GRAIN OUTLOOK

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WHERE IS THE DEMAND?

The stock market fell to a depressingly low level last week and took commodity prices down with it. It is difficult to remain optimistic about the prospects for grain and oilseeds after such a disappointing week. The fundamental supply and demand factors look supportive, but didn't mean a thing in the face of dismal economic news in the U.S. and around the world. The Federal Reserve issued a gloomy outlook for the U.S. economy, saying there would be more pain ahead and recovery would be slow. Although this recession won't be as bad as the one experienced in 1982, before it has run its course, unemployment is expected to rise by at least another percentage point. The U.S. economy will be in negative territory for the first two quarters of 2009 before dragging out of the hole in the last half of the year. Economic growth should be positive in 2010, but full recovery won't come until 2011.

The story for the rest of the world is similar except the drop off in economic activity is coming with a lag, it is more severe for most other countries, and recovery will take longer than for the U.S. Japan's economy is down 13 percent. In Western Europe, economies are down 5 to 6 percent. In Eastern Europe and Russia, the economic downturn may be deeper than that given the developing financial crisis in that part of the world.

The one bright spot is China. The red-hot Chinese economy will cool this year, but is expected to only drop from double digit growth to 5 or 6 percent. Early in the global recession, the Chinese government moved quickly and massively to stimulate its economy. Partly because of that, consumer expenditures in China may hold up better than in the U.S. The other reason is the Chinese people saved a significant portion of their income during the last few years. They can help the world now by increasing spending on consumer goods including food.

In most years, farmers and other market participants face price uncertainty because of potential supply fluctuations; and those are present this year including droughts in major growing areas of the world, wet spring field conditions in the Corn Belt, changes in planted acres from last year, and input costs and availability. However, this year, the greatest uncertainty is on the demand side. That is the major reason commodity markets are not responding to what otherwise would be considered bullish fundamental supply factors. In the past couple of years, rising incomes drove demand up for livestock protein and directly consumed grain products, consequently taking commodity prices to unprecedented highs. Now, the economic squeeze is forcing consumers around the world to change food consumption patterns including cutting back on purchases of livestock protein products.

To be sure, other demand-side factors are affecting the markets as well, including shaky banks and tight credit which is making it difficult for overseas buyers to transact business; poor ethanol profit margins and closed plants reducing corn grind; and lack of non-commercial (speculative) buying in commodity markets.

What will cause the situation to change for the better is easily stated, but hard to achieve – stabilization of the global financial situation, resumption of speculative investment in commodities, a return to economic growth that will give consumers more money to spend, and a return to the food consumption patterns developed in the years before the economic difficulties. ***When*** that will occur is very difficult to determine, in that more than ever, the past is no guide for the future. This recession will be long with a slow, faltering recovery. The best guess is recovery will take place in the last half of 2009 or early 2010 in China and the United States; sometime in 2010 or 2011 for the rest of the world. But unanticipated economic shocks ahead could cause that timetable to slip by six months to a year...or more.