NESVICK
TRADING GROUP, LLC

Monday, October 4, 2021
NTG Morning Comments
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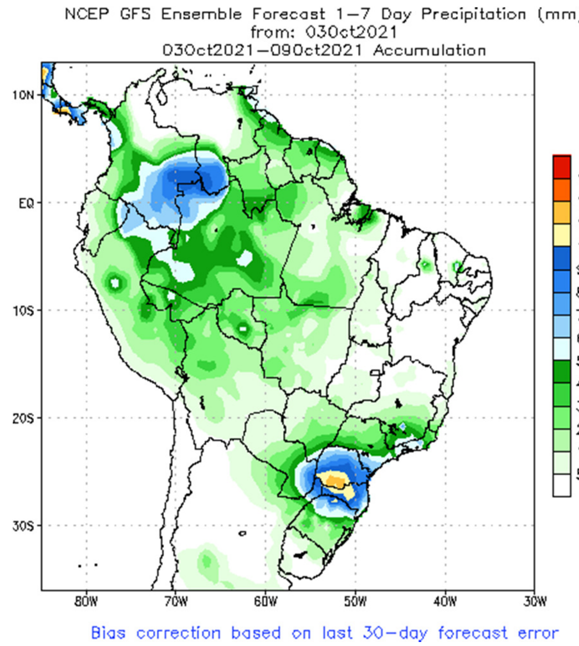
Weather

Nothing big to report on weather this morning. The US forecast features chances for rainfall in the ECB over the next few days, but the middle of the country should see mostly dry conditions. Rainfall chances will return for the middle of the country starting in the 6-10 day period. Temps should continue to average well above normal for the two week forecast, with no freeze in sight.

In South America, some good rains in southern Brazil this week but limited rainfall for northern areas. This could keep planting efforts minimal over the next week. The Week 2 outlook does show improved chances for rainfall in northern Brazil, which would certainly be welcomed to allow planting to start to pick up.



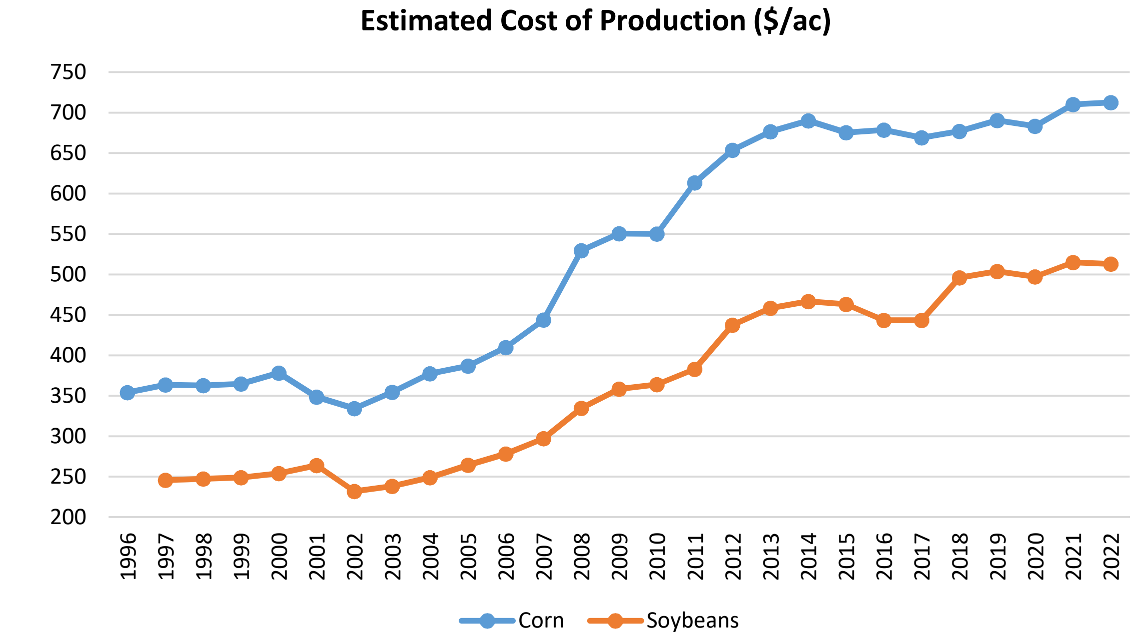
Crops

I misspoke in Friday's comments when I suggested that ERS would updated their forecasts for cost of production. They did update/revise estimates of cost of production for prior years, but for now they've left their 2022 projections untouched. Still, I think it would be instructive to look at what their projections would imply on cost of production and what that would potentially imply for acreage.

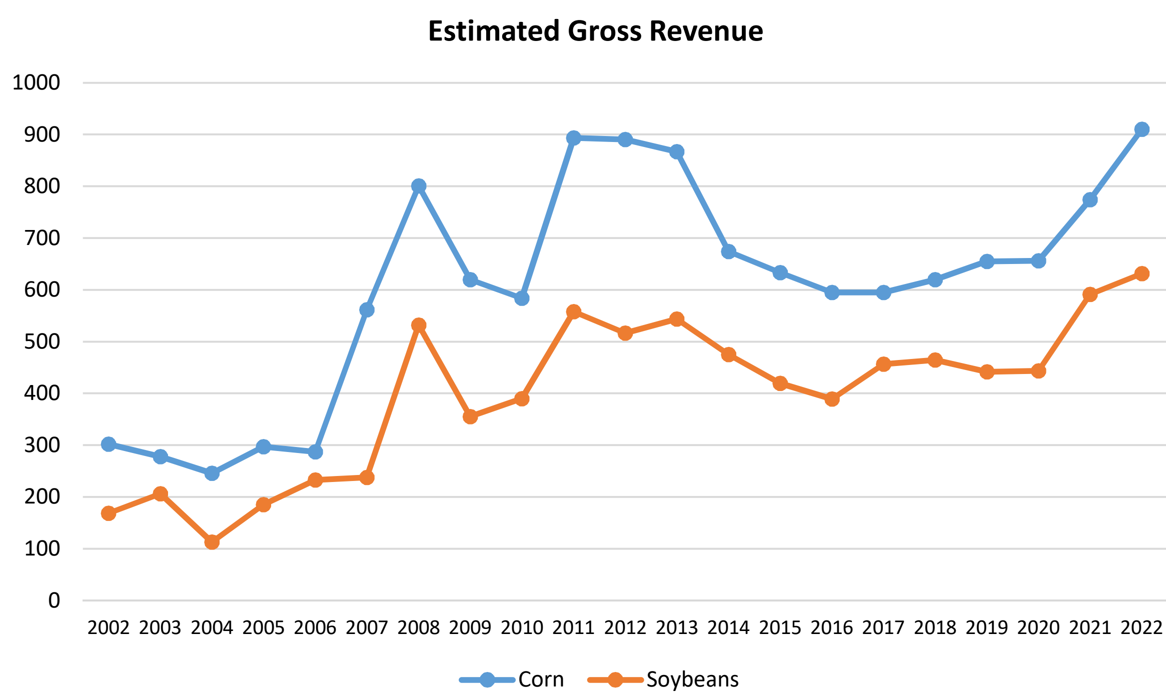
The rundown at the right is a snapshot of what ERS is showing for their current 2022 cost of production forecasts. These were most recently revised in late-June and they will be updated in mid-December. The chart just below shows a history of their cost of production estimates. What I think is interesting is that ERS's current 2022 cost of production figure is not that different from their 2021 estimates. I think we can mostly agree that in the past few months we've seen big changes to fertilizer costs that will almost certainly make for some big year-to-year cost increases. Still, this is the most recent data that we have from ERS, so just for illustrative purposes let's just roll with it this morning.

Cost-of-production forecasts for U.S. major field crops, 2021F-202

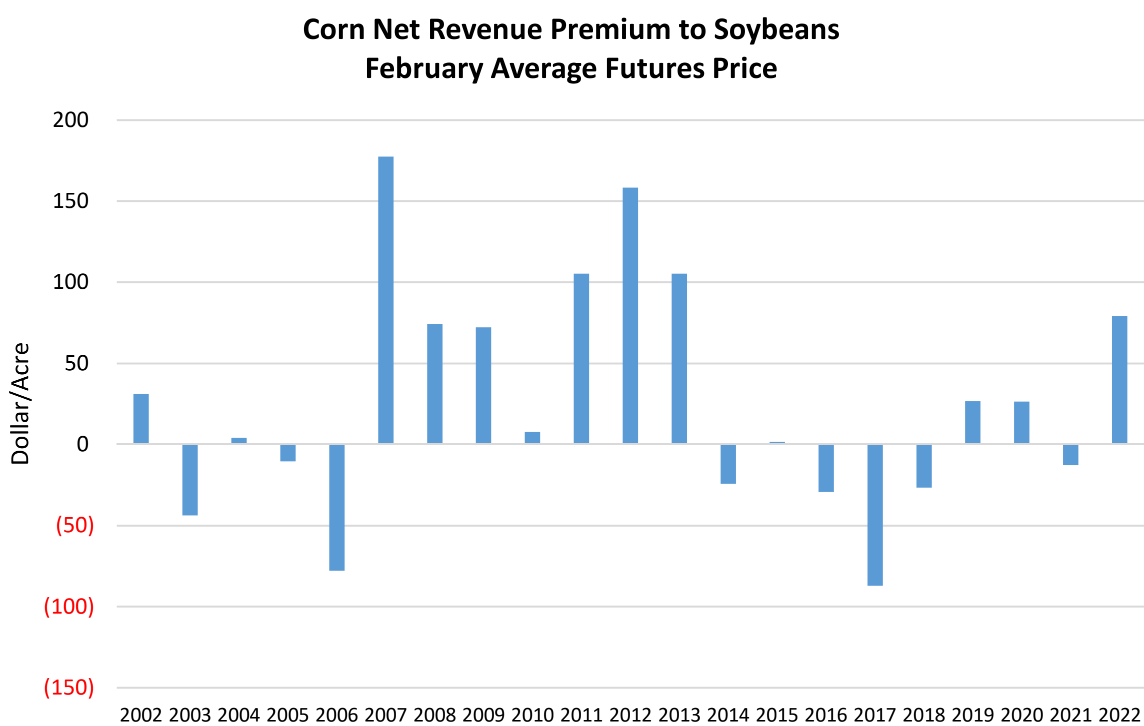
Item	Corn 2022F	Soybeans 2022F
Operating costs		
Seed	90.52	58.66
Fertilizer 1/	129.36	34.68
Chemicals	31.37	34.26
Custom operations 2/	23.38	12.91
Fuel, lube, and electricity	33.17	16.51
Repairs	36.70	30.14
Other variable expenses 3/	0.29	0.01
Interest on operating capital	0.25	0.13
Total, operating costs	345.02	187.31
Allocated overhead		
Hired labor	5.20	4.95
Opportunity cost of unpaid labor	30.27	17.39
Capital recovery of machinery and equipment	132.50	115.48
Opportunity cost of land (rental rate)	166.57	155.94
Taxes and insurance	12.52	12.67
General farm overhead	20.25	19.29
Total, allocated costs	367.31	325.72
Total costs listed	712.33	513.03



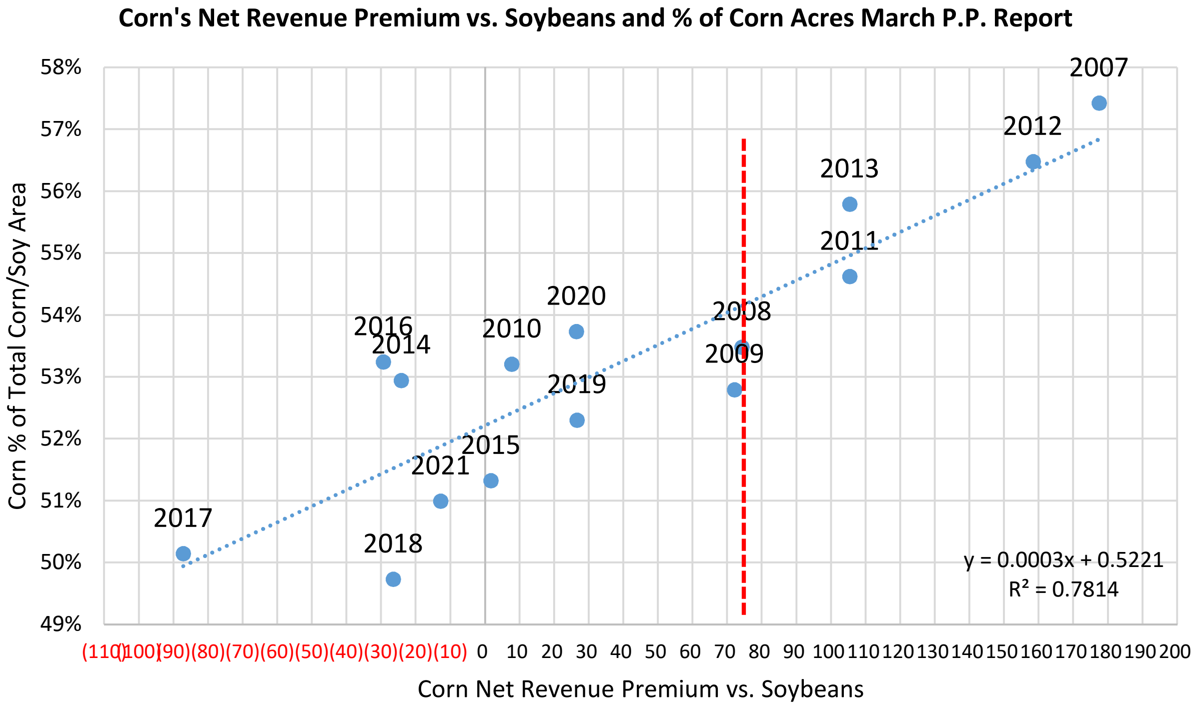
Let's assume a 20-year linear trendline yield calculation. I calculate a 20-year trend of roughly 177.9 bpa for corn and 52.0 for soybeans (which is assuming the most recent USDA estimates for 2021). Taking those assumptions on yield, some assumptions for "national average" basis, and current CZ'22 and SX'22 futures prices, I come up with the following estimates for gross revenue for each crop.



Interesting – in terms of gross revenue, current futures prices, trend yields, and my assumption on basis would potentially imply record gross revenue for both crops. Clearly, however, you can see the YOY surge for corn is larger than for soybeans. If we were to net out the current USDA figures on cost of production shown above, the net revenue comparison of corn vs. soybeans would look like this.



That would be the largest net revenue premium corn has held vs. soybeans in several years. It would be indicative of a big increase in corn area for 2022. As shown in the scatter below, such a net revenue premium would be indicative of corn getting roughly 54% of the total corn + soy area in the March Prospective Plantings report. If we were to assume the corn + soy acreage pie is 179 million (March 2021 was ~178.7 mil) that would translate to roughly 97.6 million acres of corn and only 81.4 million acres of soybeans.

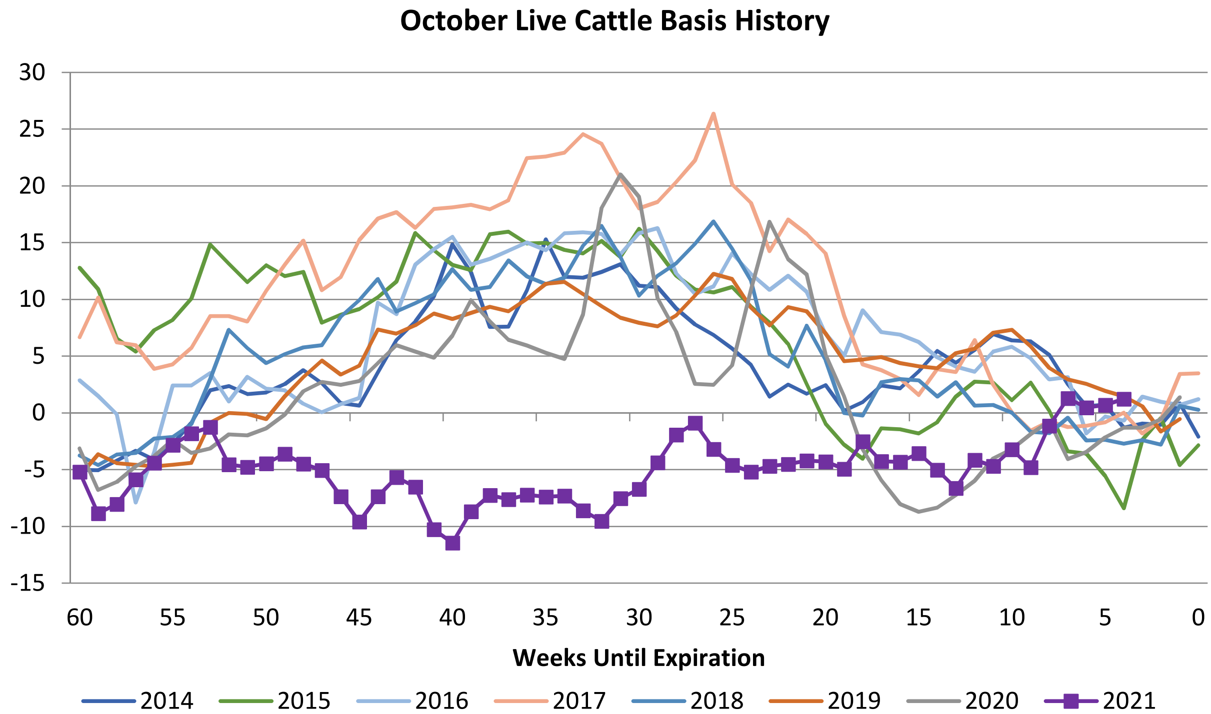


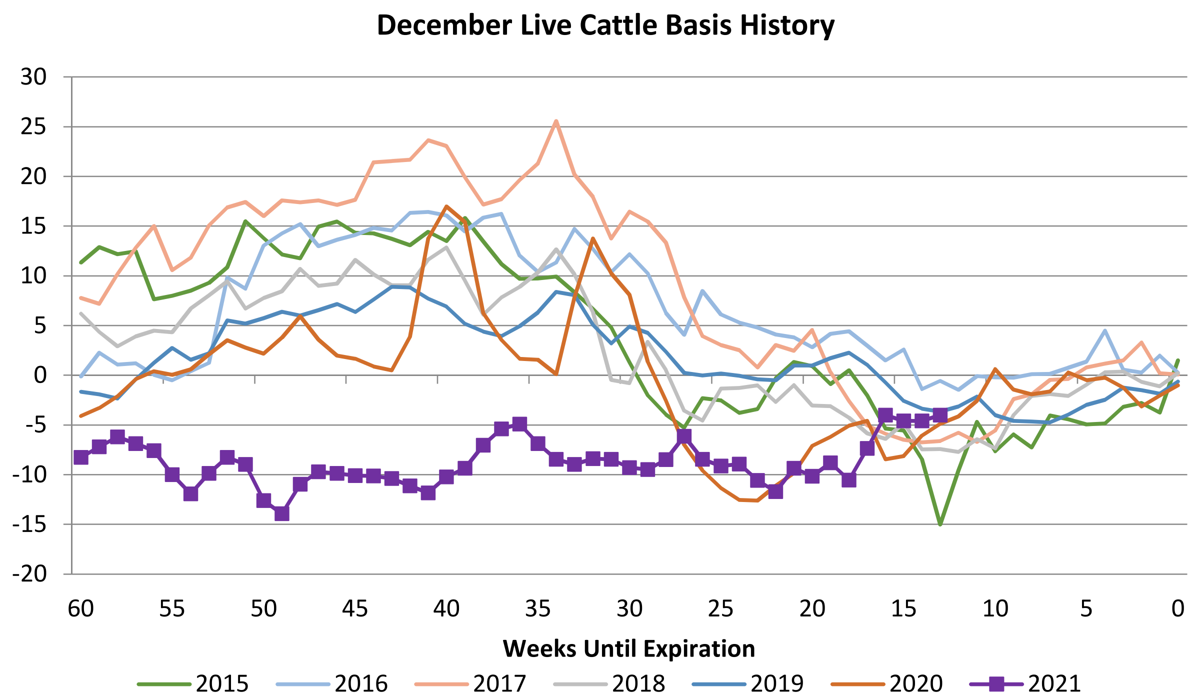
Yes, I know, I know….USDA's cost of production estimates are certainly more questionable this year than they are normally. I can say with a high degree of confidence that corn's cost of production will be higher than shown above. However, the main thing I really wanted to point out this morning was the chart on estimated gross revenue. This shows that the corn-soybean price spread has already done a pretty decent amount of work. It might still have more work to do, and certainly I still stand by the notion that CZ'22 has very little downside.

Over the next few days we'll spend our time prepping for the upcoming Crop Production & WASDE reports. After that release, however, we'll circle back around to this topic and discuss what the rally in fertilizer prices might mean for cost of production and net revenue calculations in the "real world". Thoughts appreciated.

Livestock

We haven't looked at basis in a while, so a quickie on that this morning. The charts below look at basis vs the Oct and Dec contracts. After dealing with record weak basis for a long while, we've seen basis come in substantially in the past several weeks. In fact, in the case of the Oct contract, basis is now starting to look slightly strong. Nothing that sets off any alarms, of course, but I still find the shift interesting. Basis vs the Dec contract is looking very average at this point in time. Bottom line – it's not looking like basis is pointing toward any possible shift in the near future.


October Live Cattle Basis History
30
25
20
15
10
5
0
-5
-10
-15
60
55
50
45
40
35
30
25
20
15
10
5
0
Weeks Until Expiration
2014
2015
2016
2017
2018
2019
2020
2021


December Live Cattle Basis History
30
25
20
15
10
5
0
-5
-10
-15
-20
60
55
50
45
40
35
30
25
20
15
10
5
0
Weeks Until Expiration
2015
2016
2017
2018
2019
2020
2021

Financials

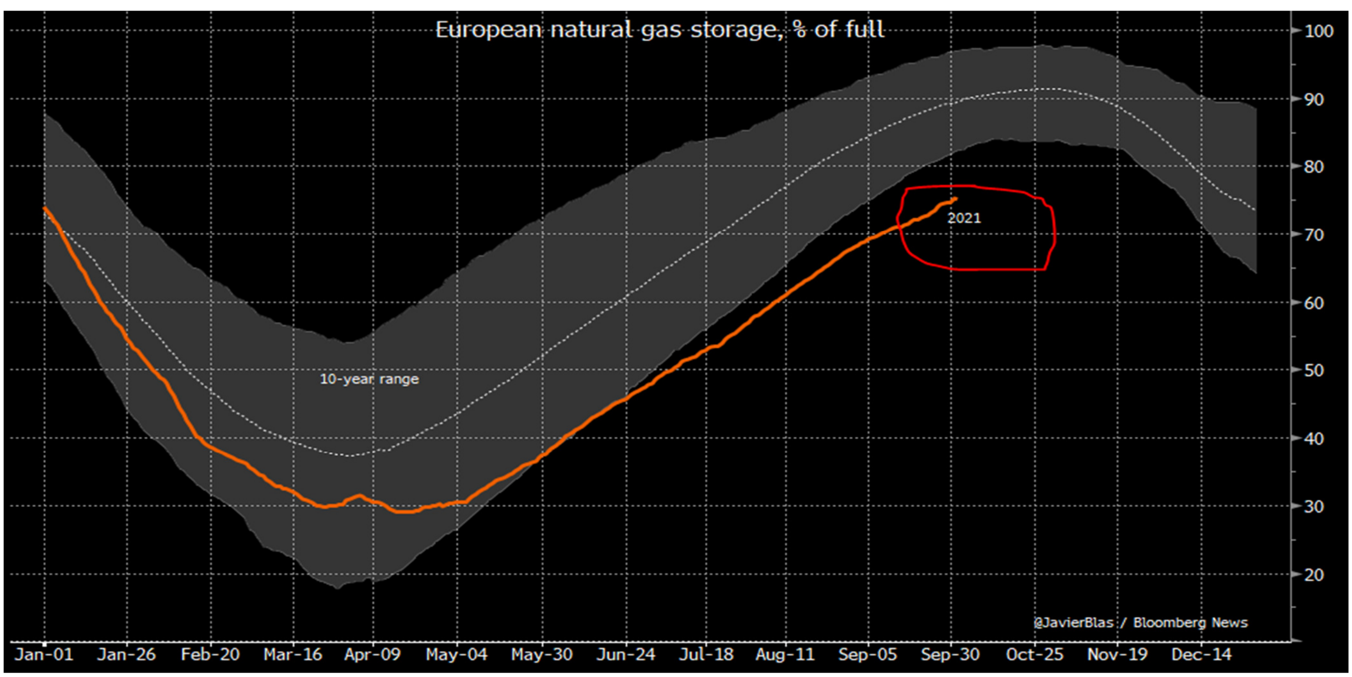
The same themes from last week remain present this week. We still have a looming major problem with the debt ceiling. Recall last week Treasury Sec Yellen said the US would hit its cash limit on around Oct 18. The CBO gives us a little more time. Still, that means if the Dems are going to have to use the reconciliation process…they have to get going on it now as it takes time. It doesn't appear they're going down that road just yet, which opens the door to more uncertainty. The general consensus is that Congress will eventually do "something", but if this remains unsettled by the end of the week I would expect the market could kick further into risk-off gear.

No change in the inflation narrative either. Remember, as discussed weeks ago we're past the point where inflation feels good and now it is starting to eat into sentiment. Last week's ISM manufacturing report showed an uptick in the "prices paid" component. Every other article seems to be about a shortage of something, somewhere. This isn't going away, and a Fed taper isn't going to help with labor or raw material shortages.

No major economic data on tap this morning. Durable goods orders is usually not much of a market mover. We have a big week for employment data, with ADP on Wednesday and NFP on Friday. This month and next month will set the stage for a taper announcement from the Fed in November….assuming the numbers are solid.

Energy

Just sharing a chart posted on Twitter by Bloomberg's Javier Blas. The chart shows the European natural gas storage situation in a nutshell. We're looking at natural gas inventories well below the 10-year range. It is also interesting as we saw a weekly inventory draw last week (admittedly small – so small you can't really see it on the chart) and normally inventories don't peak until mid/late October. This would seemingly support the argument for ongoing strength in natural gas prices.



Today's Calendar (all times Central)

- Durable Goods Orders – 9:00am
- Export Inspections – 10:00am
- Crop Progress – 3:00pm

Thanks for reading.

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