FRIEDBERG'S
FOCUS ON FUTURES
Friedberg Mercantile Group Ltd.

Volume 22, No. 4 July 9, 2019

Wet weather wreaks havoc with US corn planting

Over the past two weeks, corn prices spiked by more than 80¢ per bushel (Chart 1). Soggy weather has delayed planting across US planting regions. As of the most recent weekly USDA planting report, only 58% of the crop has been planted. This compares with 90% at this time last year and a five-year average of 90%. Planting delays are just about an annual rite of spring, but this delay is large enough for us to at least consider the possibility that final output will be affected materially. The general theory is that yield suffers when corn is planted late in the optimum planting window.

Iowa, Illinois, Nebraska, and Minnesota are the top four corn states, typically accounting for more than half of US output. The number-two state, Illinois, has planted only 35% of its crop. To qualify for Federal crop insurance, farmers must plant their crop by specific dates unique to each region. The final date is June 5, and for some regions the date has passed.

As such, the USDA's estimate for record production of 15.03 billion bushels (381.78 million tonnes) in 2019-20 is in all likelihood ancient history. The most recent acreage estimate called for planted area of 92.8 million acres. We're guessing that before the release of the June 28 acreage report, the USDA will revise planted area downwards in its monthly supply/demand situation report to be released on June 8. In addition, the USDA used a harvested-to-planted ratio of 92%, slightly higher than the two previous seasons. That too will be subject to revision.

For the moment, the effect on the global situation will not be catastrophic. However, a worst-case scenario for the US crop could alter the landscape.

Demand has been soft. US export commitments for the current 2018-19 marketing year stand at 47.3 million tonnes, down 11.4% from this time last year. The USDA target is a downwardly revised 58.33 million tonnes, and that represents a drop from last season of only 5.6%. While export sales typically tail off from this point as South American supplies become available, there have been years in which exports remained strong through June. Still, with just over three months remaining in the marketing year, it would be a challenge to meet even the downwardly revised estimate.

Furthermore, South American corn crops are at record levels. In May, the USDA revised Brazilian and Argentinean output upwards by 4 million and 3 million tonnes, to 100 million tonnes and 50 million tonnes, respectively.

The USDA used 176 bushels per acre for its initial estimate of yield, which is close to the record levels of the past two seasons. While it is quite true that rarely a year goes by without a spring-planting weather scare, this one seems to be deep. By calculating even modest downward revisions to acreage, yield, and the harvested-to-planted ratio, the USDA's estimate for US 2019-20 output should be about 750 million bushels, or close to 20 million tonnes, below the May estimate.

The May USDA forecast for 2019-20 global ending stocks was looking for an increase to 122.9 million tonnes, or 14.2% of consumption, up from 13.54% in 2018-19. Plugging in the effects of a possible US crop failure, that figure could drop to below 12% of usage, the

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lowest carryout in modern history.

We were stopped out of our short position in July corn at $4.05 per bushel, as per our March 5 recommendation. If the US corn crop does not stage a recovery, we will be headed into a new paradigm for corn. Still, we're not going to advise chasing the long side after such an exuberant rally. Remain sidelined, but stay tuned.

Note: The USDA introduced a new reporting feature for the 2019-20 marketing year. For the global balance sheet, it will provide an item called "World Less China." Among the agricultural markets that we cover, this will be particularly useful for corn. China is self-sufficient in corn, and as a result, its world trade is negligible. China's National Bureau of Statistics restated ending stocks in November by "finding" 149 million tonnes of corn. Including a bloated ending-stock figure distorts significant changes for exporting and importing countries. Going forward, when we use "global" we will be referring to the "World Less China" figure.

[By Sholom Sanik, May 29, 2019]

Chart 1 – CBOT December corn

Chart courtesy Reuters

SOYBEANS

Delayed planting is not the issue

We detailed how the extremely wet spring in the US Midwest has slowed planting progress of the corn crop (see *Focus on Futures*, May 29). Soybean planting progress is equally pathetic. As of the most recent USDA field report, only 39% of the crop has been planted, compared with 86% last year at this time and a five-year average of 79%. Planting progress in two of the top four soybean states is below the national average. Illinois and Indiana have planted only 21% and 17% of their respective crops.

Sounds ominous, and historically speaking, in years of extreme adverse weather conditions, both corn and soybeans have experienced monster rallies that have moved in tandem. For the current environment, however, we could see a decoupling of the two commodities.

First, soybeans have the benefit of a later planting window for crop insurance. While the last date for corn has already passed, key soybean states can plant until June 10, and some of the southern states have until late June.

Far more significant, though, is the lack of progress on the US/China trade spat. We're deep into the 2018-19 marketing year. Many beans continue to sit idly in their silos as the US farmer's biggest customer has taken only a fraction of its normal purchases. Consider the data: Total sales to China (shipped and unshipped) stand at 13.55 million tonnes as of the most recent USDA weekly export report. That compares with 28.65 million tonnes at this juncture of the 2017-18 marketing year.

Exports to other US customers have been very strong. US President Trump's claim several months ago that the EU would increase its US imports of soybeans was accurate – total sales increased by 100%, to 7.18 million tonnes. As illustrated, however, it's a drop in the bucket when compared with the losses suffered by Chinese cutbacks. Total US exports to date (shipped and unshipped) have reached only 46.68 million tonnes, down from 55.63 million tonnes at this time last year.

Furthermore, the Chinese have been accepting some shipments, but 6.67 million tonnes remain unshipped, an

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extraordinarily high ratio of unshipped to shipped. Last year at this time, only 1.49 million tonnes remained unshipped. Some analysts believe that given the toxic trade climate, there is a very good chance that the Chinese will cancel existing contracts. At the best of times, cancellations are prevalent at this point of the season.

The flip side of this seemingly insurmountable bearish case is that Chinese domestic soybean demand is over 100 million tonnes. Chinese farmers grow only 15% of total domestic needs and are therefore reliant on imports. While Brazilian sales to China have increased dramatically and will continue to do so, at least in the near term, the Chinese pork and poultry industry has a problem that is only being pushed down the road. At the moment, though, with South American harvests becoming available, pork and poultry producers can avoid the 25% import tariffs the Chinese government imposed on US imports by buying Brazilian.

With its near-record crop, Brazil can make up the shortfall China is suffering by not buying from the US. But Brazil consumes about 35% of its crop domestically. Even if Brazilian exporters were to deplete their inventories – the USDA estimates 2018-19 ending stocks at 26 million tonnes – Brazil can only feed China's massive requirements for so long.

Nevertheless, for the foreseeable future, we believe that burdensome carryover stocks in the US will only be exacerbated by a decent harvest this fall, which at this point is still a very real possibility. US acreage for the new crop is set to dip by 5%, to 84.6 million acres, which is still too large a crop given the environment.

Prices have rallied because of the wet US weather, but in the meantime, they have actually fallen relative to Brazilian prices as shown in Chart 3. Any stabilization in US soybean planting progress should erase the price gains we've seen this spring.

Establish short positions in November soybeans, currently trading at about $8.80 per bushel. Place initial buy stops at $9.35, close only.

[By Sholom Sanik, June 7, 2019]

Chart 2 – CBOT November soybeans

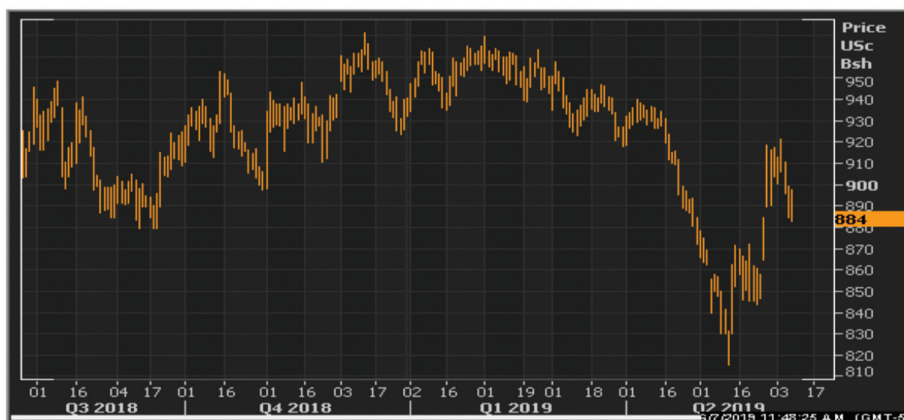

Chart courtesy Reuters

Chart 3 – Brazilian/US soybeans spread

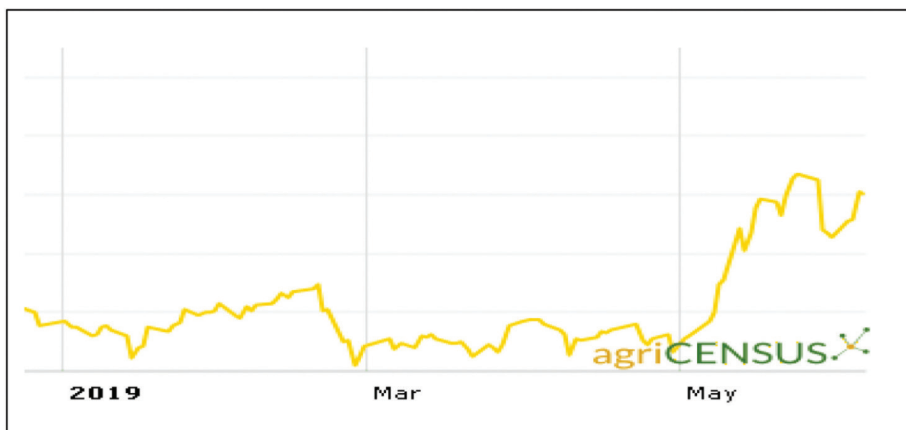

Chart courtesy agriCensus

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SUGAR

The bull is about to charge

Sugar prices have shown some signs of life (Chart 4). For the moment, key resistance levels and the long-term downtrend remain intact. Just a little counter-trend rally? It would make life simple to ascribe the strength to fund short-covering ahead of the July futures contract expiry. The short-covering, however, has been driven by important fundamental developments.

India

First, the outlook for 2019-20 Indian production levels has taken a step backwards. The monsoon is arriving late, and some regions are already experiencing drought conditions. While it is still a bit early, the government meteorologists believe that it will be difficult to compensate for the lost moisture. On a country-wide basis precipitation has been 43% below normal levels.

Of grave concern for sugar in particular is that rainfall in Maharashtra, the second-largest producing state, has been 68% below normal. One government estimate puts the output loss for Maharashtra at 4 million tonnes. That in itself could lower total Indian output below domestic consumption. These estimates are based on abandonment and do not account for yields that are likely to be below average if dry conditions persist throughout the growing season.

With uncertainty surrounding sugar output for the new marketing year that begins in October, the likelihood of seeing an increase in Indian exports is not huge. As it is, exporters have not taken the bait of government incentives. With the possibility (of course, in our mind-set that would read *probability*) of higher sugar prices down the road, any lightening of the large Indian carryout will be pushed down the road once again.

Brazil

In a surprising twist, the extremely wet weather in the US Midwest could affect Brazilian sugar production. In the 2018-19 season, Brazilian sugar output fell primarily because of a record low sugar/ethanol production ratio of 35%/65%. Analysts have asserted that this will not be repeated and that we would be looking at a return to a trendline ratio of about 40%/60%. Thus far, the ratio continues to hover around 35%/65%.

The US corn crop could be in serious trouble. Ethanol prices will rise alongside corn prices, establishing a standard for higher international prices. In turn this will maintain the incentive for Brazilian processors to continue to favor ethanol production over sugar.

It is premature to issue any close-to-accurate forecasts for the global 2019-20 production/consumption balance. But the estimates that we have seen for a reversal from surplus to deficit have not taken into consideration these new weather-related developments in India and the US, all of which occurred fairly recently. Estimates for the 2019-20 deficit ranged from about 2 million to 6 million tonnes. We believe that the next round of forecasts will show larger deficits.

It is difficult to say precisely at what price level sugar will become competitive with ethanol production in Brazil. One recent estimate puts that number at 15¢ per pound.

Commodity funds have reluctantly been covering their short positions. Chart 5 shows that the recent rally has not inspired much fear of higher prices. It will.

Liquidate long positions in October 13.5¢ calls, first recommended on January 30, and use the proceeds to roll into March 14¢ calls, currently trading at about 0.75¢.

[By Sholom Sanik, June 20, 2019]

Chart 4 – ICE October sugar

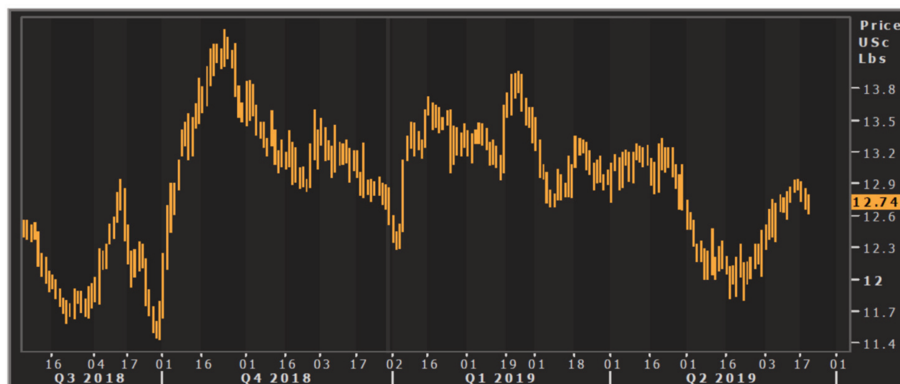

Chart courtesy Reuters

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Chart 5 – CFTC commodity fund net-short position (bar)

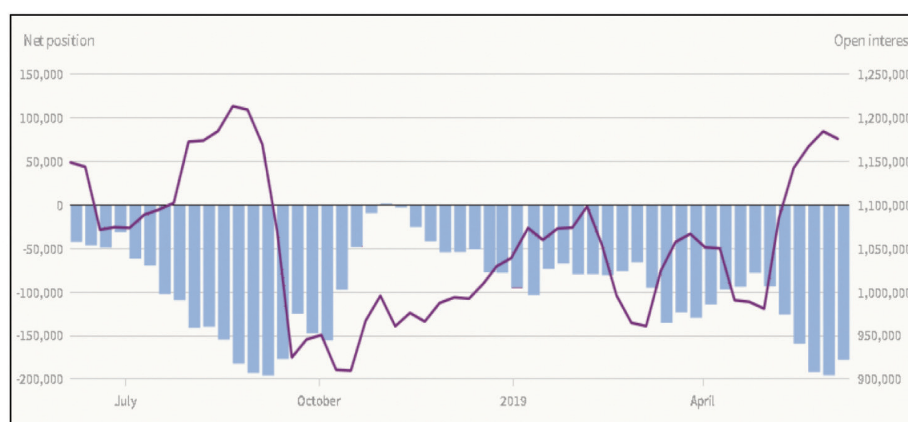

Chart source: Reuters

CORN

A meaningless acreage report

Corn prices rose by more than $1 per bushel from mid-May through mid-June. An extremely wet spring delayed planting by historic proportions. It was assumed that many acres would not be planted at all. Acres that were planted late would have a shorter growing season, which would result in smaller yields, in addition to the risk of frost for late harvest. The rally paused in the days leading up to the June 28 acreage update, as traders were eager to have a look at the USDA's assessment of the damage (Chart 6).

It was a colossal miss, and the market responded with a 50¢-per-bushel setback from the highs reached on June 17. Total planted corn area was estimated at 91.7 million acres, down only 1.09 million acres from the interim estimate that appeared in the June crop report. The average of analysts' guesstimates was 86.662 million acres, with the high end of the range at 89.8 million acres! How strange is it that well-regarded analysts were off by such a wide margin? Of course, no single analyst has the resources available to the USDA for conducting country-wide field surveys. The average guesstimate for most USDA reports, however, is typically far closer to the actual result.

Indeed, this situation was unique. There is no question that the data were dated. At the time of the survey, which concluded with the weekly reporting session of June 2, planting progress was at a historically low level of 83% – below the 10-year average. The USDA obviously included acres that were *intended* to be planted but may not get planted. The USDA acknowledged that the number might be too high by indicating that there will be a resurvey and the results will be included in the August crop report – the same as it did for the June crop report.

It would be useful to get a picture of what the US and global balance sheets might look like in the likely scenario that the USDA revises US corn acreage to reflect current realities.

While the USDA decided to adopt a cautious stance on acreage, there was no hesitation in taking an axe to yields. In the June crop report, the bushel-per-acre (bpa) yield was slashed by 10 bushels from the May estimate, to 166 bpa. The harvested-to-planted ratio was maintained at a trendline pace. Now, if we take a conservative approach and assume that when the USDA revises its planted area estimate in August it will come in, say, 1 million acres higher than the average of analysts' guesstimates, that would be 87.6 million acres. Using a 166 bpa yield and a (optimistic) 91.7% harvested-to-planted ratio, that would cut the current output estimate by an additional 350 million bushels (8.9 million tonnes), to 13.34 billion bushels (338.9 million tonnes). The stocks-to-consumption ratio would fall to 9.3%. That would be down from the average of the past several seasons of just under 15%. The last period in which the US carryout was below 10% was between 2010 and 2013, when corn prices skyrocketed to $8 per bushel (Chart 7).

The difference between now and then, some might argue, is the advent of explosive South American production growth. A US crop failure, however, would make this progress largely irrelevant. First, global demand has grown alongside the increases in output by Brazil and Argentina. Besides – very much unlike soybeans – the additional corn available from South American producing nations over the past few seasons is a drop in the bucket when pitted against US output. In the outgoing 2018-19 marketing year, the US grew 366 million tonnes of corn, compared with 150 million tonnes between

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Brazil and Argentina. By contrast, US 2018-19 soybean production was 123 million tonnes, pitted against combined output of 173 million tonnes for Brazil and Argentina.

So the US will retain its status as the supplier of last resort for corn. A sharp drop in US output would tighten supplies. All other factors being equal, in our hypothetical estimate model for the USDA's August acreage revision, 2019-20 global stocks would fall to 10.5% of consumption, down from 13.4% in 2018-19 and 14.1% in 2017-18.

In our most recent review of the weather-hampered US planting season (see *Focus on Futures*, May 29) we advised not chasing the market. Having rallied off the lows of the selloff that ensued after the surprisingly bearish USDA acreage report, prices are at about the same level they were at that time. We now advise establishing long positions in December corn. Place initial stops at $4 per bushel, close only.

[By Sholom Sanik, July 4, 2019]

Chart 6 – CBOT December corn

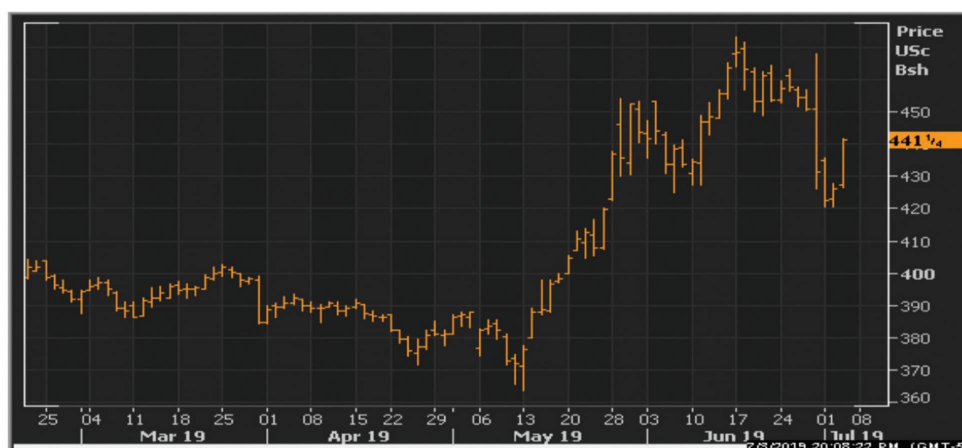

Chart source: Reuters

Chart 7 – CBOT corn, nearest contract monthly

Chart source: Reuters

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