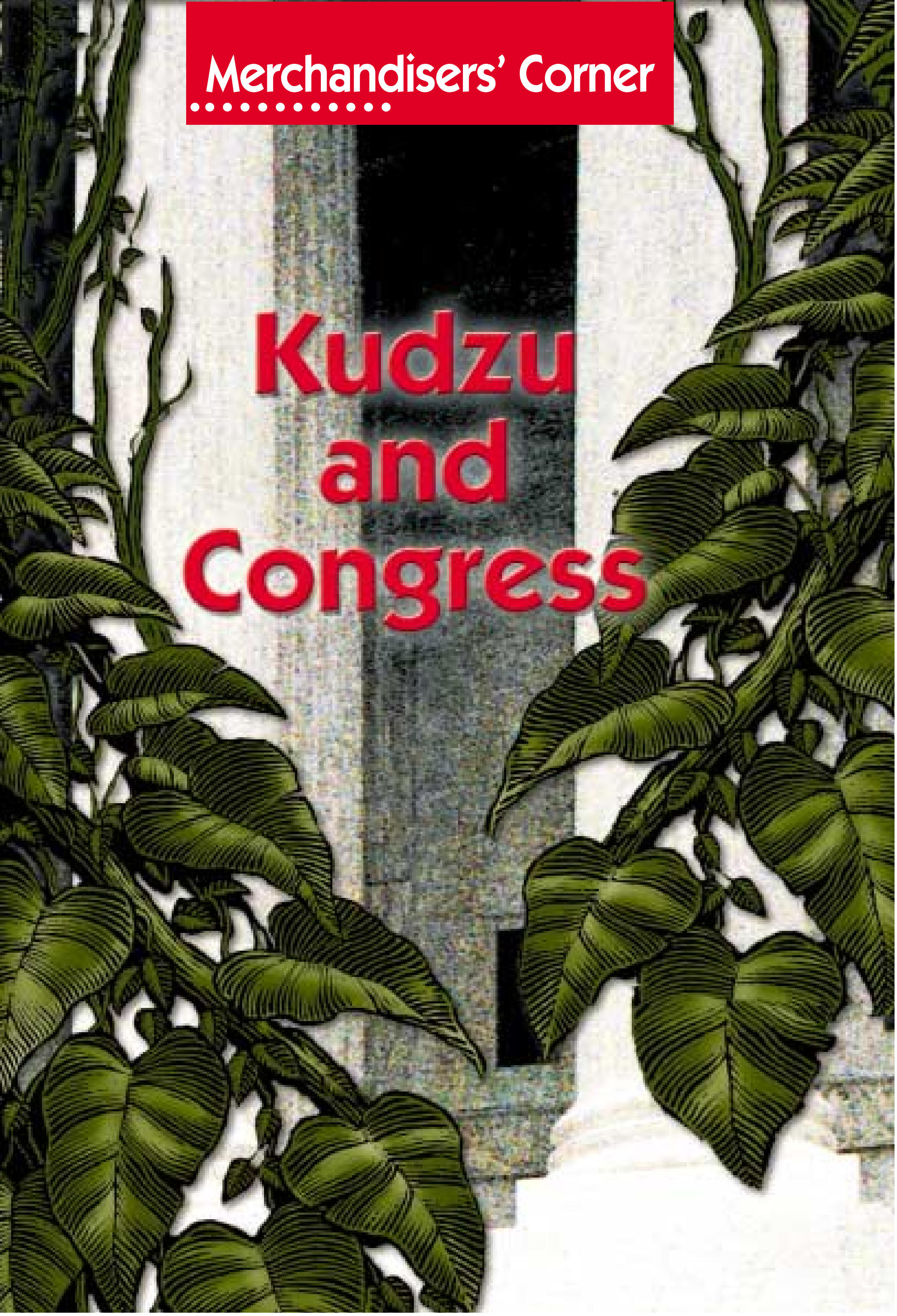

Merchandisers' Corner

Kudzu and Congress

By Diana Klemme, Vice President, Grain Service Corp., Atlanta, GA

Now after reading this headline you may be wondering what Kudzu and Congress have in common. Plenty — it may turn out.

Kudzu is a fast-growing ground-cover vine that was brought to the United States in 1876 as part of a Japanese exhibit at a Centennial Exposition. Kudzu was later promoted as a forage plant, and then the U.S. government stepped in. Through the Great Depression, government workers planted kudzu for erosion control, and in a bizarre predecessor of CRP, farmers were actually paid to plant kudzu in the 1940s.

A well-known principle is the Law of Unintended Consequences. Kudzu is a classic example. Those who promoted and planted it surely had the best of intentions. Kudzu does control erosion, but unfortunately also grows over anything in its path — including trees and roads. Estimates are that over 7 million acres in the Southeast are now covered with the annoying plant. Most herbicides won't touch it, and so far, the best cure for kudzu seems to be goats. (They love it.)

Now back to Congress for a moment. Congress recently passed an $8.7 billion emergency aid package for farmers for 1999 crops. Adding that to the existing Farm Bill and other supports, producers will see over $22 billion in direct aid this year. Producers also now have the ability to lock in a posted county price for 60 days before repaying their marketing loan(s). And if all that wasn't enough, the USDA approved a program to guarantee low-interest rate loans to build on-farm storage. Infusing such massive aid will almost certainly produce unintended consequences for the ag sector. Will Congress' solution create another kudzu calamity?

No one argues that commodity prices are low and that some regions faced catastrophic conditions — North Carolina and the

Northeast, for example. But this aid package spreads money around to virtually all grain and oilseed producers, even those likely to have a fine year financially without the emergency aid. The law of unintended consequences is almost sure to strike — somewhere.

Federal program payments (billion dollars)

	1995	1996	1997	1998	1999
Total direct payments	7.3	7.3	7.5	12.1	22.5
Commodity programs	4.5	(0.7)	(0.6)	na	na
Production flexibility (AMTA)	na	6.0	6.1	6.0	5.1
Loan deficiency	na	na	na	1.8	6.6
CRP and other	2.8	2.1	2.0	1.6	2.1
Emergency assistance[1]	na	na	na	2.8	8.7

Prior record annual aid: $16.7 billion in 1987.
[1]Includes the October 1999 legislation.

Data source: Pro Farmer/USDA Economic Research Service

Rising production costs

Many producers in the Midwest and other areas stand to collect as much as $120 to $160/acre of direct support on prime corn land this year. This gives producers and landlords extra funds to acquire land and equipment or pay down debt. One consequence is likely to be a rising cost of production because of:

- rising land costs in areas unaffected by the drought/floods;
- increased demand for equipment;
- high acreage for 2000; and
- strong demand for agronomic inputs.

The congressional kudzu effect will spill into merchandising as well as into production costs. Many producers had good to excellent yields this year and will have a lot of grain to sell. The low harvest prices encouraged massive LDP activity. More than $2 billion had been paid by Nov. 1 just in wheat, corn and soybean LDPs. This is as much as the USDA paid against the entire 1998 crop. Now producers have $5.5 in emergency aid coming, mostly before year-end.

Many folks will resist selling grain because of both tax consequences and low prices. The new PCP "lock-in'" program functions like a free "call" on the market, and provides producers who use it another incentive to hold grain back to see if prices rise. This "lock-in" program may not generate much interest this crop year; however, it does encourage speculation at taxpayer expense. (Producers will certainly seek to lock in the lowest possible PCPs).

The program to finance building on-farm storage will also encourage keeping grain off the market next year. Stockpiling grain doesn't boost prices — it becomes a sword over the market's head. Commodity prices in the CCC years of the mid-1980s proved that: $1.50 corn and $2.40 wheat.

The winter of 2000 may see slow producer marketing, but you can use that time to work out of your company-owned positions and prepare for the onslaught later.

A formula for trouble

The combined effects of the generous up-front aid package, massive LDP activity and the new PCP alternative point to producers delaying marketing. That spells trouble, with:

- pressure on futures later when the grain moves;
- logistics problem in spring/summer;
- quality problems from farm-stored "mid-moisture" corn (16% to 18%) that wasn't dried; and
- potential for very weak basis later in the year.

The aid package sets up a cycle that may feed on itself and foster another emergency bailout in 2000. It will encourage grain stockpiles, and raises inputs and land costs over time. The probability of large acres for 2000 points to another year or more of low prices. How much more good news can producers hope for from our congressional kudzu program?

The commercial sector may not collect direct dollars from Uncle Sam, but it will benefit indirectly. Big crops create demand for your services and generate merchandising opportunities. The winter of 2000 may see slow producer marketing, but you can use that time to work out of your company-owned positions and prepare for the onslaught later. You can be like the goats that feed on kudzu — you may not get a brown envelope in the mail from the USDA with direct dollars, but what you receive instead is plenty tasty: storage revenue and basis opportunities. F&G

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