

## MOVING UP THE VALUE CHAIN: Report on "Black Sea Grain" Conference

The XV Jubilee International Conference "Black Sea Grain-2018" – the leading international forum recognized by top grain and oilseed producers and exporters – was marked by the search of ways to create new added value. The conference was held at InterContinental Hotel, Kyiv, on April 18-19. The organizer: UkrAgroConsult Consulting Agency. The conference was attended by over 700 participants representing more than 500 companies from 50+ countries.

The "[Black Sea Grain-2018: Moving Up the Value Chain](#)" Conference was opened by the Deputy Minister of Agrarian Policy and Food of Ukraine **Olga Trofimtseva**. The Deputy Minister expressed her confidence that Ukraine would become one of 5-6 countries, which will be able to feed the world with grain in the mid- and long-term. At the same time, Olga Trofimtseva noted a successful diversification of agricultural production and exports of Ukraine. In particular, the increase in production of pulses to 1.2 MMT last year, as well as good opportunities for exporting processed products along with grain. What is more, the Deputy Minister stated the stepping up of activities to diversify markets for Ukrainian food products by means of finding new markets in Africa and Asia, the Far and Middle East, as well as in other regions. The government official suggested to diversify the ag market players structure, so that more small and medium-sized Ukrainian producers entered the products supply chain to the world market.



The People's Deputy of Ukraine, the chairman of subcommittee on economic and financial policy in the agricultural complex of the Verkhovna Rada, **Leonid Kozachenko**, in his welcoming speech assured the conference participants that Ukraine could triple the production of agricultural products and double the grain production. According to the Parliament representative, our country can produce more than 120 MMT of grain annually. But it is necessary to improve the industry financing and legislation, especially tax, currency and land legislation.

The Chairman of the Board of Credit Agricole Bank, **Jean-Paul Piotrowski**, expressed his admiration for the remarkable progress of agriculture in Ukraine and his certainty that the agricultural business of the country would successfully create the value added products. The banker believes that Ukraine has a very high potential for not only production and export of agricultural products, but also for its processing.

### Global trends of the agricultural market

The strengthening of the Black Sea region influence in the global agricultural market has become one of the most important trends in recent years. This thesis was stated and explained by the Director General of "UkrAgroConsult" Company, **Sergey Feofilov**. In his opinion, *"the Black Sea countries are already seen as a single and very important player in the world grain market, and we can even talk about the development of a new course in this market."* Mr. Feofilov believes that such rapid and impressive changes have happened owing to low cost of basic agricultural crops production in the region.

During the next 10-15 years, a considerable toughening of competition in the world market will be the main challenge for the Black Sea region, incl. Ukraine. It would be possible to compete successfully by increasing the planted area and production. However, the Black Sea region has rather narrow resources in this regard.

UkrAgroConsult estimates that Ukraine will be able to expand its plantings by at most 0.4-1.1 MI ha by 2025, with a 3-9 MI ha increase in Russia. By contrast, Brazil can enlarge soybean plantings alone by 19.4 MI ha and its corn sown area by 7.5 MI ha over the same time. In total, this South American country alone may ultimately boost its planted area by up to 55% against MY 2015/2016 over the decade.



Ukraine has limited opportunities for financial resources attraction in the agricultural sector. Moreover, all things are happening amid agricultural products global trade reduction. When during 2007-2017, the volume of wheat and soybean sales increased by 50-95% in the world, then for the next decade, the growth is expected to reach only 14-20%. The competition in the sphere of consumption is also strengthening. The importance of the Asian, African and other new markets is growing. *"The competition for solvent demand will be no less tough than in the production sphere"*, said Sergey Feofilov.

In the opinion of the speaker, the Black Sea region's responses to the global challenge within the next 10-15 years may follow several possible scenarios – intensification of farming, obtaining support from the government, switching to high-margin technology and practices.

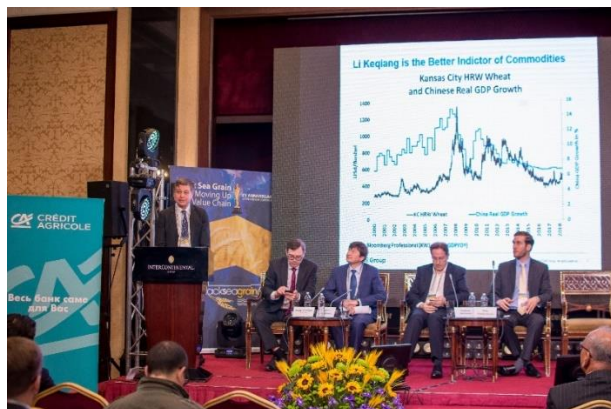
From the promising directions regarding the third development scenario, Sergey Feofilov points out an expansion of area under the most profitable crops, construction of farm silos, lowering of risk by means of hedging and futures operations, organic farming, diversification of agricultural business, and use of effective information technologies in agriculture. A combination of the first and third options would be preferable for Ukraine, but all the three combined would be the best way, Sergey Feofilov says.

The competition between regions is strengthening around the world. Southeast Asia was pulling ahead among the largest consumers of grain (corn, wheat and soybeans all together), said **Stephane Bernhard**, the Head of French company Invivo Trading. According to his estimates, the gap in the consumption of these crops between this Asian region and its pursuer – America – will be around 100 MMT before 2021, and will reach 150 MMT before 2024. At the same time, the demand for grain in regions with developed economies – in North America and the European Union – is growing slowly. Southeast Asia, along with Africa, Middle East (MEA) and South America take the leading role in grain consumption. During the next 7 years, each of these three regions will increase the annual consumption of the three main crops from the current 175-185% of the 2000 level to 215-220%, believes the French expert.

The competition among regions is also toughening because of local currencies weakening. Therefore, as Mr. Bernard said, the cultivation of wheat in Russia, Ukraine and Argentina had become more attractive than in countries with hard currencies. Similar preferences are for soybean production in Brazil and Argentina, and corn – in Brazil, Argentina and Ukraine. The expert believes that Ukraine is very lucky. *"You have the highest prices for corn over the past 25 years, so you need to produce more, the world wants your grain"*, he said.



The European continent will be the main supplier of additional wheat volumes to foreign markets in the coming years, and America will supply corn and soybeans. According to Invivo Trading, the European grain supply increase will reach nearly 14 MMT before 2024 (compared to exports of 80 MMT in 2017). American average annual exports of corn will increase by approximately 40 MMT during this period, and soybeans – by 20-25 MMT.



Prospects of the Black Sea region farmers in different regions are also determined by the state of the leading economies of the world. Analysis of the latter allows creating the so-called "beacons" for agriculture. They were defined and disclosed at the conference by CME Group Executive Director **Erik Norland**. According to his estimates, currently the state of the economy in China, India and Europe is not bad. Therefore, the Black Sea region farmers have good prospects for development, including supplies of their products to these countries. The volatility is also low in the US market. However, already in 2020-2021, the volatility may significantly increase due to the yield curve cyclical nature, and it will be a rather difficult time for farmers around the world.

FAO noted a narrowing of the food consumption gap between developed and developing nations.

FAO Chief Economist **Dmitry Prikhodko** believes the reason is that the latter show a five time faster increase in per capita consumption of food calories than the European Union. The 20-year gain in consumption reached 20% in developing countries against just 4% in the EU. As a result, the demand for food products changes in the corresponding regions, and preconditions for its redistribution and competition strengthening between suppliers for customers arise.



A new trend is a slowdown in food consumption growth. This particularly concerns foods such as grain, meat, and vegetable oil. The FAO forecasts their global use will grow in 2017-2026 nearly half as fast as it did in the previous decade. The upward trend will be maintained primarily by expanding food consumption in Asian and African countries. For instance, by 2026, per capita wheat consumption will gain 12% in Ethiopia, 10% in Bangladesh, and 8% in Mozambique. Ultimately, global imports of this commodity are expected to increase 22 MMT by the above-mentioned time.

Also, a 20% rise will be seen in consumption of dairy foods as well as meat: people will use 12% more poultry, 10% more beef, and 9% more pork. This will raise demand for feed corn by 13-20%, depending on the region. Overall, world corn imports may increase 14 MMT over the coming decade.

Global agri-market expert **G. Chandrashekar** predicts the Indian market to become more attractive to grain exporter. The expert is confident that pulse consumption in the country will increase in the coming



years. The country will use up its previously stockpiled pulse inventories by September, and the market will become balanced, the speaker said. That is when India will probably revise its tax policy towards commodity imports. The speaker estimated India's current need for pulses at 30 MMT. He stated that his country is far from self-sufficiency yet. The reason is that it grows just some 24 MMT of pulses. Therefore, India is forced to import 5-6 MMT annually.



Although India's need for imported wheat is small, Mr. Chandrashekhar believes this business is quite profitable. According to his forecasts, India will be a regular buyer of foreign wheat within the coming 5-8 years. In particular, the country imported some 2 MMT of this commodity in 2017. In addition, the expert says, India's wheat belt is located in the north-west of the country. And it is cheaper to deliver grain to the southern regions by sea from Australia or Ukraine than transporting it by land from the north-west.

### **Regional trends of agricultural products supply to the world market**

The Black Sea region role in the grain market is really important. The region's grain production and export figures, shown by the speaker **Elizaveta Malyshko**, grain market expert of UkrAgroConsult Company, proved the statement. The expert estimated that the Black Sea region produced and exported record high volume of grain – 245 MMT and 116 MMT respectively.

The Black Sea countries will be able to increase grain exports to 115 MMT this season. However, in the 2018/19 season, the exports are likely to decline to 111 MMT, according to UkrAgroConsult estimates. It will happen mainly due to the reduction of Russian supplies to foreign markets. According to estimates, Ukraine will be able to increase exports by 1 MMT, and total grain shipments will reach 42 MMT.



In the corn market, the competition between individual countries is developing into competition between regions – the Black Sea region is increasingly opposed by South America. When in the 2016/17 season, Ukraine accounted for 71% of corn supplies to the European Union, then in 2017/18 MY, this share declined to 43% (September-January period was estimated). The European market was conquered by Brazil – its share in supplies increased from 8% to 53% over the year, said Elizaveta Malyshko. In the 2017/2018 season, Russia is going to supply 10 times more wheat to the Philippines, 3-4 times more – to Indonesia and Korea, and almost 2 times more – to India. Ukraine will be able to increase wheat exports to only two of these countries – by 45% to the Philippines, and 11% - to Indonesia (compared to last season).

The role of South America in the world grain market is also rising. **Pedro Dejneka**, a partner of the Brazilian company MD Commodities, spoke on the region's market and its peculiarities. The expert estimates that soybean production in South America would increase by 11-16% to 200 MMT in the 2018/2019 season,

Brazil is currently the main producer of soybeans in South America – in recent years the country produced around 110 MMT of soy per year. And the country exports a large share of its harvest. Brazil is currently the largest exporter of soybeans in the world. What is more, the export share in the overall soybean's balance of the country has been increasing year on year. When in the 2014/2015 season, nearly 52% of all produced soybean were supplied to foreign markets, then in 2016/2017 MY, the share grew to 59%. MD Commodities estimates that in the current season around 61% of Brazilian soybeans will be exported – nearly 68.5 MMT. In the first months of 2018, the country has already shipped abroad more than over the same time last year. For example, in March, soybean exports reached 10.75 MMT against 9.5 MMT a year before.



Corn exports from Brazil is also growing. In particular, during the first three months of this year, the exports were more than twice as high as over the same period in 2017. Last year the country shipped abroad more than 30 MMT of corn.

Mr. Dejneka also mentioned that Brazil was solving the logistical problems in the sector of agricultural products export. In particular, by means of exporting goods from the ports of the so-called "Northern Arch". The fact is that the cost of shipping Brazilian agricultural goods to the ports of the "Northern Arch" is much lower than to the southern ports of the eastern coast of the country. For instance, the cost of transporting one tonne of cargo from the center of Mato Grosso to the northern port of Itaquí is \$40, while to the southern port of Santos - \$88. Moreover, the delivery of cargos by sea to Europe and China is 5-7 days faster from the ports of the "Northern Arch" than delivery from the southern ports, explains Pedro Dejneka.

As a result, over the past six years, soybean exports from the six ports of "Northern Arch" have grown by 334% - from 4 MMT in 2011 to 19 MMT in 2017. Meanwhile, the other major state ports have increased soybean shipments by only 71% (from 29 to 49 MMT). And corn shipments from the ports of "Northern Arch" have grown even more - by more than 14 times over the last six years.

The representative of the European Commission **Damien Plan** spoke about the huge role of Europe in the global grain market and expectations for the period before 2030. Currently the European Union produces more than 300 MMT of grain, of which more than 140 MMT – soft wheat. Europe is the number-one player in the world soft wheat market. And during the next 12 years, Europe and the Black Sea region would be largest players and main competitors in the global wheat market, said Damien Plan.

At the same time, Europe is a large importer of corn. Moreover, the expert expects an increase in imports of this commodity from an annual average of 13-14 MMT to 15 MMT in 2017/18 MY. If this happens, the EU will outstrip Japan and become the largest importer of corn. Ukraine is the main supplier of corn to Europe. The country already accounts for nearly 67% of all corn imports to the EU. Damien Plan believes that Ukraine will continue to be the Europe's largest trading partner in the corn market.

The European Union is also the second largest importer of soybean in the world. And despite the fact that Argentina and Brazil are currently the major suppliers of soybean to the region, Ukraine has good prospects for the future. Especially when we talk about non-GM soybean, as well as non-GM soybean meal. *"Ukraine has a great chance to become the main supplier of soybeans to Europe, especially soybeans without*

GMO", said Damien Plan. According to the expert, the EU already imports around 30 MMT of soybean products, including 18 MMT of soybean meal.

The role of Russia in the grain market is also strengthening. As of mid-April, Russia had already exported 44 MMT of grain in the 2017/18 season, including pulses. And a new record will be set before the end of the season – exports are expected to exceed 51 MMT. Wheat shipments will reach at least 40 MMT. As a result, Russia's share in the world wheat market will increase from the last year's 15% to 21% - the largest volume over the past 18 years. Such estimates were presented by **Dmitry Rylko**, Director General of Russian company IKAR.



According to preliminary results of the marketing year, exports of Russian wheat to Turkey and “exotic” countries increased most of all, said the expert. He meant such countries as Vietnam, Mexico, Venezuela, Malaysia, the Philippines and other countries which are far from Russia. Dmitry Rylko said they already accounted for nearly 21% of wheat exports. Egypt and Turkey are the largest importers of Russian grain in the 2017/18 season.

The Russian expert admits the strong competition of Russian exporters of agricultural products with Ukrainian in the world market. In particular, the countries struggle for barley market in Saudi Arabia, for corn market – in Turkey, and wheat flour market – in China.

The planted area of winter crops has been significantly expanded for the new season in the southern regions of Russia (in Rostov and Volgograd regions). And this creates preconditions for the further increase in wheat exports in season 2018/19. IKAR estimates the supplies to foreign markets in the range of 33.5-38 MMT next season.

### Added value sources

A special session at the conference was devoted to a search of added value. However, the topic of added value was regularly discussed during almost all speeches at the forum. According to speakers and other participants of the conference, the added value can be obtained by arranging production and export of grain and oilseed processed products.

Moreover, the demand for processed grain and oilseed products is growing in the world market. This is a global trend, the presence of which was noted by the FAO representative. Over the past 5 years, the volume of such products world trade had increased by 19%, while sales of unprocessed cereals and oilseeds had risen by only 9%, said the FAO expert Dmitry Prikhodko. Currently cereals and oilseeds processed products account for 32% of the world trade (and raw materials – for 68%). According to the expert, in Ukraine this ratio is fundamentally different – the processed products account for only 8% of the country's grain and oilseed exports (excluding vegetable oils). Mr. Prikhodko concluded that the potential for the further growth of processed products export from Ukraine was enormous.

The Director General of the research bureau "Grain&Oilseeds" **Viktor Aslanov** told in details about earnings on flour in Kazakhstan – the world's second largest exporter of flour. According to the expert, over the past 5 years, the share of flour in grain exports of his country has increased from 34% to almost 46%. The increase in flour exports was achieved mainly owing to supplies to Afghanistan. During 2012-2016, Kazakhstan managed to increase flour supplies to this country by 400% - to 1492 KMT in 2016/17 MY. If earlier Afghanistan accounted for only 20-25% of Kazakh flour exports, last season the share was more than 60%. However, this export direction is noticeably slowing down due to competition with suppliers from



Uzbekistan. Due to lower costs of flour production, Uzbek exporters increased their shipments to Afghanistan by more than 100 times over the past 7 years. What is more, flour millers in Uzbekistan have significant competitive advantages – a short flour supplies run along with cheaper electricity and lower taxes when working on a tolling pattern. Those who are closer to raw materials not necessarily have higher earnings, believes Viktor Aslanov. In Kazakhstan, in some regions remote from the areas of grain production, millers earn as much as in the leading regions of the country.



The main volumes of Ukrainian flour are consumed inside the country. At the same time, its exports are growing as well. Over the last 5 years, flour exports have doubled. In the current marketing year, about 410-420 KMT of flour would be exported, which would guarantee Ukraine the fifth place in the world, reported the Director of Ukrainian Flour-Milling Company **Igor Kobelya**. However, there are no largest consumers of this product like Brazil, the European Union, China among the importers of Ukrainian flour, because these countries protect their markets very well, believes the expert.

According to Igor Kobelya, the main directions of domestic flour market development are the following – support of flour exporters at the interstate agreements level; unification of the major flour market players of the Black Sea region for the promotion of goods to new markets; increasing quotas for flour exports to developed countries or their abolition; no VAT charges on grain buy and sell operations, which will be further exported. The production of flour with vitamin and other additives is one of the ways to obtain additional profit by domestic flour millers, believes Igor Kobelya.



The Director General of Turkish company “AgriPro” **Faik Genc** spoke about the variety and positive dynamics of exports of Turkish grain processed products with high added value. According to Mr.Genc, in 2017 Turkey exported more than 3.5 MMT of wheat flour. In money terms the value exceeded USD 1 billion, which is equivalent to 23% of the world market. Now Turkey is the largest exporter of wheat flour in the world. Iraq, Sudan and Syria are the main importers of Turkish flour. Turkish also supplies flour to Angola, Madagascar, Indonesia and other countries where the country competes with Ukrainian flour.

The AgriPro expert focused on the fact that Turkey also exported many other grain processed products with even greater added value. By the end of 2017, the country had supplied USD 940 million worth of biscuits to foreign markets, USD 490 million worth of pasta, USD 104 million worth of bulgur and \$ 23 million worth of semolina. Moreover, "expensive" grain exports grow year by year. According to the estimates of Faik Genc, last year they reached the level of USD 2.6 billion. At the same time, earnings per one ton of pasta were 50% higher than those in flour market, and cookies turned out to be 6.7 times more profitable than flour.



The case of Bulgarian company “Agricore” shows that additional profit may be also obtained through the production and sales of organic products. Especially when establishing sales in the European Union, where the purchasing capacity of population is higher, said the director of Agricore **Petar Dimitrov**. According to the expert, such European countries as Germany, Italy, Spain, France are the largest consumers of organic products. The EU organic market capacity has already exceeded USD 30 billion. Bulgaria shows one of the fastest growth pace of organic market in the EU – the annual average increase in this country reaches 50%.

Organic business is nominally attractive. However, it is not so easy. It is rather difficult to get a high premium. For instance, some supermarkets reduce the attractiveness of organic products for consumers, setting a premium for organic tomatoes at 130% higher than that for conventional vegetables, and 165% higher for organic apples. The cultivation of popular crops, called "golden eggs" can also turn out to be a disappointment, as it happened with spelt production. It turned out that the demand for this crop was overestimated. It is better to produce traditional organic crops like wheat or corn, Petar Dimitrov believes.



The expert suggested farmers to pay special attention to not only the choice of crops and varieties for organic production, but also to crop rotation adhering in agriculture, and strongly advised to monitor production cost and market prices. At the same time, he did not recommend becoming "night farmers" and apply chemical fertilizers in organic fields at night and prevent other violations of the basic principles of organic farming, because the pesticides and herbicides can be detected during the check of finished products. *"Organic farming is not a panamax business. It's better to start with small volumes to objectively estimate the high risk of this type of activity"*, said Petar Dimitrov.

The representative of "Kesarev Consulting" Company **Aleksandr Sakharenko** encouraged ag market participants to comply with legislation when searching the added value. He explained the statement by high budget losses due to shadow markets. For example, the country's budget loses at least UAH 18.6 billion only because of the shadow market of land lease. The average losses are estimated at UAH 34-37 billion.

The partner of “AGA Partners” company **Ivan Kasynyuk** explained how to protect the profitability of agribusiness showing the case of a large trader. Great importance of all contract provisions, including the quality of supplied goods was the most important lesson of the case. *"If you want to include any item to contract to reduce taxes, you should understand that the fate can play a cruel joke, which will cost you USD 9 million"*, warned the lawyer.