Agricultural Economy


USDA

U.S. Agricultural Outlook for 1998

The U.S. agricultural economy is edging down from the record-high income levels of 1996. In 1998, the overall economic performance is expected to be slightly below the average of 1990-97. Areas of concern continue to be producers in regions affected by bad weather, and some wheat, cattle, hog, and dairy producers who have had to reduce cash balances or incur debt to withstand short-term financial pressures. Farm cash receipts set a record of $202 billion in 1996 and were similar to that level in 1997, with crop receipts rising well above the average of the 1990's and livestock receipts at about the average.

This year, market receipts are likely to decline to $198 billion, as lower grain receipts reduce the total return to crops. Livestock receipts will decline a little as lower hog revenues more than offset a small increase in cattle returns, while dairy remains about unchanged. With overall production expenses declining slightly, held in check by lower interest rates and feed costs, net cash farm income is forecast to decline to about $52 billion, more than $2 billion below the 1990-97 average.

The farm sector balance sheet improved in 1997 as asset values rose more than debt increased. Farm real estate values have risen every year since the mid-1980's, including a 6-percent increase in 1997. A 5-percent gain is expected in 1998. Farmers will take on more debt, reaching the highest debt level since 1985, but the overall debt-to-asset ratio is expected to decline from 15 percent at the end of 1997 to slightly under 15 percent at the end of 1998 as farm real estate values rise.

Taxpayers will see stability in farm program costs with direct government payments, forecast at $7.4 billion for 1998, down from $7.9 billion in 1997 and accounting for only 3.7 percent of gross farm income. The big drop in farm payments will come for the 2001 crop year when production flexibility contract payments drop nearly 20 percent from $5.05 billion (in 2000) to $4.07 billion.

Consumers will see a year of modest food price inflation in 1998, with the Consumer Price Index (CPI) for food rising 2-3 percent. In 1997, the CPI for food rose 2.6 percent, compared with a 3.3-percent increase in 1996 when record-high grain and milk prices pushed up retail food prices. In 1998, areas to watch include meats, where retail pork prices are expected to decline by 4-6 percent; ample supplies of beef, poultry, and fruit will also restrain food price increases. The effects of wet weather on spring vegetable harvests in California could also affect vegetable prices (see "Briefs").

Strong Macroeconomy Supports Food Demand

Despite the considerable uncertainty raised by the Asian financial situation (AO February 1998), the U.S. economy looks like it will support strong food demand in 1998. At this point, world economic growth looks like it will slow from 3.1 percent in 1997 to something closer to 2.5 percent. While less favorable for exports, such growth would still be stronger than during the first half of the 1990's, when it averaged 1.9 percent.

In the U.S., after 3.8-percent growth in 1997, this year's real gross domestic product is expected to grow about 2.7 percent. This forecast includes the effects of the Asian turmoil, which trims 0.3 to 0.4 percentage points off U.S. economic growth. A slowdown in corporate profits and business investment in inventories, a tight labor market, and reduced net exports are expected to slow growth. After the U.S. economic surge in 1997 and the Federal Reserve's concern about potential inflationary effects of the tight labor market, it now appears the Asian situation will restrain growth sufficiently without Federal Reserve intervention.

Although the stronger dollar will add to the U.S. trade deficit and limit U.S. economic growth, many other positives will maintain its momentum. Lower long-term interest rates will support investment and construction. Consumer confidence remains near record highs, and inflation is likely to be little changed, held down by

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the rising value of the dollar and oil prices that recently hit a 14-year low.

While all of these macro statistics infer a firm base of domestic demand for food, they also bode well for farmers' cash-flow accounts. With energy prices and interest rates down and feed expenses likely down, farm production expenses are forecast to decline for the first time since 1992, when recession was ending, interest rates were falling, and acreage controls were limiting plantings.

Crop Market Developments

A year ago, USDA forecast that large U.S. and world crops of grains, soybeans, and cotton would lead to a softening in crop prices and a rebuilding of stocks. Those forecasts proved fairly accurate as weather was generally conducive to crop plantings and crop development. In addition to large crops, the Asian currency crisis has further contributed to the bearish price outlook for major crops.

Compared with a year ago, the price farmers received for all crops during January 1998 was down 4 percent. However, the price drops have generally been larger for the major crops. The price of corn was down 4 percent, but soybeans and upland cotton were down 8 percent and wheat was down a whopping 17 percent in January.

U.S. and world crop production were generally exceptional in 1997/98. U.S. wheat production (2.5 billion bushels) was the highest since 1990, as wheat yields were record high. U.S. corn production was the third highest on record, reaching nearly 9.4 billion bushels. U.S. soybean production exceeded the record set in 1994/95 by 210 million bushels, as planted acreage topped 70 million acres for the first time since 1982. And cotton production of nearly 19 million bales was only slightly below the record set in 1994/95. Globally, wheat production and oilseed production set records in 1997/98.

Large U.S. and world production of grains, soybeans, and cotton have lowered U.S. crop prices and raised carryover for 1997/98. The U.S. season-average farm price of wheat is expected to be down about 20 percent, and wheat stocks on June 1 are forecast to be up by over 50 percent compared with 1 year ago. Soybean stocks are forecast to nearly double this season, while soybean prices are expected to be down about 12 percent. Corn prices are forecast to fall by 6 percent in 1997/98 as carryover stocks increase by 7 percent.

Lackluster growth in U.S. exports due to large world crops and the Asian crisis is also contributing to the dropoff in U.S. grain and cotton prices. Both wheat and corn exports are expected to be well below the average of the 1990's. U.S. soybean exports, however, are expected to be record high in 1997/98 as world demand for oilseeds continues to expand.

Despite the decline in corn exports, total corn use in 1997/98 is forecast to be the second largest on record, as domestic use is expected to expand by nearly 9 percent. For corn, growth in domestic use has continued to expand faster than growth in exports. From 1990/91 to 1996/97, domestic use of corn increased by 17 percent while corn exports were up 4 percent. Continued expansion of livestock and poultry production and lower corn prices are forecast to increase feed and residual use by 9 percent and food, seed, and industrial use by 8 percent in 1997/98.

Even though stocks of major crops are expected to increase in 1997/98, stocks will continue to remain at modest levels for most crops, with the possible exception of wheat. The stocks-to-use ratio at the end of the 1997/98 season is forecast to be near 10 percent for corn and soybeans and about 23 percent for cotton. In contrast, the stocks-to-use ratio for wheat—at over 28 percent—would be the highest since 1990/91.

Large U.S. Soybean & Corn Crops Forecast This Year

In 1998/99, changes in relative returns and a 2- to 2.5-million-acre decrease in CRP enrolled acreage is expected to result in a small expansion in corn and soybean

Economic Indicators Point to a Generally Healthy U.S. Farm Sector

	Average 1990-95	1996	1997	1998
		$ billion		
Farm receipts[1]	185	213	213	209
Agricultural exports[2]	44	60	57	56
CCC outlays[2]	10	5	7	9
Government payments	9	7	8	7
Balance-sheet aggregates				
Assets	899	1,035	1,083	1,132
Liabilities	143	156	162	168
Equity	756	879	921	964
		$/acre		
Farm real estate value	742	890	945	1000
Returns[3]				
Corn	174	202	200	195
Wheat	90	112	85	79
Soybeans	138	196	172	125
Cotton	212	304	247	253
		$/cow		
Cow/calf	69	-44	0	13
		$/cwt		
Hogs	6.7	6.0	5.1	-3.6
Chickens	5.3	5.4	5.8	3.5
		$/cwt of milk		
Dairy	2.4	1.9	2.1	2.5

1998 forecast. Dairy data are on a marketing-year basis; all other data are on a calendar-year basis unless otherwise indicated.
1. Includes farm-related income. 2. Fiscal year. 3. For **crops:** returns over variable costs for program participants and soybean producers for crop years; for **cow/calf, hogs (farrow-to-finish), and dairy:** returns over cash costs; for **chickens:** returns over total costs.

Source: Economic Research Service, USDA; Office of the Chief Economist, USDA.

plantings, while acreage planted to cotton and wheat are expected to decline. Total plantings of major crops will likely be down slightly despite the decline in CRP enrollment, as lower crop prices and returns cause some producers to reduce planted area.

Assuming trend yields, U.S. soybean production is projected to exceed this past year's record, reaching nearly 2.8 billion bushels in 1998/99. Corn production is forecast at nearly 9.8 billion bushels, which would be 5 percent above last year and the second highest on record. But, lower acreage and a decline in yields from last year's record are expected to cause wheat production to fall by 9 percent to 2.3 billion bushels, and reduced planting could lead to a 7-percent decline in cotton production in 1998/99.

Declining foreign production and improved macroeconomic conditions in Asia into next year should enhance export prospects for corn in 1998/99, while large foreign supplies of wheat and soybeans are expected to continue into 1998/99, causing U.S. exports for these crops to remain essentially flat. U.S. corn exports are projected to rebound, reflecting reduced competition, especially from China. China is projected to swing from being a net exporter of corn to a net importer, and Eastern Europe and Argentina are expected to export less.

Prices of corn and wheat are expected to remain firm in 1998/99. For wheat, a small increase in total U.S. supplies is expected to be offset by higher exports and domestic use. The corn market would also appear nearly in balance, with domestic use and exports expanding as production increases. The exception is soybeans, where another record crop and large foreign production in 1998/99 are projected to lead to another decline in soybean prices.

Plantings of rice are expected to rise, reflecting firm 1997/98 market prospects boosted by exports of rough rice to Latin America and continued expansion of domestic demand. Global trade will be strong in 1998, particularly markets in Southeast Asia, including Indonesia and the Philippines where drought has reduced rice production.

Weather—A Key Uncertainty

When will El Niño cease to influence weather and what will the next weather pattern mean for crop plantings and crop development this spring and summer? At this point, all major crop growing areas except the Upper Midwest and Northern Plains have more than ample soil moisture. In fact, if there is a concern, it is whether soils in the Southeast and Southwest will be dry enough at normal planting dates. These areas typically begin planting corn in March, cotton in April, and soybeans in May. The longer that excess moisture delays planting in the South, the more likely producers will shift from corn to cotton and ultimately to soybeans.

Excessive moisture could pose a similar problem for eastern Corn Belt producers, although the current National Weather Service forecast calls for a drier April and May. Delays in planting could leave producers with the choice of planting earlier maturing varieties—with the prospect of lower yield—or switching to soybeans. Further switching of acreage to soybeans combined with the prospect of a record South American crop would soften soybean prices but boost corn prices in 1998/99.

A wet spring followed by a dry summer would support prices for both soybeans and corn, and there are insufficient stocks to prevent major price runups if a severe drought occurs. If current good conditions for winter wheat continue, however, and other crop yields are above trend, the current, somewhat bearish, price expectations could decline further.

The 1998 meat surplus, marginal milk expansion, and relatively low feedgrain stocks make for an uncertain livestock industry. Bad weather this year could cause very high feed prices. That would recommence the cattle herd liquidation and spin dairy returns well into the red. Because hog prices are now 35 percent lower than in 1996 (when cash corn hit $5 per bushel), a runup in corn prices in 1998 due to weather would have a much different effect on hogs than the effect in 1995 and 1996. The hog industry would be severely affected and, with continuing shrinkage in cattle numbers, the meat and milk sectors would face serious dislocations, with consumers facing dramatic retail meat price increases in 1999 and beyond.

Livestock, Poultry, & Dairy Market Developments

The most striking developments in U.S. agricultural markets have been occurring on the animal product side, notably the loss of export growth and the production effects of the cattle and hog cycles. With animal products accounting for 45 percent of gross farm receipts, the economic performance of this sector undergirds the well-being of much of agriculture.

During the first half of the year, record-high per capita meat and poultry supplies will drive down returns for livestock and poultry producers. Consumers will be in hog heaven as they find one bargain after another in the meat case of their supermarket. Per capita meat consumption on a retail-weight basis is expected to surge to an all-time high of 216 pounds in 1998. It was just 202 pounds in 1990 and averaged 208-210 pounds during the mid-1990's.

Obviously, such a high level of consumption can only be accommodated by sharply lower meat and poultry prices. The expected 4.5-percent increase in meat and poultry supplies that will move through domestic channels is being caused by the first decline in U.S. meat and poultry exports in the 1990's, an increase in beef imports (caused by the rising value of the dollar, weak Asian demand, and low cow slaughter), large increases in pork and poultry production, and more beef production than earlier expected.

For 1998, the beef market will see more supplies in the near term but less later on. A key development of 1997 was the continuing liquidation of cattle, a contraction that began in 1995. The pace of cow slaughter began to slow in late 1997 and early 1998, but ranchers will not begin to retain sufficient heifers to rebuild herds, and eventually turn the cycle up, until later this year. Three factors jump out as discouraging expansion—larger-than-expected supplies of competing meats, weak prices for feeder cattle, and short hay supplies, with hay prices setting a record high for the month of January.

A slowdown in fed-cattle marketings and record slaughter weights have kept beef supplies up, resulting in lower fed-cattle prices than expected. Producers placed large numbers of heifers on feed rather than retaining them for the breeding herds last summer.

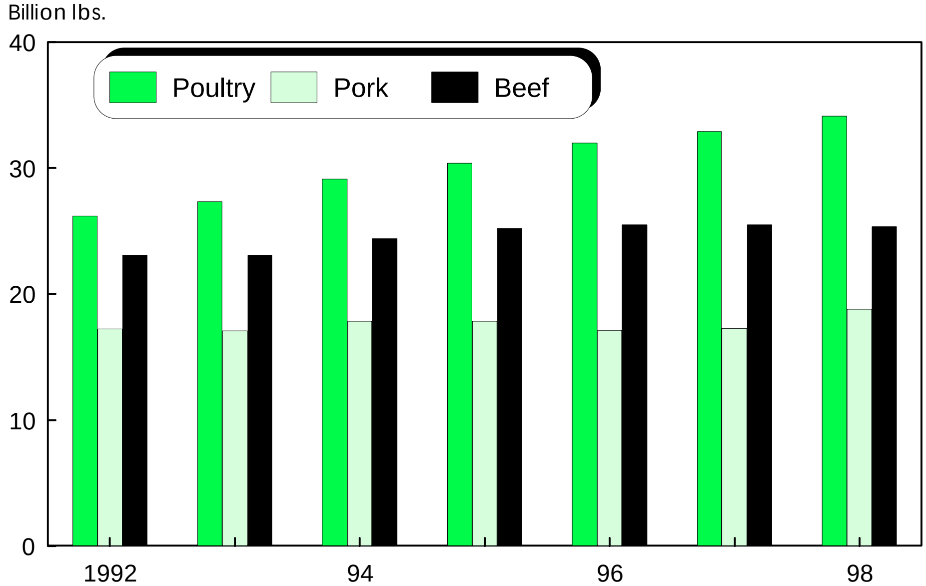
Beef production is now expected to be up slightly in first-half 1998, compared with a year earlier. This is keeping fed cattle prices in the low $60's per cwt. With break-even prices in the high $60's, feed-lots are taking a loss of $5-10 per cwt on cattle now coming out of feedlots, which depresses the price they pay for feeder cattle. This will not continue. With fewer cattle on farms, fewer feeder calves will be available to feedlots, and fewer steers will be fed and slaughtered. The question is when.

This is expected to begin later this spring, with retail supplies beginning to decline in the fourth quarter, and could go on through the year 2000. In 1996, beef production was up 1.2 percent. In 1997, beef production was unchanged, and in 1998, USDA forecasts a decline of less than 1 percent, although the drop in production will grow as the year unfolds and could be down 3 percent by the fourth quarter. The conclusion then is fed-cattle prices will rise and feedlots will have to pay more for feeder cattle.

By late 1998, fed cattle could be over $70 per cwt, 20 percent above recent levels, and feeder cattle could be in the low $80's, compared with the mid-$70's recently. This will mean better news for cow-calf producers. By 1999, returns to cow-calf producers should be strongly positive, and that would provide an incentive to rebuild herds, though this outcome hinges on good crops this year.

Pork supplies will be especially heavy in 1998 as a 10-percent increase in production is expected to combine with export losses and pull down 1998 hog prices a whopping 25 percent below the 1997

U.S. Poultry and Pork Production To Rise in 1998



1998 forecast.
Economic Research Service, USDA

average. One key development has been the pattern of expansion. Many States are continuing to pursue "moratoriums" on hog expansion and restraints on production (AO March 1998). Consequently, observers are trying to discern whether environmental, structural, or other issues will restrain future hog expansion. Some traditional producing States such as Iowa and Minnesota are expanding faster than the U.S. average, as are Oklahoma, Texas, Utah, and Colorado. North Carolina is below the U.S. average.

Broiler returns were reasonably good during 1997 and have remained above cash expenses even during the period of weak wholesale broiler prices experienced this quarter. Export growth will be slower in 1998 but still positive as Russia, Hong Kong, China, and Japan continue as major buyers. For 1998, USDA forecasts that production will rise 4 percent, and with abundant meat supplies, broiler prices are expected to average only 56 cents per pound, compared with 59 cents during 1997.

Last, the dairy market has been recovering since the very low prices during the first half of 1997. Strong cheese and butter prices pulled the basic formula price (BFP) for January 1998 to the second highest ever for that month. Nevertheless, the milk-feed price ratio is not strong enough to signal milk production expansion, and low dairy-quality hay supplies remain a concern. Consequently, milk production is expected to be about unchanged in 1998 compared with 1997. A good economy and expanding demand will keep milk prices firm, with the all-milk price expected to average slightly above the 1997 level.

One uncertainty is the outcome of the Federal Milk Marketing Order hearing to establish a floor on milk used for Class I and Class II products. Because milk prices are seasonal and likely to go lower over the next several months, a floor, if established, would raise producers' returns above current projections. For example, a $13.50-per-cwt floor on the BFP could raise the farm-level milk price during the second half of 1998 by 25-35 cents per cwt above what it would otherwise be. However, because the floor is expected to be temporary, production would likely be affected little.

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