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China Lowers Wheat Minimum Support Prices Again

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Report Highlights:
On November 16, 2018, China's National Development and Reform Commission (NDRC) announced that it will lower its 2019 Minimum Support Price (MSP) for procurement purchases of domestic wheat under its temporary reserve program for the second consecutive year. In 2019, the wheat (3rd class) MSP price will be $325 per ton (RMB 2,240), down $8.70 (RMB 60) from 2018. The lower MSP will have a limited impact on marketing year (MY) MY2019/20 (July-June) planting intentions, because Chinese farmers completed winter wheat planting in mid-November 2018.

Overview

On an annual basis, China publishes a “Notice Announcing the Wheat Minimum Purchase Price.” The MSP is available to farmers when market prices drop below the applied administered price. The MSP is provided to farmers in major producing provinces during the period immediately following harvest. By guaranteeing farmers an established price for their commodities, China’s MSP program ensures that commodity prices in the relevant provinces are maintained at the Chinese government’s chosen support level as an effective “price floor.”

On November 16, 2018, China’s NDRC announced that it will lower the 2019 Minimum Support Price (MSP) for its temporary reserve procurement program for domestic wheat. Announcement Link: http://www.ndrc.gov.cn/gzdt/201811/t20181116_919827.html

The NDRC announcement states that, subject to State Council approval, the 2019 MSP for wheat (3rd class) will be lowered to $325 per ton (2240 RMB), down $8.70 per ton (60 RMB) from 2018. The 2019 MSP policy announcement was nearly one month later than last year.

Over the past two years, China’s NDRC has undertaken a campaign to bring domestic prices more in line with the international market prices. In 2017, the NDRC lowered the wheat MSP for the first time since the policy was launched in 2006. By lowering the floor price, and lowering auction reserve prices for wheat, NDRC has reduced the policy support which served as a floor for prices of standard wheat (Grade 3). See GAIN report CH 18003 for more information.

China’s leadership intends to restructure the wheat market by liquidating China’s massive state-owned stockpiles in its temporary reserve program. The temporary reserve program has resulted in China’s government-owned inventories accounting for more than half of global wheat stocks.

Outlook

Short-term Impact Insignificant

Industry sources report that the lower MSP will have a limited impact on marketing of the current year wheat crop in MY2018/19, and prices and planting intentions in MY2019/20. Winter wheat planting across the North China Plain was completed in mid-November 2018.

Based on estimates from the Chinese Academy of Agricultural Science, the revision in the MSP policy is insignificant at the farm-level. According to analysis from China’s National Grain and Oilseeds Information Center, high prevailing market prices in MY2019/20, diminish the market impact of a lower “price floor.” Many growers in major wheat producing regions still favor the higher comparative margins for wheat in comparison to other crops.

In a lower market price environment, industry sources report that due to the risk of soil erosion, leaving the land fallow in the North China Plain is not an option. Wheat growers in major producing regions will lower their investment into seed or fertilizer, according to lower MSP levels, diminishing yield potential. Wheat growers in non-major producing regions may turn to other economic crops.

Long-term Impact Significant

In the long term, a downward revision in the MSP will diminish the influence of the temporary reserve program on domestic wheat prices, shifting Chinese domestic wheat pricing and marketing prospects more in line with global benchmark prices.

Winter wheat accounts for 95 percent of overall Chinese wheat production. However, due to the “price floor” defined by the MSP, most growers were not incentivized to plant the high quality wheat varieties that are in demand for industrial milling and baking applications. As a result, China’s domestic wheat supply does not match market demand, and the lack of correlation between domestic and global prices clearly reflects the situation. Lowering the MSP price signals a clear direction for policy changes to begin shifting towards the liquidation of China’s globally significant wheat inventories.

Other Reforms to China’s Temporary Reserve Programs

In addition to lowering the MSP, the Chinese government is undertaking other measures to reform wheat procurement and storage for its temporary reserve program.

In 2018, China implemented a pilot program to expand government-administered wheat procurement in Xinjiang. The pilot program replaces the existing model in which commodity prices are set according to central government authority, then managed and administered entirely through government programs. The pilot program adopts a new model which allows for market price discovery, competition, and quality premiums for procurement, which are then supported by emergency interventions through a government safety net program.

The Xinjiang Administration of Grain and Reserve reported that starting from June 20, 2018 until November 30, 2018. The pilot program raised procurement prices in comparison to 2017 over the same period. Provincial authorities also reported that wheat growers responded to quality premiums, resulting in overall higher farm income. They also attributed higher prices to strong competition among traders and wheat mills.