Crop Price Outlook: The View From Milan

DR. DELTON GERLOFF

MILAN, TENN.

Dr. Gerloff is well known for his expertise in crop production economics and is a frequent author and expert in media outlets, including Mid-America Farmer Grower. During Tour Q – Risk Management – at the University of Tennessee Milan No-Till Field Day Gerloff will summarize how the market arrived at its current level plus peer into price possibilities for this fall and winter. Visitors will hear first-hand how Gerloff uses the latest information for various pricing tools to compare possible marketing scenarios for the 2008 crop.

Unprecedented crop price movements in 2008 have generated both opportunities and challenges for Tennessee and other Mid-South farmers. From cotton's short-lived price rally in early March to record high grain prices this spring, 2008 has so far been filled with market uncertainty. Many questions have surfaced regarding this year's market:

1. Why have prices rallied to the extent they have?
2. Will these prices fall or are we at a "new price plateau"?
3. How can farmers capture the current prices for this fall's harvest?

Fundamentally, prices reflect a demand driven market rally that began almost two years ago. This rally began in the corn market, as the agricultural industry realized there would be a substantial shortfall of corn in the U.S. in 2007 unless corn acreage increased dramatically. The shortfall was a result of strong export demand and an increasing off take of corn into the ethanol industry. Corn prices rose during the winter of 2006/07 and over 15 million acres switched over to corn in 2007, with most of the acres coming from soybeans. With lower soybean production, ending stock projections for U.S. soybeans fell well below 200 million bushels for the 2007/08 marketing year. As soybean stock levels dropped, export demand continued to be very strong, and the ethanol industry expanded capacity again. All these factors combined in the winter of 2007/08 to establish record high prices for wheat, soybeans, and corn.

As land rents and input prices increased this past year, the cost to grow row crops rose dramatically. In the short run, however, the cost of growing a crop has little to do with how it is priced. A return to output prices of only a couple of years ago could put farmers in a net loss scenario based on the level of current input prices.

There is no guarantee that output prices will stay at their current levels. In fact, substantial price rallies have historically been short lived and may only provide higher price levels for two to three growing seasons. Additionally, input prices do not necessarily drop when crop prices decline. A cost/price squeeze could result at the end of this price rally.

Whether a result of higher transportation cost, commodity fund investments, or local buyers passing on more market risk to farmers, basis levels have weakened dramatically over the past two years. As a result, traditional marketing tools have become very risky or expensive, compared to the past. Option premiums have increased, along with margin requirements on hedging accounts. Cash forward contract prices have dropped well below harvest futures prices for grains. These factors make marketing decisions more challenging for crop farmers. Δ

Dr. Delton Gerloff is professor, extension programs in farm and financial management and crops marketing with the University of Tennessee at Knoxville.