

⊙ Action

Soft commodity prices continue to rally following the release of a bullish USDA crop forecast and bullish stock-to-consumption data. Supply forecasts for corn left inventory at precariously low levels. Further, the extreme temperatures caused by La Niña are playing havoc with planting data in the Americas. Ethanol prices also continue to climb while most soft commodity futures markets have moved into backwardation, indicating short-term tightness.

Anchor themes

- ⚓ While speculative positions have grown in a number of agriculture futures markets, spot prices for many physical non-traded farm products have risen, indicating firm demand. To date, weather disruptions have not disrupted US or Asia rice prices.
- ⚓ Asia is experiencing a perfect storm of rising food prices affecting CPI and leaving little policy options, while firming coal prices look set to accelerate PPI.

Market calls

We remain bullish on soft commodity prices. We re-initiated a basket of agriculture equities on 23 November, 2009. We have removed Wilmar and added Mewah International. The latter is the sixth-largest palm oil refiner in the world (the second-largest in Malaysia after Wilmar), with integrated downstream operations. With majority market share in West Africa, Mewah International is a strong consumer pack oil franchise.

Asia's soft commodity crunch (XXIII) (Erratum)

① An inconvenient truth

"The current strong La Niña is causing unusually cold stormy weather in the Northern Hemisphere and problems with crop production in the Southern Hemisphere. Expect more problems with extreme weather, especially in January. Some experts claim that the phenomenon has peaked, but if others who predict a new peak in March are right, the problems with crops, storms and global transportation will last for the next three months" – Browning Newsletter, January 2011

Last week's USDA report was illuminating in highlighting the ongoing tightness in supply. Dramatically, the USDA cut US corn supply estimates for the year to 31 August for the fourth time since 2010 due to weather disruptions, with inventories already at 15-year lows. Meanwhile for China, US soybean supply forecasts have left projected inventories at precariously low levels. World wheat supplies, on the other hand, are ample, but the markets continue to worry about inventories of high-quality wheat suitable for milling flour. Fortunately, there appears to be little concern over rice. The same is not true for cotton, where the divergence between planting intentions and supply remains wide.

Despite the tightness in supply, investors remain nervous about the degree of speculative interest and concerns abound that prices will be subject to a sharp blow-off. First, La Niña continues to disrupt weather patterns and hamper planting. Second, there appears to be consistent follow-through price moves as higher corn prices lead to higher feed prices, while climbing oil prices are also experiencing a sympathetic appreciation. Last, agriculture equities appear to be moving in tandem with their underlying products, suggesting some degree of rational pricing.

Short term, we believe the major concern for equity investors lies in two problems stemming from higher prices. First, governments are increasingly resorting to intervention in the form of price controls or anti-speculation measures. Second, companies flush with profits are finding it easier to invest in projects such as property where payback periods are shorter and less volatile than agriculture.

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Soft commodities basket

Company	Ticker	Nomura rating	Price
China Green	904 HK	BUY	8.5
United Phosphorus	UNTP IN	BUY	153.2
Noble Group	NOBL SP	BUY	2.3
JSR Corp	4185 JP	BUY	1,716.0
Sri Trang Agro	STA TB	NEUTRAL	39.0
Khon Kaen Sugar	KSL TB	BUY	14.0
China Yurun Food	1068 HK	BUY	27.2
China Agri-Industries	606 HK	BUY	8.7
Ruchi Soya	RSI IN	BUY	105.8
Formosa Chem & Fibre	1326 TT	BUY	97.2
Mewah (new)	MII SP	BUY	1.2

Note: As of 14 January, 2011. Prices in local currency
Source: Bloomberg, Nomura

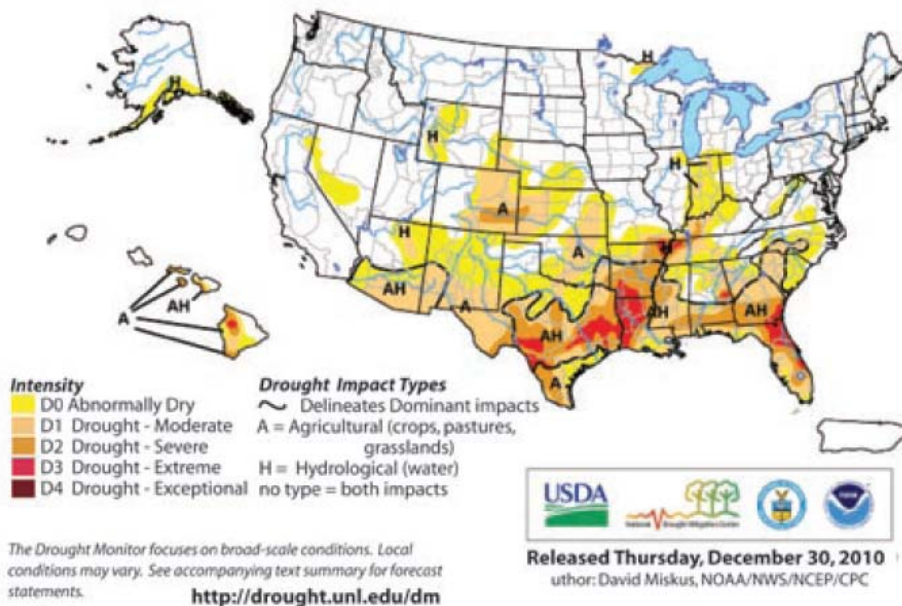
Erratum: First paragraph (Action), changed to "release of a bullish USDA crop forecast and bullish stock-to-consumption data" from "recent of bullish USDA crop forecast and stock-to-consumption data". We apologise for any inconvenience caused.

**Any authors named on this report are strategists unless otherwise indicated.
See the important disclosures and analyst certifications on pages 14 to 17.**

Drilling down

Exhibit 1. US Drought Monitor (30 December, 2010)

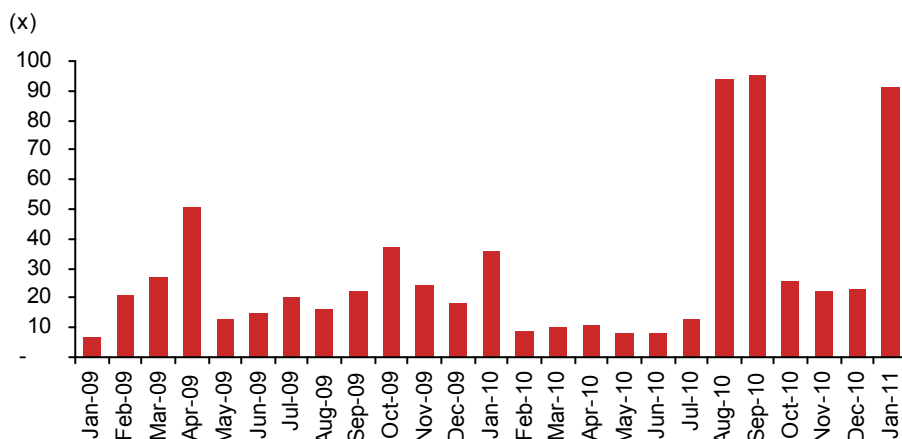
The US is experiencing a harsh winter in the north and a drought in the south. This is almost a repeat of the 2007-08 La Niña



Source: <http://drought.unl.edu/DM/MONITOR.html>, Browning, Nomura International (HK) Ltd – Investment Strategy

Exhibit 2. Number of times the word "food riots" appears in the press

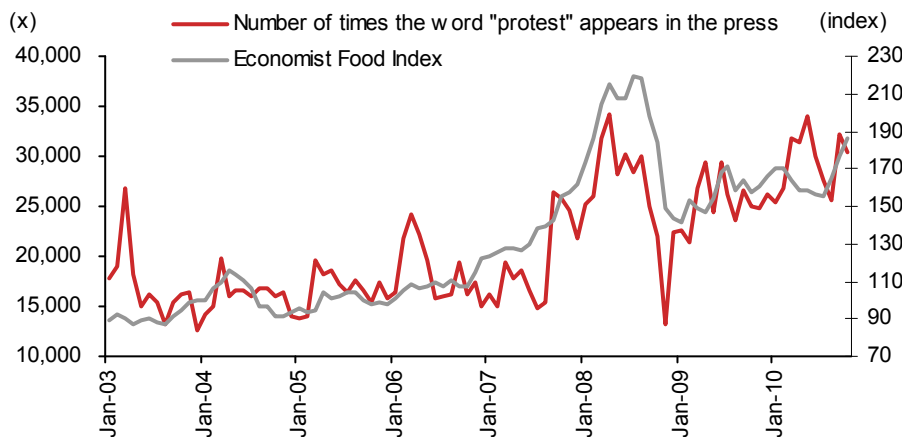
Increasing frequency of food riots...



Source: Factiva, Nomura International (HK) Ltd – Investment Strategy

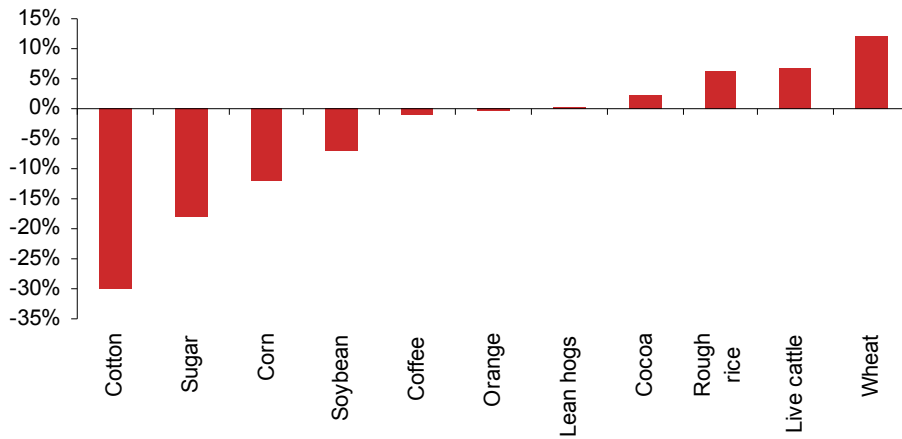
Exhibit 3. Number of times the word "protest" appears in the press vs Economist Food Index

... as food prices rise



Source: Factiva, Datastream, Nomura International (HK) Ltd – Investment Strategy

Exhibit 4. Selected commodities: year-end future – near-month future

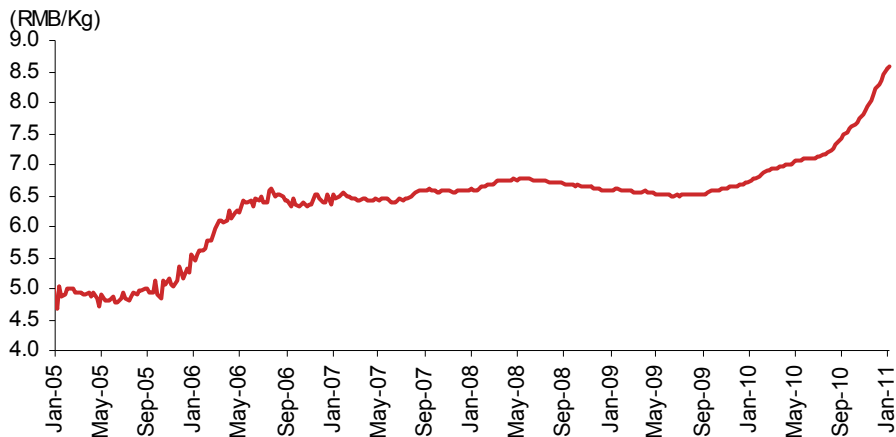


Half of the soft commodities traded on futures markets have gone into a backwardation, a sign of increasing tightness

Note: year-end future as of December 2011, except for rice, soybean and oranges (as of November 2011), sugar (as of October 2011) and rubber (as of June 2011)

Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

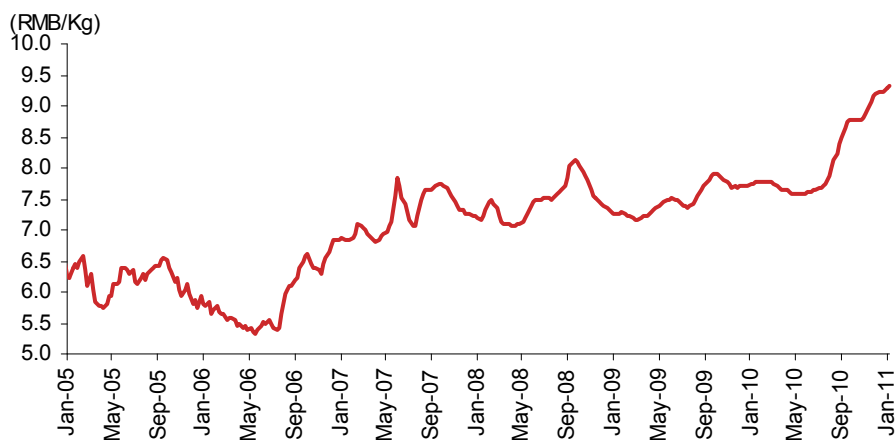
Exhibit 5. China agricultural product price: retail, sugar, white granulated sugar



Product prices are rising...

Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 6. China agricultural product price: retail, egg species, egg

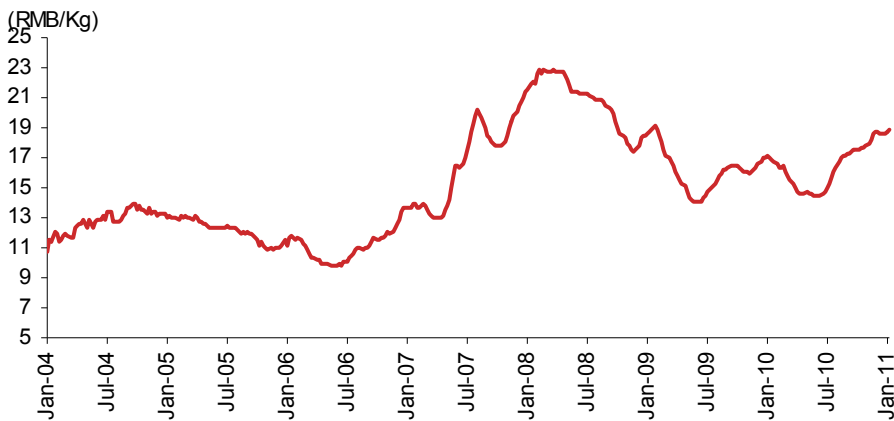


... for a whole series...

Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 7. China agricultural product price: wholesale, meat, fresh pork

... of foods



Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 8. New Zealand: export price indices for top-10 commodities with highest price rise (% y-y)

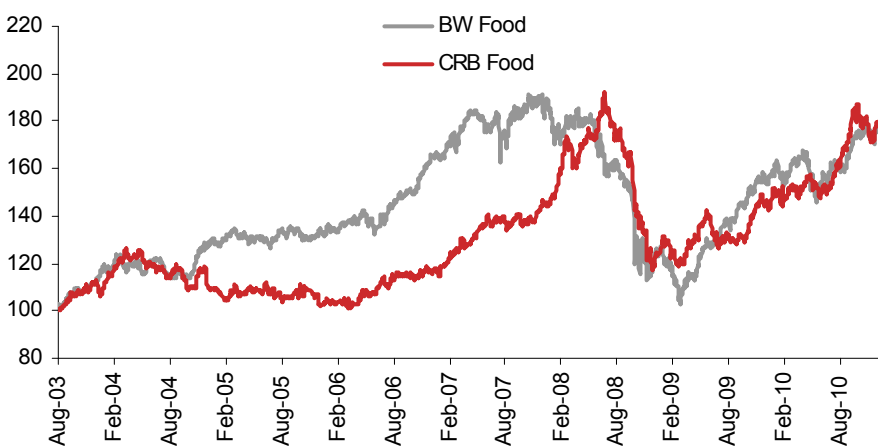
New Zealand's terms of trade are the best in history. The current export environment is without precedent

Commodity	(% y-y)	(% q-q)
Butter	101%	4%
Skimmed and buttermilk powder	55%	9%
Milk powder	52%	9%
Cheese	36%	0%
Casein	34%	5%
Hides, skins and furskins - raw	33%	9%
Leather and tanned/dressed furskins	29%	-5%
Wood pulp	21%	-3%
Wool	15%	2%
Iron and steel	15%	-2%

Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

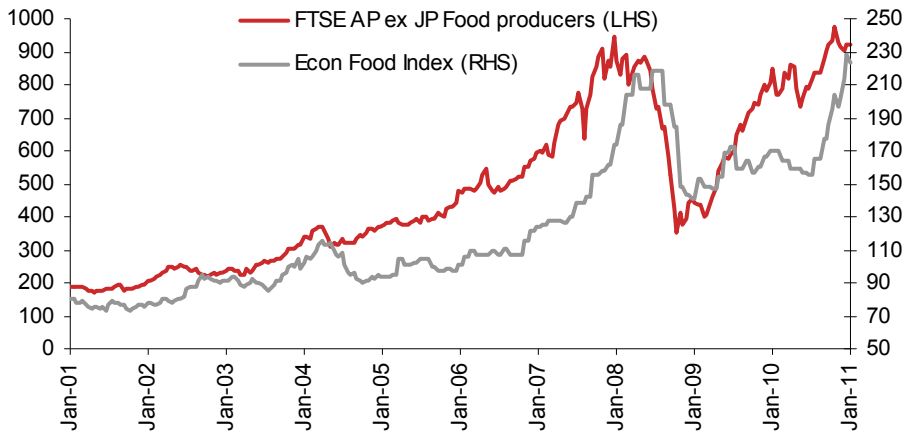
Exhibit 9. Bloomberg World Food Producers Index and CRB Food Index

The underlying equities have recently slipped in their performance against their products



Source: Bloomberg, Nomura International (HK) Ltd – Investment Strategy

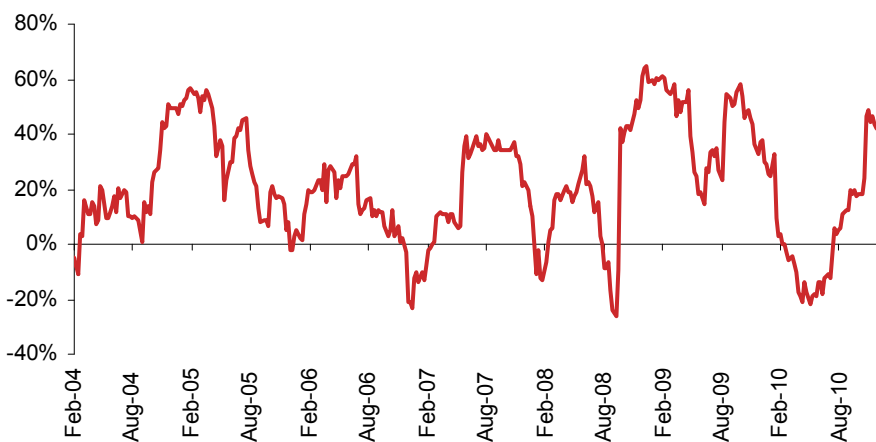
Exhibit 10. FTSE AP ex JP Food Producers Index and Economist Food Index



However, it is still much better than the 2007-08 rally

Source: Datastream, Nomura International (HK) Ltd – Investment Strategy

Exhibit 11. Correlation: Bloomberg World Food Index vs CRB Food Index

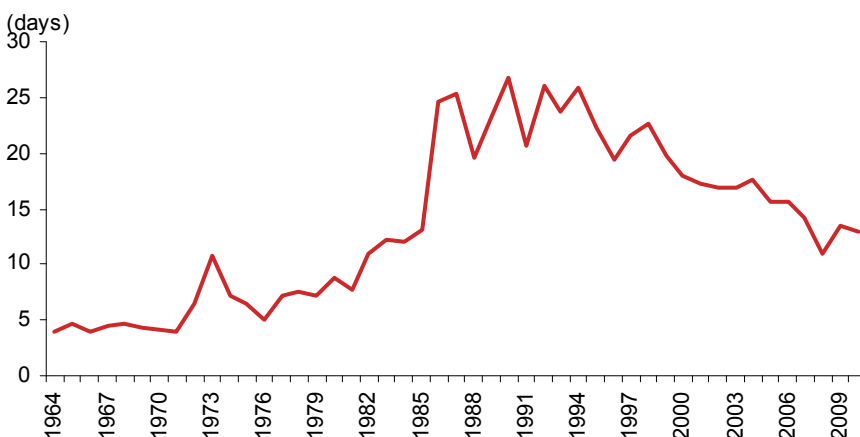


We have used a 25-week correlation between food prices and equity markets

Note: Correlation over six months of weekly returns

Source: Datastream, Nomura International (HK) Ltd – Investment Strategy

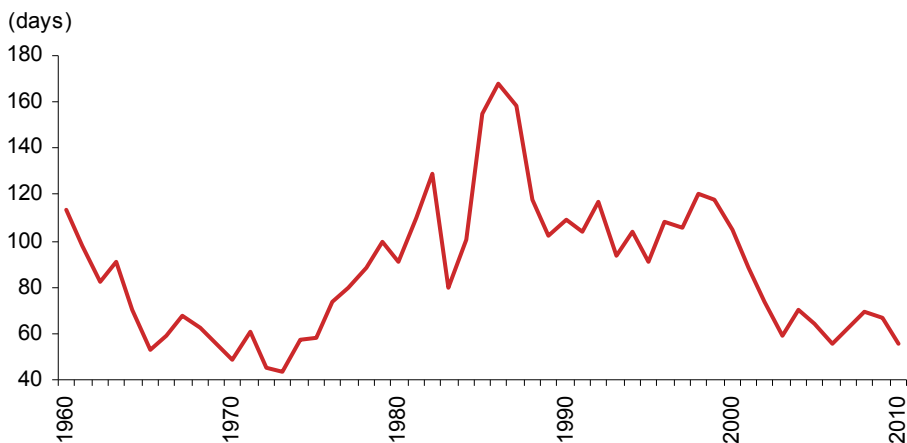
Exhibit 12. Global inventory coverage (days): soybean



Recent USDA reports conclude that the stock-to-consumption ratio...

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

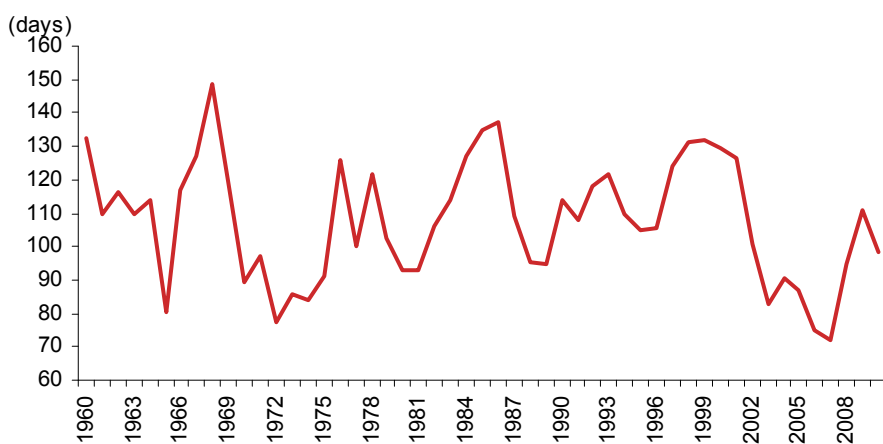
Exhibit 13. Global inventory coverage (days): corn



... for the majority of crops under their coverage...

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

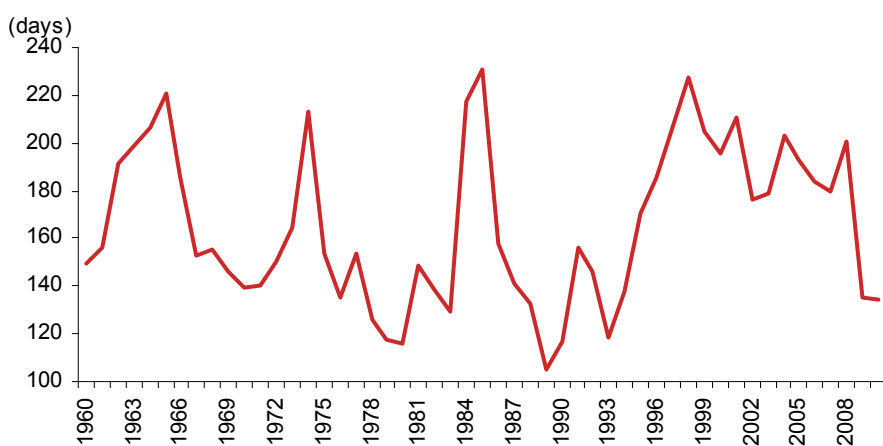
Exhibit 14. Global inventory coverage (days): wheat



... is still falling...

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

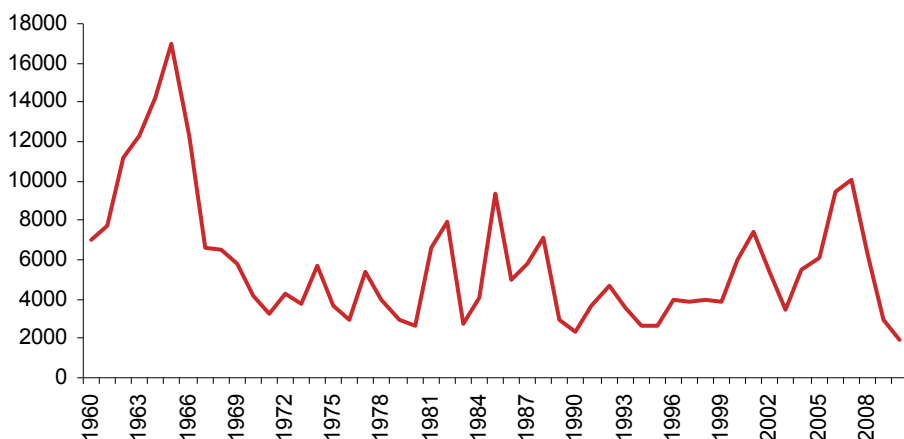
Exhibit 15. Global inventory coverage (days): cotton



... with the collapse...

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

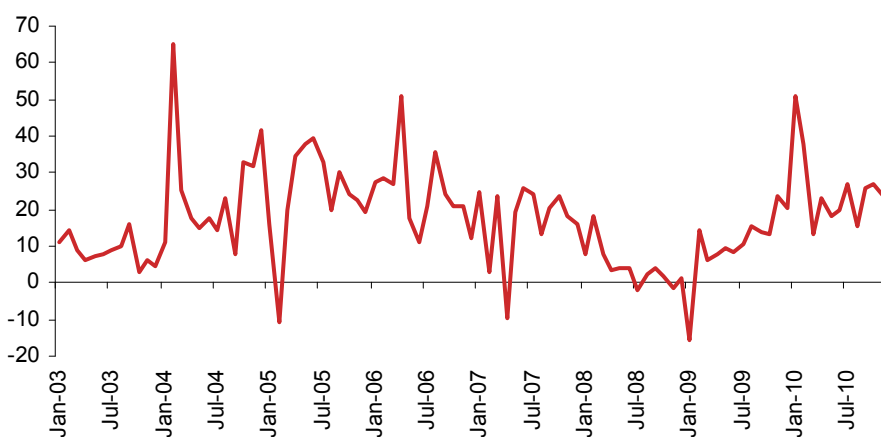
Exhibit 16. US cotton ending stocks (1000 480 lb bales)



...in cotton stocks being the most prominent

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

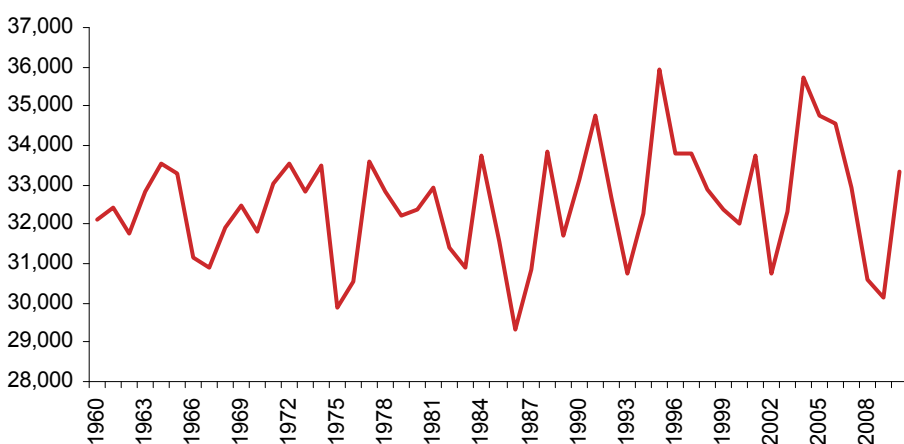
Exhibit 17. China: cotton cloth production (% y-y)



Paradoxically, demand for cotton products continues to grow

Source: CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 18. World: area under cotton harvesting (1,000 HA)

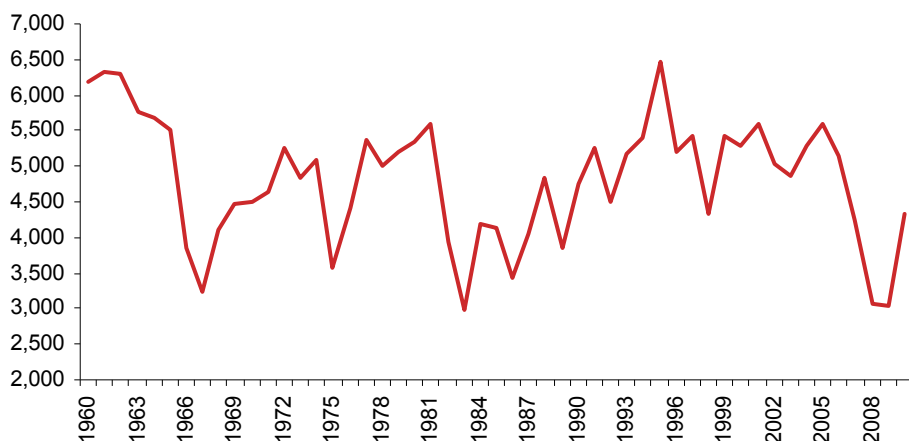


A close eye needs to be kept on the amount of acreage...

Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 19. US: area under cotton harvesting (1,000 HA)

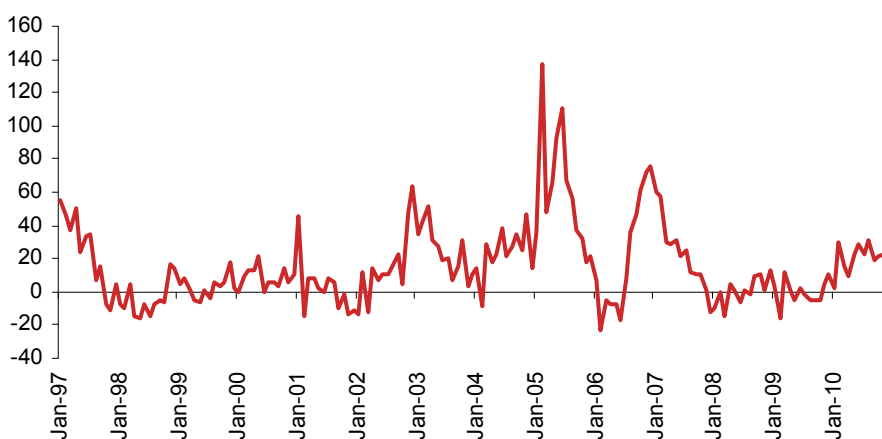
... under coverage



Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 20. US imports from China: textiles and articles thereof (% y-y)

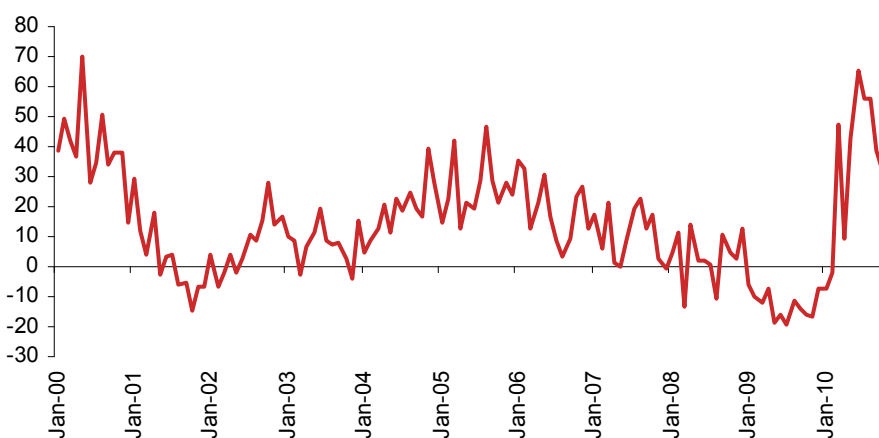
The US and...



Source: CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 21. EU imports from China: textiles and articles thereof (% y-y)

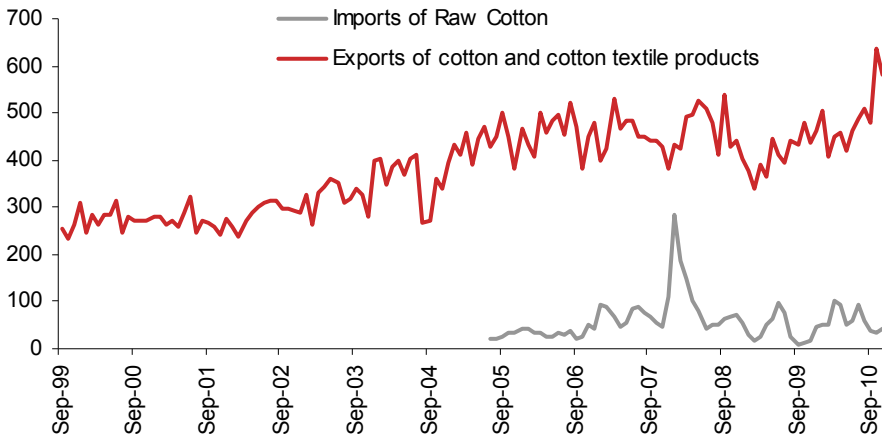
...the EU are likely to experience some mild upswing in inflation...



Source: CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 22. Pakistan: trade in cotton and products (US\$m)

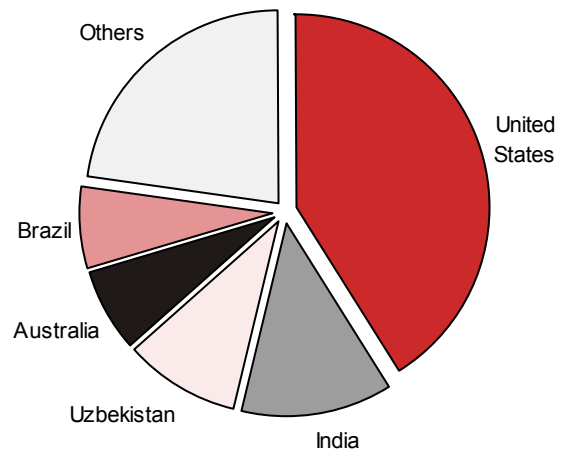
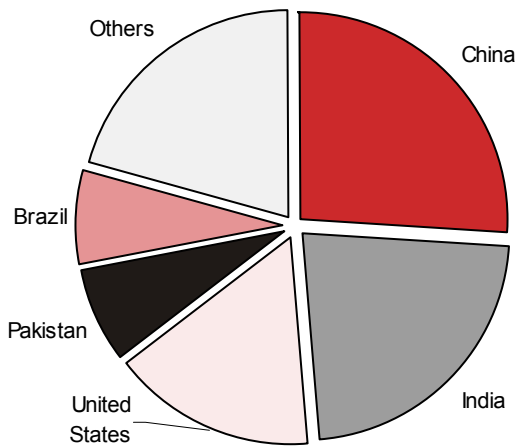
... as higher prices caused by the floods in Pakistan are passed on



Source: CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 23. Global cotton production: top 5

Exhibit 24. Global cotton exports: top 5

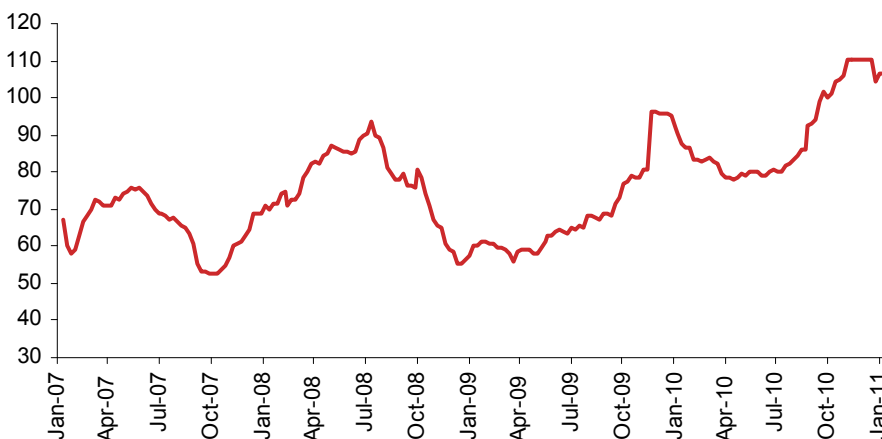


Source: USDA, Nomura International (HK) Ltd – Investment Strategy

Source: USDA, Nomura International (HK) Ltd – Investment Strategy

Exhibit 25. US: ethanol average rack prices (US\$/bbl)

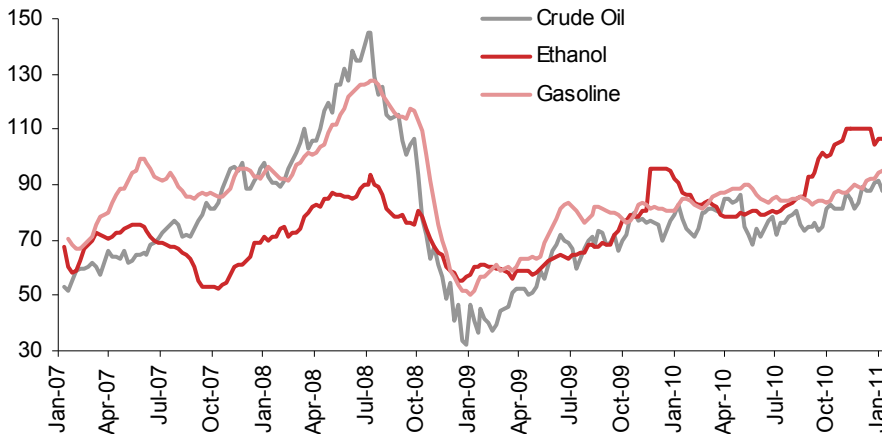
Almost unseen has been the sharp rally in ethanol. Higher corn prices are pushing through into higher ethanol just...



Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 26. US: crude oil vs ethanol vs gasoline (US\$/ bbl)

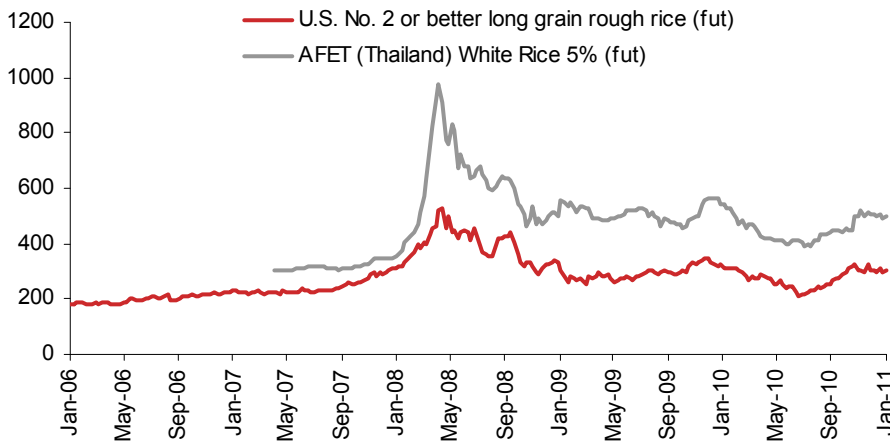
... as oil prices touch US\$100/bbl



Note: WTI Cushing crude, ethanol average rack prices, daily national average gasoline prices (regular, uNleaded)
 Source: Bloomberg, Nomura International (HK) Ltd – Investment Strategy

Exhibit 27. Rice futures: US and Thailand

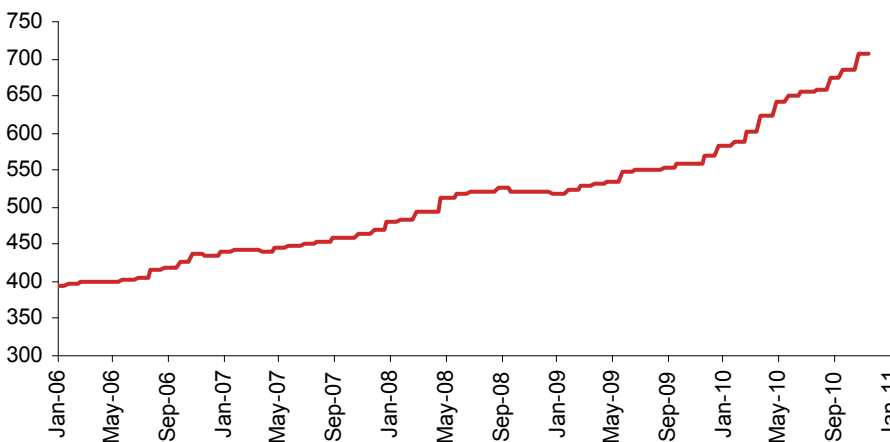
To date Asia has been spared the harsh pain of extreme food prices since rice has not moved up



Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 28. China: standard rice retail price (US\$/tonne)

However, in China, food prices have nearly doubled over the past five years



Source: Bloomberg, CEIC, Nomura International (HK) Ltd – Investment Strategy

Exhibit 29. Soft commodities basket: price performance

Name	Ticker	Inception	Absolute change in US\$ (%)						
			1D	1W	1M	3M	6M	1Y	YTD
China Green	904 HK	23-Nov-09	(2.8)	10.2	20.0	9.3	9.8	(18.1)	12.7
United Phosphorus	UNTP IN	23-Nov-09	(4.4)	(4.0)	(7.2)	(21.4)	(9.2)	(8.2)	(12.2)
Noble Group	NOBL SP	23-Nov-09	(0.2)	2.8	12.6	17.2	47.3	17.4	7.5
JSR corp	4185 JP	30-Apr-10	(0.4)	4.1	16.5	21.9	14.8	(1.3)	11.5
Sri Trang Agro	STA TB	15-Jun-10	(3.6)	(1.1)	4.1	35.1	95.0	637.6	4.3
Khon Kaen Sugar	KSL TB	15-Jun-10	(2.5)	3.9	4.5	29.7	32.8	3.4	12.3
China Yurun Food	1068 HK	8-Sep-10	0.9	0.5	5.2	(7.6)	7.4	15.3	7.4
China Agri-Industries	606 HK	8-Sep-10	0.2	(2.2)	(0.7)	(19.1)	(1.1)	(24.9)	2.0
Ruchi Soya	RSI IN	22-Sep-10	(0.7)	(3.0)	4.4	(24.7)	1.7	10.9	(13.8)
Formosa Chem & Fibre	1326 TT	14-Oct-10	1.1	6.0	2.2	26.2	50.8	50.3	(0.8)
Mewah	MII SP	17-Jan-11	0.6	(1.1)	11.6	-	-	-	10.1

Note: as of 14 January, 2011

Source: Bloomberg, Nomura International (HK) Ltd – Investment Strategy

We re-launched our soft commodities basket on 23 November 2009

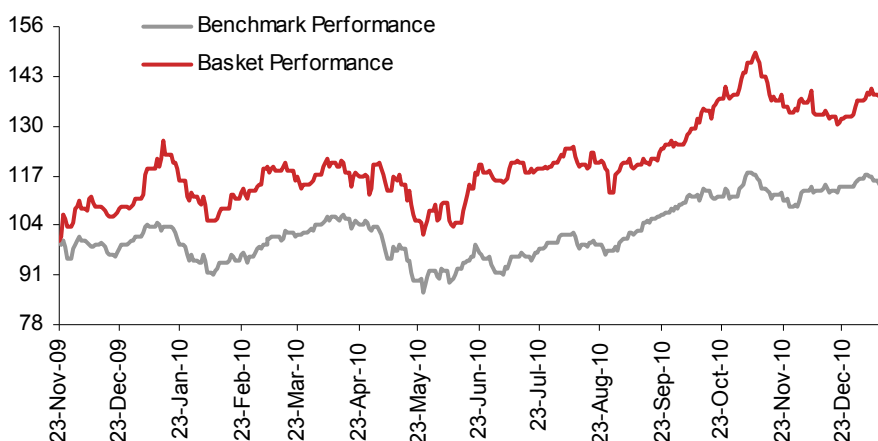
Exhibit 30. Soft commodities basket: consensus valuation

Name	Ticker	Price (local)	P/E (x)		P/BV (x)		Dividend yield (%)		ROE (%)	
			FY1F	FY2F	FY1F	FY2F	FY1F	FY2F	FY1F	FY2F
China Green	904 HK	8.5	10.4	8.4	1.8	1.5	2.6	3.2	19.6	21.1
United Phosphorus	UNTP IN	153.2	10.4	8.5	1.9	1.6	1.5	1.9	18.9	19.4
Noble Group	NOBL SP	2.3	22.5	15.1	3.1	2.7	1.3	1.7	15.2	19.1
JSR corp	4185 JP	1,716.0	16.0	14.2	1.6	1.5	1.9	1.9	10.1	10.9
Sri Trang Agro	STA TB	39.0	10.6	11.5	3.4	2.5	2.8	2.7	36.1	24.5
Khon Kaen Sugar	KSL TB	14.0	23.3	19.9	2.1	2.0	1.8	2.2	8.4	10.0
China Yurun Food	1068 HK	27.2	21.0	17.6	3.8	3.3	1.4	1.6	23.0	21.5
China Agri-Industries	606 HK	8.7	12.6	10.6	1.8	1.6	1.9	2.3	14.9	15.8
Ruchi Soya	RSI IN	105.8	14.4	11.5	1.9	1.6	0.7	0.8	14.8	16.8
Formosa Chem & Fibre	1326 TT	97.2	11.9	11.0	1.9	1.8	6.7	6.8	18.6	18.8
Mewah	MII SP	1.2	15.5	13.3	2.7	2.3	0.0	0.0	23.5	18.9

Note: as of 14 January, 2011.

Source: Bloomberg, Nomura International (HK) Ltd – Investment Strategy

We close Wilmar...

Exhibit 31. Soft commodities basket: performance

Note: as of 14 January, 2011. Benchmark is MSCI Asia Pacific ex Japan

Source: Bloomberg, Nomura International (HK) Ltd – Investment Strategy

... and add Mewah International


Exhibit 32. Recent strategy reports


Date	Title
14-Jan-2011	Asia's looming energy crisis http://www.nomura.com/research/GetPub.aspx?pid=412351
11-Jan-2011	The changing shape of Asian leverage http://www.nomura.com/research/GetPub.aspx?spid=7341
4-Jan-2011	Asia's soft commodity crunch (XXII) http://www.nomura.com/research/GetPub.aspx?spid=7306
4-Jan-2011	Australia Strategy - Sunny side up http://www.nomura.com/research/GetPub.aspx?spid=7302
3-Jan-2010	The inflation genie, China's Lewisian turning point and bond market jitters (II) http://www.nomura.com/research/GetPub.aspx?spid=7297
14-Dec-2010	The inflation genie, China's Lewisian turning point and bond market jitters http://www.nomura.com/research/GetPub.aspx?spid=7259
6-Dec-2010	Deflation, inflation and the return of the productive economy http://www.nomura.com/research/GetPub.aspx?spid=7226
20-Nov-2010	Greater China Inflation: a double whammy http://www.nomura.com/research/GetPub.aspx?spid=7183
17-Nov-2010	China: an inflationary surprise (IX) and the Engel coefficient http://www.nomura.com/research/GetPub.aspx?spid=7162
15-Nov-2010	Quarter-end, Quarterbacks and a Hail Mary Pass (II) http://www.nomura.com/research/GetPub.aspx?spid=7151
12-Nov-2010	China: an inflationary surprise (VIII) http://www.nomura.com/research/GetPub.aspx?spid=7144
10-Nov-2010	The Rebirth of the Silk Road (IV): Mongolia http://www.nomura.com/research/GetPub.aspx?spid=7130
9-Nov-2010	Return of the Spice Route (XII): Mauritius http://www.nomura.com/research/GetPub.aspx?spid=7125
8-Nov-2010	Malaysia: 1992 all over again! (III) http://www.nomura.com/research/GetPub.aspx?spid=7119
4-Nov-2010	It will be alright on the night! http://www.nomura.com/research/GetPub.aspx?pid=400443
3-Nov-2010	Greater China Inc (VIII) http://www.nomura.com/research/GetPub.aspx?spid=7096
1-Nov-2010	Nothing to declare http://www.nomura.com/research/GetPub.aspx?spid=7089
27-Oct-2010	The Rebirth of the Silk Road (III) http://www.nomura.com/research/GetPub.aspx?spid=7066
26-Oct-2010	Rare earths: China's indigenous precious metal (III) and the uranium mystery http://www.nomura.com/research/GetPub.aspx?spid=7058
25-Oct-2010	Greater China Inc. (VI) and China A shares an underground bull market (III) http://www.nomura.com/research/GetPub.aspx?pid=6660
20-Oct-2010	China A shares: an underground bull market (VI) http://www.nomura.com/research/GetPub.aspx?pid=396481
19-Oct-2010	The return to plastic tupperware and polyester clothing http://www.nomura.com/research/GetPub.aspx?spid=7018
18-Oct-2010	Quarter-end, Quarterbacks and a hail Mary pass http://www.nomura.com/research/GetPub.aspx?spid=7005
14-Oct-2010	China A shares: an underground bull market (V) http://www.nomura.com/research/GetPub.aspx?spid=6990
14-Oct-2010	A crude equation http://www.nomura.com/research/GetPub.aspx?spid=6988
11-Oct-2010	Rare earths: China's indigenous precious metal (II) http://www.nomura.com/research/GetPub.aspx?spid=6956
7-Oct-2010	Absence of the normal (IV) http://www.nomura.com/research/GetPub.aspx?pid=394163
5-Oct-2010	Musical Chairs (III) http://www.nomura.com/research/GetPub.aspx?spid=6921
4-Oct-2010	Rare earths: China's indigenous precious metal http://www.nomura.com/research/GetPub.aspx?spid=6910

Source: Nomura International (Hong Kong) Limited – Investment Strategy

Investible themes and baskets

Nomura's investible themes and baskets are listed on Bloomberg at **NMRA<Go>** for global ideas and **NMCS<Go>** for Asian recommendations. We show live tradable prices for these themes.

NMRA	N194 n Index NMRA										
	<p>Nomura International 25 Bank Street London E14 5LS United Kingdom +44 207 103 9988</p>										
Delta One Equities											
<table border="1"> <tr><td>Swap Products</td></tr> <tr><td>1) Long/Short Style Baskets</td></tr> <tr><td>2) Directional Style Baskets</td></tr> <tr><td>3) Custom Basket Swaps</td></tr> <tr><td>4) NMSS Sector Swaps</td></tr> <tr><td>5) Other Index Swaps</td></tr> </table>	Swap Products	1) Long/Short Style Baskets	2) Directional Style Baskets	3) Custom Basket Swaps	4) NMSS Sector Swaps	5) Other Index Swaps	<table border="1"> <tr><td>Certificate & Access Products</td></tr> <tr><td>11) Middle East p-Notes</td></tr> </table>	Certificate & Access Products	11) Middle East p-Notes		
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Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published prior to 30 October 2008

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A **'Buy'** recommendation indicates that upside is between 10% and 20%.

A **'Neutral'** recommendation indicates that upside or downside is less than 10%.

A **'Reduce'** recommendation indicates that downside is between 10% and 20%.

A **'Sell'** recommendation indicates that downside is more than 20%.

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