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Another Tough Year for Agriculture Ahead

Next year is expected to be another difficult one for agriculture--despite easing in cost pressures, 1983 is likely to be the fourth poor income year for many farmers.

Many forces have combined during the early eighties to increase world and U.S. agricultural supplies while depressing demand for food and fiber. With prices for the major crops at the lowest levels since 1978, and income reduced for the third year running, American farmers are under financial strain. Unfortunately, our current assessment of the supply and demand factors for 1983 suggests that any improvement will come very slowly.

To be sure, there are bright spots in the 1983 outlook. Livestock prices strengthened this year and grain and oilseed prices have moved up in the past few weeks. Reduced inflation and lower interest rates will encourage demand and will greatly ease pressure on farmer's expenses and borrowing costs. The global economy is likely to make a gradual recovery in 1983 and beyond without rekindling rapid inflation.

Supply adjustments also are likely. Signs point to reduced plantings of most major U.S. crops next year and a further drop in domestic livestock production. Rising domestic use of crop products and potential for some improvement in the volume of U.S. farm exports should slow the buildup in U.S. stocks.

Unfortunately, given the weakness of the world economy and the size of crop stocks, the expected strength of these corrections would not be enough to greatly improve commodity prices next year. The forces that led to the huge buildup in stocks and depressed global demand are deeply entrenched, and will require time to be reversed.

We thus foresee, barring the unexpected, continuing pressure on crop prices, modest gains in livestock prices, and continued low returns in farming in 1983.

Farm programs were modified this fall in light of these prospects. Deficiency payments for 1982 crops were accelerated, and advanced farm program payments offered to farmers who comply with acreage reduction and paid diversion programs for 1983. Grain producers who participated in 1982 farm programs are making heavy use of the farmer-owned grain reserve, greatly restricting near-term marketable supplies. Each of these measures will help, but even collectively they may not be fully adequate when compared with the problems at hand. There are limits as to how much farmers can restrict production, how high crop and dairy product stocks can be piled, and how expensive farm programs can become.

Consequently, policymakers are closely examining the causes of our present dilemma and options for short-term adjustments in farm policies. As we examine the outlook for 1983 in detail, I would ask each of you to consider not only what lies ahead, but what policy solutions can be found to ease the stress of this period.

#### Farm Output Expanded for a Decade

Many of the forces that shaped our present difficulty are longer term factors in U.S. agriculture and in world economic relationships. That's why it's so difficult to counteract them or offset their effects on farmers in the short term.

The tight world food situation of the early seventies triggered a decade of expansion by American farmers and increasing reliance on foreign markets, which today account for every third acre that farmers plant.

U.S. farm exports tripled between 1971 and 1981, in response to rapid growth in the world economy and population. Farm exports were enhanced by the declining value of the U.S. dollar during this period. Our own economy was generally buoyant, producing strong growth in domestic demand, especially for livestock products. Farm prices rose through the seventies. The underlying price support levels were ratcheted upward. This ratcheting, coupled with the appreciation of the dollar, has elevated the price "floors" beneath grain, cotton, oilseed, sugar, and dairy prices.

With plentiful and easy credit and rising land values during the seventies, farmers found it advantageous to escalate borrowing and make heavy capital investments. Results were dramatic indeed. Between 1971 and this year, farmers increased the area planted to principle crops--excluding hay--by more than 60 million acres. Heavier input use, availability of yield-boosting technology, and recent ideal weather have pushed yields to new heights. Crop production per acre today is 17 percent above that of a decade ago. The combined effect of expanded crop acreage and rising yields has been to thrust U.S. crop production upward by fully one-fifth over the past decade. Livestock production also expanded, rising by 7 percent over the period.

As prices and land values rose, farmers who borrowed in order to expand tended to earn a better rate of return than those with higher equity. Rapid inflation in recent years fueled additional borrowing to cover annual production expenses. Consequently, farm debt has tripled in the last decade, and interest payments now account for one dollar in every seven that farmers spend for their business.

Prolonged expansion was followed by a period of reduced incomes during the last 3 years. This has greatly increased the difficulty now of making large adjustments in production in response to current conditions.

Crop producers who have heavy debt payments to meet and large investments to protect have less flexibility in reducing production. Last year, rather than cut acreage, most grain producers opted to forego participation in farm programs.

For the last several years, dairy farmers have been responding to rising milk support prices rather than to actual demand levels. They have increased the dairy herd and production per cow. Now, under pressure to

reduce milk output, they have three hard choices: cutting back production, switching to other enterprises, or finding work off the farm.

Livestock producers were forced to cut output this year after several years of unfavorable returns. Now livestock prices are up and feed prices down. Yet apparently because many producers are financially strapped, it appears they are not gearing up for expanded production.

#### Global Demand Has Changed Course

American farmers have become especially vulnerable to fluctuations in world trade and world market prices. For the past several years, U.S. and world crop production have set new records, but global demand for agricultural products has switched from a high-growth path to one of little or no growth.

Meanwhile, the sources of strength in our agricultural exports have been eroded by other factors: financial instability in a number of countries, the strong U.S. dollar, losses related to the Soviet embargo and continued East-West political tensions, and unfair trade practices by our competitors.

The world is in the grips of recession. The industrial market economies barely grew this year, and the U.S. economy declined. Developing countries, important to agricultural trade, are growing by about 2.3 percent in 1982, well below normal.

We currently expect the U.S. economy to pick up as next year progresses, achieving real growth of 2 to 3 percent for all of 1983. The Federal Reserve has permitted faster growth in the money supply for the time being, but will probably target for moderate restraint in growth of the money supply next year. This would limit the recovery in economic activity, as well as helping us to hold down inflation.

U.S. recovery will help stimulate other economies, but the process will take time. The industrial market economies may grow only around 1-1/2 percent in 1983, and developing countries by 3-1/2 percent. But even this stimulus to incomes, and hence demand for farm products, will be tempered by lingering high unemployment levels.

A large number of countries have had financial crises that have forced them to curtail food imports. The financial problems of Eastern Europe and Mexico have been the most devastating to our trade. U.S. grain exports to these markets dropped by 8.0 million tons in the past year, compared with the 1979-81 average.

Foreign investors, seeking a haven of safety and high interest rates, have been driving up the dollar's value. Even though interest rates in the United States have recently dropped, they still offer favorable real returns to foreign investors. With an economic recovery in prospect here, the dollar is likely to continue strong in 1983.

The strong dollar increases the price of our farm products to foreign customers. Over the past year, our farmers have received sharply lower prices, but after accounting for exchange rates, prices importers pay are rising. Since there's little likelihood of a significant weakening of the dollar, our farm exports will continue to be adversely affected.

Our share of Soviet grain imports slipped from around 70 percent in the late 1970's to 17 percent following the U.S. embargo with the Soviet Union in 1980. It recovered to over 30 percent in the past year. The problem of reliability, coupled with continued East-West political tensions, continues to cloud our trade prospects with the Soviet Union. Although the Soviets harvested a fourth poor grain crop this year, estimated at around 180 million metric tons, grain imports during 1982/83 will be smaller. Thus, the United States will have to work hard to recover a larger share of the Soviet market.

Our farm export markets are being seriously undercut by unfair competition from the European Community and other nations. The EC has become the second largest exporter of farm products by spending upwards of \$7 billion in subsidies.

We have made little headway in our discussions with the EC informally and now in the GATT. We have recently begun a program of "blended credit" that combines interest-free direct credit with government-guaranteed private credit. While small, it indicates that if necessary, we are prepared to take steps to improve the competitiveness of our exports.

#### Consumption Growth Slower

The world economic problems of the eighties have had a depressing impact on consumption of agricultural products. For example, during the last two decades, global coarse grain consumption rose 16 million tons per year as diets were upgraded with more animal-product foods. Yet since 1979/80, growth in meat production has stopped and coarse grain consumption has nearly flattened out. World wheat consumption increased by over 10 million tons annually during the past two decades, but may rise only 10 million tons for the four years between 1979/80 and the end of the current season. Until economic conditions in importing countries improve, consumption growth will continue to lag. Cotton consumption is in a similar bind, since mill use is sensitive to economic conditions. World soybean usage, however, has continued about on trend.

U.S. farm exports dropped for the first time in 13 years during the fiscal year ending in September 1982. Volume slowed 2 percent below the previous fiscal year, but value plunged 11 percent because of sharply lower prices. Corn exports were hardest hit, dropping by 10 million metric tons and \$3 billion. However, cotton exports rose and wheat and soybeans broke earlier volume records. Exports of animal products equaled the record level of the previous fiscal year.

The volume of U.S. farm exports in the next year is likely to increase. Recovery in corn exports and a little further growth for soybeans will contribute to a larger volume of shipments. However, continued low prices may cause value to fall for a second year.

#### Large Output and Rising Stocks Boost Global Supplies

Following two reduced grain harvests in 1979 and 1980, excellent weather in 1981 pushed world grain production to nearly 1.5 billion metric tons. Larger U.S. crops were an important factor in the global increase. This year, with widespread good weather, world grain production surpassed the 1.5-billion-ton mark. U.S. grain output topped its 1981 record. Grain production increased in a number of importing countries, especially the Soviet Union and China.

The weather also contributed to a sharp jump in world production of oilseeds this season, another large sugar crop, and large cotton crops in foreign countries. These weather-related developments will have a negative effect on our trade during the next year.

With consumption of agricultural commodities depressed by deteriorating economic conditions for the last several years, rising production has caused stocks to accumulate sharply, both globally and in the United States. We forecast that by the end of the 1982/83 marketing year, world grain stocks are likely to reach about 250 million tons, 75 million tons higher than 2 years before. This would be equal to 2 months' supply of grain, the highest global stocks-to-use ratio in more than a decade. The measure of food security that these stocks would provide must be balanced against their lopsided distribution, since nearly 150 million tons--or nearly 60 percent--would be located in the United States.

U.S. stocks of nearly all major commodities are expected to escalate. By the end of the current 1982/83 crop year, compared with 2 years earlier, our ending stocks of rice and coarse grain will have tripled. Cotton stocks will be two-and-three-fourths times larger than 2 years before. Wheat stocks will be half again as large, and U.S. soybean stocks will have risen by 40 percent. Thus, as farmers contemplate production options for 1983, they will have to reckon with large carryover stocks.

The market impact of grain carryover stocks will be moderated by the farmer-owned grain reserve. In fact, as we enter the next marketing year three-fourths of the U.S. grain stocks are expected to be either in the reserve or under CCC ownership. This will limit free supplies, thus aiding prices.

We are strongly advising our farmers to take advantage of 1983 farm programs in order to reduce acreage and better balance supply and demand. We are also concerned that other major food exporting nations are not exercising similar measures of restraint.

I would now like to briefly look at prospects for the major commodities in the 1982/83 marketing year.

#### Some Pickup in U.S. Coarse Grain Exports Expected

Larger coarse grain crops in the United States, Europe and the Soviet Union are offsetting lower production in Mexico and expected declines in the Southern Hemisphere. World coarse grain trade is likely to be slightly above last year's level. U.S. coarse grain shipments may rise about a tenth because reduced output in other exporting countries is limiting competing supplies.

We look for partial recovery in corn exports and larger domestic feed and industrial corn use, adding up to a 400-million bushel gain in total corn use in 1982/83. Even so, ending corn stocks next fall could rise nearly 1.1 billion bushels, to over 3.4 billion bushels. Reserve and CCC holdings may rise by 1 billion bushels.

Corn prices for the 1982 crop are expected to average below last year's \$2.45 per bushel and the 1982 loan rate of \$2.55. Low corn prices are likely to hold down prices of competing feed grains.

### Food Grain Prospects Soft

World food grain production increased 1 percent this year. Record yields boosted wheat output more than 3 1/2 percent, but smaller U.S. acreage and lower yields, plus a poor monsoon in Asia, reduced the world's rice crop.

Next year's gain in consumption of food grains will be limited by the impact of sluggish economic conditions, and especially the impact on the ability of developing countries' ability to pay for imports. Since developing countries take an increasing share of world food imports, their financial situation has serious consequences for our exports.

U.S. wheat exports are likely to hold up well despite good crops in exporting countries--except in Australia, where wheat production may be down by half because of drought--and despite larger crops in Eastern Europe, the Soviet Union, and other major importing countries. Look for larger U.S. shipments to North Africa and the Middle East and to India, which may purchase 5 million tons, as well as continued large sales to China.

World wheat stocks may increase by a tenth this season, with most of the buildup in the United States, where ending stocks next June may exceed 1.4 billion bushels, the largest since the early sixties. Prices during the first half of the marketing year have averaged 20 cents below the \$3.55 per bushel loan level and may average a little below it for the season.

There is little prospect that our competitors will reduce wheat plantings for 1983 harvest. Moreover, weather thus far in wheat growing regions has been generally favorable. These indications suggest that production of wheat outside the United States in 1983 could rival this year's record. This could limit the likelihood of improvement in U.S. trade during 1983/84.

Although U.S. rice producers trimmed 1982 output sharply, larger beginning stocks pushed total supplies for 1982/83 to a record 202 million hundredweight, well above prospective use. With little or no gain in exports, ending stocks next August are expected to be large and prices are likely to remain depressed.

### Unprecedented Oilseed Crops

World production of major oilseeds increased nearly 8 percent this year to an unprecedented 185 million metric tons. A 15-percent larger soybean crop plus a record sunflowerseed harvest have boosted U.S. oilseed production.

A smaller carryin held the increase in total U.S. soybean supplies for 1982/83 to 11 percent. U.S. supplies of sunflowerseed and flaxseed also are up from a year ago, while supplies of peanuts and cottonseed are smaller.

Consumption of oilseeds, both domestically and worldwide, is increasing in response to low prices--especially in relation to competing feedstuffs. However, gains in both domestic use and exports of U.S. soybeans will be limited by reduced U.S. hog numbers, weak economic activity worldwide, and larger world supplies of competing oilseed products.

From \$6 per bushel last season, prices for the 1982 crop are currently forecast to average between \$5.25 and \$5.75. Price declines are also likely for the other U.S. oilseeds.

U.S. soybean ending stocks are rising sharply to about one-fifth of annual use, well above more typical levels. Soybean plantings in 1983 are likely to be below last spring, when higher prices encouraged soybeans on farms with diverted grain or cotton acreage and some failed cotton land was late-planted to beans. Even if smaller plantings and more typical yields cut production next year, the expected large stocks could maintain supplies for 1983/84 near their present high level.

#### Cotton Prospects Deteriorating

In recent months, the estimate of U.S. cotton production has been raised to 11.9 million bales, primarily because of record-breaking yields. Sluggish domestic and foreign demand, strong competition from imported textiles, and an excellent harvest in China have reduced prospective combined domestic use and exports to 11.2 million bales. U.S. ending stocks may rise to 7-1/2 million bales, the largest since 1967.

China purchased 850,000 bales of U.S. cotton last season, but may buy virtually none this season. This, combined with sluggish use in other major Asian markets, has lowered export prospects. However, smaller 1982 crops in other exporting countries and recent sales under the new U.S. blended credit program will preserve our one-third share of world trade.

Domestic cotton prices have been forced down towards the loan rate, which is likely to provide an effective floor this season. Given higher target prices and loan rates next year and low prices for alternate crops, a high proportion of cotton growers may opt for the 20-percent acreage reduction program. Even so, harvested cotton acreage and production may exceed this year's low level.

#### Surplus Pressures World Sugar Prices

A sharp jump in world sugar production in 1981/82 to 100 million metric tons has pushed beginning stocks for this season above 35 million tons, equal to almost two-fifths of annual consumption. World production in 1982/83 may be only slightly lower, driving ending stocks up to as much as 42 million tons by next year. World raw sugar prices may average only 6 to 8 cents per pound for 1982/83. Prices paid to U.S. growers, however, are being effectively supported at around 21 cents per pound by the sugar stabilization program.

U.S. production for 1982/83 is down 7 to 8 percent, reflecting a sharp drop in beet acreage and lower beet yields. Quotas kept excess world sugar supplies from flooding the higher priced U.S. market in 1981/82. In 1982/83, U.S. supplies are expected to fall further as production will likely decline and imports should continue to drop.

## Meat Production Declines

An 11-percent cutback in pork output triggered a 3-percent decline in total output of red meats and poultry this year. In 1983, total output may drop 1 percent further. Despite improved prices over a year ago and low production costs, producers are hesitant to expand. Larger sales of gilts by pork producers and heavy cow sales from mixed enterprise areas suggest that producers may be raising cash for current needs rather than increasing breeding herds, or are having a hard time qualifying for additional credit.

Poultry production may be up a little next year, but pork output may drop further and beef output may return to the lower 1981 level. Broiler and turkey prices could average slightly higher, but egg prices may show further weakness.

Small hog inventories point to a sharp cut in first-half 1983 pork output. Reduced farrowings, at least through winter, may hold down second-half production.

Lower feed and feeder cattle prices, and higher fat cattle prices have put cattle feeders in the black for the first time in several years. Feedlot placements are up sharply and fed cattle production will rise next year. But much lower nonfed and cow slaughter could reduce total beef output slightly.

Even with tighter meat supplies, producer prices may improve little over this year's levels. Per capita red meat consumption may drop again next year and reach the lowest level since the midsixties, reflecting the reduced supplies.

Although consumer incomes are up in nominal terms this year, real purchasing power has increased very little since 1980. High unemployment and short work weeks will continue to restrain purchasing power during the first half of next year. But retail demand for livestock products should strengthen in the second half as increasing employment and a longer work week boost buying power.

Milk production increased 2 percent in 1981/82 as both cow numbers and output per cow rose. The milk cow inventory at the beginning of the 1982/83 marketing year was larger than a year earlier, providing a basis for continued high production in 1982/83. Feed grain prices are expected to remain low during the coming year, but returns over concentrate costs will decline as the deductions from producer marketings authorized in new legislation begin in December.

Even so, with limited alternatives, the decline in milk cow numbers may be slow. Cow numbers are not likely to drop below the year-earlier level before next summer. Moreover, output per cow is likely to continue to rise. These factors may result in an increase in 1982/83 milk production of 1 to 3 percent.

Commercial disappearance of dairy products rose almost 1-1/2 percent in 1981/82. With very modest increases in retail prices this year, commercial use may rise another 1-1/2 percent. This increase, along with some additions to commercial stocks, could still leave Commodity Credit Corporation purchases near the 1981/82 level of nearly 14 billion pounds on a milk equivalent basis.

## Financial Conditions

We are now in the third consecutive year of severe financial problems in agriculture. While conditions vary widely among producers, geographic regions and the type of commodity, many farmers are experiencing difficult cash flow problems. These financial problems extend beyond the farm gate and affect farm suppliers and other farm-related businesses.

In terms of the key financial variables, cash receipts to farmers this year are lagging last year's \$143.5 billion by 1 percent. Although the reduction in inflation and declining interest rates have slowed the rise in cash expenses, farmers are spending slightly over \$1 billion more on production outlays in 1982 than the \$115.8 billion of last year. This more than offsets the additional CCC loans and direct payments, and limits the net cash income in farming to about \$31 billion, down slightly from the 1981 level, and the lowest since 1977.

Farmers' net income in 1982 is expected to total about \$19 billion compared with around \$25 billion in 1981. With severe pressure on farm prices, coupled with substantial cash flow problems, the value of farm assets has declined significantly. In the past year, as farmers' debts continued to rise, total liabilities increased 8 percent. This will reduce the total equity in agriculture on January 1, 1983, to around \$850 billion, the lowest level since 1980. The debt to asset ratio in agriculture, while still low compared with other industries, jumped to about 20 percent compared with around 16 percent in the late 1970's.

Looking on to 1983, it is difficult to accurately forecast the financial performance for agriculture at this early date. On balance there is little basis for much improvement. Cash receipts to livestock producers are expected to improve slightly, reflecting prospects for somewhat smaller output and a modest firming in demand. On the crop side, with prices expected to remain under pressure it will be difficult for marketing receipts to move above this year. At the same time, prospects for further progress against inflation and lower interest costs are encouraging, and suggest that little increase in production expenses is likely. These tentative indications give little reason to expect cash flow or net returns in farming to improve much from 1982 levels. However, a sudden change in weather patterns that might affect global crop production, or a major change in farm programs for the year ahead could materially alter this outturn. Needless to say, speculation on any of the financial aggregates in agriculture for next year is highly uncertain at this stage.

## Food Prices Slow

Retail food prices increased by 4-1/2 percent this year, the smallest increase in 6 years, and averaged well below the rate of increase for nonfood items. Annual food price increases have steadily dropped from the 11-percent peak in 1979. Abundant supplies of farm products, stagnant consumer incomes, and moderating costs of processing and marketing food all helped slow the cost of food prices at retail.

A similar situation should prevail next year. The general inflation rate is likely to slow further, limiting the rise in food processing and marketing

costs. Food supplies from crops will be abundant and fruit supplies, tight in 1982, should expand. Livestock supplies are not expected to expand, and retail prices will increase moderately. On the whole, larger food supplies will tend to offset somewhat stronger demand that develops as the economy begins to recover. Thus, overall retail food prices are likely to increase in the range of 3 to 6 percent during 1983.

### The Challenge Ahead

In the past, agriculture has been able to weather slack years through use of a combination of farm programs that take some supplies off the market, encourage farmers to restrict their output, and temporarily supplement farm income through price and income supports.

Today a complex set of circumstances is frustrating these farm policy mechanisms. As we have seen, many of the forces that are bloating world commodity supplies and blunting demand for American farm products are beyond our control. For that reason, the traditional policy prescriptions, while still helpful, may no longer be sufficient either to tighten up supplies and markets, or to provide an adequate safety net for producers. The cost of these programs is rising geometrically at a time when the Federal budget must be brought into line.

Thus, it is not just farming that is under pressure, but farm policy as well. That pressure falls on the entire agricultural community--policymakers, lawmakers, farmers and their organizations, and you who are attending this conference in your capacity as outlook specialists, professors, extension specialists, or communicators. Together, we must pool our ingenuity to find the combination of farm programs that will get us through this rough period. More challenging still, we must avoid nearsighted or inflexible solutions that only magnify problems a few years in the future. Earlier farm policies have contributed to the explosion of overproduction that now confronts us.

The demand for effective solutions, whatever their source, has never been stronger. Our challenge is not just to leave this conference with another sheaf of forecasts for those we advise, but to use the outlook material as the starting point in a search for farm policies adequate to our present situation.