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WEEKLY OUTLOOK

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PRICING 1996 CROPS

There continues to be a lot of producer interest in pricing a portion of the expected 1996 corn, soybean, and wheat crops. There is more interest in pricing corn and wheat than soybeans due to the relatively high price of corn and wheat. The interest stems from the historical evidence that prices do not remain at high levels for extended periods of time. That is, short crops are often followed by large crops and lower prices. Currently, however, higher prices not only reflect smaller U.S. crops, but tight world stocks (particularly of corn and wheat) and continued high rates of consumption.

Producers interested in pricing 1996 crops have two fundamental questions — when? and how? The answers are complicated by generally strong world demand and uncertainty about Southern Hemisphere production. That is, historical short-crop price patterns may not be followed this year. Having said that, some observations can be offered.

In the case of corn, at least two opportunities for pricing the 1996 crop may occur. The first opportunity will likely occur early in the 1995-96 marketing year, between mid-October and mid-January. That opportunity will be associated with the short crop of 1995 and the necessity of corn prices to go high enough to reduce consumption. How high prices go and when the high occurs depends on subsequent production estimates and the emergence of evidence that consumption is being reduced. There is an outside chance that the high has already occurred (December futures at $3.1525). If not, the high may occur after the October or November production estimates or after the January production estimate and release of the December stocks estimate. It is currently our judgement that higher prices are still required to reduce consumption to fit the size of the 1995 crop. Nearby futures in the $3.25 to $3.30 range will likely be required to ration demand. We would not get locked on that target, however, if the crop estimate does not get smaller this week. A second opportunity to price 1996 crops may well occur during the growing season as prices react to any adverse weather.

Currently, 1996 crop corn prices are at a sharp discount to 1995 crop prices, as the market expects a large increase in acreage and production in 1996. At the close of trading on October 6, December 1996 futures were at a $.3425 discount to December 1995 futures.

That discount complicates the decision about how to price the 1996 crop. The most straightforward method is to recognize that the new crop price is still relatively high and accept the discount with a sale based on December 1996 futures (cash contract, hedge, or hedged-to-arrive). A second choice is to make a new crop sale by selling 1995 crop futures — July or September. That strategy is based on the hypothesis that the old crop premium will decline next spring or summer, as it has historically, allowing hedges to be rolled at a more favorable spread. There is obviously some risk in that strategy, as strong demand could maintain or even increase the size of the old crop premium. In some cases, producers are requesting or buyers are offering hedged-to-arrive contracts for the 1996 crop based on an initial sale of July or September contracts. Care should be taken that both parties understand and agree to the details of these contracts. In particular, each party should understand margin risks and obligations and the status of hedged-to-arrive contracts under the grain insurance fund.

The wheat situation is very similar to that of corn. New crop prices are at a substantial discount to old crop prices so that similar strategies need to be evaluated. Wheat prices are expected to remain well supported until the winter crop is seeded. If that crop gets a good start, prices could start a long slow decline into the harvest period of 1996. That decline, however, could be interrupted by crop concerns later in the growing season. As in the case of corn, more than one opportunity to price the 1996 crop may occur.

New crop soybeans currently carry a premium to 1995 crop prices. At the close of trading on October 6, November 1996 futures were nearly $.10 higher than November 1995 futures. The premium reflects the expectation that soybean acreage will not increase and may actually decrease in 1996. The relatively low price of soybeans suggests less urgency in pricing any 1996 crop. Opportunities for higher prices would come with any growing season concerns in South America this winter or in the U.S. next spring or summer. Based on historical price levels, November 1996 futures would be expected to trade into at least the $6.70 to $6.75 level at some time.

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