

Wheat: 2010-2011 Marketing Year Outlook

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With the 2010 wheat harvest around the corner, it is time to consider marketing options for this year's wheat crop. Prices have been extremely volatile over the past few years and reached all-time highs at approximately \$14.00 per bushel in the spring of 2008. Hard Red Winter Wheat prices have remained relatively stable throughout the 2009-2010 marketing year but may become volatile as the new marketing year develops. Let's take a look at the current situation in wheat and look at several marketing possibilities for your crop.

Supply

U.S. ending stocks of all wheat have risen the past two years after a record low of 305 million bushels in 2007. Average U.S. ending stocks from 1999 to 2009 is 647.3 million bushels, with the 2009-2010 ending stocks estimated to equal 949 million bushels.

The USDA prospective planting reports projects 53.8 million bushels planted for the 2010-2011 crop year, and my personal projected harvested acres is 46.53 million acres. The USDA estimated a yield of 42.7 bushels per acre, which makes the 2010-2011 U.S. wheat crop 1.99 billion bushels.

When you add my projected total production for the 2010-2011 wheat crop of 1.99 billion bushels and add 949 million bushels left from 2009-2010 gives us a total supply estimate of 2.939 billion bushels in the next marketing year.

What does this mean? Total wheat production will be lower than the 10 year U.S. average of 2.114 billion bushels, but ending stocks will be at the highest level since the 99/00 crop year. The USDA reports that the weighted average price during that time period is \$4.01 per bushel, which is very close to the current price.

Demand

The largest factor in determining demand is based on the total amount of wheat the United States exports. Since 2000, the U.S. averages 1.01 billion bushels per year. Considering the below average U.S. Dollar value, I expect exports to remain strong but will be highly influenced by the world economy. It appears that world equity markets are stabilizing and may slightly improve throughout the next year.

The other major factor the market must consider is the effect of long-term low interest rates on commodities. Low interest rates have long been associated with rising commodity prices. Large index funds and money managers respect this relationship and

often buy commodities to hedge against inflation. If they begin to purchase futures and raw commodities, the markets could move higher.

Domestic demand for food tends to remain inelastic, which means that consumers will consume wheat without concern to price. Over the last 10 years food use averages 927 million bushels and will probably remain the same in the near future.

The United States typically will use 80 million bushels as seed. This number remains relatively constant and is somewhat insignificant in the larger picture considering food use and exports are such large numbers.

Estimating demand can be extremely difficult and requires multiple assumptions that the most common demand factors remain constant. I predict that exports will remain strong as the world economy improves and the U.S. dollar stays cheap compared to other currencies.

Conclusion

The United States will have high ending stocks despite having the lowest acres planted since the early 1970's. Improved yields and favorable weather will make up for the lower acreage. Demand will continue to focus on both the world economy and cheap U.S. dollar. If the world economy and U.S. wheat exports improve, then 2010-2011 ending stocks will be lower than currently projected and prices may increase. If the world economy does not improve or the US Dollar moves higher against foreign currencies, our wheat will be less favorably priced in the world market. These two factors could push prices lower.

I feel there is a small amount downside price action possible as harvest provides plenty of grain over the short-term time horizon. Prices will continue to meet resistance on the upside until the U.S. works through the wheat we have in storage. In order to decrease ending stocks, the U.S. domestic market will need to have lower prices in order to export the excess grain. The upside may come after harvest, as the lowest seasonal prices get the attention of foreign buyers. The other major factor is that lower prices typically mean less acreage planted, how many years of low planting acreage can the market handle without moving higher? While the long-term outlook (3 to 5 years) looks promising for producers, the short-term (next 12 months) outlook seems to be range bound with little hope for a big upside move.

Marketing Strategies

There are an infinite number of marketing strategies, but the most logical this year seems to also be the most simple.

1. Buy Put Options. If you decide you want to store your wheat through the marketing year, buying a put option will protect your stored wheat against lower prices. Put options give you the right, but not the obligation, to sell your wheat at

- a specific price. In simple terms, it places a price floor at the strike price you choose.
2. Buy Call Options. If you decide to sell your wheat at harvest, buying call options will allow you to participate if wheat prices move higher. Call options give you the right, but not the obligation, to buy wheat at a specific price. In simple terms, it places a price ceiling at the strike price you choose.



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