

Iowa Farm Outlook

Department of Economics
Ames, Iowa

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Livestock Mandatory Country of Origin Labeling

Mandatory Country of Origin Labeling (MCOOL) which was part of the 2002 Farm Bill finally went into effect September 30, 2008. The initial legislation making COOL mandatory was delayed in 2004 and 2006 and was amended in 2008 before the current version was included in this year's Farm Bill. The law amended the Agricultural Marketing Act of 1946 and is intended to inform retail consumers the origin of commodities covered in the law. These include: muscle cuts and ground meats of beef, lamb, goat and pork; wild and farm-raised fish and shellfish; fresh and frozen fruits and vegetables; raw peanuts, pecans, macadamia nuts and ginseng. Chicken muscle cuts and ground meat was added to MCOOL with the 2008 amendments.

MCOOL applies to retail grocery fresh and frozen meat sales with exemptions for small grocery stores, butcher shops, restaurants and food service. Processed meats are also exempt and USDA has definitions and categories for covered products. There is a 6-month educational phase in period where USDA will be monitoring implementation before enforcement is fully imposed. See more details at: www.ams.usda.gov/cool/.

Logistics

MCOOL requires retailers to inform consumers at the point of purchase of the origin of the covered commodity, and the retailer must maintain sufficient records to substantiate the label claim. In the Interim Rule USDA-AMS states that, "The supplier of a covered commodity (packer) that is responsible for initiating a country of origin declaration must possess or have legal access to records that are necessary to substantiate the claim." Packers are allowed to accept a signed affidavit from the producer to establish the origin of the animal. Producers are expected to maintain normal business records at their farm to support their affidavit claim if an audit of a label claim leads to their farm.

Congress and USDA have identified four categories of meat products under MCOOL. These are:

- A. Born, raised and slaughtered in the U.S.
Product of the U.S.
- B. Multiple countries of origin, i.e., Canadian born feeder pigs/cattle fed in the US.
Product of U.S. and country X and/or country Y
Ground beef: May include product of (list sources)
- C. Animals imported for immediate slaughter
Product of country X and U.S.
- D. Imported finished products (to be sold at retail)
Product of country X.

Implications

Initially, many packers and retailers planned to use Category B for most if not all their product including those animals that were Category A animals. This strategy was aimed at reducing costs of labeling and product segregation by having only one label. Proponents of MCOOL and some members of congress that supported the rule raised concerns that such action was not the intent of the law. In late September, at the urging of Congress, USDA changed their stance on the use of the Category B label to reaffirm that if animals are born raised and slaughtered in the US that their product should carry the Product of the US label. As a result, some packers have now switched to using both A and B, or in some cases only buying Category A animals.

It is too early in the process to know what the implications of MCOOL will be on prices at the farm or retail level. Some packers have stated that they will buy only US animals. Others have designated a specific plant or time (day or shift) that they will take Category B or C animals. This strategy will minimize labeling confusion and cost, but increase transportation cost for the animals and perhaps the meat that have to go to a different plant. Producers that had fed Canadian born cattle or hogs may choose to not buy imported feeders if they have to haul the finished animal further to sell them. Likewise, producers near a plant that is buying Canadian born animals may choose to feed imported animals as prices adjust.

The price impact is even less clear. The cost of labeling and record keeping is bore by all products because US as well as imported product must be labeled and records must be kept. Companies that do not buy imported animals will have less of these costs because they only have one label to track. However, if they had bought imported animals before they will have to bid additional US animals away from other packers which should be supportive of farm level prices. Packers that do buy imported animals will want to buy enough to run the plant, day or shift efficiently and may at times have to bid up for imported animals.

Conventional wisdom and early rumors are that imported animals are being discounted by packers. However, it is difficult if not impossible to track because USDA is not reporting separate prices for separate categories of product or animals. Envision the market report on the radio with prices for different grades and origins of animals. While one report for cattle prices did state “Domestic sources only” there was not a price for cattle fed in the US but born outside the US as a point of comparison.

If there is a higher cost of processing, labeling, segregation, transportation, etc for Canadian born pigs or Canadian or Mexican born slaughter cattle, it will be passed forward to consumers or, more likely, back to the feeder in the form of lower prices. In turn, the feeder will pay less for the feeder animal. All else equal, lower prices for imported feeder animals would discourage Canadian and Mexican producers from sending feeder animals to the US. One result is that the animals may be fed and slaughtered in their home country and they meat may be imported directly to retail with the appropriate label. We would expect this product to be less competitive at the retail counter otherwise this trade would already be occurring rather than importing the feeder animals to the US. Another possibility is that these animals are fed in their home country but compete with US meat in export countries. The overall supply of meat does not change until prices are low enough in Canada or Mexico to cause their producers to reduce supplies.

However, not also else is equal. First, MCOOL will increase farm-to-retail cost at least some from where it was before. Imported product going direct to retail will not have new added cost from their previous procedures. Second, and perhaps more important economically, but unrelated to MCOOL, is that the value of the US dollar has increased relative to other counties. As a result, imported products are now cheaper on our shelves that they were before the financial crisis. Likewise, feeder pig and feeder cattle producers in Canada and Mexico receiving dollars for their animals may not notice a discount for origin. Between October 1 – 23, the US dollar gain 19 and 23 percent, respectively against the Canadian and Mexican currency.

What next?

Producers must communicate with their buyers to know their marketing options and they should talk to them well in advance of marketing day in case they need to find another buyer. If they are thinking about buying imported feeder animals they should talk to buyers about locations where they can deliver and what if any price discounts they may expect. If farmers are buying feeder animals from anyone they need to get a signed affidavit from the seller stating the origin of the animals and keep the paper work on file for at least a year so that they can make a claim of origin when they sell the finished animal. More information and example affidavits are available at www.IowaBeefCenter.org.

Finally, state tuned and pay attention. Consumers are evaluating the different products and voting with their dollars on which product they prefer and at what price. This will impact retailer decisions on labels and ultimately influence packer buying decisions.

Grain

USDA Report Corrections and Crop Outlooks

Report Corrections

USDA issued corrections to the Oct. 10th World Agricultural Supply and Demand Estimates and Crop Production reports. After the Oct. 10th reports were released, USDA discovered a data mismatch between datasets used to create the reports. In many ways, the corrections move the corn and soybean data back toward the September production projections. The corrections concentrated on acreage as national corn acreage was reduced by 1 million and national soybean acreage by 1.1 million acres. Corn acreage is now estimated at 85.9 million acres, with harvest expected on 78.2 million acres. Soybean area is estimated at 75.9 million acres planted and 74.4 million acres harvested. National yield estimates are 153.9 bushels per acre for corn and 39.5 bushels per acre for soybeans. Corn production is projected at 12.033 billion bushels, 39 million bushels below the September estimate. For soybeans, production is estimated at 2.938 billion bushels, 4 million above September estimates. These estimates still point to the 2nd largest corn crop and 4th largest soybean crop the U.S. has ever seen.

For Iowa, corn harvested area is now projected at 12.5 million acres with an average yield 172 bushels per acre. This leads to an estimated production of 2.15 billion bushels, down 218 million bushels from last year. Soybean harvested area is estimated at 9.6 million acres. With yields projected at 46 bushels per acres, Iowa is expected to produce 441.6 million bushels of soybeans. This would be a decline of just over 7 million bushels from 2007. The increase in soybean area this year was pretty much offset by the yield decline we experienced this year.

At the end of September, USDA updated the grain stocks situation. In that update, both corn and soybean stocks were increased for the 2007 crop year. Corn stocks for 2007 were upped 48 million bushels, based on lower feed, food, and seed use. The total corn ending stocks for 2007 are set at 1.624 billion bushels. Soybean stocks for 2007 were increased 65 million bushels, based on higher production and lower crushing use, putting the total ending stocks at 205 million bushels. The projections for 2008 show corn ending stocks falling to 1.088 billion bushels and soybean ending stocks holding at 205 million bushels. Thus, the crop stock situation looks to remain very tight.

As of the end of October, nearly 80 percent of the nation's soybeans had been harvested. Reports in Iowa put the harvested amount near 90 percent. Many farmers have concentrated on getting the soybeans cleared out before moving to corn. Nationally, the corn harvest stood at 39 percent complete, well behind the five-year average of 66 percent. The Iowa corn harvest is also behind. Typically, by this date, over 60 percent of Iowa's corn is harvested. Current estimates put the corn harvest at 20 percent. But with relatively dry weather forecast over the next week, the corn harvest should pick up steam.

Demand

On the demand side, corn feed demand is projected at 5.3 billion bushels, up 100 million from September, partially reversing an earlier downward adjustment. Lower corn prices are seen as the major reason for this shift. Corn demand from ethanol is projected at 4 billion bushels, up 1 billion bushels from last year. The ethanol industry has continued to grow, but the pace of growth has slowed. Lower corn prices imply lower production costs for ethanol plants, but plants are also seeing lower ethanol prices as U.S. consumers have reduced their fuel demand. Corn exports are projected at 1.95 billion bushels, down 50 million from September and down 485 million from last year. As Figure 1 shows, corn exports and outstanding sales are off of last year's pace, but they are comparable to the pattern for 2006. With total corn usage estimated at 12.585 billion bushels, the corn stocks-to-use ratio for 2008 stands at 8.6 percent, well down from 12.7 percent in 2007.

Soybean crush demand is estimated at 1.76 billion bushels, off 41 million bushels from 2007. Export demand is also lower than last year, at 1.02 billion bushels. However, export pace has been brisk, exceeding what we have seen over the past couple of years. In the mid-September USDA reports, soybean stocks-to-use ratios for 2007

and 2008 were below 5 percent. In these latest reports, those ratios were raised to 6.7 percent for 2007 and 7 percent for 2008. So the soybean stock situation remains tight, but not nearly as tight as it previously looked.

Figure 1. The Pace of Corn Exports (percentage of total marketing year exports and sales)

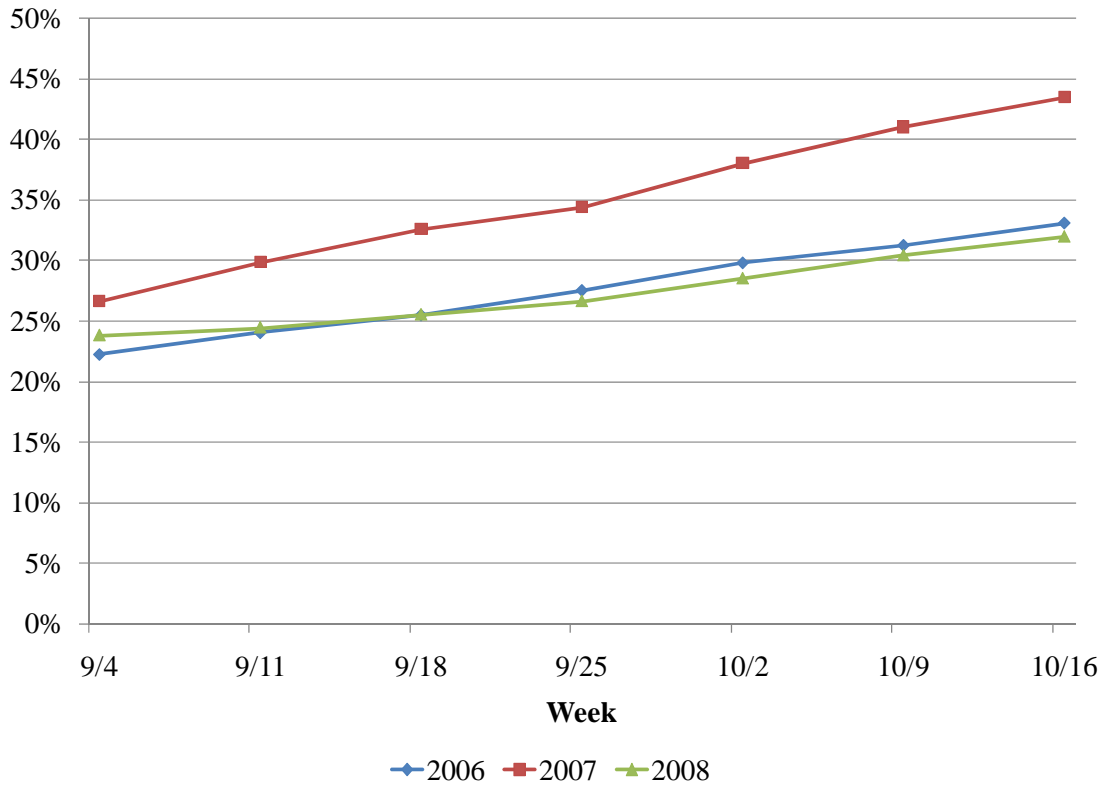
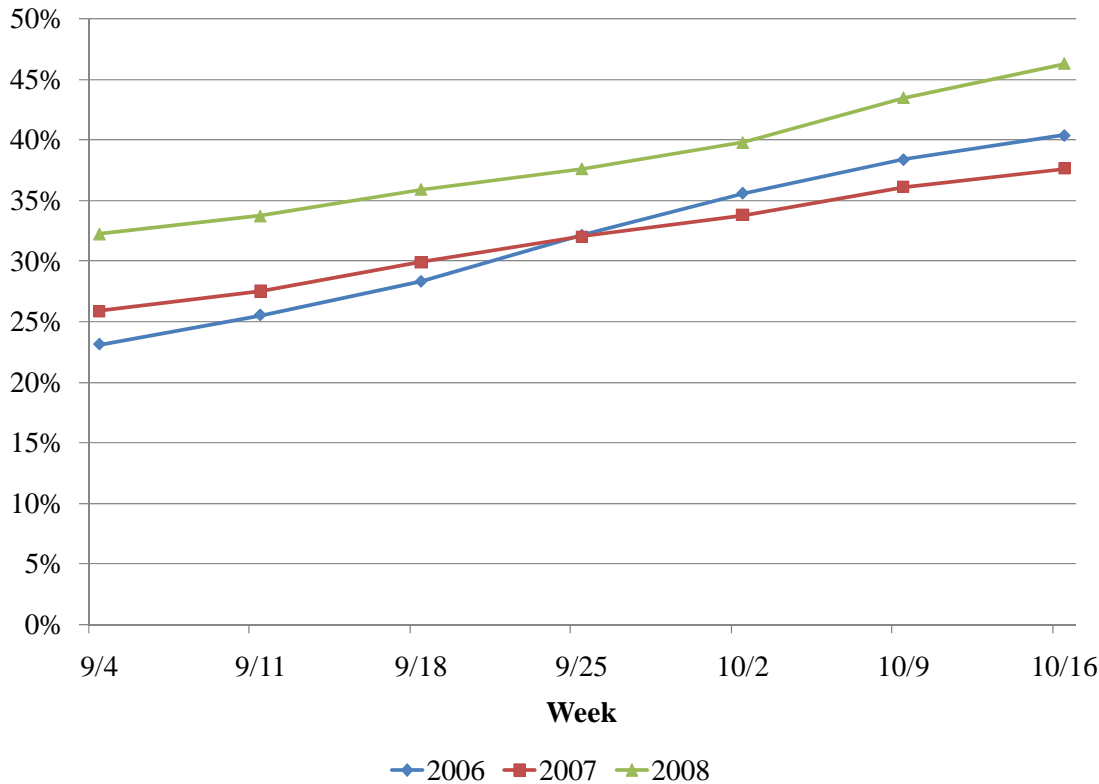


Figure 2. The Pace of Soybean Exports (percentage of total marketing year exports and sales)



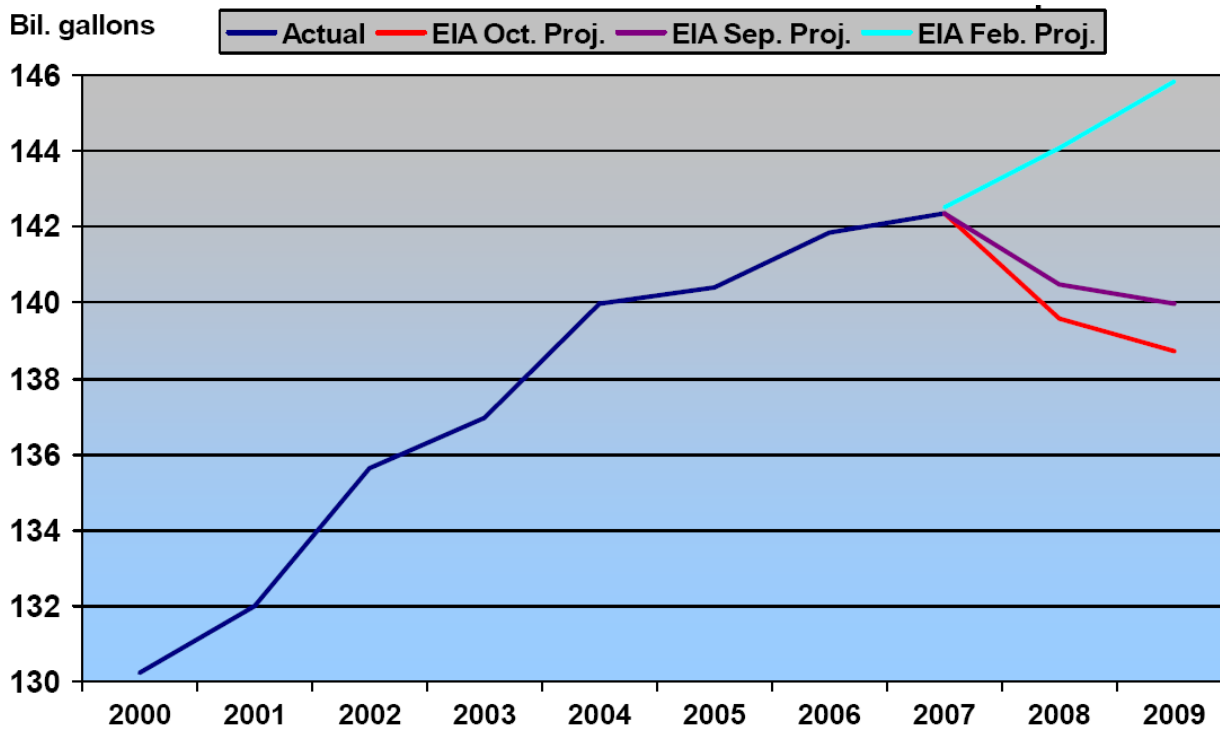
Prices and Other Factors

The corn and soybean markets, like many commodity and stock markets, have taken a pounding over the last couple of months. Concerns about the general economy both here in the U.S. and worldwide have weighed heavily on market trading and have been a significant factor to the slide in crop prices. USDA significantly

updated its season-average prices for corn and soybeans since September to \$4.75 per bushel for corn and \$10.45 per bushel for soybeans. The corn price is off 75 cents per bushel, while the soybean price is down \$1.90 per bushel from September's estimates. Futures prices point to stronger crop prices as we move toward next spring and summer. Basis levels for both crops have moved back toward historical averages. The combination of these price movements implies the potential for better crop returns for farmers who maintain ownership of their crops later in the marketing year.

Factors outside of agriculture will continue to strongly influence agricultural prices. The financial market turmoil is the dominant factor across many markets. Crop agriculture over the past couple of years has enjoyed strong demand for food, feed, and fuel use. But the concerns about the general economy lead to concerns about future crop demands both here and abroad. As Figure 3 shows, the outlook for overall fuel demand has dropped significantly over the past few months. Credit markets have tightened and, in some cases, ceased to function. Much of the funding for agricultural production and trade worldwide depends on liquid credit markets.

Figure 3. Blended Motor Gasoline Consumption in the U.S.



Source: U.S. Department of Energy, Energy Information Administration

Reports out of South America indicate the combination of higher input costs and lower crop prices may hamper crop production growth there. Estimates from the Brazilian National Commodities Supply Corporation put Brazilian soybean area at 21.5 to 21.9 million hectares (53 to 54 million acres). USDA had released an earlier estimate of 22 million hectares. The Agriculture Secretariat of Argentina has projected soybean planted area of roughly 18 million hectares (44.5 million acres), up nearly 10 percent. Drought conditions and rising costs were seen as factor leading producers away from corn and wheat and to soybean. And officials in Paraguay expect soybean acreage to be in line with last year's level.

Chad Hart

Dairy

Milk Production up 1.9%, Cheese Output Up

Sept 2008 23 major dairy states milk production rose nearly 1.9%. Production per cow rose only 7 pounds from one year ago, well below usual increases. Milk cow numbers were 118,000 more than Sept 07 and 8000 less than Aug 08. Aug milk production was revised up by 24 million pounds for a 0.2% increase.

Iowa Sept 08 milk production was up by over 2.9% compared to one year ago. Cow numbers were the same as one year ago and milk production per cow was 50 pounds higher. Aug 08 cheese production was 10.3% higher than one year ago and -2.3% less than July 08.

Third quarter US milk production was up 1.6% to 46.8 billion pounds compared to third quarter 07. The average milk cow number was up by 118,000 cows as well. Of the non-reporting states, the largest third quarter milk production increase was in Kansas at 12.5% due to 5000 more cows. Second largest was SD with +11.7% milk and 6000 more cows. NE milk production rose 4.6% with 1000 more cows and ND dropped 3.7% with 1000 fewer cows.

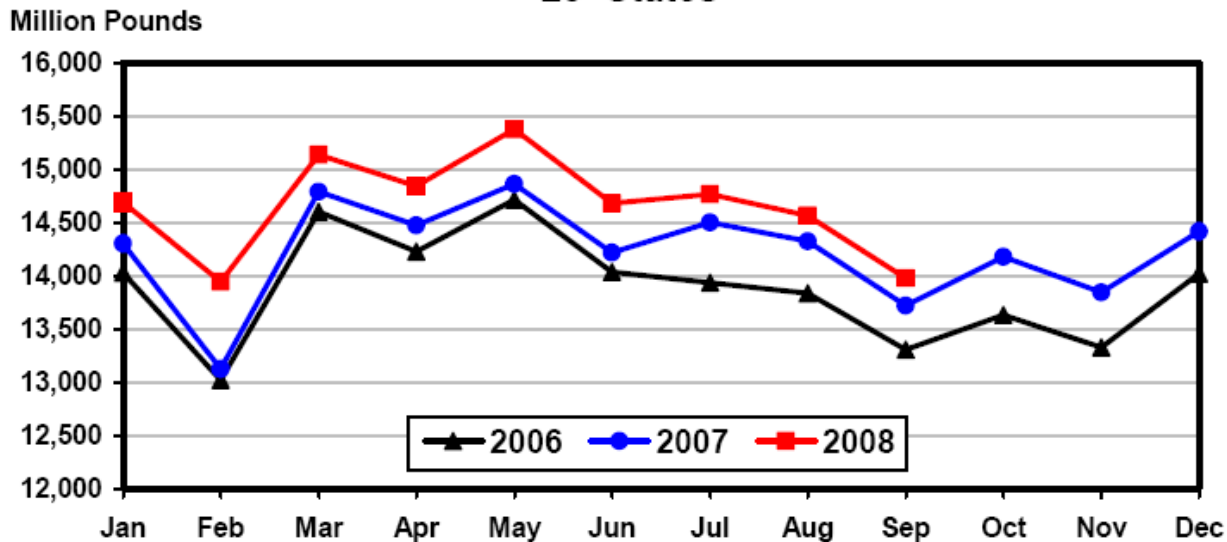
Table 1. Milk Production: Selected Dairy States, September 2008

State	Cow numbers			Milk per cow			Total milk production		
	2007	2008	% change	2007	2008	% change	2007	2008	% change
	(thousand head)			(pounds)			(million pounds)		
IA	215	215	0.00%	1,580	1,630	3.16%	340	350	2.94%
MN	463	465	0.43%	1,485	1,500	1.01%	688	698	1.45%
WI	1,248	1,253	0.40%	1,575	1,585	0.63%	1,966	1,986	1.02%
IL	103	102	-0.97%	1,440	1,425	-1.04%	148	145	-2.03%
CA	1,822	1,841	1.04%	1,785	1,780	-0.28%	3,252	3,277	0.77%
CO	120	130	8.33%	1,900	1,850	-2.63%	228	241	5.70%
ID	521	554	6.33%	1,880	1,870	-0.53%	979	1,036	5.82%
NM	336	336	0.00%	1,800	1,880	4.44%	605	632	4.46%
PA	550	548	-0.36%	1,550	1,530	-1.29%	853	838	-1.76%
NY	626	626	0.00%	1,570	1,590	1.27%	983	990	0.71%
TX	348	385	10.63%	1,640	1,710	4.27%	571	658	15.24%
23-State	8,341	8,459	1.41%	1,645	1,652	0.43%	13,718	13,976	1.88%
US total	9,166	9,269	1.12%	1,622	1,631	0.55%	14,871	15,118	1.66%

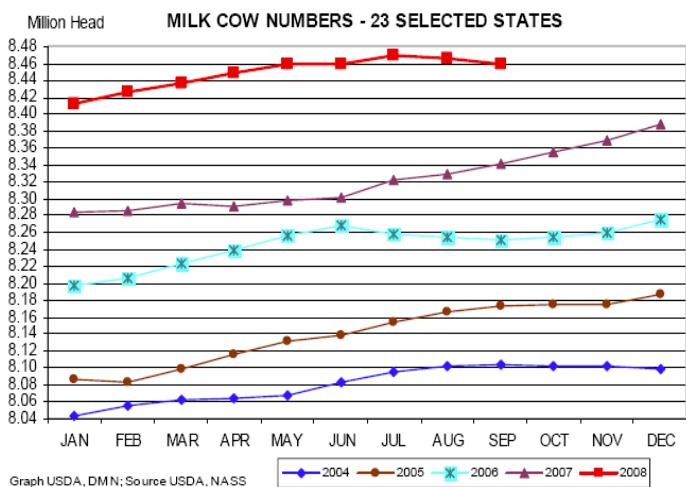
USDA estimated that 223,500 dairy cows were slaughtered in Sept 08. This is up 23,900 (+12%) from one year ago and the most since Sept 2003. Third quarter 2008 dairy cull dairy cow slaughter was up 11.3% from one year ago, 5123 more per week than the same period during 2007. Total 2008 dairy cow through Sept was about 5% higher than the same period 1 year ago.

Cooperatives Working Together (CWT) announced a second 2008 herd reduction. Bids to remove cows are being accepted through Nov 24. Regional limits will be in place and bidders can include bred heifers in their bids.

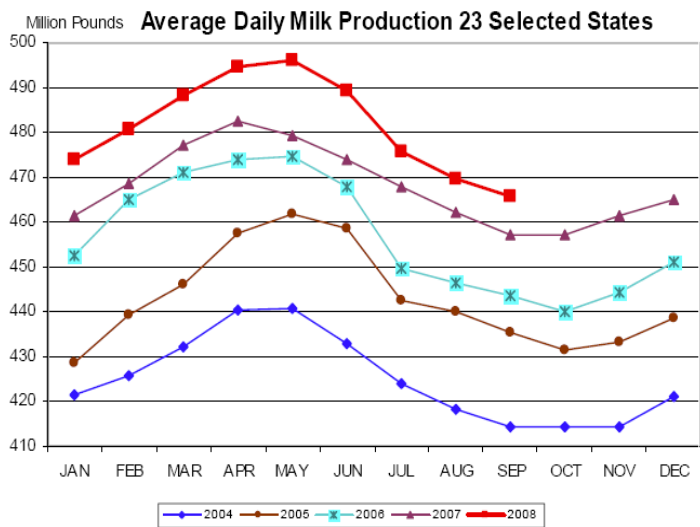
Monthly Milk Production 23 States



Source: Milk Production, NASS



Source: Dairy Market News

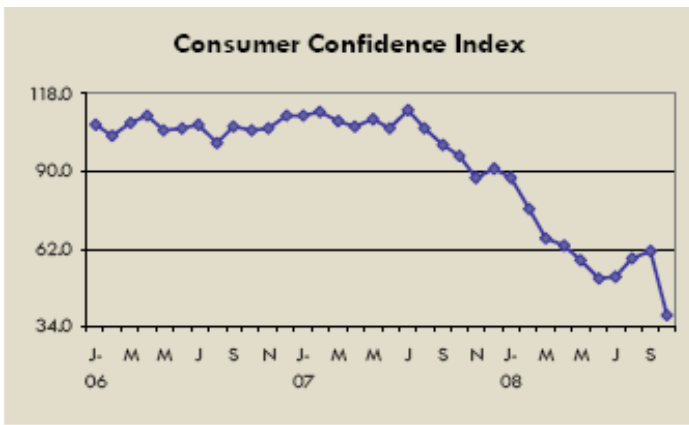


Source: Dairy Market News

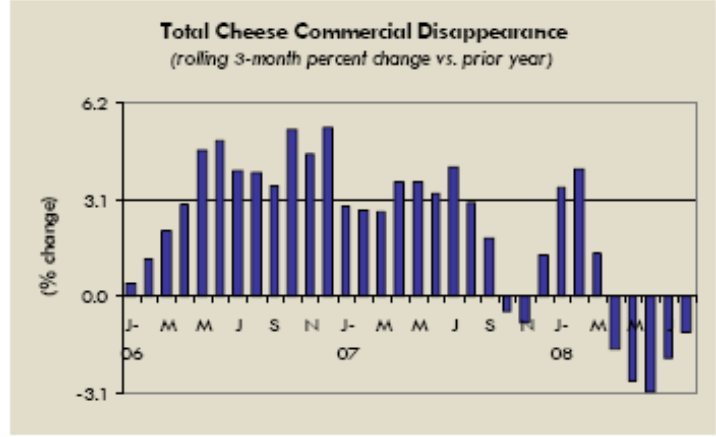
Demand or Disappearance

Commercial disappearance had remained strong for the first half of 2008, +2.4%. During Aug 08 use rose to +2.8% versus Aug 07. Aug American style cheese use was up 6.2% and butter use rose 20.8%. Butter stocks in CME approved warehouses during late Oct totaled 54.7 million pounds, down 44% from 97.8 million pounds one year ago. NDM disappearance was up by 17.4%. However, other than American style cheese use dropped 3.7% during Aug 08, leaving total cheese use down 1.1%.

The export market has continued its earlier strength. January-August butter exports were +500%, cheese +48% and NDM +80%. Dairy product exports for 2008 are expected to be near 10% of total US production. Fluid milk sales during June-Aug totaled 13 billion pounds, down 1.4% from one year ago and down 2.1% from two years ago. During the last 14 months, fluid milk sales have lagged year ago amounts after two years of growth. The Consumer Confidence Index for Oct was reported as 38, down from Septembers 61.4 and 95.2 one year ago.



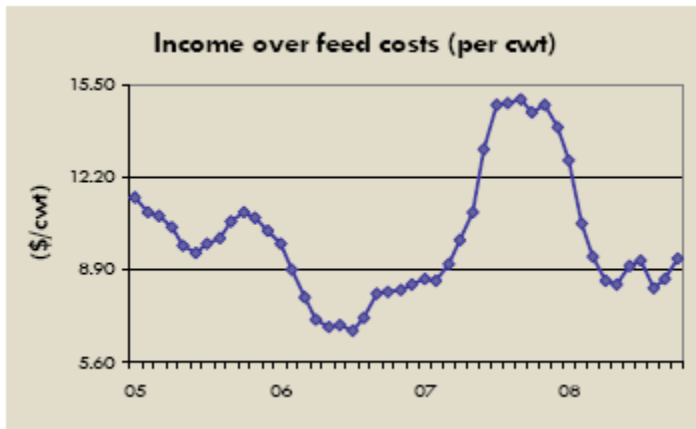
Source: Daily Dairy Report



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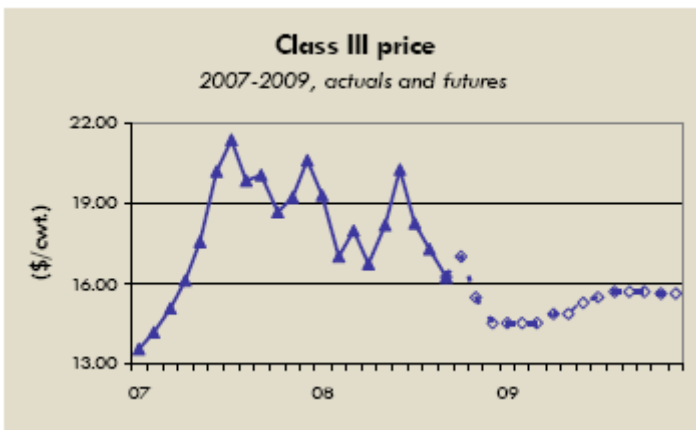
Analysis

The October stock market decline and credit crisis has seriously impacted consumer sentiment. Comments from USDA and commercial firms indicate that although milk use is up, the strength recently has come from exports. US consumption is weakening. It also is showing that food-service use is dropping. Lower other than American style cheese use gives this indication.



Source: Daily Dairy Report

The most recent income over feed cost calculation rose from Sept, \$8.57, to \$9.30/ cwt. for Oct. Even though the all-milk price fell \$0.80/ cwt., feed costs dropped more. Corn prices fell to \$3.99, soybean to \$8.66 and hay to \$172 per ton. My most recent dairy budget model calculations put total costs very close to the Oct all-milk price of \$17.60/cwt for dairy herds with milk production at 20,000 pounds per cow. However, looking at 2009 Class III futures prices, the average is \$15.25 making all-milk prices below cost.



Source: Daily Dairy Report

General Economy

Retail Trends: Iowa's Retail Sector and Holiday 2008 Projections

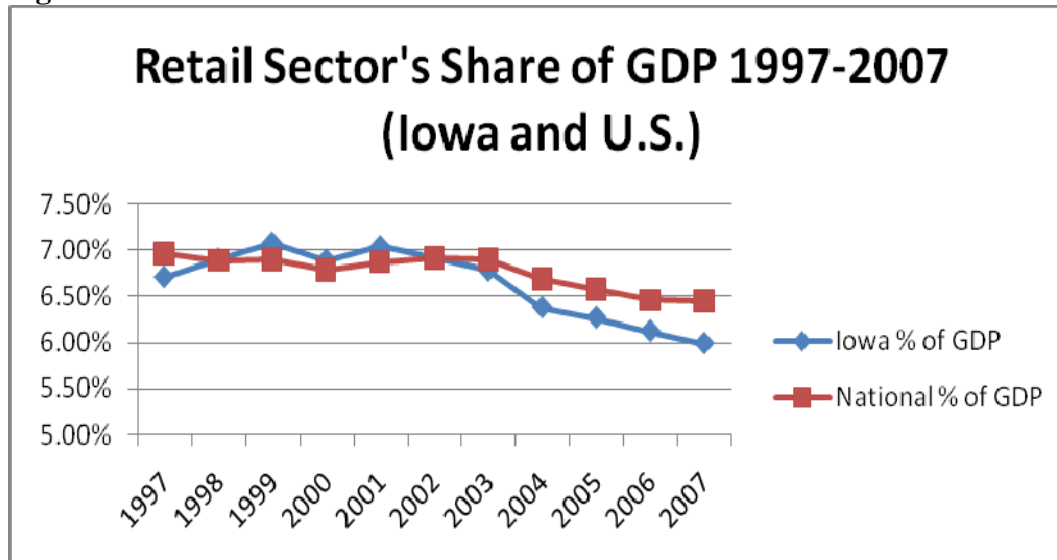
It's that time of year again where retailers hope to turn red to black in the books, however this year there probably be more red than black. The largest consumer spending expansion that paralleled the housing boom has come to a halt, with the retail sector beginning to experience declines as early as the first quarter of 2007. Consumer spending in the U.S. accounts for between 6 and 8.5% of GDP depending on which categories are included and roughly 71% of economic activity is accounted for by consumer spending. It is no surprise then that when people close their pocketbooks, the economy suffers. The question is how severe this impact will be here in Iowa.

Iowa's taxable retail sales, adjusted for inflation, fell 1% from fiscal year 2006 to 2007 and then rose 2.6% from 2007 to 2008. This unusually large increase in real retail sales from the 2007 fiscal year to the next does not mean Iowa is immune to the national trends in retail. Taxable sales when considered as a percentage of GDP have been on the decline since 2001, falling by more than 6%. Although data suggests the retail sector in Iowa has been turbulent since the recession of 2001, trends over time allow predictions to be made.

Retail Sector in Iowa

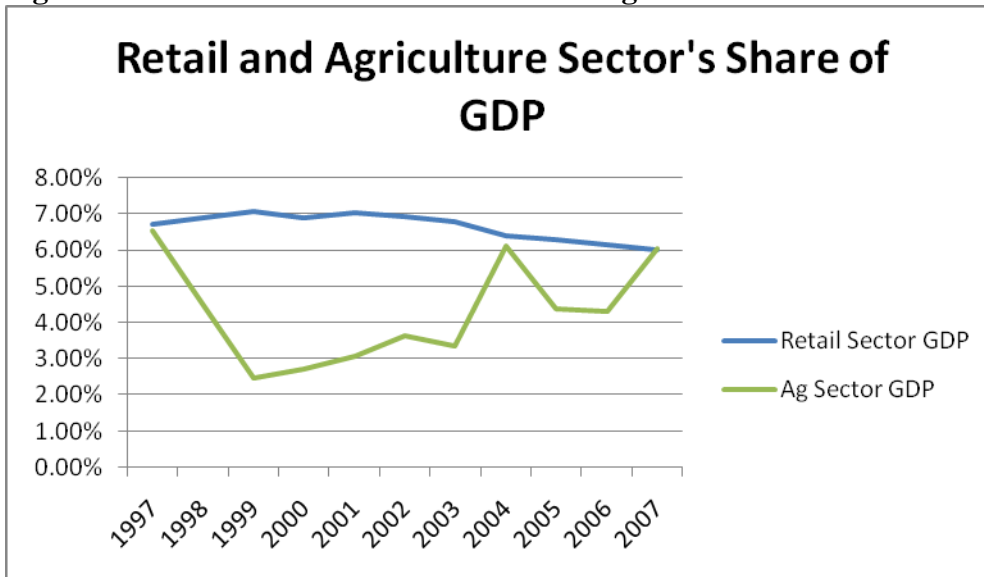
Nationally, the retail sector is the second largest economic sector in numbers of employees and number of establishments and as previously mentioned accounts for about 8.3% of GDP. Here in Iowa however, our economy does not depend on the retail sector to the same degree. In 2007 the retail sector accounted for about 6% of Iowa's GDP down from a peak of 7% in 1999. Behind manufacturing and government, the retail sector is the third largest employer with the health care sector following closely. The number of retail establishments in Iowa tops all categories despite the fact that the number of retail establishments in Iowa has been declining for more than a decade. To illustrate this decline consider that in 1997 Iowa had 19,826 retail establishments while in 2006 the number was 13,495, representing a 32% decline. The data suggests that Iowa's retail sector has been declining for more than a decade along with its relative importance to GDP.

Figure A: Retail Share of GDP National and Iowa



Given the perception (and reality) of Iowa as an agricultural state, it may be counterintuitive to discover that despite the retail sector's decline it historically contributes more to Iowa's GDP than agriculture. Over the last decade, in only one year did agriculture's share of GDP exceed that of retail. The retail sector's share of 2007 GDP in Iowa is only the seventh highest following, in descending order: Agriculture, Finance and Insurance, Government, Real Estate, Health Care, and Agriculture. The fact that retail contributes less to GDP than these other sectors does not insulate Iowa from a recession. Because the retail sector spills over to other sectors as demand for goods declines, Iowa's manufacturing base equates to substantial recessionary risk due to the reduction in spending and retail demand.

Figure B: Relative Shares of Iowa's GDP: Agriculture and Retail



Holiday 2008 and Beyond

Iowa, like the rest of the nation, has seen retail space grow in what has been described as “over-retailing”. This phenomenon describes not only the increase in commercial retail developments but the number of establishments selling similar substitutable merchandise. The overall economic climate coupled with this phenomenon adds up to a perfect storm for retailers. The necessary conclusion is that the current number of retailers is not sustainable due to the decline in consumer spending and confidence and the beginning of 2009 will witness a surge of bankruptcies and store closings.

These impacts will be felt in Iowa but not the extent of other parts of the nation largely because Iowa witnessed less speculative development. For individual retailers however, this holiday season will be bleak. The National Retail Federation forecasts a holiday season year to year increase of 2.2% which is roughly half the ten year average and not nearly enough to keep many retailers in business. Unfortunately, this is likely a best case scenario. The actual holiday season could witness sales decline preventing many retailers from making it into the black this year. For small, independent Iowa retailers this holiday season will vary but only a select few will see sales increases. Non-traditional retail such as consignment shops and upscale used merchandise stores will fare better than highly specialized and gift retailers and will probably be the one bright spot in an otherwise dismal retail sector season. The other bright spot in retail will come from discount retailers like Wal-Mart who are experiencing sales growth as other retailers sales are plummeting. For locally owned retail establishments who are counting on the holiday season the picture is gloomy as competition with the mass retailers becomes increasingly difficult.

Iowa may not have an abundance of speculative retail developments that will falter but we do have a number of old retail establishments whether they be traditional shopping malls, or strip malls with increasing vacancies and low sales per square foot. These establishments will have a difficult time surviving after this holiday season and we would expect to see the increase in vacancies be too much for some to remain solvent. With retail stores cutting back on expansion for much of 2008 and planning to cut stores in 2009, these problems will only get worse.

The bottom line for the retail sector in Iowa is dismal. The 2008 holiday season will not be enough to save many retailers, bankruptcies and store closings will follow, and our retail landscape will be forced to evolve. It ultimately will be up to the consumer how many Iowa owned retail businesses can survive these tough times. As a new decade begins we will see a new leaner and more streamlined retail landscape than we do today.

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