

Grass seed prices— during and after a food and financial crisis

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Grass seed prices– during and after a foodstuff and financial crisis

The grass seed market was highly influenced by the foodstuff crisis in 2007/08, as well as by the financial crisis in 2008/09. The foodstuff crisis and the increasing grain price resulted in increased grass seed prices, whereas the financial depression has curbed the demand for grass seeds. While a new foodstuff crisis, on a larger or smaller scale, may be on the way again, the financial crisis as well as the economic depression, seem to be a thing of the past. Both factors may cause grass seed prices to rise. It is a fact that grass seed prices are affected by grain prices, the stock size and the financial state of the market. In light of the above we are bound to see increasing grass seed prices in the near future.

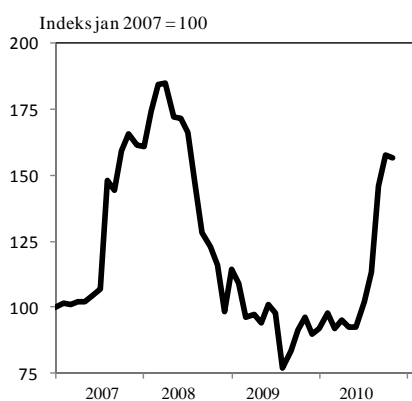
Is a new foodstuff crisis on its way?

The foodstuff crisis in 2007/08 had a major impact on grass seed markets. It is therefore imperative we evaluate whether a new foodstuff crisis is on its way.

Foodstuff crisis in terms of substantial price increases for agricultural goods and foodstuffs are not a new phenomenon. Developments in the US, where you will find the big international grain exchanges, as well as relatively free market forces, show that the international grain prices have been unstable during the last decades.

This development also becomes a reality in Denmark and we clearly saw this during the foodstuff crisis in 2007/08 and what may be a trend in terms of a new foodstuff crisis cf. figure 1.

Figure 1: Wheat prices (Bread Wheat) in Denmark, 2007-2010



Source: Own calculations based on Danish Agriculture & Food Council (several years).

Recent developments

In July 2010 the international cereal prices went up remarkably, this time by 60% during one month. The heat, drought, crop failure and fires in Russia made, by the end of June 2010, the

international grain exchanges panic. Cereal prices increased dramatically and experts predicted that grain exports from Russia, Ukraine and Kazakhstan would go down by approx. 30-50%. Furthermore, the Russian grain export ban made the international cereal markets fear a shortage which again led to further price increases.

As shown in figure 2, international wheat prices increased by nearly 60% from July to August 2010.

Figure 2: Development in international wheat price in 2010-2011



Source: CME Group (2011).

From June 2010 to February 2011 the cereal price increased by approx. 75%

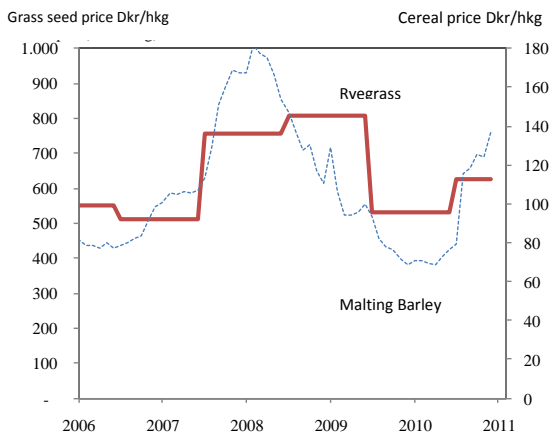
Grass seed prices follow cereal prices

Even though grains and grass seeds are used in very different areas and sold in different markets, one product still has a major impact on the other. Cereal and grass seed markets are therefore inextricably linked.

During the last 5 to 6 years, characterized by fluctuating prices and a big foodstuff crisis, it is not remarkable to see that cereal and grass seed

prices follow one another. However, grass seed prices follow 6 – 24 months after the cereal prices cf. figure 3.

Figure 3: Development in cereal and grass seed prices 2006-2010



Source: Own calculations based on data from on Danish Agriculture & Food Council (several years).

Cereal prices influence grass seed prices

The increasing cereal prices will, both directly and indirectly, as well as in the short and long term, have an impact on the grass seed prices.

Firstly, the increases in cereal prices will make farmers produce more cereals and less grass seed. Many farmers are able to substitute grass seed with grains, immediately. As a result there will be a shortage of grass seed, which again will lead to increasing prices.

Secondly, most grass seed companies want the production of grass seed to be consistent. Capacity must be utilized and long-term contracts or customer relationships must be maintained and hence the grass seed supply must not be reduced. Purchasers of grains and grass seed, respectively, thus compete to attract sufficient quantities of raw materials. As a result prices will increase to keep farmers interested in producing grass seeds.

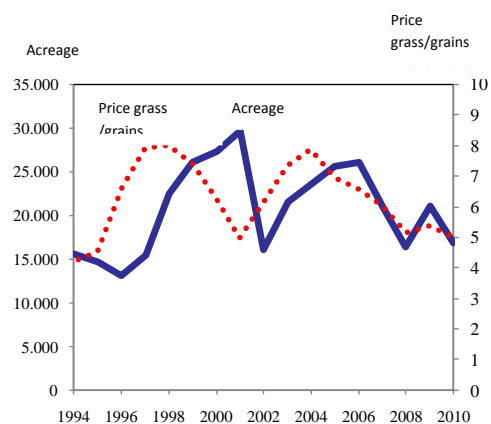
Thirdly, few players in the grass seed market have any interest in great turbulence and dramatically fluctuating prices. If the grass seed prices do not go up accordingly, entirely or partly, supply as a result will decrease. The decreasing supply will be followed by new price increases. The greater the decrease in supply, the greater the subsequent price increases will be.

Increasing cereal prices will cause a reduction in grass seed acreages

With an increase in cereal prices but with no similar increase in grass seed prices, the resulting reduction in grass seed acreage is not just a theory. You may actually see a clear connection by retrospectively studying the development.

As shown in figure 4, a relative drop in grass seed prices will, compared to cereal prices, causes the grass seed acreage to be reduced 1 to 3 years after.

Figure 4: Price of grass seed/grains vs. acreage of grass seed (red fescue)



Source: Own calculations based on Danish Seed Council (2011) and data from on Danish Agriculture & Food Council (several years).

The figure also shows that grass seed producers have during recent years, reacted quicker and quicker to changes in the price between grain and grass seeds.

Stock development

Stocks and in this context also supply and demand, often develop in cycles. Big stocks will mean decreasing prices, which again will lead to a decreasing supply and thus reduced stocks.

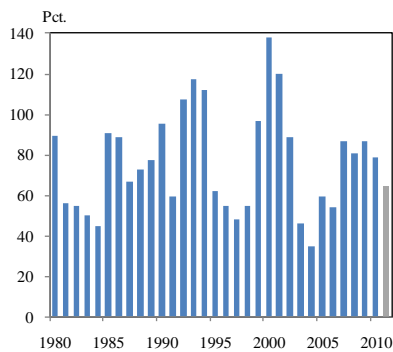
Consequently prices, supply and in the end stocks will increase to and thereby we start all over.

The market will always seek to find a balance where prices, supply and demand, as well as stocks, do not fluctuate too much.

During the recent 30 years there have been 4 to 5 peaks in terms of grass seed stocks, which could

mean that the present peak is about to go down cf. figure 5.

Figure 5: EU stocks of grass seed (perennial ryegrass) in % of production



Note: 2011: Estimate

Source: Danish Seed Council (several years) and own estimates

The stock size depends on a series of conditions, among others on the supply and demand situation and therefore you may see fluctuations that are more or less accidental from year to year. A good harvest one year may therefore increase stocks, even though the prices are relatively low.

Stock size will have an impact on prices

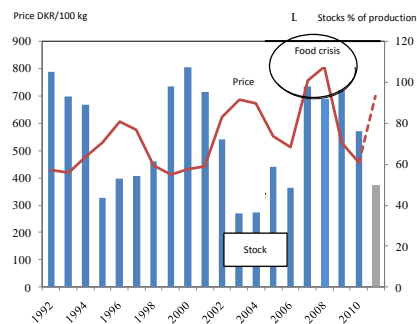
The size of the stock is one of most important factors when speaking of price development on both grass seeds and grains: if the stocks are big they will act like a buffer on the market keeping the prices down. Players in the market know that if price increases are imminent, you may use stocks and thereby increase supply.

On the other hand small stocks will always lead to price increases. You do not have the usual buffer to neutralize price fluctuations and consequently prices will go up.

When it comes to grain, stock sizes may well explain the entire price development during the last 10 to 15 years, cf. Hansen, H.O. (2009).

Developments during many of the last years illustrate clearly how stocks have an impact on the grass seed area cf. figure 6.

Figure 6: Stocks and prices on grass seeds (perennial ryegrass in Denmark)



Note: 2011 = prognosis

Source: Own calculations based on Danish Seed Council (2011)

The development shown is based on the perennial ryegrass market in Denmark, however a similar connection may be seen in many other places.

The connection between stocks and prices is relatively precise in the shown period. In the years 2008/09 and 2009/10 there are significant divergences since both stocks and prices go up. This may, however, to a great extent be explained by the foodstuff crisis and the spill over effect on grass seed prices and the extraordinary big harvest, respectively.

The figure clearly shows that the size of the stocks is a major explanation in terms of price development.

If grass seed stocks correspond to 50% of the production, which is a realistic estimate for the 2011 crop, it will correspond to a price of 600-700 DKK/100 kg of perennial ryegrass and therefore require a price increase in 2011 of 40 to 50%.

Due to expected stock decreases in the EU this will automatically lead to pressure in terms of increasing grass seed prices.

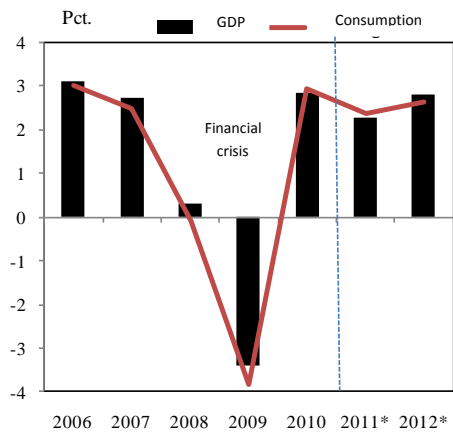
Financial crisis and economic crisis

The financial crisis which started in 2008 and which was followed by an economic crisis, had a major impact on the economic state of the market and therefore on the demand for grass seed.

In such a crisis, the building and construction sectors are particularly affected and this sector is very important in terms of sales of grass seeds.

The financial crisis, compounded by the economic crisis had a subsequent negative effect on economic growth, resulting in a significant decrease in 2008 and 2009, cf. figure 7.

Figure 7: Growth in GDP and consumption in OECD countries, 2006-2012.



Note: 2011 and 2012 estimate by OECD.
Source: OECD (2011).

Growth in both consumption and GDP dropped significantly in 2008 and 2009. In 2009 you could even talk of real wage decreases.

The figure also shows that, providing the OECD 2011 and 2011 estimates are correct, the world economy is back to normal again. As a result, we may also expect an increase in demand in the near future.

Conclusion

The grain price development during recent years has turned many market conditions upside down within the agricultural sector. Cereal production has in periods increased earnings and contribution remarkably. Crops that can be substituted with

grain will, of course, come under pressure since it will be relatively more attractive to produce grain.

Even though grain and grass seed are sold in different and separate markets, the increasing cereal prices will no doubt influence the grass seed prices, both in the short and long term.

A new market balance will result in increasing grass seed prices. At the same time indicators like decreasing grass seed stocks and increasing demand, as a result of the improved economic situation, will also be instrumental in terms of driving up the price of grass seeds.

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