December 2017 Monthly Commentary

2017 was a choppy, low volume year, which is not the best environment for me. The markets are starting off 2018 with enthusiasm at a minimum and market structure tilted heavily short in corn, wheat, and soybeans. It has been the correct positioning, but I wonder how much longer the party will last. US origins are the cheapest in the world in each class. With genetics having lessened the impact of less than ideal weather, it may take extreme conditions to have a major yield issue. The markets don't hold risk premium like they used to, and the market is complacent after the huge US and South American crops of the last few cycles.

There are a few signs the winds are shifting in the start of 2018, and there do appear to be a number of items that could have significant impact on the markets and as a result bring us a number of great trading opportunities. There has been more talk of inflationary trades with the energy sector leading. The dollar has been under pressure which could be the start of a larger trend. Commodities versus equities are at their lowest levels in years. There are also some out there touting extreme weather patterns in the next few years driven by a sun spot minimum. The risk is that the transition from La Nina to El Nino this spring/summer could result in a hot and dry spring and first half summer. The last few years, US soil moisture profiles were very healthy going into the growing season. This year we will likely be starting out in drought conditions in many areas with the Northern Plains still in a major drought, the Southern Plains/Delta in a drought and parts of the Corn Belt abnormally dry.

Wheat has had a nice bounce since mid-December. It should remain supported into the January 12 report with winter wheat seedings being potentially lower than expected. In addition, the HRW crop was not off to the best start with poor establishment reported in many areas. Kansas and the Oklahoma panhandle were subjected to single and double digit below zero temperatures with little/no snow cover over the New Year holiday. This cold spell alone could take 60-70 milbus off the HRW crop. The US and particularly the HRW and HRS balances should tighten further in 18/19. Thus the quality shortages will likely continue into 18/19. There is very little for sale and spreads/flat may need to rally further to encourage movement.

Corn has been in a narrow range since mid-November. Domestic demand has been strong in both the feed and ethanol sectors, although negative production margins are a bit worrisome for ethanol going forward. Export interest has been strong and should continue that way going forward. US corn is the cheapest grain in the world and the South American corn export programs are winding down. There is risk that Brazil's safrina crop is considerably smaller than year ago, while dry weather is threatening parts of Argentina's corn crop. Ukraine's maize crop was likely overstated - Ukrainian corn is the highest priced and their exports are slowing faster than expected. With unchanged to slightly higher area in the US next spring, stocks can contract with a slightly lower yield. The market is likely geared towards the third record yield in a row and won't be prepared for anything less. I can't get excited about sustained downside here, but rallies will also be difficult to sustain with producer sales above the market.

Weakness in the Argentine Peso and the Brazilian Real weighed heavily on beans and meal in December. Non-threatening weather (for the most part) in South America also weighed. Argentina has had a dry bias the last few months. Timely rain has fallen but there is a dry/hot stretch coming up which needs to be monitored. The other main issue in Argentina is area. There is a big difference between the Ag Min and the private estimates, with the Ag Min down 1.0 mil hectares vs last year. Brazil's weather has been nearly ideal with crop ideas getting closer to last year's whopper. World demand has been very strong but the US is losing market share. I had thought we would make some of this up in the second quarter but it hasn't happened. If Brazil has another record crop, it likely won't happen in the LH crop year either. Domestic product demand has been quite strong and a higher crop year crush should at least partially offset lower exports. I maintain that the market needs to encourage additional bean acres next spring in the US and even with a slight increase in area, the 18/19 balance sheet could tighten. Given an over 80k fund short, less than ideal Argentina weather, China uncovered, and the US the most competitively priced, it is hard to be short at these prices. As I have mentioned, there are a number of potential opportunities above I am excited about for the upcoming year. Low prices in corn and beans make things ripe for a price spike if we see issues. No reason to push the markets, but I will be ready when the opportunities arise.

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