Global Trade & International Issues Shape Long-term Outlook for U.S. Agriculture

Developments in the international arena result in relatively weak U.S. agricultural prices in the initial years of USDA's 10-year baseline projections. But the longer term picture includes sustained global economic growth and stronger agricultural trade and income prospects for U.S. farmers.

Sizable harvests in the U.S. and abroad over the past several years, partly in response to high prices in the mid-1990's, have pushed up global supplies for many agricultural commodities. Additionally, world agricultural demand in the late 1990's was weakened by the global financial crisis.

Consequently, the U.S. agricultural sector has faced strong foreign competition in a weakened global trade setting. U.S. agricultural export value has fallen from a record of almost $60 billion in fiscal 1996 to about $49 billion estimated for fiscal years 1999 and 2000. While export volume in 1999 and in 2000 is up from 1998, low commodity prices have held down total value.

U.S. net farm income is off as well—from nearly $55 billion in 1996 to $40.4 billion expected in 2000—although declines have been buffered by increases in government payments—marketing loan benefits increased as prices of major field crops dropped, and emergency legislation generated additional farm payments. Farm income is expected to decline through 2001, largely reflecting a reduction in direct government payments from recent high levels. The baseline assumes no additional payments from emergency legislation, although marketing loan benefits continue to play an important role in the U.S. farm sector in the near term as large global supplies keep farm prices under pressure. With reduced farm income over the next few years, debt management will be crucial to the financial condition of the sector. Despite near-term cash flow difficulties, a strong financial position achieved during the 1990's will help farmers during this period.

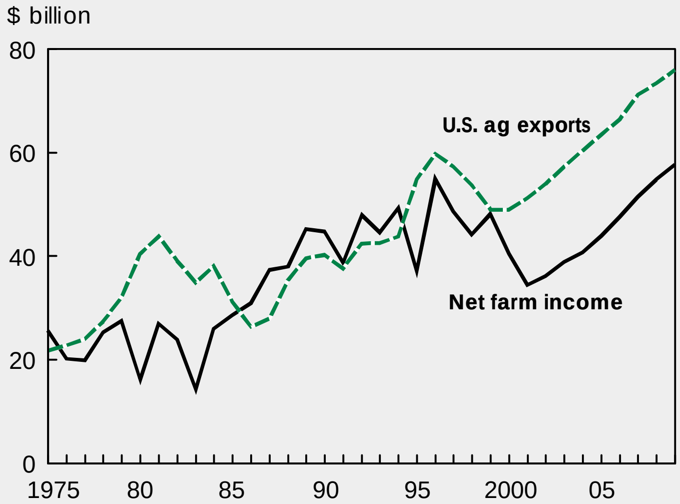
Economic recovery is now underway in most crisis-affected countries, and global demand and trade are strengthening. Export volumes and commodity prices are projected to turn upward in 2001, leading to gains in U.S. agricultural export values.

Longer run developments in the agricultural sector reflect continuing macroeconomic improvement, with the global economy moving back to a period of sustained growth, due in part to structural reform in countries most affected by the global financial crisis of the late 1990's. Economic improvements, particularly in developing countries, provide a foundation for further gains in global demand, agricultural trade, and U.S. agricultural exports. Incomes in many developing countries are at levels where consumers diversify their diets and include more meats and other higher valued food products, and where consumption and imports of food and feed are particularly responsive to income changes.

Overall, improving agricultural demand prospects are driven by the outlook for healthy economic growth in most of Asia, Latin America, North Africa, and the Middle East; moderate gains in developed countries; and continued progress toward freer trade through ongoing unilateral policy reforms and existing multilateral agreements. Solid prospects for trade expansion in these regions are expected to more than offset relatively weak growth in parts of Asia, Africa, and the former Soviet Union (FSU).

Expanding production potential in a number of foreign countries, however, will result in continued strong export competition throughout the baseline period. For example, by the middle of the projection period, U.S. wheat exports face greater competition when the European Union (EU) is able to export wheat without subsidies. Argentina and China are expected to remain strong competitors in coarse grains trade. And U.S. exports of soybeans and products face continuing competition from Argentina and Brazil.

U.S. Net Farm Income and Agricultural Exports To Rebound



Calendar year for income; fiscal year ending September for exports. 2000-09 projected.

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Despite continued competition, improved trade growth leads to rising market prices and export earnings during the last half of the baseline. The total value of U.S. agricultural exports is projected to increase to almost $76 billion by 2009, with both bulk and high-value product exports projected higher. As agricultural trade and U.S. exports expand, large global supplies are reduced and agricultural prices rise, leading to gains in farm income. Further, with commodity prices rising, direct government payments fall and then level off, and the agriculture sector increasingly relies on the marketplace for its income.

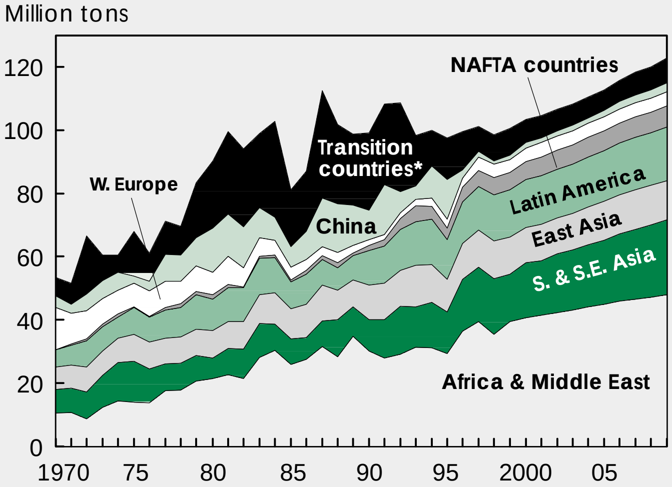
Increasing farm incomes and relatively low interest rates assist in asset accumulation and debt management, resulting in relative stability in aggregate financial conditions in the farm sector. Debt-to-asset ratios, for example, continue the downward trend of the last 15 years from the high levels of over 20 percent in the mid-1980's.

Consumer food prices are projected to continue a long-term trend of rising less than the general inflation rate. Consumers are

USDA's complete 2000 baseline projections are available at: **www.ers.usda.gov/briefing/baseline/**. The projections were prepared in October-December 1999 and are published in *USDA Agricultural Baseline Projections to 2009*, released February 2000. Projections assume no shocks and are based on specific assumptions regarding macroeconomic conditions, policy, weather, and global developments.

Agricultural Economy

Projected Global Wheat Imports Bolstered by Gains In Africa and Middle East, and in South and S.E. Asia



2000-09 projected.
*Former Soviet Union and Eastern Europe.
Economic Research Service, USDA

projected to spend an increasing share of their food dollar on meals eaten away from home.

International Issues & Uncertainties

Shaping these projections are a number of international developments, while several uncertainties could lead to alternative outcomes.

Macroeconomic conditions in developing countries. The projected strengthening of bulk commodity markets in the baseline is linked closely to macroeconomic conditions in developing countries, particularly the expectation of robust economic growth and a return to historical trends in exchange-rate movements. Baseline assumptions are consistent with many independent forecasts, but recent shocks to income growth and exchange rates associated with the Asia crisis underscore the uncertainties in projecting both economic activity and agricultural trade in developing regions.

The baseline trade outlook for bulk commodities and meats is highly dependent upon assumed income growth and local exchange rates in the developing Asia region. This stems from the region's large share of world trade volume in these commodities, relative openness to trade, and responsiveness of food demand to changes in income and prices. Global impacts of slower growth or reduced local currency valuations in the Latin American or the transition economies (the FSU and Eastern Europe) would also be significant, but smaller than for developing Asia, largely because these regions generally account for smaller shares of global demand and trade. Alternative macroeconomic assumptions for the Africa and Middle East region tend to result in smaller global impacts than for other regions. Although this region accounts for large shares of world wheat and coarse grain trade, the region's markets and consumers tend to be relatively less responsive to income and price changes.

Change in sources of global import demand. During the 1980's and early 1990's, global trade in wheat and coarse grains was unstable with no overall growth, largely because of erratic market behavior of the transition economies of the FSU, as well as China. For both wheat and coarse grains, however, underlying growth in other regions, particularly the developing regions, has been relatively strong and stable. For the 2000-09 period, markets for these commodities appear poised for growth even without significant contributions from China and the FSU.

In contrast to grains, the market for soybeans and meal has shown steadier expansion, particularly since the late 1980's, buoyed by gradual growth in the dominant EU market. For 2000-09, however, declining EU import demand is projected to slow overall trade growth, despite continued expansion in China and other regions.

World meat trade has shown strong growth since the mid-1970's, with fluctuating demand by the transition economies of the FSU accounting for the bulk of instability in trade volume. Expansion in Asian markets is projected to help sustain future growth, but developments in the volatile FSU market will be important to the overall outcome.

China's agricultural supply and demand. Prospects for China's future trade remain a major uncertainty in the outlook. Under baseline assumptions, which exclude China's potential accession to the WTO, China's grain imports are projected to show little growth through 2009. Recently announced changes in China's grain procurement policy imply somewhat lower future grain area, but trade impacts of these policy changes are expected to be more than offset by other factors. These factors include very high grain stocks that are likely to be reduced over the next decade, somewhat slower growth in incomes and food demand, and increased government investment in agricultural research, development, and infrastructure that is likely to have a positive impact on crop yields. China's accession to the WTO would likely significantly boost global and U.S. agricultural trade (*AO* March 2000).

Agenda 2000 reforms in the EU. In March 1999, the EU enacted agricultural policy reforms under Agenda 2000, including reduced intervention prices, increased direct income support, and a lower cropland set-aside. These policy changes further shift the EU from price supports to direct payments in order to increase the global competitiveness of EU agriculture. However, the baseline analysis indicates that the EU will continue to need subsidies to export most agricultural products, making those exports subject to Uruguay Round (UR) limits.

The extent to which Agenda 2000 reforms will make EU wheat more competitive in world markets is a key uncertainty in the outlook. In the baseline, the lower intervention price makes EU wheat competitive in world markets without subsidy by 2004/05, allowing exports to rise above subsidized export limits set in the Uruguay Round. How much EU wheat exports rise will then depend in part on the responsiveness of EU farmers in switching from high-yielding feed wheat to lower yielding food-quality wheat for export markets. Despite lower intervention prices, EU coarse grains are not expected to become price-competitive in world markets, and exports remain constrained by UR limits on subsidized exports.

Changes in EU oilseed payments under Agenda 2000 are not expected to have significant impacts on oilseed production. However, lower intervention and market prices for grain feeds are projected to dampen long-term demand and imports of protein feeds, including soybeans. AO

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