabobank, USDA

US

US soybean markets have been supported by the robust trade with China. Current commitments to China are 75 million bushels higher than last year but down for nearly every other country. Clearly, the US is carefully monitoring China's seasonal move to South American supplies and the weather reports from South America.

Soybean prices have also diverged from crude-oil prices, with declining demand for edible oil and supply issues as key drivers. Domestic demand drivers are negative, with falling edible-oil demand, and declining production for beef, pork and poultry.

The price support from Chinese demand is vulnerable to a seasonal shift to South American supplies and the Chinese fulfilling their stock-building agenda. US domestic crush margins—squeezed by previous purchase prices in falling market for meal/oil prices and falling demand (fewer animals to feed and more feed wheat), declining edible consumption of soy oil and export commitments for soy oil—are below a year ago and likely to lag further. Domestic use of soy oil declined by 5% YOY in October/November 2008. Crush is driven by meal demand, but, with the slow US economy and increasing competition from corn by-products, the USDA is projecting a significant decline in US soy crush.

The industry is questioning the price-supporting potential of the seasonal corn/soy acres, because lower demand and decreasing wheat/cotton plantings leave ample acreage. Neither corn nor soy is expected to need a substantial increase in acreage to meet projected demand. Soy acreage will increase if corn returns are below production costs, based on the price point that farmers locked in fertiliser costs in a falling market.

Argentina

As soybeans are planted later in the year than wheat and corn, much of the area not planted to these other crops was expected to switch to soybeans this season. Soybeans also exhibit a more favourable cost-to-price ratio, which biased farmers towards the crop at a time when prices of inputs were high relative to falling commodity prices.

Soybean plantings are estimated at 17 million ha in 2008/09, slightly higher than last season's 16.6 million ha.

As is the case with all other crops, soybean yields were under threat due to the dry and hot seasonal conditions in Argentina. Fears of major drought damage pushed CBOT prices higher in early January. Production estimates for Argentinean soybeans by the USDA were reduced from 50.5 million tonnes in December to 43.8 million tonnes in February. Local estimates are as low as 41 million tonnes, compared to last year's 46.2 million tonnes. However, rains in the last weeks of January and early February have improved the outlook for soybean yields, easing concerns both in international and domestic markets.

Brazil

Soybean planting activities have practically finished in Brazil. According to Conab's estimates, soybean 2008/09 crop area should increase by 0.8% over the previous season, implying a total soybean area of 21.5 million ha.

Soybean yields, however, are expected to decrease more than previously estimated, mainly as a result of lower utilisation of inputs and the drought in the southern states of Parana, Santa Catarina and Rio Grande do Sul and in the state of Mato Grosso do Sul in the Centre-West. These four states together account for 43% of the total domestic output. Thus, Conab's estimates indicate a soybean production of 57.2 million tonnes, 4.7% lower than the previous crop.

Outlook

The world soybean market has been strongly supported early in 2009 by weather concerns in South America,

however, improving seasonal conditions together with an unfavourable demand outlook are now forcing prices lower. Further price weakness is a distinct possibility particularly with the risk of policy changes in both China and Argentina which would both be bearish for price direction.

At current levels, US farmers are expected to increase soybean plantings in the spring which will ease any global supply concerns, particularly if livestock feed-demand continues to deteriorate. Rabobank is expecting soybeans to trade sideways to slightly lower for the duration of 2009, assuming normal growing conditions in the US.

Rabobank Soft Commodities Monthly

Palm Oil

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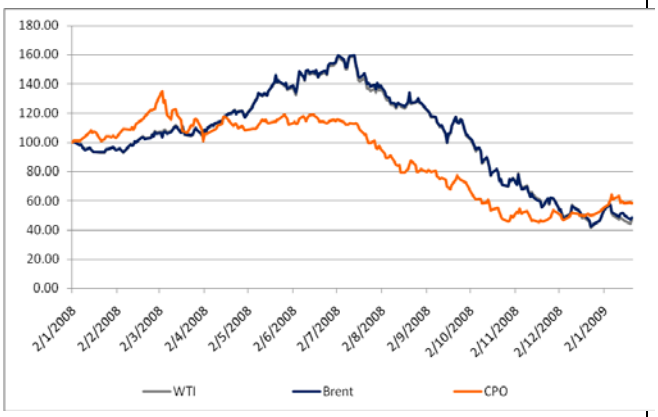
Key Market Drivers
▲Seasonal yield decline—lower output over the first few months of the year ▲Demand from India ▼Chinese palm-oil imports stagnant ▼EU biodiesel policies place restrictions on demand for palm based biodiesel ▼Low crude prices

Prices

After plummeting over 65% from its record levels in March, palm oil prices appear to have found a bottom. Prices bottomed out at MYR 1,440 in mid-November 2008 and after that staged a mini-rally, rising over 25% to reach the current level of about MYR 1,800.

Figure 19 : Index Prices (USD) – Crude Palm Oil, WTI & Brent



Source: Bloomberg, Rabobank 2008

Global fundamentals

The China-India story, which drove the commodity price rally in 2007/08, appears to have fizzled out with the current economic crisis. Import data from both countries, however, shows sustained, strong demand from India, while demand in China looks to remain stagnant.

As predicted, Indian palm oil imports spiked over the last three months of 2008. According to data from the Solvent Extractors' Association of India, total edible-oil imports into the country reached 6.22 million tonnes, a 32% increase from 2007 levels. Palm oil accounts for 85% of this volume.

For the full year, palm oil imports grew 62%. Two possible factors that drove demand for palm oil in India are the reduction in the import tariff rates and the switch by consumers to lower-cost oils as the recession tightens household expenditures. The Indian government reduced tariff rates across the board for edible oils in April 2008 after which import volumes increased dramatically.

Biodiesel

The price movements between palm oil and crude oil appear to show some level of decoupling. While crude petroleum prices have fallen significantly over the past two months, the price movement of palm oil shows the contrary. Biodiesel producers have been hit badly by the commodity-price cycle, during the upswing and even during the downswing. During the rally, record edible-oil prices made biodiesel production unprofitable. After the slump, crude-oil prices have fallen so much that biodiesel production is still unprofitable.

Biodiesel demand is very much dependent on government policies, and profitability on subsidies and provisions. With the EU27's imposing a 35% carbon dioxide savings requirement on all biodiesel imports, palm biodiesel faces a significant hurdle in meeting this requirement. Both the Malaysian and Indonesian governments are attempting to address this demand problem with their own domestic biodiesel mandates. The Malaysian government would impose a B5 biodiesel mandate by 2010 while the Indonesian government already has a 2.5% biofuels mandate in place. However, faced with increased opposition from domestic oil and gas producers, the Indonesian government is considering halving this target.

Outlook

While the supply situation points to a tightening production over the short-term, support for palm oil prices has been mitigated by the uncertain demand picture. Demand from the two largest consumers – China and India – paint contrasting pictures. While Indian palm oil imports spiked over the second half of the year, Chinese imports have stagnated. The biodiesel effect on prices has abated as record low crude-oil prices made biodiesel production unprofitable. Meanwhile, the food picture remains strong.

Over the short term, the weak economic situation will continue to suppress prices but, over the long term, as the underlying supply-demand imbalance becomes more apparent, support will be provided for palm oil prices.

Rabobank Soft Commodities Monthly

Sugar

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Key Market Drivers	
▲	Deficit of 5 or more million tonnes expected for 2008/09 international crop year
▲	Downward revision of Indian production
▼	Low oil prices
▼	Low Brazilian ethanol prices

Prices

World market raw sugar prices have traded within a range spanning USc 13.0/lb to USc 13.6/lb over the last month, reflecting an increasingly constructive fundamental outlook. The leading influences this month have been further downward revisions of India´s sugar production in 2008/09, and uncertainty over the extent to which cane and sugar production in Brazil´s Centre-South region in the forthcoming harvest will exceed the current season´s output. However, the general backdrop to these fundamentals—uncertainty regarding economic growth, the continuing credit squeeze and the general vulnerability of financial and commodity markets to further bouts of turbulence—remains challenging, and suggests that volatility is unlikely to diminish in the near future.

Global fundamentals

The global supply-demand balance for the international 2008/09 crop year continues to provide a supportive backdrop for world sugar prices in 2009. Recent developments in India have helped to increase the upper limit of the range of estimates of the global deficit in 2008/09, which some analysts are now pegging at close to 10 million tonnes.

Figure 20: Sugar Price Forecasts (ICE - NYBOT)

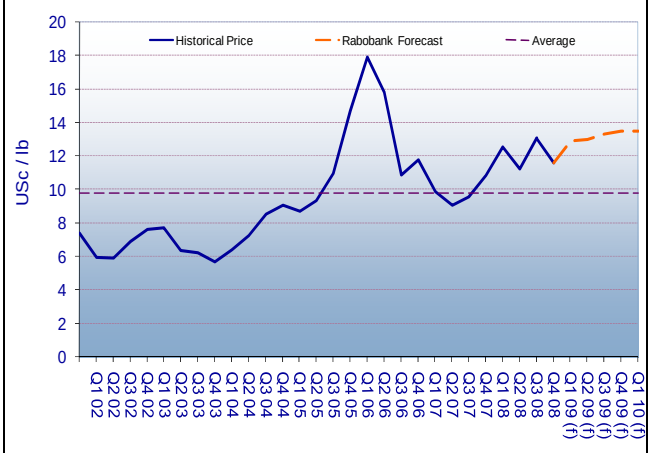
	2008			2009				2010
Usc/lb	Q2	Q3	Q4	Q1 (f)	Q2 (f)	Q3 (f)	Q4 (f)	Q1 (f)
prices	11.2	13.1	11.6	12.9	13.0	13.3	13.5	13.5

*All forecasts are period averages. Source: Rabobank, Bloomberg

However, set against these constructive fundamentals, the dollar remains relatively robust against other currencies, and the oil price remains low. Continued dollar strength (and its flip side, continued weakness of the Brazilian real) plus the possible consequences of a prolonged period of low oil prices are two factors that preoccupy some market watchers and participants.

The significance of these two factors is the extent to which they impact the relative attractiveness of sugar production versus ethanol production in Brazil. Regarding the exchange rate, all other things being equal, a weaker real implies an increase in the attractiveness of export sugar sales versus domestic ethanol sales. Regarding oil prices, the possible impact is twofold—first, that in the face of lower oil prices, Petrobras may at some point lower gasoline prices, and, second, that lower gasoline prices in the US will pressurise US ethanol prices, and Brazilian ethanol exports to the US will be reduced. The threat from all of these possible developments is that they could push the increase in Brazilian sugar production in 2009/10 far beyond what the market is perceived to require, forcing prices downwards.

Figure 21: Sugar Price Quarterly Forecasts (NYBOT)
Q4 2001 – Q1 2010

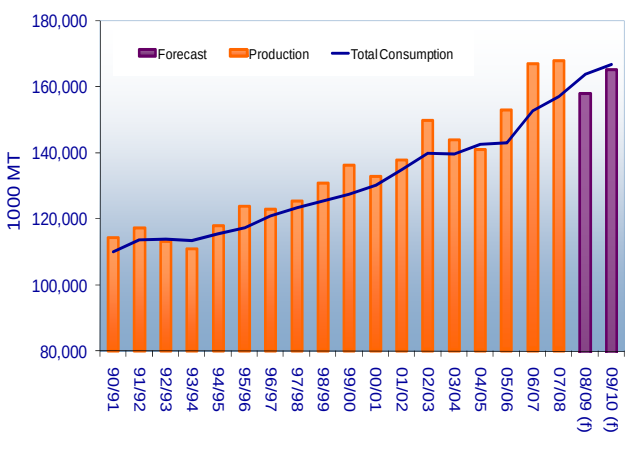


Source: Rabobank, Bloomberg

The counter-arguments are (i) that the capacity for switching is limited (there is a ceiling on Brazil´s capacity to produce sugar, though exactly where this ceiling lies is not clear) and (ii) that Petrobras is unlikely to make any adjustments in the short term. Brazilian gasoline prices remained flat throughout the recent oil price boom, so any adjustment may be unlikely unless oil prices remain low for a long time. This has not happened yet – up until September 2008, world crude oil prices averaged USD 100/barrel. In addition, if there were to be an adjustment of domestic fuel prices, it could be that diesel prices are adjusted to a greater extent than gasoline prices, as happened in May 2008, when diesel prices increased but

gasoline prices did not (diesel sales in Brazil are approximately double the volume of gasoline sales). In summary, the issue is complicated; an imminent adjustment seems unlikely, but if oil prices stay low enough for long enough, the argument becomes more compelling.

Figure 21: World Sugar Supply and Demand



Source: Rabobank, USDA

With regard to ethanol sales into the US market in 2009, the Brazilian industry is already factoring in expectations of a significant decline. US ethanol prices have fallen over the last few months, though not by nearly as much as wholesale gasoline prices. However, with a mandated blending programme and firm corn prices, US ethanol prices may well be driven to move independently from gasoline prices. The Renewable Fuels Association recently announced that the sector is running at 85% of capacity as a result of ethanol plant closures.

Brazil

The latest numbers documenting the progress of the harvest in Centre-South Brazil, released by UNICA in mid-January, show that cane crushed reached 499.5 million tonnes, with 40 of the region´s 298 mills continuing to operate in January. Even so, it is still estimated that 20 million tonnes of cane or more will stand over until the new season, which will begin in April.

According to data from ANFAVEA (Brazil´s national association of vehicle manufacturers), 2.7 million new vehicles were sold in 2008, of which 2.3 million were flex-fuel. Rabobank estimates that at the end of 2008, the total national flex-fuel fleet numbered 6.8 million vehicles.
The outlook for new car sales in Brazil in 2009 is difficult to project. Sales in November and December 2008 were sharply down (26% and 20%, respectively) compared to sales in the corresponding periods in 2007, the consequence of slowing economic growth and tighter credit availability. To assist the car industry, the government has temporarily reduced taxes on car purchases, but whether this has provided any meaningful stimulus to sales is unclear—vehicle registrations in January 2009 did show a modest improvement over December 2008´s figures (+3%), but were still down 8% on registrations in January 2008.

Any slowdown in new car sales will reduce the expansion of potential ethanol demand in Brazil. However, even assuming a severe reduction (-50%) in sales for 2009 and 2010 versus 2008, Rabobank estimates that potential ethanol demand in Brazil could grow by 2.4 billion litres in 2009/10. Whether this potential demand is fully met depends on the pricing of ethanol versus gasoline in the local market.

While domestic sugar prices in Brazil have been rising steadily, ethanol prices have been under steady pressure. Ethanol sales represent the easiest means for millers to generate ready cash, and the credit crunch has forced many mills into distress-selling. As a result, ethanol and sugar prices in Brazil are currently heading in different directions. Some in the industry fear that when the new season begins and millers can once again arbitrage the two markets, the disparity between the two markets will boost sugar production beyond the increase already expected by the market, forcing prices down. Others are adamant that the scope for producing extra sugar will already be at its limit if the Centre-South produces another 4.0 million tonnes above 2008/09´s output of 26.7 million tonnes tel quel. If this were to be the case, then even during the milling season, arbitrage possibilities would be limited, and the ethanol and sugar markets could go their separate ways. Under such a scenario, sugar margins could continue to be attractive even if ethanol prices and margins were to remain under pressure.

India

Sugar production in 2008/09 is estimated to be in the range of 16.5 to 17 million tonnes, a sharp decline from 26.5 million tonnes produced in 2007/08. This decline is largely on account of shift of crops by farmers from cane to other crops such as soybean, paddy and wheat (largely the result of the sugar cycle led by cane arrears). Moreover, in 2008/09 there has been a drop in recovery from cane to the extent of 0.5% to 1% across India. In fact, many industry players believe that the sugar production in 2009/10 will also be less than 20 million tonnes. India will import raw sugar in 2008/09 and 2009/10 to curb rise in domestic sugar prices.

Many of the sugar mills in major producing states such as Maharashtra, Uttar Pradesh, Punjab and Haryana have started running out of cane since the beginning of February 2009. Except for those in the south, the other mills in the country are likely to stop crushing in early March.

According to the government, the opening stocks as of 1 October 2009 were 10.5 million tonnes. However, as per Indian Sugar Mills Association (ISMA) the figure stood at 8.07 million tonnes. This discrepancy in stock numbers has a serious implication on government policy as well as market prices.

In fact, the government has already announced a few measures to check prices. It has announced duty-free imports of raw sugar with an obligation to export an equal quantity after two years. Also, it has imposed restrictions on the quantity of sugar a trader can hold to check hoarding of sugar stocks.

As per government sources, around 1 million tonnes of raw sugar imports has already been contracted by sugar mills and there is a possibility of another 0.5 million to 1.0 million tonnes of raw sugar imports in 2008/09.

Over the last six months, there has been a steady rise in ex-factory sugar realisations—currently in the range of INR 18,000 to 20,000/tonne (USD 360 to 400). They are expected to operate in this range and could go up by 5% to 10% over current levels over the next two years. This would also depend on the extent of raw sugar imports in 2008/09 and 2009/10.

The Cabinet Committee on Prices (CCP) has decided not to extend export subsidies on sugar in 2008/09. Given the inflationary pressures, the Government is likely to seriously consider a ban on sugar exports. In any case, we do not foresee any significant exports in 2008/09.

The improvement in sugar prices has boosted optimism in the Indian sugar industry. However, the decline in cane availability has led to sharp decline in number of crushing days and consequently lower sugar production for most sugar mills. This implies that the overhead costs would get distributed over significantly lower quantities of sugar. At the same time, factories are not generating enough bagasse and molasses this season to be able to make full use of power cogeneration and ethanol-making capacity in an attempt to de-risk the sugar commodity business. As a result, the benefits of increased sugar prices are largely being compensated by lower sugar production. Hence, sourcing strengths in cane would be critical for significant improvement in financials on a quarter-to-quarter basis going forward at least for the next two years.

Conclusions

Signs are emerging that the global deficit anticipated for the 2008/09 international crop year is deepening, largely as a result of further downward revisions of India´s production but also as a result of lower anticipated output in the EU, Pakistan and China. However, with the market looking largely to Brazil to fill the gap in world exports left by India, the US dollar/Brazilian real exchange rate and the price of gasoline in Brazil have emerged as influential factors shaping the development of Brazilian sugar output and global market fundamentals. We consider that the threat of a reduction in the gasoline price in Brazil is relatively small. However, there is real uncertainty regarding the size of the coming cane crop in the Centre-South and the maximum percentage of cane that could be used to make sugar. Nevertheless, weighing the combined sum of these influences and the wider fundamental picture, our expectation remains that world prices in 2009 should be higher than those in 2008.

Rabobank

March 2009

Rabobank Soft Commodities Monthly

Rabobank International

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