Corn

Grains in general experienced one of the more memorable third quarter market moves in recent memory. Quarterly stocks reports released September 30 went a long way in explaining that move. But regardless of the reasons, corn producers were offered some improved pricing opportunities. Export sales were the highlight of this time period with reportable export sales (those over 100,000 mt) occurring nearly every business day through the month of October. Most of these sales were booked to China directly or to "Unknown" destinations, which is many times believed to be China. Notably, current United States Department of Agriculture projections through the September World Agricultural Supply and Demand Estimates (WASDE) report estimated total Chinese corn imports of 7.00 mmt (from all originations) while total sales booked from the U.S. alone have already eclipse that. This situation underscores how vital it will be for those sales to reach the actual shipment stage where cancellation ceases to be a possibility.

Basis levels for the AgCountry service area also benefitted from these sales due to the territory's proximity to Pacific Northwest ports. Freight values for the BNSF railroad reflected this, with secondary market values trading substantially over tariff. That's a huge contrast to the past two years when freight values were modest to cheap. As shipments of the above-mentioned sales continue to occur, it's likely that producers located in the AgCountry territory will continue to run at better than historical levels.

While much of the fundamental focus in markets surrounds the monthly WASDE reports issued by USDA's Economic Research Service, the National Ag Statistics Branch of USDA issues a quarterly grain stock report. After release, this information is incorporated into the monthly WASDE as a way of "truing up" balance sheets. Note that while corn used for ethanol and corn sold into export markets is fairly easy to measure and reported quite regularly, the quarterly stocks report is really the only way to quantify feed usage. There is no survey to report this directly. Why does this matter? Because the September 2020 Quarterly Stocks report for corn is the official final carryout number for the 2019 corn crop. This last official "true up" came in at 1.995 billion bushels, which is well below the 2.25 billion bushels the trade was expecting and well below the 2.25 USDA itself had published two weeks ago. USDA also took the unprecedented step of revising June 2020 corn stocks 204 mbu lower - the bulk of which came out of on farm stocks.

So what does that mean? Due to the survey data mentioned above, there are two options: The first is that feed demand far exceeded the 5.6 billion bushels USDA was estimating. That number was already historically high, but given livestock numbers, not unjustified. The pullback in ethanol production would also have reduced DDG production and opened the door to different ration formulation that was probably not anticipated. The second possibility is that the 2019 corn crop was not as large as originally stated, although USDA actually revised this number ever so slightly higher based on other data. Test weight issues could also have factored into this.

There are a million different arguments that can be made statistically as far as what happened. However, in terms of price outlook, it doesn't particularly matter why. The trade is now aware that either we never had as much as we thought, or demand was better than anticipated. The spread action through the third quarter was indicative of as much, even if it seemed odd at the time. The point is that with this new information, the corn market remains well supplied, but likely not as burdened as previously thought. Therefore, it is reasonable to expect that we will continue to see this market better supported in the near to intermediate term than we did through much of 2020.

Soybeans

Soybeans were the major leader of the 2020 third quarter grain rally, for very similar reasons to that of corn. Export sales through August were simply phenomenal. When you add to that the fact that August was dry in much of Iowa and portions of Illinois where a very large Derecho weather impacted as many as 10 million acres in those states, the market added significant premium. This counter seasonal rally also resulted in moderate market inversions that we hadn't seen since the beginning of the trade war two years ago.

The combination of counter seasonal rallies and the collapse of carry is a strong signal that the perceived supply of soybeans is shrinking. That was confirmed by the September 30 quarterly grain stocks report which reflected a 2019 carryout of 523 mbu. That's well below the 575 mbu projected in the September WASDE report. Further, USDA revised the June 1 stocks data by 4.6 million bushels, which is the second largest revision to June 1 stocks, behind the 6.9 mbu revision they posted in 2019. The cause of that difference is a little harder to pinpoint but will probably be a combination of crop size and "residual."

Very similar to corn, soybeans continue to benefit from the resumption of export sales, but strength also reflects the very heavy fund short position that was maintained and built for months prior to the August rally. As of this writing, that short has been erased and subsequently reversed. While the Commodity Futures Trading Commission (CFTC) data reporting these positions lags, its possible that fund buyers are now holding an all time record long position in soybeans. That presents a two-fold challenge for producers who are looking to price. The first is, with such heavy length, funds will need continued encouragement to further build. It easy to often say if funds hold this many contracts, they can't keep going. However, history would tell us that's not necessarily true, nor does it mean they would have to liquidate immediately. That leads us to the second challenge. How strongly do fund traders feel about defending this long position? With this much money at stake, it seems unlikely they'd give up quickly, leaving some credence that the lows are behind us at least for the short term.

Why only the short term? It's important to remember that unlike corn, soybeans have a major global competitor in South America. As October starts, that country is just gearing up to begin planting for their major production areas. While the U.S. has a lock on the global export market roughly the last half of July through January, once February comes, price direction will be far more dependent on what the South American crop looks like. Brazilian weather conditions as of the beginning of October were drier but forecasts were beginning to call for increasing rains. Currency values will also come into play, although the trend the past two quarters has been for a strengthening Real compared to the Dollar, which also is favorable to U.S. exports.

Wheat

Wheat was no exception to the widespread surprise data issued in the September 30th Stocks Report, although due to timing, it has a slightly different implication. Wheat, along with other small grains, has a marketing year end of June 1, meaning this is really quarter one data for this commodity. Regardless, supplies here were less than expected, coming in at 2.159 billion bushels compared to the 2.242 billion the trade was expecting. That's an 83 million bushel difference very early in the marketing year. It's also 187 million bushels less than what was seen the year prior.

Notably, USDA revised the June 1 stocks number lower by 15 million bushels, which changes the carry in for the 2020 crop.

While Sept 30th stocks data sometimes gets buried for wheat because of the year end data on corn and soybeans, USDA also publishes a separate Annual Small Grain Summary, which is total wheat production for the 2020 crop year (very similar to the January Crop Production report for corn and soybeans). In it, USDA provided some further positive news, although the wheat market remains pretty comfortable in terms of stocks to use.

In the Small Grains, USDA's All Wheat production number was 1.826 billion bushels - 15 million bushels less than the trade expected and 12 million bushels less than the August NASS estimate. The entirety of that difference comes from smaller than expected winter wheat production with both Hard and Soft winter classes coming in below prior estimates. AgCountry's LSA is primarily made up of Spring and Durum classes, although areas of Wisconsin will fall into the winter wheat column. Spring wheat production actually came in 9 million bushels higher than the trade had expected, and 25 million bushels more than the 2019 crop. Durum production came in at 6.9 million bushels, slightly higher than trade estimates and well above the 2019 crop.

As far as what this means for wheat producers, outside investment money and strength in corn and soybeans is likely to continue providing some support for wheat prices. That said, we continue to see very unusual price spread action with Chicago soft wheat markets trading 30 to 50 cents over Minneapolis. That trend, while unusual, appears unlikely to change near term as fund advisors and traders prefer the more liquid Chicago market. Basis levels for spring wheat are also more variable than usual, reflecting local conditions and differing rail markets. Producers would benefit from looking at different buyers before contracting.

Cattle

Cattle markets appear to be recovering nicely, with the third quarter of 2020 showing signs that the U.S. cattle herd is cycling lower. Semi-annual inventory numbers in July showed All Cow and Heifer numbers at 41.4 million - slightly below the number posted for July 1, 2019. Beef replacement heifers were even with the year before, indicating there isn't a ramping up of heifers being held for replacement just yet. Further, that same inventory report showed the 2020 calf crop at 35.8 million head, down 1% from the prior year.

These numbers back up some of the strength in both feeder cattle and live cattle futures, although some of the strength is also due to a correction of the overdone COVID-induced lows seen in late March and

early April. For reference, as of the first week of October, November Feeder cattle futures are trading in the low $140's/cwt, off the early April peak, but still at the highest levels since late 2018. On a 600 pound calf, that represents roughly $132/head of additional revenue than that same calf would have produced just six months ago.

One note on the September Cattle on Feed data. For Minnesota, the September COF report showed on feed numbers coming down from the previous month, although the feedlot inventory in Minnesota is minimal in the national picture. Placement data showed many of those calves are likely being replaced, with placements during August up. South Dakota lots are showing similar seasonal tendencies, although its likely going to be the November Cattle on Feed report before we see significant restocking.

USDA WASDE numbers reflect beef production peaking in the fourth quarter of 2020, although some of that is seasonal. Projections for quarter one and two of 2021 show less production than the same period of 2020, which would follow largely with the on feed data mentioned above. USDA projected prices for the first half of 2021 are very similar to current levels.

Pork

Pork markets have had a whiplash-like reaction over the past six months with U.S. plant shutdowns in the spring creating a backlog and extremely strong exports in the fall. That has cleared the backlog and is now pulling some hogs forward. The move was so sudden, in fact, that not all industry experts are totally in agreement as to how this played out fundamentally. The fact remains: lean hog futures, cash markets, and total cutout values have skyrocketed. USDA reported cash hog values for the first week of October were just short of $65/cwt, higher than 2019 and higher than the five-year average by about $9/cwt. Contrast this with cash hog values that were nearly $50 short of the five-year average just four months ago and its easy to understand why the industry seems unsteady right now.

The move isn't likely to be explained in the space here. What the industry does know is that hog weights are coming down, and plants continue to run at full speed (at least full speed within the new social distancing confines). Production doesn't appear to be keeping up with an export market that's on fire, particularly since Germany (one of the top EU producers and major exporter to China) was forced out of the market by positive African Swine Fever tests in wild boars. The U.S., along with other markets, will attempt to fill that gap but processing capacity remains the lynch pin. USDA September WASDE reports showed projected pork exports of 7.5 million pounds, the same as August but up 1.2 million pounds from what shipped in 2019. Exports are expected to continue rising in the first half of 2021. Because of the bottleneck nature of processing and somewhat unsteady trade relations plus an election, it's likely cutout values will be volatile, which in turn may lead to some cash market volatility. Producers who have contracts coming up for negotiations may be put off until expiration, buying processors some time to see if things cool down.

Dairy

Dairy markets have moderated after a good summer with USDA raising its estimate for milk production due to better than expected production growth in September. Class III price projections for 2020 in the September WASDE declined by 15 cents due to softer cheese and whey markets. The All Class forecast fell to $17.75, down 20 cents. Regardless, milk and product price forecasts for 2020 remain higher than what was seen in 2018 and 2019, allowing for some healing of balance sheets to take place. Outlooks

for the first half of 2021 reflect the same market conditions as seen in the last half of 2020 with soft Class III and All Class markets with some strength in Class IV due to butter prices.

Looking at longer-term trends, the semi-annual Cattle Inventory report released in late July did show some additional cow retention, although that same thought was not yet applying to dairy replacement heifers. Show prices remain at current levels. That number may slowly creep higher, but prices currently do not have many analysts projecting major expansion in the next six month.

Sugar

Annual beet lift has officially opened in the AgCountry LSA with few major problems reported. Weather forecasts for the first two weeks of October called for dry conditions that should allow for a much smoother lift season than what was experienced in the fall of 2019. So far, while early, reported beet tonnage looks good, although its early to tell on the sugar content.

USDA's September WASDE report made some reporting adjustments for the Tariff Rate quotas that are more bookkeeping than market altering. Because of shipment delays due to COVID, USDA will give market participants an extra month to report shipments of sugar entering under the Quota, but that was largely already reported by other outlets. Total U.S. sugar production was raised by 27,095 tons, although production from beet sugar was reduced by 33,889 short tons. The difference was made up by big increases in cane sugar production out of Texas. Regardless, the stocks to use ratio fell on strong consumption, indicating price support going forward.

Dry Beans

Dry bean markets were fairly quiet and steady for most of the third quarter - although some pickup in activity was seen in September as uncontracted new crop production began to roll in. Prices in general remain strong on the dealer side, but some slight softness is showing up to the grower, which is unsurprising this time of year. August Crop production estimates from USDA showed estimated yield for all types in North Dakota at 1,800 pounds/acre, up 400 pounds from last year. Projections for Minnesota were up 440 pounds/acre to 2,480. Overall, the market appears steady to firm.

Ethanol

The ethanol market has finally found some sort of equilibrium after the crash seen in quarter two. Total U.S. gasoline consumption remains depressed due to social distancing directives and increased work from home policies. At present, U.S. gasoline consumption is down about 10% compared to last year and seems unlikely to change. Ethanol demand is down correspondingly.

The industry outlook remains depressed with margins struggling to do more than cover operating costs. The reduction in corn supply in the September 30th WASDE report offers little hope that corn prices will come down. That said, margins are much improved from February, March and April. It seems unlikely at this point that plants that were pulled offline during that timeframe will be returning soon and realignment of that industry appears underway.

Ethanol remains a political wild card. During September, the Trump administration announced they have denied hardship waivers to 54 petitions, saying the petitions did not meet the bar for proving

hardship. This is a change from policy in the past few years and comes after a 10th Circuit Court opinion that found EPA had misused the waiver program previously. Future policy, however, remains up in the air with little regulatory certainty.