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Date: 1/22/2014
GAIN Report Number:

South Africa - Republic of

Post: Pretoria

Food Price Inflation Update

Report Categories:
Agriculture in the Economy

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Report Highlights:
South Africa's agro-food system functions in a relatively free market environment and accordingly supply and demand forces set prices. South Africa's food price inflation came down steadily in 2012 and 2013 to reach its lowest point the past three years of 3.5 percent in December 2013. However, food price inflation is expected to increase coming months due to a sharp increase to record levels of local corn prices on the anticipation of possible corn imports, the drought conditions prevailing in the Northwest province, a 20 percent depreciation of the rand against the United States dollar to a five-year low, and increased import tariffs e.g. poultry products.

INTRODUCTION

The Marketing of Agricultural Products Act of 1996, paved the way for a new marketing order in the South Africa agri-food sector, after years of controlled price setting. Food producers, traders and processors are now trading in a free market and accordingly may sell or buy products locally or internationally in response to supply and demand forces that set prices. For highly perishable products that are difficult to trade internationally such as fresh vegetables, prices are determined by local supply and demand conditions. For the major commodities including corn, wheat and oilseeds, however, prices are determined by local and international supply and demand conditions, as well as, the exchange rate.

The result is that the local price for key commodities always fluctuates between import parity and export parity, effectively upper and lower price limits. The actual level of the local price will depend on local supply and demand. For example, if there is a local shortage due to a drought, prices will move closer to import parity. If there is excess local supply domestic prices will fall, but no lower than export parity. In the liberalized agri-food market of South Africa, the domestic prices of food commodities reacts predictably to changes in the exchange rate, international prices and to market perceptions of the relative local scarcity of commodities.

The major food commodities consumed in South Africa are corn, wheat, oilseeds, dairy and meat. Annually, South Africa consumes about 4.5 million tons of white corn (human consumption), 4.5 million tons of yellow corn (animal consumption), 3.5 million tons of wheat, 2.6 million tons of oilseeds, 2.3 million tons of dairy, 1.8 million tons of white meat, 1.3 million tons of red meat and 1 million tons of rice.

THE CURRENT FOOD PRICE INFLATION SITUATION

According to Statssa, South Africa's official food price inflation rate (year-on-year) in November 2013 was 3.7 percent, while the headline inflation rate [Consumer Price Index (CPI)] was 5.3 percent. The December 2013 inflation rates will be released on January 22, 2014. After reaching highs of 8.6 percent in 2009, headline inflation gradually moved into the target band of between 3 and 6 percent and has stayed there for most of the past four years (see also Figure 1). The Reserve Bank of South Africa has the mandate to keep the headline inflation rate between 3 and 6 percent. Food inflation came down from a high of 16.1 percent in January 2009, after the global food price scare, to stay below 8 percent for most of 2010 and 2011. However, by the end of 2011, food inflation increased to 11.6 percent on higher meat, oilseeds, sugar and vegetable prices, but came down steadily in 2012 and 2013 to reach its lowest point the past 33 months of 3.7 percent in November 2013. Table 1 indicates the annual average trend in headline and food inflation in South Africa since 2009, while Figure 1 illustrates the monthly values.

Table 1: The annual average rate in headline and food inflation in South Africa since 2009

	2009	2010	2011	2012	2013
Headline inflation (CPI)	7.1	4.3	5.0	5.6	5.8
Food inflation	9.4	0.8	7.3	7.4	5.9

Source: Statssa

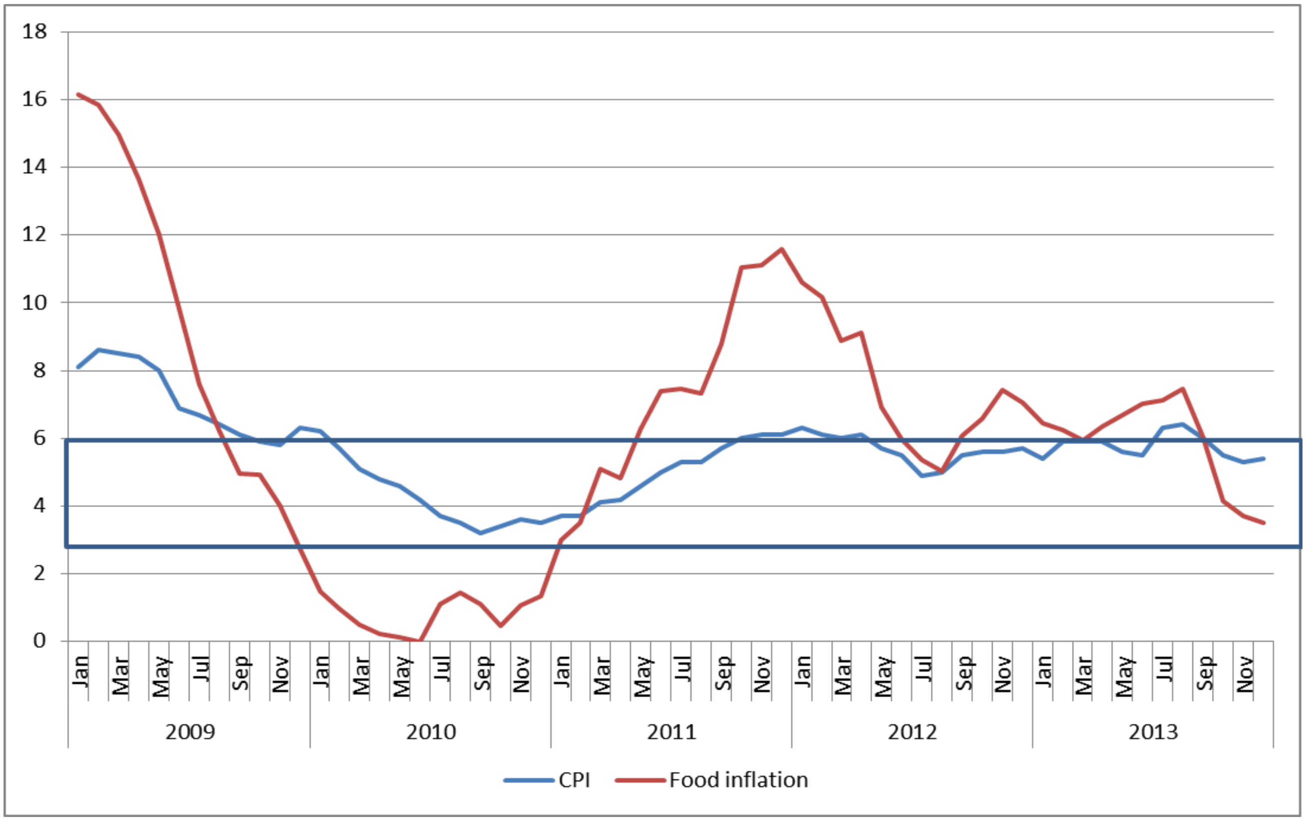

Figure 1: The monthly rate of headline and food inflation in South Africa since 2009

Table 2 illustrates the inflation rates of the specific food categories from July 2013 to December 2013. From the table it is clear that all food categories, except milk, eggs and cheese, recorded decreasing trends in inflation the past six months.

Table 2: The inflation rates of specific food categories from July 2013 to December 2013

	July, 2013	**August, 2013**	**September, 2013**	**October, 2013**	**November, 2013**	**December, 2013**
Food inflation	7.1	7.4	6.0	4.2	3.7	3.5
Bread and cereals	7.3	8.6	8.2	5.8	4.3	4.3
Meat	5.8	5.0	1.1	0.0	0.2	0.1
Fish	5.8	7.5	6.7	5.9	5.3	5.3
Milk, eggs and cheese	6.7	7.2	8.0	7.8	7.8	7.3
Oils and fats	3.5	4.4	5.3	4.2	3.9	3.1
Fruit	4.6	4.5	8.2	2.3	1.7	0.4
Vegetables	13.3	13.4	12.1	5.5	4.9	5.3
Sugar	5.9	7.9	6.6	6.0	6.2	5.8

Other food	6.8	6.2	5.3	5.7	5.7	5.6

Source: Statssa

Figure 2 illustrates the inflation rates of specific food categories from January 2009 to December 2013. After reaching picks in 2009 and again in 2011, the inflation rates of most categories of food stabilized below 10 percent since 2012.

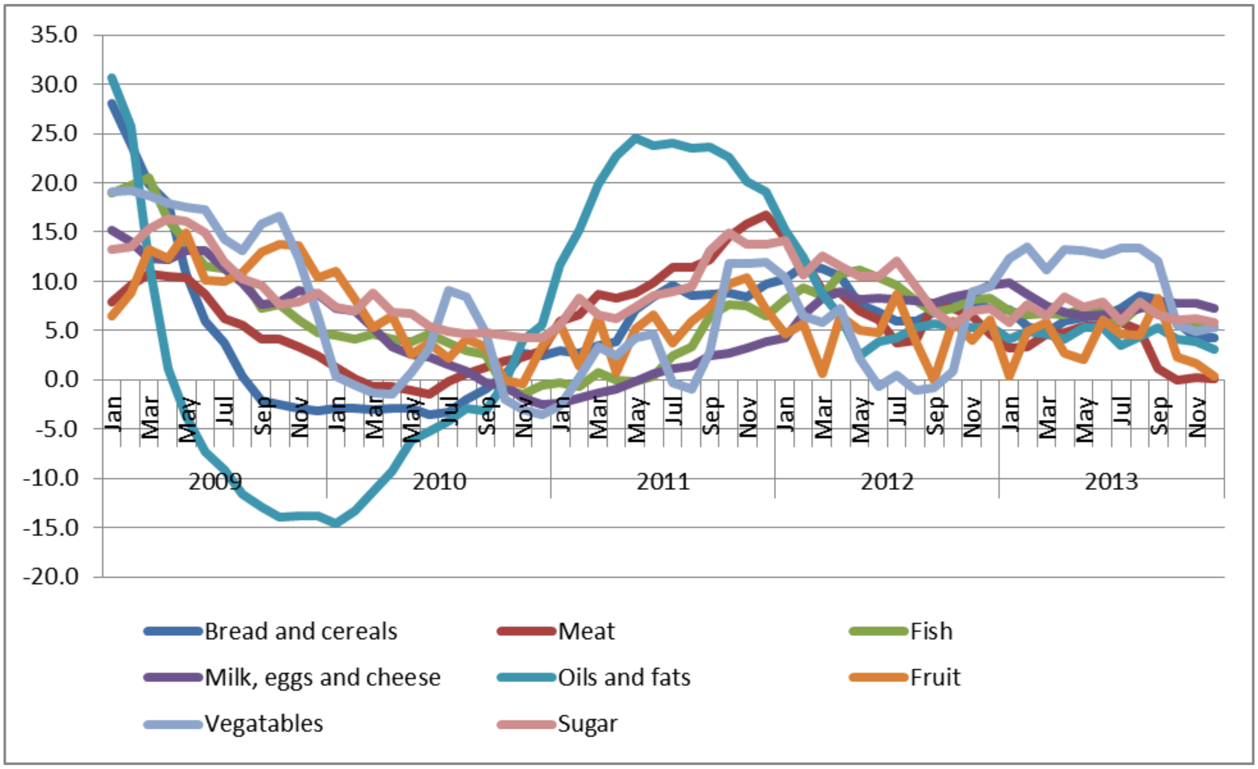

Figure 2: The inflation rates of specific food categories from January 2009 to December 2013

RETAIL PRICES

The National Agricultural Marketing Council (NAMC) is tasked to monitor food prices at the retail level and compile a report in this regard every quarter. In Table 3, the retail prices of selected food items are indicated as referenced in the November 2013 food price monitor report. Except for potatoes (12.8 percent) and pork chops (10.8 percent) all of the selected products recorded a less than 10 percent price increase on a year-to-year basis. The retail prices of maize meal (2.2 percent), tomatoes (13.9 percent) and beef mince (1.8 percent) recorded a decrease in retail prices compared to October 2012.

Table 3: The retail prices of selected food items

	Oct 2012 (Rand)	Jul 2013 (Rand)	Oct 2013 (Rand)	Change (2012 - 13) (%)	Change (Jul-Oct) (%)
Loaf of brown bread	8.80	9.16	9.36	6.4%	2.2%
Loaf of white bread	9.88	10.25	10.5	6.3%	2.4%
Maize meal (5kg)	28.59	26.14	27.95	-2.2%	6.9%
Rice (2kg)	21.23	21.51	22.54	6.2%	4.8%
Potatoes (1kg)	8.81	9.47	9.94	12.8%	5.0%
Tomatoes (1kg)	19.95	14.98	17.17	-13.9%	14.6%
Polony (1kg)	28.59	29.78	29.83	4.3%	0.2%
Whole chicken (1kg)	33.96	34.55	35.68	5.1%	3.3%
Chicken portions (1kg)	44.19	44.42	44.37	0.4%	-0.1%
Pork chops (1kg)	53.69	57.45	59.51	10.8%	3.6%
Beef mince (1kg)	62.71	60.36	61.57	-1.8%	2.0%
Fresh milk (1l)	7.48	7.6	7.81	4.4%	2.8%
Fish tinned (155g)	6.97	7.53	7.57	8.6%	0.5%
Eggs (1.5 dozen)	27.01	28.38	29.19	8.1%	2.9%

Source: NAMC

CORN PRICE INCREASES

During the end of November 2013, both white corn and yellow corn domestic prices sharply increased to record levels, despite international corn prices decreasing, as domestic corn prices moved away from export parity price levels and closer to import parity price levels (see also Figure 3 and Figure 4). The movement to import parity prices is driven by the anticipation of possible corn imports realizing as stock levels are under pressure. The drought conditions prevailing in the Northwest province where about 25 percent of South African corn is produced also plays a major role in the increase corn prices. On a year-to-year basis yellow corn and white corn prices are respectively, 38 percent and 40 percent higher and prices have increased by more than 12 percent in the past month.

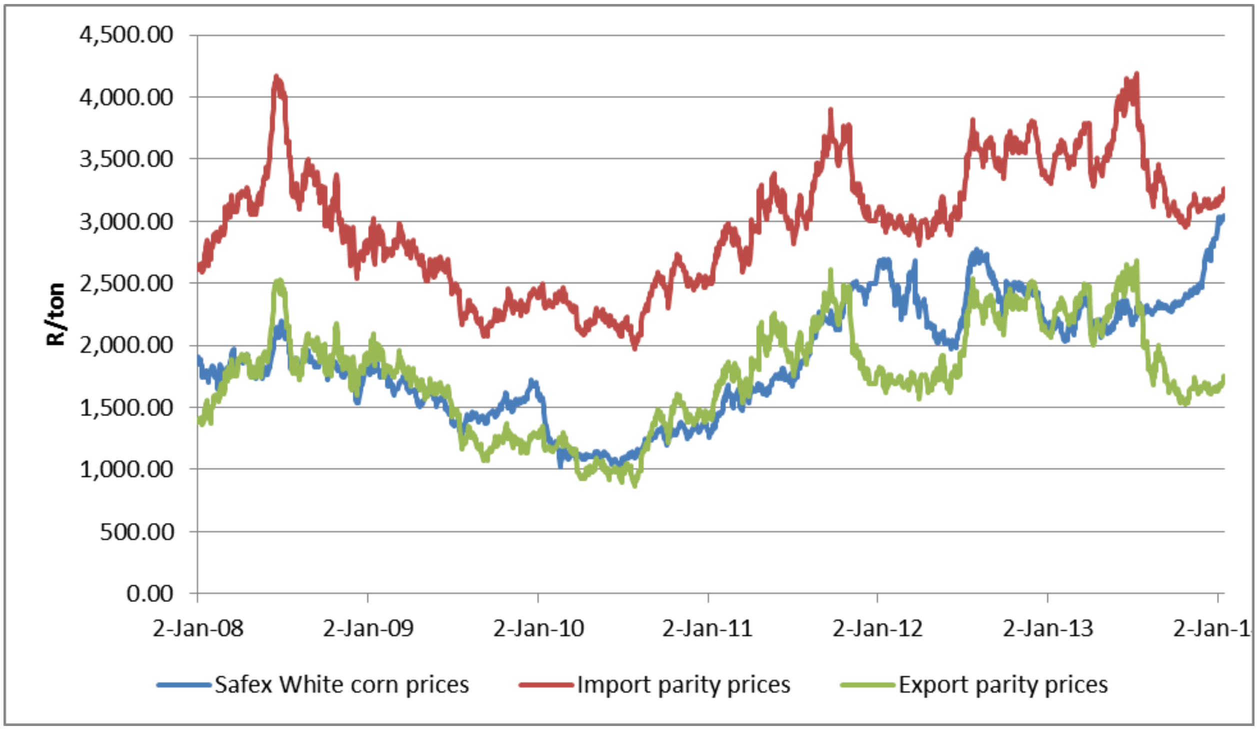

Figure 3: The trend in the SAFEX price for white corn since January 2008

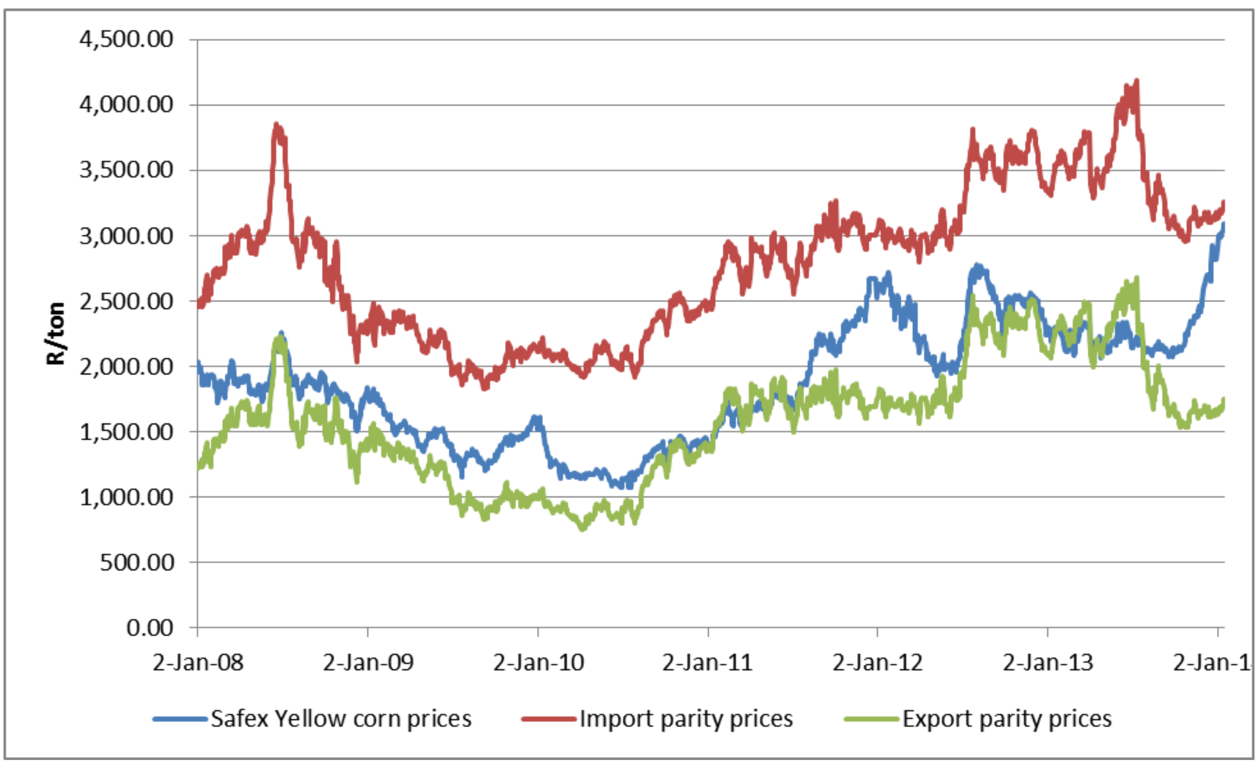

Figure 4: The trend in the SAFEX price for yellow corn since January 2008

Corn meal is a staple food for many South Africans, but can easily be substituted by bread or rice. Figure 5 illustrates the consumption trend of corn, wheat and rice in the food and feed markets of South Africa since the 1997. The demand for corn in the human food market (mainly white corn) increased by an average of 2 percent per annum the past 17 years, while the demand for corn in the animal feed (mainly yellow corn) increased by an average 3 percent per annum. After staying basically flat during the period 2001 to 2007, the demand for corn in the human market increased by 19 percent during the food price crisis of 2008. The main reason for the increase was that the domestic price of corn meal stayed relatively constant during the food price crisis compared to the prices of other starches like bread or rice that rose sharply. The increased production of corn in South Africa saw the domestic corn price moving from import parity levels to export parity levels. As a result, the local price of maize meal decreased by two percent between October 2007 and October 2008, while the price of bread increased by 35 percent.

On the other hand, the demand for corn for animal feed decreased by three percent during the food price crises of 2008. This was attributable to the economic situation which forced many South Africans to buy cheaper basic foods and use less meat and other value added foodstuffs.

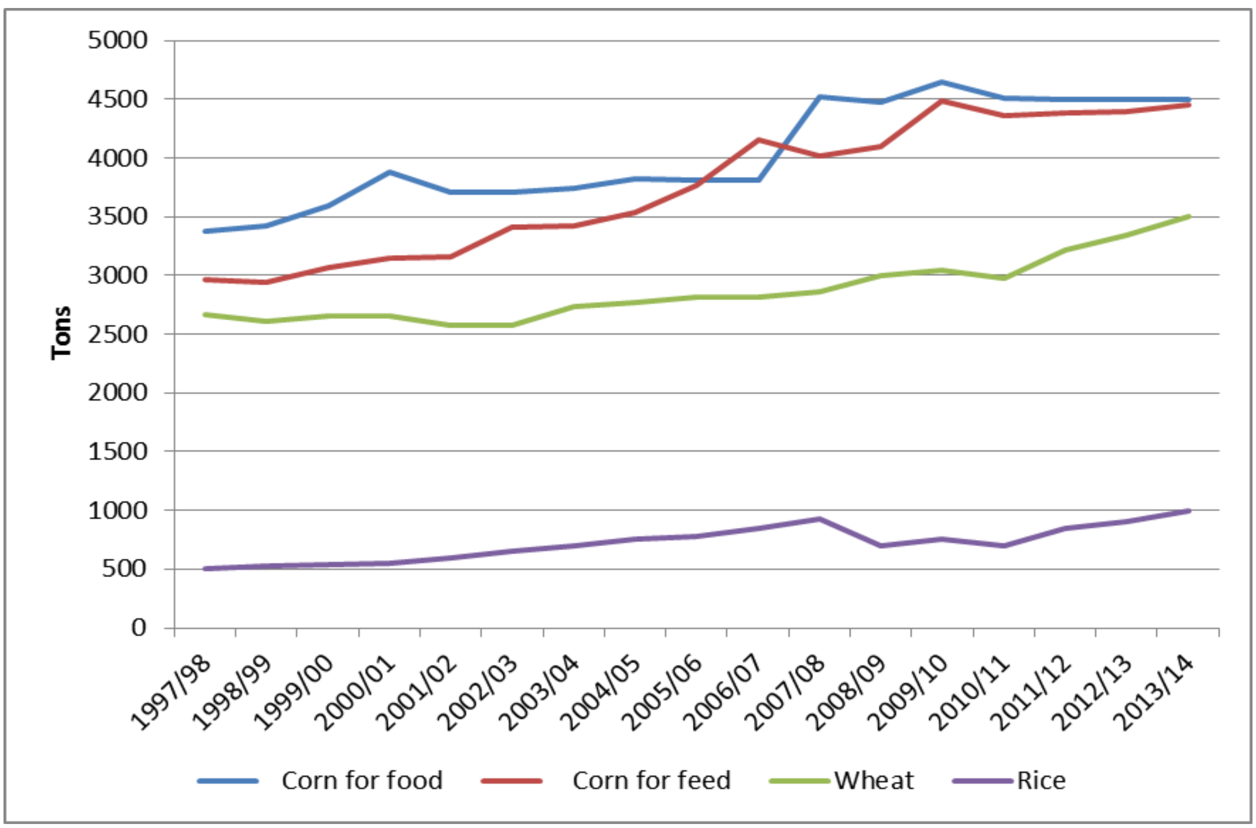

Figure 5: The consumption of corn, wheat and rice in the food and feed markets of South Africa since the 1997/98 MY

Since 2008, the demand for corn for human consumption and animal feed has flattened, due to relatively high corn prices, while the demand for wheat and rice increased by respectively, 17 percent and 30 percent. On a year-to-year basis the price of wheat only increased by 6 percent (see also Figure 6), compared to the 40 percent increase in white corn price, explaining the growth in the demand for wheat.

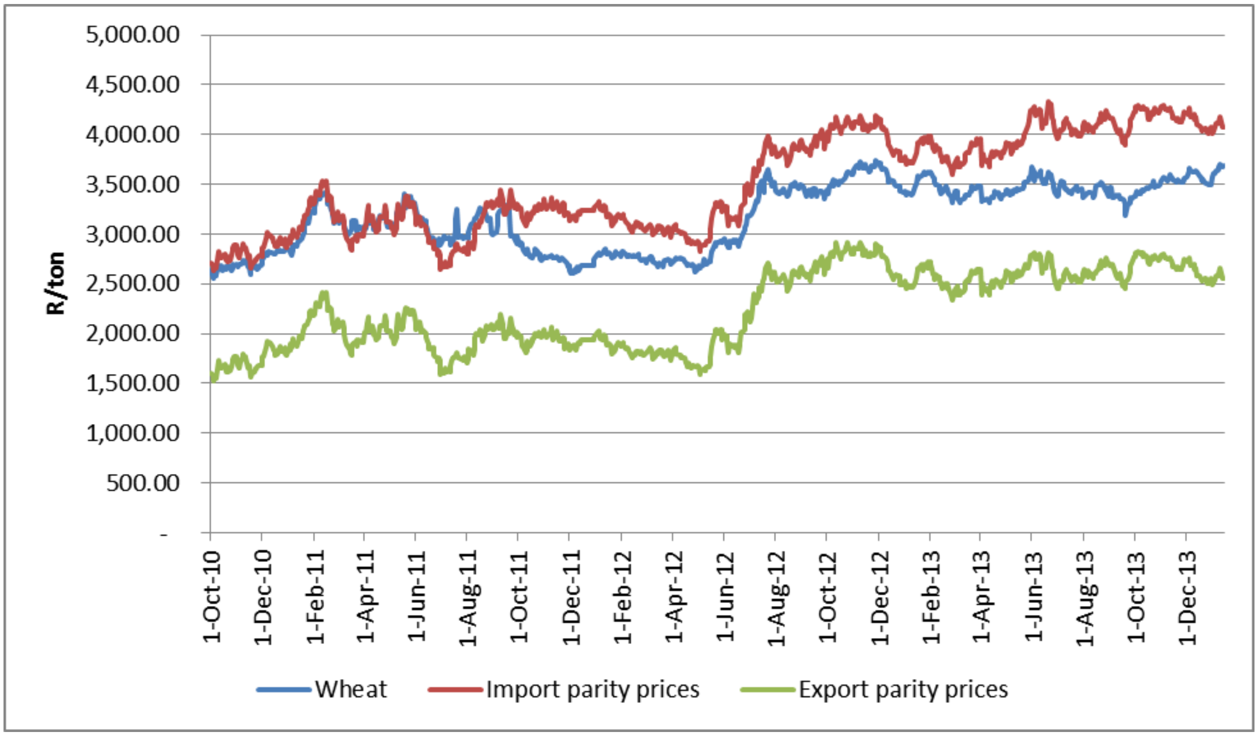

Figure 6: The trend in the SAFEX price for wheat since October 2010

THE RAND EXCHANGE RATE

Currently, a major risk to food inflation in South Africa is the deterioration of the rand exchange rate. The rand has depreciated by more than 20 percent against the United States dollar on a year-to-year basis and by nearly 5 percent in the first two weeks of the 2014 (see also Figure 7). The rand stumbled to a fresh five-year low against the dollar in mid-January, falling alongside other emerging market currencies as investors foreseen the United States central bank will press on with cutting back stimulus. South Africa's budget and current account deficits, strikes in the manufacturing and mining sectors, and the 2014-elections, also make the currency more vulnerable than most emerging market peers during periods of global risk aversion. If the rand continues to depreciate, the prices of all food items will increase, which will increase food price inflation.

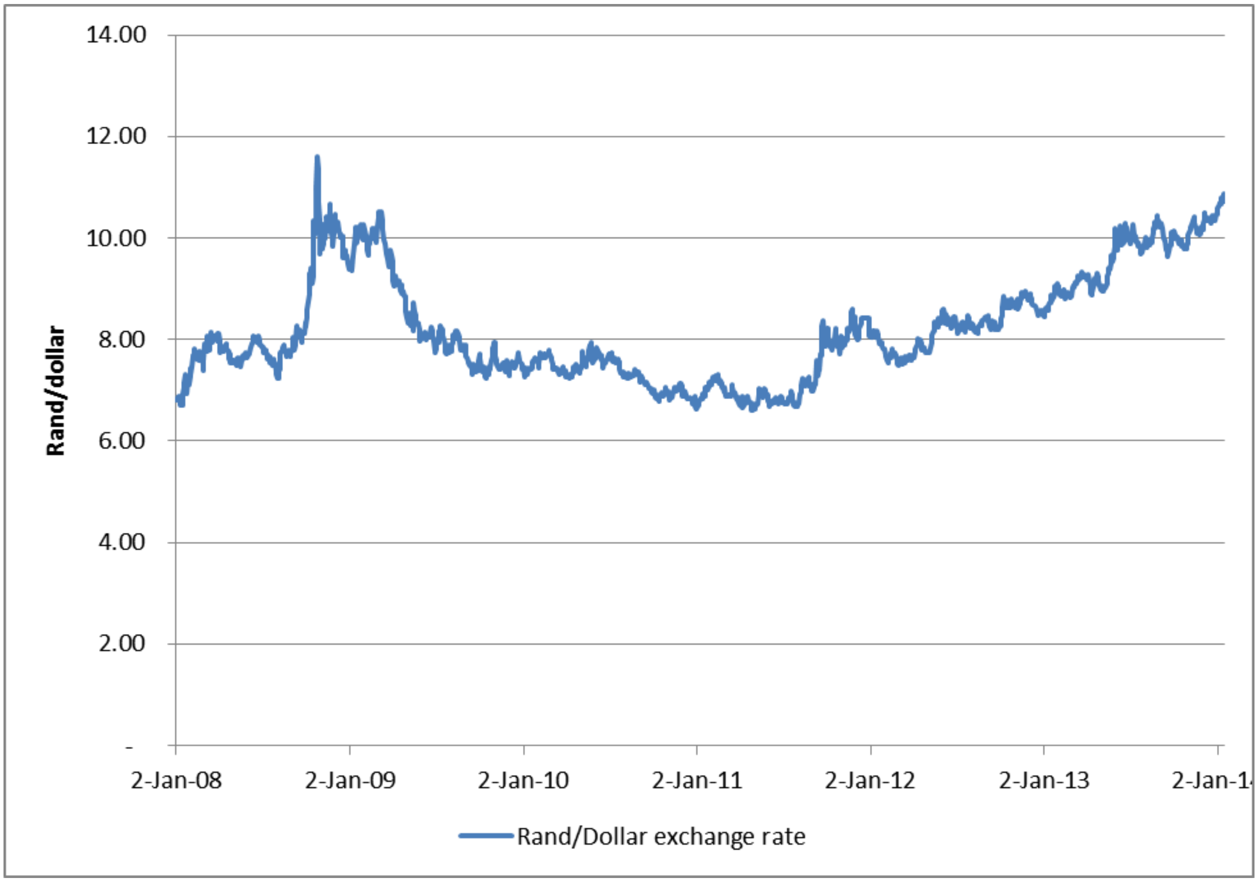

Figure 7: Rand/dollar exchange rate
Source: Reserve Bank

IMPORT TARRIF INCREASES

There is an increased tendency by the South African government to increase import tariffs to protect local industries and thousands of jobs against more efficient international producers' imports. If this tendency continues in the future, the South African agricultural sector will become more inefficient, which will have an adverse effect on food price inflation. In October 2013, the import tariff of five poultry products were increased, while the South African sugar industry also asked for more protection against imports. Higher tariffs on staples like poultry will likely increase prices for consumers. Trade data indicates that the increased poultry tariffs since October, shifted imports away from Brazil to European Union countries, at increased import prices.