David M. Kohl

Professor, Virginia Tech
Agricultural Finance and Small Business Management

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Economic Storm Clouds on the Horizon

By: Dr. David M. Kohl

The quarter-century mark is just around the corner. What a 25-year ride it has been! Economic cycles in agriculture are a fact of life. At the beginning of the 21st century, globalization and China's rapid economic growth propelled the great commodity super cycle until about 2013. Many agriculture businesses had record profits coupled by asset appreciation, specifically land. Then, the defensive domain of the economic cycle occurred from 2013 to pre-pandemic. There was a cost and price increase, which reduced profits. However, the Federal Reserve's policy of zero-bound interest rates resulted in steady land and other investment appreciation. Then, the mini super cycle of the past three years was a result of prices outpacing costs that initially brought in record profits and cash flows to many in the agriculture industry. Lush government payments that came with no cost of production spurred record farmland and asset appreciation.

Agriculture views moving toward the quarter-century mark find inflated and higher expenses will outlast prices received, resulting in margin compression. This, coupled by high interest rates that will be resistant to a downward trend, will be another burden on margins for individuals with debt financing. Over the next few years, compressed margins with increased economic volatility as a result of geopolitical military challenges will result in thinner margins of error for business and financial decision-making.

On an optimistic note, high levels of business acumen with written plans that include strategies, actions, and execution that are closely monitored throughout the year will be the call to order for successful businesses and a balanced lifestyle.

Think globally, act locally

This phrase has never been more appropriate as global economic trends are impacting strategic business and investment decisions in agriculture. Our first stop is China, the second-largest economy globally, which is experiencing a convergence of variables that is resulting in an economic slowdown.

First, demographics as a result of the one child policy is in full force. India has now surpassed China as the world's largest population. Youth unemployment is above 20 percent, even for college graduates, because the government has restricted technology development and use. This is resulting in social discourse with this group and is closely monitored by the government.

China's exports are down nearly 15 percent and over 40 percent to the U.S. and Europe, respectively, which is impacting the conservative spending habits of its citizens who saved $2.4 trillion during the three-year pandemic lockdown. The collapse of housing prices and commercial real estate is also influencing slow consumer spending and investment patterns. Late payments on 60 percent of China's $1.3 trillion in investments as a part of the Belt and Road Initiative in over 70 countries, coupled by high domestic debt, will be a burden on China's future economic growth. Slow economic growth will affect agriculture exports to China, particularly commodities such as cotton, soybeans, pork, dairy, hay, and poultry.

India will not be the engine of growth to replace China on the economic stage. Their economy is fragmented with power at the state level rather than at the federal level. About 55 percent of its population are subsistence farmers and only 23 percent of the workforce is made up of females. This is not a recipe for propelled economic growth. Despite this, India has surpassed Great Britain's economy for the fifth ranking globally and is projected to move past Germany into the third position by the end of the decade.

Moving to Europe, current economic releases find that negative quarterly economic growth is occurring. Similar to last year, Europe, which represents 20 percent of the global economy, will teeter on the brink of a full recession this winter. Too much dependence on Russia for inexpensive energy and China for export markets along with regional wars will challenge many countries within the Euro sector. Closely watch the weather for a cold winter, which could result in higher energy prices not only in Europe, but globally. There is also a "greenlash" movement emerging as the economic realities of moving too quickly from fossil fuels to green energy are becoming apparent in Europe.

The Southern Hemisphere will be a competitive force moving forward. Brazil and Argentina are increasing their corn and soybean acreage and are becoming China's preferred buyer compared to the United States. Technological advances in crop and livestock production will make this area of the world a prime-time competitor, along with Australia and New Zealand.

Domestic economy

The United States economy has a number of headwinds. One hundred billion of student debt will impact the level of consumer and housing investments, particularly for millennials. The labor strikes and resulting higher wages could eventually be a challenge to global competitiveness. The budget impasses and the erosion of governance going into the federal election cycle are key elements that could impact consumer confidence and investment decisions. To be blunt, the rapid rise of government debt and deficits in a non-recessional time is fiscally unsustainable. This has resulted in a downgrade of U.S. debt by rating agencies which in turn has resulted in a rapid rise of long-term interest rates as investors seek a higher rate of return for the risk of investing in U.S. debt.

The leading economic indicators are blinking red!

Whether it is the Index of Consumer Sentiment, the inverted yield curve, housing affordability, the Purchasing Manager Index (PMI), or the Leading Economic Index (LEI), the major economic indicators are all pointing toward a recession in 2024. Government spending and programs to stimulate the economy under fiscal policy have, in part, prolonged the economic expansion and the possibility of a recession. It will be interesting to see if fiscal policy wins out over monetary policy.

Other trends

On an optimistic note, in my travels and when conducting seminars there are some positive trends occurring.

- Lenders are expressing that some producers have working capital and cash positions that are still very strong and can weather a multi-year downturn.

- Risk management programs for both crop and livestock farms are putting floors on losses. These resources were not around during the 1980s farm crisis.

- The young and beginning producers are embracing the importance of advisory teams to provide perspectives and guidance in decision-making. This is very important for business and financial success, but also for mental health.

- The agri-entrepreneur is a growing segment in U.S. agriculture. These individuals are multitaskers using skills and expertise to generate revenues. They are opportunists by benefiting from exposure to new ideas and perspectives to get them outside the decision-making silo.

Many veterans of multiple economic cycles indicate that you build your best business successes during the downward part of the economic cycle. We will see if the proof is in the pudding and if the economic megatrends previously discussed will play out.