

Shipping out

Can rising exports sustain the farm boom?





Oklahoma farmer Orel Sallaska is selling his wheat bushels for a dollar more than he did last year. Not a bad increase, but had he not locked in that selling price a while back, he could have gotten nearly double per bushel.

Sallaska and his wife Jeanne, who farm 1,040 acres of wheat and alfalfa with their dog Cheech, can't kick themselves too much. The couple couldn't have predicted such an increase in global demand.

"I think we're in uncharted territory," says Orel, 57.

Overall, the Sallaskas' hard red winter wheat crop—used to make flour—was more profitable than Orel anticipated in 2007 and so far in 2008, but he's not sure how long the boom will last.

"(It) has allowed me to get ahead," Orel says. "Prices go up and down. Things change fast."

Recently, farm profits and investments have soared, and farmland values have surged. For farmers around the country—including those in the Tenth Federal Reserve District states of Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and New Mexico—times are good, but likely won't last indefinitely, say Maria Akers, an assistant economist, and Jason Henderson, an economist and the Branch executive, both at the Federal Reserve Bank of Kansas City's Omaha Branch. Akers and Henderson recently researched the role of exports in the current farm boom.

"In short, prosperity for U.S. agriculture often hinges on exports," Henderson says, citing global factors that most recently boosted

U.S. agricultural exports:

- droughts tightened food supplies;
- growing populations and strong economies spurred food demand;
- the weak dollar made U.S. products more affordable abroad.

“U.S. agriculture has benefited greatly from these conditions,” Akers says. “However, changing trends could quickly redraw the outlook for exports.”

After farming for more than three decades, Orel and Jeanne Sallaska have seen bad times follow good ones.

“The pendulum swing has been so wide,” Orel says. “I think there are some tough times ahead.”

Bon voyage

Since 1960, U.S. farm exports have been larger than imports. But this year, the USDA is projecting the value of those exports will

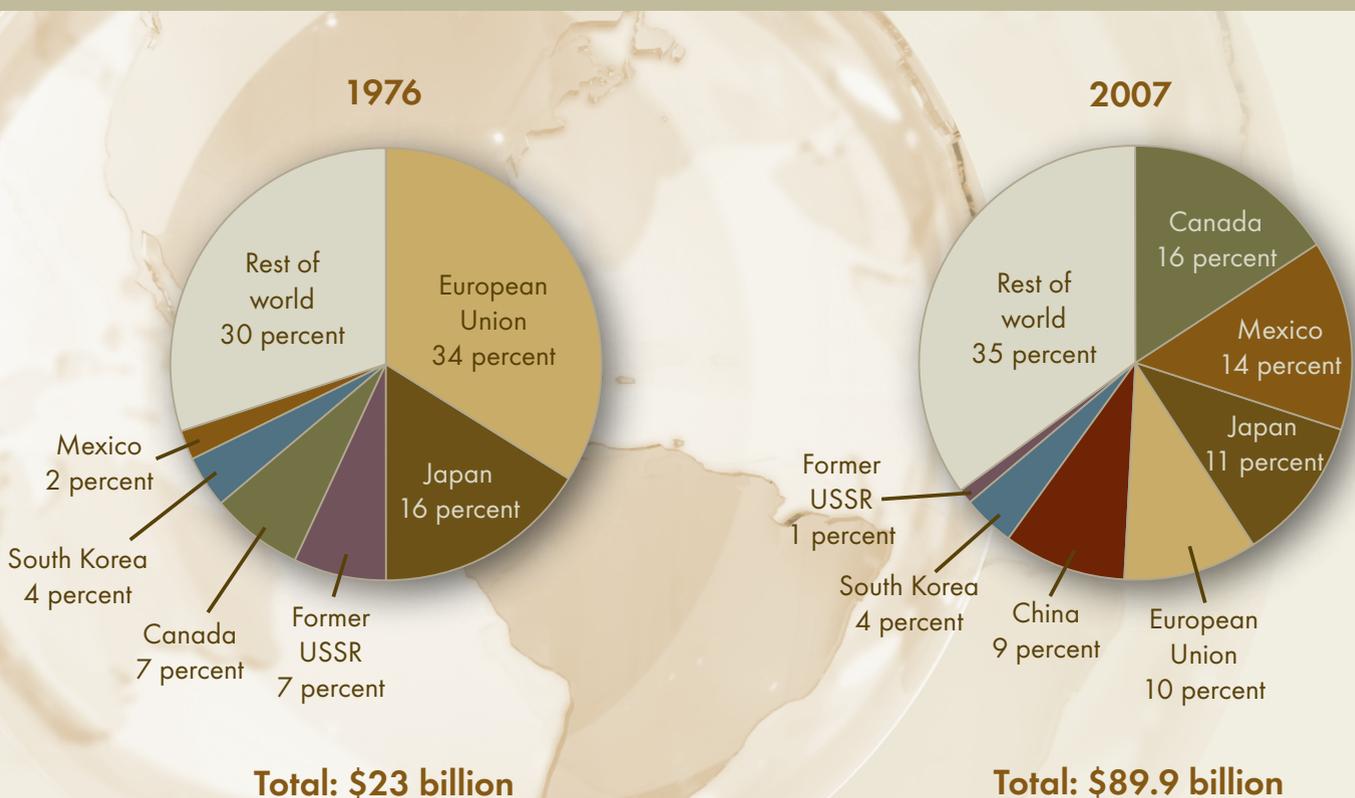
reach a record high of more than \$108 billion. The biggest gains in U.S. exports are processed agricultural goods, which have accounted for the majority of agricultural exports for nearly the last decade.

Horticultural and livestock products make up most of these exports, although livestock exports have varied as a result of foreign trade restrictions in response to Mad Cow disease in 2003.

More recently, though, “exports for beef have just been tremendous,” says Jim Timmerman, chief financial officer of Timmerman & Sons Feeding Co. based in Springfield, Neb. The family business, started by Timmerman’s father in 1946, operates feed yards and cattle ranches around the country. Timmerman also is a member of the Kansas City Fed’s Omaha Branch board of directors.

He attributes this spike in foreign demand to increasing populations and rising wealth

U.S Agriculture Export Destinations





SOME OF THE UNITED STATES' LARGEST EXPORT GAINS have been in beef and dairy, with the latter sector seeing a record export value of \$3.06 billion last year. Mexico, Southeast Asia and Canada are the biggest importers of U.S. dairy products.

as well as smaller supplies in other exporting countries due to weather conditions and other factors. Large importers of U.S. beef include Mexico, Russia and many Asian countries.

Timmerman predicts U.S. beef will remain competitive because of its high quality; U.S. cattle are grain fed whereas other beef export countries feed their cattle grass. This demand will help offset producers' rising expenses, such as fuel and feed, which is in competition with ethanol production—the type of corn used in ethanol is the same type that is primarily used for livestock feed, and, less so, for human consumption.

“The bottom line is getting better all the time,” Timmerman says.

Some of the other largest gains have emerged in the dairy sector. In 2007, the U.S. dairy industry saw a record export value of

\$3.06 billion, which is a gain of 62 percent, says Tom Suber, president of the U.S. Dairy Export Council. He says high international prices contributed to this gain, as did growth of the middle class, poor weather conditions prompting drought and other countries' export restrictions. But the biggest factor is high global demand coupled with insufficient supply from other countries that export dairy products.

While future growth may be at a slower rate, Suber says “the export market is going to continue to see their (U.S. dairy producers') product.”

This is certainly beneficial to dairy producers' profits because “with input costs, that margin is getting squeezed,” says Dave Drennan, executive director of Missouri Dairy Association, which acts as an advocate on behalf of the state's dairy farmers. Labor, electricity

and fuel expenses tend to be higher than those of other commodities due to the nature of producing and transporting dairy products.

“I don’t see it turning around and going the other way,” Drennan says, citing particularly strong growth in U.S. cheese and whey exports.

Mexico, Southeast Asia and Canada are the biggest importers of U.S. dairy products. Trade with Mexico and Canada in particular has skyrocketed since the North American Free Trade Agreement (NAFTA) was ratified in 1993 and trade tariffs were eliminated. These two countries purchase almost one-third of all U.S. agricultural exports, primarily fresh produce and grains. Asia also is a major export market for U.S. goods—primarily grains and oilseed. Additionally, U.S. grain exports have spiked recently in the European Union as a result of droughts in 2007.

Will the boom last?

Historically, U.S. agricultural prosperity has been tied to exports, say Akers and Henderson. In the 1970s and mid-’90s, surging exports led to strong farm incomes—much like we are seeing today.

“However, past export booms faded quickly,” Henderson says. “The agricultural boom of the ’70s became the bust of the ’80s.”

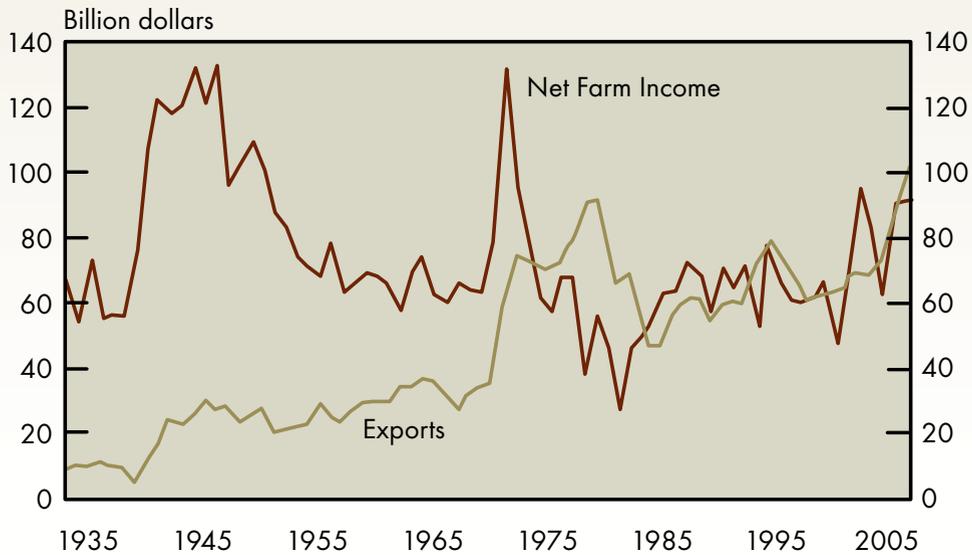
By the 1980s, agricultural exports were hurt by worldwide recession, a sharp rise in the U.S. dollar and embargos on U.S. grain sales to Russia. Commodity prices weakened, U.S. farm incomes dropped and farmland values fell quickly.

By the mid-’90s, exports had surged again, as demand grew for processed agricultural products and the dollar declined. But later that decade, the rising exports and strong farm incomes faded as a result of a financial crisis

JEANNE, LEFT, AND OREL SALLASKA DINE OUT AT TENA’S CAFE near their 1,040-acre farm in the western Oklahoma town of Corn. For the farming couple, times are good right now, but rising costs are biting into their profits. “It’s just such a capital-intensive business,” Orel says.



U.S. Real Net Farm Income and Agriculture Exports



Source: USDA

Note: 2007 is the base year, meaning dollars have been converted to that year's value.

in Asia and a rising U.S. dollar. Crop prices dropped and, as a result, farm government subsidy payments surged, underpinning farmland values.

Again today, sharp gains in both price and quantity have driven U.S. exports to their highest level in decades.

"Today's farm boom is following historical trends," Akers says. "With expectations of lean supplies and robust demand, farmers could enjoy another bountiful year of rising exports."

But, an unexpected surge in production costs, such as even higher fuel expenses, or a drop in crop prices could undercut farm incomes and farmland values, posing a financial risk to the farm sector, Akers says. Thus far, however, the industry's debt levels are up only modestly, helping to mitigate the risks of a drop in farm incomes.

The USDA predicts agricultural exports will rise steadily during the next decade. High-valued products, such as fruits, vegetables and processed foods, likely will account for the majority of this increase. Exports this year already have reached the USDA-projected levels of 2013.

"There are a lot of uncertainties with

agricultural exports though," Henderson says. "Their future will be influenced by the supply here and abroad, which is dependent on weather conditions, exchange rates, trade policies, population growth and other factors."

In Oklahoma, Orel and Jeanne Sallaska aren't sure they'll break even by the end of '08, considering that increased world wheat production has trimmed export demand while fuel costs are soaring, he says. Orel is less optimistic for 2009.

Export demand, he says, is "as unpredictable as the weather."



BY BRYE STEEVES, SENIOR WRITER

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