Palm & Lauric Oil
Price Outlook 2010

With special reference to India

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Ladies and Gentlemen

At the outset I must thank **Bursa Malaysia** for accommodating my paper today so that I can fly back to London tonight. As some of you may know, I am speaking on Palm Oil at the **NIOP Annual Meeting** next Monday. It is a mark of the growing importance of Palm Oil in the U S market that NIOP are focussing on Palm Oil this year. I am sure tribute must be paid to the excellent promotional work in North America undertaken by **MPOC.**

I also wish to congratulate **Bursa Malaysia on its JV with the Chicago Mercantile Exchange.** Palm Oil is now by far the biggest vegetable oil in terms of absolute tonnage as well as in terms of world trade. Yet investors are wary about entering this market because of its size and liquidity. Palm Oil futures need to be more broad-based and available to a much bigger worldwide audience. This JV between BMD and CME will give it that platform.

POC continues to be the Biggest Vegetable Oil Conference in the world and it should keep getting bigger with this initiative of the BMD and the CME.

Background

Someone told me you need guts to speak each year at POC and make price forecasts. I corrected him to say, you need guts and lots of humility. I have to say upfront that my prognosis on price behaviour as outlined here last year did not verify. I was far too bearish and failed to appreciate the powerful effect of the fiscal stimulus unleashed by finance ministers in most countries. My only consolation was that most other forecasters also got it wrong.

I am thrilled by the success of monetary policies rolled by eminent central bankers and finance ministers. As you know, I have admired central bankers like Messrs Greenspan and Bernanke and had faith in their ability to manage growth and prosperity in the world economy. The events of 2007 and 2008 shook the faith of many people in the ability of these central bankers but 2009 and 2010 must reinstate that faith. I believe easy money policies and growth oriented measures were the right prescription for the world economy and we are very fortunate that these measures were undertaken and with success

It is always easy for people, usually with hindsight, to condemn growth oriented measures as being inflationary. We must realise that there is no greater curse to young people than unemployment and recessions always bring unemployment. That is why it is better to tolerate some inflation rather than drive the economy into deflation or stagnation in the name of some lofty ideal like Zero Inflation. The government of China has the right idea to maintain high rates of growth even if it means tolerating some inflation.

The Palm oil complex was blessed by the fact that 2 of the fastest growing big economies of the world, **China and India grew strongly in 2009 and created the conditions for a strong recovery in commodity prices. The year 2010 also looks promising.**

The Oscars

Let me take up the Annual Pat on the Back.

At this time last year, when most of us were in the depths of bearishness, one major player was almost alone on the long side. They were confident that CPO was bound to go higher, touching 2300 Ringgits by April and then moving on 2500 and beyond. Their research and their S&DS justified much stronger markets than most of us were contemplating. Again recently, when most of the commercials and analysts were in the depth of bearishness, they stood steadfast in their bullish stance. I do not have to tell you that they have benefitted enormously from their astute reading of the market. There is no player in our industry that does his research with the thoroughness of this company, that analyses markets with the sensitivity of this team and that estimates production as accurately as they do. **Friends, for the second time in the last 3 years, it is my pleasure to shower kudos on the team at Cargill Singapore for getting the market spot on in very difficult conditions.**

We can also congratulate ourselves that as an industry we have come through a difficult period in very good health. We have suffered defaults, even from sovereign government owned companies, and yet most of our companies are in better shape than ever. During 2009, **Wilmar** became by market capitalisation the biggest agricultural company in the world, dwarfing all of the mighty A,B,C and D. At least 3 other Indonesian companies have aspirations to be the next Wilmar and we all know that **IOI** and **Sime Darby** also have big ambitions. Competition is no bad thing and the palm oil industry epitomises the vitality and vigour of South East Asia. I believe the next phase will be consolidation. It will be very interesting to see if managements and owners will have the **Wil** to turn **Gold en**to **Diamonds** !

INDIA

Let us now discuss the S&Ds for India which became in 2008-9 the largest importer of palm products.

As is well known, the South West Monsoon in 2009 was anaemic and the Kharif crops in India were adversely affected. This has led to shortfalls in the production of Groundnuts, Soybeans and Rice Bran. It is also painfully clear that Indian agriculture is in the throes of Stagnation and the Indian government has basically run out of ideas. India will gradually become an importer of all foodstuffs and India's rural population will either remain poor or more likely, migrate to the cities. The recent heated debate in India on the acceptance or otherwise of BT Brinjal was from my perspective most depressing.

On the other hand, the rest of the Indian economy did remarkably well. The National Rural Employment Guarantee Scheme has given security of income to the poorest of the rural population and this has led to strong consumption growth of basic foodstuffs. Vegetable oils have benefitted from this additional demand. During 2008-09, low prices and the abolition of import taxes on unrefined oil, enabled consumption to register a once-in-a-lifetime growth of almost 13 % or about 2 million tonnes. Almost single-handedly, India salvaged the fortunes of the vegetable oil industry in the fourth quarter of 2008 and Q1 of 2009. The election results of 2009 gave India a strong and stable government which is committed to further reform and growth.

Let us first look at India's production of vegetable oil.
(Oil year November to October)

INDIA's PRODUCTION

000 tonnes	2009-10	2008-09	2007-08	2006-07	2005-06
	Estimates	Actual	Actual	Actual	Actual
Soybean oil	1050	1200	1445	1280	1140
Cotton oil	1050	1000	1050	920	755
Gn oil	450	650	900	580	950
Sun oil	450	500	550	580	620
Rape oil	1900	1800	1700	2150	2250
Sesame oil	160	150	150	120	125
Coconut oil	400	390	380	380	400
RiceBranoil	700	740	720	680	660
Others	250	250	250	225	200
Total	**6410**	**6680**	**7145**	**6915**	**7100**

This year crushing parities in India are uniformly negative and at the end of the 2009-10 season, India is likely to carry forward a large stock of oilseeds. The Spread between popular local oils like Mustard oil and imported oils like RBD Palm Olein must narrow if local oils are to move into consumption.

We must also congratulate the Indian government on keeping open the export of oil meals and of not undertaking any rash measure to ban such exports despite considerable pressure.

Let us now look at INDIA's CONSUMPTION

000tonnes	2009-10	2008-09	2007-08	2006-07	2005-06
	Estimates	Estimates	Actual	Actual	Actual
Soybean oil	1950	2150	2100	2550	2850
Cotton oil	1050	1000	1000	900	720
Gn oil	450	650	880	580	1020
Sun oil	950	1050	580	780	680
Rape oil	1850	1800	1650	2150	2250
Sesame oil	160	150	150	120	160
Palm oil	7390	6530	5090	3925	3150
Laurics	650	600	600	600	450
RiceBranoil	700	740	720	680	650
Others	250	250	225	225	350
Total	**15400**	**14920**	**12995**	**12510**	**12280**
Pop.Mlns	1175	1160	1140	1120	1100
Per cap kg	**13.11**	**12.86**	**11.40**	**11.17**	**11.16**

I expect per capita consumption to continue to grow by about 4% and my projection of 2009-10 imports is based on that assumption. So long as RBD Olein in wholesale is available at prices below Rupees 50,000, demand and consumption will continue to grow smartly.

We can now study INDIA's S&Ds **000 tonnes**

INDIA's S&D for	**2006-7**	**2007-8**	**2008-9**	**2009-10**
Opening Stock	850	750	1025	1250
Production	6,915	7,145	6,680	6410
Imports	**5,615**	**6,300**	**8,640**	**9090**
Consumption	12,510	12,995	14,920	15400
Exports	120	175	175	150
Ending Stocks	750	1025	1250	1200

It will be seen that India will continue to be the largest market for Palm oil in the next year.

INDIA's IMPORTS of Vegetable Oil

000 tonnes	2009-10	2008-09	2007-08	2006-07	2005-06
Soya	900	990	750	1335	1770
Palm	7390	6770	5270	3665	3000
Sun	500	590	30	200	90
Laurics	250	240	200	200	240
Others	50	50			
Vanaspati			50	215	300
Total	**9090**	**8640**	**6300**	**5615**	**5400**

As always, I acknowledge the assistance of the Solvent Extractors Association and in particular Mr G G Patel of GGN Research for their help with Indian statistics.

Having discussed India I now turn to the Global Scenario

GLOBAL SCENARIO

The most important feature of 2010

It has been debated as to what is going to be the biggest price making factor of 2010. Some say it will be the latest EPA guidelines on RFS2 recently announced in the USA. Some say it will be events in the Sugar market in India and in Brazil. For my money, the biggest price making factor is much closer to home – here in South East Asia and it is the effect of the El Nino.

This current El Nino is milder and kinder than several past ones. Yet it will have a profound effect on CPO production in the next 12 months.

I believe 2009-10 will be remembered as the year when Supply became the dominant price making factor. There does not appear to be any unusual factor on the Demand side. Bio diesel demand is expected to be stronger but it is Supply which is under pressure. Let us first look at the state of various oilseeds. For the purpose of

this conference, I have analysed the S&Ds for the period April 10 to March 11 and have not used the normal period October to September.

Soya: The world has to face the prospect of additional 30 to 35 million tonnes of soybeans being produced in South America. This would normally be a bearish factor but this year that bearishness will be confined to beans and to meal. All the additional beans cannot possibly be crushed and most observers are calculating oil production based on an additional crush of about 10 to 12 million tonnes. I have been conservative and calculated basis 12 million additional crush. The next U S crop to be planted in May 2010 is yet uncertain. I have assumed a normal crop on acreage which will be substantially the same as this year.

Rapeseed: The EU crop this year is higher than expected. The Canola crop in Canada is smaller than last year and so is the Rapeseed crop in Australia. The crop in China is better and China is also carrying large stocks. Greater demand for Rapeseed oil for bio diesel will result in a bigger crush. Therefore, Rape oil will go some way towards alleviating the tight S&Ds of world vegetable oil.

Sunflower seed: The Argentine sunseed crop has not come up to expectation and may even be termed a severe disappointment. Coupled with lower production in the EU and also in Ukraine and in Russia, the production of Sun oil will be lower than the previous year and its outlook is Bullish

Palm oil: The biggest problem looms in palm oil. At the Gapki Conference in Bali on 4 December 2009 I forecast my deep reservations about 2010 CPO production. My prediction that Malaysian CPO production in 2010 will be LESS THAN that of 2009 was greeted with scepticism. The passage of time is proving me right and there are now more and more people who believe that in 2010, for the first time in history, Malaysian CPO production will fall for 2 years in a row. Last year at this conference, I predicted correctly that 2009 production would at best equal that of 2008 and could be marginally lower.

My reasons for pessimism on Malaysian production are already well know – the prevailing El Nino, the government's replanting scheme and most importantly, the biological cycle of Malaysian palm trees.

By an unusual sense of timing, it looks as though the El Nino induced damage to Malaysian Cpo will be felt in Q3 and Q4 of 2010, just as the biological cycle turns from High to Low. As I have said before, we started a new Biological High Cycle in June 2009 in some parts of Malaysia and in September 2009 in other parts. History teaches us that these cycles stretch from 8 to 11 months. So by July 2010 the High Cycle will be exhausted and the trees will be in need of rest. Just at that time the effect of El Nino will also be felt. Therefore, it will be very interesting to see CPO production in the July to December period. At this stage my estimate for Malaysian CPO production for 2010 is around 17.2 million tonnes.

I expect a similar situation to prevail in Indonesia too. Expansion of acreage will mitigate this effect. Overall I expect CPO production in Indonesia to rise by only 1 million tonnes.

Therefore, we can summarize **Global Incremental Supply** as follows

000 tonnes	**Apr 08 to Mar 09**	**Apr 09 to Mar 10**
Soya oil	- 1500	+ 2000
Rape oil	+ 1800	+ 1300
Sun oil	+ 2000	- 1000
Gn oil	- 200	- 200
Cotton oil	- 200	- 200
Palm oil	+ 1500	+ 800
Lauric oils	+ 100	+ 200
Total Increase	**+ 3500**	**+ 2900**

World Demand

Last year, World Demand expanded by about 4.5 million tonnes only. This year the IMF expects the world economy to grow by close to 3 percent. Big population countries like China, India, Indonesia and Brazil will grow more strongly. Therefore, we must expect Food Demand for vegetable oil to expand by about 4 million tonnes at current price levels.

The new and enhanced mandates being put in place in Argentina, Brazil and several other countries plus the new RFS 2 guidelines in USA make this a bullish year for bio diesel demand. Conservatively, I expect bio diesel demand to expand by at least 2 million tonnes.

Therefore, for 2010 we are faced with Expected Demand growth of 6 million tonnes against Expected Supply growth of just 2.9 million tonnes.

This situation is not tenable and something must give during the year. My guess is that prices must rise in order to make bio diesel uncompetitive in some discretionary markets and to curb food demand. It also means that Oil Share will have to rise dramatically in order to stimulate the crushing of soybeans.

To summarize the world Incremental Supply and Demand

Thus the **Global Incremental S&Ds** can be seen as

000 tonnes	Apr 08 to Mar 09	Apr 09 to Mar 10
Supply	+ 3,500	+ 2,900
Demand	+ 4,500	+ 6000

Before I speak on Price Outlook, I wish to touch on 3 other points.

Indonesia: I am disappointed that the government of Indonesia has re-imposed the dreaded Export Tax on palm products. It is even more disappointing that the Indonesian industry has stopped protesting about it.

China: As I said earlier, China continues to grow strongly and her consumption of vegetable oils will continue to register normal growth. China's imports of soybeans as well as of palm oil will continue to be strong. Any revaluation of the Yuan will be to the benefit of imports and commodity prices. May I also at this stage congratulate the **Dalian Commodity Exchange** on its stupendous success the Palm Oil contract.

RSPO

Since the beginning of 2010 the sale of Green Palm Oil certificates has picked up strongly and this is an excellent development.

At the same time, the talk of a moratorium on further expansion of palm plantations in Indonesia can have dangerous consequences. The industry is not yet ready to expand productivity on such a scale as to eliminate the need for expansion of land area. The world is not able to expand acreage of soft seeds or soybeans. The world needs expanding palm oil production. As can be seen in 2010, if Indonesian production does not expand by 2 to 3 million tonnes annually, there is a mis-match between demand and supply resulting in higher prices. The RSPO needs to consider this consequence very carefully. Are we going to restrict vegetable oil consumption to the Rich Few and deny it to the Many Poor? Is this what we mean by caring for the Planet and its People or shall we re-phrase it to say – We care for a Part of this Planet and a Portion of its People?

The RSPO has done a commendable job so far but it needs to proceed cautiously in measured steps.

PRICE OUTLOOK

This year my presumption is that we shall have to live with a Strong Dollar for the next few months. At the same time, investment money is coming back into commodities and this will, to some extent, blunt the effects of a stronger Dollar.

I am presuming that Crude oil prices will be trading in the range of US$ 70 to 95 for most of the year. We cannot rule out a spike in prices if Economic Sanctions are implemented against Iran. The probability of this is quite high given the fact that Russia has almost signalled its readiness to enforce sanctions.

I believe the palm market has a comfortable cushion of stocks for the next few months and this will be helped further by large soybean oil supplies coming out of South America. That is why, for the period March to July 2010 I expect BMD CPO futures to trade in the range of 2600 to 2800 Ringgits only.

I believe the most bullish period will be the Second Half of 2010 and Q1 of 2011. Let me explain why.

As I have said, we must expect a Strong Dollar for the next few months. A strong Dollar acts as a calming influence on commodity prices. The Dollar Strength is not a result of fundamentals. It is a technical consequence and therefore, like recent Dollar rallies must last between 6 and 10 months only. After that the dire fundamentals of the Dollar must take over. If that theory holds, and since the latest Dollar Rally stated in mid November 2009, we can expect the Dollar to begin to weaken around July 2010. That would be the time for commodity prices to move ahead strongly.

As I explained before, I expect Palm production shortfalls to be felt most in the Second Half of 2010. The peak soya oil flow from South America should be in the period May to August. Therefore, I expect BMD CPO futures post July to scale new heights in the range 2800 to 3200 Ringgits in order to ration demand.

I expect **Lauric oils** to outpace Palm because this El Nino appears to be affecting Philippines more severely. I expect Coconut Oil in Rotterdam to regain its premium over Palm Kernel oil and to trade initially at around USD 1000 cif Rotterdam and then to gradually rise to US$ 1300.

The spread between CPO and Soya oil will remain very narrow in 2010. I expect Soya oil to trade in the next few months around current levels of US$ 850 to 900 FOB South America and in Q4 to rise over US$ 1000 FOB. Traders should not get too bearish about the big Soybean harvests in South America. The fact of big crops is already in the market. Any surprise is likely to come from the bullish side and not otherwise. We must also presume that the tense stand- off between the farmers and the government in Argentina will not get worse and result in strike.

I expect Sunflower oil to begin to move ahead shortly and to command a spread of about US$ 100 over Soya in South America and over US$ 200 in the EU.

I expect Rapeseed oil to trade between Sunflower oil and Soya oil in Europe.

CONCLUSION

The Worldwide S&Ds for vegetable oil are very bullish for the second half of the year. The job of the market is to prevent things from getting so tight. That can be done by expansion of plantings, which is easier said than done or by curbing demand through higher prices. I hope my analysis today has given you food for thought and will enable you to prepare yourselves for the tightness ahead. I wish you all great success and good trading in the coming months.

My next Price Outlook will be in Dubai at Globoil International on 25 April.

Good Luck and God Bless

(My thanks as usual to my friend Alex Wells, the Walking Matrix, for his help in crunching the numbers)