

# ABSA AgriBusiness

## Agric – Economic Outlook

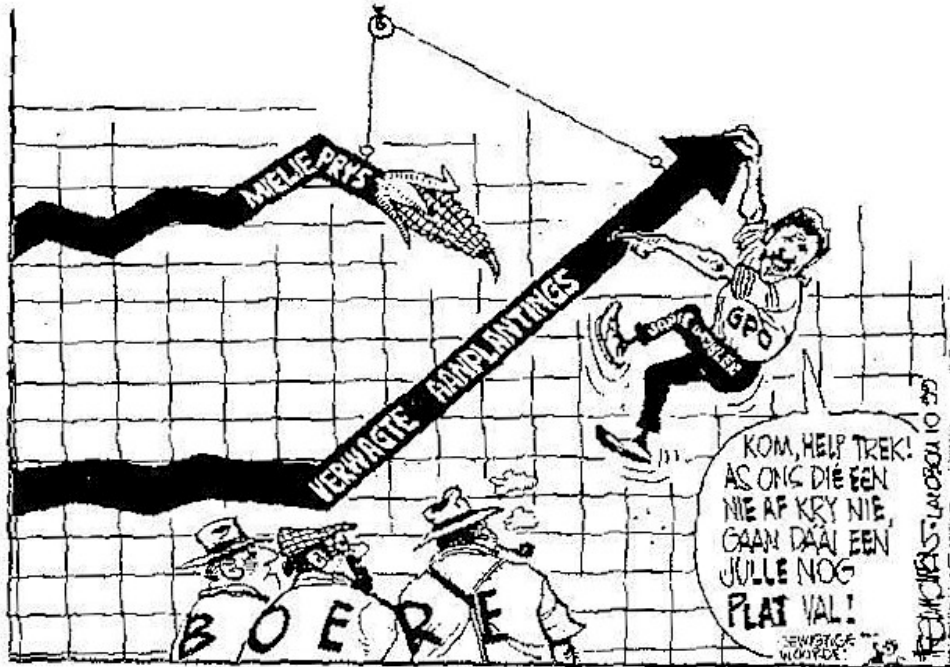
4 May 2010

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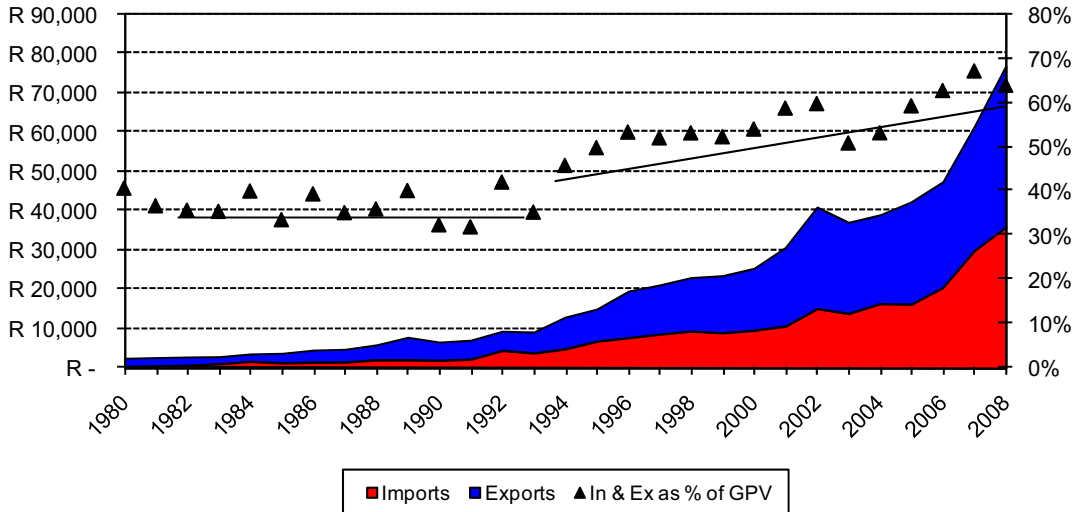
  
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# SA Farmers are international players in an international market

## SA Agriculture exposure to International market



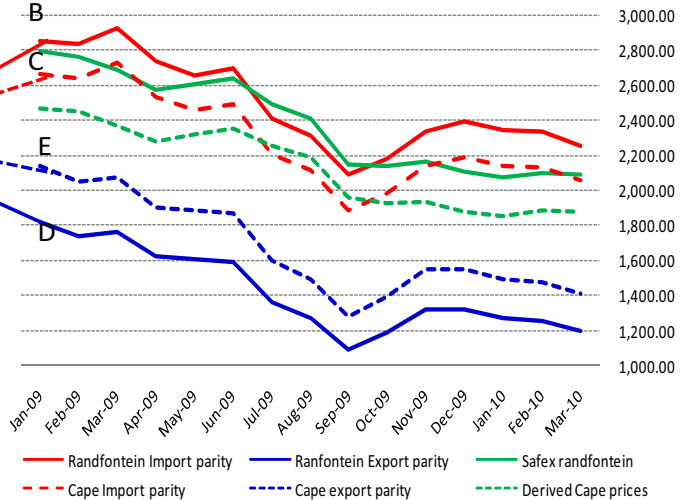
# Wheat import export and effect of transport differential on Cape Wheat prices

A. Import and export parity price on ship in harbour is identical (International price x Exchange rate)

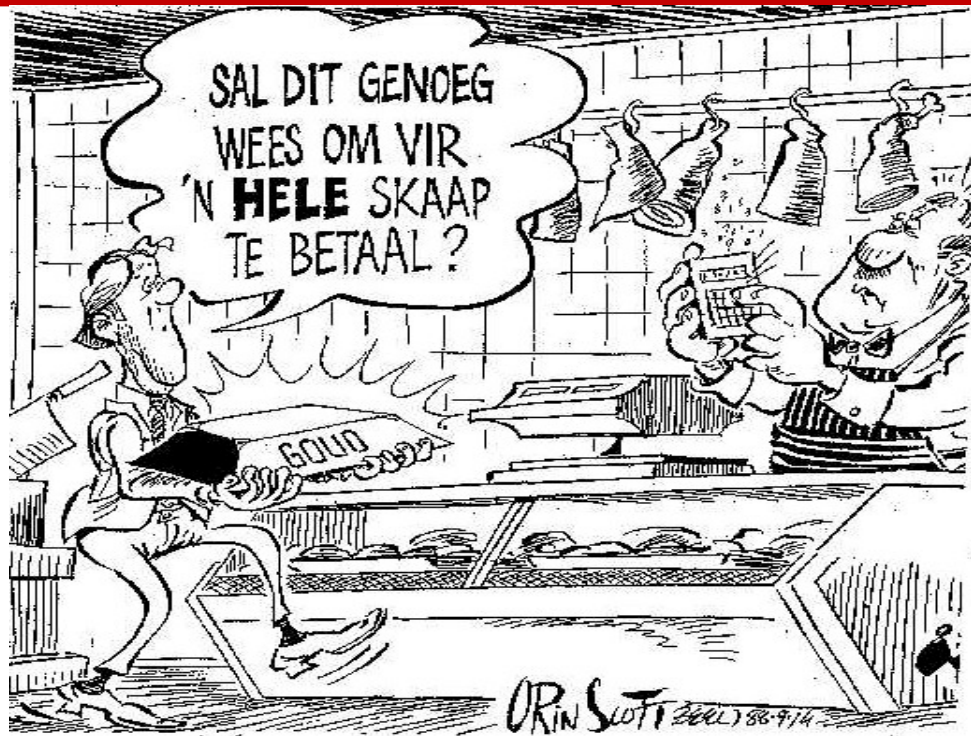


- B. Import parity price equals (A) plus freight, discharge, unload, spillage, moisture, finance, insurance, tariff and transport costs
- C. Cape town import parity price equals (B) minus transport costs
- D. Export parity price equals (A) minus upload and transport costs
- E. Cape Town export price equals (D) minus transport costs

## SA wheat prices



- Pointers:
- a) Cape town wheat prices as closely correlated to Randfontein Safex prices and do like Safex prices trend import parity prices with the same degree of accuracy
  - b) Transport differential will always be priced into the equation with defined periods under and over import parity prices dependent on surplus a shortage situations

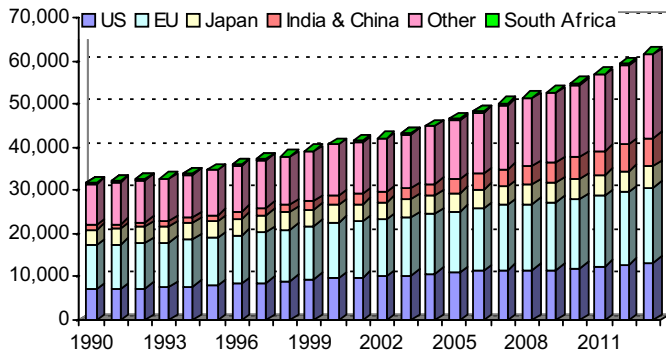


# Economic outlook - World trends

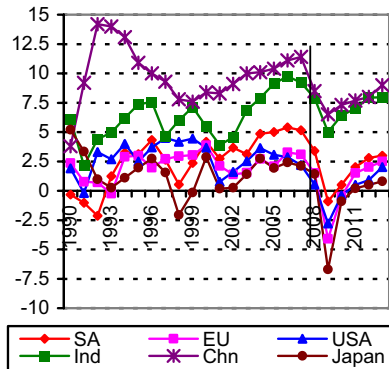
## Pointers

- World economy rebound to new heights after 911 but has recently declined substantially due to problems in US financial markets
- This is further compounded by Europe continue to struggle mainly due to the strength of their exchange rate
- South Africa's performance has also weakened due to higher interests rates
- A decrease in consumer demand due to a slowdown in the economic has placed downward pressure on agricultural commodity prices in general

### GDP For selected countries (Billion US \$)



### Economic growth trends (%)



Sources: Euromonitor, The Economist, OECD, World Bank and International Monetary Fund

# World agriculture commodity prices to increase substantial over the medium term

There are two main driving forces at work that will have a positive impact on agricultural commodity prices namely:

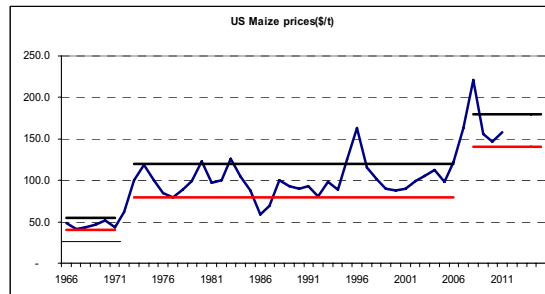
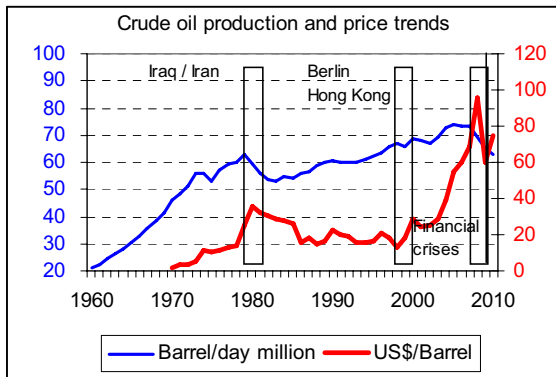
- **Global Warming**

Sentiment around global warming is **driving legislature around the world to continuously push for the implementation of so-called carbon friendly legislation**. As agriculture is the prime beneficiary this type of legislation (due to the ability of plants to extract carbon from the air) new markets will place upward pressure on agricultural commodity prices. Agriculture could however never produce enough energy to replace all fossil fuels.

- **Demand for Food and Energy**

During the late nineties Capitalism replaced Communism as economic system in the world (signs of the time where the collapse of the Berlin wall in '98 the repatriation of Hong Kong in to China in '99)

This led to an exponential economic growth in Eastern European, Middle East and Asian countries with a resulting **increase in the buying power of these consumers, hence the growth in demand for food and energy**

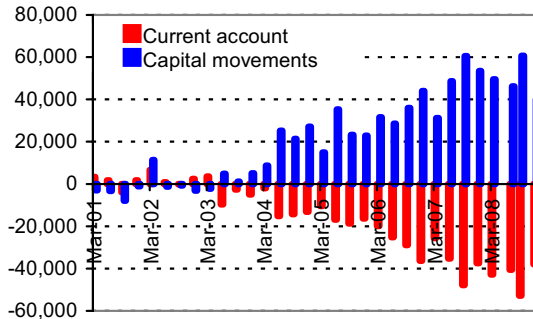


# Economic outlook - SA GDP & BOB trends

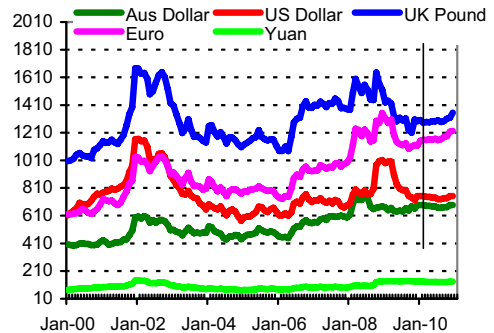
## Pointers

- **Balance of Payment indicators:**
  - Interest rates will remain relatively high compared to inflation in a bid to draw capital in to South Africa.
  - The exchange rate should tend to soften especially against the Euro while holding firm against the Dollar.
  - Import inflation could rise due to weaker rand thus placing pressure interest rates
- **Exchange rate indicators**
  - US Dollar and Chinese currencies will tend to strengthen against the Rand but weaken against the Euro
  - This is mainly due to the link between the US dollar and the Chinese Yuan as well as the current account deficit of the US (+/- 6% of GDP)
  - The Rand is expected to continue to weaken against the bulk of the other currencies

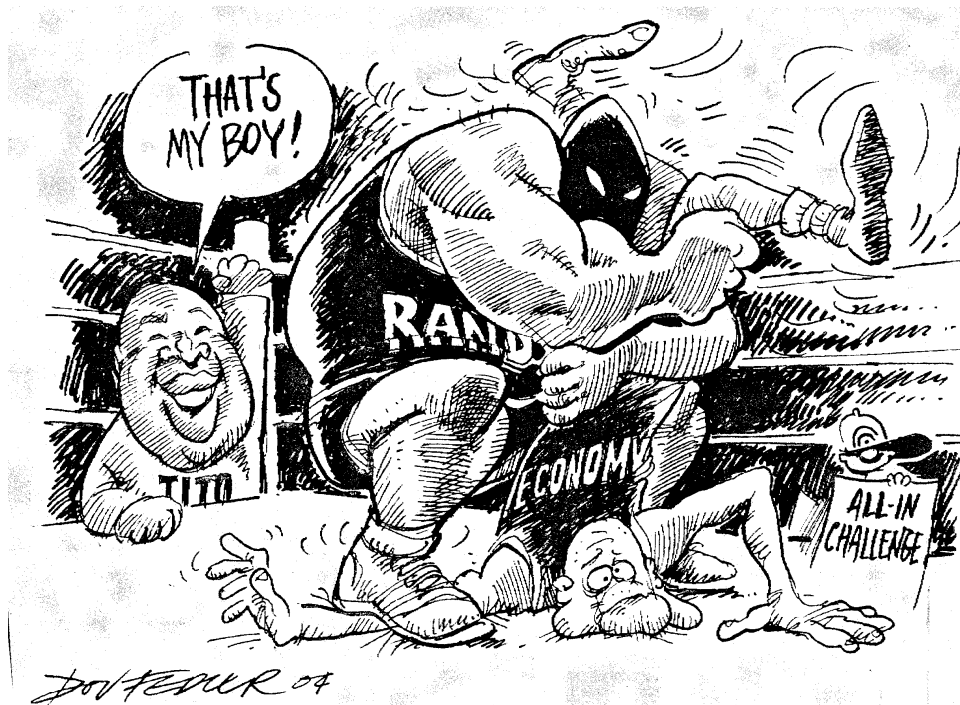
**Relation between Long-term capital movements and Balance on current Account (R '000 000)**



**Nominal exchange rates(SA cents / Fc unit)**





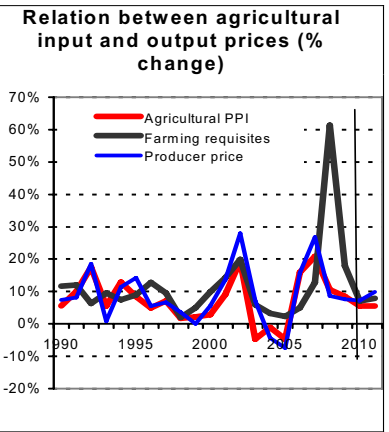
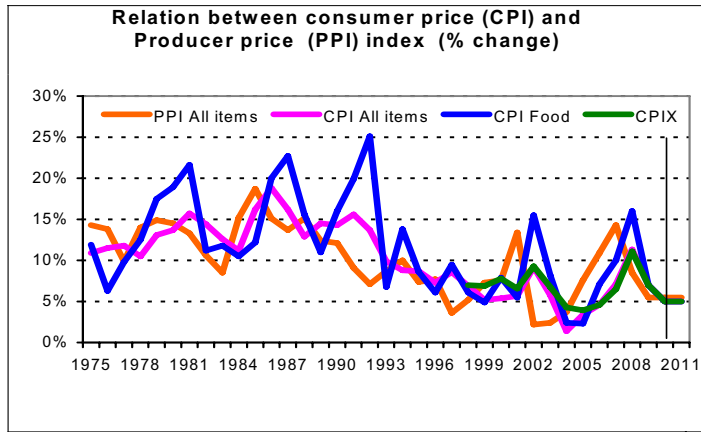


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# Economic outlook - Inflation

## Pointers

- Due to higher inflation the Reserve Bank increased interests rates in a bid to control inflation.
- All indication are that inflation is under control and it is expected that inflation will continue to decline creating some leeway for the Reserve Bank to lower interest rates.
- Farmers need to improve production efficiencies over time to counter the cost curve as input costs tend to increase faster than the value of outputs.



Sources: SA Reserve Bank, own calculations



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# Economic market principles within agriculture

## Cost curve

In the long term agriculture is experiencing a cost curve of approximately 3% per annum (The price of Farming requisites increases faster than producer prices however for 2008/09 season a cost curve of more than 30% is expected).

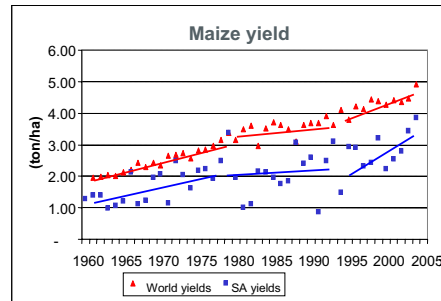
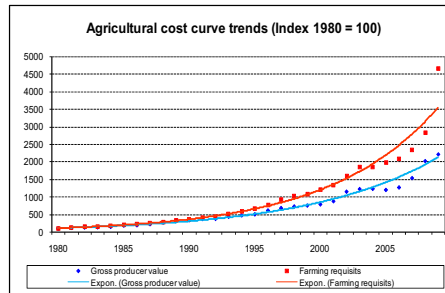
To survive this, farmers need to become more productive (increase output in relation to inputs) this is mainly done by improving production efficiencies through the use of technology, value adding and lowering fixed costs (economies of scale)

**This to a large extent implies that farming units will continue to grow in size (les clients Year on Year)**

World agriculture is poised to enter a new growth phase that will be much greater than colonization and industrialization.

- During the period of industrialization after the second world war, agricultural production expanded exponentially, compared to the growth in population (due to the development of fertilizer and production machinery).
- Production of coarse grains, beef and mutton however peaked during mid eighties due to availability of natural resources. Commodities like poultry and pork continued to grow as they were able to utilize surplus coarse grains.
- Production has once again started to increase due to advances in biotechnology (GMOS etc.)

**Production volumes will continue to increase thus improving the survival potential of agriculture in general**



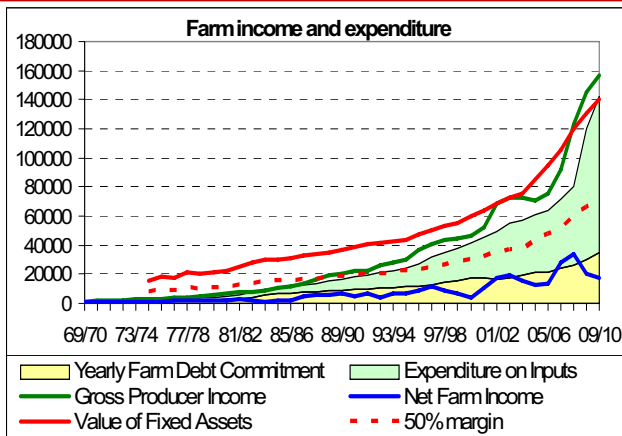
# Agricultural economic indicators

## Net Farm Income

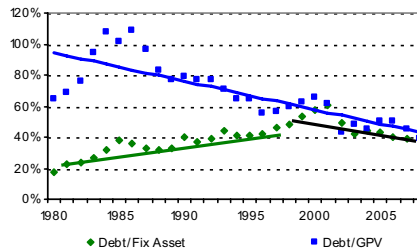
- Net Farm Income determines the rate at which capital can be repaid. As a result, **fixed investment in agriculture (property and fixed infrastructure) is to a large extent determined by Net Farm Income**. Property values are however further supported by **Lifestyle buyers as well as the Governments restitution and redistribution program of agricultural land**.
- Net Farm Income as a portion of total agricultural debt has however continued to decline over time placing pressure not only on the security value of a farm but also on the ability of farmers to repay their debt should something go wrong. This combined with the need for more production credit, has substantially increased the risk within the farming industry.

## Security

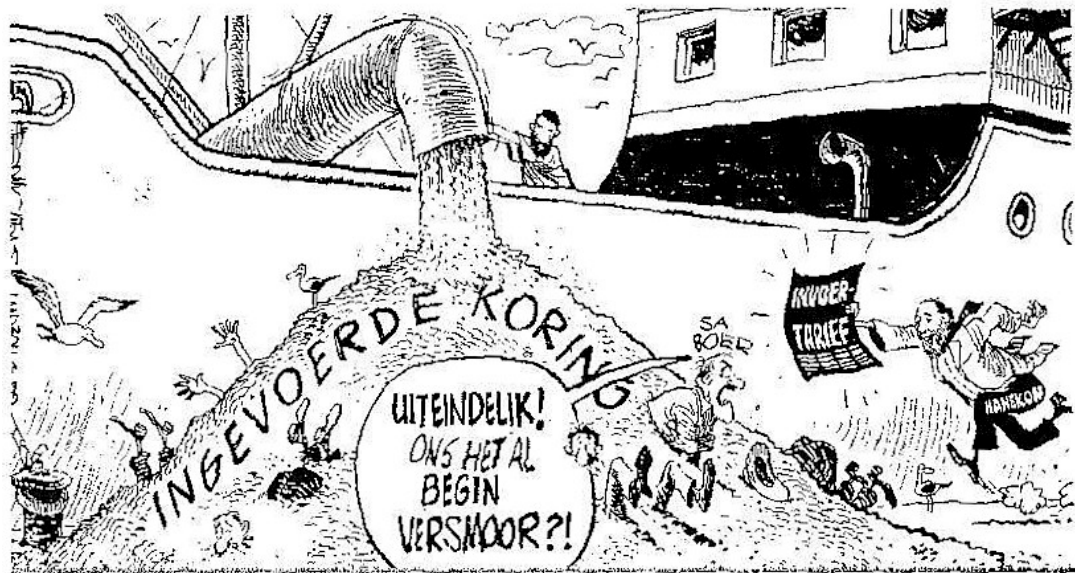
- In financing farmers there are two main criteria namely; cash flow and asset based lending. Although there has been a shift in the past few years to cash flow based financing, asset values remain important in limiting credit risk and are still being used in calculating credit exposure in terms of various ratios. The ratio of farm debt to agricultural fixed assets (farm land) has substantially improved over the past decade since the liberalisation and deregulation of the agricultural market, a clear sign that agricultural profitability has improved substantially. **The debt to turnover (Gross Production Value) ratio has also improved substantially lowering the risk of cash flow based financial lending products based on the repayable of the farming enterprise**



**Agricultural Debt to asset and turnover ratio**











# Thank you for the opportunity to share some ideas

Contact details

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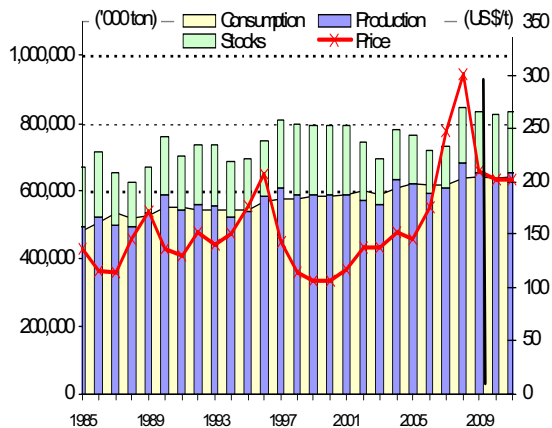
Email [ernst.janovsky@absa.co.za](mailto:ernst.janovsky@absa.co.za)

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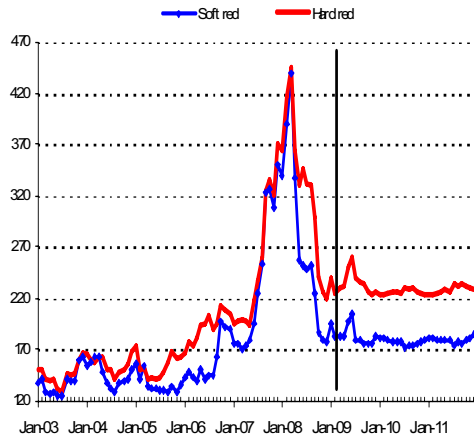
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# World Wheat price trends

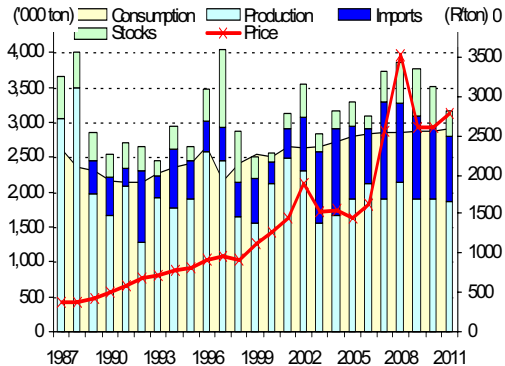
## World wheat price and stock trends



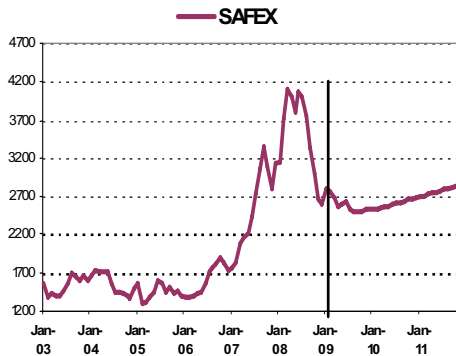
## International wheat price trends (US\$/ton)



Relationship between supply, demand and price for South Africa

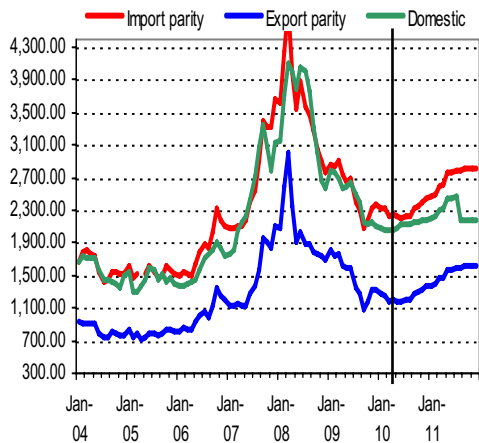


SAFEX Futures Price Trends

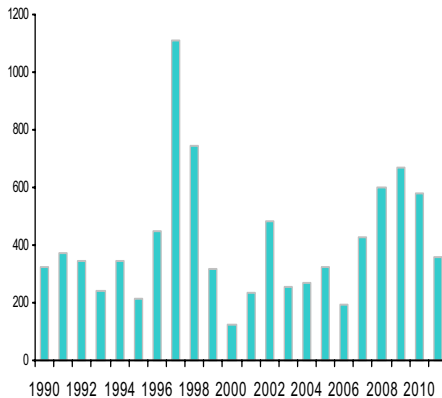


# SA wheat prices (R/ton)

## SA Wheat prices (R/ton)

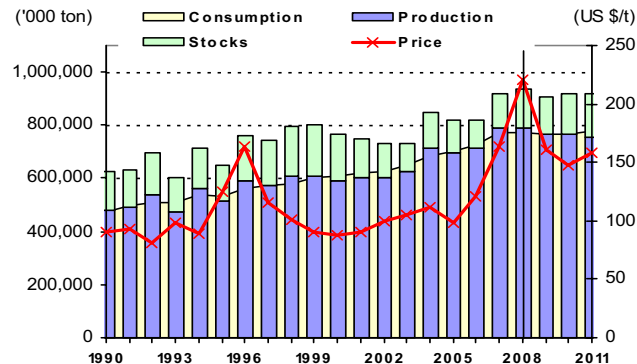


## Ending stocks for wheat ('000 ton)

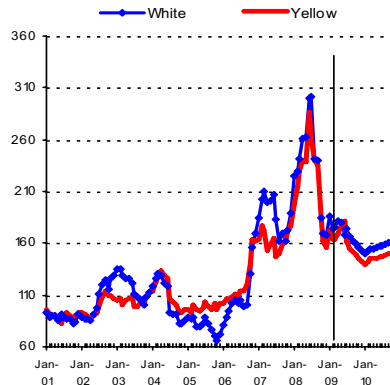


# South African maize trends

## World yellow maize price and stock trends

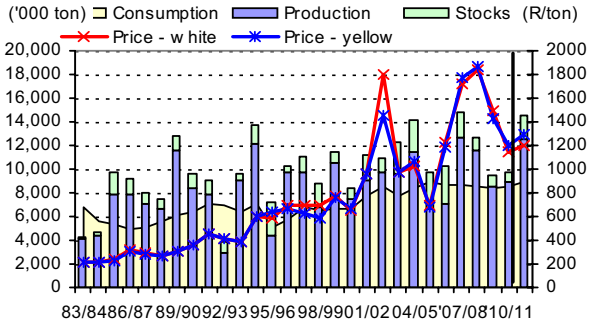


## International maize price trends (US\$/ton)

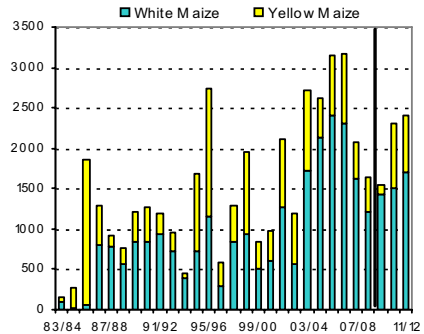


# SA Maize prices

## Relationship between supply, demand and price for South Africa

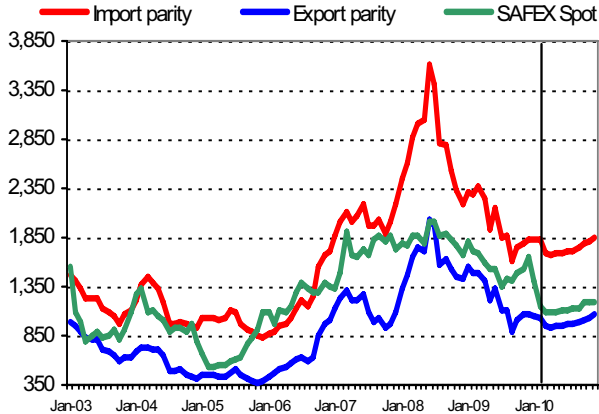


## Relationship between White & Yellow Maize Ending Stocks

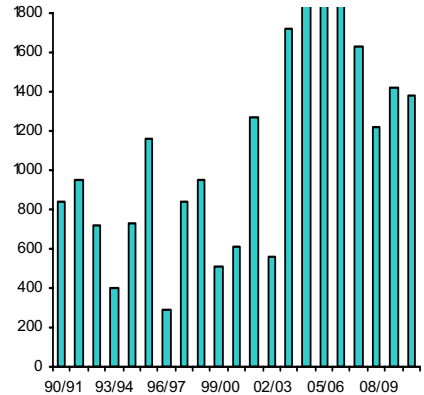


# Expected SA White maize price trends

## SA White maize prices (R/ton)

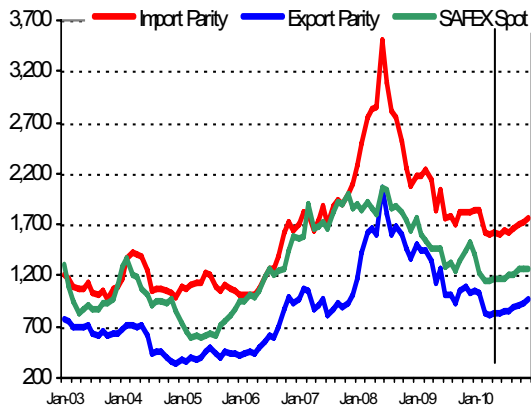


## Ending stocks for white maize ('000 ton)

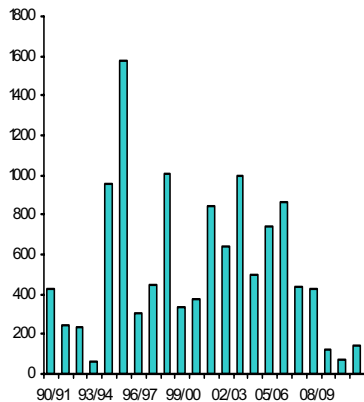


# Expected SA Yellow maize price trends

## SA yellow maize prices (R/ton)



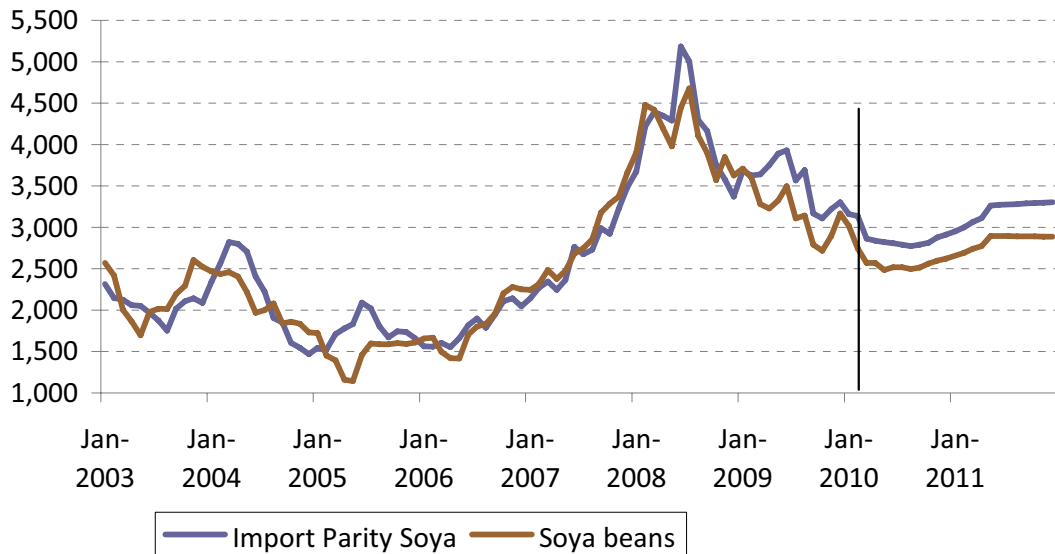
## Ending stocks for yellow maize ('000 ton)





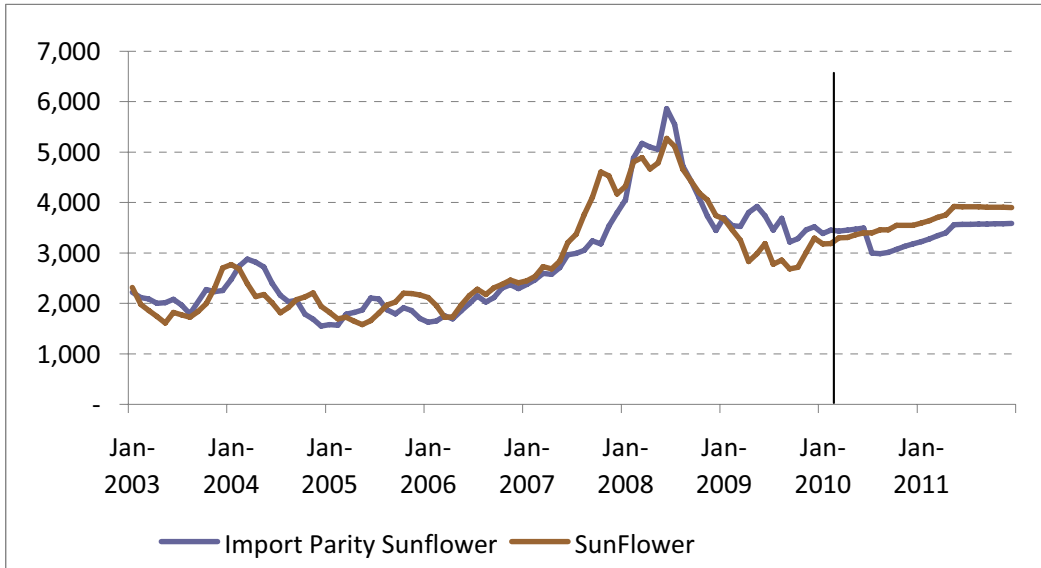
# SA Soya bean prices

Soya Beans (R/t)



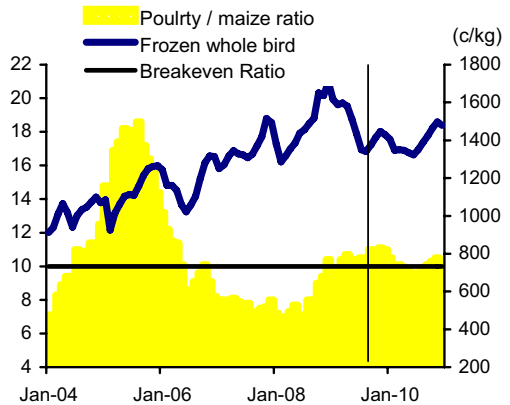
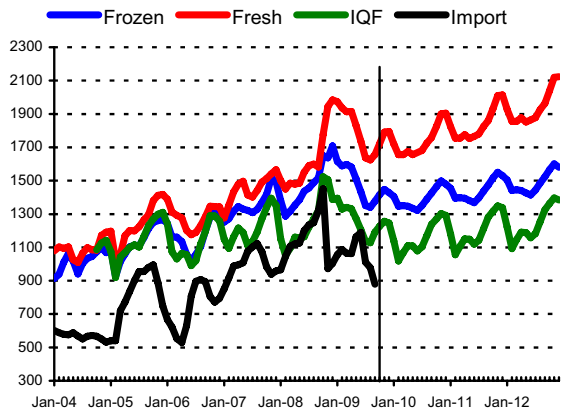
# SA Sunflower prices (R/ton)

Sunflower (R/t)



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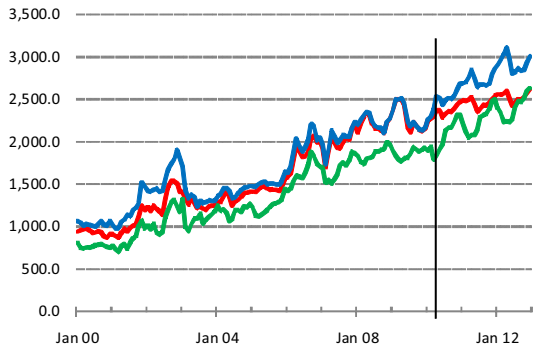
# Poultry Price trends



Source: USDA Agricultural market service (AMS), SAMIC, Abstracts of Agricultural Statistics, SAFEX, Own calculations

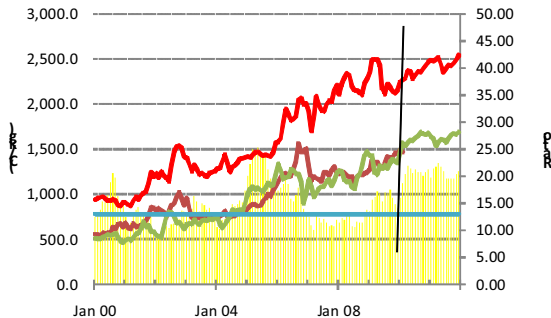
# SA Beef prices

## Beef prices (C/kg)



Class A Class C A2 Contract

## Beef prices (C/kg)

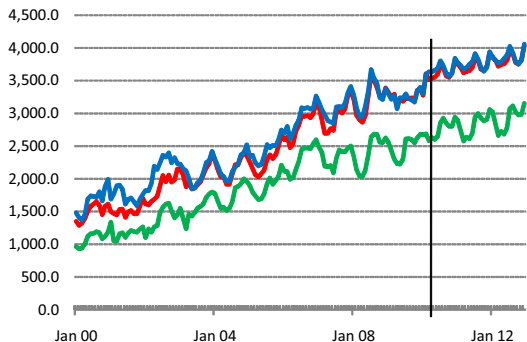


Meat / Beef ratio Class A Weaner Calf  
Bract Even Series5

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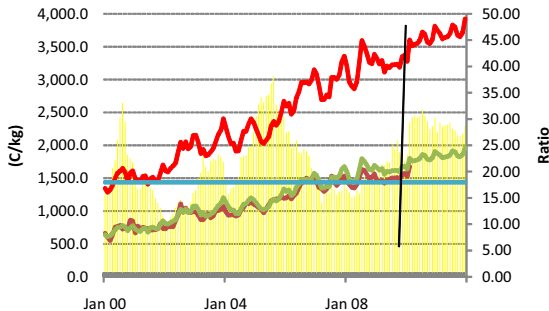
# Mutton Price trends

## Mutton prices (C/kg)



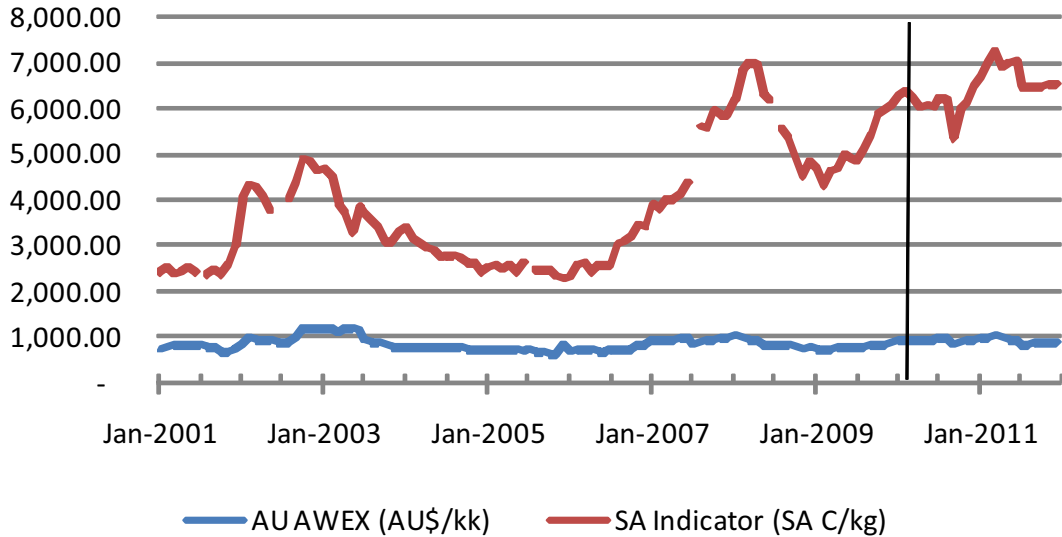
Class A    Class C    A2 Contract

## Mutton / Maize prices ratio



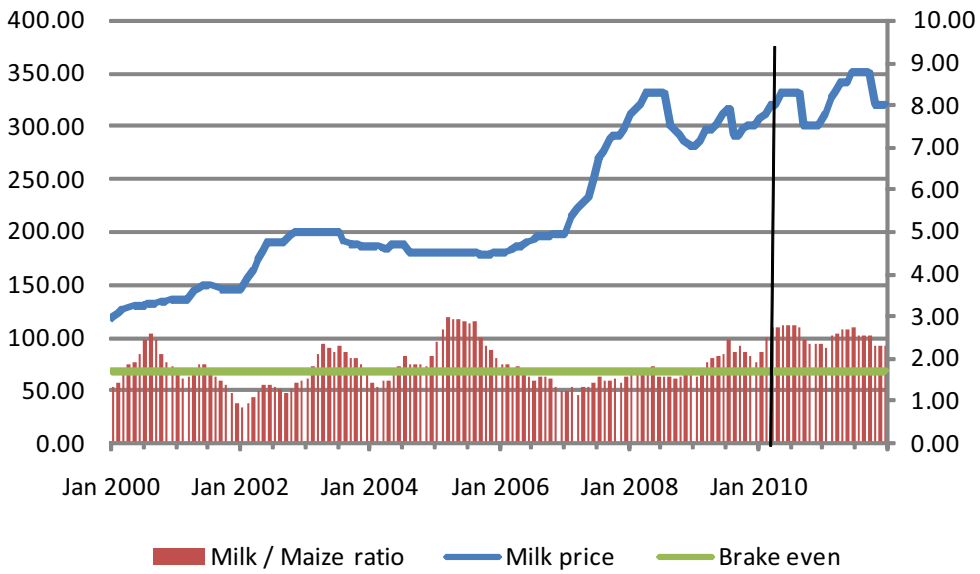
Meat / Beef ratio    Class A    Weaner Calf  
 Brake Even    Series5

## Wool price trends

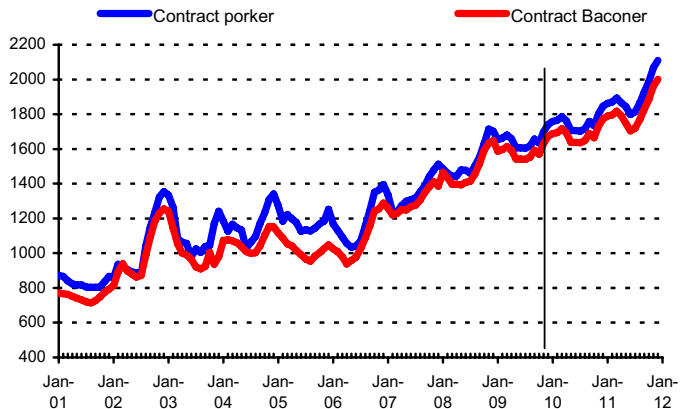


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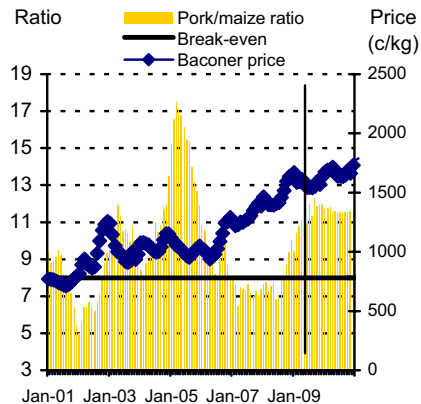
# Milk price trends



## Relationship between pork consumer prices and producer prices (c/kg)



## Pork to maize price ratios



Sources: SAGIS, SAVPO, SAMIC, Own Calculations