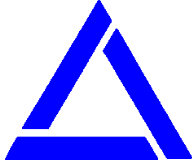

The Grain Service Newsletter

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November 15, 2018 No. 22-18

TRADE BATTLES

Trade and tariffs continue to dominate the news cycle with no resolution in sight. China sent written responses this week to some trade issues raised by the US in a videoconference earlier this week, but a senior administration official indicated China's answers are unlikely to trigger any breakthrough for the meeting scheduled between Presidents Trump and Xi at the G20 meeting later this month. Some Chinese officials were in Washington this week to 'talk trade,' also with no apparent progress. US White House Trade Advisor Peter Navarro has several times thrown cold water on ideas of a trade resolution, only to have Larry Kudlow – Director of the Economic Council – contradict him. There are some hopeful signs, but in the meantime the window is closing for the US to sell meaningful volumes of soybeans to China before Brazil's harvest begins in December/January. Some speakers at the Global Grain Conference in Europe this week said China is likely able to hold out against US soybeans until Brazil's harvest begins. US soybean export sales are currently just 69% of this time a year ago; sales to other importing countries can trim that deficit in the months ahead but the market impact (basis or futures) is likely to be much less than with big sales to China. Net soybean sales to China for 2018 crop – after cancellations – are down to 26M bushels, with half of those sales still unshipped.

On the plus side there are traders who say China will still need US soybeans this crop year, but in the meantime China is laying groundwork for longer-term alternatives. Several major international grain firms are said to have closed deals this week to establish future trade to China out of Brazil, Argentina, and Uruguay. China is also working on other long-term arrangements under their "Belt and Road" initiative to assure China of their raw material and supply needs – much like the old "Silk Road" trade from centuries ago. A valid fear is that the US has lost its biggest advantage in trade with China: Our dependability in trade, logistics, and quality. That fear extends forward that US soybean acreage may decline beyond 2019 in favor of corn.

WHEN IS A RECORD NOT A RECORD?

USDA statistics show that the total volume of September 1 corn and soybean stocks plus 2018 production is a record 21.8 billion bushels. Add to that US Sept 1 wheat stocks of 2.4 billion bushels, 113M bushels higher than a year ago. Anticipating a tsunami of grain, the industry had braced itself for widespread space and freight problems. The absence of the China soybean market this fall only compounded the expected space problems, helping to take the N. Plains soybean basis to -150Nov or weaker, and spilling into the Gulf soybean basis which traded *at negative basis values in September for the first time in over 30 years*. Yet here we are in mid-November with harvest still underway in many areas and basis levels firming in most markets – some faster than others for certain. Rail and barge freight are both weak, with barge freight trading near multi-year lows for November. Granted, there are piles of soybeans in the N. Plains along with countless bags of corn and soybeans, but the bushels are now largely 'tucked away.'

Compare the changes in spot bids from October 10 to values on November 13 as shown in the tables on page 2. We converted the October 10 soybean bids from Nov futures to January using a Nov/Jan spread of 13¢ carry to be conservative. (The Nov/Jan futures spread closed on October 10 at 14¼ carry.) All corn basis values were, and are, quoted against December futures. All spot basis values were from DTN's daily basis recap.

The change shown reflects Nov 13 basis minus Oct 10 basis):

Change:	ND/SD	ND/SD	ND/SD	MN	MN	NE	IA	IA	IL	IL
Corn	+2¢	+11		+18	+16	+13	+18	+12	+20	+17
Sbn	+30¢	+19	+43	+28	+38	+23	+23	+13	+28	+41

Note: the corn and soybean markets in the states shown are not necessarily the same; not all locations have both corn and soybean markets. For example the first corn bid selected for MN is Marshall MN, the first soybean bid is Mankato...

	Gulf	Barge freight*	MO	IN	OH	OH			
Corn	-0- ¢	(21¢)	-3	+15	+13	+7			
Sbn	+18¢	(22¢)	+42	+33	+33	+16			

*barge freight, Illinois River origins converted to ¢/bushel, change from Oct 10 vs Nov 13

Corn basis has firmed from 2 to 20¢ at the destinations shown here, with soybean basis rising between 13 and 43¢ in five weeks! Some of the firming represents 'earning the carry', but these gains exceed that.

But why is soybean basis firming in the face of the record soybean crop, large beginning stocks than a year ago, little to no demand at the PNW, and total soybean export inspections just 52% of this time a year ago? Several factors are at work: (1) farmers resisted the cheap cash prices, with many opting to store much of their production after their earlier contracts were filled, (2) the 'record' fall volumes aren't record high in all areas, and (3) the last 10+% of harvest is coming slow. Soybean harvest was 88% as of November 11, but that was the slowest in the last nine years and the second slowest in 20+ years. There were 100M bushels of soybeans in the field in the five states of IA, MN, SD, ND, and NE, and 552M bushels in the field nationwide! Last year at this point nationwide there were around 310M bushels of soybeans left to harvest. The slower pace has given elevators (and farmers) more time to move inventory or even put soybeans in less efficient storage such as 'grain bags'. And each week the US is crushing or exporting close to 100M bushels, which after two months is the equivalent of 800M bushels of bin space. Plus, wide futures carries have encouraged hedgers to hold soybeans where possible.

The rising soybean basis should encourage elevators to review their merchandising plans. Perhaps carrying hedged soybeans will not be the best strategy for much longer given the higher carrying costs for $8+/bushel plus 3-4¢/month for interest. Some markets show 20-30¢ gross carries to early summer, compared to holding costs of 25¢ or so. But some other markets show published carries of 50¢ to early summer, well more than the cost of carry.

We suggest elevators sell into the nearby or Dec/Jan values where the gross basis gains on soybeans approach or exceed 40¢/bushel from October. That would free up working capital and space for other opportunities. The basis gains won't be all profit for all elevators. Farmers were heavy forward sellers for harvest earlier this year, when harvest basis values were somewhat higher than when October rolled around. But those were past decisions. What matters now is whether it's prudent to stay long the basis going forward, or is it better to begin to sell into nearby or into forward basis opportunities – whatever nets out best. The 'right' strategy will vary by market; we just urge caution about assuming that even better (net) opportunities will surely lie ahead. They may, especially as long as soybean futures spreads remain wide. And with a 2019 carryout nearing 1 billion bushels of soybeans, futures carries may widen through the summer to compensate whoever owns those bushels. Some elevators have carried hedged soft red wheat for several years, for example, and profitably. But soybeans tie up a lot of money and those farm-owned bushels are out there waiting to move at some point. We recommend elevators not hold hedged soybeans into next summer *unless you are willing and able to hold them past the 2019 harvest.*

WHAT LIES AHEAD…..

Not all records are created equal. The US soybean crop is a new record 4.6B bushels. The combination of the Sept 1 corn plus soybean stocks plus '18 production is a record high 21.8B bushels, about 200M above a year ago. But look at data for ten states that represent around 80% of total US production and 85% or more of Sept 1

beginning stocks. This table shows how their 2018 beginning stocks plus production for corn plus soybeans compare to a year ago, by state:

Million bushels:

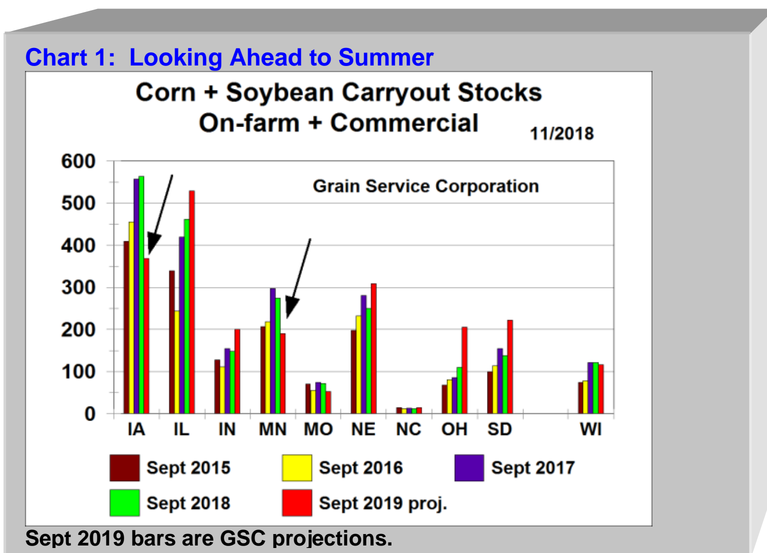
State	Change
IA	(66)
IL	195
IN	98
MN	(132)
MO	(96)
ND	(60)
NE	109
OH	142
SD	102
WI	29
10 States	**381**

Surprisingly, the three-state region of Iowa, Minnesota and Missouri had an aggregate 294M *fewer* bushels to manage this fall than a year ago. Nebraska and South Dakota, on the other hand, had to manage 211M *more* bushels, and OH/IN has to manage 240M *more* bushels. North Dakota also had a lower total volume of corn plus soybeans this fall, but had 100M more bushels of wheat on hand on September 1. Wheat stocks this fall of the other nine states listed above were either about the same as last year or within 20M bushels.

Terminals, processors and elevators in the states with lower aggregate volumes this fall may have started chasing bushels as harvest progressed, as truck lines diminished and selling slowed, raising bids in some areas against the published or anticipated carries.

But there's more to the story. These inventory differences will flow through to the end of the crop year and ending stocks may vary far more than many would expect. The US may have nearly 1B bushels of soybeans left next summer, but corn stocks are forecast to be down by 404M bushels. We have projected what those carryovers *will be for key states* and the results are interesting.

- Iowa, Minnesota, and Missouri could have the lowest Sept 1 stocks in five years (corn + soybeans) on 9/1/19
  - Iowa corn stocks could be as much as 220M bushels lower than this summer
  - Minnesota stocks could be down by 110M bushels
- Wisconsin may have a 3-year low inventory of corn plus soybeans
- Illinois, Nebraska, S. Dakota, Indiana and Ohio may each have a 10 or more year *high* inventory next summer.
  - Nebraska corn stocks might be slightly higher despite nearly 400M fewer bushels nationwide
  - Indiana corn stocks could be about unchanged from this summer, with Ohio up 50+M.

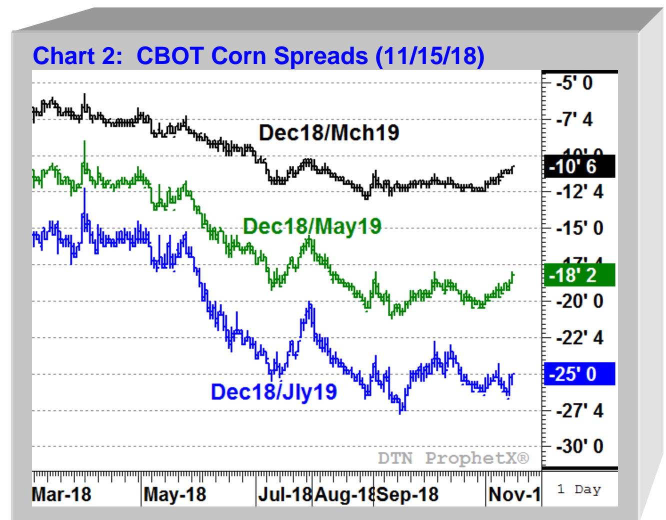


It's early, and areas where inventories are lower may attract bushels from other states and level the differences out somewhat. But it's not too early to identify the areas to watch. Near record ethanol production will keep corn disappearance high in Iowa, for example, and may support Iowa basis more than might be necessary in other areas such as Illinois or the Eastern Corn Belt.

CORN SPREADS

Cash barge basis values in December are currently 7-14¢ cheaper than delivery against December futures. That discount is small enough that corn spreads have narrowed slightly in light of declining farm selling and the end of harvest in sight.

But there are still around 500,000 contracts of open December corn futures contracts, with the start of delivery notices just nine days away. The exodus of smaller hedgers and large and small speculative positions will continue out of Dec corn, and that may weigh on Dec/March as the end of November nears.



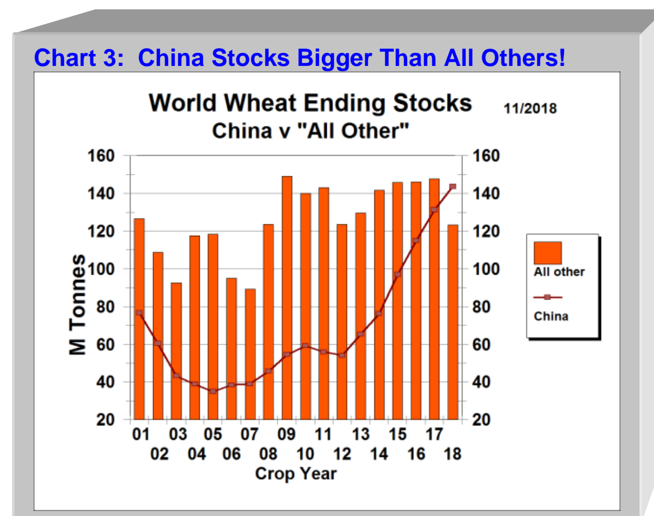
We recommend conservative managers with large volumes of short Dec corn futures to roll begin to move a percentage to March each day over the next 7-8 days and accept the average spread, perhaps with a backstop of rolling all shorts if the carry reaches 12¢ again.

We suggest more aggressive managers at least have 'good til canceled' orders working to buy Dec/sell March corn in the 12-13¢ range on most of your short hedges, and perhaps hold some percentage back until just before First Notice Day (11/30) and hope the spread weakens. Your risk is that the spread does not widen.

WHEAT COULD BE A SLEEPER?

Wheat had been the whipping boy of the markets for so long it's hard to believe that has begun to change. KC wheat futures spent most of 2016 and 2017 rarely trading much above an 80-90¢ premium over corn. CBOT wheat was similar, even dipping as low as 50¢ over corn futures in 2016. But wheat has slowly gained ground versus corn (some would say corn has lost ground to wheat, but that's splitting hairs) since April of 2018. World wheat production dropped 30M metric tonnes in 2018 (1.1B bushels) to 734MMT, with usage a new record high 746M tonnes. The world wheat carryout is forecast to decline by 12MMT by the summer of 2019, but that's deceptive because China's stocks are record high. World ending wheat stocks, *excluding China,* are forecast to fall to an 11-year low 123MMT, just 72 days of usage. (China wheat stocks, on the other hand, represent an incredible 426 days of China's domestic usage rate.) World wheat ending stocks excluding *both the US and China* will also be an 11-year low. (Chart 3)

Speakers at the Global Grain Conference in Geneva this week commented they expect world demand for milling wheat to need to tap into US inventories this winter, which will mean enticing US wheat out of VSR storage, whether it's HRW or SRW that buyers want. US cash values have held down US wheat export business, but analysts and traders see that changing in the months ahead for milling wheat as other countries' stocks decline before harvest. The challenge here is that US wheat inventories are largely held either by farmers who want higher prices, or are in commercial storage where quality may be an issue or where wide futures carries have turned elevators into stubborn holders.



CBOT wheat spreads have narrowed this month since a vessel of US wheat was sold to Egypt, and some US SRW basis values have firmed. Virtually all of the outstanding Delivery Shipping Certificates against CBOT wheat have been canceled and the truck basis for wheat into Chicago has firmed 15¢ this month to +10Dec. Barge values have been quiet, however, with minimal apparent interest by buyers at this point.

The CBOT Dec/March wheat spread has narrowed from 16¢ carry to around 8¢ this month, with March/May narrowing from 12¢ recently to around 8. Interestingly, May/July weakened slightly this week to a new high carry at 9½¢. We can argue whether the

CBOT narrowing is premature and overdone, but overall the tone of the spreads is changing from encouraging long-term storage to offering returns more in line with corn and soybeans. Elevators with short CBT wheat hedges in either Dec18 or March19 need to pay attention. Folks who are willing and able to move their wheat need to stay in touch with buyers and watch for higher basis opportunities, and managers who cannot ship SRW for logistics or quality reasons need to be more conservative about setting futures carries than in the last year or two. (See "Wheat VSR" story)

- March/May (CBT wheat) at 11¢, for example, would represent 78% of Financial Full Carry using an inferred futures delivery storage rate of $.00165/day.

- May/July (CBT wheat) at just 10¢, for example, would represent 71% of FFC, under the inferred minimum futures delivery storage rate of $.00165/bu./day, approximately 5¢/month.

HRW basis has firmed sharply at the Gulf and interior markets but open export sales are only 52M bushels, and YTD sales are just 41% of USDA's projection, with HRS at 58% of projections and SRW at 54%. It's unclear whether world interest may turn to HRW or SRW here in the US in the months ahead.

Unless CBOT wheat spreads widen again, the market is beginning to signal that holding hedged SRW may not pay significantly more than holding corn or soybeans for some elevators. Whether wheat *futures* are able to rally much is another story.

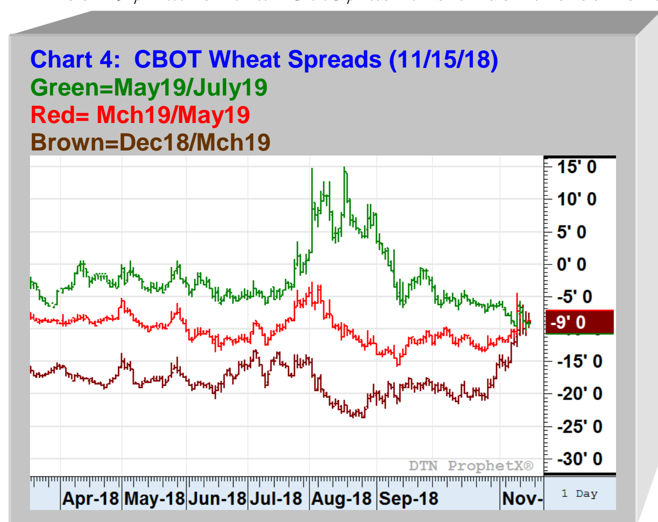
WHEAT VARIABLE STORAGE RATE ("VSR")

The 47-day CBOT Observation Period (O.P.) is in progress to determine the daily storage rate for CBOT and KC wheat delivery shipping certificates effective December 19, 2018 through at least March 18, 2019. This cycle's O.P. runs from September 19 through November 23 and measures each day's close of the Dec/March wheat spread as a percentage of Financial Full Carry. After 41 of 47 days, the CBOT Dec/March wheat spread has averaged 46.37% of Financial Full Carry, based on the current $.00365/bu/day delivery storage charge and interest at 2% over 3-month LIBOR.

- The daily CBT storage rate will decline to $.00265/bu./day effective December 19 if the 47 day O.P. cycle average is 50% of less of FFC. The new storage rate would be approximately 8¢/bushel/month.
- To avoid having the rate decline, Dec/March now has to average 75% of FFC over the remaining 6 days.
- CBT Dec/March closed on the 14th at just 23.8% of FFC, which makes it highly unlikely this spread will average 75% from November 15 through Nov 23, the last day of the O.P.

The impact of the probable storage rate decline is that Financial Full Carry for CBOT Dec/March will officially be 29¢ rather than 37.8¢ as it is under the current storage rate. The next spread to watch then is March/May, and based on where the spread is currently trading, a second storage rate decrease to the minimum $.00165/bu./day is anticipated, which would take effect March 19 through May 18.

- FFC for CBOT March/May in that case would drop from its current 26.3¢ to only 14.1¢, based on 5¢/month storage.



KC wheat spreads have narrowed slightly, but certainly not like at the CBOT. KC Dec/March is still trading at 23+, nearly 62% of Financial Full Carry. The 41 day average for KC Dec/March is 63.4% of Financial Full Carry. It appears that the delivery storage rate for KC wheat will remain at the current $.00365/bu./day.

Reminder: The National Grain & Feed Association annual Country Elevator Conference runs Sunday Dec 2 thru noon Tues Dec 4 at the Union Station Hilton Hotel in St. Louis, MO. Visit www.ngfa.org for details on the agenda and registration and links to the Hilton Hotel website.

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"Perseverance is a great element of success. If you only knock long enough and loud enough at the gate, you are sure to wake up somebody." - Henry Wadsworth Longfellow

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