December 2 , 2014

Monthly Agriculture Market Notes:

The agricultural futures markets remained highly volatile last month and frustrated both bulls and bears alike. Unfortunately through all the price volatility, the fundamental backdrop did little to provide clarity in support of either bull/bear argument.

That said, some fundamental price-factors have changed. For starters, one critical element of the Oct/Nov price rally in soybeans was an especially tight cash pipeline supply of soybeans. Recall the old crop carryout was revealed to be smaller than expected at 92 million bushels, which combined with an initial slow start to the harvest, created a huge push in the market for any cash supplies it could find. This was further exacerbated by a shortage in meal supplies, which was difficult to resolve due to both the slow harvest and rail logistical constraints.

Fast forward to present time, the tight cash pipeline supply situation feels completely resolved. Commercial contacts imply crushers have soybean ownership to last into the New Year. The barge market continues to weaken as the huge export surge has peaked and exporters are also thought to have strong levels of forward coverage. In short, the US farmer has rewarded the rally in prices with aggressive marketing of their crop.

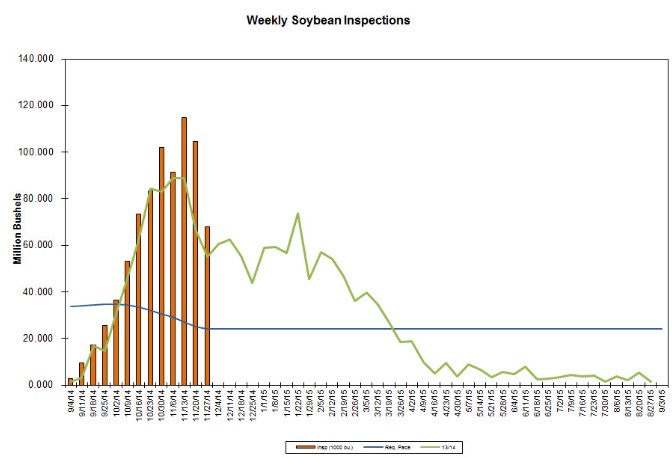
This initially allowed for a significant relaxation in the cash soybean market. However, cash meal still appears moderately tight in the nearby and this is providing some support to soybeans. The strong meal values have kept crush margins extremely attractive, which allows crushers to "push" their basis bids at times in effort to secure additional soybean supplies. Additionally, as cash soybeans weakened, exporters have been able to make additional sales to China and other destinations as US soybeans remain competitive against Brazilian offers through February and perhaps March. The duration of the US export program also remains in question as Brazilian soybean planting was delayed by a slow start to the rainy season, potentially leading to a late harvest and a late start to their export program. This will leave the market left to wonder how large the final US soybean export program will eventually turn out even after the peak demand of Q1 has waned.

Further complicating the soybean market's fundamental backdrop over the medium term is the political climate in Argenti-

US Soybean Quarterly Supply and Demand

	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14	14/15
Carryin (Sep 1)	449	574	205	138	151	215	169	141	92
Production	3,197	2,677	2,967	3,359	3,329	3,094	3,034	3,358	3,958
Sep-Nov Imports	2	2	3	3	4	3	4	7	6
Total Supply	3,648	3,252	3,175	3,500	3,484	3,311	3,207	3,506	4,056
Sep-Nov									
Crush	459	467	420	445	443	412	452	446	445
Exports	374	328	387	536	622	425	618	677	803
Seed	-	-	-	-	-	-	-		-
Residual	113	97	92	181	141	105	171	229	225
Total Use	946	892	899	1,162	1,206	942	1,241	1,352	1,472
Stocks (Dec 1)	2,701	2,360	2,275	2,339	2,278	2,370	1,966	2,154	2,583
Stocks/Use	286%	265%	253%	201%	189%	252%	158%	159%	175%
Needed Sales	495	316	691	1,021	1,051	724	1,068	1,204	1,375
Needed/Use	52%	35%	77%	88%	87%	77%	86%	89%	93%
Needed/Crop	15%	12%	23%	30%	32%	23%	35%	36%	35%

The estimated demand pull on soybeans for the first quarter of the marketing year was simply unprecedented.



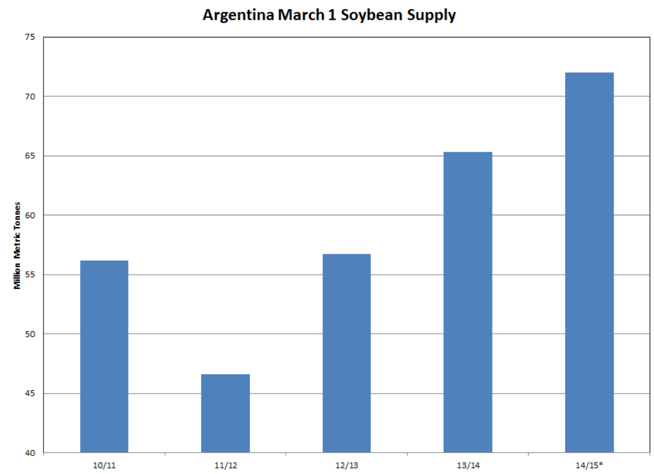
Soybean exports so far this marketing year have been extremely strong, but it is important to note that the seasonal peak in shipments has passed and demand from the export market "should" be quieter in the months ahead.

9047 Poplar Avenue, Suite 101, Germantown, TN, 38138
Tel: 901-766-4446 • Fax: 901-766-4406
www.opusfutures.com

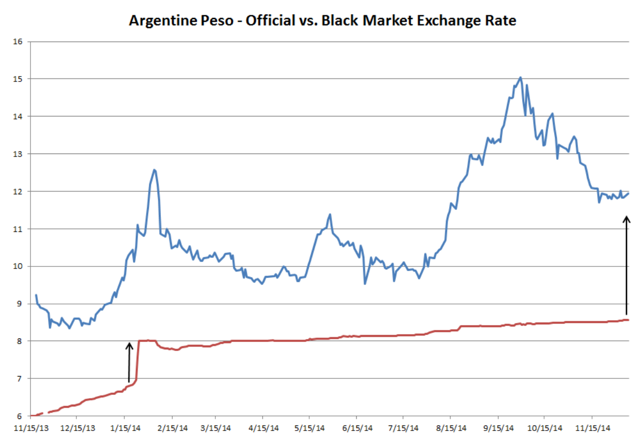
na. Farmers continue to hoard soybeans as a hedge against inflation. In the past as a hedge against inflation, farmers (and others) would take any cash and convert it into a "physical" asset such as a new car for example. The Argentine government eventually created tax implications on these types of transactions, which has left the farmer with nothing to do with his soybeans but hold on to them. He is essentially "earning a carry" as the longer he waits to sell, the more pesos he will receive as the peso weakens against the dollar. This leaves the Argentine crusher and exporter in a tough position as they are only able to sell "spot" supplies, as they remain completely unaware of what the future holds. The Oct/Nov rally allowed for some slightly more aggressive farmer movement, but that has slowed down now, and the Argentine exports just wait. The government is trying to force the farmers' hand by restricting access to bank loans now, but the farmer at this point in time has little use for cash (and as mentioned previously tries to convert cash into *anything* else as fast as possible). It remains a very important question for the global soybean market….what will make these soybeans move and when might it happen? Obviously when the new crop harvest starts to take place, Argentine farmers will have to move *something* into the export/crush channels as they are sitting on already huge old crop inventories. Outside of that movement, however, the situation is very questionable. Will the Argentine government allow for a devaluation of the peso that moves the "official" exchange rate closer in line with the unofficial (but more realistic) "blue" peso rate? Some have speculated that a devaluation could happen in the early stages of the New Year, but that is little more than a guess at the moment. Clearly the Argentine government cannot defy economic gravity forever, but they can kick the can down the road perhaps longer than we give them credit for. Something has to give here, but what and when?

I do believe that the level of Argentine farmer sales of soybeans might be the single biggest factor to watch for soybean prices in 2015.

Though, as if not to be outdone, Brazilian farmer forward sales of new crop production are running well behind average. This is keeping Brazilian export premiums elevated, which is allowing the US to perform export business perhaps a bit longer than previously expected. In the short term, this feature could work to support prices, at least to a level that encourages the Brazilian farmer to engage the market with additional sales. My bias towards soybeans over the medium/long term is for sharply lower prices. In



Estimates of Argentine soybean supplies continue to swell with farmer hoarding and expectations for an increase in production this season.



The Argentine government allowed for a devaluation in the official exchange rate in early 2014. Some speculate another devaluation could be coming in early 2015.

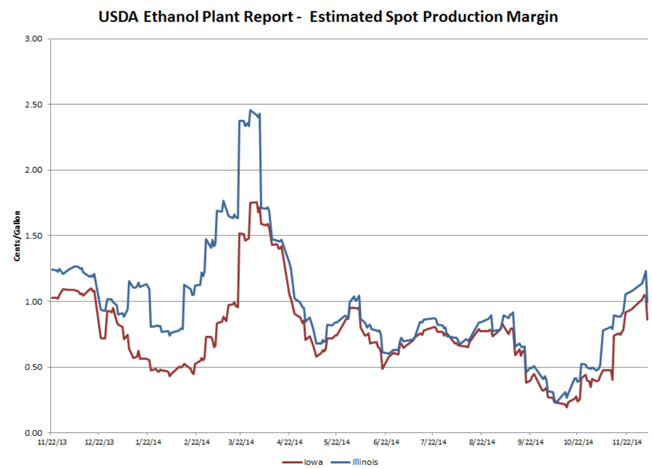
addition to ample current US supplies, South American weather has been favorable leading to prospects for strong 2015 Brazilian and Argentine production. Even if the Argentine farmer tries to hold back some crop, the stage is set for lower prices into spring 2015. US production prospects for 2015 look good for now as it is looking likely that soybean acreage will expand, mostly at the expense of corn.

The corn market has defied most expectations and has also trended higher since harvest. The slow pace of harvest was certainly a supportive factor, but the corn cash pipeline was not nearly as depleted as soybeans and shouldn't have been such an extreme issue. Farmer selling of corn remains subdued and will likely remain so until the New Year (for tax purposes).

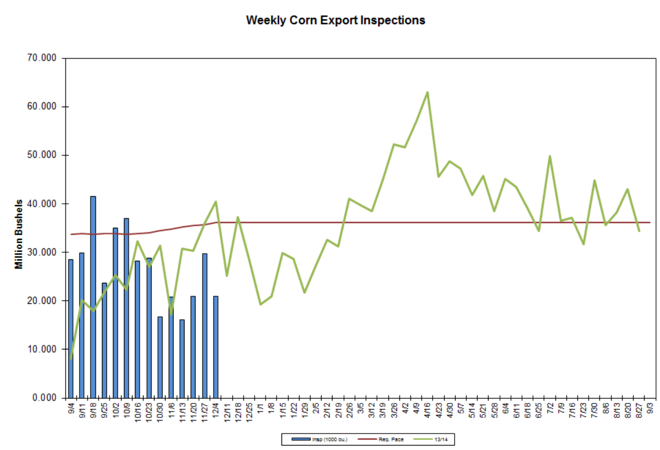
Demand from ethanol production has so far exceeded expectations this year. Ethanol production margins are very strong and the implied demand based off EIA figures looks very solid. That said, there is a seasonal tendency for ethanol demand (and as a result, production) to look very strong into the end of the calendar as the industry looks to "bank" RINs with ongoing uncertainty towards RFS requirements. I question whether this demand will stay constant into 2015.

Export demand has also exceeded expectations so far this year. First quarter exports could exceed year-ago levels by more than 50 million bushels, despite the fact that WASDE is projecting the 14/15 export total to be down roughly 170 million bushels from last year. This obviously requires some big YOY reductions going forward, which is likely to happen but keep in mind that the South American export program will switch almost entirely to soybeans in the spring, leaving the US as the world's primary corn supplier. Most private analysts have been assuming smaller export projections than WASDE (currently 1,750 million bushels), but I think these private projections will have to start creeping higher closer to the WASDE level.

So, with the prospects of continued stronger than expected demand, I have to view corn from an entirely neutral perspective. There seems to be a consensus belief that the corn balance sheets will look bullish for 15/16 due to a drop in acreage, but note that the rally in corn prices has narrowed the gap in expected revenue to soybeans for 2015. While soybean area is likely to gain some ground from corn, I don't expect a massive shift that seemed pos-



Ethanol production margins are extremely attractive.



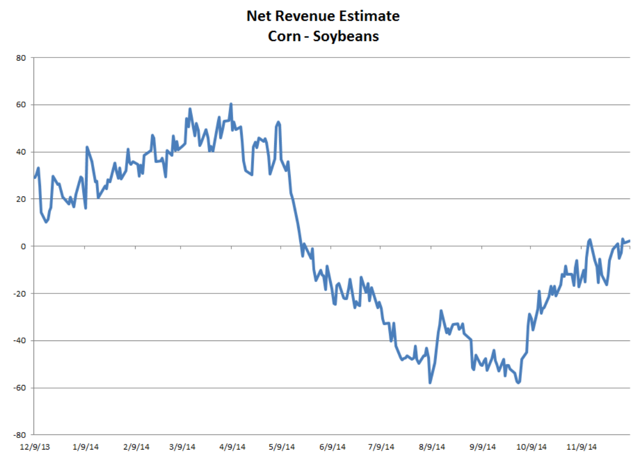
Corn shipments do need to pick up to catch up to the WASDE projection, but a strong level of commitments and a seasonal shift in South America to focus entirely on soybean exports should allow for this.

9047 Poplar Avenue, Suite 101, Germantown, TN, 38138
Tel: 901-766-4446 • Fax: 901-766-4406
www.opusfutures.com

sible with calculations from just a few months ago. Corn futures probably have very limited downside in the short/medium term, though I don't believe in tremendous upside potential in the long term either without a significant weather-related problem.

Wheat prices have been propelled higher due to concerns over possible Russian export restrictions. These concerns seem overblown to me as the Russian export program has already peaked for the season. Wheat values appear over-priced relative to corn, though I don't view the current setup as favorable for a position in wheat and will remain on the sidelines.

The bull market seen in cattle through 2014 has been nothing short of remarkable, though for now it appears that the price strength is showing signs of losing its grip, at least for a while. Beef demand and movement is struggling due to high prices. Meanwhile feedlots are losing "currentness" as packers scale back on slaughter. The short term situation feels like prices should push lower over the course of the next several weeks. Whether or not this will prove to be the top in the cattle market's massive bull run remains to be seen.



Earlier this fall, net revenue calcs strongly favored soybean planting over corn in 2015. As shown above, the relationship has narrowed significantly and the presumed loss in corn area in 2015 now looks a bit more suspect.

Respectfully,
David Zelinski

9047 Poplar Avenue, Suite 101, Germantown, TN, 38138
Tel: 901-766-4446 • Fax: 901-766-4406
www.opusfutures.com