

The Kiplinger Agriculture Letter

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Dear Client:

Washington, Sept. 25, 2009

Uncle Sam will buy a ton of food products next year, with a big new focus on fruits and veggies geared to a wide variety of public nutrition programs.

**FOOD
AID**

Flowing to farmers and other food producers:
A whopping 70% of USDA's FY '10 budget.

The wide-open spigot comes courtesy of three sources: The '08 farm bill, the stimulus bill, which is pouring \$11.3 billion into food aid, and ramped up benefits as more folks are eligible for food program benefits. Further, a full-bore campaign by Ag Sec. Tom Vilsack to improve nutrition in America will also play a role. The projected \$93.5 billion for USDA food programs in FY '10 will be up 70% since '07...a sum equal to 8% of retail food spending vs. 5% in '07. In fact, the share is greater because USDA buys at wholesale.

The biggest tab is for SNAP...

the Supplemental Nutrition Assistance Program (food stamps). Nearly 37 million people will get benefits next year, an increase of almost 30% from '08.

School lunches are next. Of 33 million kids taking the lunches, those eligible for free ones are up by almost 15% since '08, bringing the share getting free meals to half of participants.

WIC (Women, Infants and Children) will help 10 million folks next year.

New WIC rules will kick in Oct. 1, expanding eligibility and availability of fresh produce to program participants. About 25 states are already implementing the changes.

Two farmer friendly features are embedded in USDA's scaled up food aid:

First, bundles of fresh produce are tied to major programs: School lunches, SNAP, WIC and food banks. The Ag Dept.'s top fresh fruits and vegetables initiative will soar from \$10 million in FY '08 to \$101 million in FY '10 and \$150 million in '11. Plus \$21 million in '10 will be set aside for seniors to buy produce at farmers' markets.

Second, public nutrition aid is being wedded to direct farm marketing efforts, so farmers can profit more often from the USDA programs by selling to local schools, farmers' markets and food banks. USDA calls it "Know Your Farmer, Know Your Food." It is funding grants to develop local marketing channels, help schools source produce from local farms and use electronic benefits transfers (now standard in supermarkets) at farmers' markets, letting farmers make direct sales to food stamp recipients. Vilsack wants to direct food aid spending to maximize receipts going directly to farmers and rural firms, helping them to rebound from the recession. For starters, the potential of direct farmer marketing in the Northeast will be assessed by USDA.

USDA will also try to simplify access to its complex medley of food programs.

Six states...Mass., Mich., Ohio, Pa., Wis. and Wash...are funded to try improvements, including an easy application process by phone and recruiting faith based entities to help elderly citizens apply. Only 30% of eligible seniors now apply for food stamps.

AG IMPORTS IN '10

↑	Total Farm Imports Recovery of volume plus higher prices lift receipts
↑	From Mexico Lots of fruit, cattle, coffee, seafood, snacks and more
↓	From Europe Fewer high value foods
↑	Tropical Produce More Western Hemisphere fruits, nuts and the like
↔	Wood Products Lumber, plywood recover in '11 along with building pace
↑	Beef Ample world supplies and a tiny U.S. cattle herd
↓	Pigs Canadians raising fewer hogs

CROPS

The global shortage of medium grain rice varieties is setting off a scramble among rice growers in some states to raise enough of that rice for Kellogg's and other U.S. and foreign buyers. Kellogg's uses such rice in its breakfast cereals.

Ark., La. and Calif. farmers are growing more short and medium grain types at the expense of long grain rice, though they have also increased rice acres overall. USDA estimates that total acreage of short and medium types is up 7%. However, rice, like other field crops this year, matured late, and remains highly vulnerable to early frosts into Oct. in many areas...production will be a guessing game till then.

BARLEY

Good news for Eastern farmers: Barley will serve as an ethanol feedstock for a facility being built by [Osage Bio Energy](#), a Virginia ethanol producer. Its plant will be up and running in June '10. The Virginia Farm Bureau Federation and Perdue Agribusiness, a regional grain firm, are helping Osage work with farmers to seed up to 300,000 acres to supply 30 million bu. of barley for the plant's first year. Farmers will seed in the fall and harvest in early summer, replanting for a crop of soybeans in the same year. Two crops in one season make barley a viable option to corn as a biofuels feedstock...supplementing corn instead of competing with it.

Barley acreage in the Mid-Atlantic will triple just to supply the new plant. Va., Md. and Del. now harvest about 90,000 acres a year. Yield tests run by Osage on Mid-Atlantic farms showed average yields exceeded 100 bu./acre...fairly close to corn yields (100-140 bu.) in that region. Those barley yields are much higher than in the shorter season Northern Plains, where they average 40-60 bu./acre.

Barley growers want to expand their markets beyond fuel, feed and beer.

Food uses are going to get a lot more attention, rooted in FDA confirmation of hulled barley and its products...pearl barley, flakes, flour...as being heart healthy, with as much as 9% fiber. The National Barley Foods Council expects to expand sales by promoting barley's high levels of fiber throughout the kernel, even after the bran is removed...not true for wheat and oats. See kiplinger.com/letterlinks/barley.

TRADE

USDA is sure to take heat in setting sugar import quotas for the next year... From sugarcane and beet farmers, who will produce over 8 million tons, a big crop, and don't want this year's high prices to be smothered by surplus sugar.

And from U.S. food and beverage makers, who want to import lots of sugar to deflate U.S. wholesale prices to near world prices. USDA projects sugar stocks for the year ahead to be a scant 8% of national use. Plus sugar beets being harvested in the North are late to mature, so sugar content may fall short of USDA's estimate.

USDA faces a handicap in setting the quotas: Guessing exports from Mexico, which sells sugar freely to the U.S. under the North American Free Trade Agreement. In the past year, it has depleted supplies while hiking sales to the U.S., where prices are higher. Now it's importing more to refill the void. That's a new move for Mexico, and its past year's sales to the U.S. have jumped to 12% of U.S. sugar consumption.

Expect USDA to set quotas conservatively, expanding them later if need be.

Also, USDA will allocate to the domestic market U.S. farmers' full output of sugar, which will jump because farmers hiked beet acreage 15% over last year. So, although the weak economy will dent sugar use in '10, USDA is required to allocate at least 85% of expected sugar use to U.S. producers...plenty to exhaust their output.

China's threatened antidumping tariffs on U.S. chicken would pose real harm to U.S. poultry exporters. China's poultry industry has been itching to hit U.S. exports because of a provision advancing in Congress that bars USDA from approving terms for China's chicken to enter the U.S. China threatened an antidumping case on poultry shortly after Obama imposed new tariffs on Chinese tires. The rub: The U.S. exports about 700,000 metric tons of poultry to China annually. Most exports are wing tips and feet...products diverted to pet food and rendered items if China doesn't buy them.

SENATE AG COMMITTEE	<p><u>Sen. Blanche Lincoln will hit the ground running</u> as the new chief of the Senate Committee on Agriculture, Nutrition and Forestry.</p> <p>The farm-raised Arkansas Democrat has a good understanding of ag issues.</p> <p><u>Among her top goals: Mandating more discipline for commodity futures...</u> especially derivatives, limits on big speculators and more trading transparency.</p> <p><u>Revising and updating school food programs</u> for another five years... \$17 billion a year in food aid and nutrition training that affects nearly all kids.</p> <p><u>And digging in against further cuts in subsidies to big farm operations.</u></p> <p>She'll get help from Sen. Saxby Chambliss (Ga.), the panel's ranking Republican. Southern growers of cotton, rice, peanuts, soybeans and other crops expect it.</p> <p><u>Her ag panel chairmanship also boosts her leverage on other matters...</u> bills on which her committee has a role but not primary jurisdiction. Examples:</p> <p><u>Stricter food safety laws</u> and expanded FDA inspections. Food processors, in general, and the House back tougher action, so look for the Senate to act.</p> <p><u>Expanded trade</u>, including greater access for ag product sales to Cuba, which buys a lot of what Ark. produces...chicken, corn, soybeans, rice and more.</p> <p><u>And the carbon cap and trade mandate</u>, which is in the House energy bill. She'll join with Republicans and a handful of other Democrats in the Senate to block such climate change action from any energy bill OK'd in this Congress.</p>
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LIVESTOCK In the works...an idea spawned by the nation's veterinarians:
A national board to set guidelines for the humane care of farm animals.

The American Veterinary Medical Assn. is drafting a proposal for a standards board with broad participation that would set guidelines beyond the federal and state laws that simply ban animal cruelty. Livestock owners want an alternative to the series of statewide ballot measures of recent years that mandate animal care as envisioned by the Humane Society of the U.S...Calif.'s ban on cages for laying hens, for example. To succeed, national standards would have to be credible, balanced and practical, so they make clear sense to packers, food companies and others who'd apply them.

In Ohio, voters are likely to launch a trial balloon for such a board in Nov. by passing a ballot measure to create a broad based panel that would set standards and enforce animal care regs. The outcome may help those drafting a national plan.

Small, state inspected meat plants will finally get to sell nationwide in '10 when USDA implements the '08 farm bill's OK for sites with fewer than 25 workers to market across state lines. The small state meat and poultry plants must adhere to all USDA food safety regs, and their products must carry USDA's inspection mark. States with such inspection systems...presently, 27 of them...have sought the change for over 25 years. More on USDA's proposal is at kiplinger.com/letterlinks/stmeat.

Swine experts are baffled over a disorder making baby pigs sick in Europe. Pigs fewer than five days old are getting diarrhea, and some of them are dying in Denmark and elsewhere. It's worrisome mainly because its cause is still unknown. A much smaller headache than H1N1 for swine owners, but worth keeping an eye on.

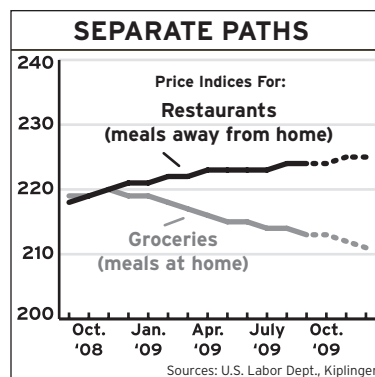
U.S. dairy farms are finally turning the corner against excess milk output and depressed prices. They culled 28,000 cows in Aug. and have reduced the herd by over 150,000 in the past year, managing to trim Aug. output 0.2% vs. a year ago. They've responded to moderating grain prices with more feed, hiking output per cow. Prices are slowly recovering...the all milk price will rise \$2/cwt., to \$14 or so by Jan. Of course, that's still far short of what's needed to pay farmers' production costs.

Congress will help out with a further round of payments: Up to \$1/cwt., on top of the \$1.60/cwt. doled out since Feb., but on a limited volume per farm.



FOOD PRICES Sluggish prices at the farmgate aren't about to improve anytime soon as crop and livestock output that has been suited to a growing economy adjusts to the recession's slower demands. Ag exports have plunged because of the global slowdown. Consumers' food expenditures have also dipped... down 2% through Aug. vs. the first eight months of '08. Average prices for crops are down 17% from Aug. '08. Milk...36%. All livestock products...20%. Into '10, price recoveries will be faster for crops than livestock.

Farmers' slice of the food sales dollar is smaller. Raw commodity prices at the farmgate represented 23% of retail food prices a year ago. At the end of '09...20%, or close to what the share was back in '05 and '06.



Supermarkets are feeling less of a pinch than farmers. Grocery prices have slipped 1.6% since Aug. '08. Fruits and veggies, down nearly 6%. Meat, poultry and fish...off 2%. However, they're paying less for transportation, labor and energy as well as for food at the wholesale level.

At the same time, other food outlets are charging more... up 3% overall compared with a year ago for food eaten away from home. School cafeterias and other institutions are raising prices to compensate for budget shortfalls. More surprisingly, restaurant prices have increased 2.4% since Aug. '08 in a bid to recoup losses from previous years when their food and labor costs soared.

PESTS & DISEASE The genome of the potato and tomato killing late blight has been mapped... Uncovering the fungus' genes is already paying off, say USDA scientists, who've found blight genes that make enzymes to attack plant cell walls, opening cells to invasion. And gene segments that create diverse proteins, enabling multiple attacks.

CREDIT Help advise USDA on its loan programs for beginning farmers and ranchers. Nominations are open for its advisory board, which helps set terms of credit and other rules for such loans. Farmers and others involved in managing farm credit, including lenders and teachers, can apply. See kiplinger.com/letterlinks/agcredit.

ACRE Heads up on a key decision for those enrolled in the new crop risk coverage: If your planted acres exceed 120% of program base acres, you may gain by selecting the priority crop for any payouts. The deadline for acting is Sept. 30.

SHIPPING When the Panama Canal's new channel and locks are finished in '14 or so... Capacity to move bulk ag commodities will double. The deeper, wider passage, additional traffic lane and much larger locks will help the canal compete with ports on the U.S. West Coast for both exports and imports. Without the project, for example, the 25% share of U.S. grain and soybean exports that now move through the canal would lose ground to facilities such as one Bunge plans to complete in Wash. in '11. Bulk shippers will pay much higher rates through the canal, but will get faster service and will fully load the ships...not possible now...greatly improving transport efficiency. But the biggest gainers in the canal project will be containerized shipments... high value U.S. ag exports, imports from Asia, cargo between this continent's coasts... moving on huge Post-Panamax ships. See an update at kiplinger.com/letterlinks/canal.

Yours very truly,

The Kiplinger Editors

THE KIPLINGER WASHINGTON EDITORS

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