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RISING FOOD PRICES SPUR INVESTMENT OPPORTUNITIES

Surging global food prices and the search for diversification against equity and fixed interest market downturns have prompted investors to turn their attention to commodities as a separate asset class, according to a new QIC report.

Fixed interest and equity markets assets are traditionally seen as diversifiers but there are times when their movements coincide. This is evidenced by the recent market downturn which has seen fixed interest and equity markets fall at the same time.

The QIC Red Paper on Rising Food Prices found that while prices for energy, metal, bulk resources and other commodities have hit record highs in recent months, food prices have risen more than 80% since 2005.

This has been led by a 130% surge in wheat prices and a 190% increase in corn and rice prices, despite recent financial market turmoil and a slowdown in advanced economies.

QIC Managing Director Strategy Adriaan Ryder said these factors had fuelled a growing interest in commodities as a separate asset class and the benefits that exposure to commodities created in an investment portfolio.

“Commodities provide diversification benefits as historically they have a low correlation to other asset classes and a high correlation to inflation,” he said.

“Historically at the early stages of a recession or economic downturn when both shares and bonds have been negative, returns on commodities have been positive. In fact during the last year of equity and bond market volatility, the commodities exposure we have provided to clients has been one of their best performing asset classes.

“QIC takes an innovative approach and gains exposure to commodities through commodity futures.

“Research has shown that a long-term risk premium can be accessed in commodities via the futures market.

“Commodity futures allow producers of commodities to obtain a known future price for the value of their outputs. This futures price is usually below the expected market price at harvest time due to the risk being taken on by the owner of the commodity future. This creates the opportunity for a profit to be made by selling the commodity at a market value which is higher than the futures price.

“The current strong food prices increases the chance of generating investment returns through commodity futures.”

The QIC Red Paper also predicted that the outlook for food prices over the medium-term was for prices to remain above their longer-term average.

Mr Ryder said there remained a number of factors driving food price increases.

“There is continued strong global demand for commodity staples including wheat, corn and rice, particularly in developing countries. Surging oil prices have seen an increase in demand for biofuel production, leading to higher prices for crops such as corn,” he said.

“When you combine these factors with drought-impacted harvests and rising inflation it explains the sharp increases in food prices. Prices for wheat, corn and rice are expected to remain high relative to their historic average over the next decade, albeit somewhat below the recent peak.”

QIC is one of Australia’s largest institutional fund managers with more than \$80 billion currently under management for its Australian and overseas clients.

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