South Africa's agricultural sector growth conditions

There has been a flurry of positive news about the past year's performance of South Africa's agricultural sector. There have also been questions about whether the sector could remain on a positive growth path in 2022 given the excessive rains at the start of the season, rising farm input costs and effects of geopolitics. Hence, in this week's note, we review the sector's growth performance of the past couple of years and offer a view on growth prospects in 2022 and 2023.

Review of 2020 and 2021

South Africa's agricultural sector has had two consecutive years of solid growth, with its gross value-added expanding by 13,4% y/y in 2020 and 8,3% y/y in 2021. This was a period of favourable rainfall, which supported crop yields and grazing conditions for the livestock subsector. The higher commodity prices, specifically for grains and oilseeds, also boosted the farmers' incomes in 2020 and 2021. The firmer global demand for agricultural commodities during this period saw South Africa exporting US$10,3 billion worth of agricultural products in 2020 and a record US$12,4 billion in 2021. The allied industries, such as agricultural machinery, benefited from improved farmers' incomes throughout this period. For instance, South Africa's tractor sales for 2021 amounted to 7 680 units, up by 26% from the previous year. Combine harvester sales amounted to 268 units in the same period, up by 46% from 2020. Notably, 2020 was also an excellent year for South Africa's agricultural machinery sales, so surpassing it means 2021 was indeed an exceptional year. In 2020, tractor sales were up by 9% from 2019. Combine harvester sales increased by 29% from 2019.

During this period, these positive agricultural production conditions were also mirrored in employment conditions in the sector, with 829 000 people involved in primary agriculture in the third quarter of 2021, up by 3% y/y, and well above the long-term agricultural employment of 780 000. When the fourth quarter employment data are released, the numbers will likely show solid employment levels, probably more than this third-quarter level.

The path ahead

If we look ahead, the South African agricultural sector will likely face more challenging conditions this year and going into 2023. The excessive rains at the start of the 2021/22 production season threatened the crops as various areas of the country experienced damages that required replanting. Still, the overall area planting of 4,3 million hectares, well above the 2020/21 season, and the expected summer crop of 17,5 million tonnes (down 9% y/y) means that the excessive rains didn't cause as much damage as initially feared, at least from a national perspective. The currently expected harvest is well above the long-term average levels. In the horticulture subsector, there were damages in some vegetable fields such as tomatoes and carrots. Still, fruits and a range of vegetables seem to be in reasonably good shape.

But the other challenge of this past season for field crops and horticulture farmers was higher input costs which had increased by over 50%. The areas that had to replant following crop damages by excessive rains incurred even much higher costs this past season.

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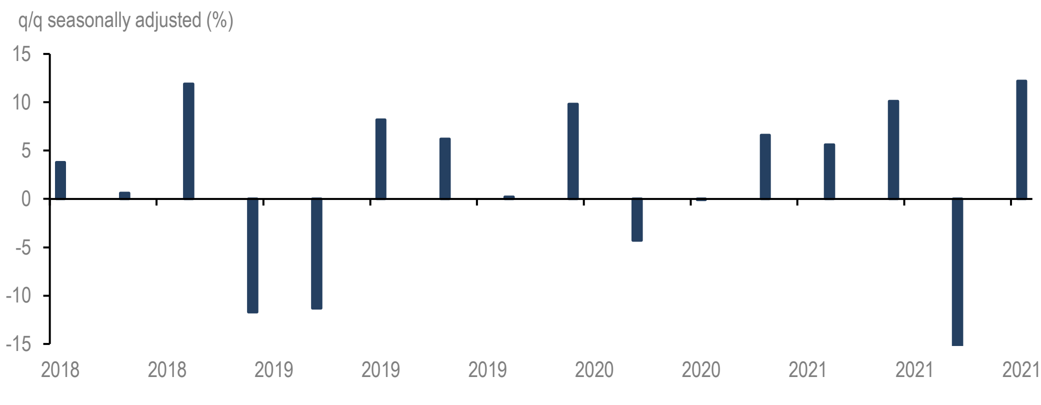
Therefore, the elevated commodity prices, while looking favourable for farmers that have the crop, gains will largely be overshadowed by the higher input costs. The livestock industry remains in solid condition, but there are still biosecurity cases (foot-and-mouth disease) in parts of KwaZulu-Natal and fears of other disease outbreaks on the back of a wet season. Moreover, the higher grains and oilseeds prices add cost pressures to the livestock and the poultry industry that utilizes these products in their feed. This is precisely the case for the poultry sector, where maize and soybeans make up over 50% of input costs. To have these products rising double-digit will add cost pressure to the poultry farming businesses.

The export conditions this year will also be hampered by geopolitics. Citrus was South Africa's leading exportable agricultural product in 2021 in value terms, accounting for roughly US$1,9 billion. Additionally, apples and pears were the fifth largest agricultural product export out of South Africa, accounting for US$689 million. These products had a presence in Russia, about 7% of South Africa's citrus exports in value terms and 12% of South Africa's apples and pears exports in the same year – the country's second-largest market. The Russia-Ukraine war and the following sanctions will likely limit South Africa's presence in these markets in the near term. Given the significance of this market, the diversion of the volumes to other export markets or the domestic market could add downward pressure on prices and, after that, negatively influence farmers' finances and the general export earnings of the country.

From a growth perspective, 2022 will likely be a break from the solid two years of expansion in South Africa's gross value added for agriculture. Our view is that the sector could see a mild contraction in 2022 because of a reduction in the summer crop harvest and the base effects. With that said, employment conditions will likely hold above the long-term agricultural employment levels of 780 000. The recovery in the Western Cape's agricultural production, particularly the wine industry reconstruction strategy, could support employment conditions in the near term.

The outlook going to 2023 will not only depend on general weather conditions but also input costs, particularly fertilizer. The length of the current Russia-Ukraine war and the severity of the damages will matter more for the upcoming season. This is specifically because Russia is the world's leading exporter of fertilizer materials, accounting for 14% of global exports in value terms. The prices have risen significantly, and there are now fears that if the war continues for longer, there could be disruptions in infrastructure and limits in export volumes which will have negative implications for the 2022/23 agricultural season and, after that, the general performance of the sector in 2023. These rising input cost pressures for farmers have also prompted us to view the agricultural machinery sales in 2022 and 2023 negatively. Farmers will likely try to manage their costs wisely and reduce spending on new tractors and combine harvesters for now; although the start of the year sales were robust, the coming months will likely show a slowdown.

Exhibit 1: South Africa's agriculture GVA



Source: Stats SA and Agbiz Research

Weekly highlights

The war is an added risk to the global grains and oilseeds market

Before the war started on February 24, our primary focus in the global grains and oilseeds market was the production conditions in South America and Indonesia, where maize soybeans and palm oil were negatively affected by dryness. The possible lower yields in these countries alone had elevated global grains and oilseeds prices over the past few months. The Russia-Ukraine war is now an additional risk, specifically to export activity. Ukraine suspended its exports activity since the war started. Russia faces some limitations in its export activity because of the sanctions and higher shipment insurance premiums in moving grains to various export destinations. This is a significant challenge because both countries constitute significant global grains and oilseeds export volumes. As we previously stated, in 2021, these countries together accounted for nearly 30% of global wheat exports, about 14% of global maize exports, roughly 32% of global barley exports, and almost 60% of global sunflower oil exports.

So, we now have to view the global grains supplies and stocks from the perspective that the availability is one thing, the most critical aspect will be the shipment of some of these products to various global markets. To this end, the recent monthly update of global Supply and Demand Estimates of grains and oilseeds by the United States Department of Agriculture (USDA) provides essential data for assessing the world supplies amid this uncertainty on trade. The USDA forecasts 2021/22 global wheat production at 779 million tonnes, marginally up from the previous season. About 14% of this harvest is from Russia and Ukraine, and therefore cannot be easily accessible by the global buyers for reasons we stated above; this is the case although both countries are forecast to have 52 million tonnes of wheat for the export market in 2021/22. This accounts for a 26% share of global wheat exports of 203 million tonnes this season.

Because of the increase in global consumption, both in the human and animal feed industry, the 2021/22 global wheat stocks are forecast to decline by 3% y/y to 281 million tonnes. This decline in global stocks, combined with challenges facing shipments in the Black Sea region, means that global wheat prices could remain elevated over the medium term, as has been the case since the days leading up to the invasion of Ukraine by Russia.

Maize is another major grain that has been a central focus, and its production is up 7% y/y in the 2021/22 season, with an expected harvest of 1,2 billion tonnes. The expansion in area plantings in Brazil and Argentina had compensated for the losses in yields. Thus, both countries are set to have a larger harvest than the 2020/21 season despite the drier weather conditions in various regions when the season started.

Russia and Ukraine's production prospects are largely positive compared with the 2020/21 production season. Thus, the available maize for exports in both countries collectively accounts for 16% of the global maize export forecast of 200 million tonnes in the 2021/22 production season. As with wheat, the limiting of exports of such a large volume of maize will continue to add upward pressure on prices in the medium term as buyers continue to place higher bids for maize from other origins such as South America, the US and South Africa, amongst other key exporters. Prices could remain slightly elevated despite the maize stocks having improved by 3% from the 2020/21 season to 300 million tonnes this year.

Rice is another key crop to watch, which countries could use to substitute maize and other wheat. The global production conditions for this crop are favourable, with the 2021/22 harvest estimated at 514 million tonnes, up by 1% from the previous season. This is supported by expected large production in various parts of Asia. Consequently, the 2021/22 global rice stocks are forecast at 191 million tonnes, up by 2% from the previous season. These positive production prospects have kept rice prices relatively under pressure since mid-2021, following a surge at the start of 2021 where some prices crossed US$500 per tonne, to now at levels below US$400 per tonne. But we think a potential surge in demand could push prices up, negatively affecting importing countries such as South Africa, which imports about a million tonnes of rice a year.

Moreover, Brazil and Argentina typically account for 50% of global soybeans production. As such, the reports of dryness in these countries since the season started and the frequent downward revision of the crop by the local analysts raised fears of the potentially lower global soybeans harvest and kept vegetable prices at higher levels since the start of the season. The recent updates from February estimates showed further downward revision of the 2021/22 soybean harvest in these countries. This subsequently weighed negatively on the global harvest, estimated at 354 million tonnes, down by 3% y/y. The firmer consumption level and this decline in production have led to a 12% decline in the ending stocks to a now estimated 90 million tonnes.

These poor soybeans production conditions, combined with expectations of a poor palm oil harvest in Indonesia and the fact that Russia and Ukraine account for nearly 60% of global sunflower oil exports, will keep the global vegetable products prices elevated over the near to medium term. Even if the war were to cease soon, the damage in Ukraine's infrastructure and disruption in society and business would still be a hindrance to production and exports resumption of sunflower oil from this region over the foreseeable future.

In sum, while we started the 2021/22 global grains and oilseeds season with South America and Asia weather challenges being the major risks to production and prices, the Russia-Ukraine war has exacerbated the risks to exports. It will likely keep global prices, and by extension, South African grains and oilseeds prices elevated over the foreseeable future.

SA agriculture machinery industry saw robust sales in February 2022, but the outlook remains uncertain

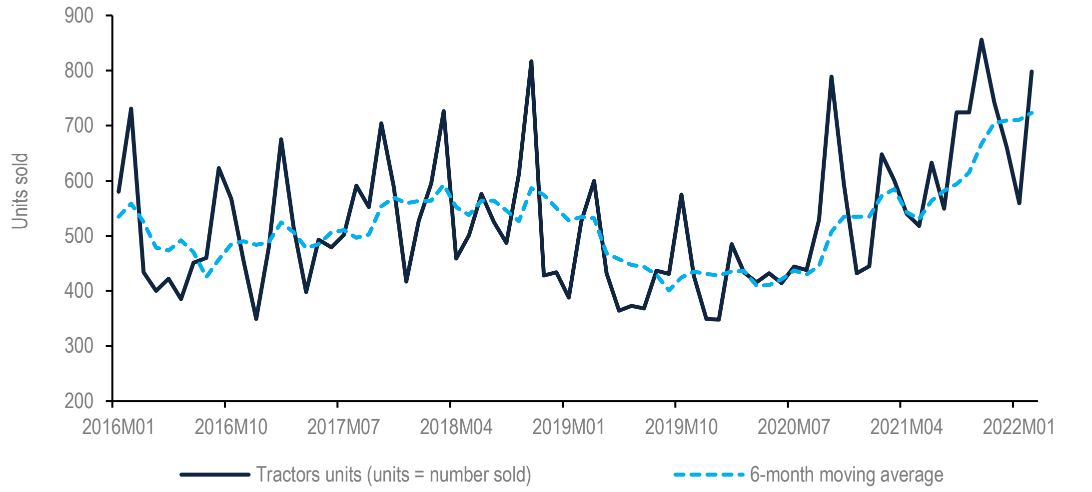
The data released by the South African Agricultural Machinery Association show that agricultural machinery sales have remained on a positive path in the first two months of 2022. The tractor sales were up by 20% y/y in February 2022, with 789 units sold. At the same time, the combine harvester sales were up 36% y/y, with 19 units sold. This builds upon the solid momentum of the past two years.

Essentially, when farmers have a good year, allied industries benefit from farmers' spending the financial gains or from the produce of the farming businesses. Agricultural machinery is one such industry that benefited from farmers' spending in 2020 and 2021. The farmers, specifically grain and oilseed producers, expanded their area planted in these past two years.

Weather conditions were favourable, resulting in a large harvest for two consecutive seasons. This was also when commodity prices remained elevated, supported by global events such as dryness in South America and rising demand for grains and oilseeds in China. Had it not been for higher global agricultural prices, the local grain and oilseed prices would have softened due to large harvests. The financial gains of these years went to improvement in agricultural equipment, among other activities on the farms. For example, South Africa's tractor sales for 2021 amounted to 7 680 units, up by 26% from the previous year. Combine harvester sales amounted to 268 units in the same period, up by 46% from 2020. Notably, 2020 was also an excellent year in South Africa's agricultural machinery sales, so surpassing it means 2021 was indeed an exceptional year. In 2020, tractor sales were up by 9% from 2019. Combine harvester sales increased by 29% from 2019.

Looking ahead, however, we think the remainder of 2022 will likely change the trend and show moderate agricultural machinery sales as the new machinery's replacement rate will probably be lower than the previous years. Moreover, the crop harvest, especially grains and oilseeds, which were the primary drivers of sales in the past few years, will mainly be lower than the past two seasons. The first production estimates already show a 9% y/y decline with an expected harvest of 17,5 million tonnes of all summer crops in the 2021/22 season. Additionally, the Russia-Ukraine war has led to a notable rise in other farming input costs such as fertilisers, fuel and agrochemicals, which will add strain to the farmers' finances.

Exhibit 2: South Africa's tractor sales



Source: South African Agricultural Machinery Association and Agbiz Research

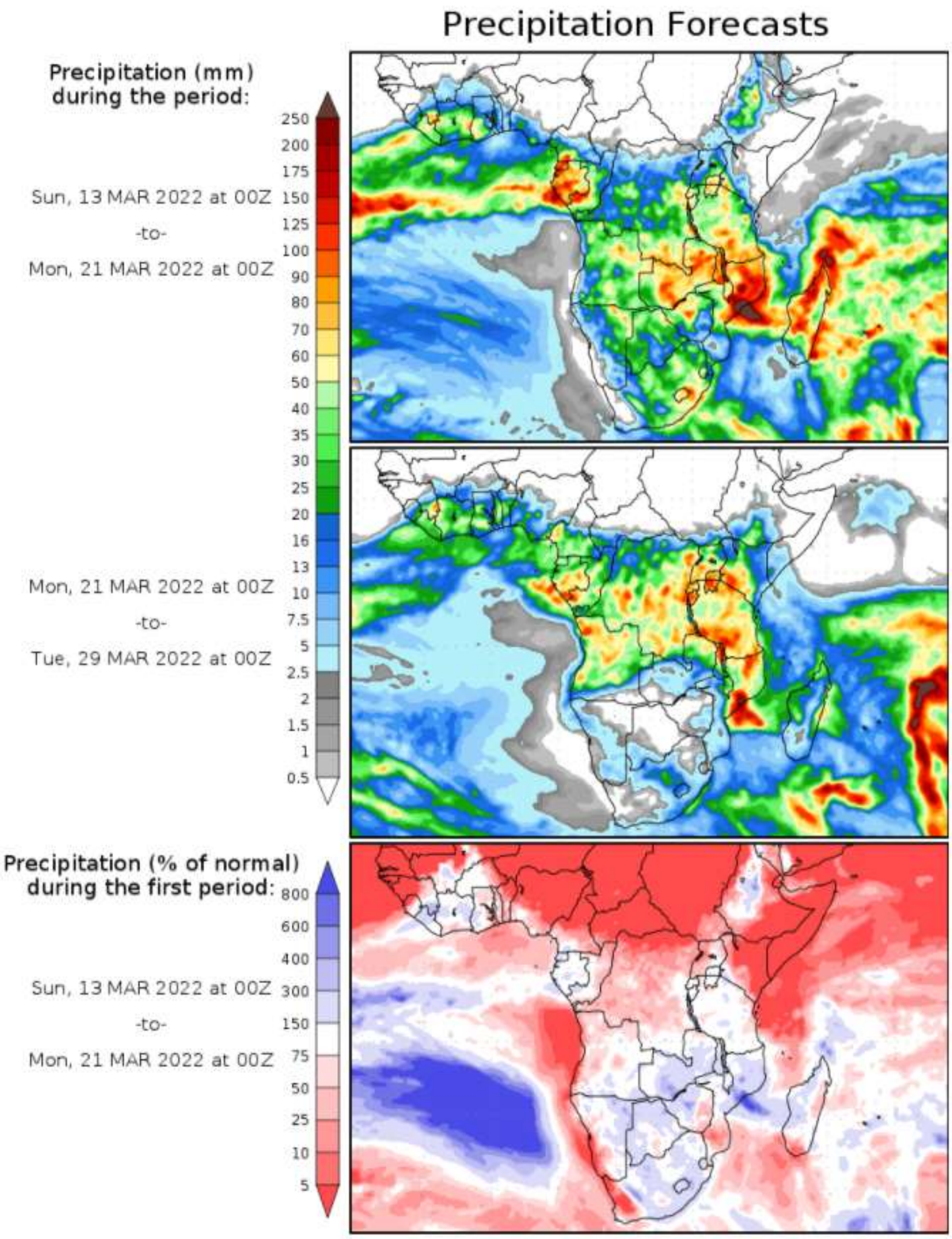
Data releases this week

We start this week focusing on domestic data release; On Wednesday, SAGIS will release the **Weekly Grain Producer Deliveries** data for 11 March. This data cover summer and winter crops. But our focus is on winter crops that have recently completed the harvest activity. The summer crops' new season is still at its early stages. Thus, we will focus on the summer crop data closer to harvest time in the coming months. In the previous release of the week of 04 March, about 2,14 million tonnes of wheat had already been delivered to commercial silos. This covered the first 23 weeks of the 2021/22 production season and equated 95% of the revised harvest estimate of 2,26 million tonnes.

On Thursday, SAGIS will release the **Weekly Grain Trade** data for the week of 11 March. On 04 March, which was the 44th week of South Africa's 2021/22 maize marketing year, total maize exports amounted to 3,09 million tonnes, equating to 79% of the revised seasonal forecast of 3,91 million tonnes (up by 36% y/y). South Africa is a net importer of wheat, and 04 March, was the 23rd week of the 2021/22 marketing year. The total imports are now at 662 826 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).

Globally, the United States Department of Agriculture (USDA) will release the **US Weekly Export Sales** data on Thursday.

Exhibit 3: South Africa's precipitation forecast



Source: George Mason University (wxmaps)

As with the previous week, the weather forecast for this week shows prospects of widespread rains across the country. This is not conducive for summer crop growing areas where there are still higher soil moisture levels.

The week thereafter also shows clear skies over most regions of South Africa, which bodes well for summer crops which now require relatively warm weather conditions as the crop finishes the pollination stage.