South Africa's wool industry strained by limited access to China

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South Africa's agricultural industries are increasingly pressured by stringent trade practices in their major export markets. The wool industry, which has been closed off the Chinese market for nearly four months now, is one example. China restricted imports from the local wool industry following the outbreak of foot-and-mouth disease, which remains a significant challenge for the sector. This is a major worry because China is South Africa's primary wool export market, accounting for roughly 70% of exports, in value terms. Other South African wool industry markets are the Czech Republic, Italy, India, Bulgaria, Germany, the US, Malaysia, Japan, and Mexico. But all of these are relatively small and thus cannot offset the losses resulting from China's restrictions.

South Africa needs to forge unique relations with China on the wool trade, which can have mechanisms to insulate the industry at such critical times. Such strategic interventions should be at the political level. This is not the first time South Africa has experienced such a challenge in China. During the 2019 foot-and-mouth disease outbreak, China followed similar harsh practices and temporarily suspended South Africa's wool imports. This measure saw South Africa's wool exports fall 24% year-on-year in 2019 to US$302 million. The decline was in exports to China, which fell by almost a third from 2018 in both volume and value terms.

What's more, the Chinese share in South Africa's wool exports fell to the lowest level in nine years – at 55%. The wool industry was under financial pressure, and arguably, the new entrant black farmers, who have less of a financial cushion, felt the impact severely. Black farmers have a strong presence in this industry. For example, the National Agricultural Marketing Council estimates suggest that black farmers account for 18%, 13% and 34% of wool, mohair, and cattle production, respectively.

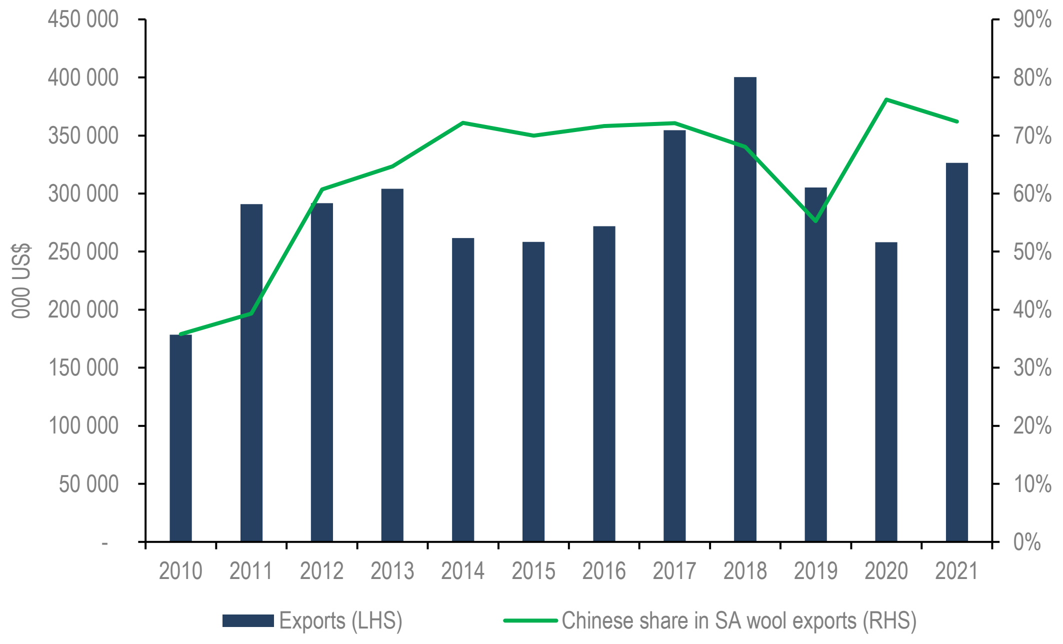
The present-day ban arrives at an even economic challenging time. Farming input prices for all agricultural industries are rising. For the livestock subsector or wool industry, the animal feed prices and all logistics costs are adding cost pressures on farmers. There are also household financial pressures for small and medium-scale farmers that rely on the proceeds of this industry to sustain families. Without access to the Chinese market, the wool industry will likely be under strain for some time. At a national level, this will also show in the export earnings. Wool was the eighth most significant agricultural exportable product in 2021, accounting for 3% or US$326 million in South Africa's exports of US$12,4 billion. Importantly, in the first quarter of this year, the export activities were still smooth. Thus, wool maintained a similar ranking in the country's agricultural exports. The glitches started at the beginning of the year's second quarter, with the foot-and-mouth disease outbreak on a few cattle farms. The episode overlapped with China's closing of some of its trading hubs with tough lockdowns to curb the spread of covid-19. This might have added to the constraints South Africa faces. Still, China has reopened its economy, and South Africa's wool industry is still strained.

The China case is not unique. There are various trade hindrances that South Africa faces on major export fronts, which present threats to this promising sector. Citrus, which in 2021, was the top exportable agricultural product in South Africa, valued at US$1,8 billion or 15% of the overall exports of US$12,4 billion, is facing constraints in the EU. The EU was one of the leading markets, alongside the UK. Hence, we should be concerned as a country that the recent changes in plant regulations in the EU will likely have a detrimental impact on the citrus industry. As we highlighted last week, the EU recently imposed protectionist measures on agriculture by changing its regulations on plant safety for citrus without notifying its trading partners within a reasonable time. The new regulation purports to protect the EU from a quarantine organism, false codling moth, by introducing stringent new cold treatment requirements, particularly on citrus imports from Africa, mainly impacting South Africa, Zimbabwe and the Kingdom of Eswatini. South Africa has put rigorous measures to control false codling moth, which the EU uses as a pretext to restrict citrus imports from Africa. We view this as a cover to protect the EU's citrus-growing countries like Spain and will increase costs to the Southern African citrus growers.

In essence, the cases of the South African wool and citrus industry present both the instances of growing protectionism across the world and a strong need for the South African government to assist in preserving these export routes actively. The threats to the farming businesses are as severe as it is to the country that has flagged agriculture as a critical industry for growth and job creation. None of the government's growth plans in the sector will be a success without political leadership to resolve these challenges.

What should happen next is an urgent meeting between the South African trade and agriculture ministers with the industry leaders to consolidate views and take forward a "South Africa" message, not industry or government, separately. While science matters in both cases, the challenge is so urgent that there needs to be a diplomatic or political resolution, and after that, the scientists can follow up with the work. Failure to prioritize these issues will be detrimental in a country already haunted by high unemployment and low growth.

Exhibit 1: South Africa's wool exports



Source: Trade Map and Agbiz Research

Weekly highlights

Global food prices soften for the third consecutive time, but agriculture production fundamentals remain a concern

In an environment of generally higher product prices for the consumer, the FAO's Global Food Price Index decelerating by 2% from May to 154 points in June is a welcome development. This third consecutive decline was mainly underpinned by softening in the prices of vegetable oils, grains and sugar. In the case of grains, the decline in prices from the higher levels we saw following the invasion of Ukraine by Russia is mainly on the back of improved wheat supplies following the harvest period in the northern hemisphere. The vegetable oil prices coincided with Indonesia's decision to reverse its policy proposals to limit the export volumes of palm oil. This policy reversal brought assurance of supplies' availability, which worried importing countries. Still, the global food prices are at reasonably elevated levels compared to last year, up 23% year-on-year (y/y).

The softening of global grains and oilseeds prices has continued into July and will likely reflect a fourth consecutive decline in prices in the update of the FAO's Global Food Price Index for July. That said, the global grains and oilseeds market fundamentals remain roughly unchanged. The Russia-Ukraine war continues to block exports and production within Ukraine. Moreover, the 2022/23 season remains at risk of a continuous La Niña, which could weigh on South America's harvest. In its June 2022 update, the International Grains Council (IGC) estimated 2022/23 global wheat production at 769 million tonnes, down 2% y/y. The expected decline in production is mainly in the EU, Australia, Argentina, Ukraine, China, and India, mainly because of expectations of unfavourable weather conditions. Consequently, the 2022/23 global wheat stocks could fall by 3% y/y to 273 million tonnes. These data support generally higher commodity prices; hence we think the current decline in prices will likely be limited or not be a complete reversal to the pre-war levels.

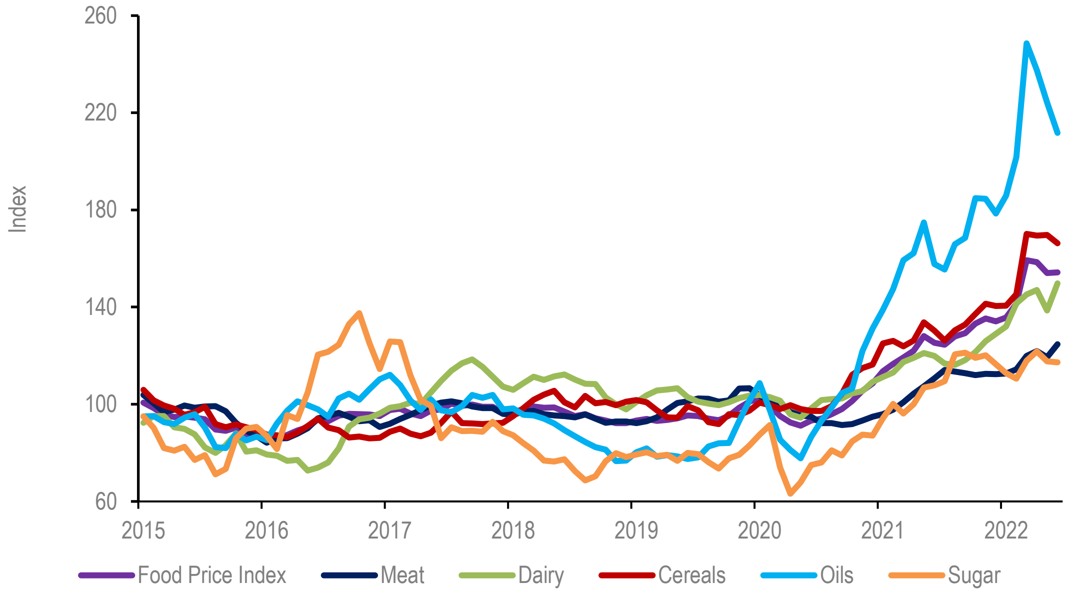
We see similar conditions with the 2022/23 global maize production, which is set to fall by 2% y/y to 1,19 billion tonnes. The IGC sees a decline in harvests primarily in the US, Ukraine, EU, and India. Consequently, the 2022/23 global maize stocks are currently forecast at 271 million tonnes, down 5% y/y.

Soybeans and rice are exceptions. The 2022/23 rice production is forecast at 518 million tonnes, up by 1% y/y. India, Vietnam, Thailand, Pakistan, Indonesia, Bangladesh, Brazil and the Philippines are all behind the optimism about improving global rice production. This will help countries battling to cope with higher wheat prices, specifically somewhat cheaper products like India's rice which remain competitive compared to other countries. The stocks will likely fall marginally from the 2021/22 season, reflective of a potential increase in rice consumption.

The 2022/23 global soybean harvest is set to reach a new peak of 390 million tonnes, up 11% y/y. The expansion in plantings in the US, combined with an expected increase in area plantings when the season starts in Brazil, Uruguay, and Argentina, are behind this expected large crop. Here one should keep in mind the point we made earlier about the potential La Niña-induced dryness in South America, which could change this favourable picture. Still, a lot of this will unfold in the coming months; the numbers as they stand are promising. The stocks will improve by 31% y/y to 56 million tonnes if the production materializes. Such an improvement would add pressure not only on soybeans and their product prices but also across the vegetable oils market.

Ultimately, the FAO's Global Food Price Index presents a welcome picture of decelerating global prices from the peaks we saw in the days and weeks after Russia invaded Ukraine and disrupted production and trade. Still, this cannot be taken as a given that global prices are normalizing; there will be some level of that in rice and soybeans. But the wheat and maize story remains uncertain.

Exhibit 2: Global Food Price Index



Source: FAO and Agbiz Research

Data releases this week

We start the week with a global focus, where, today, the United States Department of Agriculture (USDA) will publish its weekly **US Crop Progress** data. In these data, our focus is on the crop-growing conditions. In the previous release, in the week of 05 July 2022, about 64% of the maize crop was rated good/excellent, which Is in line with the rating in the same week a year ago. Moreover, about 63% of the soybean crop was rated good/excellent, compared with 59% in the same week last year. On Tuesday, the USDA will publish an update of its flagship monthly publication, the **World Agricultural Supply and Demand Estimates** report. This report will help us have an updated view of the global production conditions that we stated above, leaning on the International Grains Council estimates. On Thursday, the USDA will release the **US Weekly Export Sales** data.

On the domestic front, on Wednesday, SAGIS will release the **Weekly Producer Deliveries** data for the week of 08 July 2022. This data will help us get insight into the progress of the maize harvesting activity. In the previous release of the week of 01 July, about 4,33 million tonnes of maize had already been delivered to commercial silos, out of the expected harvest of 14,68 million tonnes. Moreover, the soybean harvesting process is nearly complete. In the week of 01 July 2022, about 1,99 million tonnes had already been delivered to commercial silos, out of the expected harvest of 2,09 million tonnes. In terms of sunflower seed, in the week of 01 July 2022, about 649 386 tonnes had already been delivered, against an expected harvest of 961 350 tonnes (second largest on record).

On Thursday, SAGIS will publish the **Weekly Grain Trade** data for the week of 08 July 2022. In the previous release on 01 July 2022, which was the ninth week of South Africa's 2022/23 maize marketing year, the weekly exports amounted to 70 450 tonnes. The key markets were Japan, Taiwan and the Southern Africa region. This brought the total 2022/23 exports to 780 243 tonnes out of the seasonal export forecast of 3,20 million tonnes. This is slightly down from 4,10 million tonnes in the past season due to an expected reduction in the harvest.

South Africa is a net importer of wheat, and 01 July was the 40th week of the 2021/22 marketing year. The total imports are now at 1,24 million tonnes out of the seasonal import forecast of 1,48 million tonnes (slightly below the 2020/21 marketing year imports of 1,51 million tonnes because of a large domestic harvest). The major wheat suppliers are now Argentina, Lithuania, Brazil, Australia, Poland, Latvia and the US. But if one looks into South Africa's wheat imports data for the past five years, Russia was one of the major wheat suppliers, accounting for an average share of 26% a year. This has now been replaced by the above-mentioned suppliers.

The weather forecast for this week shows clear skies over most regions of South Africa.

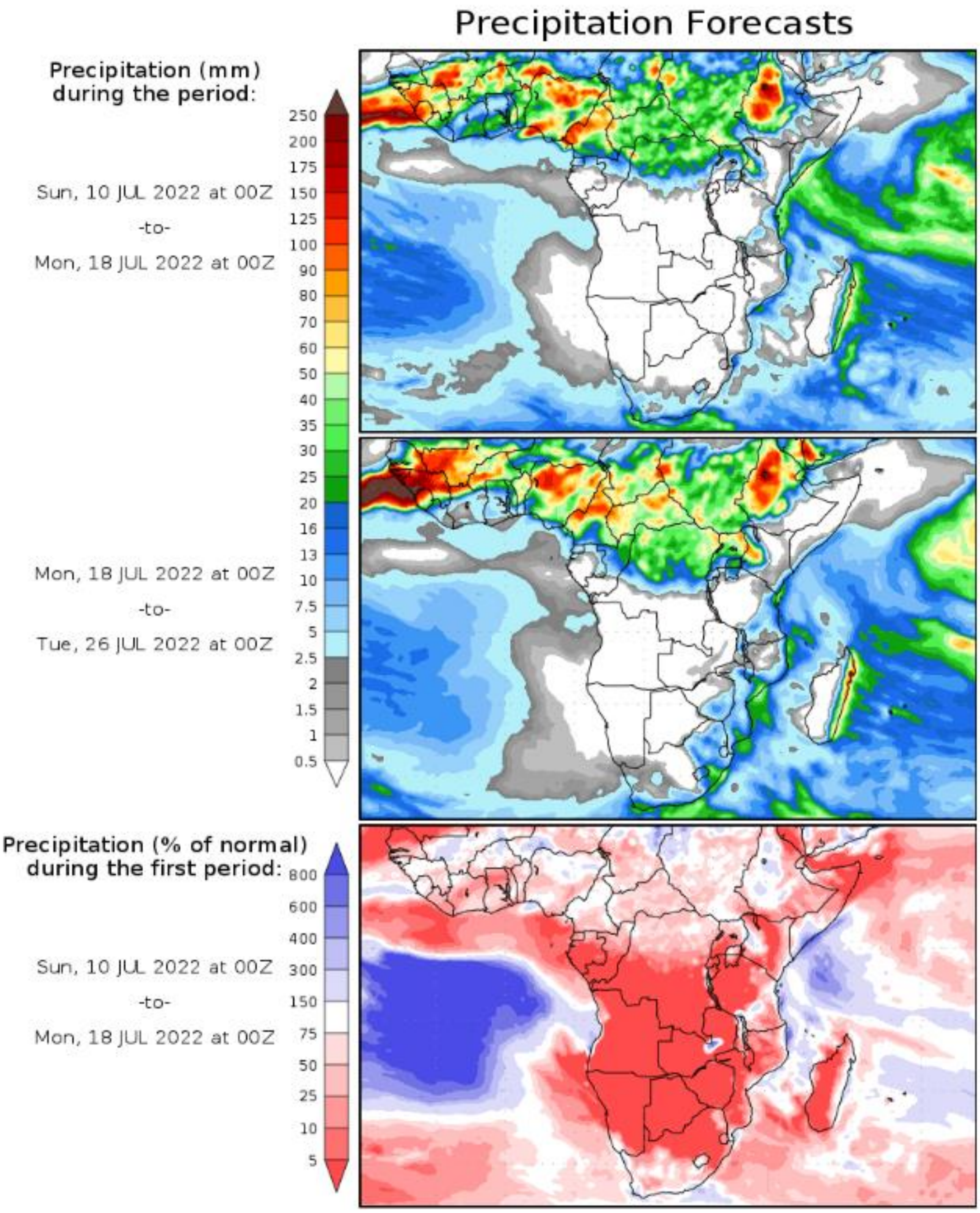
This is with the exception of possible light showers in the Western Cape.

This drier weather outlook bodes well for the summer crop harvesting process that is currently underway.

Simultaneously, the rainy weather in the Western Cape will benefit the winter crops.

The week thereafter shows prospects of rainy weather across the eastern regions of South Africa. This will, hopefully, be at a time when most of the summer crop harvesting would have been completed in the region.

Exhibit 3: South Africa's precipitation forecast



Source: George Mason University (wxmaps)