

Wheat Market Outlook and Price Report: September 17, 2018

By Marlene Boersch/ A.P. Temple
Mercantile Consulting Venture Inc.

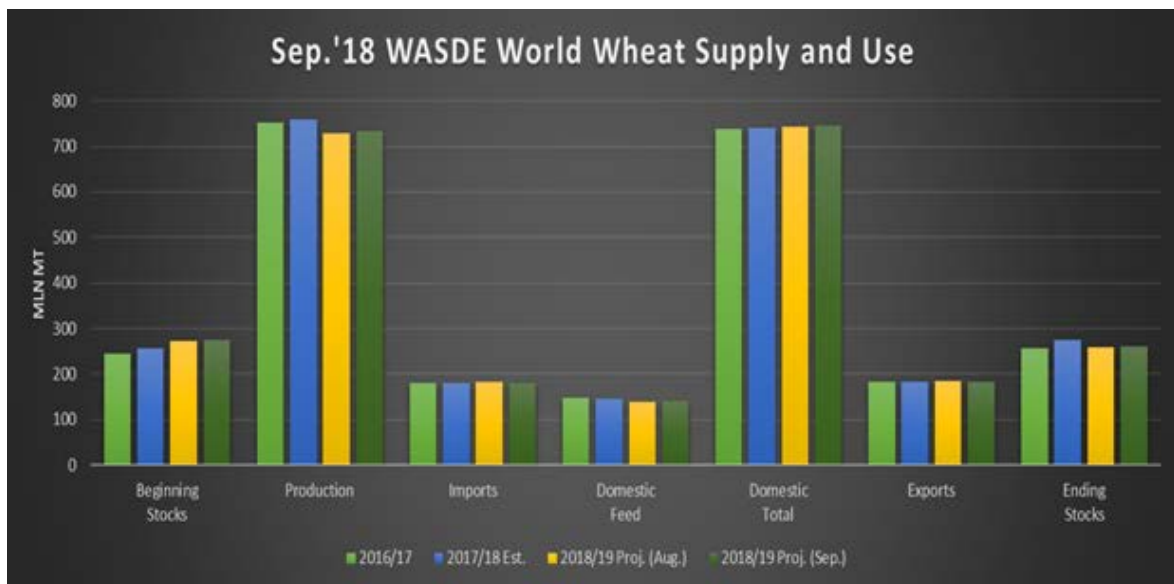
i) Background and Rationale for the Report

The following wheat market outlook and price report will be published on a weekly basis on the Sask Wheat Website. The report provides producers with an overview of world wheat markets, a market forecast, and benchmark prices at both the primary elevator and export positions (FOB Vancouver or elsewhere).

The report is made up of several sections. Following this section, a World Wheat overview is provided, which includes a summary of wheat market fundamentals, world production and trade, and a wheat market outlook. This is followed by several price tables, which include primary elevator bids at various Saskatchewan locations (Table 1), grain spreads (Table 2), and FOB port prices and basis (as measured by subtracting the primary elevator price (Rosetown) from the relevant port location price for individual crops) (Table 3). Table 3 is preceded by a description of the various assumptions, definitions and methodology used in arriving at the FOB port prices and in the export basis calculation.

ii) Wheat Market Outlook Sept. 17, 2018

September USDA - WASDE Report:



- The USDA/WASDE report left the overall US wheat balance sheet unchanged, *while increasing global total wheat supply by 4.7 mln mt on higher production and ending stocks.*
- The big surprise was that Russian production was increased by 3 mt to 71 mln mt on better than expected winter wheat harvest, and "excellent weather in the spring wheat belt" (which is against everything we have heard). Nevertheless, this increase caused global production to be 3.4 mln mt higher.
- Decreases were seen in Canadian (down 1 mln to 31.5 mln mt) and Australia (down 2 mln to 20 mln mt) wheat production, although less than StatsCan and ABARES numbers (we think StatsCan

numbers are too low and Sept is an important growing month for Aussie wheat, so there will likely be further revision of their crop in the Oct report).

- Russian and EU feed/residual numbers were increased to a more reasonable 8% decrease from last year as opposed to 16% in the last report.
- World exports were lowered due to decreases in Canada and Australia. However, EU, Russia (still at 35 mln mt), Ukraine, and US exports were left unchanged (US S&D's were left entirely unchanged as all changes made within wheat classes were off-setting)

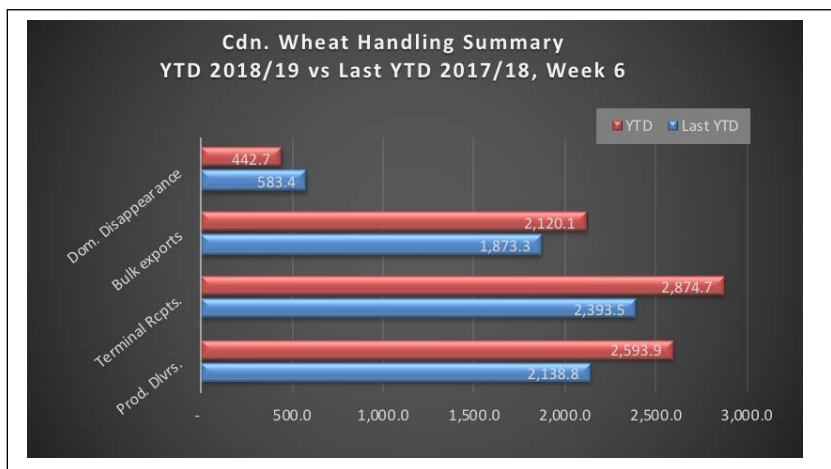
➤ **Global wheat production and trade:**

There is a lot of competition in the wheat markets as wheat is produced around the world. Below is a brief synopsis on last week's market events in the major wheat origins.

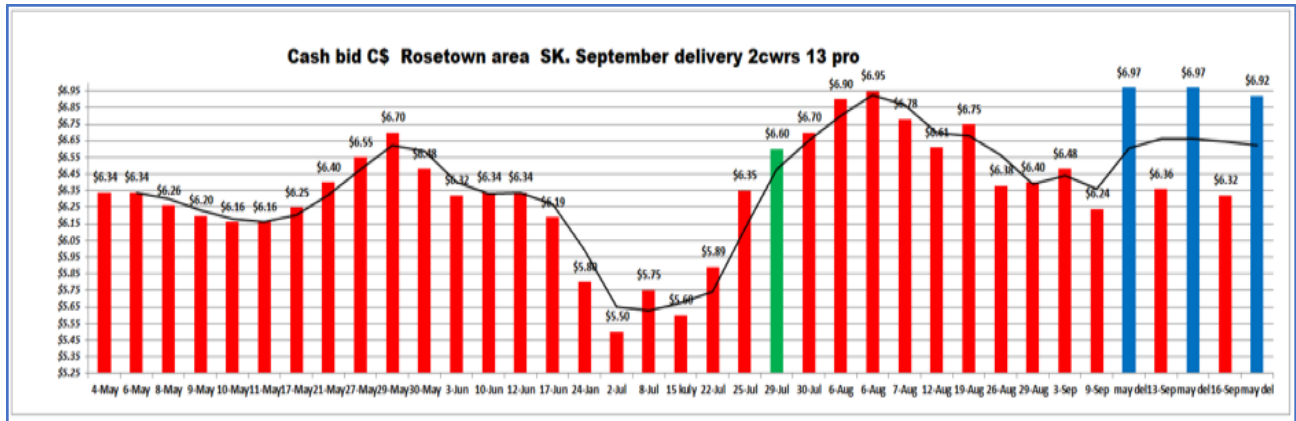
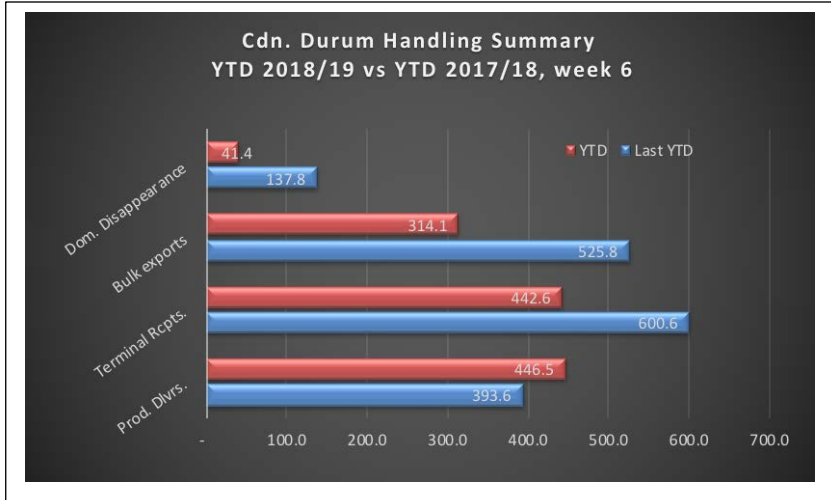
- **Futures:** Chicago winter wheat for Dec'18 contract closed at 511-4, up 14-4 cents in Friday's trade. Meanwhile, Dec'18 contract Kansas hard red winter wheat was up 14-4 cents at 516-2. In Minneapolis, Dec'18 contract hard red spring wheat closed at 572-2, up 10-2 in Friday's trade, while Mar'18 hard red spring wheat closed at 572-2, up 9-4 for the day.
 - *Pre-report, US futures were up 10-12 cents/bu as there were additional reports from Russia confirming that there is no change to the Russian situation and that the Russian Gov't will probably limit all-grain exports to around the 30 mln mt mark. Momentum was added to the wheat markets as ABARES in Australia lowered their wheat production further to 19.1 mln mt. The market then sold off following a precipitation forecast (incorrectly) in Australia and following the USDA report. Finally, uncertainty over Russian export constraints prompted a 10-15 cent rise in the wheat market Friday leaving us relatively unchanged for the week.*
- **Funds:** Last week we saw Funds get less bullish on wheat. Funds are near square in Chicago, and while still long in KC, their KC wheat position dropped by ~21%. Fund managers went net short for the first time in several months on Minneapolis hard red spring wheat prices. Any sustained rally in wheat will have to be led by the cash markets.
- **Matif:** Matif wheat in Europe traded in a €10/mt range but ended the week unchanged.

Canadian wheat:

- Harvest across the prairies is essentially at a standstill as a cold wet system has moved in and is reluctant to leave until mid-week at the earliest. Despite this, as of September 10th, SK producers were able to harvest 46% of the spring wheat crop as harvest progress is well advanced in the SW and SE regions of the province.
- YTD Cdn. wheat deliveries to week 6 (latest CGC data) at 2.6 mln are 13% (+455k mt) ahead of last year's wheat deliveries (2.1 mln mt). And exports at 2.1 mln mt are 13% (+247k mt) ahead of last year's (1.9 mln mt). Export terminal receipts are also ahead of last years by a respectable 20% (+481k mt).

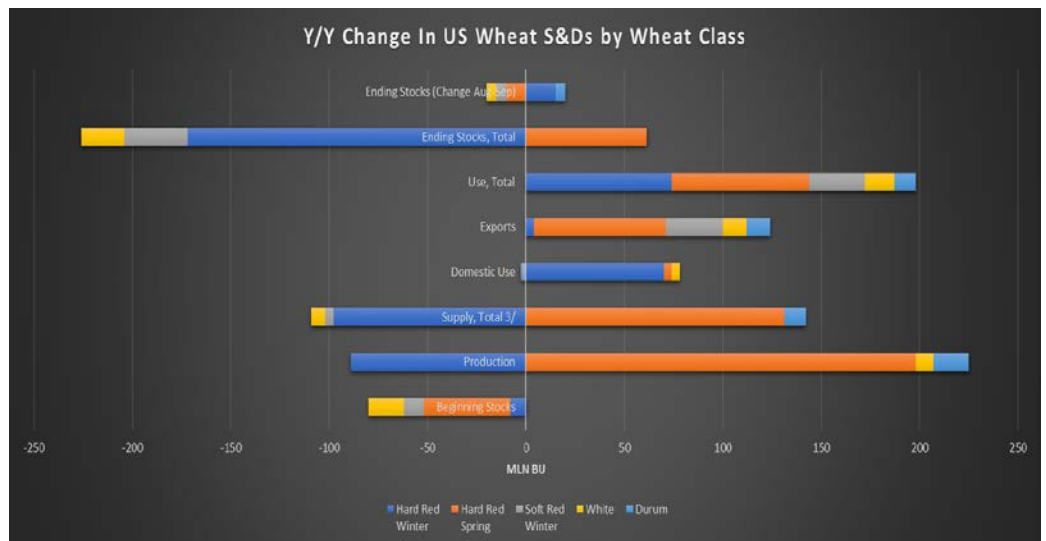


- SK durum was 73% harvested as of September 10th. Sixty percent of the durum crop is estimated to be 1CW while 34% of the crop is estimated to be 2CW and 6% is estimated to be 3CW.
- Regarding **Canadian grower bids for wheat**, note that in the chart below the blue columns show the bids for deferred delivery. As can be seen, the carry charges have widened and the prices bid for May in SK are not too bad.



US wheat:

- The USDA managed to arrange the changes in the US wheat S&D by class in such as way that there was no overall change to the US total wheat situation from the Aug to Sep reports.
- HRW and Durum ending stocks were increased 15 mln and 5 mln bu, respectively, which was perfectly off-set by decreases in HRS (-10 mln) SRW (-5 mln) and White (-5 mln). Overall, HRS, Durum and White wheat production is est. to be 198 mln, 9 mln, and 18 mln bu higher Y/Y while HRW is seen 89 mln bu lower.



- Total exports are estimated to be higher in all classes for a total of 124 mln bu.
- Ending stocks are lower for Durum, SRW and SRW by 171 mln, 32 mln and 22 mln bu, respectively, while HRS is est. to be 61 mln bu Y/Y.
- As per the USDA report, US durum Y/Y changes were: Production +18 mln bu; supply: +11; domestic consumption: -1 mln bu; exports: +12 mln bu; total use: +11mln bu, which means ending stocks are to be unchanged from last year (which is up 5 mln bu from the August report).

Australian wheat:

- USDA took 500k m off old crop Australian wheat exports, adding them into the 2018/19 carry-in. USDA took 500k mt off the 2018/19 feed demand, so with a 2 mln mt drop in exports offsetting the lower crop number (20 mln mt), Australian ending stocks actually rose by 1 mln mt (according to USDA).
- However, Australian wheat futures continue to hit contract highs on continued dryness and feed markets continue to pay well above Fob equivalent (over A\$400 for wheat and barley, A\$500 for hay). Large tonnages of wheat continued to move from the west of Australia to the east.
- ABARES (Australian stats agency) lowered wheat production further to 19.1 mln mt.

Argentine wheat:

- Confusion persisted over taxes, and no new export licences were taken out last week.
- BAGE (Buenos Aires Grain Exchange) implied potential yield losses due to the ongoing lack of rain although Gd/Exc ratings were up marginally for the week at 48% (versus last year's 66%).
- The USDA made no changes to either the old or new crop Argentine wheat balance sheet.

EU wheat:

- The USDA left the EU crop and export numbers unchanged, despite all the evidence to the contrary. Meanwhile, a higher carry-in and imports offset a 1 mln mt increase in feed usage, thereby leaving end stocks unchanged at an unsustainable 3.5 week's supply.
- EU shipments are still down 41% compared to last year.
- Algeria bought 630k mt of French wheat, so French wheat could potentially capture a large share of Friday's Saudi tender.

Black Sea wheat:

- Russian data suggests that by the end of September, wheat shipments could hit 14 mln mt. The trade will now watch to see if the Govt follows the USDA's revised 71 mln mt crop number.
- Black Sea Fob wheat prices ended down US\$5/mt with CBOT futures off \$4/mt and the Sep-Dec carry charge still at US\$21/mt.

➤ Significant purchases/ trades:

There was a good volume of cash trades last week:

- **Egypt** (GASC) bought 235,000 mt of Russian wheat for 25 Oct-4 Nov at US\$240.25/mt.
- **Algeria** bought 630,000 mt for Nov at \$262.50/mt (we think this was mostly French wheat).
- **Jordan** passed.
- **Saudi Arabia** bought 635k mt of wheat for Nov-Dec arrival against the tender for 595k mt at prices ranging from US\$267.63/mt (Jeddah) to US\$274.37 (Dammam). Prices were slightly lower than expected. Most of the wheat reportedly was sold from longs in the Baltic/ Germany, though French wheat was very competitive.
- **Tunisia** bought 50,000 mt of soft wheat at an average US\$231.75/mt, plus 75,000 mt of durum at US\$270/mt.
- **US wheat inspections** were 429,000 tonnes (season total 209 myn bushels down 31%), sales were 388,000 tonnes (season total 358 myn bushels down 24%). Iraq imports are expected to increase following the Government decision to cut the irrigated area by 50% due to water shortages.

➤ **Wheat Market Outlook:**

Significant events:

- **Turkey** banned the writing of contracts in US dollars or in Euros, and Turkish flour mills reportedly halted production due to new flour export regulations.
 - There are reports of 65 Turkish flour mills halting production due to the new flour export regulations (not bullish Russian Wheat).
- **Algeria** bought 630k mt of French wheat, so French wheat could potentially play a significant role in the big 595k mt Saudi wheat tender.
- The **USDA/WASDE report** left US wheat S&D's unchanged, while increasing global total wheat supply by 4.7mln mt on higher production and ending stocks.
 - The big surprise was that Russian production was increased by 3 mln mt to 71 mln mt on better than expected winter wheat harvest, and "excellent weather in the spring wheat belt" (this is against everything we have heard). Nevertheless, this increase caused global production to be 3.4 mln mt higher.

➤ **Outlook:**

We don't expect major weakness in the grain markets, which will probably be a little supportive to a bearish oilseed outlook. Politics and outside influences are still a major factor in the markets and there is talk of new duties and a meeting with the Chinese. The numbers show that so far, Trumps badly conceived duty activities have prejudiced the USA more than to the Chinese. Trade in July shows further negatives in the trade balance between China/USA with a 7pct loss to the USA mainly in Agriculture and Machinery products, and gain in Chinese imports into the USA. In our view, Trump needs to be very careful - the Trump administration is in danger of triggering inflation, which given the USA's record debt load could bring on another massive recession. There were also new comments that the Russians will put export duties on Russian wheat once 30 mln tonnes of sales are achieved.

Cash wheat markets remain essentially about Russian wheat, and if/when Russia will run out of cheap wheat. Funds are near square in Chicago, but still long in KC, so any sustained rally in wheat will have to be led by the cash markets.

Canadian bids for deferred delivery wheat are pretty good. Note the chart on page 3; it shows that carry charges have widened and the prices bid in SK for May wheat are not too bad.

iii) Primary Elevator Price Tables and Grade Spreads

Table 1: Canadian Primary Elevator Bids, in Canadian Dollars per Bu and per MT

NW Sask	Spot		NW Sask	Deferred	
	(bu.)	(mt)		May.'19 (bu.)	May '19 (mt.)
1 CWRS 13.5	\$6.61	\$242.88	1 CWRS 13.5	\$6.96	\$255.74
1 CWAD 13.0	\$6.13	\$225.24	1 CWAD 13.0	\$6.36	\$233.69
1 CPSR 11.5	\$5.59	\$205.40	1 CPSR 11.5	\$6.09	\$223.77
SW Sask			SW Sask		
1 CWRS 13.5	\$6.53	\$239.94	1 CWRS 13.5	\$6.86	\$252.06
1 CWAD 13.0	\$6.29	\$231.12	1 CWAD 13.0	\$6.43	\$236.26
1 CPSR 11.5	\$5.44	\$199.89	1 CPSR 11.5	\$6.01	\$220.83
NE Sask			NE Sask		
1 CWRS 13.5	\$6.32	\$232.22	1 CWRS 13.5	\$6.65	\$244.35
1 CWAD 13.0	\$5.89	\$216.42	1 CWAD 13.0	\$6.11	\$224.51
1 CPSR 11.5	\$5.41	\$198.79	1 CPSR 11.5	\$5.83	\$214.22
SE Sask			SE Sask		
1 CWRS 13.5	\$6.38	\$234.43	1 CWRS 13.5	\$6.74	\$247.65
1 CWAD 13.0	\$6.09	\$223.77	1 CWAD 13.0	\$6.32	\$232.22
1 CPSR 11.5	\$5.38	\$197.68	1 CPSR 11.5	\$5.85	\$214.95

Table 2: Grade Spreads, in Canadian Dollars per Bu and per MT

Avg. Grade Spread/ Pro Discounts	Cdn\$/bu.	Cdn.\$/mt
1 CWRS 14.0	0.11	4.15
1 CWRS 13.5	Base Grade	Base Grade
2 CWRS 13.5	(0.18)	(6.61)
1 CWRS 12.5	(0.37)	(13.60)
1 CWAD 13.0	Base Grade	Base Grade
1 CWAD 13.5	0.03	1.10
2 CWAD 13.0	(0.79)	(29.03)
2 CWAD 12.5	(0.97)	(35.64)

iv) FOB Wheat Prices and Export Basis Calculation

Background and Rationale:

Reporting FOB prices at port position and primary elevator prices allows the reader to gain an understanding of both local and international wheat prices and to understand the relationship between the two, as measured by the export basis. Export basis can be defined as FOB port position prices minus the primary elevator prices at any given prairie delivery location, and is therefore reflective of transportation costs plus any premiums being captured by terminal grain elevator companies or the railway companies, at any given time.

In general, a widening basis is indicative of decreasing system performance in terms of either reduced port capacity or rail service, or both. A narrowing basis is indicative of increased available

port capacity and/or better ability of the railways to provide ample service to grain shippers. In this regard, tracking these prices over time has value both in terms of producers being able to time the selling of their grain but also in terms of evaluating and setting policy related to various transportation and capacity issues.

Gray (2015) has calculated a normal basis to be in the range of C\$72/tonne. During the 2013/14 crop year the export basis for wheat widened to approximately C\$250/tonne, which indicated an inability of the grain handling and transportation system to adequately handle the record crop produced that year. This occurrence has highlighted the need to improve the level of rail service and take measures to expand port capacity where possible. It has also underscored the need for better price transparency and market information within the grain sector.

Assumptions, Definitions, and Methodology

The following background information should assist in understanding and interpreting international market signals and to relate them to the 'local' Saskatchewan wheat market:

- The price information generated for the weekly report is designed to show farmers at what price levels several wheat classes are trading at local primary elevators (Table 1) and in nearby international markets (Table 3). To express the Export Basis¹ (see *Export Basis* in Table 3) defined as Cdn. FOB Prices minus primary elevator bids, the FOB prices are translated into Cdn. dollars from US dollars and compared to current actual primary elevator Street prices at Rosetown, Saskatchewan (see *Street Prices* in Table 3). Rosetown is used as a proxy for all primary elevators in the basis calculation. The actual handling and transportation costs from the West Coast to delivered elevator (Rosetown area) range from ~C\$58.00-C\$74.72/mt, depending on number of cars moved and elevator used.
- Approximate relationship between U.S. wheat classes and Canadian wheat classes:
 - DNS 14% in the Pacific North West (PNW) ≈ 1 CWRS 13.5% in Vancouver
 - HRS in the Pacific North West (PNW) ≈ 2 CWRS 13.0% in Vancouver
 - HRW in the Pacific North West (PNW) ≈ 3 CWRS in Vancouver
 - SW (lowest price wheat) ≈ CPS red (mostly fed domestically)
 - HAD (Lakes) ≈ CWAD (Thunder Bay/ Lawrence)
 - Abbreviations: DNS (Dark Northern Spring Wheat); HRS (Hard Red Spring Wheat); HRW (Hard Red Winter Wheat); SW (Soft Wheat); HAD (Hard Amber Durum Wheat); CWRS (Canadian Western Red Spring Wheat); CPS (Canada Prairie Spring Wheat); CWAD (Canadian Western Amber Durum Wheat)
- Hard wheat price calculations:
Exporters in Western Canada generally derive their primary elevator wheat prices from HRS values at the West Coast (Pacific Northwest - PNW). Similarly, HRW values are used for lower grade (3) CWRS.

¹ Gray, R.S. (2015). The Economic Impacts of Elevated Export Basis Levels on Western Canadian Grain Producers 2012/13, 2013/14 and 2014/15.

“The difference between FOB Vancouver prices and the Saskatchewan elevator cash bids to producers is referred to as export basis: Basis can refer to the difference between any two prices. As the largest volume port, Vancouver FOB, minus the elevator bid prices representative measure of the “export” basis for grains in Western Canada.”

- West Coast HRS and HRW values essentially dominate the international hard wheat trade and determine its basic value.
- If premiums are paid for 1 CWRS 13.5, elevator companies are often able to retain the premium
- **Durum wheat price calculations:**

The primary export route for Canadian durum wheat is still through Thunder Bay, not the West Coast of Canada.

 - Nevertheless, the Pacific Coast has increased in importance for durum over time with 38% of total export volume crop year to date.
 - Italy is the single biggest buyer of Canadian durum wheat with 27% of total Canadian durum exports YTD (East Coast shipments).
- **Optional origin grain sales:**

Most major international grain companies sell 'optional origin' wheat to their customers and often cover their sales 'at best' closer to the shipment position. The Canadian grain system is not conducive to servicing optional origin sales because the volume of wheat kept in storage in port today is much smaller than prior to deregulation of the Canadian wheat market.

Table 3: Relevant FOB Prices and calculated Basis, US & Canadian Dollars per MT

Relevant FOB Prices and Export Basis			September 17, 2018	
Type of Wheat	FOB Prices CDA ¹ (calculated)		Street Prices	Export Basis ²
	West Coast (Cdn./mt\$)	Great Lakes (Cdn.\$/mt)	Rosetown (Cdn.\$/mt)	Basis: West Coast-Centr. SK (Cdn\$/mt)
DNS 14.0	\$325.08	\$296.43		
HRS	\$316.96			
HRW 11.5	\$305.50			
SWW 12.0	\$292.14			
1 CWRS 13.5 ³	\$325.08		\$242.14	\$82.93
2 CWRS 13.0 ³	\$316.96		\$227.81	\$89.15
3 CWRS ³	\$305.50		\$213.12	\$92.39
CPS ³	\$285.46		\$199.15	\$86.30
1 CWAD ⁴		\$312.66	\$227.81	\$84.85
Competing wheat: US\$/mt				
Russia 12.5 (Black Sea, 25k mt)				\$220.00
French 11.5 (Rouen)				\$236.06
APW 10.5 (W Coast)				
Argentine 12.0				
¹ FOB Prices CDA = FOB US\$ converted into Canadian Currency ² Export Basis = FOB Prices CDA minus Cdn. Street Price ³ DNS 14% = 1 CRWS 13.5%; HRS = 2 CWRS 13.0%; HRW = 3CWRS; SWW = CPS ⁴ Values derived to Lakehead FOB				

ADDENDUM

Futures Driven Basis Calculation, Canadian Dollars per MT

Canadian Wheat - World Price Parities					September 17, 2018
Canadian Funds	Grade				
PNW value/Vancouver	1CWRS13.5	2CWRS	3CWRS	Winter wht.	CPS
May/June delivery	\$8.67	\$8.44	\$8.13	\$7.77	\$7.77
Parity Track Rosetown	\$7.17	\$6.95	\$6.64	\$6.27	\$6.27
Track Bid Rosetown Area	\$6.59	\$6.20	\$5.80	\$5.42	\$5.42
Gross Margin at Elevator (\$/bu)*	\$0.58	\$0.75	\$0.84	\$0.85	\$0.85
Gross Margin at Elevator (\$/mt)*	\$21.26	\$27.48	\$30.72	\$31.32	\$31.32

* to cover elevation, elevator market risk, margin