Rabobank

New Global Poultry Trade Reality

Slow Growth and High Risk Require New Market Strategies

RaboResearch
Food & Agribusiness
far.rabobank.com

Nan-Dirk Mulder
Senior Analyst – Animal Protein
+31 30 712 38 22

Matz Beuchel
Associate Analyst – Animal Protein
+31 64 697 40 45

Contents

Summary

- Since 2011, global poultry markets have moved to a new reality of slower growth and higher volatility. Global poultry growth has fallen to only 1 percent to 2 percent per year, and the share of trade in global markets has fallen from 11.5 percent to 10.9 percent – the first drop in many decades. This is a reflection of a new reality in global markets.
- Global trade has increasingly been challenged by ongoing avian influenza threats, rising protectionism, changing standards in import markets, as well as local supply issues in exporting countries, such as China and Brazil, making trade significantly more complex.
- Rabobank expects markets to change even further in the coming years. Specifically, we see more growth in emerging markets, which will essentially be locally supplied, and we see growing supply from relatively new exporters, such as Russia, Ukraine, and Vietnam, which will capture some share of trade from existing exporters.
- Poultry companies should rethink their strategies in this new poultry trade reality. We see four strategies that are well-suited to the new market reality:
    1. shifting emphasis to growth in local markets
    2. investing in new export markets
    3. focusing on the fastest-growing, high-value trade markets for processed poultry
    4. establishing leadership on changing social and customer concerns to secure trade access
- These are some of the conclusions based on Rabobank's new 2018 Global Poultry Map, which provides an updated overview of global poultry trade.

New trade reality: slower growth, higher risks

Global poultry trade represented a market of USD 22.5bn in 2017, which is 2.5 percent larger than the value of trade in 2011 (the reference year for the prior Rabobank Global Poultry Map). In terms of volume, global poultry trade has grown by only 9 percent to 12.9m tonnes since 2011, which is significantly lower than the growth in global poultry demand (up 13 percent in 2017 compared to 2011) and also significantly lower than the pre-2011 6 percent YOY average growth in global poultry trade. The slower growth in trade value is mainly caused by a reduction in poultry prices since 2011, due to lower feed costs, and (partly) due to exchange rate volatility. The reference year, 2011, was in the middle of the agri-commodity price hike years, with high prices for feed, which have dropped significantly since 2013.

Despite the recent slowdown in growth, poultry meat is still the world's most traded meat protein, with a market share of around 41 percent in the global 31m-tonne meat-trade market. Within poultry, chicken is by far the most important traded poultry species with a total value of USD 21.2bn, followed by turkey (USD 1.2bn, up 2 percent in 2017 versus 2011) and duck (USD 240m, up 24 percent in 2017 versus 2011).

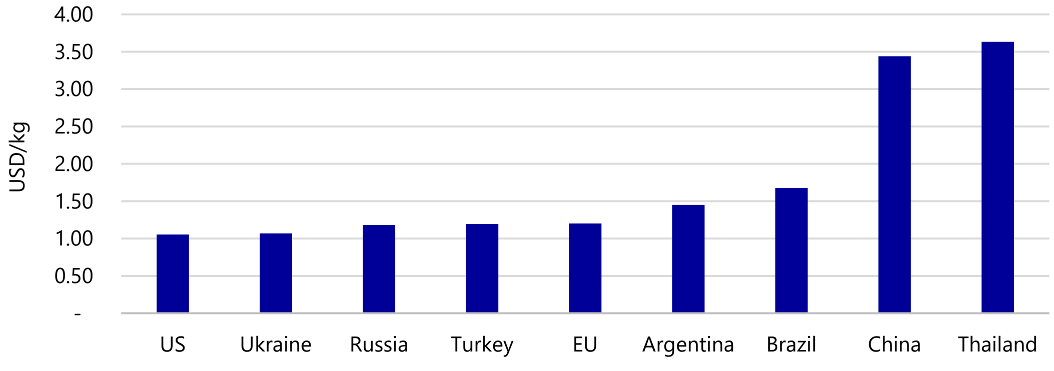
This slower and more volatile growth in global poultry trade is caused by a number of factors. The most important is the negative growth in the Chinese poultry market – the only large poultry market worldwide which has declined in the last few years – mainly due to disease issues and some scandals, for example relating to the use of antibiotics. China has also gradually increased import restrictions in response to avian influenza (AI) outbreaks in exporting countries (like the US and the EU) and more recently imposed anti-dumping measurements on some imports (from Brazil). Russia's move from being one of the world's biggest importers to a net-export position is also important, as it has led to the near disappearance of Russia as a big global poultry importer from the market. The Middle East is still an important import region, but several countries, like Saudi Arabia and the Gulf States have implemented food security programmes to strengthen the local industry. This negatively impacts global trade, especially as halal import standards are also changing in some Middle Eastern countries like Saudi Arabia and the United Arab Emirates (UAE), which makes exports to the Middle East more difficult.

From a supply position, the situation has also changed. AI has become a business risk in most regions of the world (i.e. Europe, Asia, Africa, and North America). This has greatly impacted global trade streams and led to massive volatility in global markets. Exporting countries have been banned from exports after outbreaks were found in a country or region. Returning to trade can take a long time, although officially a ban should be lifted three months after the last outbreak. Scandals also impacted global trade. China's poultry trade, for example, has been challenged a few times by food safety issues, while the weak flesh investigation in Brazil has affected Brazil's reputation in international markets and indirectly in trade. Some major trade streams like EU-South Africa, Brazil-China and US-China have also been significantly reduced by a diverse set of restrictive factors.

New alternative markets have been found, especially in Sub-Saharan Africa, the Philippines, Vietnam, and Cuba, but not enough to keep to keep global markets in the same fast growth path as in the past, with annual growth levels of above 6 percent YOY.

Key exporters like Brazil (down 14 percent 2017 versus 2011 value-based), the United States (down 17 percent) and Argentina (down 40 percent) have all been struggling under these challenging global market conditions. Other exporters are doing better: Thailand (up 40 percent 2017 versus 2011 value-based; leadership in value-added), EU (up 50 percent; improved market access), Ukraine (up 400 percent; low-cost leadership), Turkey (up 20 percent; access to Middle East) and Russia (from almost no imports). Thailand has now reached an export value of USD 3bn, which comes very close to the export value of the US industry of USD 3.6bn. Thailand is the clear leader in the processed chicken market, which has led to the situation that Thailand exports the most expensive chicken in the world on average (USD 3.60/kg), not far from its main competitor China (USD 3.40/kg) (*see Figure 1*). The US and Ukraine sell the least expensive chicken on average (USD 1/kg), followed by the EU (USD 1.20/kg) and Brazil (USD 1.60/kg), thanks to a more diversified export portfolio including processed chicken and breast meat exports.

Figure 1: Export value per country, 2017



Source: Rabobank analysis based on Comtrade, Eurostat, USDA, 2018

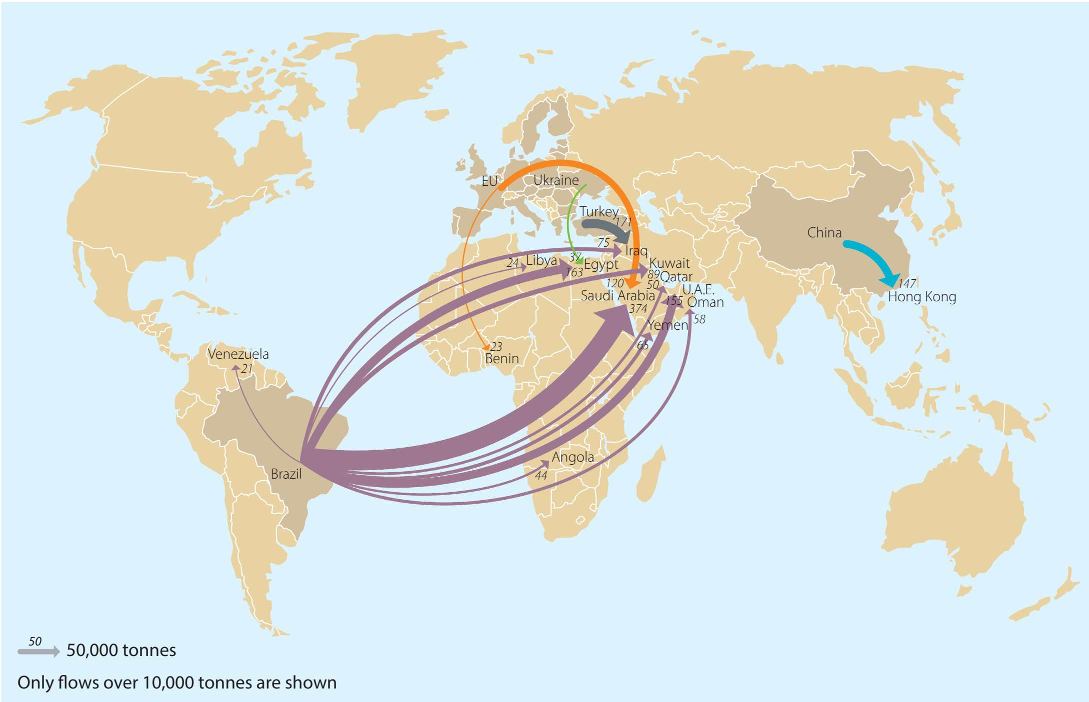
Key trade segments: opportunities for newcomers

To better understand changing dynamics, it is important to split the global market into four key categories: whole chicken meat, white chicken meat, processed meat, and dark meat. Each of these markets has their own dynamics and operates quite independently from the others. Trade in each category is influenced by cost of production factors like live broiler costs, processing costs, and differences in consumer preference.

Whole chicken meat trade: new market requirements and new players challenge Brazil's dominance

The whole chicken market is a market of 1.8m tonnes, dominated by Brazil, which has a market share of 65 percent in global trade (excluding China-Hong Kong trade) followed by the EU and Turkey, both with a market share of 10 percent (*see Figure 2*). The Middle East is the most important market for whole birds, but there is also a significant China-Hong Kong trade flow. Being competitive in this market depends very much on the cost of production and speed to supply the market (China has big benefits in supplying Hong Kong, and Turkey in supplying the Iraq market). Brazil is still the most competitive country in terms of cost of production. From this cost advantage, it has built a strong positon in the Middle East. In the past, the EU was a major player in this category, but after the removal of export subsidies, the EU gradually lost its leadership position in the Middle East.

Figure 2: Global whole-bird trade shows Brazil's dominance, 2017



Source: Rabobank analysis based on Comtrade, Eurostat, USDA, 2018

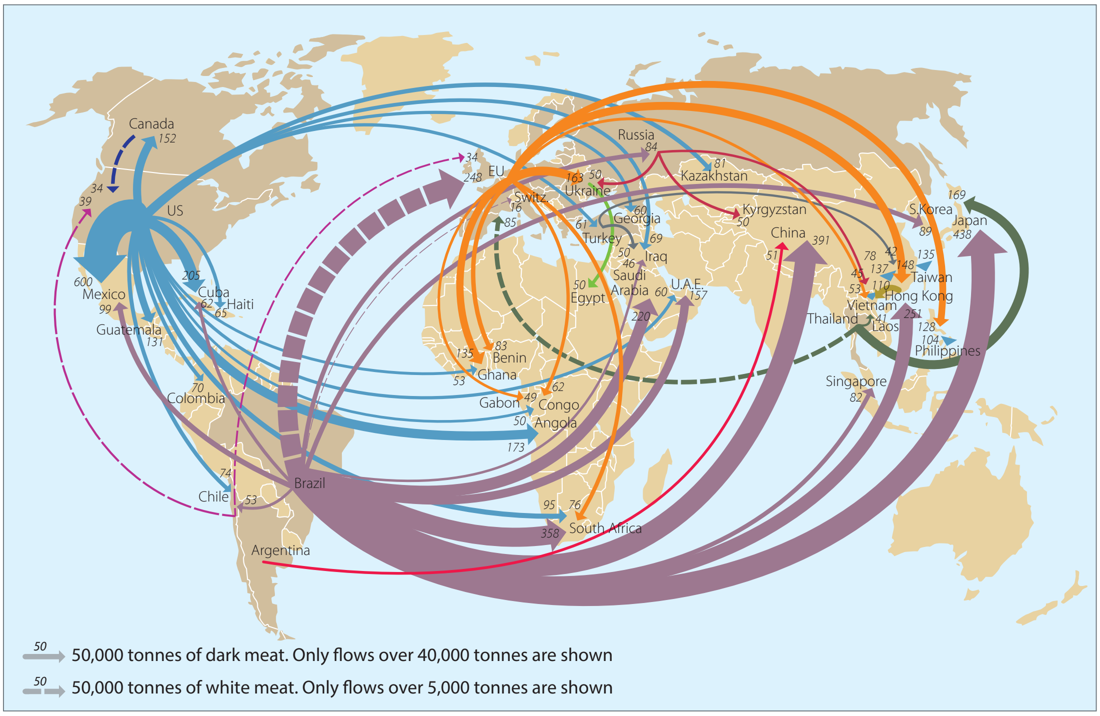
Supplying the Middle Eastern whole-bird market has become more challenging after the introduction of new halal standards in Saudi Arabia and the UAE in 2018, with stunning no longer allowed. This will remain a complication for suppliers to Middle Eastern markets as it requires an adjustment in the production process. Furthermore, governments in Middle Eastern countries have set strategic food security ambitions, which means rising local production, especially in Saudi Arabia but also in the gulf states.

Having said this, the whole-bird Middle Eastern market will remain an important market and import volumes will gradually keep rising although not at the speed of five years ago, as the emphasis on local supply is rising. Brazil will remain the leader but competition will increase some, especially from Ukraine and Russia in the next few years. Turkey will keep its regional role in supplying neighbouring markets in the Middle East.

White meat market: very much EU-focused due to limited access to other Western markets

The white meat/chicken breast market is a very EU-focused market (and therefore relatively small at 650,000 tonnes) as this is the only major western market which has opened up for sizeable imports of breast meat (*see Figure 3*). Other potential import markets for breast meat, like the US, Australia, New Zealand, and Canada, have all almost fully closed for imports of breast meat. The US has created a small opening for breast meat imports from Chile, but volumes of 75,000 tonnes in 2017 can be considered relatively limited. The Brazil-EU and Thailand-EU trade streams are still the main trade streams for this market segment and for both countries this is also the most valuable raw chicken-meat market. This is why the recent removal of 20 Brazilian export plants from the EU approval list had such a big impact on this market – there are very few alternative open white-meat markets which pay similar prices for breast meat as the EU.

Figure 3: Global white and dark meat trade, 2017



Source: Rabobank analysis based on Comtrade, Eurostat, USDA, 2018

Unless other markets open (more) in the near future, the white chicken meat market will remain focused on the EU. Total import volumes in the EU are restricted by quotas, which supports a view that trade in breast meat will show relatively limited market growth in the next years, especially as no openings are expected in market access to other potential importers of breast meat. Key for future trade will be whether Brazil is able to regain confidence with authorities and traders for exports to the EU. Ukraine and possibly Russia will become more significant players in this market. Ukraine has the potential to produce fresh chicken near the EU market and benefits from a distance advantage compared to Brazil and Thailand. Fresh chicken is a significantly more expensive product in the EU (15 percent to 20 percent more expensive) and Ukraine would be the only non-EU supplier that can competitively supply breast meat in the EU. Even though the EU restricts trade by quotas, Ukraine increasingly exports out-of-quota to the EU.

Dark meat market: more focus on Asia and Africa

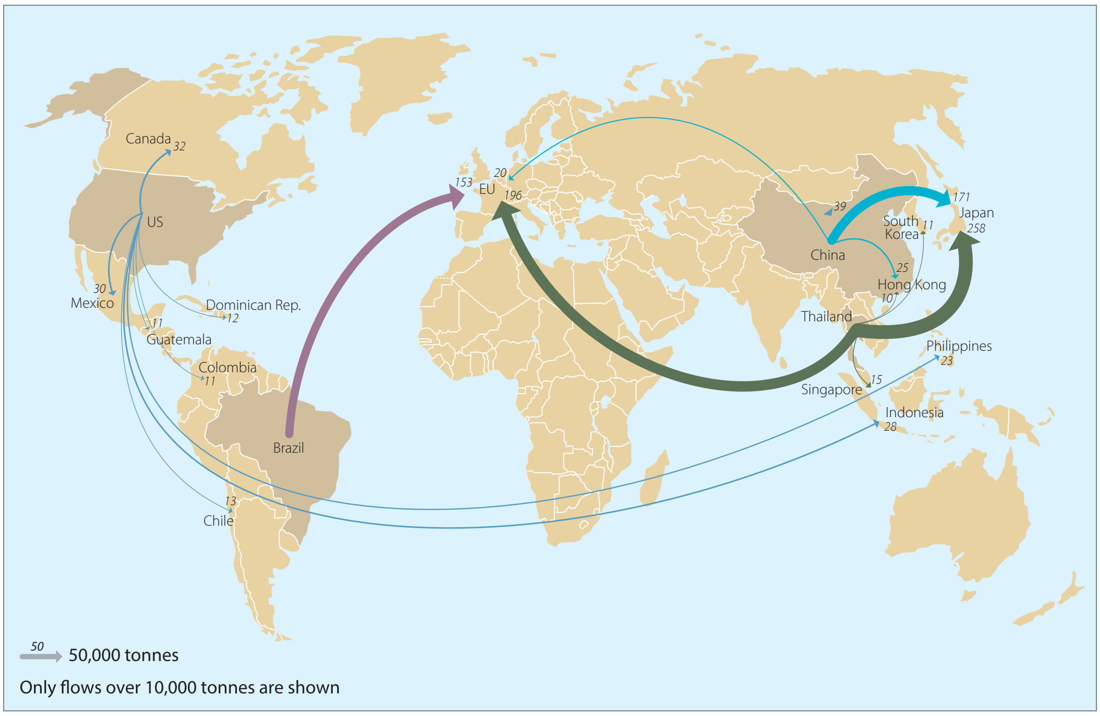
Dark meat trade in legs, wings, and chicken feet is dominated by Brazil (with a market share of 25 percent), US (with a market share of 28 percent) and EU (with a market share of market share of 13 percent), while countries like Russia and Ukraine are newcomers in this market and have been increasing their share in the market to respectively 3 percent and 2 percent (*see Figure 3)*. Traditionally, this market – sized at 11m tonnes – has always focused on optimising global demand preferences, and is therefore supportive to the white chicken meat market. Western markets tend to prefer white chicken meat (breast meat/fillets) and Asian, Latin American, and African consumers prefer dark meat. These preferences are also seen in local price differences and provide a strong base for trade. Western companies, especially from the US and the EU, try to sell their dark meat at more attractive price points to Africa and Asia, while Thailand for example sells breast meat into the EU. Dark meat trade streams are moving more to Asia (China/Hong Kong, Japan, Vietnam, and the Philippines), the Middle East (Saudi Arabia and the UAE) and Africa (Angola, Benin, Ghana and South Africa).

As the dark meat market is very much a supply-driven market, it can be expected that this market will keep growing in the coming years, and that availability from traditional suppliers (the US, Brazil, and the EU) will keep growing in line with their rising production. The challenge will be to keep adequate market access to match rising supply, which needs new market openings to keep price parity in global markets. We expect the focus to shift further towards Asia, where some of the leading exporters have been focused on opening markets, such as Indonesia and India, and increasingly Africa. As more than 90 percent of global poultry market growth is in emerging markets, and 65 percent of growth is in Asia, global markets are increasingly moving to an area where dark meat is the preferred product among consumers, making this a major driver for future trade streams.

Processed chicken meat: high-value market keeps growing

The processed chicken market is a 1.1m-tonne market (and with prices of over USD 4/kg also the most expensive poultry market). This market has been growing gradually and trade is traditionally dominated by Thailand and China and to a lesser extent Brazil (*see Figure 4*). Thailand and China benefit from their low cost, highly-skilled labour advantages, which allow them to produce tailor-made labour-intensive products for high-value markets like the EU and Japan. The demand in Japan has been growing in recent years and this has been a major growth driver for the Thai poultry industry. In Japan, China is the main competitor for Thailand in this high-value segment. Brazil has never been successful in developing this market due to its long distance from Japan. The EU market has Thailand and Brazil, who both have access to the market via quotas, while China can only sell in the EU market via a smaller 'other country' quota. Other potential large markets for processed chicken, like the US, Canada, Australia, and New Zealand, are very restrictive with access and in practice do not accept processed poultry imports. Therefore, new market development is focused on smaller high-income markets in Asia, like South Korea, Singapore and Hong Kong, and in the Middle East.

Figure 4: Global poultry processed meat trade, 2017



Source: Rabobank analysis based on Comtrade, Eurostat, USDA, 2018

This will also be the direction for future trade in processed chicken meat. The market will gradually grow as demand for processed poultry keeps growing in international markets and access into these high-value Asian markets gradually improves. Larger growth could be realised if some of the other Western markets open up to imports of processed chicken. China has tried to open the US market but has failed so far.

Another challenge will be related to cost changes in supplying countries. Rising labour costs and limited availability of labour in key countries like China and Thailand are challenging their market position. High dependence on only two or three countries, together with some food safety issues with Chinese imports in the past, has led to a rising interest among importers to diversify their import base, and this will be a driver for change in the coming years. Traders from key import markets are looking for ways to diversify imports and have started to exploit opportunities in potential new exporting countries – sourcing more products for processed poultry. This creates opportunities, especially for Vietnam and, to a lesser extent, the Philippines and India. Building up such a position is not an easy task, as high standards mean high entrance barriers for newcomers into this market. Exporters of processed poultry products usually dedicate specific products for trading houses, processors or retailers, requiring a high level of investment in technology, distribution, and product development. This is different from the poultry raw-meat market, which is more of a bulk market.

Changing market conditions require new strategies

In the coming years, we expect growth in global poultry trade volumes to remain slow – AI will be an ongoing threat for the industry, protectionism is expected to stay for a while, China's growth will stay relatively limited, Russia will become a more dominant exporter, and supply issues in some exporting countries haven't been resolved yet. Fast-growing poultry markets like Indonesia, India, Malaysia, and Colombia are not open for imports. Western markets will keep restricting imports in their high-value white and processed chicken markets. A major trend for the coming years for traders will be further changes to standards in import markets, based on social concerns like sustainability, animal welfare, and country of origin. These changes will come from both governments and from market parties. Examples of such trends are slow-growing birds, GMO-free feed, antibiotics-free production, locally-produced chickens, but also a strict reduction and monitoring of zoonotic diseases like Salmonella and Campylobacter.

Global poultry companies will need to be prepared for these changes and also ready to anticipate new areas in which trade will become slower and more complex than in the past. We have identified four strategic ideas to guide global poultry companies in their response to the new reality in global trade.

1. Companies should refocus from 'exports only' to a more global approach with strong local market growth access

Global market growth is moving towards emerging markets – 90 percent of global growth is here and 65 percent of growth is in Asia. New opportunities are increasing but, unfortunately for traders, most of the fast-growing new markets are closed to trade (e.g. Indonesia, India, Myanmar, Pakistan, Bangladesh and East Africa). So an export-focused strategy is not going to deliver the same growth in global markets as it has offered in the past. In the coming five years, we therefore expect more international companies to shift focus from being 'exporter only' to becoming a direct investor in the fast-growing markets. This will impact future trade streams and will put an emphasis on the short- to mid-term trend of moving from global trade to local production growth.

2. Exporters should invest in alternative export platforms as trade flows become more international

Global trade volume growth is slowing down and trade risks are rising. Importers are increasingly concerned about potential supply shocks due to, among other things, AI outbreaks and geopolitical trade tensions. These factors are leading to a more international, less concentrated supply of poultry in international markets. For global companies, this presents an opportunity to invest in export platforms that diversify origins and reduce risks, and create more flexibility in global trade. This new reality is also a unique opportunity for newcomers in countries like Russia, Ukraine, and Vietnam to enter the global trade landscape. Russia and Ukraine will be well positioned to supply in the raw-chicken segments, like whole chicken or dark meat, because of their low input costs (both countries are major grain exporters). Vietnam has opportunities to supply the processed chicken market where it can leverage its competitive feed grain supply and availability of low-cost labour to produce labour-intensive poultry products. Global companies will increasingly take leadership here, by teaming up with local players or by setting up greenfield projects.

3. Companies should add value by investing in the growing processed poultry trade market

Global meat companies are increasingly focused on supplying value-added products. In the case of poultry, there are big differences in the value of different poultry trade streams. This ranges from only USD 1,000/tonne for US poultry exports of dark meat, to over USD 4,000/tonne for processed poultry from Thailand. Investing in the high-value processed poultry segment is a logical business strategy for poultry companies. This market segment has performed well in recent years – it has been the only segment with significant growth in value and volume. This is demonstrated for example by the solid Chinese position, held even despite some scandals in the past, and the ongoing growth of the Thai processed-poultry export position. The US has also developed a niche position in supplying Central America with processed poultry. In the coming years, we see more emphasis being placed on this market segment, which will lead to the growing presence of international companies in countries like Thailand and China, but also in new supply countries.

4. Exporters always need to be ahead of the market in terms of changing market requirements

Importing countries and customers are increasingly adjusting production standards in line with rising consumer and social concerns. Social concerns will keep rising in the coming years; sustainability and animal welfare, and locally-produced chicken, are all trends which will be on the rise. Furthermore, supplying 100 percent safe food is clearly a fundamental requirement for any company in the business and no concessions can be made here. Exporting companies will need to follow relevant developments in their export destinations. For global companies, there is a case for investing in leadership in this area, to balance out the trust that is often given to local industries. As these social issues will only increase, the position of traders will certainly not become easier (as they operate from a longer distance from the market), but this is also an important opportunity for companies that could take leadership here. It will likely also require more direct investment from big exporters into their destination markets to allow them to get closer to their final customers.

The future: ongoing change in global markets and winners need to optimise their business models

The next global trade map will look very different from this one. Trade will keep growing, but the growth will slow and become more volatile and complex. Volatility will be caused by AI, geopolitical tensions, trade policy changes, increased competition in trade flows, and changes in market standards, among other things. All of these changes will likely require adjustments in the business models adopted by exporters. Newcomers in global trade will rise and help to make global trade streams more flexible, also reducing risks from potential volatility.

We think these fast-changing market conditions will require a refocus of any company active in global trade. Companies should rethink how they operate and whether an export focus is still adequate under these fast-changing market conditions. There is no 'one size fits all' solution, and much depends on the specific position of each company. Rabobank has identified four key considerations for global traders in adapting their business model to the new market reality. One thing however is for sure: markets will keep changing and only those companies that are ahead of the market will stay competitive in the longer term.

Imprint

RaboResearch
Food & Agribusiness
far.rabobank.com

Nan-Dirk Mulder	Senior Analyst – Animal Protein	nan-dirk.mulder@rabobank.com +31 30 712 38 22
Matz Beuchel	Associate Analyst – Animal Protein	matz.beuchel@rabobank.com +31 64 697 40 45

Banking for Food