

DEHYDRATED ONION MARKET REPORT
JULY / AUGUST 2010

OBJECTIVE & DISCLAIMER

This report is meant to provide a broad overview of the dehydrated onion market and is based on information gathered from trade sources. It is intended as a guide to market directions for the clients of Champagne Foods. However, we do not claim that this is definitive and neither does it constitute a binding offer to supply.

OVERALL MARKET STRUCTURE

The USA remains the dominant supplier of and consumer of dehydrated onion products ("onion"). Generally, their domestic need is for low bacti (<300k TVC/g) products, whereas Europe uses significant amounts of extra low bacti (<100k TVC/g) material, especially powders for seasoning applications.

Europe has seen a shift from dehydrated onion to fresh & chilled onion for wet food applications. Over time, the source of dehydrated onion imports into the EU has shifted away from the USA & Egypt and towards India & China.

Our dehydrated onion market updated December 2008 emphasised the rising cost of onion production worldwide due to competition for farm land from other crops and the rising cost of fuels. Since that time demand for cereal crops (notably corn) for biofuel applications has significantly decreased as conventional fossil fuel prices have reduced and the false economics of growing food for fuel have been largely exposed for what they were. However, this situation could easily reverse if oil prices take an upwards swing.

CURRENT CROP YEAR : 2009 – 2010

(Period : September 09– August 10 and going forward into the next campaign)

OVERALL SUPPLY & DEMAND SITUATION

The overall market position the 2009-2010 crop is that supply and demand in global terms have been balanced but with widely varying scenarios within the different origins. The USA processors have been hit by reduced demand as they lose market share in certain markets and in certain applications where the quality requirements have been reduced in order to keep prices low. These volumes have mainly been lost to processors in Asia, notably China and India whose gains might be shortlived in view of subsequent climatic and other issues.

REGIONAL SITUATIONS

USA:

Background:

* The largest processor, having signally managed to misread both the market and the mindsets of major buyers, was forced to reduce prices during the course of the campaign and others had no option other than to follow. Despite the "fire sale" nature of the market, they still entered 2010 with massive over stocks and it is thought that this was the driver behind massively reduced (circa 30%) plantings for 2010 harvest.

* Onion production costs in the USA have flattened somewhat as competition for land has decreased but concerns about irrigation costs in southern California will mean greater plantings further north.

Gilroy Food Ingredients

* The biggest producer Con Agra recently finalised the sale of its primarily California based vegetable dehydration business, formerly known as Gilroy Foods, to Olam International Inc, the major Singapore based commodity group, backed by the Singapore sovereign fund, Temasek. This major acquisition follows on from last year's smaller acquisition of the former De Francesco in Firebaugh Ca. This latest move consolidates the majority of the USA capacity into one company but the full implications have yet to manifest themselves

* This should bring a greater commercial acumen in what is essentially an agri based business where Olam's strengths are both well recognised and appropriate. If nothing else, the new ownership will ensure greater matching of supply with demand on a more global basis. It could be argued that the previous owners, being a more FMCG orientated business, failed to act as an industry leader and this resulted regularly in either feast or famine.

Sensient :

* Sensient continue to conduct themselves as a responsible number 2 who remain loyal to clients but who have been forced to follow the pricing lead of the largest participant.

Cascade Specialties Inc.

* This is our established supplying principal with whom CFL has been associated for almost 15 years.

* As the third and smallest of the USA processors and being exclusively based in eastern Oregon, Cascade's niche remains that of extra low, and low bacti onion powder. With that said Cascade is making significant improvements to its' piece milling operation and expects to make whiter pieces starting this Nov.

* The long day lengths and sandy soils, combined with hot summers and cold winters, all contribute to the propensity to produce a very high proportion of the output as extra low bacti material.

* Being located close to the mighty Columbia River, the irrigation issues of California do not apply in this growing area and it is envisaged that the Californians will gradually increase plantings in this region and then truck raw materials south to the processing facilities in central California.

* Cascade's established principal of retaining their cultivation within a 50 mile radius of the Cascade plant with minimal trucking remains valid and means that the fields supply the plant and the cold store only with pristine raw material which has not been subjected to excess food miles prior to processing.

* Processing from cold store will extend from September through till about February.

* Cascade prices will broadly follow those of the larger processors

General Note:

Overall onion pricing for the USA 2010 / 2011 campaign is expected to be down by circa 10% in USD terms FOT plant but this could change depending on what happens elsewhere in the world. Please read on!

EUROPE:

Background:

- * The 2009 /2010 campaign was relatively uneventful with the four processors all functioning as normal supplying their respective customer bases with a marked absence of unusual activity.
- * The vagaries of EU weather and high wage costs continue to challenge the conventional wisdom of having vegetable dehydration in Europe

France:

Sodeleg :

- * The 2010 growing season in Northern France will have been affected by hot weather in June (when much irrigation would have been needed) followed by an unusually wet July. Production start up might be a little later in the hope that the crop might put on weight during early August
- * The ratio between white and yellow onion will probably be maintained and the intention will be to sell everything that they process (probably circa 13,000 tonnes).

STL:

- * As usual, the output of STL is unknown for this current crop year – quite simply they remain apparently inactive in the UK
- * Also as usual, there remain questions over the viability of this smaller European operation.

Sensient :

Sensient's EU output & sales remain stable at around 1,200 mt of onion.

Spain:

Vegenat :

- * Continue to produce white product
- * It is thought that they might have excessive inventory

REST OF THE WORLD

Egypt:

- * Egyptian material is primarily from sweet yellow fresh market onions and has a special flavour profile, but supply remains limited by fresh market demand.
- * The Egyptian winter crop appears to have been very short with some companies not even processing anything for the dehydrated market.
- * Offers for main crop are in the USD 2600 / mt CFR range but the EU quota for duty free has been exhausted and so buyers are having to pay duty at 10% which will make prices from this origin more expensive

India :

- * There remains a huge polarisation of quality within this origin where producers are still having issues with micro levels (usually moulds) and flavour profile (inadequate or inappropriate feed stock). These issues continue to preclude progress for even the better shippers when it comes to selling powder to seasoning houses
- * The need for buyers to take great care remains at the lower end of the scale where quality, provenance and traceability are all compromised on a regular basis.
- * Overall supply, mainly of onion pieces, has the potential to again be higher but much will depend on the extent of crop damage caused by recent heavy rains which have forced up prices and could make it difficult for dehydrators to compete for affordable raw materials with the fresh market
- * It is believed that the next crop might be harvested early to try and make up for the currently prevailing shortages
- * No matter what happens, much of India's output will remain in Asia and eastern Europe where quality standards are less demanding

China :

- * Dehydrated onion from China can be of either yellow or white onion varieties although both tend to be from lower-solids fresh onion varieties. Overall, Chinese onion has a more delicate, less intense flavour to US and other origins.
- * Much of the dehydrated onion exported is of the yellow variety and the great majority is destined for the USA. The smaller amount of white dehydrated onion available is still not a match for USA origin material in terms of flavour.
- * Competition for land (cereals subsidies) has made onion cultivation less attractive to some growers so the potential for higher prices remains – but China is not always predictable.
- * Many buyers are finding themselves subject to late shipment or non shipment of contracts. Late shipments can be at least partially explained by the lack of shipping capacity as the SSL's have reduced the number of sailings but non shipment can be because of product shortage or speculation.
- * The continued threat that the RMB could be disconnected from the USD persists and will, one day, make for a significant and sudden increase in costs for everything made in China whether it be food, bicycles or Christmas decorations!
- * Similarly, China is fast becoming a significant consumer of its own production and, unless output continues to increase (either by way of indigenous capital or as the product of inwards foreign investment) this greater demand will again mean for higher export prices.

SUMMARY & RECOMMENDATIONS

Continued volatility (mainly upwards) with many agricultural commodity prices (cocoa, palm oil, cereals, soy etc) will impact on the costs of all food manufacturers globally and the potential for similar increases on lesser categories such as dehydrated onion remains ever present. In broad terms, the food industry globally has weathered the recession reasonably well and the survivors have emerged stronger but are directly affected by commodity prices which will eventually filter through to retail prices.

Two of the very few compensatory factors are the weakening of the US dollar and the overall lower costs of energy.

Overall, our recommendation is to go long (12 months minimum) with contracts for the current crop year to ensure both continuity of supply and stable pricing.