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CORN AND SOYBEAN PRICES: STRONG FUTURES, WEAK BASIS

Current issues in the corn and soybean markets include some concern about adverse weather and generally weak basis levels. The two issues are not related, but are impacting cash prices in opposite directions.

In general, the U.S. corn crop has made good early progress. As of May 28, the USDA reported that 97 percent of the crop had been planted and 85 percent had emerged. The 5-year average for emergence as of that date is 77 percent. Emergence was slightly behind the average pace in Indiana and Kansas. Seventy percent of the crop was rated in good or excellent condition, compared to 62 percent on the same date last year and 68 percent in 2004. Condition ratings were lowest for Indiana, Kansas, and Texas. For soybeans, 79 percent of the crop had been planted as of May 28, above the 5-year average of 68 percent, and 42 percent had emerged, compared to an average of 39 percent. Emergence, however, trailed the average pace in 5 of the 18 reporting states, including Illinois and Indiana.

While the growing season has started without widespread problems, concern centers around prospects for hot and dry weather in western growing areas this week. It now appears that the area of most intense heat will shift south after this week, centering on Texas. Current forecasts do not suggest a prolonged period of hot, dry conditions in June, but weather concerns will persist through the growing season. The market is demonstrating that it will react quickly to any indication that yields could drop below trend value in 2006. On the surface, corn prices would appear to be more sensitive to weather prospects due to declining acreage and surging demand. In contrast, soybean acreage likely exceeds that of last year and consumption appears to be slowing. However, soybeans attract a lot of speculative interest and soybean prices will likely react as much as corn prices to early weather concerns.

To date, December 2006 corn futures have a contract high of $2.88, established on May 18, 2006. That contract settled at $2.85 on June 2, 2006. A new high sometime during the growing season would not be surprising. December futures exceeded $2.88 in 7 of the past 10 years. Highs in those 7 years ranged from $2.915 to $3.89. The contract high for November 2006 soybeans is $6.60, established in July 2005. The recent high is $5.485 reached in early January 2006. That contract settled at $6.3325 on June 2, 2006. A new contract high for November 2006 soybean futures appears less likely than a new high for December 2006 corn futures, but certainly cannot be ruled out. November futures have exceeded $6.60 in 7 of the past 10 years, with highs in those 7 years ranging from $6.80 to $8.25.

While weather concerns, along with a number of other factors, are supporting corn and soybean prices, generally weak basis (old crop and new crop) is being experienced in most markets. For example, the average spot cash price of corn in central Illinois on June 1, 2006 was $.285 under July 2006 futures. That compares to $.21 under on the same date last year and an average of $.09 under in 2002 through 2004. The harvest delivery bid was $.3125 under December 2006 futures, compared to the previous 4-year average of $.23 under. The average cash price of soybeans on the same date was $.3075 under July futures, compared to $.125 under on the same date last year and a 4-year average of $.08 under. The harvest delivery bid was $.32 under November 2006 futures, compared to a 4 year average of $.23 under.

The generally weak basis is attributed to a number of factors. Transportation costs are much higher than at this time last year. Barge rates on the Illinois and Mississippi Rivers, for example, are about 45 percent higher than rates of a year ago. The inventory of corn and soybeans is also larger than last year, with a lot of crop to be moved before harvest. Combined inventories of both crops on March 1, 2006 were 518 million bushels larger than stocks of a year ago. Higher interest rates also raise the cost of crop storage and negatively impact basis. The prime interest rate is 2 percentage points higher than the rate of a year ago.

The generally weak basis can be mostly explained by cost increases and demand for storage, but other factors may be at play as well. In particular, futures prices, particularly old crop soybeans, may be a bit over-valued relative to market fundamentals due to increased speculative demand. While futures prices can be significantly influenced by such speculative demand, cash prices have to reflect the prevailing supply and demand for the crops.

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