



20 January 2012

Outlook and expectations on the environment impacting on agribusinesses in 2012

1. International arena

The International economy remains fragile, as the EU's **sovereign debt crisis** remains unresolved and prospects still appear gloomy and risky. Some economists consider the US to be in a "soft patch", as their numbers look better. However, the improved prospects are not considered to be sustainable as some predictions indicate the possibility of the US' economy moving into recession in 2013 due to their massive debt levels. As the EU has GDP growth prospects of around or below 1%, it can be considered to be in a "mild recession", of which the recovery is expected to be slow and protracted.

As the EU is traditionally South Africa's most **important agricultural export destination**, the agribusiness sector is specifically concerned about the demand for its agricultural exports. Purchasing power is relatively low, especially for high value goods and world agricultural trade is expected to be low in 2012. The relatively strong Rand is also limiting foreign earnings, making the export sector less attractive.

Emerging markets, such as developing Asia and Sub Saharan Africa, will predominantly **drive world economic recovery** and growth in 2012, and most probably the couple of years thereafter. South Africa's positioning as the new member of the BRIC (Brazil, Russia, India and China) countries, making BRICS, can assist in further enhancing the trade possibilities with, especially, China and India. This can also have significant opportunities for South Africa's agriculture export industries. However, there has been a general warning to not solely base strategies on the opportunity to trade with emerging countries, as it might only be the "flavour of the day", for the risks are difficult to calculate at this stage. South African agribusinesses have taken up the challenge in exploring opportunities in Southern Africa. As the world population increases and the need to produce food increases, the underutilised resources in **Africa remain a very good opportunity**. Agribusinesses in South Africa are very well positioned to enter into other African countries to provide inputs, services and markets to the emerging agricultural sector. In 2012 and a couple of years thereafter, these initiatives will draw much attention and expand robustly.

2. Local economy

South Africa is not only exposed to the same economic risks that any other country has to face, but also has to overcome the burden of its past, by addressing the social imbalances which are attracting much attention from policy and business decision-makers, whilst attempting to achieve economic growth.



Agricultural Business Chamber Landboubesigheidskamer

The South African economy is growing slower than previously projected. **GDP growth dropped** from almost 5% in early 2011, to a mere 1,3% and 1,4% in the second and third quarters respectively. These rates remain much lower than what is required to enable the structural changes necessary to address the social imbalances and especially unemployment. Growth forecasts were adjusted downwards by most economists and business decision-makers as well as government. It is a major concern that the **primary sector of the economy, including agriculture, has contracted** since the beginning of 2011. The contraction in agriculture is expected to ease somewhat in 2012, as higher agricultural product prices could bring about some relief.

The **Exchange Rate of the Rand** is and has been affected severely by global economic uncertainty. Developments in the US and European debt markets will continue in 2012, promising nothing but further uncertainty in this regard. Foreign investors' appetite for emerging markets ensured the recovery of the nominal effective exchange rate of the Rand after its weakening in mid-2011. Even though investors will again show their trust in the Eurozone's plans to address the debt crisis, the interest in developing countries, including South Africa, is likely to continue throughout 2012. Agricultural exporters, have adapted over the past two years to the relatively stronger Rand, can, most probably, can look forward to a more stable exchange rate scenario in 2012.

As projected, the **inflation rate** has pushed past the Reserve Bank's inflation target of 3-6% to 6,1% in November 2011. This was due to a number of exogenous factors, reflected primarily in increased administered prices such as fuel and electricity prices, as well as food prices. The Monetary Policy Committee will be faced with an enormous challenge in 2012. To achieve price stabilisation, an increase in interest rates might be expected. However, a tightening of monetary policy could further strain the growth potential of the domestic economy. Agribusinesses should probably be prepared for a **slight increase in interest rates** later in 2012, if inflation does not fall back within the target range.

It is uncertain how Basel III will affect local **credit availability**. The tougher liquidity ratios required will probably result in financiers limiting credit facilities, especially to higher risk ventures, which include various agricultural projects. The required liquidity ratios will translate into higher costs for banks, which will significantly increase the cost to lenders. This could have a detrimental effect on economic growth and recovery expectations. This development also needs to be considered by agribusinesses, especially with the probability of a marginal increase in interest rates.

3. The 2012 agenda

The **cost of doing business** in South Africa is currently the most significant challenge and reflects directly on the bottom line of business and at national level. Administered prices and cost of using national infrastructure, such as toll fees, port tariffs, etc., is simply proportionally too high. The poison is in the pudding, as the economy is in dire need of infrastructure development. However, if the cost of using it is too high, the longer term effect is destructive. The **cost of labour** is increasingly obstructing business growth; higher wages are not necessarily the concern, but wages totally



Agricultural Business Chamber Landboubesigheidskamer

outweigh the productivity levels. Agriculture and agribusiness are traditionally major employers in South Africa. Solutions to enhance sustainable employment are essential in 2012, not only for employment statistics, but primarily for economic sustainability in the rural areas, where agriculture and agribusiness have the biggest contributing effect.

High agricultural commodity and farm gate prices are of advantage to producers and agribusinesses; however, the affordability of food to consumers is becoming a big concern – now more than ever. **Food security** does not only refer to sufficient volumes of food production as compared to the population, but also the ability to distribute the food to where the consumers reside, as well as the affordability thereof. The cheapest food is unaffordable if consumers do not have an income. The emphasis should also be on creating Household food security and not just on national food security. Sufficient and sustainable employment is crucial to the agro-food industry. **Unemployment** has become a top-of-the-agenda point for politicians in 2012, and so it should be for any business decision-maker. Employment did increase in the later part of 2011, but the unemployment rate is expected to remain at elevated levels for some time still. Government cannot carry the social burden by themselves anymore. Business, in general, is doing much in this regard, but 2012 should be the year of collaboration in this regard. Partnerships between government and private sector, towards employment generation, transformation and development, are essential in achieving sustainable employment and income generation.

The **social challenges in South Africa**, being addressed reactively as they escalate and become more pronounced, have emerged from being systematic risks, to reaching the fearsome reality of becoming a systemic risk, if left unattended. The cauldron brought forth by the legacy of the past almost reached boiling point in 2011. Finding the middle ground on what actions are feasible and affordable, versus the cost of an untransformed economy, plagued with high unemployment and unequal and distorted distribution of income, will be a major challenge, especially for the agricultural and agribusiness sector in the rural areas of the country.

Land Reform remains a politically sensitive subject causing much uncertainty and lack of investment confidence. Government's lack of management and delivery, related fraud and corruption and the more recent funding constraints have caused much frustration, especially amongst beneficiaries whose expectations were often unrealistic high. Lack of sufficient support structures for beneficiaries also directly contributed to the 90% failure of farming projects, which is a generally accepted figure. Land Reform should have been beneficial toward providing social stability and more equal income distribution. However, it has resulted in a social, economic and political burden, as the cost is now higher than expected, confidence in the delivery process is low and politicians have used it to their benefit. Industry will rely heavily on constructive outcomes emanating from the current Green Paper on Land Reform process. Many eyes will be on Minister Nkwinti for effective leadership in this regard in 2012. While orderly and market-based Land Reform is a necessity, it has been politically and administratively abused.



Agricultural Business Chamber Landboubesigheidskamer



Following the acclaimed awareness on **sustainability** during COP17 in Durban at the end of 2011, business as usual in this regard is not an option from 2012 onwards. Agribusiness and agricultural producers are obliged to achieve more with less, focusing on improved technology and cultivars, implementing more efficiency-oriented production techniques, efficient water use and reduced energy consumption. Human resources are also essential in achieving sustainability, through relevant capacity development and information. Decreasing agriculture's carbon footprint and reducing emissions will also top the agenda, with consideration of "buying local", "buy in-season", "less transport" and "self-sufficiency". Agribusinesses are well positioned to head up developments regarding renewable energy. Sustainability strategies will become inevitable as consumers will demand these and as resources become more scarce and expensive.

The inability to manage **biosecurity issues** proactively in 2011 has had devastating effects on certain industries in the agricultural sector. Government's inability to effectively manage issues regarding the avian flu outbreak, rift valley fever and foot-and-mouth disease control is a disgrace, especially the lack of commitment by leaders within government. Existing and new biosecurity threats will continue to emerge in one or another form. Therefore industry and government have to address the biosecurity issue as a priority from 2012 onwards, to prevent such mammoth losses that can close down certain industries, as nearly experienced in 2011.

Most of the major topic for consideration in 2012 will ultimately impact on attracting investments, as investments are vital to achieve industry growth. The agriculture and food sectors promise sufficient opportunities, especially for South African agribusiness, which not only are well positioned in contributing significantly to South Africa, but also act as a gateway to unlocking the Southern African agricultural potential. Focus should be placed in attracting Foreign Direct Investments, as well as sufficiently directed and allocated local capital investments. The Medium Term Budget Policy Statement in 2011 promised incentives for business to invest. Agribusinesses should keep their eyes open for announcements in that regard in 2012, as partnerships with government in this context could enable many developments and further growth.

For more information, please contact:

Lindie Stroebel
ABC Manager Economic Intelligence
079 497 1594
lindie@agbiz.co.za