Wheat Market Outlook and Price Report: February 20th, 2018

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i) Background and Rationale for the Report

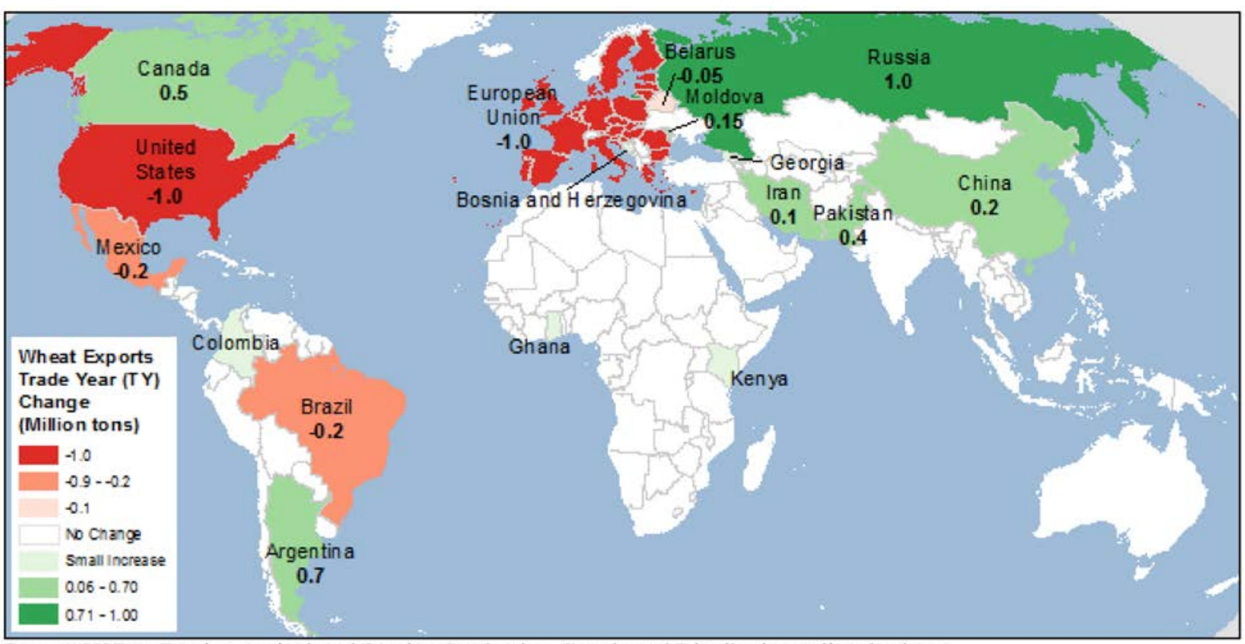
The following wheat market outlook and price report will be published on a weekly basis on the Sask Wheat Website. The report provides producers with an overview of world wheat markets, a market forecast, and benchmark prices at both the primary elevator and export positions (FOB Vancouver or elsewhere).

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 Feb. 12/'18

2017/'18 World Wheat Overview: USDA Wheat Outlook Report February 12th 2018

- **US and EU wheat exports** have been revised lower by 1 million mt each.
- **Russia wheat export projections** have been revised higher by 1 million mt, while export projections for Argentina are increased by 0.7 million mt.
- **Canadian wheat** export projections have also been revised higher by 0.5 million mt.
- **Pakistan's exports** have been increased by 0.4 million mt, while China is up by 0.2 million mt.

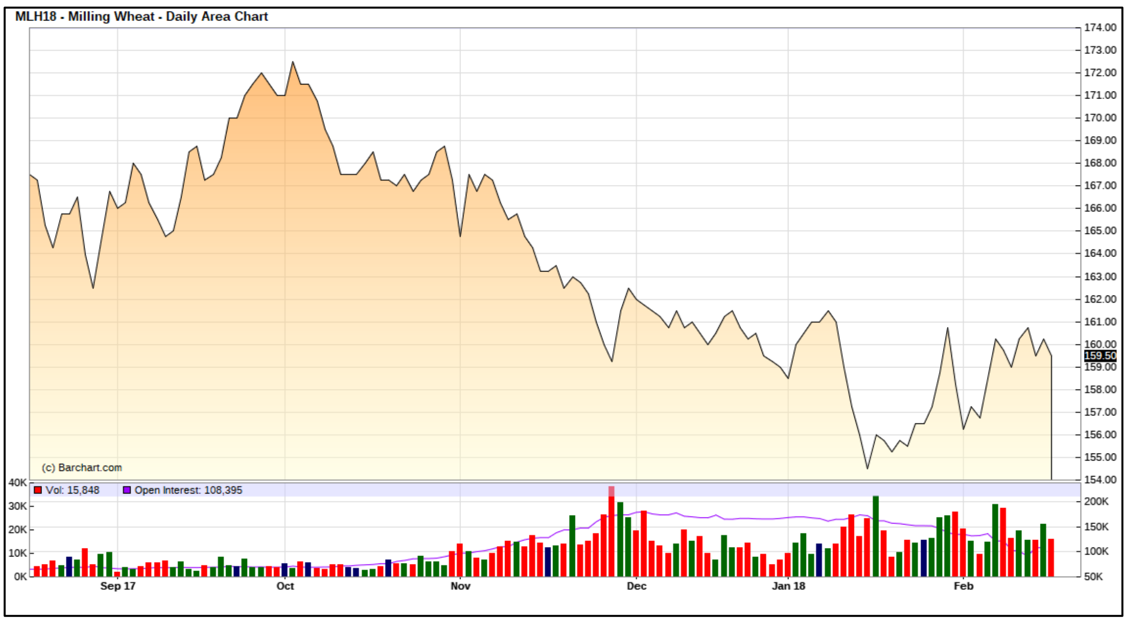


Source: USDA, Foreign Agricultural Service, Production, Supply and Distribution online database.

➢ **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:** Mar'18 contract Chicago winter wheat closed at 457.75 which was down by 4 cents in Friday's trade but up by 10.4 cents for the week. Meanwhile, Mar'18 contract Kansas hard red winter wheat closed up by 0.5 cents at 478.5, and up by 13 cents for the week. In Minneapolis, Mar'18 contract hard red spring wheat closed at 605.25, which was down by 3.25 cents in Friday's trade, but up by 1.6 cents for the week. Meanwhile, May'18 hard red spring wheat closed at 615.75, down by 3 cents for the day, and unchanged for the week.
- **Funds:** Index Funds added to their long and now have close to 93 million mt tonnes long. Specs were huge buyers last week turning their short to overall long. This will be the first time since August that the Specs. have been long. In the last five weeks Spec Funds have bought in a total of near 80 million tonnes (for all grains). *However, on wheat Spec Funds are currently still holding a net short of 9.3 million mt.*
- **Matif:** Matif wheat futures in Europe closed at €159.50 which was down by €0.75/mt on Friday, but up by €0.50 for the week.



- **Canadian wheat:** In the week 28 CGC grain movement report, Canadian wheat exports are stated at 299k mt, which is up significantly from last week's 218k mt. Current year to date Canadian wheat exports are now reported at 8.4 million mt, which is ahead of last year's 7.1 million mt and which puts Canada on pace to achieve exports of 15.9 million mt. Truck shipments to the US are estimated at an additional 1.2 million mt, which could put total exports at 17.1 million mt or slightly behind AAFC projections of 17.2 million mt.

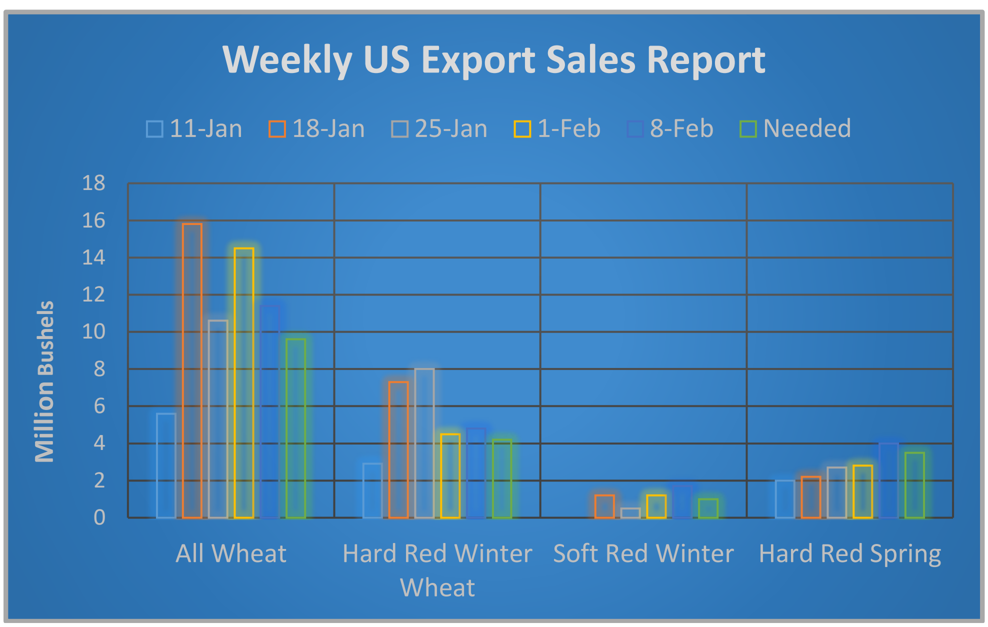
(CGC) Grain Handling Summary Wheat		Week 28	(to Feb 11/'18)	
('000 mt)	Prod. Dlvrs.	Terminal Rcpts.	Bulk exports	Dom. Disappearance
Week 28	317.9	176.5	298.7	27.0
Week ago	322.2	198.3	218.2	56.7
YTD	9,884.6	9,456.5	8,401.1	2,554.4
Last YTD	9,401.7	9,624.7	7,158.0	1,578.8
YTD less Last YTD (k mt)	482.9	-168.2	1,243.1	975.6
YTD over Last YTD (%)	105%	98%	117%	162%

Mercantile based on weekly CGC Handling Data

(CGC) Grain Handling Summary Durum		Week 28	(to Feb 11/'18)	
('000 mt)	Prod. Dlvrs.	Terminal Rcpts.	Bulk exports	Dom. Disappearance
Week 28	63.6	58.0	235.0	2.4
Week ago	74.0	66.9	153.9	7.0
YTD	2,217.7	2,528.9	2,256.1	426.2
Last YTD	2,743.7	3,078.4	2,286.8	176.0
YTD less Last YTD (k mt)	-526.0	-549.5	-30.7	250.2
YTD over Last YTD (%)	81%	82%	99%	242%

Mercantile based on weekly CGC Handling Data

- **US wheat:** While some rains have been reported in SE regions of the US plains, the heart of the US winter wheat belt remains extremely dry, and Thursdays short covering rally was driven by NOAA's updated long-term weather outlooks which show continued dryness in key wheat producing regions.
  In total, 42% of the US winter wheat belt is now reported to be in drought, which is down slightly from last week's 45% due to limited rains. Meanwhile US spring wheat is reported to be 47% in drought, a slight improvement vs 48% last week.
  In the weekly USDA export sales report sales were reported at 311k mt, which fell within market expectations of 200-450k mt. However, sales continue to lag well behind last years pace, and same week sales last year were reported at 525k mt. Slower exports promoted the USDA to lower its export projections by 950 million bushels in last weeks WASDE. Going forward, the dryness in the US wheat belt is a major concern, and US weather will be a major market focus.



- **Australian wheat:** On the Australian futures markets, Australian wheat is currently trading at $214.76 US per mt, which is up by $2.85 per mt over the past week.
- **Argentine wheat:** Argentina continues to be warm and dry, with very little moisture received over the past weekend. Rainfalls in Argentina are reported to be only 15-40% of normal precipitation and while Brazil is reported to have good growing conditions, the outlook continues to be hot and dry for the coming week which is supporting cereal and oilseed values.

12% protein Argentine FOB wheat is valued at US$192/mt (little changed). 11.5% protein wheat is priced at US$187/mt FOB. This still is a significant discount to French wheat at US$205/mt FOB (+).

- **EU wheat**: Strategies Grains recently lowered EU wheat exports for the fourth straight month to 21.4 million tonnes due to increased competition from the Black Sea and Argentina.
  Overall dryness and below normal soil moisture are reported in southern Europe, while excessive soil moisture is reported in Germany which could lower yields slightly. However, overall EU production is still projected well above last year. In the past week French wheat is reported to be 84% good/excellent, which is down from last year's YTD 92% good/excellent. French 11.5 protein wheat is currently trading at $205.39 per mt, while German 12.5 protein wheat is trading at $209.11 per mt.
- **Black Sea wheat:** Projections for Russian exports continue to be revised upwards, although recent colder weather is slowing the pace slightly. SovEcon now projects Russian wheat exports at 36.6 million mt, with the export pace aided by a mild fall/winter and a low Russian Ruble. However, some analyst now feel that Russian exports could be even higher than this (as high as 40 million mt) as EU exports continue to lag.
  Russian wheat values climbed to $202 per mt as of Friday.

➢ **Significant purchases/Trades:**

There were a number of cash trades in the past week, with some of being supplied by Canadian origin wheat.

- **Iraq** bought 150,000 mt of Australian/Canadian/US wheat at US$293-323/mt CIF.
- **Pakistan** has now sold some 750,000 mt at US$180-200/mt Fob.
- **Syria** will be tendering next week for 300,000 mt wheat.
- **Algeria** is reported to be tendering for 50k mt of wheat this coming week.
- **Iran** is reported to be holding talks with Russia to import 1 million mt of Russian wheat.
- In the past week **US inspections** were reported at 488,000 tonnes (season total 629 million bushels, down 4%) sales were 311,000 tonnes (season total 776 million bushels down 13% against USDA's projected 10% decline).

➢ **Wheat Market Outlook:**

➢ **Significant events:**

- The US dollar moved lower over the course of the past week, and Tuesdays CPI report showed that US inflation over the last 3 months has risen by an annualized 4.4%. Given higher inflation, it seems increasingly probable that the Fed will hike interest rates which could push the US dollar higher and further slow US grain exports.
- As mentioned above, Iraq bought 150,000 mt of Australian/Canadian/US wheat at US$293-323/mt CIF. But Canadian elevator bids remain low compared to USA values and very low compared to the Iraq trades which figure about C$9.00 FOB Vancouver.

➢ ***Outlook:***

- USDA estimates for EU exports are too high and the USDA number for Russia is probably too low. However, we wonder about the ability of Russian logistics to keep pace with export demand as the trade has to go progressively further in-land to find the supplies. (Port capacity has already been proven to be a non-issue).
- The US market remains about Funds and Plains dryness.

- Funds are currently close to a zero net position in Minneapolis, but if dry conditions persist in the northern US, then we could see funds starting to go long on hard red spring as planting approaches. This could bring some better new crop values.
- HRS wheat is currently bid at $6.20 - $6.70 per bushel across Western Canada.

iii) Primary Elevator Price Tables and Grade Spreads

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

Date: February 20, 2018

NW Sask	Spot		NW Sask	Deferred	
	(bu.)	(mt)		Apr. '18 (bu.)	Apr. '18 (mt)
1 CWRS 13.5	$6.59	$242.14	1 CWRS 13.5	$6.64	$243.98
1 CWAD 13.0	$6.98	$256.47	1 CWAD 13.0	$7.24	$266.03
1 CPSR 11.5	NA	#VALUE!	1 CPSR 11.5	$5.49	$201.72
SW Sask			SW Sask		
1 CWRS 13.5	$6.56	$241.04	1 CWRS 13.5	$6.58	$241.78
1 CWAD 13.0	$7.02	$257.94	1 CWAD 13.0	$7.30	$268.23
1 CPSR 11.5	NA	#VALUE!	1 CPSR 11.5	$5.24	$192.54
NE Sask			NE Sask		
1 CWRS 13.5	$6.37	$234.06	1 CWRS 13.5	$6.43	$236.26
1 CWAD 13.0	$7.06	$259.41	1 CWAD 13.0	$7.16	$263.09
1 CPSR 11.5	NA	#VALUE!	1 CPSR 11.5	$5.26	$193.27
SE Sask			SE Sask		
1 CWRS 13.5	$6.41	$235.53	1 CWRS 13.5	$6.47	$237.73
1 CWAD 13.0	$7.20	$264.56	1 CWAD 13.0	$7.32	$268.97
1 CPSR 11.5	NA	#VALUE!	1 CPSR 11.5	$5.19	$190.70

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 Basis[1] (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)

- <u>Hard wheat price calculations:</u>
  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).

- <u>Optional origin grain sales</u>:
  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

Releveant FOB Prices and Export Basis				February 20, 2018
	FOB Prices CDA[1] (calculated)		Street Prices	Export Basis[2]
Type of Wheat	West Coast (Cdn./mt$)	Great Lakes (Cdn.$/mt)	Rosetown (Cdn.$/mt)	Basis: West Coast-Centr. SK (Cdn$/mt)
DNS 14.0	$346.68	$330.66		
HRS	$339.26			
HRW 11.5	$297.09			
SWW 12.0	$265.11			
1 CWRS 13.5[3]	$346.68		$235.16	$111.51
2 CWRS 13.0[3]	$339.26		$203.93	$135.33
3 CWRS[3]	$297.09		$182.62	$114.47
CPS[3]	$258.62		$198.79	$59.83
1 CWAD[4]		$384.68	$242.14	$142.54
Competing wheat:	US$/mt			
Russia 12.5 (Black Sea, 25k mt)	$2.03			
French 11.5 (Rouen)	$205.39			
ASW 10.5 (W Coast)	$232.50			
Argentine 12.0	$188.50			

[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

Canadian Wheat - World Price Parities					February 20, 2018
Canadian Funds			**Grade**		
PNW value/Vancouver	**1CWRS13.5**	**2CWRS**	**3CWRS**	**Winter wht.**	**CPS**
Dec./Jan. delivery	$9.26	$9.06	$7.91	$7.04	$7.04
Parity Track Rosetown	$7.76	$7.56	$6.41	$5.54	$5.54
Track Bid Rosetown Area	$6.40	$5.55	$4.97	$5.41	$5.41
Gross Margin at Elevator ($/bu)*	**$1.36**	**$2.01**	**$1.44**	**$0.13**	**$0.13**
Gross Margin at Elevator ($/mt)*	**$50.04**	**$73.86**	**$52.99**	**$4.85**	**$4.85**

* to cover elevation, elevator market risk, margin