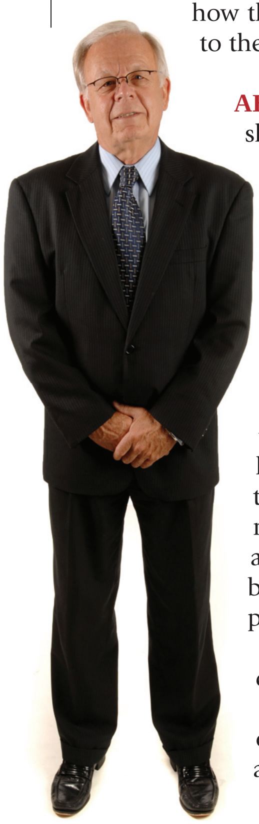
MARKET STRATEGY By Jerry Gulke

Brazilian Real versus U.S. Soybeans

The currency relationship between exporters of grains and those who import grains has long been a factor in pricing. The soybean currency relationship is probably the one that has affected U.S. farmers the most, beginning with the expansion of soybean production in Brazil brought on by the Nixon administration's export embargo. The rest has been a history of expansion in Brazil, which had an initial currency advantage.

Brazil benefited by selling soybeans in dollars, converting back to the Brazilian real at a 1:4 ratio. U.S. soybeans at $6 meant $24 to the Brazilian farmer. The chart to the right shows the acceleration of the real from 2005 through 2008. During that time, in spite of rising soybean prices, Brazil became less competitive with U.S. soybeans, as the currency ratio was two reais to $1. U.S. soybeans at $10 equaled 20 reais to the Brazilian producer, not 40!

The U.S. farmer was not only more competitive but more profitable. In fact, there were years during that period where the Brazilian government extended farmer loans. A close examination of subsequent events reveals how the value of U.S. soybeans has been tied to the hip of the Brazilian currency.

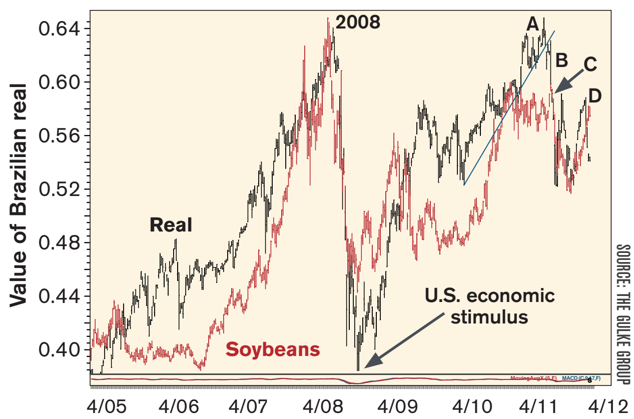


ABCD Relationship. Point A on the chart shows the real taking out the 2008 highs as if to indicate that Brazil's currency had the worst behind it and was going higher. It failed to extend, collapsed through the uptrend and tried to retest that uptrend only to post a weekly key reversal down (point B).

Coincidentally, with the attempt of the real to break out to the upside, soybeans attempted to break out to the upside of a nine-month sideways market and also failed, and then reversed trend completely on the Sept. 12 USDA report , closing lower in what turned into a $3.50 collapse into December and the beginning of the South American crop problems (point C).

The market realized that if the Brazilian currency was deflating, it made their market more competitive and the price of U.S. soybeans would need to fall ahead of the U.S. harvest, which it did into December.

Brazil's Currency Relationship With U.S.



> *During the rise of the Brazilian real from 2005 to 2008, the U.S. farmer became more competitive and profitable.*

Current Environment. The recovery attempt last month by the real, ended with another weekly key reversal lower even on the realization that S. America's crop was sub-par (D). A cheaper real makes Brazil more competitive pricewise and U.S. soybeans comparatively more expensive. However, by Sept. 1, South America will not have excess stocks, making the U.S. the major supplier. The main thrust of a cheaper Brazilian currency will be to incentivize acreage expansion in Brazil.

What to Do? A basic understanding of currency relationships and how they can affect supply and demand globally is not necessarily something you learn at the coffee shop. However, it is a subject of conversation in South America and other countries with whom we compete. Hopefully, this column helps explain the complexities of our situation. We in the U.S. have benefited from a weak currency for some time, but we have forgotten all too soon how Brazil expanded production early in its ag exporting career. If the currency relationship between the U.S. and other exporting nations continues to disfavor American farmers, our ag economy could very well suffer accordingly. ■

Jerry Gulke farms in Illinois and North Dakota and is president of Gulke Group Inc., a market advisory firm with offices at the Chicago Board of Trade. Gulke Group recently published *Technical Analysis: Fundamentally Easy.* For information, send an e-mail to *info@gulkegroup.com* or call (815) 520-4227.