June 2016 Monthly Commentary

Soybean futures rallied to new highs in June, only to give everything back and then some in the first few days of July. SX was sitting near $10.50 to begin the month of June, rallied to just shy of $11.90, and finished the month near $11.50. I was convinced that the market was finally reacting to the changing global soybean fundamentals. However, the first 4 sessions of July have seen SX drop to $10.25, nearly $2 from the highs and about $1.25 from the June close. What has happened, and where does the market go from here?

July weather has been very good with solid rains across the Corn Belt, providing relief to most of those areas in need. Further, these rains are expected to remain near to above normal through the middle of July. While this is certainly supportive to US production, the extent of the price decline seems to be far overdone, driven by liquidation. In hindsight, the June rally probably had less to do with the changing world fundamentals/demand coming to the US than I gave it credit. I still feel this is coming, but the market seems to be solely focused on supply for the time being. While I still think US old and new crop demand are being understated by USDA by roughly 100 and 200 million bushels respectively, the market does not see this as an immediate concern. Many traders may either not agree with or not fully appreciate this view, thus they are focused on the good weather and the idea that yield could reach 48-50 bpa. I feel that $10.25 SX has taken virtually all of the risk premium out of the market, but it is difficult to determine how long it might take a market to liquidate. Time will tell, but length in calls seems to make the most sense at this point.

From a demand standpoint, there were several interesting (and mostly bullish) developments in June. I have been writing about the rapid depletion of soybean stocks in South America. Production fell well below expectations in both Argentina and Brazil. At the same time, record world soybean and meal demand (led by Chinese soybean demand) pulled down Brazilian stocks at an incredible pace. In June, the effects of that massive demand were felt, with Brazilian shipments slowing down while their basis levels appreciated to levels that pushed July through September world demand back to the US.

US soybean outstanding export sales at the end of June stand at a record 6.8 MMT (250 million bushels). Export shipments have not picked up yet, but lineups and outstanding sales suggest record July and August export shipments. I am forecasting June through August exports at a record 220 million bushels while August alone should exceed 100 million bushels for the first time ever. Further, early new crop shipments also remain record large with still further decreased competition from South America. What does all of this mean? First of all, old crop carryout is likely to be in the 250-275 million bushel range, about 100 million below the current USDA forecast. Second, record early new crop demand (that will rely primarily on old crop supplies) are likely to make the old crop carryout feel extremely tight. Finally, record demand should continue at least until South America can harvest their 2017 crop in March through May, putting increased pressure on US new crop supplies.

While we were expecting higher soybean prices and favorable planting weather to increase US soybean acreage by 2-3 million acres over March intentions, USDA told us on June 30 that US farmers will plant only 83.7 million acres of soybeans this year (1.5 million above March intentions). This type of acreage essentially requires above-trend yields to satisfy new crop demand. Assuming near-trend yields, my March 1, 2017 stocks estimate is historically low and my new crop soybean carryout estimate is near zero. Obviously, this cannot happen, so either a) yields must end up well above trend, or b) price must ensure demand is not as big as I am forecasting. I still think it is too early to project record yields, so I still believe futures have further upside unless yield really does reach the 48-50 bpa level.

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June 2016 Monthly Commentary

Corn and wheat markets faced more negative developments in June. While USDA reported soybean acreage below what was feared, they also surprised the market by forecasting corn acreage at 94.1 million acres (0.5 million above March intentions) vs. market expectations for a decrease of 1 million acres. They also forecast wheat acreage at 50.8 million acres, 1.3 million above March intentions vs. market expectations for an increase of only 0.2 million acres. Combined, corn plus wheat acreage was about 2.5 million acres above expectations. Additionally, June 1 corn stocks were reported at 4.72 billion bushels, 200 million above trade expectations.

Reduced corn supplies in South America, strong soybean futures, and corn prices now at or below cost of production in many areas should limit corn downside at some point (corn can't get too cheap relative to beans in the 2017 months or soybean acreage may take away too much corn acreage). Nevertheless, this is quite simply a lot of bearish news for the market to swallow, particularly with the world already struggling with burdensome wheat supplies.

Corn is a bit more difficult to forecast as it seems a significant portion of the bearish news is already priced in and US corn export demand should remain brisk with decreased competition from South America (the market is just now fully understanding just how poor Brazilian corn production will be). I wrote last month that I expected the soybean/corn ratio (SX/CZ) to increase from 2.6 (at the end of May) towards 2.8-3.0 in coming months, but it happened even faster than I anticipated. At the end of June, this ratio had ballooned out to 3.1, but then dropped back to 2.9 by July 7. I do expect this to widen further now over time.

Regards,

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