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1994 District Agricultural Outlook

The U.S. Department of Agriculture's (USDA) overall forecast for the agricultural economy in 1994 is for moderate improvement; but there will be some winners and some losers. This year's winners appear to be growers of field crops, fruits, and nuts, while tougher conditions are in store for vegetable and livestock producers.

This *Weekly Letter* applies the USDA's forecast to the Twelfth Federal Reserve District, factoring in the unique risks, opportunities, and issues facing Twelfth District farmers. On the positive side, the District's great agricultural diversity lessens the overall risk due to weakness in any particular crop. In addition, District farmers should benefit from both the growth of their major export markets in the Pacific Basin and the progress on opening foreign markets that was achieved in 1993. On the downside, the substantial control of agricultural land and water by the federal government leaves District farmers vulnerable to increasingly strict environmental regulations.

The globalization of exports

U.S. agricultural exports to the booming economies of Mexico and several countries in Asia should be strong in 1994. The USDA forecast for 1994 puts U.S. agricultural exports at a record of almost \$4 billion to Mexico and at \$2 billion to South Korea and Taiwan. Despite Japan's sluggish economy, U.S. agricultural exports to that country in 1994 should come in at a record \$8.9 billion. Exports to the European Community (EC), which is still in an economic slump, are expected to be \$7 billion in 1994, the same as 1993, and exports to the former Soviet Union, Eastern Europe, and China are likely to decline in 1994.

Prospects beyond 1994 are substantially enhanced by several trade agreements reached last year, such as NAFTA, the successful completion of the Uruguay Round of the GATT, and market-opening agreements reached with certain Asian countries. These agreements will reduce trade barriers and help increase exports of many U.S. agricultural products, especially to Mexico, the European Community (EC), and Japan and South Korea. For example, by the time NAFTA is fully implemented over the next 15 years, U.S. agri-

cultural exports to Mexico are expected to reach \$10 billion annually.

The mix of agricultural exports expected to increase in 1994 favors District agricultural producers. Exports of most bulk agricultural commodities, like wheat and corn, are forecast to fall this year, while exports of some of the field crops that the District produces in substantial volumes, like cotton and rice, are expected to increase. In addition, U.S. exports of high-value products, like vegetables, fruits, and nuts, which District growers excel in producing, are forecast to rise in 1994.

Regulatory risks

Federal regulations and water supply issues once again pose an important risk to the 1994 District agricultural outlook. The Clinton administration appears committed to overhauling the system for regulating pesticides with an eye towards reducing pesticide use by farmers. The administration's plan proposes to replace the zero-risk standards of the 35 year-old Delaney clause, which is viewed as impractical and not widely enforced, with a standard of "reasonable certainty of no harm to consumers of food." Under this plan, all pesticides would face re-approval using the new standard. The Environmental Protection Agency will ban production and importation of the widely used pesticide methyl bromide by January 2001. The chemical is used on a variety of crops in the District, especially strawberries, grapes, and almonds.

Interior Secretary Babbitt is expected to revisit issue of raising grazing fees this year. For 1994, grazing fees on national forest and Bureau of Land Management lands will be \$1.98 per animal unit per month, a 6 percent increase from 1993. Secretary Babbitt's original plan called for an increase to \$4.28 per animal unit per month. Reform of the Endangered Species Act designed to clarify its goals and use also may occur in 1994. Increasing use of the Act has substantially cut back land use and water allocations for many District farmers.

District water supplies generally should be adequate in 1994. In California, precipitation and

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snowpack levels so far this water year have been below normal, but the substantial run-off from last year should be enough to keep water deliveries near normal. As of January 1, California's reservoirs held 101 percent of their long-term average level. Of greater concern to California farmers is the shift in water allocation to the environment. The Central Valley Improvement Act, Clean Water Act, and proposed Bay-Delta Plan all may reallocate a substantial amount of water from agriculture for environmental purposes.

The outlook for specific commodities:

Field crops

Rising incomes for District field crop growers should bring a positive boost to the District agricultural economy in 1994. Prices and exports are expected to rise for the District's most important field crops. The USDA expects a small decrease in U.S. cotton production, but cotton production should rise 4 percent in Arizona because of higher yields and 1 percent in California because of increased plantings. A global rice production shortfall is expected to boost rice prices 40 to 60 percent from 1992-1993. Amid the overall production decline, California rice production is expected to increase, however, because of increased acreage.

The outlook for potato growers is less clear. Potato prices are expected to increase from 10 to 30 percent in 1994, but reduced yields and quality due to the coldest growing season on record suggest production in Idaho will fall 4 percent. Washington potato growers should see strong returns, with production up 23 percent, reaching record levels and yields. Dry bean prices are forecast to rise in 1994 and production is expected to increase 9 percent in Idaho, 24 percent in Washington, but fall 12 percent in California.

Increasing export opportunities for District field crop growers significantly improve the outlook for 1994. NAFTA will help solidify the gains many District cotton growers have already made in Mexico. In the past two years, U.S. exports of cotton to Mexico have quadrupled, with California's San Joaquin Valley accounting for 90 percent of the increase. Trade breakthroughs in traditionally closed markets also will help District field crop farmers in 1994. California rice growers expect to export about one-third of this season's rice crop to Japan, the first U.S. rice exports to Japan since 1970.

Vegetables

In general, sluggish income growth for District vegetable farmers will weaken the 1994 District agricultural outlook. Prices for many key vegetables are forecast to decline in 1994 because of high District production and increased imports of some crops. The USDA expects the number of acres of lettuce harvested this season to increase 6 percent in California, but fall 33 percent in Arizona. Lettuce prices in California currently are down from last year's levels. Increases in the number of acres harvested are forecast for carrots (up 19 percent), broccoli (up 4 percent) and celery (up 5 percent). Prices for these vegetables are expected to decline in 1994 from last year's levels.

Fresh tomato prices are expected to fall 20 percent from last season. Imports of tomatoes from Mexico are expected to increase this year. The USDA expects California's important processing tomato crop to increase 14 percent this season, but low carryover stocks will help push prices higher in 1994.

USDA forecasts show that the District's melon crop still has not overcome the whitefly problems. Cantaloupe acreage in Arizona increased substantially this season, rising 61 percent from last season, but honeydew melon acreage is down 25 percent in Arizona and harvested acres of California cantaloupes or honeydews are still low enough that the USDA did not report estimates for 1994. Sales in California's important greenhouse and nursery industry, which slumped in 1993, will depend in part on a pick-up in economic activity in the state during 1994.

Fruits and nuts

Higher prices and expanding export markets will raise incomes of District fruit and nut producers, improving the 1994 District outlook. The USDA forecasts a smaller U.S. apple crop and 6 percent higher prices in 1993-1994. Washington apple growers will see solid income gains as apple production in the state is expected to rise slightly from last season. District grape production was mixed in 1993. The table grape crop showed solid production increases and raisin production increased 5 percent from 1992. The wine grape crush was slightly smaller than in 1992.

Citrus fruit producers should see healthy income gains overall in 1993-1994, but conditions for specific crops will be mixed. In California, 1993-1994 orange production is forecast to fall 1 per-

cent overall and 13 percent for navel oranges from 1992–1993. Navel orange prices currently are up 13 percent from a year ago. The USDA expects lemon production in Arizona and California, where most of the nation's lemon crop is produced, to drop 1 percent from last season. Lemon prices are expected to remain close to last season's levels.

USDA production estimates vary for many important District nut crops this season, mostly reflecting the alternate season bearing cycle of nut trees. In California, almond production is expected to fall 14 percent from last season and almond prices to rise. California walnut production is expected to rise 7 percent while prices should fall slightly during the 1993–1994 season.

In Hawaii, the number of acres devoted to raising crops continues to decline. The number of acres devoted to papaya production was 8 percent below a year ago, but production increased 4 percent because of better growing conditions. Sugar cane production is expected to decline 5 percent from last season.

Growing export markets will provide an additional boost to District fruit and nut farmers in 1994. The USDA forecasts U.S. fruit and nut exports to reach \$3.7 billion in 1994, a 9 percent increase from 1993. Apple exports are likely to increase this year as exports to Europe expand and the potential for exports to Japan develops. On January 1, 1994, the 20 percent Mexican tariff on U.S. almonds was eliminated, paving the way for increased almond exports.

Livestock and dairy

Weak conditions for District livestock and dairy producers will be a drag on the overall District agricultural economy in 1994. Livestock producers' incomes will be caught in a squeeze of lower prices and higher feed costs. Livestock producers are expected to endure shrinking profit margins rather than initiate significant herd reductions. Cattle on feed inventories currently are above year-earlier levels and are expected to remain relatively high through the first half of 1994.

In 1993, the U.S. dairy industry continued a long-term shift from the Mid-West to the West, and this trend is expected to continue in 1994. The Mountain and Pacific regions now account for a quarter of the U.S. milk supply. Increased supplies and lower demand will push milk prices down 3 percent in 1994. Use of the hormone *bST*, which increases milk production in dairy cows, will be allowed beginning in the first quarter of 1994. The USDA forecasts virtually no effect on total milk use and little effect on milk production in 1994.

Improved foreign market access will spur livestock and dairy export growth in 1994. The USDA forecasts U.S. livestock, dairy, and poultry exports to reach a record \$8.5 billion in 1994. Much of the gain will come in exports to countries with close links to District agriculture, like Japan, South Korea, and Mexico. Beef exports should get a boost in 1994 because NAFTA brought about the removal of the 15 to 25 percent tariff Mexico had imposed on U.S. beef. The 20 percent duty Mexico places on other U.S. meat products will be phased out more gradually.

The bottom line

In 1994, the District agricultural economy will improve solidly. Overall farm income will increase as gains for field crop, fruit, and nut farmers overcome losses for vegetable, livestock, and dairy producers. Strong agricultural export growth will produce income gains for farmers of a variety of products throughout the District. Export opportunities should expand in the future since District farmers are well-positioned to benefit from the world's fastest growing agricultural export markets in Latin America and Asia. Regulatory changes, especially environmental regulations that alter water allocations, introduce a degree of uncertainty to the 1994 District agricultural outlook, however.

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The *FRBSF Weekly Letter* appears on an abbreviated schedule in June, July, August, and December.