The *Grain Service* Newsletter

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July 15, 2015 No. 15-14

JULY USDA REPORTS

USDA offered up some surprises, cutting ending stocks of soybeans to 255M bushels on continued strong crush and exports. But USDA left soybean acreage unchanged from June 30 despite the almost certainty that 1-3M acres are now 'lost.' Missouri, for example, still had 1+M acres of intended soybean acres left to plant on July 12, and some acres were lost in Illinois and Indiana.

Projected usage was also raised for both corn and soybeans, which makes ending stocks in 2016 the main focus in corn, and '16 soybean stocks are expected to start declining in the August report. USDA raised wheat exports, which seems questionable, but even so, wheat stocks are big enough to dim the bullish enthusiasm. Another area worth noting are USDA's global wheat stocks, where 12+M tonnes were added to China's inventories on retroactive 'adjustments.' Many analysts disregard this change, however, as the quantities and quality are questionable and the stocks are isolated from the world marketplace.

WHAT ABOUT THE FUNDS?

Managed funds had accumulated a near record short in corn by the end of May of about 700M bushels (futures plus options). That marked the recent peak of the fund shorts and their reversal helped set the low in corn around June 1, in the low $3.50's. Managed funds then turned net buyers of about 310,000 contracts of corn – *over 1.5 billion bushels* – in five weeks by July 7, which also coincides with the 90¢ rally in corn. The fund buying ran headlong into heavy farm selling, with the commercial sector increasing their net *short* in corn by 273,000 contracts (1.365B bu.) in those same five weeks, which likely tempered the rally.

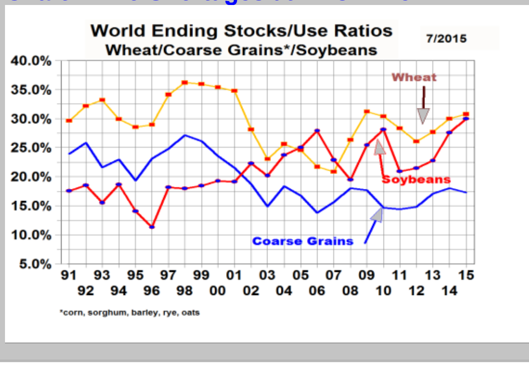
Managed funds were just as active in soybeans, buying 177,000 contracts (net), or 885 million bushels, over the same five weeks, handing farmers a $1.50 gift with Nov futures climbing to $10.40+.

Whether markets continue to climb from here remains to be seen. Funds are now long, but the US crop size is far from certain. Some areas could easily see record yields, others will lose acreage and yields will suffer. Neither corn nor soybeans act as if this rally is over – there has been no high volume blow-off day, for example, and sell-offs have been modest. But the old saying is that "short crops have long tails." Weather market rallies are typically dramatic, but often peak early.

Table 1: USDA Supply & Demand Reports 07/10/15

	2014 crop		2015		2014 crop		2015		2014 crop		2015	
	Corn		Corn		Soybeans		Soybeans		Wheat		Wheat	
WORLD	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15
Carry-in	174.50	174.73	197.01	193.95	62.77	62.73	83.70	81.68	189.98	193.52	200.41	212.06
Production	999.45	1001.74	989.30	987.11	318.25	318.60	317.58	318.92	726.32	725.92	721.55	721.96
Usage	976.93	982.51	991.12	991.10	293.97	296.07	305.64	306.23	715.89	707.38	719.56	714.20
Ending Stox	197.01	193.95	195.19	189.95	83.70	81.68	93.22	91.80	200.41	212.06	202.40	219.81
U.S.	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15	6/10/15	7/10/15
Carry-in	1232	1232	1876	1779	92	92	330	255	590	590	712	753
Produc.	14216	14216	13630	13530	3969	3969	3850	3885	2026	2026	2121	2148
+Imports	25	27	25	25	30	30	30	30	148	144	140	130
=Supply	15472	15474	15531	15334	4091	4091	4210	4170	2764	2760	2973	3031
Crush	NA	NA	NA	NA	1815	1830	1830	1840	NA	NA	NA	NA
Feed/Res	5250	5300	5300	5275	38	82	38	38	160	111	195	200
Food/Seed/Ind	6522	6546	6560	6585	98	99	92	92	1037	1041	1039	1039
Ethanol	5175	5200	5200	5225	NA	NA	NA	NA	NA	NA	NA	NA
Exports	1825	1850	1900	1875	1810	1825	1775	1775	855	855	925	950
USAGE	13597	13696	13760	13735	3761	3836	3734	3744	2052	2007	2159	2189
=End Stox	1876	1779	1771	1599	330	255	475	425	712	753	814	842
(stox/use)	13.8%	13.0%	12.9%	11.6%	8.8%	6.8%	12.7%	11.4%	34.7%	37.5%	37.7%	38.5%

Chart 1: No Shortages at This Time…..



Remember that corn harvest is just around the corner in the Deep South, and those areas generally look good. That could be a negative for the market as harvest reports roll in. And world S&Ds remain comfortable on corn, soybeans and wheat (Chart 1) for now, which can make it more difficult to sustain rallies. The world carryout on soybeans is forecast to set a record-high percent of usage this year, and world supplies of wheat are at a six-year high – for now – although questions remain about Canada and Australia. El Nino remains a wild card for world production; "comfortable" carry-outs today could change quickly down the road.

Traders are now debating the relative size of the US crops, and whether record heat that is scorching Europe will hurt those crops. Another market factor is what it means when the US can economically import corn from S. America, and France can sell wheat into our next door neighbor Mexico.

It's early to get a handle on US yields and '15 usage, but even small changes in soybeans can make a big difference for the market. USDA says the '16 carryout will be 425M bushels on soybeans, for example. Take away 2M soybean acres and cut the yield 2 bpa but leave usage alone and suddenly that 425M carryout drops to 175M bushels and this rally could just be getting started.

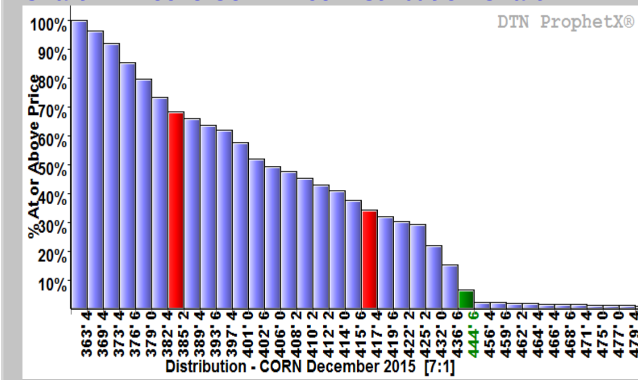
We analyzed soybean acreage and potential yields by state, and cut soybean acres 1.7M overall and slashed yields in some ECB states. We considered the crop ratings, but generally assumed high-side yields for most other states. We reduced corn acres by 400K, but did not cut corn yields proportionally as much as on soybeans. We consider these production 'estimates' to be the probable *high-end*:

Corn	13.45B bu. (USDA at 13.53B)
Sbns	3.77B bu. (USDA at 3.89B)

~~TOUGH~~ EASY MARKETING DECISIONS

Producers and end users alike need to decide: Accept current prices or wait and hope for better opportunities. We continue to recommend using option-based strategies for now to make it easier.

Chart 2: Dec15 Corn Price Distribution Chart



Dec15 has been at/above $4.45 less than 10% of the time in 2 yrs.

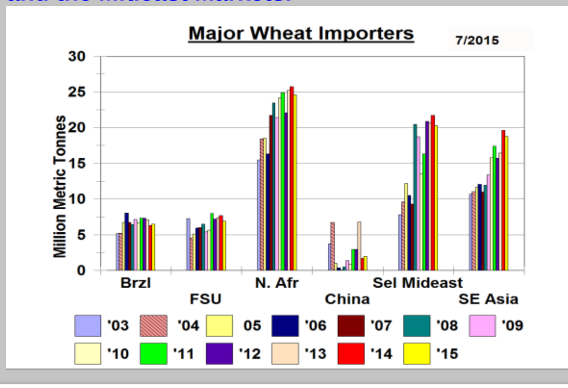
Chart 2 is a price distribution chart that shows Dec15 corn has been at or over $4.45 less than 10% of the time in the last two years. Sure makes this rally look attractive! For example, on July 14th, Dec corn futures closed at $4.39. A farmer could sell Dec15 futures and buy a Dec 440 corn call for 27½¢ to create a futures floor-price near $4.12. Another choice would be to sell Dec15 futures and buy a Short-dated (SD) Sept 440 corn call for 16½¢ Short-dated corn calls are based on Dec futures, and the Sept SD will expire on August 21 instead of on Nov 20 for the regular Dec option. The earlier expiration cuts the 'insurance' cost and raises the farmer's futures floor price to almost $4.23.

That same farmer could also have sold Nov15 soybean futures at $10.25 and bought a Short-dated Sept 1040 call option for 24¢ to create a $10 futures floor. A Nov 1040 conventional call would have cost 37+¢, lowering the futures floor to $9.87.

End-users can do comparable strategies in reverse: Buy corn futures and buy Short-dated corn puts in case prices drop. Two strengths of options are that they are not an 'all or nothing' marketing strategy, and they can give you the confidence to act. And in volatile markets where corn can swing 5-15+¢ per day, 15-20¢ to lock in a $1 rally and still benefit from further potential rallies looks cheap! Forget debating how high corn can go. Why would farmers risk leaving their current gains on the table? We say, "Get busy marketing!"

Check out the easy-to-use Option Quik Strike website, CME Option Quik Strike which is free and displays premiums for any listed type of option on grains. The free version updates premiums once daily in the afternoon after all markets have settled. That makes it easy to compare strategies and costs across months and strike prices without worrying about whether a price is current. Your broker can

Chart 3: The US is Mostly Priced out of N Africa and the Mideast Markets.



always get real-time quotes for you to fine-tune your strategy.

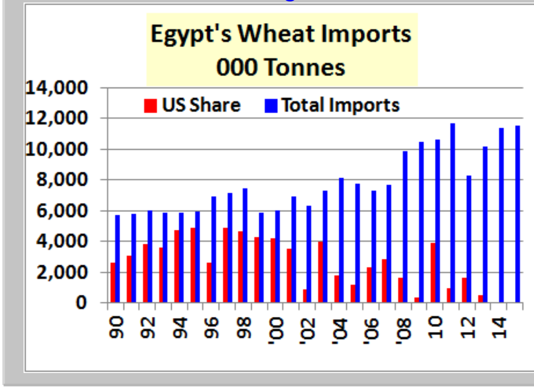
WHAT'S WITH WHEAT BASIS?

That's best answered with the long view. US wheat exports are less than 60% of what they were thirty years ago. The US supplied up to 80+% of Egypt's wheat imports until around 2000, only to see our share shrink steadily as production and exports rebounded in the Black Sea region and Eastern Europe. (Charts 4, 5) The US has lost the Egypt market even as Egypt's total imports have doubled since the 1990's! But it's not just about Egypt – the US has also lost business with other big importers: N. African and Middle Eastern countries. Big crops in the Former Soviet Union countries and cheaper ocean freight off the Black Sea make US wheat non-competitive much of the time. In a recent tender by Egypt, the US offers were more than $50/tonne, or $1.25/bushel higher than Black Sea offers. The US does sell a lot of wheat into Mexico, Central America, and Asia, but even there, Canada and Australia are solid competitors. Just this week French wheat sold into Mexico, which means Eastern US mills may also soon find imports *their* cheapest source of wheat. That's *not* bullish.

Reinforcing the shift, US HRW exports in '14 crop were just 270M bushels, an 8-year low. USDA forecasts HRW exports will eventually hit 290M bushels this season on reduced competition from the smaller Canadian crop. But so far, export sales are *down* 29% versus this time last year.

Chart 5: The World's Biggest Wheat Exporter

Chart 4: Black Sea Origins Have the Advantage



US SRW export business remains sluggish as well, at just 133M bushels for '14 crop, a 4-year low. Since June 1 SRW sales are down 15% versus a year ago, while USDA forecasts '14 exports steady at 135M. Adding to the woes, SRW is plagued with vomitoxin and light test weight in many areas, eliminating it from the export market. HRW dodged the vomitoxin problem but has test weight issues. CBT and KC wheat are both already near a 2-year low premium over corn and could slip further.

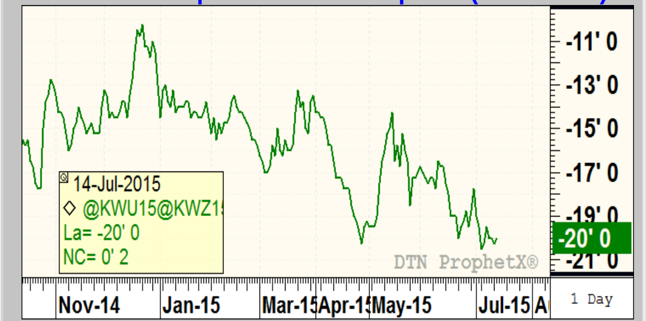
The end result is falling basis values at the ports for both HRW and SRW even while high quality wheat may command a premium. Eastern mills appear stymied trying to find sufficient good quality SRW and are easing up on their discount schedules. That leaves a lot of US wheat that nobody wants right now. Basis had to weaken to levels where someone will take the ownership and hold it longer term, perhaps into 2016 crop. Elevators with space and money and patience may find it attractive to buy such wheat now and hold it.

WHEAT SPREADS

The KC Sept/Dec wheat spread (Chart 6) is around 20¢ carry right now, about 65% of financial full carry. We said last issue and repeat again – go ahead and move short Sept KC wheat to Dec at current levels. 20¢ is better than any other carry out there right now. It could widen, but why risk it narrowing? For folks holding off-grade HRW, consider setting KC Sept15/July16 at 48¢ instead, the equivalent of 4.8¢/month to cover your costs until next summer.

KC Sept/Dec offers so much right now in part because KC storage rates are different than for CBOT wheat, operating under what's known as the Seasonal Storage Rate program, implemented

Chart 6: KC Sept/Dec15 Wheat Spread (a/o 7/14/15)



before KC and CBOT merged. Storage rates on KC delivery wheat change seasonally:

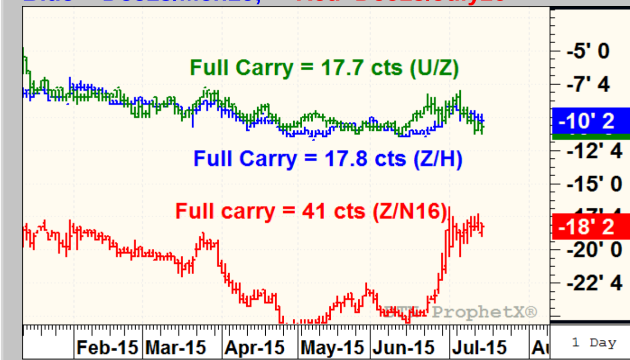
$.00197/day	KC Dec-June
$.00296/day	KC J/A/S/O/N

Because of the lower winter rates, full carry on the KC Dec/March spread is only 21.5¢.

CORN SPREADS

The Sept/Dec corn spread is especially important to Southern areas where harvest comes early. With farm selling rising with futures, and basis weakening, Sept/Dec has widened to around 11¢ (carry). That's close to our objective of 12¢ to roll short hedges forward, with conservative managers starting around 11¢. Our recommendation stands; 12¢ is 68% of full carry and we're satisfied. Set a

Chart 7: Corn Spreads to Watch Green = Sept15/Dec15; Blue = Dec15/Mch16; Red=Dec15/July16



higher goal around 13¢ - just in case - on maybe 10% of the bushels you'll need to roll, (Chart 7)

Dec15/March16 and Dec15/July16 corn spreads are critical for all elevators. Dec15/March16 is also widening and we recommend managers and merchandisers set initial objectives for this carry, and have orders working. We suggest 12¢ (68% of full carry) as a level to protect on up to 50+% of your anticipated harvest ownership that you will need to carry into or past December. Increase the percentage to 75% if Dec/March hits 13-13½¢.

Dec15/July16 is bucking the trend and narrowing, which may be due to uncertainty over the crop size; 18¼¢ is just 44% of full carry and for that reason we suggest focusing on Dec/March for now.

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IN THIS ISSUE

"Life is not a matter of holding good cards, but of playing a poor hand well." Robert Louis Stevenson