

The Agriculture Letter

Insight and Analysis for Agribusiness Leaders

• Vol. 93, No. 25

Dear Client:

Washington, Dec. 23, 2022

A look at end-of-year issues and how they could unfold in 2023...*continued on pages 2 and 4.*

CHINA

China... lots of issues.

China's economy: Despite a pause of some key economic reports, it's clear China's previous zero-Covid policy was a mistake as it led to repeated shutdowns and negatively impacted businesses and logistics, both impacting the world of ag. Now that China is taking a more flexible approach, the initial concern is that its health care system won't be able to cope with around an estimate one million cases of Covid eventually.

It will take time to turn China's economy around.

Many market strategists expect Covid infections to peak in China after the Lunar New Year, which begins in late January. But only about two-thirds of the elderly population is vaccinated.

Still, China is priming the economic pumps again, including propping up a debt-fueled property bubble... millions of Chinese have invested in real estate. Recent data showed weaker-than-expected retail sales, investment spending and industrial output. The gov't of President Xi Jinping is focused on reviving domestic consumption. Given China's appetite for energy, autos and more, that is good news for the global economy... raises odds the world could perhaps avert a recession, even as the U.S. and Europe slow. China's recovery is expected to hit its stride in next year's second quarter... when economies in the developed world will be slowing.

Trade: China used to get a lot of corn from Ukraine, but the Russian invasion has forced China to tap Brazilian corn supplies for the first time and it could be a game changer ahead, reducing U.S. export prospects over time and putting more pressure on the U.S. to increase market access in other countries.

FARM BILL

Fate of new farm bill rests on House.

Reason: Most expect the Senate Ag Committee to deliver a new farm bill before the August congressional recess in 2023. They are not so sure about the House Ag panel. Why? A new incoming panel chairman, Rep. Glenn "GT" Thompson (R-Pa.), must accelerate his approach to the task, including asking members from both political parties about their priorities. Field hearings also need to take place, with one coming up in Thompson's home state of Pennsylvania.

Different approaches. Climate and conservation are key issues for Democrats but not Republicans, who want to focus on strengthening the farmer safety net... indexing for prices to keep reference prices relevant. Also, improving crop insurance, and perhaps margin coverage of some sort.

Look at the box on this page for what we have learned, and what other veteran farm bill watchers say, after dealing with many farm bills of the past.

KEYS TO NEW FARM BILL

All farm bills are different, even though most are evolutionary and not revolutionary. Here are some suggestions of what we and other farm bill watchers have learned over the years:

- **Sharpen your pencils** and figure out what you believe is needed with analysis and let Congress determine if and how it can get there.

- **Best approach in past:** When Ag panels asked farm groups what they wanted, why it was needed, and how much it would cost, they didn't ask them how to pay for it because that's Congress' job to sort out how to reconcile needs and finite resources.

- **Speak up:** You won't get everything but if you don't ask you don't get.

- **Spending:** House Republicans are not going to be keen on more gov't spending and Dems want more, but not for Title I... farm programs... or crop insurance.

Upshot: Recognize you're not tilting at windmills, nor is this a cake walk. It will take hard work and yes even some luck.

Source: Ag Letter editors

FOOD
SECTOR

EU takes steps to unblock transit of Russian fertilizers. The European Union implemented a new sanctions package on Dec. 16. The sanctions agreement, pushed through by EU leaders when they met for a summit, came amid intense lobbying by United Nations Secretary-General António Guterres. He called several European leaders to persuade them to ease the transit of Russian fertilizers through EU ports.

The issue: The EU has consistently noted language in its sanctions' legislation stating that food, fertilizers and other key humanitarian goods are exempt from sanctions. But vessels carrying fertilizers have been held up for weeks or denied permission to transit through large European ports, such as Rotterdam in the Netherlands, because of concerns over sanctions. Example: Russia's elites being sanctioned are current or former owners of some of Russia's biggest companies producing and distributing fertilizer. Custom officials said that in some member states, vessels carrying fertilizer linked to sanctioned Russian oligarchs couldn't transit through their ports because the facilities couldn't accept payments for harbor fees and other costs or permit payments to companies linked to oligarchs whose EU assets had been frozen. Some vessels did transit through but were held up for weeks because of the need to receive clearance from national authorities who themselves were unsure of the sanctions rules, the *Wall Street Journal* detailed.

Details: National governments can unfreeze the assets if strictly necessary for shipments of fertilizers. Exemptions must be reported to the European Commission, the EU's executive body, to ensure they are being properly applied. To halt sanctions circumvention, exemptions would only apply to people or entities linked to a significant Russian agri-food business active in the field before being sanctioned. The shipment must also be part of a U.N. program shipment or go to a developing country covered by the U.N.'s food-security priorities.

Impact: The exemption is expected to significantly improve the transit of fertilizers through the bloc, although glitches could linger, such as identifying which countries count as being U.N. priority destinations and ensuring that the final destination is what is claimed. Also, Ukraine needs fertilizer... analysts have lowered expectations of the country's new-crop prospects.

U.S.
ECONOMY

Investors search for the answers to two key questions:

- 1) How fast will inflation decline?
- 2) How bad will the economy get?

Here's how the *Sevens Report*, an economic letter, answers:

"The answers to those, and not whether the Fed hikes to 4.875% or 5.125%, will determine the fate of stocks over the first several months of 2023, because investors will need to know those answers to determine A) Expected 2023 earnings and B) The right market multiple. Between now and year-end, however, we shouldn't be shocked by a continued selloff as investors, who were hoping for a Santa Claus rally, are largely "throwing in the towel" and instead focusing on harvesting tax losses (and Friday could be especially volatile with the looming quarterly options expiration)."

PORTS

U.S. ports are sending warning signals about trade flows in the new year. The first reports from gateways on both coasts suggest container imports turned sharply downward last month. The *Wall Street Journal* reports shipping executives say they are bracing for weak demand in the first part of 2023.

A continuing decline at the Southern California ports deepened in November, with combined imports into Los Angeles and Long Beach plummeting 26% to the lowest level since the start of the pandemic. Inbound volumes at the ports of Savannah, Ga., and Charleston, S.C., also retreated.

Dockside business is feeling the impact of wavering U.S. consumer demand and weakening China exports. Container lines and ports usually get a wintertime bump from Lunar New Year volumes out of Asia, but executives aren't expecting to celebrate much in the coming weeks.

About the U.S. GMO corn trade skirmish with Mexico, which says it wants to halt the product beginning in 2024, with a recent suggestion from Mexico any ban could be delayed until 2025 to study the issue. All this has raised deep concerns among U.S. corn growers, lawmakers and Biden administration officials, including USDA Secretary Tom Vilsack.

Meetings between U.S. and Mexican officials have taken place and the issues have been clarified, with Mexico promising more information ahead.

Mexico said it will reconsider its rejections of petitions for GM corn traits and would exempt imports of feed corn from any restrictions. But when it comes to GM white corn, Mexico would allow it to enter Mexico but bar domestic food companies from using it to make tortillas or other products. U.S. interests do not like that approach.

Opposition to Mexico's approach. The Biotechnology Innovation Organization said in a statement that it is "crucial that Mexico meet its commitments under the U.S.-Mexico-Canada Agreement and resume a science- and risk-based regulatory approval process for all agricultural biotechnology products...."

Corn: Attention as 2023 opens will be on prospects for planted acreage as farmers are still dealing with elevated input costs... USDA forecast the largest increase for inputs in 2022. Those costs are not likely to moderate much in 2023. Profitability for corn acres still remains solid even though some are being swayed by the rise in soybean prices to potentially put in some additional soybean acres.

Soybeans: Besides 2023 U.S. acreage prospects, the soybean market will keep a close watch on conditions in South America where Argentina and portions of southern Brazil are seeing dry conditions slow soybean planting. That has kept a floor under U.S. prices and potentially generated some extra demand for U.S. soybeans. That price premium is a factor in the U.S. acreage mix in 2023.

Wheat: Focus remains on the Black Sea and the ability of supplies to move from the region into global channels. Ample supplies from Russia and Australia are providing incentive for buyers. Snow and recent rain in Plains HRW and Northern Plains areas have provided some needed moisture, but spring weather is key.

Rice: Production woes in California are a lingering impact for rice. While rice did not see the price rise of other commodities, the market is still high enough to temper any aggressive foreign demand for U.S. supplies. Acreage prospects for 2023 are murky but trade factors outside the U.S. remain the major driver for markets.

Cotton: The macroeconomic picture remains the global focus... will a number of economies contract into recessions? If they do, trouble for cotton demand ahead, keeping pressure on prices. Demand for newly harvested supplies needs to stay solid. Key will be whether prices fall to the point of triggering farm program payments for the crop.

Cattle/beef: Cattle numbers will tighten with U.S. beef exports moving well... October exports were a fresh record for the month. But macro factors could come into play, particularly if beef prices at the store remain at lofty levels and the U.S. economy takes a dip. U.S. beef exports are already expected to contract in 2023.

Hogs/pork: USDA's Dec. 23 Hogs & Pigs Report will be important for the supply outlook. Those numbers are likely to tighten from year-ago levels and that sets the stage for a positive price outlook. But trade will be an important component in that outlook and strength in the U.S. dollar could be a limiting factor.

Poultry: Turkey sector continues to grapple with highly pathogenic avian influenza (HPAI). Infections appear to target older birds which is part of the reason more turkey operations have been affected. But the U.S. egg laying flock is also at risk. If infections spread, that could set the stage for it to continue as a poultry factor well into 2023.

Dairy: U.S. dairy cow numbers have edged up and the milk-per-cow output continues to move higher. That sets the stage for increased supplies and price pressure on farmgate prices... could trigger some additional government payments. Acreage prospects for 2023 will have a lot to say about feed costs.

WRDA

WRDA clears Congress and signed into law. The Water Resources Development Act (WRDA) was attached to National Defense Authorization Act. The 427-page bill authorizes hundreds of projects and includes federal cost share. WRDA is the main vehicle Congress uses to authorize the study, design, and construction of federal water infrastructure projects... flood control, ecosystem restoration, river navigation, and coastal port deepenings.

Key: Barge interests using the inland waterways will have their share of construction costs for locks and dams that make navigation feasible reduced to 35% from the general Treasury fund (instead of 50%)... permanently, and 65% from the Inland Waterway Trust Fund. The new WRDA removes a provision that would sunset the 65-35 cost-share back to 50-50 in 10 years. When including operation and maintenance costs, the inland waterway industry already benefits from a greater than 90% federal subsidy.

WATER
ISSUES

U.S. seeks Colorado River drought plan from states by Feb. 1. California, Arizona, Navajo Nation and other U.S. states and tribes reliant on the Colorado River should aim to reach an agreement by Feb. 1 on slashing water use in response to a devastating drought, the U.S. Interior Dept. said. The U.S. gov't will be ready to mandate water cuts by next summer if needed in absence of a deal.

Seven Western states that rely on Colorado River water to cut usage by 2 to 4 mil.-acre-feet... up to a third of the river's annual average flow... to try to avoid dire outcomes. But the states have so far failed to reach a voluntary agreement on how to make that happen... thus the threat of mandates.

What could happen: Ted Cooke, general manager of the Central Arizona Project, which delivers Colorado River water to central Arizona, said that "there's a real possibility of an effective dead pool" within the next two years. That means water levels could fall so far that the Glen Canyon and Hoover dams... which created the reservoirs at Lake Powell and Lake Mead... would become an obstacle to delivering water to cities and farms in Arizona, California and Mexico.

Dilemma: Negotiations will ultimately have to weigh cuts in rapidly growing urban areas against those in farming communities that produce much of the country's supply of winter vegetables. Drought has already led to a record number of wells running dry in California, forced huge swaths of farmland to lie fallow and required homeowners to limit how much they water their lawns.

Cuts are likely to hit hard in Arizona and California, where major farming regions consume big portions of the available supply. These states, which get water after it passes through Lake Mead and the Hoover Dam, also face the greatest risk if the reservoirs fall to dangerous levels,

Water issues are part of most meetings we attend in the ag sector... but especially west of the Mississippi River. Water issues are on the rise, including its price, availability and state and federal regulations. Those will increase in the years ahead.

NEW
CONGRESS

With this Congress now adjourned, a quick look ahead shows the new Congress next year a split one relative to control, with the Republicans leading the House and Democrats the Senate. While most predict gridlock, we've learned to give any new Congress six months to see if some compromises can be reached ahead.

HOLIDAY
WISHES

We want to wish you and your family a blessed, happy holiday season.
We will be back next year with more coverage of issues and their impacts.

Best regards,

The Ag Letter Editors
THE AGRICULTURE LETTER EDITORS

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