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CROP PRODUCTION UNCERTAINTY TO PERSIST

The USDA will release the September forecast of the U.S. corn and soybean crops, as well the monthly updates of projections of world crop production and consumption, on September 12. The projections of U.S. crop size will be of most immediate interest to the market. Corn prices rallied sharply following the USDA's August production report. On a closing basis, December futures moved from \$2.615 to \$2.8475. Late August precipitation pushed that contract \$.18 lower by the end of August. By the close on September 6, however, December futures had recovered to \$2.8325. A new contract high of \$2.96 was reached on September 9. The latest rally was fueled by sharply higher wheat prices and some concern that late season weather conditions may have trimmed yield potential in some areas.

For the third consecutive year, the midwest growing season has finished on a warm, dry note. While the market will react to the September production forecast, considerable uncertainty about crop size may persist into October and November. In 2000, both the corn yield and production forecasts were about unchanged in September, but declined in October and again in November. The November production forecast was 315 million bushels, or 3 percent, smaller than the August forecast. In 2001, the yield and production forecasts declined marginally in September, but increased in October and again in November. The November production forecast was 280 million bushels, or 3 percent, larger than the August forecast.

Soybean prices also rallied following the USDA's surprisingly small August production forecast. On a closing basis, November futures moved from \$5.2525 to \$5.73. As in the case of corn, late August rainfall pushed November futures to a close of \$5.39 on August 29. By the close on September 6, November futures were back up to \$5.60 and that contract traded to \$5.80 on September 9. Late season weather conditions, along with relatively large exports of soybeans and higher wheat prices, contributed to the higher prices of last week.

The soybean yield and production forecasts in 2000 and 2001 followed a pattern similar to that of corn forecasts. In 2000, the yield and production forecasts declined each month from September through November. The November production forecast was 219 million bushels, or 7.3 percent, below the August forecast. In 2001, both the yield and production forecasts declined from August to September, but increased in October and again in November. The November production forecast was 56 million bushels, or 2 percent, larger than the August forecast.

In addition to U.S. corn and soybean production forecasts, the market will also be interested in projections for spring wheat production in the U.S., total wheat production in the rest of the world,

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corn production in China, and soybean production in South America. Last month, the USDA's wheat production estimates revealed larger crops than in 2001-02 in Western Europe, India, and Turkey. Smaller crops were expected in Canada, Australia, Argentina, and Eastern Europe. For corn, the August projections revealed prospects for a much larger (nearly 10 percent) crop in China due to higher average yields than in 2001. Some observers expect that the projection will increase this month. The USDA has projected a 7.4 percent increase in South America soybean production in 2001, reflecting a 6.5 percent increase in acreage and a 0.8 percent increase in average yields. The size of both the Chinese corn crop and the South American soybean crops will influence the export demand for U.S. crops during the 2002-03 marketing year.

Unless U.S. and world crop projections are much larger than now expected, supplies will be relatively tight during the 2002-03 marketing year. U.S. and world stocks of coarse grains, wheat, and soybeans are expected to decline significantly by the end of the 2002-03 marketing year. At this juncture, however, supplies are expected to be large enough to sustain world consumption at current, or even higher, levels. While consumption of U.S. soybeans, and perhaps feed grains and wheat, will have to be reduced, it now appears that world consumption will not have to decline. That scenario could change, depending on how crops in the southern hemisphere develop. In addition, the expected low level of inventories means that prices will be very sensitive to the prospective size of the 2003 crops in the northern hemisphere.

The shift from the pattern of large crops, low prices, and expanding consumption of the past three years has given way to one of small crops and reduced inventories. That shift suggests that the volatile prices of the past few years will continue, but that prices may continue to trade at a higher level, at least for several months. This price pattern will likely provide attractive prices for the 2002 crop and perhaps the 2003 crops. A conservative approach to pricing 2003 crops should be considered, given the uncertainty about crop size next year.

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