

# Newsletter

from Rural Funds Management Ltd

YOU MAY FIND THIS ARTICLE BY DAVID BRYANT TO BE OF INTEREST

## **THEN & NOW:**

**HOW TECHNOLOGY DRIVES FARMLAND PRODUCTIVITY AND INCOME GROWTH**

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YOU MAY FIND THESE ARTICLES MEANINGFUL IN THE CONTEXT OF YOUR PERSONAL INVESTMENT PORTFOLIO

## **RURAL FUNDS GROUP UPDATE**

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## **STOCKBANK UPDATE**

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**Photo 1: The Dust Bowl**  
Photographer unknown. Caption reads: "Buried machinery in barn lot, Dallas, South Dakota, during the Dust Bowl, an agricultural, ecological and economic disaster in the Great Plains region of North America in 1936." 13 May 1936 <sup>1</sup>

# Then & Now:

How technology drives farmland productivity and income growth

**David Bryant, Managing Director**

This article uses three photos to make an important point about agriculture: during the past century technology has driven massive productivity gains. It then uses a chart of 125 years duration to make an important point about agriculture in the context of investment: productivity gains support capital growth and increasing investment income.

The three photos were taken during the US Dust Bowl, the period of drought in the US, where crops failed, topsoil eroded and 3.5 million people were forced to move in one of the biggest migrations of mankind. These are powerful photos that capture the pathos of this environmental and economic tragedy.

Photo 1 shows buried machinery and illustrates how the combination of over ploughing and drought brought about an environmental catastrophe. Looking closely at Photo 1, it is possible to gauge the depth of the windblown soil that has enveloped the farm yard of this anonymous and now ruined farm, located in one of the States occupying the Great Plains of the USA. It is also possible to see the scale and power of the machinery used during that period. There are horse drawn carriages buried in more than a metre of sand and in the background a pasture mower and a tiny seeder probably two metres in width. What is not visible is the cause of this catastrophe: the tractor.

<sup>1</sup> Source: [http://en.wikipedia.org/wiki/File:Dust\\_Bowl\\_-\\_Dallas,\\_South\\_Dakota\\_1936.jpg](http://en.wikipedia.org/wiki/File:Dust_Bowl_-_Dallas,_South_Dakota_1936.jpg)



**Photo 2: Economic Refugees**

**Photo by Dorothea Lange. Her caption reads: "On Arizona Highway 87, south of Chandler. Maricopa County, Arizona. Children in a democracy. A migratory family living in a trailer in an open field. No sanitation, no water. They came from Amarillo, Texas. Pulled bolls near Amarillo, picked cotton near Roswell, New Mexico, and in Arizona. Plan to return to Amarillo at close of cotton picking season for work on WPA" [Works Progress Administration, a New Deal government agency]. November 1940**

Tractors represent one of the greatest technological revolutions to occur in agriculture. Labour shortages during World War One drove the emergence of these machines. Sales then exploded in the 1920's when Henry Ford discounted his Fordson tractor from \$625 to \$395. Ignorance combined with over-ploughing powered the destruction of soil structure over the Great Plains. This caused the vast wind erosion that came with the inevitable onset of drought in 1934.

Photo 2 provides an image of children and the raw poverty confronted by families burdened by the low commodity prices of the depression and a drought that lasted six years. This image and the third, were taken by Dorothea Lange, a woman who revolutionised photo journalism through powerful photos of the plight of the poor. A biographer of Lange used these words to capture her art and the character of these bankrupt American farmers: "Lange saw America as a worthy work in progress, incomplete and capable of better. By portraying her subjects as nobler than their current conditions, she emphasized the strength and optimism of our national character."<sup>2</sup>

The children in Photo 2 are a reminder of just how much we have all prospered since those times. These kids probably had a similar life expectancy to all kids born

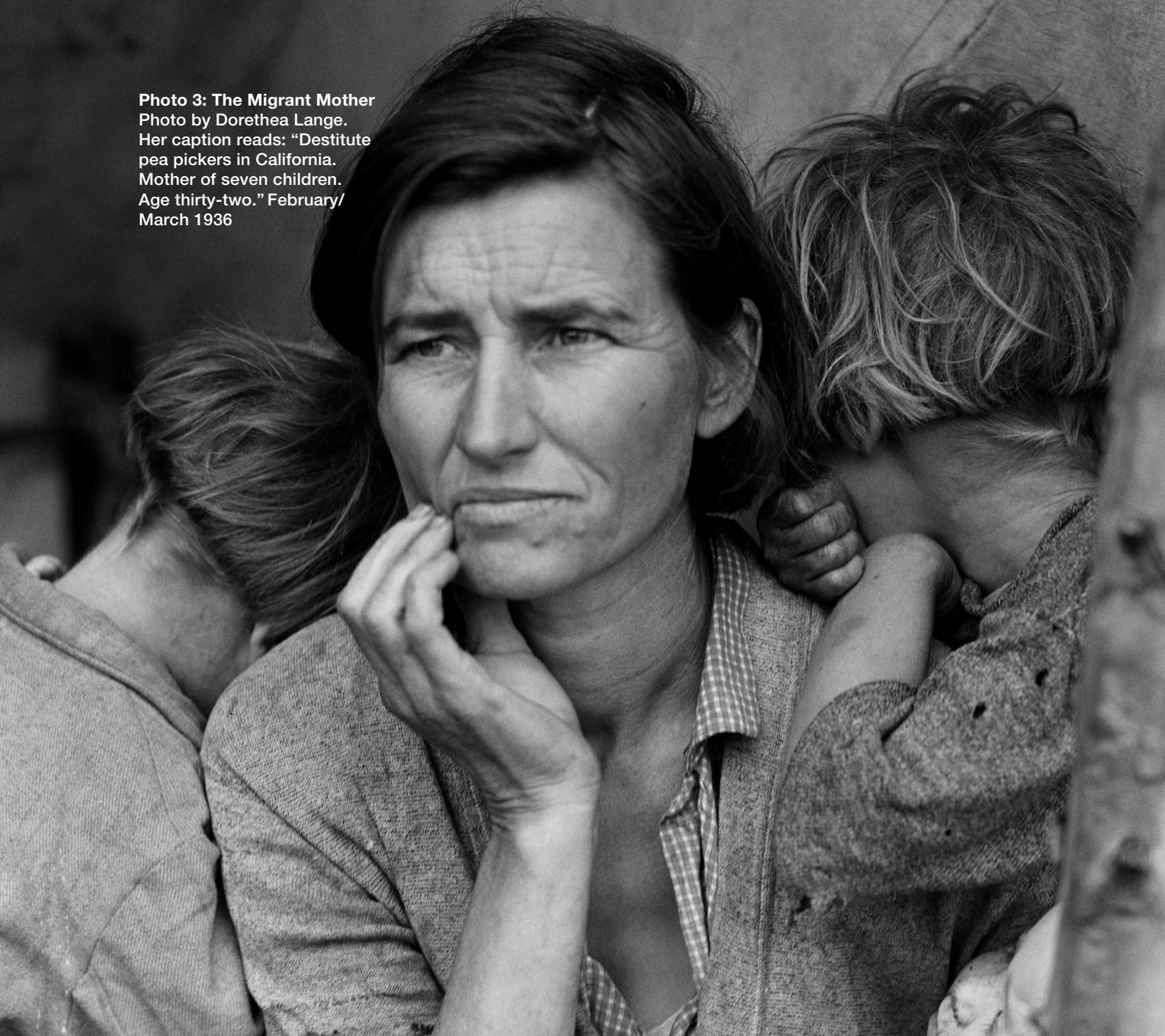
at that time in countries like Australia, the United Kingdom and Western Europe - today's developed economies. These kids, like our parents, survived infant mortality rates that were higher than those of third world countries today. Though they were unlikely to starve, they had to survive numerous life threatening illnesses that have today been virtually eradicated due to technologies such as immunisation.

Photo 3 is an image of Florence Owens Thompson, a refugee from Oklahoma, taken in California when as a mother of seven she worked picking vegetables and cotton. This photo became an iconic image of America's rural depression, and is known as the 'Migrant Mother'. It is probably its subtle suggestion of the future that most appeals to that optimistic nation. And in the case of its agricultural economy, this was not misplaced.

Since these photos were taken, vast improvements have occurred in agriculture that will ensure the mistakes so clearly depicted will not reoccur. Soil conservation farming techniques quickly emerged to prevent erosion and while tractors have increased in size, they are used with GPS precision. But improvements in agriculture have not been limited to a recovery from drought or a cyclical depression. Other technological strides have occurred such as the introduction of fertilisers, plant breeding and genetic

<sup>2</sup> Gordon, L., 2009, Dorothea Lange, A life beyond limits, W.W. Norton and Company, New York

**Photo 3: The Migrant Mother**  
Photo by Dorothea Lange.  
Her caption reads: "Destitute  
pea pickers in California.  
Mother of seven children.  
Age thirty-two." February/  
March 1936



modification to reduce the use of pesticides. These three productivity revolutions have in turn contributed to vast improvements in the prosperity of farmers so as to ensure the cause of the mass bankruptcies of the 1930's will not be repeated.

Technology feeds into the farming economy in more subtle ways as well. The children in the photos today would be immunised, literate and healthy. Their parents would have access to the internet, cars that travel faster and with fuel consumption ten times greater. Their family farming business has now been stable for several generations due to better access to credit, the ability to hedge their production and the tertiary educations they have received in farming practices. Technology then, has driven continuous gains in the productivity of their businesses and like us, the quality of our lives.

The chart presented as Figure 1 measures the economic impact that these productivity improvements have brought

for the business of farming. It provides three data series over the past 125 years: inflation, agricultural commodity prices, and the change in farm values. The data is from the US because Australian data over such a long period is not available - though it displays similar correlation since records began in 1978. Finally the chart presents rolling ten year periods, so that it is easier to see the major trends.

The chart shows that there is a high correlation between each of the three data series over the period. A chart characterised by three great waves, with inflation and agricultural commodities increasing and then feeding an increase in land values. Each of these waves is followed by a period of slower growth and occasionally decline, as economic factors conspire to prevent either uncontrolled inflation or unaffordable food prices. At the right of the chart there is evidence that we are now well into a fourth wave of increasing prices and perhaps now a period of slower price growth.

There is some hard data that should be highlighted from this chart. Firstly, during the 125 year period, US inflation rose at an average rate of 2.9% per annum while agricultural commodity prices rose by 2.6% - therefore marginally declining in real terms. Secondly, US farm land values rose by 4.3% per annum during the period.

A surprising feature of this data is the much greater increase in farm values compared to commodity values. If you bought \$1 worth of say wheat in 1890, it would be worth around \$25 today. But if instead you had bought \$1 of agricultural land, it would be worth \$192 today. What caused the big difference between commodity prices and land values?

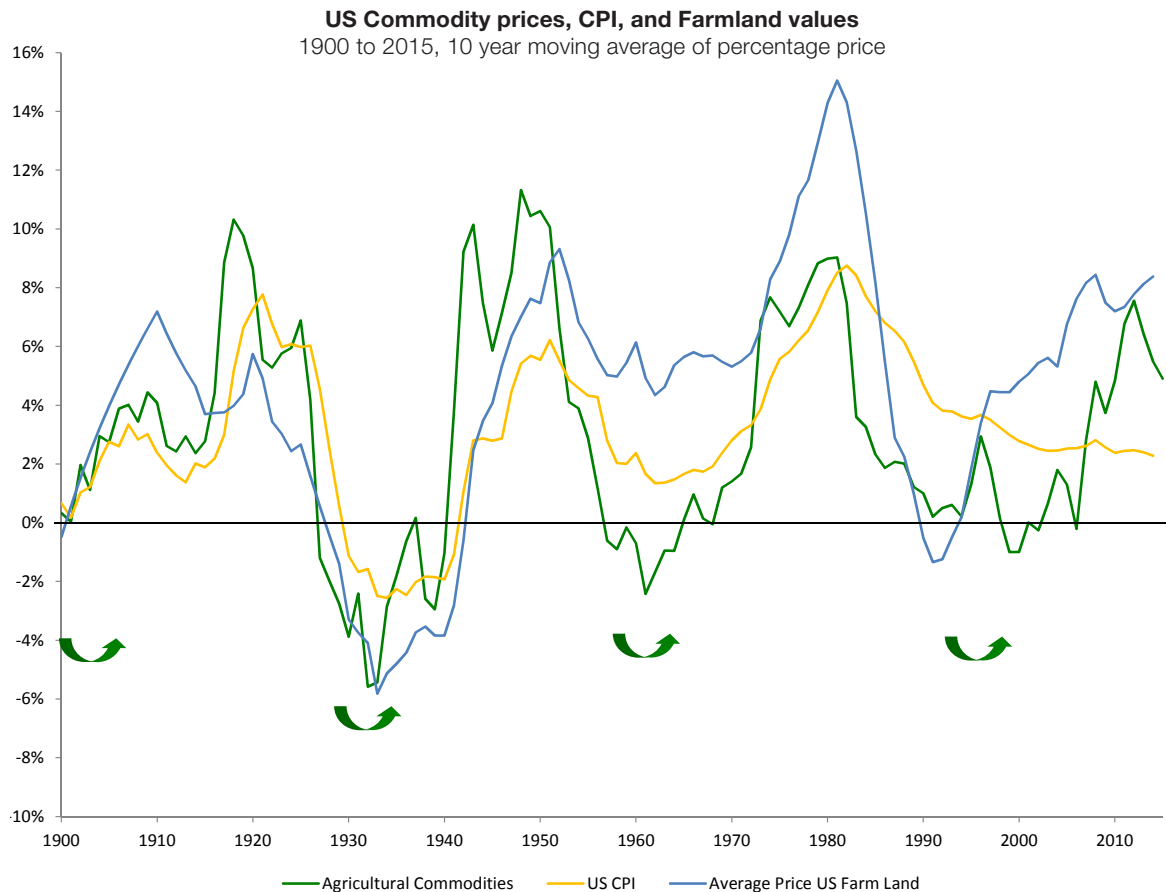
Technology. The innovations discussed above have fed through to higher crop yields, faster animal growth rates, and higher quality produce that has enabled farm businesses to realise greater profits despite declining real commodity prices. They have then used the proceeds of these increased profits to acquire additional farm land that became intrinsically more productive and hence valuable.

Productivity gains from new technology, have a significant investment implications for those of us who invest in farmland: over time, productivity powered by technology, has increased income and capital at a faster rate than inflation.

If you are an investor in farmland through the Rural Funds Group (RFF), you will be able to observe the benefits of any productivity gains through the long term increase in RFF's underlying assets. Because these assets are leased, you may also experience an increase in your income due to indexation clauses in the lease agreements. Clauses that are underpinned by the productivity gains of the lessee.

Productivity gains then, are a critical element in the success of your investment. They drive the year by year growth in your income and ultimately drive the long term capital value of your nest egg. So if history is any guide, it is right to be optimistic that farming is capable of better and that productivity gains will continue to drive income growth for careful investors.

Figure 1: 125 years in farming<sup>3</sup>



<sup>3</sup> Rural Funds Management, Data sources: US Census Bureau and R.J. Schiller.



A harvester 'shakes' almonds from trees on Rural Funds Group (RFF) property outside Hillston, New South Wales.

# Rural Funds Group (RFF) Update

RFF is a stapled security comprising  
Rural Funds Trust ARSN 112 951 578 & RF Active ARSN 168 740 805

## Rural Funds Group (RFF) achieved its third major milestone in six months with the completion of a \$15m capital raising.

In August 2014, RFF entered into an unconditional contract to acquire Tocabil Station at Hillston in central NSW, for \$5.2m. The purchase settled in October adding another valuable asset to RFF's portfolio.

In early March 2015, RFF announced a 22-year lease with Olam Orchards Australia Pty Ltd to develop and operate a 600 hectare (ha) almond orchard on the property.

Shortly after executing the lease, RFF conducted a \$15m capital raising, comprising a \$7.5m Institutional Placement

and a \$7.5m '2 for 33' non-renounceable Entitlement Offer to eligible RFF unitholders. A total of \$2.08m was received from unitholders with the balance of the \$7.5m allocated by the underwriter to institutional and sophisticated investors.

The Placement component, also allocated to institutional and sophisticated investors, was oversubscribed, reflecting the confidence investors have towards RFF.

Proceeds from the raising will initially be applied to pay-down debt and subsequently redrawn to fund the Tocabil almond development.

During the capital raising process, RFM updated the distribution forecast for the financial year 2016 to 8.85 cents per unit (cpu), up from 8.6 cpu for financial year 2015, or by 3%.

**Figure 1: Recent RFF Milestones**



While announcing RFF's half yearly results in February 2015, David Bryant, Managing Director of RFM commented on RFF's broader strategy.

"We are optimistic about the potential for future expansion in the almond sector. The almond industry, like many of the agricultural industries where RFF owns assets, is benefitting from a lower Australian dollar."

"This should translate to higher margins for our lessees and has the potential to drive asset prices, resulting in good news for owners of those assets, the RFF unitholders," he said.



**A new bore on Tocabil Station located outside Hillston NSW.**

During the capital raising process, RFM updated the distribution forecast for the financial year 2016 to 8.85 cents per unit (cpu), up from 8.6 cpu for financial year 2015, or by 3%.



RFF's Geier Vineyard in the Barossa Valley, South Australia



## RFF maintains focus on premium winegrape varieties

RFF's vineyard assets include 666 ha of vines leased to Treasury Wine Estates Limited (TWE). TWE's focus is to produce grapes that meet the quality standards necessary for the 'ultra-premium' wine category and contribute to some of Australia's best known and highest quality wine labels.

According to RFF Business Manager, Daniel Edwards, RFF funded the conversion of just over 26 ha of vines from Merlot to Shiraz and Cabernet Sauvignon in 2014. This occurred on Geier Vineyard, RFF's largest vineyard situated in the Barossa Valley, at the request of the lessee, TWE.

"TWE maintains its focus on growing grapes in the ultra-premium wine price category. This provides higher

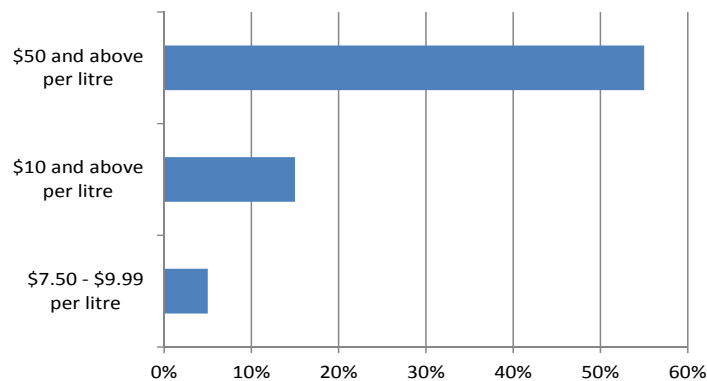
value product to the tenant and a more desirable vineyard," said Mr Edwards.

"The recent upsurge in premium wine export values provides further support to this strategy," he said.

Figures from the Australia Grape and Wine Authority (AGWA) showed a 55% jump in export demand for ultra-premium wines (above \$50 per litre, see Figure 2), a market segment where RFF has historically supplied fruit.

More than 90% of Australia's ultra-premium wine exports are now exported to Asia, as reported by AGWA. In 2014, Hong Kong, Singapore and Malaysia significantly increased imports of ultra-premium wines by 127%, 123% and 60% respectively.

Figure 2: Growth in premium wine price segments 2014<sup>4</sup>



**"The recent upsurge in premium wine export values provides further support to this strategy," – RFF Business Manager Daniel Edwards.**

<sup>4</sup> Australian Grape and Wine Association (AGWA) Media Release, 'Australian wine exports see rise in volume and value in 2014', 21 January 2015.

## RFF Half Yearly Financial Reports

RFF released 2015 Half Yearly Financial Reports in February, highlighting achievements such as the acquisition of Tocabil Station and the change of RFF to a stapled security structure. For the period RFF generated a \$3.9 million net profit before income tax and adjusted funds from operations (AFFO) of \$5m.

The AFFO of \$5m was in line with the previous forecast and RFM confirmed the forecast distributions of 8.6 cpu for 12 months ended 30 June 2015.

From a market price perspective, the RFF trading price to 31 December 2014 had increased 44% since listing (on 14 February 2014); substantially higher than the price movement of the S&P/ASX 300 A-REIT index (Figure 3).

The full half yearly report and investor presentation are available online at: [www.ruralfunds.com.au](http://www.ruralfunds.com.au)

**Figure 3: Comparison of RFF to S&P/ASX 300 A-REIT index<sup>5</sup>**



<sup>5</sup> Sources: RFF closing prices – IRESS, S&P/ASX 300 A-REIT index – au.spindices.com/indices/equity/sp-asx-300-a-reit-sector  
Note: RFF is not part of the S&P/ASX 300 A-REIT index

**Table 1: Key Portfolio & Financial Statistics — as at 31 December 2014**

RFM updated the 31 December 2014 reported key portfolio and financial statistics on a pro-forma basis, to include the purchase of the Tocabil property. Both sets of figures have been provided below:

	31 December 2014 Pro forma <sup>6</sup>	31 December 2014 Pre-Tocabil
Total assets	\$247.4m	\$247.4m
Net Asset Value (NAV)	\$150.9m	\$136.7m
Units on issue	131.7m	117.5m
NAV per unit	\$1.15	\$1.16
Gearing ratio	35.4%	41.1%
Forecast distribution	8.85 cpu (FY16)	8.6 cpu (FY15)
Weighted Average Lease Expiry (WALE)	13.4 years	12.2 years
Number of properties	27 properties	27 properties
Occupancy	100%	100%

## Upcoming Key Dates

<b>Quarterly Distribution Record Date</b>	<b>30 June 2015</b>
<b>Annual financial results announced</b>	<b>August 2015</b>
<b>Quarterly Distribution Announcement</b>	<b>2 October 2015</b>

## RFF Investment Profile

RFF is structured as a specialised real estate investment trust that owns a diversified portfolio of high quality Australian agricultural assets including almond orchards and associated water entitlements, commercial scale poultry growing infrastructure, premium vineyards, and livestock, all of which are leased to suitably qualified and experienced agricultural operators (or tenants).

RFF's investment strategy is to deliver a stable income stream from leasing assets and capital growth through the appreciation in the value of RFF's assets.

RFF benefits from strong industry dynamics with growth in Australian agriculture, driven by increasing world population growth, the emerging Asian middle class and constraints in the global supply of agricultural land.

<sup>6</sup> Pro forma figures assume:

- the proceeds from the Offer (disclosure date 6 March 2015) are initially applied to debt reduction
- forecast FY15 revenue from existing counterparts and revenue from Olam Orchards Australia Pty Ltd based on the expected total project cost of \$32.1m, calculated as if the project were completed 1 July 2014
- gearing initially reduced, reverts to current levels as development progresses

RFF's full disclosure is available on the ASX website, 'Equity Raising Presentation', 6 March 2015, visit: [www.asx.com.au](http://www.asx.com.au)



# RFM StockBank Update

ARSN: 153 436 803

**RFM StockBank continues to be a sound alternative to traditional livestock finance, with those Operators in areas enjoying rainfall taking advantage of favourable seasons and market conditions.**

The climate variations across the South East (Figure 2) highlight the need for a flexible livestock leasing facility, such as StockBank. Andrew Vardon, RFM StockBank Business Development Manager, notes that farmers are accessing StockBank's leasing facility in place of traditional avenues, including bank finance.

"It's not been about those who can't get alternative finance – we've been helping experienced operators and inter-generational farming families unlock the equity they've got as landholders," he said.

High farm gate prices are expected in 2014-15, according to figures presented at the Australian Bureau of Agricultural Resource Economics and Sciences (ABARES) Outlook conference in March.

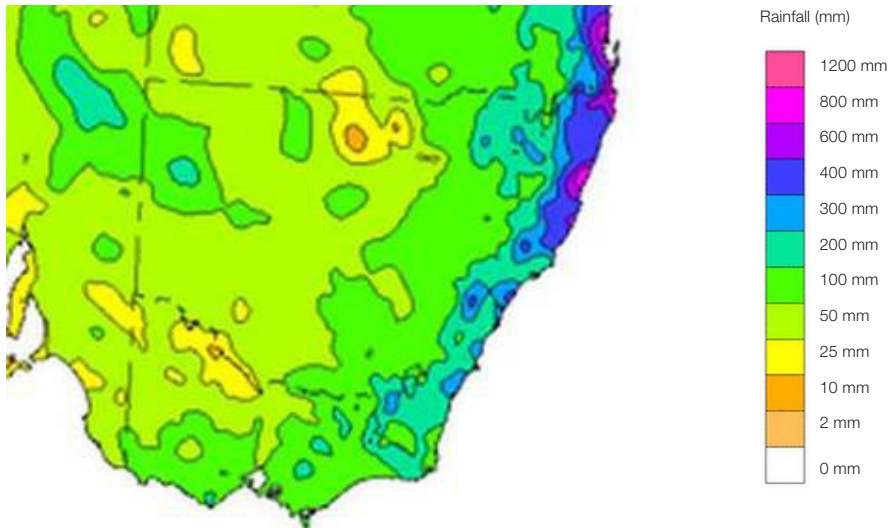
The weighted average saleyard price of beef cattle is forecast to increase by 19% to average 349 cents a kilogram in 2014-15 and by a further 16% to average 405 cents a kilogram in 2015-16.

The saleyard price of lambs is also forecast to increase by 7% to average 510 cents a kilogram in 2014-15 and by a further 15% to average 584 cents a kilogram in 2015-16, according to ABARES.

**Figure 1: RFM StockBank Livestock locations map<sup>7</sup>**



**Figure 2: Rainfall Analysis (mm) 1 January 2015 to 31 March 2015<sup>8</sup>**



“Store lambs purchased specifically to grow out on feed or grain can expect premium prices,” said Mr Vardon.

The benefits of the seasonal conditions and market prices are not limited to the Operators and Stock Agents. RFM recently paid a quarterly distribution to StockBank unitholders of 1.97 cents per unit (cpu) including a franking credit of 0.59 cpu. The next quarterly distribution for StockBank will be paid on or around 15 May 2015.

Andrea Lemmon, RFM Executive Director - Funds Management, is planning for growth in the number of StockBank livestock leased across south-eastern Australia.

“Whilst there is a focus on the increasing global demand for our meat products, the domestic market also continues to grow. StockBank is part of that growth, allowing Land owners to take advantage of good seasons by increasing their herd size,” she said.

Meanwhile, a recent advertising campaign by Meat and Livestock Australia (MLA) ‘You’re better on beef’ was also presenting a positive message about the nutritional benefits of beef to the Australian consumer.

<sup>7</sup> Source: Google Maps and updated monthly at: [www.ruralfunds.com.au](http://www.ruralfunds.com.au)

<sup>8</sup> Source: Australian Bureau of Meteorology: [www.bom.gov.au](http://www.bom.gov.au)

The benefits are not limited to livestock operators; investors recently received quarterly distributions of 1.97 cents per unit including franking credits.

**Table 1: Key Portfolio & Financial Statistics – as at 31 December 2014**

Total assets	\$14.3m
Net Asset Value (NAV)	\$11.1m
NAV per unit	\$0.9991
6mth Livestock turnover – cattle	6,578 purchased
	9,173 sold
	15,718 on hand
6mth Livestock turnover – sheep	28,968 purchased
	24,804 sold
	44,204 on hand
Change in livestock placements	Growth of -2.4% from \$13.321m to \$12.995m
Livestock locations	New South Wales: 14,059 cattle, 40,572 sheep
	Victoria: 1,111 cattle, 2,470 sheep
	South Australia: 548 cattle, 1,162 sheep

### Upcoming Key Dates

<b>Quarterly distribution payment date</b>	<b>On or around 15 May 2015</b>
<b>Quarterly distribution record date</b>	<b>30 June 2015</b>
<b>Quarterly distribution record date</b>	<b>30 September 2015</b>

### StockBank Fund Profile

StockBank is a liquid, alternative investment fund that aims to provide investors with a reliable yield, by financing the acquisition of livestock that are leased and grown out by Operators on a portfolio of diversified

properties. StockBank receives payment upon the sale of livestock, calculated as a fixed return on capital, regardless of livestock sale price, weight gain or mortality rates.

# About Rural Funds Management Ltd

AFSL: 226701

RFM is an experienced fund and asset manager that specialises in Australian agriculture.

RFM manages a diverse portfolio of large-scale farming and agricultural enterprises for investors who seek the opportunity to diversify their portfolios away from the traditional equity and property markets. Our primary assets are in land, water, infrastructure, poultry, cattle, sheep, viticulture, cotton and almonds.

Established in 1997, RFM is the responsible entity for seven agricultural investment funds and as of 31 December 2014, had approximately \$313m of assets under management in New South Wales, South Australia and Victoria.

RFM is one of the oldest and most experienced managers of agricultural assets in Australia. In addition to RFM's corporate office located in Canberra, RFM has offices in Sydney, Melbourne and Western NSW and employs around 40 staff in fund and asset management activities.

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## To make an investment

Rural Funds Group (ASX: RFF) is a listed investment. StockBank operates as an unlisted fund (APR Code: RFM0009AU).

To make an investment in RFF please contact your broker or financial adviser.

To make an investment in StockBank please contact your financial adviser or RFM.

## Provide us your email address

We use email to communicate with our investors. Please take the time to contact our Investor Services team and provide your email address so that you don't miss out on any important information.

## Australian Executor Trustees Limited (AET) Privacy Policy

AET is the custodian for the Rural Funds Group and RFM StockBank. To read more about their privacy principles, please visit [www.aetlimited.com.au/privacy](http://www.aetlimited.com.au/privacy)

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