January 7, 2019
Advanced Ag Program Commentary

Roughly one month ago I posted a report entitled "Why the debate over soybean tariffs no longer matters". In the report, I detail several reasons why soybean prices should head lower whether or not US-China trade negotiations reach an agreement to end tariffs and, more importantly to soybeans, the de facto embargo China has held on US soybeans since June. To summarize seven pages into one sentence, US (and world) soybean prices should head lower as global supplies exceed demand and inventories are likely to continue to grow even beyond 2019.

Since I published that report on 11/30/18, nearby soybean futures have *rallied* more than 20 cents. While that is not an especially dramatic move on its own, it obviously has come as a surprise to me as most fundamental data I've seen over this period has supported my bearish thesis. Yes, the US-China talks in early December did yield a Chinese concession to buy up to 5 mmt of US soybeans, but more importantly, in my opinion, is that Brazilian FOB premiums have fallen sharply and now the US is losing business to the rest of the world. Outside of the token Chinese government purchases, US demand prospects have actually *fallen further* despite the trade truce.

Yet, I have clearly underestimated the "hope" the market holds towards the trade negotiations. In general, it seems the world believes that a trade deal reached at some point before the March 1 "deadline" would lead to increased demand for US soybeans (and feedgrains?) which would, in theory, alleviate the oversupply the market is currently dealing with. As I explained in the aforementioned report and I can show in very simple math, I do not agree with that rosy assessment. Simply put, Brazilian new crop supplies look likely to price out US soybeans for global export business in the months ahead… at least at these US price levels.

Admittedly, as we move into early January we have some concerns over Brazilian production prospects starting to creep up. Brazil has seen lower than normal rainfall over much of its growing season and the outlook calls for below normal precipitation through January as well. So now, in addition to the over-optimism regarding US soybean export prospects we also have a race lower in Brazilian production estimates. I tend to believe the market is over-reacting to the percent-of-normal precipitation figures for Brazil, but my contrarian bias towards both US export demand and Brazilian production prospects has unexpectedly put me in a position of "fighting the market" here in the early stages of 2019. I must admit I'm bewildered by the speculative interest in owning soybeans when we are looking at record global supplies plus a 15+ mmt YOY production increase in South America (even after lower Brazilian production estimates) all while demand in the world's biggest consumer (China) is slowing (in part due to African swine fever).

I noted in my comments last month that I simply viewed the soybean market as one of delayed gratification. My expectations for sharply lower price action has been pushed back due to unfounded optimism that a trade deal will "solve" the US over-supply. I still feel that way today. I concede that South American production levels need to be watched closely, but there is little in my mind that can change the slow-motion train wreck that has already been set in motion in soybean prices.

Turning to corn and wheat, I have little new to add regarding my opinions. I think both markets are stuck in range-bound price action for the foreseeable future. Corn demand prospects look suspect at the moment. Ethanol production margins are negative and we see several US ethanol producers idling production capacity. Meanwhile, US export shipments have not been as strong as expected and new sales have been relatively slow as well. Here again, Brazilian weather is key. If dryness in northern Brazil persists into the "safrinha" growing season (mostly spring) resulting in lower production estimates, then we could see demand for US corn exports increase significantly. In wheat, it is highly likely that US winter wheat planted area will be lower than expected due to excessive rains through the southern US that has delayed soybean harvest and prevented winter wheat planting. On its own, however, I don't view this as enough to spur wheat prices out of its current range. Instead, only spring weather extremes (either good or bad) in either the US or the FSU will likely be necessary to push wheat prices to either new lows or new highs.

I remain negative to summer cattle contracts, June forward. The market has priced demand perfection for both cattle and hogs in my opinion. There is little doubt that ASF has affected Chinese pork production levels but there is little evidence as of yet that US export demand is strong enough to support prices at these levels. Cattle futures also appear to be pricing in exceptional demand. Meanwhile, it is likely we're looking at YOY increases in cattle on feed (following what might be a new record December placement level) and I still feel issues with packer capacity during the summer months have not been solved.

Though it seems we've been stuck in the mud for the past few months, my optimism towards 2019 has not waivered. I feel we're in an excellent position to benefit from heightened interest and volatility in the agriculture markets.

Please let me know if you have any questions.

Thank you,
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