ABSA AgriBusiness

Agric – Economic Outlook

4 May 2010

Disclaimer: Although everything has been done to ensure the accuracy of the information, the Bank takes no responsibility for actions or losses that might occur due to the usage of this information.
SA Farmers are international players in an international market

SA Agriculture exposure to International market

- Imports
- Exports
- In & Ex as % of GPV
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

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 deferential will always be priced into the equation with defined periods under and over import parity prices dependent on surplus a shortage situations
SAL DIT GENOE?G
WEES OM VIR
'N HELE SKAAP
TE BETAAL?
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 decrees in consumer demand due to a slowdown in the economic has placed downward pressure on agricultural commodity prices in general

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)
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
ANEEA,
SÓ DRUK HULLE NIE
GOEDKOPER KOS UIT
HOM NIE!

GROENPLANNE
WATERPLANNE

SA BOER
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 extend 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 Government's restitution and redistribution program of agricultural land**.
- Net Farm Income as a portion of total agricultural debt has however continued to declined 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**.
DAGSÉ, MANNE! EK Kom Julle Help Klippe Kou...
EK SE NOG:
KRIG NET 'N PAAR MANNE MET RUMATIEK!
Thank you for the opportunity to share some ideas

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World Wheat price trends

World wheat price and stock trends

International wheat price trends (US$/ton)

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Relationship between supply, demand and price for South Africa

SAFEX Futures Price Trends
South African maize trends

World yellow maize price and stock trends

International maize price trends (US$/ton)
Expected SA White maize price trends

SA White maize prices (R/ton)

Import parity
Export parity
SAFEX Spot

Ending stocks for white maize ('000 ton)
Expected SA Yellow maize price trends

SA yellow maize prices (R/ton)

- Import Parity
- Export Parity
- SAFEX Spot

Ending stocks for yellow maize (‘000 ton)

- 90/91
- 93/94
- 95/97
- 99/00
- 02/03
- 05/06
- 08/09
SA Soya bean prices

Soya Beans (R/t)
SA Sunflower prices (R/ton)

Sunflower (R/t)


- 1,000  2,000  3,000  4,000  5,000  6,000  7,000

Import Parity Sunflower  SunFlower
Poultry Price trends

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

Mutton prices (C/kg)

Mutton / Maize prices ratio

- Class A
- Class C
- A2 Contract

- Meat / Beef ratio
- Brake Even
- Series5

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Wool price trends

AU AWEX (AU$/kk)  SA Indicator (SA C/kg)
Milk price trends

- Milk / Maize ratio
- Milk price
- Brake even

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

Pork to maize price ratios

Sources: SAGIS, SAVPO, SAMIC, Own Calculations