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LETTER

AGRICULTURAL EXPORTS in fiscal 1979 are expected to reach \$32 billion, according to a recently revised USDA forecast. The new estimate is \$1.7 billion higher than the previous projection and 17 percent higher than the record set last year. Most of the projected increase from last year is due to higher prices. But volume of shipments—previously forecast to be unchanged this year—are now expected to increase 4 percent. Feed grains and soybeans account for all the projected increase in volume of shipments.

The improved prospects for a larger volume of shipments is despite the large increase in world grain production from both the Northern Hemisphere last fall and Southern Hemisphere countries this winter. Increased utilization and rebuilding of stocks has maintained strong world demand for grains. Furthermore, another year of drought that held the Brazilian soybean harvest this spring well below expectations has supplemented world demand for U.S. soybeans.

Nearly all this year's projected increase in export tonnage was achieved during the first six months of fiscal 1979. But in contrast to earlier expectations of smaller shipments this spring and summer, it now appears that the volume of exports from April through September will about match the record pace of a year ago. These prospects have been reinforced by a recent flurry in grain sales. Corn purchases for delivery to the USSR and unknown destinations have dominated the recent buying spree. Some analysts suggest this may reflect Soviet concerns about their fall planted grains and delays in their spring plantings.

The latest figures indicate the USSR has purchased 10.5 million metric tons of U.S. grains so far for delivery in fiscal 1979—including 2.6 million tons of wheat and 7.8 million tons of corn. Moreover, past experience suggests that a large portion of the 2.9 million metric tons of outstanding corn sales for delivery to unknown destinations may also be delivered to the USSR. These factors would seem to support the USDA's expectation that corn ex-

Agricultural exports to most areas of the world will be larger in fiscal 1979

	Fiscal year ending September 30		
	1977	1978	1979*
	(billion dollars)		
Western Europe	8.6	8.7	9.9
European Community	6.9	6.7	7.4
Other Western Europe	1.8	2.0	2.5
Eastern Europe	1.0	1.1	1.4
USSR	1.1	1.9	2.0
Asia	8.1	9.5	11.9
West Asia	1.1	1.3	1.5
South Asia	.7	.7	.8
Southeast & East Asia	2.5	2.9	3.8
Japan	3.8	4.2	4.8
China	—	.4	1.0
Canada	1.6	1.6	1.8
North Africa	.8	1.0	1.0
Other Africa	.6	.7	.7
Latin America	2.1	2.8	3.2
Oceania	.1	.1	.1
Total	15.9	27.3	32.0

*USDA forecasts.

ports to the USSR in fiscal 1979 may approach last year's level of 11 million metric tons.

Fiscal 1979 represents the third year of the five-year U.S./USSR grain agreement. That agreement calls for annual Soviet purchases of at least 6 to 8 million metric tons of grain, split about evenly between corn and wheat. Again this year, the U.S. government has indicated the Soviets can buy up to 15 million tons without prior consultation.

China is also importing large amounts of U.S. grain this year. Current USDA projections suggest wheat ex-

Feed grains and soybeans account for the projected increase in agricultural export shipments for fiscal 1979

	Fiscal year ending September 30		
	1977	1978	1979*
	(million metric tons)		
Wheat and flour	24.7	32.8	32.0
Feed grains	50.6	55.5	58.5
Rice	2.2	2.1	2.6
Soybeans	15.2	19.7	21.8
Vegetable oils	1.1	1.5	1.4
Oilcake and meal	4.3	5.8	6.0
Cotton, including linters	1.0	1.4	1.4
Tobacco	.3	.3	.3
Fresh fruit	1.3	1.3	1.3
Animal fats	1.4	1.3	1.3
Total	102.2	121.7	126.6

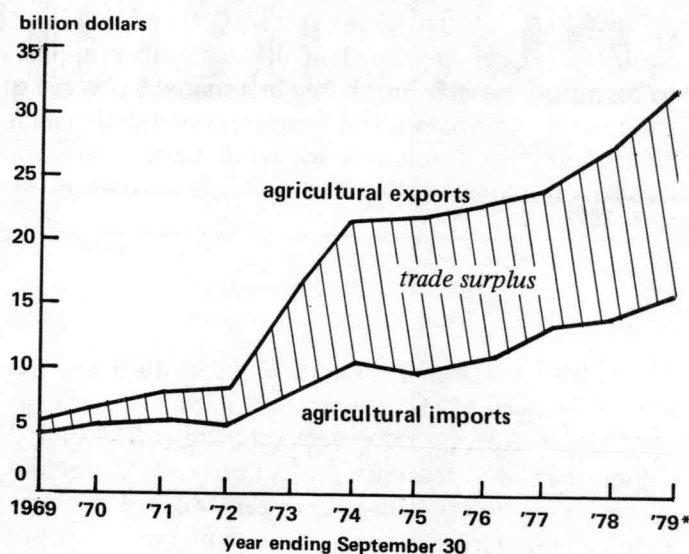
*USDA forecast.

ports to mainland China in fiscal 1979 may reach 3 million tons, against 1 million last year. And corn exports to China may approach 4 million tons. Last year, China imported no corn from the United States.

Soybean exports, which registered a large rise in fiscal 1978, may record an 11 percent jump this year. Shipments to Western Europe, which accounted for nearly three-fifths of U.S. soybean exports last year, are expected to be up a tenth. Soybean shipments to the USSR may be up a fifth to 1 million metric tons, while shipments to Southeast and East Asia may rise two-fifths to around 2 million metric tons. Soybean exports to Japan, which totaled 4 million tons last year, may rise only marginally this year, partly because of the softening in the value of the yen relative to the dollar.

Agricultural imports are also on the rise, paced by sharply higher prices of imported meats and a larger volume of higher-priced sugar imports. Although meat imports may be up only about 13 percent in volume, sharply higher beef prices will boost the value more than

Record U.S. farm exports expected in fiscal 1979



*USDA projection.

two-fifths. Sugar imports are expected to rise nearly a fourth in value. The volume of coffee imports is expected to rise a fifth, but lower prices will offset most of the increase in value.

The 17 percent projected increase in the value of agricultural exports for fiscal 1979 would be the largest year-to-year increase since fiscal 1974. Moreover, it would cap a remarkable decade of growth for agricultural exports. If the \$32 billion estimate is realized, it will mark a sixfold increase in agricultural exports since the year that ended September 30, 1969. Agricultural imports have also risen sharply in the 1970s, but not as fast as exports. Consequently, the agricultural trade surplus has risen from about \$1 billion in the late sixties to \$13.4 billion last year and a projected \$16 billion for fiscal 1979.

Gary L. Benjamin
Agricultural Economist

FOREIGN INVESTMENT IN U.S. FARMLAND continues to be the subject of much interest. Lack of data on the extent of foreign ownership of farm real estate has been reported for some time—as well as the lack of information on the reasons behind foreign investment and the possible consequences. To gain a better understanding of the situation, Congress ordered several government agencies to conduct studies of various aspects of the issue. One such study, authorized by the Revenue Act of 1978, requires the Treasury Department to report

on the tax treatment of nonresident alien real estate transactions in the United States. In a recent report of its findings, the Treasury Department observed that foreigners rarely pay capital gains taxes on the sale of real estate holdings in the United States and recommended modification of some statutes to prevent this tax avoidance.

Although the Treasury study was not limited to farmland, the report noted that data were more current

for foreign investment in agricultural land than for real estate in general. The report acknowledged the findings from studies conducted by other government agencies, showing that foreign ownership of U.S. farmland appears to be quite nominal—probably less than 0.5 percent of this country's farmland. The Treasury concluded that the possibilities for foreigners to avoid paying taxes on capital gains stem largely from U.S. tax statutes, rather than treaties.

Rules governing U.S. taxation of income and capital gains accruing to foreign investors from U.S. real estate holdings are complex. In general terms, foreign entities have two types of taxable income in this country—income from the conduct of a trade or business and income generated by a passive investment. If foreigners actively engage in the conduct of a U.S. trade or business, the income derived from the operation—including capital gains—is taxed in essentially the same manner as income to U.S. entities. That is, gross earnings are adjusted for ordinary and necessary business expenses. On the other hand, if foreign-owned land is considered a passive investment (one in which the foreigner exhibits few characteristics of being materially involved in the management of the business) then, in the absence of a treaty, the gross income is taxed at a flat rate of 30 percent with no allowable deductions. In some cases, a lower rate may apply if there is a tax treaty between the United States and the alien's country of residence. Statutes provide that foreigners can elect to have income from a passive investment in real estate taxed as though it were connected with a U.S. trade or business—an option most foreigners would prefer on ordinary income. The main benefit to foreign investors from passive-type investment tax treatment stems from section 211 of the Revenue Act of 1936, which stipulates that, when the land is sold, no tax is due on capital gains provided the foreigner was in the United States less than 183 days of the year in which the gain was realized.

Although foreigners can elect to have their U.S. real estate income taxed as though it came from a business and, therefore, deduct business expenses from operating income, the choice cannot be revoked later

without special permission from the Internal Revenue Service. An exception to this general rule is provided in about half the tax treaties between the United States and other countries. If a resident of one of these treaty-protected countries makes a passive investment in U.S. real estate and then elects to be taxed as though he were involved in the conduct of a business, he can unilaterally revoke that choice in the year he disposes of the land. If the foreigner is not a resident of one of these countries, he can still qualify simply by incorporating a holding company in one of these particular treaty countries and using it as a conduit for his investment. The Netherlands Antilles and the British Virgin Islands were identified as being the most important conduit countries.

It is important to note that the treaties per se do not permit the tax avoidance. The treaties merely facilitate the change back to a passive investment status. It is this status that can result in tax avoidance because of the special provisions under section 211. While the tax treaties may provide the easiest means for foreigners to change from being treated as a business to a passive investor (in order to escape U.S. taxation of capital gains), they constitute only one way. The Treasury report identified four other ways to effectively avoid capital gains taxation through careful use of existing U.S. tax statutes.

The Treasury report recommends changes in the statutes to eliminate the possibilities for foreigners to avoid taxes on capital gains. Several proposals were presented that would, in effect, treat all capital gains from U.S. real estate investments by foreigners as though they resulted from the conduct of a U.S. trade or business. Even before the Treasury released this report, however, bills were introduced in both houses of Congress that are intended to do essentially the same thing. Taxing capital gains on foreign investments in U.S. real estate would appear to many no doubt to be a more equitable tax treatment than currently exists. The increase in tax revenues, however, would likely be quite nominal.

Don A. Langford
Agricultural Economist

Selected agricultural economic developments

Subject	Unit	Latest period	Value	Percent change from	
				Prior period	Year ago
Farm finance					
Total deposits at agricultural bankst	1972-73=100	May	192	0	+ 7
Time deposits	1972-73=100	May	229	+ 0.8	+ 9
Demand deposits	1972-73=100	May	129	- 2.6	+ 1
Total loans at agricultural bankst	1972-73=100	May	245	+ 1.4	+16
Production credit associations					
Loans outstanding					
United States	mil. dol.	April	15,807	+ 2.8	+16
Seventh District states	mil. dol.	April	3,184	+ 2.5	+20
Loans made					
United States	mil. dol.	April	2,621	- 9.3	+29
Seventh District states	mil. dol.	April	594	-15.5	+31
Federal land banks					
Loans outstanding					
United States	mil. dol.	April	26,294	+ 1.7	+17
Seventh District states	mil. dol.	April	5,821	+ 2.0	+24
New money loaned					
United States	mil. dol.	April	580	-10.8	+54
Seventh District states	mil. dol.	April	144	-40.8	+33
Interest rates					
Feeder cattle loanst†	percent	1st Quarter	10.28	+ 5.2	+16
Farm real estate loanst†	percent	1st Quarter	10.33	+ 4.3	+14
Three-month Treasury bills	percent	5/17-5/23	9.69	+ 5.3	+51
Federal funds rate	percent	5/17-5/23	10.17	+ 0.8	+37
Government bonds (long-term)	percent	5/21-5/25	9.13	- 0.7	+ 8
Agricultural trade					
Agricultural exports	mil. dol.	March	2,877	+22.1	+14
Agricultural imports	mil. dol.	March	1,389	+12.5	0
Farm machinery sales					
Farm tractors	units	March	14,624	+66.0	+ 3
Combines	units	March	840	+19.5	- 9
Balers	units	March	1,066	+116.2	+67

†Member banks in Seventh District having a large proportion of agricultural loans in towns of less than 15,000 population.

††Average of rates reported by District agricultural banks.

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