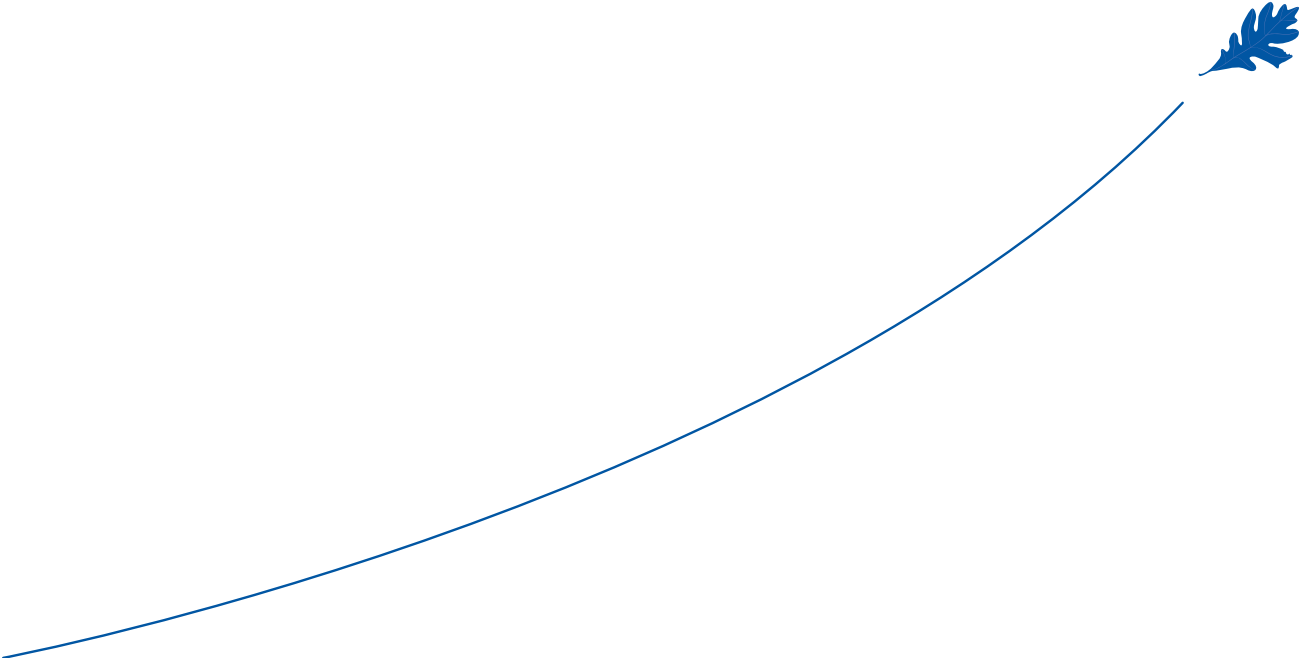


McLean Budden Perspective

The Global Need for Greater Agricultural Productivity

October 2011



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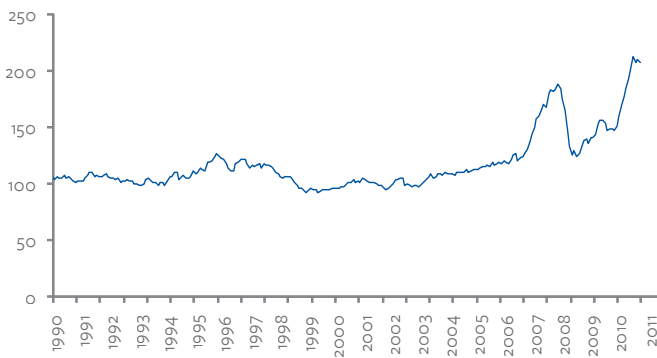
The Global Need for Greater Agricultural Productivity

From the United Nation's October 2009 report titled "How to Feed the World in 2050"

"By 2050 the world's population will reach 9.1 billion, 34 percent higher than today. Nearly all of this population increase will occur in developing countries. Income levels will be many multiples of what they are now. In order to feed this larger, more urban and richer population, food production must increase by 70 percent."

It is difficult to read a newspaper today that does not mention rising food prices, the possible causes, or the potential impact it could have on the fragile economic recovery. According to the Food and Agriculture Organization (FAO) of the United Nations, the FAO's Food Price Index is currently hovering around its highest reported level.

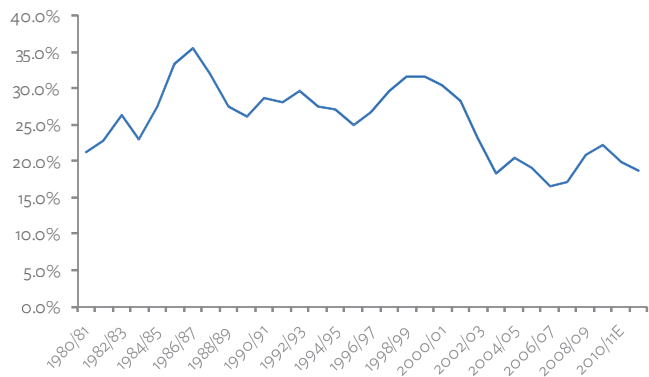
Graph 1: FAO's Food Price Index



Source: FAO

The suggested causes for the rising food prices are numerous including increasing inflation due to the stimulative effects of quantitative easing in the U.S., poor weather causing production disruptions, greater biofuel production, and the rise of the middle class in developing countries demanding more food. While the impact of each of the various causes of the rise in today's food prices is up for debate and the current price levels are likely unsustainably high, at McLean Budden, we feel the current market conditions are symptomatic of a number of longer term trends that will support generally higher food prices going forward. It is the longer-term trends that will be the focus of this McLean Budden Perspective as higher grain prices prompt farmers to increase the amount of investment in their crops and operations, with agricultural equipment and other input providers set to benefit from this trend.

Graph 2: USDA's Global Ending Grain Inventories as a Percentage of Estimated Usage

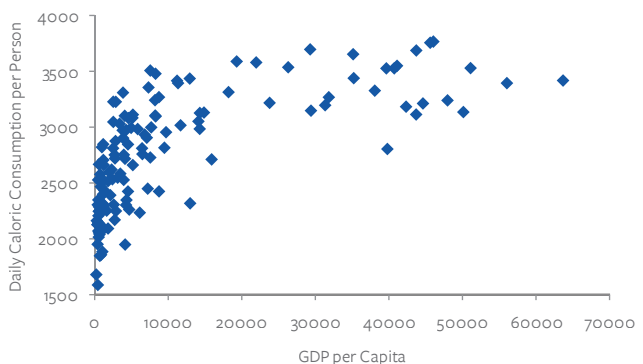


Source: USDA

Changing Diets in the Developing World

Arguably the most powerful long-term trend currently impacting global food demand is the increasing middle class in the developing world and how the rising incomes in these countries are resulting in an evolving diet that includes the consumption of not only more calories per day, but more calories from meat. The graphs below show the relationship between incomes and the consumption of calories and protein in various countries around the world. The graphs show that as populations become wealthier they tend to consume not only more calories but the source of the calories changes to include more animal protein. This increase in consumption of animal protein creates a multiplier effect on grain demand. For example, it takes approximately 7 to 8 pounds of grain for an animal feeding operation to produce an extra pound of beef.

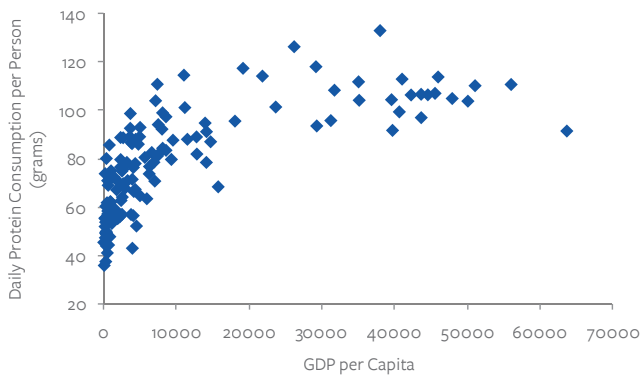
Graph 3: Daily Caloric Consumption per Person



Source: World Bank, United Nations Food and Agriculture Organization

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Graph 4: Daily Protein Consumption per Person

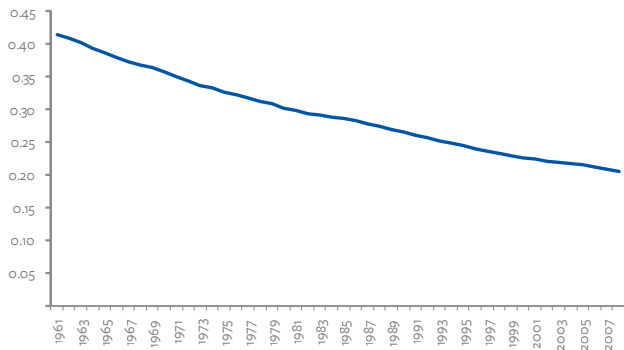


Source: World Bank, United Nations Food and Agriculture Organization

Declining Arable Land Per Capita

Another key factor driving the need for greater agricultural productivity is that the increase in arable land is not keeping up with population growth. The causes for this are numerous, including urbanization of farm land in places like China, where the authorities trying to stop the process with questionable success. Also, Saudi Arabia has announced it is stopping farming in some places in the country as water resources are becoming harder and more expensive to access.

Graph 5: Global arable land per capita (ha/person)



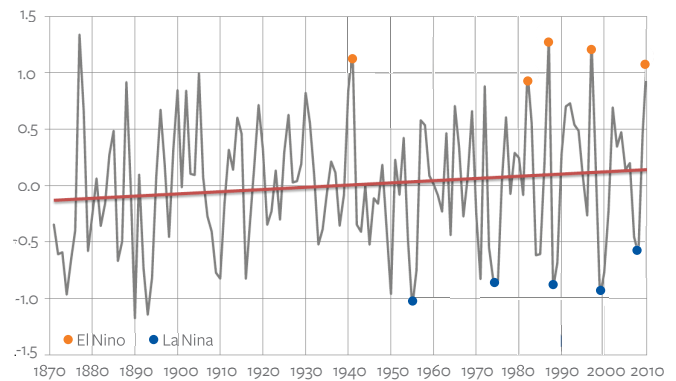
Source: FAO

Severe Weather Events Increasing

Some of the weather and grain market observers we follow have suggested there has been an increase in the number of severe weather events, such as drought, floods and storms, over the past decade. While this is difficult to quantify – and even more difficult to determine the reason – what is an issue is that with the general decline in grain inventories, weather related disruptions have, and are set to have, a much greater impact on grain prices going forward. This trend will not reverse until the world is able to replenish depleted grain inventories.

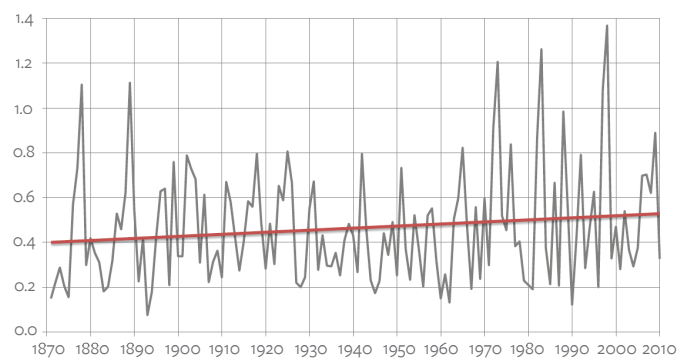
Below are two interesting graphs from a recent presentation we attended by the EarthWatch Institute showing that the temperature fluctuations in the Pacific Ocean, otherwise known as El Ninos and La Ninas, have begun to show wider deviations around the average temperature and that the average surface temperature of the ocean is indeed rising. It is the current La Nina that is being blamed for the devastating floods in Queensland, Australia which contributed to the rise in food prices as grain land was flooded.

Graph 6: Monthly Nino3.4 Deviations (C)



Source: Dr. Dan Bebber (Earthwatch), NOAA

Graph 7: Yearly Standard Deviations of Nino3.4 Deviations (C)



Source: Dr. Dan Bebber (Earthwatch), NOAA

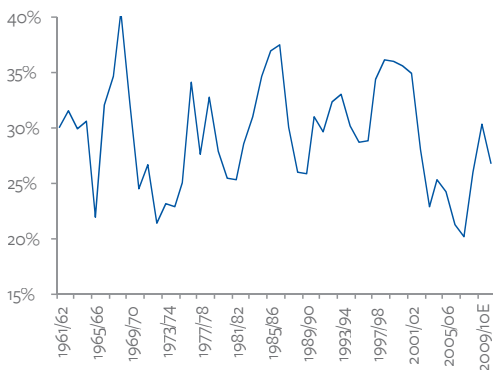
The Nino3.4 is an index of sea surface temperatures of the Pacific Ocean which has a significant impact on the weather many of the world's key grain growing regions will experience at any one time.

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Increase in Government Intervention

As is often the case when grain prices rise, governments react with policies that typically exacerbate the situation externally in order to avoid problems internally. As an example, global wheat inventories as measured by the United States Department of Agriculture (USDA) (see below) are not necessarily in short supply relative to historic levels, but this did not stop a steep rise in prices due in part to Russia, a key global wheat exporter, banning wheat exports in August of 2010, despite having adequate wheat stocks themselves. Russia banned wheat exports in reaction to the drought they were experiencing and wanted to keep internal wheat prices down. Russia recently lifted the ban which had the predictable effect of lowering global wheat prices, but how long the ban stays lifted depends on this year's crop in Russia. Another way governments can exacerbate the situation in countries that are net grain importers is by grain hoarding during periods of tight supply in the hopes of keeping local prices down to placate the local population. We witnessed this in the wheat markets shortly after the riots began in Tunisia in early 2011 as other North African countries, fearing high food prices would cause similar unrest, began buying wheat in greater quantities than normal.

Graph 8: Global Wheat Stocks-to-Use



Source: USDA

Graph 9: Soft Red Winter Wheat Prices (St. Louis Basis)

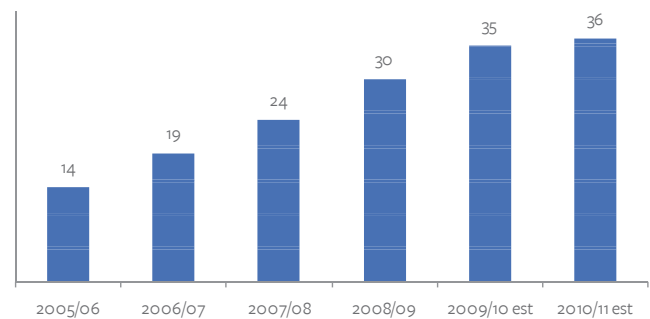


Source: CIS

Increase in Biofuel Production

In order to promote greater self-sufficiency in energy supplies and to diversify away some of the exposure to fossil fuels, a number of countries such as the U.S. have supported the development of domestic biofuel industries. The graph below shows how support for ethanol since the middle part of the last decade in the U.S. has displaced a greater amount of corn each and every year. The U.S. is the largest exporter of corn, so rising or falling U.S. corn prices have a significant impact on global grain prices and U.S. corn prices are a key bellwether for global agricultural equity prices. The problem with biofuels is the questionable economics. Crops used for fuel displace acres used for food, which could be playing a significant role in increasing food prices world-wide. However, the farm lobby in the U.S. remains very powerful and the ethanol industry is now a very large employer, suggesting that support for ethanol will be sustained. We continue to monitor the situation closely.

Graph 10: Percentage of U.S. Corn Crop Used for Ethanol



Source: USDA

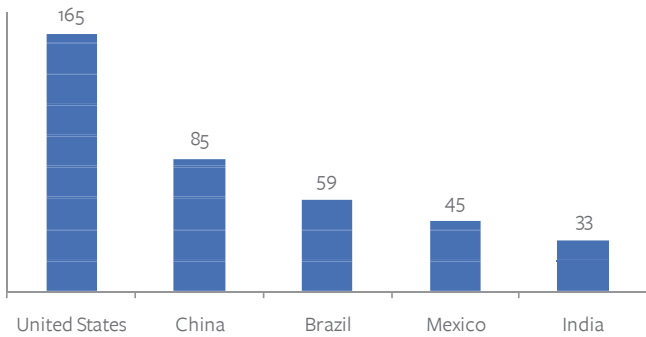
But all is not lost!

Ultimately, despite rising food costs resulting in agencies such as the FAO reporting rising global malnutrition rates, we do not believe there will be any meaningful and long-lasting food shortages for a number of reasons which will prove to be beneficial for agricultural input providers like Potash Corp, Agrium or Syngenta. First, nothing can get the attention of governments more than high food prices and the potential destabilizing effect this can have. While on the one hand, through export tariffs and hoarding, governments can exacerbate the problem, in the long-run, governments recognizing the need to grow more food internally can and will look to increasing productivity of their own farmers (if possible), which will have a positive impact on agricultural input demand. The graphs on the following page show the differences in yield between the U.S., arguably the most technically advanced agriculture country in the world, and select developing markets along with a graph showing the

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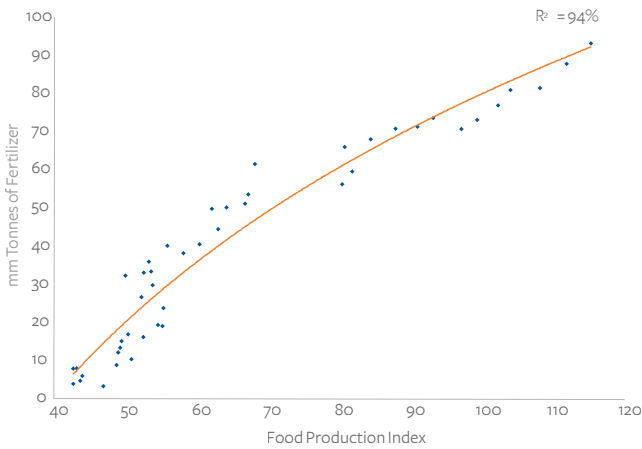
relationship between yields and fertilizer use. These graphs highlight the significant potential for developing markets like India, which has one of the world's lowest fertilizer application rates in the world, to increase production by following better agronomic practices, including the greater use of inputs like fertilizer and seed.

Graph 11: Corn Yields (Bushels/Acres)



Source: FAO

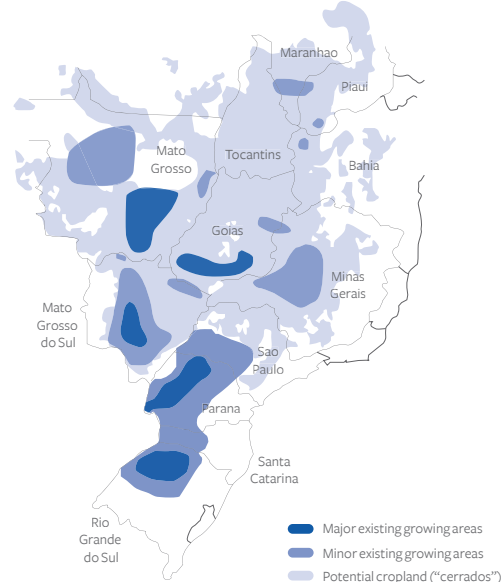
Graph 12: Relationship Between Food Production and Fertilizer Application Rates



Source: FAO

Also, there are opportunities to increase the land available for farming in places like Brazil, as shown in the following chart from Doane, a U.S. farmer consultancy. The development of this farmland will require major investments in infrastructure, including rail lines and ports, but it will also be a major new source of fertilizer demand to bring the soil up to commercial levels of productivity.

Image 1: Current and Potential Brazilian Soybean Areas

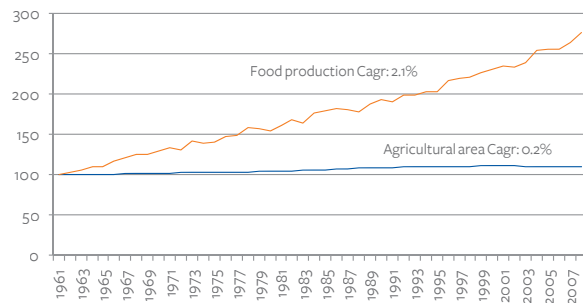


Source: Doane Advisory Services

Along the same vein, there are plenty of opportunities for many global regions to increase export capacity to take advantage of strong Asian grain demand. This includes the Black Sea area, with some of the richest soil on the planet, that can produce a lot of grain, but where getting it to market is constrained by infrastructure. This creates opportunities for companies like Bunge or Viterria to potentially help open up this area for greater grain exports by building terminals.

In conclusion, we point to the last graph below which highlights how food production has continued to grow despite the near-nil increase in arable land. It should come as some relief that there is still much room for greater agricultural productivity, which will help keep grain inventories at comfortable levels while benefitting the agricultural input providers who play a key role in improving productivity.

Graph 13: Grain and Cereal Production vs. Agricultural Area



Source: FAO

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