

## **GRAIN OUTLOOK**

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### **FUNDAMENTAL DIFFERENCES**

The prices of the three major crops: wheat, corn and soybeans are marching to the tunes of different drummers...but they are marching the same direction. Since early September, the price of corn has increased about 40%; wheat is up about 25%; and the price of soybeans, the biggest surprise of all, is up about 17%. The price for each crop influences the others, perhaps more this year than in past years because of the competition for increased acreage, but the fundamental supply and demand factors are strikingly different.

Demand for corn as the raw material for ethanol production is driving that market. On average, one new ethanol plant is coming on line per week now; each new plant boosting the demand for corn by approximately 37 million bushels per year. That rate of new ethanol plant startups will continue well into the New Year. About 20 percent of this year's corn crop will be used to make ethanol.

Rain and wet fields are making corn harvest difficult in the Ohio Valley and perhaps will reduce final yields in some of those states. The USDA lowered estimated national corn yield in its October report and may lower it again in its November report. At least, that is the buzz in the trade.

The USDA estimates that the U.S. will use about one billion bushels more corn this year than will be harvested, putting the crop year-end supply at a precariously low level. Overseas buyers are responding by purchasing corn now rather than later in the marketing year. Strong export demand has contributed to the run up in corn price.

Competition for acres is one reason the price for soybeans has moved higher than anyone expected during this fall harvest period. From planting time until early September soybean price was trending downward based on a large crop in the field and a huge expected carryover that is now estimated to be 555 million bushels.

Attention has now turned south to Brazil. Soybean farmers there are going into planting time in crisis. Higher production costs due to higher prices on fertilizer and diesel fuel and multiple spray applications for Asian Rust combined with lower soybean prices caused by a sharp rise in the value of the Brazilian currency compounded by very high interest rates on borrowed operating loans squeezed the profit out of soybean production. Brazilian soybean plantings were expected to drop by 10 to 15 percent. But that was before soybean price started to increase. With March 07 and May 07 soybean futures contract prices in the \$6.50 range, Brazilian soybean producers may be able to lock in prices that will allow them to make a profit on the crop now being planted. That means the reduction in plantings may not be as large as expected.

Shortage sums up the wheat situation. World wheat stocks are at all time lows because of weather related reductions in production. All major wheat exporters, except Argentina and Canada, have harvested or will harvest smaller wheat crops this year. Total wheat production in the U. S. fell by 14 percent this year. But the big story is Australia. A drought of Dust Bowl proportions, caused by an El Nino, is devastating the wheat crop. Latest estimates put the Australian wheat crop at 9 to 11 million metric tons (MMT), down drastically from the expected 24.5 MMT. Some in the trade are saying the crop may even be below the low end of that range. There is doubt that Australia will export any wheat this year and some are saying they may even import some feed wheat.

The trade is trying to get a feel for the number of wheat acres planted to winter wheat in the U.S. Wet fields are hampering planting in the Eastern Corn Belt, but in the Great Plains a substantial increase in winter wheat planting appears to be underway. In Kansas, for example, immediately after soybean harvest many fields were planted to wheat.

Although no hard numbers are available yet, estimates put wheat acreage expansion at about 4.5 million acres.

We will need the production from about 7 million additional acres of corn and perfect growing conditions next year just to meet our needs. In order to assure that many more acres, corn price will need to remain high relative to soybeans and other alternative crops. That raises the issue of land allocation among the crops and from where will we get the additional acres of corn. Corn and wheat prices have historically been about one-half of the soybean price. Until the last week or so, market price relationships favored corn and wheat. Now corn and soybean prices are near the historic relationship, with corn having a slight advantage; but wheat is favored over both. That means a toe-to-toe battle between corn and soybeans for acreage. However, if wheat price drops before corn planting time, some of those acres will be replanted to corn.

Speculators have taken notice of the world wheat situation and are attracted to corn by the hot demand from ethanol producers. Some speculative funds were badly burned by falling petroleum prices and have moved money out of the energy complex into agricultural commodities. While speculative funds are pushing corn, wheat, and soybean prices higher now based on fundamental factors, once they have hit their profit goals or when changes in fundamentals reduce or eliminate the chance of upside gains, they may quickly exit the markets or take short positions. This creates a potentially costly situation for commodity producers who have not yet taken advantage of current strong prices to sell this year's wheat, corn, or soybeans. Prices could drop sharply, taking farm level revenues and profits down with them. Wheat, corn, and soybean producers should be selling 06 crops and even 07 and 08 crops in increments on price peaks. Selling in increments reduces production risk; the risk that a farmer will not produce all that he has contracted to deliver. It also reserves the opportunity to sell other increments later on if prices continue to increase into winter and spring.