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WEEKLY OUTLOOK

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HIGHER CORN PRICES AHEAD?

Last week's newsletter outlined the likelihood of declining U.S. and world stocks of coarse grains during the 1997-98 marketing year. The unfolding supply and demand prospects for the U.S. corn crop continue to point to the potential of higher prices some time during the 1997-98 marketing year. Due to relatively small world inventories and the trend of increasing consumption, price increases for other commodities cannot be ruled out, but corn appears to have the most potential.

Traders now appear to be anticipating a U.S. corn crop smaller than the USDA's August estimate of 9.276 billion bushels. Ideas that mid to late August precipitation would add to yield potential faded as temperatures declined and some forecasters called for an earlier than normal killing frost in parts of the corn belt. Some private crop surveys supported the contention of a smaller crop. Those observations should be viewed with some caution, however, since they lack sampling rigor.

The market is also taking note of private estimates of a much smaller Chinese corn crop in 1997. In its August report, the USDA estimated the potential for the Chinese corn crop at 4.33 billion bushels, compared to last year's crop of 5.018 billion bushels. The smaller crop is expected to reduce China's net exports of corn from 105 million bushels this year to 30 million bushels during the upcoming marketing year. Some estimates for the Chinese crop are as low as 3.6 billion bushels. If the crop is significantly smaller, China would be expected to be a large net importer of corn in 1997-98. Some analysts are suggesting China could import 350 to 400 million bushels of U.S. corn during the year ahead. China imported 87 million bushels of U.S. corn during the 1995-96 marketing year, none during 1996-97, and has not purchased any U.S. corn for delivery during the 1997-98 marketing year. In fact, China continues to export corn from last year's harvest. An already small projection for U.S. stocks at the end of the 1997-98 marketing year would become even smaller with large Chinese purchases. Some increase in prices would be required to ration the available supply.

In addition to the size of this year's corn crop in the U.S. and China, the market is being influenced by the strong El Nino weather pattern. There is not complete agreement about the implications of the current pattern on world and U.S. crop production potential during the year ahead. Much apparently depends on further development of the pattern and the timing and speed at which the pattern reverses. The bottom line is that the market is anticipating a continuation of very unsettled weather which could lead to additional production shortfalls in

1998. The last time the El Nino pattern significantly impacted U.S. weather and crop production negatively was 1983. Concern about such an impact surfaced in early 1992, but quickly faded as growing conditions became very favorable in the U.S.

What To Do. December 1997 corn futures established a contract high of $3.10 in August 1996, declined under $2.60 this past winter, rebounded to $2.98 in March, declined to $2.275 in July, and rebounded to $2.78 last week. This roller-coaster pattern of prices may well continue into the year ahead. If so, more than one good opportunity to price the 1997 crop will be available. In general, then, total pre-harvest sales may be limited to modest quantities. Current strength, and any additional strength prior to harvest, would be an opportunity for catch-up sales if the higher prices of March and April were not captured on a portion of the crop. Ownership of a significant portion of the crop appears to be warranted on the basis of the major uncertainties ahead.

On that portion of the crop owned beyond harvest, the market will dictate the best choice for ownership. A weak basis and large carrying charges favor storage. As of August 22, the December basis in central Illinois averaged $-.19. With a $.16 carry from December to July futures and an expected basis of $-.05 in June 1998, the market is paying about $.30 to store corn from harvest to June. The spreads have narrowed somewhat as the price level has increased. A continuation of that narrowing and/or an improvement in basis would make storage less attractive and require an evaluation of alternatives -- owning futures or call options directly or indirectly with cash related contracts.

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