5 March 2014 / Vol 16 Issue 17

# MI Prospects

## Analyst's Insight: Local versus global

The AHDB/HGCA winter planting survey for England and Wales provides a first insight into UK areas for harvest 2014. Although Scottish areas (due 19 March) and spring cropping are still unknown, the results, so far, suggest a return to more normal cropping patterns after the extremes of 2013.

The survey suggests that more wheat had been planted by 1 December in England and Wales, for harvest in 2014, than was harvested across the whole of the UK in 2013 – click here for more. This increases the likelihood of the UK returning to the wheat export market in the next marketing season, but will ultimately depend on final yields and quality. Read more on current crop conditions in the latest ADAS Crop Report.

Price is also a crucial factor in the UK's export potential, with the domestic crop size and quality setting the relationship to world markets.

Since the autumn, November-14 futures prices have been trading at a discount of £5-10/t to the equivalent Paris contract. However, the last time the UK was a net exporter of wheat (2011/12), this discount was closer to £15/t, suggesting there is potential for UK prices to decline further relative to European levels come harvest if the weather is kind.

The impact of Sterling is also being felt as the currency recently reached its highest levels against the Euro since January 2013 and against the US dollar since 2009.

The relative strength of Sterling is pressuring both old and new crop prices in the UK and is a key determinant in establishing relative trade flows, both in and out of the UK.

While the UK's relationship to world markets may vary from season to season, this variation is small when compared to the overall movements in global markets. There are still many unknowns as, across the Northern Hemisphere, farmers are assessing crops post-winter and commencing spring planting.

While there are no major concerns at this stage, there is still a long way to go and with 80% of the global wheat area in the Northern Hemisphere, the potential for volatility as these crops head towards harvest is high.

**Helen Plant**

**Upcoming HGCA Workshops**

**Protecting your Profit** – how can you manage the most common risks facing your arable enterprise? Cambridge 11 March, Lincoln 2 April, Tewkesbury 8 April

**Meet the Processor** and **Meet the Exporter** – want a better insight into what happens to grain beyond the weighbridge? See www.hgca.com/events for the full range of dates & venues.

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# Milling Wheat Update

***Despite the improved quality of the UK wheat crop this year, domestic availability is limited by the small volume of the 2013 crop. However, although milling premiums have expanded recently, they are likely to be limited, principally, by German and Canadian imports.***

**Jack Watts, Market Specialist team**
**02476 78760, jack.watts@ahdb.org.uk**
20 February 2014

## Introduction – global drivers

The 2013/14 marketing season has been characterised by record grain production, and thus, downward pressure on prices compared with last season. In response, demand has been re-stimulated, preventing a complete price collapse and leading to relatively tight stock-to-use ratios – although these are noticeably higher year-on-year.

After a number of seasons of largely following volatility in the maize market, wheat has become **more interesting in its own right** as strong import demand, from mainly China and Brazil, has helped reduce US stock levels – the global safety net of exportable wheat stock. By 6 February, the US had exported/sold 27.3Mt of wheat – up 26% and 20% compared with the corresponding time in 2012/13 and 2011/12 respectively.

However, this season's Canadian crop is more than 10Mt higher, year-on-year, at 37.5Mt with the USDA estimating a 4.79Mt increase in closing stocks to 9.84Mt. This is more than enough to offset the 4.35Mt decline in US stock estimates to 15.19Mt, but the market is likely to be mindful of internal Canadian logistics, which may impact the ability to execute exports.

As we will examine later in this article, the **greater availability of Canadian wheat has direct consequences for the UK milling wheat situation**. See the recent Prospects article on UK trade and usage for insight into the first six months of this season.

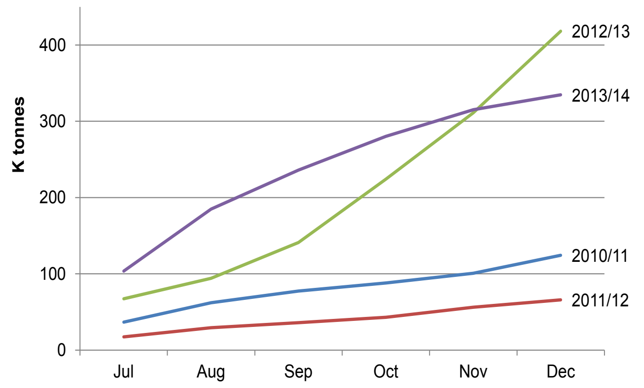
## UK milling wheat availability

The headline for UK milling wheat this season is the much improved quality with 38% of Group 1 samples meeting the full bread wheat specification (76Kg/hl, 250s, 13%), according to the AHDB/HGCA Cereal Quality Survey. Although this is a marked increase from the 3% meeting specification in 2012, the c.20% decline in area is a limiting factor for availability. AHDB/HGCA analysis presented at the recent Milling Wheat Breakfast meetings estimated that there was **around 620Kt of full specification UK bread wheat produced from the 2013 harvest** – up from 70Kt in 2012, but noticeably below the 990Kt of 2011 and 790Kt of 2010.

With lower than average domestic milling wheat supplies, imports have again been a key feature. In the first six months of the season (Jul-Dec) the UK had imported 1.34Mt of wheat. Although this is very similar to the same point last season, it is still high compared with 'normal' seasons, where around 1Mt are typically imported.

Germany is a key supplier of milling wheat into the UK and, as Figure 1 shows, cumulative imports have been strong so far at around three times the 'normal' level.

**Figure 1 Cumulative imports of German wheat into the UK (Jul-Dec)**

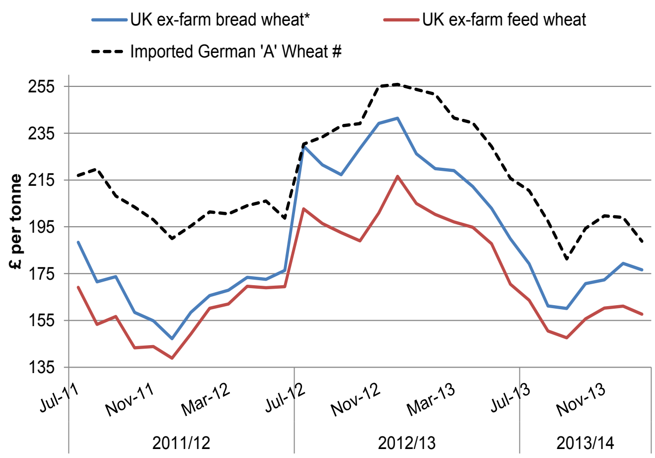



*Source: HMR&C*

Some of the strength in this season's imports can be attributed **to pre-harvest purchasing by consumers as a hedge against, what was at the time, a very uncertain outlook for the domestic wheat crop**. However, cumulative German imports now appear to be levelling off and are below 2012/13 levels.

As the season progresses, fresh import purchases cannot be ruled out given the price relativities depicted in Figure 2.

**Figure 2 Imported German wheat acting as a cap to UK milling premiums (monthly averages)**




** min. of 13% protein, 250HFN & 76kg/hl # CIF UK ports*

*Source: AHDB/HGCA*

# Milling Wheat Update

When the UK is required to import milling wheat, UK milling premiums can become 'capped' by imported prices – principally **German 'A' wheat**, which is of comparable quality to UK bread wheat. Further analysis reveals that in January, imported German 'A' wheat (CIF East Coast) was at around a £12/t premium to UK ex-farm bread wheat. This is by far the lowest of the season so far – it peaked at £36/t in August – and current levels haven't been seen since the end of 2012.

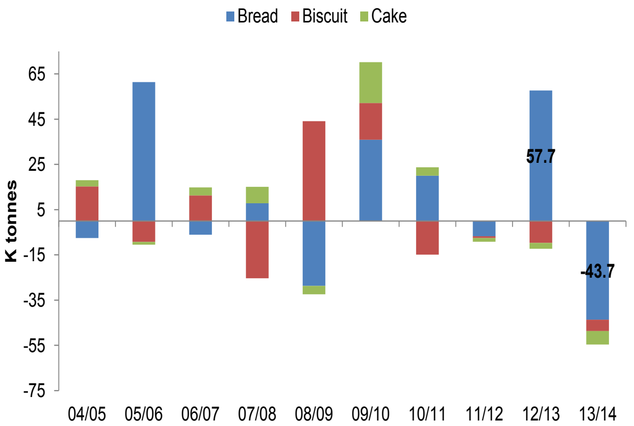
Although German imported wheat prices are seen as the traditional cap to UK milling premiums, attention should be given to Canadian cargoes destined for the UK. In December, HMR&C report that the UK imported almost 69Kt of Canadian wheat – **the largest monthly volume since 1999**. This takes the cumulative imports from Canada to 189Kt, 7.5Kt higher year-on-year.

Furthermore, **against the Canadian Dollar, Sterling has appreciated by 8.6% over the last three months; 13.6% over the last six months; and 16.5% over the last year**. This makes Canadian wheat cheaper in Sterling terms and given the size of Canada's wheat surplus this season makes this a key area to watch.

## UK flour production

As Figure 3 shows, UK flour production in the first half of the season has seen noticeable year-on-year declines, and in the case of bread flour, nullifies much of the gains of last season. As the season progresses, this could be a **key limiting factor** for domestic milling wheat demand.

**Figure 3 Year-on-year changes in UK flour production for the Jul-Dec period**




*Source: Defra*

## Closing comments - New crop prospects

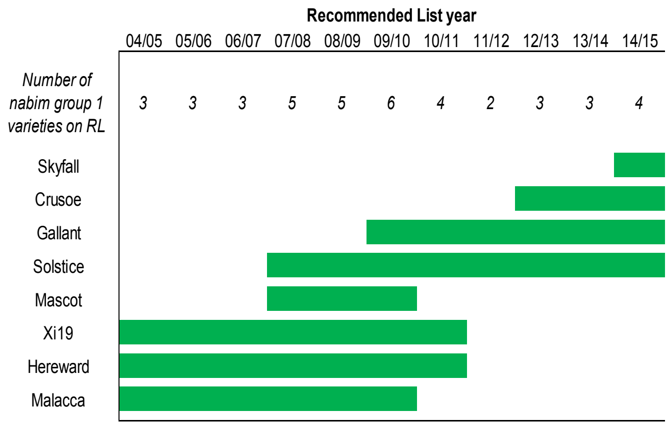
As always at this time of year, it is difficult to make precise predictions for the new crop as the weather over the coming months will be the key driver. Globally, the International Grains Council expects the 2014 wheat harvest area to increase by 2.5% to similar levels seen in 2008 and 2009. However, this assumes more normal levels of abandonment, which can't really be assessed with much confidence until winter crops emerge from dormancy and spring crops are planted. The EU wheat area is expected to grow as wheat has regained some competitiveness against maize, which may prevent the region from operating at the level of the premium seen this season.

For the UK, the expectation is for **a return to a more normal wheat area** (up to around 2M ha). If this is met with reasonable yields, then it is likely to mean a return to the export market, which will require more competitive pricing especially if Sterling continues to strengthen.

With lower feed base prices, milling wheat may regain more attention as gross margins become more competitive. From a Group 1 perspective, the **portfolio of varieties continues to expand** giving farmers more options which might be supportive of the area share.

Figure 4 shows how the Group 1 segment of the HGCA Recommended List has evolved in recent years.

**Figure 4 Evolution of nabim Group 1 Varieties on the HGCA Recommended List (RL)**




*Source: HGCA Recommended List*

## Key Points

- Despite better quality, imports remain a key component of the UK milling wheat sector.
- Fresh import purchases cannot be ruled out this season given current price relationships.
- Larger global wheat area expected in 2014 with the likelihood of the UK returning to the export market.

# Funds Update

***The positions held by speculative traders within the Chicago wheat and maize futures markets indicate a more bearish attitude than 12 months ago, while for Chicago soyabean futures, speculators continue to hold bullish positions.***

**Robert Wardle & Helen Plant**
**024764 78759, helen.plant@ ahdb.org.uk**
25 February 2014

## Introduction

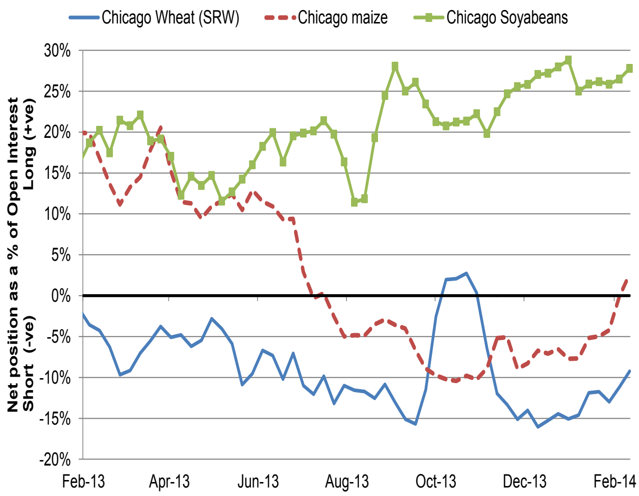
Volatility remains a key part of modern grain markets, clearly demonstrated by the price movements in futures contracts. **Speculative traders**, who trade futures contracts without producing or taking delivery of the product, **try to take advantage of the opportunity this volatility creates.**

The Commodity Futures Trading Commission (CFTC) is the organisation tasked with regulating futures trading in the US. In the CFTC weekly reports, speculative traders are broadly classed as 'non-commercial traders' but they are more commonly referred to as 'the funds'. Monitoring positions taken by the funds can give an indication of their anticipated price direction and risk areas should the market move against them.

## Chicago maize futures

The positions held by speculative traders in the Chicago maize futures market have moved significantly during the past year (shown in Figure 1).

**Figure 1 Net positions held by non-commercial traders (the funds) as a percentage of open interest**




*Source: CFTC*

Through all of 2011 and 2012, the funds held more long positions than short positions, known as a 'net long', indicating a bullish view of the market. A net long suggests the holder (or holders) of these positions views that there is greater potential for upward price movement – in 2011 and 2012 this reflected the tightness in feed grain supplies.

However, through 2013 the funds shifted to a net short position - the **first time the funds had taken a bearish stance in the Chicago maize market since the end of 2005**.

As 2013 progressed the market became increasing confident of the US maize crop achieving its potential, and prices declined as a result (Figure 2).

**Figure 2 May-14 Chicago maize futures prices**


*Source: AHDB/HGCA*

Since the start of 2014, old crop maize prices have seen a small amount of support and the funds have moved back to a more neutral position. The recent changes reflect the rapid pace of US exports (showing a smaller stock recovery is more likely than earlier forecasts suggest) and reductions to South American crop estimates. Nevertheless, the current supply and demand picture for feed grains is still more comfortable than last season.

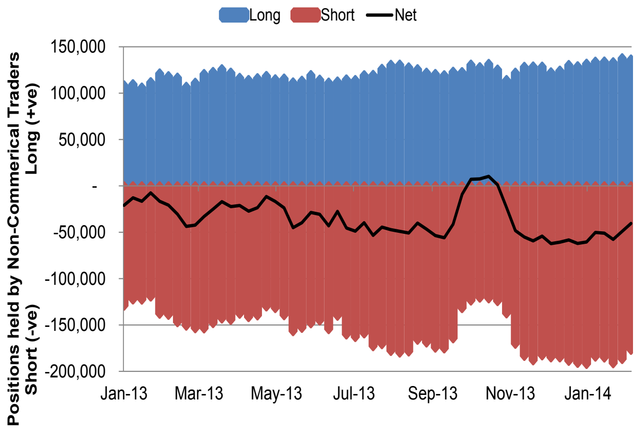
## Chicago wheat (SRW) futures

Since the start of the marketing year in July, the **funds' have largely maintained their bearish position within the Chicago wheat (SRW) market,** except for a period in the autumn.

The funds market position quickly changed from a net short position of 15.7% in mid-September to a net long position of 2.0% a month later in October. The main driver of this was a **reduction the number of short positions held by speculative traders** (Figure 3) and overall the funds reduced their involvement in the market. At the same time there was a quick rise in the price of nearby CBOT Wheat futures, increasing from \$233/t in mid-September to \$254/t in mid-October; an increase of 9.1% in 4 weeks.

# Funds Update

**Figure 3 Chicago wheat (SRW) futures: Positions held by non-commercial traders**




*Source: CFTC*

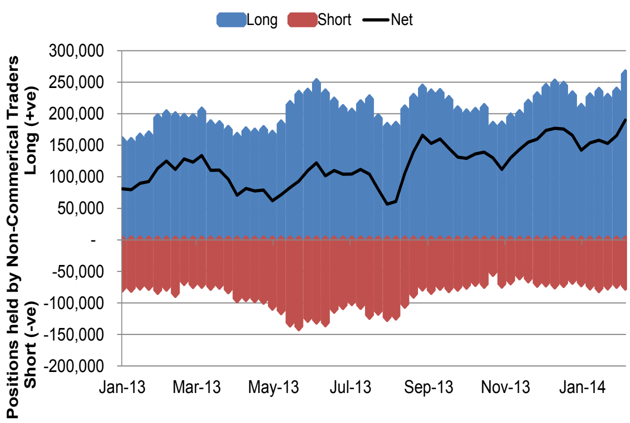
After initial good harvest results from most major exporting countries, it became apparent that import demand would also be higher. The federal shutdown in the US during October is also a potential factor – reducing information published during this key period for the market and arguably reducing investors' appetite for risk.

**In November the funds returned to holding a net short position** as prices dropped back again, a position that has been maintained into 2014. Though the size of the net short has fluctuated slightly, it remains – indicating that overall the funds view that the potential for downward price movement is greater than upward movement.

## Chicago soyabean futures

**Over the past year the funds have increased their already large net long position within the Chicago soyabean market** (Figure 4). Between mid February 2013 and 2014, the net long position held by speculative traders increased from 125K contracts to 190K contracts – when compared to the size of the market (the open interest), this shows an increase from 20% to 28%.

**Figure 4 Chicago soyabean futures: Positions held by non-commercial traders**




*Source: CFTC*

Since late September, the main change has been a sizeable increase to the long positions held, seemingly related to the underlying level of risk in the market. Although the US harvest had begun and prices had declined from the levels seen earlier in the year, global demand has been strong. Then and now, the market remains dependent on the forecast South American crops in order to meet this demand.

**At the moment, the risk associated with the South American harvest persists** as the Brazilian harvest is still in relatively early stages and the Argentine harvest is yet to start. However, should the current record crops forecast for the region be realised and if there is no further increase in demand, the positions held by speculative traders present an additional risk to prices. In this situation, prices would be likely to fall and the funds would need to realign with the market quickly – which may add further momentum to market direction.

## Concluding comments

Ultimately, supply and demand are the drivers of agricultural markets and, therefore, price. However, **in the short term, the activity of speculative traders can influence markets**, for example by adding additional momentum to price movements if the markets moves in opposition to the positions they have taken.

The positions recently taken by **speculative traders indicate a more bearish attitude towards both wheat and maize than twelve months ago**. This reflects the general change in market sentiment as grain supplies have rebound during harvest 2013. A **more bullish perspective is maintained for soyabeans**, reflecting the high degree of risk remaining in the market, until the South American harvest is safely gathered.

### Key Points

- Positions held by speculators in Chicago maize and wheat futures are more bearish than 12 months ago.
- Bullish position for Chicago soyabean futures reflects risk associated with ongoing South American harvest.
- Risk of additional volatility if markets move in opposition to positions held by speculative traders.

# AHDB Outlook Conference 2014

***The annual AHDB Outlook Conference took place on 12 February in London. The event, which covers the meat and dairy sectors, attracted around 180 delegates to hear about prospects for the year ahead. Forecasts suggest some increase in production across the livestock sectors as 2014 progresses.***

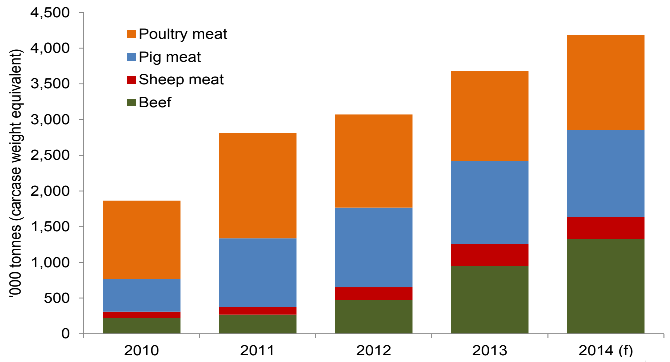
**Stephen Howarth, Market Specialist team**
**024 7647 8856, Stephen.howarth@ahdb.org.uk**
27 February 2014

This year's AHDB Outlook Conference was opened by **Food and Farming Minister George Eustice**. The Minister highlighted the increasing importance of food and drink exports, with potential for further growth in places such as China and India, where there is strong demand for Western products. His speech identified a number of issues of importance in ensuring this growth can be sustained, including support for new entrants to farming and the Agri-Tech strategy. Mr Eustice also touched on the role of government procurement in supporting UK farmers and, inevitably, on the recent flooding.

Following the minister, **Connor McVeigh, Supply Chain Director at McDonald's UK** spoke about some of the issues facing livestock supply chains over the last year, including the discovery of horse meat in beef products. Although McDonald's wasn't implicated, McVeigh talked about how all supply chains have faced greater scrutiny as a result. He emphasised the importance of strong long-term relationships with suppliers – or 'partners' as McDonald's refers to them – and short, simple supply chains. He cited that McDonald's has worked with many of its partners for decades, which has helped it to ensure the quality and continuity of its products. He also stressed the importance of supporting UK agriculture with more than 17,500 British and Irish farmers supplying ingredients for its menu.

Rounding off the opening session, **Richard Brown, director of strategic market research and consultancy firm, GIRA**, covered developments in international trade. With better economic growth expected this year, he saw a positive demand outlook for meat and dairy products. With demand outstripping supply in much of the developing world, prices are often higher than in more established markets, providing attractive opportunities for exporters. In particular, he highlighted the growing importance of China across all sectors; Chinese meat imports in 2014 are projected to be more than double those in 2010.

**Figure 1 Increasing Chinese meat imports**




*Source: Gira*

Mr Brown also touched on the many bilateral trade agreements which are in place or being negotiated, although he felt that the short-term impact would not be dramatic. Finally, he suggested that the move towards a more export-oriented supply chain would be positive for the UK meat and dairy industries but would require structural and cultural change for producers and processors.

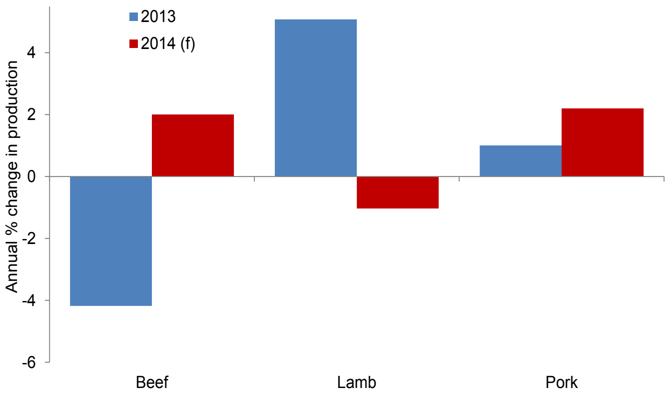
The conference then split into three sessions covering different sectors.

## Beef and sheep

**Paul Heyhoe and Debbie Butcher from AHDB Market Intelligence** began the beef and sheep session with their outlook for the sector. The 2013 UK lamb kill was the highest for four years because of a large carryover of lambs from the 2012. Bad weather last winter resulted in a smaller 2013 lamb crop and less carryover, so sheep meat production is set to be lower in the first half of 2014. With better seasonal conditions, the 2014 lamb crop is expected to be more normal, which should mean increased supplies later in the year, with production little changed for 2014 as a whole.

Beef supplies have been tight for several years and only a 2% increase in production is expected this year. The downward trend in the suckler cow herd is continuing but there are increasing signs of optimism in the dairy sector (see below). However, even if this does lead to some expansion, it won't be reflected in increased beef supplies until well into 2015.

**Figure 2 Change in UK production of beef, lamb and pork**




*Source: Defra, AHDB Market Intelligence*

# AHDB Outlook Conference 2014

Margins for most beef and sheep producers remain negative, preventing any significant expansion. However, with beef and lamb supplies also tight globally, exports could grow if production were to expand. The top 10 export opportunities for British beef and lamb were identified by **Jean-Pierre Garnier, Export Manager from EBLEX**. The Far East, and particularly China, featured prominently, with Africa, the Middle East and Russia also in his sights.

## Pigs and Poultry

The pigs and poultry session began with **Stephen Howarth from AHDB Market Intelligence** on the outlook for the pig sector. The impact of high feed prices in 2012-13 was still being felt, with pig supplies expected to remain tight until the spring. Productivity gains should push up finished pig numbers later in the year, meaning a 2% rise in output for the whole of 2014. However, despite positive margins since the summer, pig producers remain cautious as a rise in feed prices like the one in 2012 could wipe out these profits very quickly.

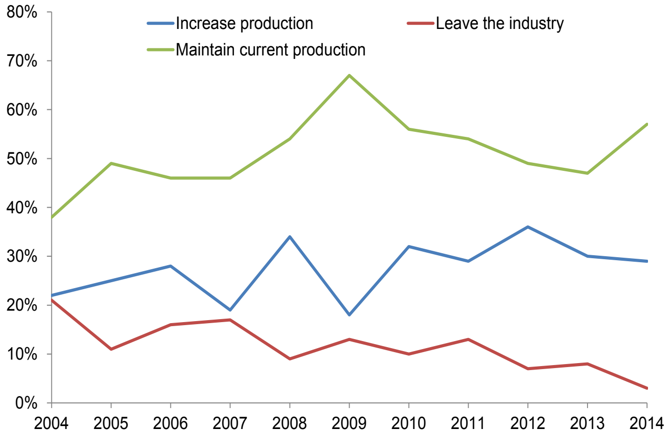
**Chris Dickinson from the NFU** then gave an overview of the poultry sector and some of the challenges it faces. Unlike the other meats, around three-quarters of production is vertically integrated, so producers are less exposed to market volatility. Nevertheless, the growth trend in UK consumption has reversed somewhat over the last year, due to price increases and fewer retail promotions. Despite this, producer confidence remains high and further expansion can be expected. However, this needs to be monitored to prevent over-production and falling prices.

## Dairy

Rob Newbery, Chief Dairy Advisor for the NFU began the dairy session by talking about the 'Leading the Way' strategy developed by Dairy UK, DairyCo and the NFU. The next steps are to build the momentum of support, populate the pillars with actions and activities and engage with interested parties. The strategy will be officially launched in the summer.

A preview of the results of the 'Farmer Intentions Survey', which was conducted in December 2013, was delivered by Julie Macleod from AHDB Market Intelligence. One of the key messages was that farmers' confidence has significantly increased, with only 4% of respondents planning to leave the industry in the next 2 years. Those planning to increase production remained stable while over half planned to maintain their current rate of production. Farmers also have stronger confidence in milk buyers and contracts.

**Figure 3 Production intentions of GB dairy farmers**




*Source: DairyCo Farmer Intentions Survey*

**Managing Director from Eucolait, Bart Van Belleghem**, speaking about the dairy industry post-quota, suggested that EU production is likely to see long term growth similar to the current rate. However, stronger growth is antcipated soon after quota ends in April 2015, slowing down in later years. Therefore, there is expected to be an increase in price volatility, especially over the shorter term.

## Concluding comments

The UK livestock sector is one of the major customers for arable producers. Overall, the outlook for these sectors suggests modest expansion over the coming year, which should lead to some increase in feed demand (all else being equal). However, margins are tight and any increase in costs (or decrease in producer prices) could alter the outlook. With feed a significant contributor to costs for all livestock producers (and dominant for pig and poultry producers), the medium-term outlook will be closely linked to developments in the global cereals and oilseeds markets.

Copies of presentations from the conference can be downloaded by clicking here.

## Key Points

- Meat supplies set to remain tight in 2014 but small increase expected from 2013 levels.
- Increasing optimism and ambition in the dairy sector could lead to rising production.
- Export opportunities available for livestock products but culture change needed to take advantage.

# Why Ukraine Matters to the Global Grain Market

***Growing instability in Ukraine has been closely watched by the world grain market for a number of weeks now, but the situation has only just started to have an impact on prices.***

**Jack Watts, Market Specialist team**
**02476 78760, [jack.watts@ahdb.org.uk](mailto:jack.watts@ahdb.org.uk)**
4 March 2014

## Introduction

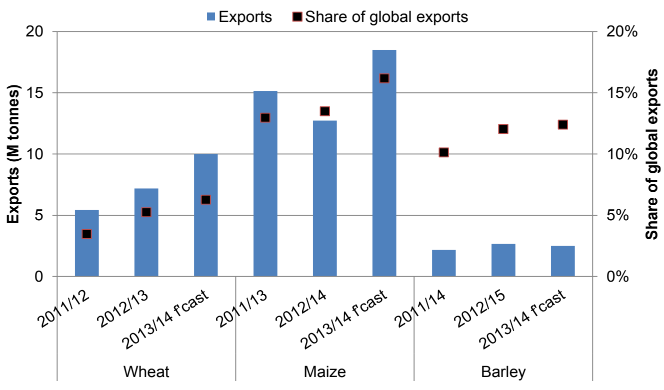
The ongoing unrest in Ukraine has recently helped support European and UK grain prices, with UK May-14 wheat futures settling at £162/t on 3 March, up £5.25/t in one day and **the largest daily movement for the May-14 contract since July 2012**. Although this has taken grain markets back to levels not seen since early January, prices of course remain some way below the c.£200/t levels a year ago due to the main fundamental of record global grain production in 2013/14.

## Ukraine's position in the global grain market

Ukraine has established itself as a prominent exporter of milling wheat and feed grains to the global market. Given the country's climatic conditions, its role in driving price usually comes about from changing supply dynamics, which are driven by factors such as winter kill, late springs and drought. However, 2013 production levels were good with the USDA estimating that 22.28Mt of wheat was produced, up 7Mt on 2012. The record maize crop at 30.9Mt (up 10Mt on 2012) is seen as a leading factor with **the country expected to be the world's third largest exporter** of the commodity this season behind the US and Brazil.

With production not an issue in 2013/14 for Ukraine, it is the ability of the country to move grain into export markets that is creating nervousness. Figure 1 summarises export estimates for Ukraine and its relative shares in the world market. Again it is clear from Figure 1 that maize is the front runner for the country –being exported to **key importers such as Egypt, Iran, Korea, Japan and the EU**. Even from a UK perspective there is some direct reliance on Ukrainian maize imports due to our low level of wheat production and the need for alternative feed grains.

**Figure 1 Ukranian grain exports and market share**



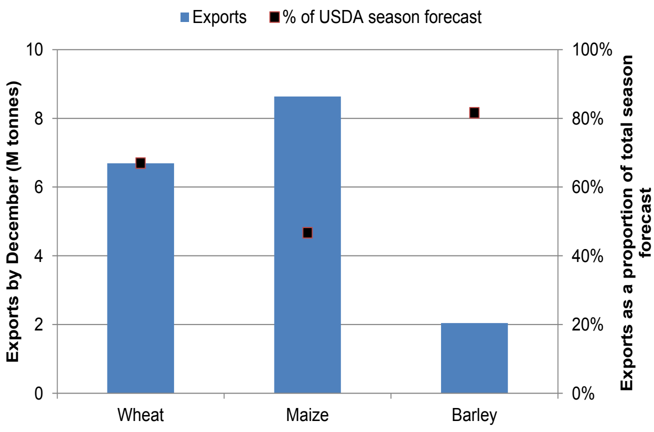

*Source: USDA*

## Timing is everything

To understand the market dynamic that Ukraine is creating, it is important to understand the timing. As is well understood, wheat and barley crops are harvested mid to late summer, which enables the marketing seasons of these crops to progress (typically from July) ahead of that of maize (typically from October), which is harvested in the autumn.

Keeping this in mind, Figure 2 gives an overview of grain exports up to and including December 2013. Based on the USDA total season forecasts, Ukrainian exports of wheat and barley at 67% and 82% are well ahead of maize at 47%. Essentially this means that **any export disruption caused by the situation would likely have a bigger impact for the progression of maize exports**.

**Figure 2 Ukranian grain exports by December 2013**




*Source: USDA/UkrAgroConsult*

## Closing comments – definitely one to watch

Despite the ongoing situation, market commentators in the region state that ports are **continuing to function as normal**. However, this is likely to be based on previous trade and an important factor will be if new sales can be maintained or whether traders and consumers will take a safer approach and move demand to other origins such as the US and South America. Certainly from the broader and fragile Ukrainian economy perspective, maintaining exports will be critical to any government.

Longer term, the market will want to assess the impact (if any) on the 2014 crop. **The spring planting season is just starting with Crimea** (the focus of the recent tensions) one of the first regions to start sowing. Some questions are being asked about financing the growing of the coming crop, but without a resultant impact in crop area or yield the market is unlikely to react to this matter at this point.



AHDB-HGCA
Stoneleigh Park
Kenilworth
CV8 2TL. UK

T +44 (0) 24 7647 8760
F +44 (0) 24 7647 8904
mi@hgca.com
www.hgca.com