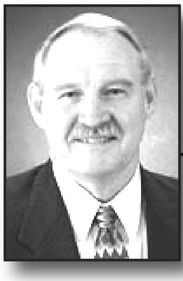
Corn Demand Not Improving



grain outlook

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The corn market continues to struggle with a number of negative fundamental factors. As a result, prices continue to hover just above marketing year lows.

The most significant fundamental factor influencing corn prices is the sharp decline in ethanol prices. Over the past 15 months, the price of corn has been highly correlated (more than 90 percent) to the price of ethanol. The price of ethanol (December 2008 futures) has declined from near $2.35 per gallon in late August 2008 to the current price near $1.67 per gallon. The average price of ethanol at Iowa plants reached a high of $2.82 on July 3, 2008, but was reported at $1.57 per gallon on November 14. The decline in ethanol prices has followed the decline in unleaded gasoline prices which has followed the decline in crude oil prices. The wholesale price of unleaded gasoline has declined by about 40 percent since early October. While ethanol production will likely continue to expand as new capacity is completed, that expansion will only occur at relatively low corn prices as long as ethanol prices are low.

Concerns about feed demand for corn have also emerged as livestock prices have declined. February lean hog futures, for example, reached a high near $85 per hundredweight in late June 2008. That price was still near $80 when the financial crisis began to unfold in early September, but is currently near $62. Live hog prices at terminal markets have declined from the mid $60 level in August 2008, to the current level in the upper $30 range. Some further liquidation of the breeding herd may result from these lower prices, even as feed costs have declined.

February live cattle futures prices peaked near $117 per hundredweight in late June 2008, were near $106 in early September, and are now near $89. Cash market prices exceeded $100 in July, but are currently near $89. The USDA estimates that the number of cattle in feedlots with capacity of 1,000 head or more has been less than that of a year ago since April of this year.

Corn export demand was especially strong during the 2007-08 marketing year. Exports reached a record 2.436 billion bushels in the face of record high corn prices. Demand was supported by two consecutive years of a shortfall in world wheat production, growing world economies, and expanding livestock production. The relatively low value of the U.S. dollar also made U.S. corn very competitive with corn from other exporters.

That strong export demand has given way to a much weaker scenario for the 2008-09 marketing year. Record large wheat and coarse grain crops in the rest of the world, slowing economic growth, and a stronger U.S. dollar all contribute to that weaker demand scenario. The USDA projects exports during the current year at a 4-year low of 1.9 billion bushels, 22 percent below the record shipments of last year.

There are three sources of information to help monitor the pace of exports and export sales as the marketing year progresses. These include the weekly USDA export inspection report released on Monday, the USDA's weekly report of export sales released on Thursday, and the Census Bureau's monthly report of exports released with about a six-week lag. The Census Bureau estimates become the official estimate of exports carried in the USDA's supply and demand balance sheets.

Comparing the pace of exports during the current year to previous years can be somewhat misleading since the seasonal pattern of exports is not consistent from year to year. Last year, for example, exports were very large in the first half of the marketing year and relatively small in the last quarter of the year. Similarly, the seasonal pattern of sales varies from year to year. Even with these caveats, the current pace of exports and export sales are unimpressive. Through the first 10.5 weeks of the 2008-09 marketing year, export inspections lag the total of a year ago by 38 percent. Through November 6, total export commitments lagged those of a year ago by 43 percent. To reach the 1.9 billion bushels for the year projected by USDA, new export sales need to average about 29 million bushels per week. The average for the three most recent reporting weeks was 16.3 million. Finally, the Census Bureau estimate of September 2008 corn exports was 20 percent below that of September 2007. None of the large importers of U.S. corn (Japan, Taiwan, South Korea, and Mexico) are buying at a faster pace than last year.

Many observers continue to be optimistic that corn prices will increase as the marketing year progresses. At this point, it is not clear where the fundamental support will come to generate such a recovery. At the risk of sounding like a broken record, a recovery in financial markets and energy prices will likely be required to generate higher corn prices in the near term. Δ