

First State Global Agribusiness Fund

Monthly report

May 2013



Market review

- Global agribusiness equities were weak over the month, underperforming global equity markets.
- Corn prices (+1.9%) edged higher, reflecting speculation that delayed planting due to cold, wet weather will affect production volumes. Flooding in parts of the US is also jeopardising some corn area. Wheat (-3.5%) declined after the US Department of Agriculture suggested that global production will rise to a record level in the next 12 months.
- Soybeans (+7.9%) rose strongly, reflecting low inventory levels in the US. There has been a record soybean crop in Brazil, but strong sales and some logistical issues appear to be limiting current supplies.
- Sugar prices (-6.0%) continued to trend lower, extending a decline which began in early 2012. Consumption levels are little changed and there appears to be excess supply in the global market. Brazil, the world's largest sugar exporter, is expected to crush a record crop this year, while Thailand and Mexico are also expected to increase output.
- Palm oil prices (+4.2%) reversed most of their declines in April as commentators forecasted a recovery in exports from Malaysia, the world's second largest palm oil producer.
- Lumber prices rose strongly in late 2012 following an improvement in housing starts in the US, but have since drifted lower as sawmills have responded to this higher demand by increasing supplies. Demand from China also declined during May.

Fund activity

- We added to our position in Bunge, which is a grain originator and handler as well as a processor of oilseeds for animal feed and consumer products. Bumper crops in the US and Brazil are expected to provide significant earnings leverage, but the stock still trades on a reasonable valuation.

- We increased our position in pork producer Smithfield Foods. The price of feed stocks for hog farms is coming down and the company is expanding its branded food business in the US. This earnings growth did not appear to be factored into the share price. Late in the month, Chinese pork producer Shuanghi International Holdings made a takeover offer for the company at a 30% premium to its last traded price. We also added to our existing position in Tyson Foods, which is seeing improving margins in its chicken business and beef processing business.
- A recent pullback in the share price of Syngenta provided an opportunity to increase our holding in the crop protection business. Improving weather in the Northern hemisphere augurs well for crop protection demand over the next few months. This purchase was funded by reducing exposure to Monsanto, a comparable company which was trading at a less-appealing valuation.
- Relatively high inventory levels of potash in China and Brazil along with expectations of delayed contract negotiations with India and China could continue to exert downward pressure on prices and volumes. This prompted us to sell our holding in Chilean potash producer SQM and reduce investment in Russian potash producer Uralkali.
- We used recent share price strength as an opportunity to lock in partial profits from positions in Kubota Corporation and Agco Corporation. The valuation of Kubota was starting to look demanding following the recent rally in Japanese equities, while Agco performed well after reporting a strong result for the first quarter of 2013.

Market Outlook and Fund Positioning

- In spite of ongoing share [change to 'stock'] market volatility due to macro-economic uncertainty and central bank intervention in financial markets, the long-term fundamentals supporting the agribusiness sector remain compelling. Global population growth supports long-term food demand and improving wealth in emerging regions is resulting in not only increasing demand for food but also more grain-intensive protein.
- Weather conditions continue to affect the prices of individual commodities. This can have an important influence on sentiment towards the share prices of companies in the soft commodity sector. We do not forecast commodity prices and continue to select quality stocks with good earnings growth profiles and sound balance sheets.
- The Fund maintains a high level of diversification by geography, commodity type, within the agricultural supply chain and company size. Around 55 stocks are currently held in the portfolio.
- Our research effort continues to be based on a high level of contact with agribusiness companies globally. There is no substitute for visiting companies' operations first-hand in order to assess the economics of each asset and to better understand the everyday challenges that are faced.
- Merger and acquisition activity continues to be a feature of the sector, with ADM making its final and agreed offer for Australia's Graincorp at the end of April and China's Shuanghi International's takeover offer for Smithfield Foods in May. We also continue to see the expansion of the sector with new listings and capital raisings to fund growth plans.

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