

January 15, 2010

2010

Will the year 2010 present the risk management challenges that 2009 did? So far, it looks like it could. During 2009 prices were volatile. Nearby corn futures prices had a range of about \$1.50 per bushel and soybean futures prices ranged \$4.50. 2010 futures prices are starting out with similar volatility. In less than two weeks, March corn futures prices have ranged about \$0.57 and March soybean futures prices have moved more than \$1.00 per bushel!

Risk and uncertainty were not just limited to prices. The 2010 production season started out wet with field work delays and didn't get any better. The wet conditions continued into fall with muddy fields and harvest is still not complete with estimates of 400 million or more bushels of 2009 corn production remaining in the field. In spite of these production problems and price risks, record crops were produced and there were many opportunities to lock in very profitable prices.

The USDA's final production and supply/demand estimates released on January 12, 2010 included production surprises. In spite of everything that seemed to go wrong in 2009, corn yields were reported to be record high at 165.2 bpa. A slight increase in harvested acreage also added to total production with corn production estimated at a record 13.151 bushels. In spite of financial stress in the livestock industry and a slow export pace, first quarter corn use appears strong. So the USDA increased expected corn feed and residual use, which added to expected record total use. But the large production caused corn 2009-10 projected ending stocks swelled to 1.764 billion bushels.

The USDA's bearish news continued for soybean and wheat prices. The soybean production in South America will soon offer export competition. The US and World soybean carryovers are expected to increase, since record demand with strong exports will not offset record soybean production from the US, Argentina and Brazil. Although the lowest winter wheat acreage since 1913 seems bullish, increased World wheat production and slow US exports is resulting in burdensome ending stocks. The low winter wheat acreage also frees up an estimated nearly four million acres that could go to corn or soybeans.

Uncertainty remains. The USDA's final production estimates may not really be "final." Producer production surveys were conducted when significant amounts of 2009's crops were still in the field. Some analysts also question whether the USDA's estimating methods adequately account for impact of lower test weight on production. The USDA will re-survey some states and may (or may not) update the numbers in March. Although currently overshadowed by the supply/demand estimates, many other factors also impact market uncertainty, volatility and risk. Briefly, some these are:

- ***Energy Prices:*** Ethanol production amounts to about one-third of corn use and many have placed the blame for high feed prices and corn market volatility on ethanol production. Although oil prices have obviously added to market risk and volatility, there are many other factors affecting the markets as well.

- ***Economic Conditions:*** The weak economy has weakened commodity demand and reduced investment. Is the economy recovering? Many believe it is and that it will support commodity prices. Others worry about how long a “jobless recovery” with large public and private debt can last.
- ***The Value of the Dollar:*** A weaker dollar contributes to stronger export demand. However, strength in the dollar pressures export demand and prices. Uncertainty about the economy and the dollar value adds to market volatility.
- ***Speculation/Investment:*** Speculators, fund traders, swap dealers and others have either been credited with supporting commodity markets or blamed for market volatility. Action by these traders will contribute to price direction and add to volatility and risk.
- ***World Grain Supply and Demand:*** Coarse grain supplies are tightening up, but wheat supplies are burdensome. South American production expectations are on track to increase soybean supplies and export competition. Grain export demand will also be influenced by foreign economic recoveries and the value of the dollar. The focus of soybean export demand continues to be China and whether their strong appetite for soybeans will continue. This mixed export outlook adds to uncertainty.
- ***2010 Acreage:*** Market analysts are beginning to talk about 2010 crop acreage and what is needed. However, with increased US corn carryover and increasing World soybean supplies, some are questioning about how much “bidding for acres” really needs to occur in the markets.
- ***Weather:*** The muddy field conditions that delayed harvest also caused delays in tillage and fall fertilizer applications for 2010 crops. Good spring conditions are needed for timely planting. The expected need for large crops again in 2010 will also make the markets sensitive to growing season conditions.
- ***Politics:*** Whether the biodiesel credit is extended and how EPA decides on ethanol mandates will be watched. Climate change discussions may impact grain markets. These along with other domestic and foreign policy discussions add significant political uncertainty to market structures.

These many factors have contributed to complicated and risky markets that are difficult to predict. It is easy to get focused on one or more factors that seem to be currently driving the markets then another factor unexpectedly influences trading and dramatically changes market action. Trying to outguess the markets seems to be more futile and costly than ever.

The latest supply and demand estimates have made storing 2009 corn and soybean production more risky. Among the most difficult marketing decisions is making sales after a significant change

occurs in the market, especially if prices have turned lower. This situation requires a disciplined approach to marketing that takes into account profitability and market price risk management.

The sharp price declines triggered technical sell signals. The penetration of: short-term uptrends, areas of price support, moving averages, etc. are signals of a possible market turn around. The problem, of course, is that the rapid price drop results in significantly lower and disappointing prices when compared with recent prices. However, futures prices in most cases still result in profitable cash bids that are within or near the USDA's projected price ranges. Downside risk should be recognized before rejecting adding to sales, especially if a large percentage of the 2009 crop is still in storage.

What about new crop marketing plans? These also require discipline by identifying profit potential and recognition of acceptable or unacceptable risk.

In spite of the price declines, new crop corn futures prices continue to offer profit potential. Although the prices are sharply lower, they result in new crop corn bids near many analysts' projections for average 2010-11 corn prices. While these are less favorable prices than only a week ago, it is hard to argue against making new crop corn sales at profitable levels. However, in spite of the downside price risks, seasonal trends and other market factors suggest that prices could recover. This, along with all of the uncertainty and volatility in the markets, suggests a cautious approach of spreading sales and protecting profits.

New crop soybean futures prices are also offering profits. Prices are well above what is needed to breakeven and also somewhat above some analysts' expectations for average 2010-11 soybean prices. There is significant downside risk in soybean prices due to expectations for increasing South American production and world supplies. Technical signals are weaker for soybeans as well. This suggests a somewhat more aggressive soybean new crop sales strategy, since delaying sales in soybeans may carry more risk than delaying corn sales.

Volatile markets create risk, but they also provide opportunities. The year 2010 is beginning with volatile markets. A large number of market fundamentals and outside factors are contributing to market risk, but they may also be a key to marketing opportunities. The challenging task, as always, will be to spread sales and capture profitable marketing opportunities when they are offered.