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Brazil

Grain and Feed

Wheat Update

2005

Approved by:

William Westman, Agricultural Counselor
U.S. Embassy

Prepared by:

Oliver Flake, Agricultural Attaché

Report Highlights:

Post forecasts 2005/06 production at 5.0 million tons on 2.3 million hectares and imports are forecast at 5.2 million tons for the trade year. Forecast imports for 2004/05 remain unchanged at 5.0 million tons with Argentina supplying the vast majority. Brazilian prices have recovered somewhat over the past few months but changes regarding domestic taxes on wheat and wheat flour are likely to depress consumer prices in the top producing states of Parana and Rio Grande do Sul.

Includes PSD Changes: Yes
Includes Trade Matrix: No
Unscheduled Report
Brasilia [BR1]
[BR]

Brazil							
Wheat							
	2003	Revised	2004	Estimate	2005	Forecast	UOM
	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]	
Market Year Begin		10/2003		10/2004		10/2005	MM/YYYY
Area Harvested	2464	2464	2756	2756	2500	2300	(1000 HA)
Beginning Stocks	656	886	508	701	1379	1321	(1000 MT)
Production	5851	5851	6021	5845	5000	5000	(1000 MT)
TOTAL Mkt. Yr. Imports	5179	5339	5000	5000	5200	5200	(1000 MT)
Jul-Jun Imports	5559	5558	5000	5000	5500	5500	(1000 MT)
Jul-Jun Import U.S.	369	369	0	50	0	150	(1000 MT)
TOTAL SUPPLY	11686	12076	11529	11546	11579	11521	(1000 MT)
TOTAL Mkt. Yr. Exports	1378	1375	50	25	50	50	(1000 MT)
Jul-Jun Exports	1378	1375	50	25	50	50	(1000 MT)
Feed Dom. Consumption	200	200	300	300	200	200	(1000 MT)
TOTAL Dom. Consumption	9800	10000	10100	10200	10200	10400	(1000 MT)
Ending Stocks	508	701	1379	1321	1329	1071	(1000 MT)
TOTAL DISTRIBUTION	11686	12076	11529	11546	11579	11521	(1000 MT)

Production

Large wheat crops in 2003 and 2004 reduced import need significantly with Brazil supplying over 50 percent of consumption needs. This coming year production should supply nearly 50 percent of demand (see table below) with Post forecast production for 2005/06 at 5.0 million tons on 2.3 hectares. Meanwhile, Brazilian government forecasts by both IBGE and CONAB are for 5.7 million tons of production. Posts forecast production is below the government forecasts due to lower expected planted area in Rio Grande do Sul (RS). Some Post contacts suggest that area could be as much as 30 percent less than last year due to adverse planting weather and poor price prospects. Pasture or alternative cover crops should replace wheat in some parts of the state. Post also forecasts yields down from last year since much of the wheat in RS and Parana was planted late, thereby increasing the risk of frost and being subject to reduced daylight hours. Furthermore, it is expected that producers will cutback on fertilizer use due to its high costs and low prices for the soybean harvest. Fertilizer sales are reportedly 20 to 30 percent behind the pace of last year. Production financing is also a major challenge and many producers are laden with heavy debt from last year and interest rates that have been on the rise for the past six months.

Production as a Percentage of Total Supply			
	Production	Imports (Marketing Year)	% Production/Total Supply
1999	2,403	7,698	23
2000	1,666	7,201	19
2001	3,250	7,007	32
2002	2,925	6,727	30
2003	5,851	5,179	53
2004	6,021	5,000	55
2005*	5,000	5,200	49

*Post Forecast

Post expects a slight retraction in planted area in the center-west as area shifts to dry beans due to high prices, particularly in Goias. Additionally, planted area in the South, where the vast majority of wheat is grown, is not expected to be greater than last year. Nevertheless, planted area in Parana is expected to be greater than the previous Post forecast. This is primarily due to a recovery in wheat prices and dry soil conditions that forced producers to plant wheat instead of winter corn. Wheat prices reached a low in December at R\$46 per ton below the government set minimum price to just R\$354 per ton. Since then, prices have been on the rise but may fall again over the next few months due to strong Argentine imports and changes to domestic taxes on wheat and wheat flour.

2004/05 Parana Wheat Prices												
R\$ Per Ton Wholesale												
	June 04	July	Aug	Sept	Oct	Nov	Dec	Jan 05	Feb	Mar	Apr	May
Parana Price	572	507	446	412	381	378	354	374	353	394	450	416
Parana Price less Gov. price (\$400)	+172	+107	+46	+12	-19	-22	-46	-26	-47	-6	+50	+16

Source: Wholesale prices from Deral

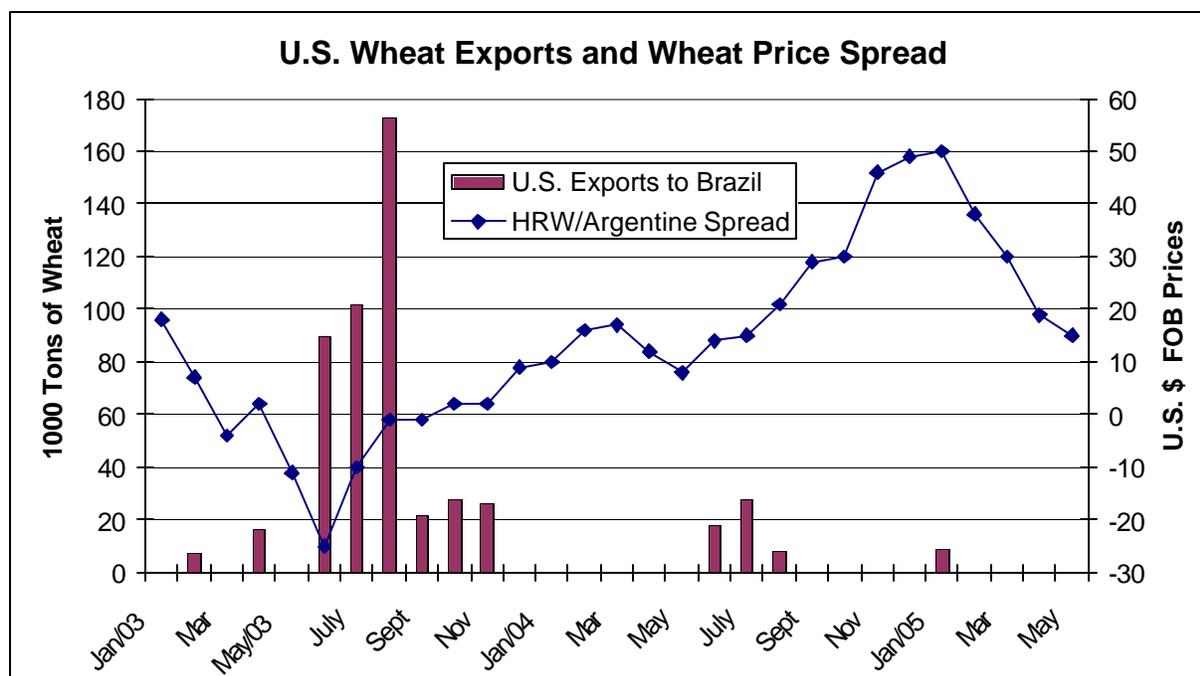
*Post forecast

Trade

Argentine wheat is currently arriving at the port of Santos, near Sao Paulo, at R\$420 per ton. To compete, producers in Rio Grande do Sul (RS) would have to sell at R\$370 per ton given high transportation costs. However, producers in the state are unwilling to sell at such low prices and therefore are restricted to selling to nearby markets such as Curitiba. Wheat growers are likely to face falling prices over the next several months with the recent elimination of the ICMS tax in Sao Paulo state on wheat flour and imported wheat. It is estimated that over one million tons of flour were shipped into the state of Sao Paulo from southern Brazil last year. Therefore, millers in Sao Paulo, who's mills run at only 40 percent capacity, successfully lobbied the state government to remove the 12 percent ICMS tax on wheat flour produced in Sao Paulo and sold within the state. With Sao Paulo flour now 12 percent cheaper, mills in the south will face more intense competition.

The elimination of the tax also applies to imported wheat. Therefore, Argentine, and potentially U.S. supplies, will arrive at mills priced 12 percent lower, thereby forcing sellers in Parana and RS to drop the price of their wheat to remain competitive in Sao Paulo. As stated above, many cooperatives in Parana and RS are unwilling to sell at prices sufficiently low to compete with Argentine supplies. Therefore, it is expected that the pace of Argentine purchases will continue steady over the next few months.

Though Argentine prices have risen over the past few months, as seen in the chart below, with the falling HRW/Argentine spread some contacts believe that remaining exportable supplies are quite large. This is primarily due to some early season Argentine sales to importing countries with the option to change destination. As Argentine prices have risen, these buyers have opted for cheaper supplies. Therefore, Post believes that actual Argentine exports will fall short of reported sales, thereby freeing up more supplies from Brazil. Given the current and expected pace of Argentine shipments to Brazil, Post has increased the July/June import forecast to 5.0 million tons, which is 200,000 tons above the previous forecast.



The chart above illustrates that U.S. Hard Red Winter wheat (HRW) is competitive into Brazil, primarily the Northeast, at around U.S. \$10 per ton over Argentine supplies and significant imports of U.S. wheat occur when U.S. prices are even or slightly below the price of Argentine wheat. This is primarily because U.S. supplies of HRW and Soft Red Winter (SRW) are considered higher quality and preferred by Northeastern millers. Though the HRW/Argentine spread has narrowed over the past several months, U.S. wheat is still uncompetitive at an \$18 premium. U.S. wheat also faces a 10 percent tax applicable to all wheat from non-Mercosul suppliers, so the actual U.S. premium is greater than \$30 per ton. Nevertheless, Argentine exportable supply, though larger than some currently estimate, is diminishing and prices are expected to increase minimally before harvest in December. Meanwhile, the price of HRW is expected to fall over the next several months due to a large forecast harvest, increased export competition, and rising stocks. In fact, the average producer price for U.S. wheat is forecast down \$22 per ton from last year. This combination of falling U.S. prices and steady to increasing Argentine prices should narrow the price spread and thus there is a possibility of limited (up to 50,000 tons) imports of U.S. wheat by Brazil before the Brazilian harvest in October and November. Contacts suggest that up to 25,000 tons of SRW have already been purchased for June or July delivery.

U.S. wheat benefits in the Northeast of Brazil from a slight freight advantage over Argentine supplies and exemption from the Merchant Marine tax. However, U.S. wheat faces the Common External Tariff of 10.0 percent as well as competition from wheat supplies from Southern Brazil that receive a transportation subsidy to the Northeast. Under this subsidy program known as "Market the Harvest" (PEP, in Portuguese), the government subsidizes the freight cost from Southern Brazil to the Northeast in an attempt to encourage northeastern mills to buy more Brazilian supplies from southern production states. Under the PEP, a Northeastern miller that buys wheat from the south receives a set premium to compensate for transportation. In theory, this premium should be the difference between the government set minimum price in the south and the price of imported wheat to the Northeast. Though much attention lately has been focused on U.S. domestic support, little attention is paid to this highly protectionist subsidy.