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The Wheat Market Does Not Have Reason to Rally

The wheat is oversold, but so far, nothing has triggered a short covering rally. The market has not been able to trigger a short covering rally. The primary factors, such as adequate global supply and weak demand, weighing on these markets, remain firmly intact. Progress is being made in the winter wheat harvest, which provides additional resistance.

The large global wheat supply has been well documented. Expect this factor to continue to weigh on these markets and limit any short covering rallies. Getting wheat sold, as the northern hemisphere harvest kicks into gear, is going to be a difficult task. Outside of a major collapse of the US dollar, I do not believe the wheat market is going to be able to sustain a rally of more than 20 to 30 cents. That being said, I even question whether the wheat market would react to a weaker dollar at this point. Much of the May rally was predicated on dollar weakness and short covering by funds. Many shorts had gotten caught with a sizeable position and market momentum forced many of them out. Of late the wheat market has been slow to react on days that the dollar has traded lower. This tells me that the fund community is not very concerned about the threat of inflation. I believe the threat of inflation is real, but I do not believe this scenario is going to develop in the next few months.

Expect the winter wheat harvest to progress nicely. Few interruptions are expected between now and early next week. The market has not been concerned about the disappointing yields experienced thus far in the southern plains. Do not expect that to change. Harvest has begun in Kansas. Some early yields have been disappointing, but the overall quality of the Kansas crop has been favorable. The overall spring wheat crop in the US is in great shape, but some areas of western Canada are experiencing dry conditions. A few rain events are expected in portions of western Canada, but a general soaking rainfall is doubtful at this point. This issue merits some attention, but it is not severe enough at this point to stem the current down trend.

The issue of convergence in the wheat market has been addressed by a Senate Subcommittee. Their investigation determined that the lack of convergence was primarily the result of index fund buying. These findings, which are being disputed by the CME Group, could result in additional regulations and possibly a limit on the number of positions index funds can hold. A few believe this may be providing some of the current resistance. Perhaps it is, but that is not going to be the issue. Any legislation regarding this is going to take time to get in place and at this point they are still in the process of determining the proper type of legislation. Additionally, they need to get said legislation passed and implemented. This should allow index fund participants ample time to develop ways around the legislation. As a broker that deals primarily with hedgers, I need convergence to occur. However, I also like the opportunities that index fund buying provides my customers. Do not expect this to be a factor anytime soon.

Do you have a question about this article? For a personal response within 24 hours, please email brian.henry@archerfinancials.com.

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