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Miell Agri-Business Agricultural Insights

Special points of interest:

- Soft landing for U.S. farmland prices.
- Input prices not yet responding to production signals
- Farm rents holding-up.

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2014—What Just Happened?

With the U.S. 2014 corn & soybean harvest now finished, analyzing the implications of the record yields and production levels for these two crops is now underway.

USDA's December 2014 World Agricultural Supply and Demand Estimates (see Table 1.) revealed that the record per-acre yields and total U.S. production for corn and soybeans will further build global ending stocks and provide little bullish news for prices in the short-term.

Most of the world's major grain producing regions had good 2014 production, further building global supplies and depressing market prices.

We now have answers for one important question— the 2014 production outcome and can now work on formulating responses to three other important questions:

- **What impact will this year's production have on commodity prices and demand?**
- **What does a record corn and soybean crop mean for U.S. farmland prices and farm rents? and**
- **What is the near term production outlook considering the size of this year's crop and forecast supply, demand and ending stocks projections?**

Throughout much of 2014, commodity prices anticipated the prospect of a large U.S. corn and soybean crop with prices for both sectors declining significantly before recovering as harvest progressed.

Demand generation will now be a major focus to consume these record corn, soybean and wheat stocks. Record 2014 production levels make it imperative to begin aggressive marketing to build demand to ensure ending stocks do not become a long-term drag on prices and industry development.

When analyzing the impact of this record production, it is important to understand that there is more to agriculture than the fortunes of the U.S. corn, wheat and soybean sectors.

Important as these commodities are, investors must also focus closely on the other agricultural sectors that are equally as important and also provide high quality investment opportunities such as: livestock; permanent crops; forestry and even off-farm agri-business activities that provide value-added vertical integration options.

Agricultural assets should be a key component of a well-balanced investment portfolio. Diversity within the agricultural portfolio itself will further protect against production, weather or other market shocks.

2014 has provided a very good example of the benefits of a well-balanced mix of agricultural production options, we will explore some these alternative investment options in future editions of *Agricultural Insights*.

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2015 Production Outlook

Record corn and soybean yields and 2014 production levels make it imperative to begin aggressive marketing to build demand to ensure ending stocks do not become a long-term drag on prices

Table 1. USDA November 2014 Crop Production Estimates

Commodity	2013 Acreage (million)	2014 Acreage estimate (million)	Yield (bushels/acre)	2014 Production estimate (billion bushels)	Average Farm Price ($/bushel)
Corn Planted Harvested	95.4 87.7	90.9 83.1	173.4	14.4	$3.20 to $3.80
Soybeans Planted Harvested	76.8 76.3	84.2 83.4	47.5	3.958	$9.00 to $11.00
Wheat Planted Harvested	56.2 45.3	56.8 46.4	43.7	2.026	$5.80 to $6.20
Sorghum Planted Harvested	8.1 6.5	7.2 6.2	66.1	.408	$3.20 to $3.80

Records

Commodity	2013 Acreage (million)	2014 Acreage estimate (million)	Yield (pounds/acre)	2014 Production estimate (million bales)	Average Farm Price ($/lb)
Cotton	10.4	9.88	773	15.92	$0.59 to $0.64

Commodity	2013 Acreage (million)	2014 Acreage estimate (million)	Yield (pounds/acre)	2014 Production estimate (million cwt)	Average Farm Price ($/cwt)
Rice (all)	2.49	2.91	7,597	221.1	$14.00 to $15.00

As Table 1. illustrates, the 2014 record production of corn and soybeans will ensure that there is no global shortage of these commodities in the near future, a fact that is reflected in ending-stocks forecasts and grain and oilseed commodity market price activity this past year.

However, oversupply in one market has created opportunities in others. The livestock sector, comprising: cattle; hogs; chickens; and dairy are benefiting from the current level of grain and oilseed prices and their over-supply. Both production and consumption of livestock product are responding accordingly.

Grain and oilseeds export demand is also growing and uses such as ethanol production are also responding to the market's price signals.

Farmers themselves are also now in the midst of determining their 2015 production actions in response to the current and forecast price levels. For 2015, early market commentary is suggesting lower corn plantings, higher soybean plantings and perhaps diversity into other crops such as wheat, sorghum and cotton as producers seek to protect their bottom-lines by choosing crops that have lower production costs and perhaps slightly better price outlooks.

So far, major input prices for seed, fertilizers and chemicals have not responded to producers' production pressures. As producers seek to reign-in their cost base, current prices for these inputs will come under pressure if there are indications that producers plan to significantly reduce their acreage of a particular crop.

One bright spot for producers is the current downward trend in fuel prices which should also be reflected in fertilizer prices. Both will help improve per/acre production costs for all cropping activities.

In addition to a final review of 2014 production outcomes, USDA's January 2015 World Agricultural Supply and Demand Estimates will provide the first official estimate of producers' 2015 planning intentions.

Expect market reactions to any significant reduction in total 2014 production numbers or 2015 forecasts for significant corn and soybean acreage declines.

2015 Forecasts for Farm Values and Farm Land Rents

The past 4-6 years have been very good for investors in agricultural properties, in particular those engaged in grain and oilseeds production. During this time land values have appreciated significantly. Farm rents have followed this upward trend and both production outcomes and commodity prices have placed the sector in a position of financial strength unlike any experienced in recent decades.

2015 brings a different range of scenarios. In the grains and oilseeds sectors, it is now very much a buyers market. Opportunities will arise and are indeed available now to build the foundations of a high quality agricultural portfolio. Land values are expected to soften, there will be less competition in the marketplace.

At this time, farm rents have largely held firm at 2014 levels. Farm operators are focusing on productivity improvements and tighter management of input costs to deliver profitable operations in 2015.

Early indications are that 2015 grain farm rents are not likely to decline significantly from 2014 levels, while some land values are softening

Livestock operations are rebounding quickly as seasonal conditions improve, market demand grows and grain input prices decline to more favorable levels for these operations. Beef, pork and chicken products are in high demand, dairy is soft, but will benefit from lower grain prices and the strength of the wider livestock sector.

In the U.S., cattle herd rebuilding is limiting market availability which will guarantee tight supplies, continue to support prices for the immediate future and underpin strong asset values.

In the permanent crops sector, crops such as: nuts, berries, wine grapes, fruits and vegetables are providing attractive investment options, with demand supported by both strong and expanding domestic and export consumption.

A primary issue to consider in the permanent crops sector is access to high quality, secure and affordable water supplies. Without this one key input, annual production and investments values can be hit hard during times of drought-induced water supply constraints or market-base competition from other uses.

California's current three year drought illustrates these pressures being applied to agricultural and urban water users with devastating consequences.

Sector	2015 Asset Value Trends
Grain & Oilseeds	↘
Livestock	↗
Permanent Crops	↗
Forestry	↗
Agribusiness	→

Two other agricultural investment options often overlooked when considering long-term portfolio design are forestry and off-farm agri-businesses. Both are high value portfolio additions that provide further diversification to an agricultural investment portfolio.

Forestry is an ideal long-term investment vehicle that complements other agricultural production options. We will explore the intrinsic values of this asset class in later editions of *Agricultural Insights*.

Off-farm agri-business options can add value to farm production through processing and marketing options, or be associated with other products and services essential to farm business operations. There are a lot of exciting agribusiness options centered around innovative products and services that provide investment diversity and global opportunities.

When looked at through this wider perspective, the current downturn in the fortunes of the grain and oilseeds sectors is offset by opportunities in livestock, permanent crops, forestry and agri-business. A well-balanced agricultural investment portfolio with exposure to all sectors and across different geographies would be well-placed to deliver competitive and attractive investment performance in the current market climate.

Other Global Markets — Australia

The Australian federal government concluded three Free Trade Agreements in 2014 with Japan, South Korea and China. Agriculture was a key feature of each of these trade agreements.

After many years of negotiations, the successful conclusion of these three agreements is positive news for the Australian agricultural sector. Depending on the market and the specific sector, these trade agreements will see market access grow through immediate or phased tariff reductions and preferential market access over those market competitors who do not have similar agreements in place.

Overall, live cattle exports, processed beef, sheepmeat, malting barley, sugar, dairy products, wine, fruit and vegetables and inbound investment flows can be considered the initial 'winners' in these agreements.

Three trade liberalization agreements will stimulate investment activity

An immediate market response to the signing of these agreements was seen in increased interest in large beef cattle properties and dairy assets in both production and processing sectors.

In the lead-up to the signing of the China/Australia agreement, two Chinese investment groups announced a AUD$3 billion investment fund focused on beef, diary and aquaculture. If it comes to fruition, that level of investment will significantly and positively impact some of the existing market structures.

All of the excitement of this initial investment activity must be tempered by the understanding that there are some industry, social and political concerns with foreign investment in Australia's agricultural sector that will become increasingly evident as more investment deals are concluded.

Clearly, Australian agricultural exporters have secured a market access advantage with these agreements. However, many of the benefits of these agreement will accrue over many years and may well be offset by increased competition from other major exporting countries who will seek to protect their existing market access through negotiation of similar trade agreements.

The Trans Pacific Partnership is one example of trade negotiations currently underway that may be concluded in such a way as to minimize Australia's competitive advantage in some of these markets; time will tell.

And we must not overlook competing agricultural investment opportunities in other markets such as: New Zealand, North America and Latin America that will make good business sense now, irrespective of emerging trade agreement benefits.

These areas are Miell Agri-Business' area of special expertise, please make contact if you wish to explore opportunities in these regions

For further information please contact:

Doug Miell
Director
Miell Agri-Business

Office:	+1-770-807-0457
Cell:	+1-404-771-8635
Email:	doug@miell-consulting.com
Web:	www.miell-consulting.com