



Grain Marketing Outlook Monthly Update

Weather and Yield Uncertainty Create Wild Market Swings

While the early summer saw wild volatility and a strong rally across all crops due to flooding. But as the water receded in late June, and fields were replanted, the markets slid on expectation of a return to normalcy. But for much of the eastern corn belt, there have been no rains since early July. With worries high about the crop's strength and size, this has given prices further reason to rally.

August Crop Reports

Many observers were surprised and dismayed at the August crop reports. The USDA estimated that national corn and soybean yields would be 155bu/ac and soybeans would be 40.5 bu/ac. While these were not terribly out of line with many industry forecasts, they were greeted with strong skepticism by many growers looking out their own windows, who saw late maturity plants, uneven stands, drought stress, and drownout spots. Understanding how the USDA puts its numbers together helps clarify the situation, and provides some insights into where the market may be going.

Each year, the August Crop Production/WASDE report is the first monthly estimate that incorporates yield estimates based upon actual conditions instead of trendline yields. (This isn't quite true, as the USDA has a history of adjusting the June & July reports for planting rates or other major deviations.) To do this, the USDA sends people out into fields in early August each year to weigh and measure hundreds of locations around the nation. The collected data is compared against historical yields and historical weights and measures, and forecasts are produced. This year, for example, the USDA samples produced the highest ears per acre that they've recorded, about 27,800, which surpassed the previous year's record of 27,400. Meanwhile, the grain weight estimate was higher than last years, and the fourth highest on record. So the USDA had very legitimate reasons to project a very large corn yield this year.

But I believe that bigger cause of the disconnect between the report and the growers' own perceptions was due to the time lag. In early August, when the data was collected, dryness had started to set in across the corn belt, but it was still quite modest. By the time the report was released two weeks later, many areas were quite dry, having gone four weeks without moisture, and drought stress was evident. However, the USDA could not, and does not try, to forecast such weather events. How-

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ever, one weather event that will likely matter that does not show up in the USDA forecasts is the first frost. With the very late (~2 weeks) maturity this year, even a normal first frost will likely reduce yield. An early frost could have a noticeable effect.

Corn Market: Flood? Drought? Frost?

The Corn Market has swung wildly in recent weeks as the market has tried to assess the damage to the crop from the flooding in June, as well as the areas affected by drought in July and August. Finally, with maturities running late, and August unusually cool, there are continuing anxieties about frost damage this fall.

Besides the headline number of 155bu/acre national yield, the largest change of note was the increase by 150m bushels of corn going to ethanol for the upcoming marketing year. The combination of higher yields and higher production nonetheless resulted in a 300m bu increase in projected ending stocks in the upcoming year, to 1.133bn bushels. However, the ethanol revision seems somewhat suspect to me, as it is based upon the assumption that ethanol margins are improving significantly due to lower corn prices. To this point, however, those lower corn prices have been largely offset by lower ethanol prices, leaving ethanol processing margins only slightly improved from this spring. This calls into doubt the pace at which capacity will expand for the remainder of 2008 and into 2009. At this point, enough capacity exists to meet the RFS for 2009, but only with the help of imports and credits left from consuming beyond mandated amounts in previous years. Therefore, there is some question as to whether the current 2008/09 projection of ethanol use of 4.1bn gallons is too high. The market will be closely watching new plants coming on line this fall to get some idea about the direction of capacity.

The other area of uncertainty is feed demand. With the high prices and tight margins in the livestock industries, it is clear that feed consumption will have declined this summer compared to previous months and years, but the market is still waiting for solid confirmation of the amount of that decline. Until the September

Grain Stocks report emerges, guesswork will reign, and worry will continue.

What does this mean for marketing? The market has traded largely sideways for the last few weeks, looking for direction. Each time a rally has built, it has stalled quickly; the same is true for declines. For growers with old crop left to sell, I would sell it as December Futures prices move above \$6. For new crop, marketing is harder; I think that the first question is whether we can expect to see bidding for acres this year, to which I believe the answer is yes. Given that, is there a case for pricing bushels now? I don't believe so. I think that this market has found its downside near \$5, and that there should be opportunities above \$6.50 to be had later this year, and into early winter. Also, especially for those near ethanol plants, pay close attention to basis improvements, and use those when possible.

Soybeans

While the August reports also forecast better soybean yields than had been anticipated, the reaction in the market was a bit more muted, as this was still a reduction from the July projection. The soybean market right now remains focused on the low ending stocks this year, and the projections that they will remain unchanged to the end of the '08/'09 marketing year, even with the better-than-expected yield prospects.

Besides yield, the soybean market remains anxious about '08/09 exports and the price it will have to pay to defend acres for '09/10. For '08/09, the USDA is projecting a 1bn bushel export number for soybeans. However, for the past two years, soybean exports have run significantly higher than 1bn bushels, in spite of higher prices. With no large increase in South American production foreseen this year, it is not clear that US exports will fall by 15%. This observation increases the need for soybean acres to remain unchanged or increase slightly next year. For that reason, soybean prices should also rally in the Dec-Jan-Feb timeframe, though to pick a number to which they will rally is difficult. Instead, hold off on sales, but take advantage as prices move above \$14.50.

Wheat

Between winter wheat harvest and fall harvest and winter wheat planting is always a bit of a lull in the wheat markets. The biggest issue facing ECB growers is the substantial oversupply of soft red winter wheat in the market, especially when we look at possibilities for the '09 harvest. While production was much greater this summer, and consumption increased somewhat, SRW stocks jumped from an estimated 57m bushels in 07/08 ending inventories to a projected 174m bushels in 08/09. With a total use of only 497m bushels, this translates into an ending inventory of over 30%.

Further, the wheat basis situation remains dysfunctional. When the July futures contract ex-

pired, wheat basis in NW Ohio was \$1.50 beneath futures prices. This indicates to me that the wheat futures market does not currently reflect the cash market, and should not be taken as any sort of a guide to planting decisions. Instead, as growers think about fall wheat acreage allocations, they should base their decisions on prices bid for new crop wheat at their local elevators. If, like many locations, the local elevators aren't offering bids, then adjust the futures bid with the basis contract bid. But in any case realize that even though the futures markets are bidding over \$8.50 as I write this, the real spot bid is more likely to be \$6.50 or \$7—which still can be interesting, but that \$2 makes a big difference.



Crop Progress: Corn in United States, 2008

_____ 2008, - - - - 2003-2007 Average

