Is there anybody out there?

Bring your oxygen tanks. Before we get to Happy Valley, the mountain we have to climb is much taller than it looks.

When I try to talk about old crop corn everyone tunes out as they believe there will be so much early new crop corn harvested this year that the situation will resolve itself. As far as I know the Deep South and the Mid South are planting 350 extra acres this year. If all goes well that is 50 million bushels of August corn available over and above a year ago. I simply do not believe that there will be a meaningful amount of August corn harvested in the Midwest. There may be plenty of mid September or even early September corn, but as I will try to explain, the big hole in the balance sheet will occur much earlier.

According to the USDA on March1, 2012, we have 514 million bushels less corn on hand than a year ago. I believe the shortfall is far greater. Several factors come into play. The first is test weight. The United States is the only place on the planet, apart from some tribes in Papua, New Guinea, that does not weigh its grain. It measures it by volume. Since each bushel may have a different weight than the standard 56 pounds per bushel, it is like assuming that every similarly sized suitcase on the carousel weighs exactly the same. During the harvest of 2010, I warned my clients that although the crop was much smaller than what was commonly believed, ironically it would grow as we consumed it. It was a very poor yield with a very good test weight. I have just finished a comprehensive study of thousands of test results in fifteen corn states that shows that this year's test weight averages .76 of a pound or 1.35 percent below last year. So the 6.009 billion bushels of corn on hand March1 are really 5.927 billion bushels or 82 million less. The 514 million bushel shortfall now becomes 596.

Secondly, as I have been saying for some time, the USDA doesn't "do" pipelines. They believe the amount of corn in transit is a constant. It is not. In March 2011 the basis was historically weak, yet by September 1st, 2011 the basis was on fire. Clearly the pipeline had contracted sharply. On March 1st this year the basis was at all time highs indicating a continued empty pipeline. We do not have the luxury of de-pipelining as we did last year. You cannot de-pipeline twice without filling up in between. Given that a normal pipeline of corn would contain close to 1 billion bushels, the difference between a heavy pipeline and a very empty pipeline could easily be 200 million bushels. The shortfall of 596 million bushels now become 796. Is there any corn out there?

Has anyone really thought through the logic of the USDA not calculating changes in the pipeline? March 1 stocks are therefore about 5/6th supposed fact and 1/6th fantasy. The June 1 stocks are 2/3 supposed fact and 1/3 fantasy. Things get really interesting by September. The Sep 1 stocks last year were reportedly 1.1 billions bushels. Since I do not think that it is possible to have a pipeline below 750 million, 350 were supposed fact and 750 fantasy. Therefore, at least 68 percent of the Sep 1 stocks number is uncorroborated statistical fluff. If 30 percent of a survey strives for accuracy and 70 percent is completely bogus, then surely the entire survey is bogus. In a tight carry out year like last year, the USDA methodology of not counting corn in transit automatically excludes their data from having any legitimacy whatsoever. Yet this number is taken by the entire trade as gospel. Well, not according to John.

In last Friday's report, there were 122 million bushels less sorghum,barley and oats. That is 122 million bushels fewer feed grains available to compete with corn than last year (the total amount of corn, wheat, barley and sorghum on March 1 this year is a staggering 866 million bushels less than March 2011). Counting sorghum,barley and oats the shortfall now becomes 918 million bushels versus last year.

Since mid 2011 the ethanol industry has started to strip corn oil out of distiller's grains (DDG'S). From March 2011 to March 2012 I am told that at least 50 percent of the ethanol grind has moved to this practice. This means that 15 million tons of DDG'S that compete with corn as domestic feedstock have had some feed value removed. Since the feed value of corn oil is energy, a good part of what will replace it will be corn which is energy rich. I understand that in the chicken industry up to 70 percent of the shortfall is being made up with corn. And if just 10 percent of the feed value of the DDG has been extracted then 1.5 million tons of feed are missing, compared to a year ago, or 750 thousand tons March to Sep. If corn replaces 50 percent of this feed, that equals another 12 million bushels of corn being fed. Now the shortfall is 930 million. Compared to a year ago the corn-meal ratio is much lower today suggesting that corn will be hotter in the ration going forward. People in the chicken and hog industries tell me that they are using more corn than a year ago, so they are moving in the wrong direction. The real shortfall is now somewhat higher than 930. Is there any corn out there?

The March stock survey is taken around March 1st. If 50 percent of the survey was taken prior to February 29, then half of the survey would exclude the leap year effect This will increase my shortfall by 17 million bushels. Accuse me of nitpicking, but if the trade wants to make such a hullaballoo of 50 million bushels of corn harvested in August, I am entitled to my leap year effect and round out my shortfall to 950 million bushels.

The argument that the ethanol yield is 2.8 gallons and not 2.7 per bushel is valid. The USDA knows this but they would rather have a consistent error as opposed to correcting an error. However, I do not believe that there has been any efficiency improvement in the yield from last year so each gallon the ethanol industry produces this year will require the same amount of corn as last year. Effectively ethanol has been using less corn for years and animals have been eating more corn.

Lastly there is the perennial USDA fudge factor. I recently did a study of the seasonal movement of corn from on farm to off farm as a percentage of total supplies using USDA data for fifteen years. The results were, as I expected, so strikingly constant over the entire fifteen years, they could only have been created by man. I have thought for a long time that the USDA strongly believes in their off farm statistics, and in their own words the overall stocks are evaluated in line with their balance sheet. Therefore the on farm stocks become a residual dumping ground, just as in the supply and demand, the feed number is nothing more than a huge funeral pyre for all their collective errors. I recently conducted a nonscientific survey of on farm stocks in Illinois. The average was down by close to 10 percent from last year. The USDA pegged Illinois on farm stocks at exactly the same as a year ago, while off farm was down 16.5 percent. Go ahead and pull the other leg! It came to my attention last year, that every state total off farm is calculated to the nearest thousand bushel. The on farm stocks are calculated to the nearest 1 million bushel, and the large states on farm are calculated to the nearest 10 million bushel. Is the USDA telling us that their off farm calculation is between 1 thousand and 10 thousand times more accurate than their on farm? I would presume so. The USDA gives the off farm stacks their best shot. The on farm comes from the fudge factory. God only knows how much higher the USDA fudge factor increases the shortfall.

Now let us bring in the early Southern corn and reduce the shortfall by 50 million bushels. We will then have put it into its true perspective.

To sum up, from March1 we needed to reduce consumption by more than 900 million bushels compared to last year, to get to the same carry out on Sep 1. And at the end of last crop year the basis was on fire, telling us that we were running on fumes, close to a minimum carry out. I presume end consumers now own corn until at least May 1. In my book we have four months to ration over 900 million bushels of corn and I suspect in one month's time it will still be over 900 million bushels, but now in only three months. This amount of rationing would amount to 33 percent across the board. But exports will not be rationed and the hog industry has locked in record profits through the end of the year so there is nothing to ration there. The cattle industry, at an extreme, could consume 200 million bushels more wheat than a year ago. We would then need to ration 700 million bushels between ethanol and the chicken industry. In the last quarter of last year, those industries consumed 1.63 billion bushels. They would need to ration 42 percent from June to August versus last year. People ask me how high will corn go under this scenario. I respond with a precision that comes directly from the USDA statistical handbook, think of a number and double it.

I am told the view of Happy Valley is spectacular from on high. See you at the Summit!

John Macintosh
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