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Upward Trend of Food Prices in Bulgaria

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Report Highlights:

Over the last two weeks, there have been fierce public debates in media and at the political level about increasing food prices. The focus has been on staple products such as bread and sunflower oil. Baking and oilseeds crushing industries have tried to educate the public and politicians about the global market trends which lead to inevitable price increases on the local market. However, the general public remains skeptical. It inclines to agree with the opposition's view that the situation was caused by the government's inefficient control over exports and food prices, by speculations, secret cartel agreements, and tax evasions. It remains to be seen if the current challenges will lead to longer term changes in agricultural policies or other political implications.

General Information:

Summary

Over the last two weeks, there have been fierce public debates in media and at the political level about increasing food prices. The focus has been on staple products such as bread and sunflower oil. Baking and oilseeds crushing industries have tried to educate the public and politicians about the global market trends which lead to inevitable price increases on the local market. However, the general public remains skeptical.

General public inclines to agree with the opposition's view that the situation was caused by the government's inefficient control over exports and food prices, by speculations, secret cartel agreements, and tax evasions. The opposition called for new regulations to restore the "strategic grain reserve" – a practice abolished years ago as conflicting with the EU norms, and to introduce more regulations over the grain market.

It is speculated that the Government has been under the pressure of the opposition, certain industry groups and general consumers to open the State Reserve. The State Reserve is an institution from the pre-EU membership time which was used for intervention purposes and was often associated with scandals and corruption practices. Despite the establishment of EU model interventional agency, the GOB has not shut down the grain State Reserve. The Reserve was supposed to only play a role as a war-time buffer for grains and not intervention in the grain market which would be a violation of the EU law. Despite this situation, the trade rumored that the Reserve sold 30,000 MT -50,000 MT of wheat to one buyer with no open tender in June 2010 and this wheat was quickly exported. The Director of the Reserve refuses to reveal any grain figure about the Reserve volume since this is a confidential information. This situation leads to more speculations that the Reserve might decide to make a hidden sale to selected companies in order to maintain lower flour and bread prices.

It remains to be seen if the current challenges will lead to longer term changes in agricultural policies or other political implications.

Local Market Specifics

Bulgarian consumers who have the lowest purchasing power in EU and spend over 40% of their income on food, are very price sensitive, especially when prices of bread, number one staple product, escalate. Although bread and bakery products consumption has been declining since 2000 with the overall economic improvement, bread still holds the priority in the daily diet.

This is a convenient theory which has been often used for political purposes. Imports of wheat/wheat flour have always been perceived by public eyes as a "taboo" which will lead to an expensive bread/food, and political instability. In terms of macroeconomics, food inflation has been considered as a major driving force behind general inflation due to the high percentage of food expenses in the consumer basket.

Consumption and bread and cereals, 2000-2009				
Cereal products	Year 2000	2003	2006	2009
Bread and bakery products, kg	134.8	124.2	116.6	105.9
Flour, kg	12.5	11.1	8.2	8.3
Other cereals, kg	0.5	0.6	0.7	0.8
Confectionary made of flour, kg	3.9	4.9	6.0	6.3
Total, kg	151.7	140.8	131.5	121.3
Source: National Statistical Institute, annual data				

Official data for 2009 shows 36.9% of income spent on food. However, most polls and consumers estimate these expenses at 40% to 50%. This percent has been declining until 2009 when it rebounded again as a result of economic challenges. According to a recent GfK agency study, Bulgaria ranks 35th among 42 European countries in purchasing power with 2,618 Euro/capita compared to average 11,945 Euro/capita in Europe.

Industry and Government Positions

Over the last year, bread, bakery and cereal products had relatively stable prices. Manufacturers were able to maintain this stability through various technological or marketing techniques such as smaller packages, mix of various ingredients, shrinking margins, product diversity, etc, despite slowly creeping prices. Consumers, however, became more sensitive to bread prices over the last 1-3 months. In January 2011, manufacturers announced that they could not hold on price increases any longer due to significant price hikes on the market. They argued that 20%-30% price increase for bread by February could not be avoided.

The MinAg made an effort to calm down the public by actively reaching out to the consumers and consulting with industry. It confirmed that prices will grow but at a slower, gradual pace by not more than 15%. However, according to the Chamber of Industrial Bakers (its members account for 80% of the market), the current price of a kilo of bread is 1.10 leva-1.20 leva (0.55 –0.60 Euro), below the production cost (estimated at 1.40-1.50 leva/kg (0.70-0.75 Euro/kg). Since manufacturers can't continue to operate at a loss, the price should go closer to the production cost or by at least 25% -30%.

This will be the second major price increase of bread since June 2010. Between June and January 2011, the bread price has increased 60%. According to the industry, despite these increases, local bread remains at 27% of average EU prices.

The industry rejected allegations of speculation and presented the bread cost structure showing that 59% of the final price comes from wheat. Prices of wheat flour on the local market followed the world trends and went from average 370 leva (185 Euro/MT) in June 2010 to 620 leva (310 Euro/MT) in January 2011. Over the same period, diesel prices went up by 19% and natural gas by 36%, excises on oil also increased.

The industry strongly denied allegations from consumer organizations that the quality of bread is poor or lowered on purpose to save on cost. In 2010, the share of milling quality wheat in total output was 30% or 1.2 MMT and most of this wheat has been traded and used by millers (900,000 MT to 1.0 MMT) while feed wheat are exported. Certain millers, however, prefer to work with cheaper wheat.

According to grain traders, farmers understand and see the market trends and are reluctant to sell in a hope for higher prices in the future. In the current marketing year, farmers are not cash strapped, they received very good subsidies and their motivation to sell is not as high as in the past. As a positive result of higher prices, planted areas under grains and oilseeds have increased and further expansion is expected in 2011. This lowers the amount of idle agricultural land, an issue which has not been addressed by any administrative tool so far. At the same time, demand and price of agricultural land is going upward. Data from the stock exchange in Sofia shows that two investment funds increased their revenue from agricultural land by 50% in 2010 through renting out 34% more agricultural land. It is expected that the current trends will lead to higher land rents in 2011 as well.

Another positive result of bigger market revenue has been increased demand for agricultural equipment and investment at farms which will inevitably lead to higher productivity and better competitiveness. Exporters also reported very profitable business spurred by favorable regional and global demand which motivates them to invest in infrastructure, distribution and logistics.

Currently, traders report that exported wheat (FOB price) is cheaper than wheat offered on the local market by about 10 Euro. At the same time, imported wheat of little better quality than local can be imported at a price about \$90/MT higher than the local wheat but the spread is shrinking every day. Therefore, millers do anything possible to lower the price of the final product by using more local, less expensive wheat.

Traders doubt that wheat or flour imports will be massive, if any, due to low purchasing power. This is true not only for the final consumers but also for the buyers of imported wheat which usually can't afford to buy significant quantities. In rare cases when Bulgaria used to import wheat in the past, imports were usually in smaller lots and slow. In addition, traders think that in such situations, bread consumption rations as a result of higher prices. Over the last 10 years, the highest annual wheat imports were 134,469 MT (in CY 2004, source WTA), see Table 3.

Mills have different levels of wheat stocks, and some of them are integrated with farming and /or baking, so those with higher stocks can still afford lower flour and bread prices which increases the competition tension on the market but does not change the general trend of climbing prices. On the other hand, this leads to regional differences in flour and bread prices which often puzzles consumers and leads to rumors about speculations.

Industrial bakers made a special press conference where they disagreed with the association of smaller bakers and the MinAg that retailers' exercise pressure on suppliers to lower prices, thus leading smaller companies to bankruptcy but admitted that there has been more tension between the industry and retailers lately. The local market is highly fragmented, there are many small suppliers who have no sufficient experience and knowledge to negotiate with expanding retailers whose power has been growing steadily over the last 3 years.

Recently, various food industries have stated that due to retailers' lowering delivery prices and increasing various fees to suppliers, producers are not able to make descent profit. Others say that this leads to lower quality of food products. On February 2, 14 branch organizations from the food and light (meat, dairy, soft drinks, beer, wine, poultry and eggs, flour and baking products) met to establish a

special Committee for Fair Trade to protest against retailers and to demand urgent GOB's actions in regulating a more balanced relationship between suppliers and retailers. Currently, the retailers share on the market is about 25%-30% but it is estimated that it can realistically go up to 50% very soon.

Domestic suppliers and producers are also appealing for removing hypermarkets from downtown areas, limiting retailers' margins and mark-ups, changing certain terms in contracts, having the same terms of supply as the foreign suppliers, guaranteed 70% presence for the Bulgarian origin products, etc. The Association of Retailers responded that suppliers are free to choose where to sell their products.

The baking industry also made proposals how to reduce the grey sector and tax evasion in the sector. Reportedly, 50%-60% of total number of bakers, especially smaller ones, operate in the grey sector and could maintain lower prices by not paying all due taxes. The proposals include mandatory VAT registration regardless of companies' size; lower VAT for foods (6% vs 20% currently); online connection with the central tax authorities; ban on in-kind rents in rural areas, usually in a form of flour or bread; etc.

It remains to be seen if the authorities will pursue any of the above ideas.

Wheat and Sunflower Supply and Demand

Wheat and products

At a meeting with the grain and grain products industry associations, the MinAg released data about available grain stocks, supply and demand.

Available wheat stocks as of Dec. 31, 2010:

1.5 MMT; of which 102,000 MT in all 54 public warehouses; 237,000 MT in total 170 non-public grain warehouses; 750,000 MT at warehouses of processors and 495,000 MT in farmers' hands.

Out of these stocks, 318,000 MT are at flour mills which corresponds with the average monthly stocks as mills in the period July-December (320-360,000 MT) and represents the pipeline stocks for about 3 months. Total stocks are 58% less than stocks in post harvest time (July 2010).

Wheat exports as of December 31, 2010 were officially at 1.586 MMT of which 69% or 1.099 MT for the EU countries and 31% for third countries. This is 84% more than exports a year before (873,000 MT). Exports had peaks in second halves of months of August, September and November. Since January 1, 2011, exports were 24,000 MT, only to EU markets. Another 40,000 to 50,000 MT are likely to be exported in February.

According to WTA data, wheat exports (1,509,897 MT for July-October 2010) went mainly to Spain (553,000 MT), South Korea (226,000 MT); Romania (186,000 MT), Italy (133,961 MT), Portugal (65,000 MT and Greece (65,000 MT). Industry data shows exports as of early February of 1,654,000 MT.

According to WTA data, wheat imports in the current marketing year were 8,971 MT (July-October) of which 6,406 MT from Serbia and 1,071 MT from Austria; and 23,976 MT for the calendar year (till October). Industry data shows imports at 11,600 MT (July 2010 – January 2011). There is a rumor

about imports of 15,000 MT of Kazakhstan/Ukrainian milling quality wheat part of which is mixed with local feed wheat for bread purposes, although this has not been confirmed. The MinAg confirmed imports of only 3,000 MT of Kazakh wheat so far.

The MinAg estimated that with current stocks Bulgaria could export another 486,000 MT-500,000 MT of wheat without a need to import substantial volumes. About 897,000 MT of wheat will be needed to meet local demand (550,000 MT for food and 347,000 MT for feed) until the new crop. The MinAg estimates ending stocks in MY2010/2011 (June 2011) at 200,000 MT.

According to the Association of Grain Producers, what prices on the local and the international market are currently at equilibrium. Feed wheat is exported at 380-420 leva/MT (190-210 Euro/MT), milling wheat is traded at 450 leva/ MT (225 Euro/MT). Due to price parity, the association thinks exports may slow down.

Table 1. Wheat Supply and Demand, MY2010/2011

Wheat supply and demand, MT, January 2011	MY2010/2011
Beginning stocks	288,000
Production	3,900,000
Imports (as of Dec 31, 2010)	12,900 (6,400 MT from EU and 6,500 MT from third countries)
Total supply	4,201,000
Exports (as of Dec 31, 2010)	1,586,430
Food, feed, seeds (in the first half of MY)	1,032,000
Stocks as of Dec 31, 2010	1,583,000
Source: Bulgarian MinAg	

Sunflower and products

According to the MinAg data, available sunflower stocks as of Dec 31, 2011, are as follows: 1.017 MMT; of which 102,000 MT in public warehouses; 141,000 MT in non-public grain warehouses; 471,000 MT at warehouses of processors and 303,000 MT in farmers' hands.

Consumption in the period Sep.1 – Dec 31, 2010 is 160,000 MT (40,000 MT/month) and exports 325,000 MT (296,000 MT or 91% for the EU and 29,000 MT or 9% for third countries). This is 43% lower than exports for the same period in MY2009 when exports were 574,000 MT (of which 60% for the EU and 40% for third countries); mainly due to slow exports to Turkey. Exports to date in January 2011 were 45,000 MT, only for EU, and another 18,000 MT to 20,000 MT may be exported until end-January.

The crushing plants hold on average 91,000 MT to 105,000 MT per month as pipeline stocks which meet their needs for 2.5 months.

The needs for crush until the new crop are estimated at 320,000 MT (480,000 MT for the year) which

means that the remaining 697,000 MT is the exportable surplus.

Sunflower prices have been increasing during 2010. On January 6, 2011, the price was 836 leva/ MT (418 Euro, no VAT) compared to 509 leva/MT (254 Euro) on the same date in 2010 or 64% growth. Sunflower oil prices in December 2010 were 40% more than in January 2010. Industry estimates further price increases in 2011.

Table 2. Sunflower Supply and Demand, MY 2010/2011

Sunflower supply and demand, MT, January 2011	MY2010/2011
Beginning stocks	39,000
Production	1,426,000
Imports (as of Dec 31, 2010)	1,239
Total supply	1,502,000
Exports (as of Dec 31, 2010)	325,000
Food and seeds (in the first half of MY)	160,000
Stocks as of Dec 31, 2010	1,017,000
Source: Bulgarian MinAg	

Table 3. Wheat Production, Exports and Imports in 2002-2008 calendar years

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