

COLLATERAL DAMAGE ON SOYBEAN MARKET: PRICE GAP BETWEEN US AND LATIN AMERICAN PRICES WIDEN

Aneeka Gupta – Director, Macroeconomic Research
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China is the world's biggest importer and America's largest buyer of Soybeans. Growing population, urbanisation and rising incomes have helped pave the way for a steady rise in Chinese soybean imports for the last couple of decades. Last year, China imported 57% of US soybeans, equating to a third of global shipments. Since the US import tariffs on US\$34bn of Chinese goods went into effect on 6 July 2018, China responded by imposing a 25% import tariff on US soybeans. The trade war has intensified after the Trump administration said it would impose 10% tariffs on an extra US\$200bn worth of Chinese imports. This tit-for-tat trade war has had a noticeable impact on the soybean market as importers and processors scramble to secure supplies for the next marketing year. Not only have soybean prices in the US declined 15% since the start of June this year, we have also seen the price gap between soybeans from US and those from Brazil widen to a five-year high equivalent to US\$70 per ton.

Figure 1: Latin American soybean prices trades at the premium to the US



Source: Bloomberg, WisdomTree, data available as of close 13 July 2018.

Historical performance is not an indication of future performance and any investments may go down in value.

China will have to pay a premium for diverging exports away from the US

The Chinese ministry of agriculture has lowered its forecast for soybean imports in the

2018/19 crop year (which begins on 1 October) by 2% compared with last month to 94 million tons. The director of China National Cereals, Oils and Foodstuffs Corporation (COFCO), the authority responsible for grain imports, said that China plans to import more soybeans from other countries in a bid to reduce its dependence on the US in response to the punitive tariffs by the US. Over the short term, China is likely to import more soybeans from Latin America. Considering the price gap, we previously alluded that this would be to the detriment of China as it would be buying soybean at a higher price. This would inflate the costs for farmers and potentially raise retail prices of foods, fuelling inflation. We still believe it is unlikely that China will be able to replace the entire amount of its US imports with other major exporters like Brazil and Argentina in such a short time frame. Added to that, even with Beijing's 25% imposed tariffs, US soybean prices are competitive in comparison to its Latin American counterparts, incentivising China to resume US soybean imports. Interestingly, the US soybean price advantage is helping drive exports outside of China which reached record territory in May and expectations remain high for June based on export inspections. Cumulative net sales in the US to countries outside of China since late March have reached 7mn tons, 50% ahead of last year's pace. In sharp contrast, cumulative net sales to China have declined in recent weeks as cancellations mount.

Tariff wars resonate through USDA's latest updates

Overnight (as on 12 July 2018), the US Department of Agriculture (USDA) also revised its previous (June) estimate of China's 2018/19 soybean import lower by 8mn tons to 95mn tons this month. Meanwhile US exports in the 2018/19 crop year were revised lower by 6.8mn tons, leading to higher US soybeans stocks at the end of the crop year by 5.3mn to 15.8mn tons. This is likely to exceed the previous record level from the 2006/07 crop year. This is in line with the Chinese Ministry of Agriculture's estimates. So far, China's imports are 10% lower for June. Unless a resolution is negotiated in the current trade disputes, we expect to see further pressure on US soybean prices.

Figure 2: World Soybean Supply and Use

| Item | 2017/18 | | 2018/19 | | |
|-------------------------|----------|---------------------|----------|---------------------|-----------------------|
| | Estimate | Change from June 12 | Forecast | Change from June 12 | Change from 2017/2018 |
| Beginning stocks | 96.7 | -0.7 | 96 | 3.5 | -0.6 |
| Production | 336.7 | 0 | 359.5 | 4.3 | 22.8 |
| Total Supply | 433.4 | -0.7 | 455.5 | 7.8 | 22.1 |
| Crush | 296.3 | -3.4 | 309.3 | -4.2 | 13 |
| Total use | 339.4 | -3.1 | 354.3 | -3.4 | 14.9 |
| Trade | 152.2 | 0.1 | 157.3 | -5.1 | 5.1 |
| Ending stocks | 96 | 3.5 | 98.3 | 11.2 | 2.2 |
| Addendum | | | | | |
| Beginning stocks | | | | | |
| Argentina plus Brazil | 61.9 | -0.8 | 54.4 | 1.7 | -7.6 |
| Imports | | | | | |
| China | 97 | - | 95 | -8 | -2 |

Source: World Agricultural Supply and Demand Estimates report comparison of July 12 report with June 12 report, WisdomTree, as of 12 July 2018.

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