

June 2018 Monthly Commentary

A perfect storm of weak emerging market currencies, favorable US weather, and most importantly a quickly escalating trade war that is essentially stopping US exports of soybeans to China combined to pummel US agricultural futures in the month of June. For the month, wheat lost 5%, KC wheat was down 13%, corn down 11%, soybean oil down 6%, soybean meal down 11%, and soybeans were the biggest loser dropping 16% in a single month.

A month ago it seemed as if the conflict between the US and China (and less notably the EU, Mexico, Canada, etc.) would find a resolution before tariffs were fully implemented. However, it became increasingly clear throughout the month that our protectionist president is committed to level the trade balance, in the meantime protecting some US industries at the expense of others – with US farmers and US agriculture obviously being the losers. The US decision to slap a 25% tariff on numerous Chinese imports has been met with counter measures from China, most notably a 25% tariff on US soybeans. These tariffs could be fully implemented in early July. It is important to note that China imports two-thirds of world soybean exports. US soybean futures have responded by giving back two-thirds of the value of the tariff. In the meantime, South American basis has slowly started to rally as China can be expected to bleed South American supplies dry in an attempt to avoid US soybeans. China is also likely to use more substitutes, import more soybean meal from neighboring countries (which, ironically, will be crushed primarily from US soybeans), and release soybean reserves in an effort to get by until South American new crop harvest early in 2019. If unresolved, this would cut US exports significantly and boost US 2018/19 carryout from approximately 400 million bushels easily up to the 700 million to 1 billion bushel range.

The question of course is: Are these tariffs actually reducing world demand and thus increasing world stocks, or are they just rearranging trade? I think it is a bit of both. Certainly, China will cut back on meal demand, increase use of substitutes, etc. Chinese imports could be flat or lower year-on-year, which has been virtually unheard of over the past 20 years. They will also buy up virtually all of the South American supplies now, and be lined up again in early 2019 post-South American harvest.

The strong Chinese pull on South American beans are likely to reduce South American soybean meal supplies between now and early 2019. This should boost US (and world) crush margins, encouraging max crush in the US and around the world (outside of China due to tariffs and South America due to the Chinese pull on soybeans). Long meal against short beans is a trade that will continue to work if there is no resolution.

In the meantime, US weather has quietly moved from ‘near-perfect’ to ‘non-threatening’ to ‘leaning too hot’. Soil moisture is solid, and that will allow for corn and soybeans to withstand some heat. Weather all the way through August and even early September will determine yields, and it does seem as if markets took risk premium out too quickly. Corn is less dependent on China, thus corn futures could bounce back on any weather concerns. The Black Sea and Europe are also having weather issues, which should provide underlying support for both wheat and corn, especially from these lower levels.

Soybean meal and the grains should lead rallies. Soybeans should lead breaks. Overall, it seems as if markets have gotten a little ahead of themselves to the downside – but the trade war, weather, and emerging market currencies will all continue to be very important in July.

Regards,



Mark Ditsch

July 2, 2018

The information contained herein has been taken from trade and statistical services and other sources we believe are reliable. Opinions expressed reflect judgments at this date and are subject to change without notice. Ditsch Trading, LLC does not guarantee that such information is accurate or complete and it should not be relied upon as such. There is risk of loss in trading futures and options and it is not suitable for all investors. PAST RESULTS ARE NOT NECESSARILY INDICATIVE OF FUTURE RETURNS. This document contains only commentary on economic, political, or market conditions and is not intended to be the basis for a decision to enter into any derivatives transaction. The contents of this commentary are for informational purposes only and under no circumstances should they be construed as an offer to sell or a solicitation to buy or sell any futures or options contract. This material cannot be copied, reproduced, modified, or redistributed without the written consent of Ditsch Trading, LLC. No one has been authorized to distribute this for sale.