

GRAIN OUTLOOK

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MARKETS WORRIED ABOUT DEMAND

An all time record large global wheat harvest continues to put downward price pressure on U.S. wheat price and abundant feed wheat is undercutting U.S. corn exports. The grain trade already knew those things. However, the USDA's November World Agricultural Supply and Demand Estimates report would have been bullish for soybeans if everyone wasn't so worried about global demand for grain and oilseeds.

The USDA lowered the U.S. expected average soybean yield to 39.3 bushels per acre giving a crop size of 2.92 billion bushels, down 17 million bushels from the October report. Ending stocks were left unchanged at a tight 205 million bushels. Some industry analysts are predicting a further reduction in national average soybean yield in the USDA's final production report due out in early January. Adding to the bullish tone was a 2.5 million metric ton (about 92 million bushels) drop in Brazil's expected soybean production. High production costs and lack of farmer credit is causing Brazilian soybean production to shrink a little from last year rather than to increase as was predicted earlier. In the November report, the USDA dropped world demand for soybeans by one percent, but total demand will still be two percent greater than last year.

Soybean price did improve after release of the report, but the trade remained in a nervous state because of uncertainty about the global economy. The fear is the world will slide into a deep and prolonged recession that will severely reduce demand for animal protein products and grain-based products for human consumption. It is being called 'demand

destruction' and no one can predict how bad it might become. The recent announcement by the Chinese government of a \$600 billion stimulus package for that country gave global markets; especially Asian markets, reason to hope the recession will not be as bad as some fear.

Ocean freight rates, a good barometer of world economic activity have fallen to record low levels in the past few months. But the drop may be due to lack of credit as much as demand destruction. The credit crisis is severely impacting ocean freight traffic. Trade credit has dried up and banks are restricting lines of credit. Exporters are hesitant to accept letters of credit guaranteeing payment issued by overseas banks. Consequently, commodities have been piling up at ports awaiting shipment. One bright spot in international trade has been soybean exports to China. Chinese soybean crushers have been buying U.S. beans because of an agricultural policy that makes domestic Chinese soybeans more expensive U.S. imports. There is talk in the trade that the Chinese government will soon level the playing field for Chinese soybean growers by taxing soybean imports. If that occurs, U.S. soybean exports to China will drop.

U.S. corn exports have been disappointing recently because Black Sea wheat from Ukraine and Russia has been undercutting U.S. corn by about 50 cents per bushel. The feeding of wheat to livestock around the world is projected to increase about one billion bushels from last year when global wheat stocks were at a 30 year low. Adding to the bad news for corn, the USDA decreased corn use for domestic livestock feed in its latest report by 674 million bushels from last year. Even so, the ending stocks to use ratio for corn remained at about nine percent; still low when compared to usage level. The slow pace of the U.S. corn harvest; only 71% harvested in the last report, may result in weather induced yield reduction. The final corn yield number will be reported in the January USDA report and if it drops will be bullish for corn price. Grain analysts say a higher corn price will be needed to get enough acres of corn planted in the spring to meet next year's demand for corn.

Another unknown is the U.S. demand for corn to make ethanol. The USDA did not change the estimated amount of corn used for ethanol in the November report although U.S. vehicle drivers have not responded to lower pump prices by increasing purchases of ethanol blended gasoline. Ethanol price is now above the price of blending gasoline which means the Renewable Fuel Standard mandate and blender's tax credit are driving demand. Ethanol stocks are increasing and ethanol plants are cutting back on capacity utilization. It is likely the USDA will lower estimated corn usage for ethanol production in its next report.

Wheat producers around the world responded to unprecedented high wheat prices by increasing area planted this year and the weather cooperated. Global wheat production for 2008/09 is now estimated to be 682.4 million metric tons, the largest wheat harvest in the history of the world. It appears the huge supply is slowly being absorbed by the marketplace for livestock feeding, to fill a depleted pipeline, and to replenish safety stocks in some countries. Even with all the wheat, there is a relative shortage of high quality milling wheat. The USDA increased its estimate of U.S. grown hard red winter wheat exports this month and lowered ending stocks again to reflect the strong global demand for milling wheat. Countries in the Middle East are active buyers of U.S. wheat because a severe drought devastated the wheat crop in that region of the world.

Attention now turns to the Southern Hemisphere wheat crop and area planted to winter wheat in the Northern Hemisphere. Because of dry conditions during the reproductive period in Argentina and Australia, the USDA lowered estimated production in both of those countries; down about 37 million bushels in Argentina and 55 million bushels in Australia. Although the USDA did not report acreage, plantings of hard red winter and soft red winter wheat in the U.S. will be lower this year because of the late corn and soybean harvests and wet field conditions. If global demand for milling wheat holds up in a recessionary market and when stocks of feed wheat are used up, wheat price should rally.