AGBIZ RESEARCH

Commentary – PPI Food Manufacturing

Food producer inflation remains unchanged – 30 June 2016

- The latest producer price index (PPI) data released by Statistics South Africa indicates that in May 2016, producer inflation for final manufactured goods slowed to 6.5% from 7% year-on-year (y/y), in April 2016. However, **producer inflation for food products remained flat at 10.9%.**
- The food products basket consists of four broad categories, which include "**meat, fish, fruit, vegetables, oils and fats**", "**dairy products**", "**grain mill products, starches and starch products, and animal feeds**" and "**other food products**". Each of the above-mentioned categories within the food products basket is allocated a weight, with the largest being "**meat, fish, fruit, vegetables, oils and fats**" and "**other food products**", which make up 37% and 41%, respectively (**figure 1**).
- Even though the PPI for food products remained flat from the previous month, there were some movements in various food sub-sector categories indices. The "**meat, fish, fruit, vegetables, oils and fats**" decreased by 1.3% from the previous month, largely underpinned by a fall in meat and oils product prices.
- However, this decrease was offset by a 4.3% increase in "**dairy products**", which is in line with seasonal increase in dairy products prices. **We foresee dairy price increases to pick up pace in Q3, 2016, and possibly easing in Q4, 2016 as grazing fields improve during summer season, thus leading to an increase in milk production**.
- The "**grain mill products, starches and starch products, and animal feeds**" increased by 1.2% from the previous month, a trend that is reflective of the increases in raw commodities prices (**figure 2**).
- The "**other food products**" category also increased by 0.5% from the previous month, with sugar being the key driver of the increase. This again is reflective of the raw sugar prices, which have been mainly been underpinned by lower supplies on the back of the current drought.

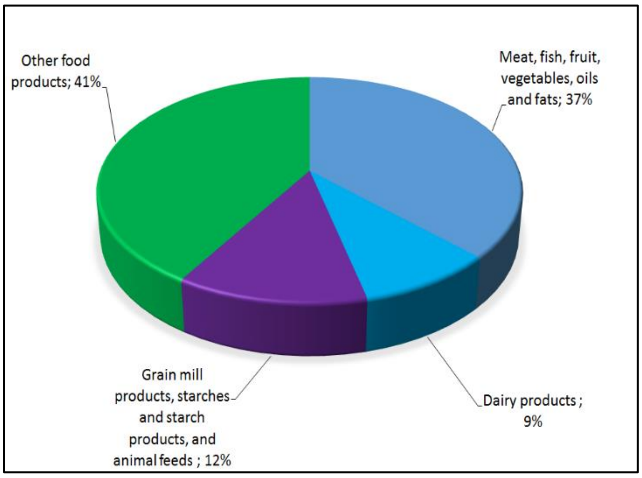

Figure 1: Weights of products in the food basket

Source: Statistics South Africa, Agbiz Research

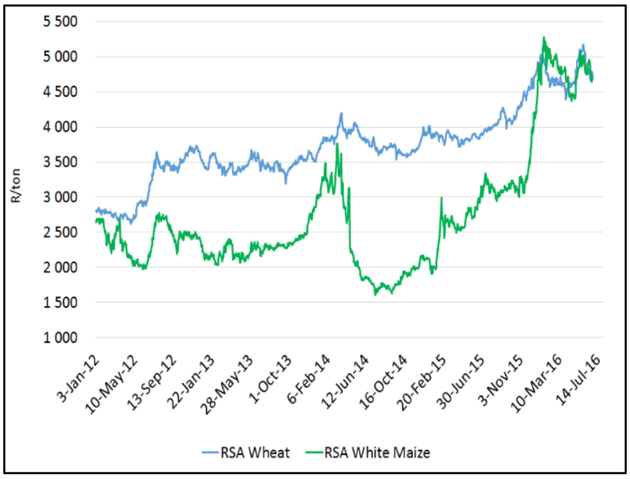

Figure 2: Maize and wheat

Source: JSE, Agbiz Research

Looking ahead:

- In the short to medium term, **we expect grain and oilseeds commodities** (critical inputs in food manufacturing) **to remain at higher levels, at least until mid-2017**, assuming that there will be favourable weather conditions in the 2016/17 production year to replenish market supplies.

- **A number of weather forecasters already suggest that the El Nino event is at its final stages, with possibilities of La Nina event by end of the year already increased to 75%,** according to the US Climate Prediction Centre. A La Nina weather event could lead to above normal rainfall in South Africa, which is essential to replenish soil moisture, and beneficial for crops and livestock.

- Moreover, **the wheat tariff is expected to increase by at least 30% from the current level of R1 224.30 per ton to R1 591.40 per ton**. All of this is expected put input costs of food manufactures in the grain milling and bakery products sub-sectors under pressure. Worth noting is a proposed review of the existing variable formulae for wheat, sugar and maize import tariff from the Ministry of Finance, whose findings will have implications on food manufacture's input costs in the medium term.

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