Ditsch Trading

April 2018 Monthly Commentary

The impending trade war between the US and China has altered grain flows and has set up a puzzle regarding when grains, and even more significantly soybeans, will be pulled from the origin countries.

The US attempt to reduce their trade deficit with China beginning with tariffs on US imports prompted backlash from China. China set a huge import charge of 179% on sorghum imports from the US, stopping US sorghum exports to China. China has become a significant destination for US sorghum, but in terms of volume soybeans are obviously the key trade. China has threatened a 25% import tariff on soybeans. Further, there is concern that Chinese import officials are finding any problem they can with US soybean cargoes arriving in China. The tariff threat (which could go into effect at any time) along with the risks at discharge (even if there is no tariff) have Chinese crushers and importers avoiding US soybeans as much as possible. They are buying as much as they can out of South America and supplementing this with soybean purchases from Canada along with taking a few more substitutes such as canola/rapeseed.

The huge Brazilian crop has allowed China to swing virtually their entire import program to Brazil. However, the Argentine crop continues to get smaller and their farmers aren't selling the smaller crop aggressively due to ongoing inflation and export tax concerns. Further, with the reduced Argentine crop, world soybean meal buyers are incenting Argentina to crush their soybeans at origin to help satisfy world soybean meal demand. Thus, China is down to one major origin.

How will this all play out? Well, it obviously depends on how quickly a trade deal is reached. However, this is probably not a black and white issue. Even if both sides agree not to tax imports, the fear of reescalation likely keeps Chinese buyers avoiding US soybeans as long as the friction continues. Although Brazil had a record crop, China is draining their excess supplies at record rates. At some point late this summer or early this fall, Brazilian soybean supplies could likely become tight enough that their premium over US beans explodes higher. This should ultimately push China back to the US, 'the only store in town', even if no agreement is reached.

There are a number of side impacts from this altered trade flow. China aggressively buying Brazilian soybeans likely cuts Brazil domestic soybean crush by early this fall at the latest. That, combined with the reduced Argentine crop, has the potential to create a severe worldwide soybean meal shortage (as soybean meal is by far the most dominant source of protein in world feed rations). The vast majority of soybeans remaining in the world post-US harvest are likely to be in the US, and the US simply doesn't have the crush capacity to supply the world's meal needs.

Beyond the US/China trade frictions and resulting trade flows, grain fundamentals have not changed significantly. US old crop corn and soybean stocks are more than ample (soybeans even more so with China avoiding US purchases). US planting weather is a mixed bag, with cold/wet weather delaying an early start but much warmer conditions now allowing for rapid progress in many areas.

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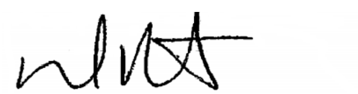
The new crop corn balance sheet looks constructive, but on the other hand prices tend to drop as the crop is planted. US and world wheat weather has been far from ideal, providing underlying support to wheat prices. Soybeans are caught in a tug-of-war with soybean supplies piling up in the US and soybean meal being supported by the potential lack of soybean availability for crush in South America by early fall. Meal obviously looks the most constructive, with the potential to go much higher in an attempt to ration/defer demand or find substitutes.

Overall, I still expect corn, soybean and wheat prices to be well supported at current levels. However, the political uncertainty can add volatility. Setbacks on trade concerns are likely buying opportunities.

Regards,



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