

# What's Hot: Soybean oil – simmering or bubbling?

Published 22 March 2021

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The Bloomberg Soybean Oil Subindex total return has more than doubled in the past year. After initially declining in the first three months of 2020, soybean oil prices have rallied into 2021. The natural question is whether this rally can continue? We identify several constructive factors:

- Fuel demand is rising.
- Soybean oil stocks are declining.
- Backwardation in futures curve structure is supportive.

## Fuel Demand

In the US, biodiesel production accounts for 30% of soybean oil demand. Soybean oil is the primary feedstock for biodiesel production in Argentina. With fuel demand rebounding after the pandemic driven negative shock last year, soybean oil demand is also rebounding. With biodiesel regarded as a “renewable” fuel, increased focus on renewables’ energy transition could provide a demand tailwind.

In Brazil and the US, exportable soybean supplies are down due to growing diversion of soybean oils into the fuel market<sup>1</sup>. Argentina has been able to increase its exports of soybean oil this year, but as its domestic economy recovers, its demand for biofuels could also rise. Furthermore, the Argentine Biofuel Law of 2006, which requires a 10% blend of biodiesel in diesel, is due to expire in May 2021. If the law is renewed or requires a higher blend, then the market for soybean oil could be even tighter.

## Soybean oil stocks are declining

Soybean oil production and consumption are both rising. But consumption is rising faster than production according to the United States Department of Agriculture (“USDA”) projections and thus drawing on stocks. Stocks relative to use are therefore declining, indicating a tightening market.

## Figure 1: Soybean oil stocks-to-use

*Source: Bloomberg, USDA, annual data taken as of 17/03/2021. Historical performance is not an indication of future performance, and any investments may go down in value.*

## Backwardation in futures curve structure is supportive

Soybean futures are in strong backwardation with the spread between the 1st and 2nd contract, at 1.79 cents, is the widest it has been since 1985. Commodities in backwardation enhance performance of a futures market exposure.

On 31 March 2021, the USDA will release its Prospective Plantings report. It is likely that acreage devoted to soybean planting will increase. That said, we are unlikely to see a dent on soybean demand from big export markets like China. Therefore, soybean available for the crush to convert to soybean oil could remain tight for the foreseeable future.

1 US Department of Agriculture, Oilseeds World Market and Trade, March 2021

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