PREFACE

The core business of this directorate is to do analysis on national level in order to produce agricultural economic information and advice for sound decision-making on the South African (SA) agricultural sector. To support this important task the Division Economic Research concentrates on economic analysis of performance of and external impact on the agricultural sector and its industries.

This publication developed from a need within the Department of Agriculture (DoA) to be regularly informed on developments and expected economic trends in the agricultural sector and the macro economic environment that impacts on its performance. This quarterly report has now been established as a new feature in the Directorate's work plan. From the end of 2006 this report will also published for outside consumption to add value to a number of existing regular economic publications on the agricultural sector. It is our vision to maintain it as indispensable reading for every serious student of the SA agricultural sector.

At this stage most of the content is based on sources inside the DoA. However, progress is being made to incorporate more external generated material.

Any new comments on the content of this quarterly report series are most welcome.

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CONTENTS

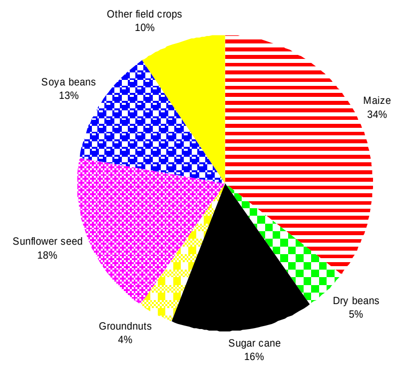
1. CONSUMER EXPENDITURE ON AGRICULTURE

Expenditure on secondary agricultural products by households recorded a quarter to quarter improvement of 5,7% to approach R4,5 billion in the second quarter (April - June 2006), from R 4,2 billion during the same period in the previous year. Availability of disposable income to local consumers and a relatively relaxed macro economic environment combined with high prices for red meat and maize, explains increased expenditure at retail level. The gradual sunset on the benign macro economic environment due to tightening **interest rates** will eventually restrain the 5% plus growth on agricultural expenditure by households, which has been prevalent during the past few years. However the effect of the tightening monetary stance will only be evident in 2007, as the festive season spending in the fourth quarter will result in higher growth on agricultural spending compared to the second quarter.

2. FARM INCOME

Income from field crops fell to 4,11 billion in the second quarter of 2006, a 21 % decrease from R 5,23 billion in the corresponding quarter of 2005.

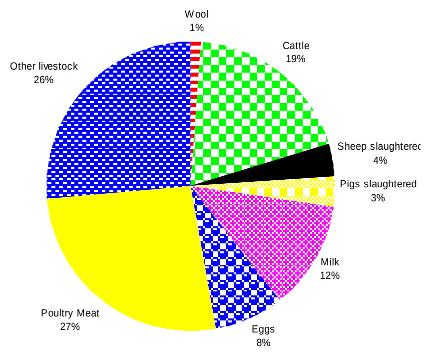
Figure 2.1: Revenue from field crops



Source: Agricultural Statistics 2006

Maize which is the largest component of field crops was the major contributor to the decline falling by 47% in 2006 from R 2,78 billion to R1,46 billion, in quarter two of 2005. The slide in field crops was minimized by 21% growth in sugar cane from R 0,53 billion in 2005 to R 0,64 billion in the second quarter of the subsequent year. **Horticultural** crops revenue grew by 5% in the second quarter of 2006 to R 6,28 billion from R 5,98 billion in the corresponding quarter of the previous year . While citrus fruits generated 1,8% less income of R 1,14 billion in quarter two of 2006, from R 1,16 billion in the previous year. Income from vegetables expanded to R 1,68 billion from R 1,48 billion in 2005, a 17% increase in the second quarter of 2006. Income from **animal** products advanced by a healthy 10% to R 8,86 billion in quarter two of 2006 from R 7,9 billion during the same period in 2005. Healthy growth in animal product's revenue was supported by a robust increase in beef prices, as revenue form cattle and calf slaughtered expanded by 26% to R 2,23 billion in 2006 quarter two from R 1,76 billion in the same quarter of 2005.

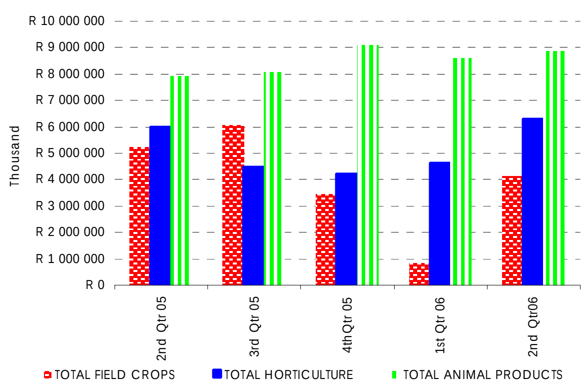
Figure 2.2: Revenue from animal products



Source: Agricultural Statistics 2006

Poultry products revenue also improved by 8% supporting an upward momentum in the revenue performance of animal products. Overall, gross income from agricultural products in the second quarter of 2006 rose by a negligible 0,7% compared to the previous year's second quarter. Despite the growth depicted by animals and horticulture products of 10,2% and 5% respectively. Field crops negatively affected the overall performance, with maize being the main culprit as it recorded a 47% slide in revenues.

Figure 2.3: Total Income from agri-products



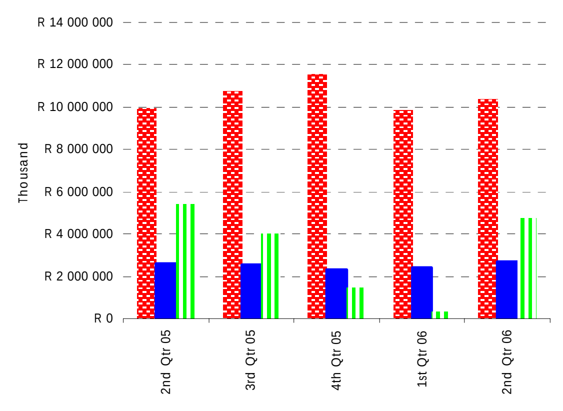
Source: Agricultural Statistics 2006

During the period under review, **net farm income** fell by 12% to R 4,75 billion from R 5,4 billion in 2005. The major contributing factor is the dramatic fall in maize revenue, which was partly influenced by poor price performance. Given that growth on other costs like interest paid, intermediate goods and services and labour were subdued. **Maize futures** are indicating an improved price performance towards the end of the year. Furthermore the price of wheat and sunflower is set for a rebound in the near future, as supply concerns are boosting prices. Given the overall contribution of the above crops to gross income, net farm income performance should improve in the coming quarters, provided that operating costs are contained.

3. AGRIC-INPUT EXPENDITURE

Expenditure on **intermediate** goods increased by 4% in the second quarter of 2006 to R 10,37 billion from R 9,93 billion in 2005.

Figure 3.1: Expenditure on Agricultural inputs



Source: Agricultural Statistics 2006

The equivalent growth trend is evident in **labour** costs as it advanced to R 2,67 billion in quarter two of 2006 from R 2,57 billion in the corresponding previous quarter. The cost performance of the above items is consistent with the benign inflation environment that was prevalent during the period under consideration. Quarter to quarter performance of **interest** paid by farmers rose marginally by 0,9% to R 1,04 in 2006 from R 1,03 million in the previous second quarter. The turning tide in the interest rate cycle explains the reluctance of farmers to commit on further debt financing, as loan servicing becomes more expensive. Falling **currency** might negatively affect cost control measures applied by farmers, increasing inflation on imported capital goods and a higher fuel bill.

4. PRICES

The **consumer** price index (CPI) for grain products increased by a modest 3,3 % to 133,9 in the second quarter of 2006 compared to 129,6 attained in the same quarter of the previous year (Stats SA). This modest rise reflects the inability of retailers to pass the higher maize prices to the consumers, given that the maize price increased dramatically during the period. CPI for **meat** advanced by 13,5 percent in the second quarter of 2006, buoyed by strong performance of red meat compared to the second quarter level of 141,4 in 2005. The **vegetables** price index at retail level increased by 5,8 % to 142,2 in quarter two of 2006 from 134,4 in the corresponding quarter of the previous year. The performance was in line with the prevailing inflation rate at the retail level. Inflation at retail level is expected to rise before the effects of rates hike begin to reverse the upward trend. **Producer** Price Index (PPI) for agricultural products leaped to 140,5 in the second quarter of 2006, an 18% surge from the corresponding quarter of 2005 which was 119. This advance signalled the strong inflationary pressures that are adversely affecting the economy at present. **Imported** inflation gained 5,8% from 120,1 in quarter two of 2005 to 127,1 in the current year's corresponding quarter. A relatively stronger rand during the period under review assisted in containing inflation at the producer level. High inflation environment is still expected on agricultural products as the weakening currency is expected to reverse the benefits provided the prevailing lower world oil price. However the expected tight monetary environment might curtail demand for some agricultural products thus reducing the sector's contributions to the overall inflation

5. SOUTH AFRICA AGRI-MARKET INDICATORS

TABLE 5: Domestic prices of selected crops per ton

	End Sept 2005	End Sept 2006
White Maize price	R 847	R 1 283
Yellow Maize price	R 772	R 1 276
Wheat price	R 1 421	R 1 803
Sunflower price	R 2 200	R 2 464

Source: Safex

After falling below the 1000/ton level in February, white **maize** prizes rebounded strongly, trading very close to R 1500/ton by July 2006, which was a two year high. The falling currency and perceived shortages in the domestic market were cited as the causes of the rally. However, as the news of excess stocks filtered to the market. The upward momentum of the price subsided with prices hovering around R 1100/ton towards the end of the third quarter, white maize price ranged between R 600 – R 850/ton as the strong currency and excess supplies depressed prices. Agricultural futures for white maize are pointing towards a price level of R 1200/ton in the first two quarters of 2007. However summer rainfall is improving prospects of a good crop and higher yield per hector next year. The **crop estimate** committee has raised its maize forecast this season to 6,28 tons as a result. Furthermore the US government assessment that this season's maize crop will be the second biggest ever can also weigh down on white maize prizes. The deteriorating currency and low production from SADC countries are only of the factors that can support the maize price locally going forward. At the beginning of July 2006 the yellow maize price was just above R1300/t and ranged between R1 200 – R1300/t for the rest of the second quarter of 2006. During the same period last year, the price was hovering between R600 – R800, the recovery was supported by the weaker rand and strong fundamentals. The support is expected to continue well into 2006/07 season. The bureau for food and agricultural policy (B.F.A.P) forecast and increase in yellow maize production which will be above the long term average levels. Furthermore it foresees a small reduction in maize demand for human consumption, while a slight increase in demand for animal feed is expected. Production levels in SADC countries will have a major influence in maize exports. **Sunflower** has been trading around R2 300 in the third quarter of 2006, compared to an average of R2 000/t that prevailed in the previous third quarter. An improvement which is in line with strong fundamentals of the oilseed markets globally. High world oil price are also contributing to the price resilience. The B.F.A.P expects an increase in area harvested in 2007. However the negative effects of higher output on prices is likely to be limited locally by currency effects.

6. WORLD AGRI-MARKET INDICATORS

TABLE 6: US prices of selected crops per ton

	End Sept 2005	End Sept 2006
Yellow Maize price	$105,40	$111,99
Soybean price	$266,48	$230,38
Wheat price	$131,54	$142,20

Source: Safex

The international **maize** price is set to strengthen, due to robust demand from the ethanol sector and reduced global output. According to the Food and Agricultural Organization of the United Nations (FAO), maize output is set to fall by 13 million tons, in addition to falling world stock inducing strong price performance in the near term, despite the US bumper crop. Globally **oilseeds** production is forecasted to expand due to a slowdown in soybean production, rising inventories may be negative for the international prices, with high oil prices providing cover against a downward movement in prices. Global supply of wheat is expected to be tight given reduced exports from Australia and Argentina, coupled with higher consumption in India. However, expected higher production from Canada might lessen the effect of shortages on prices. International prices for **wheat** are likely to remain firm in the medium term due to lower world stocks exacerbating the prevailing tight supplies situation. The FAO is predicting a 10 million ton decrease in production in the current year. Supply discipline by farmers will ensure that strong prices are sustainable. Given the global fundamentals which are mainly characterized by supply shortages and low inventories, robust prices can be maintained well into 2007. Revenue performance can be reasonably expected to outperform input cost escalations. This should be positive for farmer's net income in the near term.

7. MAIN EXTERNAL SOURCES CONSULTED

Business Report June - September 2006
www.busrep.co.za

Bureau for Food and Agricultural Policy, South African Agricultural Outlook, BFAP Baseline June 2006

United States Department of Agriculture, World Agricultural Supply and Demand Estimates, 12 October 2006.
www.usda.gov/oce/commodity/wasde/latest

Food and agricultural organization of the United Nations
www.fao.org

8. ACKNOWLEDGEMENT OF INTERNAL (DOA) CONTRIBUTORS

Directorate: Agricultural Statistics: Livestock numbers and Crop Production and Estimates