

Are retailers and food producers exploiting South Africans through higher-than-warranted food prices?

The Competition Commission's recent report on agriculture and food markets dominated the conversations in the industry groupings last week. Therefore, we thought it was necessary to outline some shortcomings of the report in an essay published in the Sunday Times this past weekend. This morning, we jointly present our arguments in the Sunday Times essay with Professor Johann Kirsten of Stellenbosch University's Department of Agricultural Economics.

We live in a time of higher food prices, part of the global polycrisis triggered by the pandemic and Russia's war on Ukraine, which caused seizures in supply chains and pushed up energy and food prices. In short, this is not unique to South Africa.

This is also the wrong time to cry wolf, as the Competition Commission recently did in its Essential Food Price Monitoring Report. If you raise a false alarm when none is warranted, it undercuts your credibility when danger is afoot. Let us consider the real factors that have influenced recent food prices.

The drought in South America in the 2019/20 season and the growing demand for grains and oilseeds in China were the primary drivers of global prices. China was on a path to rebuild its pork industry, which African swine fever devastated, requiring increased volumes of grains and oilseeds. China's growing demand had a consequential impact on global grain prices because of its share size of imports. For example, the country imports about 60% of globally traded soybeans.

As Covid-19 spread in early 2020, several major grain producers, such as India, Kazakhstan and Vietnam, worsened the increase in global prices by temporarily banning exports. As this unfolded, shipping costs soared, contributing to already elevated global grain prices. Throughout this period, drought in South America didn't stop, weighing on global supplies. This matters because Brazil and Argentina account for half of global soybean production and about 15% of global maize production. Thus, when these countries face drought, the impact is visible in global grain supplies and prices. In sum, a combination of trade policy actions by other countries, logistics and weather conditions placed an upward pressure on food prices.

These are all-important fundamentals that challenge food supplies, further worsened by the Russia-Ukraine war. Russia and Ukraine are substantial players in the grains and oilseeds market. The former produces about 10% of global wheat, while Ukraine accounts for 4%. This is nearly the size of the EU's total wheat production. Wheat is for domestic consumption as well as export markets. Together the two countries account for a quarter of global wheat exports. Moreover, Russia and Ukraine are notable players in maize, responsible for 4% of production combined. However, their contribution is even more significant in exports, accounting for an average of 14%. Both countries are also among the leading producers and exporters of sunflower oil. Pre-war, Ukraine's global exports of the product accounted for 40%, with Russia accounting for 18%. Thus, the start of the war led to a surge in grains and oilseeds prices for much of 2022. As the war intensified, the drought in South America continued.

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During this period, there were also sharp increases in energy prices because of Russia's major contribution to global energy supplies, which was suddenly disrupted. These events affected all countries, and food price inflation suddenly became a worldwide topic.

Linkages to South Africa

South Africa, while a net exporter of agricultural products, was not insulated from the price shock, even with its large domestic harvests. This underlines the interconnectedness of global food supplies.

Some may argue that governments should have placed export bans to limit the surge in domestic grains prices. But such policy prescriptions never work. Notably, in the South African case, one must remember that agriculture is highly exposed to global markets given that about half of output by value is exports and that many inputs into the farming need to be imported.

As a country, we import more than 80% of our annual fertiliser usage and 98% of agrochemicals, fuel and equipment. We had limited control over these prices, which increased pre-war and accelerated further when it started. Before the war, China, which accounts for about 12% of global fertiliser exports, limited these to focus on its domestic market. When the war started, Russia, which accounts for 14% of global fertiliser exports, was suddenly in chaos.

As such, if policymakers considered limiting South Africa's grain exports to protect the country from global challenges, the results could be a reduction in competitiveness in maize production and, ultimately, lower plantings and output as farmers would opt for other profitable crops. The long-term effects of such an approach would be higher prices, exactly the opposite of what those policymakers would have aimed to control.

In the past year or so, food producers and processors had to deal with higher agricultural commodity prices and process such commodities further to produce the food products we see on shelves. The activities between producer (or importing country) and retailer do not happen without costs. The food value chain first depends on expansive logistical systems and networks, while processing involves labour, energy, packaging and finance costs, among others. Once the food is processed it must be distributed to thousands of retail outlets, which also bear these costs. We all know what happened to fuel prices and the interest rate in South Africa. On top of that, we can add inflation-related wage increases and the dramatic costs of load-shedding and crime.

It is, therefore, no wonder that food value chain costs soared, amplifying the initial increase in commodity prices. A lot of these cost increases are self-inflicted through state failure regarding energy, crime and local government collapse. We should think about the terrible conditions in which role players in the food value chain have to do business in South Africa today.

If food processors and retailers accounted for all these cost increases across the value chain, consumers would face a much sharper increase in prices. But this was not the case in South Africa. Food prices increased at a moderate pace, having averaged 9,5% in 2022, compared with 6,5% year on year in 2021 and 4,8% in 2020. Countries such as the US, Kenya and Brazil, as well as those in the EU, saw much higher consumer food price inflation rates than South Africa, though some had decent agricultural production conditions.

This meant food processors and retailers, if anything, absorbed the costs and didn't pass them fully on to the consumer. Their strategy is understandable, considering this country's economic environment and unemployment. With this in mind, we find the Competition Commission's comments puzzling and irresponsible. It suggested various food price

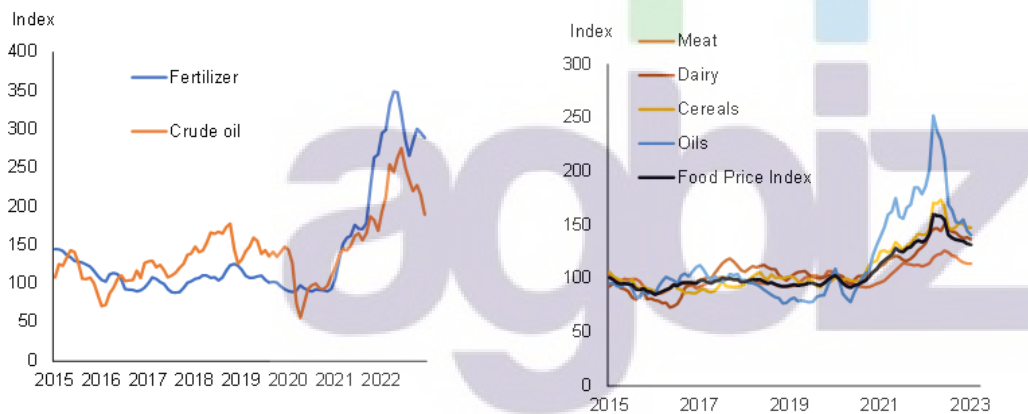
increases in the past few months were "unjustified", insinuating someone in the value chain is taking advantage of South African consumers. This is an unfortunate mischaracterisation of reality. If anything, one could argue that food processors and retailers had to apply smart pricing strategies to benefit the consumer while sustaining their businesses.

A regulating body such as the Competition Commission should be mindful of the critical role it plays in society and be more thoughtful in its research and statements, especially on politically and socially charged food security issues.

The drivers of food prices are evident and a global challenge. In the coming months, as the country faces rolling blackouts, which add to the dynamics, food prices are likely to remain elevated, softening in the second half of the year. There is also a lag (of anything between three and nine months) between farm and retail prices, which some researchers tend to ignore.

Public anxiety about high food prices does not need to be further aggravated. Reporting on such must be done responsibly and with great care.

Exhibit 1: Global agriculture input prices are starting to soften, but there is a lag before all this appears through some food products at the retail level



Source: FAO, IMF and Agbiz Research

Weekly highlights

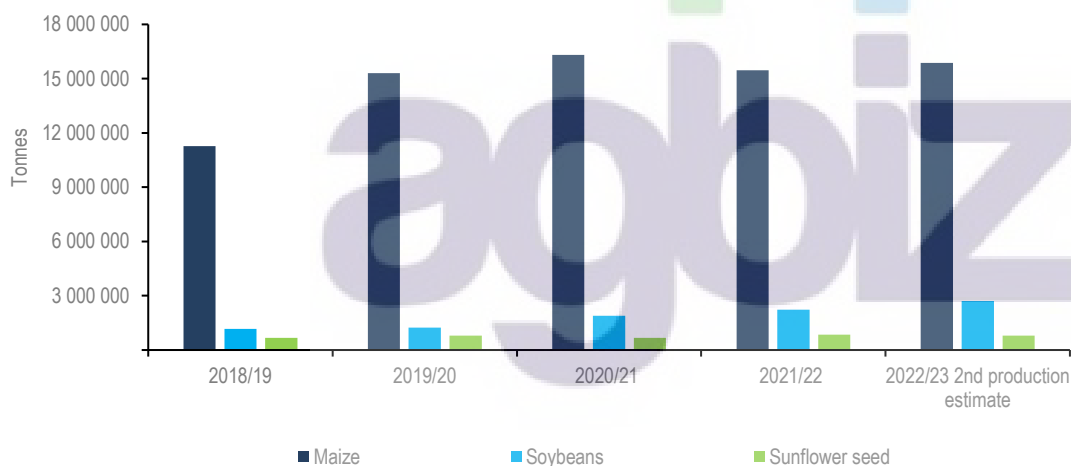
SA is in for another ample grains and oilseeds harvest

At the end of March, we received additional comforting information that the erratic weather conditions at the start of the 2022/23 summer production season had minimal impact on South Africa's summer grains and oilseeds. The data released by the Crop Estimates Committee placed South Africa's 2022/23 summer grains and oilseeds production at 19,6 million tonnes, up 2% from last month's figure and 5% higher than the previous season. This is primarily on the back of expected higher yields as the overall planted area for summer grains and oilseeds are 4,4 million hectares, roughly unchanged from the previous season. The persistent load-shedding raised concerns that areas under irrigation could receive poor yields. Thankfully, the favourable rainfall, at a moderate pace, from mid-February provided a much-needed breather and improved crop conditions. Within summer grains and oilseeds, roughly 20% of maize and 15% of soybeans are produced under irrigation. The various energy interventions, such as possible load curtailment and expansion of renewables, are some options that could assist the irrigation regions in the medium term.

The Crop Estimates Committee's data provides sufficient comfort that South Africa will have adequate staple food supplies in the 2023/24 marketing year (which corresponds with the 2022/23 production season). For example, if we consider the large crops like maize, soybeans and sunflower seed, production is forecast at 15,9 million tonnes (up 3% y/y), 2,7 million tonnes (up 22% y/y), and 797 610 tonnes (down 6% y/y), respectively. To underscore our point, the expected improvement in the maize harvest is on the back of better yields, as the area plantings are down marginally from the 2021/22 season. Meanwhile, the robust forecast increase in soybeans results from both expected large yields and an expansion in planted areas. The fall in the sunflower seed production forecast mirrors the reduced planted area and yields in some areas. Other small crops, such as sorghum and groundnuts, have a reasonably large expected harvest of 109 400 tonnes and 47 930 tonnes, respectively.

South Africa's 2022/23 summer grains and oilseeds are now at pollination stages in some regions, and others are maturing. This could be another excellent harvest season if the weather conditions remain favourable. Notably, these data bode well with the already softening maize, which is now hovering around R4 000 per tonne, roughly at the same levels as a year ago and well below the higher levels we saw a few months ago. Sunflower seed and soybeans prices have also moderated notably, and spot prices currently trade around R8 192 per tonne and R8 660 per tonne, respectively.

Exhibit 2: South Africa's major summer grain and oilseeds production



Source: CEC and Agbiz Research

Data releases this week

We start the week with a global focus. There are two major data releases this week. First, the United States Department of Agriculture will release the **U.S. Weekly Grains and Oilseeds Exports** on Thursday. Secondly, the Food and Agricultural Organisation of the United Nations (FAO) will release the update of the **Global Food Price Index** for March 2023 on Friday. The FAO's Global Food Price Index averaged 129.8 points in February 2023, marginally down (0.6%) from January, continuing the downward trend for the eleventh consecutive month.

On the domestic front, on Wednesday, SAGIS will release the **Weekly Producer Deliveries** data for 31 March. In the previous release of 24 March, the 2022/23 wheat producer deliveries amounted to 1,9 million tonnes, out of the expected harvest of 2,1 million tonnes. We will report on the 2022/23 summer grains and oilseeds when the harvest gains momentum in the coming months.

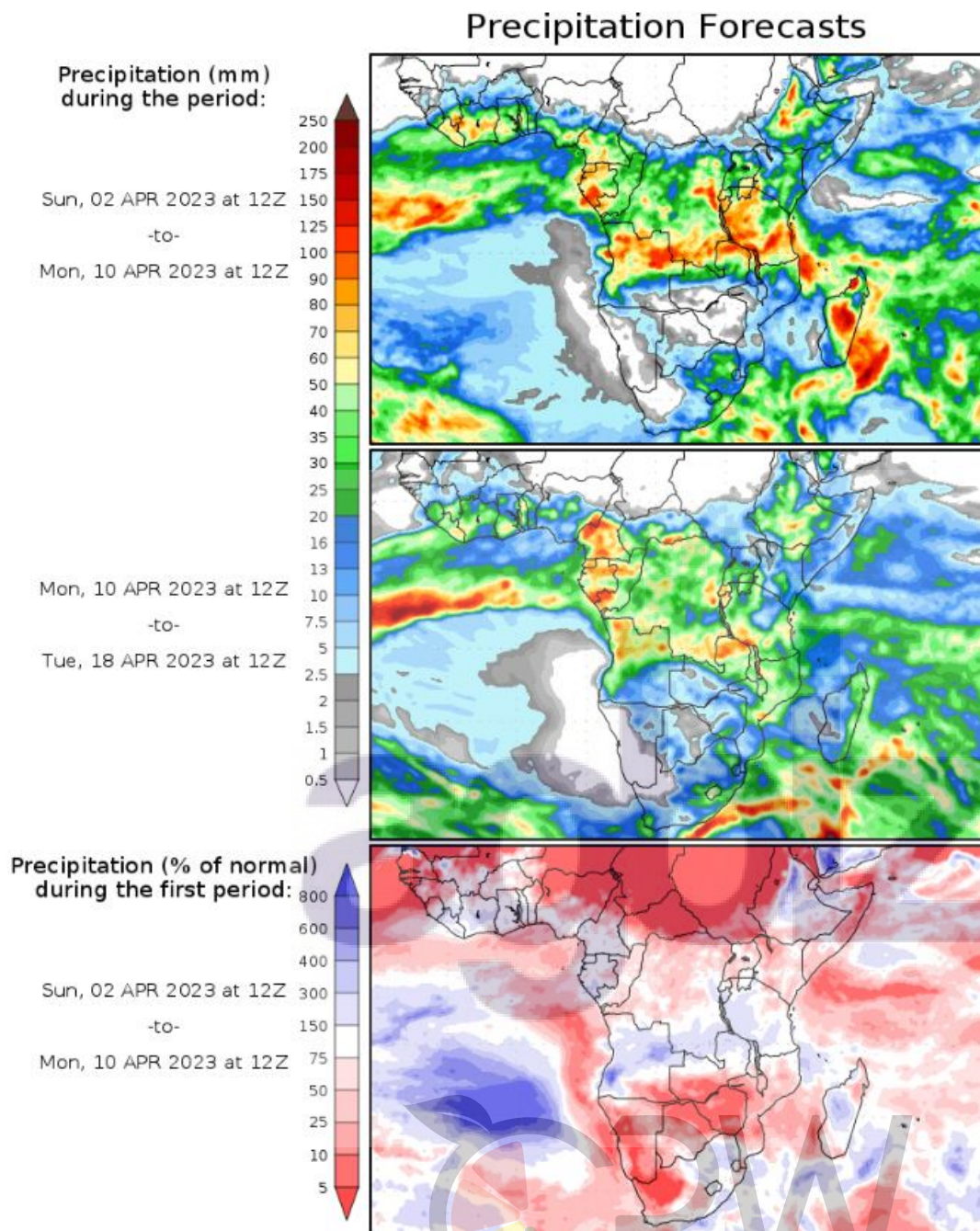
On Thursday, SAGIS will publish the **Weekly Grain Trade** data for 31 March. In the previous release on 24 March, the 47th week of South Africa's 2022/23 maize marketing year, the weekly exports amounted to 40 284 tonnes. About 52% went to Kenya, and the remainder to the neighbouring countries. This brought the total 2022/23 exports to 3,2 million tonnes out of the seasonal export forecast of 3,3 million (slightly down from 3,7 million tonnes in the past season due to an expected reduction in the harvest).

South Africa is a net wheat importer, and 24 March was the 25th week of the 2022/23 marketing year, with 35 794 tonnes, all from Lithuania and Australia. South Africa's 2022/23 wheat imports currently stand at 699 216 tonnes. The seasonal import forecast is 1,6 million tonnes, roughly unchanged from the previous season.

As we stated in our earlier notes, the major wheat suppliers in the 2021/22 season were Argentina, Lithuania, Brazil, Australia, Poland, Latvia and the U.S. If one looks into South Africa's wheat import data for the past five years, Russia was one of the significant wheat suppliers, accounting for an average share of 26% yearly. Argentina and Brazil replaced this in the 2021/22 season. However, Russia is back on the suppliers' list in the 2022/23 season and is again one of the significant wheat suppliers to South Africa thus far.

On Thursday, Statistics South Africa will release data for the **electricity generated and available for distribution** in February 2023.





Source: George Mason University (wxmaps)

The weather forecast for the next two weeks shows prospects of light showers over most regions of South Africa.

While the summer grains and oilseeds regions need warmer conditions at this time of the year -- nearing harvest period -- the forecast light showers will likely have minimal impact on the crop.

However, the expected showers over the Western Cape regions are a welcome development, and could help improve soil moisture ahead of the start of the winter grains planting season.