Commodities: Agri Updates

01 July 2010

US Crop Acreage and Grain Stocks Summary

"Reduced corn area and inventories sets the market on fire"

- Last night's USDA Acreage and Quarterly Grain Stocks reports provided a significant boost to corn market sentiment.
- Corn prices rallied a staggering 9% overnight due to a significant reduction US corn area and inventories.
- The reports were not bullish for wheat prices, with both US wheat area and stocks coming in above expectations. Nonetheless, the US wheat market followed corn higher last night.
- Nearby tightness remains apparent in US soybean inventories, however the larger than expected US soybean area suggests big crops.
- US cotton acreage was raised this month. This puts upward pressure on production forecasts and reduces the supply shortage.

Summary

The big reduction in the US corn acreage and stocks estimates resulted in huge price gains last night. This is understandable considering the results came as a complete surprise to the market. The lower corn acreage means that production this year could fall by around 130m bushels from prior forecasts, resulting in a tightening in US ending stock estimates. Preliminary calculations suggest that the US stock-to-disposal ratio in 2010/11 could fall below the extremely tight level observed in 2006/07. Furthermore, the reduction in corn area means yield estimates become even more important, and we expect price volatility to lift as any future weather scares carry increased importance.

But the USDA reports last night were not bullish for all commodities. In fact, wheat specific news was reasonably negative in our opinion, with higher than expected area and stock estimates. The key question is, '*how much support will wheat markets draw from the bullish corn report?*

The cotton numbers were not bullish. US cotton acreage was revised higher and exceeded private trade estimates. This implies a larger than expected US cotton crop in 2010/11, but even so, US cotton stocks will remain tight.

Finally, the USDA's latest projections had a variable impact on US soybean prices. Old crop prices should be supported because of very tight supplies for nearby delivery. But the bigger than expected estimate of US soybean area (to a record 78.9million acres) should add pressure to new crop prices. The key question to ask is *'will the reduction in old crop stocks (and therefore lower carry-in stocks in 2010/11), be enough to counter the revision to 2010/11 production?'*

Figure 1: US crop area 2010/11, actual vs expectations.

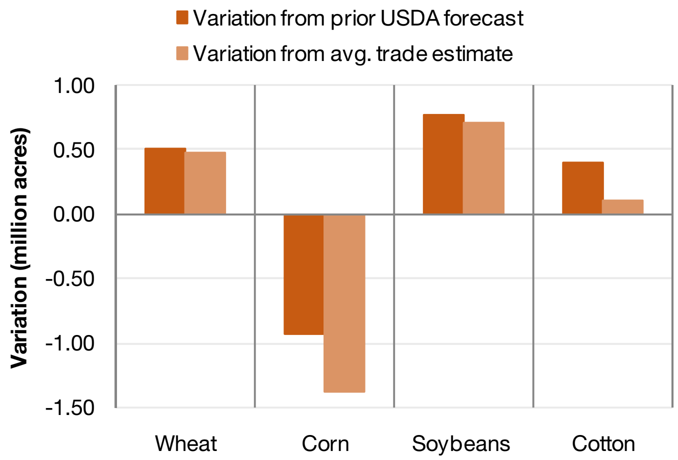
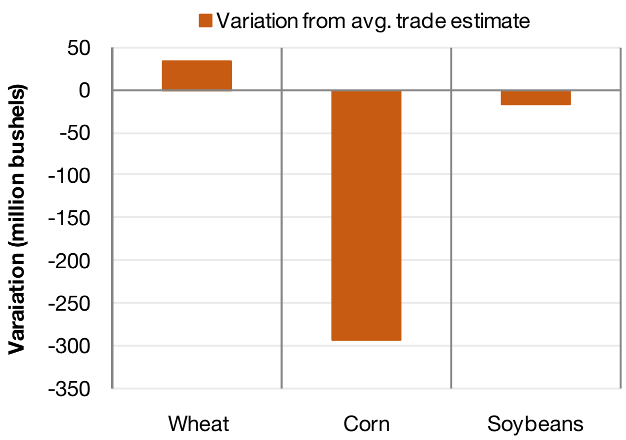


Figure 2: US grain stocks June, actual vs expectations.



Luke Mathews Commodity Strategist T. +612 9118 1098 E. luke.mathews@cba.com.au

US Acreage Report

US wheat acres revised higher...

The latest wheat area forecast provided little reason to get excited. The USDA suggested that the current wheat acreage in the US is 54.31m acres, up around ½ million from the USDA's previous forecast. It was also higher than trade expectations of 53.8m acres. This suggests there is 2-3% upside to US wheat production forecasts for 2010/11.

Nonetheless, despite the upward revision, US wheat area is forecast at its smallest area since 1971. There is a 13% yoy reduction in US winter crop area (37.7m acres) but a 5% yoy increase in spring wheat area.

...implies upward pressure on US wheat stock forecasts.

Our preliminary calculations suggest that US wheat ending stocks in 2010/11 may rise around 1.04bn bushels, up from the USDA current end of season forecast of 0.99bn bushels.

US corn area unexpectedly reduced...

US corn area was unexpectedly trimmed last night to 87.9m acres, from the previous forecast of 88.8m acres. This reduction set the market on fire, particularly considering the trade was expecting area estimates to be raised to 89.3m acres, some 1.4m acres (2%) higher than what the USDA actually forecast.

...now corn stocks may become uncomfortably tight...

Simple calculations suggest that US corn production and ending stocks could be nearly 130m bushels less than predicted by the USDA earlier this month. This would result in the US corn stock-to-use ratio falling below the level observed back in 2006/07.

...which means volatility and prices may increase.

The corn market should remain supported by these developments. Volatility may increase as any future weather scares will now have a greater influence on final crop prospects.

US soybean acreage was revised higher and exceeded private estimates.

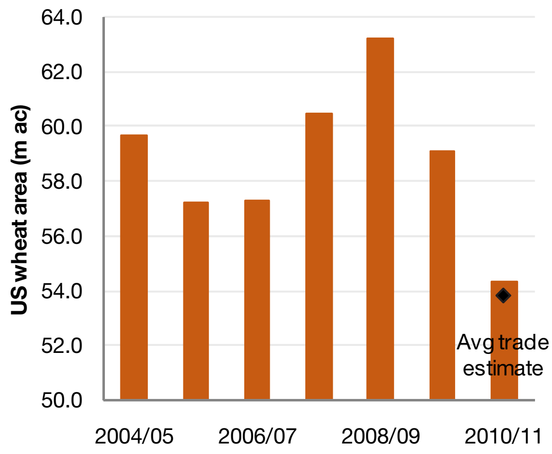
The US soybean acreage was raised significantly this month to a fresh record of 78.9m acres. The USDA's prior forecast was 78.1m acres and the market had expected an area of only 78.16m acres.

This suggests a 1% increase in potential US soybean production (based on existing yield expectations of 42.9bpa). This would put 2010/11 production close to last season's record of 3.36bn bushels.

US soybean crop conditions are good.

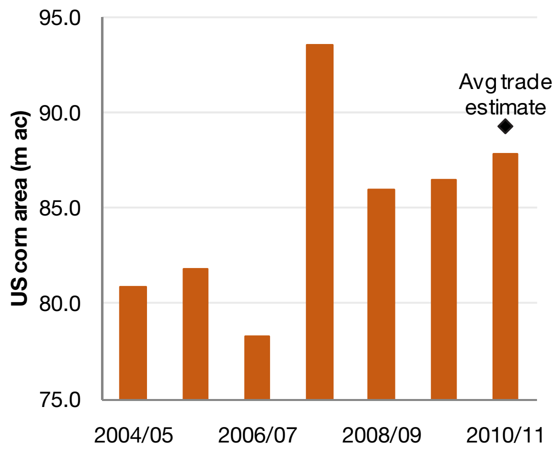
The USDA noted that early season soybean planting progressed under mostly favourable conditions this year. Crop conditions are generally rated favourably.

Figure 3: US wheat area (million acres)



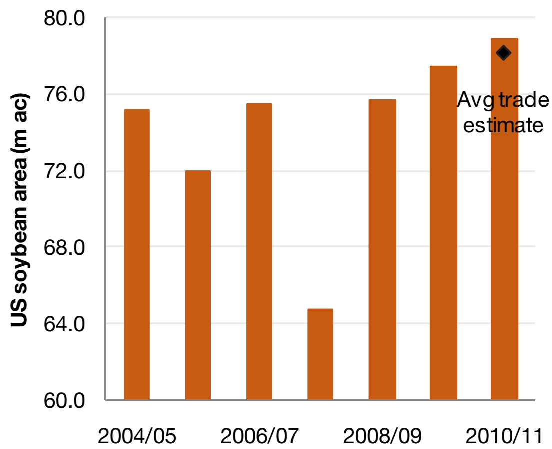
Source: USDA and CBA Research

Figure 4: US corn area (million acres)



Source: USDA and CBA Research

Figure 5: US soybean area (million acres)



Source: USDA and CBA Research

US cotton area was revised higher...

The USDA's latest US cotton acreage estimate exceeded their prior forecast and average trade estimates.

At 10.9m acres, the USDA's forecast was nearly 4% above the previous official estimate; 1% above average trade expectations; and 19% above last year's very small area. US cotton acreage this year is forecast to be the largest since 2006/07.

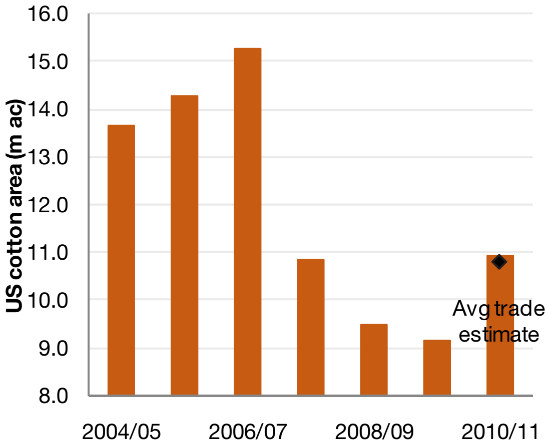
...placing upward pressure on previous production and stock forecasts...

The latest area forecast implies US cotton production may reach ~17.3m bales this year, up from the prior forecast of 16.7m bales and significantly higher than 2009/10 production of 12.2m bales.

...but stocks are still tight by historic standards.

As a result, US cotton ending stocks could climb to around 3.4m bales in 2010/11. This is up from 2.9m bales last season and the previous 2010/11 forecast of 2.8m bales. But stocks will still be significantly below the prior five year average of 7½m bales.

Figure 6: US cotton area (million acres)



Source: USDA and CBA Research

US Quarterly Grain Stocks Report

US wheat stocks are around 50% higher than year ago levels...

US wheat stocks as at the 1st June were reported to be 973.4m bushels, up 4% from average trade expectations of 940m bushels and nearly 50% higher than June 2009 stocks of 656½ m bushels.

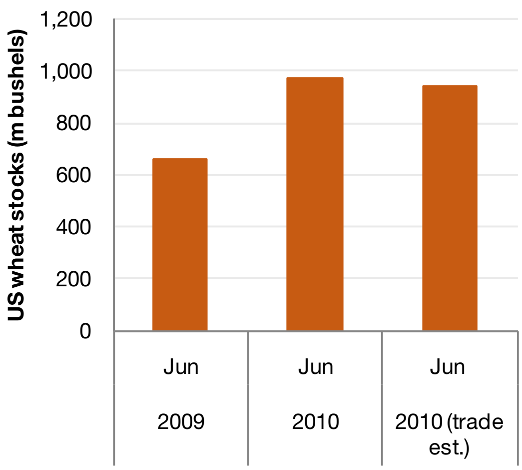
...and higher than expectations...

US wheat use (disappearance) during the March to June period this year was 383m bushels, around ½m bushels less than the same period last year.

...which should maintain pressure on prices.

Roughly 78% of total wheat stocks as at 1st June 2010 were held off-farm. This is in line with the June 2009 result.

Figure 7: US wheat stocks, 1st June



US corn stocks fell sharply below expectations...

US corn stocks (June 10) fell well short of expectations.

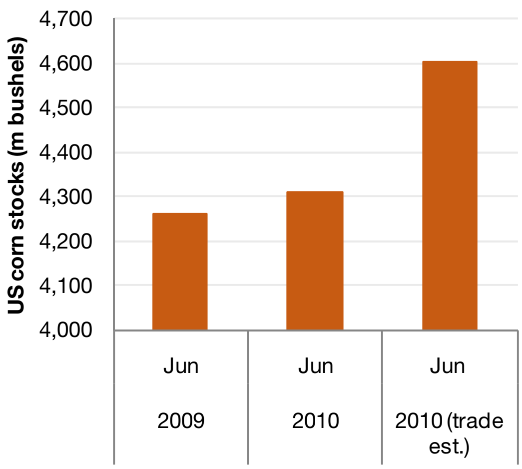
At 4.31bn bushels, stocks were only marginally higher than June 2009 stocks of 4.26bn bushels, and well short of trade estimates which averaged 4.60bn bushels.

...this should help support prices.

US corn use from March to June 2010 was 3.38bn bushels, up sharply from the 2009 result of 2.69bn bushels (Mar-Jun).

Around 50% of US corn is currently being held off farm, up from 48% in June 2009.

Figure 8: US corn stocks, 1st June



US soybean stocks were tighter than expected...

The USDA's June soybean stock estimate was supportive for old crop soybean prices, and confirms the anecdotal reports of nearby tightness in the US market.

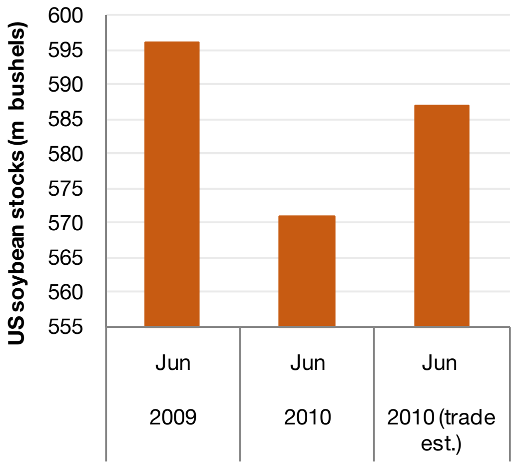
US soybean stocks at 1st June 2010 were pegged at only 571m bushels, down 25m bushels from June 2009 stocks and 3% less than average trade estimates.

...pointing to lower than expected end of year stocks...

...which will support old crop prices.

Based on these results, end of season stocks (September) this year could fall below the USDA's existing forecast of 185m bushels. The extremely tight result of 138m bushels observed in 2008/09 may be achievable if late season demand remains strong.

Figure 9: US soybean stocks, 1st June



Research

Commodities		Telephone	Email Address
David Moore	Base & Precious Metals, Oil	+612 9118 1099	MoorDa@cba.com.au
Luke Mathews	Agri Commodities	+612 9118 1098	luke.mathews@cba.com.au
Lachlan Shaw	Iron Ore, Coal, Steel, LNG	+613 9675 8618	lachlan.shaw@cba.com.au

Economics		Telephone	Email Address
Michael Blythe	Chief Economist	+612 9118 1101	michael.blythe@cba.com.au
Michael Workman	Senior Economist	+612 9118 1019	michael.workman@cba.com.au
John Peters	Senior Economist	+612 9117 0112	john.peters@cba.com.au
James McIntyre	Economist	+612 9118 1100	james.mcintyre@cba.com.au

Fixed Income		Telephone	Email Address
Adam Donaldson	Head of Debt Research	+612 9118 1095	adam.donaldson@cba.com.au
Philip Brown	Fixed Income Quantitative Strategist	+612 9118 1090	philip.brown@cba.com.au
Michael Bors	Credit Research Analyst	+612 9118 1108	borsma@cba.com.au
Steve Shoobert	Credit Research Analyst	+612 9118 1096	steve.shoobert@cba.com.au
Winnie Chee	Securitised Product	+612 9118 1104	winnie.chee@cba.com.au
Tally Dewan	Quantitative Analyst	+612 9118 1105	tally.dewan@cba.com.au
Kevin Ward	Database Manager	+612 9118 1960	kevin.ward@cba.com.au

Foreign Exchange		Telephone	Email Address
Richard Grace	Chief Currency Strategist	+612 9117 0080	richard.grace@cba.com.au
Joseph Capurso	Currency Strategist	+612 9118 1106	joseph.capurso@cba.com.au
Sara Hoenig	Economist	+612 9118 1107	sara.hoenig@cba.com.au

Delivery Channels & Publications		Telephone	Email Address
Monica Eley	Internet/Intranet	+612 9118 1097	monica.eley@cba.com.au
Ai-Quynh Mac	Information Services	+612 9118 1102	maca@cba.com.au

New Zealand		Telephone	Email Address
Chris Tennent-Brown	CBA NZ Economist	+64 9374 8819	chris.tennent-brown@asb.co.nz
Nick Tuffley	ASB Chief Economist	+64 9374 8604	nick.tuffley@asb.co.nz
Jane Turner	Economist	+64 9374 8185	jane.turner@asb.co.nz
Christina Leung	Economist	+64 9369 4421	christina.leung@asb.co.nz

Sales

Institutional		Telephone
Syd	FX	+612 9117 0190
		+612 9117 0341
	Credit	+612 9117 0020
	Japan Desk	+612 9117 0025
Melb		+613 9675 6815
		+613 9675 7495
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Equities	Telephone
Syd	+612 9118 1446
Asia	+613 9675 6967
Lon/Eu	+44 20 7710 3573
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Corporate	Telephone
NSW	+612 9117 0377
VIC	+612 9675 7737
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Metals Desk	+612 9117 0069
Agri Desk (Corp)	+612 9117 0157
Agri Desk	+612 9117 0145