Banana
World market

Is the party over?

So, the economic storm predicted a year ago in these columns has come to pass, and could even become a cyclone in 2018. The equation is uncommonly simple, with no unknowns: there are too many bananas on the international market, and the European Union is in the firing line.

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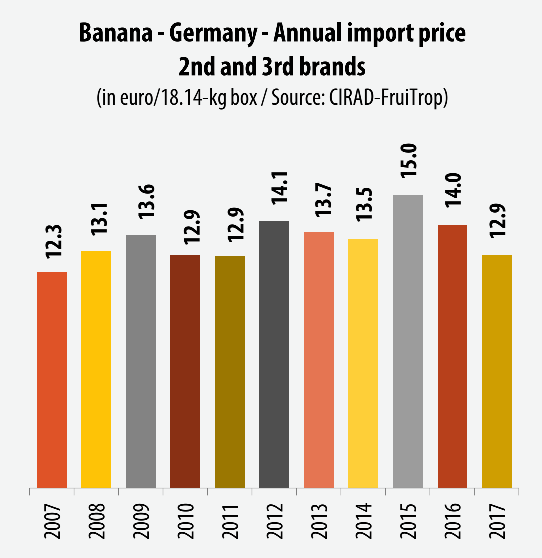

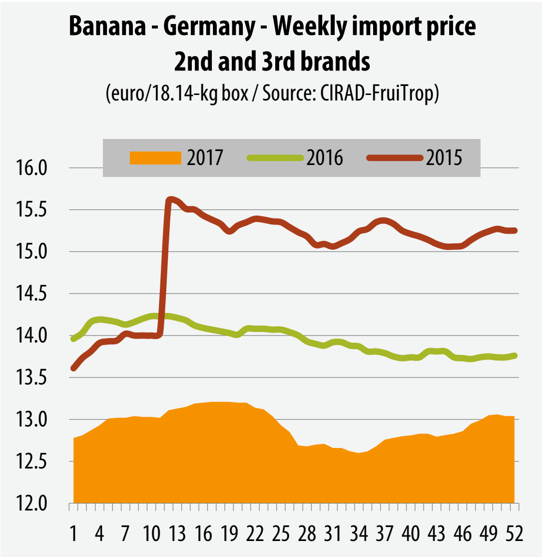

It is hard to find reasons for satisfaction from 2017. To lift their spirits, operators could always tell themselves that the worst has for the moment been avoided. If they give due consideration to the pessimistic prospects for 2018, they will admit that ultimately 2017 was a gentle stroll. Let's not jump the gun on the tricky subjects, but share this review of 2017. Exactly a year ago, **FruiTrop** bore the title "Calm before the storm?", illustrated by a monkey covering its eyes. One year on, we might admit to making a mistake... in putting a question mark in that title. In fact, 2017 was marked by a storm, and the expression "a perfect storm" would make an ideal description.

The first indicator is the green banana price in Germany. A genuine long-term yardstick of the European market due to a very high upstream-downstream contractualisation rate, this market lost one euro per box between 2016 and 2017 to barely hold up at 13 euros, i.e. a fall of 7 %. The worrying thing is that a similar fall had already been registered in 2016 from 2015 (- 1 euro to 14 euros). And it seems that it will also be the case in 2018. Although it remains to be confirmed at the time of writing this article, we are talking about a fall in the contract price of just under 6 %, i.e. the equivalent of 90 eurocents. So the German contract is set to lose nearly 3 euros in the space of three years, and for good merchandise at that, we are not talking about category II. Furthermore, that is without counting the depressive effect of inflation, low as it is, in Europe (see inset).

The EU barometer determined every week by the CIRAD-FruiTrop cyclical forecasters, factoring in the prices of a representative panel of origins and European markets, confirms the German trend. The price per box sold lost one euro in 2017, to reach 12.6 euros. As a reminder, in 2015 it was around 14.1 euros. Studying this price on a weekly basis can teach us a lot about 2017, which was a highly complex year.


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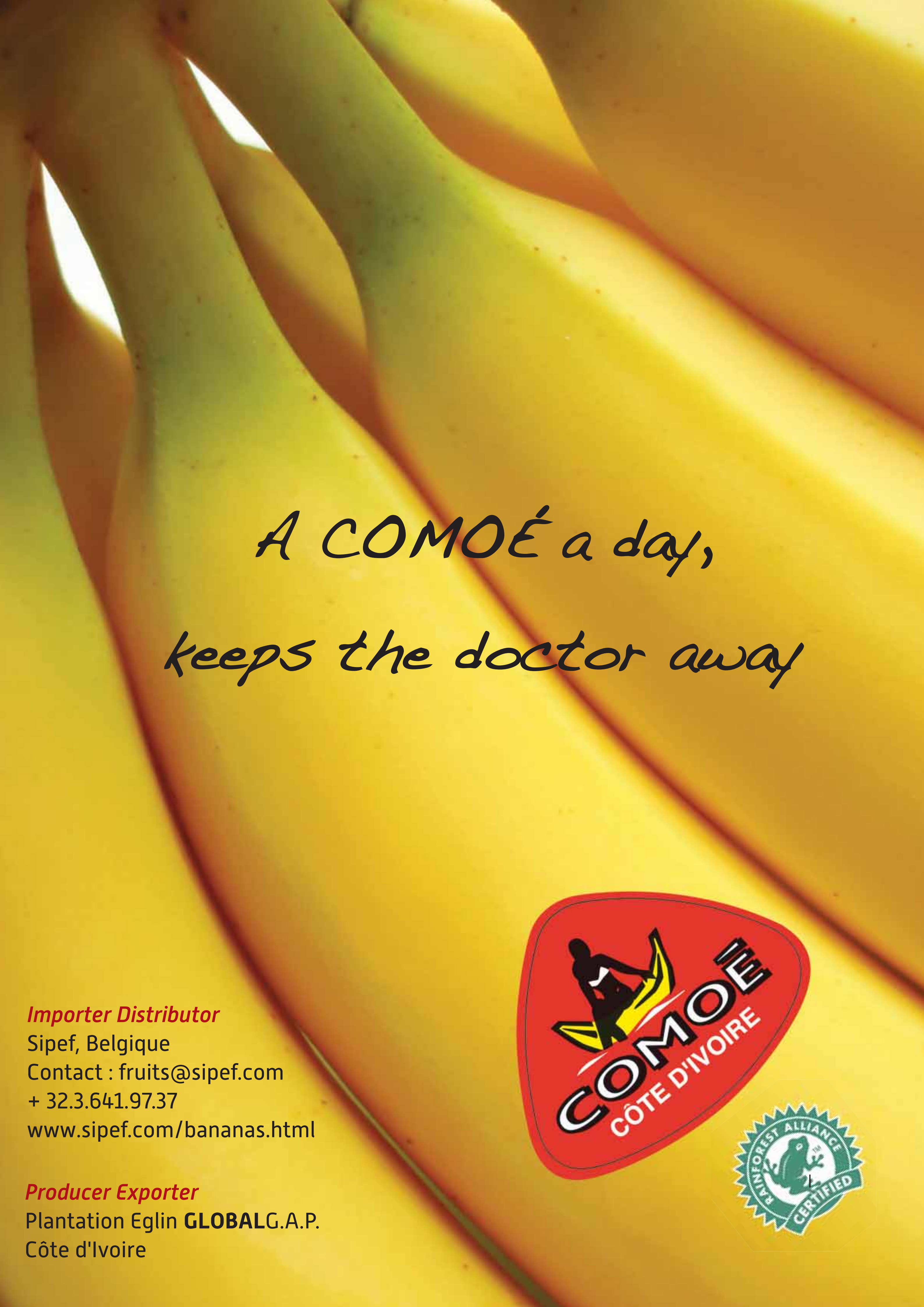
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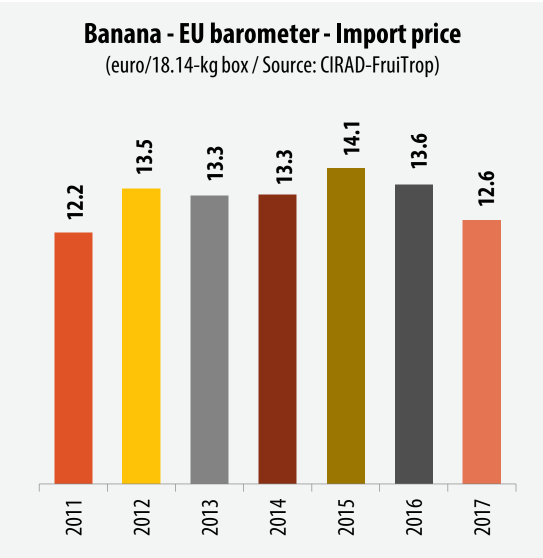

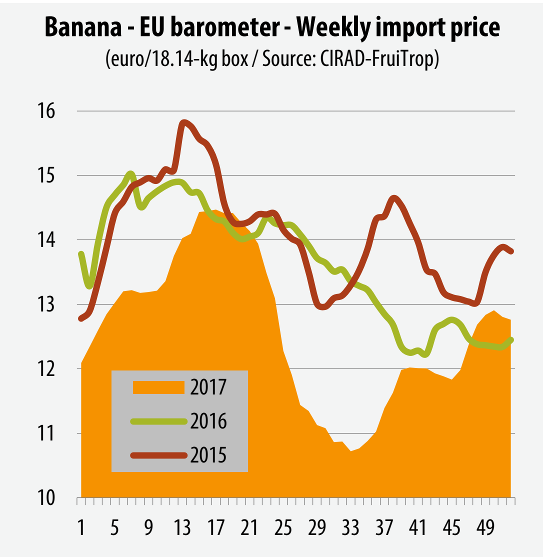

A film classed in the "catastrophe" category

To start with, we had a long take extending over weeks 1 to 14 of 2017. We might even consider that this very poor period began in September 2016, with an import price tunnel leading from bad to very bad which lasted 33 weeks in a row! The recovery was slow and laborious, with prices only climbing above the 14-euros mark in week 12. Over these first fourteen weeks, the price dropped by 9 % on average.

Then came a more positive sequence in terms of prices, which lasted a mere 6 weeks (weeks 15 to 20). Without reaching the heights, i.e. a long way off the peaks of 2015, prices climbed above their 2016 levels, to between 14 and 14.5 euros/box. Operators finally seemed to have passed the recurrent supply peaks during the first five months of 2017 (+ 5 % on the same period of 2016), after of course absorbing those of the last third of 2016. The light could finally be glimpsed at the end of the tunnel.

Barely had optimism established itself on the scene, when the market swung back into the red. Weeks 21 to 32 brought a very steep slide, with a low point of 10.7 euros in early August. The high temperatures, a very large and competitive supply of seasonal fruits (contraction and therefore overlap of the production campaigns throughout Europe) and finally a strongly increasing banana supply launched the market into one of the worst summer crises of the decade. True, not a single kilo of bananas was discarded in European ports. Consumption was dynamic, or even exceptional. Yet nor could this avalanche of volumes be expected not to adversely affect import prices.

The grand finale (weeks 33 to 52) played out with a second attempt at a recovery in the year, which took time to come together. It is true that rising from the abyss is never easy, especially at the end of the summer period. The slight technical recovery in September was a mere illusion. It was only really from week 47 that prices resolutely shot up to end the year not with a fanfare, but at least with a sort of measured calm, verging on 13 euros. The very contracted and lean campaigns for the grape (ending very early), apple and pear (small harvest and stocks at a low) supported this resurrection. Yet it was above all slightly lower pressure from the dollar origins, after a record October, which enabled this brief brighter spell at the end of the year.







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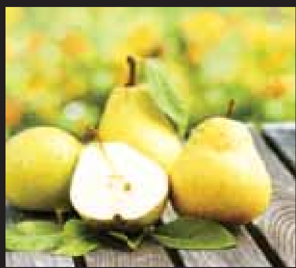








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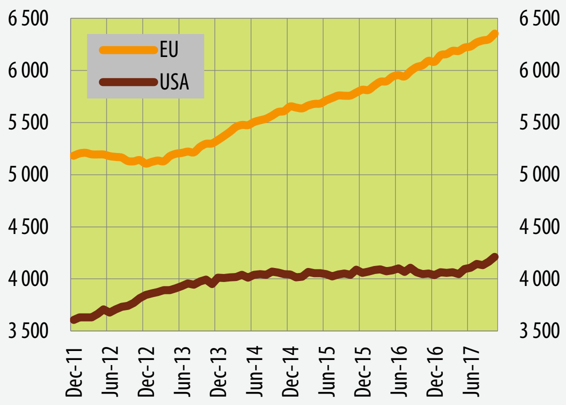
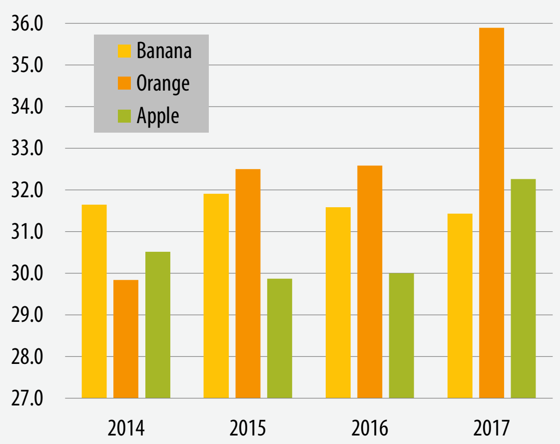
Banana - EU & USA - Estimated supply on a sliding 12-month basis (November to October)
(in 000 tonnes / sources: CIRAD, Eurostat, US Customs)

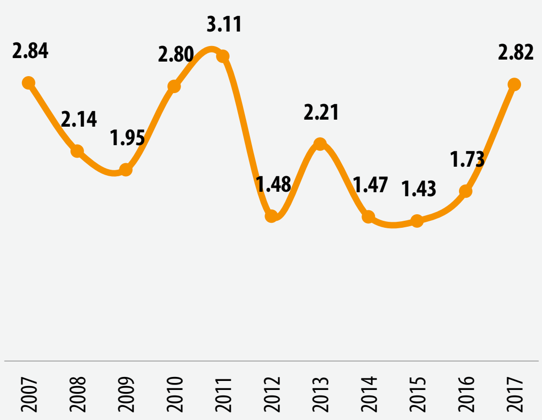


Note: each point represents 12 months of supply

Fruits - Czech Republic - Retail price
(in CSK/kg / national source)



Banana - Import price difference between Germany and Poland
(in euro/box / source: CIRAD)



"Eastern Europe" failsafe no longer sufficient

So it was a tricky year. Adversity came from all sides, both in terms of banana supply and competing fruits, especially during the summer, but also from the climate conditions in Europe, marked by several heat waves. But let's come back to the banana component of the crisis. As we already highlighted, it was first and foremost a banana influx which triggered the crisis, then amplified it and made it last. A comprehensive review will be offered in our April 2018 edition, when all the 2017 data has been consolidated. However, we might already say that over the first ten months, the banana supply from the 28 EU Member States climbed by 5.3 %, we should recall on top of a rise of 4.6 % between 2015 and 2016 (in full years this time).

Indeed the past five years (2012 to 2017) have seen Europeans scoff 1 million tonnes more of bananas, to reach a figure of 6.3 million tonnes. True, Eastern Europeans are primarily responsible for this expansion, attributable to a consumption catch-up dynamic. Yet that is still not sufficient to absorb the surplus. And this is not for lack of charging extremely attractive prices. In the Czech Republic, banana retail prices, compared to those for the apple or orange, were ultra-competitive in 2017. The heavy downward pressure on sale prices in Eastern Europe clearly shows that these countries remain clearance markets where the import price remains the only argument. If the supply into the EU is booming, prices are tumbling on its eastern flank, to the point of losing all meaning. They are flirting with an annual average decrease of 3 euros per box, a level that had not been observed since 2010 and 2011. Then again, that is only an annual average. The monthly analysis shows a reduction of 7 euros, or as much as 7.5 euros/box in July and August: a historic record! Yet even at crazy price levels (of around 7 euros/box at the height of the summer crisis, but also plenty of post-sale prices), Eastern Europeans cannot consume all the excess supply.

So the so-called mature markets are also under pressure. We will have an estimated supply balance for each Member State in our April 2018 edition, when all the figures are available for 2017. However, certain indicators such as banana activity rate in Germany, data from the consumption panels in France or Spain and the feeling among European operators indicate that net consumption climbed across the board, including on markets where big groups or big origins seemed to have greater control of the supply than elsewhere. And as regards prices, there were no more miracles on these mature markets than on the East European ones. They too made a downward adjustment in the face of this avalanche of volumes, with contractualisation limiting the damage.

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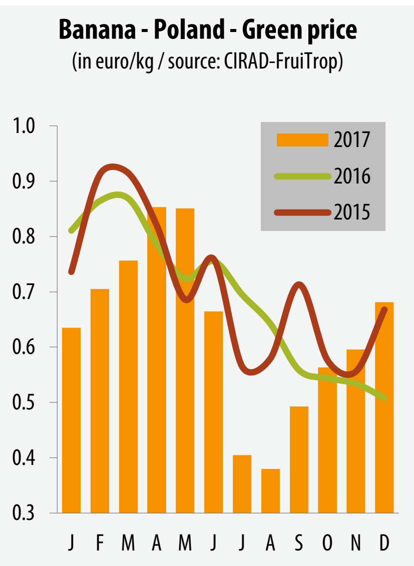
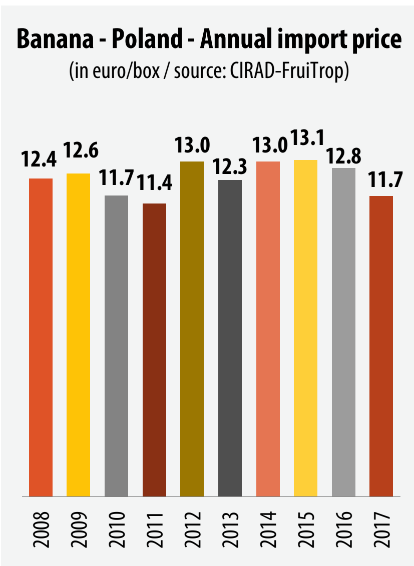
A time for the big operators

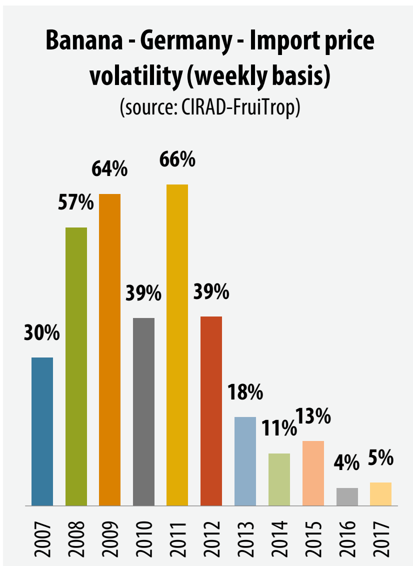
It would doubtless be a bit hasty to put everyone in the same basket. In times of crisis, it is the markets with an annual contract system which can best resist the drop, if the contracts are observed of course. True, at the end of 2016, during the upstream-downstream negotiation round, the fall in contract prices was a bitter pill to swallow. Yet looking back, it ultimately proved to be a powerful remedy to the generalised collapse. The import price curve in Germany can confirm this. The volatility of weekly import prices in 2017 remained at a historically low level, of around 5 %, yet with a ridiculously low standard deviation of 19 eurocents per box. As a reminder, the volatility was as high as 66 % in 2011, for a standard deviation of 2.4 euros/box! Levels worthy of Poland for the past decade at least.

While contractualisation offers a safety net of sorts, it also has its flip side. First, it formalises a glass ceiling which excludes once again any possible price increases. In addition, as is the case during a continuous price fall, an upturn is even more difficult. There would need to be a massive reversal in the balance of power to be able to win back the ground lost over the past two years, soon to be three years. Whereas falls take the lift, increases take the stairs.

The eternal question is to determine whether it is better to shun the contractualisation system, a question which will soon be inapplicable due to the rampant predominance of contract volumes. Staying outside means gambling that the future will be less saturated with bananas. The answer of course depends on the business structure. For those which are producers or which control their costs (high vertical integration) there is no debate; they have an increasingly financial management style, with less and less to do with economics. They must ensure that the majority of the volumes to which they are committing (whether own volumes or contract volumes) will find customers. Their managers work their spreadsheets hard, and they have the final say. Conversely, the least integrated operators manage the product and the markets more closely, with expertise in place of spreadsheets. Their volumes are also much smaller and so easier to place. These operators can adjust their fruit supply both downward and upward: especially since the spot volumes are growing as the worldwide supply expands. Hence these operators are better able to take advantage of short-term movements such as restocking, top-ups and specific demands from their customers. So we have an artisanal segment as opposed to an industrial-financial strategy.







Artisanal segment still has a future

Over the past decade, the “artisans” have rather had the wind in their sails. The highly disruptive effects of climate vagaries and strong consumption trends in Europe have enabled them to stick as close as possible to demand while keeping their distance from the phenomenon of contractualisation. Their agility enabling them to switch origin, adapt and improvise, in the final analysis to play their role as an importer to the full, has enabled these “artisans” to optimise their sale prices and very substantially improve their margins.

The situation that we have seen for the past two years, and which will go on at least through 2018, is very different. The production zones are practically all at their optimum, and there would seem to be nothing impeding the volumes race of the world supply, apart from a mild La Niña phenomenon which seems very short-lived. The commercial space is shrinking, as are opportunities. Control of all the links in the supply chain is giving the big players in the sector back some clout against the supermarket sector. They are not expected to be agile, but to be the lowest tenderers and provide a mass supply of ripe bananas, every week and at low prices, practically throughout Europe. It is up to them to make economic and financial realignments between their various functions: production, transport, import, ripening, etc. Among these, the ripening function is becoming strategic and is one of a set of logistical services that the operator must be able to offer its supermarket customers, including on a simple service provision basis.

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It is all a question of flow management. And they must be controlled from one end of the industry to the other. At the same time, they need to make economies of scale and be a sole point of contact for the retail trade. It is not by chance that many intermediate groups aspire to join the very exclusive “big players” club, which handles more than 500 000 tonnes of bananas per year, and which has substantial ripening plant networks.

As we can see, the place for the “artisans” has shrunk accordingly in these times of world overproduction. The only space still open to them consists in standing out from the competition via ultra-specific products such as top-end banana, production modes, services, etc. Their agility enables them to be more creative, but also to manage great diversity in the supply. They can definitely better serve customers demanding something specific and who can also pay for it. The example in France of “Grand Frais” symbolises a retail trade which is trying to reinvent itself, and which for the operators is a real remedy to the massive ongoing erosion of added value.

Creating value to stand out is good, and it is also the universal recipe. The citruses sector understood that before everyone else, with for example the huge varietal diversity offered, especially for easy peelers. The avocado sector adds value via the fruit stage of maturity, even offering ready-to-eat. The banality of the banana sector has now become all-conquering. Even socially and environmentally virtuous production systems, such as organic and Fairtrade, are managing to stand out less and less. As proof, in late 2017 in a French hypermarket, a loose banana from Cameroon and a pre-weighed bagged banana from the Dominican Republic, which was organic and Fairtrade labelled, sold at practically the same price (1.89 and 1.99 euro/kg respectively), and on the same shelf (see photo below). Segmentation can also be achieved by means of brand – though this is very rare – or origin, as with the French banana. Apart from these initiatives, there is only wasteland. When will we dare to offer new varieties? When researchers have finally found cultivars of interest in terms of agronomy, trade and taste. Yet also when, or rather if, distributors and producers decide to pool their resources for this diversification. Since nothing is happening, it would seem that none of them yet feels that "there is something rotten in the banana kingdom". The 2018 trend should force them to think about it more deeply.

From catastrophe to horror

The big players in production and exports, or their representatives, are nonetheless starting to be afraid. Yet they are not alone. The interprofessional association representatives and the States themselves are starting to express their fears publicly. The most responsive, i.e. the least competitive and therefore the most exposed of the dollar suppliers, such as Costa Rica, are even officially troubled by the strongly downward trend for 2018. Ecuador could end up complaining to the European authorities: which would be the last straw, when we bear in mind the trouble it has taken to dismantle the most lucrative market on the planet.

And they are of course right, especially since the ink on the report from the recent World Banana Forum, held in Geneva in November (see **FruiTrop** 253), had barely dried before the moral commitments made started drifting or being ignored haughtily. In the renegotiations of the contracts for 2018, a fairer distribution of the value or fair remuneration for the work done by the various industry stakeholders are concepts more at home in a fairy story than a realist novel.

The 2018 contract prices between importers and distributors are at least 5 to 6 % down from 2017. Some are even talking of a price into Europe for fine merchandise of below 11 euros per box. Welcome to the great price drop ride! The scapegoat has already been found, in the shape of the retail trade. As the purchaser from the rest of the industry, the downstream segment is demanding ever lower prices. In taking advantage of a blatant dissymmetry in terms of negotiating power, but also an avalanche of commercial offers and all these signals indicating that the world supply is more than sufficient, it is just doing its job. In any case, the commercial part of its job. As to the social (i.e. economic) commitments that it claims to be taking, it is maintaining radio silence.

This attitude is just as perfectly scandalous as it is tragically banal. Since, ultimately, if the distribution sector only has to wait to receive ever more indecent proposals in terms of price, it is most of all because of the excessive supply. Since everyone wants their own little corner of paradise on the European supermarket shelves, all the players are developing their production and transforming paradise into hell on earth. In focusing on fantasising that the distribution sector can solve all these problems by increasing prices, the upstream is forgetting that it too must alter its practices and comprehensively think about a supply level satisfactory for all. So should we give credence to those calling for the return of UPEB, the banana equivalent of "OPEC", as practiced incompletely and fleetingly in the 1970s for the dollar zone? This seems improbable in a world as open as the one we are living in. Yet how do we get a host of producers to understand that they must restrict their production for a common good, market balance, while they will doubtless never see the positive effects? We must also agree that managing a supply is never going to be as easy as that, so fragile is the world banana stock given its high exposure to climate vagaries, as we have seen for the past decade, but also to the quiet or explosive development of diseases and pests. To sum all that up: let's produce and pray that Mother Nature takes its share, but no more than is needed to continue to supply the export markets, but also no less than to boost world prices. What a plan!

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Rewarding shareholders no longer sufficient

In the final analysis, the market is responding to a truly classic stimulus: world supply. There are three possible attitudes to take.

Of course, they can wait for better days, i.e. climate vagaries which will ruin certain areas and therefore relieve others. Here we have chaos theory, where unpredictability is the rule. We can only make hypotheses as to the recurrence of phenomena, especially the weather. For 2018 for example, La Niña is expected to reduce the supply, unless the reverse happens causing sufficient rains in Colombia without causing catastrophes. Some are hoping to see an increase in freight rates, still on a downward trend. We might also expect the euro to tumble against the dollar, even while it is on an upward trend. As we can see, this is more akin to a lottery than a strategic vision. But what does it matter? It is only results that count.

The second attitude is clearly that of the big European and world operators: control price competitiveness, with not all the players making exactly the same choices. They are all diversifying in terms of origins by seeking, as a constant, the best place either for low-cost production of their own bananas, or production under a more or less long-term contract. That is the basis of the business. They are also all adding a layer of vertical integration ranging from pure and simple internalisation, or via contractualisation, of the transport, transit and even ripening functions.

The final attitude, which in my view has the brightest future, consists in doing all of the above, but in addition has an eye on the future, by not just marketing carbohydrates. These companies are now selling products whose social and environmental content is improving bit by bit. True, the remuneration of the shareholders is always the primary objective, but it will no longer be the sole criterion for a firm's success, even commercial. We might only regret that it is taking too long and that large swathes of this industry remain culpably passive ■

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