



USDA's Supply Shockers Present Dilemma for Corn Market

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The Agriculture Department's quarterly estimates of U.S. corn inventories have become a source of substantial surprises for the grain market.

Dating from March 2010, 11 of the past 13 quarterly stocks estimates have deviated from expectations by enough to generate large price movements. During that period, USDA stock estimates have been both much larger and much smaller than generally expected.

Market participants form expectations for the quarterly stocks estimates based on the level of stocks at the beginning of the quarter and a projection of use during the quarter. Exports and domestic processing uses of corn during the quarter can be projected fairly closely.

Projections of feed and residual use of corn are based on a variety of factors, including historical use, the most recent levels of use, livestock numbers, livestock feeding profitability, and likely levels of feeding of other commodities.

Surprises in the USDA estimates, then, mean that feed and residual use during the quarter deviated from market expectations. Those deviations, in turn, alter expectations for feed and residual use for the remainder of the marketing year and the likely level of stocks at the end of the marketing year.

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While it should be expected that the market will not always correctly anticipate USDA estimates, the recent pattern of large and seemingly alternating direction of the surprises in the quarterly corn stocks estimates is problematic.

One of the results is a pattern of feed and residual use of corn that varies considerably from quarter to quarter and from year to year. That pattern can make it difficult to anticipate future use and can result in wide swings in projections for feed and residual use for the marketing year, or estimates for the previous year, in the case of the September 1 stocks estimate.

Surprise number sends corn futures tumbling

A number of examples can be cited, but consider the most recent experience. The smaller-than-expected estimate of stocks as of September 1 resulted in the estimate of feed and residual use for the 2011-12 marketing year being increased by 162 million bushels.

The smaller than expected December 1 stocks estimate resulted in the forecast of 2012-13 marketing year feed and residual use being increased by 300 million bushels in the USDA's February Supply and Demand report.

That forecast was increased by another 100 million bushels in a rare change in the March report. Presumably, the projection will be reduced sharply in the report scheduled to be released on April 10.

The difference between the USDA's March 1 stocks estimate of 5.399 billion bushels, released March 28, and the average trade guess was about 370 million bushels, one of the largest differences in the past 30 years.

Old-crop corn futures declined by more than 80 cents per bushel in the initial reaction to the larger-than-expected estimate (on April 1, May corn futures on CME Group settled at \$6.42 ¼ a bushel, down 93 cents, or nearly 13%, in the two trading days since March 27).

Questions over June 1 stockpiles

The dilemma now, however, is what to expect for the June 1 stocks estimate. The implied rate of feed and residual use of corn in the first half, and particularly in the second quarter, of the 2012-13 marketing year is quite low.

The slow rate of feed and residual use does not seem consistent with livestock numbers, a sharp reduction in the production of distiller's grains, and the implied negative feed and residual use of wheat during the same six-month period.

March 1 wheat stocks also exceeded market expectations by a large margin. Experiences over the past three years suggest that the June corn stocks estimate may "correct" for some of these apparent inconsistencies.

If that turns out to be the case, the magnitude of the current price weakness may not be justified. Because the reasons for the sometimes-large deviations between USDA estimates and market expectations are not obvious, the June estimate may or may not provide another surprise.

While not normally an issue, the March 1 soybean stocks estimate was also a surprise. At 999 million bushels, the estimate was about 50 million bushels larger than the average trade guess.

While the USDA no longer estimates quarterly feed, seed, and residual use of soybeans, the stocks estimate implies negative use in that category for the quarter. The only other instances of negative use during the second quarter of the marketing year in recent history were in 1988-89 and in 2009-10. The June 1 stocks estimate this year will also be difficult to anticipate.

With the large March 1 stocks estimate, the "small crop-long tail" price pattern for corn and soybean prices continues.

While planting intentions for corn and soybeans revealed on March 28 were near expectations, new-crop prices have also weakened as expectations for larger stocks at the end of the current marketing year provide some additional supplies for the 2013-14 marketing year.

Focus will now turn to planting conditions and planting progress. Without widespread planting delays, new crop price weakness is expected to continue.

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