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Weekly Outlook: Corn Prices Fade as Supplies Expected to Remain in Surplus

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Corn futures prices increased about \$0.90 per bushel from mid-June to mid-July. The increase was driven by a combination of a smaller-than-expected USDA estimate of June 1 stocks and production concerns stemming from record June rainfall in much of the eastern Corn Belt.

Over the past two weeks, corn futures prices have declined nearly \$0.65 per bushel as production concerns have subsided. Expectations are for corn supplies to remain in surplus during the 2015-16 marketing year. Prices, then, will remain at the current low level unless there is some evidence that the supply and demand balance is potentially much tighter than currently expected.

A slightly tighter supply and demand balance for the 2015-16 corn marketing year could be generated by a smaller carryover of old crop corn than currently projected. Based on the current pace of ethanol production, for example, the use of corn for ethanol production during the current marketing year (ending August 31) could be about 10 million bushels more than the current USDA projection of 5.2 billion bushels. Similarly, exports could be slightly larger than the projection of 1.85 billion bushels if Census Bureau export estimates for June, July, and August exceed the USDA export inspection estimates as was the case in the first nine months of the marketing year. However, for carryover stocks to be lower than the current projection of 1.79 billion bushels by enough to meaningfully alter the 2015-16 supply and demand balance would require larger than expected feed and residual use of corn during the final quarter of the marketing year. The USDA's projection of 5.3 billion bushels of feed and residual use for the year implies fourth quarter use of 522 million bushels. That is 111 million bushels more than use of a year ago and the largest fourth quarter use since 2009. Use is expected to exceed that of a year ago due to an increase in pork and broiler production and small increases in the number of dairy cows and the number of beef cattle on feed. The number of layers has been sharply reduced due to bird flu. Fourth quarter feed and residual use will be revealed with the estimate of September 1 stocks of old crop corn to be released on September 30 and a surprise is always possible.

A tighter supply and demand balance could also result from larger than expected consumption during the year ahead. Such a development would obviously take time to unfold, but opportunities for consumption to exceed the current projection appear to be limited. The USDA currently projects 2015-16 marketing year

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exports at 1.875 billion bushels, 25 million more than projected for the current year. However, interest in U.S. corn is currently limited by abundant supplies of low-priced South American corn. As of July 16, the USDA reported that only 152 million bushels of U.S. corn had been sold for export during the upcoming marketing year. On the same date last year, outstanding sales of new crop corn totaled 232 million bushels.

Corn used for ethanol production is projected to increase by 25 million bushels during the upcoming marketing year. The expected increase in ethanol production and corn consumption reflects expectations for growth in domestic gasoline consumption. Growth beyond that, however, will be limited by the 10 percent ethanol blend wall and the very slow pace of growth in the consumption of higher ethanol blends. In addition, ethanol exports are already large so that growth potential is likely limited.

The USDA projects feed and residual use of corn to decline by 25 million bushels during the year ahead. Consumption should be supported at a relatively high level due to larger livestock inventories. However, hog producers have indicated that they will reduce the number of sows farrowed during the last half of 2015 and growth in the other animal sectors will likely be very modest.

The most obvious opportunity for a tighter corn supply and demand corn balance during the year ahead would come from a smaller than expected harvest. The USDA's *Crop Production* report to be released on August 12 will contain the first survey-based yield and production forecasts for the 2015 crop. Expectations for the U.S. average yield projection are in a wide range, but have generally increased over the past two weeks as weather conditions have become less stressful and as crop condition ratings have stabilized at a high level. The average yield expectation appears to be near 165 bushels, 1.8 bushels less than projected in the July 10 USDA WASDE report. The August production forecast will also reflect the estimate of harvested acreage, but a large change from the June acreage forecast is not expected. Based on the projection of 81.1 million acres harvested for grain, a yield of 165 bushels would result in a crop of 13.38 billion bushels, about 150 million bushels less than projected in the July WASDE report. Still, if 2015-16 marketing year consumption is near the current USDA projection of 13.735 billion bushels, year-ending stocks would be abundant at about 1.45 billion bushels. On the other hand, a yield forecast of 161 bushels or less would likely be sufficient to push prices back to the mid-July highs.

Recent corn price declines indicate that the market is removing the production risk premium from the price structure in anticipation of another year of surplus. The question is whether that removal is premature.

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