UNIVERSITY OF ILLINOIS EXTENSION

WEEKLY OUTLOOK

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MARKET STILL MULLS POTENTIAL CROP SIZE

Weather conditions, weather forecasts and production prospects continue to dominate the corn and soybean markets. Last week's price action was dominated by talk of "irreversible" damage to the corn crop and prospects for continued hot, dry weather over a large part of the midwest. December 2002 corn futures traded to the highest level for the summer and within $.065 of the contract high. November soybean futures regained much of the loss experienced between July 23 and July 29, but remained well below the contract high of $5.65 established on July 23. Weekend precipitation in Iowa and parts of the upper midwest, along with forecasts of cooler temperatures, suggested that prices would start this week on a weaker tone.

Summer weather conditions often provide volatility to the corn and soybean market, but the almost daily "yo-yo" pattern of prices this year is a little unusual. There are at least two fundamental reasons for the pattern of quick price reversals experienced this year. First, there is a significant difference of opinion about yield potential for the 2002 crop. Forecasts by those quoted in the press vary by as much as 15 bushels per acre for corn and 4 bushels per acre for soybeans. For corn, the difference in yield expectation represents about 1 billion bushels of production. For soybeans, the range in expectations represent about 360 million bushels of production. The wide range of expectation reflects the fact that crop stress has continued into the reproductive stage of crop development.

A second reason for the large daily price changes is that U.S. and world stocks of grains and oilseeds are small enough that changes in 2002 production prospects have significant implications for the magnitude of price that is necessary to clear the market during the year ahead. Year ending stocks of U.S. soybeans will be especially small and corn inventories will represent less than a 2-month supply. There is little cushion for a shortfall in production in 2002. The current situation is one that has been anticipated for several years. Markets have become accustomed to small inventories and production has been large for 6 consecutive years. However, market analysts have generally warned that low inventories would translate into volatile prices if and when production was threatened.

For corn, harvested acreage for grain is expected to be near 72 million acres this year. At the low end of yield expectations , about 120 bushels, the crop would total 8.64 billion bushels. Last month, the USDA projected a market for 9.96 billion bushels of corn during the 2002-03 marketing year, if prices averaged near $2.00. That combination of production and consumption would project to year ending stocks of about 300 million bushels. Inventories cannot be reduced to such a low level, so prices would have to increase enough to reduce consumption by 300 to 400 million bushels. The strength of demand would determine how high prices would have to be to accomplish the reduction. At the high end of yield expectations, about 135 bushels, the crop would total about 9.72 billion bushels, resulting in ample carryover stocks of about 1.4 billion bushels. Under this scenario, the average price would not likely be much above the $1.90 average of the current year.

Harvested acreage of soybeans is also expected to be near 72 million acres. A yield near the low end of expectations, about 35 bushels, would produce a crop of 2.52 billion bushels. A crop of that size would require consumption to be about 250 million bushels less than projected by the USDA last month. An average yield of 39 bushels would produce a crop of just over 2.8 billion bushels. A crop of that size would result in a further reduction in inventories, but would allow use to be at the level projected by the USDA. These two scenarios have very different price implications.

Price stability will not likely return until the market is comfortable with production prospects. The USDA's August *Crop Production* report will provide the starting point for refining these expectations, but confidence in production prospects may be delayed until the September or October report. History for those years when a small crop occurs, or is expected, suggests that prices will experience an early peak this year. The high may have already occurred, or it could come as late as November, underscoring the difficulty of making pricing decisions. We have advocated the use of an averaging strategy on a portion of expected production to ensure that at least some of the crop gets priced in the window of opportunity for high prices.

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