

The Clover and Grass Seed Market - during and after the High Cereal Prices

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Cereal prices have nearly doubled during the last year. The reasons for this are both temporary and longterm. The cereal price is expected to have peaked by now, however, the price level will also in future be above the recent 10 year average. The high and unstable cereal prices also have an impact on the grass seed production - both directly and indirectly. The relationship between the price for cereal and clover/grass seed is very crucial in terms of future grass seed acreages. At the same time, clover and grass seed stocks in the EU are expected to decrease – and this will indeed cause prices to rise again. Reduced stocks, expectations that production will go down and a wish to have stable markets, will thus more or less re-establish the price relationship between cereal and clover and grass seed.

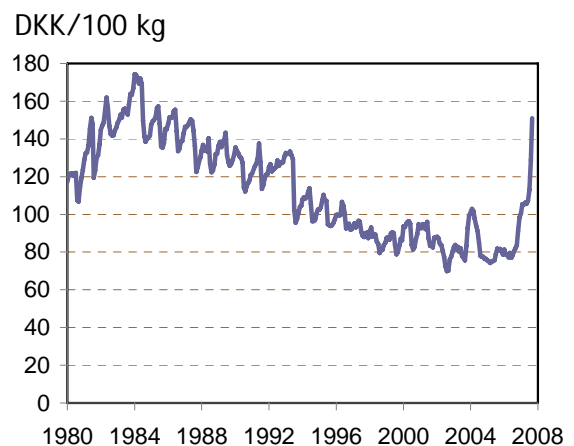
Cereal prices have doubled

Cereal prices – both on Danish and international markets – have increased dramatically during recent years.

The increase of prices vary from market to market, however 40-50 per cent increases can be seen many places. By the gradual elimination of agricultural import and export regulations, prices on the world market as well as on the national markets will become more and more alike.

In Denmark, cereal prices have doubled during the last six months, cf. Figure 1.

Figure 1. Development in Grower Sales Prices on forage barley in Denmark, 1980 Sept 2007



Note: Average invoiced prices.

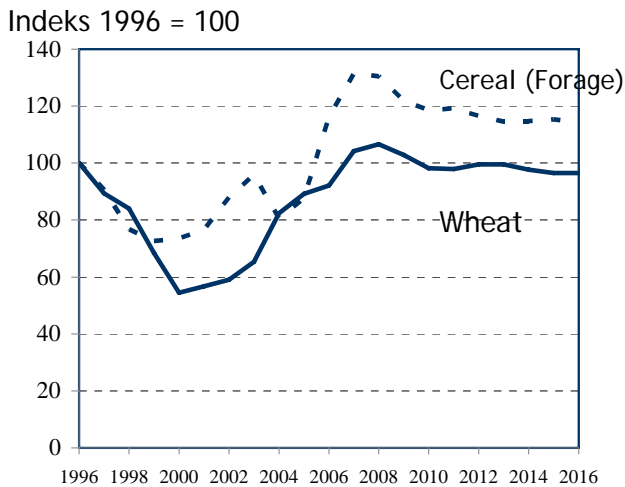
Source: Own production based on data from Dansk Landbrug (the organization Danish Agriculture).

As you will see from figure 1, there has been a dramatic increase compared to the last 20-25 years.

The International Cereal prices – today and in future

The development in international prices for fodder cereal and wheat is shown in figure 2, likewise showing a prognosis for the development until 2016.

Figure 2. World Cereal Prices 1996 – 2016



Source: OECD-FAO (2007)

The prognosis made by OECD and FAO in 2007, shows that cereal prices are likely to top this year, whereupon they will weaken gradually. The prices, however, will still be significantly above the level up to 2006. Of course, there are many uncertainties in connection with a prognosis for international cereal prices made 8 to 10 years ahead in time – especially when the figures you base your prognosis upon are influenced by great turbulence as regards temporary and structural market adjustments.

Why do Cereal Prices Increase?

There are several explanations to the question about increasing cereal prices.

Some causes are temporary or accidental, and their effect is likely to disappear within a short period of time.

Other causes are more longterm and structural, and they will most likely have an impact for a long period of time, and will thus be instrumental in terms of increasing cereal prices also in the long run.

These causes are :

Temporary/accidental Causes

- Poor harvest several places in the world, e.g. Australia and Europe. Drought has caused the Australian cereal crop, last year, to drop by 50 per cent compared to an average crop year.
- Very small stocks. Small stocks always mean higher prices, and big stocks mean lower prices.
- A boom in many countries – in average income countries for example – will increase the demand for foodstuffs, including particularly animal food.

Structural/longterm Causes

- Bioenergy means increasing demand for e.g. cereals.
- Long-lasting growth and increase in consumption in e.g. Asia and Central and Eastern Europe
- Higher energy prices influence on agricultural prices in an upward direction
- Agricultural policy deregulation. When restrictions in agricultural subsidiaries, based on production, are made at the same time as a reduction of supply, this will cause prices to rise.

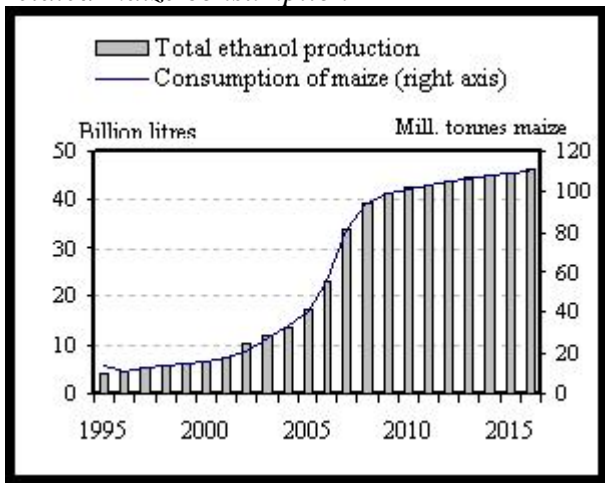
Bioenergy

Bioenergy is one of the main explanations as to why cereal prices are going up recently.

Bioenergy may also well be the reason why cereal prices in future will be at a relatively high level.

Countries like the US and Brazil have created a substantial production of ethanol, and this development is likely to continue in future.

Figure 3. The US ethanol production and related maize consumption



Source: OECD-FAO (2007)

Approx. 20 per cent of the maize production in the US will be used for bioenergy in 2007.

A series of other countries have also invested in an ethanol production based on agricultural goods.

In the EU, the consumption of bioenergy is to increase by 170 per cent in the period 2006-2010, and the growth is expected to continue in the coming years.

Also countries like China and Canada plan to increase their bioenergy production.

On top of this, many countries have a strong wish to become more independent in terms of importing oil from “insecure” regimes like the Middle East countries and Russia. Therefore you see a heavy political pressure in great many countries in order to boost the bioenergy development.

Bioenergy plant expansions are in some places kept on the low. Both in Europe and the US you see examples of investment projects being given up, and in several instances production sites have been closed down. The reason being solely the present, high cereal prices.

The development also shows, however, that the bioenergy industry will be instrumental in terms of securing minimum prices.

If the cereal prices drop dramatically, the bioenergy sector will, again, grow and the demand for cereals will increase, and thereby the cereal prices will not go back to their previous very low level.

All in all, you may conclude that there are both political (supply), environmental and agricultural interests at stake when it comes to the future development of bioenergy production.

The pros and cons change along with the development of new technologies, changed prices on cereal and energy, as well as the international financial and political situation.

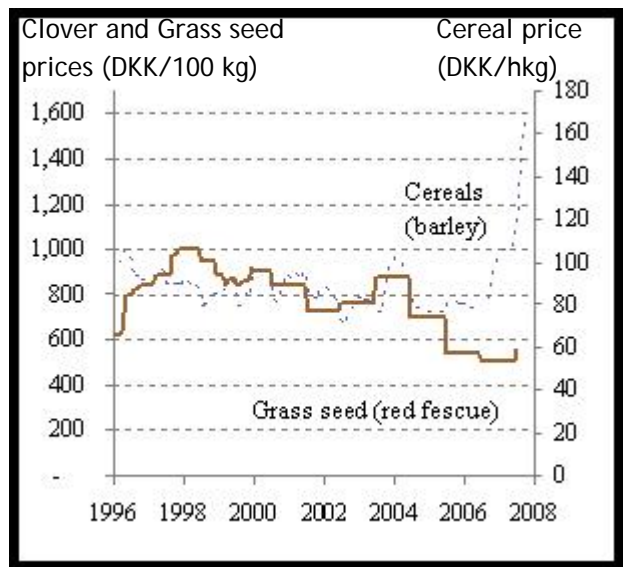
Regardless of all uncertainties it is a fact that the bioenergy production will put an upward pressure on cereal prices both in the short and long run.

Cereal and Grass Seed Prices

Eventhough cereals and grass seeds are used in very different ways, and are sold on different markets, the two products still influence significantly on one another.

The cereal and grass seed markets are thus affected indirectly by one another. Seen over the recent 10-12 years, cereal and grass seed prices have had the same trend, cf. figure 4.

Figure 4. Development in cereal and grass seed prices



Source: Own production based on data from Dansk Landbrug (the organization Danish Agriculture).

Cereal prices will affect clover and grass seeds prices

The increasing cereal prices will – both directly and indirectly as well as on a short term and long term – affect clover and grass seed prices.

Firstly, increases in cereal prices will make farmers produce more cereal and less clover and grass seed. Many farmers produce cereals as a direct substitute. The result will be less supply of clover and grass seed, which again will lead to price increases.

Secondly, most clover and grass seed companies wish to have a stable supply of clover and grass seeds. They have to make maximum use of their capacity, and longterm contracts and cooperation with customers must be maintained, and therefore the supply of raw material must not be reduced. The result will be increase in prices to maintain the interest of the farmers in producing clover and grass seed.

Thirdly, only few players on the grass seed market take interest in a great turbulence and very fluctuating prices. If the clover and grass seed prices do not follow – in part or completely – the result will be a decreasing supply. Such a decreasing supply will be followed by new price increases. The bigger decrease in supply, the bigger the subsequent price increases will be.

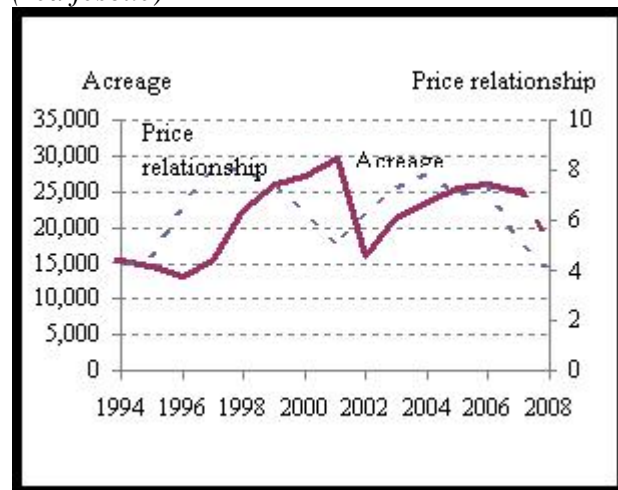
Increasing Cereal Prices alone Mean Reduced Clover and Grass Seed Acreages

That increasing cereal prices – without similar price increases in clover and grass seed – result in reduced acreages with clover and grass seed is not just pure theory.

You can actually see a clear connection by studying the historical development.

As you will see from figure 5, clover and grass seed prices that decrease relatively, compared to cereal prices, will entail a reduction in clover and grass seed acreages within the following 1 to 3 years.

Figure 5. Price relationship between clover and grass seed/cereal and acreages with grass seed (red fescue)



Source: Own production based on data from Dansk Landbrug (the organization Danish Agriculture).

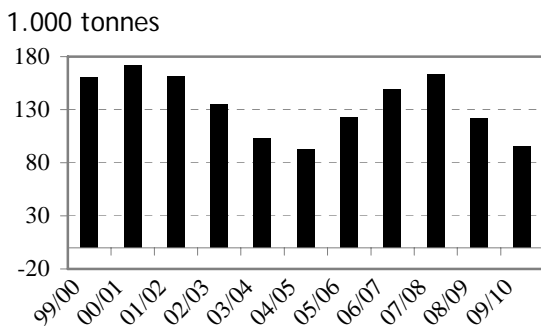
In the figure, the 2008 development is shown with unchanged clover and grass seed prices and extrapolated cereal prices. We may

therefore experience a substantial reduction of acreages in the years to come, if the prices for clover and grass seed remain unchanged compared to the present cereal price level.

EU Grass Seed Stocks will decrease in the coming years

The consumption of clover and grass seed is relatively stable from one year to another. When production, at the same time, is likely to drop in the years to come, the EU-stocks of clover and grass seed will go down by nearly 50 per cent within the next 2 years, cf. figure 6.

Figure 6. EU-stocks with clover and grass seed including a 2009/10 prognosis.



Source::Markedsdata and own calculations

Therefore, the production cycle has probably peaked by now, and the consumption in the coming years will by far exceed the production.

Stock Volume Affects the Prices

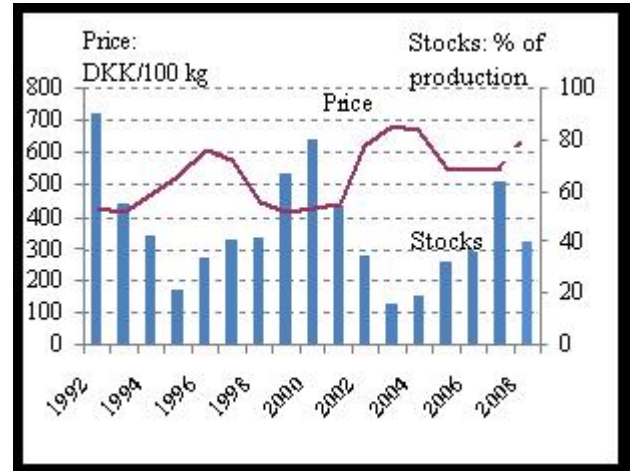
The volume of the stocks is one of the main reasons for the price development of both clover and grass seed and cereals.

If the stocks are big, there will be a buffer on the market, keeping the prices down. The players on the market know that if the prices are likely to go up, you can use your stocks and thereby increase supply.

On the other hand, small stocks will make prices go up. You do not have the usual buffer

to even out fluctuation in prices, and this will make an upward pressure on the prices. The development throughout recent years shows this clearly, cf. figure 7.

Figure 7. Stocks and Prices for Grass Seed (Perennial ryegrass in Denmark)



Note: 2008 = prognosis

Source: Own figures based on data from Danish Seed Council.

The development shows the perennial ryegrass market in Denmark, however, a similar connection can be found in many other countries.

The figure clearly shows that the size of the stocks has a major impact on the price development.

Since the EU-stocks are expected to go down, there will be a pressure in terms of increasing clover and grass seed prices.

Conclusion

Recent price increases on cereals have turned many market conditions in the agricultural sector up side down.

The cereal production has had a remarkable profit performance, whereas the livestock production, for instance, in many places suffers from the fact that fodder prices have increased,

as a result of the increase in cereals, however this has not lead to higher prices on animal foodstuffs.

Produces that can be substituted by cereals, will of course be under pressure, since it will be relatively more attractive to produce cereals.

Eventhough cereals and clover and grass seed are sold on different and separate markets, the increasing cereal prices will no doubt, before or later, influence on the clover and grass seed prices. A new market balance will make clover and grass seed prices go up. This seen together with decreasing stocks of clover and grass seed in the EU, we are likely to see, very soon, a positive development in prices.

Sources: OECD-FAO (2007): Agricultural Outlook. 2007-2016.