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Views from the Road

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The farm management newsletter is back with the first edition kickoff after focusing on engagement with producers, lenders, and agribusinesses in 37 states this year. Recently, I was in Milwaukee, Wisconsin, to address the American Bankers Association's Agricultural Bankers Conference. Approximately 500 individuals from the U.S. and Canada were in attendance. A full docket of speakers on a broad range of topics provided additional perspectives on the state of the agriculture economy.

Defensive domain

A three-year mini-super cycle, or an offensive domain, spurred by temporarily favorable economics and lush government stimulus checks provided somewhat of a buffer going into this downturn. However, the negative triple play consisting of lower prices received, inflated costs, and interest rates that are double compared to a decade ago is compounding the losses and reducing working capital reserves. As the agriculture industry consolidates with more zeros and commas on the balance sheet and income statements, some losses are in the six- to seven-digit range. One large agricultural lender attending the conference indicated that he had $300 million in distressed or foreclosure debt in his portfolio! Other lenders confirmed this to a lesser extent. One of the themes at the conference was that this downturn is a first-time experience for many new lenders, management, board members, and regulators. One can only hope that we do not get a knee-jerk reaction across the board.

On a side note, some producers who have diversified operations, businesses with livestock, value-added enterprises, or outside income are in a much better position to weather this economic storm.

Duration

A major question in the hallways and networking sessions was how long and how deep will the downturn be? Will the government provide disaster checks similar to previous years? To answer it bluntly, one certainty about the government's strategy for agriculture and rural America will be its uncertainty.

The new administration will be required to "thread the needle" of tariffs, sanctions, trade policy, and government exports markets. With one in every five dollars of net farm income generated from the sale of agricultural goods outside our borders, trade negotiations will be a delicate balance. Careful analysis of counter tariffs on manufacturing and technology is critical, since they could result in negative tariffs on agriculture. Our neighbors to the north experienced this with the 100 percent tariff that was placed on electric vehicles from China only to then lose the Chinese canola market.

One must examine the economic health of our big three trading partners: Mexico, Canada, and China. Mexico's first female leader will follow the policy of the past administration. However, the recent downgrade of the Mexican economy's debt outlook to negative by Moody's does not bode well for consumer spending. Closely watch the aggressive strategy of the Mexican drug cartels, possible U.S. involvement, and additional U.S. scrutiny on immigration. Canada is experiencing a down economy along with China. Despite recent stimulus, demographic issues in China and paper wealth declines in the real estate and stock markets have placed Chinese consumers in a defensive consumption mode.

India, boasting the world's largest population, is in an agricultural protectionism mode. Germany, Europe's largest economy, and most of the European region are operating just above recessionary levels.

What is different today compared to a decade ago is that there is more intense competition from the Global South. Many nations in the Southern Hemisphere have been a part of the Belt and Road Initiative spearheaded by China and the BRICS nations (Brazil, Russia, India, China, and South Africa). Approximately $1.3 trillion has been invested in infrastructure projects which is resulting in direct trade to the growing populations and economies in the Asian Rim.

A framework for another currency to compete against the U.S. dollar is now being implemented. The aggressiveness of these efforts will be predicated on how the U.S. utilizes the dollar as a strategic weapon in military and global political influence.

U.S. economy

The U.S. economy is one that could be coined as fragile, despite run ups in the stock and real estate markets and resulting paper wealth increases. The extent of a possible recession will depend on the economic health and consumption of a cast of three economic characters in the U.S. economy.

1. *ALICE: Asset Limited, Income Constrained, Employed*

   This segment of consumers has spent their stimulus funds and are now incurring large amounts of credit card and consumer debt. In some cases, this group is experiencing increasing delinquencies. While this segment of the economy is in recession mode, it is not enough to put the entire U.S. into a recession.

2. *HENRY: High Earner, Not Rich Yet*

   The HENRY segment of consumers is an important group to observe. These individuals and households are high income earners, but housing costs are a burden on their consumption. This group has not had the time or opportunity to garner paper wealth in homes, the stock market, or with cryptocurrencies. These individuals are often white-collar workers who are very prone to corporate restructuring or being replaced by artificial intelligence (AI). Closely analyze the economic health and job status of this group in 2025 for signs of a possible recession.

3. *HERMAN: High Earner, Rich, Mobile, Appreciated Net worth*

   These individuals are high earners, rich, mobile, and have appreciated net worth often between $1 and $10 million dollars. This group has had time to accumulate paper wealth in the stock and real estate markets. Job losses or a correction in either the stock market or the housing market could impair this group's spending patterns and place the U.S. into a steep and long downturn.

Interest rates

The Federal Reserve is in interest rate cutting mode. However, will tariffs result in higher inflation, which could push interest rates higher? The national debt and deficit buildups may also result in long-term interest rates remaining higher. Investors and people who finance debt often perceive the lack of discipline in government expenditures and debt buildup as additional risk, which ultimately results in higher charges for interest. Interest expense on the national debt is now larger than the military budget and fast approaching the Social Security and Medicare budgets.

When it is all said and done

The agriculture industry and its producers have been in a similar position before, but each down cycle is different. Some producers will discontinue business or be forced out of operations while others will adjust their business operation as the industry goes through its cycle. The first phase is the offensive or growth domain and that is often called the “spring” and the “summer” where profits and equity are strong. Aggressiveness and greed in management behavior is often observed in this phase.

Currently, the industry is in the defensive domain where the fear of producers, lenders, and suppliers is most notable. However, around the corner is the regenerative domain. This is where the businesses that are operated with a management mindset can not only carve out a path for profits, cash flow, and wealth building, but also fulfillment of the business and personal goals. Also, the path forward will not be a one-size-fits-all method of management, which is a part of what makes the agriculture industry both challenging and opportunistic.