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A Correction Will Be Limited by Excessive Supplies

As expected, the USDA Crop Production and Supply and Demand Reports released on Thursday morning confirmed ample to excessive supplies of wheat for the foreseeable future. As the fundamentals of the market weigh, wheat futures are going to have to find support from outside factors.

The USDA increased winter wheat production by 24 million bushels from 1.458 million bushels on the May report to 1.482 million bushels on the June report. The majority of this increase came from the HRW crop, which was increased by 19 million bushels. The white winter wheat crop increased by 4 million bushels and SRW increased by 1 million bushels. However, this is not necessarily a huge winter wheat crop. In terms of reducing the carryout, the reduction of acres was a start, but excellent crop development ensures that the US will have excess supplies going forward. Basically, the USDA is expecting a spring wheat crop in the neighborhood of 585 million bushels. The spring wheat crop that has gotten planted and has not flooded out looks to be in very good condition. Wet weather in the northern plains has limited some spring wheat planting and the productivity of many fields has been reduced due to excess moisture.

The world wheat carryout was reduced by 4.1 mmt. This reduction was primarily the result of the EU crop being reduced by 2.1 mmt. In addition, Syria was reduced by 1.3 mmt and Turkey was reduced by 1 mmt. I feel the USDA will be able to reduce Canadian production by as much as 2 mmt due to extremely wet conditions. Rains have continued in many of these regions. In many cases the producer has run out of time to get wheat planted. I understand the insurance deadline has been extended to June 20th. Unfortunately, many fields will not be ready to plant in that time frame.

Regarding the spring wheat crop one has to wait to see how the crop develops. Crop progress reports indicate that the crop is in very good condition. However, the market is oversold and in need of a correction. The wheat market posted a higher close on Thursday. I believe this correction could last for another 15 to 20 cents. At this point, a rally of that nature should be sold. Upward momentum will be limited, as the excessive supply is not going away anytime soon.

The wheat market has had the same obstacle in its way for many months. US wheat needs to trade lower to stimulate export demand. The excess supply is the result of decent crops and very poor export activity. Wheat needed to be trading near these levels at the beginning of the year to increase export activity. I never underestimate the ability of the Russians to sell wheat cheaper, but lower prices may have allowed for more business. The export activity of late has basically consisted of routine hard wheat business into Asian countries. Currently the HRW basis in the Gulf is 50 cents under the KC futures. Recent history has HRW basis at 50 to 60 cents over the futures.

Barring a substantial break in the dollar and/or another reason for the fund community to liquidate short positions in the Chicago contract wheat should go lower, after correcting oversold conditions.

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