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WEEKLY OUTLOOK

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CROP MARKETS ABSORB A LOT OF NEGATIVE NEWS

Corn, soybean, and wheat prices have been hit by generally negative developments since November. March corn futures have declined about $.45 per bushel since mid-October; July wheat futures have dropped about $.60 since late October; and January soybean futures have lost about $.85 from the mid-November high. January soybean meal futures have declined nearly $40 per ton (17 percent) while January oil futures have declined only about $.017 per pound (6 percent).

As we have pointed out in previous letters, the October rally in prices was driven by speculative buying based on El Nino concerns and enthusiasm about export demand. The list of negative price developments over the past two months is extensive. These developments include generally favorable weather conditions in South American soybean growing areas; absence of widespread dry conditions in South African corn growing areas; very favorable conditions for the U.S. winter wheat crop; continuation of Chinese corn exports; availability of grain for export in Eastern Europe; an extremely slow pace of corn exports and export sales; sharp declines in U.S. livestock prices, particularly for hogs; economic and financial problems in southeast Asia; and indications of and concerns about a period of deflation in the U.S. and world economies. While the strong El Nino weather pattern continues and some unusual weather events are occurring, no widespread crop threats have developed at this point. Last fall the attitude was that severe crop problems would develop "somewhere" in the world "sometime" in 1997-98. The attitude now seems to be that problems may be avoided and that the market will wait on the fact rather than trade the expectation. Without major crop problems, and with additional planted acreage as more land comes out of the Conservation Reserve Program and acres of other crops are shifted to corn, soybeans, and wheat, additional supply pressures could develop in the year ahead. Substantial farmer ownership of the 1997 crops also suggests ample near term supplies.

Even though prices have declined sharply in recent weeks, it is tempting to become more negative about price prospects over the next several months. This is particularly true for corn and wheat prices, because 1998 crop prices still carry a substantial premium to 1997 crop prices. There is some potential, however, for the recent price action to be reversed in the weeks ahead. The first opportunity will be the array of USDA reports released on Tuesday morning. These reports will include the final 1997 corn and soybean production estimates, the estimates of grain stocks on hand on December 1, 1997, updated consumption and carryover projections for U.S. crops, updated world supply and demand estimates, and the estimate of U.S. winter wheat acreage. With so much negative news already influencing prices, there may be room for a friendly surprise in these reports. The most important estimates will be the final production estimates, the estimate of December 1, corn inventories, and the winter wheat acreage estimate.

With world crop inventories still at relatively low levels, the market will have to reflect any significant threats to production in 1998. Southern hemisphere corn and soybean crops are nearing the most critical stages of development and the entire planting and growing season is ahead for the northern hemisphere. Weather related price rallies almost always occur, although the magnitude varies considerably.

A third area of potential price strength is associated with Chinese corn trade. Based on USDA estimates of crop size, the need for China to import U.S. corn sometime later this year cannot be ruled out. Several reversals in the flow of corn in and out of China have occurred in recent years. It is difficult to assess the likelihood or timing of these or any other price supportive developments. Beginning in November, we recommended defensive pricing strategies using options. Some downward price protection may still be warranted.

We have argued that one of the implications of the new marketing environment would be increased price volatility within the marketing year. Corn futures for the 1997 crop have traded to the $2.95 level twice (March and October, 1997). Soybean futures have also traded to the $7.50 level twice (March and November, 1997). Will a third pricing opportunity present itself yet this year?

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