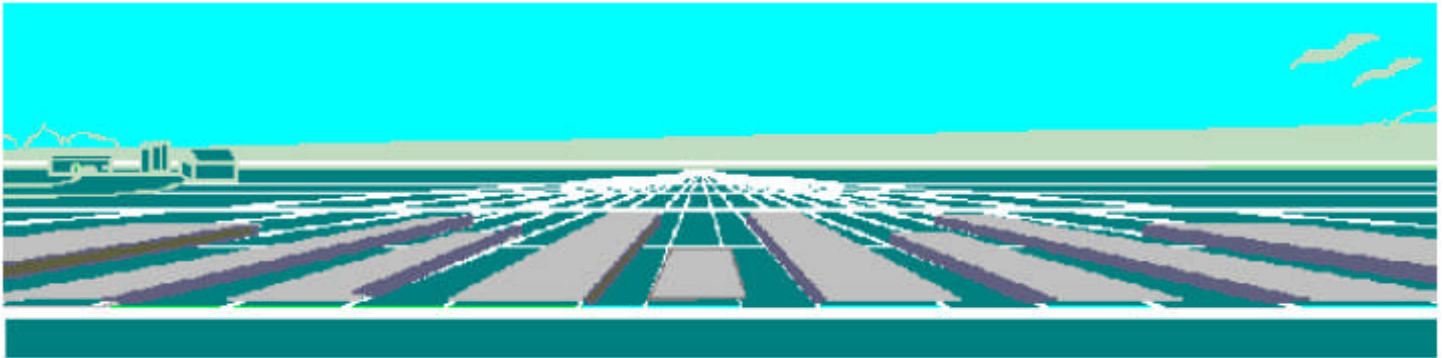


# Iowa Farm Outlook



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## USDA Reports Show Tighter Corn Supplies, Ample Soybean Carryover

USDA's January 12 revised crop estimates, supply-demand report and grain stocks estimates show a moderately tighter corn supply situation for the current marketing year than its economists anticipated a month ago. ***The most significant change was a 216 million bushel reduction in the U.S. 2006 corn crop estimate from the previous estimate in November.*** USDA economists also increased their corn export projection by 50 million bushels from last month. ***Even that higher number could be a bit conservative, considering the season to date export sales (one-third of the way through the marketing year) are 40% larger than a year earlier.*** Also, last week USDA's Chief Economist indicated to Congress that corn processing for ethanol in the 2007-08 marketing year may be a billion bushels larger than this year. Some industry economists believe it will grow by an even larger amount. This news pushed prices for the first four 2007 corn futures contract months up the \$0.20 daily maximum limit on January 12. By January 17, prices on July futures had risen \$0.54 above the close on January 9. The old-crop new-crop inverse was widening, with December 2007 futures up only \$0.32.

Revised production data still show the second-highest U.S. corn yield on record in 2006, with a U.S. average yield of 149.1 bushels per acre. Even so, the crop was 1.3 to 1.4 billion bushels below potential market demand (if fully adequate supplies had been available). ***This is the second consecutive season that production has fallen short of market demand. The 2005 U.S. crop was about 200 million bushels below total use.***

Most of the production-use gap this year can be filled by drawing down the large beginning carryover stocks to minimum levels needed for normal operations from August 31 until new-crop supplies are available. ***However, the market will also need to ration away about 200 to 300 million bushels of demand through higher prices.*** For the 2007-08 marketing year, beginning carryover stocks are expected to be about the minimum level needed by the grain trade, a very tight 3.0 to 3.5 weeks supply. ***That means production will need to be large enough to fill the current production-use gap and also accommodate at least another billion bushels of demand growth that is anticipated as newly-constructed ethanol plants come on line in the next 12 to 18 months.*** Total ethanol processing capacity under construction at this time is about 2.1 billion bushels, and nearly all of that additional capacity should be on line before the end of the 2007-08 marketing year, although not all plants will be operating for the full 12 months.

U.S. feed demand also appears likely to remain large from now through summer, but may decline modestly in the September 1, 2007-August 31, 2008 marketing year. Corn exports appear likely to remain strong into late spring, but may decrease modestly during the summer and next season if foreign crops are better than in 2006. Foreign corn and feed wheat production were reduced in a number of countries in 2006 by adverse weather.

## Market Buying More Corn Acres

Because of rapidly expanding ethanol demand, a major part of the futures market's job through spring will be to keep corn prices high enough to encourage at least a 12 to 14 percent increase in 2007 U.S. plantings. Additional large increases appear almost certain to be needed again in the following two or three years.

***Acreage of grain, soybeans, and cotton nationally has declined by about 15 million acres in the last 10 years. Declining total acreage tells us that most of the extra corn acres will have to come from other crops.*** That means a substantial amount of cropland will need to be shifted from soybeans to corn, although a few extra corn acres will come from oats, hay, and pasture, as well as wheat in the eastern and extreme western parts of the Corn Belt in 2008. For the 2007 harvest, USDA reports that winter wheat planted acreage is 3.5 million acres larger than last year. Probably around 2 million of those acres would have been in corn or soybeans, except for the sharp rise in wheat prices at planting time last fall.

In the main Corn Belt, 7.1 million acres are in the Conservation Reserve Program. That includes buffer strips along streams and ditches, reclaimed wetlands, and reforested land. Realistically, probably around 3.5 to 4.0 million CRP acres may come out of CRP for corn and soybean production over the next few years. Some analysts speculate that because of this season's tight supply, CRP acres will be released for cropping in 2007. At this writing no decision has been made to do that. Much of the 37 million acres of CRP land is in the Great Plains, in areas too dry for corn and soybeans. As the Soybean Belt moves further west, displacing wheat, oats and barley, some CRP acres in that region may be returned to wheat and grain sorghum production.

**Figure 1. U.S. Corn Carryover Stocks in Weeks Supply**

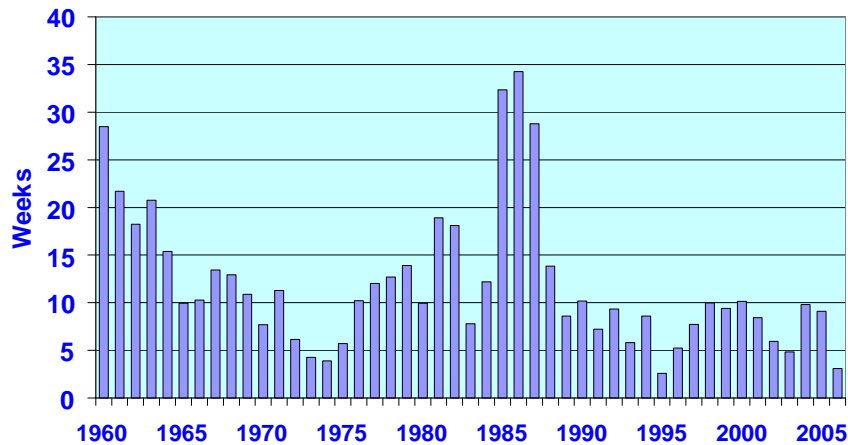


Figure 1 shows U.S. corn carryover stocks for the last 15 years and current projections for 2006-07, as a percent of annual use. August 31, 2007 U.S. corn carryover stocks are expected to be the lowest since 1995-96, when Iowa cash corn prices exceeded \$5 per bushel for nearly six months. Ending stocks that year were a 2.6 weeks supply, compared with a 3.3 weeks supply projected by USDA for this year. Much less rationing of demand is likely to be needed this year than in 1995-96. But much more corn acreage will need to be planted in 2007 than last season, and that will be the major influence on prices. High prices in 1995-96 were driven by low world stocks, U.S. and foreign weather problems, and a 10% acreage set-aside.

## Corn Balance Sheet

Our latest corn supply-demand and price projections for the current marketing year, along with early and very tentative projections for the next two marketing years are shown below. Our corn feed and residual use and exports for 2006-07 are slightly higher than those from USDA's latest projections. USDA projections place the 8/31/07 carryover stocks at 752 million bushels or a 3.2 weeks supply. Ours are at 693 or a 3.1 weeks supply. Either way, it appears that supplies will be very tight by late summer and some users may be

scrambling for supplies. The mid-to-late summer corn basis may at times be stronger than indicated by current forward contract bids for late summer delivery. Columns A represent weather-reduced U.S. corn yields in 2007 or 2008. In that case, a sharp reduction in domestic corn feeding would be expected as higher prices rationed demand. Columns B represent approximately normal weather. Yields we show in Columns B may be a bit optimistic, especially considering that agronomic research shows yield reductions on corn following corn of 10 to 14 percent vs. a corn/soybean rotation. Perhaps partially offsetting will be this year's much higher than normal corn prices, which will encourage farmers to fertilize heavily. However, the increased acreage could cause some plantings to be delayed a little beyond the optimum planting dates and might affect yields in that way.

1/12/07	Corn Balance Sheet (Mil. Bu.)		2004-05	2005-06	Projected	Projected 2007-08			Projected 2008-09		
					2006-07	A	B	C	A	B	C
<b>Supplies:</b>											
Plant. A(mil.)			80.9	81.8	78.6	86.5	86.5	86.5	90.5	90.5	90.5
Harv.A.(mil)			73.6	75.1	70.6	78.6	78.7	78.7	82.3	82.3	82.3
Bu./A.			160.4	147.9	149.1	146.0	156.5	161	146.0	158	163
Production			11,807	11,114	10,535	11,469	12,317	12,672	12,022	13,010	13,422
Carryover			958	2,114	1,967	693	693	693	690	690	690
<b>Total Supply</b>			12,776	13,237	12,508	12,174	13,025	13,379	12,724	13,714	14,126
<b>Feed &amp; resid.</b>			6,158	6,141	6,000	5,100	5,720	5,900	4,760	5,525	5,745
Food, ind. & seed			2,686	2,981	3,540	4,615	4,640	4,665	5,510	5,650	5,675
Corn for fuel ethanol*			1,323	1,603	2,150	3,225	3,250	3,275	4,110	4,250	4,275
Exports			1,818	2,147	2,275	1,800	1,975	2,000	1,775	1,850	1,950
<b>Total Utilization</b>			10,662	11,270	11,815	11,515	12,335	12,565	12,045	13,025	13,370
<b>Carryover</b>			2,114	1,967	693	659	690	814	679	689	756
<b>U.S. FARM PRICE</b>			\$2.06	\$2.00	\$3.35	\$3.90	3.50	3.30	\$4.40	3.60	3.35
<b>IOWA AVE. PRICE, \$/Bu.</b>			1.96	1.95	\$3.30	3.85	3.45	3.25	4.35	3.55	3.30
Counter-Cyclical Pmt.			0.30	0.35	\$0.00	0	0	0	0	0	0
HARV. PRICE, C.IA			1.60	1.40	\$2.80	3.80	3.20	2.95	4.00	3.25	3.15
DEC. FUT. @ HARV.			\$1.98	\$2.00	\$3.15	\$4.20	\$3.60	\$3.40	\$4.40	\$3.70	\$3.65
Historical Probability						18%	65%	17%	18%	65%	17%
<b>Weeks carryover supply</b>			10.3	9.1	3.1	3.0	2.9	3.4	2.9	2.8	2.9
<b>Feed use % chg. Drought years vs. current</b>						-15.0%			-20.7%		
Corn replaced by increased DDGS					97		194			177	
Decline in corn feeding vs. prev. year					-141		-280			-195	
<b>Percent Decline in corn feeding vs. prev. year:</b>						-17.0%			-16.8%		
<b>* Corn for Ethanol is Included in Food, ind. &amp; seed above</b>											

### Declining Crude Oil Prices a Caution

With the shift of Midwest agriculture to a major producer of energy in addition to food, crude oil prices are a potentially important influence on corn prices. Crude oil prices have declined by almost 20% since just before Christmas. At this writing, crude oil prices are about \$52 per barrel. We expect that market to begin to stabilize, but it is a difficult one to forecast. A drop into the low to mid \$40 range for several months probably would slow the expansion in the ethanol industry. At this writing, wholesale gasoline prices have declined by about 32 cents per gallon since December 19. Iowa rack (wholesale) ethanol prices have declined by about 48 cents per gallon during the same time period, with much of the decline occurring in the last 10 days. The lower ethanol prices, if the decline continues, would lower the maximum price new ethanol plants can pay for corn.

### Soybeans

On January 12 USDA lowered its 2006 U.S. soybean production estimate by a very slight 16 million bushels from the November crop report. At the same time, USDA economists lowered projected 2006-07 marketing year U.S. soybean exports by 25 million bushels. *The carryover stock projection for 8/31/07 was*

***raised 10 million bushels from last month and now stands at a very large 9.8 week supply.*** In the past, that would have been very negative for soybean prices. However, the grain trade is looking ahead to the next one to three years and anticipating a sharp decline in carryover stocks in 2008 and 2009 as corn pulls acres away from soybeans.

USDA left its Brazil and Argentina crop projections unchanged from last month. Argentina's crop is projected to be up 5% from 2006 along with a 2% increase for Brazil. South American crop conditions are reported to be very good, and some trade analysts are beginning to increase their Brazilian crop estimates slightly. Weather during the next six or seven weeks will be the key to the size of crops in that region.

***Strength in soybean prices following the USDA January 12 reports has been led almost entirely by the meal market. It is questionable how much further strength is likely in soybean meal, with competition from distillers grain and tighter profit margins in poultry and hogs.*** The soy oil market has been pressured some by declining crude oil and diesel futures prices and has been in a downtrend for the last few weeks, even after the January 12 reports. Soybean crushing margins have declined substantially in the last two weeks.

Our latest soybean balance sheet can be found on our web site, <http://www.econ.iastate.edu/faculty/wisner/> It is in the right hand column, along with the updated corn balance sheet.

*Robert Wisner*