WEEKLY OUTLOOK

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CAN THE SOYBEAN CROP BE AS GOOD AS IT LOOKS?

Soybean prices declined sharply following the USDA's August 11, *Crop Production* report, even though the soybean production forecast was nearly 100 million bushels less than expected. The decline, at least in part, reflects expectations of a larger production forecast on September 12.

November 2006 soybean futures traded between $5.90 and $6.40 from mid-January 2006 through August 10, 2006. That contract settled at $5.515 on September 1, just $.095 above the contract low established in February 2005. The average spot cash price of soybeans in central Illinois traded to a 2005-06 marketing year low of $5.065 on August 28. That was $.99 below the high established on January 4 and $.085 below the 2005 harvest low. Prices have declined even though consumption has remained large. Consumption of soybeans during the 2005-06 marketing year ended on August 31 likely exceeded the most recent USDA projection of 2.832 billion bushels. The August crush needed to total only 128.3 million bushels to reach the USDA's projection of 1.725 billion bushels for the year. The crush in August 2005 was 130.3 million. Census Bureau export estimates are only available through June 2006, but USDA export estimates for July and August suggest that exports for the year reached 935 million bushels, 5 million above the current USDA projection. Seed, feed, and residual use for the year will not be known until the release of September 1 *Grain Stocks* report on September 29.

Improving crop conditions have offset the positive impact of the high rate of consumption. The percentage of the U.S. soybean crop rated in good or excellent condition increased for three consecutive weeks ending on August 27 . As of that date, 59 percent of the crop was rated in good or excellent condition, well above the long term average for that date and 6 percentage points above the rating of a year earlier. The states with the highest percentage of the crop rated good or excellent were Kentucky (80 percent), Indiana (73 percent), Illinois (70 percent) and Iowa (69 percent). The improved crop ratings suggest that the 2006 U.S. average soybean yield could exceed the August forecast of 39.6 bushels. Historically, the percentage of the crop rated good or excellent at the end of the growing season has explained 85 percent of the variation in the annual trend-adjusted national average yield of soybeans. Since 1986, the actual average yield was within 1.1 bushels of the predicted yield in every year except two. The actual yield was 2.77 bushels lower than predicted by crop ratings in 2003 and 1.99 bushels higher than predicted in

2005. In 2003, the low yield was generally explained by the widespread presence of soybean aphids.

Good vegetative appearance of the soybean crop does not always get translated into pods and seeds. In addition, we don't know what the crop condition ratings will be at the end of the season. If 59 percent of the crop is rated in good or excellent condition at the end of the season, historical relationships would suggest that the most likely average yield would be 42.2 bushels per acre, with a high degree of confidence that the yield would be within one bushel of that forecast. If harvested acreage is near the 73.935 million acres projected by the USDA, an average yield of 42.2 bushels would produce a crop of 3.12 billion bushels, 192 million larger than the USDA August forecast and very near the record crop of 2004.

Assuming that September 1, 2006 U.S. soybean inventories will total 505 million bushels, (10 million less than currently projected by USDA) and allowing for use during the 2006-07 marketing year to exceed the current projection of 2.996 billion bushels by 20 million bushels, stocks on September 1, 2007 could exceed 600 million bushels with a yield of 42.2 bushels. That level of stocks would point to a 2006-07 marketing year average farm price of about $5.35. At the close of trade on September 1, the futures market reflected an average farm price of about $5.50 for the year ahead. On the surface, then, it appears that the market has already factored in a much larger soybean crop than forecast in August. Additional downside pressure is possible if the September production forecast is near 3.1 billion bushels. With harvest bids near or below the loan rate, there is no incentive to price additional amounts of the 2006 crop for harvest delivery, unless further price declines are expected through the harvest period. Bids for post-harvest delivery generally exceed the loan rate, so there may be opportunity to collect loan deficiency payments on the stored crop and price at least a portion of that crop for later delivery.

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