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Grain Marketing October Market Update - October 16, 2000



by Steve Riggins,
Grain Marketing Specialist

The October "Crop Production" and "World Agricultural Supply And Demand Estimates" (WASDE) reports by USDA contained a lot of well anticipated news and a few important items of unanticipated news.

As expected, USDA cut its estimate of U.S. average corn yield. Yield was dropped from 141.8 bu/acre to 139.6 bu/acre (still a record yield) while harvested acreage for corn was reduced from 73.1 million acres to 73 million acres. This resulted in an October projection by USDA of 10.192 billion bushels of corn for harvest this fall, a drop of 170 million bushels from the September number. It appears that most corn market watchers expect USDA to further lower the production estimate, at least slightly, in the November report. Also as expected, USDA cut its estimate of Chinese corn production for this year from 115 million metric tons (mmt) to only 105 mmt, a cut of about 390 million bushels. Additionally, USDA lowered its



forecast even further for U.S. sorghum production this year. Sorghum production is now pegged at 465 million bushels compared to last year's 595 million bushels.

These changes, in combination with the recently released "September Grain Stocks Report", set the stage for a very friendly surprise for market bulls contained in the WASDE. Traders were expecting total corn supplies for the 2000-01 marketing year to be reduced from last month's report, but they were not expecting a 200 million bushel increase in projected disappearance of U.S. corn to be revealed in the October numbers. The net effect of the supply and demand changes was to drop USDA projected ending stocks of U.S. corn for next August 31 by 425 million bushels compared to its September projection. Stocks are now listed at 1.817 billion bushels for the end of the 2000-01 marketing season. This is still an increase of 100 million bushels in carryover stocks compared to the just concluded 1999-2000 crop marketing year. However, it is much less than was anticipated just a few short weeks ago and several market participants seem to think the U.S. crop will still shrink somewhat from the October estimate. Finally, with total disappearance now projected by USDA at an incredible 10.1 billion bushels this may not be a very burdensome stock level.

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Market focus is quickly beginning to shift to the demand side of the price equation. Market traders will now require evidence that USDA's projected record disappearance, up 800 million bushels in just two years, is achievable. U.S. corn exports are projected at 2.275 billion bushels, the 4th best ever, and nearly 44 million bushels/week on average. Farmers need to keep track of the weekly export inspection report and the weekly export sales report. These reports need to validate the USDA's robust total annual export projection or the market will come under pressure. For domestic demand, market participants will have to wait for release of the 1st Quarter Stocks Report, January 2001, to get some idea if record feed, food and industrial uses are on target through the first quarter of the 2000-01 marketing year.

As expected, USDA also cut its projection of soybean production in the U.S. and increased its projection for soybean production in South America for the 2000-2001 soybean marketing season. The unexpected news for soybean price outlook was a drop in projected domestic crushing of U.S. soybeans by 15 million bushels (lower exports of soybean meal) and a 35 million bushel drop in projected U.S. export of whole soybeans. The net effect of the changes on the October soybean WASDE was to leave projected soybean carryover stocks unchanged from the September WASDE at 365 million bushels and 77 million bushels larger than stocks left at the end of the just concluded 1999-2000 year. With the U.S. heavily into harvest of a record soybean crop now pegged at 2.823 billion bushels the market headed lower.



The "good news" for wheat in the USDA's October numbers was a 63 million bushel drop in estimated U.S. production this year and an increase of 25 million bushels in wheat feeding compared to the September WASDE. Additionally, at the world level, USDA lowered its projection for wheat production in Canada and Australia while listing very slight increases in projected wheat production in Kazakstan and North Africa. Projected ending world wheat stocks are now listed at 111.39 mmt for the 2000-01 year compared to world ending stocks of 128 mmt last year and 136 mmt two years ago. World wheat stocks compared to global wheat use is only 18.7 percent, the tightest on record and slightly below the 19 percent figure recorded in both 1995-96 and 1996-97.



Dry weather in the plains coupled with the above price supporting news has provided support to wheat prices over the past several days. Price strength has been tempered by where the world wheat supplies are held, the exporting nations, and by the size of stocks these countries possess. However, given the tight world stocks to use ratio and finally some slight drop in projected U.S. ending wheat stocks it seems likely there should be some marketing opportunities for the 2001 wheat crop between early winter and about April 15 next year. Farmers should understand that U.S. wheat stocks are still large relative to use and to recent history and should not form unrealistic price expectations. It should take a significant weather problem in one of the major wheat exporting nations to produce prices above \$3.50.

For "old-crop" corn and soybeans, farmers should study their basis data from the past two crop marketing seasons. Just because the crop is in the bin doesn't mean

the marketing job is finished. If this year is anything like the past two seasons much of the basis gain will be over with by late November. This doesn't mean that storage will no longer be profitable, but it may mean that it is more efficient to own the crop in a different form.

For 2001 crop corn and soybeans, farmers should make their initial marketing price targets and have a plan ready to act on. It is easier to change a positive market action when market conditions turn out differently than expected than it is to attempt to overcome a non-marketing decision.

Tax Planning — A Must

*by Rick Costin and Darwin Foley,
Area Farm Business
Management Specialists*

In 1999 many farmers were surprised when the year ended and their tax preparer informed them of the amount due for 1999 income tax. With income tax planning before year end, the liability will not be a surprise and in many cases can be managed and reduced.



In 2000 income tax liability for many farmers has the potential of being much larger than what they realized in 1999. With larger corn and soybean yields for most grain producers along with government payments, tobacco money for TLAP and Phase II, and higher hog and cattle prices, net farm income could be high!

After completion of tax planning, farmers should consider all possibilities available to them. Assuming tax liability is too high, some strategies might be:

(1) Prepay by purchasing a specific quantity of fertilizer, seed, chemical, feed, and/or other expendables at a specific price.

(2) Capital purchases/investments to expand an existing enterprise or start a new enterprise.

(3) Postpone sales until after the first of your tax year.

(4) Make sure FICA tax deposits are current.

These strategies are not the only strategies that a Kentucky farmer might consider when he has extra farm income and high tax liabilities. They are simply some possibilities. When planning strategies the goals of the farmer and farm family, along with the current financial position of the farm business is very important in making decisions.

Swine Contracting

by Suzy Martin,
Area Farm Business
Management Specialist

The traditional form of hog production over the years has been for producers to independently raise the animals, make all management decisions and provide the resources necessary for production by themselves. However, technological and industry changes over the past few decades have drastically altered hog production. Small independent producers are struggling with ways to remain competitive within the industry. One avenue producers have explored is contract production. There are two basic types of hog



contracts. They are production contracts and marketing contracts.

Production contracts are generally contracts where the producer does not own the animals. The producer will provide the land, labor and buildings necessary to raise the hogs and will be compensated based on some absolute performance standard. Various payment programs could include number marketed, number weaned, pounds gained, etc. Additionally, bonuses and penalties often apply to those measures which the grower can influence (i.e., feed conversion and mortality). Production contracts often include farrowing contracts, finishing contracts or even farrow-to-finish contracts.

On the other hand, marketing contracts are agreements between a producer and packer for future delivery of hogs. Generally the producer agrees to sell a specified quantity of animals or percentage of production to the packer at various intervals throughout the year. Examples of marketing agreements are formula contracts, window contracts and costs plus contracts. The full array of contract possibilities, various arrangements, advantages and disadvantages are outside the scope of this article, but it is important to consider some of the general advantages and disadvantages when thinking about contracting.

The advantages for a producer entering into a contract agreement include a reduction in market price risk, income smoothing, relaxing of capital constraints, employment of idle labor resources, and access to technology. The disadvantages of contracting can be seen as a reduction in managerial control, an increased demand for record keeping, increased potential for disease, limited upside price

potential and small rewards for efficiency.

Regardless of the type of agreement entered, there are some points that need to be addressed prior to signing any agreement. First there should be a written agreement that specifically states the duration of the contract, termination clause, how and when payments will be received, and who has control over various managerial decisions. Furthermore how the animals will be marketed and the when and where of delivery should be considered. Additional attention should be made (when applicable) as to the quality of livestock supplied, feed quality supplied, the division of expenses, conflict resolution and renegotiation clauses.

Producers have varying skills, expertise, financial positions and attitudes toward risk. Therefore, what is right for one farmer may not apply to another. Some of the advantages described above may not apply to all farmers. In other words, contract production may not be for everyone. However, for those looking into the possibility, the points above are considerations that should be accounted for.



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