The Farm Economy Turns Down

By Mark Drabenstott and Alan Barkema

After more than four years of robust recovery, the farm economy turned down in 1991 and the slump seems likely to continue in 1992. Farm income slipped more than 5 percent due to a drop in livestock profits and just an average year for crop producers. The earnings slide came after farm income posted record highs in three of the past four years. Farmland values stalled in 1991 after four years of solid gains, further underscoring the end of the farm recovery.

Despite the backslide in 1991, the farm economy remains on solid financial footing. Farm balance sheets remain healthy after more than five years of high income and debt reduction. Most farm lenders have very few problem loans heading into 1992. And even though farm income may edge a bit lower, crop prices are improving and could soar if exports strengthen or bad weather cuts crop yields. Thus, U.S. agriculture seems likely to endure at least two years of downturn—but is well positioned to do so.

The Farm Downturn of 1991

The 1991 farm downturn was widely shared in U.S. agriculture, but livestock producers felt the biggest blow. Strong livestock prices were the main strength of farm income the past three years, so a sharp break in cattle and hog prices in late summer hit one of the pillars of the farm recovery. Crop producers, meanwhile, contended with a wet spring and dry summer but managed to harvest average crops overall. As farm income slipped and farmland values stalled, farm balance sheets weakened.

A sharp drop in livestock profits

The slump in livestock prices was a tale of supply and demand (Chart 1). Meat supplies rose 3 percent to a record high, while consumer

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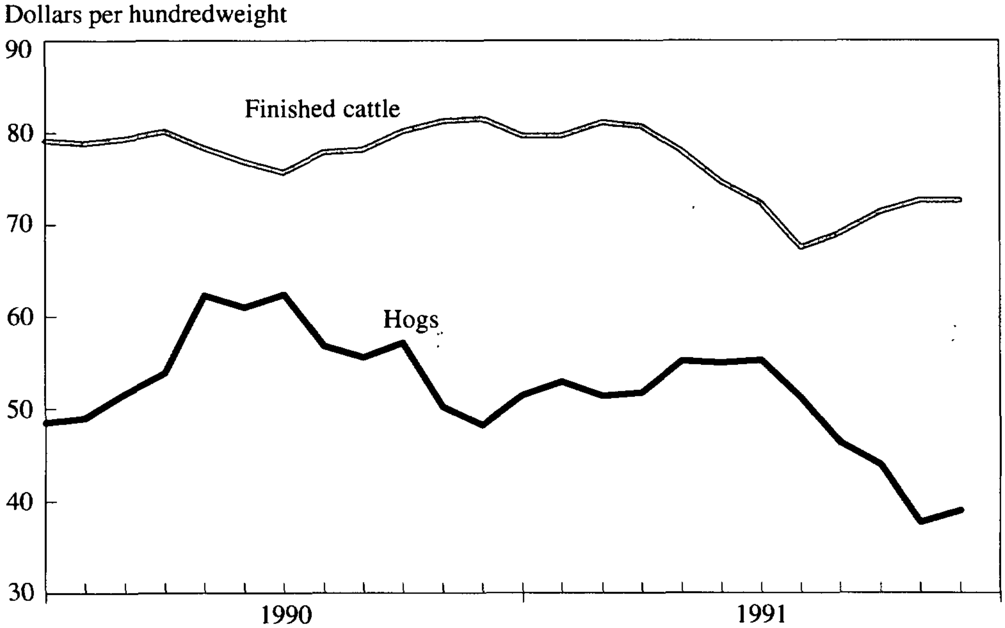
Chart 1
Livestock Prices



Source: U.S. Department of Agriculture, Economic Research Service.

demand weakened due to the recession. Consumers shopped for value, but per capita consumption still climbed to a record 215.6 pounds. The drop in cattle and hog prices was especially pronounced. An unusual surge in fed cattle marketings caused cattle prices to fall nearly 15 percent in August before recovering somewhat later in the year. Hog prices fell about a third from summer to fall as producers expanded production after two years of wide profit margins.

Beef production increased 1 percent in 1991 amid signs that producers were expanding the nation's cattle herd for the first time in many years. The main reason for the rise in beef output was that producers sent heavier cattle to market. In late spring, feedlot operators began holding back marketings, hoping for higher prices. Soon, a backlog of heavy cattle developed. Prices fell sharply in late summer as producers sent a large wave of cattle to market. By fall, the backlog had been worked off, and prices recovered somewhat. For the year as whole, beef carcass weights averaged almost 700 pounds, shattering the old record.

Year-average cattle prices fell in 1991, but not as much as the summer sell-off would suggest. Finished cattle prices climbed to a record high in the first quarter and remained fairly strong through most of the summer. Prices for choice steers at Omaha averaged \$75 a hundredweight, down \$3.50 from 1990 (Table

Table 1

U.S. farm product price projections

(December 11, 1991)

	Marketing years			
Crops	1989-90	1990-91*	1991-92†	Percent change
Wheat	$3.72/bu.	$2.61/bu.	$2.85-3.05/bu.	13.03
Corn	$2.36/bu.	$2.28/bu.	$2.20-2.60/bu.	5.26
Soybeans	$5.69/bu.	$5.75/bu.	$5.25-5.75/bu.	-4.35
	Calendar years			
Livestock	1990	1991*	1992†	Percent change
Choice steers	$78.56/cwt.	$74-75/cwt.	$73-79/cwt.	2.01
Barrows & gilts	$54.45/cwt.	$48-49/cwt.	$39-45/cwt.	-13.40
Broilers	$.55/lb.	$.51-.52/lb.	$.47-.53/lb.	-2.91
Turkeys	$.63/lb.	$.60-.61/lb.	$.56-.62/lb.	-2.48
Lamb	$55.54/cwt.	$53-54/cwt.	$49-55/cwt.	-2.80
Milk	$13.68/cwt.	$12.20-12.25/cwt.	$11.85-12.85/cwt.	1.02

* Estimated.

† Projected.

Source: U.S. Department of Agriculture, Foreign Agricultural Service, *World Agricultural Supply and Demand Estimates.*

1). High prices for feeder cattle and huge losses in the third quarter caused most feedlots to lose money in 1991.

Feeder cattle prices were surprisingly strong in 1991, making ranching one of U.S. agriculture's strongest performers for the year. Large financial losses in cattle feeding in the second half of the year pushed feeder cattle prices down only modestly because feeder cattle remained in tight supply. Prices for feeder steers at Oklahoma City averaged $93, up from $92 in 1990. Ranching profits have stayed strong for three to four years. A rise in cattle inventories in 1991, the first increase since 1982, suggests that ranchers are beginning to expand in response to the string of profits.

Pork producers expanded aggressively in 1991, boosting pork production 4 percent. Long anticipated, the expansion received a cool market reception. In July, before the expansion hit full swing, prices averaged more than $55 a hundredweight. By November, prices had fallen to just $38. For the year as a whole, prices for barrows and gilts at the seven major markets averaged $49, down more than $5 from the year before. Wide profits in 1990 turned into sizable losses by late 1991.

Poultry producers continued their lengthy expansion in 1991, as total poultry production grew 5 percent. Broiler output jumped 7 percent, while turkeys edged up 3 percent. Consumer demand remained strong for poultry

Table 2

U.S. agricultural supply and demand estimates

(December 11, 1991)

	Corn (bu.)			Feedgrains (mt.)		
	Sept. 1-Aug. 31			June 1-May 31		
	1989-90	1990-91	1991-92	1989-90	1990-91	1991-92
Supply						
Beginning stocks	1,930	1,344	1,521	65.9	45.5	47.7
Production and imports	7,528	7,937	7,488	222.3	231.9	219.9
Total supply	9,458	9,281	9,009	288.2	277.4	267.6
Demand						
Domestic	5,745	6,034	6,200	173.0	178.2	181.6
Exports	2,369	1,727	1,575	69.7	51.5	47.0
Total demand	8,113	7,761	7,775	242.7	229.7	228.6
Ending stocks	1,344	1,521	1,234	45.5	47.7	39.0
Stocks-to-use ratio	16.57	19.60	15.87	18.75	20.77	17.06

	Soybeans (bu.)			Wheat (bu.)		
	Sept. 1-Aug. 31			June 1-May 31		
	1989-90	1990-91	1991-92	1989-90	1990-91	1991-92
Supply						
Beginning stocks	182	239	329	702	536	866
Production and imports	1,927	1,928	1,967	2,060	2,773	2,020
Total supply	2,109	2,167	2,296	2,762	3,309	2,886
Demand						
Domestic	1,247	1,281	1,331	992	1,376	1,247
Exports	623	557	650	1,233	1,068	1,225
Total demand	1,870	1,838	1,981	2,225	2,444	2,472
Ending stocks	239	329	315	536	866	414
Stocks-to-use ratio	12.78	17.90	15.90	24.09	35.43	16.75

Note: Data represent millions of bushels or metric tons.

Source: U.S. Department of Agriculture, Foreign Agricultural Service, *World Agricultural Supply and Demand Estimates.*

products, as poultry increased its share of total meat sales to 44 percent. Nevertheless, large meat supplies overall and weak consumer income led to a fall in broiler prices. Prices at the 12 city markets averaged 52 cents a pound, down from 55 cents in 1990. Despite lower prices, broiler producers still made profits, thanks in part to moderately priced feeds. Turkey prices averaged 61 cents a pound in 1991, down 2 cents from the year before.

A mixed year for crop producers

A wet spring, dry summer, and early frost threatened crops in 1991, but ultimately production of most crops fell much less than expected. Periodic fears of a fall in production made prices volatile during the growing season. Those fears proved unfounded, however, and farmers harvested an average crop overall. Still, weather was unusually spotty across the farm belt, creating a quiltlike pattern of good and bad crops. Despite weaker farm exports, total U.S. grain inventories declined in 1991.

Wheat prices softened in the first half of the year but moved higher in the second half. U.S. wheat production plunged more than a fourth due to adverse weather and smaller acreage (Table 2). Such a fall in output normally leads to sharply higher prices, but large supplies of wheat worldwide limited the price advance. The European Community (EC) harvested a record wheat crop in 1991, and the Canadian crop was only slightly less than the 1990 record.

As 1991 wore on, U.S. wheat prices increased about a dollar a bushel. The rise was due to low U.S. wheat stocks, dry growing conditions for the 1992 winter wheat crop, and expectations of subsidized sales to the Soviet Union. Average farm prices for the 1990-91 marketing year that ended June 30 were $2.61 a bushel, more than a dollar lower than the previous year.

Feedgrain production fell 5 percent in 1991 due to spotty dry weather across the Corn Belt. The corn crop was 7.5 billion bushels, down about 6 percent from the year before. But demand also fell in 1991, swelling corn stocks to 1.5 billion bushels. Foreign demand was especially weak, as corn exports fell more than 600 million bushels. For the 1990-91 marketing year ended August 31, farm-level prices averaged $2.28 a bushel, down slightly from the previous year and the lowest in four years.

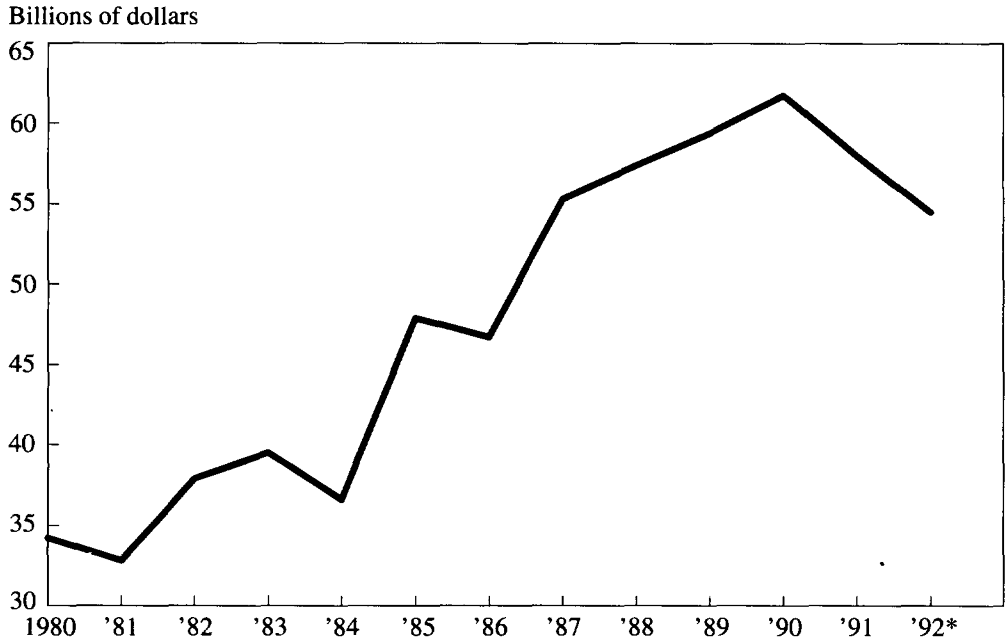
Soybean production in 1991 was unchanged from 1990, despite a dry summer and an early autumn freeze in the northern Corn Belt. Production netted 1.9 billion bushels for the third year in a row. Competing world supplies were quite large in 1991, while world demand was sluggish. Soybean prices shot up in midsummer when dry weather threatened the crop. But as evidence mounted that weather damage was much less than expected, prices eased through the fall harvest. For the 1990-91 marketing year ended August 31, farm prices averaged $5.75 a bushel, narrowly higher than the year before.

Farm financial conditions

Farm financial conditions worsened in 1991 for the first time in several years. The farm recovery that began in early 1987 had proven quite strong. Farm income was high and financial gains were broadly shared across different types of farms and different regions of the country. The recovery gave both farmers and lenders an opportunity to pay down debts while asset values rebounded. Thus, the 1991 downturn must be viewed against a backdrop of sizable financial gains during the farm recovery.

Farm income fell in 1991 due to a drop in livestock receipts and a mediocre year for crops (Chart 2). The extent of the drop, however, remains uncertain. The U.S. Department of

Chart 2
Net Cash Farm Income



* Forecast.
Source: U.S. Department of Agriculture, Economic Research Service, Agricultural Outlook Conference.

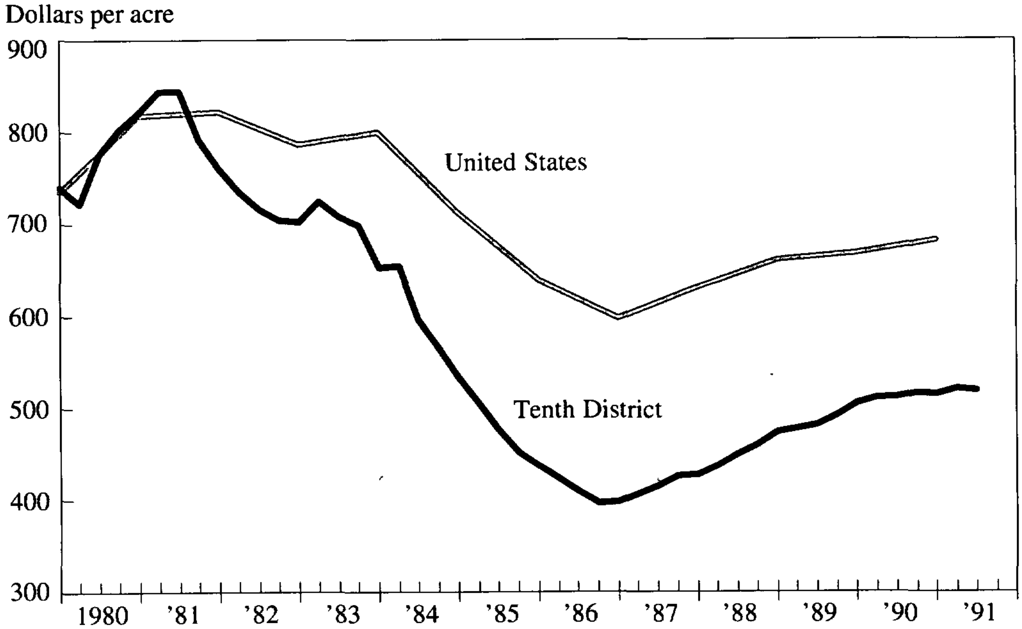
Agriculture currently estimates that 1991 net cash income—gross receipts for the sector less gross cash expenses—was $58 billion, a 6 percent decline from a record $61.8 billion in 1990. If the $58 billion income estimate holds, it would mark agriculture's third-best year ever.

But the current income estimate may not fully describe the softening that occurred in the Midwest farm economy. The USDA estimate includes a strong 14 percent jump in sales of fruits, vegetables, and horticultural products—all products of little importance to the Midwest.[1] Livestock losses in the last half of the year were an important factor to the Midwest, and the size of those losses is still being counted. Finally, the 1991 income estimate may have been boosted by a dollar-a-bushel advance in wheat prices in the second half of the year. Anecdotal evidence suggests, however, that the rise has not yet helped producers' incomes. Many farmers sold at harvest, before prices rose. Those that held on to their crop postponed sales to 1992 for tax reasons or because they thought prices would move even higher. Overall, 1991 farm income could turn out weaker than currently estimated. Moreover, midwestern farms appear to have suffered a greater income decline than national indicators suggest.

Farm asset values stalled in 1991 after more than four years of solid advances (Chart 3). During the first three quarters of 1991, farmland values in the Tenth District increased a meager

Chart 3

Farmland Values



Sources: U.S. farmland values from U.S. Department of Agriculture, *Agricultural Outlook;*
Tenth District land values from Federal Reserve Bank of Kansas City, *Agricultural Credit Survey.*

1.4 percent, less than half the gain in the same period the year before. Most of the gain came early in the year, as land values stayed essentially flat in the second and third quarters. At the end of the third quarter, values were up about a third from the market low at yearend 1986.

Reflecting sluggish land values, the farm balance sheet softened in 1991 (Table 3). For the nation as a whole, farm assets increased slightly more than 1 percent, while debt was essentially unchanged. Farm net worth, therefore, edged up a little more than 1 percent. After adjusting for inflation, however, net worth actually slipped about 3 percent. The sector's debt-asset ratio edged down to 16.2 percent, the lowest since the mid-1960s.

A Lackluster Year Ahead

The downturn in the farm economy that began last year will continue in 1992. A sluggish export market may limit gains in crop prices, despite crop inventories that are quite small by historical standards. And livestock prices will stay well below the record levels of recent years due to a slow recovery in consumer demand and expanding supplies of beef, pork, and poultry. The dim outlook for crops and livestock signals a further decline in farm income in 1992. Nevertheless, agriculture's balance sheet remains in sound condition after more than four years of solid gains.

Table 3

Farm balance sheet excluding operator households and CCC loans on December 31
(Billions of dollars)

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
Assets												
Real estate	785.6	750.0	753.4	661.7	586.1	542.2	578.6	599.4	605.1	614.4	624	630
Nonreal estate	197.2	195.1	190.6	195.4	186.5	182.4	194.2	205.6	214.6	220.2	221	226
Total assets	982.8	945.1	944.0	857.1	772.6	724.6	772.5	805.1	819.7	834.6	845	855
Liabilities												
Real estate	98.8	101.8	103.2	106.7	100.1	90.4	82.4	77.6	75.3	73.4	73	74
Nonreal estate	83.6	87.0	87.9	87.1	77.5	66.6	62.0	61.7	61.8	63.1	64	65
Total liabilities	182.4	188.8	191.1	193.8	177.6	157.0	144.4	139.4	137.1	136.5	137	139
Proprietor's equity	800.4	756.3	752.9	663.3	595.0	567.6	628.1	665.8	682.6	698.2	708	715
Debt-to-asset ratio	18.6	20.0	20.2	22.6	23.0	21.7	18.7	17.3	16.7	16.4	16.2	16.3

Note: Figures represent billions of dollars. Figures for 1991 and 1992 are forecast.
Source: U.S. Department of Agriculture, Economic Research Service, *Agricultural Outlook.*

Farm income and financial conditions

Weaker farm income is likely again in 1992 (Chart 2). While income will be down overall, the outlook is somewhat brighter for crop producers than for livestock producers. Tighter grain inventories promise to support prices and income for grain producers, while pushing up feed costs for livestock producers. Profit margins in the livestock industry will tighten further as a surge in red meat and poultry production pushes down livestock prices. Meanwhile, the cost of farm inputs will continue to creep up, boosting production costs 1 to 3 percent. Together, steady farm receipts and slightly higher expenses could push down net cash income to a range of $52 to $57 billion, about 6 percent below the 1991 level.

The two-year downturn in farm income may dampen gains in farmland values. Sharply lower interest rates have pushed down rates of return on most financial assets and focused attention on farmland as an alternative investment. Nevertheless, as 1991 ended, gains in farmland values had slowed to a crawl. Some regions may see further modest gains in farmland values, especially for high-quality land that has remained in strong demand. But values will be flat to down in other regions. Overall, land values are not likely to keep pace with inflation in 1992.

Farm credit conditions will probably weaken in 1992. Interest rates on farm loans may edge down further as the heavy spring borrowing season approaches, following declines in interest rates in national money markets late in 1991. But with farm income eroding, farmers will borrow more cautiously. Farm loan demand will probably remain slack, leaving agricultural lenders with a surplus of loanable funds and continued low loan-deposit ratios. Weaker income may also tighten farm liquidity, slowing repayment rates on farm loans. Thus, farm lenders may struggle to maintain the strong earnings recorded in recent years.

Food prices outlook

Food prices should rise only slightly in 1992. Modest increases are expected in processing, packaging, and distribution costs—which account for about 70 percent of retail food costs—as inflation slows in the national economy. A sluggish economic recovery will also limit growth in consumer income, holding food demand in check.

Meanwhile, record large supplies of red meat and poultry will push down prices at the meat counter. Fresh fruit prices may also ease, as production in California continues to recover from its crippling freeze in December 1990. But other food prices may creep up. A serious whitefly infestation promises to cut yields of fresh vegetables in California, Arizona, and northern Mexico, boosting prices this winter. And dairy product prices will rise modestly in the year ahead, now that the glut of milk that pushed down dairy prices last year has passed through the market.

Overall, food prices are likely to rise 2 to 4 percent in 1992. The rise is about equal to the 3 percent increase last year but is well below the nearly 6 percent annual increases in 1989 and 1990.

Farm policy outlook

The year ahead may be uneventful for domestic farm policy, but it may be critical internationally. The Uruguay Round of talks under the General Agreement on Tariffs and Trade (GATT) is scheduled to end in 1992, one way or another.

The Round collapsed in December 1990, when the European Community rejected proposals for cutting agricultural subsidies. Negotiations were essentially suspended in early 1991 as Congress weighed whether to extend fast track authority, originally set to expire in June 1991. Fast track authority limits Congress to a thumbs-up, thumbs-down vote without opening the agreement to amendment. After long deliberation, Congress extended fast track authority for two years. Notwithstanding that time span, GATT principals have agreed to end the Uruguay Round in 1992, with or without an agreement.

Agriculture will determine the success of the Uruguay Round, despite brighter prospects for agreement on other trade issues. The Round appears to be nearing success in achieving path-breaking agreements on services and intellectual property—both issues of critical importance to the United States.[2] But the inability of the EC and the United States to reach an acceptable compromise on farm trade still threatens the entire Round.

The EC and the United States have generally agreed that reductions in three kinds of trade-distorting farm policies are needed: export subsidies, domestic farm subsidies, and import barriers. Last November, a compromise appeared close at hand that would cut export subsidies 35 percent and farm subsidies and import barriers 30 percent over five or six years. But the negotiators have been unable to agree on how to achieve those reductions.[3] The EC favors cutting budget outlays, while the United States favors cutting the quantity (or tonnage) of subsidized farm exports. Another sticking point in the negotiations is that the Europeans want to "rebalance" tariffs if they agree to any reductions. Rebalancing would require new tariffs on U .S. soybeans and corn gluten feed entering Europe, products that now enter the EC duty free. The United States, of course, resists the new tariffs.

Thus, after five years of exhaustive negotiations, the Uruguay Round seems more likely to end with a whimper than a bang. If a compromise on farm subsidies and trade is struck, it is likely to bring only modest benefits to U.S. agriculture, and the benefits will unwind slowly. But a compromise on farm trade may pave the way to meaningful agreements on other important trade issues.

Export outlook

Exports of U.S. farm products may rebound slightly in 1992 after falling last year. The outlook for exports of red meat and poultry—about a seventh of all U.S. farm exports—is relatively bright. Sales of U.S. beef and pork to Mexico and the Pacific Rim nations, especially Japan and South Korea, are expected to climb steadily in 1992. Stronger exports to the Middle East, Japan, and Mexico could boost broiler exports to a new high. Overall, red meat and poultry exports may climb 5 percent in 1992.

Exports of U.S. grains and oilseeds—about three-fifths of all U.S. farm exports—may strengthen slightly in 1992. Higher export volume and higher prices will boost U.S. wheat exports. And exports of soybeans and soybean products will be much stronger due to last year's poor crop in South America, a major competitor in the world market. But weak corn exports will offset much of the gains in wheat and soybean sales.

The disintegration of the Soviet Union accounts for much of the overall sluggishness in U.S. grain exports. During most of the past two decades, the Soviet Union was a leading buyer of U.S. grain. But during the past two years, the Soviet Union became a credit-only customer as its economy fell apart. With Ukraine and other Soviet republics opting for independence from the central government, the disintegration of the Soviet Union now seems assured.[4]

Exports to the Soviet Union will depend on credit backed by the U.S. government. Since December 1990, the United States has granted export-credit guarantees backing the sale of about $3.75 billion of U.S. farm products—primarily grain—to the Soviet Union.[5] The last $1.25 billion of credit, announced last November 20, will be allocated in four increments: $600 million immediately, $200 million each on February 1 and March 1 of 1992 and $250 million on April 1.

Whether additional credit guarantees are extended remains an open question that will add uncertainty to grain markets in the year ahead. The need for food assistance will stay great while the former Soviet republics adjust to a new market economy. But getting food assistance to the regions that need it most will be difficult due to the worsening distribution problems within and among the republics.

Crop outlook

Crop inventories are low, but sluggish export markets may limit gains in crop prices in the year ahead. Even more than in recent years, the outlook hinges on exports and weather. Large crops in other producing nations and the Soviet economic disarray will limit U.S. grain exports. With exports slow, prices may rise very little despite low U.S. crop stockpiles. Still, wheat and corn inventories are precariously low, and dry weather has already threatened the winter wheat crop across the heart of the U.S. wheat belt. An unexpected surge in exports or unfavorable weather this winter and spring could send prices soaring.

The wheat outlook has changed markedly from a year ago, when a surge in the world's wheat production pushed inventories up and prices down. This year, a much smaller world wheat crop will shrink the world inventory.

In the United States, wheat use will fall to about 1.25 billion bushels, down nearly 10 percent from a year ago due to a sharp drop in wheat feeding. Following the harvest last summer, low wheat prices spurred extensive feeding of the new crop. But by autumn, tightening wheat inventories had pumped up wheat prices, allowing cheaper corn to quickly replace wheat in cattle rations.

A modest rebound is in prospect for U.S. wheat exports. Smaller crops in the United States and the Soviet Union account for most of the decline in global wheat production. Meanwhile, discount pricing of large wheat crops from the EC and Canada will keep the world marketplace fiercely competitive. Thus, extensive use of export subsidies under the Export Enhancement Program (EEP) and government credit guarantees will be required to boost U.S. wheat sales. About 40 percent of the latest $1.25 billion credit guarantee for grain sales to the Soviet Union—an unexpectedly large share—was allocated to wheat sales. As a result, U.S. wheat exports could be up 15 percent from last year's depressed level.

Despite the sharp drop in domestic use, the modest rebound in exports will shrink the U.S. wheat inventory to just 414 million bushels, the smallest stockpile since the mid-1970s. The tighter inventory will boost wheat prices to an average of $2.85 to $3.05 a bushel, well above last year's average of $2.61 a bushel (Table 1).

The U.S. corn stockpile will also shrink in the year ahead (Table 2). A small crop and large domestic use will tighten inventories, but the boost in prices due to tight supplies will be dampened by smaller corn exports. The world corn harvest was the largest on record, flooding the world market.

In the United States, domestic corn use will be the biggest ever. Feed for the nation's growing cattle and hog herds and poultry flocks will account for most of the increase in domestic corn use. But food and industrial uses of corn will consume nearly a fifth of the nation's 1991 corn crop, due to steady gains in the production of high-fructose corn syrup, glucose, and starch.

Competition in the world marketplace, however, dampens prospects for U.S. corn exports. Corn production rebounded in the EC and Eastern Europe in 1991 after poor crops the year before. China—the largest foreign corn exporter—produced its second largest crop on record in 1991. Large supplies of barley and feed wheat from the EC, Canada, and Australia will also compete effectively with U.S. corn exports in key markets, including South Korea and the republics of the Soviet Union. In sum, U.S. corn exports may shrink nearly 9 percent to the smallest level in five years.

The smaller domestic corn crop, combined with steady gains in domestic use, will shrink the U.S. corn inventory to about 1.2 billion bushels, the smallest since a drought and the government's PIK program drew down inventories in 1983. Higher corn prices will ration the dwindling inventory. With inventories tight, unexpected strength in exports or disappointing production prospects next spring could send corn prices soaring. More likely, however, corn prices will rise only modestly above last year's average. Corn prices are expected to average $2.20 to $2.60 a bushel during the 1991-92 marketing year, bracketing last year's average of $2.28 a bushel.

The outlook for soybeans suggests supplies will be adequate to meet strong demand both at home and abroad. But prospects differ sharply for soybean meal and soybean oil, the two major products obtained when soybeans are crushed. More soybean meal will be fed to the nation's expanding hog herd and poultry flock, shoring up meal prices. But the world market is already saturated with supplies of vegetable oils, which will push down prices for soybean oil.

Strong domestic and foreign demand for U.S. soybean meal will boost the domestic soybean crush to a record 1.24 billion bushels. The feed needs of the nation's expanding hog herd and poultry flock will boost domestic meal consumption to a new record, and meal exports will be the largest in four years.

Prospects for exports of whole soybeans are also much brighter than a year ago. Drought reduced the size of the South American crop, easing competition in the world market—at least until the second half of the marketing year when the next South American crop is harvested. Meanwhile, government-guaranteed credit will support larger soybean sales to the Soviet Union. While up sharply from a year ago, soybean exports will remain about 30 percent below the peak a decade ago, when competition from South American growers began.

The U.S. soybean stockpile will be drawn down only slightly, however, despite the larger domestic feed needs and the modest rebound in exports. An ample projected inventory of 315 million bushels will hold the season average soybean price in a range of $5.25 to $5.75 a bushel, which extends well below last year's average of $5.75 a bushel. Strong demand will boost the average price of soybean meal to $165 to $185 a ton, up from $170 a ton last year. With a further buildup in inventories, however, the average price of soybean oil will fall to 17.5 cents to 20.5 cents a pound, down from 21 cents a pound last year.

Livestock outlook

The livestock outlook suggests bigger supplies of beef, pork, and poultry are headed for the nation's supermarkets in 1992. How market prices respond to the expanded supplies depends on the health of consumer income. If the economy remains sluggish, demand for meat and poultry may be weak, pointing to sharply lower prices at the meat counter and on farms and ranches. If the economy gains momentum, however, demand may strengthen, prompting only modest price declines to induce consumers to buy the larger meat and poultry supplies.

Slightly more beef will appear at grocery stores in 1992. The nation's cattle herd began growing again in 1991, after shrinking to the smallest size in nearly three decades. But lingering memories of the farm financial crisis and dry pastures and rangelands in the late 1980s have slowed the pace of expansion. The small herd will produce just over 40 million calves in 1992, still too few to fill feedlots and fully replenish breeding herds. Imports of feeder cattle from Canada and northern Mexico will again augment the relatively tight supply of young cattle. Meanwhile, gradual changes in technology and management practices have produced more beef from fewer animals. Overall, the gradually expanding beef industry will produce 23.3 billion pounds of beef, up nearly 1.5 percent from a year ago.

A small but growing portion of the nation's beef will be sold to foreign customers. Beef exports are expected to surge more than 8 percent to 1.2 billion pounds. Japan will remain the largest buyer of U.S. beef. But other markets are growing as income rises in Mexico, import quotas rise in South Korea, and food-service demand rises in Canada.

The lion's share of the nation's huge beef production, however, will be shipped to domestic grocery stores. The large beef supplies, as well as competition from expanding supplies of pork and poultry, will hold retail beef prices in 1992 well below the record of nearly $3 a pound set last spring. Retail prices may average about $2.90 a pound for the year as a whole, slightly below last year's average. With only a slight decline in retail prices and keen competition from other meats, per capita beef consumption will stay almost unchanged from a year ago at 67.5 pounds. Steady consumption should support cattle prices well above the lows recorded late last summer. Thus, the outlook suggests an average fed cattle price of $73 to $79 a hundredweight, little changed from $75 a hundredweight in 1991.

Pork producers recently launched a major expansion that promises to outpace the modest expansion in the beef industry. Two years of solid profits have encouraged pork producers to gear up for record-breaking output in 1992. Hog producers have increased their breeding herd 7 percent from a year ago, setting the stage for large pork supplies in 1992. At 17.2 billion pounds, pork output is expected to be up 7 percent from a year ago.

The enormous supply of pork will compete with large supplies of beef and poultry for space in retail meat counters. As a result, lower retail prices will encourage consumers to eat more pork, boosting per capita consumption to 54.4 pounds, up 4 pounds from 1991. The lower retail prices will also push down hog prices to break-even levels or below, slowing the pace of expansion in the second half of the year. For the year as a whole, slaughter hog prices may average $39 to $45 a hundredweight, sharply lower than $49 a hundredweight in 1991.

The poultry industry is also expected to expand in 1992, although at a slower pace than in recent years. Smaller profits will rein in the expansion. Larger competing supplies of beef and pork promise to hold down broiler prices, while higher feedgrain and soybean meal prices will push up feed costs, squeezing profit margins. Broiler production could be up 4 percent, well below the industry's 5.5 percent annual rate of increase during the past decade. Turkey production will also expand in 1992, but at a relatively cautious pace. Low profit margins in the last half of 1991 are likely to discourage expansion plans in the year ahead. Turkey production may increase only 2.5 percent in 1992.

The larger poultry supplies suggest increased poultry consumption and lower poultry prices. Per capita poultry consumption could increase 3 pounds, as poultry products maintain their high level of consumer acceptance. But with large quantities of beef and pork competing for a place in the consumer's shopping cart, poultry prices are likely to slip. Broiler prices may average 47 cents to 53 cents a pound and turkey prices 56 cents to 62 cents a pound, both down a few cents from a year ago.

Conclusion

The farm economy dipped in 1991 for the first time in five years. Farm financial conditions softened due to a 5 to 10 percent drop in farm income and a stall in farmland values. After being the engine of farm recovery the past few years, livestock prices fell in 1991 as meat supplies hit a new record high. Despite eroding financial conditions, agricultural lenders closed 1991 with few problem loans, thanks mainly to an aggressive pruning of bad loans early in the farm recovery.

The farm downturn will probably continue in 1992. Farm income will move lower due to further weakness in livestock prices and only moderately higher crop prices. Meat supplies will climb again in 1992, and prices will depend heavily on the strength of the economy. Crop inventories are small entering 1992, and thus crop prices are poised to move much higher if weather is bad or export demand is unexpectedly strong. But with chaotic conditions in the Soviet Union and weakening economies in other parts of the world, U.S. farm exports will probably grow little in 1992. Overall, nothing seems likely to arrest a mild downturn in the farm economy in the year ahead. But the industry should be able to ride out the downturn on its solid financial reserves.

Endnotes

[1] Fruit and vegetable prices soared in early 1991 due to adverse weather. Horticultural products, meanwhile, have benefitted from strong export demand.

[2] Agriculture is only one of several trade areas at issue in the Uruguay Round. A year ago, the Round was stymied when the Cairns Group—several agricultural producing nations—refused to discuss liberalization of trade in services or intellectual property unless the EC compromised on farm trade. An agreement on services would liberalize trade in banking and other financial services, insurance, transportation, and telecommunications, and an agreement on intellectual property would harmonize protection internationally for patents, copyrights, and trademarks. For a more detailed account of the issues in the Uruguay Round, see Alan Barkema, "Tenth District Agriculture and the Current International Trade Negotiations," Federal Reserve Bank of Kansas City, *Regional Economic Digest*, First Quarter 1991.

[3] Arthur Dunkel, director general of the GATT, recently proposed a compromise that would cut budget outlays 36 percent and subsidized quantities 24 percent during a six-year period beginning in 1993 and measured against a base period of 1986-1990. Dunkel's proposal would also convert all import restrictions to tariffs. The tariffs would then be cut 36 percent and domestic supports would be cut 20 percent during the six-year period. The negotiators will consider the merits of Dunkel's compromise when they return from the holiday recess on January 13.

[4] The political and economic linkages that may emerge among the republics of the former Soviet Union remain uncertain. This article uses the expression "Soviet Union" to describe collectively the republics that previously comprised the nation.

[5] The amount of credit guaranteed thus far is large relative to the annual size of the Soviet market for U.S. farm products. During the past five years, Soviet purchases of U.S. farm products averaged about $2.1 billion. For a more detailed account of farm trade with the Soviet Union, see Alan Barkema, "How Will Reform of the Soviet Farm Economy Affect U.S. Agriculture?" Federal Reserve Bank of Kansas City, *Economic Review*, September/October 1991.