16 June 2012

“My sympathies to your subscriber who recently asked about corn. Sympathies because it appears that he has got himself entangled with a truly dysfunctional market. The corn basis has been posting record high levels for months, and now it is screaming that we appear to be on the verge of running out. You would never know it looking at a chart of July corn. The Illinois river stations, on which the contract is based, are bidding up to 80 over July futures. For cash and futures to be in equilibrium they should be 6 under July futures. Anyone trading the grain markets must realize that the contract is heavily biased in favour of the short. The domestic user is locked out of taking delivery as the contract is based on exports to Centre Gulf. Centre Gulf exports at this time of the year are between 5 and 10% max of total consumption. Last September Eastern belt corn processors were running out of corn, but the Sep/Dec spread was near full carry. The CME showed its true colours during the MF Global fiasco. It cares not two hoots about integrity. It has sold out is core, the hedgers, to high frequency trading. The only convergence is between shareholder equity and director compensation. There is no convergence between cash and futures until perhaps the last minute when the CFTC makes sure that positions are so small as to be meaningless to a large trader. If you want transparency, leave the CBOT building and walk 3 blocks west. Look down into the Chicago river and you will find greater transparency in its depths than we have on the grain floor. The CFTC is Fairy Godmother, Guardian Angel and Patron Saint to the short. If you are short during the delivery cycle when the basis is above delivery, you may sleep tight. But if you are a long, even when the basis is on fire, and you should be able to exercise your right to turn futures into cash, the CFTC will go into the dungeon and wheel out the rusty and blood stained tools of the Spanish Inquisition.

“To the CFTC and the CME, just add the USDA, and you have the perfect Hose Me Trinity for the long. The stubborn pigheaded stupidity of the USDA knows no bounds. Last year they claim domestic feeding of corn dropped 79 % from the first quarter to the last quarter, with roughly the same number of animals. As I said at the time, what are the animals eating, chicken on grass, hogs on pork, cattle on Big Macs? Or is it the USDA on Jack Daniels? From May 2011 to May 2012 for the crop year of 2012 the USDA dropped domestic feeding of corn and other feed grains by almost 12%, and also reduced soybean meal and DDG production, the by product of ethanol, but at the same time, they increased production of milk ,eggs, poultry, pork and beef. At this rate within 6 years we will be producing ever more meat with zero corn and other feed grains. The wonders of modern science! Just this week the USDA, no doubt pursuing the dream of a Nobel Prize for most inventive bureaucratic data, raised their Chinese corn carry out for this year from an already ludicrous 57.9 million tons to 59 million tons. This year the Chinese substituted some 30 million tons of wheat for corn, imported Australian feed wheat, and are importing 5 million tons of US corn. Despite all that, Chinese corn prices remain in the stratosphere. To suggest that China will carry out four months usage is truly mind boggling.

“A glimpse into the mindset of the USDA was provided by Will county radio last month. The head of the USDA World Out look division (WASDE) was interviewed for about 40 minutes. Everyone listener whom I know was amazed at how he managed to tie himself in knots , contradict himself and say the most ridiculous things. Twice he talked about the grain market on the ICE trading platform in 1994??? He defended the discarding of last years bad corn yield in the trend line, because "our sophisticated computer told us to". He then said that heat at pollination was the culprit. So pray, what did the USDA do to the corn yield from July 1 2010 to August 1 in 2010 when we also had blazing heat at pollination? They lowered the yield by only 1.5 bushels. They were subsequently forced to lower it another 12.5 bushels. Don't talk the talk if you cannot walk the walk. But his star act was defending last year's carry out which he said nly contained old crop corn. He was adamant as to its accuracy several times. But when asked if new crop corn had already been consumed straight off the farm, would that not artificially inflate old crop stocks? Well, that is when he started tying himself in knots. Houdini he was not. More like the Michelin man in a gale.

“Unfortunately, the disfunctionality of the corn market risks driving away those who need to use the market more and more into the hands of those who wish to distort it more and more. The wheat market has completely lost its purpose. Perhaps it is time to take the Goddess Ceres off the top of the building and replace it with a neon roulette wheel. And bring a thousand slot machines into those empty pits. Many years ago I would give seminars in Spanish to South Americans on the origins of futures trading and hedging. At the end of my talk I would take them to the visitor’s gallery above the pits, and proudly exclaim that this was the most efficient marketplace in the world, bar none. My oh my how times have changed. If I smell of sour grapes, then believe me that is not the case at all. The last few years have been extraordinarily kind to me. I have taken full advantage of the bad USDA data. In August 2010 my corn yield was 12 bushels below the USDA's. They got there many months later. What upsets me is the destruction of a beautiful meaningful viable market. If this is a cri de coeur, it is not for me, but for the institution itself.”

Best regards, John Macintosh