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Corn everywhere. Is it enough?

Estimates for 2016-17 South American corn crops continue to grow. In its April crop report the USDA raised Brazilian production by 2 million tonnes, to 93.5 million tonnes. Argentinean output was increased by 1 million tonnes, to 38.5 million tonnes. The combined total of 132 million tonnes surpasses by far the record set in the 2014-15 marketing year of 113 million tonnes.

The dazzling results, however, are still dwarfed by record US output of 385 million tonnes. In the previous 10 years, combined Brazilian and Argentinean corn output averaged 10% of world production. With this year's explosive gains, that ratio moves to 12.5%, definitely making strong inroads, but not displacing the US. As such, with the US still the world's largest grower and exporter, traders have been focused on the outlook for the 2017-18 crop that is now being planted.

The March 31 US planting intentions report was not a great shock. During the period in which farmers make the bulk of planting decisions, soybean prices were outperforming corn – as indicated in Chart 1. It had been known for months that a huge shift was underway – from corn to soybean acres – and the magnitude of that move was mostly in the market, although analysts were off with their guesstimates for both commodities. The average trade guesstimate for the 2017-18 crop was 90.7 million acres, but the actual figure came in at just under 90 million acres, down rather dramatically from the 94 million acres of corn US farmers planted in 2016-17.

The US crop achieved record yields of 174.6 bushels per acre in 2016-17. We're not even going to hazard a guess of how well yields will do this summer, but even with no weather problems and a repeat performance, the US corn crop will be 4.2% smaller than in 2016-17.

Post harvest, corn prices have sloshed around in a narrow range of \$3.50 to \$3.80 per bushel (Chart 2). We believe this is because the extraordinary crops in both North and South America have not created a comfortable global inventory position. This month's production revisions were largely mitigated by an increase in the estimate for consumption. Global ending stocks were revised upwards, to 223 million tonnes, or

21.38% of usage, up from the March estimate of 21.23%. That is actually down from the 2015-16 carryout of 22.03%!

The supply side certainly did its job to bolster inventories. But demand remains strong. US export commitments stand at 50 million tonnes, still 43% above this time last year, compared with the USDA forecast for 56 million tonnes, an increase of only 19%. With 19 weeks remaining in the marketing year, shipments of 34 million tonnes, compared with only 22 million tonnes at this time last year, are commensurate with the USDA projection.

So it is imperative for the 2017-18 US crop to perform well. Thus far, wet weather has meant planting has gotten off to a slow start. As of the most recent crop progress report, only 6% of the crop has been planted, compared with 12% at this time last year and a five-year average of 9%. It is still very early. Ten days of optimum conditions will quickly erase the late start.

It would be a stretch to say that we're looking at a *bona fide* bullish situation. At best, there is a vulnerability issue because demand is strong and the robust crops have done nothing to pad global stocks, as illustrated amply above. We advise holding on to long positions established as per our January 18 recommendation. Maintain stops at \$3.40 per bushel, basis July corn, close only.

[Sholom Sanik, April 21, 2017]

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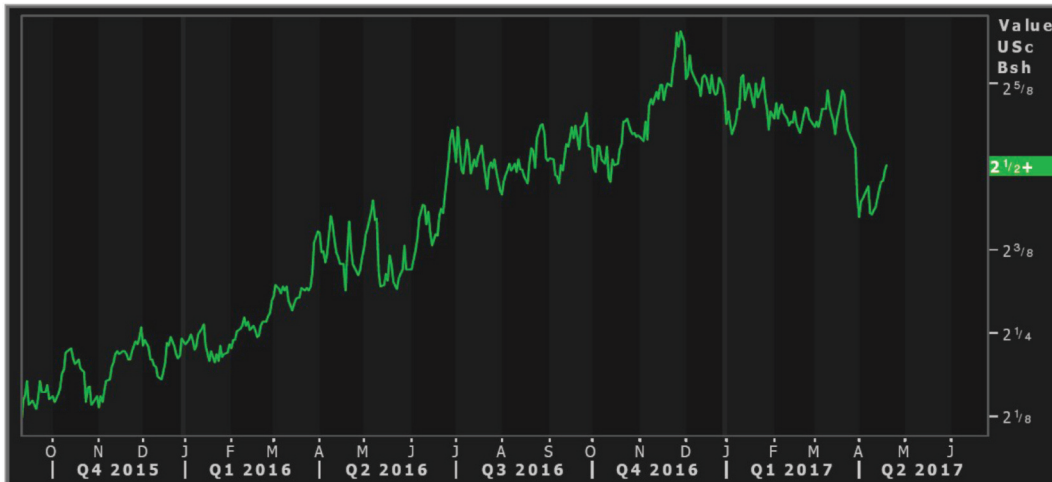
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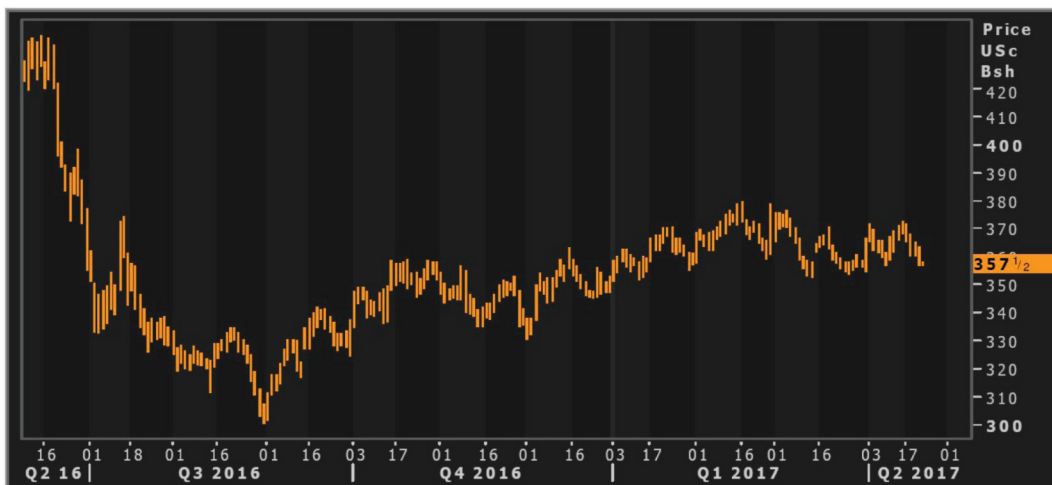
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Chart 1 – November soybeans/December corn ratio



Courtesy Reuters

Chart 2 – Nearest contract corn



Courtesy Reuters

SUGAR

Crops set for recovery. Lights our for the bull?

After two consecutive years of global production/consumption deficits, sugar output in the 2017-18 marketing year is expected to jump to a record high of 190 million tonnes. The increase should bring the balance sheet back into surplus.

Crops of the key producing/exporting nations are in their early stages. Even in Brazil, where the cane crush is underway, it's a bit premature to make any bold predictions. Here's what we do know:

Brazil

Cultivated cane area will be about 3.5% smaller than in 2016-17. At present, analysts estimate that sugar output in the Center South, where 90% of the crop is grown, will fall by only 1%, in part because of an anticipated uptick in the amount of sugar diverted from ethanol production. One forecast puts ethanol output at a ratio of 53%/47%, down from 53.7%/46.3% in 2016-17.

There are two reasons why this estimate might be pre-

mature. First, sugar spent most of last year's crushing season at prices that at one point reached close to 24¢ per pound. The incentive was obviously slanted towards sugar production. When sugar was trading between 10¢ and 14¢ per pound in 2014 and 2015, the ethanol/sugar output ratio was as high as 59.4%/40.6% (Chart 3). Unless sugar prices rally from their recent deep slide, we are confident that these estimates are stale and that we will see ethanol production strengthen.

Which brings us to the second point. Brazil is the largest customer for US ethanol. This situation developed precisely because Brazilian crushers were diverting more cane to sugar than they had been in recent years, which tightened the ethanol market in Brazil. This matter infuriated ethanol producers who were losing market share to US exporters in some regions. The government is now supporting a proposal to slap a 20% import tariff on all ethanol imported from the US. Demand for ethanol in Brazil is a given. Smaller imports would translate directly into less sugar production.

India

After two consecutive droughts, the 2017-18 season is expected to see Indian crops bounce back, with sugar output estimated at about 24 million tonnes. The current season eked out between 20 and 21 million tonnes, down from 25 million tonnes in 2015-16. The crushing season does not begin until October, and much has to go right before any forecasts become meaningful. A healthy monsoon is absolutely essential. Indian consumption has risen to about 26 million tonnes per annum, so even if the production forecasts are accurate, we're still looking at a drawdown.

Thailand, China

Rounding out the other important Asian players, China and Thailand should also benefit from a return to normal precipitation patterns.

Thailand is a vital exporter, and is also expected to recover to 11.7 million tonnes, up from 10 million tonnes in 2016-17.

Chinese output should jump by 10%, to close to 10 million tonnes, but the production/consumption deficit is still at least four million tonnes, which will require imports to fill the gap.

EU

The EU is working towards eliminating export quotas, and that has created an incentive for farmers to expand beet crops. One estimate puts the increase in sugar available for export at 2.5 million tonnes.

So the supply side looks healthy, and as a result, commodity funds have thrown in the towel on the bull. Chart 4 shows that the net-long position is all but gone.

The sharp drop in prices, in our opinion, brings us back to square one. Mills in Brazil and India do not earn a profit at these prices. In fact, the reason that cane area in Brazil has remained stagnant is because capital available for new investment is scarce. And that angle will not improve if prices remain weak. Furthermore, it all hinges on good weather in Asia. We therefore believe that a lot of vulnerability remains.

Maintain long positions in long-dated call options. Buy March 2018 18¢ calls, presently trading at about 1¢ per pound. *[By Sholom Sanik, May 2, 2017]*

Chart 3 – Weekly nearest contract ICE sugar



Courtesy Reuters

Chart 4 – CFTC net fund position (bar chart)



Source: CFTC

COCOA

Production soars

The 2016-17 main crop in the Ivory Coast is complete, and the mid crop is now being harvested. The most recent data show that port arrivals have reached 1.496 million tonnes, compared with 1.26 million tonnes at this time last year. With five months remaining in the marketing year, we will easily surpass last year’s output total of 1.57 million tonnes. Barring unforeseen circumstances, production should set a record, above output levels reached in 2014-15 and 2013-14 of 1.796 million tonnes and 1.746 million tonnes, respectively. In its most recent monthly bulletin, the International Cocoa Organization (ICCO) forecasts Ivorian output at 1.9 million tonnes.

Information for output developments in Ghana, the world’s second-largest producer, are sketchy. From what we do know, production should climb to over 800,000 tonnes, exceeding early-season estimates, and possibly challenge the 897,000-tonne record set in the 2013-14 season. The ICCO estimate for the season is 850,000 tonnes.

On the demand side, first-quarter grinding data reported in mid-April show anemic growth in importing regions. The EU grind was up 1.09% year-over-year, while the North American grind was similarly weak, only 1.16% higher.

Processing results in origin countries, however, underscore the shift in grinding away from Europe and North America. The first-quarter Asian grind was down 5.9% from the previous quarter, but was up 19.2% year-over-year.

The Ivory Coast is now the single largest grinding country. Statistics are reported monthly, rather than quarterly. So far for this marketing year, grindings are running 8% above the same period in 2015-16.

Product prices have remained steady *vis-à-vis* bean

prices. As indicated in Chart 6, the combined butter/powder ratio has firmed towards the high of the end of the recent range, which could give processors some incentive to increase bean purchases.

After including grinding results in origin countries, global demand is expected to grow by 3% in 2016-17. Even if we were generous and assumed that weak bean prices and slightly stronger product prices will result in demand growth of 4% to 5%, it will still be dwarfed by the estimated 15% growth in global output. According to the ICCO, the previous three seasons ended with global inventories that averaged 36.7% of consumption. This season that figure is expected to jump to 39.3%.

Revenue from cocoa exports is a key component of the economies of West African producing nations. Normally, the governments are busy making projections – often unrealistic ones – about how much cocoa its farmers can and will produce. The tone has changed. The Ivory Coast and Ghana have been issuing statements about the crisis their countries face from the drop in cocoa prices. They have now added a call to stimulate chocolate consumption and increase quality.

They will not achieve better-quality beans in a bear market. The drop in farm revenue will have the opposite effect, with less capital available for fertilizer and pesticides. And eventually, production will begin to falter with global prices at levels that cannot sustain proper maintenance of plantations. For now, though, burdensome stocks will have to be whittled down before prices can recover.

Remain short as per our July 21 recommendation. Lower the stop suggested on February 24, from \$2,350 per tonne, to \$2,150, basis July, close only.

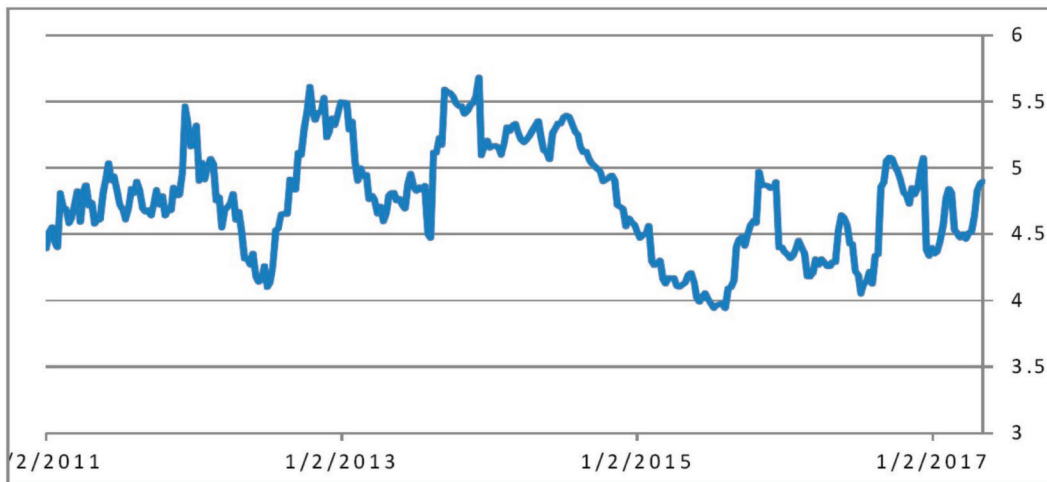
[By Sholom Sanik, May 4, 2017]

Chart 5 – July cocoa



Courtesy Reuters

Chart 6 – Butter/powder ratio



SOYBEANS

Soybeans galore

Soybean prices have tumbled by about \$1.50 per bushel since the beginning of the year. The three countries that grow more than 82% of the world’s soybeans – the US, Brazil, and Argentina – keep pumping out bin-busting crops.

Argentina is the weakest link, after struggling with weather over the past two seasons, but it is still a contributing factor. Early season fears of a crop failure were unfounded. In its April crop report, the USDA puts 2016-17 output at 56 million tonnes, up 500,000 tonnes from the March estimate, but down from the record crop achieved in 2014-15 of 61.40 million tonnes.

Estimates for Brazil, however, kept rising through-

out the growing season. With the harvest nearly complete, the USDA estimate is 111 million tonnes, 3 million tonnes above the March estimate and 14.5% above 2015-16 production of 96.5%!

The US harvested 117.21 million tonnes, compared with 106.9 million tonnes in both 2014-15 and 2015-16.

And the trend continues. Planting of the 2017-18 US crop is in its early stages, but off to a good start. As of the most recent USDA weekly crop progress report, 10% of the crop has been planted, slightly ahead of the five-year average of 7%.

US farmers are expected to expand planted area rather dramatically. The average guesstimate for the

March 31 planting intentions report was 88.214 million acres. That compares with only 83.433 million acres planted for the 2015-16 crop. Traders already knew from the February USDA Forum estimate that a huge shift was afoot – away from corn acres and over to soybeans. But the actual figure came in at 90 million tonnes. With normal weather and if yields and the planting-to-harvest ratio are similar to last year's, that would mean a crop of 127 million tonnes.

Demand is strong. The USDA estimates that Chinese imports for 2016-17 will grow by 5.7%. Government customs data show that for the first-quarter, imports were up 20%, year-over year.

US export commitments stand at 56.6 million tonnes, compared with the USDA's forecast for total annual sales of 55.1 million tonnes. Exporters have already shipped 49.8 million tonnes. That's 90% of projected sales, compared with 80% shipped at this time last year. So it's a

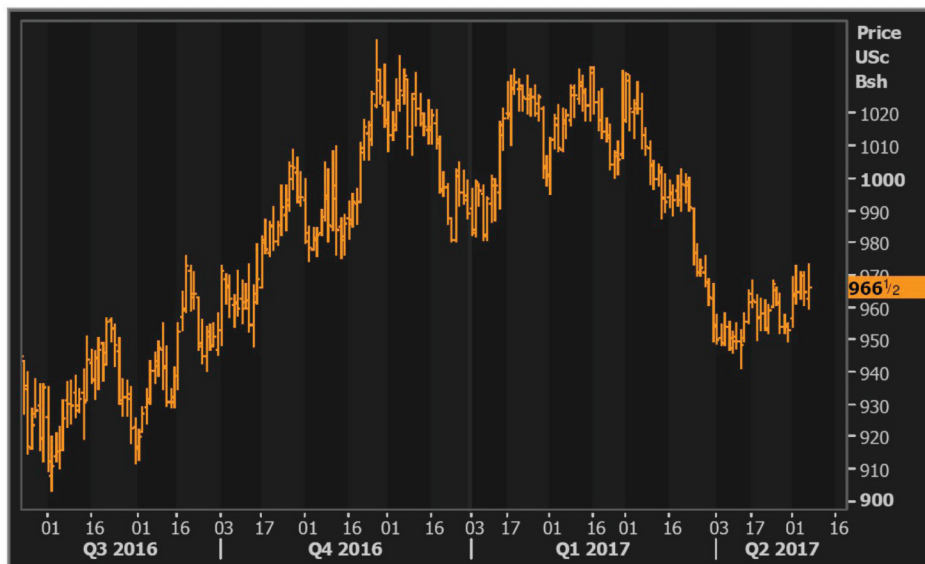
good bet that this target will not only be met, but that it could be exceeded.

The upward revision to South American crops had a material impact on 2016-17 ending stocks, rising from the March estimate of 24.9% to 26.3%. That will be the largest carryover since 2010-11 when global ending stocks reached 27.8%. So even with the dazzling production tallies, it is fair to say that demand has kept pace.

By all rights, in light of the massive number of additional acres being planted, US farmers should harvest a huge crop this coming fall, and prices should head lower. However, it's a tricky time of year for trading US crops. While crop progress is steady, there's no way of knowing what kind of weather we'll get in July and August.

We recommend establishing a moderate-sized short position in November soybeans, currently trading at about \$9.65 per bushel. Place initial protective buy stops at \$10, close only. *[By Sholom Sanik, May 8, 2017]*

Chart 7 – November soybeans



Courtesy Reuters

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