Access to production finance could be a challenge for SA farming sector in 2020/21

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South Africa's 2020 large agricultural output, coupled with higher commodity prices which were precipitated by the weaker domestic currency, coupled with growing global demand improved farmers' finances somewhat. The benefits of this improvement were also observed through robust agricultural machinery sales, with tractor sales for the first nine months of this year up slightly from the corresponding period in 2019. Yet, the challenge of growing farm debt in the sector persists as it will not be solved by one good harvest like the one, we recently recorded, which was preceded by years of poor output in various provinces of the country.

In 2019, South Africa's agricultural debt was at a record R187 billion, which was a nearly three-fold increase since 2010, according to data from the Department of Agriculture, Land Reform and Rural Development.[1] About 29% of this farm debt was held by the Land Bank, 61% by the commercial banks, and the balance spread between agricultural cooperatives, private persons and other institutions. The escalation of debt, particularly in more recent years, was because of both the expansion in area farmed, specifically in horticulture and to some extent, the financial pressure brought by frequent droughts, which have limited agricultural output on various farms.

Exhibit 1 illustrates that the levels of farm debt as a percentage of the agricultural gross value added, are not at higher levels as that we had seen prior-1994. Still, there are growing concerns amongst various farmers that access to credit in 2020/21 production season is proving to be a challenge. This is the case, despite the large harvest of the 2019/20 season that we have previously mentioned. It appears that the liquidity constraints that are currently facing the Land Bank[2], coupled with general uncertainty brought by the pandemic have made various financial institutions more risk-averse. There is anecdotal evidence from various farmer organizations and agribusinesses that previously worked closely with the Land Bank on providing finance to the sector, who are now worried about the 2020/21 season. Land Bank's involvement in South Africa's agricultural sector is through various direct and indirect financial services dedicated to supporting both on and off-farm agricultural activities and businesses including input provision, land purchase, production, distribution, wholesale, processing and marketing.

The spillovers of the current liquidity challenge are particularly important as the planting season began this month and farmers currently need to acquire production inputs and various agricultural implements. While the scale of the problem on the farming sector is unclear at this point about the upcoming season, the growing concerns from various interactions have introduced additional risks to the 2020/21 production season.

In essence, while we have previously outlined an optimistic view about the 2020/21 season because of attractive higher commodity prices, and favourable weather outlook with La Niña

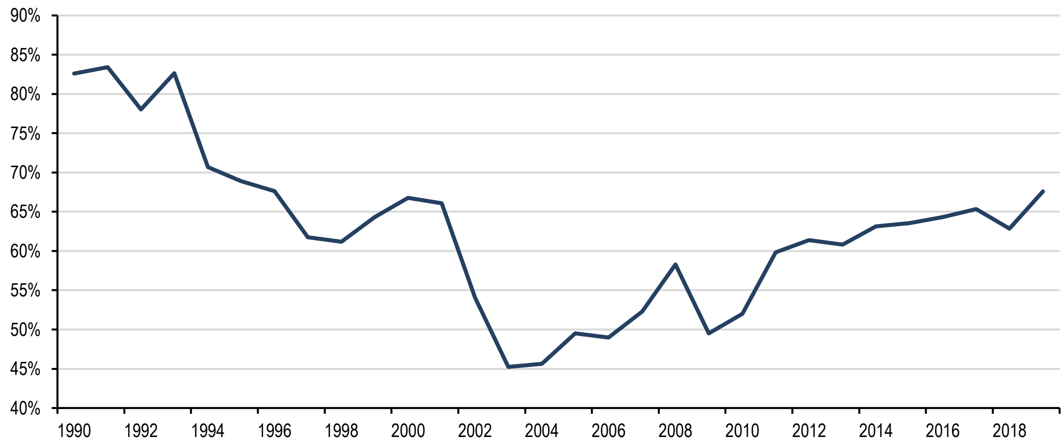
[1] The Abstract of Agricultural Statistics by the Department of Agriculture, Land Reform and Rural Development can be accessed here: https://www.dalrrd.gov.za/Portals/0/Statistics%20and%20Economic%20Analysis/Statistical%20Information/Abstract%202020_organized.pdf
[2] For more information on the Land Bank crisis, please see the link: https://www.futuregrowth.co.za/newsroom/land-bank-a-vital-role-player-in-sa/

forecasts on the horizon; the access to production finance in the sector is now increasingly becoming a concern for farmers. The solution to this will begin by first addressing the liquidity challenges at the Land Bank, a responsibility which largely falls on the hands of the government, primarily the National Treasury and the Department of Agriculture, Land Reform and Rural Development, as the Bank's Act mandates.[3]

With that said, we are not necessarily saying the sector is in financial crisis, rather signalling growing risks to the 2020/21 production season, which need close attention and monitoring. We will be listening closely when the Finance Minister releases the Medium-Term Budget Policy Statement on 28 October for any messaging related to the Land Bank challenges.

Agriculture is one of the sectors that the South African government has highlighted as having a potential for expansion/growth and job creation, the realization of such potential depends on also solving the current impending financial challenges. A swift response to the current challenges will also show the seriousness of the aforementioned importance of this sector for growth and job creation, specifically in the rural economy. We won't venture into sharing opinions on how the mechanics of the resolution should be as that is best suited for those with intimate information on the Bank's operation and interlinkages to agribusinesses. The purpose of this note is merely to flag the financing as an additional risk to production in the 2020/21 season.

Exhibit 1: South Africa's farm debt as a percentage of the agricultural gross value added



Source: Department of Agriculture, Land Reform and Rural Development, and Agbiz Research

Weekly highlights

Zimbabwe's maize demand to increase towards the end of 2020 and into 2021

In the 2019/20 marketing year, Zimbabwe's maize imports, specifically from South Africa didn't gain much momentum until the start of 2020. This is when Zimbabwe's maize stocks were already depleted following a season where the country produced roughly 777 000 tonnes, which is way less than its annual consumption of about 1.8 million tonnes. The poor harvest was a result of unfavourable weather conditions during the season; dryness at the start of the season, and Cyclone Idai later in the season.

The same pattern of maize import activity could prevail this year as Zimbabwe has yet another poor maize harvest. According to data from the United States Department of

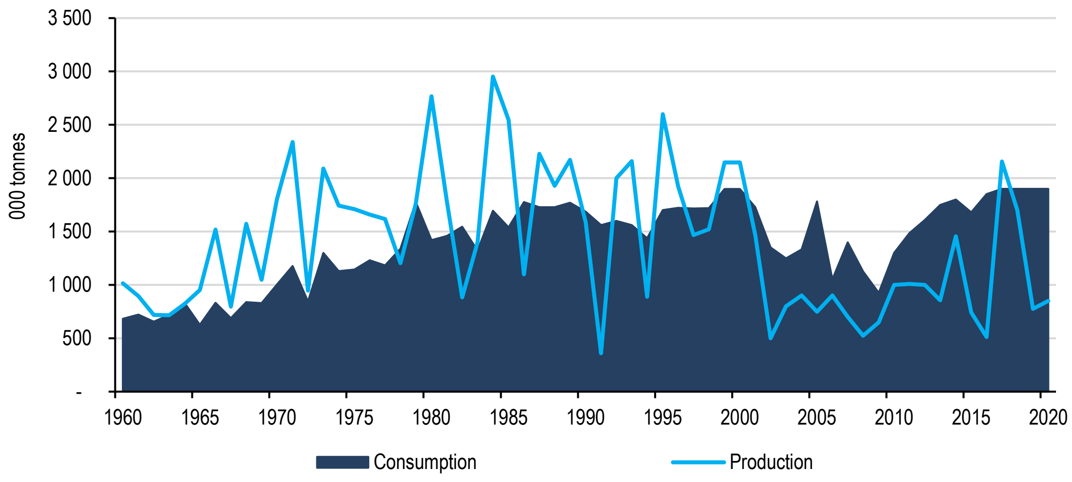
[3] Republic of South Africa. 2002. Land and Agricultural Development Bank Act 15 of 2002. http://www.treasury.gov.za/legislation/acts/2002/a15-02.pdf

Agriculture (USDA), Zimbabwe's 2019/20 maize harvest lifted by 9% y/y to 850 000 tonnes.[4] With annual maize consumption in the 2020/21 marketing year (which corresponds with the 2019/20 production season) estimated at 1.9 million tonnes, Zimbabwe will need to import at least a million tonnes of maize to meet its annual needs.

Between May and last week, Zimbabwe imported 192 366 tonnes of South African maize (both white and yellow). South Africa's maize exports could remain thin in the coming weeks as Zimbabwe still relies on its domestic harvest. But there will likely be some momentum at the end of the year and into 2021. This is when Zimbabwe's maize stocks will likely be depleted or at low levels. This is also the time when there will likely be reports about cases of rising hunger, which the World Food Programme has been consistently warning about.[5]

One of the implications of this expected increase in Zimbabwean maize needs for South Africa could be through maize prices, which will likely be lifted or remain at elevated levels. This is primarily because South Africa, as a neighbouring country with surplus maize, will potentially be a source of imports in the coming months. As we have noted in our recent notes, South Africa's maize prices have remained at elevated levels over the past couple of months, in part because of growing demand from the Far East countries, the weaker domestic currency and generally higher global grains prices on the back of growing Chinese grains and oilseed demand. On 15 October 2020, South Africa's white and yellow maize spot prices were up by 23% y/y and 21% y/y, trading at R3 465 per tonne and R3 622 per tonne, respectively.

Exhibit 2: Zimbabwe's maize market



Source: United States Department of Agriculture and Agbiz Research

Data releases this week

This is again another fairly quiet week from a data front. Starting from a global calendar, today we have the **US weekly crop progress data** which will be released by the USDA. The previous report of 11 October 2020 showed that US maize and soybean crop conditions were rated in a better condition compared to the corresponding period in 2019. Moreover, the harvest activity was gaining momentum with nearly half of the US maize and two-thirds of soybeans already harvested. The yields are reportedly higher than the previous season. On

[4] Zimbabwe's maize production estimates can be accessed here: https://www.indexmundi.com/agriculture/?country=zw&commodity=corn&graph=production

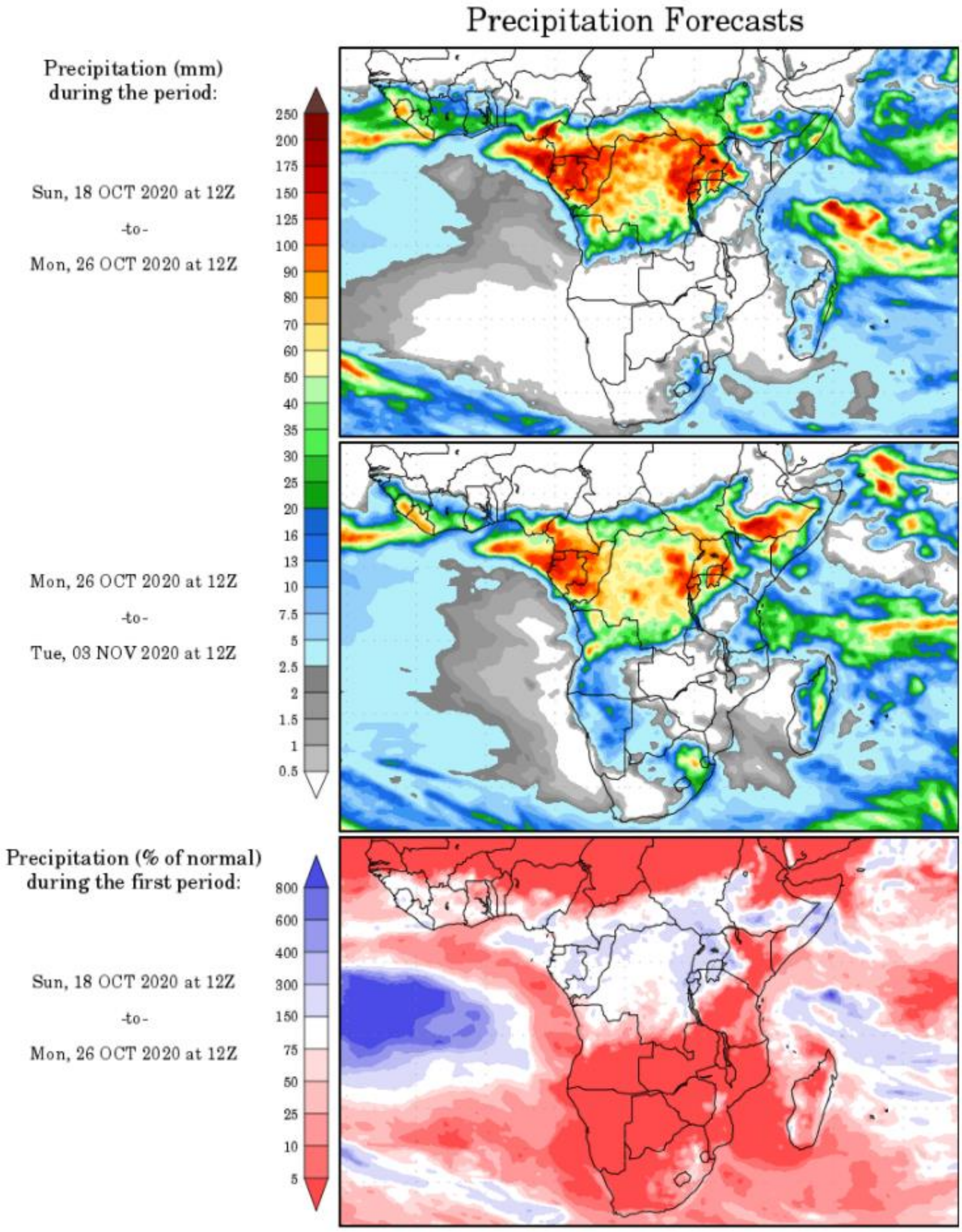
[5] The World Food Programme released communication at the end of July this year warning about potential increase in hunger in Zimbabwe. The Statement is available here: https://www.wfp.org/news/wfp-urgently-seeks-international-support-prevent-millions-zimbabweans-plunging-deeper-hunger

Thursday, the USDA will release the **US weekly export sales data**, which also help in tracking the agricultural trade activity between the US and China.

On the domestic front, on Wednesday, the South African Grain Information Service (SAGIS) will release the **weekly grain producer deliveries data** for the week of 16 October 2020. This data covers both summer and winter crops. But the focus is on summer crops where the harvesting process has recently been completed.

On Thursday, SAGIS will release the **weekly grain trade data** also for the week of 16 October 2020. In the previous week of 09 October 2020, South Africa’s 2020/21 total maize exports were at 1.52 million tonnes, which equates to 61% of the seasonal export forecast (2.50 million tonnes). In terms of wheat, South Africa is a net importer, and in the week of 09 October 2020, the second consignment for the 2020/21 marketing year arrived. This placed South Africa's 2020/21 wheat imports at 97 382 tonnes which equates to 6% of the forecast season imports of 1.64 million tonnes (down by 12% y/y because of a large domestic harvest).

Exhibit 3: South Africa's precipitation forecast



Source: George Mason University (wxmaps)

This week could be fairly dry and warm across most regions of South Africa, which should allow for increased planting activity in areas that already have sufficient soil moisture.