

Global Vegetable Oil Price Outlook 2010-2011

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Ladies and Gentlemen,

I am delighted to speak once again at this Globoil India conference organised by my friend Mr Kailash Singh and his organisation **TEFLAS** in conjunction with our industry body **The Solvent Extractors Association of India**. SEA has done a sterling job for our industry over the years and its dynamic President Ashok Sethia and its even more dynamic Executive Director Dr Bharat Mehta deserve kudos. They are fortunate to have a large number of very distinguished past presidents and elders who support them and help them at all times.

I can also say that the MOU signed by SEA with PORAM is a landmark achievement. The plan to hold a joint training programme in Contracts & Dispute Resolution is a step in the right direction and will bring great benefit to the trading companies of both countries. **SEA has shown once again that in terms of worldwide perspective, service to the industry and global representation it is the first and only organisation of its kind in India.**

Without much ado I shall go straight to the topic – the performance of our markets and the outlook for the next several months.

From a personal point of view, I could not have asked for a better year. I have been saying all these months that we are going to see a problem in CPO production in 2010 and that prices are going to move higher. So far it looks like all 3 of our predictions for 2010 are coming true. CPO production is a problem, the biological cycle of the Oil Palm is working almost exactly as I had predicted and the U S Dollar began to fall almost from the day I had forecast. What is more, these bullish forecasts have been realised in the midst of great economic uncertainty and rather weak outside markets.

INDIA

The size of individual oilseed crops in India is no longer relevant from a world standpoint. This is true, howsoever sad it may be. On the other hand, the marketing of the Indian crop is relevant and year after year, we are seeing that the crop comes to market later than expected. Farmers are getting cleverer and their price expectations are getting higher. Oilseed Minimum Support Prices are too low. We have the peculiar situation that our MSP for soybean translates to a price of US\$ 8.40 per bushel, about 25 percent below the current world price. If we are to take a price of US\$ 11.50 per bushel it would translate to about INR 20,000 per tonne and I believe that would be a fair price for farmers this year. My guess is that farmers will only bring the soybean crop to market if and when prices are Twenty Thousand Rupees per tonne or higher.

Indian import forecast

If you recall I have been projecting India's total vegetable oil imports for the Indian oil year November 2009 to October 2010 at 9 million tonnes. This figure was disputed by a number of Indian experts. I am very pleased that my forecast has proved to be fairly accurate once again. The Indian growth story goes from strength to strength and vegetable oil consumption has been strong.

Many Indian experts have raised alarmist voices about stock levels in India. Let me say again that it is the hallmark of a developed economy that stocks are held. It is a sign of a frugal subsistence economy if very low stocks are held. Some of my distinguished friends are clearly living in the past and have yet to wake up to the new resurgent and prosperous India. As the economy becomes more prosperous and as the total market expands, stocks will also need rise and higher stocks are not a cause for bearishness. At the same time, may I make a fervent plea to the Indian Government to refrain from imposing stock limits on traders. The market is now sufficiently developed to do its job. Similarly the government must be congratulated on desisting from placing any fetters on the export of oilseed extractions. Let us also hope that futures markets will be allowed to be developed without fetters and next time prices rise, we shall not have any ban on futures markets.

For the next oil year Nov 2010 to Oct 2011 Indian vegetable oil imports will expand further to between 9.3 and 9.5 million tonnes. Production of oilseeds will recover somewhat but as I have said previously, Indian production is now largely irrelevant and will constitute a smaller and smaller proportion of consumption with each passing year. China has gone this way and India is simply following a well trodden path. It is too early to say what oils India will import next year but clearly imports of sun oil will decline due to high prices. Higher soya oil tonnages will depend on the price relationship with palm. Also, do bear in mind these estimates are tentative because Rapeseed has not even been planted.

My estimate of the break- up of vegetable oil imports for 2010-11 is:

Sunflower oil	400,000 mt	Soybean oil	1,500,000 mt
Lauric oils	200,000 mt	Palm oils	7,200,000 mt

Let me now cover the developments so far this year since my paper at the Palm Oil Price Outlook Conference (POC) in Kuala Lumpur on 9 March 2010.

Market Developments so far

Many of you will recall that as early as 4 December 2009 at the Gapki conference in Bali, I sounded the alarm on prospects for CPO production in 2010. I explained this more fully in my POC paper in March this year and forecast that for the first time in history, we shall see two consecutive years of production decline in Malaysia. My estimate of 9 March was for Malaysia to produce only about 17.2 million tonnes of CPO as compared with 17.556 mln mt in 2009 and 17.727 million tonnes in 2008.

I had further stated that Indonesian CPO production will rise only on account of expansion of mature acreage and that production will rise at best by 1million tonnes in 2010.

Since then, the outcome of CPO production in Indonesia has been worse than expected whilst Malaysia has performed more or less in line with my expectations. Recently, the uptick in August CPO production in Malaysia has raised some questions as to whether a general recovery in production has already started. My answer is that CPO production during and around the Ramzan period is always choppy and cannot be extrapolated. We shall have to wait until October to judge how production in Malaysia is performing. In August, as we all know, Peninsular Malaysia performed flat whilst Sabah gave us a very healthy increase of almost 14 percent.

At the same time I would like to add that estimating CPO production one year in advance is not an easy task and my figure of 17.2 million tonnes could be within the margin of error. The important point is that my model has over the years been one of the most accurate, more accurate than either MPOB or the Malaysian government and this year too it has delivered the correct trend.

Indonesian CPO production has disappointed and there is a greater consensus now that growth will be just 500,000 tonnes for 2010. Hence overall, for 2010, there will be very little or no growth in CPO production.

Other Developments on Supply Side

Firstly we all are aware of the cruel and unfortunate drought in Russia and in parts of the Ukraine. That drought is still not over and its repercussions will stretch well beyond this harvest and into the next growing season. The shortfall in wheat and in barley has directly led to greater demand for corn as a feeding stuff and led to a major bull market in corn prices.

Secondly we have had very peculiar weather in Canada this year. First we had a very wet spell at planting time and recently when the crop required warm dry weather, we have run into wet weather and killer frosts. This has reduced the estimates for canola as well as for wheat.

We also have uncertain weather in parts of China with possibility of frosts. **All Chinese oilseed estimates for 2010-11 are lower than their crops for 2009-10.**

And on top of all this we have a strong La Nina which is affecting rainfall in Brazil, in Paraguay and in Argentina. This year the transition from El Nino to La Nina has been one of the most rapid in history and we are experiencing a prolonged spell of uncertain weather. It is too early to say how the dry weather in Brazil and Argentina will shape and how much it will affect crops. It will be alarmist to speculate on that but this area needs to be very closely monitored.

Demand scenario

Despite a weak scenario in most of the developed world, vegetable oil consumption has held up and expanded remarkably well. This is due to the expansion of bio diesel mandates in several countries and to growth in population and in per capita consumption in the developing world. The fast growth seen in China, India and in most of the developing world has meant that at least 3 billion people are eating better and living better. This has kept growth in food demand at a steady 4 million tonnes during the past year.

Incremental S&Ds

For the purpose of this conference, I have reverted to preparing World Incremental S&Ds on the basis of the normal oilseed crop year which is October to September. Hence these figures will differ from some of my earlier papers where I discussed the year April –March.

For the oil year October to September 2009-10, palm oil production expanded overall by about 1.3 million tonnes over the previous year. Most of this growth came in the period October to December 2009.

The biggest growth was in the case of soya oil primarily on account of the record harvests and the record crush in South America. Soya oil availability in 2009-10 expanded by almost 2.2 million tonnes over 2008-09.

Rapeseed oil availability also expanded by about 1.3 million tonnes primarily because we had better crops in the EU and we carried forward bigger tonnages of rapeseed which were crushed in the year 2009-10.

The supply of lauric oils also expanded but as in the case of palm, most of the increase took place in the early part of the year. Groundnut oil and cotton oil supply declined.

Sunflower oil availability declined by about 300,000 tonnes from the previous year. This decline was much smaller than I had anticipated earlier. The better availability of sun oil led to bigger than expected imports of sun oil by India.

So we are ending the oil year Oct-Sept 2009-10 with the following Incremental S&Ds

000 tonnes	Oct 09 to Sept 10
Soya oil	+ 2,200
Rape oil	+ 1,300
Sun oil	300
Gn oil	200
Cotton oil	200
Palm oil	+ 1,300
Lauric oils	+ 500
Total Increase	+ 4,600
Demand	+ 6,000

As a result, in the current year which is just going to end, we have seen steadily rising prices and this price rise is being accentuated as we complete the year by drawing down world stocks.

What about the shape of things to come in 2010-2011?

In the case of the most important oil, Palm oil, we must hope and expect that the biological Low Cycle will come to an end around June 2011. A new higher Cycle should coincide with the beneficial after-effects of good rainfall in 2010. Therefore, we must be cautiously optimistic about Palm oil production for the next oil year. **At this stage, I expect combined production in Malaysia and Indonesia in 2010-2011 to expand by about 2.5 million tonnes.**

There is a question mark on the production of soybeans in South America but we shall carry forward ample stocks of beans into the next year. We are also optimistic about the forthcoming crop in North America. We must presume that China will continue its policy of importing beans as against oil and that the crush in China will continue to expand. After the strong increase in worldwide crush of almost 13 million tonnes in the current year, I am anticipating a further increase in crush of 12 million tonnes next year. **That would mean an increase in soya oil supply of about 2.1 million tonnes.**

I expect the Rapeseed crush to drop due to limited and lower availability of rapeseed and the reduction in rapeseed carry forward. **I expect Rapeseed oil production to be lower by 1 million tonnes and possibly by 1.2 million tonnes.**

Sun seed availability for next year will also be lower. **I expect sun oil supply to be lower by at least 300,000 tonnes next year.** This will come on top of a reduction of 300,000 tonnes in the current year. I expect the supply of **cottonseed oil and groundnut oil to be up a combined 0.5 million tonnes.** Coconut oil supply is expected to decline but palm kernel oil will make up for that. **Overall lauric oil supply will NOT expand.**

What about expansion of Demand? We must remember that we are entering 2010-11 with prices at a high level and likely to go higher. These high prices will affect consumption and demand in price sensitive markets. Therefore, I am forecasting food demand to grow by only 3 million tonnes and bio diesel demand to grow by just 1.5 million tonnes. Overall demand will grow by less than normal, by about 4.5 million tonnes.

Now we can see the developing Incremental S&Ds for next year

000 tonnes	Oct 10 to Sept 11
Soya oil	+ 2,100
Rape oil	1,000
Sun oil	300
Gn oil & Cotton oil	+ 500
Palm oil	+ 2,500
Lauric oils	-----
Total Increase	+ 3,800
Demand	+ 4,500

There is one caveat here. If the bio diesel subsidy is restored in USA or if RFS2 is implemented with retrospective effect, bio diesel demand will grow by 2 million tonnes and will be very bullish for U S soybean oil.

At present, it looks like for the third year in a row, Incremental Supply will not match Incremental Demand. There are 2 interesting possibilities. Higher prices and a return of good weather can lead to big production increases for Sun seed and Rapeseed in Ukraine and Russia in 2011. Secondly it may be that palm oil production can rise more than I have expected. It is too early to forecast S&Ds for 2010-11 accurately. There is potential for Supply to exceed Demand but not by much – **prices cannot fall much and oilseeds will need to fight for acres against other crops by means of price competitiveness.**

Normally, we have seen in history that every El Nino- inspired bull market has been followed by a very cruel bear market. This year is different. The El Nino has been followed almost immediately by a La Nina. So whilst palm production may recover, we shall encounter lower production of Soybeans and Sun seed in South America. Overall oilseed and oil production will not a chance to recover strongly.

PRICE OUTLOOK

The general economic outlook remains uncertain for 2011 in the developed world and strong in the developing world. Interest rates are likely to remain low for an extended period of time and the US Dollar is also likely to remain soft. The EU will continue to support its weaker members and the Dollar will remain weak against the Euro. Currencies of China, India and the developing countries should keep gaining against the Dollar. Based on this analysis, my outlook for vegetable oil prices for 2010-2011 is as follows:

PALM – I expect prices to remain Sideways with a lower bias for the next 4 to 6 weeks. Due to the peculiarity of the Indonesian Export duty, producers will wish to export as much as possible out of Indonesia this month and in October. The market makes its prices based on more transparent Malaysian statistics. Besides, October will also see a strong recovery in CPO production which will spill over into November. Malaysian month-end stocks will rise and prices will need to go lower. Between now and the end of October, we could lose about 150 to 200 ringgits in price. After that weak spell, prices should begin to recover as exports remain strong, harvest pressure in destinations like India and China subsidies and pipelines are re-filled. My forecast is that we shall reach my target of 3000 to 3200 Ringgits by January 2011, well before we meet in Kuala Lumpur for the next Price Outlook Conference.

Soybean oil - We must realise that there are political moves afoot in Argentina by parliamentarians aligned to the farmers lobby to reduce export taxes on soybeans and soy products as from 1st January 2011. Therefore there is a lack of farmer selling at present and this factor will keep premiums very strong. I also presume China will continue to favour Brazilian and US origin soya oil in preference to Argentina. We in India will continue to buy Argentinian soya oil. My forecast is that soya oil will also move sideways to slightly lower for the next 4 to 6 weeks but the drop will be marginal and the gap between soya oil and palm oil will widen considerably. In December I expect soya oil prices also to race ahead and by January to reach my target of USD 1050 FOB Argentina.

Events in Russia and Ukraine and anticipated problems in Argentina have fuelled a powerful bullish momentum in sunflower oil prices. I believe Sunflower oil will exceed my earlier forecast of US\$ 1200 FOB.

I expect Rapeseed oil prices also to climb closer to US\$ 1200 in the first quarter of 2011.

Finally, I have to reiterate that lauric oils will enjoy the most bullish outlook. Coconut oil prices have already run up to US\$ 1250 FOB. I expect them to continue to rise beyond US\$ 1300 CIF Rotterdam so that they can ration demand.

Many of you will find my price forecasts a repetition of what I have been predicting for several months. When you are proved right, you do not need to change your forecast!

What can spoil the party for vegetable oil prices?

The greatest threat to vegetable oil prices comes from Outside Markets. If Equities tank, for any reason, then all commodity prices will also fall and will take vegetable oil and oilseed down as well. The world economy is growing once again but that growth is very lop sided with the developed world still not out of the woods. Contagion is the biggest threat to our markets. There is also a threat crude oil prices may fall or that the US Dollar gets stronger.

Conclusion

We are in the midst of a developing La Nina phenomenon. That factor will give us some very interesting developments on the weather front. I believe the Indian crushing industry will have a much better year in 2011 because of better local oilseed production and higher meal prices. Prospects for farmers and for plantations all over the world have never been better. They must use these good times to switch to sustainable practices and embrace the Round Table on Sustainable Palm oil.

My next paper will be on 7 November 2010 in Guangzhou at the 5th China International Oils Conference hosted jointly by the Dalian Commodity Exchange and Bursa Malaysia

Good Luck and God Bless