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SA agriculture machinery sales on a firm footing

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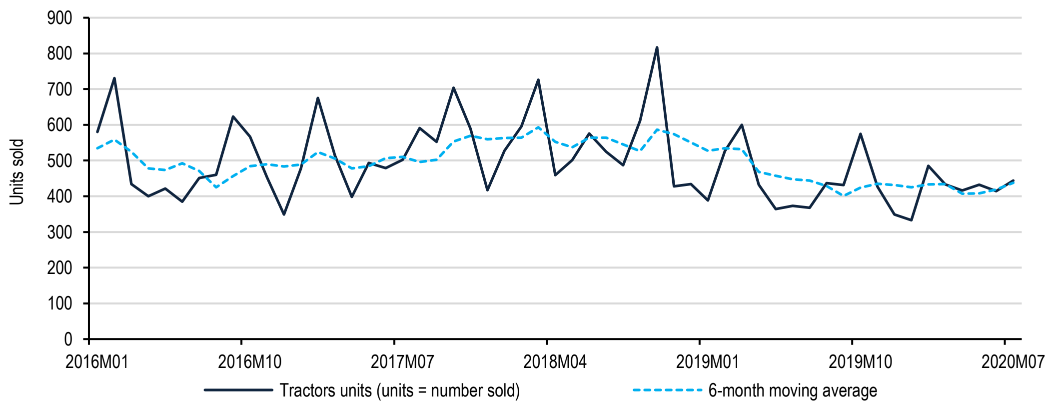
South Africa's tractor and combine harvester sales were up by 21% y/y and 38% y/y in July 2020, respectively, with 444 units (Exhibit 1) and 11 units sold. An important driver of sales in July and the preceding two months has primarily been farmers' decision to buy the existing stock at relatively affordable prices, ahead of the inevitable price increases which will prevail as a result of the weaker rand. Also, the large summer grains harvest in 2019/20 production season and relatively favourable prices have somewhat improved the farmers' financial position to acquire additional machinery.

While South Africa's agricultural machinery sales this year could largely be positive than we initially expected because of the aforementioned reasons, we expect subdued performance going into 2021. As we have previously stressed, the drag on South Africa's agricultural machinery industry will likely emanate from weak exogenous macroeconomic fundamentals. First, the weaker domestic currency will lead to higher prices for imported agricultural machinery, which will reduce farmers' ability to acquire tractors and combine harvesters. Second, the further downgrade of South Africa's sovereign credit rating to the sub-investment grade could negatively influence the financing of agricultural equipment. Ordinarily, the South African Reserve Bank would have responded to the downgrade by raising interest rates in anticipation of possible exchange rate depreciation and associated inflation risks, which would have increased the cost of capital.

However, now the situation is different. The global supply chain disruptions associated with the COVID-19 pandemic has led to deteriorating economic conditions. Several central banks, including South Africa, have responded by reducing interest rates to ease financial conditions. With that said, while the implied prime rate after the recent policy rate cuts would suggest easier financing conditions, the commercial banks are likely to be more risk-averse in the current unprecedented environment. This, in turn, would influence the farmers' ability to continue purchasing the agricultural equipment in high volume. Lastly, a year of relatively good sales is likely to be followed by a subdued period as the rate of replacement of machinery with new ones would generally be low.

Exhibit 1: South Africa's tractor sales



Source: South African Agricultural Machinery Association (SAAMA), Agbiz Research