

## Macro-economic Situation

Some well-known economists in here China are forecasting that the odds for China to have typical inflation next year would be lower than expected with the problem of overcapacity probably outweighing the growth in loans and money supplies in the third quarter dramatically declining from the previous quarters, while the market are unanimously concerned about a high inflation with huge amount of money already put into the market by the government to stimulate the whole economy. Fundamentally, impacts of international market are blamed for the various hikes in overall domestic prices since 1998. The recent CPI increases have been induced only by the rebound in foods prices, one of the above-mentioned experts think. The overall prices are widely expected to pick up again but not as much as to leading to a notable inflation. A typical textbook inflation might be reflected mainly in assets prices however. What really concerns those local forecasters is assets prices ballooning while CPI (one of indicators of physical economy situation) shrinking. This scenario would result in overall economy's growth slowing down persistently or a long-term recession. Therefore, the central government's think tank is recommending that the focus of regulating domestic prices should be shifted from controlling inflation to strengthening regulation of assets bubble. Meanwhile, the key job of anti-inflation is to guard against foreign impacts and the focal point of regulating domestic prices should be put on monitoring and manipulating the supply and demand of two core farm produce: grains (including oilseeds and vegetable oils) and pork.

Rumor that China might import biodiesel from international market has yet to be confirmed. As far as our investigation goes so far, none of local oil traders has heard of it yet. China government has indeed phased out a couple of policies and programs to encourage the development of renewable fuels and energies like wind power, solar power, nuclear power, biomass fuels etc.. A consensus has been reached among the government, official think tanks and private analysts that China has limited arable lands compared with her huge population and cannot afford to develop and use grain or vegetable oils based biofuels so that other biomass based biofuels are realistic. However, China might import biodiesel theoretically if foreign biodiesel is cheap enough compared with mineral diesels and there occur a huge short supply of mineral diesels on domestic market. Even if it would happen, it seems more logical that China's buyers would probably opt to take palmoil based biodiesels from Malaysia or Indonesia rather than soyoil based one from the other side of the earth.

## Government Grains Policy

The central government may well have made their final decision on new crop local beans stockpiling program a couple of days ago as we reported last week

though they has not published it yet, as Sinograin has already started to carry it out on domestic market now according to our reliable inside news resources.

The international trading division of this company has also begun to rotate those foreign beans in their reserve by importing beans directly from the international market. Compared with private importers or crushers, they are enjoying much more favorable terms and conditions like D/P payment term in concluding their physical deals with foreign suppliers.

As we reported in our earlier wires, their reserve is divided into two parts, permanent reserve and provisional reserve. What they are expanding is the latter and what they are rotating is the former. As for the former, it is also divided into two parts, local beans, which account for the bulk of it, and foreign beans, which are roughly estimated to be around 1-2 mmt. The rotation of the whole permanent reserve would normally be carried out step by step and part by part and completed within two years at most according to the traders working with Sinograin. It seems to me that they would probably expand the percentage of foreign beans in their permanent reserve sooner or later with ever increasing imports of foreign beans and crushing demand here in China.

## **Domestic Livestock Market**

The first half of October saw an off season for pigs and chickens on farm. The placement started to pick up around the middle of October as the period from mid-October to mid-November is normally the last time window for hogs to be placed on farm for sales busy season during new lunar year festival, which normally take place some time in the second half of January and the first half of February. Therefore, hogs and chickens on farm are expected to move up seasonally and kept at seasonally high level until February. The increases in the number of hogs and chickens do not necessarily mean meals prices would continue their uptrend during the coming months but would lend underlying support to their higher lows.

## **Domestic Grains Market**

More and more local analysts have adjusted down their estimates about the foreign beans shipments arrivals, from previous much more optimistic numbers between 3.5-4.0 mmt to the current more realistic ones around 2.0 mmt, due to delay in many early new crop US beans shipments which are originally intended to reach China main ports as early as possible so as to catch higher spot soy meal prices and good crush margins. Now that many more shipments have been delayed into next months some local analysts are beginning to worry that China's buyers might slow down their purchasing pace of US beans earlier than most imagined and shift their attention to S.American beans as Brazilian farmers are advancing their planting as early as possible to take advantage of the inverted market and US beans sales window might be squeezed. Actually they have already turned to secure some Brazilian or Argentine shipments which are quoted at much lower prices in term of basis. Sinograin's action to expand their reserve in full wing might however prompt more US beans buying to fill up the vacuum that local beans stockpiling would leave. Based on the new crop US

beans shipments that China buyers have secured so far, there would be 3.5 mmt to arrive in each month from December through next March, which is expected to be comparable with normal monthly imports for this period in the past years.

Meal prices are widely expected to be on track to the downside movement with more and more foreign beans shipments flowing into domestic market to replenish crushers inventories and feed mills continuing their hand-to-mouth buying strategy in anticipation of lower prices down the road.

## Dairy Market

China has surpassed Japan and taken the first place in the world in milk powder consumption. It is widely expected that China's dairy industry would consolidate and expand very rapidly during the period of 2008-2015 and then would probably move into a phase of rather stable and sustained albeit slow growth after 2015. Right from the outset of 21<sup>st</sup> century China's annual birth rate has been averaging 12.7% with about 17 million babies born every year. This might be one of the major driving forces behind the amazing growth of China dairy industry.

With overall economy's sustained growth, continued urbanization and milk drinking program for primary and middle school students to be unfolded and spread gradually, a significant growth is expected to be seen either in total dairy products consumption or per capita consumption. It is officially estimated that the aggregate dairy products consumption would reach over 25 million tones, around 2.7 times 1999's level with annual growth rate at 6.83% on average while per capita consumption climb at 17.83 kg, almost 2.43 times 2000's level with annual growth at 6.1%. From now on until 2015, the milk drinking program for primary and middle school students launched by the government alone is expected to boost dairy consumption 1.54 mmt each year.

When looking at dairy products production, the above-mentioned program is predicted to stimulate the national dairy production up to 19.30 mmt and 25.01 mmt in 2010 and 2015 respectively, 2.1 and 2.72 times the level in 2000. The annual growth of dairy production is pegged at 5.32% during the period of 2010-2015 vs. 5.8% during the period of 1990-1998.

Pls feel free to contact me if you have any question and comment.

Best regards

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