

The Economic Outlook for Kentucky Agriculture in 2010

Editors **Kenny Burdine & Sara Williamson**

Kentucky's Agricultural Economy Craig Infanger & Kenny Burdine

2009 Review: After two years of record-high income, the bursting of the commodity price "bubble" in 2008 and the global recession hit the agricultural sector hard in 2009. Prices for major commodities were more than 50% below recent high levels. In addition, the big drop in U.S. agricultural exports this past year – down 15% -- created serious market pressure on traditional export commodities like horses, corn, soybeans, and pork.

As a result of these market forces, cash receipts from livestock — equine, cattle, dairy, poultry, hogs and other small ruminants — are estimated to be only \$2.46 billion, a drop of about \$450 million from 2008. The majority of this reduction comes from lower sale prices and stud fees for Thoroughbred horses, although dairy income was down substantially and cattle sales declined modestly. Both dairy and hogs have been particularly distressed this past year. Poultry was the largest component of livestock income in 2009, continuing three years of increased sales.

For the crop sector, with prices down substantially from the 2008 highs, cash receipts declined for corn, wheat, hay, fruits, and greenhouse products. Soybean income increased with better yields, and tobacco receipts were up with expanded acreage. Total cash receipts for crop marketing are estimated to be \$1.83 billion, 43% of total farm cash receipts in Kentucky, compared to 40% last year.

Total Kentucky farm cash receipts are estimated to be \$4.29 billion this year, down about \$550 million from the record-high level of 2008, but just at the five-year average for cash receipts of \$4.28 billion. Net farm income is estimated to be \$1.07 billion.

2010 Outlook: Because Kentucky's agricultural economy is trade dependent, the outlook for 2010 must focus on how well global economic recovery proceeds and whether or not ag exports will begin to increase again. There are clear signs of positive economic growth in Asia, Brazil, and Russia. The U.S. economic recovery can only be described as "positive but fragile" at this point in time. If the dollar remains "cheap" relative to other currencies, ag exports

should begin to expand with improvements in price and volume.

With this cautiously optimistic macro-economic outlook, the outlook for 2010 is encouraging for the livestock sector. Live-stock cash receipts should improve across the board, with sales receipts trending up for the major livestock components – poultry, horses, and cattle. Projected live-stock cash receipts in Kentucky should be in the range of \$2.5 to \$2.7 billion.

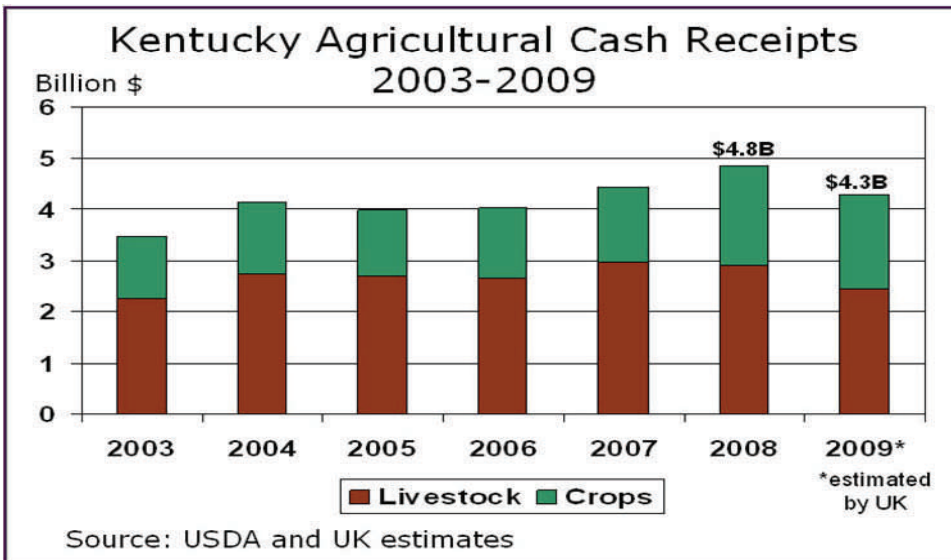
On the crop side, the outlook for tobacco will not be encouraging until the trade situation changes significantly. For grain crops, a return to trend yield for both corn and beans and indications of flat prices for soybeans into harvest 2010 will keep prospects only modestly improved, if at all. There may be some minor improvements for sales of fruits, vegetables, greenhouse products, and the small grains. Assuming normal weather next year, total cash receipts on the crop side should be in the range of \$1.6 to \$1.8 billion.

Thus, total 2010 Kentucky farm cash receipts should be in the range of \$4.1 to \$4.5 billion.

Kentucky's Tobacco Outlook Will Snell

2009 Review: Kentucky's tobacco farmers faced a very wet growing season, causing both yield and quality concerns among some producers. Despite the challenging production and curing season, Kentucky tobacco farmers grew a relatively large crop as a boost in burley acres (primarily due to a significant increase in non-contracted burley acreage) and better yields helped offset a significant drop in dark tobacco acres.

According to USDA, Kentucky's tobacco production is forecast to total 207.4 million pounds, slightly more than the 2008 crop and the highest production level since the



2004 buyout. Nationally, USDA projects burley production at 214.9 million pounds (+7%), with dark fire-cured pegged at 53.6 million pounds (-14%) and dark air-cured at 17.5 million pounds (-31%). Worldwide burley production is projected to be up more than 10% in 2009 and over 30% since 2007, with most of the increase in lower-quality African markets.

On the demand side, both domestic use and exports of U.S. burley declined in the midst of higher tobacco taxes, smoking restrictions, shifting of U.S. cigarette production overseas, depressed U.S. and world economic conditions, and ample world tobacco supplies. Thus, after several years in the early post-buyout era, when total U.S. burley disappearance was in the 250 to 300 million pound range, U.S. burley use will likely decline below 200 million pounds for the 2009-2010 marketing year.

With ample U.S. and world burley supplies, excessive inventories of lower quality U.S. burley held by manufacturers from previous crops, and declining overall demand, quality will be an even greater factor in determining the fate of the 2009-10 U.S. burley market. Excellent quality burley, based on contract prices plus incentives, should continue to gross in the \$1.70s and \$1.80s per pound. However, lower quality tobacco within contracts will likely receive noticeable price discounts, while lower quality tobacco grown outside of contracts could generate very disappointing offers.

For dark tobaccos, the dramatic drop-off in production was more supply driven, rather than demand driven. Snuff consumption, the primary user of dark tobaccos, has been increasing steadily over the past two decades, although snuff sales have been somewhat stagnant during 2009. Contract prices indicate that good quality dark air-cured

prices will average around \$2.25 per pound and \$2.55 per pound for dark fire-cured – slightly above last year's and pre-buyout prices.

Overall, the value of the 2009 Kentucky tobacco crop (depending on how the quality of cured leaf materializes) may be near last year's \$382.6 million level, which represented the highest valued crop during the post-buyout era.

2010 Outlook: In response to ample supplies and product demand forecasts, burley and dark tobacco buyers are not likely to ask Kentucky tobacco growers to plant additional acres in 2010. Some growers, especially low quality burley growers, may see contracts reduced or eliminated. Many non-contracting producers may decide to exit following disappointing results from the 2009 market.

An improving U.S. economy, additional smoking restrictions, and perceptions of lower health risks relative to cigarettes could result in smokeless product sales rebounding in 2010. Increased use of smokeless products, when coupled with recent acreage adjustments, should help improve the overall supply/demand balance for dark tobaccos. For burley, domestic needs will continue to decline in response to anticipated lower consumption. Export demand will remain the critical factor for burley, depending greatly on the value of the U.S. dollar.

The cheap U.S. dollar may enable some of the excess 2009 crop to find a home in foreign markets during 2010. If the U.S. dollar remains relatively low compared to the Brazilian currency and the world economy begins to rebound, international cigarette manufacturers, seeking flavor burley, may reevaluate U.S. burley in their purchasing and blending decisions for 2010 and beyond. Implementation of FDA regulations on tobacco may begin to impact production

practices as required by contracting companies, which may cause some producers to exit. With anticipated contract volume reductions and minimal contract price adjustments, look for the value of Kentucky tobacco production to fall below \$350 million in 2010.

Kentucky Farm Business Analysis Trends

Jerry Pierce & Jennifer Rogers

2009 Review: Net Farm Income (NFI) for farms participating in the Kentucky Farm Business Management (KFBM) program has increased fivefold over the last 10 years. NFI is the value of farm production less total operating expenses, plus gain or loss on machinery and buildings sold. It includes a return to the operator's labor, capital invested, and management. Grain farms in KFBM generally produce a higher return than livestock farms. NFI for the two farm types were similar in direction through 2005. Beginning in 2006, incomes on grain farms increased, while livestock farms experienced a steady decline.

Family living expenditures for KFBM farms have increased an average of 7.6% each year for the same 10-year period. Last year's record NFI likely influenced these farms to increase family living expenditures by 11%. The average KFBM farm family spent \$71,742 in 2008. Included in 2008 was a 71% increase in non-farm capital purchases. Family spending in 2008 was more than NFI in six of the last 10 years.

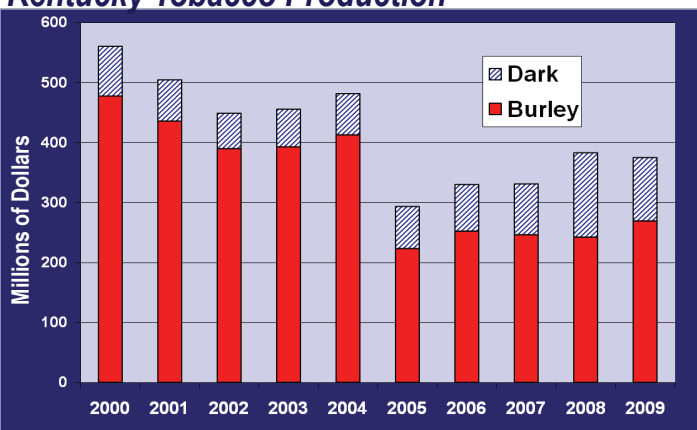
2010 Outlook: Current input prices and available crop prices for next year suggest that NFI for KFBM grain farms will be close to 2008 record levels. Total returns are expected to drop 8% compared to 2008, but total farm costs are expected to drop by 10%. The result would be a NFI of \$411,000, close to the record \$416,000 earned by KFBM farms in 2008. These projections are based on prices and conditions in November 2009 for the typical KFBM grain farm in the Purchase area.

Grain Marketing *Cory Walters*

2009 Review: The estimated size of the 2009 corn crop peaked in October at more than 13 billion bushels, and despite decreases due to recent weather, it is still expected to be 7% higher than 2008. The November 2009 USDA crop report estimated the corn crop at 12.92 billion bushels, and decreased the corn yield to 162.9 bushels per acre, down 1.3 bushels from October.

On the corn consumption side, exports were decreased by 50 million bushels from the October USDA Report, while feed and ethanol use held constant, for a total use of 12.98 billion bushels. Ending stocks came in

Value of Kentucky Tobacco Production



at 1.62 billion bushels, down 50 million from the October report. With the changes in production and use, it appears that corn use will exceed production. The report also pegged average farm price at \$3.55. Global corn production estimates and ending stocks were reduced from previous estimates.

For soybeans, crop size was increased slightly to 3.32 billion bushels (a record) from the October USDA crop report, which would be 12% greater than 2008. Estimated yield was increased by 0.9 bushels per acre over the October report to an average of 43.3 bushels per acre.

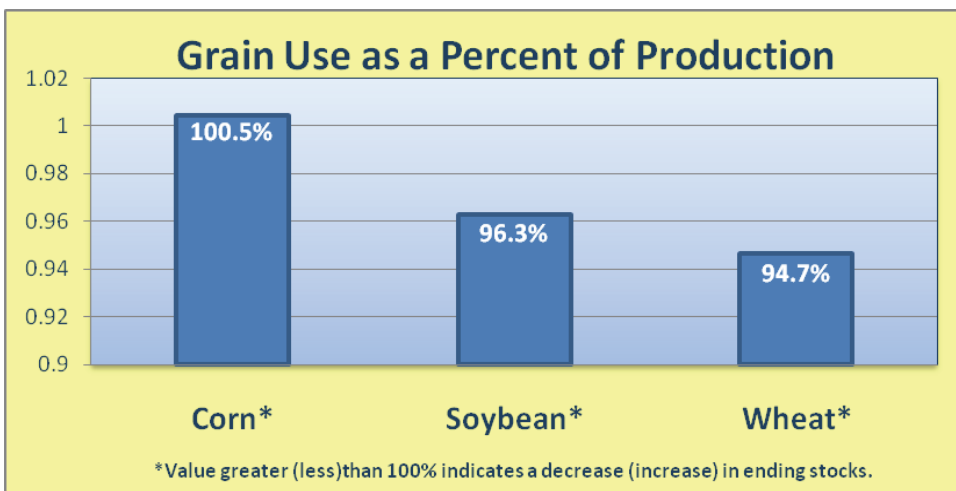
Total use was increased from the October USDA report to 3.19 billion bushels, coming from a 25 million bushel export increase and a 5 million bushel crushing increase. With a larger increase in production than use, ending stocks were increased by 40 million bushels to 270 million bushels in November. So, soybean production should exceed use for the 2009 / 2010 marketing year. The November report pegged average farm price at \$9.20. Global soybean production and stocks are expected to increase over last year.

For wheat, crop size was slightly decreased from the October USDA crop report to 2.22 billion bushels, which will be well below last year's crop. Exports and feed use are expected to be below last year's levels, while food and seed use are expected to increase. Overall, ending stocks are expected to increase by 228 million bushels from last year, to 885 million bushels. As with soybeans, wheat production should exceed use.

2010 Outlook: Corn and soybean prices will continue to be influenced by the rate of harvest (corn 35% and soybeans 7% behind five-year average as of mid-November), value of the U.S. dollar (currently declining), crude oil (currently strengthening), index fund investment (currently strengthening), demand prospects, South American crop size (which is predicting a large soybean crop), and crop condition.

Horticulture Tim Woods

2009 Review: Just eight years ago, when Kentucky was starting to make a concerted push toward diversification and development of the horticulture industry, the value of all horticulture cash receipts was \$78.6 million, which included floriculture, nursery, greenhouse, and sod (\$59.7), and produce



(\$18.9). Kentucky's produce (vegetables/fruit) industry and green (nursery/greenhouse) industry have experienced steady growth over this period, even through a difficult economy. Current industry sales trends point toward 2009 gross sales winding up somewhere around \$110-\$115 million. Gross produce receipts appear to be slightly ahead of 2008 as more producers, especially farmers' market vendors, benefited from additional direct market channels. Over 2,000 vendors sold in farmers markets in 2009 and the number increases each year.

Total sales for produce in 2009 are estimated to be primarily from direct market channels, although auction and other wholesale channels have experienced significant growth as well. A continued weak overall economy and relatively high input costs, especially labor, resulted in another weak marketing season for Kentucky's green industry – greenhouse, nursery, and sod.

Preliminary produce planting intentions for 2009 indicated an expected acreage increase for produce crops of 8% overall and a total of around 14,000 acres. Fruit crop acreage was projected to be up slightly at an estimated 2,800 acres, with particular growth in grapes and small fruit, while vegetable crop acres were estimated at 11,200. For comparison purposes, Kentucky had around 10,500 acres of produce in 2002.

Green Industry: The green industry nationwide is fueled by new home construction and healthy consumer spending. Product sales are important, but the growth nationally has come from the service component of the industry. This sector grew rapidly between 2002-06 but has since been hit hard by the recent economic slowdown. Opportunities for farm producers in this sector lie in regional and direct marketing

and services accompanying nursery product sales. The \$81.2 million sales level in 2006 for nursery and greenhouse products (floriculture, nursery, sod, Christmas trees, etc.) represented the highest level ever for Kentucky producers. Kentucky will be fortunate to pass \$65 million in 2009.

2010 Outlook: The outlook is for steady growth in commercial fruit and vegetable production in Kentucky for 2010. Direct market, auction, and independent or allied grower-shipper wholesale sales will again increase – particularly with strong demand for local products in local markets. Gross sales will continue to be driven by higher-value direct marketing at farmers' markets, directly off the farm, and to food service.

The major policy issues for produce will be related to food safety, mandated production audits, and labor. The green industry may see a slight improvement in 2010 as projected home sales and consumer disposable incomes see improvements at the turn of the year. An improving consumer income situation could positively influence consumer spending at farmers' markets and agritourism destinations.

Livestock Lee Meyer & Kenny Burdine

EQUINE

2009 Review: Equine receipts typically lead Kentucky's agricultural sector, however it is not clear if this trend will continue in 2009. Receipts from sales were down considerably from 2008 as the weak U.S. economy showed its impact on the equine industry.

2010 Outlook: Farm level equine receipts are primarily derived from sales and stud fees. As with most agricultural sectors, equine sales will likely follow suit with the overall U.S. economy. Further, it appears

that stud fees will be lowered for several sires during 2010, putting further pressure on receipts. As a result, sales prices will need to be much stronger next year to see serious improvement over 2009.

BEEF

2009 Review: Wet weather was a welcome change for beef cattle producers in 2009, as cattle were able to graze much longer and hay was largely in comfortable supply. However, producers struggled to cover their costs on a calf market that was very similar to 2008. Although calf prices rallied from late 2008 levels and spent much of the spring and summer above \$1 per lb., they plummeted in the fall, once again squeezing cow-calf operators and resulting in a price decline of more than \$20 per cwt. from spring to fall.

2010 Outlook: Beef cow numbers are as low as they have been since the 1960s, yet prices have remained soft in the face of weak beef demand. Calf prices should rally as we move into spring and have the potential to improve upon 2009 levels if demand strengthens. Demand improvement will need to come from a stronger U.S. economy, which remains a wild card in the near future. Corn prices will also play a major role, and it is likely that yet another very large corn crop will be necessary in 2010.

be much lower by the time 2010 arrives.

2010 Outlook: The dairy industry tends to be slow in lowering production and this was certainly the case in 2009. But high production costs, low prices, and three rounds of CWT dairy herd retirements should result in a moderate reduction in dairy cow numbers for 2010. This reduction, coupled with some improvement in dairy stocks, should result in more favorable milk prices in the upcoming year. Kentucky mailbox prices will likely be \$2 - \$4 per cwt. above 2009 levels.

SHEEP & GOATS

2009 Review: Lamb production was down another 3% in 2009, to 168 million pounds. Imports continued to exceed domestic production, at 185 million pounds (according to the USDA).

Following economic principles, prices rose modestly and averaged just over \$.90 per pound. Kentucky's lamb sector saw modest growth, with inventory increasing by 3,000 head, up to a total of 40,000 ovine. Direct to consumer and food service sales continued to be an important marketing method and captured somewhat higher net prices than commercial sales.

Kentucky's meat goat industry continued to mature, with about 20% growth over the last six years. However, numbers dropped by 8% between Jan. 1, 2008 and 2009. The high cost of feed and was

mercial lamb prices at national markets are likely to average about \$.90/ lb., with the highest prices in the second quarter (about \$1.00 to \$1.10 per pound). Goat prices typically peak in April and May at 20% over the annual average, which could be \$1.40 per pound or higher for 40-60 pound kids.

HOGS

2009 Review: Despite a slight decline in hog production, hog prices plummeted during 2009 due to weak demand. The weak economy reduced consumer expenditures. Exports, while still high, declined. And, the H1N1 flu, formerly known as "swine flu," impacted consumer attitudes about pork. As a result, prices averaged just under \$40/cwt. (live weight basis), down 20% from the previous year. With feed costs remaining at high levels, most producers struggled to cover cash expenses.

2010 Outlook: Hog prices are likely to improve in 2010 on the basis of smaller supplies and an improving economy. If exports rebound as forecasted by USDA, prices could improve by 10%, averaging in the mid \$40s. However, the increase will not begin until later in the year. Futures markets are more optimistic, with summer contracts trading in the \$70s (equivalent to a \$55/cwt. live price). The industry is not expected to return to profitability until the summer of 2010.

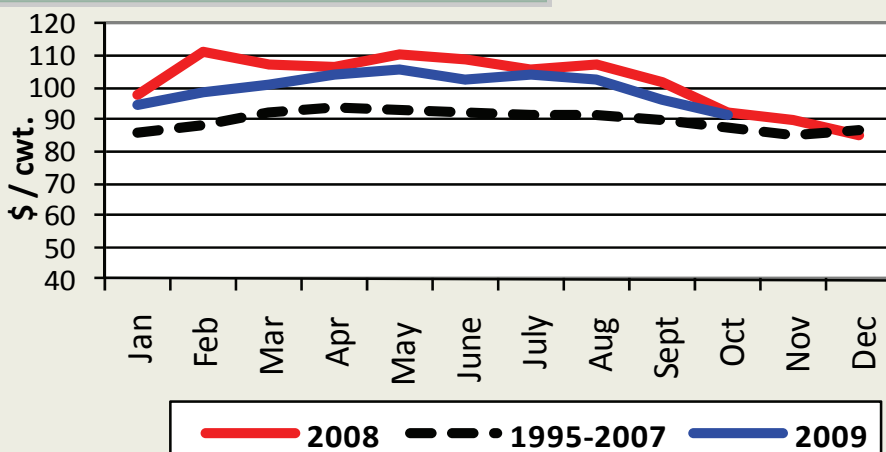
POULTRY

2009 Review: The broiler industry was hit very hard by the high feed costs of two years ago. For the first time in recent years, production did not increase. In fact, total broiler production for 2009 was down 4% from 2008. Another change was the drop in exports – down 6%. The industry typically exports almost 20% of its production. That proportion stayed about the same, with declines in both production and exports. The 2009 broiler price averaged about \$.78 per pound, a small decline from a year earlier.

2010 Outlook: Broiler production for 2010 is expected to increase about 2%. Stronger demand will offset the production increase, so prices are expected to be near the level of the past two years (about \$.80/lb.). Exports may decline slightly due to increased competition from other producing/exporting countries like Brazil. For turkeys, the USDA forecasts slightly higher production in 2010, but also stronger demand, so prices should rise modestly.

Kentucky Auction Prices

500 to 600 Med/Large Frame #1 Steers



DAIRY

2009 Review: Dairy producers also felt the wrath of a weak global economy in 2009. Kentucky mailbox prices were under \$13 per hundredweight in the spring and summer, and will likely average around \$6 per cwt. below 2008 levels. According to the USDA, Kentucky began the year with around 86,000 dairy cows, but that number is expected to

probably a major cause of the decline but primarily impacted operations that were not grazing based. Late 2009 prices for Selection #2, 40-60 pound kids were in the \$115 to \$123 per cwt. range at graded sales, and ranged from \$1.00 to \$1.40 per pound during the year.

2010 Outlook: Both lamb and goat prices are expected to change little in 2010. Com-

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