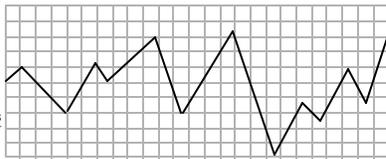




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POTENTIAL FOR POST-HARVEST RALLY IN CORN PRICES

Harvest time corn basis in 2002 has been very strong in many areas, perhaps record strong in some markets. The small crop and resulting ample storage space account for part of the strength in basis, as does strong domestic demand in some markets. In addition, producer sales are generally reported as light as producers apparently believe that there is a strong possibility of a post-harvest rally in prices.

In each of the past four years there has been modest to significant recovery in cash prices in central Illinois, for example, from harvest lows. That recovery occurred by early November to early December. In 1998, the cash price in that market reached a low of \$1.72 in mid-September and recovered to \$2.14 by mid-November. In 1999, the cash price bottomed at \$1.67 in early October and rallied to \$1.87 in early November. In 2000, the harvest low of \$1.51 occurred in mid-September, with a price rally to \$1.98 by mid-November. Last year, the harvest low of \$1.79 came in the third week of October, with a recovery to \$2.00 by the first week of December.

The composition of the post-harvest recovery in cash prices is important. In 1998, \$.22 of the \$.42 recovery in cash price came from basis improvement. In 1999, \$.17 of the \$.20 recovery in cash prices was from basis improvement. In 2000, \$.20 of the \$.47 recovery was from basis improvement and last year, \$.13 of the \$.21 recovery was from basis gain.

The other similarity in the price pattern in each of the past four years was the significant decline in cash prices from spring before harvest into harvest. In each of those years, the cash bid for harvest delivery peaked in March. The decline from the spring peak ranged from \$.40 to \$1.00 per bushel.

The price pattern for the 2002 crop has differed from that of the previous four years in every respect. First, the harvest time price is significantly higher than in each of the previous years, currently averaging about \$2.40 in central Illinois. Second, the price is about \$.50 higher than spring time harvest bids. Third, the harvest time basis bottomed at about \$-.15 this year compared to \$-.30 to \$-.35 in the previous four years.

The elements that generally result in a quick recovery in cash prices following harvest, namely a weak harvest basis and a significant decline in cash prices into harvest, do not exist this year. The implication is that higher cash prices will have to be generated more by higher futures prices than by an improving basis. Higher futures prices in turn, will require a change in market

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fundamentals, either a smaller production forecast in November or a rate of consumption that exceeds current projections. History is not on the side of a lower production forecast. The November forecast has been equal to or above the October forecast in 15 of the past 20 years and in 5 of the past 6 years. Yield reports this year do not point to a lower forecast.

In the short run, then, the burden of higher prices seems to fall to consumption. For the year, the USDA has forecast a 6 percent increase in domestic processing use of corn, reflecting an expected 15 percent increase in use of corn for fuel alcohol. There is no reason to doubt the projected increase, with monthly consumption figures confirming the expansion. Exports of U.S. corn are expected to increase by about 5 percent during the current year, to a total of 2 billion bushels. Through the first 8 weeks of the marketing year, cumulative export inspections are about 28 percent less than shipments of a year ago. The lack of shipments to South Korea is of most concern as the decline reflects on-going exports from China. Unshipped sales as of October 17 were 7.5 percent less than outstanding sales of a year ago. Again, smaller sales to Asian destinations are of most concern. While it is still early in the marketing year, there is some concern about the U.S. export potential this year. It will likely require large imports by Mexico and Canada to propel exports to the projected level.

Finally, the USDA projects a 3.6 percent decline in feed and residual use of corn during the current marketing year. The projected decline reflects an expected reduction in the number of animals fed and a decline in the amount of grain fed per animal. The USDA's *Monthly Hogs and Pigs* report released on October 25 confirmed a decline in the size of the breeding herd. Based on the projected quarterly pattern of livestock production, most of the decline in feed and residual use would be expected to occur later in the marketing year. The first indication of use will come from the December 1 *Grain Stocks* report to be released on January 10.

While prospects for a quick recovery in cash corn prices do not appear as likely as in recent years, the generally low level of U.S. and world inventories should prevent a significant decline in prices in the near term. It may be that prospects for the size of the 2003 crop in the U.S. will become the most important price factor.

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