

Ag Financial Strategies

RF Posson & Company

Annual Corn Report for 2009

12/4/2008

2008 Review (First published 11/6/08 and revised for public use 12/4/08)

- Corn crop condition and weather based production forecast were some what right for 2008. The forecast had been for lower condition to reflect a crop problem. This was the case for early in the season with Midwest flooding but not the case for year end value. Annual yield forecast was for 143 and intra year model forecasts did reach this low but the crop recovered.
- The forecast since 1993 had called for a record high price for corn during 2004 to 2008. The 2008 Annual forecast offered objective as high as \$6.80. Spot corn traded to \$7.76.

2009 Forecast

- Bullish corn for 2009. Major retracement due and new record high can not be ruled out. Bullish support may linger into 2010.

Weather

Two Benner Drought Cycle events were due this decade. The only evidence of occurrence is the drought event in 2005 for Illinois which was a wonder to watch. There is still time for the second or first and only true event and for 2009-2010 with slight chance 2011 should be allowed. Without a last minute disaster in 2009-2010, I believe global warming interfered with cyclical structure this decade. I find it interesting that the price forecast for a new record high was correct but not for the weather forecast.

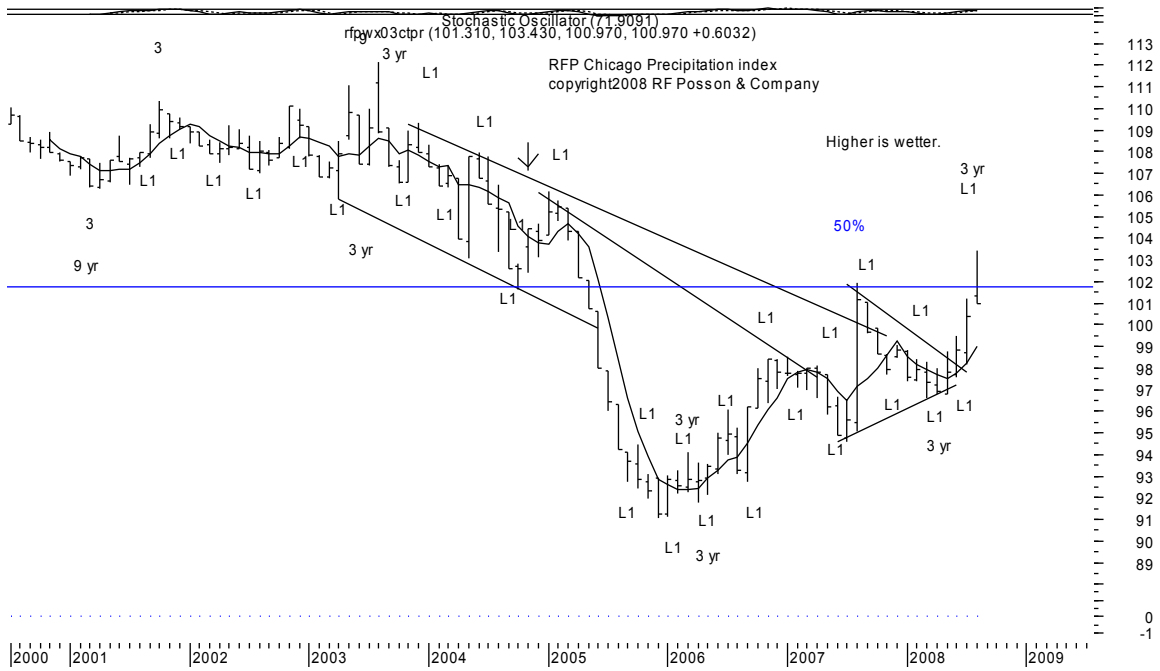
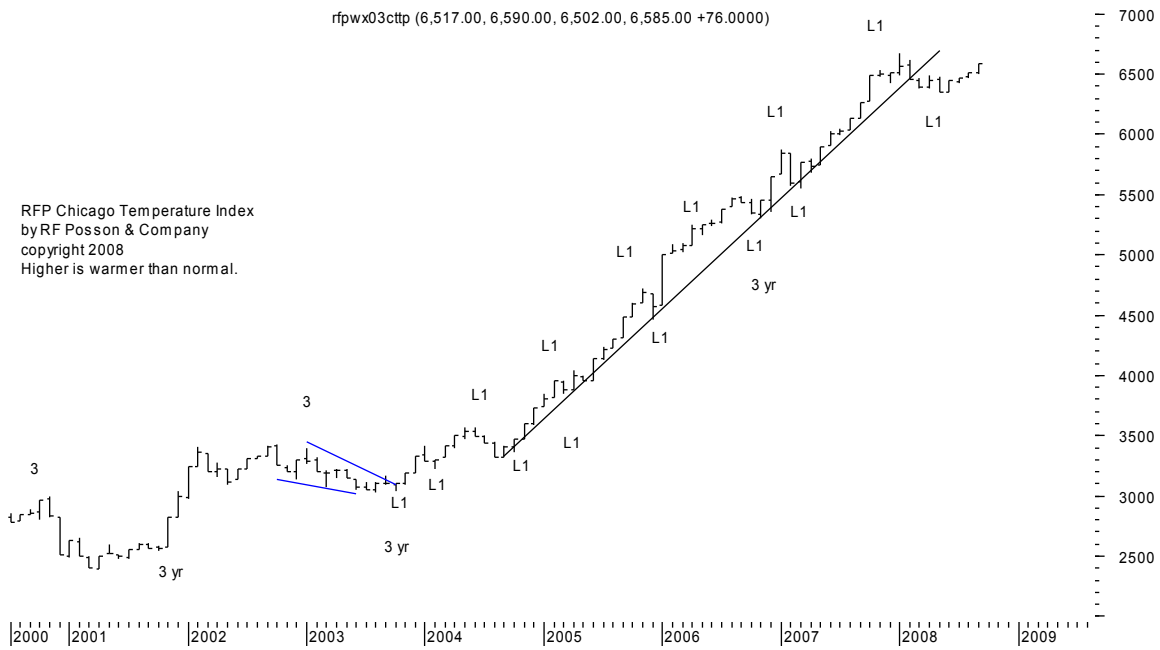
(Weather forecast was correct for wheat and soybeans.)

Global Warming

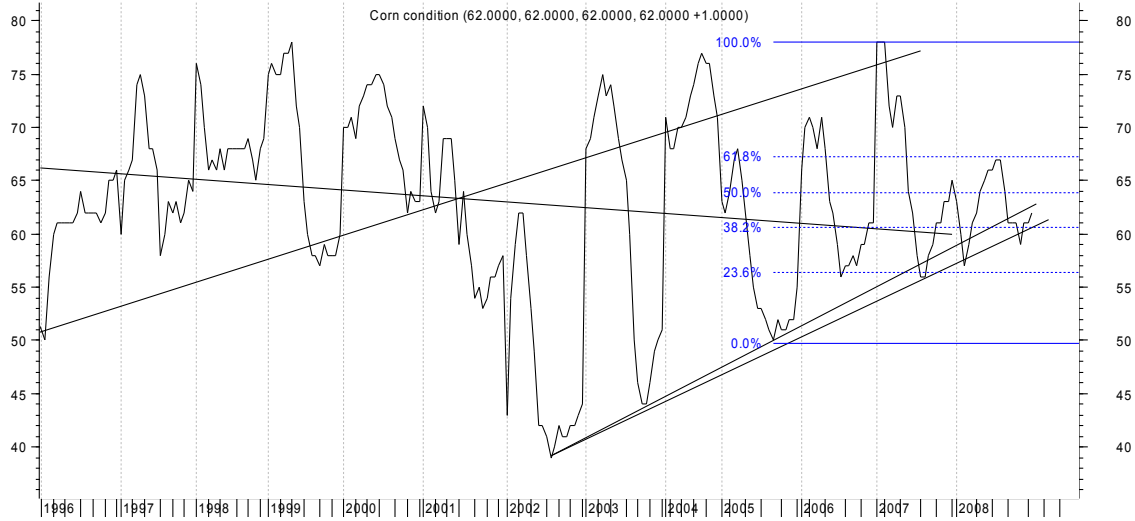
From the 2006 report-- A 1,000 year cycle of warmer than normal temperature peaked in the years of 1,000 and is due to peak this century. Research shows that this cycle can run a wide range of time to peak or that there is a tendency toward after shocks or secondary tops in that important temperature peaks can be found as late as years of 1300. The trend from the top was first for not so above temperature and then cooler than normal temperature climaxing with the Mini Ice Age of the 1600s.

Trend has been warmer since then with corrections during the 1700s and 1800s followed by acceleration from shorter term cyclical turns during the 1930s, 1980s and 1990s. Use of the shorter cycles suggests timing of the 1,000 year cyclical warm trend is not due for a top (hottest) until the 2030s the earliest. With this cyclical trend there are phases of wet versus dry conditions as well as corrections of short term periods of cooler temperature.

2008 update-- There is a decadal cyclical trend that is due to cause a correction of the global warming trend. To what degree of correction is not known at this time but 2008 seems to have been cooler than recent years although some regions set records this year for warmth. The corn belt may show relative strength over the Northeast or US in terms of warm temperature. Weather volatility to continue.



Precipitation is due for a cyclical peak for my firm's index study shown above.



Crop condition shown as consecutive year on year rather than stacking as standard statistical techniques offers a more visible trend following examination. The use of technical techniques of trend lines and fibonacci retracement offers insight to trend fluctuation. I am concerned that the supporting up trend line from 2002 to 2008 has been too good to be true. Seems time for decadal cyclical decline. The pattern from 1996 to 2002 offers graphical portrayal of such a cycle.

Weather summary- Many years ago I assumed I would lower weather crop impact probability following 2008. I have reached the conclusion it is best to allow another high probability year for a weather based crop impact.

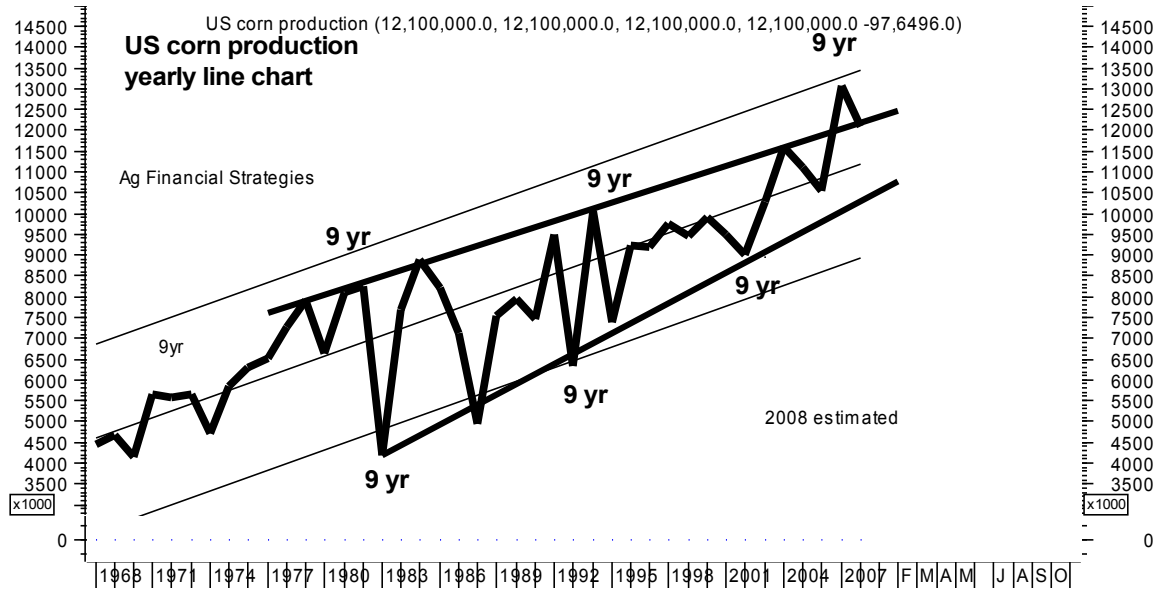
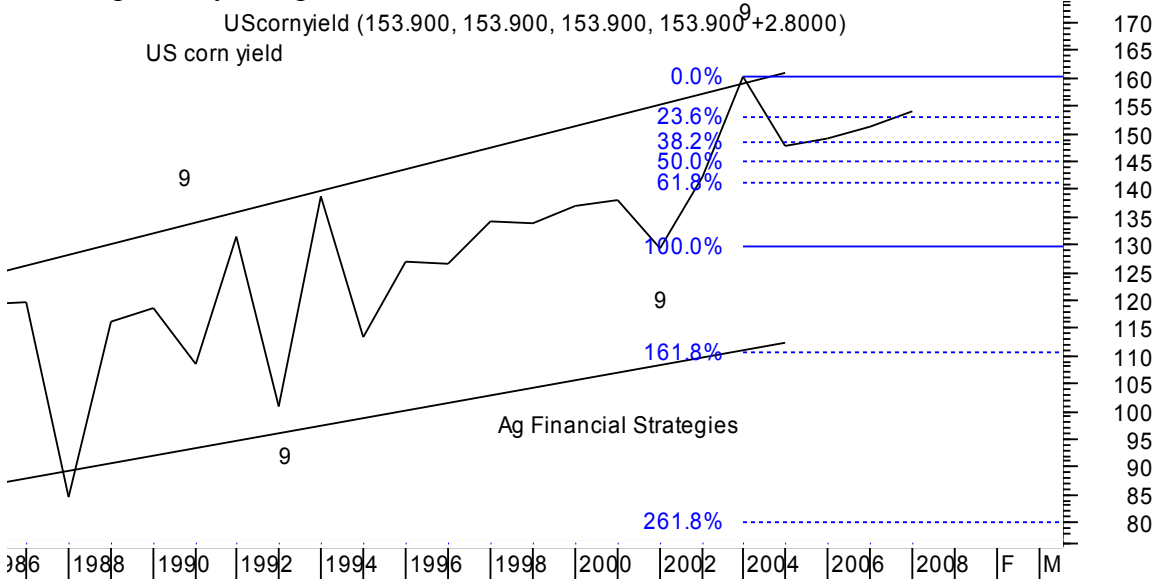
Production

- Will there be sufficient financing for optimum production for 2009.
- Balance sheets suggest more acres are required for 2009 than 2008 while current pricing will not buy these acres.
- Higher cost of production and relation to soybean pricing favors bean production over corn –at the time of writing this report.

Yield fluctuates with similar cyclical structure as weather and prices. About 75% of the time for past 140 years yield of corn has been of a 3yr cyclical trend. When yield does not follow this trend the next degree of fluctuation is a 5yr cycle that occurred 16% of the time. A huge decline in occurrence and so I assume a huge decline in probability. What is more interesting is the occurrence of still larger trend fluctuation is one quarter of that of the 5yr. 2008 was year five for the yield cycle!

The trend for yield since 2005 (Illinois drought bottom) has been higher but of peculiar slow momentum. Is a struggle a sign of correction within larger bearish yield trend? Has global warming interfered but only to a point when normal decline will occur (at latest allowed)? I am going with 80% probability that yield declines in 2009. I remind myself

that statistics are a wonderful thing but regardless of probability the next data entry may be forecast no better than with a flip of a coin. Something trend followers understand and more importantly --respect.



Cyclical trends of production and acreage have been a little less of the 3yr variety and more of 5yr to 7yr. Current trend status suggests equal opportunity for higher or lower production and acreage.

Production summary- I will bias toward the yield study which suggests chance for lower yield. Acreage to range from 84 million to 89 million with a forecast for 85. **Harvested acres to be 10% less but my research warns it has been too long since a larger than normal reduction of harvested acres.** Yield to range from 156 to 136 with forecast for 144. Production to decline about 13% or more. One should keep in mind that production number by itself offers equal probability for higher or lower production for 2009.

Demand

- Models forecast recovery for the stock market during 2009.
- Models forecast recovery for some economic indicators such as the ISM manufacture index.
- Interest rates to be flat for 2009.
- US dollar to peak late 2008 or early 2009 for 3yr business cycle. May only lead to range trade and range trade still means a low dollar. A low dollar is good for exports.
- A forecast is made for 8% +GDP for China. Global economy to show stability.
- US prints large sums of cash. More difficult to fight inflation.
- The increase in socialization is right on cue. Socialization will not fight inflation. Not all socialization is negative but intelligent management if at the right time. And if not then negative results may only come to fruition following a boom from the turn to socialization. The only truth to an economic concept is that it will burn out sooner or later and the earlier concepts deemed “don't work” will work. And for a season as well.
- Non US regions in terms of weather trend patterns are similar to US. Lose production in some global regions and US markets become more important.
- Ethanol industry to maintain near capacity so corn burn rate to remain high.
- High grain prices during 2008 were not high enough and for long enough to damage demand trend for this decade. Still huge demand volume wise.
- **The seasonal down trend always relates to less demand per pricing pressure as trade waits for new crop. During 2008 this trend was exaggerated beyond comprehension and in relation to US financial crisis. Result was a decline in price that was too far and too fast and when volume demand was and still is near record. So under valued a disgrace to free markets.**

Conclusion-Demand to improve at brisk intense pace last quarter 2008 through first quarter 2009. Slower but still net growth pace for at least pricing pressure into summer 2009 with chance emotional explosion if there is a crop problem.

Price –The indicator of demand.

The models continue to expand the wardrobe.(More historical data is equal to more roots. And more roots creates more and sweeter fruit.)

- 2004- Kondratieff cycle top added. The related bottom is not used.
- 2004- 216 year cycle bottom added.
- 2008-216 year cycle top is added. Quest for addition of 170 year cycle tops comes to an end. Now non price model cycle and still a cycle of global climate and affairs of man.
- 2008- Allowance for decadal business cycle (9yr) trend within the models to increase by one year. This allows for bullish surprise for new record high for corn for 2009. This alteration comes from a statistic that has not occurred in 204 years.

100 year bull markets and the 216 year business cycle.

From the 1200s through the 1400s commodities were range bound closing with a new low for wheat. The trend for wheat has been higher since then. A turning point of about year 1500 fits with global climate cycles of 170, 510 and 1000 years. The human race took this to heart with spiritual, social and political awakening combined with massive increase in global population, an explosion of creativity, productivity, standard of living and increase of gross domestic product. And from a 216 year business cycle bottom.

Bull markets for 216 year cycles last for about 100 years when following bottom to top. When following highest price between cycle bottoms bull markets can last as long as 140 years. The difference is from a characteristic of new highs a few decades following true cyclical peak and such rallies have been unsustainable.

The Three Bulls

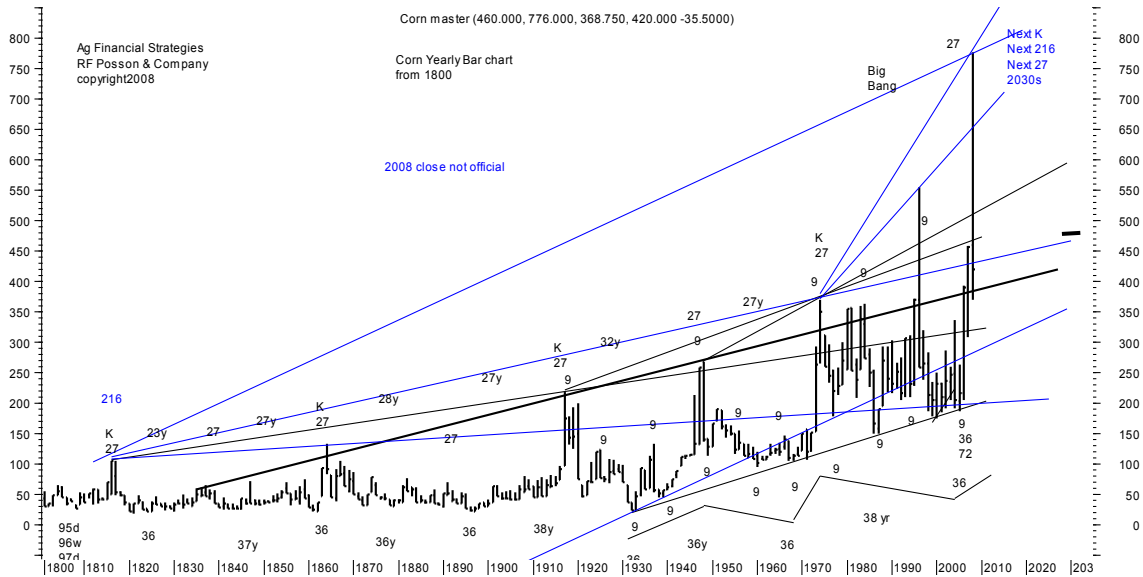
The current 500 year trend for some commodities such as grains breaks into two complete bull markets of near 100 years each and a third is in session.

1500s- 4400% increase in price for wheat for some countries. In France, Catherine de Medici (of The Medicis) struggles to keep a son at the throne and financing for her favorite palace. While Protestants and Catholics murder one another even on a palace lawn and in palace halls. A cut to the throat is preferred. I find this interesting when watching another religion in another country and during this decade. A prince hangs blocks of ice over his bed to offset the heat of the late 1500s. Spies abound and if you are not a member of an organization or group you do not exist. Martin Luther comes forth asking what happened to love. And yet business, innovation and knowledge grew at record setting pace. Economies grew and prices increased as man learned printing presses can also create synthetic gold --money. In terms of price we now are around 1560s. And if price were to remain true to this history corn is on its way to \$22 by 2030s and near \$10 by next decade.

1700s- 2200% price increase for commodities such as wheat and corn. A bull market for a little over 100 years and into 1817. French revolution and US independence revolution. By time of the top the US will experience its first international test as to a nation that can last. And a cold strike as remnant of earlier mini ice age creates snow every single month for some US states for one year. Crop damage assists the final leg higher into the end, the climax of this trend. We are currently around 1780s if similar to this trend. If near exact re-occurrence of price swings corn can trade to near \$11 next decade and near \$16 by 2030s. Similar trend for 1780s was up 307% while the for this decade corn was up 317%.

1933 to 2034(?) (Subject to revision due to chance of end of this world any day now until then.) With 3400% price increase for corn as of 2008 high! History did repeat and I can now visit a skeptics grave. 75 years in trend as of 2008. From the dark side are World War II and the lesser wars and the Great Depression and 9/11. From the light side the home appliances, aviation, automobile and the computer. This trend has been the fastest of technological development, fastest transmittal of news/ideas, greatest of social

achievements and record setting economies. And the printing presses keep printing. Commodity producers must maintain equality to non producers for rightful share of the consumer dollar or this trend will fail to achieve the full number of years and so also the global macro economy will fail. **Message to Americans: Do not fight prosperity by fighting commodity bull markets.**



Cycle Series Analysis based research of price.

By now this cyclical based chart has become famous. I have used this chart since the 1990s. For this year I added the 216 yr top and some trend lines in relation to a variety of cyclical tops. The forecast since 1993 had been for a new record high for corn during 2004 to 2008. During 2008 corn traded to a new record high. For past 6 years I had felt the bull market this decade would be the “Big Bang” of corn prices. And reflective of commodities in general. The markets did not let me down although in 2005 I was very suspicious of manipulation by the bear side. Meaning it was taking too long for the illusion that low prices were a good thing to convert to reality that prices were too low. Corn was the latest of commodities to bottom. It made up for this by dropping some skeptics to their knees and for repentance.

The current low of 2008 was near an important cyclical based parallell line of support near \$3.00 spot.



The monthly bar chart of spot corn futures is labeled with 3yr business cycle turns and alternates plus annual price trend turns. The chart includes retracement studies that offer potential up side objectives as well as resistance. And the indicator at the bottom suggests a deeply oversold market which I believe correlates with other studies suggesting an extremely under valued market. The horizontal blue line at left hand top of chart is time frame for seasonal and annual tops. Also for the 3yr,9yr and 27yr tops if corn did not peak in 2008.

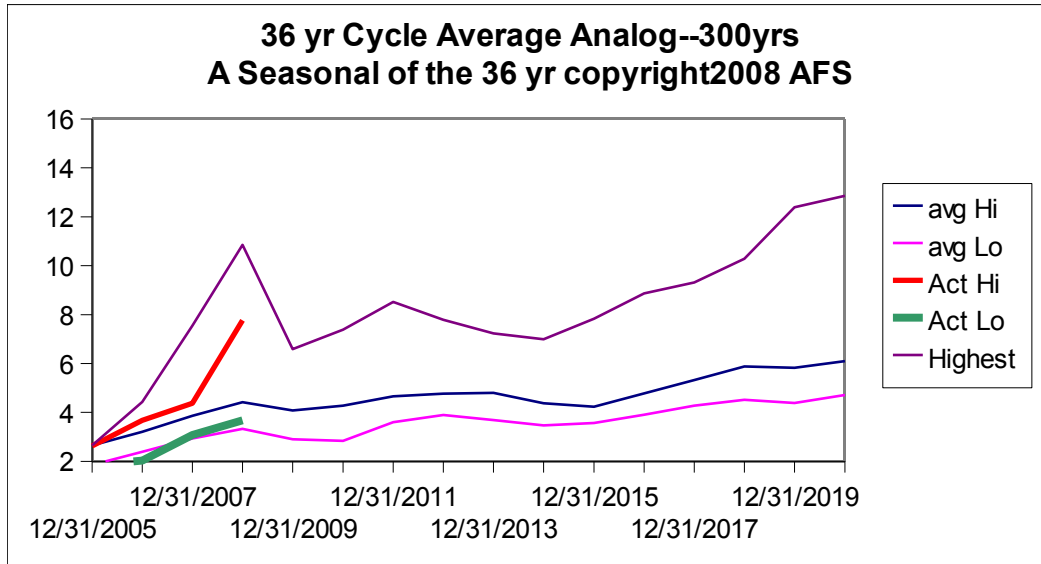
Models assume a late 3yr business cycle bottom arrived in October 2008. Models also assume 3yr, 9yr and 27 yr business cycle tops occurred near the high of 2008. If correct a new record high for 2009 and 2010 is not anticipated. (Still larger business cycles are still up and will remain so for many years.) However, recent model review uncovered evidence over 200 years ago that a slightly longer 9yr cycle should not be ruled out. This statistic would allow for a new record high during 2009 but not for 2010 and would require that the high of 2008 is not the cyclical tops currently stated by the models.

I ran the models with a forced input that the 2008 high was no more than annual, seasonal and intermediate trend tops and that the decline was over reaction due to financial crisis and not a corn economic crisis. The end result was that such a script is allowed and by using an earlier forecast that allowed for a 3yr top during 2007. If this is correct we should see an explosive relentless rally during 2009 and back to near the 2008 high with chance for a new record high.

At this time this is not the favored forecast but deemed worthy enough to be considered in light of the corn yield and weather possibilities.

With use of the 27yr top as of 2008 the forecast calls for a significant retracement higher for 2009 and in terms of seasonal and annual trends. This trend can be a component that allows for a trend higher into 2010 (next 3yr top).

Note the long term trend line from 2005 through 2007 lows acted as support for the October low for 2008. For now I think this suggests the long term trend is still up. If so then the spring weather based rally took price of corn too high too fast but did not reduce demand per long term trends. The decline for 2008 was also too far too fast and goes a long way to supporting demand.



A 36 Year Cycle Analog

In 2006 I presented this analog comprised of the highest annual price of a group of 36 years cycles dating back to 1720. It was fascinating to watch price rally at similar time and pace toward the \$10.84 high for 2008. Note that for 2009 the highest price should be \$6.59. In addition the price high of 2008 seems to be more in no man's land. It does not compute all that well. When corn rallied well over \$6.80 to \$7.00 expected resistance level it was if it might as well rally to around \$8.50. Sense it did not I am left with a feeling that the price of 2008 is unfinished business but how long will it take.

Other analogs

For a few years now I have noticed a strong correlation of this decade's bull market with major bull markets of the 1930s and 1970s. Current correlation will allow 2008 high to remain so through 2009 but allows 2009 to be a last high priced year of this decade's up trend. Similar to model opinion. There has been much talk of US economy similar to 1970s stagflation or 1930s depression.

Other price statistics

During 2008 there was a surge in anti bullish commodity and anti commodity investment characteristics. "Unprecedented" was offered in some news articles about price. Commercials complained the market was broken as prices rallied. (Interesting that they do not complain about broken market when prices crash.) For fun I ran a rate of change study to isolate 2 year bull markets and more so to eliminate seasonal bull markets.

The study suggested that a little more than 50% of the time price rallied over 2 years time and for the past 500 years. I feel most of my adult life I was told commodities trend lower most of the time if not all the time. This statistic suggests many professionals in the trade have been incorrectly educated! In addition half of these bull market were of 60% or more price increase and price can increase as much as 400% in two years. With the cyclical and technical perspectives I find no evidence that the bull market this decade should not have occurred in the fashion it did. What was different this time around was the fact that the World woke up that we are running out of oil and demand for oil is highest ever and that the backyard hobby of ethanol production had become an industry. It seems it is harder to predict fundamentals during cyclical trends than to predict cyclical price trends. **Without the inclusion of quantitative price or technical analysis with fundamental analysis the market analyst or economist is working with one hand tied behind his back. And I believe Cycle Series Analysis beats all of these and is the best bridge between these disciplines of price analysis.**

Recession

I believe corn can be strong priced during recessions. The correlation is not as strong as one might expect. **In addition the recent development of a trend following study of an economic indicator suggests that if the US is in recession then the recession can end some time in 2009 even as soon as January.** If not then a sizable recovery but as correction within the recession trend should occur.

Political

For past 160s years there have been more commodity bull markets when a Democrat was President than other wise.

Forecast

Corn- Higher now into spring to summer perhaps later. Potential for \$5.50 to \$6.59. A crop impact could cause higher price than this during 2009 but recession will probably negate chance for new record high until 2010 if then.

Soybeans- Higher to \$12.00 to \$15.00. There is a model script that offers new record high 2009-2010 but of less probability than to \$15.00.

Soymeal-Higher to \$350. Like beans there are model scripts that allow for \$400 to new record high for 2009-2010.

Soyoil-Higher to 45 to 55 cents. Different model script than grains allows for bullish potential into 2012 with potential for new record high.

Wheat-Higher to \$7.00 to \$9.00 for Chicago wheat market for 2009.

Input forecasts for Fusion models (fundamental and technical)-

Energy- Higher into 2012. Long term bottom this year to early 2009. Preference for this year.

Livestock/dairy- Higher into late 2009 and may extend into 2010.

Economy- Recovery for 2009 but true decadal boom cycle may not begin until early next decade and with potential to begin 2 years earlier than this decade's boom.

Commodity indexes- To trend higher into 2010.

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Past results are not necessarily indicative of future results.

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