June 11, 2013

MERCHANDISING MEETING NOTES

TURN UNCERTAINTY INTO OPPORTUNITY

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High Prices Cure High Prices:

- Intl Grains Council Executive Director Etsuo Kitahara – “Higher prices encouraged farmers globally to boost planting, increasing the amount of grain major suppliers will have available to export in the next season”, according to prepared remarks before a speech in London on 6/11.“Some key importing countries have responded by stepping up efforts to achieve a higher degree of self-sufficiency amid continuing efforts to ensure food security. If successful, this could result in smaller purchases from the world market in future years”

Farm Bill:

- Congress moved a step closer toward completing a sweeping five-year, $500 billion farm law Monday night, with the Senate approving legislation that would cut farm subsidies while expanding crop insurance.

- Federal spending on crop insurance would climb by 5 percent under the Senate bill and by 10 percent under the House bill. The government pays 62 cents of each $1 in crop insurance premium.

- Interesting to see Crop Insurance going up in spending, but then maybe not, as special interest groups that support crop ins gave politicians $52mil in the 2012 election cycle.

Livestock Demand Fundamentals from Phil Gore for Corn, SBM and DDG’s:

- Rising cash hog prices give pork producers strongest positive returns since October 2011. Cash hog prices expected to remain firm through summer, before beginning to decline as market hog supplies increase in the fall.

- Cattle feeders continue to suffer large losses.

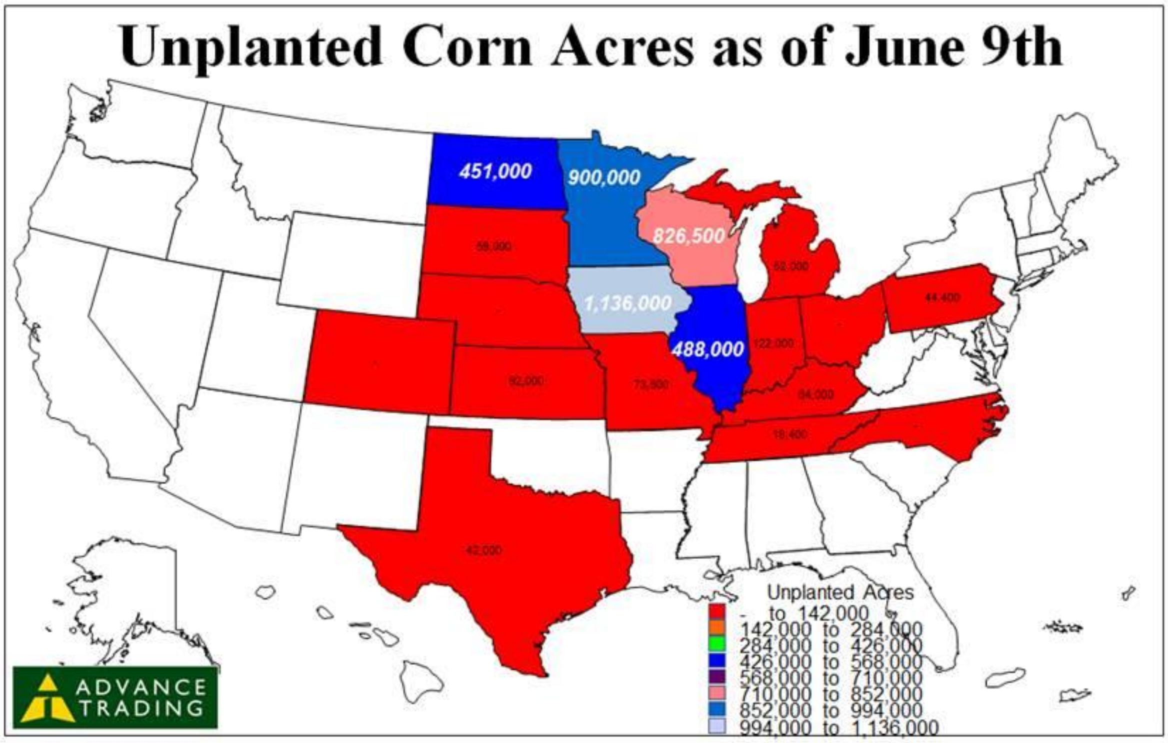
- Returns for milk producers right around break-even.

- Chicken prices ease from record high two weeks earlier, but estimated profits for producers still 98-cents per bird.

- Despite consistent estimated profits since November, broiler egg set still remains within 1% of last year. Could producers be concerned about near term feed availability??

- Falling egg prices leave Midwest egg producers with estimated losses during last two weeks.

CORN



- Roughly 4.5 mil acres left to plant on 6/9 with bulk in NW part of the cornbelt that would have increased risk of a killing freeze prior to maturity.

- Lots of ethanol plants in the north may have to learn how to utilize low test weight corn if a cool growing season or early frost occurs.

- Paranagua Brzl basis -100b/-85a vs. CIF at 102b/106a. US is $1.80/bu + more expensive. Page 11 of WFR shows many other origins that are offering corn or fd wheat at $30-50/t below where US corn would be offered. This has resulted in Dr. Shonkwiler reducing exports from 730mbu to 700.

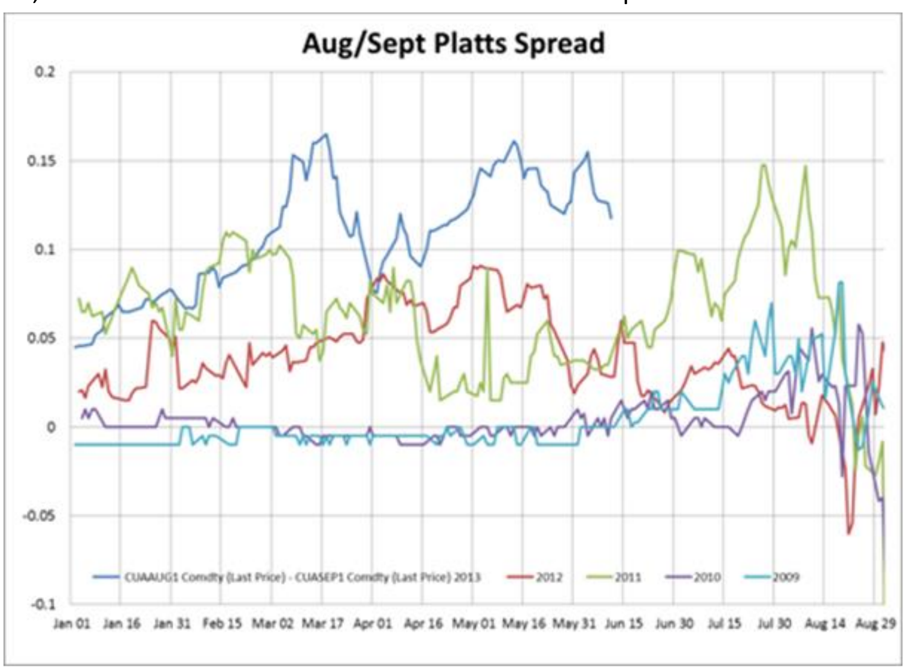
Brazilian Ethanol Lineup:

Vessel Name	Tonnage	Position	Shipper	Charter	Destination
Total:	138,785				
Port of Paranagua					
Atlantic Jupiter	10,000	In Roads	Louis Dreyfus	Green Energy	n/a
Stolt Facto	8,000	Expected	Cpa	Bunge	n/a
Chem Bulldog	7,125	Expected	n/a	n/a	n/a
Port of Santos					
Bow Atlantic	6,770	Berthed	Raizen	n/a	n/a
Fairchem Yuka	6,120	Berthed	Louis Dreyfus	Louis Dreyfus	n/a
Nordisle	3,900	In Roads	Raizen	n/a	n/a
Stolt Gulf Mirdif	20,000	In Roads	Green Energy	n/a	U.S.A.
Stolt Basuto	40,745	In Roads	Copersucar	Copersucar	U.S.A.
Chembulk Kobe	10,500	Expected	São Martinho	n/a	n/a
Chembulk Yokohama	12,625	Expected	Noble	n/a	n/a
Fairchem Birdie	8,000	Expected	Noble	n/a	n/a
Stolt Gulf Misheref	5,000	Expected	Raizen	Raizen	n/a

- ATI corn grind for ethanol estimate raised 34mbu this week on back of strong recent production #'s and good margins.

- But, margins fell hard on Tuesday as rumors of significantly increased import activity circulated (see above yellow highlite).

- So, not sure the 34mbu increase forecast holds if imports materialize in size.

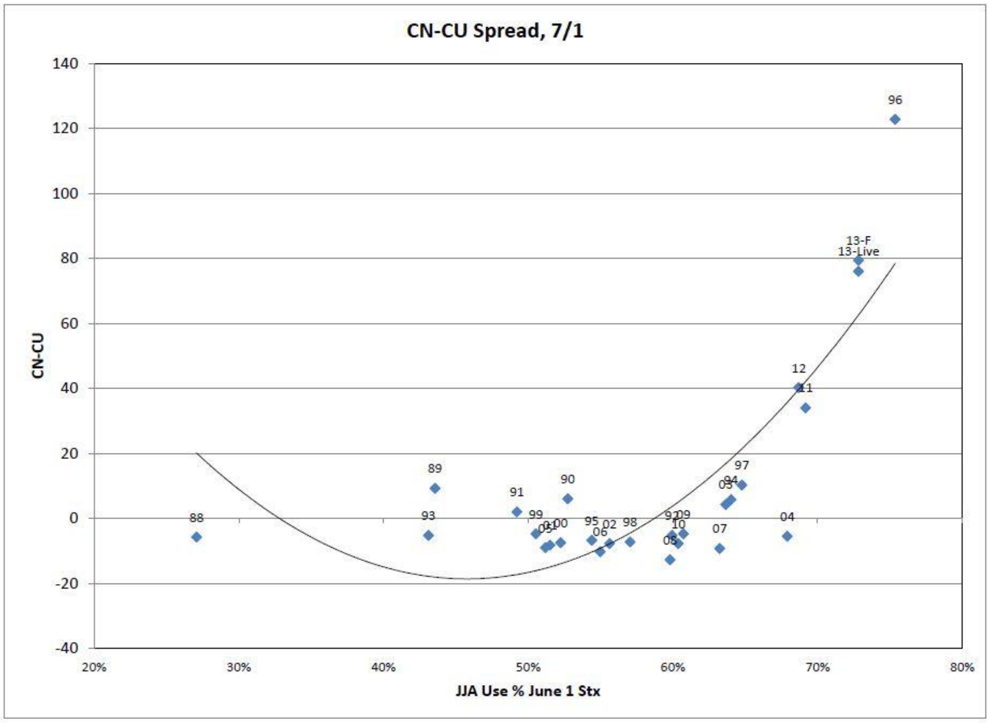


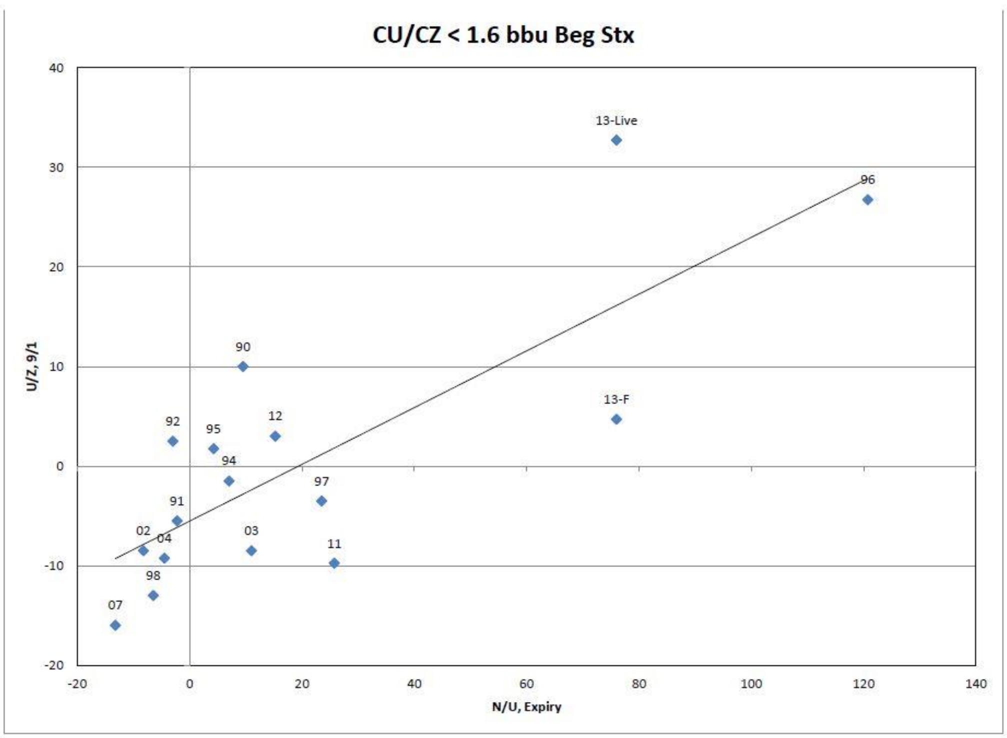
- Strength in the spread and concern over imports and excess production leads us to suggest bearspreading Platts Q/U ethanol

- ATI carry-out is now estimated at 776 mbu for 12/13. New crop production was adjusted up 5 to 13.178 bbu; c/o for 13/14 1 mbu higher at 1.479 bbu. That results in forecasted price for CZ2013 up slightly to $4.99 per bushel.

- **CN/CU and CU/CZ**—The following two graphs reflect possible scenarios for the CN/CU and CU/CZ spreads. The 1st, "CN-CU Spread, 7/1" gives historical and current/expected values for the CN/CU spread on/about July 1st. Three variables were used in the analysis: (1) June-August use expressed as a percentage of June 1 stocks; (2) SON Use as a percentage of USDA reported September 1 stocks and (3) JJA corn use expressed as a percentage of June 1 **on-farm stocks**. The R-squared for the period 1993/94 through 2011/12 was 91.5% with an 11 cent per bushel standard error. Excel fitted a polynomial curve to the regression forecast and the chart shows the current or "Live" value of the spread along with the forecast value, "13-F". Former closed at 74 cents, the estimate from the model "13-F" is 79 ½ cents, suggesting the market is appropriately priced at this time. All three variables are statistically significant and the spread appears to be strongly related to both increasing amounts of JJA use relative to June 1 stocks and the more corn that needs to be pulled out of producers hands, the stronger the inverse. FWIW, we are assuming the this summer's total use will be approximately the same percentage of the June 1 on-farm stocks as it was in the summer of 1996, or 166%. Note the spread is NOT forecast to reach the 96 high of a $1.20 premium to the CU.

- There are 2 caveats to this: 1) current crop development is roughly 2 weeks behind normal indicating that 2 weeks of additional usage must be supplied by old crop bushels or 360mbu +/-, 2) farmer holding due to adequate cash flow and previous summer rally's may result in slower marketing than the historical norm. These caveats would suggest further upside in spreads if confirmed.


CN-CU Spread, 7/1
CN-CU
JJA Use % June 1 Stx
13-F
13-Live
96
12
97
89
90
91
88
93
04
07


CU/CZ < 1.6 bbu Beg Stx
U/Z, 9/1
N/U, Expiry
13-Live
96
13-F
90
92
95
12
94
97
91
02
04
03
11
98
07

- The 2nd graph, "CU/CZ<1.6 bbu Beg Stx, 9'1" gives the value of the U/Z spread on September 1 using those years in which September 1 beginning stocks were less than 1.6 bbu. 14 years, beginning in 1990 were included in the analysis. Important variables were the expiration value of the CN/CU spread and an estimate of the amount of corn harvested by September 1. A total of the amount of corn harvested using the latest 5-year average by on approximately September 1 for AL, AR, GA, IL, IN, KY, LA, MS, MO, NC, SC, TN, TX and VA was computed and we readily admit this was not an exact estimate. For 1996, this was approximately 4.2% of total U.S. corn production. This same ratio was then applied to total U.S production for each year in the analysis and treated as the "amount of new crop corn available to the market prior to September 1". Depending on crop size, this ranged from a low of 314 mbu in 95 to as high as 500 mbu in both 2012 and 2003. The analysis yielded an R-squared of 75%. Other analysts frequently show the similarity of behavior in succeeding spreads and the strength or weakness of N/U versus the U/Z was evident in this analysis. Increasing amounts of pre-Sep 1 corn harvest impacted the spread negatively (i.e., more carry) while years of limited new crop harvest tended to firm the spread. There is only 1 year which is similar to the current one with regard to "supply tightness", the summer of 1996. Note the following table which gives estimated SON use, beginning stocks, amount harvested by September 1 (Growing Degree Days will be extremely important); total September 1 Supply and the number of weeks of use supported by this supply. Note that under the assumption of normal GGDs, 2013 should have more weeks (4.32) of available supply than did the fall of 1996 (3.87). The latter year saw the CU/CZ spread close at a near-27 cent inverse. The forecast for this year using the model assumptions is a 4 cent inverse, significantly less than Monday's 29 ¾ close.

- While the model suggest a significant easing of the spread, the slow development of this year's crop will more than likely result in a stronger inverse than suggested by the model. Plugging in an extra 360mbu of old crop demand (2 weeks of feed and eth demand) would effectively drop Sep 1 Supply from 1,336 to 976. That would drop the Wks of Use/Sep 1 supplies to 3.16 vs. 4.32 with normal development and 3.87 in 1996. Obviously the speed of development of this year's crop will dramatically impact spreads.
  September 1 Comparison: 1996 and 2013

	1996	2013-F
SON USE (mbu)	2,759	4,026
September 1 Stocks (mbu)	426	759
Harvested by September 1 (mbu)	392	577
Supply (mbu)	818	1,336
Wks of Use/Sep 1 Supplies	3.87	4.32
CU/CZ, September 1	26 ¾	4 (est)

ATI estimates.

WHEAT/CORN—There was a slight increase in both the competitiveness of Toledo SRW and KC HRW the past week. The former was priced at 87% of corn, down from 88.7% the prior week and KC HRW dropped to 93.5% from 96.8%.

EXPORTS--New crop sales were down sharply. However, thanks to some good numbers in the previous week, U.S. exporters have been selling corn for 13/14 delivery at the rate of 12 million/week, 2 higher than a year ago and nearly double the 5-year average of 6.7 mbu. Of the 191 mbu of 13/14 corn that has been sold, China and the Unknown have 116 million of the total, 20 million bushels fewer than a year ago. Non-PRC/Unknown purchases total 75 million, 6 less than in 12/13. Keeping in mind SON exports in 12/13 were a meager 220 mbu, the outlook for 13/14 at this point looks about unchanged, subject to summer growing conditions in China.

<u>Basis Levels</u>

Southeast	no significant change from last week, flat
West	strong, high priced HRW and SRW working into rations in more locations
Central	relatively low compared to east and west yet near Decatur “hard DVE” of +59

<u>DP positions</u> Recommendations run from 60% sold to 95% sold within our brokers. The job of the nearby spread is to knock the basis down to DVE and it was able to accomplish this vs. the CZ, CH, and CK. Therefore we expect basis levels to fall and convergence to occur. Question is whether a drop in demand causes convergence or dramatically inverting spreads do.

<u>New Crop Corn Spreads</u>

Lots of demand will be chasing Oct/Nov bushels: ethanol, feeding, exports, and empty bins.
We suggest locking in cz/ch or cz/ck on 25-30% of anticipated fall purchases.
This is a bit of a crop hedge against bad weather.

SOYBEANS

- Argentine truck drivers will vote to strike Monday after their request for 34% salary increase was lowered to offer of 20%.

- Argentine Farmers are also going on strike which history says will last 1 week.

Planting progress now moving along with 71% complete vs. 84 average. Trade looking for 1 mil additional acres from corn. Recent SX/CZ ratio of 2.41:1 suggests more aggressive bean planting and previous 2 years of poor corn on corn results does as well. 2-3 mil acres more would appear possible.

SX/CZ ratio over last 5 years:

ATI BALANCE SHEET CHANGES—Dr. Shonkwiler notes exports have been gyrating 2-3 mbu the past few weeks; this week they were reduced by 3 and carry-out was upped a like amount to 132 for 12/13. New crop carry-out 3 higher at 252, point estimate for SX on November 1 at $12.02, versus today's $13.19 Board close.

EXPORTS:

Aggressive South American shipping program has reduced recent U.S. inspections to less than 4 per week of late, or about 1.5 mbu below what's needed to make the USDA forecast. As a result, the ATI estimate continues to run 12-15 mbu below the USDA's 1.350 bbu forecast. Near-term, expect4-5 mbu per week with a port split of 300-350 K for the Atlantic; 1.5-2.0 for the Mississippi River and 1.5-2.0 via the Interior. Markets to watch:

- China, no further shipments expected in 12/13;
- Japan—BOY loadings of 10 mbu LY; guess is 8 this year with unshipped sales only 1 mbu fewer at 11 million;
- Other Asia—Vietnam, Malaysia, Indonesia and the Philippines—this important group of importers took 30 million during the remainder of 11/12; ATI has them in at 11 million with unshipped down 60% from14 mbu LY at this time to 6 this year; lot of container business;
- Mexico—this could be the big surprise—took 24 mbu during JJA of 11/12; unshipped sales are identical at 14 million; yet we are anticipating loadings of around 13-15 for the duration;
- Unknown destinations (discrepancy between AMS and Census)—12 LY, we expect 9 this year; unshipped sales to Unknown are down 60%, 25 versus 58 a year ago at this time.

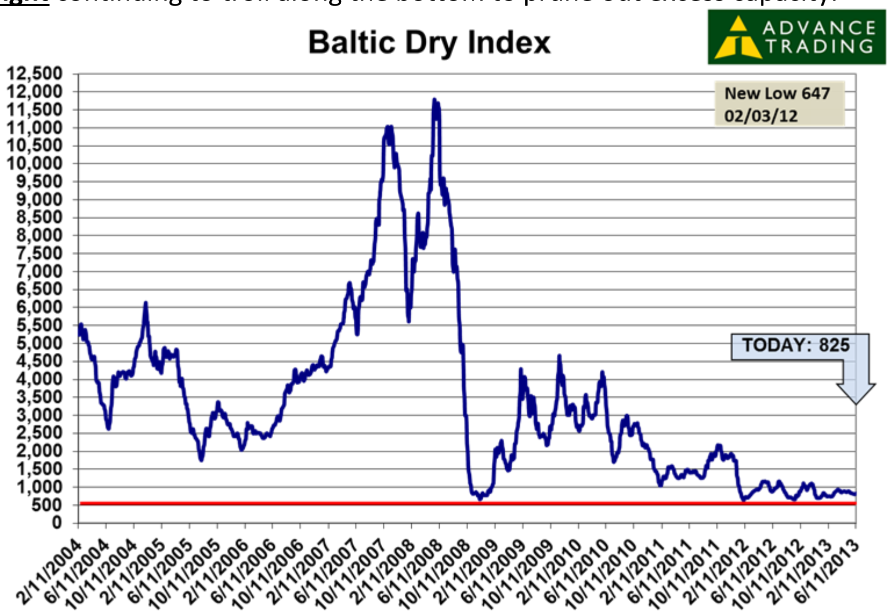
– It is early in the season, but the U.S. continues to be a strong seller of new crop beans (mostly to China/Unknown—see “Unshipped Sales and SON Export Demand” table below). 13/14 sales were 21.7 mbu this week versus 27.8 LW and 10.1 LY with 14-24 expected. Total new crop sales are 439 million, a near-35 mbu increase over the same time last year. China’s buying has moved past its 11/12 pace, 331 versus 310; sales to Unknown are down a like amount (18) and interest from all other destinations (mostly the EU and Japan) are unchanged year to year at 18 million.

<u>SOYBEAN MEAL EXPORT OUTLOOK—</u>This week solid sales numbers for both old and new crop meal. 134 K MT was reported for the former and 137 for the latter. Comparative year-ago figures were 75 and 5 and this week’s totals surpassed the respective 5-year averages for each of 108 K and a modest 30 K for new crop. Old crop sales at 9.2 MMT have surpassed the USDA’s 8.98 MST forecast number and this typically means an upward revision. Meal shipments this week, however, were a little weak at 111 K MT, below both LW and a year ago. Still the 4-week average at 138 K/week remains above the 5-year average and with unshipped sales at 1.4 MMT 5-6% above average, near-term exports are expected to be on the order of 145-150 K per week. LY, up-coming shipments averaged 154 K.

<u>DP positions</u> – Should also be 60-95% short on DP bean bushels. Tuesday’s explosion in SN/SQ illustrates the need to be long the nearby futures instead of having DP bushels in your house.

<u>New Crop spread</u>
SX/SF at 6c – Lack of farmer selling and aggressive PRC buying has kept this spread close to interest cost. Like locking in some carry at 8 and wider.

Ocean Freight continuing to troll along the bottom to prune out excess capacity.



WHEAT

Brian Basting's key fundamentals:

- ATI winter wheat crop model declines 6mbu to 1.441Bbu; HRW, 746; SRW, 497; White, 198;
- Slight reduction in U.S. winter wheat production anticipated in Wednesday's USDA report; avg. trade guess is 1.457Bbu (range 1.401-1.503) vs. 1.486 in May;
- U.S. winter wheat harvest progress at 5% vs. 37% last year and 5-year avg. of 16%--maturity of crop may accelerate next 10 days, however, due to above-normal temps;
- U.S. spring wheat crop conditions are 62% Good/Excellent vs. 645 last week and 75% last year;
- Avg. trade guess for U.S. 13/14 all wheat ending stocks is 634mbu (range 501-686); ATI at 639;
- Outstanding export sales of all wheat (combined 12/13 and 13/14) at 2nd highest level since at least 1997, which suggests a June-August shipment program of 25/week vs. 20 last year;
- SRW crop maturity running well behind 2012' suggests harvest could be 2-3 weeks later than last year

Wheat carries: Chi, KC, Mnpls

WN/WU	-8.25	KWN/KWU	-5.25	MWN/MWU	15.75
WU/WZ	-14.5	KWU/KWZ	-18.75	MWU/MWZ	-6.5

Chicago - Like hedges in the WU as deferred export demand looks poor and deferred feed demand looks poor. Poor SE weather decreasing quality of Carolina crop, but it almost all goes to feed anyway.

Kansas City – Have liked hedges in the U or Z but starting to get interesting with KWN/KWU narrowing into the 4-5 range from 8-9. More and more geography has HRW working into the feed ration given the very high western corn basis. Basis levels are very hard to own at 15-25c over DVE in central Ks and Ok or 30+ over DVE in western feedlot areas. Look to sell if you can get this type of a premium.

Mnpls – All old crop should be moved and some DP should as well given the inverse. Up to 1mil lost acres and low protein HRW concerns are supportive the spreads and supportive of MW vs. KW.

JEFF HAINLINE