NESVICK TRADING GROUP, LLC

Wednesday, May 20, 2020
NTG Morning Comments
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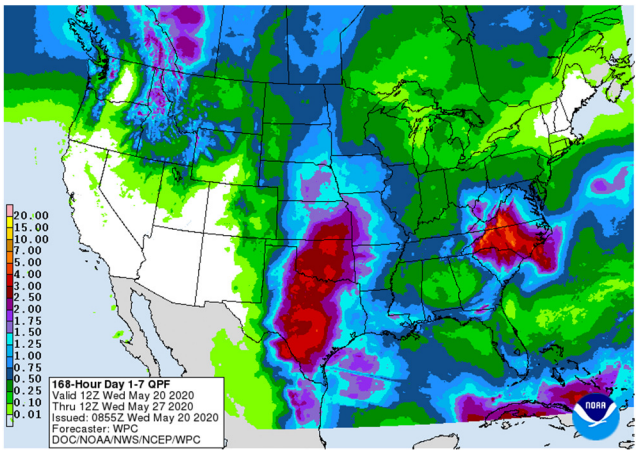
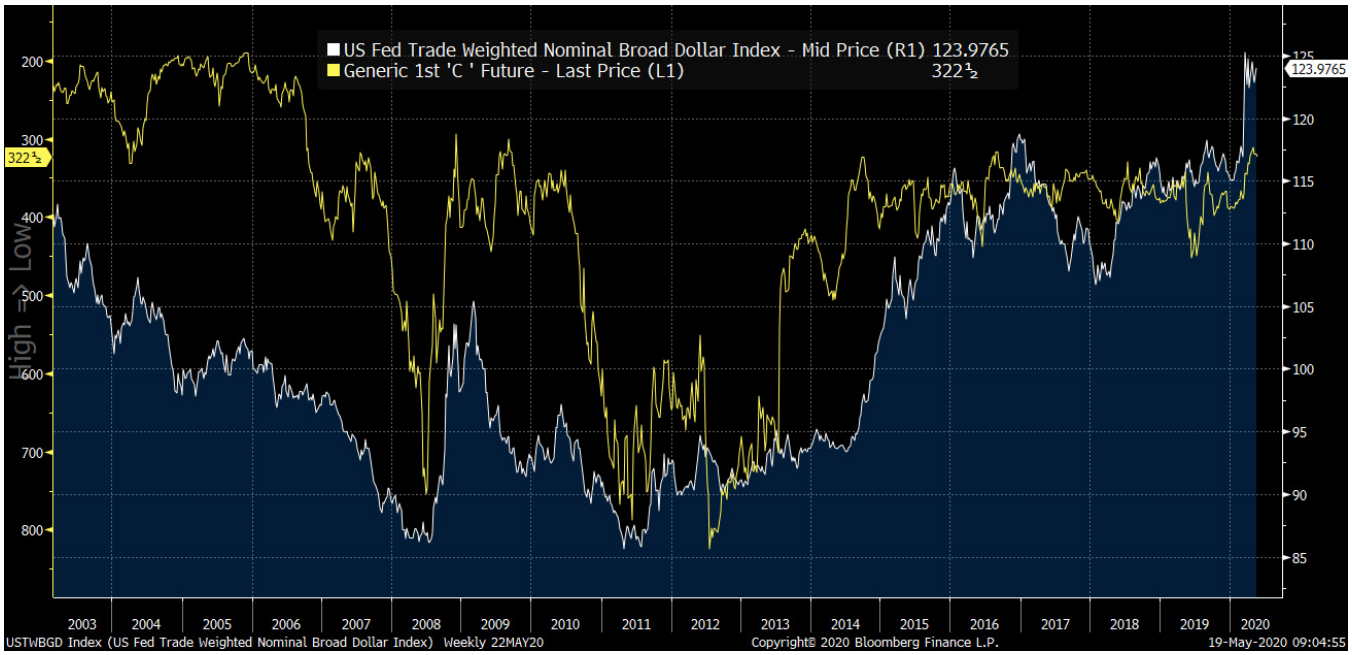
Weather

No big changes in the forecast. You can see rainfall in the ECB will not be real big during the next week, but cloudy conditions will keep drying conditions poor for the next several days. Significant rainfall chances will return for the ECB in the 6-10 day period. The WCB should see rainfall chances pick up tomorrow and rainfall should remain in place here through the weekend. You can see the HRW belt sees a lot of precipitation over the next week and rainfall chances will likely continue in the 6-10 day period. A lot of warm weather expected over the next two weeks with most of the Corn Belt averaging near to above normal.



Crops

So we're taking a break from getting in the weeds on fundamental data this week and we're looking at what it might take for ags to be "back"…like oil (according to President Trump). Today I'll make a possibly controversial statement – *The strength in the US dollar over the past decade has been the biggest factor impacting grain and oilseed prices during that period.* I'll admit I'm not entirely convinced I believe that statement, but just look at the chart below. The white line shows the Fed's trade-weighted dollar index since the early '00s. The yellow line is simply spot corn futures over the same time frame, but the axis is inverted. The relationship here is pretty obvious, and I could use several other commodities in place of corn and the chart would look pretty similar.



One big reason the dollar has proven to be such a negative influence on grain and oilseed markets in recent years is that it has encouraged expansion of production from competing suppliers. Brazil is the obvious example

here. The chart below looks at corn and soybean prices in Brazil in BRL terms. You can see the trend over the past several years has been for higher corn and soybean prices in BRL terms. This has encouraged expansion in area and inputs, leading to bigger and bigger revenue. As the Brazilian farmer continues to see increasing production (I don't need to put a chart of Brazilian corn and soy production history here, do I?) and higher and higher prices, they simply continue to invest more into their efforts. This is a US-defeating loop that is, at least in large part, due to the strength in the USD and weakness in BRL.

In order to break this cycle of rapid and non-stop advancement in Brazilian (and others) expansion in production, it would certainly help to see a turnaround in the direction of the USD. Instead, as shown in the first chart above, the dollar index has broken out into new highs this year. Does that mean more up-up-and-away action for the USD or is there a possible mean reversion to come? I don't think anyone has any confidence in making that call in this environment, but we'll look at some factors over the next few days.

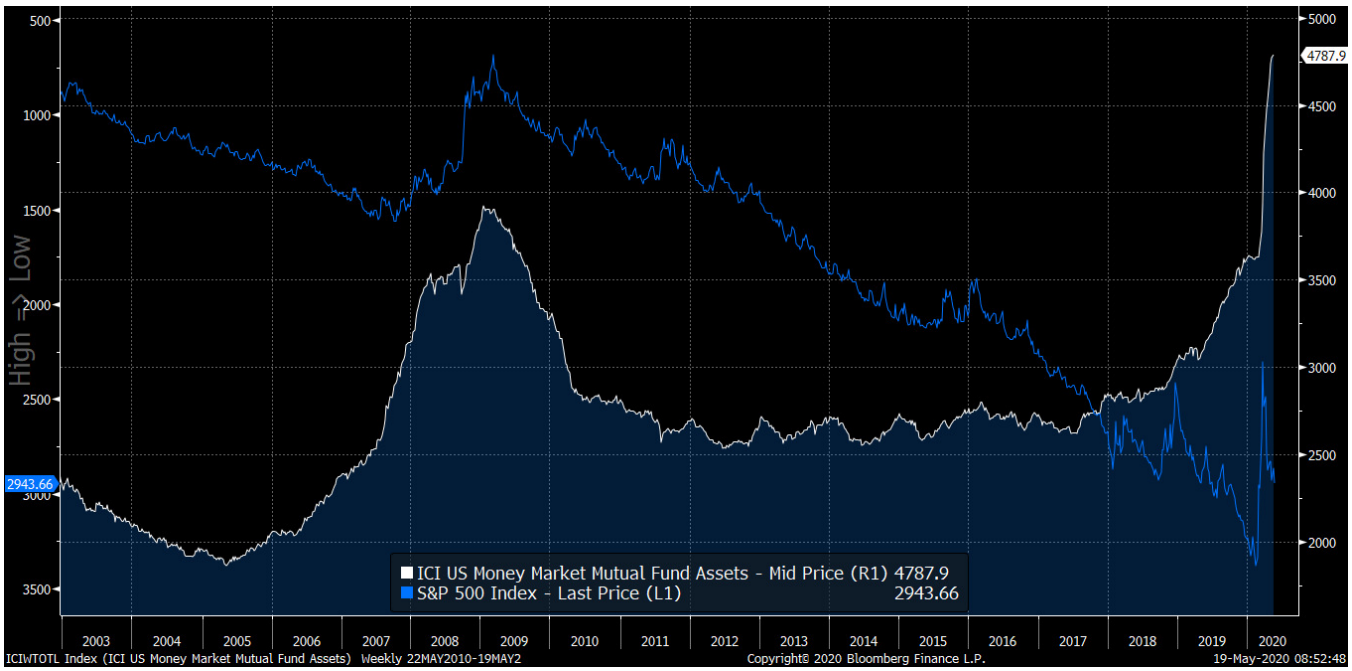
Livestock

Nothing truly "new" to pass along here this morning, so I'll keep it short. We saw some cash cattle trade yesterday range from 115-120, but the large majority of the action was at 120. Beef continues to lose some value, but honestly the pace of decline has not been as dramatic as I might have feared. Still, I would not rule out the choice cutout dropping more than $100 in a fairly quick fashion here as slaughter picks up. Slaughter this week is running +20k from last week but is still -50k vs last year, so cattle supplies continue to back up. For those two reasons, I remain a bit concerned for a bit of a hangover after this surge in cash prices over the past ~2 weeks. While basis remains wide and I'm not negative the board, I simply don't see packers paying 120 for cash if boxes are back under 300.

Financials

Nothing major on tap today. We do get the minutes of the April FOMC meeting this afternoon and the market will be looking closely at that for any clues for additional policy moves. That said, I doubt there will be anything in there that will change the market's sentiment following Powell's comments of the past several days. Otherwise, not much new to report this morning.

I was passed an interesting chart yesterday, and I've included a version of it below. The white line represents a weekly estimate of total assets in US money market funds. It is no surprise to see that as the equity market has been hammered and the world has grown hyper-concerned about the impacts of Covid-19, money market funds have seen a lot of investments as a flight-to-safety. I have overlaid the SPX on the chart (blue line) with the axis inverted. I added the SPX to show that in the 08/09 period, money market funds saw their assets peak right near the bottom of the equity market. I think that is interesting to keep in mind again this time. Money market funds are obviously not making much with interest rates near zero, so once the world is deemed to be "safe", all those assets that have moved into money market funds might come back out just as quickly into equities. Of course that is part of the Fed's goal with holding rates near zero. If and when the world is deemed "safe", we could see a wave of assets moving out of money markets again…on top of the huge supplies of liquidity provided by central banks.



Then again, I do suppose it is also worth noting that money market assets had been trending higher over the past few years even before the Covid-19 situation. Obviously the spike in 2020 is Covid-related, but the gains in '18 and '19 have to be attributed to something else…especially as equity markets were still moving higher at that time. Thoughts appreciated.

Energy

The Trump administration has thrown a bone to some oil producers that drill on federally owned land. The federal government will temporarily lower royalty rates so that oil companies can pay the federal government as little as 2.5% of the value of the oil and gas extracted from the land. This is down from the usual 12.5% royalty rate. The president of the Conservatives for Responsible Stewardship earns the best quote of the day award with this gem – "They're neck deep in oil and we're throwing them an anchor….Not only does this boneheaded move shortchange American taxpayers and Western states at the worst possible time, it incentivizes oil production during the worst oil glut in history". Whether or not you agree with him, that gets an A+ grade from me for bluntness.

On tap today we get the weekly inventory numbers. Crude oil inventories were expected to increase 2 million barrels last week, but interesting to see the API release yesterday afternoon show a ~5 million barrel *decline* in inventories. That would be something to really get the market's attention if confirmed with the EIA release.

Today's Calendar (all times Central)

- EIA Petroleum Inventories – 9:30am
- 20Y Treasury Auction – 12:00pm
- FOMC Minutes – 1:00pm

Thanks for reading.

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