Viewpoint

Crushers hope for continued improvement

The following text is an abridgement of the talk presented by A. Mergell, president of the International Association of Seed Crushers (IASC), to the group's 59th Congress held during February in Manila. In this "President's Review", Mergell described 1982 as a better year than 1981 for the international seed crushing industry, but still not as good as could be desired. Increased supplies of soybean and rapeseed worked to crushers' advantage, but depressed oil markets hurt crushers' margins. Mergell warned of long-term problems if crushing capacity surpasses oilseed crop production. Improved world economic conditions would aid the crushing industry, he said.

One of the strengths of our association is that its membership embraces seed crushing and refining, product markets and associated activities throughout the world. Each area or country will have its particular interest, and questions of the compatibility of interests will inevitably arise. But all members have a common interest and shared concern with all aspects of the world market and in seeing that a healthy growth in world product markets and world crushing activities is fostered.

This year, it was with great pleasure that we accepted the invitation of our Philippine hosts to meet in Manila. It is a country which was achieving impressive rates of economic growth until, as happened in many developing countries, low commodity prices and a protracted world recession brought slower growth. It is a country, however, which remains a significant element in the international seed crushing industry and in the world oils and fats market.

Coconut oil ranks high in the total world exports of vegetable oils, with wide ranging industrial as well as edible use. Three quarters of the needs of importers for coconut oil are met by the Philippines. Equally, the coconut sector is of considerable significance to the Philippine economy. This is well recognized in the programs to extend plantings of high yielding coconut palms, giving prospects in the coming decades of an even more significant role for the Philippines in the world oils and fats market.

It is the longer-term aspects of the world oils and fats market that has been adopted as the theme of this Congress. The precise theme is "The influence of production and consumption trends and technological developments on world trade in oil and fats".

During the past ten years, world consumption of vegetable and marine oils has risen on average by 5 % per annum from 26.5 million tons in 1971/72 to 43 million tons in 1981/82 – a trend now equivalent to an additional consumption of 2 million tons every year. In the developing countries, the expansion in consumption, at 6.5% per annum, has been twice that in the affluent countries where population growth rates are lower, while per capita edible fat consumption is close to its physiological maximum and no longer increases significantly as incomes rise. The growth in vegetable oil consumption in developed countries has been more of a reflection of the trend away from the animal fats of butter and lard than of a total increase.

But it is among the higher income countries with well developed agricultural sectors that the most rapid increase in production has occurred. Across a wide range of developing countries, expansion of oilseed crops has fallen far short of rising domestic consumption needs. This situation is also shared by the Russian/East European area.

If we exclude China, where oilseed crops have risen dramatically in recent years, world edible oil production has risen since 1971/72 by nearly 14 million tons. The USA, Canada, Malaysia, Brazil and Argentina account for nearly 11 million tons of this increase with only 3 million tons being contributed by the rest of the world.

Production and consumption trends are, therefore, characterized by marked regional divergences. In a group of five countries, production has been expanding at 7.5% per annum, well in excess of the growth in domestic requirements, and increasing surpluses for export have been generated. In the rest of the world, largely developing countries with consumption growth of 6% per annum, local production has been expanding less than 2% per annum, with the resultant need for more imports. The major features of the changed structure of world trade arising from these trends are as follows.

First: Five countries – USA, Canada, Malaysia, Brazil and Argentina – now dominate world export supplies of all oils. They account for 85% of the total compared with 50% ten years ago – a rise in their net export position to 11.7 from 3.6 million tons.

Second: Here in the Philippines, exports have remained at the level of ten years ago. But for all other developing countries, consumption growth not matched by higher production is reflected either in declining exports, in countries shifting from net exporters to net importers, or in sharply rising import levels. Within this group of other developing countries, those countries that provided exports of 1.9 million tons ten years ago now provide less than a million tons. Importing countries within this group absorbed 5.8 million tons in 1981/82 compared to no more than 1.6 million tons ten years ago. These countries in total are now nearly as important as Western Europe as importers of oils and fats.

Third: One may also note the similar pattern in the Russian/East European region – once a major exporter but now importing over a million tons of oils and fats.

Underlying these historical trends are many factors which provide much food for thought and discussion about future trends and here I do no more than pose some of the major questions.

First, the continuing ability of such countries to finance imports will be crucial. The most sizeable increase in edible oil imports in the 1970s were by the petroleum producers, with their ability to finance imports enhanced by the dramatic rise in petroleum prices, and by India as ample foreign exchange became available for a time. Moreover, international finance was readily available and drawn upon to a point where international debt problems for many countries have reached serious proportions. Thus there is at least a financial question mark over the continuation of rapidly rising imports of edible oils through the 1980s.

A second consideration is whether countries which experienced slow growth in their oilseed production in the 1970s will be motivated to expand production to satisfy rising domestic needs. On a broader horizon are all those questions of government objectives and policies toward their oilseed sectors not only in the developing countries but also in the USA and in the EEC.

A third set of considerations arises from the dominance of a small number of countries as suppliers. Production trends in the USA, Canada, Malaysia, Brazil and Argentina are of vital importance. However, in these countries 70% of the past increase in edible oil production has been derived from higher acreages. Can acreages be increased further or can rising production trends in these countries be sustained through increases in yields per acre?

Attention at this time is focused on palm oil. The introduction of tree pollinating insects into West Malaysia in 1981 has significantly raised palm oil yields per acre. While other influences also will be present, the increase of 25% in 1982 is impressive. In the future is the potential of cloned palms – essentially a technique enabling a large number of individual plants to be propagated from a single piece of root tissue. Each newly formed plant will have genetic characteristics identical to those of the parent plant. The parent plant may be selected for its high yield but also may be selected, for example, for a particular fatty acid composition of its oil. This technology is reaching the commercial stage for palms, and research to extend the technology to coconut is being pursued with every expectation of success.

Beyond these developments is the possible impact of genetic engineering – a technology which appears to be advancing rapidly although with the usual imponderables to the nonscientist of the potential breadth and time-scale of its commercial application. Equally imponderable is the extent to which consumption trends for vegetable oils will be influenced by increasing industrial use. The major economic imponderable is whether the gap between oil and fat prices and petroleum prices will narrow further in the long term. In the present period of particularly low vegetable oil prices, the Philippines is not alone in seeking to extend the use of vegetable oils as a fuel additive.

More immediately, in the international seed crushing industry, the guarded optimism for improved profitability with which I concluded my review in Munich a year ago has to some extent materialized. But an improvement from particularly low levels still leaves profitability at a far from satisfactory level. Moreover, there are disparate experiences between countries and according to the type of seed crushed.

Market developments have favored crushers in the EEC more than those in the USA. One essential condition for good margins is adequate seed supplies. In the EEC the domestic rapeseed crop in 1982 rose by 35% to 2.7 million tons. This is more than double the crop of three years ago and this year's harvest may reach 3 million tons. Improved soybean margins have recurred in the EEC where meal markets have been stronger. First, EEC meal consumption has been encouraged as prices have fallen relative to cereal prices fixed under the CAP regime – a marked contrast to the price competitiveness of surplus feed grains in the USA.

Second, EEC crushers have benefited more directly from the large Russian meal purchases – in total some 2.5 million tons. Finally, through much of the past year or so the strengthening of the U.S. dollar on foreign exchange markets has given EEC crushers a competitive edge in satisfying product markets and provided additional benefit to EEC margins over those of U.S. crushers.

Both the U.S. and EEC share the improvement in soybean margins which stems from the record 1982 U.S. soybean harvest. The increase of just over 8 million tons combined with stocks at the beginning of the season brought total supplies to a level of 5% above the previous peak in 1979/80 when soy margins were last at a reasonable level. Unfortunately, margin experiences do not now match those of 1979/80. More capacity exists to compete for available supplies, and support to margins from product prices is generally much weaker than in 1979/80, particularly in oil markets. Moreover, some potential benefits of an increased supply undoubtedly have been lost because of the flow of soybeans into support under the U.S. loan rate mechanism. This diversion of beans from the market, and the fact that the loan mechanism provides more direct support to bean prices than to product prices, inevitably affects crushers' margins adversely.

The EEC and USA also have continued to face poor crushing margins on sunflowerseed. New plants have come on stream in the USA. Still too much capacity chases inadequate seed supplies despite the larger U.S. crop. This also typifies the position of Brazilian soybean crushers with capacities far in excess of current crop levels and with import possibilities limited. For crushers of Canadian rapeseed, total supplies are again down.

Outside these major areas are the crushing industries in the developing countries. Here, shorter term experiences differ according to local circumstances and variations in domestic oilseed crops. But the common feature of crushing in many of these countries is the longer term dependence on domestic crops – often characterized by sharp year-to-year fluctuations. Against a background of slowly expanding oilseed crops, a more rapid expansion in local crushing capacities has been sustained in many cases by absorbing seed supplies previously exported.

The classic illustration is here in the Philippines. The combined exports of copra and oil in 1981/82 were close to those of ten years ago. But a decade ago, exports of copra were nearly a million tons. In 1981/82, copra exports were down to 200,000 tons; they were below 100,000 tons in 1980/81. In countries exhibiting this pattern there are two particular implications for their crushing industries. As total dependence on domestic crops nears, production trends become more crucial. And, the vulnerability of local crushers to year-to-year crop fluctuations increases. In the past, this burden was shared by overseas crushers of exported seed. These circumstances suggest increased risks from excess capacities and poor long-run profitability unless capacities can be supplied from domestic crops even in poor production years. Moreover, in consequently maintaining some seed exports, one may reasonably suppose that marketing opportunities for domestic crops are maximized for a country from the presence in export markets for seed.

In summary, it is clear that the improvement since our 1982 Congress has been limited and patchy. Such improvement as has occurred has largely been the result of better seed supplies this season, helped by easing inflation rates, interest rates and energy costs. Nevertheless, the difficult conditions faced over a number of years essentially persist. Reports of plant closures in the USA and capacity reductions in the EEC provide the disturbing evidence of those difficulties.

Sustaining a reasonable level of profitability requires strong product markets which require a strong world economy. Instead, the situation has been one of protracted world recession. Initially, the major impact of the sharp rise in petroleum prices in 1980 was on the industrialized countries. But by 1982 developing countries were faced with a declining demand for their exports from the industrialized countries, export revenues were affected by falling commodity prices and, particularly in the case of OPEC, by a reduced volume of exports. Moreover, many developing countries, which previously had borrowed heavily abroad to sustain economic growth, faced growing constraints of rising debt burdens, the increasing cost of servicing their debt, and greater cautiousness among international lenders as fears of default mounted.

This spread of recession to the developing world fed back to the rest of the world during the second half of 1982 as orders to the industrialized countries contracted. Moreover, among the industrialized countries, only the USA has an expansionary monetary and fiscal policy – elsewhere, recession-induced budget deficits are causing concern, and planned expenditure cuts rather than expansion predominate.

Not surprisingly, the world economy has now been described as worse than at any time since the early 1930s. A resumption of world economic growth is a prerequisite for sustained profitability in our industry. It is needed for resumed growth in developing countries.

In view of the fundamental importance of world economic growth, this association has long been and remains an advocate for liberalization in world trade as being beneficial for long-term world economic growth.

It is, therefore, with concern that one notes increasing moves and pressures toward protectionism. The intensity of those pressures was very evident in the acrimonious and near failure of the ministerial meeting of the GATT last November. Given the present state of the world economy, it must be deemed an achievement that agreement was reached on a number of points. The principle of resisting protectionist measures was endorsed; it was agreed to study measures affecting trade in agricultural products, a highly contentious issue between the USA and the EEC; and safeguards for industries hit by surging imports and trade in services also are to be studied. GATT's powers are increased by the agreement that parties to GATT disputes should no longer block rulings going against them, while sanctions imposed for noneconomic reasons will be banned.

Such agreements unfortunately do not represent progress toward trade liberalization at this time. Nevertheless, the hope must be that the slide toward protectionism and the increasing risk of trade wars will be halted. It also may be hoped that the studies of problem areas will, as in the past, eventually prove to be the basis for a new round of trade negotiations within GATT.

Within this world context, the international seed crushing and refining industry has its own role to play in supporting the free flow of its raw materials and products on world markets and in avoiding the wider range of protectionist measures implicit in such measures as subsidies to domestic crushing and refining industries. Along such a route lies the long-term danger of excess world capacities and poor crushing margins worldwide. Moreover, in the highly interrelated and competitive trade flows of different commodities, no individual country is likely to escape for long the effect of poor margins worldwide.

In the shorter term, one must recognize the complex political, social and economic factors which must influence governments in formulating industrial and trade policies. Understandably, these pressures are likely to overshadow long-term ideals. Nevertheless, it remains important that long-term ideals are not lost sight of, that a desire to move toward them is sustained, and that friction between countries is minimized.

For seed crushing and refining, I believe there are areas in which this association has an important role to perform. It is a role which seeks to foster greater mutual understanding of the position and attitudes of crushers and refiners in different countries, an understanding of the wider repercussions of policies in individual countries and an understanding of long-term ideals important for the stability of the international seed crushing industry.

It is in this role that the IASC provided the umbrella for a meeting last November in Brazil between the NSPA, FEDIOL and the Brazilian Association of Vegetable Oil Industries - ABIOVE. The objective was to seek an understanding of each others' industrial and policy problems. It was a meeting marked by a full and open discussion in a spirit of friendship. In recent years, some open criticism has arisen as a result of the repercussions elsewhere of the various direct or indirect subsidies given to Brazilian crushers. It was of particular interest, therefore, to learn of the measures already taken which put the Brazilian industry on a fairer competitive basis on world markets. The present excess capacity in Brazil gives hope that further expansion or a return to old practices is minimal. It was readily recognized that all three regions shared poor margins and cost pressures and a common interest in expanding world markets. The benefits of cooperation in the overall development of markets also was considered to be an area possibly worthy of examination.

I would rate highly the value of such discussions and the value of this association as the forum and catalyst for pursuing matters of concern internationally.

It remains important that trading contracts and their administration retain the principle of their conclusion which was undermined when, for example, Peru by government decree embargoed the export of substantial quantities of fish oil last year and as U.S. trade embargoes become an instrument of foreign policy some years ago. The recent endorsement of contract sanctity in U.S. legislation is much to be welcomed.

It would be of considerable satisfaction if I were able to close my review this year by further expressions of optimism for the coming twelve months. I could do so on the basis of the high levels of efficiency in our industry and the high levels of technical, trading and management skills. Unfortunately, the continued depressed world economic environment and its repercussions on our markets only suggest prospects of another difficult and challenging year. Having made this forecast, however, nothing would give me greater pleasure than to announce at our 1984 Congress that my forecasting abilities are abysmal.