

THE TRADING ROOM

Recommendations & Comments

Friday
January 28, 2005

We should have several new option selling recommendations within the next few days.

Futures Focus

Both fundamental and technical indicators are negative for all CBOT ag commodities.

Preview

The outlook for 2005 is focused on the prospects for record global grain/soybean production and larger than normal stocks of unsold farmer grain (US & South America). Additional negative factors include recent tempering of global economic growth (due to high energy prices) and slowing growth in Chinese soybean imports. US & global soybean and wheat stocks are poised to advance further over next year and a half in the absence of major crop adversity. Funds have little incentive to cover large shorts. Adverse weather in South America and/or much stronger than expected Chinese purchases of grains and oilseeds are only major hazards to otherwise negative price outlook.

Wheat

The world wheat stockpiles are at record levels. On December 10th, the USDA reduced its estimate of the 2004-2005 U.S. ending stocks from 568 to 553 million bushels, up from 547 million bushels in the previous year. Globally near perfect growing conditions exist. The large world ending stocks resulting from massive crops from the world's exporters should continue to dampen any meaningful rally. Fund short covering and ideas of less planted acreage are the only things supporting. Worldwide, the USDA is expecting 2004-2005 ending stocks to increase from 131 to 143 million tons, or 24% of annual use, matching the highest in three years. The price downtrend in place since May '04 is still intact and longer-term fundamentals remain bearish. Hemisphere growing conditions, continuation of lackluster Chinese import demand and favorable early spring weather in the US should cause further **erosion to the \$2.75-\$2.80 area.**

Soybeans

The recent 40-cent rally from the contract lows which was inspired by fund short covering has fizzled and now March Soybeans are only 15 cents from the contract lows near \$5.10. Due to excellent weather the '05 South American soybean crop is off to an above average start. Private and public sector estimates on the gain in '05 South American soybean production range from 17-19.5 mmt. If realized, a gain of this magnitude will set the stage for record spring '05 soybean supplies in the western hemisphere. Chinese imports are down compared to last year's numbers. In the absence of weather adversity in South America, the soybean market is not only headed substantially lower but may be in for an extended period of low prices if a trend of higher '05 US soybean yield unfolds on early indications of even higher '05 US soybean area than the record 75.1 mil acres planted in '04. Farmers continue to hold out for higher prices in Brazil and the United States and this factor alone should cause prices to fall forward unless the farmers decide to sell when

South American begins to harvest their crop. **At that point you would probably see soybeans in the low \$4.00 level.** World Soybean ending stocks are near the highest level in almost 2 decades and should continue to put a lid on any large rallies. Risk/reward still strongly favors the downside.

Corn

\$1.85 Corn should not be too far away. Massive crops through out the entire grain floor should cap any chances for rally. Short covering from the funds and small speculators are about the only supportive factors. With China selling corn to our normal Asian buyers and Russia trying to step up production and get on the world export market things don't look good for those bullish Corn. Farmer selling should push March **Corn to new lows to the \$1.85-\$1.90 area** if '05 South Hemisphere crops aren't threatened. US stocks are simply too large to allow farmers to earn carry on stored corn. The 2-year price up trend in corn is over for now.

New Recommendations:

- **Coffee** – **A bullish scenario seems to be brewing in the Coffee.** The coffee market seems poised for further gains following the 13-cent sell off that started at the very end of last year and continued until January 11th. Funds have lightened up their long positions and commercials began covering their shorts, putting the market into better balance from which it can trade from going forward. Absent on the decline in price was aggressive producer selling. This is the most bullish factor of all and key difference between this correction and past hasty retreats on the other failed rally attempts last year. Sources continue to talk of firming differentials for better quality coffee and difficulties in getting this coffee at “reasonable” prices. *The market it seems is finally becoming more demand driven than before, another bullish indicator.* There is currently strong demand in the industrialized economies, aided by some increase in demand in Latin America, which is helping to sustain coffee prices at current levels. The International Coffee Organization estimated world exports totaled 6.73 million bags in November 2004, up 9.81% from the 6.13 million bags. Pronounced concern about supply as the market looks to a seasonally reduced 2005/06 crop, further depressed by the preponderance of older trees more affected by exhaustion than new growth, dominates. Coop stocks have risen substantially from last year's levels, but even so this number represents a fall from November levels and the incidence of higher exports in December suggests some farmers may be taking advantage of recent higher prices, with the implication that this will limit supply further down the road when the reduced output hits. Market sentiment is overbearingly bullish, and many traders look to a break over the contract high at 108.70 next week. Fundamentally, declining Brazil output, reduced Central American production, and raging upside sentiment are bullish. **We continue to recommend buying Coffee Futures or buying a May 115 call, and then to pay for 70% of the call sell a 160 call, a 150 call, a 90 put, and 85 put.**
- **Gold and Silver** – No clear direction is apparent yet. A possible secondary *bear flag* could be setting itself up. If this proves to be the case we could have another large, quick move downwards. A move below \$421.50 in April Gold and \$6.48 in May Silver are the points to watch for a possible breakdown. We feel if these levels are taken out that we will see a decline to \$410-\$400 gold and \$6.00 -\$5.80 in silver.

Thursday's Trading Activity Recap:

- [January Feeder Cattle Puts](#) – The January Feeder Cattle 90 cent puts we sold @ 90 pts. (\$450) on November 23rd expired today for 100% of **profit of \$450.00**.

Current Positions:

- [Soybeans](#) – Sold March Beans @ 538 on January 13th. **Move protective stop to 526**. Settled @ 516 3/4 for an **open profit of \$1062.50**.
- [Corn](#) – Sold March Corn @ 202 1/4 on January 13th. Stop is 209. Settled @ 195 3/4 for an **open profit of \$325.00**.
- [Coffee](#) – Bought May Coffee @ 104.50 on January 21st. Protective stop is 100.50. Settled @ 105.55 for an **open profit of \$393.75**.
- [Coffee](#) – Bought a May Coffee 115 call. Then we sold a 160 call, 150 call, 90 put, and 85 put to pay for approximately 70% of the price the 115 call. Trade date is January 21st. Total paid was 180 pts (\$675). Settled @ 143 pts. for an **open loss of \$138.75**.

Corn, Soybeans Fall on Report of Crop Gains

Corn and soybean prices fell yesterday in response to the U.S. Department of Agriculture report confirming U.S. farmers harvested record crops in 2004. The reports confirm supplies are burdensome and the market will be under pressure as farmers are forced to sell into late January and February to raise cash for seed, fertilizer and taxes. The futures market is saying the crop is too big and prices will eventually fall.

The report put the 2004 final corn production at 11.807 b.b. up from the November report of 11.741 and a year ago of 10.114. Carryover stocks for the start of next falls harvest was put at 1.960 b.b. vrs. 1.843 last month. Stocks on hand as of December 1st were 9.449 b.b. vrs. 7.954 a year ago. Soybean production was 3.141 b.b., up from 2.454 a year ago. Stocks as of December 1st were put at 2.305 b.b. vrs. 1.689 a year ago but the ending stocks for next falls harvest were dropped from 460 m.b. last month to 435.

Summary 1) the US and world corn surplus is greater than expected, **2)** there will be more acreage for Midwest row crops in '05 than previously imagined **3)** US soy oil stocks will not be as tight as anticipated, **4)** record global soybean stocks continue to edge higher despite better than expected US soybean exports, **5)** high ocean freight rates-which represent over 3/4 the value of US corn-are crimping Asian demand despite low US farm gate prices and **6)** the wheat market may need more time to digest lower than expected wheat area although both US and global wheat stocks are poised to trend higher 05/06. **Bottom line - maintain row crop shorts and sell rallies in wheat.**

Current Short Option Positions:

- [March Coffee Calls](#) – Sold March Coffee 150 calls @ 80 pts. (\$300) on December 8th. Settled @ 2 pts. for an **open profit of \$292.50**. Expires February 11th.
- [February Hog Strangle](#) – Sold February Hog 80 calls and 66 puts for 105 pts. (\$420) on December 30th. Settled @ 12 pts. for an **open profit of \$372.00**. Expires February 4.
- [March OJ 150 Calls](#) – Sold March OJ 110 calls for 100 pts. (\$150) on December 30th. Settled @ 5 pts. for an **open profit of \$142.50**. Expires February 18.

- [March Copper Strangle](#) – Sold March Copper 170 calls and 120 puts for 200 pts. (\$500) on January 3rd. Settled @ 15 pts. for an **open profit of \$462.50**. Expires February 23.

Open Orders:

- [NONE](#)

TRADER'S AXIOM

By
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2004

Losses are Pain.
Realized losses are realized pain.
Realized Pain, man seeks to avoid, at all cost.
The Cost is high for pain avoidance.
Therefore, the loss is avoided, thus unrealized.

The market's design and function is to produce unrealized losses,
it's a zero sum game.
Unrealized losses produce Pain.
Therefore, the Market is Pain.

Pain is against Man's Nature.
This Pain signals an invading, adversarial force at work against man's natural condition.
Therefore, the Market is against Man.

But, what if Man must live with the Market?
He must, therefore, control the Pain, which is against his Nature that the
Market produces through its designed role to produce losses,
it's a zero sum game.

Controlling Pain is achieved by taking losses that the market produces.
The losses taken should be done so before the Pain becomes overwhelming and lethal.

So...control Pain by willingly taking losses that are now small.

Profits are Gain.
Gain is the absence of Pain.
The absence of Pain is aligned with Man's nature and should be embraced and held.

Embraced and Held profits, overtime can expand.
Expanded Profits are Big Profits.

Big Profits can never be achieved by taking small profits.

THEREFORE, CUT THE PAIN AND HOLD THE GAIN.

calculated without considering commissions and exchange fees. Trading in futures, options, and securities futures involves a high degree of risk and may not be suitable for everyone. Only risk capital should be used. Hypothetical performance results have many inherent limitations, some of which are described below. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved by any particular trading program. One of the limitations of hypothetical performance results is that they are generally prepared with the benefit of hindsight. In addition, hypothetical trading does not involve financial risk, and no hypothetical trading record can completely account for the impact of financial risk in actual trading. For example, the ability to withstand losses or to adhere to a particular trading program in spite of trading losses are material points which can also adversely affect actual trading results. There are numerous other factors related to the markets in general or to the implementation of any specific trading program which cannot be fully accounted for in the preparation of hypothetical performance results and all of which can adversely affect actual trading results. Past performance is not necessarily indicative of future trading results.