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Outlook 2018: Promising Outlook but Rising AI Concerns Require Supply Growth Discipline

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The outlook for the global poultry industry in 2018 is promising, with relatively positive fundamentals. This includes ongoing demand growth in most markets, except China, and low(er) feed prices in 1H 2018, if not longer. The main concerns for 2018 are a return of avian influenza (AI) during the Northern Hemisphere winter and the increasingly competitive market conditions due to rising red meat supply. Given these growing but uncertain and more competitive market conditions, supply discipline will be important.

China's industry is struggling, with winter rapidly approaching and many wet markets yet to be closed. This situation could negatively affect prices and global trade. The industry needs to further reduce supply to rebalance supply and demand.

The Brazilian industry is recovering from the 'weak flesh' meat scandal and exports have returned to 2016 levels after significant drops in Q2 and Q3, but the risk of Brazilian imports being substituted by new suppliers remains.

Global prices for chicken have remained strong, especially for whole chicken and breast meat, but dark meat has fallen. Competition from red meat will grow next year, on rising supply and softening prices. This will require a more disciplined supply strategy in the poultry industry.

Global poultry trade will again be hit by volatility driven by AI, exchange rate volatility, and changes in traders' procurement strategies, in response to earlier scandals in trade. New suppliers will continue to enter the market.

Global chicken monitor* Q1 2015-Q4 2017f

Whole chicken



Breast meat



Leg quarters



* Chicken price trend for cuts entering global trade

Outlook for 2018: strong fundamentals, but with AI and oversupply concerns

US: Growth but in a more competitive market



- Production up 1.8% with strong exports
- More competitive red meat supply with lower prices
- Feed costs expected to be favourable

Brazil: Gradual recovery after meat scandal



- Improved domestic market conditions
- Export demand moves back to pre-crisis levels
- Some price concerns on lower second corn crop

EU: Ongoing positive margins despite AI worries



- Ongoing strong demand (+1.6%) and rising exports despite 1H AI restrictions
- Further shift east for low-cost production, while the west focuses more on concepts
- New AI concerns in the upcoming winter season

China: Sluggish demand drags production down



- Chinese poultry industry is turning around with ongoing AI pressure at wet markets
- Prices remain low despite improved restaurant sales
- Weak domestic demand will push the industry to further reduce production

Global outlook 2018

Promising market outlook, provided supply growth is disciplined

The outlook for the global industry for 2018 is promising, but a disciplined supply growth strategy will be needed, especially as uncertainties are rising.

Global poultry is facing 2018 with below-average market growth, of only 1.3%, due to ongoing difficult market conditions in China, where poultry demand is again predicted to decline by 4%. Other markets show good growth continuing, especially South-East Asia and Africa, where many markets look set to grow by more than 5% per year.

The industry will face ongoing avian influenza (AI) pressure. AI has become a new business reality and companies in high-risk areas should, and most have, adjust their business models and strategies to this reality.

The key fundamentals look reasonably promising for most markets, with ongoing growth and ongoing low(er) feed prices—especially in 1H 2018—on an expected

good crop outlook for the Southern Hemisphere, in combination with current high stock levels.

The biggest risk for the poultry industry in 1H 2018 will be new AI outbreaks in the Northern Hemisphere, which could shake up global trade streams, as happened in 2016 in the US, and in 2017 in Europe and Asia. Other risks are the rising supply of competitive meats and declining prices.

In these more challenging market conditions, disciplined growth can strengthen the industry outlook.

Stronger fundamentals, keep margins up

At the end of 2017, the global poultry industry is generally performing well, although some regions are entering an oversupply situation.

The best performing regions are currently United States, South Africa, EU, India, and Japan, while industries in Russia and Thailand have recently entered a situation of oversupply after overly optimistic expansion in response to strong market conditions earlier this year.

Brazil is gradually returning to profit after the 'weak flesh' scandal in 1H 2017 led to a poor period, with low exports due to lost confidence and weak domestic market

Table 1: Global live broiler and feed ingredient monitor, Q1 2016-Q4 2018f

		2016				2017				2018				Change	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4f	Q1f	Q2f	Q3f	Q4f	Q3-Q2	Q4-Q3
Live broilers USD/kg	EU	0.99	1.05	1.06	0.99	0.97	1.01	1.09	1.09					+1%	0%
	Brazil	0.70	0.76	0.95	0.93	0.85	0.78	0.79	0.83					0%	+5%
	China	1.18	1.22	1.20	1.08	0.71	0.93	1.07	1.01					+12%	-6%
Grains & oilseeds	Wheat (USD/bu)	466	471	406	403	429	435	466	440	450	470	460	470	+7%	-6%
	Corn (USD/bu)	363	391	332	348	364	368	365	350	365	380	400	390	-1%	-4%
	Soymeal (USD/tonne)	267	356	337	311	330	307	311	315	315	320	325	315	+1%	+1%

Source: Eurostat, Food and Agriculture Organization of the United Nations, national statistics, UBABEF, Rabobank 2017

Table 2: Global whole chicken and chicken cut markets (USD/100kg), Q1 2015-Q4 2017

		2015				2016				2017				Change	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4f	Q3-Q2	Q4-Q3
Whole chickens	Brazil wholesale	125.4	116.9	106.1	107.4	100.5	106.5	134.5	136.4	119.7	112.8	109.4	114.2	-3%	+4%
	EU wholesale	210.3	210.5	212.6	199.3	197.0	203.5	198.1	188.7	189.0	200.6	216.0	213.4	+8%	-1%
Breast meat	EU import price	257.5	253.7	235.2	223.2	222.1	207.4	204.1	191.2	193.6	219.3	240.0	252.1	+9%	+5%
	Thailand	328.4	340.3	320.1	273.5	268.2	248.8	243.6	244.2	243.5	233.6	257.9	274.2	+10%	+6%
Leg quarters	US leg quarters, north-east	84.7	70.3	55.8	52.0	60.5	73.5	73.7	72.2	75.5	87.7	93.2	82.5	+7%	-12%
	Japan import price	180.2	176.5	177.6	170.5	191.5	157.7	168.0	185.9	167.1	171.0	157.3	155.0	-8%	-2%
Feet	China import price	160.0	211.1	224.4	221.6	202.5	204.5	217.7	220.1	220.1	215.2	218.3	207.3	+1%	-5%
Processed chicken	EU import price	302.3	301.6	283.1	229.9	236.3	211.8	216.2	213.5	193.5	236.3	248.8	231.1	+5%	-7%

Source: Eurostat, Food and Agriculture Organization of the United Nations, national statistics, UBABEF, USDA 2016; Rabobank 2017

conditions. Key for Brazil in 2018 will be maintaining the confidence of importers, and competing against the major traders in Europe and Japan that are looking to substitute Brazil in poultry trade with Thailand, Poland, and Ukraine, or new regions such as Vietnam and Russia.

In the United States, the biggest concern is from rising red meat supply, which could negatively affect market conditions. Under these circumstances, a disciplined approach to supply is needed, and the predicted 1.8% expansion looks positive.

A similar challenge exists for South Africa, where prices were very high due to AI outbreaks in Q3 2017 and capacity restructuring in previous years. The industry is now restocking and learning lessons from the past—that under such bullish market circumstances, expansion is usually too optimistic.

India has been achieving strong profits for more than a year, mainly driven by good local demand and low(er) feed prices. This is expected to continue into 1H 2018, although the rising cost of local grains could become a concern.

The EU industry is also expected to perform well, but faces the big uncertainty of new AI pressures in the Northern Hemisphere winter, which could shake up EU conditions. Having said this, last year the industry showed great flexibility by increasing exports despite more than 2,000 AI cases across the EU.

Russia and Thailand will need to be more disciplined in local supply, as markets have recently turned to oversupply after growth was too optimistic and the competition from other animal proteins mounts. This is a particular challenge for Thai exports, as markets,

especially Japan, are doing well and the industry will face this and record export levels again next year.

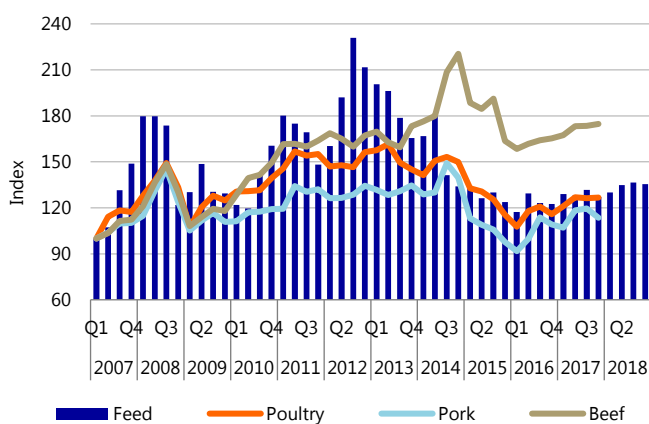
In the case of Indonesia, the culling programmes set by the local governments are paying off and leading to improved market conditions.

The big exception to the relatively optimistic outlook is China. In 2017, the industry went through a roller coaster, with margins initially positive due to low breeding stock levels, before the big negative impact of human AI cases and falling poultry prices, with some recovery in prices after that and a drop in the number of cases in the summer. But with prices again falling and with the Chinese winter coming soon, concerns are rising about the industry impact—especially as some wet markets have only recently been closed. This negative market situation in China will also impact trade next year, with volatile demand in China.

Global trade outlook

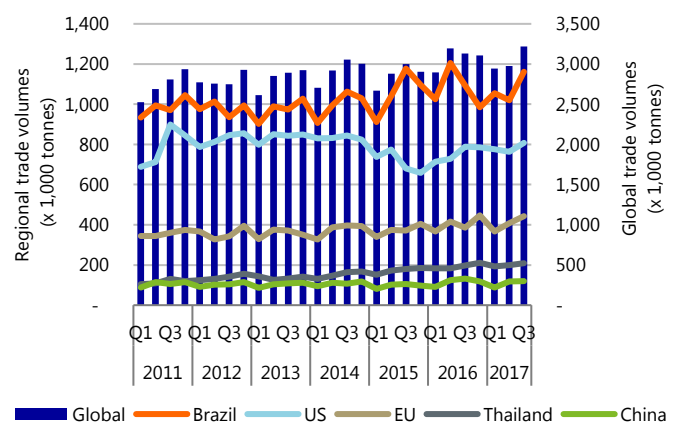
The outlook for global poultry trade remains challenging for 2018. Global trade volumes are expected to grow more or less in line with global poultry market growth, at around 1%-1.5%, but volatility should be expected as AI has become endemic in Asia, Europe, parts of Africa, and also parts of North America. Furthermore, prices could be pressured as competition from red meat is expected to rise and traditional exporters like Brazil, the US, and the EU (for pork) look for new markets. This could impact global poultry trade in terms of prices, depending on supply discipline within the poultry industry.

Figure 1: Global broiler, beef, and pork prices vs. feed cost monitor, Q1 2007-Q4 2018f



Source: Bloomberg, Food and Agriculture Organization of the United Nations, national statistics, Rabobank 2017

Figure 2: Rabobank global poultry trade monitor, Q1 2011-Q3 2017



Source: Bloomberg, national statistics, Rabobank 2017

Ongoing AI pressure during winter months can be expected again in 2018. Besides the impact of seasonal AI outbreaks, global trade in 2017 was affected by the impact of issues such as Brazil's weak flesh scandal and the earlier food safety/antibiotics scandal in China.

Brazil's exports were 6% down over the first three quarters of 2017, while China's export volumes were 7% down compared to last year. Traders have been shifting to other regions where possible. US (+5%), EU (+4%), Ukraine, and Thailand (+7%) have been benefiting, and have all increased their market share in global trade.

For 2018, Brazil appears to be recovering, as export figures indicate a return to 2016 export levels. This could start to affect the export positions of the US and EU in early 2018.

Ukraine, and, to a lesser extent, Russia will keep extending their export position and this will gradually challenge Brazil's export position in Europe and the Middle East. This is also the case for Poland, which is gradually gaining some of the market position from Thailand and Brazil in the EU market, especially in further-processed products.

The rising volatility in global trade, together with some recent scandals, all in the context of ongoing dependence on a few global traders, are pushing importers to support the development of new exporters in the global poultry market. For the coming year(s), Russia, Vietnam, and possibly Indonesia might develop as exporters of poultry meat with support of some importers from Japan and Europe.

Trade agreements will keep affecting global trade streams. South Africa recently imposed higher levies on EU products as a safeguard mechanism. It is also possible that China might impose safeguard protections in response to a possible Brazilian dumping case. These sorts of actions can heavily impact global trade and prices. On the other hand, some recent developments to open trade could lead to new opportunities, such as the EU-Japan trade partnership and a pending EU-Vietnam free trade agreement, the US-China processed poultry opening, and the opening of Vietnamese poultry exports for Japan.

Although some serious concerns and wild cards exist for 2018, we are optimistic that this could be a positive year for most of the global industry.

Dashboard

Legend and units

<i>Production</i>	<i>Exports</i>	<i>Imports</i>	<i>Price</i>	<i>Feed price</i>
tonnes production weight			kg	kg

Δ = year-on-year change

All prices in local currencies

EU: Ongoing strong margins but with rising AI concerns

<i>Production broiler</i>		<i>Export poultry</i>		<i>Import poultry</i>		<i>Whole frozen broiler price</i>		<i>Feed price</i>	
Ongoing growth		AI impact		Lower Brazil		Ongoing strong		July wheat price peak	
Dec: 1,050	YTD: 1,2686	Sep: 140	YTD: 1,217	Sep: 70	YTD: 605	Oct: 1.82	YTD: 1.82	Oct: 0.32	YTD: 0.31
Δ +3.0%	Δ +2.7%	Δ+4.0%	Δ +2.1%	Δ -12.0%	Δ -11.9%	Δ +2.0%	Δ +2.1%	-0.2%	-1.9%

Source: Eurostat (f), MEG 2017

US: Good performance but supply discipline needed as red meat supply rises

<i>Production broiler</i>		<i>Export poultry</i>		<i>Composite broiler price</i>		<i>Whole broiler price</i>		<i>Feed price</i>	
Growth to slow		US exports recover		On the upswing		Ongoing strong		Feed cost relief to slow	
Sep: 1,531	YTD: 14,144	Sep: 272	YTD: 2,531	Jul: 2.8	YTD: 2.11	Oct: 1.88	YTD: 2.12	Nov: 0.35	YTD: 0.35
-1.3%	+1.9%	+3.3%	+0.8%	+8%	+8.9%	+19.0%	+11.6%	-1.1%	-1.2%

Source: USDA 2017

Brazil: Gradual recovery after 'weak flesh' market shake-up

<i>Production broiler</i>		<i>Export poultry</i>		<i>Live broiler price</i>		<i>Whole broiler price</i>		<i>Feed price</i>	
Slowdown in growth		Disappointing levels		Lower costs		Lower costs		Better feed grain crop	
Jun: 1,117	YTD: 6,744	Oct: 359	YTD: 3,601	Oct: 2.63	YTD: 2.56	Oct: 3.64	YTD: 3.60	Oct: 0.69	YTD: 0.65
-5.8	+0.6%	+16.1%	-0.7%	-15.0%	-10.1%	-21.1%	-12.2%	-15.1%	-32%

Source: CECEX, MDIC 2017

US

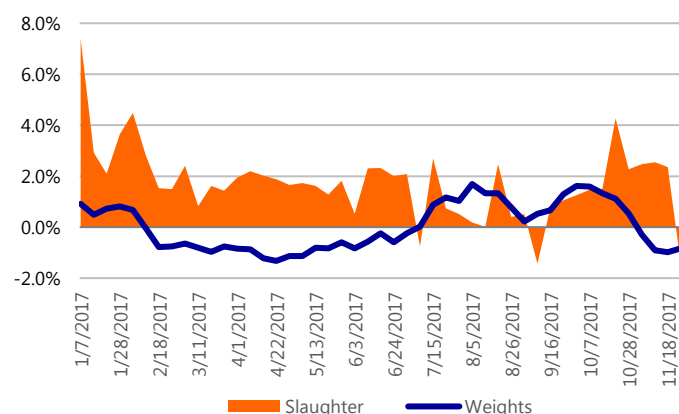
Composite chicken prices remain well-ahead of year-ago levels, despite seasonal softness in breast meat and wings. Dark meat markets remain the standout, aided by good exports and stronger domestic consumption. Chicken breast prices softened late in Q3 and continue to struggle with high stocks (+13% YOY) and sluggish demand. Wing prices are falling as NFL viewership has waned and high prices curbed demand. They should rebound, however, with rapid growth in wing concept chains expected in 2018. Pricing is unlikely to replicate 2017 levels, given large competing protein supplies, but slow production growth remains supportive.

Production gains remain constrained by little-to-no increase in live weights and limited growth in the current layer flock, supporting our outlook for 1.7% growth in 2017 (see Figure 3). We see no immediate reacceleration in productivity in early 2018, as the age of the flock and breed changes have dampened productivity, and growth is limited by an effort to constrain bird weights to address the woody breast issue. The industry remains on track for 1.8% growth in 2018.

Exports of US chicken are up 1.4% year-to-date, with continued growth in shipments to Cuba and Angola (both +8%) compensating declining exports to Mexico (-9%) and Canada (-6%). We expect a strengthening of the Mexican peso and limited supplies in Canada to support stronger trade into 2018, barring any unforeseen policy-driven interruption—changes to NAFTA remain the key wildcard for 2018.

Margins should remain favourable as feed costs for the balance of 2017, and the outlook, remain solid for the year ahead.

Figure 3: US average live weight, Jan 2015–Nov 2017 (YOY change)



Source: USDA, Rabobank 2017

Mexico

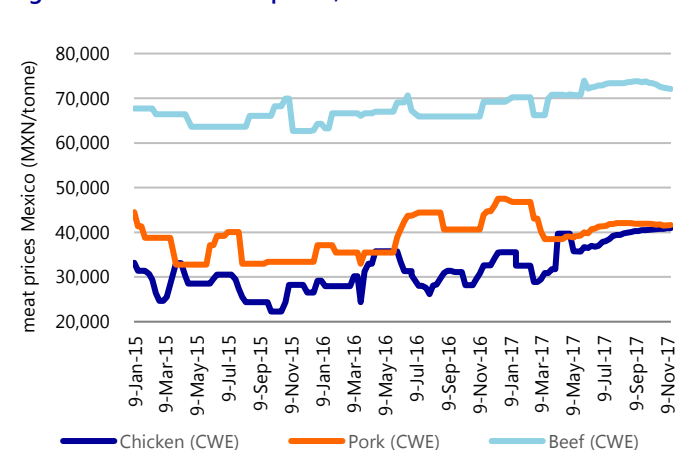
Mexico continues to increase its domestic consumption, with a record year of 4.1 million tonnes expected for 2017, an increase of 104,000 tonnes, or 2.6%, compared to 2016. Competition from other proteins and increasing income per capita might slow down chicken consumption as consumers move to other proteins, and, while chicken prices continue to be more competitive than beef and pork, the price advantage is declining (see Figure 4).

Domestic production is increasing. With no AI impact this year, Mexico continues to grow the national flock and increase production. Production for end of year is expected at 3.3 million tonnes, increasing by 2.2% compared to 2016. Good margins this year should continue to incentivise production growth. In 2018, production is expected to increase by 2.4%–2.8%.

Trade remains an important component for filling the gap between consumption and production. However, while imports help reduce the deficit domestically, from January to October imports from the US were down 9% compared to 2016. As the US is the main source of leg quarters, prices for legs have increased by 8%. This has been partly compensated by importing more chicken from Brazil (January to October), accounting for 11.8%, although this did not fully compensate for lower US imports.

Mexico's expected production increase in 2018 will likely put downward pressure on prices, improving the price advantage chicken has enjoyed over other proteins.

Figure 4: Mexican meat prices, Jan 2015–Nov 2017



Source: GCMA, Rabobank 2017

Brazil

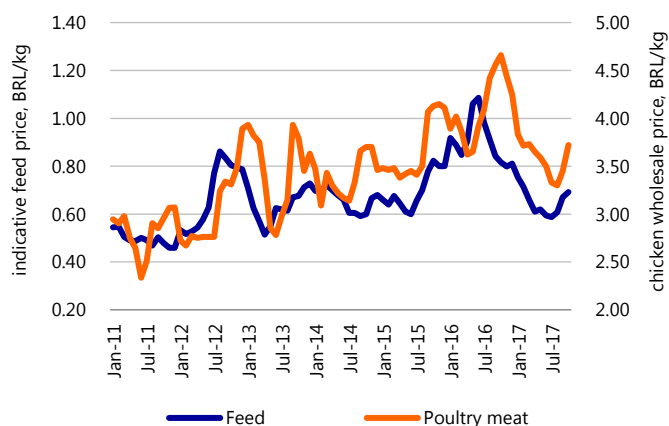
Leaving behind a challenging period in the international poultry market, Brazil is putting its exports back on track. After having declined by around 7% during 1H 2017, Brazilian poultry exports exceeded 3.6 million tonnes YTD in October 2017, which is almost the same volume as was exported in the same period of 2016.

The gradually recovering global confidence will push Brazilian poultry exports to finish 2017 slightly above 2016 levels, and exports are anticipated to increase by 2% in 2018, in volume terms. Saudi Arabia is likely to continue to be the largest destination for Brazilian poultry, followed by Japan, China, and the EU.

Regarding the domestic market, given the improved economic outlook for 2018, Rabobank expects a gradual recovery in Brazilian meat consumption. This additional demand will be more than welcome, as poultry in Brazil is expected to increase by 1.7% in 2018. On costs, feed prices are expected to remain flat in Q1 2018, compared to Q4 2017. However, depending on the performance of the second corn crop (southern hemisphere winter), feed prices could start trending upwards as of Q2 2018.

All in all, during 2018, Rabobank expects an increase in the demand for Brazilian poultry both domestically and internationally. However, given that there are still questions on the developments of feed prices in Brazil during 2018, it is too soon to talk about increasing margins (see Figure 5).

Figure 5: Brazilian broiler and feed price trend, Jan 2011-Oct 2017



Source: SECEX, MDIC, Rabobank 2017

EU

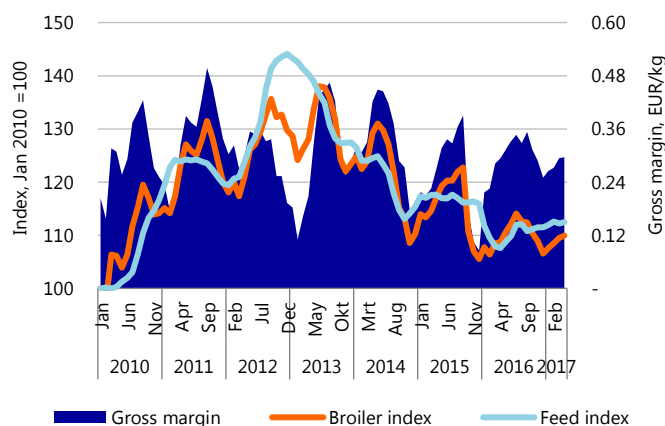
The EU poultry industry is performing relatively well, based on a favourable supply-demand balance in the European market, given restricted production growth in the aftermath of the AI cases earlier in 2017 and the constrained growth in north-western Europe due to environmental regulations which restrict expansion. Margins are currently above historic averages with broiler price levels 4%-5% above last year's levels and stable feed prices (see Figure 6).

The industry is facing strong demand for poultry with intra-EU poultry demand up by 1.6%, while exports have been growing by 2.5% compared to 2016 levels. Export growth has been a great achievement in a situation where many markets have been closed (including the EU's key export market, South Africa) after more than 2,000 AI cases were recorded in the EU in 2017.

On the supply side, production keeps growing in Eastern Europe, especially Poland (+8%) and Romania (+10%), while Hungary is recovering from AI outbreaks. In Western Europe, production is relatively stable to slightly declining (Italy, Spain, and Netherlands).

The outlook for the EU poultry industry for 2018 looks positive with ongoing demand growth expected (+2%), while production is expected to remain restricted due to increased AI risks in Europe's winter. Western Europe is restricted in supply and will move to less intensive production concepts, while standard chicken production continues its move to Eastern Europe. From a trade perspective, the industry has shown great flexibility in dealing with the negative impact of AI in export markets, while imports from Brazil and Thailand are increasingly shifting to Eastern Europe.

Figure 6: Broiler feed price and margin trend in north-western Europe, Jan 2010-Oct 2017



Source: Bloomberg, Rabobank 2017

Russia

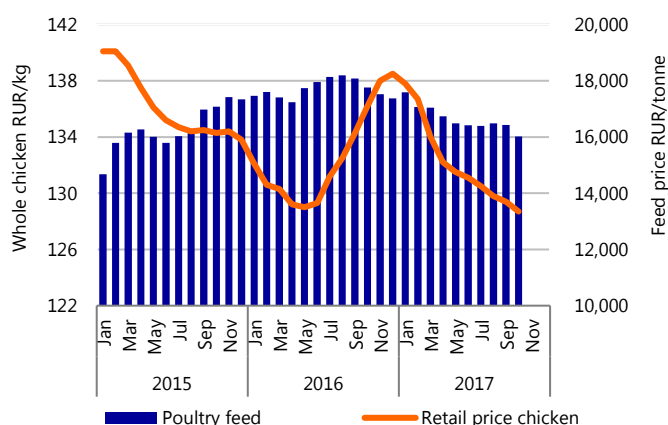
The Russian poultry industry is operating in more challenging market conditions than earlier in 2017, due to rapid growth of local production (+4%), to 4.85 million tonnes, compared to sluggish demand (+3%). Prices of poultry in November dropped by 13% compared to last year (see Figure 7). The industry is also facing competition from the rising oversupply of pork in Russia, with prices also falling in the last few months.

The industry is increasingly focused on exports with a forecast total export level of 150,000 tonnes for 2017, well up from 115,000 tonnes in 2016. Exports to Ukraine, Vietnam, and Kazakhstan have been particularly strong.

The industry is developing a local breeding capability, backed by the recent signing of the EAEU agreement on developing a stronger local breeding industry. Recently several big breeding projects have been implemented at GPS level in broilers and turkeys, and this trend is expected to continue.

The outlook for the Russian industry for 2018 is moderately positive. Key will be a changed focus on more balanced supply growth and a higher focus on exports. If the industry refocuses effectively, the outlook looks good, especially as the crop year forecast suggests a record high level of 130 million tonnes of grains, which should support competitive feed costs in the coming year. An ongoing positive for the industry is support from the Russian government in opening new export markets in the Middle East, and more recently in Asia, with the potential for the Japanese and Chinese markets to also open to Russian exports.

Figure 7: Russian retail frozen broiler (LHS) and feed price (RHS) trend, Jan 2011-Oct 2017



Source: Rostat, Rabobank 2017

South Africa

The South African poultry industry was affected by AI outbreaks in Mpumalanga and Western Cape in 2017. Around 4 million layers, 360,000 broiler breeders and 310,000 layer breeders were culled during the wave of AI cases in Q3 2017. The situation has now improved somewhat, with the last case reported on 18 October 2017, but many affected farms are still in quarantine.

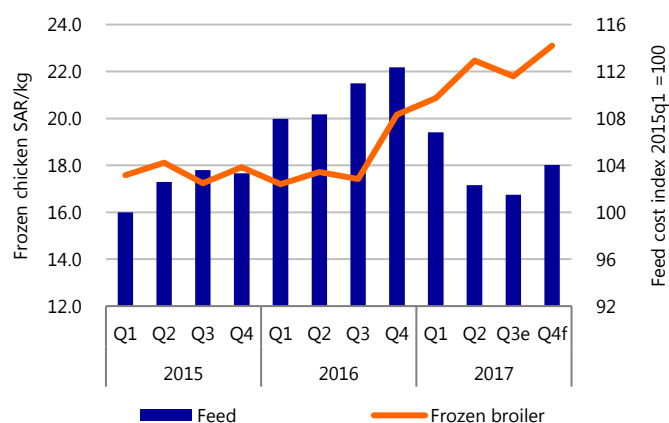
The impact on the South African market has been very significant, with poultry and egg prices now 15%-25% above last year levels (see Figure 8). The industry is still receiving some price support from low import levels earlier in 2017 due to AI in Europe (and the ensuing bans on imports from many European countries). Another factor has been production restructuring in South Africa, which has led to several plants closing.

Positive for the industry are the current relatively low feed prices compared to last year (-8%), due to a much better crop year with adequate local grain supplies.

On the negative side, poultry meat exports have dropped significantly in 2017 (-20%), due to restrictions on trade. This is also the case for the trade in hatching eggs and DOC—South Africa is a major supplier for the Sub-Saharan poultry industry.

The outlook for the South African poultry industry for 2018 is challenging, despite the high margins enjoyed by companies still able to supply chicken. The risk is of overproduction as local companies might be too optimistic in expanding, coupled with EU imports gradually returning to South Africa. A disciplined supply growth strategy for local players is key, given the current uncertain market situation.

Figure 8: South African broiler and feed price trend, Q1 2012-Q4 2017e



Source: SAPA, Rabobank 2017

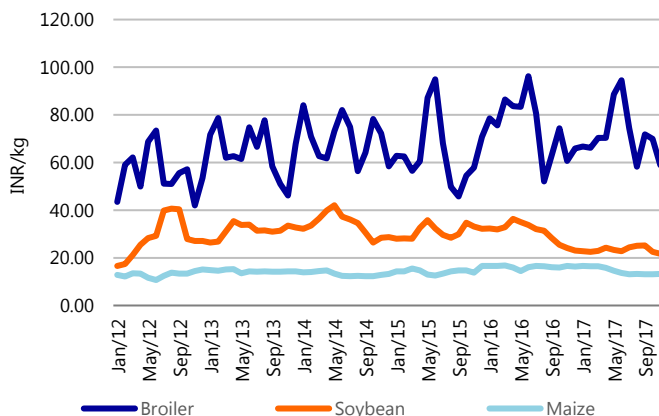
India

Broiler commercial farm margins softened in Q3 2017, in line with seasonally lower demand. Despite the sequential price decline, margins remained significantly higher compared to year-ago levels—thanks to lower soybean and corn prices (translating to lower feed cost) and buoyant demand on the back of good monsoon seasons since 2016 (see Figure 9).

Live broiler prices in November 2017 ranged between INR 59 and INR 98/kg lwt—recovering from INR 55 and INR 71/kg lwt in August. At the same time, egg prices have jumped. November 2017 wholesale egg prices ranged between INR 4.6 and INR 5.3/piece—up 40% from between INR 3.2 and INR 3.9/piece in August 2017. We understand that many farmers did not place layers in 2017, as egg prices had been below cost (between INR 3.2 and INR 3.3/piece) in 2016. Current high egg prices are expected to be temporary, as consumption will likely subside with some substitution going into broilers. Despite lower costs this year (between INR 2.8 and INR 2.9/piece), the supply of eggs may not be able to respond immediately. Unlike broiler placement, egg production has a comparatively longer gestation period from placement to laying.

Feed raw materials (soybean and corn) remained 10%-20% lower YOY lower in 2017. The cumulative rainfall between June and September for the Southwest monsoon is indicatively 2% lower YOY, according to the USDA. We continue to expect feed raw material costs to remain low for the remainder of 2017. However, faster soymeal and corn demand growth for the poultry feed industry in the long term will make ensuring price stability and self-sufficiency in poultry feed production a challenge.

Figure 9: Indian broiler, DOC, and feed price index, Jan 2013-Nov 2017



Source: Bloomberg, Rabobank 2017

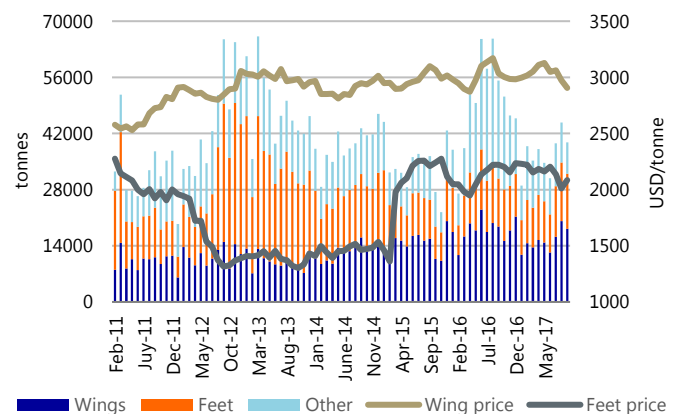
China

Following a weak performance in October 2017, China's broiler prices returned to RMB 7 per kg in the last week of November. The fluctuations are driven by supply, while demand remains weak. AI risks are rising, and many live bird markets remain closed. Consumers in the south still need some time to respond to the new market channel, and shift their purchasing habits from live birds to chilled meats. Thus, consumer demand at retail markets is believed to temporarily decline in 2017. Other distribution channels have mixed performances. While dining out, food ordering and food processing have grown steadily and offered strong support for poultry demand, canteens at factories and plants are estimated to have lower demand after environmental measures resulted in the closing of many small factories.

The broiler industry has experienced supply-side restructuring under the pressure of weak demand. Disciplined supply has resulted in the decline of poultry meat output in 2017. However, even with this decline, broiler prices have not trended upward but have fluctuated around breakeven points. Given the tighter supply in the coming months, we expect poultry prices to rise, but only to a limited extent.

Poultry imports in the first nine months of 2017 declined by 26% YOY, to 331,000 tonnes (see Figure 10). While Brazil still accounts for above 80% of total imports, shipments from Brazil have declined by 25%. We believe the weak domestic market and Brazil's weak flesh scandal are the reasons for the decline. On the other hand, China's poultry exports increased by 9% YOY, with major growth coming from cooked poultry meat export. In 2018, we expect exports to continue to rise while imports should stay stable.

Figure 10: Chinese imports of poultry in volume (tonnes) and prices (USD/tonne), Feb 2011-Oct 2017



Source: China Customs, Rabobank 2017

Japan

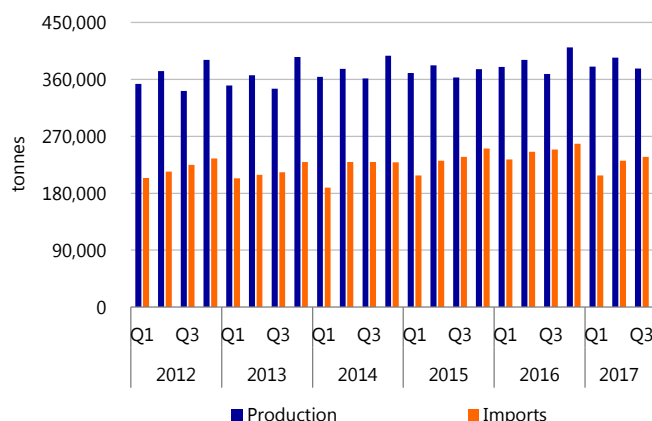
The Japanese poultry industry has experienced relatively positive market conditions over recent months, with rising domestic poultry prices (+15%-20%) for all cuts, whole chicken, legs, and breast meat, compared to Q1. Strong domestic demand (+1.5%) for 2017 has been supportive, and the industry has also received price support from high domestic beef and pork prices.

Production and trade has been relatively balanced (see *Figure 11*) and this has provided no relief from the high stock position in the Japanese market. Japanese trading houses benefitted from this situation as it provided purchasing power in international markets and they could optimally benefit from Brazil's weak flesh scandal by buying competitively-priced raw chicken.

Interestingly, despite this competitive Brazilian supply, Thailand keeps increasing its share in the raw chicken market in Japan, now moving to 12,000-13,000 tonnes monthly export levels (up from 8,000-9,000 tonne levels earlier in 2017); although still below Brazil (around 35,000-40,000 tonnes). Imports of processed poultry from Thailand are also growing.

The outlook for the Japanese poultry industry remains positive and the industry will still focus on traditional fresh local chicken supply (around 60% of the market) and given ongoing rising demand (1%-1.5% growth in 2018); the outlook remains positive. From a trading perspective, the Japanese industry is well-positioned taking into account its current healthy stock position. They will further move imports to Thailand and potential new suppliers in South-East Asia and potentially Russia to mitigate risks.

Figure 11: Japanese domestic supply, Q1 2012-Q3 2017



Source: ALIC, Rabobank 2017

Thailand

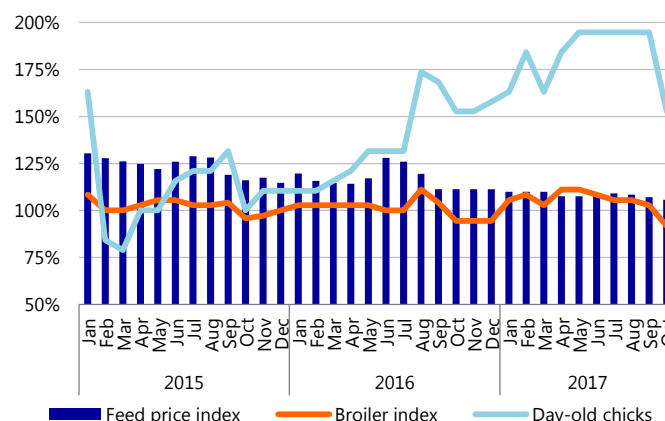
The Thai poultry industry's performance has changed significantly in recent months, driven by rising oversupply for poultry but also for competitive proteins.

Total chicken production will grow by 7% in 2017, to 1.9 million tonnes, which is one of the fastest expansion years in the past decade. Many local companies have expanded their production capacity, and this has led to an oversupply situation in Thailand.

Strong exports (+5%-7% to 770,000-800,000 tonnes expected for 2017) and increasing domestic chicken demand is still not sufficient to protect the industry from falling local chicken prices (-15%) compared to June (see *Figure 12*). The industry is also affected by general weak animal protein demand in Thailand, with pork prices (-22%) and egg prices (-12%) down sharply since June 2017. Only shrimp prices remained relatively strong. Prices for DOC have dropped sharply which illustrates well the changed sentiment in the Thai poultry industry with lower incentives to expand.

The outlook for the Thai poultry industry for 2018 is moderately positive. Key for the outlook is a more disciplined supply strategy by local players. Growth in the range of 4%-5% will be healthier than the current 7% growth rate. If growth is better managed by the local industry, the outlook will be positive for 2018. Thailand's export position will also be strong and the industry should be able to grow exports to 850,000 tonnes by increasing exports to Japan and new countries in South-East Asia and the Middle East. The positive outlook for feed costs, likely to maintain their slightly declining trend of recent months, is also favourable for the industry.

Figure 12: Thai broiler-to-feed price monitor, Jan 2015-Oct 2017 (index)



Source: Bloomberg, Rabobank 2017

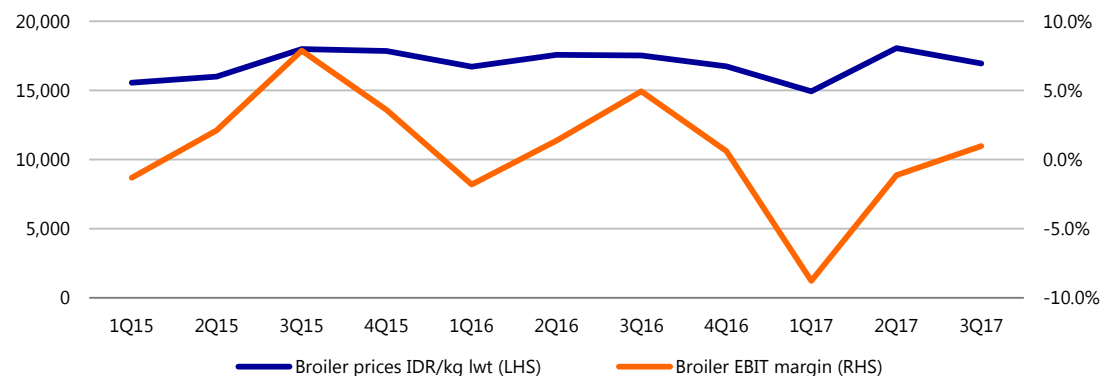
Indonesia

The poultry integrators' Q3 2017 broiler EBIT margins had sequentially improved; helped by both higher prices and volumes—despite having come out of a relatively weak Lebaran season. This was overshadowed by slightly lower day-old-chick (DOC) prices and higher unit costs, stemming from the four culling instructions issued up to September 2017. A fifth culling instruction was announced on 25 October 2017 for broiler final stock hatching eggs; to be undertaken between 30 October and 30 December.

Coinciding with weaker consumption during the month of Suro (22 September – 21 October 2017), both broiler and day-old-chick prices fell to average at IDR 15,486/kg and IDR 4,050/bird in October, from an average of IDR 17,781 and IDR 4,574/bird, respectively, in August. Prices have since recovered to between IDR 18,000 and IDR 19,000/kg live. We expect poultry integrators' overall margins to sequentially improve slightly in Q4 2017, helped by more favourable feed prices and rising DOC sales volumes, offset by high DOC unit costs and flat broiler prices. In the first nine months of 2017 we estimate DOC volume to have expanded by 10% YOY and we continue to expect 10%-15% growth for the year, despite culling instructions.

On 9 November 2017, Indonesia lost its appeal in the WTO's Appellate Body in cases brought by New Zealand (DS477) and the US (DS478) over 18 measures imposed by Indonesia on imports of horticultural products, animals, and animal products. Indonesia has 18 months to revise its regulations and we expect Indonesia to proceed with negotiations prior to implementation. Outside processed chicken and fast food chains, Indonesia consumes mostly fresh chicken in wet markets. The impact of frozen chicken-part imports should therefore be limited in the medium term. But further processors would benefit from cheaper raw materials, subject to phytosanitary/labelling requirements and/or other costs.

Figure 13: Indonesian integrator broiler EBIT margins, Q1 2015-Q3 2017



Source: Rabobank, Bloomberg, 2017

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