U.S. Commodities Markets

USDA's Prospective Plantings Report: A Corn Assessment For The Texas Cattle Feeder

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- Corn data from the March 31, 2023, the USDA's Prospective Plantings and the Grains Stocks revealed two narratives that can influence the price path of market year (MY) 23/24 corn.
- The initial acres data shows contracting area in the high plains, precipitously higher acres in the Mississippi Delta and moderate growth in the key producing states.
- In the USDA's Prospective Plantings, the USDA estimates that acres are forecast to decline by -5% YoY in Texas, and -1% YoY in Nebraska. Adding Kansas corn acres forecasted at +2% YoY, the estimated net loss between the 3 central states is 100,000 acres.
- Severe drought can restrict corn plantings. Compared to 2022, an overwhelming majority of the 3-state's corn acres reside in areas that are experiencing structural drought.
- Total on and off farm stocks in Nebraska and Kansas are 921 mbu, -334 mbu, -27%, YoY. Total stocks for the two states are the lowest level since 2014 and the 5th lowest in 20 years.
- What does this mean for the Texas feedlots? For the near term we expect corn basis and corn futures volatility to remain elevated. While CME corn futures prices may decline, cash values in Texas, Kansas and Nebraska should remain firm.

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Corn data from the March 31, 2023, the USDA's Prospective Plantings and the Grains Stocks revealed two narratives that can influence the price path of market year (MY) 23/24 corn. First, U.S. corn producers intend to increase planted acres by 2.0 ma YoY to 91.9 ma. This would be the second largest acres in 6 years and is a bearish input for futures prices. Second, domestic MY 23/24 corn production should experience stark regional variances. The initial acres data shows contracting area in the high plains, precipitously higher acres in the Mississippi Delta and moderate growth in the key producing states. Ultimately, we believe that the regional corn scenarios will influence basis along with the breeding intentions of broilers, layers, cattle, and hogs.

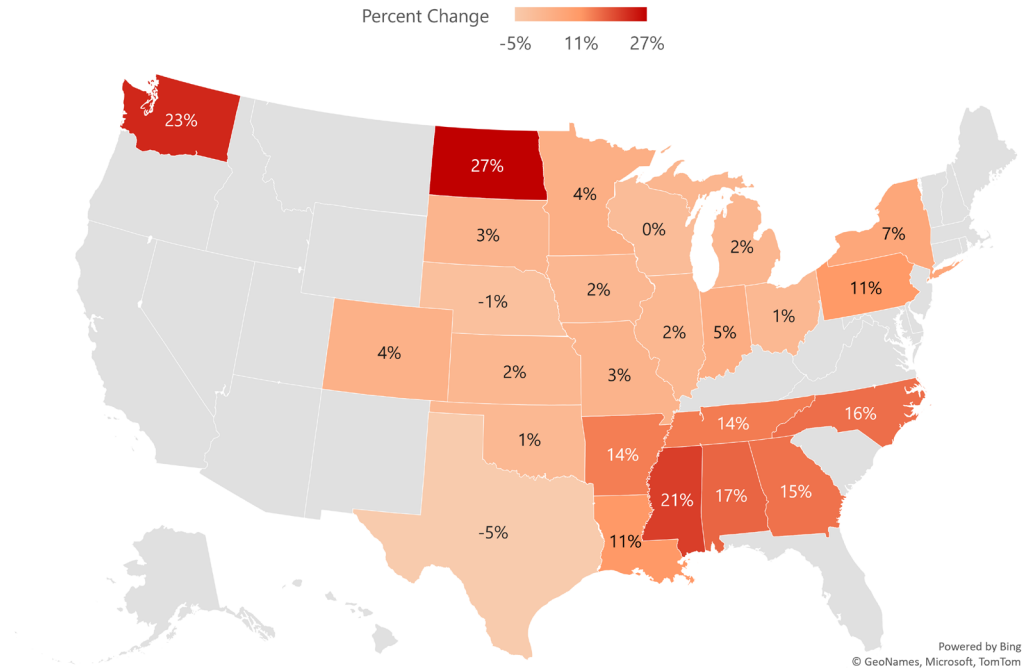
At 91.9 ma, U.S. Planted Corn Acres Would Be Fourth Largest in 10 Years

The 2.0 ma YoY increase in prospective planted corn acres was not a surprise to us. In our note about corn acres prior to the USDA's acres assumptions, we argued that the U.S. corn producer possessed ample financial incentives to expand MY 23/24 acres. From declining input and production costs to robust corn futures prices, 2022 and early 2023 presented the U.S. corn grower with numerous opportunities to secure favorable hedges for MY 23/24 and MY 24/25.

Our assumption that strong futures and cash prices would dramatically increase corn acres in the secondary and tertiary corn producing state was correct.

Please see disclosure starting on page 5.

Year-on-Year Change in Planted Corn Acres



Source: USDA, HilltopSecurities.

Precipitous Acreage Increases in the Mississippi Delta and the Deep South

Our assumption that strong futures and cash prices would dramatically increase corn acres in the secondary and tertiary corn producing state was correct.

We believe that the increased corn acres and the prospect of climbing production can weaken basis and provide further economic incentive to expand broiler and layer flocks in the Mississippi Delta and Deep South.

Prospective planted corn acres in the Mississippi Delta (Louisiana, Mississippi) and the Deep South (Alabama, Georgia, Arkansas, and Tennessee) saw an acute expansion in the March report. The average intended acres expansion across these six states is +16% YoY. We believe that the increased corn acres and the prospect of climbing production can weaken basis and provide further economic incentive to expand the region's broiler and layer flocks.

Corn acres are expected to expand incrementally in the core producing states, (Iowa, Illinois, Minnesota, South Dakota). Average planted acres in these four states are expected to rise by 3% YoY. Nebraska is the only core, top five corn producing state, where planted acres are projected to decline.

Planted corn acres in Nebraska and Texas are at a five-year low. Planted acres are forecast to decline by -5% YoY in Texas to the lowest value since 2012. Nebraska corn area is estimated to decline by -1% YoY to the lowest level since 2018. Kansas corn acres are forecasted at +2% YoY. This would be the fourth largest level in 10 years.

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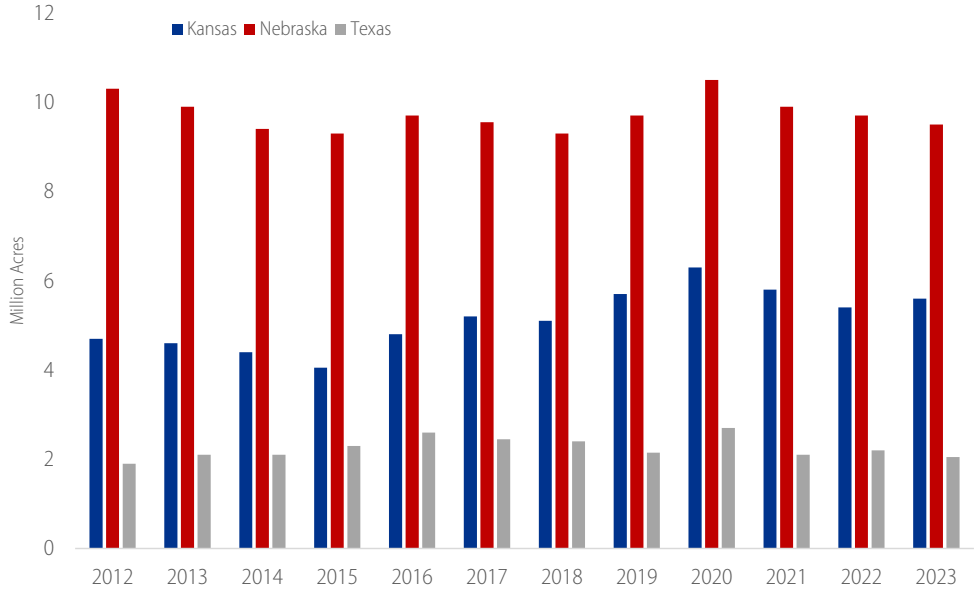
Three-State Planted Corn Acres



Source: USDA, HilltopSecurities.

Estimated Three-State Corn Acres, 17.15 ma, Are the Lowest Since 2018

Despite an entire growing season ahead, unless a supply or demand shock emerges to push the CME corn futures curve sharply higher, or the three state region experiences precipitation that mitigates the drought, we don't believe that corn producers have reason to increase planted acres.

We find it noteworthy that, after removing the outliers, the mean acres expansion is four times as large as the mean contraction.

Over the last 10- and five-year periods, the difference between the three-state actual planted acres and the prospective plantings data is mixed with a 60%-40% split between contraction and expansion. We find it noteworthy that, after removing the outliers, the mean acres expansion is four times as large as the mean contraction.

Severe Drought Can Restrict Corn Plantings

Compared to 2022, an overwhelming majority of the three-state's corn acres reside in areas that are experiencing structural drought. While an entire crop year lies ahead, the starting soil moisture levels are a source of concern.

- Nebraska: 40% of the corn crop is in areas experiencing extreme to exceptional drought while 45% of the state's corn is in a severe drought. This compares to 19% and 55% in 2022.
- Kansas: 54% of the state's corn is in areas experiencing an extreme to exceptional drought and 13% of the state is in a severe drought. This compares to 28% and 33% during the same time in 2022.
- Texas: 52% of the state's corn is in areas experiencing an extreme to exceptional drought and 23% of the state is in a severe drought. This compares to 53% and 21% during the same time in 2022.

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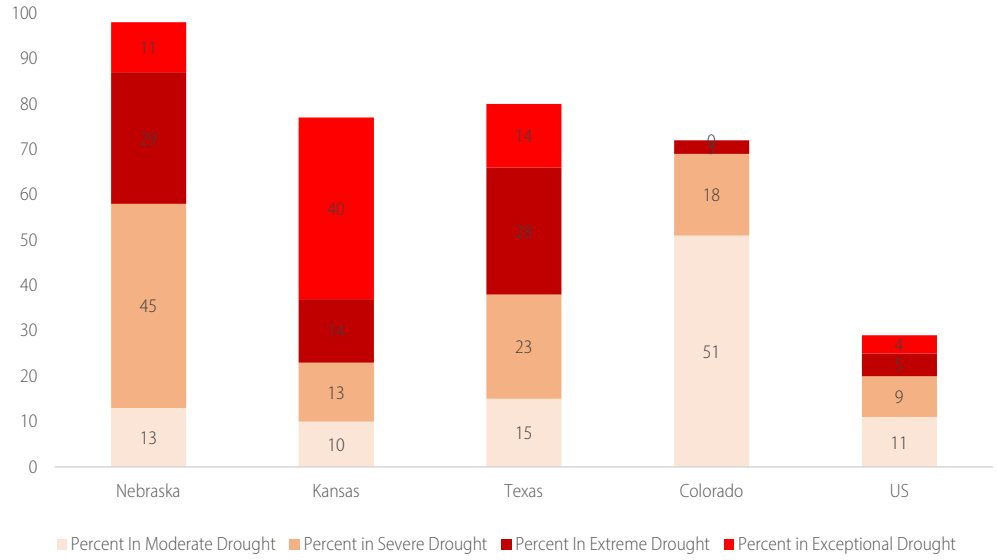
Percent of Corn Located in Drought: 4/4/2023



Source: HilltopSecurities.

While we are not prognosticating corn yields scenarios, the pivot from a La Nina to a neutral ENSO or a weak El Nino pattern can improve the national corn yield objective. Unlike the eastern corn belt the three-state region requires substantial moisture to improve early-stage plant development and remedy the structural dryness. **As the crop gets planted, close scrutiny by Texas feedlot operators should be paid to the region's yield and production potential.**

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The Three-State MY 23/24 Corn Yield Potential Remains Ambiguous

Despite the evolving ENSO pattern to a neutral/weak El Nino, we do not have a strong yield outlook for the three states. Fifty years of state-level yield and climate data, shows that mild El Nino patterns have a mixed impact on regional yields. We see the structural soil moisture deficits throughout the region as a key impediment that can limit the yield potential.

Declining Corn Area and Low Stocks Can Adversely Impact the Western Cattle Feeder

On paper, the estimated -100,000 YoY decline in three-state acres is minimal, representing less than 1% of the total acres. However, the implications on future cash prices can be material. Using the March 1 corn stocks data, total on and off farm stocks in Nebraska and Kansas are 921 mbu, -334 mbu, -27%, YoY. Total stocks for the two states are the lowest level since 2014 and the fifth lowest in 20 years.

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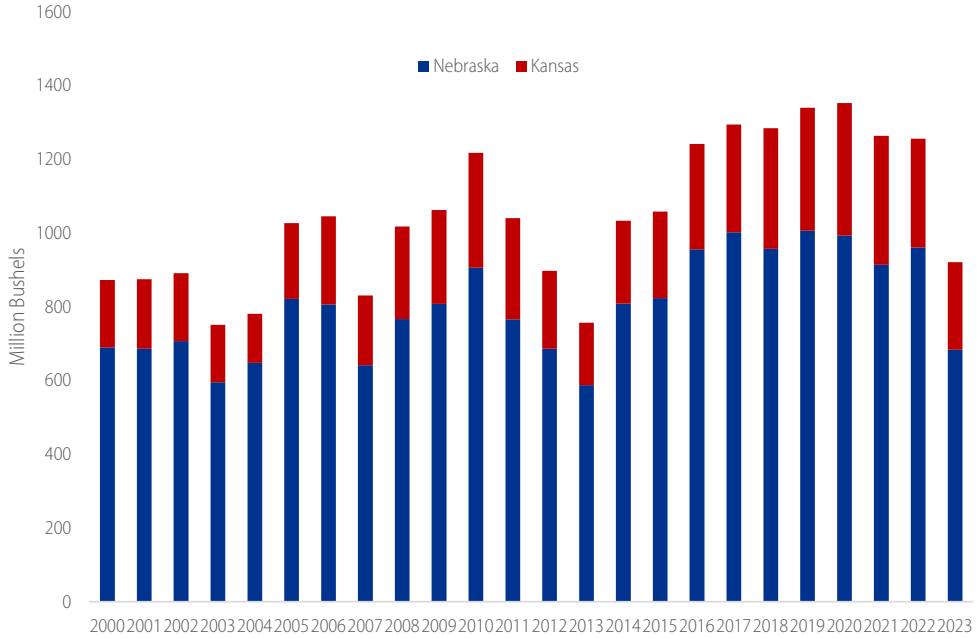
March 1 On-Farm + Off-Farm Stocks



Source: USDA, HilltopSecurities.

What Does This Mean for the Texas Feedlots?

For the near term we expect corn basis and corn futures volatility to remain elevated. While CME corn futures prices may decline, cash values in Texas, Kansas and Nebraska should remain firm. The combination of tight upstream corn stocks, competition with other mid and downstream corn users and uncertainty about MY 23/24's crop size should keep cash values firm.

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When adopting the MY 23/24 91.9 ma into our price model and maintaining the USDA's initial yield and demand projections from the Agriculture Outlook Forum **we lower our December'23 futures fair value price range to $4.70-$/5.28 bu**.