

## Opportunities and limits of import replacement for South African veggie oils

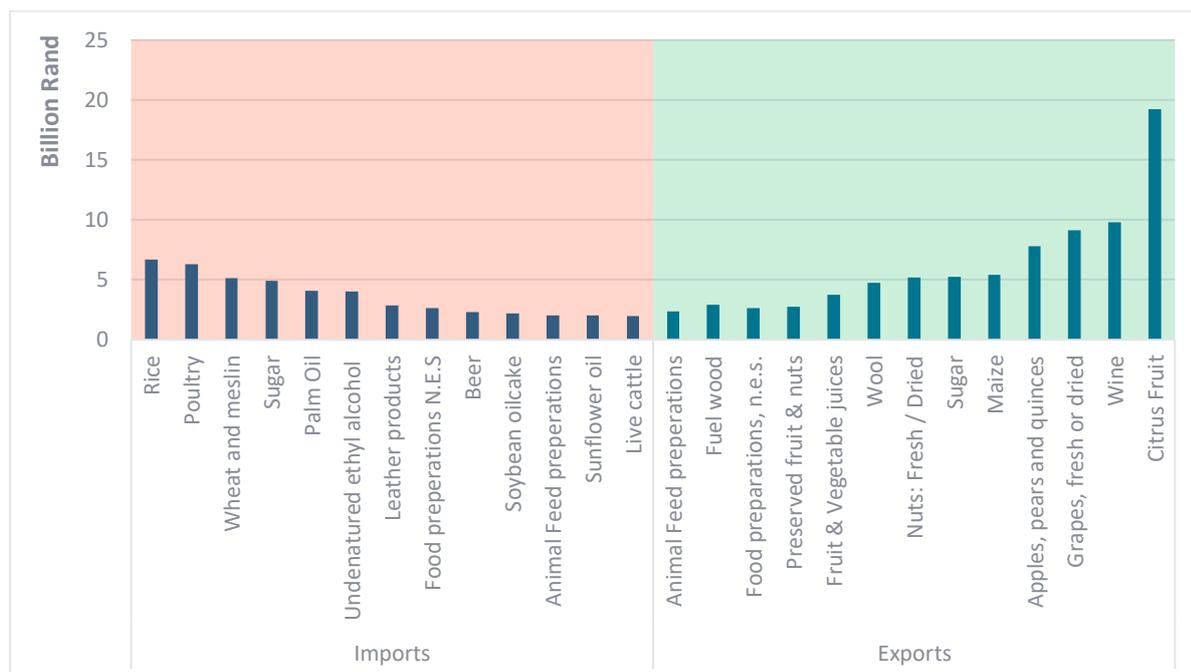
*By Ferdi Meyer and Tracy Davids*

South Africa's agricultural sector is currently in another planning phase with the drafting of the Agriculture & Agro-processing Master Plan (AAMP). This social compact between government, labour and industry is envisaged to result in practical and actionable reforms to drive inclusive growth and job creation in agricultural value chains. The foundation of this new plan is anchored on inclusive, sustained and profitable participation in South Africa's agricultural economy.

Whenever stakeholders gather to discuss reform at the sector level, import replacement or localisation of food production is often first on the agenda. Proponents argue that this boosts local production and results in higher levels of investment, economic growth, and job creation in the domestic economy as opposed to in some other countries. A wide range of policy instruments are available to achieve this, but, tariffs, and tariff quotas are used for the most part. There are, however, compelling counter-arguments that merit careful consideration.

For example, it serves little purpose to protect potential market monopolies, other forms of inefficiencies in the value chain including poor infrastructure and services or boost local production where South Africa does not have the natural resource base. There are numerous case studies in African markets where food prices are notoriously high and policymakers continue to implement blunt trade policy measures and do not address the core challenges of inefficiencies within the value chain that are driving cost structures. To illustrate these arguments, we briefly analyse the opportunities and constraints to import replacement for vegetable oils in South Africa.

Vegetable oils that are used in human diets (cooking oil, margarine, etc.) and animal feeds constitute one of South Africa's largest categories of processed food imports, with a trade deficit of R8.6 billion in 2020. Palm oil imports are the largest within this category, ranked 5th out of all food and agro-processing imports (**Figure 1**), with more than R4.5 billion being imported per annum. Palm oil imports have been growing consistently over time, more than doubling from 248 000 tons in 2001 to 525 000 tons in 2020. Just a few places down the list, annual sunflower oil imports of more than R2 billion also appear among the top imported agro-processing products. In contrast, soybean and canola oil imports have gone in the opposite direction, with the imported product consistently replaced by locally manufactured imports of oilcake. In the case of soybean oil, import volumes declined from a peak of 278 000 tons in 2011 to 150 000 tons in 2020. Based on Bureau for Food and Agricultural Policy (BFAP)'s latest outlook, less than 50 000 tons will be imported annually by 2030.



**Figure 1:** Top agriculture and agro-processing imports and exports (Avg. 2017-2019)

**Source:** Quantec, 2020

Thus, there are contrasting trends within the same industry (vegetable oil manufacturing), which beg the question: why does South Africa not replace palm oil imports with an import replacement strategy? The obvious answer is that South Africa does not produce palm or palm oil because we lack the tropical climates of the big producers such as West Africa, Indonesia and Malaysia. However, if planting palm is not an option, then why not substitute palm oil use with locally produced oil from sunflowers, soy and/or canola? To address these types of questions, BFAP has employed a detailed and end-to-end value chain approach to unpacking the underlying drivers of demand and supply, assess the overall competitiveness of these industries, and consider the best use of a wider range of policy measures.

The first element to consider is the relative pricing of vegetable oils. Palm oil trades at much lower prices in international markets than any of the other major vegetable oils and this relationship is not expected to change, despite the current spike in vegetable oil prices. Palm oil is not only a low-cost alternative to many other vegetable oils but yields up to ten times more oil per unit area than other oilseed crops.

Furthermore, the fact that there are no commercially produced genetically modified (GM) palm trees are attractive to the European market. Secondly, due to the high level of imports, local vegetable oil prices are closely linked to international prices. Therefore, from a pricing perspective, palm oil trades at a discount of approximately 25% compared to sunflower and soybean oil. Thirdly, apart from competitive pricing, the initial rapid growth in palm oil imports was ignited when the South African Department of Health drew up legislation regulating the use of trans-fatty acid in foods in 2010. The implication was that food manufacturers and many fast-food outlets required a fat alternative that did not convert to trans fats with heating, still providing the same solid texture and taste in foods without the industrial addition of hydrogen.

Palm oil provided the solution to this problem and has since taken over this market segment with little opportunity to substitute any of the other oils. A considerable amount of research has been undertaken in the development of high-oleic sunflower and soybeans, which will also comply with the health regulations. Yet, this oil cannot be produced cost-effectively in the bulk market and is currently traded only in niche premium markets.

The result is that the opportunity for import replacement in the bulk vegetable oil consumption market is limited to replacing imported sunflower-, soybean- and canola oil. Localisation strategies should be based on improved competitiveness from the farm to the processing and retailing of the product. In this regard, the production of soybeans and canola has already increased rapidly through the introduction of high performing cultivars, best farming practices and major investments in the processing and handling of canola and soybeans. However, the production of sunflower seed has concomitantly declined, and the local value chain is in distress. Therefore, rather than indiscriminately applying a blunt instrument such as tariffs on all vegetable oil imports, there is scope for more targeted interventions. To this end, BFAP recently published a comprehensive sunflower value chain report funded by the Oilseed Advisory Committee, where challenges and the required reforms are highlighted. These include stagnant yields over the recent past and lower oil content compared to other major producers.

One of the main problems identified is that, while maize is the predominant cash crop in the main sunflower seed-production regions, sunflower is often planted as a “catch crop”, with preference not being given to the timing of production, such as optimal planting date, fertiliser applications, soil analysis, or much of the required pest, weed or disease programmes required for optimal production.

Improved farming practices such as the selection of high-oil cultivars can result in significant increases in domestic production. Furthermore, an incentivised pricing mechanism has already been tested where producers receive a price premium for delivering sunflower with high oil content.

In sum, while localisation might be an ideal policy approach for other sectors of the economy, in agriculture, it is limited. Vegetable oils are just one example of the complexities and potential unintended inefficiencies of the localisation policy approach to agriculture. In our view, the focus should instead be on boosting inclusive growth through utilisation of uncultivated land in joint-venture approaches while at the same time exploring avenues of expanding export markets. Furthermore, the maintenance and expansion of infrastructure remains a critical driver to ensure the global competitiveness of South Africa’s food system.

***Ferdi Meyer** is the Managing Director at BFAP and an extraordinary professor in agricultural economics at Stellenbosch University*

***Tracy Davids** is a senior agricultural economist at Bureau for Food and Agricultural Policy (BFAP)*