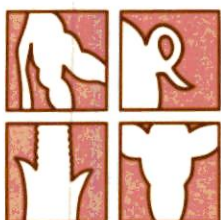




Cooperative
Extension Service
University of Illinois
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WEEKLY OUTLOOK

Department of Agricultural Economics
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University of Illinois at Urbana-Champaign

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PRICING 1989 CROP CORN AND SOYBEANS

Years with small crops and high grain prices, recent history indicates, are usually followed by years with accumulating surpluses and lower prices. The fundamental reasons for the pattern are fairly obvious: high prices bring more acres into production in the United States as well as in other parts of the world, and dry years in the United States have typically been followed by normal or nearly normal weather conditions. With the likelihood of that pattern being repeated in 1989, opportunities for forward pricing the 1989 crop should be evaluated. The fact that prices for the 1989 crop have remained relatively stable in the face of the recent sharp decline in prices for the 1988 crop make this a good time for evaluation.

Corn futures peaked on July 5, 1988, with December 1988 futures trading at \$3.70 per bushel and December 1989 futures peaking at \$2.95, a difference of \$.75 per bushel. By November 11, December 1988 futures had declined to \$2.70 while December 1989 futures were at \$2.60, a difference of only \$.10 per bushel. The spread of only 10 cents seems remarkably small in view of the fact that the transition is from an extremely small crop to probably a very large crop. The market is basically saying that next year's price will be quite close to the price of the 1988 crop. One of the fundamental reasons for the small difference in price is the expectation that the increase in production next year will be mostly offset by smaller carryover stocks so that the supply situation will be similar to the current supply situation. For that to be true, next year's crop will have to be near 7.5 billion bushels.

Corn yields will probably rebound sharply next year, but perhaps not to the average of 119 bushels per acre experienced from 1985 through 1987. Lingering effects of the drought and increased planting on lower-yielding acreage would be expected to limit the yield recovery to approximately 112 bushels. At that yield level, corn plantings will have to increase by 6.5 million acres to produce a crop of 7.5 billion bushels. Reduced set-aside requirements and relatively low prices for next year's soybean and oats crop suggest that if seed is available, planted acreage could increase by at least 10 million acres and maybe by as much as 12 million acres. If so, next year's crop could be near 8 billion bushels. Under that scenario, some pricing of 1989 crop corn seems warranted.

Sales levels should probably be a relatively small percentage of expected production if cash sales are made because of uncertainty about the weather and production. Larger sales could be justified if the futures market is used. Sales should probably be made in the December 1989 contract because the spread between July 1989 and December 1989 futures has already narrowed from 65 cents down to 22 cents. History suggests however there may still be some slight advantage to placing the hedge in July futures, expecting the spread to narrow even more by next summer.

Soybean futures for November 1988 peaked at \$10.46 on June 23, but closed at \$7.61 1/2 on November 11, a decline of \$2.84 1/2. November 1989 futures peaked at \$7.93 on June 28 and closed at \$7.23 3/4 on November 11, a decline of nearly 70 cents. The difference between November 1988 and November 1989 futures prices declined from about \$2.25 in late June to less than 40 cents in mid-November. Again, the current difference seems small when comparing a short-crop year to one with probably a normal crop. On the surface, the current price relationships indicate that old-crop prices are too low or that next year's prices are too high. Broad fundamentals suggest that the recent sharp decline in the old-crop price may be overdone. New-crop soybean prices are not high enough to buy much of an increase in acreage. With normal yields, the 1989 crop will not be any larger than the 1986 and 1987 crops unless plantings increase by more than 3 million acres.

The pricing of 1989 crop soybeans should probably be done in the futures market because of the increased flexibility. Those hedges probably should be placed in the August 1989 contract. That contract is currently 53 cents above the November contract. In each of the past 5 years, the price of November futures has been equal to or higher than the price of August futures by the first of August. In the 5 years before that, November futures remained at a discount in 3 years, but never by more than 20 cents. With a hedge in the August contract, a producer can probably lock in a price that is 30 to 50 cents above that offered by the November contract.

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