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SOYBEAN PRICES – MANY FACTORS AT PLAY

Soybean prices have moved sharply higher since mid-August. November 2007 soybean futures traded to about $8.00 in mid-August, established a contract high of $9.965 on September 19, and closed at $9.79 on September 21. The average spot cash price of soybeans in central Illinois was near $7.50 in mid-August and at $9.165 on September 21.

Soybean prices have been supported by the smaller U.S. supply of soybeans forecast by the USDA on September 12, the need to motivate an increase in soybean acreage in South America, and prospects of continued strong Chinese demand for soybeans. These three factors: the size of the U.S. crop, South American acreage, and Chinese demand – will continue to direct prices. In addition, prospects for U.S. soybean acreage in 2008 will have significance for price direction.

The USDA projects that the 2007-08 marketing year ending stocks of U.S. soybeans will total 215 million bushels, or 7.3 percent of projected use. Consumption is forecast at 2.964 billion bushels, 127 million less than he record use during the 2006-07 marketing year. The expected decline is for exports, as the South American share of the world soybean market is projected to grow from 52 percent in 2006-07 to 61 percent this year. The projected U.S. crop of 2.619 billion bushels reflects a national average yield of 41.4 bushels per acre, the lowest in 4 years and 1.6 bushels below the record yield of 2005. Like corn yields, reports of actual soybean yields have been relatively high, suggesting that the average may be higher than currently forecast. The early yield forecasts (August and September) are based partly on a survey of producer expectations of yields. Reported expectations may have been below the actual yields being experienced. Soybeans will remain in tight supply, but perhaps not as tight as currently forecast.

In its report of September 12, the USDA projected a 6 percent increase in soybean acreage in Argentina, a 4 percent increase in Brazil, and a 4.5 percent increase in all of South America. On the surface, projected acreage and average yields in South America in 2008 would appear to fall short of offsetting the 18 percent decline in U.S. production. However, current stocks of soybeans in South America are quite large. Stocks at the end of the 2006-07 marketing year are estimated at 1.545 billion bushels, or 61 percent of projected use. Stocks at the end of the 2007-08 marketing year are projected at 1.42 billion bushels, or 52 percent of projected use. The stocks-to-use ratio is large since the USDA adjusts the South American marketing year to an October through

September year, about the middle of the actual marketing year. There may be room to reduce stocks even further during the 2008-09 marketing year so that increased consumption doesn't have to be met entirely with increased production. The recent strength in soybean prices may motivate a few more acres to be planted to soybeans as well.

U.S. soybean exports will depend heavily on Chinese demand. As of September 13, the USDA reported that export commitments for delivery to China in the 2007-08 marketing year totaled 174 million bushels, compared to 125 million bushels that had been committed a year earlier. Last week, China announced at least a temporary reduction in the import tax on soybeans, from 3 percent to 1 percent. The reduction is aimed at increasing imports to augment the small harvest and to help curb the inflation in food prices. For now, Chinese demand for U.S. soybeans will likely remain strong, encouraged to some extent by the low value of the U.S. dollar.

U.S. producers may need to increase soybean acreage in 2008, depending on the outcome of the South American crop and prospects for world stocks. Some early surveys suggest that U.S. producers have already planned a significant increase in acreage, motivated by opportunities to sell the 2008 crop above $9.00. However, 2008 corn prices near $4.00 makes corn a potentially more profitable crop than soybeans in many areas, even with escalating production costs. The market's job of directing planting decisions in the U.S. in 2008 is far from done.

The pricing and storage decisions for the 2007 soybean crop are being influenced by the current high price, the weak basis, and the availability of storage. The weak basis in many areas suggests storing the crop to capture a post harvest strengthening of the basis. Hedging the stored crop would allow the producer to benefit from any such improvement and to capture the current high price. Storing the crop unpriced would also allow the producer to capture an improving basis, but at the risk of lower prices and the potential for higher prices. The weak basis and large carry in the corn market also make storage of that crop attractive. In cases of limited storage capacity, producers may need to examine the relative returns to storing soybeans and corn. In central Illinois, the net return to corn storage, as measured by potential basis improvement, exceeds that of soybeans due to the high interest opportunity cost of holding soybeans.

Darrel Good
Extension Economist
University of Illinois