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MI Prospects

Volatility Returns

With fresh information from the USDA acting as a catalyst, volatility has returned to grain prices with both old and new crop prices falling. This followed a period of calm in late 2013, and as the graph below shows, new crop (Nov-14) feed wheat futures **continue to set new lows**.

For arable farmers, not only have new crop ex-farm feed wheat prices slipped through £150/t, but also £140/t more recently, for some. This is likely to continue to instil a **wait and see attitude** towards new crop selling in the hope of a weather issue somewhere in the world this coming growing season. However, it is important to remember that in the short to medium term, commodity markets do not respect costs of production.

From a **broader perspective** though, it is important that markets work effectively, otherwise there is a risk of artificial measures being put in place to **"make them work"**. Current political attention on energy and banking are current examples of this. The recent fall in UK inflation has in part been attributed to lower food prices, which can be traced back partly to lower grain prices. As a result, it is becoming more important that grain markets remain responsive and demonstrate that they do work.

Grain and particularly oilseed markets continue to become less dominated by the Northern Hemisphere as South America becomes a **strengthening powerhouse of production**. This helps to spread the risk (or opportunity) of volatility throughout the year. However, logistics are likely to remain a bottle neck for the region, which may prevent markets responding fully to changes in supply and demand fundamentals.

With the biggest crop in 15 years, UK barley has a great deal of attention this season especially as this is the largest crop in modern times, which is very unlikely to be balanced by the use of intervention. It is worth bearing in mind that 2013 was the **third harvest in 13 years that saw major disruption** to the crop area because of a previously wet autumn. As a result, having a spring crop back-up plan (spring barley for most) is a valuable asset.

Jack Watts

UK Feed Wheat Futures: November 2014

Source: AHDB/HGCA

In this issue...

USDA Supply & Demand Estimates and US Quarterly stocks

The latest supply and demand estimates from the USDA offered few surprises apart from forecast closing stock levels. Together with the latest quarterly stocks information, this data was responsible for an injection of volatility into the market.

Amandeep Kaur Purewal
Market Specialist team
02476478954, amandeep.kaur.purewal@ahdb.org.uk

Introduction

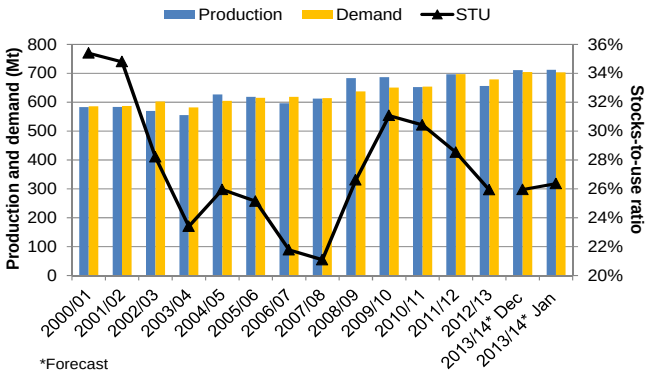
The USDA published their latest world supply and demand estimates on 10 January, as well as data for quarterly stocks as at 1 December 2013. This article provides an overview of the released information and examines its implications.

Wheat

Global wheat **production** was revised slightly higher by 1.24Mt to 712.7Mt, with higher estimated output in China (+1Mt) and the FSU (+0.96Mt) off-setting declines in Argentina (-0.5Mt) and the EU (-0.22Mt). In terms of **trade**, the **EU export projection** was revised 1Mt higher, whilst for the US, exports were revised almost 0.7Mt higher. Total global **demand** was lowered by 1.08Mt, mainly **due to lower use in animal feed in the US and EU, where maize is currently more competitive**. The key piece of news, however, was the increase of global wheat stocks by 2.62Mt to 185.4Mt, due to a combination of higher supplies and lower consumption.

As a result, the global 2013/14 wheat **stocks-to-use ratio (STU)** is now forecast at 26.4% (25.9%, December), which puts the wheat market in a slightly more comfortable situation (25% is considered to be a key level for wheat), although there is little room for any major shortfall in production in coming years.

Figure 1 Global Wheat Production, Demand and STU



Source: USDA

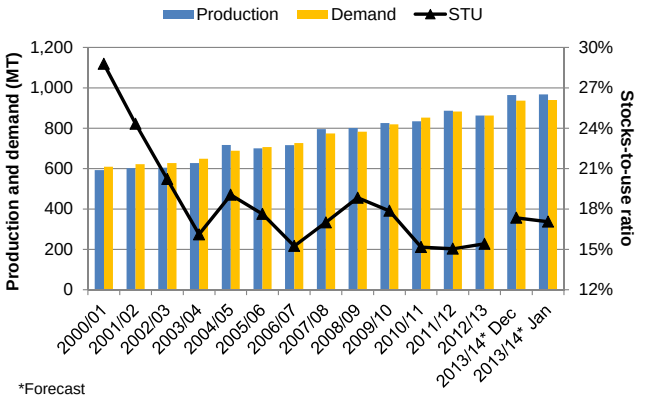
With the **US wheat stocks** considered to be the world's "back-up supply", the release of quarterly wheat stocks data as at 1 December were of further interest to the market. Despite a 12.4% year-on-year decline in stocks, the published figure of 39.81Mt was 1.7Mt higher than many trade estimates. Between 1 September and 1 December 2013, stock levels fell by 11.07Mt compared to 11.82Mt for the same time period in 2012, suggesting lower demand for wheat during this time period in 2013.

Maize

For maize, **global production** was increased by 2.64Mt from December's estimate, representing a year-on-year increase of 12.0%. Although **US maize production** was reduced by 1.61Mt (due to a reduction in the forecast yield) and Argentine output was reduced by 1Mt (following dry weather experienced in December), a 6Mt increase in Chinese maize production was more than sufficient to take the global production higher.

Total global maize demand was revised higher by 2.93Mt from December's estimate to reach 939.7Mt (8.9% increase year-on-year) due to higher usage in feed and ethanol production. The increase in consumption led to the forecast of closing stocks of maize for 2013/14 being reduced to 160.2Mt from 162.5Mt in December.

Figure 2 Global Maize Production, Demand and STU



Source: USDA

Nevertheless, with the year-on-year increase in production outweighing the increase in demand, maize stocks are 20.4% higher than a year ago, bringing the STU to 17.1%. Although an improvement on the average STU of 15.2% obtained over the previous three years, the STU for 2013/14 is still historically low and a production surplus over demand is needed for a number of years in order to return to more "safe" levels. This would be largely dependent on the weather, which brings the biggest level of uncertainty, and thus volatility.

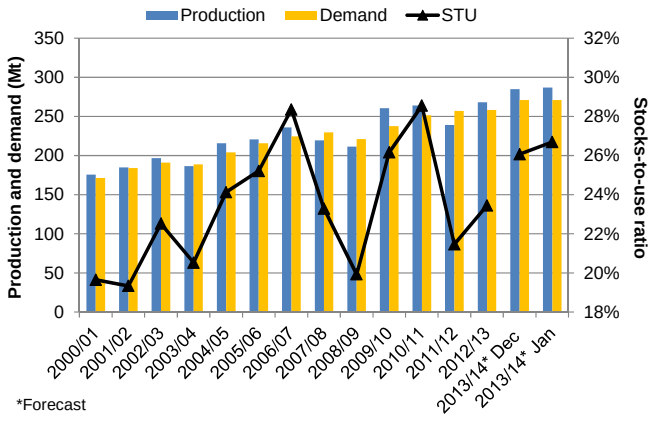
US maize stocks, as at 1 December 2013, were 29.8% higher year-on-year, but at 264.8Mt, were 9Mt lower than trade expectations. The latest estimate for **US end-stocks** was 4.1Mt lower than January's forecast. In contrast to wheat, the timing of the maize harvest means that stocks on 1 December are higher than as at 1 September, which is mainly old-crop supply. Between 1 September and 1 December 2013, maize stocks increased by 244Mt, 36.4% higher than for the same time period in 2012, and reflects the boost in production.

USDA Supply & Demand Estimates and US Quarterly stocks

Soyabeans

World soyabean production was raised by almost 2Mt to 286.8Mt, following higher output forecast for the US and Brazil. Brazilian soyabean production is now pegged at 89Mt compared to 89.5Mt for the US. The Brazilian government's crop agency, CONAB, currently forecasts the national crop at 90.3Mt. Should the latter estimate turn out to be correct then Brazil would overtake the US as the leading soyabean producer. For the US, exports were revised higher by 55Kt to 40.69Mt in order to keep pace with the total export commitments for the year so far. However, this still falls short of the 41.45Mt of total export commitments as at 9 January.

Figure 3 Global Soyabean Production, Demand and STU



Source: USDA

With global **demand** estimated at a similar level to December's projection, the increase in soyabean output has led to a 1.7Mt increase in global soyabean end-stocks to 72.33Mt. Global **STU** for soyabeans is, thus, estimated at 26.7%, 3.2% points higher than in 2012/13 and higher than the previous five-year average.

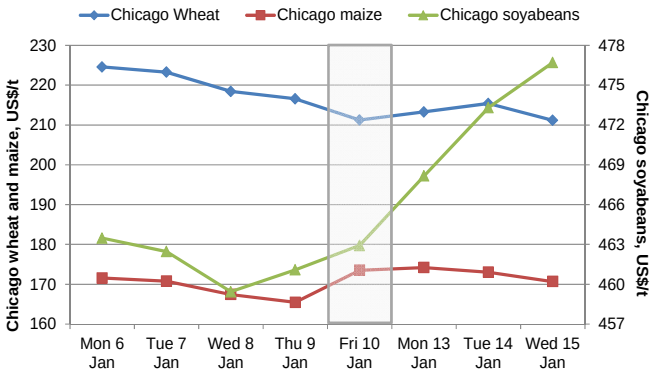
US soyabean stocks as at 1 December were 9.2% higher year-on-year, at 58.5Mt, and were slightly below the trade estimate of 58.8Mt. As with maize, the harvest timing means that stocks at the start of December are higher than at the start of September, due to replenishment with new crop supplies. Stock build up between the first and second quarter of the current crop year was 54.6Mt, compared to 48.9Mt for the corresponding time in 2012. As with maize, this is a result of the 8.4% year-on-year increase in production.

Effect on prices

The release of the USDA data normally stimulates a reaction from the market. Increasingly, more surprises are usually afforded by the US quarterly stocks report rather than the world supply and demand estimates.

The **May-14 Chicago wheat price**, already on a downward path prior to 10 January (Figure 4), fell even further by Friday's close (10 January). The biggest drop in price ($5.33/t) was observed for the time period shown, reflecting the higher than anticipated stock levels. Prices then increased gradually, partly due to the first Egyptian tender for US wheat this season, but fell back to levels seen on 10 January.

Figure 4 May-14 Chicago wheat, maize and soyabean prices (before and after USDA reports published on 10 January)



Source: USDA

As shown in Figure 4, the **Chicago maize price** (May-14) recorded a daily increase of over $8/t (4.9%) following the release of the USDA data, due to the lower than anticipated stock levels. The settlement price on Monday was slightly higher (0.4%), but fell during the next two sessions.

The **May-14 Chicago soyabean price** was the least affected. Although stocks in December were slightly lower than the trade estimate, the daily increase in Chicago soyabean prices was similar to that observed in the previous session. For the time period shown in Figure 4, higher gains were made after 10 January due to further US export sales and strong domestic demand (the National Oilseed Processors Association revealed that the monthly US soyabean crush in December, at 4.5Mt, was the highest monthly total since 2002.

Concluding comments

For the remainder of this season, unless a major weather event affects the remaining Southern Hemisphere harvest, changes in production estimates are likely to be minimal. Demand and, therefore its impact on stock levels will be the area to watch. With the price relativities of wheat and maize favouring the latter, and continued strong demand for soyabeans, the stock levels will be key factors in bringing volatility to the market.

Key Points

- Lower demand leads to higher than expected wheat stocks.
- Higher demand leads to lower than expected maize stocks.
- Changes in soyabean stocks levels offer few surprises.
- Wheat and maize prices react more than soyabean prices.

US Winter Wheat Plantings and Condition

Farmers in the US have planted 3% less winter wheat for harvest in 2014, compared to last year, with a sharp decline in SRW wheat partially offset by higher HRW plantings. While improved soil moisture should raise the crop's potential during spring, winter kill remains a risk due to limited snow cover.

Helen Plant, Market Specialist team
0247 647 8759, helen.plant@ahdb.org.uk

Introduction

US farmers planted 3% less winter wheat for harvest 2014 than in 2013 according to the US Department of Agriculture (USDA). However, estimated at 17.0Mha, the winter wheat area is, still 0.3Mha above the area planted for harvest 2012 and considerably above the record low of 15.1Mha for harvest 2010.

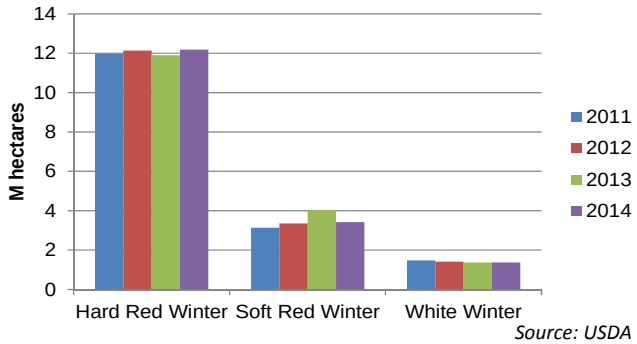
This decline comes despite a considerable improvement in soil moisture levels across the main growing regions and relatively favourable planting conditions. A **considerable fall in prices compared to last year is likely to be part of the reason** but there are specific differences between the classes of wheat.

Fall in SRW wheat area, partially offset by HRW

Soft Red Winter (SRW) AND Hard Red Winter (HRW) wheats are the two most important export grades for the US. The lower winter wheat area is primarily due to a decline in the SRW wheat plantings. The USDA reports that **SRW wheat plantings are estimated to have fallen in most major growing states**, with the total area down 0.6Mha from the area for harvest 2013 (Figure 1).

Price is likely to be a major reason behind the decline. In September 2013, the Dec-14 Chicago futures contract (based on a SRW wheat specification), was trading around $250/t, approximately $70/t lower than the Dec-13 contract a year earlier.

Figure 1 US Winter Wheat Plantings by Class and Harvest year



Source: USDA

In contrast, the **area planted to HRW wheat, the largest class of winter wheat, is estimated to be around 0.3Mha** higher than for harvest 2013, though the picture varies by state. In **Kansas**, the largest winter wheat growing state (mainly HRW), the planted area fell by 283Kha to just under 3.6Mha (Figure 2). Some commentators have indicated the late harvesting of 'double-crop' soyabeans in some parts of the state contributed to the lower wheat area – limiting the time frame for planting the 2014 HRW crop.

Figure 2 US Winter Wheat Area in Selected States

M hectares	2012	2013	2014	% change
Kansas	3.80	3.84	3.56	-7%
Texas	2.31	2.51	2.51	0%
Oklahoma	2.19	2.27	2.14	-5%
Colorado	0.95	0.93	1.17	26%
Montana	0.93	0.81	1.01	25%
United States	16.68	17.44	16.95	-3%

Source: USDA

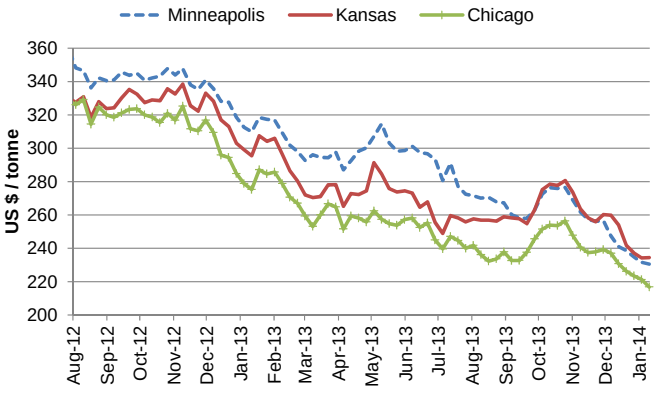
In the mainly HRW growing state of **Oklahoma**, the area was also markedly lower but plantings in Texas were largely stable. Conversely, **for HRW growing states further north, the area generally increased**. Significant increases are reported for Colorado, Montana as well as North Dakota, where a record area of 0.3Mha was reported (up from just 89Kha last year).

Price Impact on HRW area?

Some of the northern states where HRW wheat is grown, are also the main producers of Hard Red Spring (HRS) wheat, primarily North Dakota, Montana and South Dakota. Changes to the price relationship between HRW and HRS wheat, may also have contributed to the general increase in HRW plantings in the region.

The Minneapolis futures (based on a HRS specification) typically trades at a premium to the Kansas futures, reflecting the higher protein content of HRS. However, since autumn 2013 the **nearby futures contracts have been trading at parity** (Figure 3). While this relationship has only recently been replicated in the Dec-14 contracts, there is some suggestion that this has encouraged some farmers to switch to winter wheat from spring wheat.

Figure 3 US Wheat Futures Prices (nearby contracts)



Source: AHDB

Crop conditions much improved entering winter

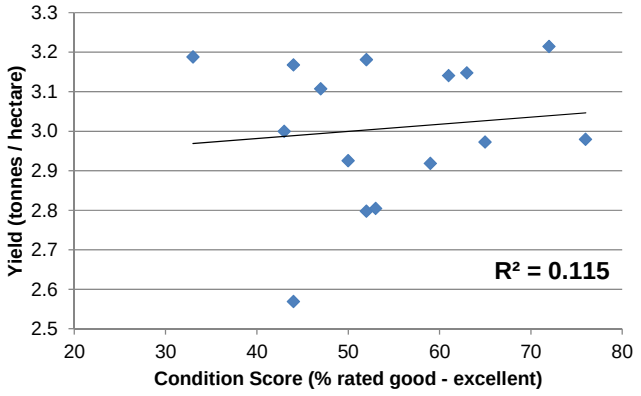
Soil moisture levels were much improved during planting in autumn 2013, compared to autumn 2012 – reflected in the crop condition scores in the run up to winter. Nationwide crop progress and condition reports typically finish for the winter in late November and resume at the start of April – though some states continue to report during the winter. In the last nationwide report of 2013,

US Winter Wheat Plantings and Condition

62% of winter wheat was rated as in a good or excellent condition, considerably above the 33% at the same point in 2012.

However, there is **no correlation between the nationwide condition scores prior to winter and the final yields** (Figure 4). While the condition of crops entering winter may impact the 'winter hardiness' of the crop, the lack of correlation shows that crop conditions before winter do not ultimately determine yields. As a result, it is important to read condition score prior to winter with an element of caution.

Figure 4 Correlation between last nationwide condition score prior to winter and US average yield (1999-2013)



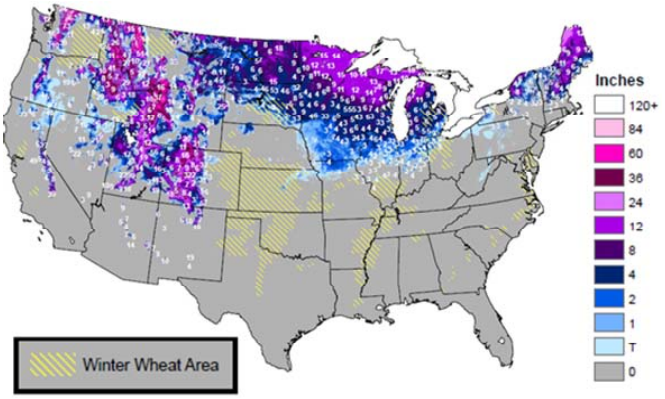
Source: USDA/AHDB

Current conditions

Over the past couple of weeks, the **US** has experienced some very low temperatures, which had the potential to damage crops. Snow cover is reported to have been adequate to provide insulation through most areas of the winter wheat belt. However, the USDA reports that **snow cover was lacking in much of Nebraska, as well as southern South Dakota and northern Kansas;** consequently it's possible that crops there were impacted as temperatures fell as low as -26°C.

Snow cover has receded slightly over the w/e 12 January and much of the Great Plains is now without this cover (Figure 5). This leaves crops potentially vulnerable should temperatures decline again, if further snow does not fall.

Figure 5 Snow Cover as at 12 January 2014



Source: USDA Agriculture Weather Monitoring

The winter storms have generally helped improve soil moisture levels and reduced the area of drought, which will be beneficial for crops once they emerge from winter dormancy. However, drought conditions persist in the southern High Plains, including parts of Texas. The Texas crop reports state that by 12 January, more than one-third (38%) of the Texas wheat crop was rated very poor to poor— compared to 28% in late November 2013.

The resumption of nationwide crop reporting on 7 April will give an indication of how crops have fared over winter. However, it is important to bear in mind that there is **limited correlation between nationwide crop condition scores in the spring and final yields,** as spring commences at different times across the country. Consequently, the growth stages reached can vary considerably across the country. On a state by state basis, however the scores will give an indication of the crops' potential – particularly in the southern states where winter crops are approaching flowering in April, when the nationwide reports resume.

Concluding comments

While the area planted to winter wheat for harvest 2014 is smaller than 2013, it could be argued that the US winter wheat crop has better production potential than a year ago. This is due to the much improved soil moisture levels, which will be beneficial to the crop once spring arrives. However, winter kill remains a major risk over the coming weeks, especially given the limited snow cover in some areas.

The final outcome will very much depend on how much winter damage occurs and weather conditions in the rest of the growing season. HRW and to a lesser extent, SRW wheat are the two most commonly exported grades of US wheat and the size of the crops will contribute to export availabilities in 2014/15.

Key Points

- Planted area 3% smaller than for harvest 2013
- Sharp decline in SRW, partially offset by an increase to HRW area
- Potential improved from 2013 due to higher soil moisture?
- Winter kill risk due to limited snow cover in some areas
- Drought remains a concern in southern High Plains, mainly Texas

Barley Market Update

Similar to other grains, global barley production increased this season adding further downward pressure to prices. With the largest UK crop in 15 years, exports have so far helped balance supply and demand, although pace is expected to slow in the second half and build carry-over stocks.

Jack Watts, Market Specialist team
02476 78760, jack.watts@ahdb.org.uk

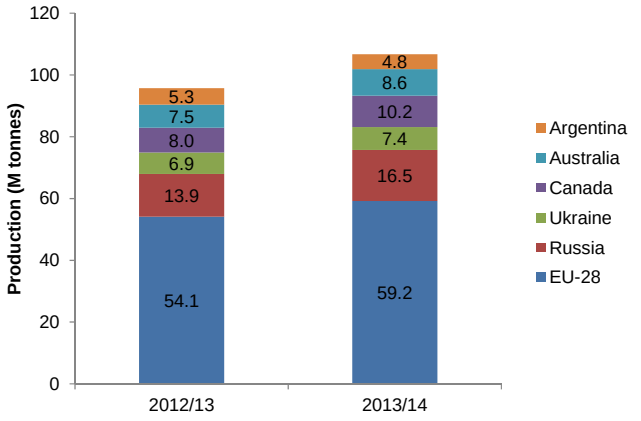
Into context: Barley versus other grains

Before getting too in depth with specific barley supply and demand fundamentals, it is important to remember that barley operates within the wider global grain market. With 2013/14 global barley production estimated by USDA at 145Mt, it is evident that it is dwarfed by maize (967Mt) and wheat (713Mt) - but still has to compete with these commodities for animal feed demand.

Heavier barley supplies in 2013/14

As Figure 1 shows, there is an 11.5% increase in barley production for the key producers this season. Although the year-on-year increase has been apparent for some time, additional details have emerged. In December, Canadian barley yields were estimated at record levels adding further supply to this key exporter. The recent Australian harvest sees a crop more than 1Mt higher than a year ago, which will also need to compete for demand.

Figure 1 Key Global Barley Producers



Source: IGC, EU Commission, Statistics Canada, ABARES, BAGE

Although the **Argentine** crop is down on last season, the decline is less than initially expected with the 19% fall in crop area largely offset by good yields in southern growing areas (BAGE).

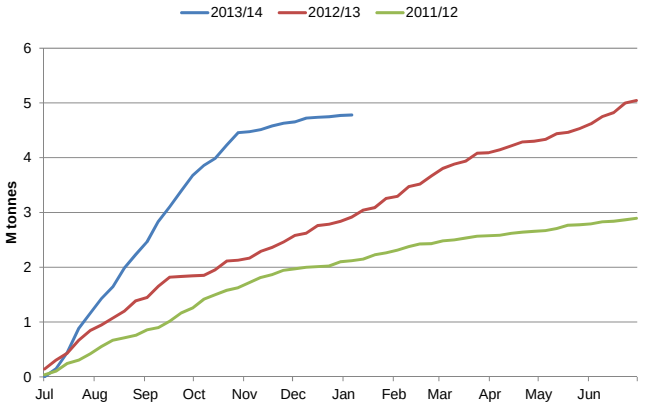
Key competition for the UK crop comes not just from a larger crop in Europe, but also from **Russia and Ukraine**. This competition is more apparent this year as the UK must access markets outside of Europe to help deal with the largest crop in 15 years.

A strong start for EU barley exports

Despite good crops elsewhere in the Northern Hemisphere, there appears to have been good demand for EU barley in the first four to five months of the season. Between July 2013 and early January 2014, the EU Commission had granted 4.78Mt of barley export licences, somewhat higher than the 2.92Mt granted by the same point last year.

However, as Figure 2 shows, progress has been much slower since late October, probably due to strong competition and the anticipated arrival of a good Australian crop. The Commission's current expectation for the entire season is that exports will be 7Mt, which is in fact lower than the 7.8Mt exported last season.

Figure 2 Cumulative EU Barley Export Licences

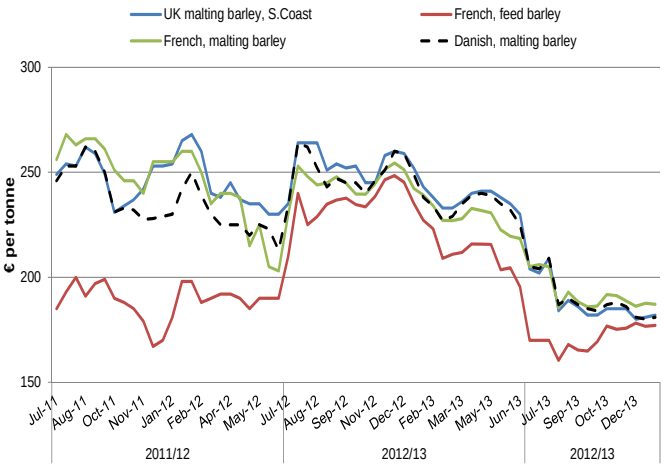


Source: EU Commission

Price trends

With better grain supplies, barley and specifically malting barley, prices have had to decline as shown in Figure 3. The previous two seasons have seen either quality or feed grain supply issues, which have supported the malting barley price. However, there are relatively few issues of concern in either camp this season. However, good demand and relatively low stock-to-use levels are preventing a complete price collapse.

Figure 3 Barley Export Prices (FOB Basis)



Source: RM International

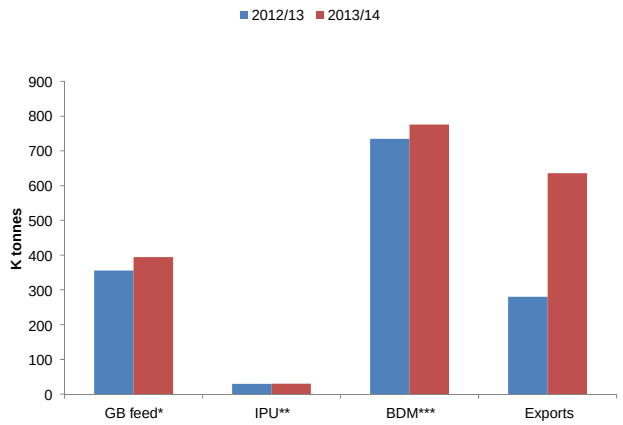
From a **UK** perspective, the large barley crop exacerbates the issue, forcing both feed and winter malting barley to discount levels against feed wheat. This is very specific to this season and it is likely that the price relationships will change for next season due to different fundamentals – discussed later.

How is the UK dealing with the largest barley crop in 15 years?

At just over 7Mt, the UK barley crop is some 28% up on the previous year and presents a huge challenge for the market to balance. However, the first five months of the season have shown encouraging signs. It is worth remembering that unlike the most recent large barley crops of 2001 and 2009, **Intervention is very unlikely to be used** to help balance the supply and demand.

Figure 4 gives an overview of key barley usage and trade data, cumulatively for July to November 2013. The one area that is not covered is the feeding of barley on-farm, which is expected to be larger this season due to the price differential with wheat and higher availability on mixed farms.

Figure 4 Barley Usage and Exports (Jul - Nov)



**Retail compounders, **Integrated Poultry Units, ***Brewers Distillers & Maltsters*

Source: DEFRA, HMR&C

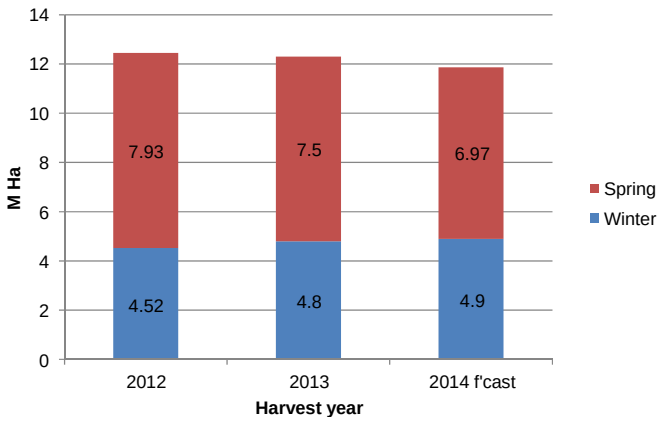
It is clear to see that **exports have been the key driver** so far, which has enabled the overall demand (excluding fed-on-farm) to be 31% higher than a year ago. Although this is encouraging against the 28% increase in production, the pace of exports is expected to slow through the remainder of the season. Even in the November export data, a slowdown in pace was evident with the monthly volume almost 25Kt down on the 202Kt shipped in October. More concerning is the declining Non-EU demand for UK barley, which was 28% of the total in November (75% in October). To deal with this season's surplus, large trade volumes outside of the EU are very important.

This indicates that an increase in carry-over stocks is likely, which could be an opportunity for brewers, distillers and maltsters to secure some supplies into next season, as a hedge against the currently unknown quality of harvest 2014. However, this will be dependant on storage and working capital availability.

Prospects for 2014

Although barley supplies, especially in the UK, are plentiful at the moment it should not be assumed that this will continue into the new crop season. A better autumn in 2013 will undoubtedly lead to a **lower UK barley area for harvest 2014**. In addition, the EU barley area is also expected to be lower with the spring barley acreage forecast by Strategie Grains to be down 7% (Figure 5). This is unlikely to shift the feed base price massively, but could have greater implications for malting premiums, especially if there is any weather threat to quality.

Figure 5 EU-28 Barley Area Estimates



Source: Strategic Grains

Concluding comments

It must be remembered that, spring barley offered a lifeline to many UK arable farmers in 2013, acting as the **wet autumn insurance policy** for the third time in 13 years. This of course has had price implications, but the 2014 performance of the crop shouldn't be written off.

Longer term, barley may come into greater focus as a tool to manage the CAP's three crop rule, Black Grass and help spread harvest workloads.

Key Points

- A good Australian crop and higher than expected Canadian crop add downward price pressure.
- A strong start to EU and UK exports looks to be fading and could well lead to a larger UK carry-over stock.
- Lower UK and EU areas expected for harvest 2014.

South American Crop Update

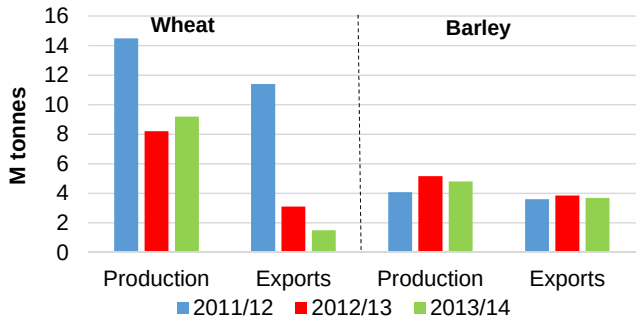
Forecast record soyabean crops in both Argentina and Brazil are expected to result in increased export availability. However, the next few weeks will be critical to the realisation of the current estimates.

Sarah Nightingale, External Contributor

Argentina

The Argentine Ministry of Agriculture in January increased its forecast for the 2013/14 **wheat** production to 9.2Mt, up 12% on 2012/13. The **wheat harvest is now complete**, and although there was a 15.5% increase in sown area, dry and cold conditions in many wheat growing areas led to yield declines. Exports were forecast by the Ministry at 2.1Mt in December, but so far only 1.5Mt have been authorised for export (Figure 1). Further authorisations may be made depending on the domestic situation throughout the season. Trade reports have suggested that some wheat was imported into Argentina at the end of 2013 but there are no official figures to show this.

Figure 1 Argentine Production and Export Forecasts



Source: Argentine Ministry of Agriculture

The **barley harvest** has also been completed and the Ministry estimates the crop at 4.8Mt (down 6.9%). Exports are seen marginally lower at 3.7Mt (3.9Mt), of which 0.7-0.8Mt are expected to be malting barley (USDA).

The **maize area** is currently predicted to be down 6.5% to 5.7Mha. Dry weather during the spring delayed sowings considerably, and further dry weather in December caused some stress. However, **78% of the maize crop was reported to be in "good" or "very good" condition** as at 16 January (when 88% of the intended area had been sown). Most forecasts put Argentine maize production in the region of 26.0Mt, similar to last year's production of 26.5Mt. Some confusion remains, following the large upward adjustment to the official figures for maize area and production in Argentina last year (of around 5-6Mt), but it is believed much of this is accounted for by forage maize. The government authorised exports of 16.0Mt of maize for 2013/14 in June last year in a move to encourage maize sowings (21.0Mt is forecast to be exported in 2012/13).

The Ministry figures show an increase in **soyabean** sowings of 4% to 20.8Mha. As at 16 January, 92% of this area had been sown with 86% of the crop reported in "good" to "very good" condition. Most forecasts put Argentine soyabean production for 2013/14 at between 54Mt and 58Mt (49.3Mt, 2012/13). USDA forecasts an increase in soyabean exports from 7.7Mt in 2012/13 to 9.7Mt.

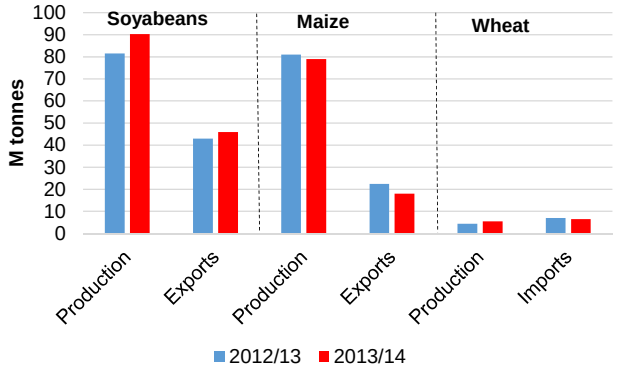
Brazil

Wheat production in Brazil is seen 24.9% higher in 2013/14 due to a larger sown area and better yields. **Rio Grande do Sul**, which accounted for just over 3.0Mt, overtook Parana as the principal wheat producing state. Wheat producers there have successfully lobbied for a reduction in the VAT on wheat sales to nearby states in order to ensure its production remains competitive with other Mercosur countries. CONAB forecasts import requirements for the country as a whole at 6.5Mt, down from 7.01Mt in 2012/13 (Figure 2).

The **maize crop** is seen lower at 78.9Mt (81Mt, 2012/13), as farmers in many regions switched to soyabeans. Exports are seen lower at 18.0Mt (22.5Mt), though CONAB reports firm export demand to date, boosted by Brazil's relatively weak currency situation.

Soyabean production is currently projected 10.8% higher to a record 90.3Mt (CONAB). There have been concerns about an increase in the pest "*helicoverpa armigera*" which is very difficult and expensive to control but it has been reported recently that farmers have managed to control the pest. The biotech companies are working hard to produce GM varieties resistant to this pest. Total soyabean exports are also forecast higher, though there are some concerns again about the logistical situation in Brazil which has been further complicated by a recent fire at the port of Santos.

Figure 2 Brazilian Production and Trade Forecasts



Source: CONAB, January 2014

Concluding comments

Large soyabean crops in both countries should bring more exportable supplies to the world market which continues to see strong demand this season. However, it remains to be seen how well balanced supply and demand will be. The wheat situation continues to look tight and it is likely that Brazil will import wheat from non-Mercosur countries again in 2013/14.

AHDB-HGCA
Stoneleigh Park
Kenilworth
CV8 2TL. UK

T +44 (0) 24 7647 8760
F +44 (0) 24 7647 8904
mi@hgca.com
www.hgca.com