Fats & Oils Outlook

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For Soybeans Now It Is Demand Versus Supply

For the first half of the United States marketing year (Sept.-Feb.), the market is most responsive to supply considerations. Harvest begins in September and is mostly completed by November. There are crop estimates in August, September, October, November, and January. So market traders go from one report to the next registering their opinions about crop size as either being too much or not enough. That's easy to do. The government provides the figures. Most traders prefer to use the simple approach.

Calculating demand is much more difficult. It requires much more independent thought. And if the results of such effort seem too radical, there is a challenge to one's credibility.

So most market traders defer serious consideration of demand factors until the season is half gone. By that time they can view consumption reports for the first half and then project these trends into the second half of the season. This approach is much more secure. There is less problem with a "credibility gap" in one's projections.

It's true that there are some individuals who make demand projections earlier. But too often these are based on econometric models designed by persons looking only at past performance statistics. Frequently this mathematical sophistication is employed to compensate for a lack of personal experience – experience that would explain market anomalies that are not otherwise detectable.

During the past several years USDA has been publishing demand projections made by their economists following each crop-and-stocks report. The decision to publish these is commendable. Previously these were available only to select persons in the industry, though eventually they became public information in government periodical publications. But there is one problem with these estimates of demand. The market trader tends to place too much emphasis on them, again preferring to have information handed to him instead of doing some independent thinking.

We detect a weakness in the USDA demand projection procedure that should be noted by the market trader. It is the generally conservative policy adopted by the government economists. In seasons when demand is expanding, the successive revisions published are only gradually increased. Never do they project the full extent of expansion early in the trend. The exact opposite is true in seasons of retarded demand.

There is, of course, a readily understood reason why the government agency would adopt a conservative policy. To publish a clearly bullish figure early in the season would force prices up, and ultimate demand might fail to be so large. It could also induce farmers to hold supplies off the market in hope of prices higher than can be achieved. On the other hand, to publish a clearly bearish estimate too soon could unnecessarily reduce farm income.

A dramatic example of the latter circumstance was in the 1975/76 season. The first demand estimate left a carryover projection of 470 million bushels. Prices dropped to the $4.50/5.00 area and stayed there for four months. Many farmers were sold out before the early spring advance to $7.00 was realized. This was a situation where government economists were very slow to recognize a change of trend in demand, from sluggish to sharply larger. Part of the cause, of course, was farmer's selling heavily into market channels, making the soybeans available for expanded consumption at very attractive prices. The actual carryover was only 245 million bushels.

What then does demand look like for the remainder of this season? It's exceptionally good! Still in force are the dominant influences we referred to in earlier articles. Most significant are the weak dollar and the big vegetable oil imports by India and other countries. We expect the carryover at the end of this season to be only moderately comfortable at about 150 million bushels. The latest USDA projection was 270 million, while the previous one said 250 million bushels. It could go even lower than 150 million if the South American crop is no larger than last season. Weather problems still exist there.

Now for a word about next season's supply. It looks larger. Just how much will be a significant question for months to come. The January planting intentions report showed 8% larger acreage. When the survey was made, soybean price was $6.00 per bushel, and this looked better than major alternatives such as corn and cotton. That could change to the advantage or disadvantage of soybeans by the time planting takes place in April to June. Moreover, when the survey was made, farmers had been told of tentative government plans to have an acreage reduction program for corn, with compensatory payments to those who cooperate. If that program is not widely accepted, then some area will no doubt switch back from soybeans to corn. Additionally farmers had assumed the government support price will be raised from the 1977 crop level of $3.50 per bushel. If it is not, or is not raised to at least $4.00 or more, then some of the intended soybean expansion will revert to corn or other crops.

Another consideration in determining actual planted acreage will be the weather at planting time. Corn and cotton are planted before soybeans in most areas. If weather is cold or wet when these crops should be sown, then there could be a last minute decision to switch toward soybeans.

The next planting intentions report will be released April 13 based on a survey taken the first of that month. Until then, the market for new crop soybeans will be sensitive to its potential modification.

One additional observation about 1978 crop potential is in order. Soil moisture supplies in the U.S. are very good, and certainly much better than last year. Moreover, we would point out that in our study of long term weather cycles, the best seasons are those near the end of the decade. So 1978 should see very good yields. Therefore, it could be that once again surplus stocks will be accumulating in the next two or three seasons, partly due to a higher government support price that overstimulates soybean acreage. The same thing happened in 1967 to 1970. If these circumstances come to reality, we would project prices to drop below $5.00 late this year and into 1979.

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Soybean price predicting studied

Feature article in the February 1978 Fats and Oils Situation is an article by R. McFall Lamm Jr. on "A Simple Model for Predicting Quarterly Prices for Soybeans, Soybean Oil, and Soybean Meal." Lamm is a USDA agricultural economist. •