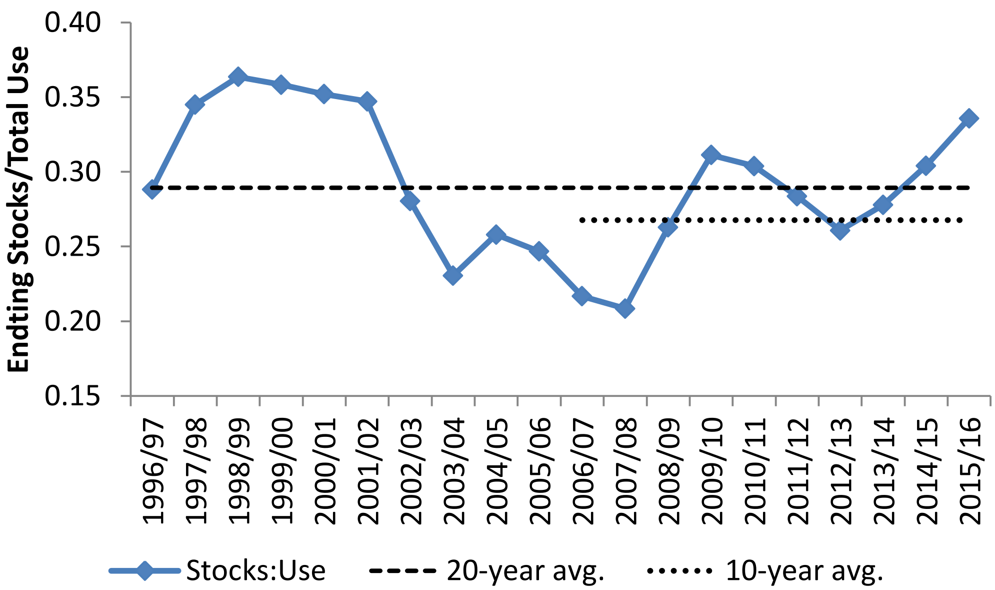
February 2016 – Crop Market Update
Public Policy Department
Budget & Economic Analysis Team

World Wheat Stocks Climb Higher

February is usually a pretty boring time of year as far as USDA reports are concerned. We are far enough removed from the U.S. harvest to have all of the supply side numbers pretty well pinned down and we are also far enough into the marketing year to have a pretty decent handle on at least the broad contours of the demand side of the market. Add to that the fact that the late-February USDA outlook conference gets most of the attention and February reports can be kind of hard to get excited about.

With that said, the February World Agricultural Supply and Demand Estimates (WASDE) report was not without its points of interest. The world wheat demand estimates were perhaps the most striking figures in the report. USDA dropped their estimate of 2014/15 wheat use by around 2.0 million metric tons (MMT) and also dropped their estimate of 2015/16 use by over 4.5 MMT. Almost all of the demand changes in both years were due to revisions in use estimates for—surprise!—China.

The decline in use estimates with little change in production figures has resulted in substantial upward revision in wheat carryover estimates. Figure 1 provides an updated version of a picture that I have shown several times over the past few months: the world wheat stocks-to-use ratio.



Data Source: USDA Foreign Agricultural Service, PSD online

Figure 1. World Wheat Stocks-to-Use Ratio: 1996/97 to 2015/16 (forecast)

At the end of the 2012/13 marketing year, wheat stocks were a bit below their 10-year average. However, that year has been followed by three consecutive record world crops: 715 MMT in 2013/14, 726 MMT in 2014/15 and 736 MMT in 2015/16. With only modest growth in demand, these large crops have rapidly raised wheat stocks. Right now, if current projections hold, wheat stocks will be back to about the same level as in the late-1990s/early-2000s—obviously not a great market environment.

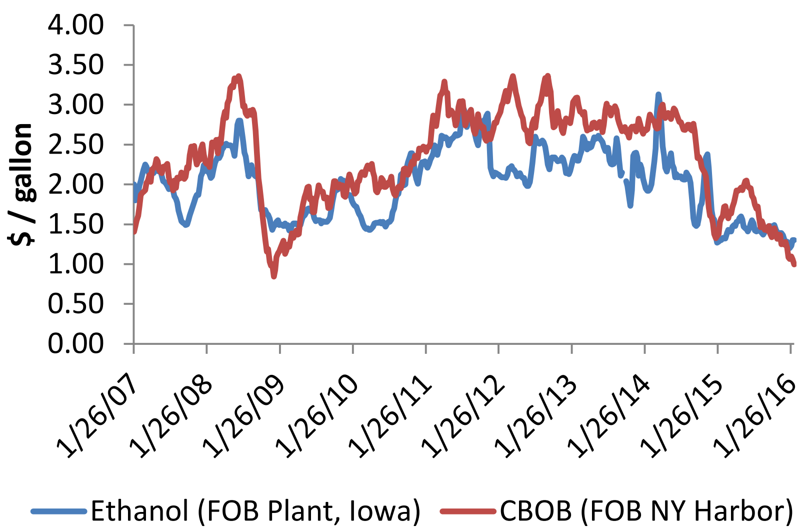
Ethanol and Gasoline Prices

The February WASDE included a couple of minor tweaks to the corn balance sheet. Exports were dropped by 50 million bushels—not much of a surprise, as the difficult export market has been a topic of discussion since about mid-year last year. Ethanol use was bumped up by 25 million bushels. These changes, along with a 10 million bushel increase in corn imports added 35 million bushels to estimated carryover.

The ethanol sector has been in the news a bit over the last few weeks. Petroleum prices have continued to slide lower even as corn prices have more-or-less stabilized. The pressure of lower gasoline prices on ethanol prices has put a squeeze on ethanol producer margins. Weekly estimates of ethanol plant operating margins from the Center for Agricultural and Rural Development (CARD) at Iowa State University indicate that some plants are probably having a difficult time even covering operating costs. The basic economic principle is that if you can't cover variable costs, the profit maximizing thing to do is shut down. In fact, over the last several weeks a number of plants around the country have announced temporary shutdown or slowdown plans.

Despite the bad news, ethanol production remains surprisingly robust. So far this year, weekly production has consistently exceeded the prior year's level—if only just barely. Weekly use has also compared favorably to year ago levels for the most part. Still, with ethanol priced high relative to gasoline, refiners seem determined not to use any more ethanol than they have to meet octane needs and hit RFS requirements. But even at a substantial premium to conventional blendstocks (CBOB), ethanol prices are, as noted, too low to support positive margins.

Figure 2 shows spot ethanol (Iowa) and CBOB (NY Harbor) wholesale prices going back to 2007.



Data Source: Department of Energy and USDA AMS through Livestock Marketing Information Center

Figure 2. Ethanol and Conventional Gasoline Blendstock (CBOB) Weekly Wholesale Prices

The decline in gasoline prices has been almost uninterrupted since late-summer 2014. It has not been quite as dramatic as the financial-panic-induced decline in the second half of 2008, but it has been close. The price levels reached on the wholesale gasoline market are certainly comparable. For the week ending Feb. 12 this year, the NY Harbor CBOB price fell to below the $1 mark for the first time since the last week of 2008. The NY Harbor CBOB price has now been below the Iowa ethanol price since the end of September.

Looking ahead, the gasoline price scenario could begin to get better for the ethanol sector. Seasonally, we are not too far away from stronger demand. Perhaps more significantly, this week, some of the major OPEC players (Saudi Arabia and Russia) started seriously talking about the prospect of an oil production freeze. This is an indication of just how much pain lower oil price are inflicting on those countries and they have probably fared better than several others (e.g., Venezuela, which would be an economic basket case even with high oil prices). Still, energy market fundamentals seem pretty bearish. For one thing, the world economy is not exactly surging right now. That's not good for demand. For another, across the U.S. oil patch, tremendous production capacity has been idled by low oil prices. This week, Bloomberg reported that across U.S. shale fields, 4,000 wells have been drilled and capped (to say nothing of the drilling rigs that have been parked). So a rise in prices could, in relatively short order, be met with a surge of U.S. production. Of course, OPEC knows this too; so it's not at all clear that their talk of a production freeze will really materialize.

Crop Insurance Price Discovery Update

Projected prices for revenue insurance products on corn and soybeans have just been released for those areas with a sales closing date of Feb. 28. The price discovery period for those areas runs from Jan. 15 through Feb. 14. For corn, the projected price is the average daily closing price over that period from either the September contract (SC, LA, GA, FL, AL) or the December (AZ, AR, CA, MS, NV, NC) contract. For soybeans, the November contract (AR, LA, MS, parts of TX) or the January contract (AL, FL, GA, NC, SC) is used.

For areas with a sales closing date of Feb. 28, projected corn and soybean prices for 2016 are summarized below. For comparison, projected prices from 2015 are also included.

Table 1. Crop Insurance Projected Prices for Corn and Soybeans for Areas with a Feb. 28 Sales Closing Date

Crop	Contract Month	2015	2016	% Change
Corn	Sept.	$ 4.05	$ 3.81	-5.9%
	Dec.	$ 4.13	$ 3.89	-5.8%
Soybeans	Nov.	$ 9.62	$ 8.86	-7.9%
	Jan.	$ 9.67	$ 8.91	-7.9%

Insurable corn prices are down about six percent from a year ago, and insurable soybean prices are down about eight percent from a year ago. In a couple of weeks, we will get projected prices for the key production areas of the Midwest, but year-over-year changes will likely be in about the ballpark laid out in the above table. I don’t really know what these prices say about the bidding for acreage that goes on between these crops each year. Certainly, the percentage changes indicate that the balance has shifted somewhat toward corn this year compared to last year, but only just a little. Right now, it looks like this year, much like last, is not offering any great incentives for farmers to deviate too much from their current rotation.

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