



WEEKLY OUTLOOK



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WHAT WILL BE THE SUPPLY RESPONSE TO HIGH WHEAT PRICES?

Wheat prices moved to all time highs this fall, with December futures at Chicago reaching \$9.60. New crop, July 2008 futures, traded to a high near \$6.95. Some of the reasons for the extremely high prices were outlined in the September 10, 2007 issue of this newsletter.

Prices have softened over the past week as the market begins to anticipate some showdown in consumption and that the small 2007 crop has been fully reflected in current price levels. Decisions in the European Union to allow import licenses for 20 million bushels of corn and eight million bushels of sorghum could help ease the tightness in the supplies of feed wheat there. In addition, the recent Canadian estimate of the current crop there was a bit larger than expected. Improved weather in Argentina and ideas that the drought damage to the Australian crop has been fully anticipated by the market also contributed to recent price weakness.

Prices for the 2008 crop remain well below prices for the 2007 crop as the market anticipates an increase in world wheat acreage in 2008, motivated by the historically high prices. In addition, an increase in acreage in the European Union will be accommodated by the lifting of the 10 percent acreage set-aside requirement. The acreage response to high wheat prices will unfold over a fairly long period of time. Winter wheat producers in the northern hemisphere have the first opportunity to respond to the higher prices as seeding is underway. For example, the USDA reported that 42 percent of the U.S. winter wheat crop had been seeded as of September 30. Seeding now likely exceeds 60 percent. Private sources forecast that soft red winter wheat producers are likely to make the largest percentage increase in acreage due to the combination of high wheat prices and the potential opportunity to double crop some of those acres to high-priced soybeans. This is consistent with the experience of 1996 when wheat prices reached the previous high. Seedings of soft red winter wheat increased by nearly 10.5 percent and area seeded to hard red winter wheat increased by about five percent.

Decision by southern hemisphere producers and northern hemisphere spring wheat producers will presumably be influenced by the acreage increase reported for northern hemisphere winter wheat producers. The net result may be a more measured response to current high prices. That is, if all wheat producers were making the seeding decision

simultaneously a very large increase in the face of record high prices might be expected. However, the progressive nature of the response means that some producers will respond to decision of those planting first and to the prices of other crops.

In 1996-97, the USDA estimates that world harvested acreage of wheat totaled nearly 571 million acres, 5.2 percent more than harvested in 1995-96. A similar increase this year, would put 2008-09 harvested acreage at 566 million acres, the most since 1996-97. Some current private forecasts are for a 3 percent increase in world wheat acreage. Such an increase would put harvested acreage at 554 million. Forecasts have to be viewed as extremely tentative because of the progressive nature of the planting decisions.

Almost as important as the magnitude of planted acreage will be the level of yields in 2008-09. Over the past five years, world average yields have ranged from 39.3 bushels (2003) to 42.8 bushels (2004). The USDA's September forecast for the 2007-08 year was 41.4 bushels. A five percent increase in area harvested and an average yield of 42.5 bushels, for example, would result in a 2008-09 crop of 24 billion bushels. A three percent increase in area harvested and a yield of 39.5 bushels would produce a crop of only about 21.9 billion bushels. The USDA estimates that world wheat consumption is currently near 22.8 billion bushels. A modest increase in world wheat acreage and yields near the low end of recent experience would point to the need to ration wheat consumption in 2008-09, while a larger acreage increase and yields near the upper end of recent experience would allow some rebuilding of world inventories. With a 3 percent increase in area harvested, an average yield near 41.5 bushels would be needed to allow world wheat consumption to increase modestly in 2008-09.

Wheat prices appear to have peaked, at least for now. Prices may remain generally high, but very volatile as 2008-09 production prospects, both acreage and yield, unfold. The USDA's *Winter Wheat Seedings* report, to be released in the second week of January will provide the first indication of how U.S. producers responded to the high prices.

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