Cooperative
Extension Service
University of Illinois
at Urbana-Champaign

WEEKLY OUTLOOK

Department of Agricultural Economics
College of Agriculture
University of Illinois at Urbana-Champaign

March 2, 1988

PRICING NEW CROP CORN AND SOYBEANS

Prices for the 1988 corn and soybean crops have risen sharply since futures contracts for those crops started trading last summer. December 1988 corn futures started trading in the $1.90 per bushel range and for the most part remained under $2.00 per bushel through December. November 1988 soybean futures started trading at the $5.00 per bushel level and remained under $5.60 per bushel through October.

The September 1987 *Grain Stocks* report set the stage for the subsequent rally in soybean prices. That report showed a significantly smaller inventory of soybeans than expected and forced a downward revision in the estimated size of the 1986 harvest. Prices rallied further with the Soviet purchases of U.S. soybeans and soybean meal in November. Additional price strength came in January with the downward revision in the estimated size of the 1987 harvest. Prospects for a significant reduction in carryover stocks and the belief that U.S. producers will need to be encouraged to plant more soybeans in 1988 have kept prices firm. Prospects of a record South American harvest have cooled the rally only slightly. November 1988 futures reached a contract high of $6.66 per bushel on February 19 and were trading around $6.60 per bushel on February 29.

The rise in new crop corn futures has been less dramatic. December futures reached a high of $2.20 3/4 on February 19 and were trading at $2.20 on February 29. The rise reflects an improved export situation, a downward revision in the size of the 1987 production estimate, and a surprisingly small December 1 stocks estimate. That stocks figure implies that domestic corn feeding is proceeding at a record high rate.

The market attitude remains generally bullish for both corn and soybeans. That attitude reflects expectations that acreage of these two crops will increase only modestly in 1988, that average yields will be well below those of recent years, and that the rate of use during the 1988-1989 marketing year will not be adversely affected by higher prices. The conclusion then is that carryover stocks of these two crops will be reduced sharply during the year ahead. Ideas that November futures will move to the range of $7.00 to $7.25 per bushel and that December corn will advance to the $2.45 to $2.50 per bushel area are quite common. In essence, the market is anticipating a "short crop." Short crop years generally result in early price peaks.

What are the pitfalls in the case for higher prices? There are basically two. First, increases in planted acreage of corn and soybeans could exceed current expectations. Farmers' planting intentions will be revealed with the USDA's *Prospective Plantings* report on March 31. Second, the current rate of corn and soybean use may not persist. Particularly confusing is the recent surge in feed and residual use of corn. The magnitude of use in that category is not explained by livestock numbers or the level of feeding of other grains. There is some danger that use in that category will correct back to a more normal level in the year ahead. Export prospects are also difficult to forecast because of variation in production levels outside of the United States.

What to do? It appears that the market will offer good pricing opportunities prior to the 1988 corn and soybean harvest. Factors determining how high prices could go will unfold slowly, beginning with the *Prospective Plantings* report. Marketing strategies should be centered around managing the price uncertainty from now through late summer. One approach is a scale-up pricing strategy. Pick a point to begin pricing a small percentage of expected production. If prices move higher, additional sales should be made. The goal is to have a substantial portion of the crop sold before harvest. If prices fail to rally, at least part of the crop has been priced at profitable levels.

Another approach is using the options market. Substantial early season pricing could be done at profitable prices with options providing the producer the opportunity to benefit from a subsequent price rally. Buying put options instead of selling futures or cash contracting is one general approach to using options. The second approach is to buy call options to offset new crop sales. In either case, the magnitude of the premium is the cost of the price insurance. If prices do rally, the producer will have to decide when to cash in on the increase.

Darrel Good

Issued by Darrel Good
Extension Specialist
Prices and Outlook

Cooperative Extension Service
United States Department of Agriculture
University of Illinois
At Urbana-Champaign
Urbana, Illinois 61801

FIRST CLASS