

Wheat Market Outlook and Price Report: July 17th, 2017

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).

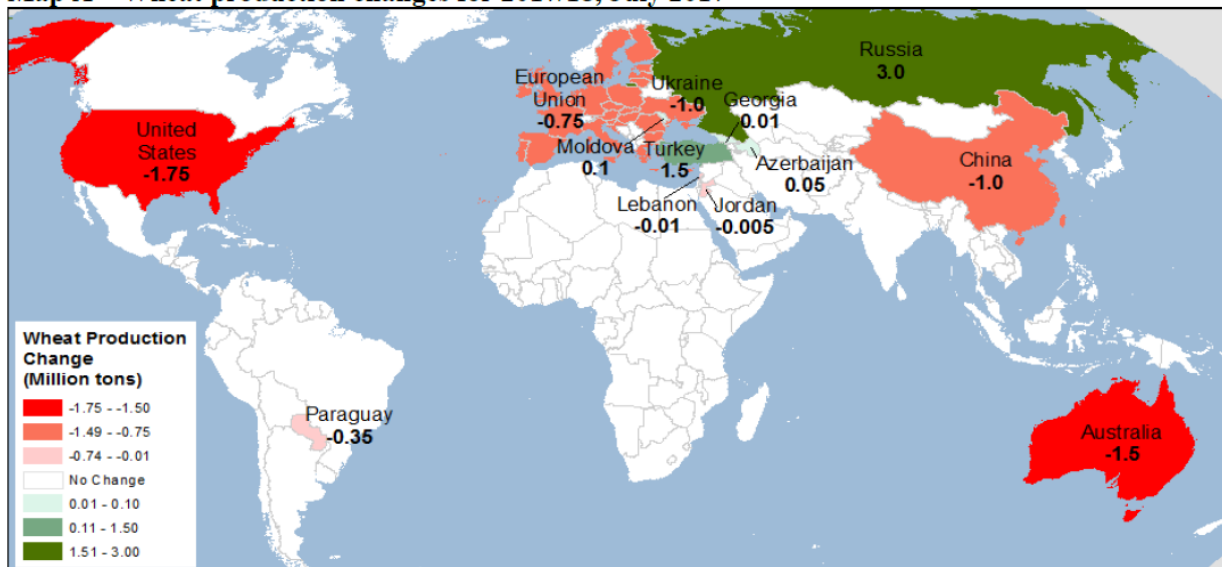
The report is made up of several sections. Following this section, a World Wheat overview is provided, which includes a summary of wheat market fundamentals, world production and trade, and a wheat market outlook. This is followed by several price tables, which include primary elevator bids at various 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 July. 14/17

2017/18 World Wheat Overview:

- **July 14th USDA Wheat Outlook Report:**
 - At 737.8 million mt, **world wheat production** for 2017/18 is projected to fall by 1.7 million mt from last month's estimates.
 - **Production estimates** have been reduced for the US, Australia, China, and Europe, while Russia and Turkey have been revised upwards due to favorable conditions.

Map A – Wheat production changes for 2017/18, July 2017



Source: USDA, Foreign Agricultural Service, Production, Supply, and Distribution online database.

- **July 12th USDA World Agriculture Supply and Demand Estimates (WASDE) report:**
 - **Russian wheat** production has been revised upwards by 3 million mt to 72 million mt, as weather and crop conditions seem on track with last year when Russia achieved record yields.
 - **Turkish production** estimates have also been revised upwards by 1.5 million mt due to favorable conditions.
 - **US, Australian, EU, and Chinese** production is estimated at a combined 5.05 million mt lower vs last month's estimates, largely on dry growing conditions.
 - **Ending stocks** for world wheat are now projected marginally lower at 260.6 million mt from last month's 261.2 million mt.

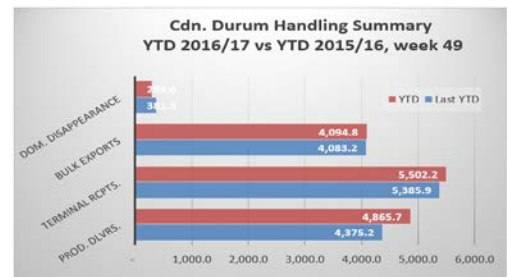
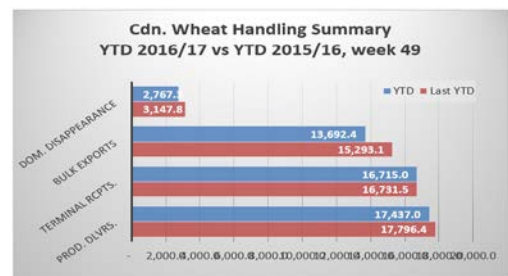
➤ **Global wheat production and trade:**

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

- **Futures:** Chicago September wheat closed down one cent in Fridays trade and was down by 24.2 cents for the week, while Minneapolis, September Hard Red Spring wheat closed up by 8.4 cents on Fridays, but down by 8.6 cents for the week
- **Funds:** The message of the Spec Funds was clear: They bought everything in style last week, covering their shorts. From Tuesday to Monday they bought ~21 million mt, +13 million mt grains and 6 million mt soybeans. Wednesday to Friday, they bought another 7 million mt overall, but sold 1 million mt of wheat. They are still long 1.4 million mt of wheat.
- Speculators are now long wheat in both Chicago and Kansas City, which is a reversal from the past three years. Unfortunately, without a corn production problem there is more than enough winter wheat to go around right now which may see them shift back to being short futures which would lower prices.
- **Matif:** Matif exchange in Europe closed at 174 which was down by 1.25 on Friday's trade and down by 5.00 for the week, which was a 2.8% decline in value.

Canadian wheat:

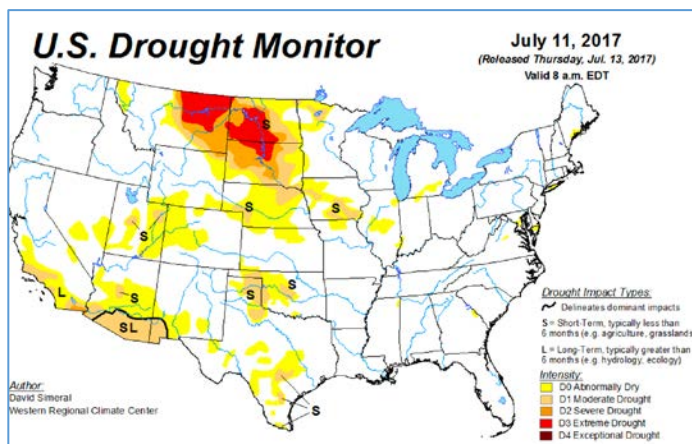
- According to the CGC, producers delivered 405k mt of wheat into the handling system, which is down from last week's 537k mt. Exports for week 49 were 365.5k mt, down from last week's 387k mt, and down 10% (-1.6 million mt) from last year's YTD exports.
- Producers delivered 74k mt of **durum** into the handling system over the past week. Durum *exports* during week 49 amounted to 19k mt; 4.095 million mt year-to-date. This is very close to last years year to date exports of 4.083 million mt.
- Manitoba: Dryness has been reported in parts of the south central and southwestern regions and rain would be beneficial.
- Saskatchewan's crop progress report indicates that most crops are developing normally, but that crop conditions vary greatly across the province. Hot temperatures and a lack of rain continue to be a concern in southern regions. Rainfall fell in amounts ranged from 0 – 80 mm across the province and topsoil moistures is rated as 2% surplus, 41% adequate, 46% short, and 11% very short. Many southern and central regions have received less than 100 mm or rain since April 1st.



- The July 11th Alberta crop report indicates that crop conditions across the province have declined by 5% since last week's report, largely due to hot dry weather in southern Alberta. 70% of crops in Alberta are currently rated as good or excellent, which is down from 75% last week, and slightly below the 5-year average of 73% good/excellent from this time of year. The largest declines in crop quality were in the southern and central regions of Alberta where crop condition declined by 11 and 6 percent respectively. Across the province, topsoil moisture ratings are 13% poor, 17% fair, 34% good, 25% excellent, and 11% excessive.

- **US wheat:**

In the July 9th USDA crop progress report the US winter wheat crop is reported to be 67% harvested vs 53% last week. The Kansas wheat harvest is now reported to be 99% complete with the harvest now centered in Colorado and Nebraska which are both 75% harvested as of July 14th. The harvest has also now progressed into South Dakota which is currently estimated to be 31% harvested and into eastern Montana which is estimated to be 5% harvested. *A significant percentage of the wheat crop in western South Dakota, eastern Montana, and western North Dakota has suffered from drought and will be baled for livestock feed.* According to USDA projections, US wheat production is set to fall to its lowest level since the 2002/2003 crop year and is now estimated to be 1.76 billion bu, which is down from last month's estimates of 1.82 billion bu. *However, the projections for US ending wheat stocks have still increased in the most recent WASDE report from 924 million bushels to 938 million bushels.* Private projections for US ending wheat stocks range from 722–957 million bushels, with the average estimate being 867 million bushels.



- **Australian wheat:**

Australia has had favorable rain which has helped to stabilize crop prospects, but production estimates for the Australian wheat crop have still been cut by 1.5 million mt in the latest WASDE report due to below normal rainfall.

Argentine wheat:

- Over the July 2–8 time period, Argentina is reported to have had heavy showers with adequate to locally excessive moisture. Projections for the Argentine wheat crop remain unchanged.

- **EU wheat:**

Widespread rain was reported over much of the continent which boosted some crop prospects, but Spain and regions of southern Europe remain dry. Conditions in the northern Ukraine are also reported unchanged from the previous drought status.

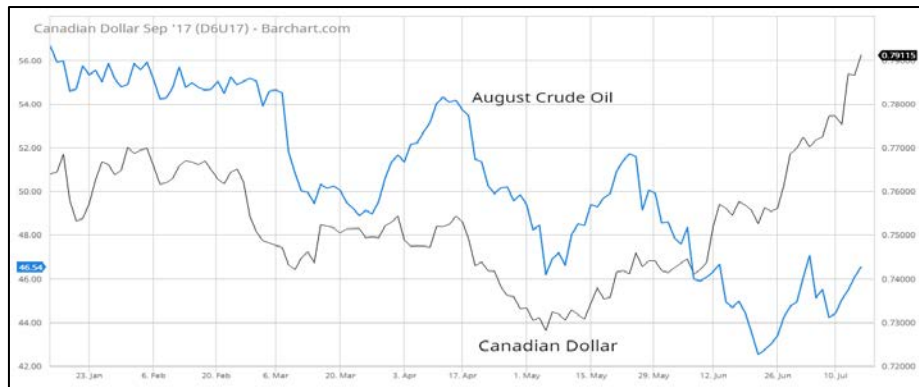
- **Black Sea wheat:**

- USDA raised the Russian crop by 3 million mt to 72 million mt (just below last year's record 72.5 million mt), and lowered the Ukrainian crop by 1 million mt
- Black Sea wheat prices had risen sharply ahead of the USDA report with the bid-offer on August at US\$196- 200/mt. The harvest pace was running some 40% less than a year ago and the early harvested wheat was showing low protein. But by Friday, August wheat had traded down to US\$195/mt and the bid-offer spread closed at US\$195-197/mt. The 11.5% protein discount ended at around US\$8/mt. Although feed wheat today does not calculate for new business, there is a big short program to Asia, which kept values around US\$180/mt Fob.

Wheat Market Outlook:

➤ Significant events:

- A significant event in the past week was the shift in the value of the Canadian dollar which has increased by 1.79% over the course of the week. This makes Canadian grain more expensive on the world market and has effectively lowered the Canadian cash bid values for grain commodities in western Canada. The value of the Canadian dollar has become less correlated with crude oil over the past month, and market valuation appears to be driven by other factors. Speculation about interest rate hikes has been ongoing for several months and most of the market was anticipating some type of an interest rate increase. Some of the correlation loss with crude oil might be attributed to investor speculation about a rate hike, and it seems probable that the dollar might fall in value in the coming months to once again follow the price of crude oil.



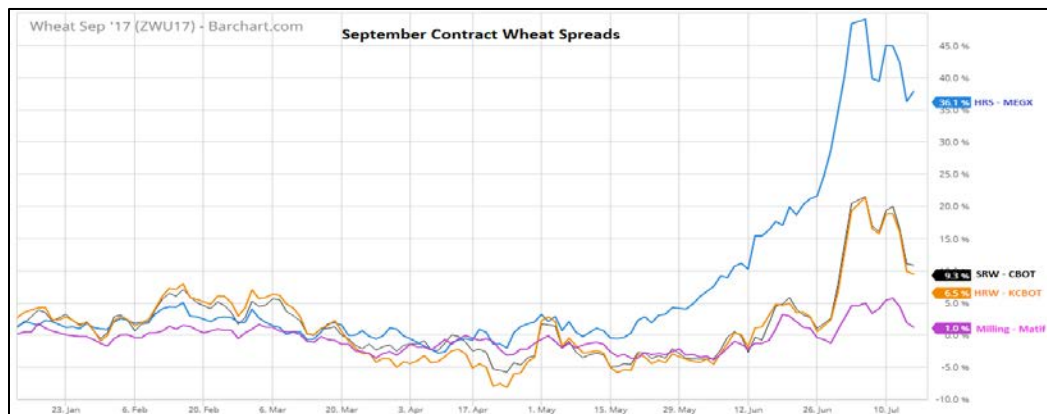
Significant purchases:

Not a lot to report here this week:

- **Jordan** passed on their tender and did not buy.
- **Tunisia** bought 25k mt at US\$205/mt and 17k mt at US\$208/mt.
- **Iraq** bought 50k mt Australian wheat at US\$319/mt.

➤ Outlook:

- Wheat spreads remain wide these will likely narrow to a more historically typical norm in the coming months.



- The WASDE report still shows the USA exporting spring wheat, which does not justify the current premium for spring wheat over hard wheat considering Canadian/ Russian/ Australian competition at these prices.

- World wheat production estimates still indicate that there will be adequate supply and projections for ending stocks seem bearish given the recent price rally. While it seems probable that wheat will trade lower, the timing is hard to predict and further dryness could drive markets higher in the short term.
- Dryness over US and Canadian spring/durum wheat crops is worsening, there is very little rain in the Australian short term forecast (-the long term is also hot and dry), the market is waiting for more quality data from Russia and for the start of the German/Baltic harvests. Therefore, while the world is not running out of wheat, quality spreads will remain an issue, and given current prices, there still have to be some major re-alignments of the USDA's world trade matrix between the different origins.
- We are still of the opinion that spring wheat is a good sale, but the Canadian 'basis' is wide we would expect to see prices of \$8.50 or better and would hold for that for the present.

iii) Primary Elevator Price Tables and Grade Spreads

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

Date: July 17, 2017

| NW Sask | Spot | | NW Sask | Deferred | |
|--------------------|--------|----------|--------------------|---------------|---------------|
| | (bu.) | (mt) | | Oct '17 (bu.) | Oct. '17 (mt) |
| 1 CWRS 13.5 | \$7.78 | \$285.87 | 1 CWRS 13.5 | \$7.92 | \$291.01 |
| 1 CWAD 13.0 | \$7.48 | \$274.85 | 1 CWAD 13.0 | \$7.26 | \$266.76 |
| 1 CPSR 11.5 | \$5.52 | \$202.83 | 1 CPSR 11.5 | \$5.39 | \$198.05 |
| SW Sask | | | SW Sask | | |
| 1 CWRS 13.5 | \$7.84 | \$288.07 | 1 CWRS 13.5 | \$8.00 | \$293.95 |
| 1 CWAD 13.0 | \$7.46 | \$274.11 | 1 CWAD 13.0 | \$7.37 | \$270.80 |
| 1 CPSR 11.5 | \$5.50 | \$202.09 | 1 CPSR 11.5 | \$5.40 | \$198.42 |
| NE Sask | | | NE Sask | | |
| 1 CWRS 13.5 | \$7.62 | \$279.99 | 1 CWRS 13.5 | \$7.65 | \$281.09 |
| 1 CWAD 13.0 | \$7.89 | \$289.91 | 1 CWAD 13.0 | \$7.37 | \$270.80 |
| 1 CPSR 11.5 | \$5.36 | \$196.95 | 1 CPSR 11.5 | \$5.18 | \$190.33 |
| SE Sask | | | SE Sask | | |
| 1 CWRS 13.5 | \$7.76 | \$285.13 | 1 CWRS 13.5 | \$7.80 | \$286.60 |
| 1 CWAD 13.0 | \$7.96 | \$292.48 | 1 CWAD 13.0 | \$7.56 | \$277.78 |
| 1 CPSR 11.5 | \$5.39 | \$198.05 | 1 CPSR 11.5 | \$5.26 | \$193.27 |

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

| Avg. Grade Spread/ Pro Discounts | Cdn\$/bu. | Cdn.\$/mt |
|-------------------------------------|------------|------------|
| 1 CWRS 13.5 | Base Grade | Base Grade |
| 2 CWRS 13.5 | (0.20) | (7.35) |
| 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)

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."

- 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.

 - 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 | | | | July 17, 2017 |
|--------------------------------------|--|-----------------------|--------------------|--|
| 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 | \$419.17 | \$389.40 | | |
| HRS | \$412.20 | | | |
| HRW 11.5 | \$282.86 | | | |
| SWW 12.0 | \$263.79 | | | |
| 1 CWRS 13.5 ³ | \$419.17 | | \$275.95 | \$143.23 |
| 2 CWRS 13.0 ³ | \$412.20 | | \$260.88 | \$151.31 |
| 3 CWRS ³ | \$282.86 | | \$242.88 | \$39.98 |
| CPS ³ | \$257.27 | | \$198.79 | \$58.49 |
| 1 CWAD ⁴ | | \$488.49 | \$264.56 | \$223.94 |
| Competing wheat: US\$/mt | | | | |
| Russia 12.5 (Black Sea, 25k mt) | \$196.00 | | | |
| French 11.0 (Rouen) | \$196.13 | | | |
| ASW 10.5 (W Coast) | \$255.00 | | | |
| Argentine 12.0 | \$185-195 | | | |

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 | | | | | July 17, 2017 |
|--|------------------|--------------|--------------------|--------------------|---------------|
| Canadian Funds | | | | | |
| PNW value/Vancouver | 1CWRS13.5 | 2CWRS | Grade 3CWRS | Winter wht. | CPS |
| Dec./Jan. delivery | \$11.23 | \$11.04 | \$7.52 | \$7.00 | \$7.00 |
| Parity Track Rosetown | \$9.73 | \$9.54 | \$6.02 | \$5.51 | \$5.51 |
| Track Bid Rosetown Area | \$7.51 | \$7.10 | \$6.61 | \$5.41 | \$5.41 |
| Gross Margin at Elevator (\$/bu)* | \$2.22 | \$2.44 | -\$0.59 | \$0.10 | \$0.10 |
| Gross Margin at Elevator (\$/mt)* | \$81.73 | \$89.81 | -\$21.52 | \$3.50 | \$3.50 |
| * to cover elevation, elevator market risk, margin | | | | | |