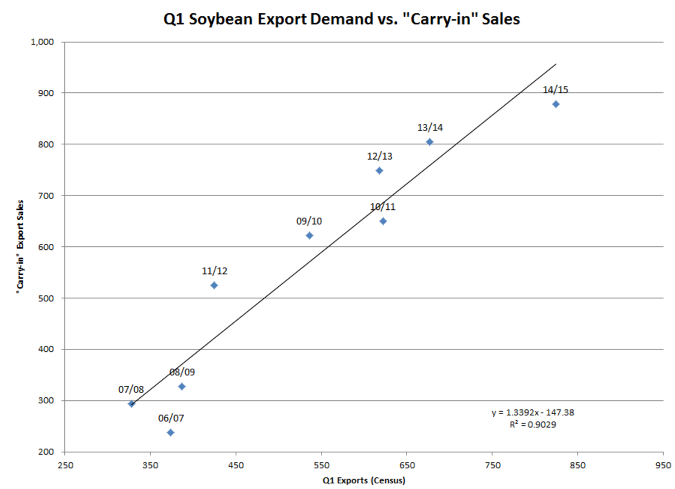
Opus LLC

F U T U R E S

August 3, 2015

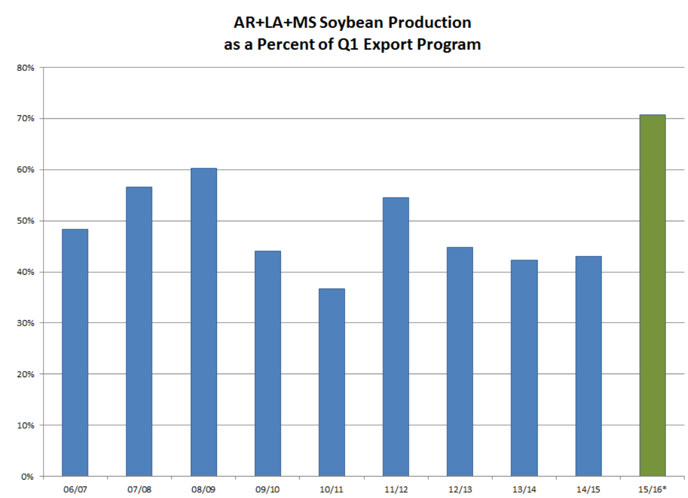
Monthly Agriculture Market Notes:

Whatever one thinks of the current state of affairs of US corn and soybean crops, most observers would probably agree that the recent weather conditions and forecast appear good enough for a *stabilization* of the crop. The crop is (probably) not getting worse than whatever it was a few weeks ago. Of course there is a very wide disagreement on what that “baseline” production level is, but agreement on at least stabilization allows us to focus on demand prospects momentarily.



There is a very strong relationship between “carry-in” sales for soybeans and Q1 exports. This allows us to have a very good idea of what Q1 export demand will total.

With that in mind, note that “carry-in” export sales (or rollover + NMY sales) are a very good indicator of Q1 total US export demand. The scatter showing the relationship in soybeans is to the right. If we assume we see a weekly average of 500k mt of NMY sales and we have a rollover amount of 1.5 mmt. Theses assumptions might turn out to be conservative in the end, but for now they provide with a fair baseline scenario. Based on these assumptions, and the attached relationship, we can assume Q1 export demand of roughly 440 mil bu, which sounds small. It would be the smallest since 11/12 and roughly half of what we exported in Q1 last year. Most will argue that assumption is too low, but the assumptions for carry-in seem fairly reasonable (in my opinion) and that is what the relationship would imply (and as shown it is a consistent relationship).



The graphic above shows lower-Miss soybean production as a percent of Q1 export demand. If current assumptions hold, the Delta soybean crop might handle most of the Q1 program, which will take some pressure off the IL River.

So with that (perhaps controversial) assumption in hand, let’s then compare that against Delta soybean production. Here I’m taking total soybean production for AR, LA, and MS, which of course are tributary to the Gulf export program. I came up with a 5-year average for yield in the 3-state area and applied that to this year’s NASS harvested area estimate. That would give a 3-state production total of 311 mil bu, which would be smaller than last year’s 355 mil bu total. This year’s area is bigger (AR will be resurveyed), but last year’s yield was big and the average I’m assuming is much lower.

The second chart attached shows this 3-state total soy-

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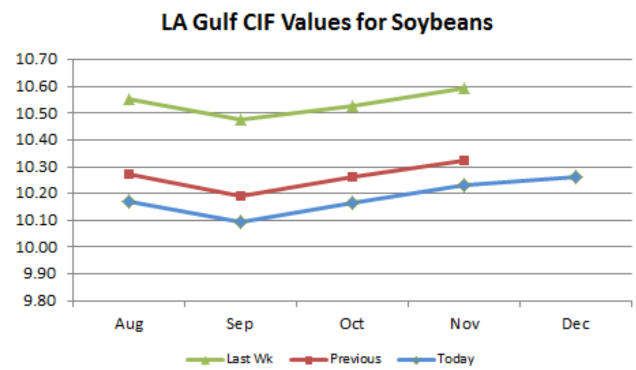
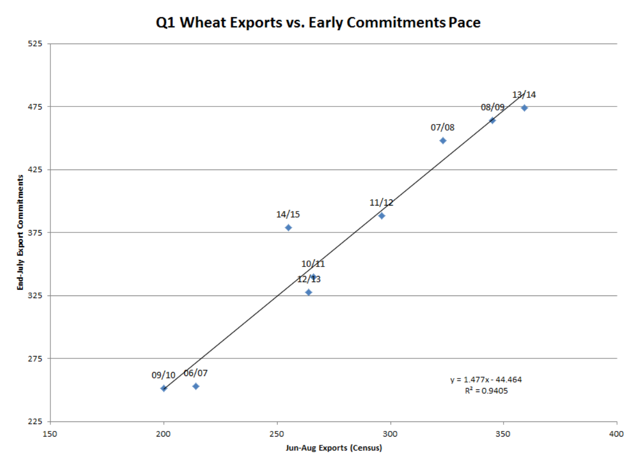
bean production as a percent of Q1 export demand. As you can clearly see, the Delta soybean production this year can suck up a lot of the projected export demand. Again, many will argue that I'm too low with my export projection, but I'd counter that possibility with feeling a bit too low with my production estimate. I've also left off MO and TN, which perhaps I should have included.

If these assumptions and projections are anywhere close to being accurate, it somewhat makes me wonder what sort of function the SU-SX spread is performing at an inverse? Old crop basis levels remain tight in the ECB of course, but the delivery system is geared for the export channels and if the Delta crop can really suck up this much of the export program, I question what sort of pull the export program will need off the IL River. I think it is also worth pointing out that Sep-Nov CIF quotes are a carry, yet the futures are trading an inverse. It also reflects a flat-price bearish situation for soybeans. Based on demand alone, the soybean market is still looking at considerable headwinds in the weeks and/or months ahead.

Turning now to wheat, export demand prospects also look fairly bleak. Again there is a pretty solid relationship between end-July export commitments against the marketing year's Q1 Census exports. Depending how this week's export sales data turns out, total end-July export commitments are unlikely to be much better than 290 mil bu. Based on the scatter relationship shown here, this would imply total Q1 wheat exports are unlikely to total much better than 225-230 mil bu. Since the 06/07 season, Q1 exports typically make up roughly 26% of the marketing year total. If that were to be the same case this year, it would imply a total marketing export figure near 880 mil bu. This is clearly a long way off from the current WASDE projection of 950 mil bu. WASDE is currently grossly overstating US wheat export demand, and a strong FSU crop along with steady Australian production are unlikely to allow much room for US exports at current price levels.



The Gulf cash market starting in new crop is a carry, so why are futures inverted?



Current export commitments as tracked by FAS are a very strong indicator of Q1 total wheat exports.

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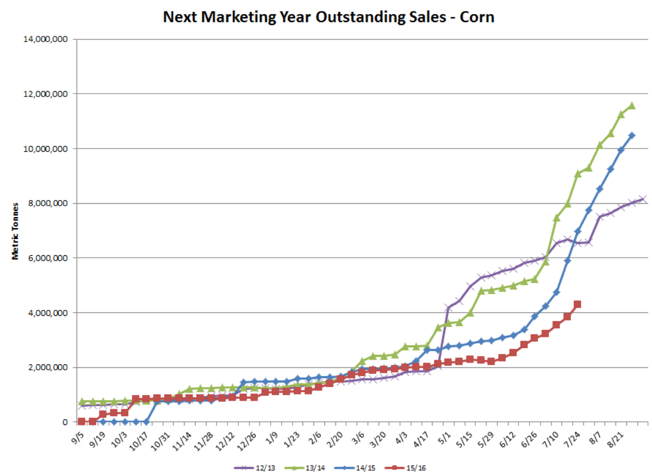
In corn, the relationship between carry-in sales and Q1 export demand is not very solid, so I won't provide that graphic here. However, shown here is the pace of next marketing year's outstanding sales. These are export sales for the new crop (15/16) season. As you can see, sales are well under the pace we've seen over the past several years. This is largely due to major competition from Brazil, where a record corn crop and added export capacity (in the northeast and along the Amazon river) has allowed the country to steal typical US market share.



New crop corn sales are running well behind the pace we've seen over the past several years.

The bottom line: if market direction were entirely based on demand prospects, it would be a fairly easy decision to be short all three markets. However, we still have a lot of question marks surrounding corn and soybean production. As noted earlier, I do feel comfortable with the thought the crop has stabilized and is improving from some level. However, given the especially wet spring through portions of the Corn Belt and earlier hot and dry weather in southern portions of the country, I'm not quite sure from what level the crop has stabilized. With that in mind, I will attempt to take advantage of the poor demand prospects via spread markets in the short term. I am short calendar spreads in soybeans and I am spread HRW vs. SRW for demand reasons. Once I have a better handle on US crop potential, I'll be more comfortable having a flat-price bias.

Regards,
David Zelinski

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