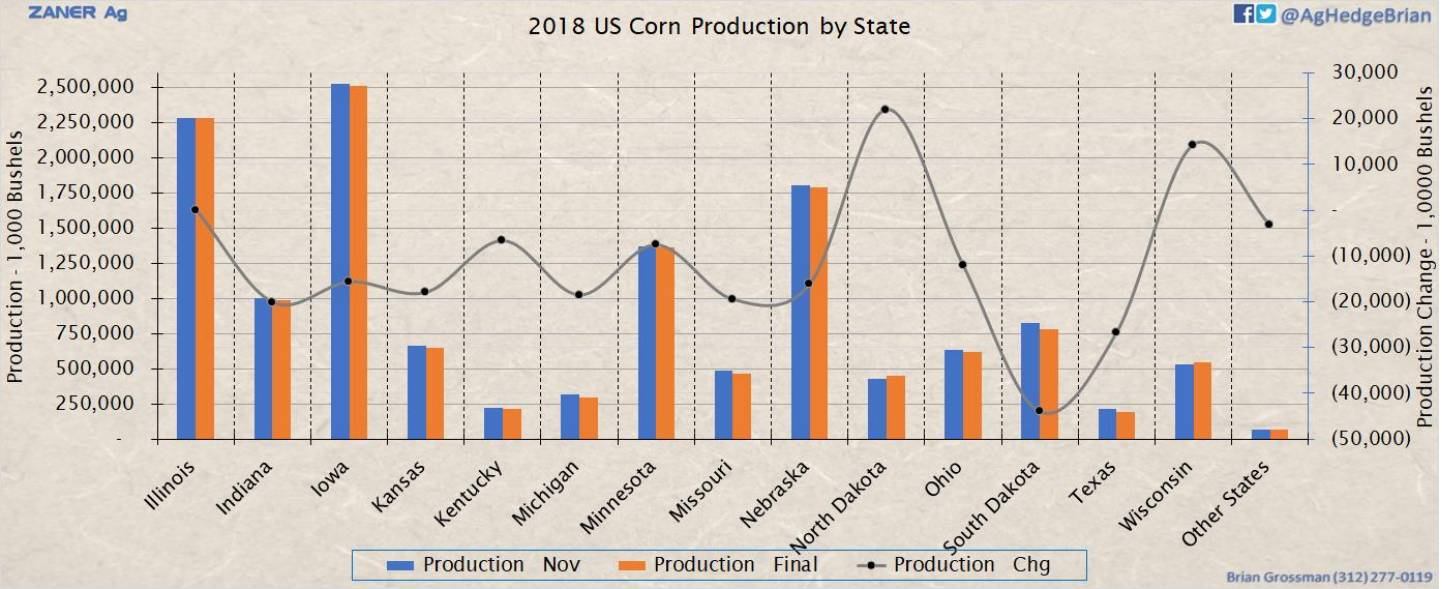
Brian Grossman | (312) 277-0119 | @AgHedgeBrian | bgrossman@zaner.com | ZANER Ag

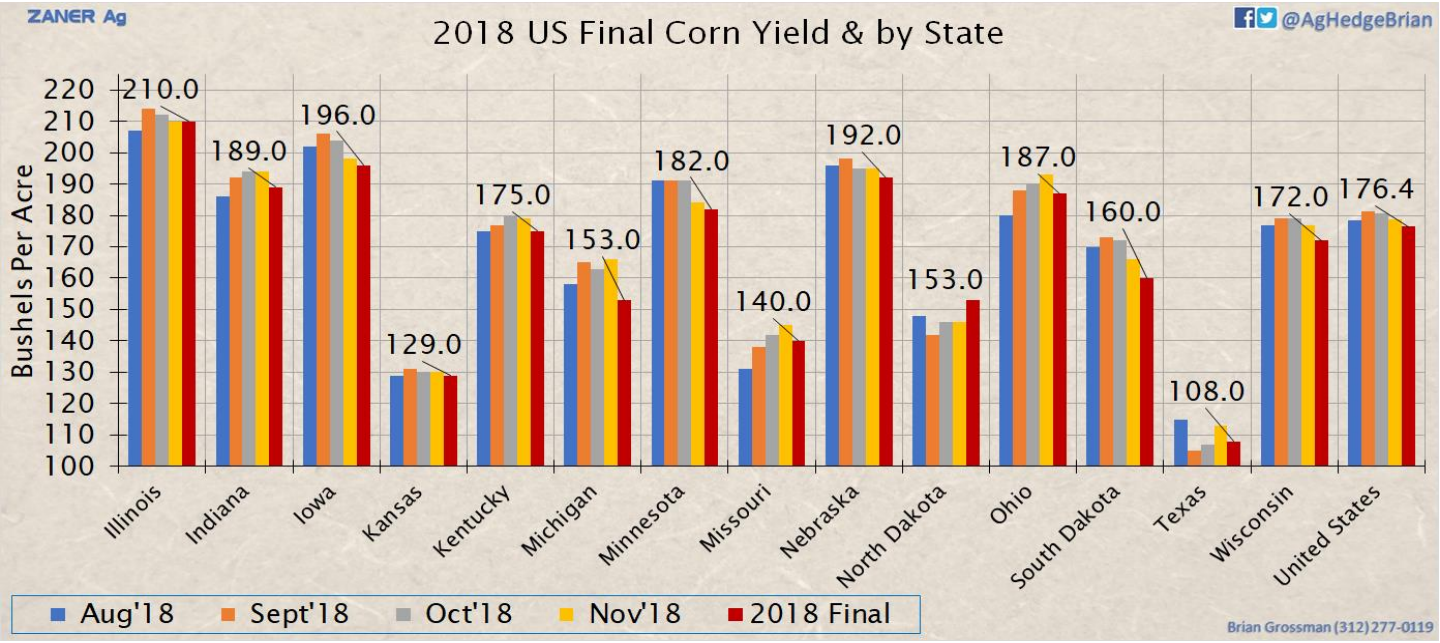
USDA February Report Highlights

Corn

Corn Concerns

March corn finished the Report day session 2'2 at 374'2 and December down 1'0 at 399'2. For all the data the USDA offered the market, there really wasn't much that changed or much to really get excited about. Corn had a truly "mixed bag" of reports. On the supply side of the balance sheet is Crop Production. To no surprise, the corn yield was lowered, however, it did go well below what the average trade was estimating.





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At face value, this is typically a bullish scenario corn, but the market closed lower while soybeans managed to post a higher close on a mostly bearish, but expected, series of reports.

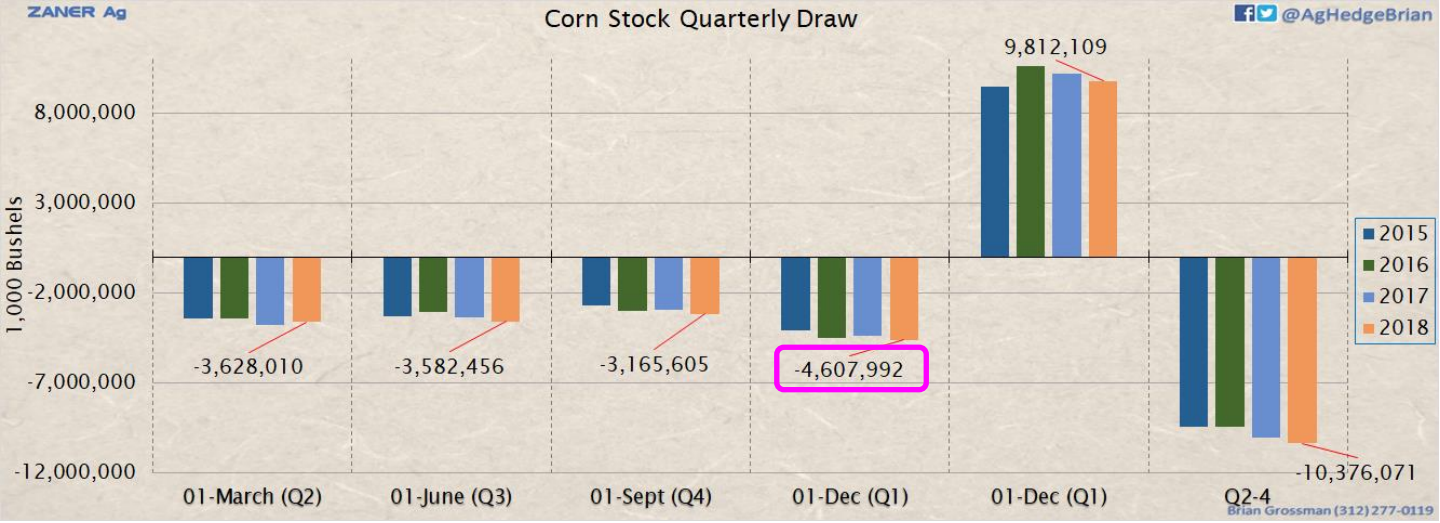
Dropping below the average trade estimate and last year's record, the national average yield came in at 176.4 bushels per acre. This lowered production by 205.875 million bushels from the November estimate.

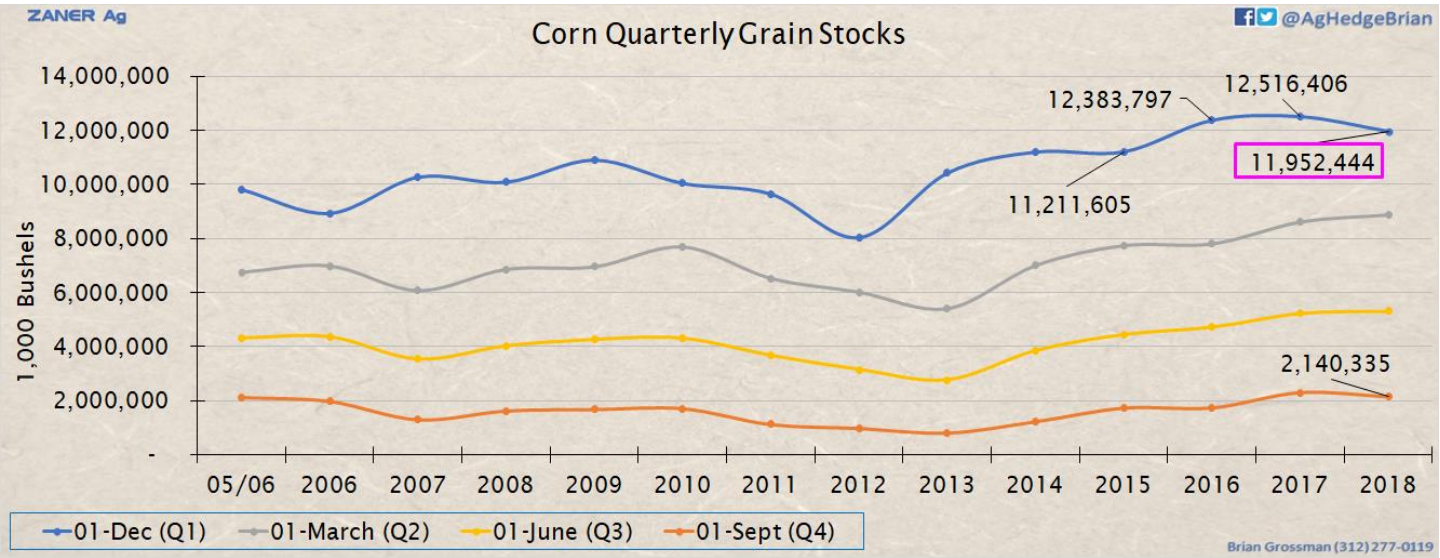
Of theTop-14 producing states, North Dakota was the only to see yields rise from the November estimate while Michigan was cut by 13 bushels/ac or 18.58 million bushels.

Building on the supply concerns is the ever-growing South American corn crop. Brazil's soybeans were badly hurt by drought, but high hopes remain for the corn crop and Argentina's corn crop looks like it will be a record of its own; currently estimated by the USDA at 46.0 MMT. This has mostly off-set the sizeable decrease seen in the US and leaves global production mostly unchanged; demand, however, is forecasted lower.

Quarterly Grain Stocks

Another bullish factor for the corn market. Posting the largest quarterly demand on record at 4.607 billion bushels, Dec-01 stocks have now fallen to a 3-year low. This also gives us a range target for final 2018/19 ending stocks to be between 1.576 and 1.972 billion bushels. Obviously, a pretty wide range and it is based on last year's demand for Quarter (Q)2-4 and the 3-year average demand for Q2-4 so by no means 100%.





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Last year, corn saw exceptionally strong demand in Q2-4. While 2017/18 pushed us to recent record highs in inventory that pushed futures prices to the low 3's. Low prices cure low prices by generating demand and that we did as stated above with record Q1 demand. However, there are headwinds to face in the coming months that may take much of the bullish steam out of the market.

Problems Brewing

It is not a well-kept secret that the US EPA continues to grant "hardship" waivers to Big Oil. The impact of this has been catastrophic for the US ethanol market. As tracked by the ***Hightower Report***, Iowa ethanol profit margins have been negative for going on 6 months now. This strain has led to less and less weekly consumption to the point that weekly demand is no longer meeting the weekly required quota to reach the original USDA target.

#SupportAmericanEthanol

The impact of this has shown it's face in the US balance sheet. Now down 75 million bushels from the Sept18-Nov18 estimate, the likeliness that total ethanol demand continues to fall is very high without a major course change by this Administrations EPA.

#RFSWorks

What Does USDA See Coming?

As said earlier, based on last year's Q2-4 demand and the 3-year average of Q2-4 demand we have a likely ending stock of 1.576 to 1.972 billion bushels. Now, once I adjusted my Quarterly Stock estimate to match the USDA's production volume, my estimate of Q1 demand was off by only 11.505 million bushels. My ending stock estimate was 1.590 billion bushels.

The USDA set ending stock estimate at 1.735 billion bushels. Why such a difference if I was off by less then 12 million on Q1 demand? Obviously, the USDA "sees" or is forecasting for a decline is domestic demand. The way I saw it, I left ethanol unchanged and just slightly raised the Feed & Residual. The USDA lowered Feed & Residual by 125 million and lowered ethanol by 25 million with Food, Seed & Industry (including ethanol) down 40 million bushels.

The large change in Feed & Residual (down 125 million) really took me by surprise as the USDA also lower Wheat(s) Feed & Residual by 30 million. Definitely odd as the US animal herd shouldn't be reducing demand and for s**ts & giggles… It didn't come from SoyMeal either.

This leaves me in the mindset that the demand reduction is coming from Residual. This is a tricky one as Residual demand is "unknown" or "unexplainable" demand. It could actually be from a lower yield, higher feed, mix of the above. Ultimately, it is the number that "balances" the balance sheet to make everything make sense.

(*Now I am wearing my Tin Foil hat*) Given the chaos of this year's harvest and the added Government shutdown, did the USDA make that large of a reduction in Residual simply to keep U.S.

ending stocks relatively close to the prior ending stock estimate. This would "buy time" for the March-01 Quarterly Grain Stock report which may provide more accurate data not too far away.

Even more interesting is the USDA Average Farm Price per Bushel Estimate. Lower ending stocks yet the higher end of the price range for corn came down by 0.10 per bushel. *I do not know how accurate their price estimate is* Either way, it doesn't appear the USDA is overly optimistic.

Now What?

Unfortunately, this report didn't answer many questions. Much of the information was very close to what the average trade was expecting and the lack of change in the market reflected the lack of impact on traders. One thing that we do need to keep in mind is the number of "unknowns" we have on the trade front this year. Will China buy soybeans? Will that cut into corn acres? Will China buy corn?? Or will everybody turn to South America and their advantage in currency exchange?

My mindset for corn is a sideways market for now. The trading range of 370-385 is likely to continue. The US acreage debate is soon upon us and we are already in spring crop insurance month. And, there is always the South American weather market to be aware of and to take advantage of!

When it comes to the strong U.S. corn exports, we need to keep in mind that last year both Brazil and Argentina were severely impacted by drought that lowered their corn production by 20-some MMT. With weakened supplies in the world's second and third largest exporters, the U.S. was leaned on even more.

The Brazilian soybean crop suffered from drought this year, but the Safrinha (winter) corn crop that is heavily exported is off to a record planting pace and is expected into see dramatically improved weather through February and into March. Argentina's corn crop in excellent condition as well.

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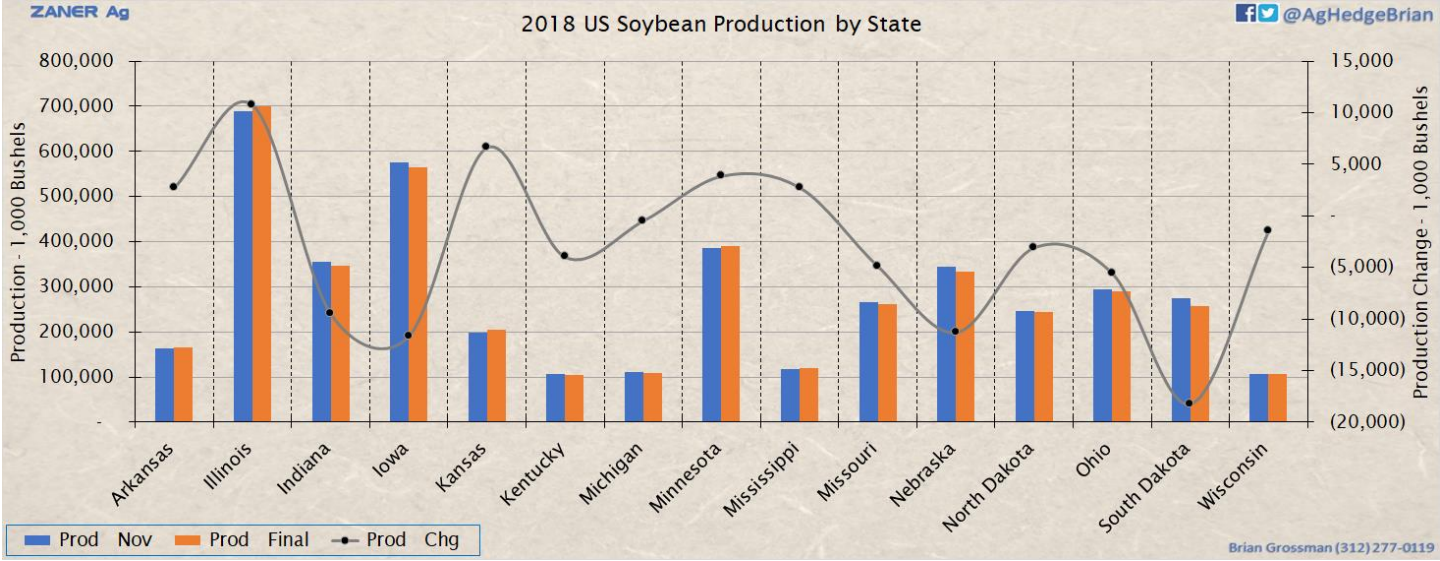
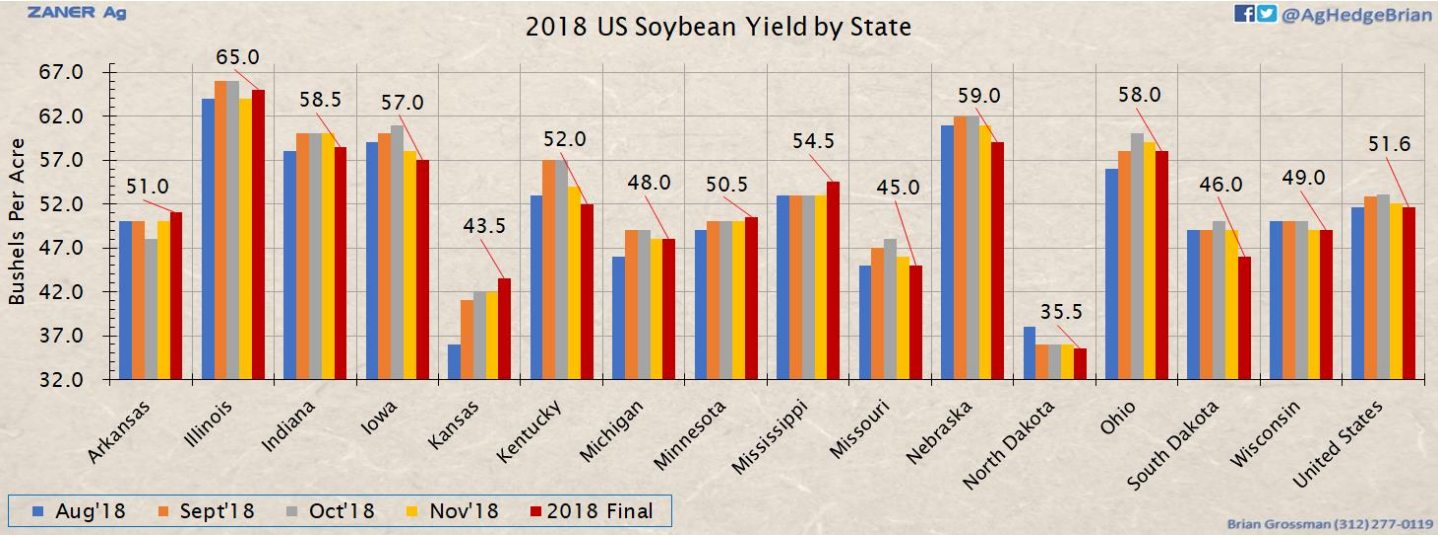
Soybean





Soybean production came to a "surprise" to me. As a fundamentalist (supply/demand) I wasn't surprised. The math is the math. However, as a technician (charts) I knew that there was either going to be a story to be told in the Crop Production or the Quarterly Stocks. In this case, it came in the Stocks.

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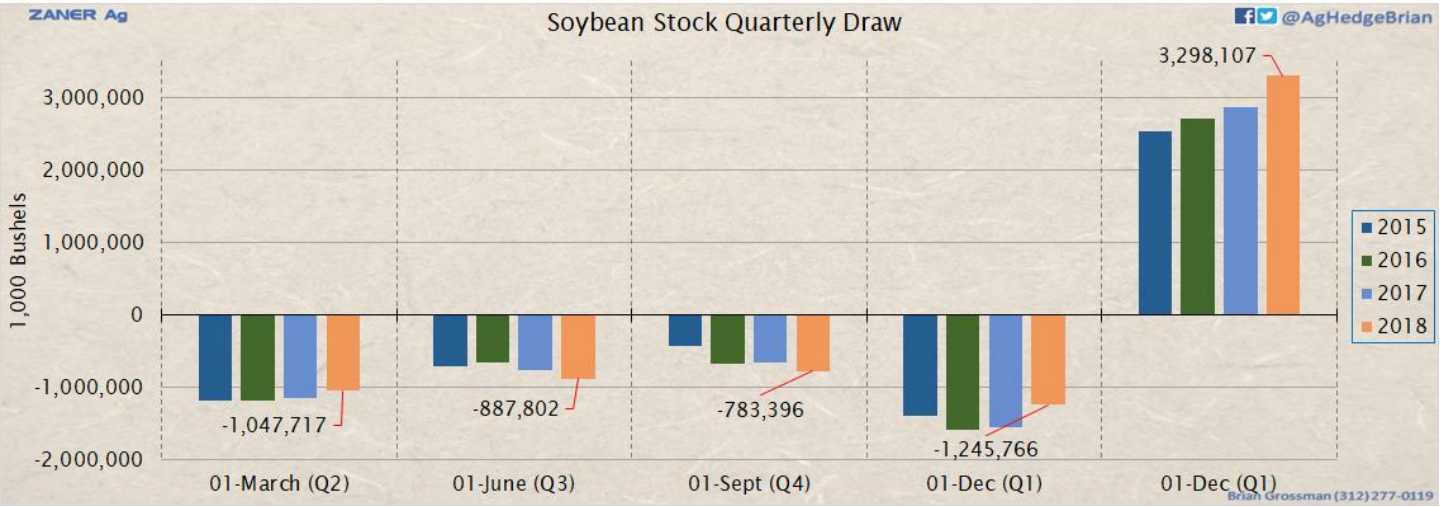
"On Farm" soybean stocks came in at a record high of 1.935 billion bushels; well above last year's 1.485 billion and national cash prices have been poor due to terrible local basis. This abnormally weak local basis may be the influencing factor that has kept the soybean calendar spreads from reaching 100%+ cost of carry.

Monthly Storage Rate	0.0017	0.05	ZSH19	ZSK19	ZSN19	ZSQ19	ZSU19	ZSX19	ZSF20
Interest Rate	4.00%								
		2/9/2019	3/14/19	5/14/19	7/14/19	9/14/19	8/14/19	11/14/19	1/14/20
			914.5	928.75	942.25	947.75	950.25	957	966.25
3/14/2019 ZSH19	914.50	Market Carry		14.25	27.75	33.25	35.75	42.50	51.75
		Cost of Carry		16.10	32.19	48.29	40.24	64.39	80.48
		Percent Full Carry		88.51%	86.20%	68.85%	88.84%	66.01%	64.30%
5/14/2019 ZSK19	928.75	Market Carry			13.50	19.00	21.50	28.25	37.50
		Cost of Carry			16.19	32.38	24.29	48.58	64.77
		Percent Full Carry			83.38%	58.67%	88.52%	58.16%	57.90%
7/14/2019 ZSN19	942.25	Market Carry				5.50	8.00	14.75	24.00
		Cost of Carry				16.28	8.14	32.56	48.85
		Percent Full Carry				33.78%	98.27%	45.30%	49.14%
9/14/2019 ZSQ19	947.75	Market Carry					2.50	9.25	18.50
		Cost of Carry					-8.16	16.32	32.64
		Percent Full Carry					-30.64%	56.68%	56.68%
8/14/2019 ZSU19	950.25	Market Carry						6.75	16.00
		Cost of Carry						24.50	40.84
		Percent Full Carry						27.55%	39.18%

There is no denying that the calendar spreads are indicating the will to slow down the inflow of soybeans, but it definitely doesn't appear to indicate a 910 million bushel ending stock as the USDA is predicting. **To find more on this topic, follow the link: http://intranet.zaner.com/uploads/bgrossman/2019/What%20Do%20the%20Soybean%20Bulls%20Know.pdf

However, the "official" final estimate (until next year) is what it is, and the current ending stock is estimated at 910 million bushels. All now equating to Dec-01 Quarterly Grain Stocks at a record volume and Quarter 1 demand was the lowest since soybean Market Year Quarter 1 in 2011.



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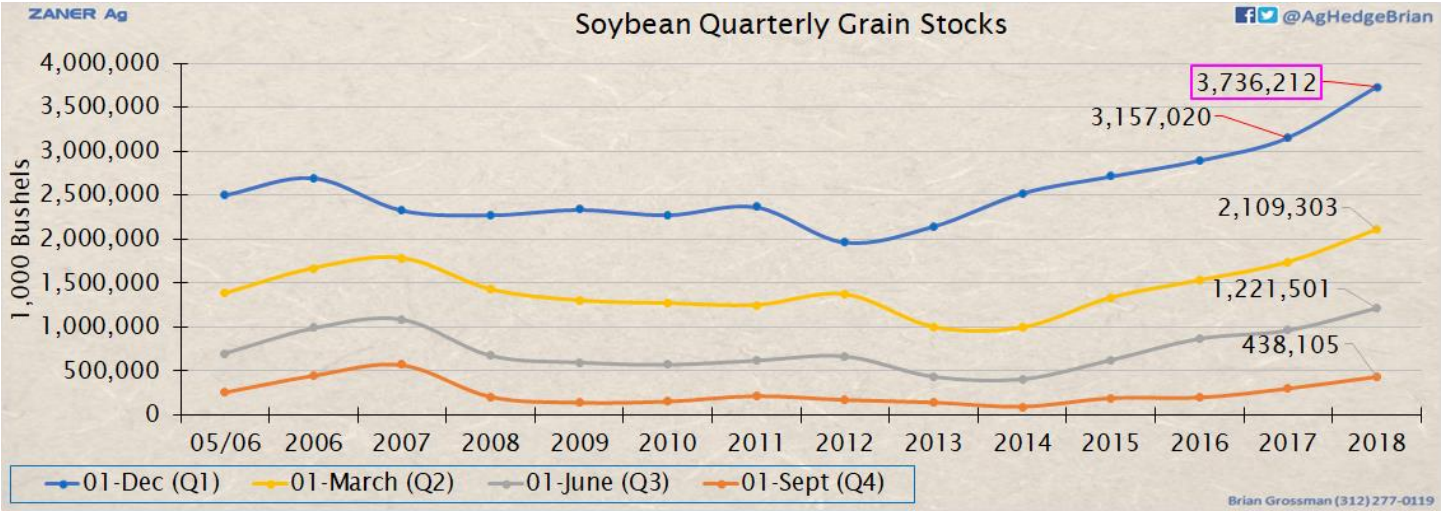
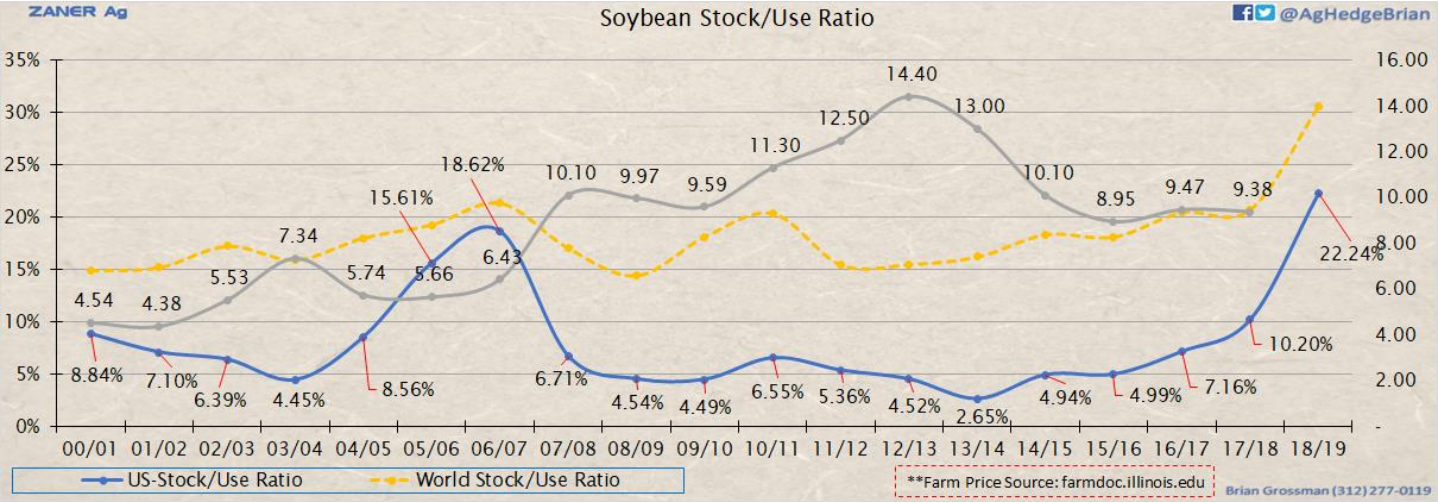


Now, we have the question of when OR will the shoe drop on soybeans? Now that we have an "official" final yield estimate; the demand side of the balance sheet is all that can change to move the needle off 910 million bushel ending stock. Where can that demand come from?

Soybean demand is made up of 1) Crush 2) Exports 3) Seed 4) Residual.

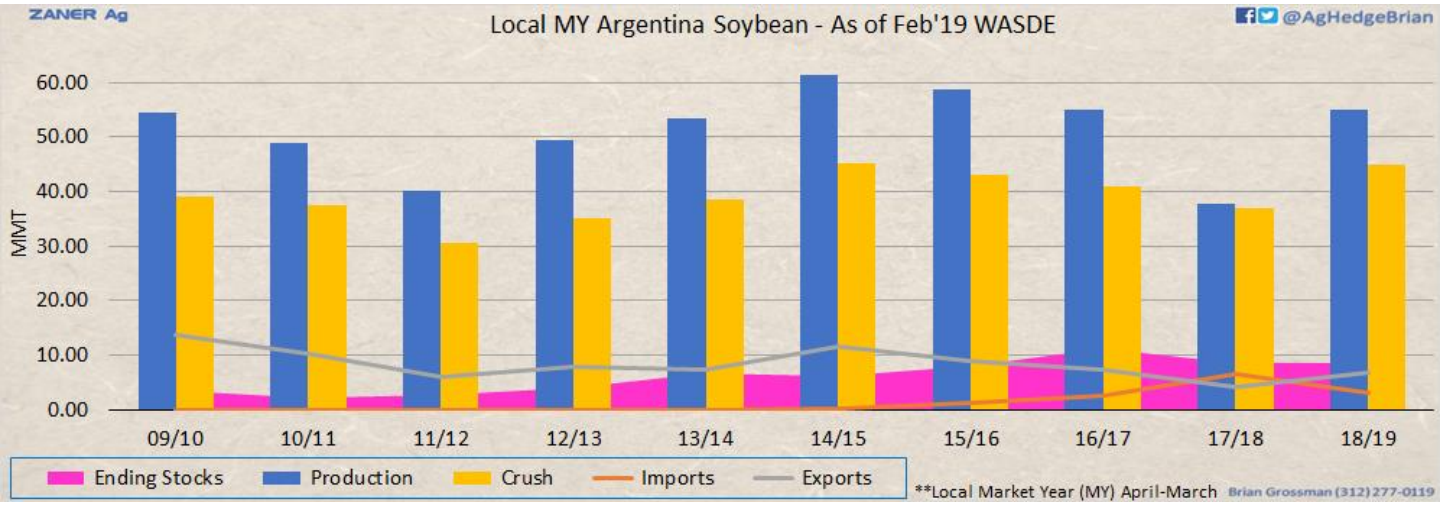
The USDA raised crush by 10 million bushels to 2.090 billion, which 2.100-2.250 is estimated near full capacity. However, it definitely doesn't represent the same year over year increase we saw from 2016/17 to 2017/18. This may have room to grow yet. As of now, I think it will eventually rise to 2.170 or an additional 80 million bushels; resulting in an ending stock of near 820 million bushels. Still plenty high….

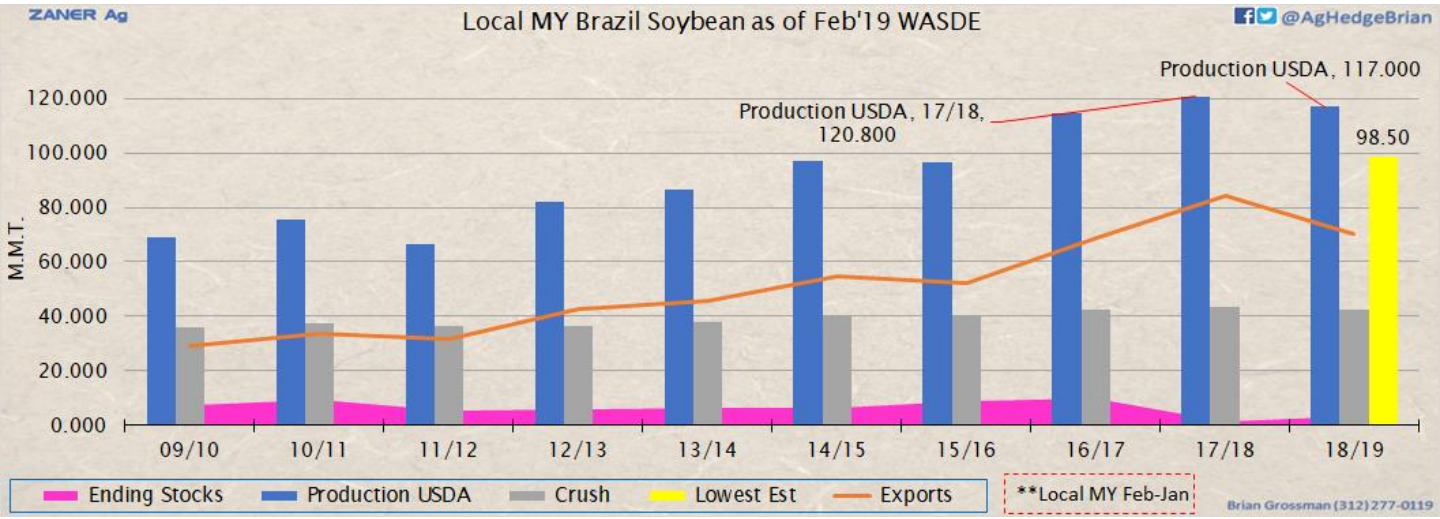
Where Now?



Without a doubt, there is a soybean supply problem not only in the U.S. but also in the world. Decreasing demand from China has deeply cut into overall demand; if this is a true change in efficiency rather than ASF, we will have a real problem at the current rate of growth in production.

Globally, the USDA did lower Brazilian soybean production by 5.0 MMT (183.7 million bushels). This was slightly offset by an increase in Argentina production, however, that is less concerning for me. Brazil as a whole prefers to sell nearly all of their reserve soybeans. Argentina does not. In recent years, Argentina has been "okay" with holding upwards of 10.0 MMT (local MY year).

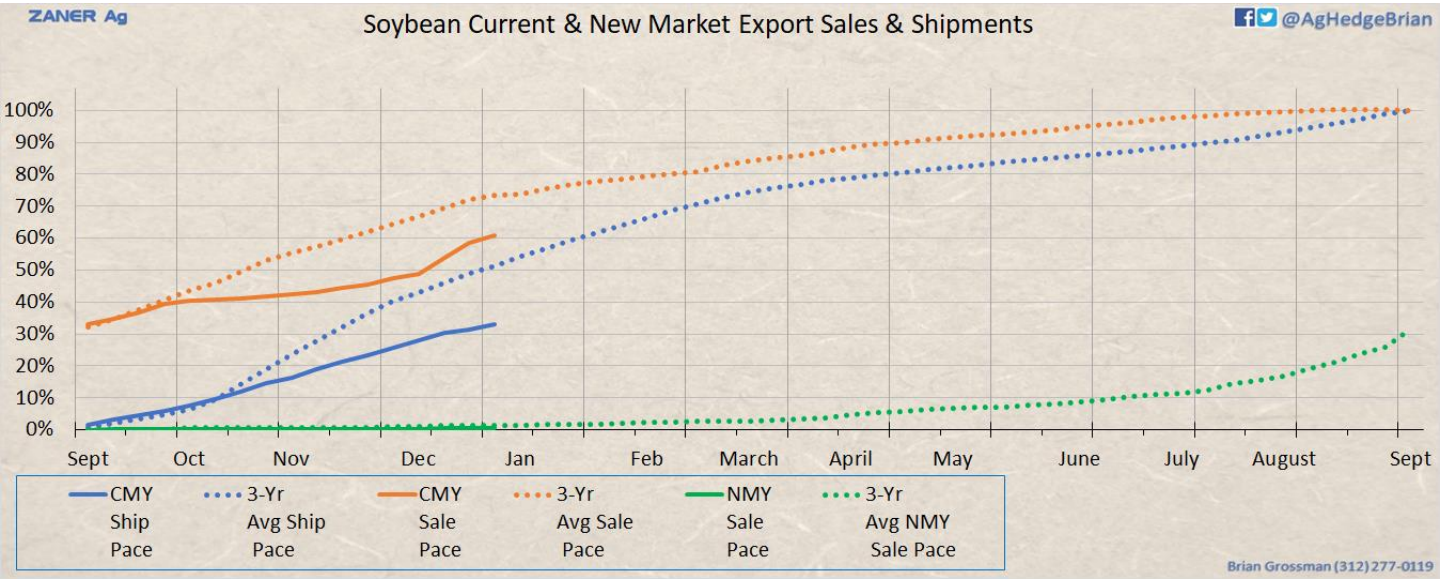




Without large year over year reserves, Brazil will have to adjust to shorter production by either less exports or less crush. Exports are likely to take the brunt.

Exports

The only other line item big enough to substantially change U.S. ending stocks is the exports category. The USDA lowered the forecast by 25 million bushels in February which definitely leaves some optimism on the table that China will, at the very least, take delivery of what they have booked and maybe even more. It may also be reflecting the smaller exports expected from Brazil.



(Export Chart Not Current Due to US Gov. Shutdown)

Based on the past three years of export data, the current 2018/19 market year of exports is on pace to be around 1.586 billion bushels. Obviously, a lot can change between now and then, but it is devastating low and would equate to ending stocks over 1.0 billion bushels; leaving little hope for a local basis improvement.

Similar to my math in corn; using last years Quarter2-4 demand and the last 3-year average of Quarter2-4, the 2018/19 stocks calculate out to 1.017 – 1.126 billion bushels.

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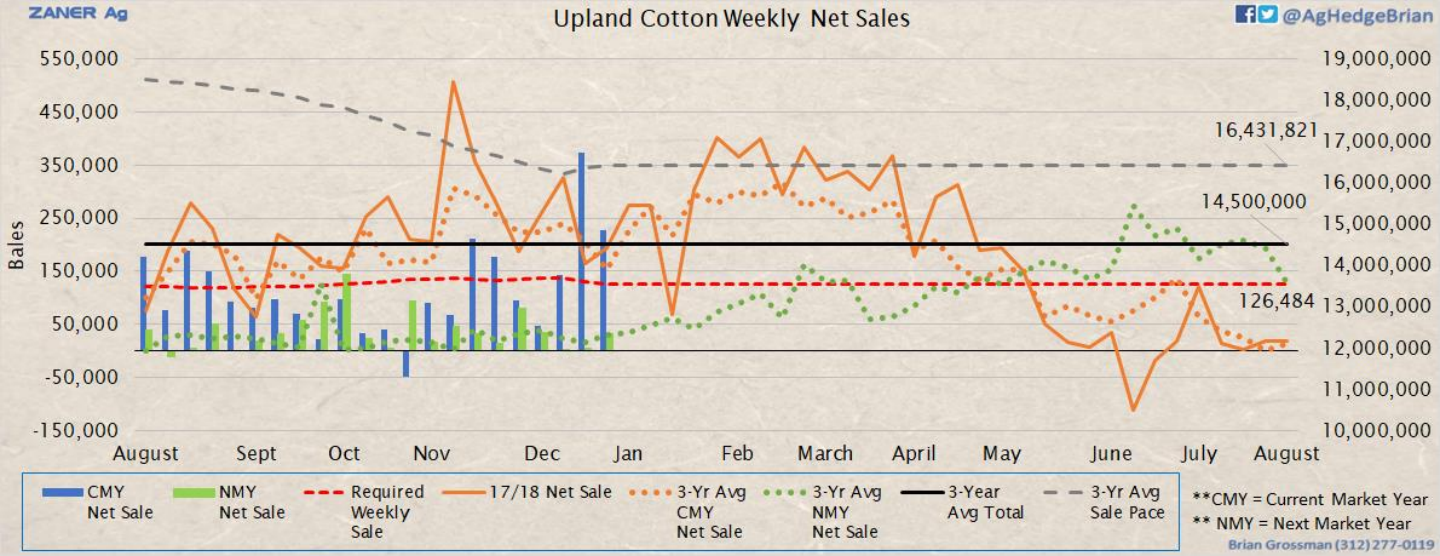
Cotton

The USDA took a very interesting take on the cotton market and this view by the USDA, I believe, has the potential to change the "mood" in cotton land. Now, at the end of the day, demand ultimately is the key factor, but the USDA sees demand.

Exports

This line item was the most surprising to me. Fueling a rally that pushed cotton to multi-year highs was a global crunch due to overbuying by some and a general shortage of high-quality fiber. Well, Cotton has been suffering from a 2017/18 hangover.

At this point we can only speculate on what China was planning with the massive purchases they made last year. However, since the trade war turned hot, China has been busy cancelling their massive orders. As a whole, including China, recent export sales have been sluggish this time of year compared to last year and compared to the 3-year average.



Not necessarily a bad thing given the volume of sales made prior to the start of the marketing year, but now the volume of cancelations has diminished prospects that the US will still reach 15.0+ million bales in exports. At the current rate, it is achievable, but cancelations are adding up fast. I was concerned the USDA was going to address this issue. They did not. Wait and see for a trade deal. If cotton would be included in a trade agreement and China takes delivery on their current purchases, exports should move higher on the balance sheet and tighten US supplies.

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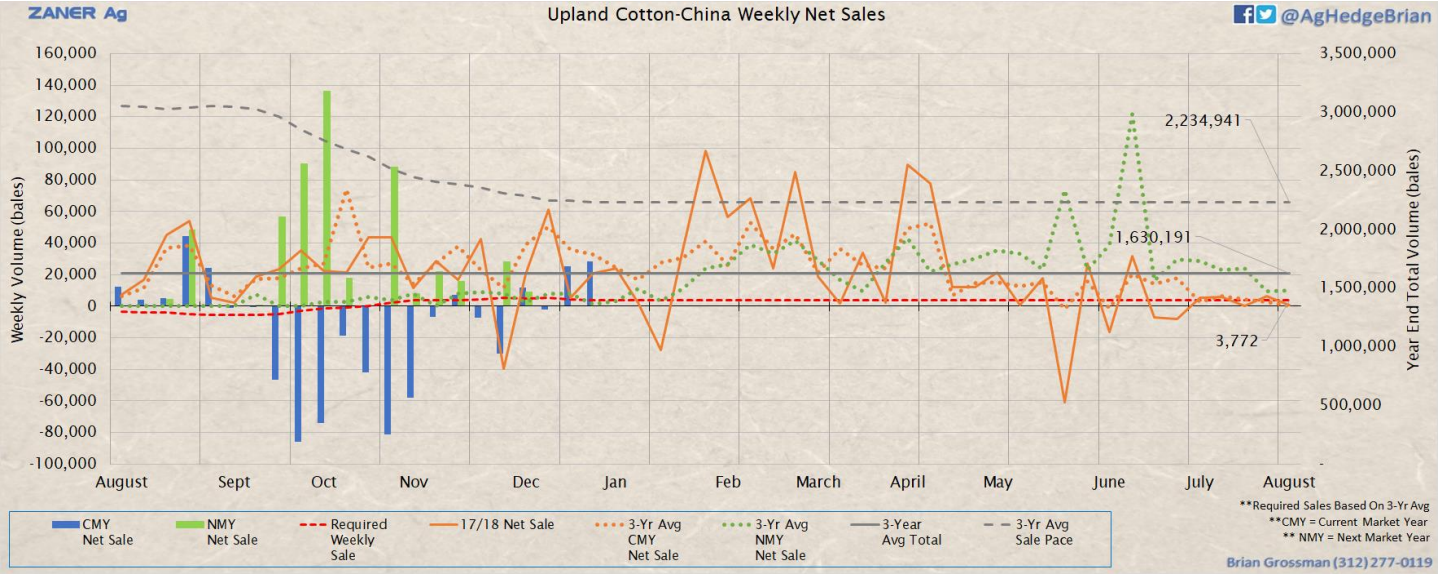
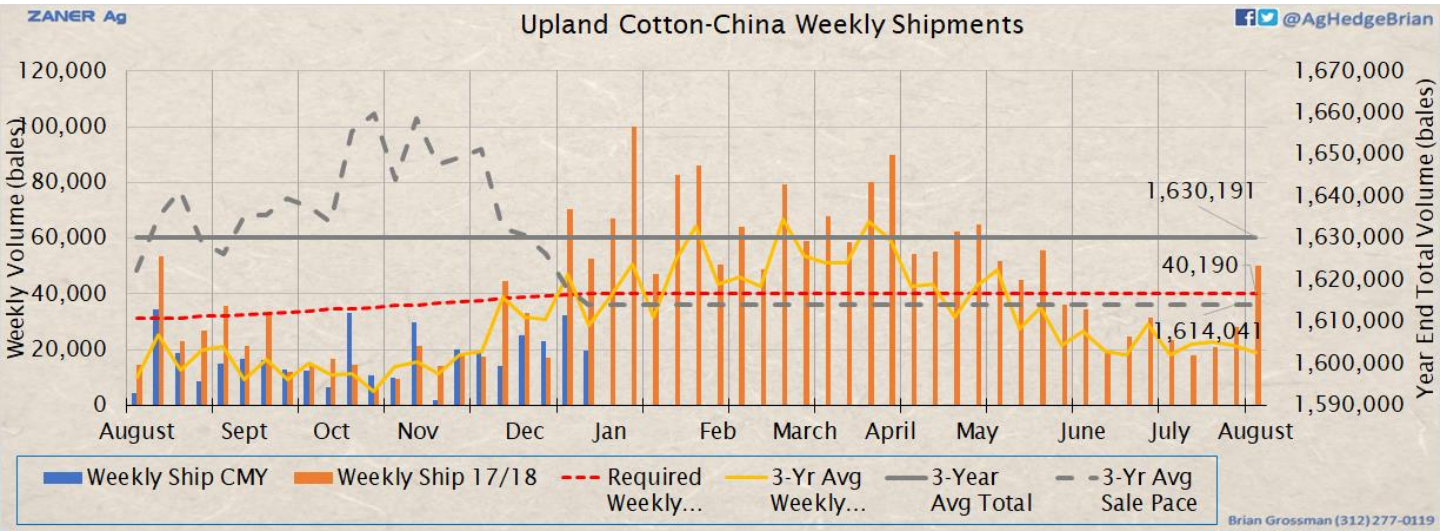


Was this "overbooking" by China simply too good to be true? We will never know, but China has not treated cotton and soybeans equally. Compared to the previous 3-years, China is nearly on par; just slightly lower.



The cotton market is currently in a very critical stage. With USDA data still not 'current', as you can see in all of my export charts, but we are now in the "big push" on cotton exports. From December through May, the U.S. ships 70% of what China buys. 30-some % of which happens in February and March.

In early January, I was turning some-what bullish cotton due to the seasonal increase and the cotton calendar spreads appearing as if they were trying to bottom as well. That attempt now has failed and may send cotton to new recent lows on the futures market.

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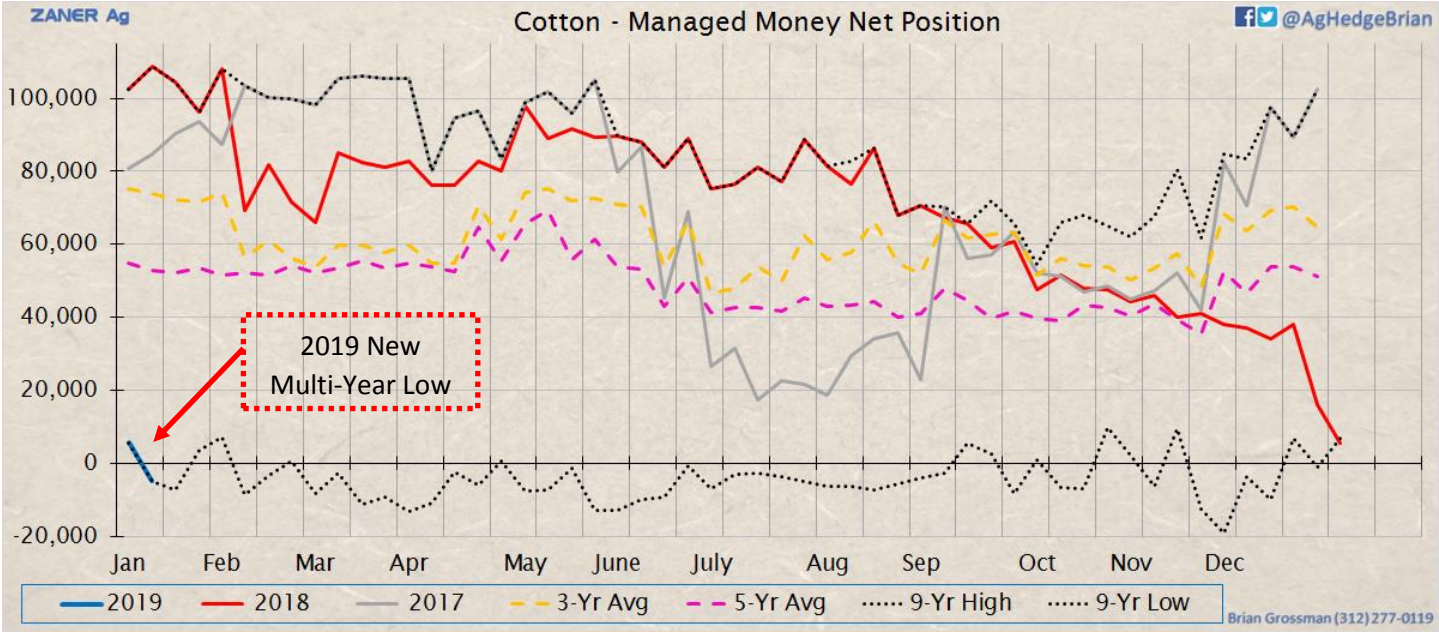
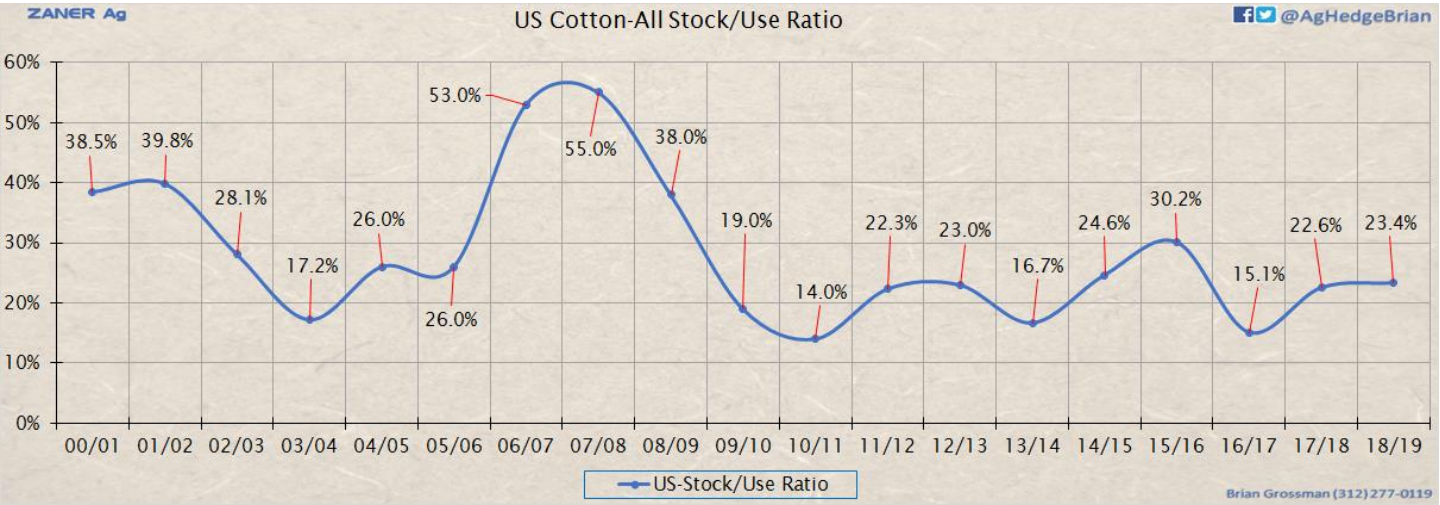
Also jumping on the Cotton Bear wagon is managed money. Here too, we don't have "current" data due to the Government shutdown but on USDA Friday, the CFTC also released data for as of Jan-08. Within that data, we see managed money dropping into a Net Short position. Completely against the seasonal tendencies of managed money and the first time they held a Net Short position since January of 2015, of which lasted for only one week. As CTFC data continues to be released, we will find out more on this topic.



One thing we know from history is that managed money doesn't spend much time holding a short cotton position and they also don't take on a large short position. 2012 was the year that managed money was the most bearish in recent history. During this time period, cotton stocks/use was about equal to todays.



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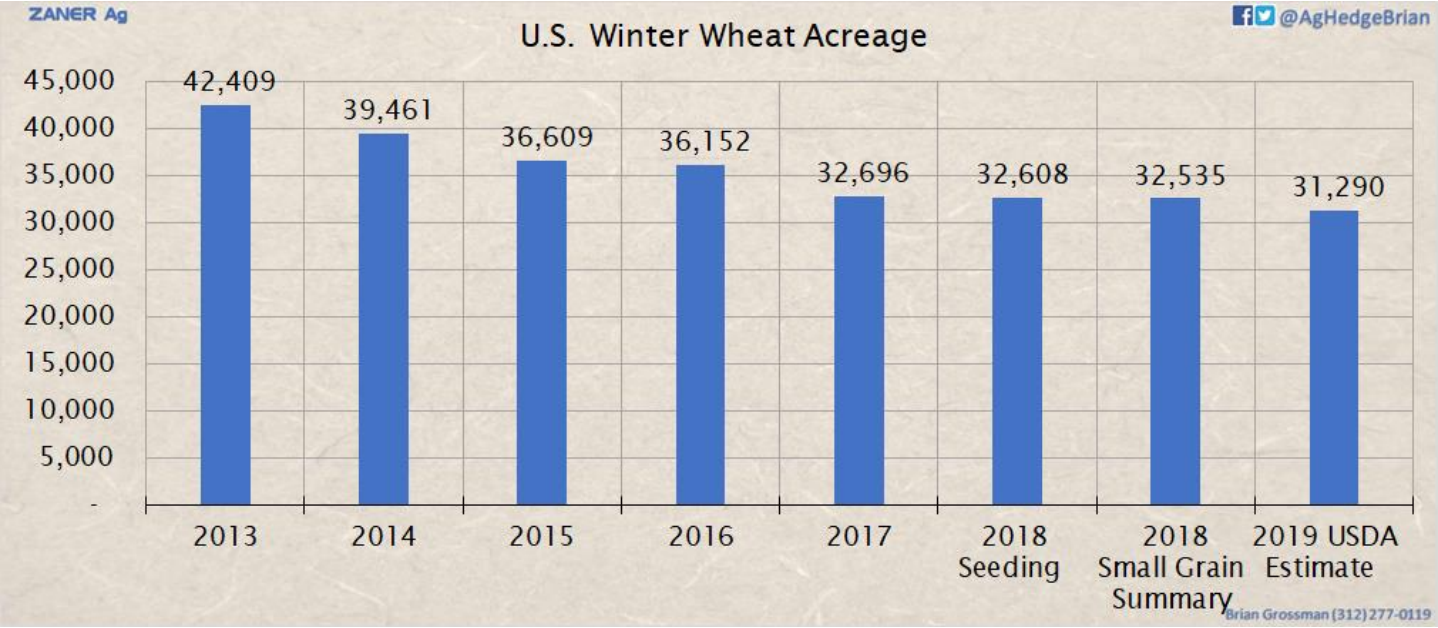
Wheat



To no surprise of the market, the USDA estimated winter wheat planted acreage again, at a new 100-year low as it fell below 32 million. Chicago wheat closed positive, Kansas closed lower. The market appeared to have little interest for what the USDA had to say, or it already knew. Or is it simply that wheat exports are so slow that low acreage doesn't matter?

Russia remains the wheat heavyweight of the world with large supplies and currency exchange rates to encourage it. Even trusty neighbors like Mexico have been buying up the cheaper wheat. Now more recently, Black Sea milling prices have been on a steady rise. Talk from Russian officials remain mixed when it comes to their export intentions, but the "talk" is now showing in the cash market. There may be some truth to these rumors, but the Russians seem to be playing the "game". Time will tell if the world turns to the U.S. or just turns down demand.

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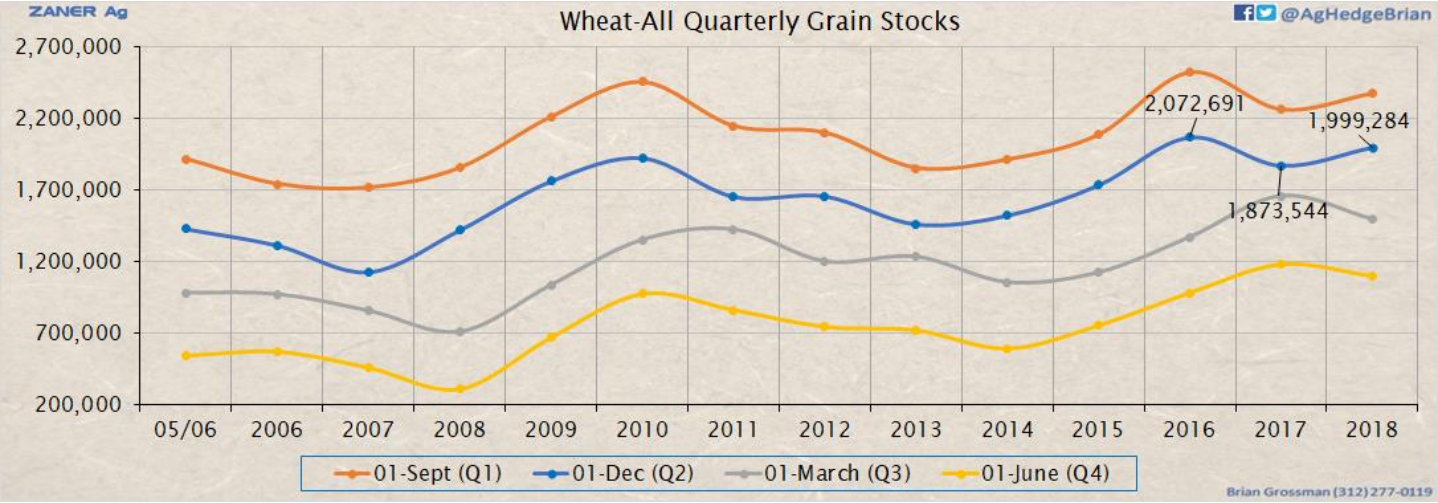
Until then, there was nothing to get exceptionally bullish on wheat in general. Quarter 2 demand came in low; below the 5-year average and a fresh 10-year low. Stocks, on the other hand, are at the second highest level in 10-years.



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Thanks!

Brian

ZANER Financial Services

Brian Grossman
Market Strategist -- Agricultural Hedging
(312) 277-0119 -- Direct Line
(312) 277-0150 -- Fax Line
bgrossman@zaner.com
@AgHedgeBrian
www.zaner.com

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Abbreviations & Conversions:

MT	= Metric Ton
TMT	= Thousand Metric Ton
MMT	= Million Metric Ton
1 MT of Wheat/Soybean	= 36.74 bushels
1 MT of Corn	= 39.36 bushels
WASDE	= World Agricultural Supply & Demand Estimate

Jan – "F" | Feb – "G" | Mar – "H" | April – "J" | May "K" | June – "M"

July – "N" | Aug – "Q" | Sept – "U" | Oct "V" | Nov "X" | Dec – "Z"

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