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University Extension

Iowa Farm Outlook

Department of Economics
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Hog Return Outlook Deteriorates

Hog returns in 2008 were the worst since 1998 on the ISU Estimated Returns Series and while 2009 is expected to be better, it is not shaping up to be the a recovery year.. The USDA December Hogs and Pigs report released in late 2008 and along with expected demand factors at that time combined for a forecast of a breakeven year for producers in 2009. Since that time feed prices have decreased, but so has demand for pork and the **profit forecast for 2009 has deteriorated to an average loss of $15 per head**. Either world economic conditions will need to improve to strengthen domestic and export demand or pork supplies will need to decrease to return the industry to positive returns.

Corn and soybean meal prices have declined from the record levels of last June, but remain well above previous levels. Hog prices that briefly reached record prices in August have retreated and weaken further since the first of the year. Part of the weaker market is due to demand concerns related to consumer spending and exports during the current recession. These topics are addressed below. However, there are also supply concerns beginning to arise for late 2009 and 2010.

Supply Concerns
The USDA December Hogs and Pigs report indicated a reduction in hog supplies during 2008. The inventory of market hogs was lower than the year before as was the breeding herd inventory and farrowing intentions. However, since the report was released there are indications that US pork producers are ending the contraction and planning an expansion that could impact supplies as early as the fourth quarter of 2009.

Table 1 summarizes barrow and gilt and sow slaughter by quarter reported in the USDA report. The quarters are 13 week periods that match closely to the calendar months. The number of barrows and gilts slaughtered in US packing plants has declined from 9.1% over the year before to 2.0% under the year before for the ten weeks from early December through the first week of February. A portion of the decline is accounted for by a reduction in Canadian hogs slaughtered in US plants, but US finished hogs slaughtered in US plants continues higher than the same period the year before.

Canadian imports masks sow slaughter even more than barrow and gilt slaughter. Notice that the number of sows slaughtered in US plants that was running over 10% higher than the year before in the first half of the year was nearly 7% below the year before in the current quarter. After adjusting of imports of sows from Canada which have increased dramatically from 2007, the number of US sows slaughtered decreased nearly 7% in the fall quarter and 16% in the winter quarter. Based on sow slaughter, US producers appear to building the breeding herd. Gilt retention is the other part of the change in breeding inventory. University of Missouri gilt slaughter data also indicates that producers are rebuilding the breeding herd.

The Canadian hog inventory continues to decline. Fourth quarter 2008 marked the 13th consecutive quarter of year-over-year declines in sow farrowings. Its pig crop is 9% smaller than its fourth quarter peak posted in 2004. The Canadian 3rd and 4th quarter pig crops were down 2.0% and 3.5%, respectively from their 2007 levels. Farrowing intentions for the 1st and 2nd quarters of 2009 are down 5.4% and 2.7% from their 2008 levels.

Table 1. Barrow and Gilt and Sow Slaughter in US Plants, Imports from Canada and Hogs from US Farms, by Quarter 2008 versus 2007

	Total US B&G Slght	CND Import B&G Slght	US Finished B&G Slght	Total US Sow Slght	CND Import Sow Slght	US Sow Slght
Mar-May	9.1%	-25.3%	9.9%	10.3%	59.4%	3.0%
Jun-Aug	7.6%	-53.7%	9.5%	10.4%	29.4%	7.5%
Sep-Nov	1.5%	-68.1%	3.6%	-0.5%	43.3%	-6.8%
Dec-Feb	-2.0%	-78.5%	0.6%	-6.8%	58.0%	-16.0%

The number of slaughter hogs and feeder and pigs coming from Canada has declined since MCOOL went into effect September 30, 2008. There were approximately 1.38 million feeder pigs imported from Canada during the 13 weeks (one quarter) beginning November 1. This compares to the 8.753 million Canadian pigs born October – December or about 16% of the fourth quarter pig crop. The import number is 50,200 fewer than the year before and there were 309,000 fewer pigs born than the year before. This suggests that Canada will finish about 250,000 fewer pigs during this period than the year before. Slaughter hog imports from Canada have also declined, down 77% or more than a million head between early October and mid-February. Unless Canadian consumers increase their pork consumption significantly the extra pork will enter the export market to the US or compete against the US in other markets. Since the Canadian currency value has decreased relative to the US, Canadian pork may be a better value in export markets.

Demand Concerns

Pork exports in 2008 were nearly 50% higher than 2007 and well above the trend line growth of 15% per year. It is unlikely that US pork exports will increase in 2009 over 2008 and could decrease significantly. The current recession is global reducing the purchasing power in customer countries. Also, the value of the US dollar has increased relative to most currencies making US products more expensive to importing consumers. Pork not exported adds to the domestic supply and pressures prices here.

Table 2 shows the domestic per capita pork consumption for three export scenarios based on production being 2.8, 3.9, 3.5 and 3.0 percent lower in 2009 than 2008 for quarters 1 to 4, respectively (predicted from the December Hogs and Pigs report). The table also has Iowa Southern Minnesota carcass hog prices for 2008 and the 2000-2008 average to show the quantity and price relationship. Demand in 2008 was below average in the first quarter and arguably the fourth quarter as prices were lower for the comparable supply. Second and third quarter prices were significantly higher than the average on a modest decrease in supply suggesting that demand in these two quarters was quiet strong due largely to aggressive exports.

Domestic per capita consumption for 2009 is shown assuming the reduced production noted above and three export scenarios. The first assumes exports equal to 2007 levels. The second scenario puts 2009 on the 2002-2007 export trend-line growth of 15% per year for 2008 and 2009. The third assumes that 2009 exports equals 2008 levels in each quarter.

While no prices are forecast for these scenarios, it is important to notice that domestic per capita supplies are significantly larger than 2008 and the average. The first two scenarios have domestic supplies larger than any year since at least 2000 for the first three quarters. In the fourth quarter, the trend line exports are actually larger than where 2008 ended. All else equal, larger supplies will result in lower prices.

Table 2. Per Capita Pork Consumption and Iowa Southern MN Carcass Price by Quarter, 2008 Actual, 2000-2008 Average, and Three 2009 Export Scenarios

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	Cons. Lbs	ISM $/cwt	Cons. Lbs	ISM $/cwt	Cons. Lbs	ISM $/cwt	Cons. Lbs	ISM $/cwt
2008	12.6	56.13	11.7	74.38	12.0	79.32	13.2	58.80
Avg	12.6	58.79	12.2	68.20	12.4	67.47	13.6	57.22
2007	15.0		13.9		13.7		14.3	
Trend	14.3		13.4		13.2		13.6	
2008	14.2		12.1		12.7		14.1	

Other factors, however, are not equal. Chicken, turkey and beef supplies are all forecast to be lower in 2009 than they were in 2008. Smaller supplies of competing meats should be supportive of pork prices. The big unknown is how consumer spending impacts pork demand. Rising unemployment is reducing consumer income. Increased personal savings by consumers as they become more conservative with purchases reduces consumer spending even further. In general, as consumer spending declines so does the demand for pork. In previous price forecasting models, cross-price elasticities (impact of chicken and beef on pork price) are slightly larger than income elasticities (impact of consumer spending on pork price). However, it is unclear if previously developed models apply during the current economic conditions.

Summary

The optimism of smaller meat and pork supplies and lower feed prices is quickly giving way to weaker demand and falling prices. What was expected to be a breakeven year two months ago is now looking like another year of losses. While six-eight consecutive quarters of losses is common for hog cycles, the concern is that the breeding herd appears to be growing before the industry returns to black ink.

John D. Lawrence

The Early Word on 2009

USDA held its annual Agricultural Outlook Forum at the end of February. During the Forum, USDA analysts released an early preview of crop projections for the 2009 crop year. The projections are unofficial, but they do highlight current issues to monitor as the 2009 crop season progresses. Below is a summary of that preview for corn and soybeans. The full preview can be found at http://www.usda.gov/oce/forum/2009_Speeches/Speeches/GrainsOilseeds.pdf.

Corn Outlook

For corn, USDA analysts foresee planted acreage holding at 86 million acres, the same level as 2008. Based on the yield trend from 1990 to 2008, 2009 corn yields are projected at 156.9 bushels per acre, up 3 bushels from 2008. The higher yield and higher ending stocks from 2008 lead to a total corn supply of 14.17 billion bushels, just 200 million bushels under 2007 supplies. Feed demand is projected to continue falling as the livestock industry is still under contraction and ethanol co-products continue to fill part of overall feed needs. Corn demand via ethanol is projected to grow to 4.1 billion bushels. This is somewhat below the level required to fill the Renewable Fuels Standard target for conventional biofuels, as USDA projects that some fuel blenders will utilize Renewable Identification Number (RIN) credits to meet their biofuel requirements over the couple of years. Food, seed, and other use is held steady at 1.3 billion bushels. Exports are expected to rebound slightly in 2009 to 1.85 billion bushels with a projected fall in the supply of feed wheat. Overall, total use is projected to exceed total supply by 70 million bushels, leaving ending stocks for 2009 slightly below those for 2008. Prices are projected to continue to slide, down to $3.60 per bushel.

Table 1. U.S. Corn Supply and Use

		2007	2008[a]	2009[b]
Area Planted	(mil. acres)	93.5	86.0	86.0
Yield	(bu./acre)	150.7	153.9	156.9
Production	(mil. bu.)	13,038	12,101	12,365
Beg. Stocks	(mil. bu.)	1,304	1,624	1,790
Imports	(mil. bu.)	20	15	15
Total Supply	(mil. bu.)	14,362	13,740	14,170
Feed & Residual	(mil. bu.)	5,938	5,300	5,200
Ethanol	(mil. bu.)	3,026	3,600	4,100
Food, Seed, & Other	(mil. bu.)	1,337	1,300	1,300
Exports	(mil. bu.)	2,436	1,750	1,850
Total Use	(mil. bu.)	12,737	11,950	12,450
Ending Stocks	(mil. bu.)	1,624	1,790	1,720
Season-Average Price	($/bu.)	4.20	3.90	3.60

[a]Projections from USDA's February 2009 WASDE report
[b]Unofficial projections from USDA's Agricultural Outlook Forum

Soybean Outlook

For soybeans, USDA analysts are projecting a record year. They project a slight increase in planted area, to 77 million acres, as other crops see reduced plantings. This would be a record amount of land planted to soybeans. Much of the shift is attributed to soybeans' lower input costs. As with corn, projected yields are 3 bushels than in 2008, based on 1990-2008 trends. This puts production at 3.24 billion bushels, which would be a record. Domestic soybean crush is projected to increase to 1.675 billion bushels, mainly based on higher expectations for soybean meal exports. Soybean exports are also expected to set a record, with 1.225 billion bushels leaving the country. But the growth in production exceeds the growth in usage and ending stocks are expected to climb to 380 million bushels. The 2009 season-average price for soybeans is forecast at $8.00 per bushel.

Table 2. U.S. Soybean Supply and Use

		2007	2008[a]	2009[b]
Area Planted	(mil. acres)	64.7	75.7	77.0
Yield	(bu./acre)	41.7	39.6	42.6
Production	(mil. bu.)	2,677	2,959	3,240
Beg. Stocks	(mil. bu.)	574	205	210
Imports	(mil. bu.)	10	9	3
Total Supply	(mil. bu.)	3,261	3,173	3,453
Crush	(mil. bu.)	1,801	1,650	1,675
Seed & Residual	(mil. bu.)	93	163	172
Exports	(mil. bu.)	1,161	1,150	1,225
Total Use	(mil. bu.)	3,056	2,963	3,073
Ending Stocks	(mil. bu.)	205	210	380
Season-Average Price	($/bu.)	10.10	9.25	8.00

[a]Projections from USDA's February 2009 WASDE report
[b]Unofficial projections from USDA's Agricultural Outlook Forum

Overall, soybean was the crop projected to increase in acreage. In fact, total land area devoted to farm program crops (corn, soybean, wheat, barley, oats, sorghum, cotton, and rice) is expected to fall by roughly 5 million acres. The general economic conditions, both here in the U.S. and worldwide, will continue to weigh on agricultural markets. Some of the projected fall in season-average prices is due to more limited forward pricing opportunities. During the 2008 marketing year, many producers were able to lock in prices above the cash market and this helped boost the 2008 season-average prices. The market for 2009 thus far has not provided similar opportunities.

Looking Over the Short Term

The status of the South American crops is still a major issue for the markets, but more recent rains have eased some concerns. It remains to be seen how much production was lost to the drought down there and the impact these later season rains have on crop recovery. The February USDA projections for South American production show corn production down 21 percent from last year and soybean production down 6 percent. The soybean production drop is despite a 6 percent increase in soybean planted area in Argentina.

The latest weekly export figures show declines across the board for corn as sales were off 66 percent from the previous week and exports were down 15 percent. The sales figure was well below trade expectations. Exports commitments so far this marketing year are 44 percent lower than last year. Soybean export also showed some weakness this week. Net sales were down 69 percent for the week and exports were down 28 percent. But soybean export commitments are still 5 percent ahead of last year.

Two major USDA reports will also be released later this month. The Grain Stocks report will provide mid-marketing-year snapshot of crop usage thus far. While the Prospective Plantings report will provide an updated look at 2009 acreage decisions.

Chad Hart

January Milk Production up 1.16%, 2008 Milk up 2.3%

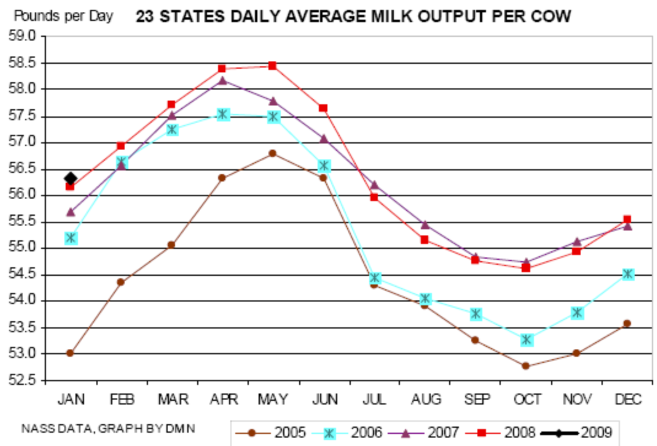
January 2009 23 major dairy states milk production rose nearly 1.4%. Production per cow was almost unchanged from one year ago, up only 5 pounds. Milk cow numbers were 58,000 more than Jan 08 but 12,000 less than Dec 08. This is the first month since Feb 07 that month to month cow numbers have declined. December 08 milk production was revised up by 44 million pounds, a 0.3% point increase.

Iowa Jan 08 milk production was up over 0.8% compared to one year ago. Cow numbers were the 1000 lower than one year ago, but milk production per cow was up by 20 pounds. Dec 08 Iowa cheese production was 17% higher than one year ago and 13% more than Nov 08.

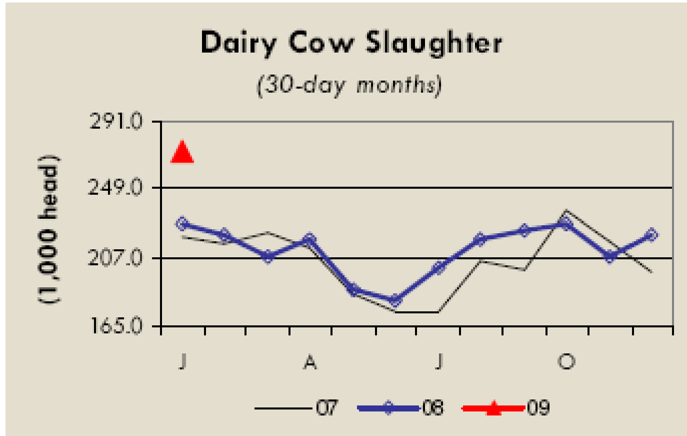
Milk Production: Selected Dairy States, January 2009

State	thousands 2008 cow numbers	thousands 2009 cow numbers	% change cow numbers	pounds 2008 milk per cow	pounds 2009 milk per cow	% change milk/cow	million pounds 2008 total milk production	million pounds 2009 total milk production	% change total milk
Iowa	216	215	-0.46%	1680	1700	1.19%	363	366	0.83%
MN	463	468	1.08%	1610	1630	1.24%	745	763	2.42%
WI	1250	1255	0.40%	1635	1645	0.61%	2044	2064	0.98%
IL	103	102	-0.97%	1615	1610	-0.31%	166	164	-1.20%
CA	1838	1831	-0.38%	1900	1880	-1.05%	3492	3442	-1.43%
CO	126	129	2.38%	1880	1940	3.19%	237	250	5.49%
ID	534	554	3.75%	1870	1820	-2.67%	999	1008	0.90%
NM	336	334	-0.60%	1900	2015	6.05%	638	673	5.49%
PA	552	550	-0.36%	1630	1630	0.00%	900	897	-0.33%
NY	626	624	-0.32%	1660	1670	0.60%	1039	1042	0.29%
TX	402	430	6.97%	1685	1780	5.64%	677	765	13.00%
23-State	8451	8509	0.69%	1741	1746	0.29%	14714	14885	1.16%
US total	9276	9320	0.47%	1722	1727	0.29%	15976	16100	0.78%

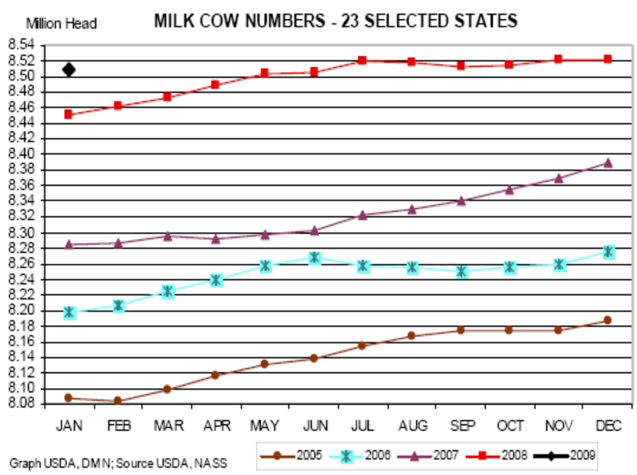
USDA estimated that 281,100 dairy cows were slaughtered in Jan 09. This is a very large increase from one year ago, +19%, up 45,400 from one year ago. The Jan 09 was the largest monthly slaughter since Jan 97. Even though this is a large monthly laughter, about 70,000 more than the previous month, the milking herd decline was only 12,000 lower. Replacement heifer inventories are very large, thus unprofitable dairy cows can be replaced with heifers that may prove to be better financially for dairy herd owners.



Source: Dairy Market News



Source: Daily Dairy Report



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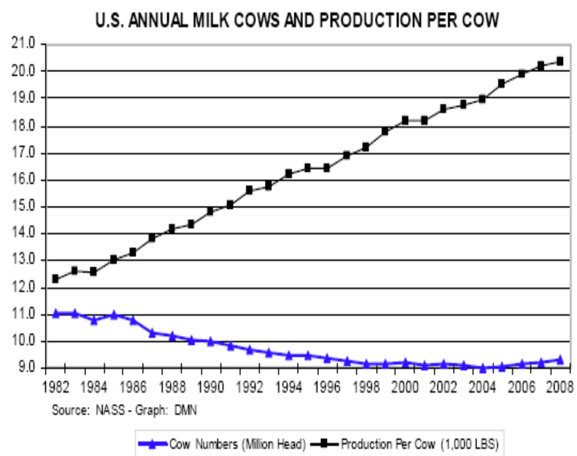
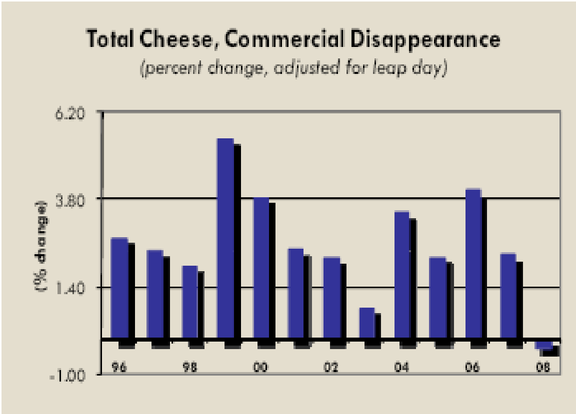


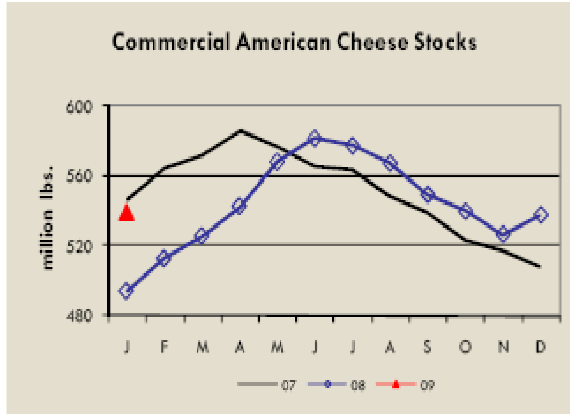
Source: Dairy Market News

Demand or Disappearance

Total cheese disappearance during 2008 was down 0.3% compared to 2007 adjusted for calendar composition. This is the first year since 1975 that cheese consumption declined. During the past 10 years, cheese consumption has increased 2.9% on average. American style cheese increased 2.5% but all other cheeses dropped by 2%. Export sales of cheese were up by 31.7% while US cheese use was 1% lower. Butter consumption was 12.5% higher for the year with US usage up 5.7% while export use rose 124.4%. Fluid milk sale for 2008 was 0.18% lower compared to 2007. That is the second year for fluid milk consumption decline. It had risen during 2005 and 2006.



Source: Daily Dairy Report



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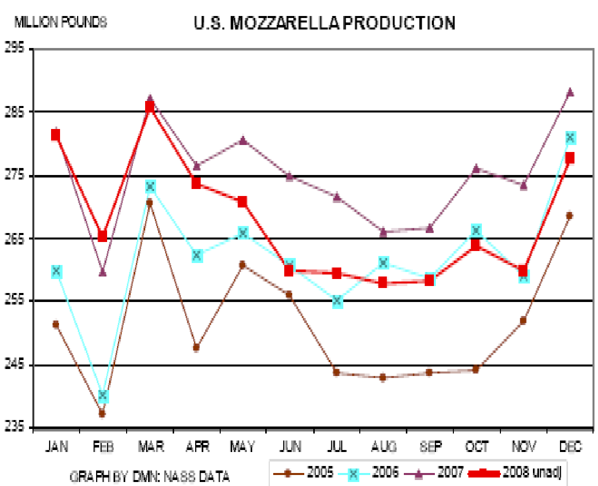

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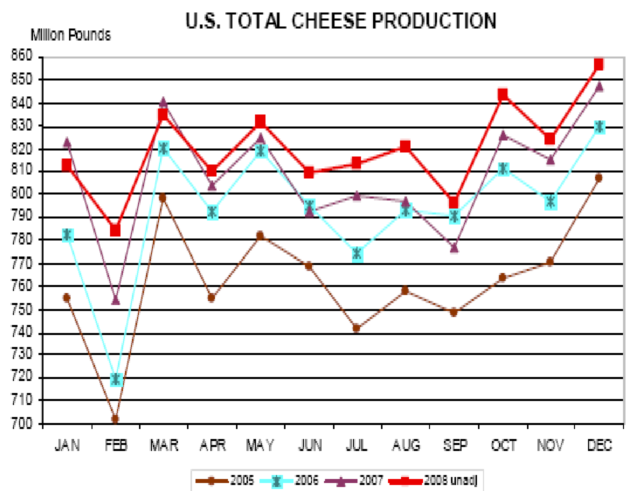


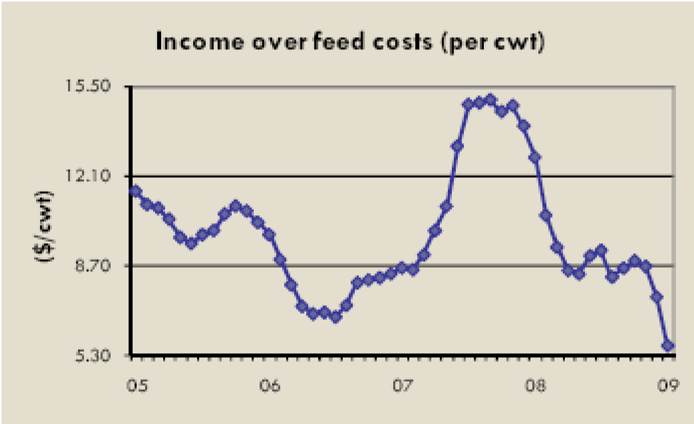
Source: Dairy Market News, USDA

The Consumer Confidence Index reported in January declined 37.4 and then in February was reported at an all time low of 25. The Consumer Confidence Index began in 1967. Lynn Franco, director of the Conference Board's Consumer Research Center was quoted as saying that "All in all, not only do consumers feel overall economic conditions have grown more dire, but just a disconcerting, they anticipate no improvement in conditions for the next six months."

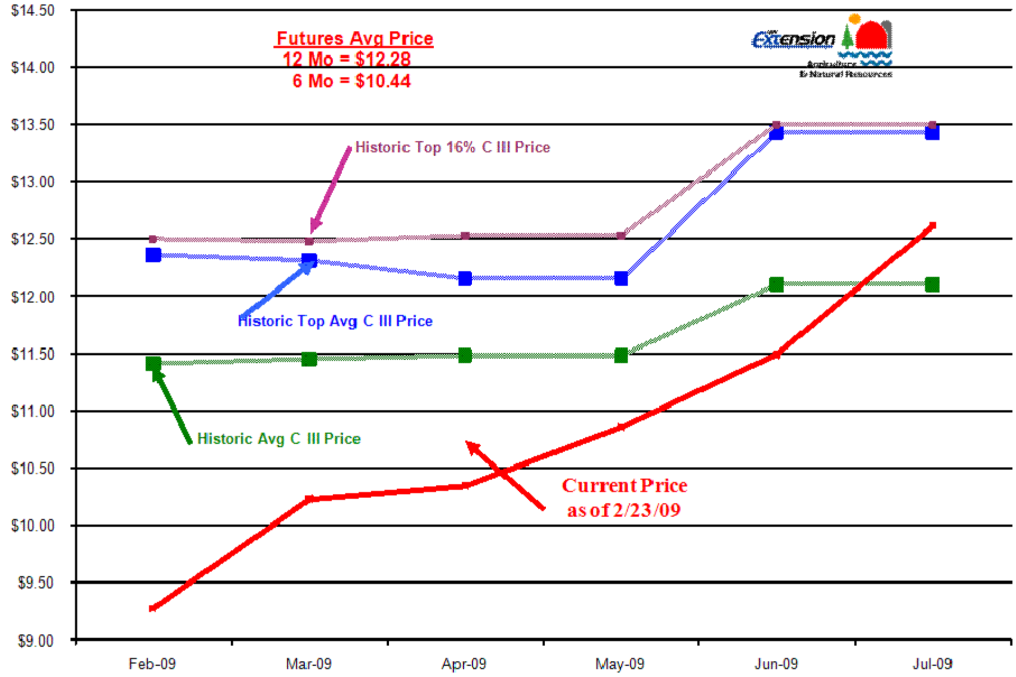
Source: USDA, NASS

Analysis

Cheese prices are showing some strength recently. From Nov 13 to Nov 26 cash cheese price rose 9.5cents mostly on unfilled orders. That shows an unwillingness of cheese sellers to move product at early Nov prices.

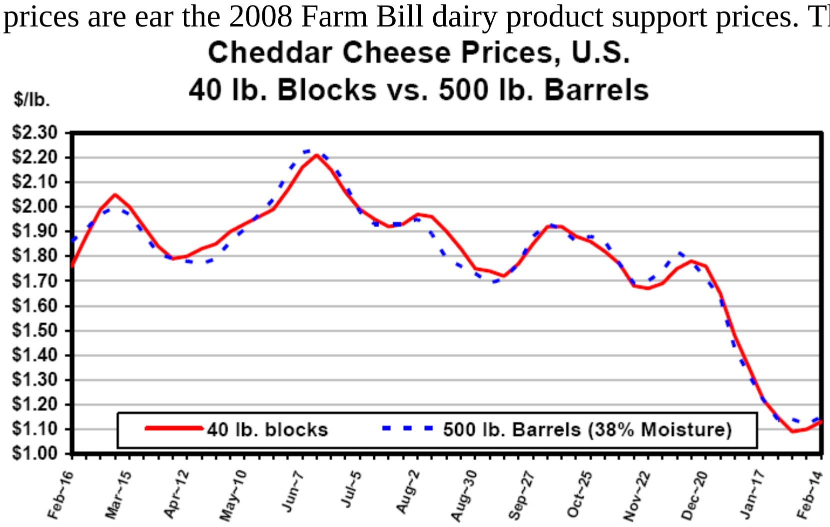


Milk pricing opportunities still appear to be non-existent, at least compared to production costs. My latest Iowa dairy budgets showed production costs ranging from $14.75 to just over $17.43. The closest to breakeven was the freestall model selling at least 24,000 pounds of milk per cow. The most recent milk-feed ratio was calculated at 1.69. That is near historic lows. Most of the current milk prices offered at the CME for the first half of 2009 are near support price. Thus it does not make sense to do any milk pricing for the next few months.



Source: Hedging Opportunity web site, UWEX

As the chart below describes, cheese prices have been suffering since June of last year. The current cheese prices are ear the 2008 Farm Bill dairy product support prices. These are $1.13 for blocks and $1.10 for barrels.

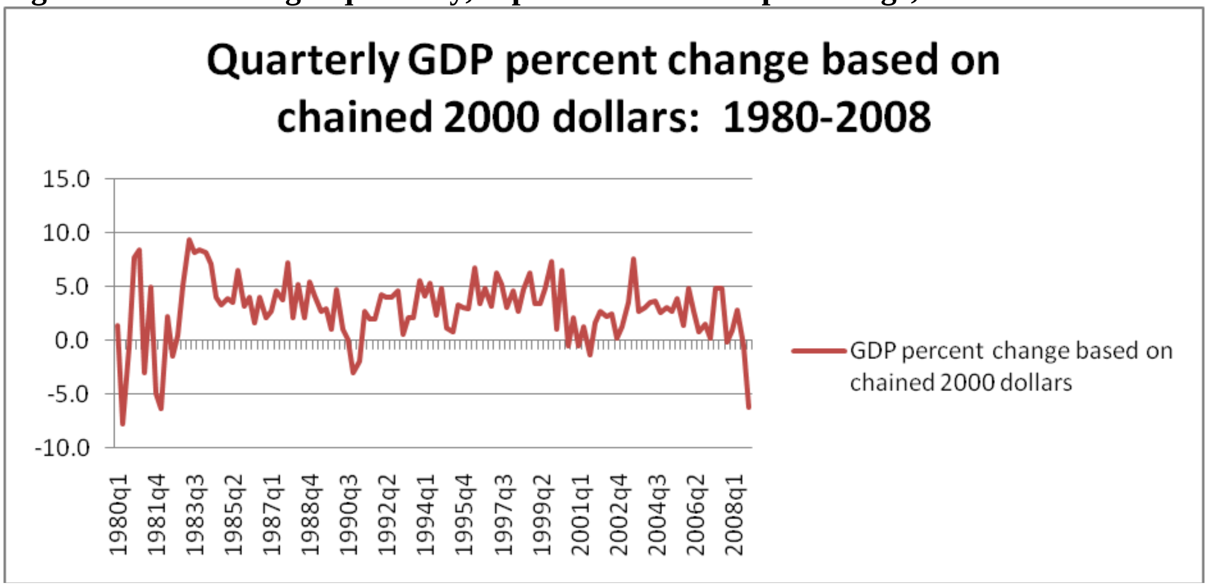


Robert Tigner

Why a Little Recession Now and Then is a Healthy Thing

Updated figures from the Bureau of Economic Analysis show that U.S. GDP fell by an annual rate of 6.2% in the 4th quarter of 2008, or in current terms a 5.8% drop. Since 1947, the U.S. has only experienced greater annualized declines from one quarter to another four times in 247 observations, with the most recent of these events occurring in 1982. The rarity and magnitude of this event cannot be ignored, although its meaning and implications may still be hotly contested.

Figure 1: GDP changes quarterly, expressed as annual percentage, 1980-2008.

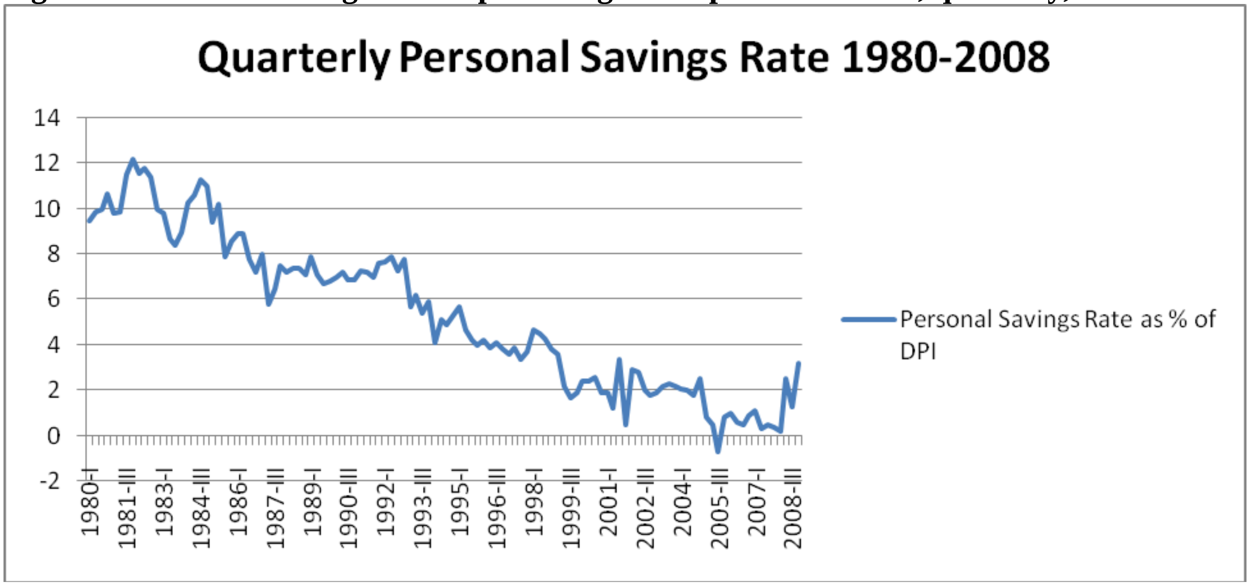


What we do know for sure is that this 6.2% drop occurred with a simultaneous fourth quarter decline in consumer spending of 4.3%. Estimates peg the role of consumer spending in the economy at about 2/3 of gross domestic product, indicating that when Joe the consumer closes his wallet the whole economy feels the tremor and the end of 2008 confirms how important this aspect of our economy is.

The so-called Paradox of Thrift, which describes how the consumer's rational response to an economic downturn of increasing savings actually worsens the economic picture, has taken a lot of blame recently for declining GDP and the exacerbation of the recession. This simplistic approach to our business cycle implies that the recession would end if everyone would just spend money as though we aren't in one. The major problem with this approach is that it ignores that the fact that the record consumer spending expansion that pre-dates the recession may be symptomatic of the very causes of the recession, and therefore prescribing spending as a solution is in effect suggesting the cause and the cure are the same. This would be like a doctor telling you that one of your bad habits caused a serious decline in your health and then telling you that the good news is that that same habit can also improve your health. Sound unreasonable? It is.

What gets lost in the mainstream version of this discussion is that savings is necessary to the growth and strength of the economy, and while its increase in the short term may be negative it is a long term benefit. Fundamentally, savings represents a pool for lending that in turn can be directed towards productive investment and capital growth, requirements for economic growth. Because there has been little to no incentive for people to save due to very low interest rates, the recession provides a signal to consumers that interest rates were failing to. At the macroeconomic level this savings has positive benefits and implications for sustainable and growth enhancing levels of interest rates. Often forgotten at the microeconomic level, savings represents emergency reserves and the consumer's ability to stay liquid. Liquidity reduces risk and serves an important stabilizing role for both businesses and the individual allowing individuals to smooth consumption and businesses to fund investment with working capital. The importance of liquidity has been declining as a goal across the board in our economy with the ill effects apparent in the housing crisis, leverage ratios for firms, and in our government budgets. The figure below demonstrates how the U.S. savings rate has been under attack.

Figure 2: Personal savings rate as percentage of disposable income, quarterly, 1980-2008.



Another upside of the recession as it relates to consumer spending is the correction that necessarily has to be made in the retail sector. A new term, "over-retailed", describes the current phenomenon of too many malls, retail venues, and retail stores competing for the same retail dollars. The result has been the squeezing out and consolidation of profits amongst a select group of firms. Given that the retail sector is the second largest employer nationally and the third largest here in Iowa, any retail contraction will have serious implications for employment in the short term. In the long run however, the bankruptcies and closings of retail stores will help restore profits to the sector and allow firms that survive the recession to better position themselves to respond to consumer demand and hence capture producer surplus. In the commercial property arena, this trend towards equilibrium will provide opportunities for new businesses by lowering the costs of entry into this sector and promoting investment and growth for existing businesses.

The recession, while painful in the short run, will serve a vital role in promoting our long term economic growth by correcting distortions dictating consumer choice between spending and saving. The correction will also address the distortions created by easy credit in the business sector which has misdirected resources away from their highest and best uses. While the news may seem grim, the spring cleaning of our economy will rid our economic house of malinvestment and return us to sustainable patterns of consumption and savings behavior.

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