2018 – 2019 Kentucky Agricultural Economic Situation and Outlook
University of Kentucky College of Agriculture, Food and Environment

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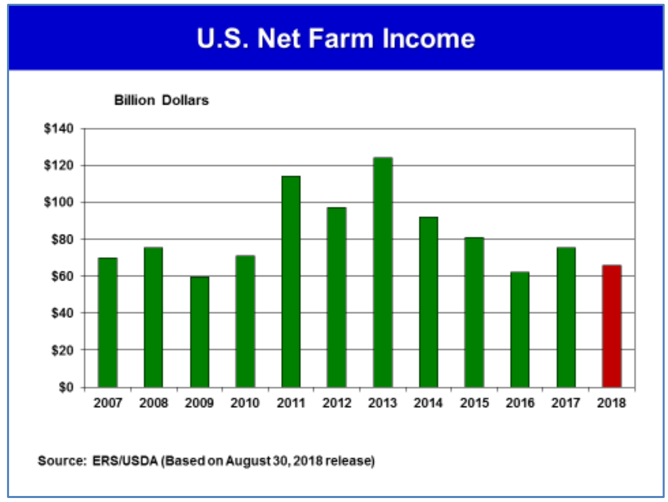
U.S. Agricultural Economy

The U.S. agricultural economy continues to be challenged, following an unprecedented/record breaking period of growth during 2007-2013. In August, USDA projected net farm income to total $65.7 billion in 2018, down $9.8 billion (-13%) relative to 2017. Adjusted for inflation, USDA's estimated U.S. net farm income level for 2018 would only be slightly higher than 2016, which represented the lowest level since 2002. USDA will be updating their 2018 forecast on November 30th, reflecting revised price and yield projections, crop losses from recent hurricanes, along with trade-payments made from the Market Facilitation Program (MFP). After accounting for these factors, U.S. net farm income will still likely be near 50% below the record level established in 2013.



The August USDA farm income estimates predicted that 2018 U.S. ag cash receipts will remain relatively stable in 2018 in response to improved poultry and wheat sales, offset by lower corn, soybeans, dairy, cattle, and hog receipts. After falling two out of the past three years, production expenses are expected to increase by 3.3% in 2018, due to higher labor, fuel, and interest costs. Government farm payments, which generally accounts for approximately 10 to 20% of net farm income, will reflect lower 2018 farm bill-related payments, but will account for the portion of the $4.6 billion of MFP payments paid in 2018.

Despite a higher valued U.S. dollar and all the trade tension this past year, U.S. ag exports actually increased 2% in FY 2018 (which ended September 30, 2018) on the heels of strong corn (+17%), and meat exports (beef +16%, poultry +7%, dairy +5% and pork,+3%) exports, offsetting lower soybeans exports (-8%). Canada replaced China as the leading destination for U.S. ag exports, followed by Mexico, China, EU, and Japan. Undoubtedly the strong export market, fueled by a robust global economy, helped support ag prices in 2018 in the midst of abundant global supplies.

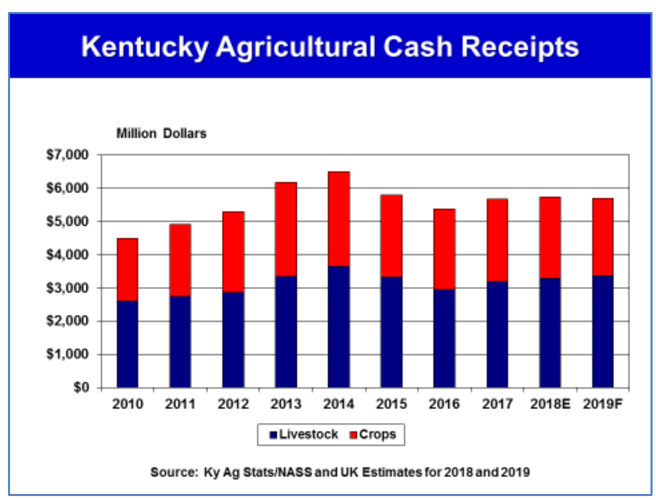
Without a major supply shock, prices for most ag commodities will likely remain relatively low in 2019 in response to abundant global grain supplies, growing meat supplies, and an uncertain trade environment. Export growth will be constrained by a slowing global economy and an anticipated stronger U.S. dollar. While welcomed by U.S. agriculture, the U.S. Mexico Canadian Agreement (USMCA) will not likely result in an immediate boost to U.S. ag trade in the region given retaliatory tariffs still being assessed. Plus the USMCA, which must be ratified by Congress, still faces political challenges following the 2018 U.S. midterm elections. The Trump administration has now turned to developing bilateral trade discussions with other important ag export markets like Japan and the EU to boost future U.S. ag exports.

Amidst a prolonged dip in the farm economy, ag lenders are beginning to observe financial stress among some of their customers. Relatively low interest rates (along with cash purchases) initially constrained growth in farm debt levels, and also provided support to land values in the early years of the recent downturn in the U.S. ag economy. While farm asset values remain surprisingly strong, continued low commodity prices are causing cash flow/liquidity challenges for many producers, forcing increasing operating loan activity. Despite the slumping farm economy, the overall balance sheet for U.S. agriculture as a whole still remains relatively strong compared to the farm crisis days of the early 1980s, but financial conditions are deteriorating in the midst of anticipated higher interest rates and continued low crop and livestock prices.

Besides monitoring trade policy developments, U.S. agriculture will be watching what evolves within the farm bill, immigration debate, crop output in South America, and actions by the Federal Reserve in the coming year. Food price inflation has once again increased modestly in 2018 (+1%) and is expected to remain below historical annual levels (+2.5%) in 2019 as consumers benefit from intense competition in the grocery sector, abundant ag/food supplies, and continued food marketing efficiencies and innovations. However, disruptions in trade flows among food importers could begin to creep into U.S. food prices if trade tensions accelerate.

Kentucky's Agricultural Economy

The University of Kentucky's Department of Agricultural Economics is forecasting that Kentucky ag cash receipts will be relatively stable in 2018 at $5.7 billion, matching last year's level, but well below the record $6.5 billion in 2014. Higher yields for most crops, except tobacco, along with continued strength in equine and poultry markets, helped offset lower soybean and dairy prices. Gains are expected for horses (+10%), poultry (+3%) and soybeans (+7%), while losses are anticipated for dairy (-15%), wheat (-15%), hogs (-9%) and tobacco (-6%). Despite modest expansion and competition from other meats, cattle prices and value remained relatively flat in response to strong export markets for beef.



Poultry will likely remain Kentucky's number one ag enterprise, accounting for 21% of projected 2018 sales, followed by equine (18%), soybeans (15%), cattle (13%) and corn (12%). For 2019, Kentucky ag cash receipts are expected to be remain around $5.6 to $5.8 billion with continued strength in the equine and poultry markets offsetting anticipated losses for soybeans, tobacco, and cattle. Look for continued growing demand for local produce/meats and value-added agriculture, with a slowing U.S. economy constraining greenhouse/nursery sales.

Kentucky's net cash income declined from averaging $2.3 billion during the boom period of 2011-2014 to averaging $1.8 billion over the past three years. Farm income in Kentucky has held up better than national trends given our mix and diversity of agriculture and above average grain crop yields. Kentucky farmers will receive approximately $100 million in 2018/19 for the first round of MFP payment funding, which help counter declines in farm-bill (ARC and PLC) payments. Like the U.S., trade developments and weather will dictate the direction of Kentucky farm income for the upcoming year.

Selected Commodity Profiles

Cattle-- Despite higher production levels across all three major meats, cattle prices managed to hold relatively steady for 2018. A strong economy and impressive export levels (despite trade issues) both worked to somewhat offset the supply challenges. Frequent rain created some challenges, but also resulted in good forage growth through summer and fall for much of Kentucky. Calf prices for the year actually averaged about $8 per cwt higher than 2017; heavy feeder cattle prices were virtually changed. While there are signs that cow-herd expansion may be slowing, expect an increase in beef cow numbers for 2019. This, coupled with another round of production increases for pork and poultry, suggests lower prices for cattle year-over-year for 2019. Look for a seasonal increase in prices during the spring, but expect prices by fall 2019 to be below fall 2018 levels.

Poultry--The poultry sector continues to grow in Kentucky as receipts are forecast to approach $1.2 billion for 2018. Broiler prices spent most of the spring and summer above 2017 levels, but did fall sharply from late summer to early fall. This decline is seasonal, but the drop in 2018 was sharper than usual. All indicators are that the sector will continue to grow in Kentucky in 2019.

Hogs-- With pork production up nearly 3% for 2018, hog prices came under pressure, averaging around $60 per cwt in the Eastern Cornbelt on a carcass weight basis. This represents more than a $5 per cwt decrease from 2017, and is likely near, or below, production costs for most operations. Looking ahead to 2019, another sizeable increase in pork production is expected as hog inventory continues to grow at the national level. Trade will be an especially important factor for hog prices as over 20% of U.S. pork production is typically exported.

Equine-- Kentucky equine receipts continue to show strength and should exceed $1 billion for 2018. A relatively strong economy and another Triple Crown winner likely supported both sales and stud fees for 2018. The Keeneland September yearling sale was up more than 20% from 2017. It is likely that this strength will continue into 2019.

Dairy-- Kentucky dairy cow numbers were estimated by USDA to be flat from January 2017 to January 2018, but have certainly declined during this year. Many producers were impacted by loss of contracts with Dean's and all were impacted by unattractive margins. Farm level milk prices for the year were down more than $1.50 per cwt from 2017. Prices are forecast to improve slightly, especially in the second half next year, but margins will still be very challenging.

Corn—U.S. planted area and harvested area of corn declined by 1.1 and 0.9 million acres, respectively, from 2017. The potential record yield of 178.9 bushels/acre produced a Kentucky corn crop totaling 14.6 billion; however, smaller carry-in offsets the larger crop and reduces supply from last year. Strong domestic and export use is projected to reduce stocks to an 11.5% stocks-to-use ratio. The U.S. marketing-year average farm price for 2018/19 is pegged at $3.60/bushel up $0.24 per bushel from 2017. Currently, USDA projects 2019 corn area to increase by 2.9 million acres from 2018, with an updated estimate to be released in February 2019.

Soybeans—U.S. planted and harvested area of soybeans declined by 1 and 1.2 million acres, respectively, from 2017. The potential record yield of 52.1 bushels per acre provides a record U.S. soybean production of 4.6 billion bushels. Total use is projected to fall by 189 million bushels because of reduced exports with China. Ending stocks are forecast to increase to a record 955 million bushels and the largest stocks-to-use ratio since 1985. The U.S. marketing-year average farm price for 2018/19 is projected at $8.60 per bushel. Currently, USDA expects 2019 soybean area to decrease by 6.6 million acres from 2018.

Wheat-- U.S. wheat planted and harvested increased by 1.8 and 2.1 million acres, respectively, from 2017. Harvested yield also increased from last year to 47.6 bushels per acre. The larger 2018 wheat crop was partially offset by a smaller carry-in and reduced imports. Total use is projected to increase from 2018 with exports driving the increase. The strong demand is expected to reduce stocks to below a stocks-to-use ratio of 43.7%. Reduced stocks will support a higher U.S. marketing-year farm price of $5.10 per bushel. USDA projects 2019 wheat area to increase by 3.2 million acres from 2018. The delayed corn harvest and wet fall weather may reduce this amount.

Tobacco-- Slumping demand/contract volume coupled with an extremely poor growing season resulted in a significantly lower burley crop. Beltwide 2018 marketings may struggle to exceed 100 million pounds, compared to over 140 million pounds in 2017. In the midst of declining global demand for burley, world burley production was up by 15%. Overall demand for U.S. burley may only total around 100 to 110 million pounds given declines in domestic cigarette sales (-4 to 5%) and burley leaf exports (-5 to 7%). After two decades of growth, sales of snuff show signs of leveling off, hindering dark tobacco demand. E-cigarettes/vaping products, which contain virtually no U.S. tobacco content, continue to take market share away from traditional tobacco products. Cigarette manufacturers continue to invest in new reduced risk tobacco products, although the leaf content of these products likely contain limited amounts of U.S. leaf. Tumbling U.S. burley demand, and slowing snuff sales will likely lead to additional reductions in contract volume for 2019. The value of Kentucky tobacco production may struggle to exceed $300 million in 2018 compared to averaging $366 million over the past ten years. Given the current outlook, labor/regulatory challenges, product demand changes, and tighter margins, look for continued concentration in the number of Kentucky farms growing tobacco in 2019.

Fruits, Vegetables and Greenhouse-- Generally favorable growing conditions in 2018 led to expansion of local produce supply out of Kentucky. Market shortages in 2017 played strongly to Kentucky's favor. Prices were generally back near typical regional prices leading to slightly lower overall revenue for fruit and vegetable growers. The 2018 estimate of $48 milllion in produce sales is made up substantially of farm market and other direct to consumer sales, contributing around 40 to 50% of the total. The nursery industry benefitted from an 11 year high in housing starts in early 2018, but has since been adversely impacted by higher interest rates. Consumer spending, which also increased sharply in 2018, is expected to slow somewhat in 2019, constraining the growth in sales.

Forestry-- The forestry sector has been stable in 2018 contributing a total of $13.2 billion to Kentucky's economy. Upward price trends for white oak stave (barrel) logs and railway tie logs are predicted to continue into 2019. Rapid log exporting to China has flattened. The third and fourth quarters have seen a decline black walnut, red oak, and ash. Downward pressure on log prices for red oak and ash due to tariffs and sluggishness of China's economy have been countered by wet weather, keeping log inventories low, and prices stabilized. It will be early spring before which of these countering forces will prevail. Declines in housing starts will likely depress domestic demand for oak, hickory and yellow-poplar leading to stable stumpage prices in 2019.

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