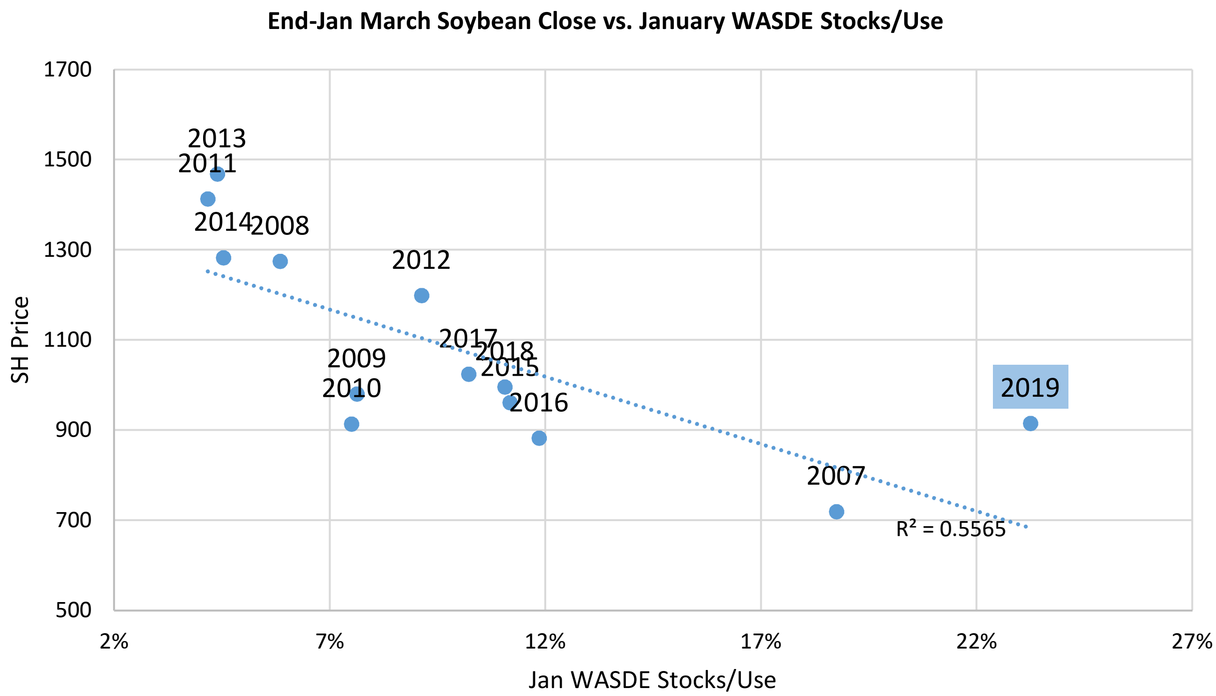
February 5, 2019

Advanced Ag Program Commentary

January 2019 has come and gone with no significant changes to my outlook. I mentioned in last month's commentary that we've been "stuck in the mud" for several months, and unfortunately that continues to be the case. My fundamental case for soybeans appears to be in complete contrast with price action over the past several months. I'll offer up just one simple example. The chart below plots the January closing price in March soybeans over the past several years vs. the WASDE stocks/use estimate. While the relationship is not perfect, you can see there is *typically* a fairly strong relationship between the two. This year, as you can see, prices are matched up nowhere close to where the December WASDE (no January report due to the shutdown) would imply. I have many other simple studies like this, and they all point to soybeans being overvalued relative to current fundamental assumptions.



So why is the soybean market pricing in a different world relative to our current assumptions on reality? Well clearly the ongoing US-China trade negotiations are allowing the market to factor in some sort of resolution to the ongoing conflict. WASDE has gone out of its way to note their US export projections assumed zero Chinese demand and the market could be foolishly believing their figures and assuming the recent Chinese soybean purchases will allow for tighter US supplies and potentially supported prices. I, instead, would make the argument that WASDE was either clueless or flat-out dishonest in their commentary to suggest that their figures accounted for zero Chinese demand. Instead, even with the recently announced 10 million metric tonne purchase of US soybeans, reaching the current WASDE projection feels like it could be a stretch. Many in the media, even President Trump himself on Twitter, have claimed that the Chinese will blindly buy "X" amount of US agricultural products, but I continue to ask the question of where this demand is suddenly coming from? I have yet to see a satisfying answer.

Looking further into the future, the current pricing structure for soybeans actually means it is *favored* on a national average basis for 2019 planting considerations based on our analysis. The month of February is important as insurance price levels

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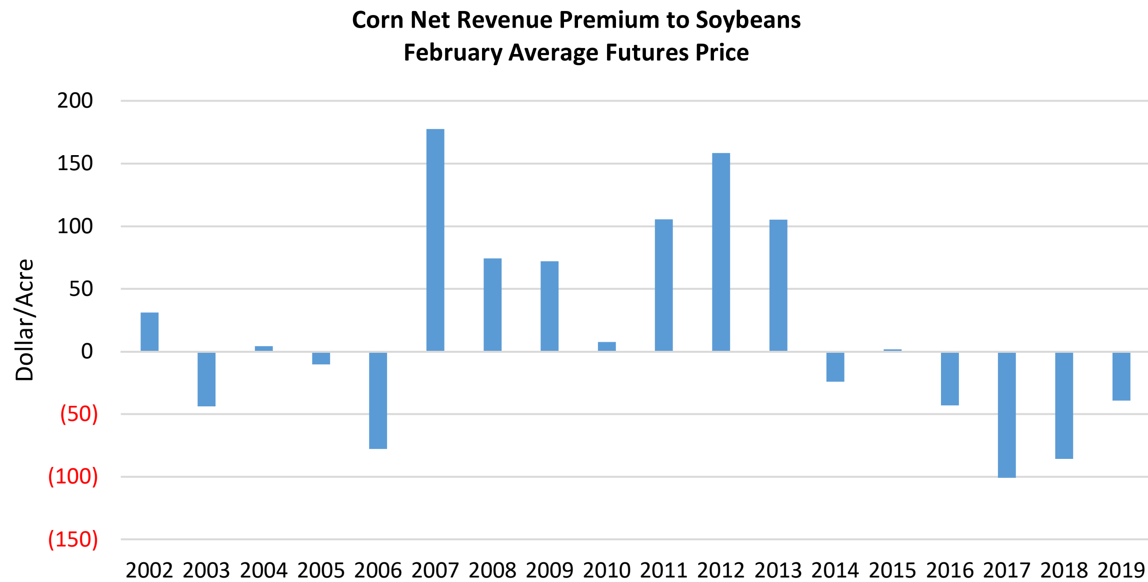
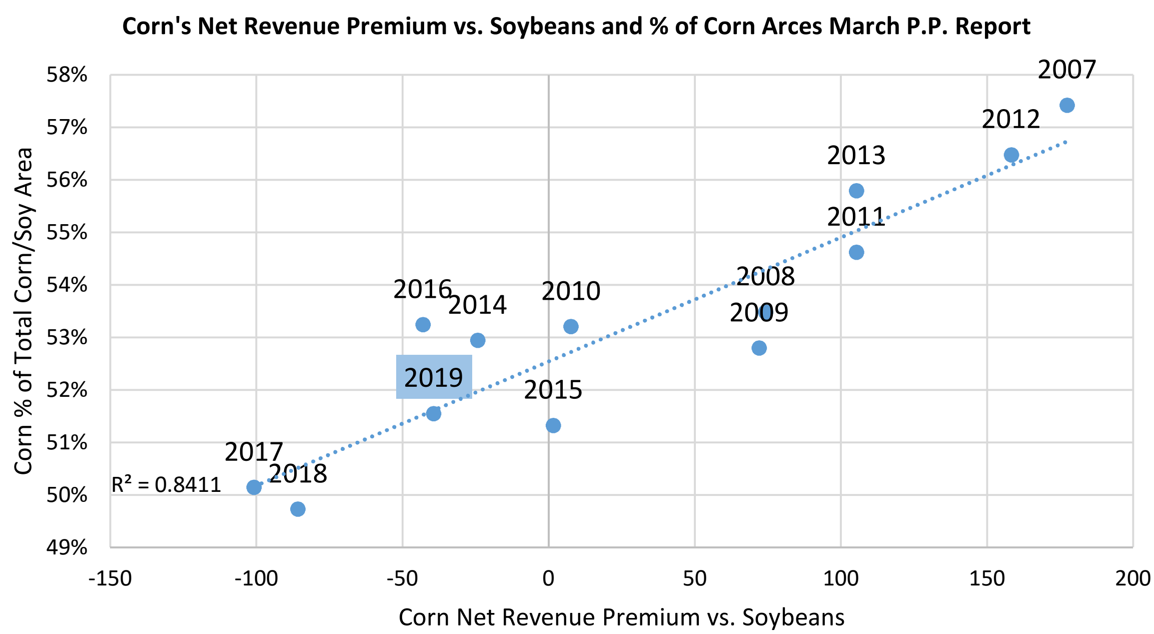
are set during the month based on SX and CZ futures contracts. An analysis of the February prices and relative cost of production for corn vs. soybeans shows that soybeans would seem to have an advantage over corn *on paper* as shown in the first chart below. This obviously contradicts what many have repeatedly said about a massive decrease in soybean area and an increase in corn. Instead, the acreage shift is likely to be more conservative. Our numbers point toward a corn area of roughly 91.5 million acres and soybeans of roughly 86 million acres in 2019. You can see in the second chart below that this would match up very closely with our analysis of the net revenue comparison at current price levels.





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What's the point? If the US really does plant 86 million acres of soybeans this spring, it will likely take a massive crop problem to bring the US soybean balance sheet toward equilibrium. While that is always a possibility any year, the simple truth is that is just not something I am willing to bet on at this point in the year. **If you're friendly to soybeans at these price levels, you're either betting on planting economics taking the year off, a 2019 US crop problem, or Chinese soybeans purchases that defy any semblance of rational economics. Any one of those might eventually come true, but in my opinion these are not items on which one should base supposedly rational trading decisions.**

I continue to hold a long corn position, but that isn't necessarily due to a bullish case for corn. Much like soybeans, I think the bullish argument for corn likely depends on some sort of 2019 crop problem here in the US or potentially in Brazil. However, as noted above I think the market's function is to eventually try to switch acres from soybeans to corn, and in order to do so we need to see that spread work in favor of corn relative to soybeans.

I have recently added a very modest long position in wheat. This is based largely on expectations that winter wheat plantings will turn out smaller than expected due to unfavorable fall weather. We will finally get the USDA's planting estimates on Feb 8, at which point we'll know whether to maintain this position or to look for opportunities elsewhere.

Please let me know if you have any questions.

Thank you,
David Zelinski
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