19 May 2009

Wheat: To trade lower on arrival pressure

Introduction:

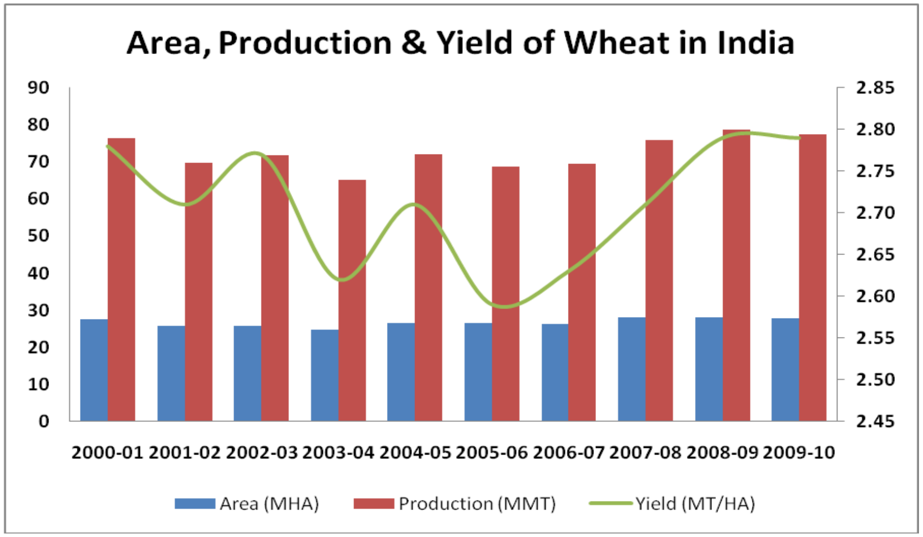
Wheat, cereal plant of the genus *Triticum* of the family *Gramineae* (grass family) that produces a dry one-seed fruit commonly called a kernel, is a major food and an important commodity in the world grain market. Wheat was one of the first of the grains domesticated by humans. Its cultivation began in the Neolithic period. Bread wheat is known to have been grown in the Nile valley by 5000 B.C., and its later cultivation in other regions (the Indus and Euphrates valleys by 4000 B.C., China by 2500 B.C., and England by 2000 B.C.) indicate that it spread from Mediterranean centers of domestication. The civilizations of West Asia and of the European people have been largely based on wheat, while rice has been more important in East Asia. Since agriculture began, wheat has been the chief source of bread for Europe and the Middle East.

Wheat is an annual crop cultivated in summer and winter seasons in different countries. For its early growth wheat thrives best in cool weather. Among the more ancient, and now less frequently cultivated, species are einkorn (*T. monococcum*), emmer (*T. dicoccum*), and spelt (*T. spelta*). Modern wheat varieties are usually classified as winter wheat (fall-planted and unusually winter hardy for grain crops) and spring wheat. And hard wheat (high gluten content) and soft wheat (high starch content) based on content.

Flour from hard wheat (varieties evolved for the most part from (*T. aestivum*) contains a high percentage of gluten and is used to make bread and fine cakes. The hardest-kerneled wheat is durum (*T. durum*); its flour is used in the manufacture of macaroni, spaghetti, and other pasta products. White- and soft-wheat varieties are paler and have starchy kernels; their flour is preferred for piecrust, biscuits, and breakfast foods. Wheat is used in the manufacture of whiskey and beer, and the grain, the bran (the residue from milling), and the vegetative plant parts make valuable livestock feed.

Production Scenario in India

India is the third largest producer of wheat in the world after European Union – 27 and China. In India, wheat is grown in Rabi season starting from October and continues till end of December. However, weather condition in Haryana and Punjab during the month of December plays a vital role in ascertaining final output.



Over the decade, area under wheat cultivation hovered in the range of 25-29 million hectares. Whatever may be the area coverage, final production will depends upon the temperature in the months of December and February.

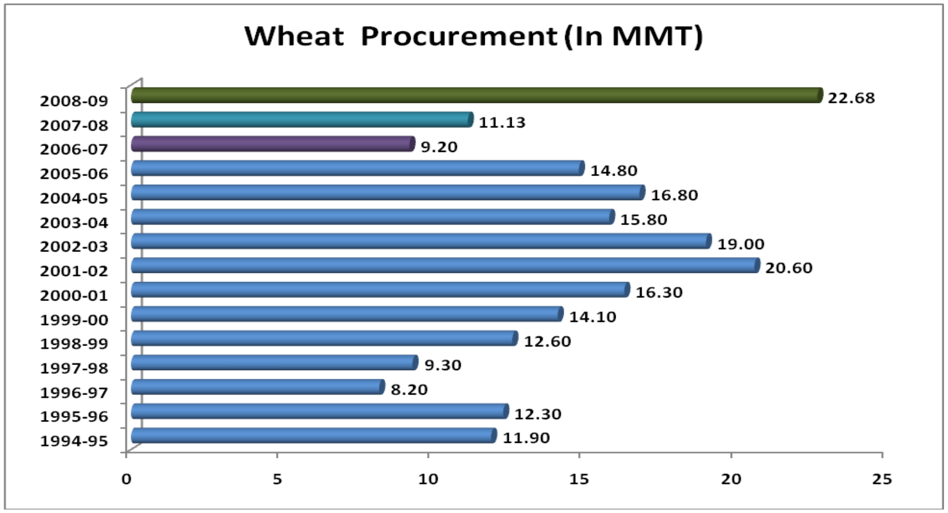
In last three years, production has been showing increasing trend due to good yield level supported by favourable climatic condition and moderate rise in acreage. For 2008-09, USDA has projected India's wheat production at 77.50 million tonnes slightly down from 78.60 million tonnes produced last year due to fall in acreage. Though the government hiked Minimum Support Price to Rs1080 a quintal from Rs1000 a quintal it failed to encourage farmers to plant more because this decision came when the crop was at maturity stage.

In 2008 Rabi season, Indian farmers have planted 27.80 million hectares of area with wheat against 28.15 million hectares sown in previous year.

Demand Situation in India

In India, wheat is one of the essential commodities, which is consumed by majority of the people. It is also one of the commodities supplied at concessional price to Below Poverty Line populace through Fair Price Shops in order to maintain food security in India. To meet any contingencies if arises from natural calamities like flood, earthquake government procure wheat and maintain it as buffer stocks. In last two years, government had procured huge quantities of wheat following bumper production and to maintain a buffer stock.

As part of government intervention scheme, the Food Corporation of India will procure wheat on behalf of government. In 2008-09, FCI had procured a record 22.68 million tons of wheat, up from 11.13 million tonnes procured in previous year.



Government policy:

The Government of India has included the wheat under its controlled commodities list because it one of the staple foods of millions of people and it is used to maintain food security in India.

Some of the Government intervention schemes are:

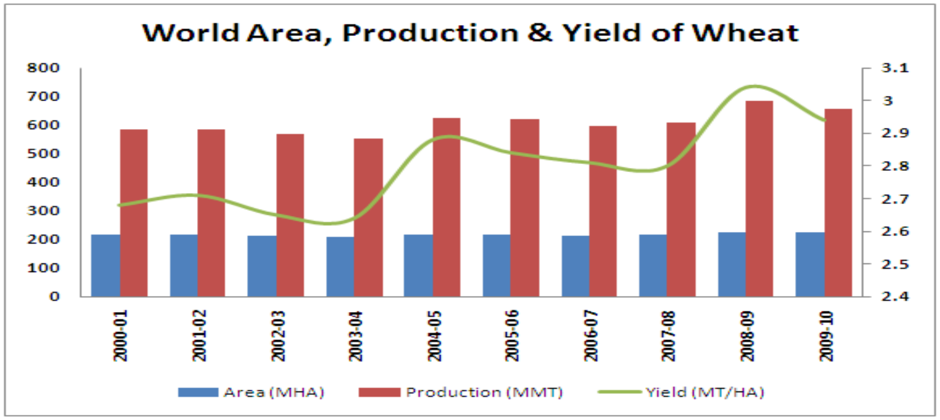
Price Support Scheme

Minimum support prices (MSP) or procurement prices are announced by the government every year at the beginning of every season. These prices are based largely on the cost of cultivation, which is systematically studied based on farm-level information every year by the Commission on Agriculture Cost and Prices (CACP). The issue prices or the price at which the grain is released to the government Public Distribution System (PDS) is fixed and revised only from time to time. The distribution is mainly by state governments through thousands of fair price shops spread throughout the country in the urban and rural areas.

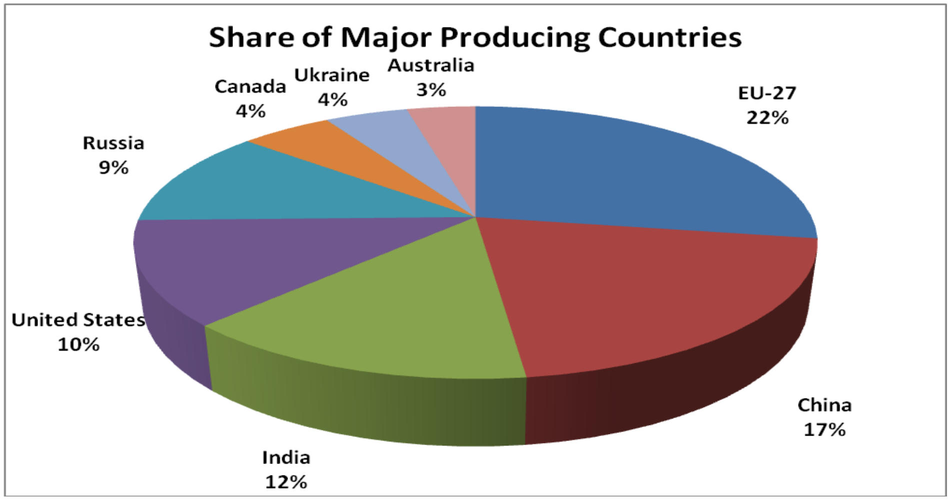
Procurement

In order to maintain food security in the country, the central government procures wheat at MSP for supplying it through Public Distribution System. It normally procures 25-30% of total production every year. The support price operation and the PDS play a significant role in maintaining reasonable and stable food grains prices in the country for both the producers and consumers. However, substantial stocks are sometimes accumulated in the process and these could rise to almost 20 million tons after the harvest and market arrivals, but decline over rest of the year.

Global Scenario



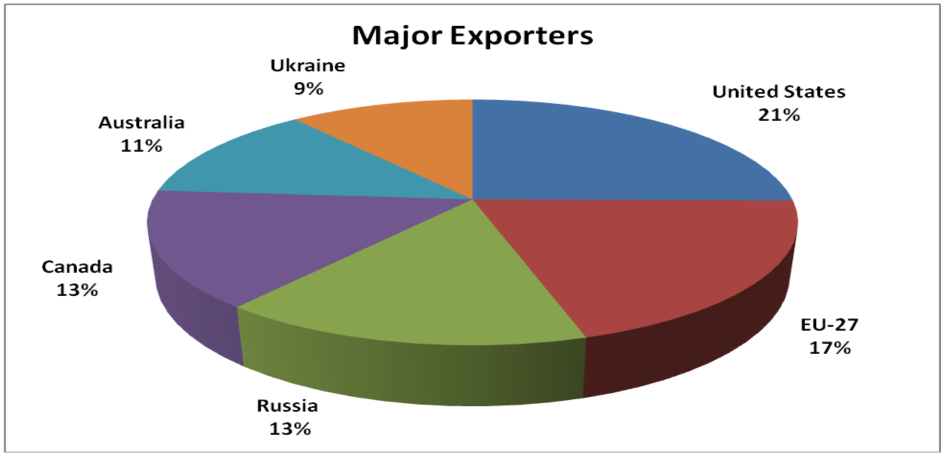
Over the decade, even though world acreage under wheat cultivation remained stagnant in the range of 210 to 230 million hectares there was a huge fluctuation in production due to varying climatic condition in different countries. In 2008-09, world wheat production increased dramatically to 682 million tonnes from 609 million tonnes seen in previous year. For 2009-10, world wheat production is projected at 657.63 million tons down by 5% from 620 million tons produced in 2005-06.



European Union – 27 is the major producer of wheat in the world with a contribution of 22% of total global wheat production. Other major producing countries are China (17%), India (12%), USA (10%), Russia (9%), and Canada (4%).

World Trade in Wheat

USA, EU-27 and Russia are the top most exporting countries. USA contributes to 21% of the global wheat export followed by EU-27 (17%) and Russia (13%). Though Australia is 8th largest producer of wheat it ranks 5th in export because it exports nearly 75% of its production, while USA exports 50% of its wheat production. Egypt, EU – 25, Brazil and Japan are the major importing countries.



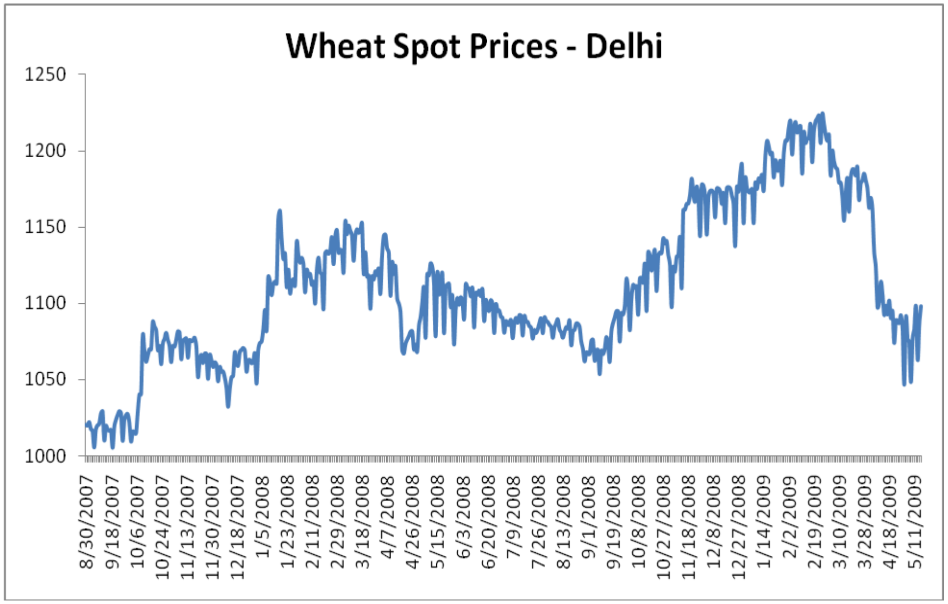
Global Balance Sheet (in Million tonnes)

	2005-06	2006-07	2007-08	2008-09	2009-10
Beginning Stocks	149.66	146.66	126.98	120.07	167.05
Production	619.56	595.62	609.70	682.68	657.63
Consumption	616.93	618.19	612.75	633.86	637.66
Ending Stocks)	146.66	126.98	120.07	167.05	181.90
Stock/Use Ratio	23.77	20.54	19.59	26.35	28.53

Spot price movement

Delhi is the terminal for wheat trading in India. Price movement in this market is considered as benchmark price for other markets across the country. Flow of the goods from major producing areas and large participation of wheat mills, agri trading corporate house made Delhi as a benchmark market. This market gets produce from Uttar Pradesh, Madhya Pradesh, Rajasthan, parts of Haryana and Punjab.

After ban on futures trading in wheat by the central government, the wheat prices in spot market ruled at higher levels. In 2008, it traded above Rs1200 a quintal because of strong demand from millers, MNCs and on aggressive government procurement.



Wheat in spot market touched all time high of 1220 in the month of February even when freshly harvested crop started moving to the market because of good demand. After making a high in February, spot prices started easing following improvement in arrivals to the market. As a result of higher arrivals prices fell drastically and presently trading at Rs1100 a quintal level.

Price Outlook

Considering the factors like full-fledged arrivals to the spot market, we expect fall in spot prices in near term. However, marginal fall in production due to lower acreage and stagnant yield level, we can expect prices to rebound in medium to long term. Higher MSP of Rs1080 a quintal may halt sharp fall in the prices. Spot prices are expected to trade below MSP for some time because of higher arrivals. Government may not procure enough quantity of wheat because it is having huge quantity in its godowns and does not have space to store more produce.

Technical Analysis

CBOT wheat prices saw a rose of more than 500 times from its life time low of 222 levels in the year 1973 to its life time high of 1334 during the year 2008. In the year 2007, prices breached its previous swing high of 746 levels and posted a new high of 1334 levels in the year 2008 since then prices fell to its trend line support levels.

Off late wheat prices fell sharply to post a low of 445 during December 2008 after witnessing the break out of its head and shoulder pattern (in weekly chart). The prices took support at its trend line after the break out of head and shoulder pattern.

After the triangle break out of the chart currently prices are trading near to its 50 weeks EMA as resistance (600 levels). A single day close above the same (600) would rally to its next resistance of 677 levels which is 23.6% of Fibonacci projection (222 to 1334). The momentum indicator weekly RSI-14 is treading at (0.57) levels slightly higher which suggest a lower correction in the prices before it actually rally. The short term lower trend is also being supported by its averages along with another indicator called ADX-17 (average directional index) which is slightly lower. Higher the ADX higher the probability of buying signals in the prices.

Our stance: We expect an initial correction in the prices supported by the above mentioned indicators. The correction on the prices may bring down to 10 and 20-weeks EMA levels. If market hold above the EMA levels prices may turn higher and move towards 677 levels. On break of the same it may test 812 levels. However, if prices fail to sustain above 677, then market might take correction towards 550-550 range.

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