

## STOP, DROP AND ROLL?

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The next issue of the *ANZ Commodity Price Index* is scheduled for release on: 5 February 2008 at 3pm.

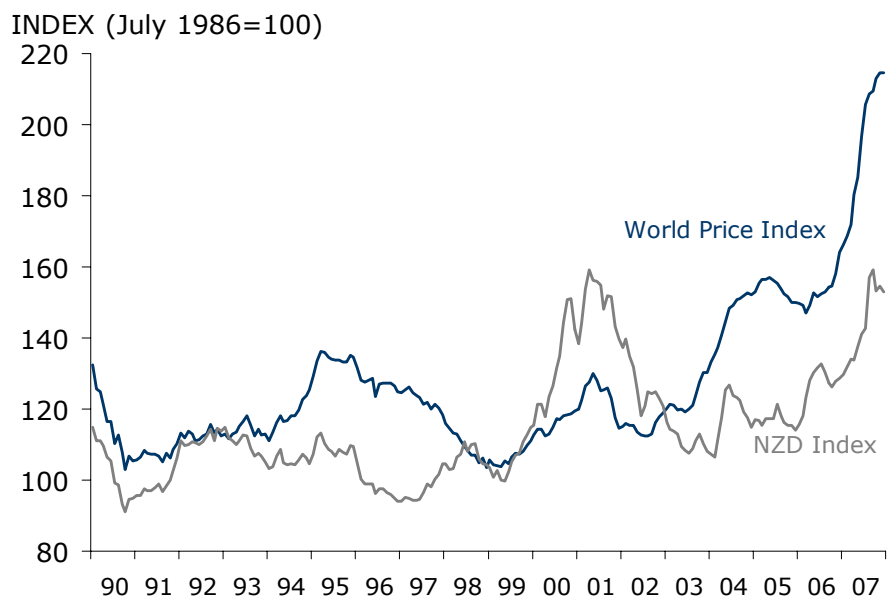
**The recent surge in NZ's key commodity prices has lost momentum.** The 18-month span of improving commodity prices came to an end in December, with the ANZ Commodity Price Index unchanged in the month. Nonetheless, while the momentum may have been lost, it is difficult to go past the elevated level of prices, which remains 37 percent above the previous cyclical peak.

**Pelt prices recorded the largest rise in December.** Seven commodities recorded a rise in prices in the month of December, one series was unchanged and five registered price declines. Pelt prices recorded the largest increase, jumping 22 percent from a month earlier – to sit at a five-year high. Wool and log prices increased 1.5 percent in the month, wood pulp and seafood posted a 1.3 percent rise and venison and kiwifruit prices rose 0.6 and 0.5 percent, respectively.

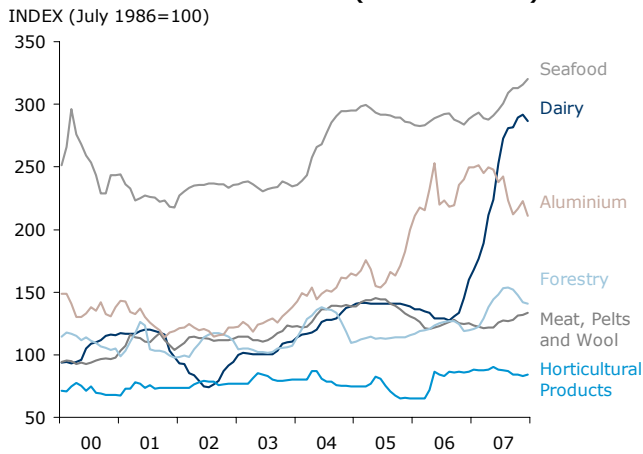
**International dairy prices have eased.** The dairy sub-group of the Commodity Price Index recorded a 1.8 percent drop – the first monthly decrease in the component since August 2006. Price declines were also noted in aluminium, sawn timber, beef and lamb. Aluminium prices dropped 5.1 percent and sawn timber 2.4 percent. The price of beef dropped 1.7 percent and lamb prices eased 0.7 percent.

**A rise in the value of the kiwi dollar dampened the NZD Index.** The New Zealand dollar appreciated against all of our major trading partners. The kiwi dollar lifted 0.7 percent relative to the greenback, but the largest appreciation was with Australia, where the NZ dollar rose 3.7 percent in value. Consequently, when converted to NZ dollars, the ANZ NZD Commodity Price Index eased 0.9 percent in December.

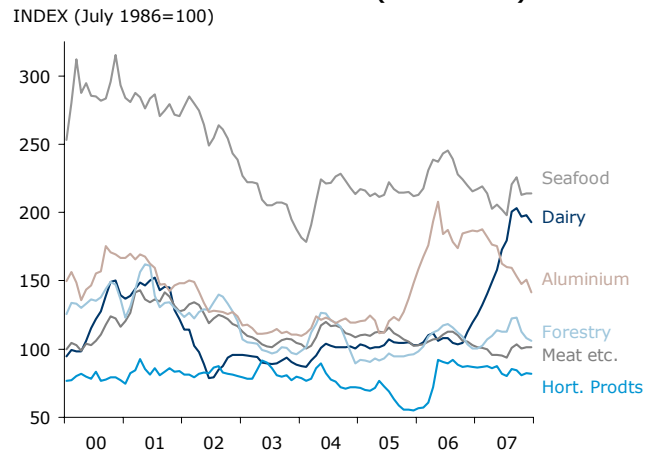
### ANZ COMMODITY PRICE INDEX



SUB-GROUP INDICES (WORLD PRICES)



SUB-GROUP INDICES (NZD PRICES)



Both aluminium and forestry prices have eased over the second half of 2007. The two series are key inputs to the transport, packaging and construction industries, and as such are bell-wether indicators to gauge the pulse of the global economy. As demand from several economies has begun to cool, so has the price of these commodities. However, the latest fall in dairy prices can't be put down to the same cause. The surge in dairy prices last year was in response to the Australian drought and several European countries phasing out export subsidies; combined with the bio-fuels euphoria. The latest reversal in international dairy prices has been in response to increased supply from other dairy producing countries, as producers increase production levels to take advantage of the increased dairy prices. Moreover, after such a huge surge, it is perhaps not surprising to see some retracement.

Is the retracement in dairy prices the start of a correction? Clearly the supply-demand dynamics for dairy look better than historically – indicating the uplift contains a structural element. However, an analysis of the price trends of several food commodities over 40 years shows that, on average, booms in food commodity prices are followed by a median decline of 50 percent from the peak. While it is still early days to start drawing such comparisons, it is an interesting calculation, nevertheless. And a 50 percent reduction off the August/September 2007 dairy commodity peaks still leaves dairy prices at a historically high level, in USD terms.

	World Price Index	Monthly % Change	Annual % Change	NZ\$ Index	Monthly % Change	Annual % Change
<b>Dec-02</b>	<b>118.9</b>	0.8	3.7	<b>120.8</b>	-1.8	-13.5
<b>Dec-03</b>	<b>130.3</b>	0.1	9.6	<b>108.2</b>	-1.8	-10.4
<b>Dec-04</b>	<b>152.1</b>	-0.3	16.7	<b>115.0</b>	-2.1	6.3
<b>Dec-05</b>	<b>149.9</b>	-0.1	-1.4	<b>114.0</b>	-1.1	-0.9
<b>Dec-06</b>	<b>164.0</b>	3.8	9.4	<b>128.7</b>	0.7	12.9
<b>Jun-07</b>	<b>196.7</b>	6.3	29.8	<b>141.2</b>	2.7	7.4
<b>Jul-07</b>	<b>205.7</b>	4.6	35.1	<b>142.7</b>	1.1	7.5
<b>Aug-07</b>	<b>208.6</b>	1.4	36.3	<b>156.9</b>	10.0	20.3
<b>Sep-07</b>	<b>209.4</b>	0.4	35.7	<b>159.3</b>	1.5	25.1
<b>Oct-07</b>	<b>213.1</b>	1.8	37.8	<b>153.2</b>	-3.8	21.5
<b>Nov-07</b>	<b>214.7</b>	0.8	35.9	<b>154.5</b>	0.8	20.9
<b>Dec-07</b>	<b>214.7</b>	0.0	30.9	<b>153.1</b>	-0.9	19.0

Commodity Price Index weights are based on contributions to merchandise exports. Weights for the 2007 year are: Wool 0.048; Beef 0.103; Lamb 0.137; Venison 0.015; Skins 0.027; Dairy 0.333; Apples 0.018; Kiwifruit 0.044; Logs 0.032; Sawn Timber 0.056; Wood Pulp 0.034; Seafood 0.068; Aluminium 0.085.

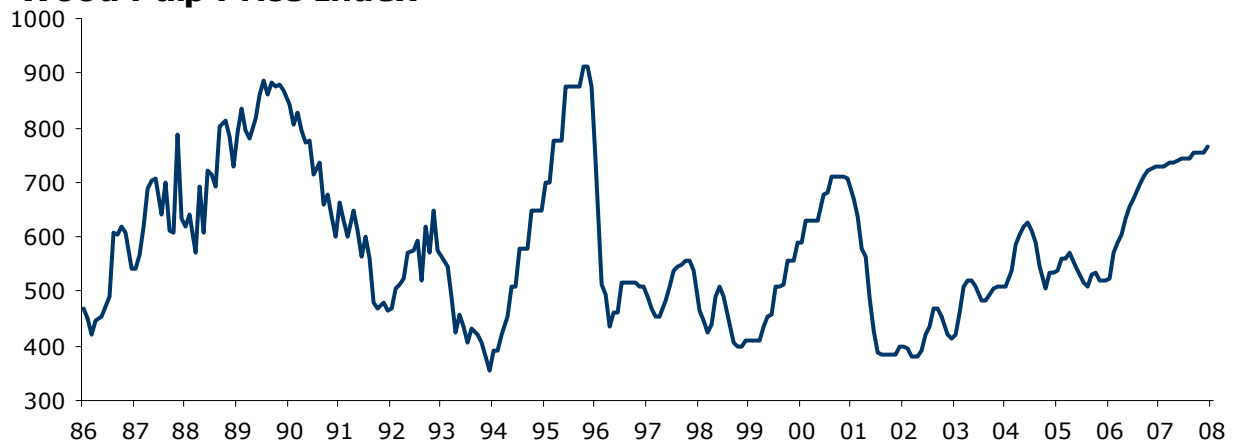
## Featured Commodity: WOOD PULP

International wood pulp prices have been steadily climbing over the past two years. This went hand-in-hand with increasing world-wide demand. But with a slow down in the global economy looming, it is unlikely that this trend will continue.

Wood pulp is the key ingredient of the manufacture of paper and paperboard. Pulp is derived by breaking down the fibrous cellulose contained in wood (or any plant material) into its component fibres. The method of breakdown is done by either a mechanical or chemical process. The later option is known as the 'kraft' process. The kraft process involves the use of caustic sodium hydroxide and sodium sulphide to extract the lignin from the wood fibre. The name of this process is derived from German word kraft, meaning strong. It was first developed 120 years ago and now is used for about 80 percent of the worldwide production of paper.

The process of paper making, in simplistic terms, involves mixing wood pulp (or other vegetable fibres) with water. This slurry is spread, making a thin layer of matted fibrous strands. The water is then removed, and the layer of fibres remaining is essentially a crude form of newsprint. Other materials may be added to give the paper a better surface or extra strength.

### Wood Pulp Price Index



Source: ANZ

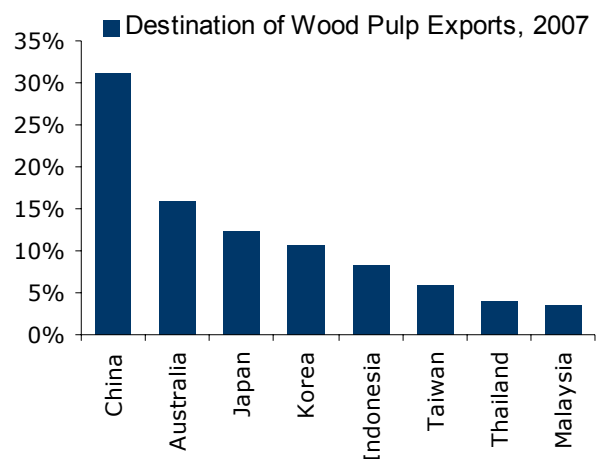
International demand for wood pulp rose by almost 6 percent last year, reaching a new record high in the amount of wood pulp traded globally (about 40 million tonnes). Consequently, the price of wood pulp has mirrored this increased demand, with prices increasing unabated for the past two years. The level posted last month eclipses the previous high set in 2000, to hit a twelve-year high. Common with other commodities, increased demand from an expanding Chinese economy has been a factor of the recent rise in wood pulp prices. In the past seven years, China's demand for wood pulp has more than doubled to 16 percent of world-wide trade.

Industry sources expect the outlook for wood pulp prices to weaken from here. The factors behind this are three-fold. Firstly, an increase in supply is in the pipeline, due to new capacity in Latin America and China over the next two years. Secondly, demand in China looks to have peaked. And lastly, a slow down in the US and European economies will result in a slackening in demand for print advertising, which in turn will have a negative effect on the demand for printing and writing paper.

In the twelve months to June 2007, wood pulp exports totalled NZ\$663 million, which accounted for 1½ percent of New Zealand's total merchandise exports. Wood pulp represents a fifth of all forestry (logs, timber, pulp and paper) related exports.

China took nearly a third of all of New Zealand's wood pulp exports in the year to June, followed by Australia, Japan and Korea. The Asian rim takes a large proportion of our wood pulp exports, with the APEC region receiving 97 percent of all wood pulp from NZ.

Wood pulp exports to China grew by 62 percent last year, and accounted for 11 percent of our exports to that nation. By comparison, a similar import penetration figure for Australia and Japan is only between 1 to 2 percent.



Source: ANZ, Statistics NZ

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