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Miell Agri-Business Agricultural Insights

2015—Production Forecasts

The much awaited release of the United States Department of Agriculture’s (USDA) March U.S. crop production forecasts provided investors with their first indication of how U.S. farmers are responding to the record corn and soybean crops produced in 2014 and, the decline in market prices for these commodities over the past 12-18 months.

It had been anticipated that corn production would dip in favor of expanded soybean acreage, while wheat and other crops such as cotton and sorghum would also exhibit changes in 2015 planting intentions. The USDA’s forecasts, as outlined in Table 1, confirms those industry predictions.

Table 1. USDA’s March 2015 Crop Planting Forecasts

Commodity	2014 Acreage (million)	2015 Acreage estimate (million)	Acreage Change (million)
Corn Planted	90.6	89.2	-1.4
Soybeans Planted	83.7	84.6	+0.9
All Wheat Planted	56.8	55.3	-1.5
Sorghum Planted	7.1	7.9	+0.8
All Rice Planted	2.9	2.9	0
Cotton Planted	11.0	9.5	-1.5

Source: [USDA](#)

If the corn planting forecast eventuates, this will be the third consecutive year of an acreage decline and would be the lowest planted corn acreage in the U.S. since 2010.

With the 2015 planting season just beginning across the U.S. grainbelt, weather conditions in the next 6-8 weeks will determine how close these forecasts come to fruition.

At this time, commodity markets are not providing farmers with price signals that would likely alter the trends outlined in these USDA forecasts.

Special points of interest:

- Growers switching production to soybeans and sorghum for 2015 season.
- Some farmland values easing.
- Farm rents holding-up.

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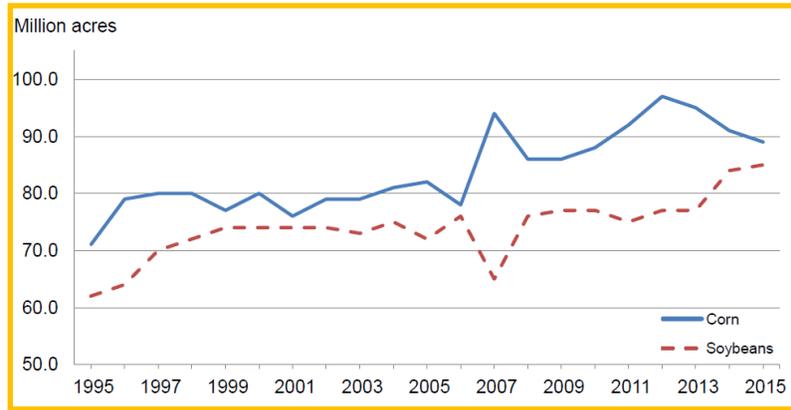
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It is close to a decade since the overall size of the U.S. corn and soybean crops have converged to the extent forecast by the USDA, see Graph 1. This is a rational risk management response by farmers, as soybeans have lower production costs and under today’s market outlook, more profitable margins. The increased area being devoted to sorghum production reflects similar economic reasoning, underpinned by increased demand emanating from China.

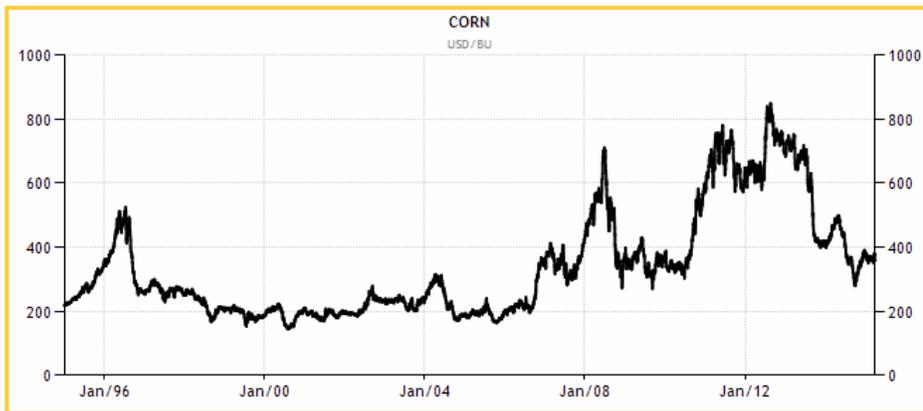
Graph 1. U.S. Corn & Soybean Planted Acreage—1995-2015



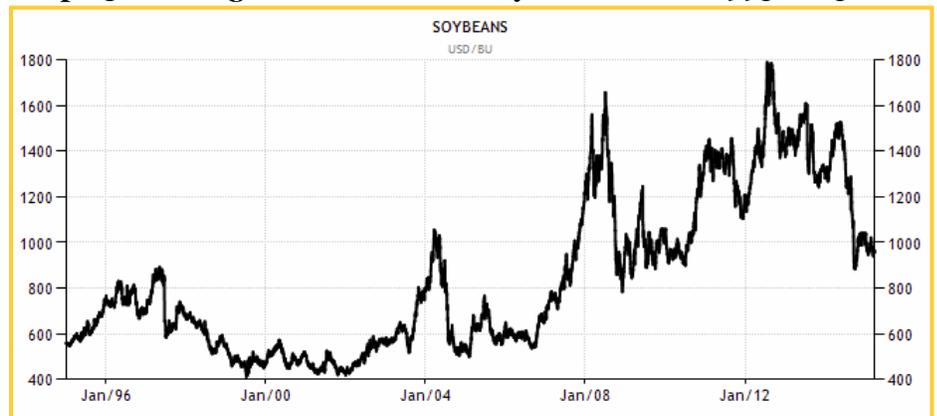
To provide a reference for readers, the historical price pathways that have lead to this year’s crop forecast are outlined in graphs 2 & 3. The run-up in prices for both corn and soybeans (and other grains) during the 2010-13 period was a direct responses to growth in global demand and drought-induced production declines in major production regions, most notably, the U.S..

Industry profitability, farmland prices, production costs and associated farm rental rates all exhibited similar patterns of change over this period and, are now beginning to respond to changing demand, price and production scenarios.

Graph 2. Chicago Board of Trade Corn Prices—1995-2015



Graph 3. Chicago Board of Trade Soybean Prices—1995-2015



Trans-Pacific Partnership Trade Agreement

Negotiation of the Trans-Pacific Partnership (TPP) trade agreement is moving decisively through its concluding phase. For agricultural trade into the Asian and Pacific Rim regions, there are few initiatives with as much potential to determine the short to medium-term profitability and attractiveness of investment in U.S. agriculture as a successful TPP agreement.

The proposed TPP is a trade and investment agreement under negotiation by 12 Pacific Rim countries, with a combined population of about 800 million and a combined gross domestic product (GDP) of about \$28 trillion. In 2012, these 12 countries encompassed 11 percent of global population and almost 40 percent of global GDP. The total size of their market for agricultural imports averaged \$279 billion over 2010-12, 51 percent of which was sourced from TPP partners.

For the U.S., the TPP accounts for 42 percent of the global agricultural exports of the United States and 47 percent of its agricultural imports. The region will be of similar trade importance to all TPP countries.

Bilateral and multi-lateral Free Trade Agreements (FTA) have delivered very beneficial outcomes for agricultural industries in the countries involved. New Zealand dairy farmers and Australian beef producers are just two prominent examples of recent agricultural FTA beneficiaries.

On a recent international trade conference call U.S. Agriculture Secretary Tom Vilsack stated that: “...*signing of the North American Free Trade Agreement (NAFTA) resulted in a 130% increase in U.S. agricultural exports.*”

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The big question is: will the TPP deliver similar outcomes for participating countries?

A recent USDA study found that if the TPP results in the removal of all remaining tariffs and tariff-rate quotas, the value of agricultural trade among TPP countries would increase by 6%, or about US\$8.5 billion by 2025.

The U.S. share of this increase is projected to result in a 33% increase in agricultural exports valued at approximately US\$2.8 billion.

Twenty percent of U.S. farm income comes from agricultural exports. U.S. food and agricultural exports to the world reached an all-time high in 2013 of over \$148 billion. Of that total, the U.S. exported more than \$58 billion to TPP countries – a figure that would increase as a result of tariff elimination under TPP. As just one example: U.S. poultry currently faces a 40-percent tariff in Malaysia. U.S. poultry would become more affordable in Malaysia under a TPP agreement that reduces these duties to zero.

It is, therefore, very easy to see the beneficial trade opportunities that the TPP would present to the U.S. agricultural sector and, indeed, to agricultural industries in each of the participating countries.

While global agricultural trade liberalization is a very long-term challenge, the recent acceleration of FTAs is delivering significant gains for agricultural producers. When these gains are combined with global food and water security concerns, diminishing availability of quality arable land, global population growth, burgeoning shifts in middle-class lifestyles and the attendant demand for high quality lifestyle choices, demand for quality agricultural output has very promising long-term prospects.

Participating countries:

Australia

Brunei Darussalam

Canada

Chile

Japan

Malaysia

Mexico

New Zealand

Peru

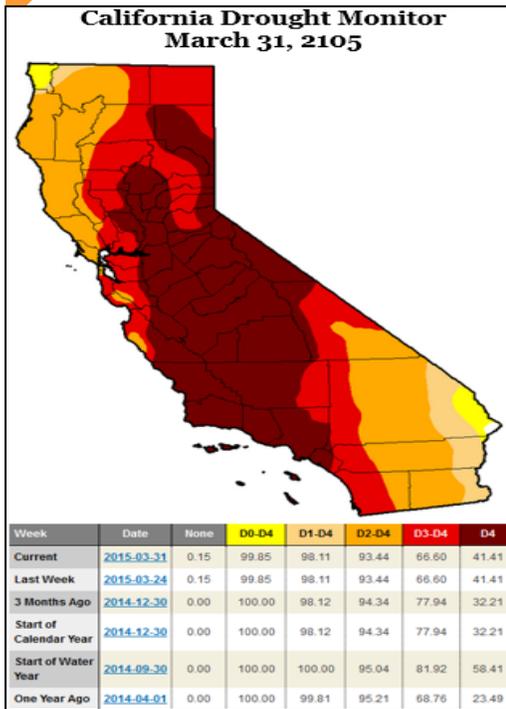
Singapore

Vietnam

United States

Drought Devastating Californian Agriculture

On a state basis, California's economy is the largest in the United States, with a Gross State Product of approximately US\$1,800 billion. If it were a country, it would rank in the top ten of global economies.



Click map for larger image

From an agricultural perspective, California is the nation's top agricultural state, and has been for more than 50 years. Agriculture generates approximately \$37.5 billion a year, more than any other state.

California produces more than 400 crops. Of those, the following are commercially produced only in California: almonds, artichokes, dates, figs, raisins, kiwifruit, olives, clingstone peaches, pistachios, dried plums, pomegranates, sweet rice, ladino clover seed, and walnuts.

California grows nearly half of the nation's fruits, vegetables and nuts.

The leading commodity is milk and cream, accounting for nearly \$6 billion in cash receipts. The second leading commodity, grapes, account for \$3.2 billion in cash receipts annually.

Livestock and poultry account for about 24% of California's gross cash income, with a combined total of \$9.8 billion.

California leads the nation in milk production with over 1.75 million dairy cows, \$5.9 billion in cash receipts

Over 5.3 billion eggs are produced each year by more than 19 million hens and pullets of laying age.

As California heads into its 4th year of what seems to be a never-ending drought cycle, the impact on agriculture has been severe. As the Drought Monitor map above illustrates, there are no areas immune from the ravages of drought and is getting worse each month. The Governor recently imposed stringent statewide water restrictions. Most agricultural producers will again receive little or no irrigation water supplies. Circumstances are indeed dire for agricultural producers. There will be long-term impacts on industry structure and enterprise productivity.

The ongoing drought is forcing structural adjustment within some agricultural sectors. Already there are reports of dairy farmers relocating their operations to states with greater water and rainfall reliability. Some irrigation farmers are selling their water entitlements to towns and cities. These trends are expected to continue for many farmers with operations where such dramatic moves are a viable option.

For agricultural property investors, California's current predicament highlights two important points:

- ♦ The need to undertake comprehensive due-diligence on a region's and an individual property's resource base; and
- ♦ Recognition that those regions with high quality rainfall and water resources must be prioritized for the production and investment security they provide.

It does not matter where an agricultural investment is located, there is no substitute for these two important resources.

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