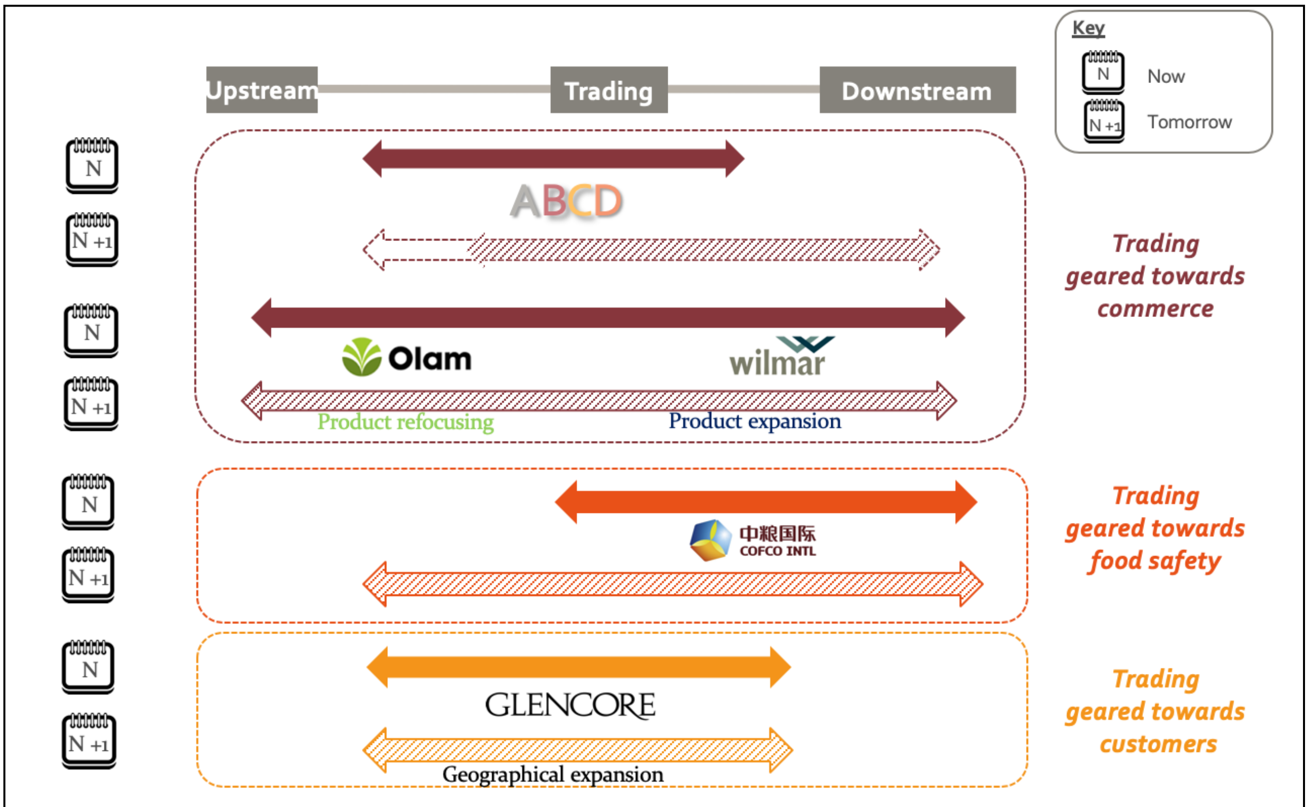
International agricultural trading: A model in question

The physiognomy and purpose of international agricultural trading are changing



Source: Unigrains

➢ International grain trading is no longer profitable

Traditionally, international trading companies generate profits from two activities: commercial, by providing services, and speculative, through good - or sometimes bad - market timing in arbitrage operations.

Several factors are now contributing to a deterioration in profitability:

- About five years ago international grain trading entered a phase characterized by low prices and volatility, which limit arbitrage opportunities.
- New technologies are now providing widespread access to information. In this context the trading companies, which until then had kept one step ahead thanks to their "sensors" across the globe, are losing a key competitive advantage.
- In recent years, significant investments have been made in both inland and port silos as well as in crushing capacity. This has led to infrastructure and production overcapacity, and thus *de facto* to falling profits.
- Following the 2008 financial crisis and the 2011 food crisis, a number of government authorities, including the US and Europe, took measures to limit speculative moves on financial markets while improving their transparency.

Moreover, politics is moving back to the forefront, challenging free trade and rendering profit generation more uncertain and less arbitrable.

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The sector is becoming increasingly competitive

Historical players include companies mostly founded in the 19th century, the so-called ABCDs* and the big Japanese conglomerates (*"sogo shosha").* New operators are now emerging, with varied profiles and trajectories.

These new market players include:

- Non-agricultural commodity trading companies moving into agricultural products. A case in point is Glencore with its acquisition of Viterra, and more recently South Korea's Posco Daewoo with the acquisition of a port terminal in Ukraine.
- Asian companies with a very advanced vertical integration model such as Singapore's Olam, and Wilmar. Another example is Cofco, a Chinese public conglomerate formed through the acquisition of the historical operators Nidera and Noble.
- Upstream agricultural companies which, as they grow in scale, no longer require intermediaries: cooperatives like CHS (United States), Zen Noh (Japan), BayWa (Germany), or the French family-run company Soufflet.

New threats are emerging with trade digitisation and consumers' growing requirement for transparency

The advent of digital technology has led to the emergence of new players managing platforms that directly connect producers and users. Although they have only local influence, they represent a threat:

- Immediate, as they compete with the ABCDs in their origination activity. For example, 12% of the North American grain now reportedly trade through Farmlead, a Canadian online market place.
- In the medium term, should they be interested in international trading, with the help of blockchain technology.

At the other end of the value chain, the trading companies' clients are keen to meet consumers' growing demand for supply chain transparency. For example, Nestlé recently announced it would disclose a list of suppliers alongside a variety of data of its 15 priority commodities, ie 95% of its annual sourcing raw materials. Furthermore, a growing number of food manufacturers are giving priority to local supplies.

New features are now associated with international trading

Some operators no longer consider international trading as a possible core business. They still see it as a necessary backbone for the trading in finished and semi-finished products, but only as part of a vertically integrated supply chain. The ABCDs are deeply transforming their business models in this direction (see In Brief: "The ABCDs' transformation: how far will downstream integration go?"). For others, first and foremost Cofco, the main purpose of its international trading activity is to ensure food security for a whole country, i.e. China.

Some other players still believe in pure international trading in agricultural commodities as a stand-alone business. For Glencore, operational excellence is to be reached through a presence in all major trade flows.

In any case, new features are now associated with international trading. They enable the traders to restore their leading positions by recreating barriers to entry. The latter are all the more efficient that:

- The trader is positioned in niche or speciality markets, in which product prices only have a few benchmarks and where relationships are mostly over-the-counter,
- It can offer customised services,
- And it can prove that its supply chain is sustainable and transparent.

This In Brief is based on a June 2019 study entitled: "International grain trading: what's next for the ABCDs?", available in restricted access on the www.unigrains.fr website.

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