La Niña and prices surprises will make farmer fingers itch for the soil

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SA is about a month-and-a-half from the start of the 2020/2021 summer crop planting season. Commodity prices and the weather outlook are the most important indicators of farmers' potential planting decisions for the season ahead.

I recently discussed the latter on these pages, highlighting that the forecast La Niña weather event this summer signals higher rainfall, which is conducive for crops. The former is the one I find most interesting and is also supportive of a potential increase in plantings in the 2020/2021 season.

I am surprised that domestic grain and oilseed prices have remained firm for so long given the underlying supply and demand conditions. In the week of August 13, yellow and white maize spot prices were up 5.3% and 0.2% year on year respectively, trading at R2,895 and R2,880 per tonne.

Sunflower seed and soybean prices were up 22% and 27% year on year in the same time, trading at R6,698 and R7,317 per tonne. Such price levels would be expected in years of scarcity when there has been drought or lower plantings, but that is not what the country is experiencing. The 2019/2020 harvest was an abundant one, with the maize harvest up 38% to the second-largest on record at 15.5-million tonnes. The sunflower seed harvest was up 13% at 765,960 tonnes, and the soybean harvest up 8%, with 1.3-million tonnes expected. This raises the question of what the underlying drivers of prices are, and whether prices can be sustained at these levels.

The major drivers of maize prices are the following:

- Strong demand from the Southern Africa region and deep-sea markets. In the week of August 7 about 1.1-million tonnes of maize had already been exported to these markets. It equates to 41% of the expected 2.7-million tonnes, slightly more than in a typical season, in which exports, specifically to Southern Africa, would gain momentum towards year's end. This is an indication of strong external maize needs, and we expect exports to continue, specifically to bigger markets such as Zimbabwe, and outside the continent to the likes of Japan, Taiwan and South Korea.

- The delay in maize deliveries due to the late start of the season.

- The weaker domestic currency is a contributor to the uptick in prices, as I have recently demonstrated in Agbiz research notes. The correlation between maize prices and the exchange rate over the past year is 79%. As the currency weakens maize prices tend to rise.

Global commodity prices, specifically Chicago maize prices, might have had minimal influence on domestic maize prices as they had softened 7% year on year on August 13.

Regarding soybean and sunflower seed prices, the interaction with the global market is different as SA is a net importer of these commodities. The domestic market thus tends to be sensitive to global developments. To this end, Chicago soybean and EU sunflower seed prices were up 8% and 10% year on year respectively on August 13, supporting the domestic oilseed market. The weaker domestic currency is an additional factor that adds support to the domestic oilseed market.

Overall, these factors have overshadowed the news of a large crop harvest in the 2019/2020 production season, which would typically be associated with lower commodity prices. This environment provides a greater incentive for farmers to maintain or increase plantings in the 2020/2021 production season, which begins in October.

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