



STATE BANK & TRUST Co.

DOANE'S Farming for Profit®

January 2012

Bearish EU Summit Outcome: Euro may survive, but barely. The “make-or-break” meeting of EU leaders in Brussels in mid-December met with this no-punches-pulled warning from French President Sarkozy: “Never has the risk of Europe exploding been so big.” But all the European Central Bank (ECB) did was lower interest rates a quarter point and offer another \$160 billion in funds to EU banks over the next three years, less than a third of the amount needed to forestall default by Italy (and possibly Spain as well). Markets reacted negatively around the world as recession fear escalated. The Euro-crisis remains a wet blanket over commodity prices from the demand side.

The failure of the super committee derailed farm bill efforts by some in Congress to pass a new farm bill this year and avoid floor fights in both Houses of Congress. The details of the plan drafted by Senate Agriculture Committee Chairman Debbie Stabenow (D-MI) and House Agriculture Committee Chairman Frank Lucas (R-OK) were never made public, but leaked reports indicate that a “shallow loss” revenue protection program was a key component. The proposal would have eliminated direct payments, the ACRE program, and the SURE program and gradually reduced the cap on the CRP to 25 million acres. With the super committee option for passing a farm bill now gone, development of policies will now revert to what is called “regular order”. Agriculture committees will hold hearings and get input from stake holders. Then, whatever plan the committees devise will be subject to changes when the proposals are voted on by the full House and Senate. The ideas put forward in the plans provided to the super committee by Stabenow and Lucas may or may not survive.

Unless new legislation is passed and approved by the president, the government now faces more than \$1 trillion in automatic spending cuts, beginning in 2013. Under the current law, spending on agriculture programs will be reduced by about \$15 billion over 10 years. Some programs, including food stamps (the Supplemental Nutrition Program) and probably the Conservation Reserve Program, will be exempt from the automatic spending cuts. The cuts that are implemented will be concentrated on crop subsidies, other conservation programs, and crop insurance. Some members of Congress will try to change the law that requires the automatic cuts, but the president has promised to veto any such effort.

The World Trade Organization has ruled against the U.S., agreeing with charges the U.S. Country of Origin Labeling law (COOL) violates global trade rules by discriminating against imports of livestock. The law, which was a part of the 2008 Farm Bill, was challenged by Canada and Mexico. The Office of the U.S. Trade Representative will appeal the ruling, contending that COOL provides valuable information to consumers about the meat products they buy. With the appeal pending, the dispute over COOL will continue for at least several more months.

Ethanol use has “hit the wall” at 10 percent of all blended gasoline according to the Energy Information Administration. But this longstanding “blend wall” is not impenetrable. Ethanol use can theoretically exceed the 10 percent level because of EPA’s approval of the use of E-15 in some vehicles. However, as a practical matter, E-15 still faces several regulatory and market hurdles and is essentially unavailable. Excess ethanol production is thus currently being exported.

THE BLUE-CHIP BORROWER

The kind lenders compete for!

New record highs for farmland don’t even make news anymore, it seems, unless they break some new “threshold,” such as when Iowa and Illinois farmland auctions cracked the 4-digit barrier with several reported sales over \$10,000 per acre just last year. And this isn’t land primed for some commercial development; just highly prized for its yield and coveted by rival farmers - often neighbors.

Then, last October, an 80-acre tract near Sully, IA cracked the \$15,000 mark, with a price of \$16,750. And just this month (December) there was a 74-acre parcel sold at auction near the town of Hull in Sioux county Iowa that hit the \$20,000 mark, smashing the October record.

Economist emeritus Neal Harl of Iowa State University called the prices “amazing”, but declined to warn farmland being at a “bubble” similar to the late 1970s. He noted a lot of differences in today’s yields, grain prices and farmer equity compared to the highly-leveraged late-70s. But others aren’t so bashful. The farmer who alerted this editor to the story had a different word for paying \$20,000 per acre for farmland, no matter how deep, flat and black the soil: “*Insane!*”

That may be an extreme and somewhat emotional assessment, but at some point you still have to push a pencil on land investment and ask yourself a very important question: Does income-earning potential alone justify the asking price or is the wisdom of paying such a price depend on the assumption that land will keep rising on inflationary expectations alone, regardless of year-to-year profitability from farming it?

That was the bitter lesson learned when land prices deflated sharply in the early 1980s. They had not only priced in the “actual” inflation of the 1970s, but the expectation that inflation rates would continue to exceed interest rates, turning “insane” purchase prices into “good investments” over time. But instead, a major change in U.S. monetary policy in 1979 sent interest rates rising with the expressed purpose of bursting the inflation bubble. It worked. And late-comers to the land boom got burned big-time.

Doane's **MARKETING MENTOR**

CORN

The Eurozone debt crisis continues to provide a negative backdrop for corn and other commodity markets, but the corn market does face some direct challenges. USDA's supply and demand estimates for December were up only 5 million bushels from last month with 2011/12 ending stocks at 848 million bushels. U.S. corn export demand has slowed amid widespread competition particularly from feed quality wheat. Black Sea wheat has been competing with corn in the export market through the fall. More recently, Argentina and Canada are also aggressively pricing wheat to North Africa. Export commitments are down 3 percent from a year ago. Even so, sales are above USDA's forecast for a 13 percent decline. Much will depend on China's import demand in 2012. Next month's reports will be more significant for the market. A smaller crop and/or tighter December 1 stocks could quickly rejuvenate the market.

SORGHUM

USDA updated supply/demand forecasts on December 9th. Production is not adjusted again until January, so the focus was on demand. Export commitments in 2011/12 total only 21 million bushels so far, down 65 percent or 40 million bushels from a year ago. But USDA left its export forecast unchanged though as they were already projecting a 60 percent cut in exports this season due to tight supplies. In fact, there were no changes whatever to the balance sheet. All that changed was USDA lowering its forecast range for average farm price from \$6.00-\$7.00 in November to \$5.70-\$6.70 in the December 9th report. The extent of post-harvest recovery will hinge on USDA's final production and December 1 stocks estimates released in January.

SOYBEANS

In its December supply/demand revisions, USDA raised projected ending stocks to 230 million bushels from the November forecast at 195 million. Anticipation that ending stocks will top 200 million bushels eases market worries about adequate supplies to transition to the 2012-crop and for the soybean market to have to aggressively ration supplies. Of course, those views could change if South American soybean production were to encounter production issues. December in South America is roughly equivalent to our June. There is still some planting including double-cropping after the wheat harvest. Most bean fields are in their early growth stage with flowering not until later this

month or into January. Across most of central and southern Brazil, November rainfall averaged between 50 percent and 75 percent of normal. That is not yet a critical shortfall by any stretch, but it could be symptomatic of a shift in the weather patterns toward drier conditions that eventually could harm production.

WHEAT

In its December supply/demand outlook update, USDA was forced to further lower its export forecast by 50 million bushels due to ferocious competition from the Black Sea region. Projected ending stocks were also raised by 50 million bushels, in contrast to an average pre-report trade estimate for only a 2 million bushel increase. The global balance sheet outlook was by far the most bearish news. USDA hiked the estimated global supply by 9.3 million metric tons (mmt) while boosting projected global usage by just 3.4 mmt, for a net hike in projected global ending stocks of 5.9 million versus a pre-report average trade estimate just 290,000 metric tons higher. As for the 2012 outlook, we've got considerable vulnerability to winterkill for much of the U.S. southern Plains and parts of SE Europe and southern Russia, Ukraine and Kazakhstan. And we don't have any good handle on how much acreage actually got planted to start with, nor planting intentions for spring wheat. All remain wild cards.

FEEDER CATTLE

The CME feeder cattle index is at a new all-time high of \$144.73. However, weakness in summer and fall 2012 fed cattle futures have put some pressure on March feeders. March feeders are down from the early November peak at \$150.87 to near \$145 currently. Feeder cattle supplies are set to tighten next spring based on a smaller calf crop this year and the fact that many calves normally in backgrounding programs moved to feedlots through the fall due to the of lack pasture and forage. Feeder cattle have further upside potential into the spring with the CME index likely to push well beyond the \$150 mark. In the meantime, though, with fed cattle facing some near-term pressure from increasing market-ready supplies and softening demand, feeders could weaken over the next 30 to 45 days.

CATTLE

Economic data in the U.S. have shown modest improvement, but not enough to offset concern that fallout from the EU debt crisis could lead to a slowdown in the global economy. As a result, the

Eurozone crisis continues weigh on the cattle market. Fed cattle supplies are expected to increase through year-end into early 2012. At the same time, beef demand is expected to weaken seasonally. Beef prices are already down \$5 to \$6 from the peak in November. These factors have begun to pressure cattle prices along with weakness in the corn market. We expect cash cattle and futures prices to pullback further into the early 2012. Fed supplies should peak in January and then turn down through the rest of the year, which is bullish for prices longer-term. We expect fed cattle prices to ease to the \$115-\$120 range for winter lows and then turn higher, reaching the high \$120s for a spring high.

HOGS

The weakness in hog futures has run counter to the generally improving stock market. Efforts to control the financial crisis in Europe are at a critical stage but U.S. investors seem to think there will be a positive outcome. Even so, this optimism has not spilled over into the commodity markets. Hog futures prices are down near their recent lows of a month ago. Hog supplies remain high with slaughter this week expected to be up as much as 4 percent compared to year ago levels. At the same time, demand is easing as retail orders for Christmas hams are filled. USDA's December hog inventory report is expected to show that the modest expansion in hog numbers is continuing. Even so, cash hog prices are expected to turn higher early next year, as they usually do.

MILK

Cheese production increased seasonally in the third quarter, but was below year-earlier levels. This was the first time in 13 quarters that cheese production was below the year prior level. But as cheese production grows in the fourth quarter and as holiday buying ends, cheese prices are expected to moderate. Also, international cheese prices are weakening as increased supplies are coming online from New Zealand and Australia. Fluid milk sales for the year are down 1.4 percent. This has left more milk available for manufacturing. Milk production is expected to increase slightly more than 1 percent in 2012 while export demand moderates from the strong levels this year. Farm-level milk prices are expected to ease from the record level in 2011 at an average for the year of slightly above \$20 per cwt to the mid-\$18 range for a yearly average in 2012.

