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HGCA MI Prospects

AHDB Agriculture & Horticulture DEVELOPMENT BOARD

# Analyst's Insight: No splendid isolation for grain and oilseed markets

While the grain and oilseeds market takes most of its cues from the fundamental drivers of supply and demand, it does not operate in isolation. The **markets sit against a wider global economic backdrop** – which is often more in focus when fundamental news thins, such as towards the end of the calendar year. So what does the bigger picture show?

The **US and Eurozone economies continue to diverge**. Recently the European Central Bank scaled back its projections for economic growth in the Eurozone in 2015, from the 1.6% forecast three months ago to 1%. In contrast, the Organisation for Economic Co-operation and Development recently forecast US economic growth in 2015 at 3.1%.

Nonetheless, not all is positive in the US – the current budget deal expires on 11 December, and immigration policy is a key sticking point for a new deal. Negotiations are underway to try and avoid a Federal shutdown, as was seen in October 2013, which would restrict the flow of US data to the global market.

There is **also talk of further declines in the rate of economic growth in China**, though this is always subject to debate due to the nature of the managed economy in the country. However, lower Chinese demand has been mooted as part of the reason for a recent fall in iron ore and copper prices; purchases of these commodities are often seen as a precursor to economic growth.

A reduction in global economic growth may cap the potential growth in demand for grains and oilseeds on the back of lower prices.

More immediately, changes to the relative strength / weakness between economies hits grain and oilseed markets via exchange rates. The strength of US dollar is likely to have a limiting effect on grain prices as several of the 'benchmark' futures for our markets are traded in US dollars, and the US dollar is at a four year high against a basket of currencies.

**One factor, which many commentators are looking to stimulate global economic growth, is the fall in crude oil prices** to a five year low. While currently bearish for oilseed prices (due to the price link between vegetable oils and biodiesel), longer term, if lower crude oil values stimulate economic growth, it is likely to prove positive for grain and oilseed demand.

In short, the 'bigger picture' is a mixed one as the grain market heads for the half-way point in the 2014/15 marketing season, but it is definitely still better than when the 'credit crunch' was at its height.

**Helen Plant**

**Save the date!**
AHDB/HGCA's Grain Market Outlook Conference will take place on Wednesday 14 October 2015 at the Grange Tower Bridge Hotel, situated near the Tower of London. Further details to follow closer to the time.

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# Initial concerns over Black Sea grain production and trade prove to be unfounded

***Earlier this season, political tensions raised concerns regarding the levels of grain production and trade in the Black Sea region. Despite this, the region has fared particularly well from grain harvests in 2014/15, with a continued appetite from the world export market.***

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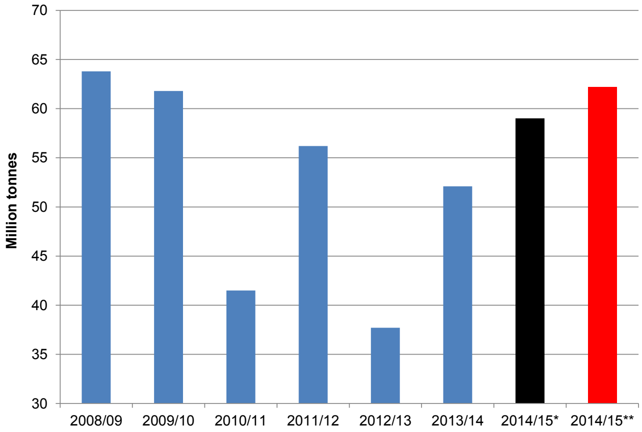
28 November 2014

## Russia

**Wheat output in Russia this season has reached volumes not seen since 2009/10.**

According to the Russian Federation Ministry of Agriculture, 62.2Mt was harvested this year, up 14% on last year's output and 3.2Mt higher than the USDA's current forecast. The record wheat crop is a result of significantly higher yields in 2014/15 (2.61t/ha), compared with 2.29t/ha in 2013/14. Harvesting of both spring cereals and maize has progressed without any adverse weather constraints.

**Figure 1 Russian wheat production**



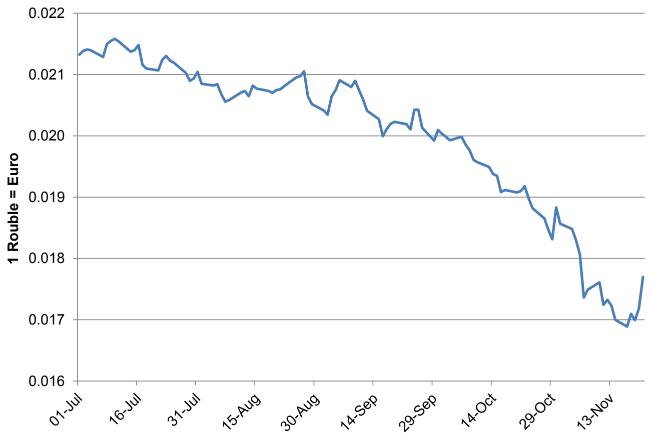

** USDA f'cast **Russian Ministry of Agriculture estimate*
*Source: USDA / Russian Ministry of Agriculture*

Russia commenced the 2014/15 season with exceptionally high shipments of wheat (during July and August). Despite this promising outlook, **Russian wheat exports lost momentum during September and into October, as export prices struggled to keep pace with the price declines from other suppliers.** This allowed EU wheat to have a competitive advantage, as the EU harvest (particularly feed wheat) arrived on the market.

At the end of October, Russia made a comeback to the wheat export market. This was partly attributed to the weakening of the Russian currency as well as a period of rising global grain prices, allowing the country's wheat crop to edge back into a competitive position in the global market.

Russia is also looking at record output volumes of barley (19.5Mt this year, the largest volume since 2008/09) and maize (12Mt this year compared with 11.6Mt in 2013 and the highest output on record for Russia) this year. Barley and maize are the other two largest grains produced in the country.

**Figure 2 Depreciation of Russian Rouble against the Euro**




*Source: AHDB/HGCA*

In recent weeks, there has been some speculation regarding the establishment of the autumn planted wheat crop for 2015. The analytical firm, SovEcon, reported the winter wheat crop as being in an 'extremely weak condition'. Colder than usual weather has also risen concerns (see Tuesday's Grain Market Daily). Despite these early reports, spring planting conditions provide more of an insight into the state of the 2015 crop.

## Ukraine

**Production of wheat in Ukraine is estimated to be 24.5Mt this year (USDA), up from 22.3Mt in 2013/14.** It has been reported that the quality of the Ukrainian wheat crop suffered due to heavy rains during the summer, as was the case for parts of Europe. This resulted in the proportion of feed wheat to be estimated as 35% of the total wheat harvest, up from 25-30% last year. The grain harvest in Ukraine is now almost complete. UkrAgroConsult have reported that 97% of the planted area was harvested as at 20 November, totalling 62Mt of grain which is similar to last year's output. Of the total grains harvested, maize is estimated to make up 25.5Mt (30.9Mt last year).

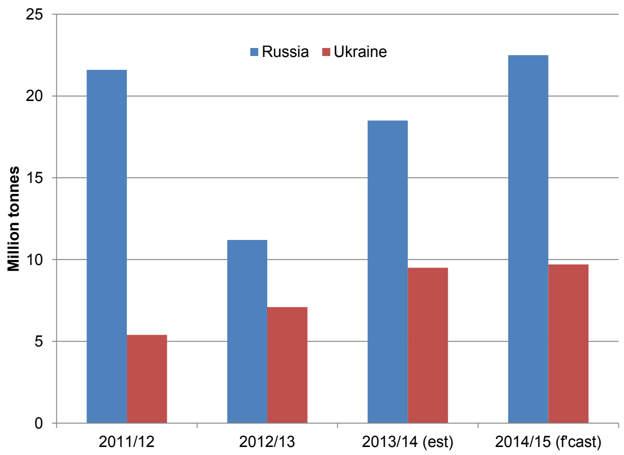
The general situation in Ukraine this year has been characterised as "**one of the most troublesome in its 23 year history**" (UkrAgroConsult), as a result of geopolitical tensions which caused the economic downturn of the Ukrainian economy. Despite the loss of assets in the Donetsk and Lubansk regions of Ukraine, **agricultural commodities are said to be the only group of goods whose exports are on the rise**, with exports to the EU up 15.2% year-on-year.

The latest trade estimates indicate that 1.7Mt of wheat were exported from Ukraine in October (6.2Mt during this season to end-October). Egypt was the key importing destination in October, making up 17% of all

# Initial concerns over Black Sea grain production and trade prove to be unfounded

wheat exports. The International Grains Council (IGC) estimate that Ukraine's total grain exports will be 30.1Mt this year (32.2Mt last year), despite concerns that Ukrainian grains could have difficulty entering the export arena this year.

**Figure 3 Wheat exports from Russia and Ukraine**




*Source: IGC*

Looking ahead, 82% of winter grains are said in good/ satisfactory conditions (including 83.6% of the winter wheat crop). Recent reports however suggest a diminished Ukrainian barley crop this season, as a result of a loss of area and reportedly around 30% of the planted area in some regions as being in weak and sparse condition. According to UkrAgroConsult, 2% more winter cereals have been planted than was forecasted, to an area of 7.6Mha in Ukraine by 20 November.

## Romania and Bulgaria

Romania, like many European countries, faced difficulties as a result of a wetter than usual summer this year. Strategie Grains initially reported that wheat grain quality would be downgraded on account of the wet weather, meaning that the proportion of milling wheat in the total wheat harvest was estimated at 50% compared with 55% in 2014/15. Strategie Grains have reduced their earlier estimates of **soft wheat production in 2014/15 by 60Kt to 7.57Mt, due to a small decrease in yield**.

However, **weather conditions have been favourable for the maize crop, with dry weather contributing to expected yields at, or near to, record levels** for both maize and sunflowerseed crops (EU MARS crop bulletin). Strategie Grains have recently raised their earlier forecasts for Romanian maize output to 10.84Mt due to the prospect of record yields at 4.30t/ha.

Total grain exports from Romania are forecast to be 4.3Mt in 2014/15, down by over 600Kt on 2013/14. This is partly as a result of **Romanian exports losing out to Ukraine for the key Egyptian import market**.

In Bulgaria, according to the EU Commission's October MARS crop bulletin, abundant rainfall has caused significant problems for this year's maize and sunflower harvest, with high moisture content for both crops. High mycotoxin levels have been reported for maize samples.

Bulgaria is expected to reap 4.7Mt of wheat this year, down from 5.24Mt last year. **Milling wheat quality has also suffered in Bulgaria this year, with the proportion of milling wheat falling by 5 percentage points to 25% this year compared with last year and 80% in 2012/13**. The lower export capacity of Bulgaria's Black Sea grain ports also increases the challenge the country faces when competing with Russia and Ukraine for exports.

## Closing comments

At this stage in the season, market attention is focussed on continued trade of the newly harvested crop, as well as prospects for weather conditions for the planted new crop. Crop production and trade in the Black Sea region has not suffered to the extent that was initially feared when political tensions surfaced earlier this year. Looking ahead to the crop for 2015/16, although plantings in Ukraine have progressed well, there are some concerns for the Russian wheat crop. Aside from the ongoing political and financial situation, the weather remains as a key factor to watch.

### Key Points

- Wheat output in Russia this season has reached volumes not seen since 2009/10
- Agriculture commodities are said to be the only group of goods whose exports are on the rise in Ukraine this year
- The proportion of milling wheat in Bulgaria and Romania is reduced this season due to wet weather

# Will the funds 'crush' soyabean demand?

*The 'funds' have developed sizeable net longs on soya oil and are beginning to reduce their large long positions in Chicago soyameal futures, whilst maintaining a shortened net position in Chicago soyabeans. By taking positions favouring smaller gross crush margins, the currently strong incentive to crush soyabeans may be reduced which could have knock-on effects for UK rapeseed prices.*

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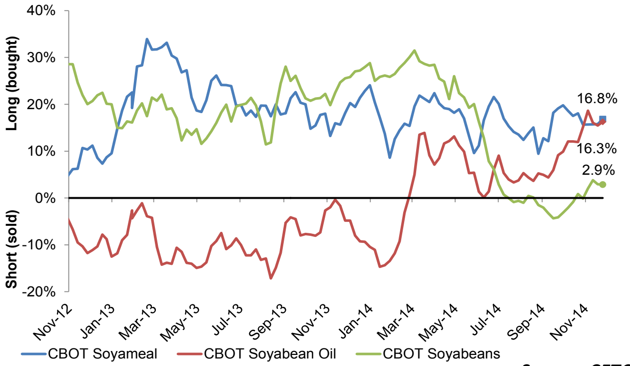
2 December 2014

Non-commercial traders (the 'funds' - traders not involved in the physical market) in the US futures markets have held a much less bullish view towards soyabean prices since July than they held for the past three years. An outlook far closer to neutral, based their net positions, reflected the bearish direction in prices. However, with gross crush margins expanding recently, the funds are taking positions anticipating that margins will reduce once more. While the funds will react to anticipated market movements by selling contracts (taking a 'short', bearish position) or buying contracts (taking a 'long', bullish position), the scale of this can, in turn, amplify or dampen price movements once they occur.

## The funds are making the soy complex, complex

The situation becomes more complex when we look at fund involvement in soya meal and oil markets, the co-products of soyabean crushing. It must be remembered that European rapemeal and rapeseed oil prices are heavily related to soyameal and soyabean oil prices, as they compete in the same market.

**Figure 1 Net positions held by Non-commercial traders (the funds) as a percentage of Open Interest**



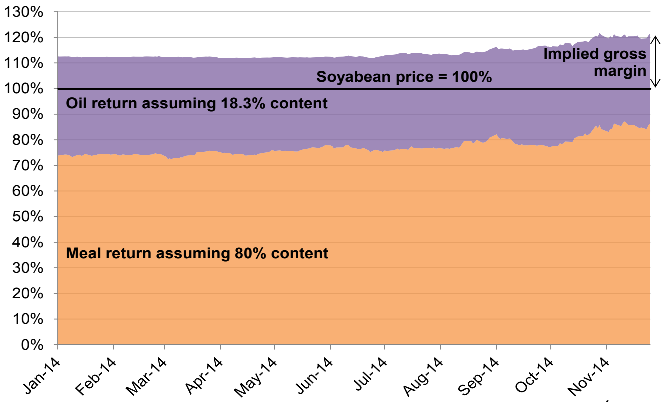

*Source: CFTC*

- Soyameal: Funds remain significantly long although there is a recent downtrend in the net-long position. Soya meal is the world's 'go to' source of animal feed protein and as such the demand is very challenging for the market to regulate – which likely explains the long-term net-long positioning.
- Soya oil: Funds have built substantial net-long positions – especially in recent weeks. This could well be linked to the fact that soya oil currently has historically low premiums to palm oil, which is a lower quality grade of vegetable oil for food use, with investors speculating that a premium may have to re-establish at some point.

**Shortening soyameal positions as gross crush margins widen**

Soyameal has been an important driver of the recent soyabean price rally, with increasing gross margins from strong soyameal prices (see Figure 2) offering increasing incentives to crush. By tightening supplies across the oilseed complex, this has pulled rapeseed prices up also.

**Figure 2 Implied Jan-15 Chicago futures crush returns as a percentage of soyabean values**




*Source: AHDB/HGCA*

Although the funds are maintaining a relatively bullish outlook on soyameal, their net position has shortened since early-Sep while positions on soyabeans have simultaneously lengthened. Funds are likely to be of the view that soyameal can't rise much more in price without having a greater upward influence on soyabeans.

The funds' net positions on soyameal may well continue to shorten, potentially dampening the soyameal price rally that has driven the oilseeds complex. However, if positions on soyabeans become noticeably longer once more, this would add upward price pressure to narrow the price spread with soyameal. The relative contribution of oil to crush margins has also been decreasing, likely adding to the funds' lengthening position on soya oil in anticipation of oil and meal contributing to more 'normal' proportions of crush margins. Either way, fund activities are likely to continue adding pressure to narrow the soya complex price spread, in turn reducing gross crush margins.

## Conclusion

EU rapemeal and rapeseed oil prices are heavily related to soyameal and soyabean oil prices, as they compete in the same market. As such, fund activity in the soya complex futures can indirectly impact the UK rapeseed market.

If fund activity continues to shorten positions on soyameal relative to soyabean futures, it could imply that crush margins are going to narrow. This would reduce the currently strong incentive to crush soyabeans, which may result in a corresponding reduction in the physical supplies of soyameal and soya oil in the market. With less competition for rapemeal and rapeseed oil in the food, biodiesel and animal feed industries, this may act to sustain rapeseed demand in the short term. However, supplies of rape oil and rape meal will continue to be driven by the amount of rapeseed that is crushed and this will continue to be a function of if and how prices in the whole oilseed complex continue to move together.

# Another bumper oat crop for the UK

***Although down 14% from last year, the 2014 UK oat crop is still 20% above the average for 2008-2012. With the largest carry-over in recent seasons, balancing the 2014 crop may be tricky, and exports and animal feed demand will be key areas to watch. However, if a smaller area for harvest 2015 is realised, a higher carry-over may be welcome.***

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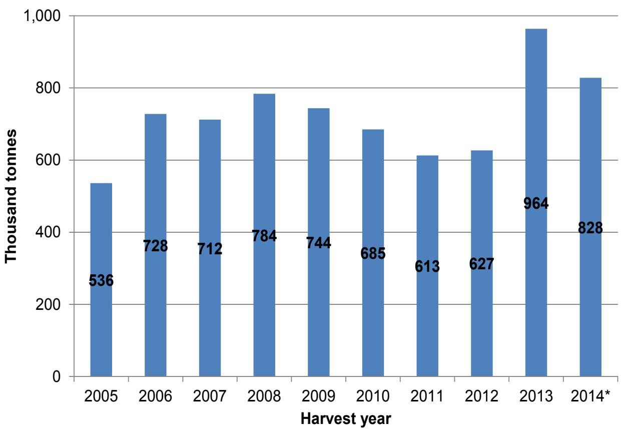
4 December 2014

## Bumper oat production for the UK in 2014

The UK oat crop in 2014 is provisionally estimated at 828Kt by Defra (see Figure 1). While this represents a 14% decline from last season's exceptional crop, it is still 20% above the average for 2008-2012, and the second largest crop in 40 years (behind last year). Although the area planted to oats is estimated to have fallen by 23% to 136Kha, this is partially offset by provisionally the highest average yield (5.9t/ha) since 2006. Final results are expected on 18 December.

**Figure 1 UK oat production**



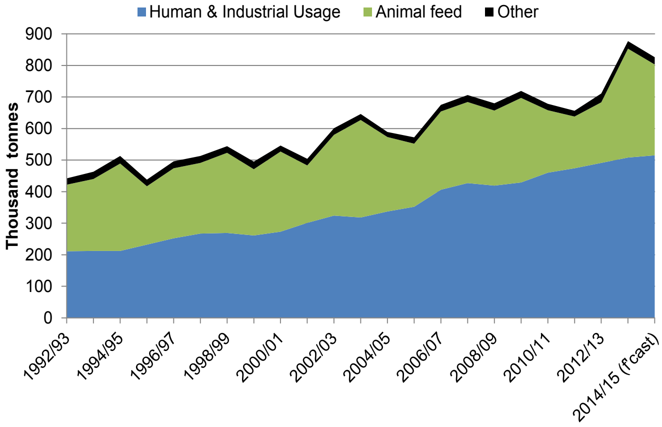

**provisional* *Source: Defra*

With the largest amount of oats carried into this season in recent times (166Kt) and another large crop in 2014, absorbing the crop could be a challenge. However, quality was generally reported as satisfactory, read more in the final 2014 ADAS harvest report, which should limit import requirements.

## Animal feed demand - a key watch area

The first supply and demand estimates from Defra for 2014/15 point to a reduction in the amount of oats used as animal feed from last season's high (Figure 2). Although down 17% year-on-year, at 288Kt, the forecast for oats used as animal feed would still be the third highest level in the past 20 years, behind only 2013/14 and 2003/04. **Animal feed demand would still account for over a third of total UK oat demand.**

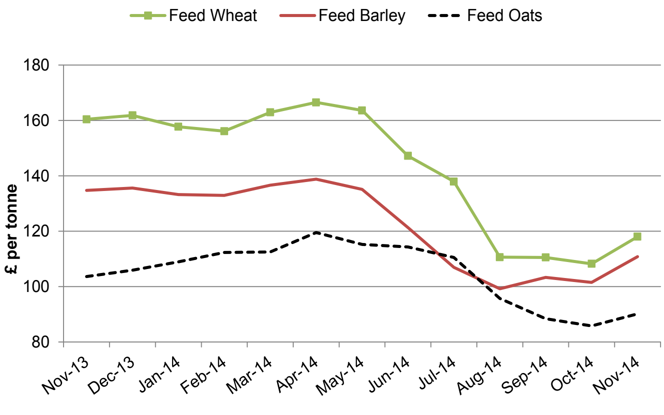
**Figure 2 Usage of oats within the UK**




*Source: Defra*

The supply and demand commentary indicates that a larger decline is expected in compound feed use of oats, compared with fed on farm; a trend supported by price relationships (Figure 3). In 2013/14, UK ex-farm prices for feed oats were on average nearly £43/t lower than those for feed wheat and £19/t less than the season average for feed barley. Last season a record 120.4Kt of oats were used in retail compound feed production. So far this season (up to 27 Nov), the discounts for feed oat prices to feed wheat and barley have been smaller, at £20.20/t and £12.50/t respectively. However, the discounts have begun to widen over the past month or so, making **animal feed demand for oats an important watch area**.

**Figure 3 Monthly average UK ex-farm prices for feed grains**




*Source: AHDB-HGCA Corn Returns*

## Human & Industrial demand continues to grow

The amount of oats used for human and industrial (H&I) purposes is expected to continue to grow this season, although the current information suggests at a slower rate (Defra). Over the past five seasons, oat H&I demand has grown by 4%, or 18Kt per season (on average); in 2014/15 a more modest increase of 1% or 7Kt is expected.

A greater proportion of this demand is expected to be met by home-grown oats, leading to an overall **increase in home-grown usage to a new record of 492Kt**.

# Another bumper oat crop for the UK

In 2014/15, 96% of the forecast H&I usage figure to be used is projected to be home-grown, up from 92% (465Kt) last season, which had strong imports in the early months of the season.

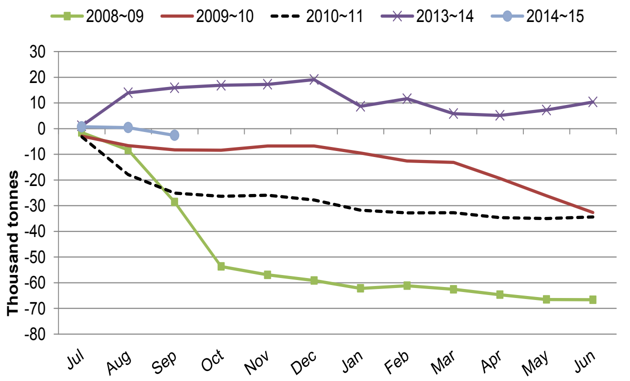
## Better start for exports but still lagging the pace needed

So far, **UK oat exports have got off to better start than last season** with 16Kt exported in July – September; the equivalent for 2013/14 was 6.8Kt. However, when compared to imports this still gives a net-export figure of less than 3Kt (see Figure 4).

**Figure 4 UK cumulative net-trade in oats, selected years**

Net-imports shown as postive, adding to UK supplies

Net-exports shown as negative, reducing the UK surplus



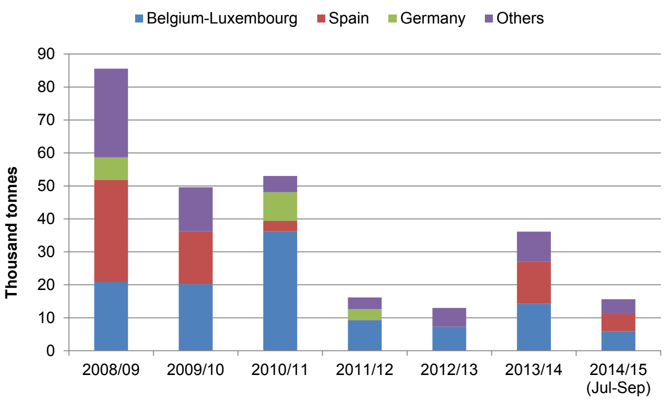

*Source: HMR&C*

For the 2014/15 season as whole, Defra currently forecast the exportable surplus at 50Kt versus imports of 20Kt, or potential net-exports of 30Kt. Figure 4 shows how the pace of exports relative to imports compares to the last time the UK was a net-exporter of oats, in 2009/10 and 2010/11. If the current forecasts are to be realised, the relative pace of exports needs to pick up.

## Export potential?

Belgium-Luxembourg and Spain have been the most consistent destinations for UK oats in recent seasons – together accounting for around 60% or more of total exports (see Figure 5).

**Figure 5 UK oat exports by destination**




*Source: HMR&C*

Although Germany is Europe's largest oat importer, it is rarely a destination for UK oats due to quality requirements and competition from the EU's largest oat exporters, Finland and Sweden.

**Spain has potentially increased grain import requirements** this season, after dry weather reduced yields, and impacted pasture conditions. The 2014 Spanish oat crop is estimated at 671Kt, down 30% from last season (965Kt) by the Spanish Ministry of Agriculture. However, the exact levels of **oat imports will depend on the price relative to other grains**. So far this season, Spain has imported increased volumes of maize from the US, as well as wheat from the Black Sea region (Jul-Sep), and France (Jul-Aug).

## Concluding comments

The challenge for the UK this season will be absorbing another large oat crop, after last season's bumper crop. As for the UK's other main grains, exports and animal feed demand will be key in order to avoid further stock build up. The next estimates of UK supply and demand this season will be released by Defra on 28 January 2015.

The Early Bird Survey points to a potentially smaller UK oat area for harvest 2015. If the lower areas are realised, then an above average carry-over into 2015/16 as is currently forecast for the UK (138Kt vs 2008-2012 average of 80Kt), may provide some cushion.

More information on winter crop areas will be provided by the AHDB-HGCA winter planting survey in early March.

## Key Points

- A second large UK oat production year
- Slower growth in H&I usage forecast
- Animal feed demand and exports key watch areas for 2014 / 15

# Australian crop forecasts revised lower but strong global supplies provide cushion

***The latest Australian crop report shows a further decline in production forecasts due to dry weather and unfavourable crop conditions for majority of the country. However, the impact of this is not as severe as was the case in 2006/07 and is mitigated this season by high global production forecasts.***

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9 December 2014

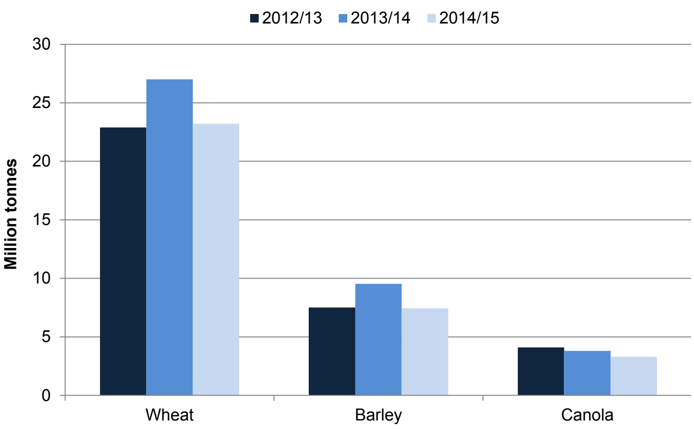
## Introduction

Drier than average weather conditions have led to concerns over the quantity and quality of Australian winter crops. This has led to the downward revision of crop production forecasts prospects in 2014/15 (Figure 1).

**The recent estimates from ABARES, the Australian government's department of Agriculture, peg total winter crop production at 37Mt, down from 38.6Mt in their previous estimates in September, and 16% lower year on year**. However, despite the reduction, this figure is still 4% higher than the previous ten year average.

In percentage terms, the largest year on year decline is seen for barley which, at 7.4Mt, is 22% lower compared with 2013/14. Canola (rapeseed) and wheat production forecasts are down 12% and 14% on the year respectively.

**Figure 1 Australian Winter Crop Production**




*Source: ABARES*

## Wheat

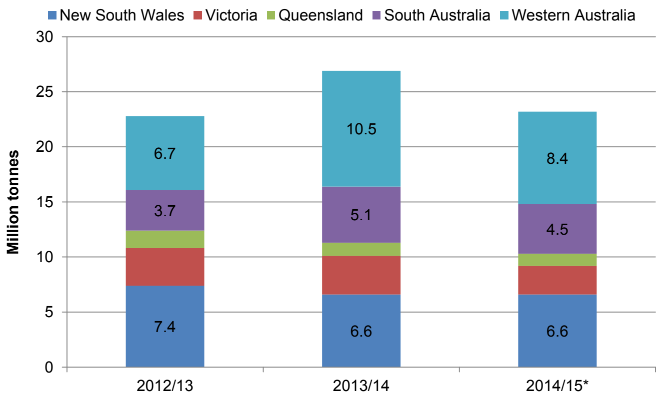
The total Australian wheat area this season is forecast at 13.8Mha, up 2% year on year, although as previously mentioned, production is forecast to fall from last year. Compared with estimates made in September, wheat production has been revised 1Mt lower to 23.2Mt reflecting the detrimental effect of unfavourable weather conditions during this period.

In Western Australia (WA), the weather was favourable at the start of spring, but soon turned. During October, hail and rain damaged certain areas of crops in central regions of the state, which resulted in quality downgrades for some cropping areas. **The wheat production forecast for WA in 2014/15 is 20% lower year-on-year at 8.4Mt** (Figure 2).

Unfavourable weather conditions were also experienced in New South Wales (NSW), including lower than average rainfall and above average temperatures, which led to the depletion of soil moisture levels throughout September and October. **Average wheat yields in NSW are forecast to reach 1.7t/ha.**

In South Australia, higher levels of precipitation were received which was favourable for the crops. However, during the second half of the winter season, the weather deteriorated with lower than average rainfall and higher temperatures. Winter wheat production for this region is forecast to fall by 12% to 4.5Mt, in comparison to 5.1Mt produced last year.

**Figure 2 Australian wheat production by state**

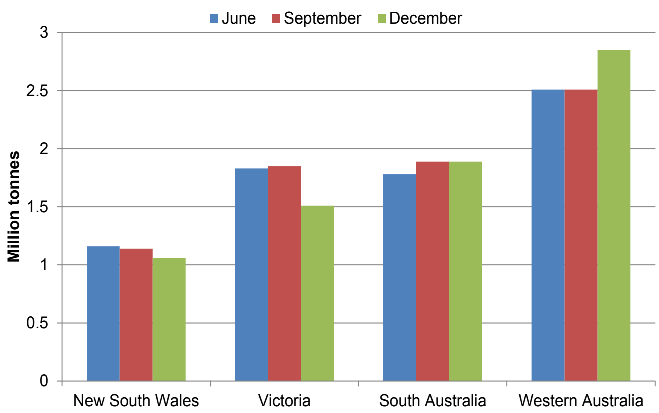



*Source: ABARES*

## Barley

At 7.4Mt, total barley production is similar to September's estimate. However, at the state level, various changes have been made, including a 0.3Mt downward revision for Victoria (Figure 3). This is mainly due to a further decline in the average state yield which is now estimated to be 30% lower year-on-year. The forecast for production in WA has been revised upwards as above average rainfall was received in September for some cropping regions within the state.

**Figure 3 Australian barley production forecasts**




*Source: ABARES*

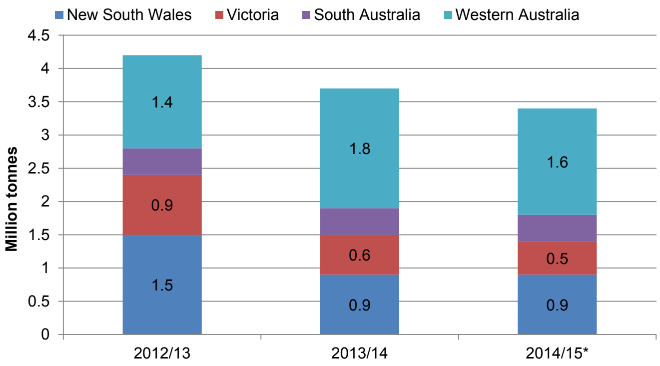
# Australian crop forecasts revised lower but strong global supplies provide cushion

## Canola (rapeseed)

**The forecast for Australian canola production now stands at 3.3Mt**, down 12% year on year and 0.1Mt lower than the estimates made in September.

In WA the canola production forecast is 1.6Mt, 13% lower than 2013/14 (Figure 4). Average yields are forecast to fall by a noteworthy 14% year-on-year, despite a slight area increase (2%).

**Figure 4 Australian canola (rapeseed) production by state**




*f'cast *Source: ABARES*

## More dry weather on the horizon

October was a particularly dry month for Australia, with 'below average' rainfall experienced for most of the country. On a national scale it was the seventh driest October on record, and some areas of Victoria and NSW experienced the driest October on record.

The Australian Bureau of Meteorology's monthly outlook for December rainfall indicates that a drier than usual month is likely for NSW and Queensland. The weather outlook for December 2014-February 2015 suggests that there is a chance of below average rainfall for cropping zones, which could lead to further depletion of soil moisture levels and thus further quality downgrades.

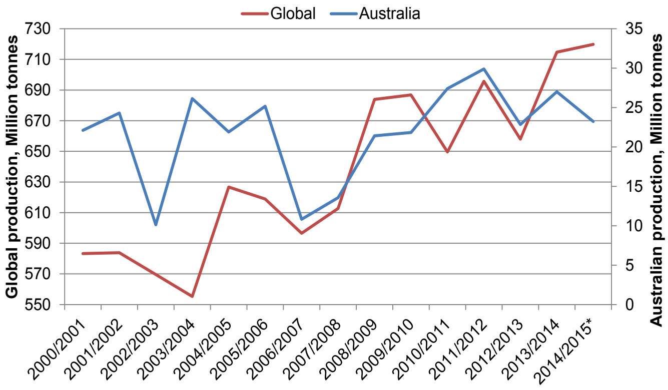
**Concerns about a forthcoming "El Niño" weather event, seem to have been partially confirmed** due to weather conditions that are currently being experienced. Temperatures in the tropical Pacific Ocean have been reported as 'average' to cooler than average' in areas surrounding northern Australia. A model designed by the Australian Bureau of Meteorology shows that El Niño-like weather conditions are likely to be at the strongest in December but should diminish into January and February.

## Global wheat export share to remain stable

Australia is one the world's top wheat exporters and over the past ten seasons has exported an average of 70% of total domestic output per year. In 2014/15, Australia is forecast to export 17.5Mt of wheat, an 11% share of the total global export forecast (USDA), a similar level to 2013/14 but slightly below 2012/13 when 18.7Mt (14%) was exported.

In 2006/07, when severe drought previously damaged Australian crop production, levels of global production were also low (Figure 5). However, this season ample global production forecasts are creating some cushioning for the market.

**Figure 5 Wheat production**




* Forecast
NB: 2014/15 Australian wheat production estimate is from ABARES
*Source: USDA / ABARES*

## Concluding comments

Despite unfavourable weather conditions parts of Australia hampering crop progress, and the downward revision of the country's wheat output, the impact of this is limited by good crop production elsewhere this season. Although the market has been concerned about the quality of crops in Australia, record levels of production at a global level mean that there is a sufficient cushion to offset any output declines in the country.

## Key Points

- The forecast for total winter crop production has decreased by 16% year on year
- The barley production forecast is 22% lower year on year
- The scale of global production forecasts are likely to outweigh the concern over drier weather in Australia



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