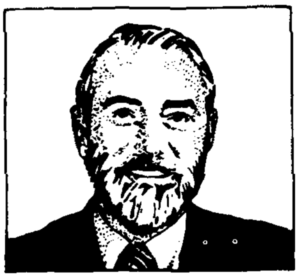
Soybeans and the stock market

The following article was prepared in late October by David H. Bartholomew, oilseed specialist for Merrill Lynch Futures Inc. at the Chicago Board of Trade.



Weakness in the stock market in recent days has had a similar effect in the soybean complex. It happened this way. Much of the long positions were held by speculators, and an important percentage was held by participants in managed fund accounts. At least some of those accounts also were involved in stock index trading. As that collapsed, the managers found it desirable or necessary to liquidate long positions in agricultural commodities in order to conserve equity and maybe to meet margin calls in stock indexes.

Then came massive commercial buying in soybeans and soybean meal plus corn, said to be against sales to the Soviet Union or East Europe or both. Herein lies a situation that is extremely significant in the global economic picture.

It is inevitable that parallels be drawn between the 1929 stock market and this week's collapse. Even the dates in October in both years are frighteningly similar. In both instances, there were policy developments in the preceding years that created the environment making conditions right for a collapse. More than 10 years ago, I began making a list of policy decisions being made that could lead to economic chaos.

Those decisions have not been reversed, and are not likely to be, so more chaotic times lie ahead. These could be potentially much more severe than this week's brief sampler. As for the stock market specifically, here is a most intriguing consideration. On every occasion in the past when it has broken down due to poor economic conditions, it has dropped by the same percentage as the then existing margin allowance; i.e., when the requirement was 70%, stocks declined 30%. In other words, the amount of leveraged investment is wiped out before the market stabilizes and recovers. Currently, the margin requirement is 50%. So it is to be expected that the Dow Jones can drop to about 1350 from its recent high of 2700 before stabilizing. Maybe a new high will be made before the 50% drop is accomplished, in which case the low would be proportionately higher. However, the formula is sound for a viable economic reason. Even if the margin requirement changes, the formula still would apply.

Some things are not the same as in the 1920s leading to the 1929 collapse and the chaos which followed, and that may be of considerable benefit. One of special interest to the agricultural sector is the Russian situation referred to previously. Russia is a major importer of grains and oilseeds and products. This was not true in the 1920s and 1930s. That country was then a leading exporter of wheat. But with huge world surplusses and very poor marketing expertise, the Russians just loaded ships and sent them to Europe unsold, accepting whatever the buyers would pay. This practice guaranteed that prices would keep falling. (Incidentally, they did something similar more recently. In 1967, sunflowerseed oil was dumped on Europe to such an extent that the EEC imposed a countervailing duty). But now the Soviet Union almost consistently is unable to be even self-sufficient, and it will be several years before new agricultural and social policies could possibly change that. As long as gold and/or petroleum values do not weaken too much, Russian import needs will continue to be an economic supporting factor of significance.

The prospect of an EEC oils tax could become more real in upcoming discussions. When world prices of oilseeds and grains decline, there is a greater drain on the EEC budget for export subsidy purposes. Thus, additional sources of revenue will have to be found because of an already tight financial situation.

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