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Is the Corn and Soybean Rally for Real?

By Chris Lehner (Aug 8)

Anyone that has read my reports knows I was a long time bear, but reversed and I have been buying. In the short run, I am friendly. In the long run I am bullish. But, it is going to take some time before a fire can be built under grains.

It is easy to say corn, soybeans and wheat have bottomed, but when are they going to rally? A rally where large funds make markets move up and not move up and then go sideways. December 2018 corn bottomed on July 12th at $3.50 ¼ and as I write on August 7th the high was $3.88 ½ on July 31st, 38 ¼ cents off the low. November bottomed on July 16th at $8.26 ¼ and on July 31st moved to 9.22 ¼ for a 94 cent move up. December 2018 Chicago wheat has had the best move, and from July 12th to August 2nd it moved up $1.23.

Before soybeans can take off to the upside, cash basis needs to improve, but over the past couple weeks it has been the opposite. Basis in many areas of the U.S. widened instead of narrowing over the past week. As of this writing there have been 5,341 loads of August soybeans delivered. Producers or merchandisers near to terminal markets or who own trucks delivered on the CBOT prices where basis is par Chicago, or just slightly more delivered on their hedges instead of taking local prices. It may take a while for markets to use or move grain delivered, either to a crusher or down river to export markets. In order not to get completely overrun with soybeans, buyers widened the basis.

As you may recall on the June 29th USDA Grain Stocks report, there were 26 percent more soybeans stored than the year before. Normally grains stored, especially off the farm where monthly charges are incurred, are moved before the start of new crop harvest. With the 2018/2019 ending stocks estimate as of the July 12th WASDE Report at 580 million bushels versus a year ago at 465 million bushels, and farmers hoping futures rally combined with a narrowing basis, you can count on more soybeans going to storage for new crop than ever before.

Don't be surprised to see the USDA raise the estimate for new crop soybeans and corn. From June to July WASDE showed the USDA raised ending stocks from 385 million bushels to 580 million bushels. It is no secret since the "Trade Wars" began exports have slowed, but as I have pointed out several times, exports slowing are not all due to the trade wars. The U.S. is competing with Brazil and trade agreements Brazil has made with China and other exporting countries. If a country wants to build market share, trade agreements have become essential. With the countries that produce industrial commodities and agricultural commodities, they need to know they can move what they produce beyond their own needs to countries such as Brazil to bring in money from other countries. Brazil, along with many countries, have been aggressively building new trade agreements. Money to build infrastructure also has been moving into Brazil from foreign companies including the U.S. and companies investing expect products in return.

Brazil's soybean was bigger than ever before. As I have pointed out, a year ago they learned they had to not only sell more, but to move more at harvest which meant scheduling more ships and for a longer time. For years, Brazil would move most of their soybeans and corn from May through August. A year ago, shipping was into the end of September, but they still needed to store, which meant moving early in 2018 and will mean moving more into October and possibly November 2018. A report on August 6, 2018 from the consulting firm in Brazil, DATAGRO, noted, "Soybean stocks in Brazil at the end of the 2018/19 cycle are expected to be around 861 thousand tonnes. If the projection is confirmed, the volume stored will be 37% lower than the amount of oilseed stored in the 2017/18 season [1,175 million tons]."

Sounds good at first, but what it means is Brazil has been moving more soybeans because they had a larger crop in 2018 than the year before. However, it will hopefully mean moving more grains at a faster pace will allow more time for U.S. soybeans to be moved likely from November into late February and possibly May. But with the expected growth in land in Brazil, it is very possible that Brazil will have more soybeans in 2019. As of now, using trend line yields, 2019 soybean production is expected to be as large as this year's excellent production with its surplus growth.

U.S. farmers also are competing with themselves this year. The July WASDE yield estimate was at 48.5 bushels. Don't be surprised on the August report to see estimates over the 2017/18 estimate of 49.1 bushels to the acre. As the old saying goes, soybeans are made in August and current forecasts appear to be favorable soybean growing weather. Without an ounce of doubt, I know I will receive emails about areas that have too much rain, or where beans were flooded out during planting to where it has been too hot. But most farmers are now concerned about the massive vines soybeans are producing and how it will slow down speeds when combining. It is sort of like a person who is paid overtime and complains about paying more taxes. It is too bad they can't go as fast as they want because the crop is too big. Yes, the size of the vines doesn't insure big yields, but with the recent Crop Progress report showing blooming at 92 percent compared to the five year average at 86 percent and a year ago at 89 percent, and beans setting pods at 75 percent compared to the five year average at 58 percent and a year ago at 63 percent, anyone concerned about lower yields this year is like a farmer hoping other farms have lower yields because they know theirs is big. Unless Mother Nature throws a wild pitch in August or early September, looking for lower yields is living in a false reality.

If you are a patient trader and don't expect big quick rallies, then buy corn and soybean futures. I don't advise buying call options now that corn and soybeans have full carrying charges. The option train has left the station. The time value in the options will be eaten up, especially buying out of the money calls a few months out. With the current carrying charges, it is about the same as a farmer storing. A market will need to move fast and more than the carry and extrinsic value to see calls from this point on build premium. If you like using options, buy futures and then buy a put to protect any big unseen down move.

More importantly, watch the basis before getting too bullish. The soybean basis as I hear over and over, which I can't write in this report, but suffice to say, it is horrible. In many parts of the Midwest, it is wider than it was a year ago. About the only improvement and only a few merchandisers are offering it, can be had with a little narrower basis for contracting soybeans and corn into 2019. The nearby basis for old crop and for new crop fall delivery off the combine needs to contract before soybeans can move much more than $9.40 to $9.50. I am friendly corn, but it too will need to see basis narrowing before it can move much past $4.10. If you are patient, wait until farmers can sell corn for $3.85 to $4.00 cash. Farmers will dump it like a hot piece of Hawaiian lava. After a quick break, load up on corn. Or as I have been suggesting since late March, buy three corn contracts and sell one soybean contract on a spread.

Yes, the rally is real, but don't expect a quick and sustained move to the upside. It is also not the kind of market to pyramid adding positions with profits. There can be setbacks and stair steps up. Place patient when initiating positions.

Trading is not easy. For close to 35 years I have been working with farmers and speculators. Make it a bit easier, work with a broker with experience. If you have been reading past commentaries over the last month or longer, you will know what I mean. Past reports can be found archived on **www.insidefutures.com.**

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