

DITSCH



TRADING

AUGUST 2013

MONTH END COMMENTS

August was one of the driest in modern history across the heart of the Midwest. Much of Nebraska, southern Kansas, southern Missouri, Arkansas, Kentucky and Tennessee did receive beneficial rainfall. However, the much larger (in terms of national production) IA/IL/IN/MN/WI/eastern Dakotas/western Ohio areas were extremely dry. Soybean production is largely driven by critical August rainfall, which is required to

set and fill the pods. National soybean yield and production has certainly been hurt by this weather. At this time, I believe national soybean yield is likely in the 38-41 bpa range with production in the 2.9-3.1 billion bushel range (vs. USDA 3.255 billion bushels). I do not think USDA will adjust that low right in the September report (more likely in the 41-41.5 bpa range), but I do think they will get there by the October or latest the November report. If realized, this would represent one of the most significant August to final yield declines in history.

New crop soybean demand has been very strong. China has been the primary buyer, but all world buyers have turned to the US to replenish their depleted soybean stocks. World soybean markets have now been steeply inverted for the last 18 months. World consumers pulled down stocks waiting on the cheaper US soybeans, assuming US production would return to normal. Now, many are caught short with depleted pipelines and are forced to return to the market even as the inverse intensifies once again. It looks like the next potential relief now won't come until March-May of 2014 when South America is expected to harvest a record crop. However, as the US crop gets smaller, more pressure is put on South American production because it looks like the world will be forced to pull down inventories even further over the next 6 months.

Higher prices and stronger inverses are expected to slow US demand somewhat. World consumers will try to keep pipelines skinny until South America's 2014 harvest is available. South America also has more incentive to pull old crop stocks down to the bare minimum prior to their new crop harvest. China is selling reserve stocks and is likely to continue to do so. This should reduce December-February US export demand somewhat. Despite this, it looks like the US will begin the new 2013/14 marketing year with a record 22 MMT of soybean exports on the books. That would also be a record 59% of my 2013/14 total export projection of 1375 million bushels. Soybean meal exports are also exceeding expectations. This ongoing export business suggests March 1, 2014 US stocks are likely to dip below last year's record tight levels.

Despite this anticipated tightness, soybean futures and spreads are trading well below year-ago levels. South American carryin supplies are larger than last year, but the US is the cheaper market. US cash markets are at historically high levels. Demand is flowing to the US. All of this suggests limited downside and significant upside potential in soybean futures and spreads. Volatility is trading cheap relative to fundamentals, so long delta and long vol positions are preferred at this time, especially until US crop size can be better defined.

Corn is a much different story. Corn yield is driven more by rainfall earlier in the season along with lack of heat during the critical pollination period. While the August dryness and late August/early September

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9047 POPLAR AVENUE, SUITE 101, GERMANTOWN, TN 38138

901-766-4446

WWW.DITSCHTRADING.COM

GFIRTIK@NESVICK.COM

ADUHON@NESVICK.COM

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heat surely took the top end off the corn yield, it still appears as if the far Eastern Corn Belt, Mid-South, Delta, and Atlantic Coast states should all produce record corn yields. This should offset the sub-trend yields expected in the Western Corn Belt. Although I anticipate final corn acreage could fall about 2 million below current projections, I anticipate national yield near 155 bpa will keep the balance sheet well supplied. World feed grain supplies are ample and US demand has reached a plateau.

The amply supplied corn S&D and historically tight soybean S&D suggest soybean futures continue to gain relative to corn. While this ratio has rallied from near 2.5 a month ago to near 2.95 today, fundamentals suggest there is still considerably more room to move higher. In similar years, it is not uncommon for the soybean/corn ratio to push towards 3.2-3.5.

Regards,
Mark Ditsch
Ditsch Trading, LLC
September 9, 2013

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