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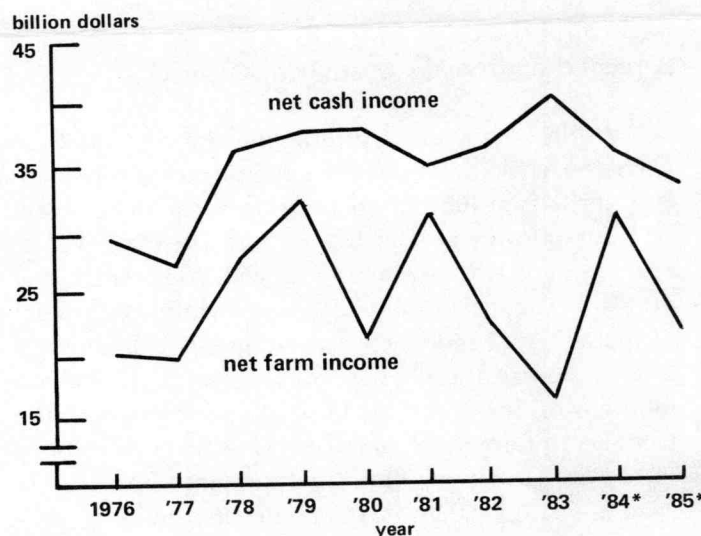
LETTER

THE AGRICULTURAL OUTLOOK for the coming year, recently summarized at the USDA's 61st Annual Outlook Conference, points to continued difficulties for the sector. World crop production is expected to reach record levels during the 1984/85 fiscal year, while the growth in world demand is expected to be moderate. Much of the global increase in output is attributable to large U.S. crops. The resulting lower prices will likely lead to a slight rise in the volume of U.S. agricultural exports and improve livestock feeding margins. But overall, U.S. farm income is expected to decline in 1985 as production cost increases outstrip gains in receipts. Moreover, the continued financial stress implied by falling sector income is expected to contribute to additional declines in asset values and further erosion of farm equity in the coming year.

Gross cash income in 1985 is forecast to be virtually unchanged from this year's level. Cash receipts for both crop and livestock farmers are expected to rise slightly, while government payments are expected to decline as PIK disbursements come to an end. Cash receipts of crop farmers, including net CCC loans, are expected to register a year-to-year gain of 1 to 5 percent. Much of the expected gain is accounted for by food grains, as increased marketings will likely offset weaker prices. Soybean receipts, however, are expected to fall as sharply lower prices will offset the projected increase in marketings. In the livestock sector, lower meat supplies next year are expected to result in higher prices and a slight increase in meat animal receipts. This gain, however, will be tempered by lower egg and dairy receipts, holding total livestock receipts less than 4 percent above the 1984 level.

Farm production expenses are expected to continue to climb in 1985. Following a 6 percent increase this year, cash expenses are forecast to rise from 1 to 5 percent in 1985, while total production expenses may record an increase of up to 4 percent from this year's level. Among farm origin inputs, feed expenditures in

Net income of the farm sector



*Mid-point of forecast range.

1985 are expected to hold near this year's level as increased consumption offsets lower prices. Purchased livestock expenses are forecast to be up 5 to 9 percent next year, with most of the rise attributable to higher feeder livestock prices. Expenditures for manufactured inputs such as fuel, fertilizer and chemicals are forecast to rise moderately next year as are interest charges on farm debt. With gross cash income forecast to remain unchanged and cash expenses expected to rise, net cash income in 1985 will likely range from \$31 billion to \$36 billion, down from the \$34 billion to \$38 billion forecast for this year.

Exports of U.S. agricultural products, on a tonnage basis, are forecast to rise for the first time in five years during fiscal 1985, despite the strong competition implied by large world crops. The rise coincides with an expected 4 to 6 percent increase in the volume of world agricultural trade. U.S. export shipments are projected to reach 149.5 million metric tons during the fiscal year that began October 1, up 4 percent from the previous year's level but still well below the fiscal 1980 peak.

Much of the anticipated increase in export volume is attributable to higher grain and soybean exports offsetting lower cotton and meat product exports. Continuing economic recovery in many regions of the world, a high level of meat animal production, and lower prices are stimulating feed use and the demand for U.S. agricultural products. However, debt constraints in many developing countries and the persistently high value of the dollar relative to other currencies will continue to temper export gains in 1985. Moreover, lower prices will limit the value of U.S. agricultural exports to about \$36.5 billion, down 4 percent from fiscal 1984. The decline in export values combined with rising imports, particularly fresh fruits and citrus juices, will hold the agricultural trade surplus to about \$17.5 billion in fiscal 1985, an 8 percent drop from the previous year's level.

World coarse grain production during 1984/85 is expected to total a record 789.3 million metric tons, with almost all of the 100 million metric ton year-to-year gain accounted for by greater U.S. output. The major use of coarse grains is for animal feed, with food, seed, and industrial uses accounting for the remaining 40 percent of global use. Feed use of coarse grains worldwide is forecast to rise about 2 percent this year to 453 million metric tons. Increased feed use of coarse grains in the U.S. accounts for much of the increase, while declines in the Soviet Union will limit total foreign use to a slight year-to-year gain. Global trade in coarse grains is likely to rise substantially from the depressed levels of the last several years, reaching almost 100 million metric tons in fiscal 1985. The increased trade is being stimulated by lower prices and a high level of livestock production across much of the world.

U.S. corn production this year is estimated at 7.5 billion bushels, up sharply from last year's drought- and PIK-reduced crop, but short of the record 8.2 billion bushels harvested in 1982. This year's larger crop will contribute to greater corn utilization and replenish stocks. Feed use of corn is expected to rebound significantly to 4 billion bushels during the 1984/85 marketing year that began in October as corn regains a relative price advantage over wheat. Food, seed, and industrial uses of corn are expected to climb on the strength of greater high fructose corn syrup and ethanol production. Corn exports this marketing year are forecast to total more than 2 billion bushels, a gain of almost 12 percent from last year and the highest level since 1980. Although total corn utilization will likely jump 8.5 percent this year, the large crop will facilitate a rebuilding of stocks to more than 1.1 billion bushels, more than a 55 percent increase from the ending stocks of the last mar-

keting year. With the rebuilding of carryover stocks, average corn prices for the October-to-September marketing year are expected to range from \$2.60 to \$2.85 per bushel, down from \$3.20 in the 1983/84 marketing year.

Soybean production this year has been pegged at 1.9 billion bushels, up 16 percent from a year ago. However, small carryover stocks at the beginning of the current marketing year held the rise in total soybean supplies to less than 5 percent. Increases in crushings and exports of about 2 and 5 percent, respectively, are projected for soybean utilization this marketing year. Although still tentative, USDA forecasts of Southern Hemisphere soybean production point to another large crop this year that will pressure U.S. exports. Soybean prices for U.S. producers are currently expected to average between \$6.00 and \$7.00 during the 1984/85 marketing year, well below the \$7.75 average of last year.

Domestic wheat supplies for the 1984/85 marketing year that began on June 1 totaled nearly 4 billion bushels, up almost 1 percent from the previous year's high level. The large supply is attributable to continued high carryover stocks and to relatively low farmer participation in the acreage reduction program and above average yields that pushed production to 2.57 billion bushels, the third largest harvest on record. Wheat exports in the 1984/85 marketing year are expected to rise almost 7 percent as the Soviet Union substantially increases imports. Domestic utilization of wheat is expected to be down 4 percent because of a sharp decline in feed use. Wheat prices this year are forecast in the \$3.35 to \$3.55 per bushel range. Carryover stocks next June are expected to remain near the previous year's high level of 1.4 billion bushels. With an expected large 1985 crop, wheat supplies for the 1985/86 marketing year are forecast to remain near the current high level.

U.S. meat production, expected to total more than 54.9 billion pounds this year, is forecast to drop marginally to 54.7 billion pounds in 1985. Beef production next year is projected to decline about 4 percent, with much of the year-to-year decline occurring in the first half of 1985. Pork production in 1985 will remain virtually unchanged, with a year-to-year decline in the first half of the year offsetting an increase in the second half. The slight drop in red meat supplies next year will be largely offset by a 5 percent increase in poultry meat production.

The inventory of all cattle and calves on January 1, 1985 will likely show a 2 to 3 percent drop from a year ago. A high level of cow slaughter in 1984 and a drop in

the number of beef replacement heifers suggest that the downtrend in cattle inventories will continue in 1985. Feeder cattle supplies, already low because of a smaller calf crop and rising feedlot placements, may tighten further as lower feed prices and better prices for fed cattle encourage more placements of feeder cattle in 1985. Nonfed steer and heifer slaughter is expected to decline in 1985 with fed cattle marketings accounting for a larger proportion of total slaughter. Choice steer prices in Omaha are projected to average in the high \$60 per hundredweight range next year, slightly above the mid-\$60 estimate for this year.

Commercial hog slaughter during the first quarter of 1985 is expected to be down 3 to 5 percent from year-ago levels, consistent with the September 1 inventory of hogs weighing less than 60 pounds. Second quarter slaughter, which comes largely from the September-November pig crop may be down 2 percent if producers carry out their September 1 farrowing intentions for the period. Commercial pork production in the first half of 1985 is not expected to fall as much as slaughter, as lower feed costs encourage producers to feed hogs to heavier weights. Second half hog slaughter is expected to be 1 to 3 percent larger than a year ago. Hog prices next year are forecast to trend higher during the first three quarters and average in the \$48 to \$54 per hundredweight range for the year compared to an average price of around \$48 this year.

Milk production in 1985, following a 4 percent drop this year, is projected to rise 1 percent, totaling 137.3 billion pounds. The rise in output is expected to commence in the second quarter following the expiration of the paid diversion program. A large inventory of dairy heifers this summer suggests that the number of milk cows on farms will increase next spring. Moreover, lower feed costs could increase feeding rates and result in greater output per cow. Although greater commercial disappearance of milk will temper the production increase, CCC net removals will likely remain large, eliciting further cuts in the milk support price during 1985.

Retail food prices in 1984 rose about 4 percent. Ample supplies of most foods and moderate increases in marketing costs, which reflect the relatively low level of inflation in the economy, limited food price gains in 1984. For the year ahead, retail food prices are expected to average some 2 to 5 percent above the 1984 level.

Most of the expected increase is attributable to rising food marketing costs, forecast to be up 3 to 5 percent from 1984 levels. Meat prices are expected to rise moderately during 1985 with the largest year-to-year rise in prices expected late in the year. Poultry prices, however, are expected to average 2 to 5 percent lower next year. Egg prices will likely hold at current levels next year, well below the high average of 1984 brought about by tight supplies due to avian flu. Similarly, dairy product prices in 1985 are forecast to show little appreciable gain from this year's level. With disposable personal income expected to rise faster than food prices, the proportion of income spent on food in 1985 will likely fall to 14.6 percent.

The financial outlook for farmers in 1985 points to continuation of the depressed conditions that have plagued agriculture through most of the 1980s. A downtrend in farm income is expected to result in continued financial stress for many farmers, particularly those highly leveraged with debt. Farmers with debt-to-asset ratios greater than 40 percent are most susceptible to financial stress. At the beginning of 1984 that group consisted of about 18 percent of all farm operators but accounted for 56 percent of all farm debt.

The farm sector balance sheet is forecast to show further deterioration at the beginning of 1985. Farm real estate values are expected to show a drop of 2 to 4 percent from the beginning 1984 level. Because real estate accounts for about three-fourths of farm assets, a moderate rise projected for nonreal estate assets will have a negligible effect on the value of total farm assets. The level of both real estate and nonreal estate farm debt outstanding on January 1 of next year is forecast to show little change and may register a second consecutive year-to-year decline. However, the drop in farm asset values is expected to dominate any change in debt levels, boosting the farm sector debt-to-asset ratio to 21 percent or more, the highest level since 1940 when this information was first compiled. Moreover, these trends will likely lead to the fourth consecutive annual decline in farm equity, forecast to drop between 2 and 5 percent from a year ago. Expectations for lower income, rising debt-to-asset levels, and further erosion of equity foreshadow continued financial stress for the agricultural sector in 1985.

Peter J. Heffernan

	Latest period	Value	Percent change from		
			Prior period	Year ago	Two years ago
Receipts from farm marketings (\$ millions)					
Crops*	August	11,102	+ 1.3	- 7	+ 2
Livestock	August	5,225	+ 0.7	- 8	+ 4
Government payments	August	5,722	+ 6.4	+ 2	- 2
	August	155	-60.3	-73	+91
Real estate farm debt outstanding (\$ billions)					
Commercial banks	June 30	10.0	+ 3.8†	+13	+18
Federal Land Banks	October 31	48.2	0	0	+ 2
Life insurance companies	September 30	12.6	0	- 1	- 2
Farmers Home Administration	June 30	10.1	+ 2.2†	+ 5	+10
Nonreal estate farm debt outstanding (\$ billions)					
Commercial banks	June 30	41.3	+ 5.4†	+ 7	+16
Production Credit Associations	October 31	18.4	- 3.0	- 5	-14
Farmers Home Administration	June 30	16.7	+ 8.1†	+ 5	+ 4
Commodity Credit Corporation	June 30	6.53	-25.9†	-59	-34
Farm loans made (\$ millions)					
Production Credit Associations	October	1,934	+23.6	- 2	- 5
Federal Land Banks	October	212	+12.5	+ 1	-23
Life insurance companies	September	30	-83.6	-70	-13
Interest rates on farm loans (percent)					
7th District agricultural banks					
Operating loans	October 1	14.44	+ 0.7†	+ 5	- 7
Real estate loans	October 1	14.00	+ 0.8†	+ 5	-10
Commodity Credit Corporation	December	10.13	-10.0	+ 3	+11
Agricultural exports (\$ millions)					
Corn (mil. bu.)	October	2,861	- 1.9	-10	- 1
Soybeans (mil. bu.)	October	155	+42.9	0	- 7
Wheat (mil. bu.)	October	41	+115.7	-39	-57
	October	141	-41.9	+14	+37
Farm machinery sales^P (units)					
Tractors, over 40 HP	October	6,727	+41.8	-26	- 7
40 to 139 HP	October	4,616	+52.1	-24	-18
140 HP or more	October	2,111	+23.5	-32	+35
Combines	October	2,188	+57.3	+ 4	-27

*Includes net CCC loans.

†Prior period is three months earlier.

^PPreliminary



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