Short Insight – Grains

Group Economics
Emerging Markets & Commodity Research

27 January 2020

Casper Burgering
Senior economist Agricultural Commodities

Phone: +31 6 109 760 34
casper.burgering@nl.abnamro.com

Soybean and wheat market relationships changed

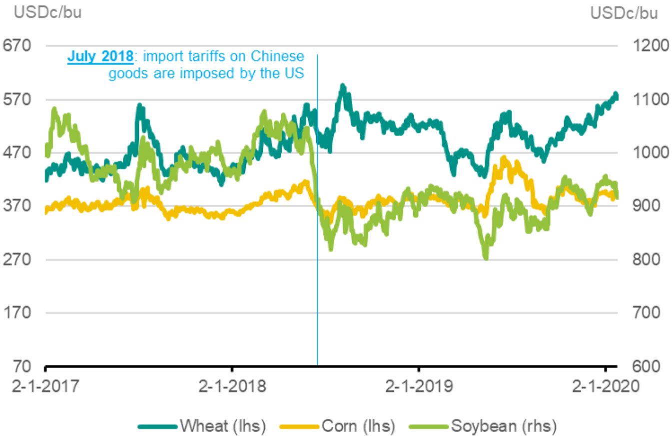
The US and China have signed the phase one trade agreement, under which China promises to buy more US agricultural products over the next two years, provided market conditions are favourable. However, the question remains whether grain markets will benefit from the truce. In the meantime, the relationships in the soybean and wheat markets have also changed considerably.

- **Wheat: Russia's output and export share have falling**
- **Corn: low price volatility and limited fundamental changes**
- **Soybean: soybean trade has changed dramatically in only 18 months**

Phase one trade deal is only a truce, but good for sentiment

Trump has promised that American farmers will benefit from the trade agreement between the US and China. Under the agreement, China will buy an additional USD 12.5 billion in agricultural products from the US this year compared to 2017. In 2021 that amount will increase to USD 19.5 billion over. The question remains whether these amounts will be achieved, given that the Chinese have stipulated in the agreement that the market conditions for these purchases must be favourable. In other words, the price of the products must be competitive. Moreover, China's additional purchases must be covered by sufficient domestic demand for the products. In any case, the current truce is a step in the right direction, which has resulted in a slight improvement in market sentiment. A really good deal for US farmers would entail the elimination of trade rates. Only then will products from the US become more competitive internationally.

Price trends in grain markets

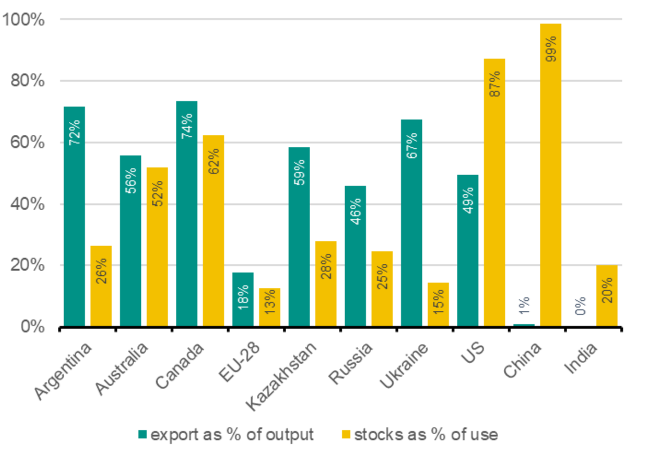


Source: IGC, Refinitiv

Wheat: Russia's output and export share have fallen

Export demand for wheat has been strong in early 2020. This, together with some tightness in supply, has boosted prices. Total demand is expected to grow this year by 2.4% yoy. Growth in demand from the animal feed industry is mainly responsible for this trend. The growth in total demand this season has improved significantly compared to the previous two seasons, during which it remained virtually unchanged. Meanwhile, however, wheat production will increase this season by around 4% yoy, which will ultimately result in oversupply and higher stocks. Next season, the global agricultural area will only increase marginally. This is mainly due to the shrinking harvest area in the EU and Latin America. China and India jointly produce 30% of the global wheat output, little of which is destined for the export market. The largest producer is Europe, but this continent's export market activity is also has relatively limited. Russia remains the largest exporter in volume terms. Still, Russia's exports have declined over the past two seasons due to lower harvests. This means that Europe, the US and Canada will play a greater role in the export market in terms of export volume. Together, the four control two-thirds of the export market.

Export and inventories wheat (2019/2020)

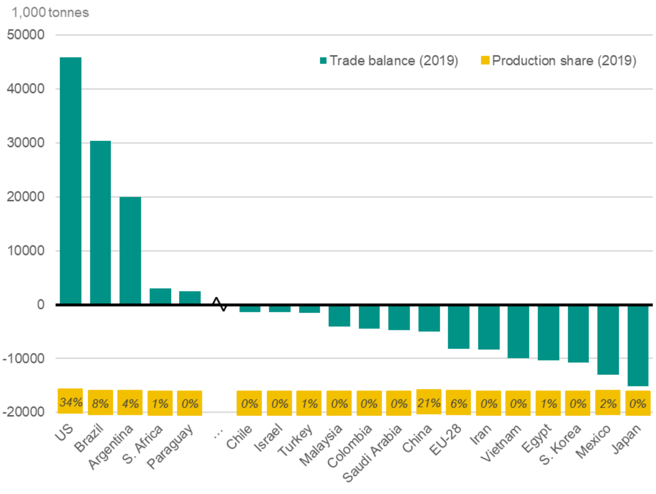


Source: IGC

Corn: low price volatility and few fundamental changes

Since 2014, the corn price has fluctuated between USDc 460 and USDc 315 per bushel. This is a relatively narrow bandwidth compared to other grain markets. It indicates that price volatility is low and that few fundamental changes have taken place. The US is currently the largest producer of corn in the world. With a 34% share of global output, the US has a substantial lead over China - with a 21% share. China's domestic corn needs are high, and the country will remain a net importer in the coming years. Latin America accounts for approximately 15% of global corn production. The US and most Latin American countries are the major net exporters. This season, the International Grains Council (IGC) expects both output and demand to shrink slightly. On balance, however, the corn market will be left with a deficit of 39 million tonnes or approximately two weeks of consumption. Industrial demand for corn remains an important growth segment for the coming year, partly due to the recent recovery of ethanol production in both the US and China.

Trade balance corn 2019 and share in production

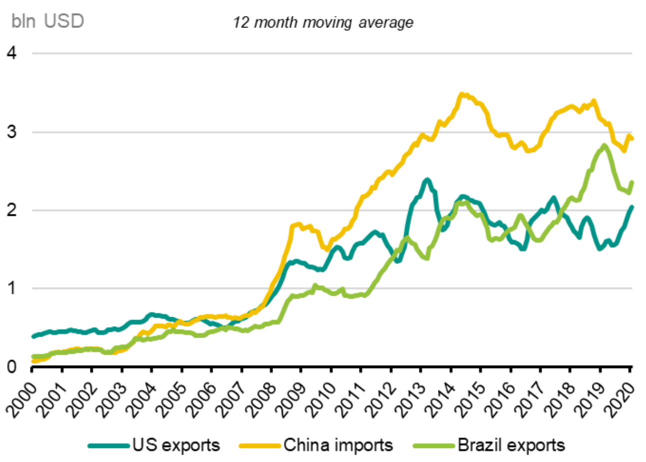


Source: IGC, OECD

Soybeans: soybean trade has changed dramatically in 18 months

The soybean trade between the US and China has virtually dried up over the last 18 months. According to the IGC, output in the US will fall this year by 20% on an annual basis. To meet the domestic demand for soybeans, China has been looking for sources from Latin America. Brazil has become an important trading partner. Brazilian output and export levels increased and made Brazil a formidable player in the soybean market. This comes at the expense of US competitiveness. Indeed, the harvest in Brazil was good at the start of 2020 thanks to favourable weather, and global availability is increasing. Now that China has reopened its doors to US soybean imports under the trade agreement, price competition will once again increase. Moreover, China has not stood still and has expanded its harvest area in an effort to become less dependent on foreign soybean deliveries. China's output has increased by 26% since the 2016/17 season. Despite this increase in output, a shortage in the market is still expected this season, mainly due to falling production in the US.

Trade in soybeans



Source: Refinitiv