What is happening on the global agricultural markets?

Caitriona Murphy writes exclusively for **The Property Valuer** on the factors that have been producing a rollercoaster effect on world agricultural markets

When the price of wheat overtakes the banking crisis to become the first item on RTE's business news, you know there is something major happening in agriculture!

Last summer drought and wildfires in Russia threatened to destroy much of the country's wheat crop and with it, the largest and cheapest source of grain on the world market. When the Russian catastrophe was combined with lower projected yields in the Ukraine, Kazakhstan and Canada, speculation about the price of wheat went into overdrive and fears of a repeat of the 2007/2008 food shortages began to grow.

Speculative hedge funds piled into the commodity markets, as they had done previously during the 2007/2008 food price spike, and further fueled the fire. By the time Russian Prime Minister Vladimir Putin announced a much-anticipated ban on Russian wheat exports on August 15, the price of wheat on the world market had risen by over 56pc in less than eight weeks.

Here at home, Irish prices followed the international trend and tillage farmers saw prices on offer from the merchants jump from € 120 per tonne of dry wheat in June to € 170 per tonne by September.

The fact that this all happened even though all the experts pointed to more than adequate grain stocks and good yield prospects for the EU region and the United States, highlights just how volatile the market for agricultural commodities can be.

For 2011, European grain stocks look set to be tighter as grain exports from Britain and other European countries in 2010 increased. By December 1 last year, wheat exports out of Europe were three tonnes ahead of 2009 and barley exports stood at 2.6m tonnes, a massive 2.3 million tonnes ahead of the 2009 total of 300,000 tonnes.

Weather

As in the past few years, severe weather events will be one of the biggest factors at play in the world grain market. The weather - which could range from devastating floods to parching drought and everything in between - has the potential to make or break the annual global harvest.

Speculation has been mounting in the past month that China's annual harvest could be down by 20 million tonnes of grain in 2011 due to dry weather, while only 46pc of the US crop has been classified as being in good shape. In the meantime, Australia's east coast is suffering from flooding that could reduce its crop from milling quality to animal feed grade at best.

The effect of such extreme weather variations is exacerbated by hedge fund speculation on the commodity markets, where one bounce on the Chicago Board of Trade (CBOT) can send ripples around the world. Only two percent of the world's grain is traded by hedge funds but even the slightest movement on the market can have huge effects on the price. As the feedstock for the world's animals, the price of grain naturally feeds into the price of other agricultural commodities, including milk and beef.

South American Beef

Here in Ireland, the mere mention of Brazil and Argentina used to be enough to send shivers down the collective spine of the Irish beef industry. However, the South American giants are not perceived to be the huge threat to our beef exports that they used to be, for a number of reasons. Rising prices on their own internal markets are one of the biggest factors keeping South American beef exports out of Europe at present.

The main attraction of South American beef imports used to be their extremely low cost when compared to European beef production. However, in the past year the price of live cattle in Brazil has risen by 50pc and Brazilian beef prices are now almost on a par with Irish returns.

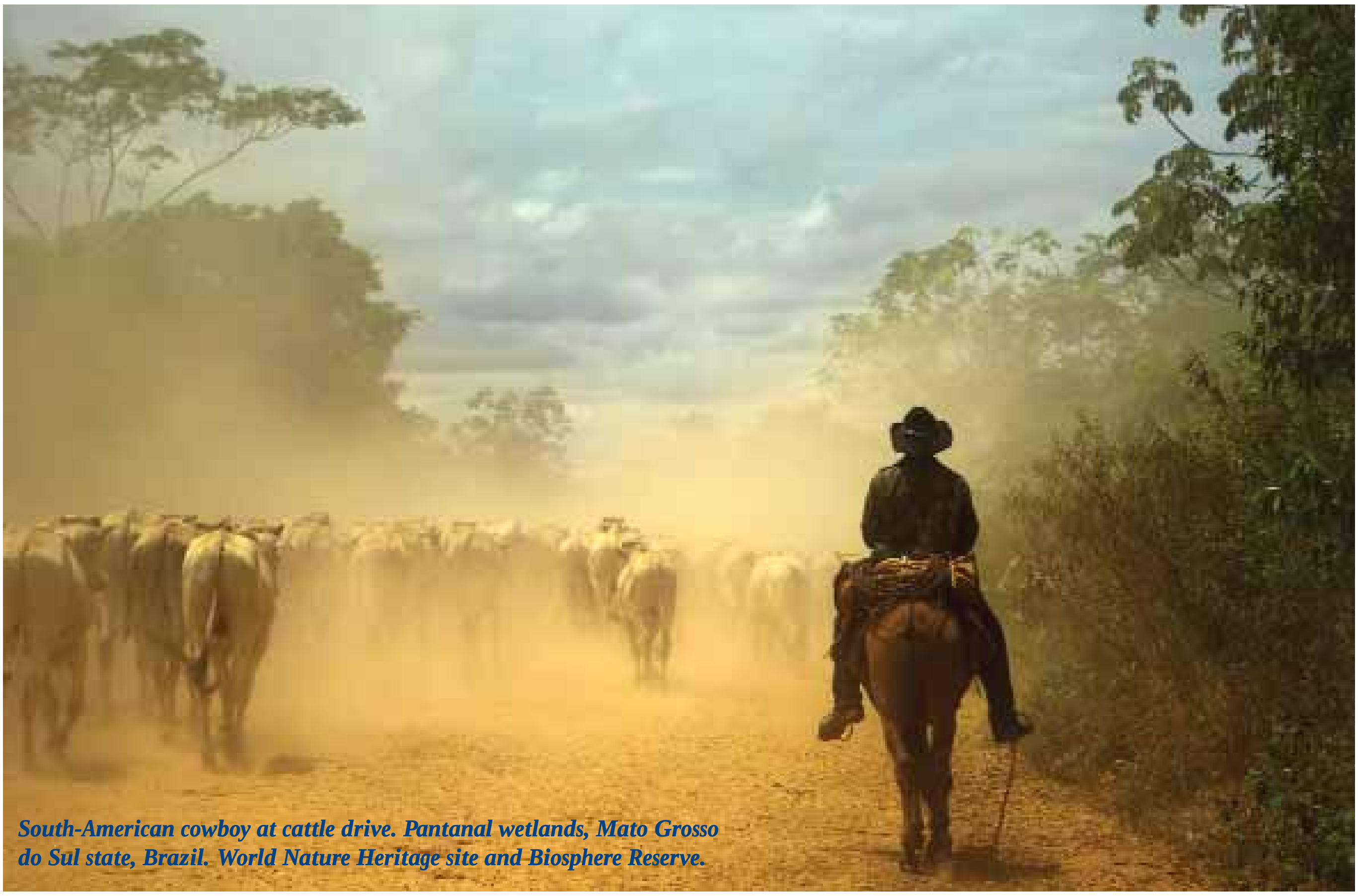
The rise in costs has been attributed in part to a switch from finishing cattle off grass to feedlots. This trend has been driven by increased sowings of soya and other cereal crops in both Brazil and Argentina but it has pushed up production costs for beef farmers.

As a consequence, production of stock for the feedlots is being pushed onto more marginal land, away from the pampas in Argentina to poorer ground in the north and northwest of the country. In Brazil beef production has moved into environmentally sensitive regions such as the Pantanal in the southwest and into the Amazon rainforest.

Cow numbers in both countries are also well back. In 2008 when Brazilian beef exports were at their peak, half of the cattle slaughtered in Brazil were female animals. This undermining of the national herd has translated into tighter cattle supplies, which, coupled with higher domestic demand for beef, resulted in higher prices.

Now that beef prices available on the domestic market and from Russian and Asian beef buyers have reached the same levels as in Europe, South American beef processors are not as dependent on European outlets.

In Argentina, the government tackled rising domestic beef prices by introducing high export tariffs to discourage beef



South-American cowboy at cattle drive. Pantanal wetlands, Mato Grosso do Sul state, Brazil. World Nature Heritage site and Biosphere Reserve.

exports to Europe and Asia. In effect, Argentina has a self-imposed ban on exports in order to maintain cheap beef for its own people.

However, just because South American beef exports are no longer the topic of conversation among Irish beef farmers, it does not mean they have gone away.

The mind-boggling productive capacity of the South American nations would be ignored at our peril and the flow of multinational companies into Brazil, Argentina, Uruguay and their neighbours is a sign of their potential. Large scale investments by global players is a sign that South America will be a huge productive force into the future, whether it be in beef, cereals, ethanol or even dairy products.

Dairy Farming and Milk Production

Here at home, Irish dairy farmers are only now beginning to recover from their plunge to the bottom of the world dairy market in 2009. Without the protection of intervention and export refunds from Brussels, farmers in Ireland and Europe have been exposed to the true force of the world market volatility.

Without milk quotas and Brussels as a bodyguard, European dairy farmers will have to face the brutal starvation/excess cycle that typifies the world market. When prices are low, milk production will fall, leading to a scarcity of product that will feed a rise in prices. Production will increase until there is a glut of milk on the market and prices will plummet again. Dealing with such extreme price volatility will be the single biggest transition that Irish and European farmers will have to make in the coming years.

Elsewhere in the world, China and India are two looming giants in terms of both dairy production and consumption.

India is the largest milk producer in the world, with an annual production of more than 100 million tonnes and a projected demand of 180 million tonnes by 2021/2022. Milk is now the single largest agricultural commodity in India in terms of output value. However, almost 46pc of milk produced in India is consumed as liquid milk and only 15pc of milk is processed and packed.

Despite various constraints and a lack of modernisation in the industry, India has become an important exporter of milk products and the Indian dairies have invested heavily in improved hygiene controls to ensure their milk products meet international standards.

At the same time, European businesses such as Danish company Danisco are opening manufacturing units in India to create functional food systems for ice cream and other products such as enzymes for the South-Asian market.

Meanwhile, the Chinese government is creating a whole new generation of dairy consumers by promoting a school milk programme, meaning Chinese companies can grow sales by just keeping up with domestic market growth. Although China consumes just 20 litres of dairy products per head per annum (compared with around 300 litres per head in the Netherlands), the Chinese market is expected to grow along the same lines as Japan and South Korea from zero levels five years ago to stabilise at around 50-60 litres per head per annum.

The 2010 Rabobank “Global Dairy Top 20” highlighted the growing influence of China and Japan in the world dairy sector. The top 10, headed by Nestle, is still dominated by companies from the mature markets of Europe but Japanese company Meiji Dairies moved up three places from eighth in 2009 to number 11, while Yili from China entered the rankings for the first time at number 17.

New Zealand dairy giant Fonterra appears to be one step ahead of the international pack in gaining access to the Chinese dairy market, having agreed a formal deal with the Chinese government to develop a second 3,000-cow dairy farm in the Heibei province in November.

The NZ$42m (€ 22.7m) investment signalled the next step in Fonterra's strategy to expand local milk production on the ground in China. The 42-hectare farm will house 3,000 cows imported from New Zealand and follows the success of Fonterra's first pilot farm in Hangu which doubled in size since 2007 to over 6,000 cows today and is currently producing around 25 million litres of milk for local consumption.

However Irish farmers are also getting in on the act, with the value of Irish food and beverage exports to China rising by 44pc to € 118 million in 2009, mainly through exports of infant formula and dairy ingredients.

Bioenergy

At the moment, the jury is still out when it comes to the bioenergy sector. Globally, energy analysts are predicting a gas glut over the next decade and this will obviously undermine demand for biofuels and impact on the viability of the bioenergy sector.

While bioenergy development is being supported in Europe through price supports such as the REFIT scheme here in Ireland, it is still not certain how many acres of agricultural land globally will be moved into biofuel production. Indeed this uncertainty has taken a lot of steam out of the food versus fuel debate that raged until recently.

The most recent trend has been to push for multi-faceted industries, such as Germany's sugar beet sector, which has been developed to produce ethanol from excess sugar. Over production of sugar has been replaced with the dual production of sugar and ethanol.

The Future in Europe

Looking to the future in Europe, no one knows what the full extent reform of the Common Agriculture Policy (CAP) will bring for farmers and consumers. Current proposals from the agriculture arm of the European Commission would place a greater emphasis on environmental protection and continued income support for farmers, albeit at a much lower level.

The fear for Irish farmers is that lobbying from the more industrialised EU member states could shift funding away from agriculture towards technology, research and development and innovation. If that were to happen, it is possible that the high value European markets for agricultural products could be offered up in a WTO deal in return for access for European manufacturing goods and services to potentially lucrative markets such as South America. The potential for this to happen was brought sharply into focus by the recent Mercosaur negotiations.

However, the fact remains that the world population is set to reach a staggering nine billion people by 2050. All of those people will need to be fed and agriculture is the only sector that can do that. ◆

International Land Sales

By Daithi O'hAnluain

Fears about food security went into overdrive in the wake of the food price rises of 2008, with millions of hectares of agricultural land being locked up in long-term leases in a worldwide rush to secure fertile ground.

Both global conglomerates and governments are behind the move to secure vast tracts of fertile soil across the globe. According to some reports, there could be as much as 50 million hectares bought and leased through completed and ongoing international deals for arable land.

South African investors leased 2,000 square kilometres in the Democratic Republic of Congo for 30 years, with an option to extend.

Cash rich countries, like Gulf States and powerful Eastern economies like China, India and Korea, are securing land anywhere they can.

China has signed a contract with the Democratic Republic of Congo for 2.8m hectares, while United Arab Emirates has about 1.3 million hectares of land leased internationally of which about 300,000 hectares is in Pakistan.

Dubai sought a 99-year lease on 28 farms on New Zealand's South Island, while China is involved in the potential purchase of 22 farms owned by one family in the Northern Island. Australia, too, is another popular target.

In Ethiopia, Saudi investors are building vast greenhouses, reaching 20 hectares in size, to grow tomatoes, peppers and other hothouse crops. Indian investors are leasing vast tracts of land to supply the cut flower market.

And last year a deal by Korean conglomerate Daewoo to secure 1.3 million hectares in Madagascar- 40pc of the island's arable land – fell through after protests led to a coup. Daewoo had intended to use the land for palm oil and food production, hoping to replace more than half of the corn that South Korea, the world's third largest buyer, imports from the US and South America.