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The silos will be bursting with beans

At 4% of consumption, US ending stocks of soybeans are estimated to close out the 2013-14 marketing year at their lowest level in modern history. Booming exports were the main factor. The USDA estimates that US farmers will sell a record 43.55 million tonnes abroad before the marketing year ends on August 31, 20% more than in 2012-13. While the possibility of cancellations looms large with South American crops now ready for shipment, it is largely irrelevant to the balance sheet. Exporters have already shipped 43.36 million tonnes. In fact, commitments stand at 45.5 million tonnes and have overshot the USDA estimate. Ending stocks could tighten further if those 2 million tonnes of outstanding sales ever get shipped. That, however, is pretty much where the bullish story ends.

Dry weather during the growing season threatened the 2013-14 Brazilian crop. Early-season estimates ran as high as 90 million tonnes, but then for a while it seemed that there would not be much improvement over last year's output of 82 million tonnes. The weather stabilized, though, and estimates have been inching back up. The current USDA estimate calls for a record crop of 87.5 million tonnes.

Argentinean crops struggled with weather over the past three seasons, but 2013-14 production has recovered handsomely, with a near-record crop of 54 million tonnes.

As we look ahead to the 2014-15 US crop, we find acreage estimates at record highs. Over the past year soybean prices have risen precipitously *vis á vis* corn prices, and the shift in acreage has been commensurate with higher bean prices (Charts 1 and 2). The March 31 planting intentions report estimated soybean acreage at 81.5 million acres. In 2013-14 US farmers planted only 77.12 million acres, and harvested 75.87 million acres. On June 30 the USDA will release its final acreage report. Analysts believe that farmers added even more acres – the average guesstimate is 82.2 million acres.

And the crop is in great shape thus far. The most recent weekly crop progress report shows that 72% of the crop is in good-to-excellent condition. This compares with 65% last year at this time and the five-year average of 63%. In addition, it is the highest rating for the third week in June on record. The USDA is therefore forecasting record yields of 45.2 bushels per acre (bpa). That compares with 43.3 bpa last year and the record 44 bpa set in 2009-10.

Global ending stocks for 2013-14 are estimated at 25.8% of consumption, their highest level since 2010-11. The forecast for the incoming 2014-15 marketing year is a record 29.3% of usage. Just to be clear, the robust inventory-level forecast for the 2014-15 marketing year is based not only on the assumption of perfect weather for the US crop that is currently growing, but also on South American crops that will not be planted for months yet.

Still, farmers in both the US and South America have obviously taken advantage of historically high prices, and we are moving from a period of tightness into a period of bounty.

Sell November soybeans. Place initial sell stops at $1,300 per bushel, close only.

[By Sholom Sanik, June 27, 2014]

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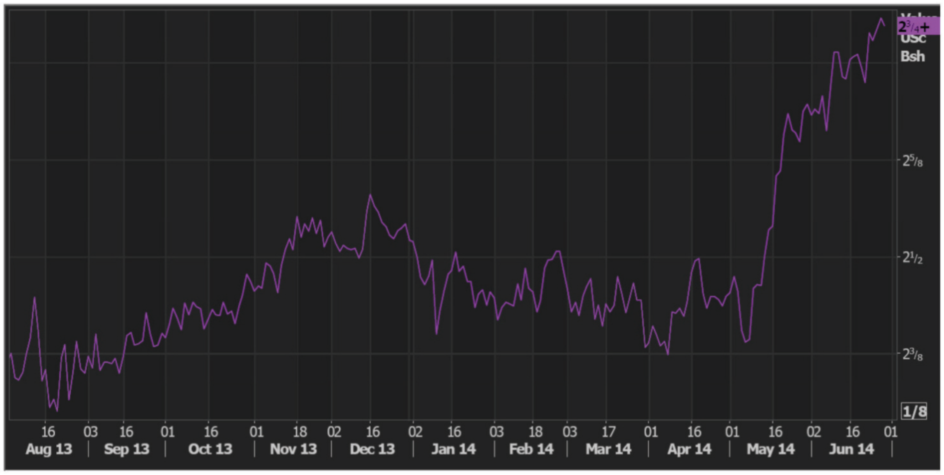
Chart 1 – November soybeans/December corn ratio



Courtesy Bloomberg LP

Chart 2 – Weekly nearest contract soybeans/corn ratio

Courtesy Bloomberg LP

CORN

Has the bear arrived?

Corn prices have erased all of this year's gains – over $1 per bushel, or about 20%. A recovery in US exports to their strongest level since 2010-11 will leave the soon-to-be completed 2013-14 marketing year in a relatively tight position. But even the old-crop picture took a bit of bearish hit, with the most recent key USDA report showing that US inventories as of June 1 were stronger than anticipated. The June 30 quarterly stocks report put stocks at 3.853 billion bushels, 131 million bushels above trade guesstimates. The market took a 20¢ dive on that news and has continued lower into July.

Most – but not all – developments for the upcoming 2014-15 season have been viewed by the market as bearish. Most prominently, despite the fact that US farmers planted substantially fewer acres of corn for the 2014-15 crop, output is expected to equal last year's record crop.

Soybean prices have been consistently higher, and as a result, a massive amount of acres shifted away from corn. Consider that US farmers planted only 76.5 million soy acres for the 2013-14 crop. In the March 31 planting intentions report, the USDA estimated soy acreage would jump to a record-by-far 81.6 million acres. Traders had expected an increase in the June 30 acreage update – the average guesstimate was 82.15 million acres, but the USDA shocked the street with a massive revision, raising its estimate to 84.84 million acres.

In the meantime, the March intentions report estimated new-crop corn acres at *91.67 million acres, down from 95.4 million acres in 2013-14*. Traders were expecting a small upward revision, but instead they got a small downward revision. But the USDA is forecasting record yields of 165.3 bushels per acre, compared with last season's yields of 158.8 bushels per acre. The previous record was 164.7 bushels per acre, set in 2009-10.

Weather has been excellent for the corn crop thus far, with a smooth planting season and mostly perfect conditions for the developing crop. The most recent weekly crop progress report shows that 75% is in the good-to-excellent category, compared with 66% at this time last year and the five-year average of 65%. There is a long summer ahead, though.

The status of Ukrainian corn output is a significant factor. The country's ability to maintain its position as the world's third largest corn exporter was obviously of great concern to the market given the chaotic political environment several months ago. In 2013-14 output reached a record 31 million tonnes, and exports were 20 million tonnes, or 16% of world trade. At one point, analysts were forecasting a crop no larger than 23 million tonnes, but estimates have increased substantially. In its June crop report the USDA estimated 2014-15 output at 27 million tonnes. So this issue is off traders' radar screens, at least for now.

Global ending stocks for 2014-15 are estimated to rise to 18.9% of consumption, compared with the five-year average of 16%. If achieved, that would be the highest level since 2008-09. Even so, there is still a marked contrast between corn and the other major global agricultural products which are now at inventory levels not seen since the early 2000s.

The US crop continues to be the make-or-break of the market. For now, although ideal weather conditions persist throughout the US Midwest, we believe that it is too early to be pricing a perfect crop. Stand aside for now.

[By Sholom Sanik, July 7, 2014]

Chart 3 – December corn

Courtesy Bloomberg LP

COTTON

Don't count on China to fight the bear

Global cotton production for the 2014-15 marketing year, which begins on August 1, is estimated to fall for a third consecutive year. Among the three largest producing nations, only the US is expected to see output grow. Planted area was up 960,000 acres from last year, or 9.2%, and at 816 pounds per acre, yields will be about the same. Harvested area is expected to be much higher, though, at 85%, which is the 10-year average, compared with 72% last year. As a result, the USDA's early estimate for US output is 16.5 million bales, up 3.6 million bales, or 28%, from 2013-14. It's early, but the crop looks pretty healthy. The most recent weekly crop progress report shows that the good-to-excellent portion of the crop is 55%, compared with 44% at this time last year.

The US gains, however, will be overshadowed by the other two key producers. Based on planted area, Chinese output will be 2.5 million bales lower than last year, or 7.8%. Indian production is set to fall by 2.5 million bales as well, or 8.2%.

As far as India is concerned, there is a potentially important variable. The El Niño weather disturbance could cause a weaker monsoon, which would certainly limit the size of the crop. Thus far, Indian cotton areas have seen weaker-than-normal monsoon rains – about 90% of average. Currently, the forecast calls for an improvement over the summer, so there is no reason for alarm.

It's all about China and its program to encourage local processors to eat into domestic stockpiles and scale back sharply on imports. Chinese domestic mill demand for 2014-15 is actually estimated to increase by 1.5 million bales, to 36.5 million bales. But imports, which determine US prices, have shriveled. Total Chinese imports in 2012-13 and 2013-14 were 20.3 million bales and 13.5 million bales, respectively. For the new marketing year, they are estimated to plunge to only 8 million bales. To illustrate, consider that as 2013-14 comes to a close, the Chinese have imported only 2.08 million bales from the US, compared with 4.8 millions at this time last year.

Forward US sales for the new marketing year stand at 2.6 million bales, about average for this time of year. Chinese participation is almost nonexistent, which is probably an indication of where we're headed with Chinese foreign demand.

Global consumption is expected to rise by 2.6%, but it will not even make a dent in burdensome inventories. Ending stocks will increase to a record 105.7 million bales, or 94.9% of usage, compared with 92.7% in 2013-14. It could take several seasons of uninspired plantings to work off ending stocks whose size is unrivaled by any agricultural market that we know of.

How to trade this market? Spot prices were hanging in at the 90¢-per-pound level, but with first notice day of the July contract, prices collapsed, dropping by about 15¢ per pound. New crop prices are already heavily discounted. On April 9 we recommended establishing a short position in July cotton, but we mercilessly stopped out right near the highs. Should you have been so fortunate as to have ignored our stop recommendation, by all means, remain short. Getting short at this level this early in the summer, with the invariable weather scares both in the US and in India, does not seem to be a prudent strategy. Rather, stay patiently sidelined and look for weather-related rallies to get short at the 74¢-per-pound level, basis December.

[By Sholom Sanik, July 11, 2014]

Chart 4 – July cotton

Courtesy Bloomberg LP

Chart 5 – December cotton

Courtesy Bloomberg LP

SUGAR

Not so sweet in Sugarland

The hefty premium built into new-crop contract months is eroding (Chart 6). A number of bearish factors emerged to contribute to the decline. July sugar went off the board very weak. And rightly so. Although estimates for the 2013-14 global surplus declined through the marketing year, inventories have been sufficient to meet the needs of world trade. The most recent estimates put the 2013-14 surplus at 2.9 million tonnes.

Down the road, however, the market was pricing in a weak Indian monsoon that might be triggered by an El Niño weather system and flat output in Brazil.

Indeed, the early part of the monsoon season, which began in June, was considerably below normal levels. Indian agriculture relies on the June-through-September monsoon rains for about 70% of annual precipitation. Estimates published as recently as one week ago still put the monsoon rains at 43% below the 50-year average. Yet forecasts for improved rains later in the season overshadowed the current dry conditions, and as a result, traders are pricing a normal-sized crop.

Another consideration that has been somewhat overlooked is that among the major crops grown in India, sugar is probably the least vulnerable to a weak monsoon. Just about all sugar growing regions in India have access to some irrigation, compared with rice, for example, for which irrigation covers only 58% of its crop areas. So while a seriously deficient monsoon would deplete irrigation sources and affect sugar crops as well, a moderately poor monsoon might not have the impact that sugar bulls had anticipated.

In yet another setback to the bullish case we've been building, the sugar-to-ethanol ratio in Brazil has favored sugar more than we expected, despite a drought earlier this year. At present, about 45% of the cane crop is being converted into sugar. In past seasons there were periods when as little as 40% of cane was turned into sugar. We believed that with crude oil prices this high, ethanol efficiency would improve to the point that there would be greater demand for ethanol, and in turn that processors would crush less cane into sugar.

It is a bit puzzling. Mills in both Brazil and India continue to struggle with profitability – particularly in India, where the government has been subsidizing mills to meet their cane costs. Cane prices have not fallen along with world sugar prices. Yet sugar production in both countries remains robust.

Analysts continue to forecast a modest global sugar deficit for the 2014-15 marketing year, citing strong demand growth. Recent estimates for the deficit are in the 500,000-tonne area.

Our exuberance for a bull market in sugar has understandably waned. However, the market is highly complacent that El Niño is not the threat it was believed to be several months ago. If precipitation in Asia over the next few months does not meet current forecasts, cane crops in both India and Thailand will still suffer. This will remain a variable until ample rainfall arrives.

We've been rather complacent ourselves, believing that the coming of a bull market in sugar was just a matter of time. In the meantime, the market continues to tumble, and you cannot fight the tape. For holders of long futures, we advise placing sell stops at 16.75 per pound, basis October, close only. However, our original strategy of taking on the limited risk afforded by purchasing long-dated call options still stands.

[By Sholom Sanik, July 17, 2014]

Chart 6 – October sugar

Courtesy Bloomberg LP

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