2007/08 Grain Market Outlook and Review

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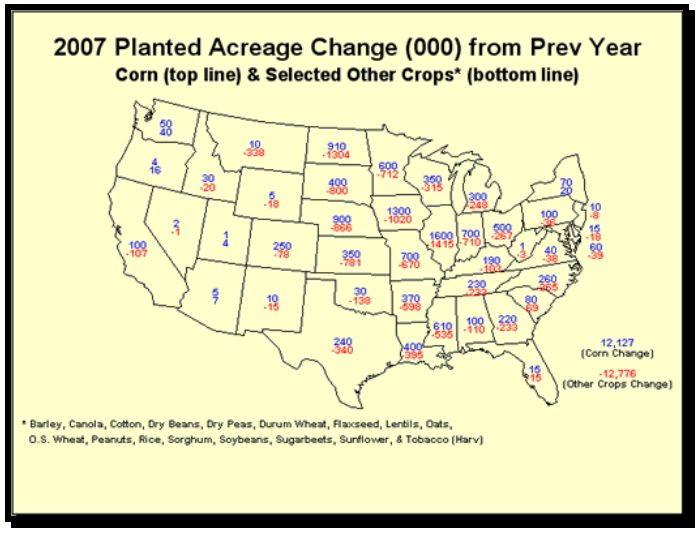
ONE OF THE LIMITATIONS OF HYPOTHETICAL PERFORMANCE RESULTS IS THAT THEY ARE GENERALLY PREPARED WITH THE BENEFIT OF HINDSIGHT. IN ADDITION, HYPOTHETICAL TRADING DOES NOT INVOLVE FINANCIAL RISK, AND NO HYPOTHETICAL TRADING RECORD CAN COMPLETELY ACCOUNT FOR THE IMPACT OF FINANCIAL RISK IN ACTUAL TRADING. FOR EXAMPLE, THE ABILITY TO WITHSTAND LOSSES OR TO ADHERE TO A PARTICULAR TRADING PROGRAM, IN SPITE OF TRADING LOSSES, ARE MATERIAL POINTS WHICH CAN ALSO ADVERSELY AFFECT ACTUAL TRADING RESULTS. THERE ARE NUMEROUS OTHER FACTORS RELATED TO THE MARKETS, IN GENERAL, OR TO THE IMPLEMENTATION OF ANY SPECIFIC TRADING PROGRAM WHICH CANNOT BE FULLY ACCOUNTED FOR IN THE PREPARATION OF HYPOTHETICAL PERFORMANCE RESULTS AND ALL OF WHICH CAN ADVERSELY AFFECT ACTUAL TRADING RESULTS.

TABLE OF CONTENTS

2007/08 GRAIN MARKET OVERVIEW

The 2007/08 growing season looks like it will be an incredibly interesting year for Grain traders.

The year started off with the greatest acreage shift in history. According to the *Prospective Plantings* report, producers should plant 90.5 million acres of corn - the largest area since 1944 and 12.1 million acres more than in 2006. This increase in Corn acreage came in large part from a decrease in acreage from other crops – notably from Soybeans. U.S. farmers plan to plant 67.1 million acres of soybeans, the lowest total since 1996 and a decrease of 8.4 million acres – or 11 percent – from 2006.



However, the run-up in Corn acreage is off-set in great part by increased demand, all from ethanol as higher prices are expected to decrease exports and feed demand. With Total Usage forecast at 12.46 billion bushels, the record crop forecast will still result in a "Very Tight" supply to usage situation.

Conversely, Soybeans which are expected to see a drop in acreage of 11%, are being forecast to an increase in Ending Stocks of 166 thousand bushels and an "Excessive" supply to demand situation.

In the Soy Complex, the big winner may well be the Meal. The loss of Corn for feed purposes is forecast to result in increased domestic usage of Soymeal. The result of lower supply, coupled with increased usage should result in a "Very Tight" supply to usage situation.

The Wheat market should see a transition back to normal pricing of protein, meaning that Hard Red Winter Wheat (symbol KW) should once again trade at a premium to the lower protein content Soft Red Winter Wheat (symbol W).

Using the "Modified Grandmill" Tables on the following pages, we are forecasting the following price scenarios:

GRAIN FUTURES PROJECTED RANGES

Contract	Stocks /Use	Class	Projected High	Projected Low
C2007Z	7.6%	*Extremely Tight*	439	331
S2007X	20.3%	*Excessive*	903	710
SM2007Z	0.70%	*Tight*	256	193
BO2007Z	10.3%	*Normal*	37.00	29.00
W2007Z	23.4%	*Plentiful*	578	440
KW2007Z	18.0%	*Extremely Tight*	600	450

Note: Projected High/Low derived from appropriate average % changes from specific Grandmill Tables using May 15th, 2007 settlement prices

With demand being so huge, traders should expect "weather" markets to begin sooner rather than later, as even small fluctuations in supply will have measurable effects on the supply/usage balances.

Hopefully traders can use the following pages to assist them in making rational and informed decisions in the coming months. Space is provided to update the records and estimates yourself, so you can always stay on top of how changes may effect the markets.

Understanding The Modified Grandmill Method

The Concept of the Right Price for Grain Futures

Much akin to a super market shopper, grain traders need to know when the price of a is "cheap" compared to supply and use, or if the price is "dear" relative to supply and use, and should be sold. The key to this right price for grain prices is the relationship between the Total Supply of a particular grain and its Total Use (demand).

The Total Supply of a grain underlying a particular grain futures market is the Beginning Stocks, plus Production, and Imports. When Total Supply is large, grain prices tend to fall under the weight of this excess, as end users put off buying the grain they need until later in the season when the current years production is available as well. When Total Supply is tight, grain prices tend to rally very strongly from planting to pollination as end user scramble to fulfill needs ahead of schedule when faced with higher probable prices.

Total Use is the amount of grain consumed or processed in any given marketing year. This includes domestic consumption (crushing), seed use, feed and residual use, exports, and other measures of disappearance. When Use is running at a strong pace, consumers tend to be aggressive in their purchases, while producers tend to with hold supply, causing early season rallies to be strong. However, when Use is slow, consumers tend to put off purchases, to avoid higher storage costs and increased chances of having their stocks spoil or become damaged. This tends to cause prices to break, especially during periods when the risk to supply is diminished (around pollination) or when supply is plentiful (harvest).

So even though in plenty of years, grain prices do tend to rally from planting to pollination, and break from pollination to harvest, in many years they do not because of the current Supply and Use situation. But, if one can understand when prices are "cheap" or "expensive" relative to Supply and Use, then this "right price" can be used in conjunction with the seasonal nature of grain prices to make more accurate price forecasts.

Finding the "Right Price"

The author Wm. Grandmill's greatest contribution to grain futures trading was his work with comparing Ending Stocks to Total Use. Grandmill hypothesized (we believe correctly) that the relationship between supply as a percentage of Total Use can correctly forecast the general trend of grain futures prices months into the future.

Ending Stocks are used because Ending Stocks represent the amount of grain left over from this crop year "carried over" into next crop year. Ending Stocks is simply the surplus left over at the end of the year .

Total Supply - Total Use = Ending Stocks

By using Ending Stocks as the measure of supply, one can see in a nut shell when Supply is growing relative to Use, and vice versa. Because Ending Stocks can very greatly from year to year, and the absolute size has increased dramatically in the past decade, this figure can not be used alone. Just

using ending stocks is like saying that weighs 200 pounds, and saying they are fat. If this person is 6' 6" tall, then a 200 pound person may be quite thin, while a 200 pound 5' tall person, may be portly. Just as doctors look at height relative to weight, the commodity trader must judge Ending Stocks relative to Total Use, to get an accurate forecast of the relationship between Supply and Use.

What Grandmill did was to compare all the Ending Stocks to Use ratios (Ending Stocks / Total Use) to the price of the particular commodity. What he found was that the higher the Ending Stocks to Use ratio was, the lower prices tended to be around harvest. Lower Ending Stocks to Use ratio's generated higher prices, as supply was tight.

Modified Grandmill Method

The same basic principles of the relationship between supply and demand are kept in tact with our modifications, however we have broken down supply to use into 5 categories and we use relative changes in prices (% change) instead of absolute price levels.

SAMPLE MODIFIED GRANDMILL TABLE FOR DECEMBER CORN

Classification	Stocks to Use	% Rally	% Break	% Close
Extremely Tight	<10%	16.0%	-12.5%	-4.0%
Tight	10.1 to 16%	14.0%	-14.0%	-4.5%
Normal	16.1 to 21.0%	13.0%	-14.5%	-6.0%
Plentiful	21.1 to 50.0%	8.0%	-7.0%	-18.0%
Excessive	>50.1%	6.0%	-16.0%	-6.1%

Note: % high refers to the average % change from the May 31st settle to highest price between June and November 31st (October 30th for November contracts). % Low refers to the average % change from the May 31st settle to the lowest price between June and November. % Settle refers to the average % change from the May settle to the November Settle (October for Soybeans). Past performance is not necessarily indicative of future results.

We examined the last 25 years of Ending Stocks to Usage ratios for the last 25 years and separated them into five descriptive classifications: Excessive, Plentiful, Normal, Tight, and Extremely Tight. For each of these classifications, we have calculated a typical market behavior for the percentage change to the seasonal high and low, and the % change from a start date to the end of the month prior to delivery of the futures contract being analyzed.

This methodology is intended to be used as a guide for identifying extreme pricing situations. These forecasts are not intended to predict absolute highs or lows, but are intended to identify periods where historically prices are “cheap” or “dear” relative to the known supply and usage situation. Pricing irregularities can and often do last for longer than usually can be expected, and prices can go extremely irrational levels, well beyond what is predicted by this model. None of these discounts this method, as its purpose is to identify extreme valuation. It is our belief that this technique can assist participants in the grain futures markets to identify periods of irrational pricing, thus hopefully allowing grain traders to place the situation in its proper context and act accordingly. Obviously, past performance does not guarantee future results.

Using the Grandmill method, one can put the relationship between supply and usage into perspective. Each month, around the 12th, the USDA/NASS issues the necessary information to make a “guesstimate” of price.

For example, on May 12th 2006 WASDE report showed the following:

Total Supply	12,786 million bushels
Total Use	11,645 million bushels
Ending Stocks	1,141million bushels

On May 31st, December '06 Corn (C2006Z) settled at 279 3/4. With a Stocks to Use Ratio (Ending Stocks/Total Use) of 9.8%, we check the tables for the December contract. A 9.8% Stocks to Use ratio classified as "Extremely Tight" and yields the following:

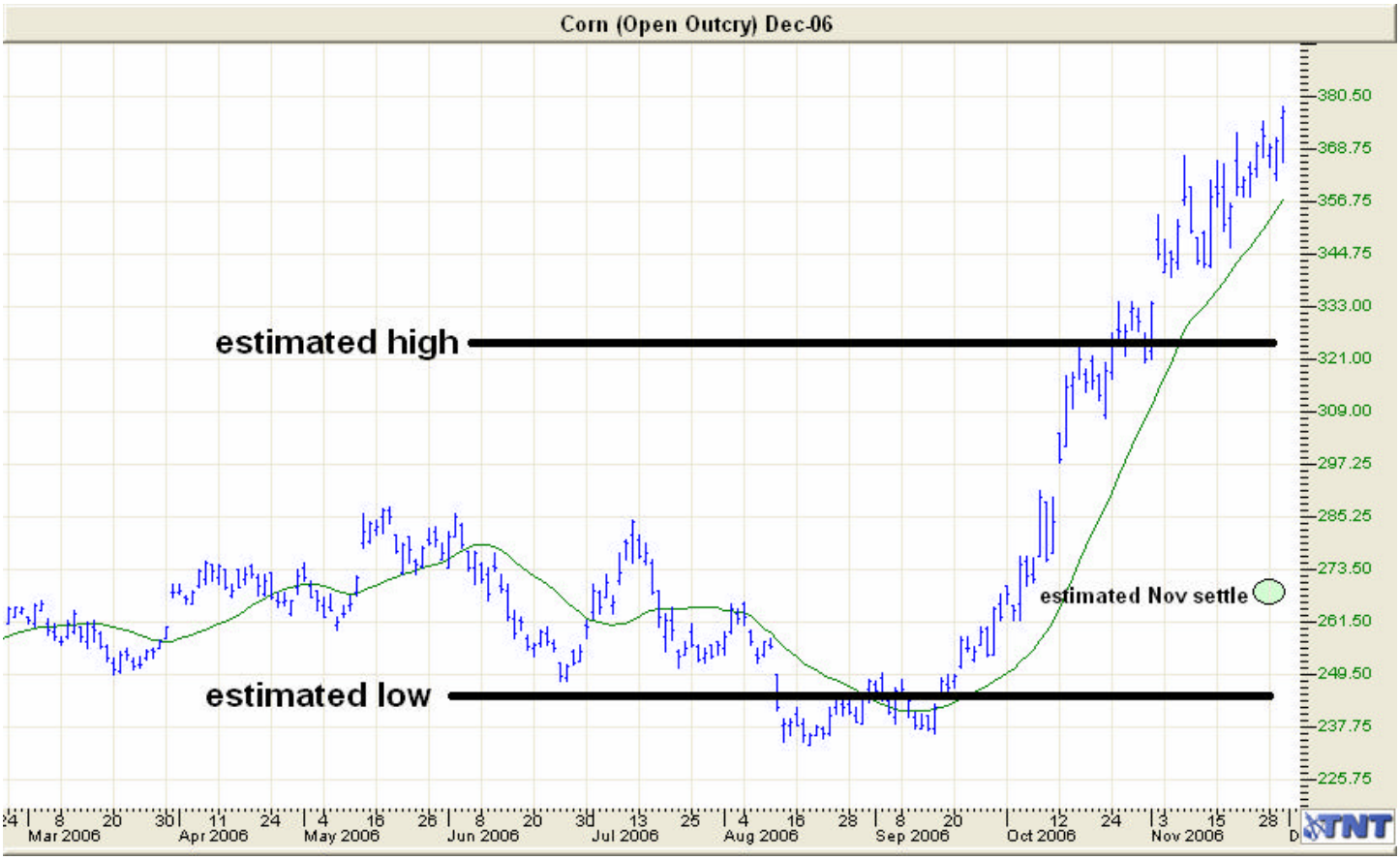
With a % Low of –12.5% and a % High of 16.0%, we can expect that December will have a range of 245 to 325 between June 1st 2006 and November 30th, 2006 and a November 30th, 2006 settlement of 268 basis the December '06 Corn contract. These figures were arrived at in the following fashion:

Low Price from 06/01 to 11/30 = May settle * (1+% Low)
= 279 3/4 * (1-.125) = 245

High Price from 06/1 to 11/30 = November Settle * (1+% High)
= 279 3/4 * (1+.16) = 325

November 30th settlement price = May Settle * (1+% settle)
= 279 3/4 * (1-.040= 268

The June to November High was 378, and the June to November low was 233 ½ , or slightly below the predicted low of 245, and the November settlement was 377, off from the anticipated settlement of 268.



However, though both the high and low extremes were violated, traders should be able to see the usefulness of this example. In August, traders should have realized that prices were extremely under valued. As such, when others were panicking about upcoming harvest, the informed trader was aware that the supply to use situation was still tight and prices should rally. Prices did rally, all the way from 233 ½ up to 378 in the ensuing months. Though prices exceeded the predicted high, traders should have been able to enjoy a great ride earlier in the season from a cheap situation to a expensive one.

Due note that not every year will yield as accurate results as this method was in 2006; however, understanding the relationship between Total Use and Ending Stocks and the resulting implications on price can be a powerful tool in the arsenal of grain traders, helping them to discern value in the grain markets.

Using the Grandmill Method

Use the following tables to record the "guesstimated" high and low prices for the December/November 2007 grain futures contracts. Each month, when a new USDA/WASDE report comes out, the forecasted prices can be adjusted – space is provided to assist traders in doing this.

Note: Total Supply, Total Use, and Ending Stocks are available from the USDA/NASS in the monthly World Agricultural Supply and Demand Estimates Report (WASDE). Classification, % High, % Low, and % Settle are derived from past performance and may not necessarily yield accurate results in the future. This is intended as a general market pricing guide, not as a solicitation to buy or sell. Past performance is not necessarily indicative of future results.