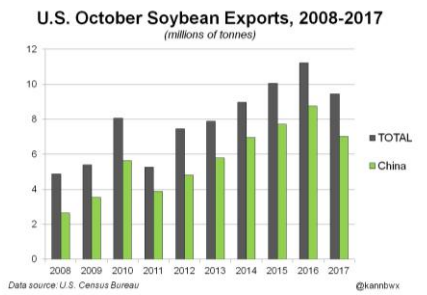
Diversified Crop Insurance Services

Revenue Management Update

Tuesday, December 12, 2017

What We Thought…

There weren't really any surprises in the USDA December Supply/Demand Report. The December report only gave us changes in cotton yields/production – other crops will get final production estimates in January. But USDA did make a few changes in some demand & ending stocks estimates. Some changes by crop were:



Soybeans – USDA confirmed the idea that US exports this year wouldn't meet expectations, cutting their estimate for this year 25 million bushels to 2.225 billion, and raised ending stocks 20 million bushels to 445 million. The chart above from Reuters shows though that year-to-date sales are currently running well below last year, yet USDA is still forecasting exports up 50 million. What this means to me is that we could see USDA make further cuts to soybean exports in future months. The "market" started trading this idea prior to the report's release, & as of this writing nearby soybeans had posted lower closes in 6 of the last 7 sessions. Add this to the fact that world stocks grew, and South American prospects look pretty good at the present time, and it doesn't seem too friendly to soybean futures.

Corn – USDA made a 50 million bushel bump in ethanol grind, and dropped ending stocks a like amount – but still at a whopping 2.437 billion bushels, the largest in 30 years. Corn export sales are also lagging the pace needed to reach USDA's target, which could mean a decrease in exports at some point.

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December 2017 WASDE Report

US 2017/18 Ending Stocks:		USDA December	Analysts' Average	Estimate Range	USDA November
Corn	↑	2,437	2,478	2,394-2,517	2,487
Soybeans	↓	445	438	425-486	425
Wheat	↓	960	938	925-960	935
Cotton	↑	5.80			6.10
World 2017/18 Ending Stocks:		**USDA December**	**Analysts' Average**	**Estimate Range**	**USDA November**
Corn	↔	204.1	202.7	195.7-205.0	203.9
Soybeans	↔	98.3	97.8	95.2-99.0	97.9
Wheat	↓	268.4	267.1	264.0-270.0	267.5
Cotton	↑	88.0			90.9

Bullish ↑ *Bearish* ↓ *Neutral* ↔

Wheat – It'd be hard to get more bearish the wheat market, but USDA tried. Going with the same theme, USDA cut wheat exports 25 million bushels, and raised carryout a like amount. USDA also raised world wheat stocks to what would be a new record 268.42 million metric tonnes.

Cotton – The crop that's been the lone bright spot has been cotton. Cotton exports continue to run ahead of USDA's projected pace, prompting them to bump their estimate 300,000 bales, and reduce carryout a like amount to 5.80 million bales. That's still more than double last year, but the trend suggests we could see further cuts ahead. USDA did a bunch of shuffling on state yields (AL, FL, GA, LA, MS, SC lower, TX & VA higher), but the bottom line was barely any change. World cotton stocks tightened 2.88 million bales, a very significant cut! Much of that cut came from India, which should help future US exports.

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USDA Final & Projected MYA Farm Prices

($ per bushel, cents per pound, $ per cwt)

	PLC Ref Price	Final 2014-15	Final 2015-16	Final 2016-17	2017-18	
Corn	$3.70	$3.70	$3.61	$3.36	$3.20	unch
Soybeans	$8.40	$10.10	$8.95	$9.47	$9.30	unch
Wheat	$5.50	$5.99	$4.89	$3.89	$4.60	unch
Cotton	N/A	60.5	58.0	68.0	66.0	up 3 cents
Sorghum	$3.95	$4.03	$3.31	$2.79	$3.10	unch
Barley	$4.95	$5.50	$5.52	$4.96	$4.50	down 10 cents
LG Rice	$14.00	$11.90	$11.10	$9.62	$12.10	down 0.20 cents
Peanuts	$0.2675	$0.2200	$0.1930	$0.1970	$0.2050	up 1 cent

Most program crops stayed unchanged on Market Year Average prices this month, with small changes in barley, rice, & peanuts. But cotton made a big jump!

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Revenue Management Update

Paradigm Shift in Corn Futures

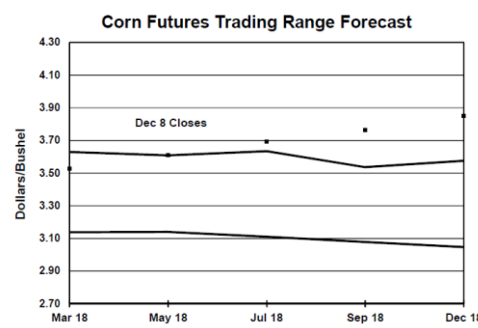
I wrote about this back in September as the trend was changing and as harvest was kicking into gear, but we've seen a dramatic change in how we view the corn market. The shift I'm talking about is the carry opportunity that's available now in the corn futures market. Consider the current market structure in corn futures:

Contract	Net Change	Last
Corn		
ZCZ17	-0^4	336^2 S
ZCH18	-0^4	348^4 S
ZCK18	-0^4	356^6 S
ZCN18	-0^4	365^0 S
ZCU18	-0^4	372^0 S
ZCZ18	-0^4	380^6 S
ZCH19	-0^6	390^4 S
ZCK19	-0^6	397^0 S
ZCN19	-0^4	402^4 S
ZCU19	0^0	402^0 S
ZCZ19	-0^2	404^6 S

From December '17 to December '18, that "carry" is now at 44 ½ cents, or nearly 4 cents per month. That is the incentive that the futures market is "paying" to keep corn for 12 months. To get perspective, the same carry back in the spring/summer was only 10-15 cents (right/bottom chart). But once we got an idea of the size of this crop, and the size of last year's carryover, this spread shot out. So basically, what the market structure today is telling us right now is that it doesn't want your corn until 2018, or even 2019!

This is a HUGE deal for all corn producers, but especially those storing corn on farm. Last year on December 1st the "On Farm" corn stocks were 7.6 billion bushels. This year it's probably higher. Producers holding that corn have the opportunity to "earn" the carry in corn futures (plus basis gain), but the only way to truly earn the futures carry is to

hedge the deferred futures contract. Why? Because in a typical large carry market like this, is you just hold bushels waiting for the 40 cents when we get to next year, it's typically gone. This chart from **Informa Commodities** shows their projected trading range for the year ahead, with the dots showing last Friday's closes.



In a typical carry market, when the nearby futures contract expires, the next month tends to drift down to that same level over time. September futures expired at $3.42, and today December futures expired at $3.36 ¼. Barring any unforeseen event that would drastically affect world corn supply, you would guess that subsequent futures contracts will migrate down to this same area. So the opportunity to "earn" this carry only comes by forward selling futures. I would be in favor of hedging September '18 or December '18 on a 10-15 cent rally against inventories, then look to set basis in the months ahead. This is a very good opportunity that you can't afford to miss out on this year and possibly next year too.