

The Kentucky Agricultural Economic Outlook for 2009

edited by Laura Powers and Jennifer Hunter



Kentucky's Agricultural Economy

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2008 Review: The year started with a strong base – Kentucky's farm cash receipts for 2007 were up 10% from a year earlier. Cash receipts are estimated to increase another 7% for 2008, to \$4.7 billion. This is a \$1.2 billion, or a 34% increase from 2001.

Estimated receipts from livestock, which include equine, cattle, dairy, poultry, hogs and small ruminants, probably declined during the year due to lower prices for horses and cattle, and smaller sales due to drought. The livestock total is estimated at \$2.7 billion, about 57% of the total. Crop receipts rose about 40% during 2008, adding over \$600 million to the 2007 level. Crops made up about 43% of the total, compared to 37% five years ago.

High crop prices contributed to the high row crops cash receipts. Income forecasts by crop include the following: tobacco - up 13% to \$375 million, the highest level since 2004; corn – up 51% to \$701 million; soybeans, up 41%;

and wheat up three times the 2007 level.

Net farm income shifted dramatically between livestock and crops. Inputs for all enterprises jumped – feed purchased for livestock was up about 20% and fertilizer costs rose by more than one-third. Of course fuel prices, up by 25%, added to the increasing costs of production. In spite of these higher costs, net farm income rose by more than 10%.

2009 Outlook: The mix of income between crops and livestock is not expected to change much. Overall cash receipts are predicted to decline slightly (2%) to \$4.6 billion. Livestock receipts are forecast to increase about 2% to \$2.7 billion on the strength of the poultry industry and modest improvements in the equine industry. Cattle and dairy are likely to continue to decline. Income from the crop side of the ledger is forecast at \$1.9 billion, down 6%.

Kentucky's net farm income for 2009 will probably continue to improve over the 2008 level. While cash income is predicted to decline slightly, there is considerable uncertainty

about the costs of inputs for crop production. If they do drop, net farm income from crops could improve. Feed purchases for livestock should drop by 10 to 20%.

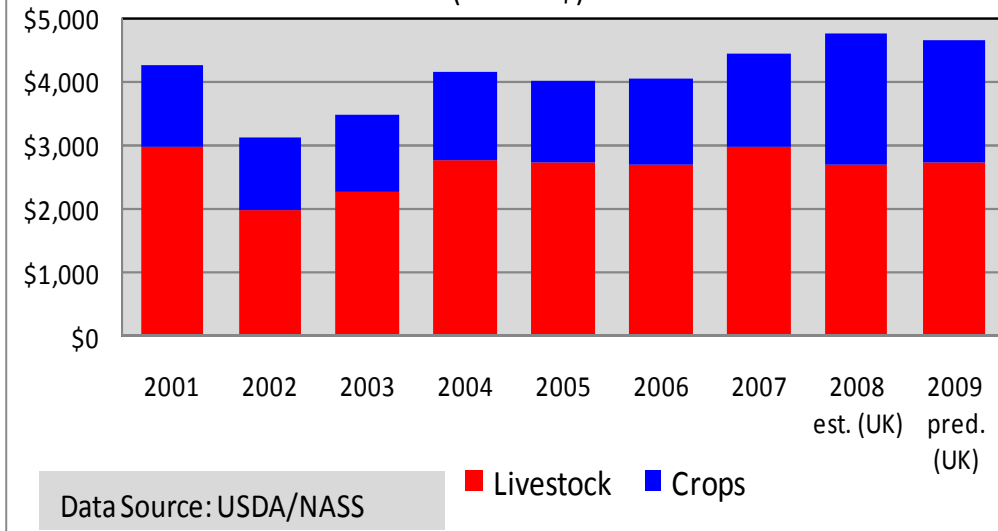
Tobacco

Will Snell

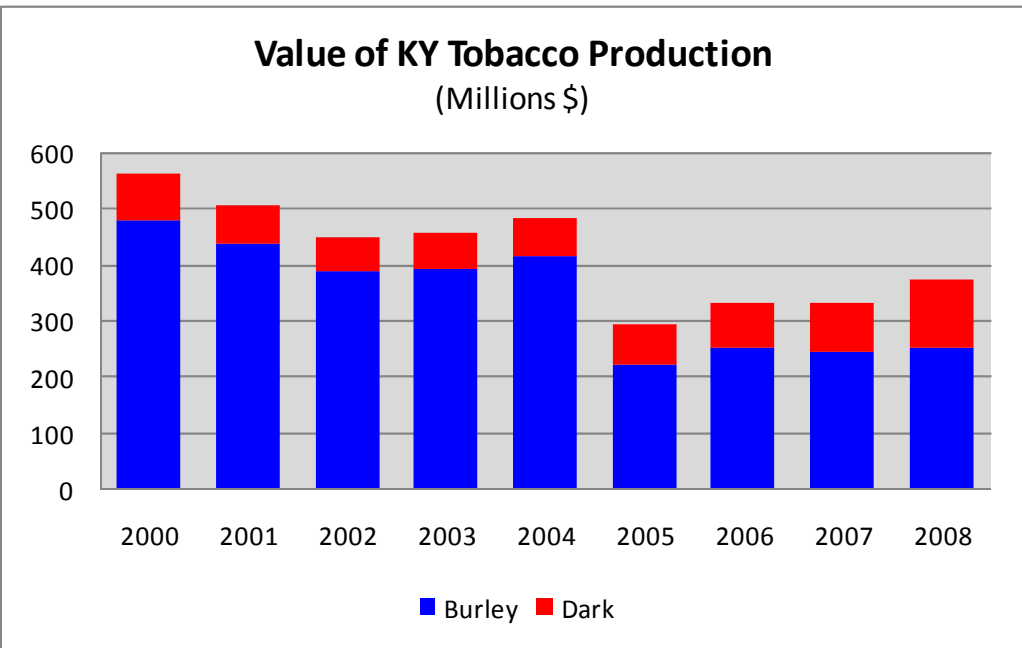
2008 Review: Kentucky's tobacco farmers faced another challenging growing and curing season in 2008 which led to concerns over both yield and quality. However, increased acreage on the heels of a big increase in dark tobacco acreage, boosted the size of Kentucky's overall tobacco crop by an estimated 6%. While burley acreage was down around 10% this year amidst escalating input costs and more profitable opportunities for other enterprises, dark tobacco acres in the Commonwealth grew by more than 40% in 2008 as growers responded to continued higher smokeless product consumption, the entry of new firms, and better profit potential for dark relative to burley. Consequently, unlike burley which is down some 30% since the buyout, dark tobacco acreage has actually expanded well beyond pre-buyout levels.

Despite the loss in burley acres, the value of Kentucky tobacco production will likely be up in 2008 in response to higher grower prices and especially increased dark tobacco acres. While there are some quality concerns for this year's burley crop, contract prices should allow prices plus incentives to average in the \$1.70s to near \$1.80/lb, compared to \$1.55 to \$1.60/lb for last year's lower quality crop. Alternatively air-cured tobacco will average around \$2.25/lb and fire-cured near \$2.50/lb. These higher prices and increased volumes should allow the overall value of Kentucky's tobacco production to grow from an average of \$330 million in recent years to around \$375 million this year, with dark accounting for nearly 1/3 of the total value.

Kentucky Agricultural Cash Receipts
(Million \$)



2009 Outlook: Increasing product demand and limited foreign competition will likely allow the dark tobacco outlook to remain relatively strong in 2009, although expansion will be much smaller as new manufacturers begin to meet their desired inventory targets. The burley outlook is much more uncertain. World stocks of quality burley remain relatively tight, but anticipated production gains in South America will provide some modest relief to tight quality supplies. Overall world burley production is expected to gain around 10% in 2009, following nearly a 20% boost in 2008. However much of the increase is occurring in Africa which produces primarily a lower quality/filler style leaf.



A key issue related to U.S. burley demand will be the exchange rate. In recent years, the declining value of the U.S. dollar has considerably improved the price competitiveness of U.S. burley in international markets, allowing U.S. burley exports to exceed 200 million pounds annually since the buyout. However, the dollar began to gain strength late in 2008, which clouds the 2009 export outlook.

acres remaining at relatively high levels and improved overall yields could still boost the value of the 2009 Kentucky tobacco crop to approximately \$400 million – its highest post-buyout level.

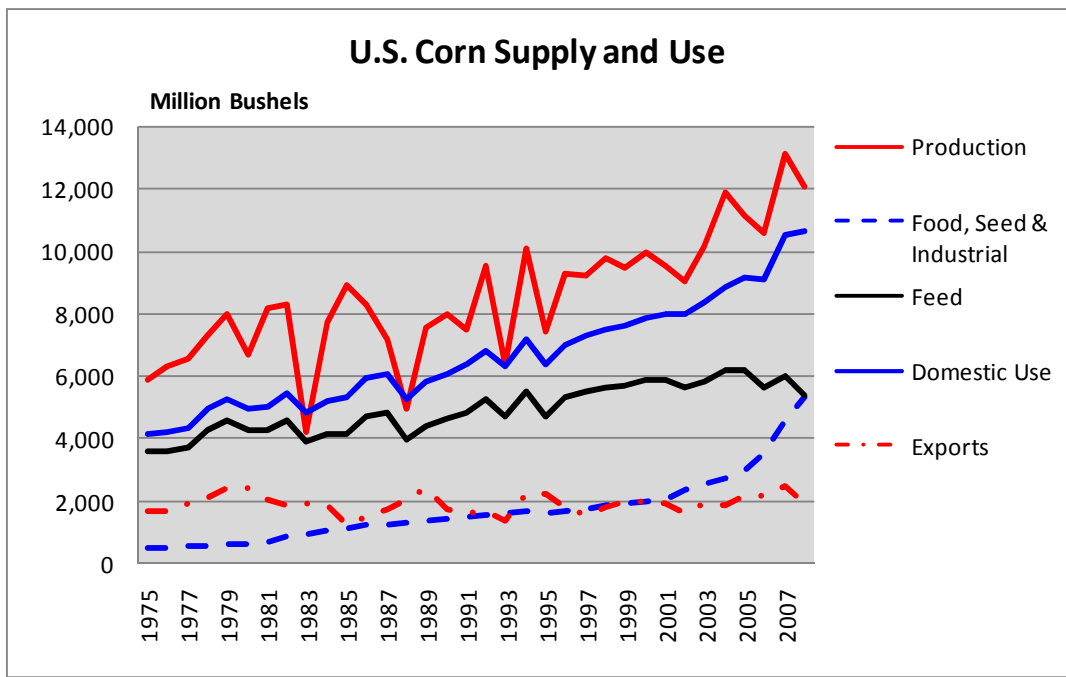
Consumption of corn is expected to be about 12.75 billion bushels, a record for the fifth consecutive year. This record demand is being driven by the increase in corn use for ethanol. Between 2006 and 2007, corn use for ethanol increased approximately 50 percent or just under 1 billion bushels from 2.12 billion to 3.0 billion bushels. Corn for feed is expected to increase by 0.4 billion bushels to 5.97 billion bushels.

Grains *Cory Walters*

Consequently, with increasing foreign supplies and the potential of a deterioration of the U.S. price competitiveness, buyers may not be as eager to offer price incentives sought by growers to entice a larger U.S. burley crop. Coupled with anticipated high input costs, this could easily result in lower U.S. burley acres again in 2009. Collectively, higher grower prices, dark

2008 Review: The 2007-08 corn crop is expected to be a record at around 13 billion bushels. This record is being driven from an increase in both corn acres and corn yields. Corn yields are expected to be the second highest on record, behind the 2004 crop.

The 2007-08 soybean crop is expected to produce 2.67 billion bushels, down from the previous year's record of 3.19 billion bushels. With total use (3.05 billion bushels) being greater than production, ending stocks are expected to decrease, a result that should keep prices high when compared to historical standards.

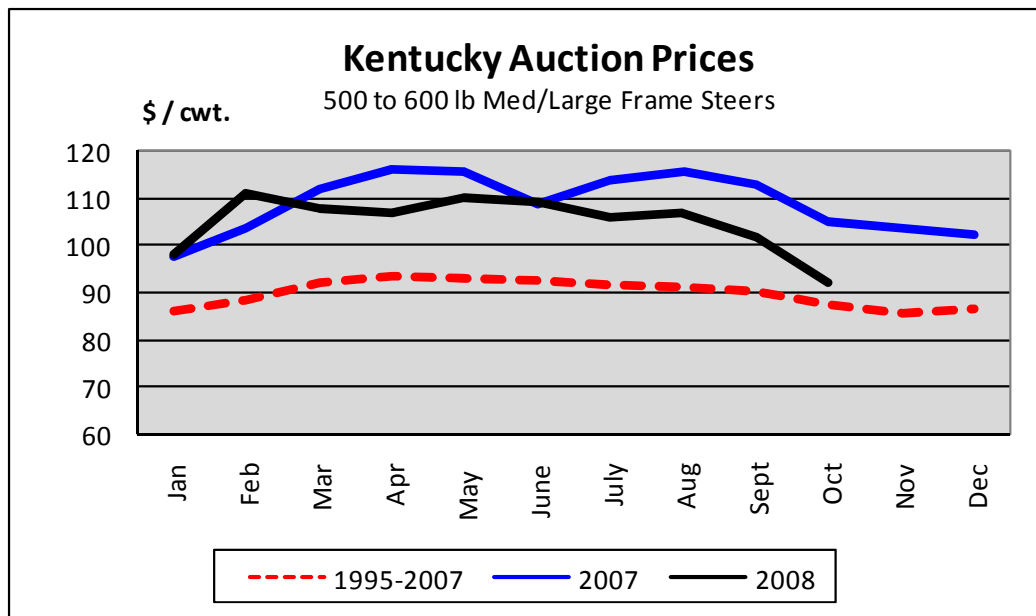


The 2007-08 wheat crop is expected to produce around 2.07 billion bushels, up from the previous year's production of 1.81 billion bushels. Wheat exports are expected to increase about 39 percent or about 356 million bushels, a result caused from low world wheat production and a lower U.S. dollar value. With increased exports, U.S. ending stocks are expected to be tight heading into the 2008-09 crop year.

2009 Outlook: Corn, soybean, and wheat prices are going to be influenced by global consumption, financial markets, energy markets, currency markets, and (particularly for soybeans and wheat) crop development below the equator.

For corn, the most significant factor affecting price is the decrease in ethanol price. Ethanol price from August to now has dropped around \$0.68 per gallon to \$1.66 per gallon. The drop in ethanol prices is attributed to the drop in crude oil prices.

For soybeans, prices over the next few months will be influenced by Brazilian and Argentine production. Currently, the size of the Brazilian soybean crop has been reduced by 92 million bushels. From the October projection Brazilian exports were reduced by 55 million bushels, whereas Argentine exports increased by 30 million bushels.



Livestock and Meats

Kenny Burdine & Lee Meyer

Meat Prices and Consumption

2008 Review: Meat consumption per person declined for the first time in more four years, dropping by 2% to 217 pounds per capita - in spite of a 3% increase in total meat production. This seeming contradiction occurred because of dramatic increases in beef, pork and poultry exports. More of the production went to overseas markets. Strong economies and a weak dollar strengthened demand and increased buying power.

This foreign competition added price pressure. Overall meat prices rose about 5% for the year, with beef up about 2%, pork at a record level and chicken prices up 6%.

2009 Outlook: Under pressure from high feed costs, the production of beef, pork and poultry are all likely to decline slightly around 1-2%. Export demand will stabilize with the globally weak economy and a stronger dollar. These supply factors will keep the pressure on prices, but weak consumer demand in the U.S. and declining transportation costs will help stabilize prices.

Cattle

2008 Review: 2008 was another tough one for beef cattle producers as both production costs and dry weather squeezed profit levels. Feeder cattle prices flirted with 2007 levels in the spring and summer, but fell dramatically into fall and winter. Talk of financial crisis, recession and layoffs forced the cattle complex to reassess where consumer demand was likely to be. The result was much softer than previously expected fed cattle prices. Even cheaper

corn wasn't able to offset this negative effect as feeder cattle prices followed the beef complex down.

While producers dealt with softer prices, they were also dealing with production costs higher than they had ever seen. Fertilizer likely had the largest effect as it impacts both pasture maintenance and hay production costs, but feed and fuel prices also remained high for most of the year. The net of all these factors was an incredibly challenging year that saw red ink flow for most beef cattle producers.

2009 Outlook: Despite the widespread pessimism and challenges that currently exist, most supply-side fundamentals are fairly positive for feeder cattle. Corn prices have dropped, cattle on feed numbers are below historical levels, and all indications are that we are decreasing the size of the U.S. cow herd. With so much uncertainty in the U.S. economy, demand will be the wildcard in 2009. It is our expectation that prices will rally from fall 2008 levels to spring of 2009. Price levels in 2009 will likely start the year below 2008 levels, but will be stronger in the fall on a year-over-year basis.

Dairy

2008 Review: Dairy producers enjoyed a slightly better year in 2008. Although fluid milk prices trended downward throughout the year, they will average only slightly below 2007 levels by year's end. The components that drive fluid value were mixed, but generally weaker.

Cheese started the year above 2007 levels, but was steady at best by summer. Non-fat dry and dry whey were both well off year ago price levels. Butter was the one bright spot as it tracked 2007's pattern very well until summer,

when it broke to the upside. The U.S. all milk price will likely average between \$18 and \$19 per cwt by the end of the year.

2009 Outlook: Growth in the U.S. dairy herd will likely slow in 2009 and so will the growth in milk production. However, milk demand will be affected by the same macroeconomic factors that are affecting all other livestock products and 2009 milk prices will have difficulty reaching 2008 levels. In Kentucky, it appears that dairy herd liquidation has continued and our state will begin 2009 with fewer than 90,000 milk cows in production.

Hogs

2008 Review: After a profitable 2007, 2008 turned into a losing year for the hog enterprise. Pork production increased by 7%, but prices actually increased because export demand offset the increase in slaughter. But the nearly 40% increase in production costs easily offset the higher prices, leaving the enterprise with substantial losses. The number of hogs in Kentucky showed signs of a turnaround starting the year with a 13% increase, compared to a 4% increase for the rest of the U.S.

2009 Outlook: Volatility in selling prices and production costs will mark 2009. Pork production is expected to decline. The number of sows is down about 3% and farrowings for late 2008 were down as well. The result will be a small drop in pork production.

Hog prices should start the year in the mid \$40s, (live weight basis) and increase to the \$55 to \$63 per cwt range during the middle of the year. A key factor will be exports. Pork exports were up 60% for 2008. Another large increase is virtually impossible. In fact, a small

decline is more likely as a stronger dollar increases the in-country costs to the importers.

Broilers

2008 Review: A 3% increase in production fed customers in other countries during 2008, as exports rose by 15% over 2007's level. However, the increased cost of feed, along with uncertainties on the demand side led to a small decline in production late in the year. Prices were up slightly from 2007, but not enough to offset the higher costs. The average price was just under \$0.80 per pound, and unusually stable for the year.

2009 Outlook: Late 2008 hatchery reports indicated a significant drop, probably about 5% in the broiler production for early 2009. Production may level out, with expected total 2009 production down about 2 percent. The drop in production is likely to be offset by a decline in export demand, which the USDA is forecasting to drop by 6 percent. Prices are likely to be near the 2008 level, but profitability should improve due to much lower input prices.

Sheep and Goats

2008 Review: Sheep numbers have stabilized in Kentucky. The USDA's estimate for 2008 was 37,000 head. The total U.S. sheep flock has also been somewhat stable, at just over 6 million head. By comparison the goat inventory continues to grow, but at slower rates than a few years ago. The USDA estimated that there were 81,000 goats in Kentucky and 2.5 million in the U.S. at the beginning of 2008.

Prices for both species have been stable as well. Lamb prices averaged about \$88/cwt for 2008, with a normal seasonal price peak in the middle of the year over \$110/cwt. Goat prices were not as high early in the year, but late in the year increased and sold over \$1.10 per pound (40-60 lb. Selection 2 kids) at Kentucky markets.

2009 Outlook: More than half of both lamb and goat meat consumed in the U.S. is from imports – primarily from Australia and New Zealand. A stronger dollar will raise the cost, supporting demand for the domestic product. Production levels for 2009 are likely to see little change from 2008, so supply should not have much of a price impact. However, the weak economy will impact consumer incomes and could lead to slightly weaker prices, especially for lamb.

Horticulture

Tim Woods

2008 Review: The value of all horticulture cash receipts in 2008 is projected to be \$115 million, with floriculture, nursery, greenhouse, and sod (\$81), and all produce (\$34). This is up from \$110 million in 2007 and \$68 million ten years ago. Industry growth has been steady. Gross produce receipts rose slightly in 2008 as producers benefited from more direct market channels, especially farmers' markets, and an outstanding fruit production and marketing season. Over 2,000 vendors sold in farmers markets in 2008, with additional growth observed in the produce auctions, restaurants, wineries, and other wholesaling. A weaker overall economy and relatively slower housing starts led to modest overall declines for Kentucky's green industry.

Commercial Vegetables

Kentucky has more than doubled cash receipts from vegetables over the last ten years. Total vegetable acreage for 2008 should wind up around 10,500 acres, up 17% over 2007 and up 45% from the level reported in the 2002 Ag Census. A significant amount of commercial marketing has continued through private wholesale arrangements. Direct marketers continued diversifying product offerings to meet strong demand for locally grown products, while wholesale vegetable prices were exceptionally strong across all crops during Kentucky's season. Volume of vegetables marketed through auctions, CSA's, on-farm retailing and to restaurants increased in 2008. Over 350 producers sold through the produce auctions in 2007 and the total will be higher again for 2008.

Commercial Fruit

Tree fruit growers overcame generally dry conditions to report good apple quality and an outstanding fall festival season. Apple and peach yields reached near record levels for Kentucky, while prices remained very strong as supplies declined from the Great Lakes. Berry growers continued to increase acreage, utilizing more value-added and local grocery sales. Kentucky wineries report purchasing more local grapes in 2008 and bottling more wine. Grape sales make up a growing component to the \$10 million total fruit sales. Registered wineries have grown from five in 2004 to 44 in 2008. Vineyard and winery expansions are continuing, according to our recent survey, increasing the need for improved planting coordination.

Green Industry

The green industry nationwide is fueled by new home construction and healthy consumer spending, obviously off substantially in this slow economy. This sector grew rapidly between 2002-06, with growth leveling out, but then dipped sharply this year. Wholesalers, garden centers and landscaping firms have all faced challenges across the country.

2009 Outlook: The outlook is fairly bullish for commercial fruit and vegetable production in Kentucky for 2009. Forty-seven percent of growers surveyed in 2008 indicated they expected to see their produce sales increase somewhat over the next three years. This held true for growers primarily involved in direct markets, wholesale, and direct to retail markets. Auction and independent grower-shipper wholesale sales will likely again increase. Gross sales will continue to be driven by higher-value direct marketing at farmers' markets, directly off the farm and to foodservice. Overall vegetable acreage will likely expand along with new interest in small fruit and orchard crops based on profitability in 2008. Higher-value market channels should keep sales steadily increasing.

New grape and berry plantings continue to reach fruiting age. There are approximately 500 bearing acres of wine grapes in Kentucky with new plantings going in. Wine production is expected to continue its increase in 2009 as more wineries come into production. There is plenty of room for growth in local markets for berries.

Nursery/Greenhouse

Green industry growth could be hampered by higher energy costs and continued housing market slowdowns in 2009. While well-managed firms will weather tighter profits, smaller firms could face exit or consolidation. Several larger, high technology systems have been developed that have contributed substantially to the wholesale dimension of the business in Kentucky. Service-oriented firms, like landscapers and retail centers, however, may be better positioned for growth in 2009.