Another narrow escape for soya

Fears of a recessionary hit to world demand have dominated the oilseed complex in the first quarter of 2009, eclipsing drought and political problems in South America and the potential for slower growth of oil production in the year ahead. John Buckley writes

Fears of a large shortfall in soyabean supply and signs of world economic revival drew speculators back to the futures markets in droves towards mid-2009. Amid weaker palm, rapeseed and sunflower output, vegetable oil prices returned to six-month highs. While brighter soya prospects and faltering oil demand have since deflated this 'mini-boom', speculators may not lack excuses for excitement in the months ahead.

Soyabean output on the up

The first half of this year has seen extreme volatility in fats and oils prices, led by US soyabean futures. Strength in soya, half the world's oilseed supply, was inevitable when the Argentine crop turned out even worse than expected – around 30M tonnes against early forecasts of over 50M tonnes. Brazil's was also 4M under target at 57M tonnes and Paraguay's crop almost halved to 3.8M tonnes. With high hopes pinned on the USA to fill a looming deficit in 2009 and 2010, markets went through a nail-biting period in May and June this year when, for a second year running, endless rain delayed sowing in key US states well beyond optimum dates. Consumers, already nervous about the impact of Latin American shortfalls, stepped up buying, especially top importer China, which made continued raids on dwindling old US crop supplies, pushing futures close to US$13/bushel in early June.

However, last year's Midwest floods demonstrated that late sowing doesn't necessarily lead to disaster and, on a larger area, 2008's average 39.6 bushel/acre yield was enough to deliver a 10% rise in output (*see Figure 1, right*). Now that this year's US crop area has clearly expanded again (although perhaps by less than many expected), crop ratings are very high and yields are officially well above last year's. Even with the risks to a late crop from summer heatwaves and early frosts, the crop could easily add another 8-10% in its 87M-91M tonne range.

The demand side of the soya balance also offers less encouragement for speculative bulls. US crush – which despite a late season rally for meal export demand – is still expected to finish 2008/09 8% down. The USDA suggests it may only rally 1.5% in 2009/10 as a recession-hit livestock industry holds domestic meal demand 2M tonnes below the 2007/08 level for a second year. US soyabean exports, in contrast, are expected to improve on the past year's stronger, 34M tonnes-plus level (even if the next Latin American crop rebounds to record levels). However, combined domestic and export use still implies US 2009/10 ending stocks of more than double this season's wafer thin 3M tonnes.

FIGURE 1: SOYA OUTPUT (M TONNES) SINCE 2005 AND 2009 FORECAST

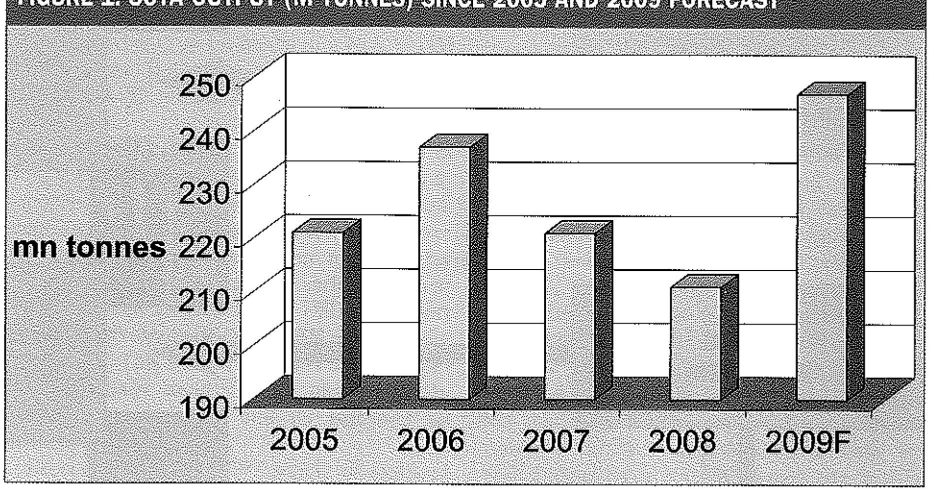


FIGURE 2: CHINESE SOYABEAN IMPORTS (M TONNES)

Despite the reduced weather risk to the US crop, soya has been more reluctant to give up on the speculative bull run than grains, which recently saw massive drops to seven-month lows (maize nudging three-year lows). Chicago's soya industry shed about US$2-US$3/bushel in July but put half of that back on again in early August as China stepped up new crop purchases and funds sensed another opportunity for quick profits. However, the prospect of sky-high prices as US old crop stocks ran out altogether appeared to have been allayed by crushers shutting early for summer plant maintenance, amid the less attractive margins.

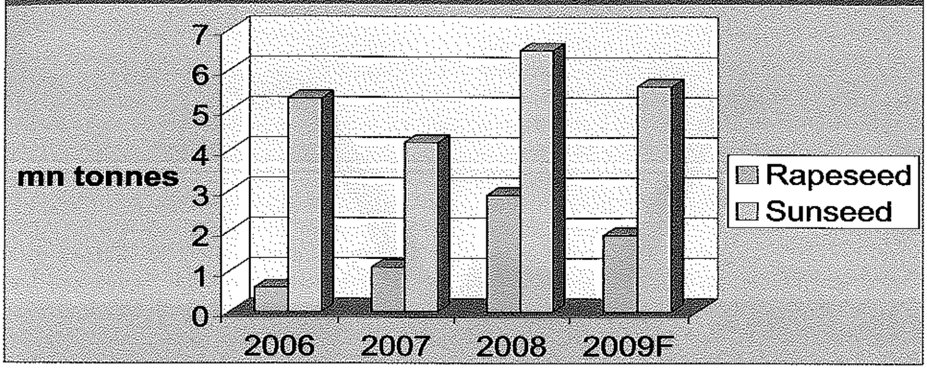
Some analysts have predicted a further break to US$7 by the autumn if the US crop hits target and South American producers actually sow the larger areas forecast. Brazilian consultancy Celeres recently estimated that its next crop could rise over 11% to 64.7M tonnes due to the now highly favourable price ratio between soya and maize. Argentine sources forecast a 15-20% rise in sowings and a 50-60% crop rebound if yields recover from this year's drought-reduced levels. All of this is a long way off and subject to weather and other factors but clearly points to potential for far looser soya supplies.

The forecast US oil balance for the season ahead has something for bulls and bears. Biodiesel remains a disappointment for the former, with the USDA cutting its forecast for soya use in this sector again from almost 1M to 900,000 tonnes – better than last season's 750,000 tonnes but nowhere near the 1.47M tonnes of 2007/08. With food sector use flaccid as well, US soya oil demand is expected to stay at almost one million tonnes under the 2007/08 peak level – important for world demand as the USA is the second largest consumer of this oil.

However, oil exports were expected to perform better with the USDA forecasting a near 50% rise amid tighter Latin American supplies in the first half of 2009/10 and a recovery in global consumption of 1.44M tonnes or 4%, led by top consumer China (up 500,000 tonnes to almost 10M tonnes). Even so, at just over 37M tonnes, world demand would still be lower than in 2007/08, before last year's record prices and the recession began to cramp demand.

China remains a bullish, but ambivalent factor for soyabeans and the vegetable oil complex as a whole. Despite a 2M tonnes jump in its own soya crop, it has continued to raise imports by a further 1-1.5M tonnes in the 2008/09 season while tucking away 6M tonnes of its domestic harvest in a strategic reserve stock to support producer prices and encourage domestic output (*see Figure 2, left*). However, the past month or so has seen a raft of conflicting signals on what will happen next. For many weeks, officials have been ▶

FIGURE 3: UKRAINE OILSEED PRODUCTION (M TONNES)



indicating that the record level of soyabean imports in June and July would be scaled back due to congestion at ports, while some of the reserve stock has been offered back to the domestic market – although at prices that have drawn little interest to date. Some officials, meanwhile, put next season's soyabean imports 1-2M tonnes higher at a record 40M+ tonnes (accounting for well over half of the world soya trade). The outcome partly depends on China's own soya crop, which many analysts expect to contract this year after various weather problems. China is also reported to be suffering from a glut of meal amid swine flu and recession fears reducing feed demand and encouraging surplus soya meal exports to neighbouring countries. However, while the primary reason for China's emphasis on meal-rich soyabeans is its large domestic feed deficit, the oil side of the equation needs to be watched closely too. Soya dominates Chinese oil consumption – accounting for 10M tonnes next season out of total vegetable oil demand of 23M tonnes) and demand for it is expected to grow at least as fast as that of palm oil in the coming year. To date, China has kept up brisk buying of old and new crop US and Latin American soyabeans and as well as palm oil and rapeseed. However, recent bouts of weakness in its domestic oil markets and ongoing reports of declining crush margins suggest it may remain a wild card in both oilseed and oil imports.

Dip in output for rapeseed

Although EU rapeseed farmers planted more than expected this year – about 3% over 2008 – early forecasts were for a dip in output of about 700,000 tonnes (to 18.3M tonnes) based on yields retreating from last year's above-average levels. This might turn out too pessimistic while large 2008/09 ending stocks will also supplement next season's crush. However, biodiesel consumption appears to be on the rise again and total industrial use may account for any extra oil produced, taking over two-thirds of the projected 9M tonnes supply and capping food demand close to the past year's level of about 2.7M tonnes.

Rapeseed production is seen more sharply down in the Ukraine due to a cut in area and a more significant drop in yields, which could reduce output by 1M tonnes from last year's 2.9M (*see Figure 3, above*). Lower exports may show up in a significant drop in imports by the EU, as the main outlet for Ukraine.

The main grey area for rapeseed supply is Canada, where a late spring drought in some areas and too much rain in others have seen trade and official figures diverge widely over crop potential. The USDA's July forecast of a 2M tonnes drop to 10.5M tonnes output assumes sown area of 6.2M ha (vs 6.5M ha last year and 5.64M ha in 2007) and yields down about 13%. Local observers sit both sides of this forecast and appear to disagree considerably over yield potential too, leaving crop estimates in a wide 9-11M tonnes range. If Canada maintains exports of around 6.5-7M tonnes and domestic needs of over 5M tonnes, that could mean a current crop deficit. However, around 2.3M tonnes carried in from the past bumper crop can be drawn on to supplement supply. Whether Canadian exports come anywhere near 2008/09's peak level of over 7M tonnes depends heavily on top importer China – which bought actively earlier this year but is currently forecast by the USDA to import only 950,000 tonnes against 2.35M tonnes in the past season. This estimate appears too low, however, especially amid China's own uncertain oilseed crop prospects and its supposed oil demand growth.

Recently, the large 2009 supply of rapeseed has been weighing on the market with rapeseed oil prices in Europe (bulk, ex-tank Rdm) about 15% below their late May peak of US$700/tonne.

Sunflower and palm oil prospects

The past year's good EU/CIS supply has also seen sunflower oil prices tumble about 18% from their highs, despite forecasts that this year's world sunflowerseed crop will drop by almost 1M tonnes as recovery from last year's poor crop in Argentina is outweighed by smaller Russian, Ukrainian and EU harvests. The CIS countries' smaller supplies will be felt in Europe, which has become a major destination for their exports in recent years. Dry weather has taken a toll in Spain and Eastern Europe and while the French crop looked promising, a return to lower average yields is expected to outweigh larger planted area, cutting total EU output by about 500,000 tonnes from 2008's bumper 7M tonnes. However, while EU crush rose sharply in the past season, starting stocks are still larger this year and can supplement 2009/10 supply.

Thanks to last year's big CIS crops, world sunflower oil supply rose by about 1.9M tonnes or almost 20% this past season but current crop estimates suggest crush levelling or declining in 2009/10. Although oil supplies should remain higher than the average level of recent years, demand for this oil has increased sharply with the contraction in its former big price premium over other food oils. EU, South Asian and Middle East consumers have all responded, adding about 2M tonnes to world offtake. Prices of sunflower oil may therefore get less competitive as 2009/10 wears on and the market attempts to ration supply amongst these competing buyers.

Palm oil prices saw the biggest drop over the past two months (27% at one stage) as the earlier peak in prices and more competitive soya oil cut import demand from some of the key buyers. The most notable fall in second quarter 2009 trade was in Malaysian shipments to south Asia, with second largest palm oil buyer India's intake declining from over 200,000 tonnes at the start of the year to just over 57,000 tonnes by June. Pakistan's imports also fell from over 225,000 tonnes in January to 86,000 tonnes in June, although both still took considerably more in the first half of 2009 overall than in January-June 2008. Malaysian sales to top buyer China, meanwhile, stayed robust, gradually rising through the April-June period after a slow start to the year and leaving January-June shipments overall up 9% up on the year at 7.57M tonnes.

The USDA forecasts world palm oil output in 2009/10 at about 45M tonnes – about 2.2M or 5% more than last year, based on gains in Malaysia (+800,000 tonnes), Indonesia (1.25M tonnes), Thailand (+100,000 tonnes) and Colombia (80,000 tonnes). Malaysian officials, on the other hand, expect a possible 700,000 tonnes or 4% decline for calendar 2009 based on performance to date, land held out of production by the replanting programme and smallholders cutting back fertiliser use. First half of 2009 figures bear this out with output running below the levels expected earlier in the year, whereas this time last year, output exceeded forecasts by 8% and ended up 12.5% over. Indonesian officials are only looking for a 300,000 tonnes rise to 20M tonnes next year although some local traders put the figure higher (*see Figure 4*).

Demand for palm oil has sent mixed messages recently. Earlier, port stocks in India and China were reportedly building up to burdensome levels, raising concerns that these top buyers would have to cut offtake in third quarter 2009. However, the July export figures from Malaysia have improved considerably in response to lower prices and the emergent recovery in Malaysia tank stocks (which hit a 1.3M tonnes low in second quarter 2009) appeared to be stalling. Other top buyers – China, Europe, Pakistan and the USA – also appeared to be buying more, although origin suppliers must be aware that too rapid a price response to this trade might kill the goose. Much depends on India's coming oilseed crop, currently in question amid a late and faltering monsoon, as palm usually supplies almost 40% of India's huge vegetable oil import requirement. ●

FIGURE 3: INDONESIAN PALM OIL OUTPUT (M TONNES)