



An Outlook for the U.S. Economy and Agricultural Sector

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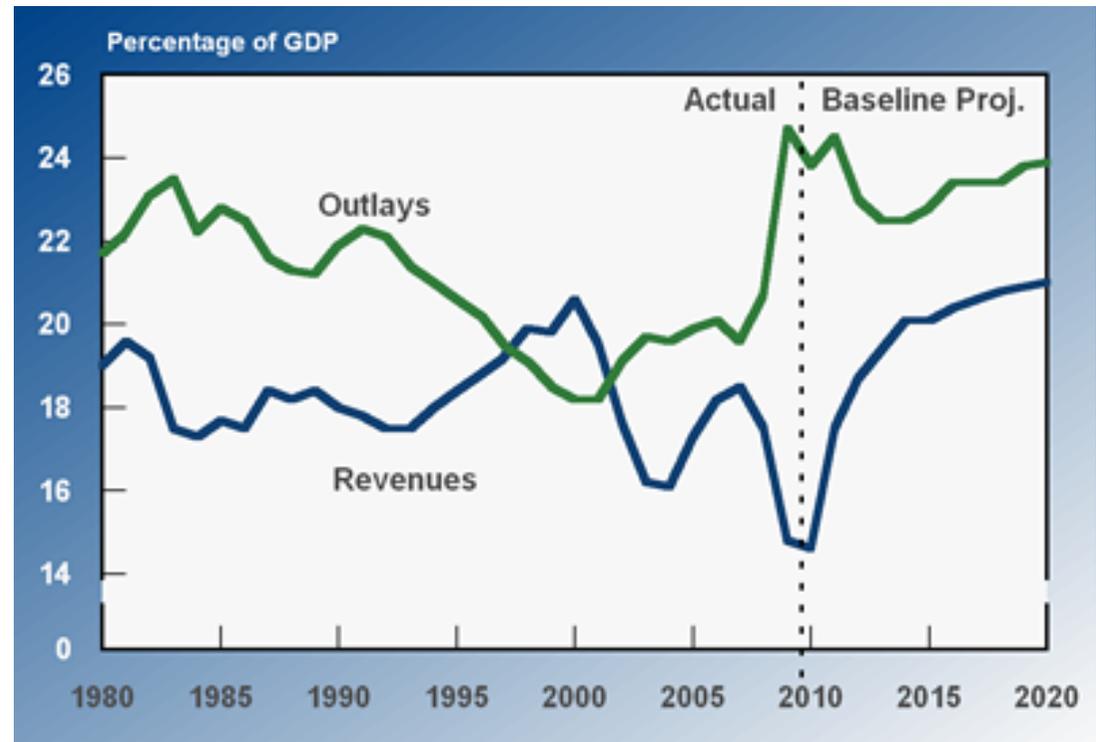
Larry Combest Chair of Agricultural Competitiveness

Lamesa Chamber of Commerce, September 1, 2010

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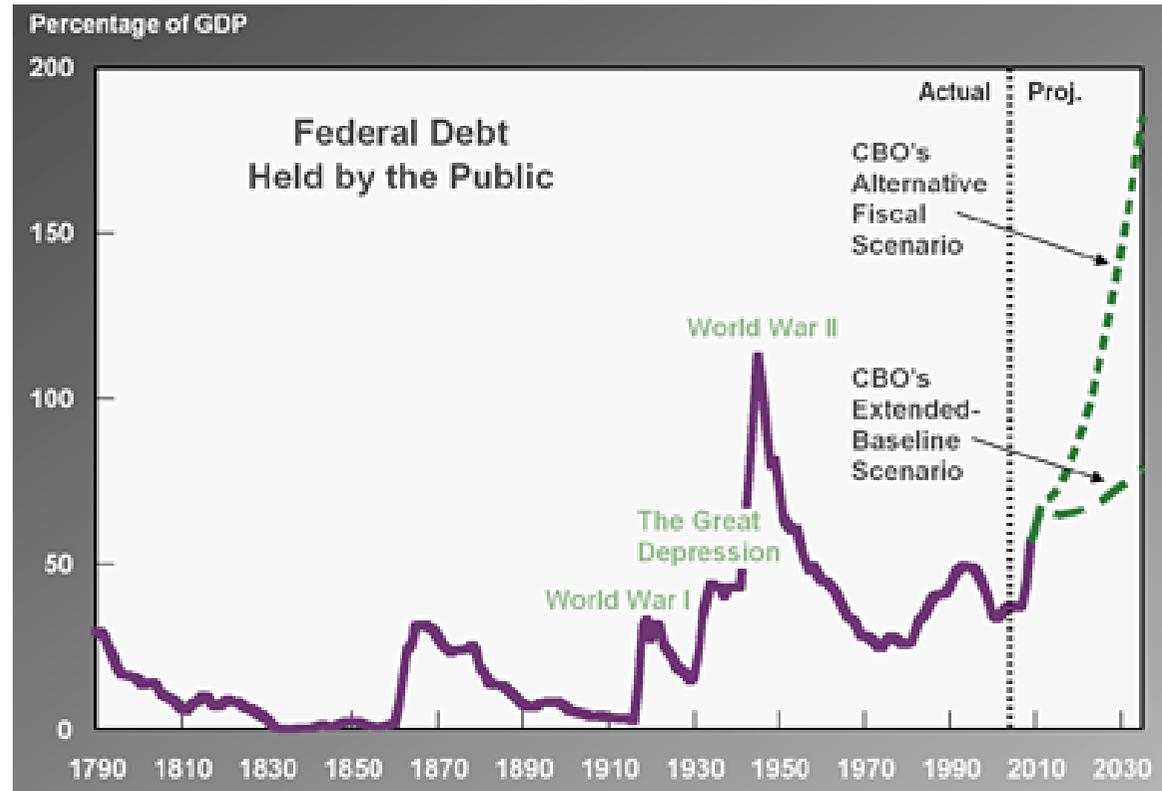
Where We Are...

- Federal debt has spiked and will continue to grow over time.
- I predict that the health care bill, if left as is, will balloon the deficit because spending is mandatory, but tax revenue may or may not materialize.



Where We Are...

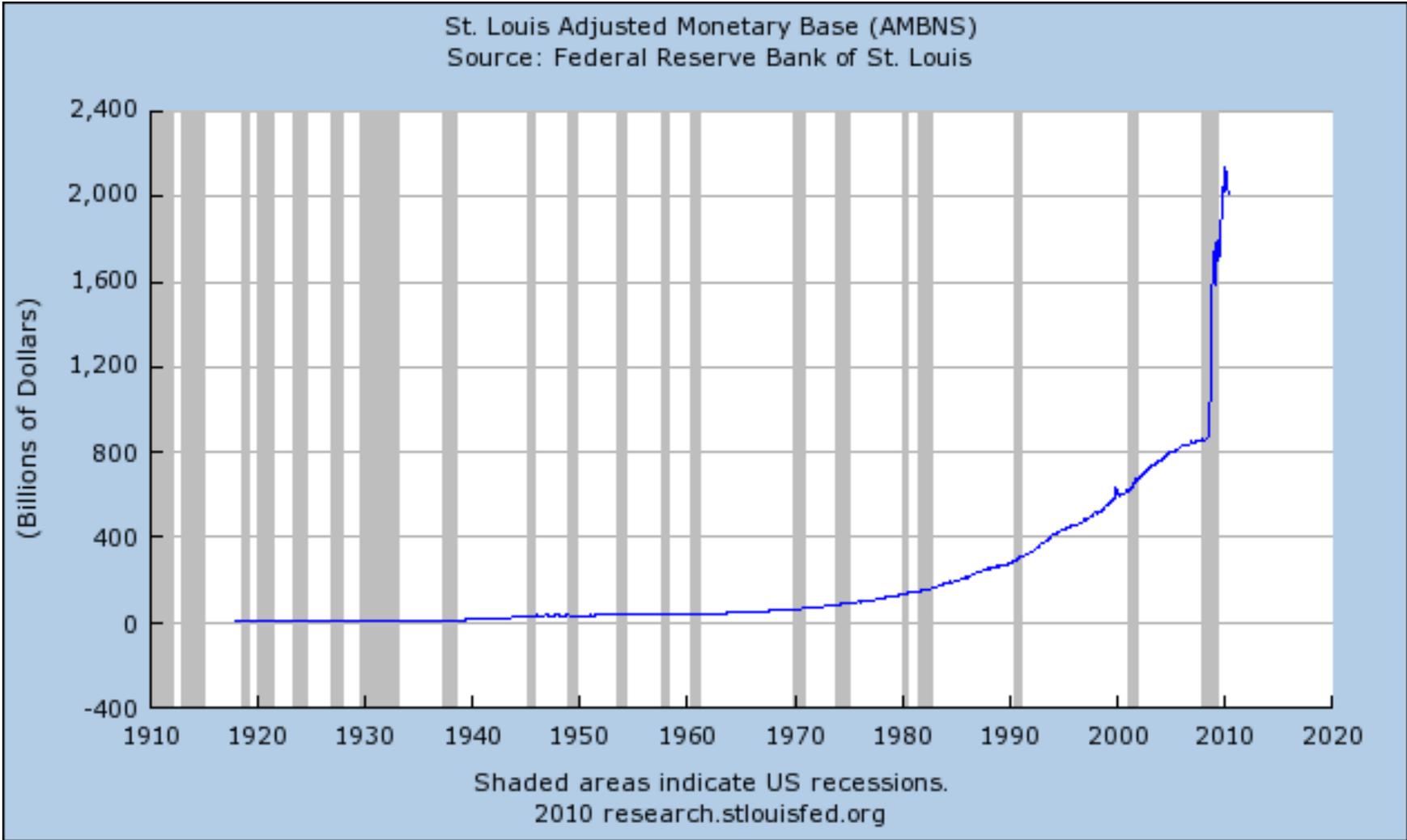
- Current debt-to-GDP is by no means unprecedented, but...
 - At the end of WWII, 85% of federal spending was military, and that went away.
 - Today, 85% is mandatory entitlement spending, and that will not go away.
- Creates tremendous pressure
 - Interest rates will adjust to account for both the risk of default and the competition for private sector money...not happening yet, but the risk is real
 - Higher taxes and/or lower spending



Macro Effects

- Large budget deficits have led to tremendous pressure to reduce spending
 - Congress will be seeking “low hanging fruit” to cut out of the budget
 - Farm programs are increasingly unpopular in urban centers
- Over the longer term, borrowing costs are likely to rise
- Fed is playing a “blind nello” hand
 - Largest mortgage holder
 - Primary objective of inflation fighting

Money Supply



Inflation

$$\textit{Inflation} = \textit{Money Supply} * \textit{Money Velocity}$$

Near Zero



Why no spending?

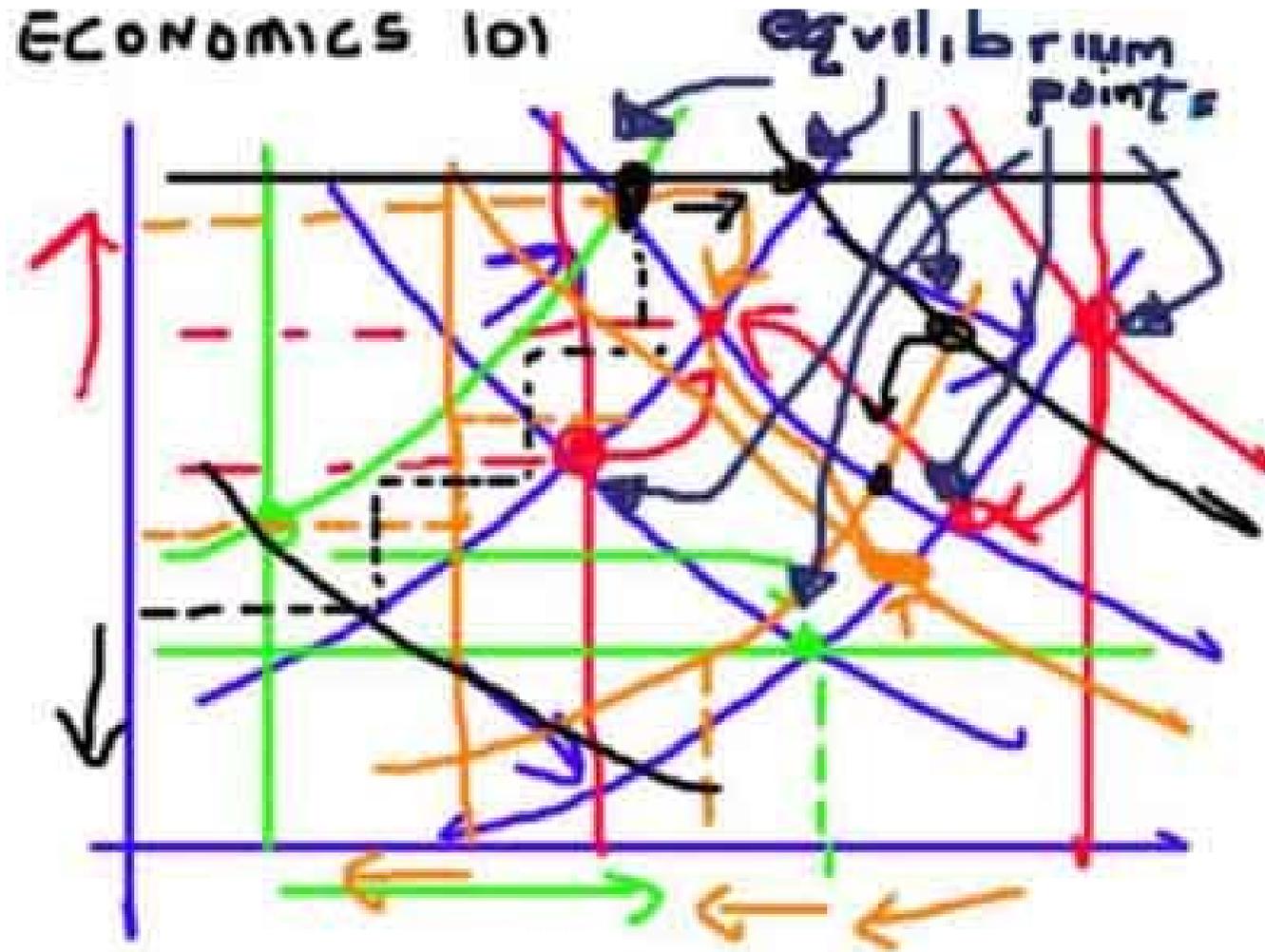
Annual Change in US Debt



Outlook

- Much more downside risk, than upside in the short-run
- Too much policy uncertainty
- Risk of inflation low in short-term, but high risk in the 4-8 year time frame

Prediction is Difficult



Which leads to guessing...



So here goes...



Why the support for this rally?

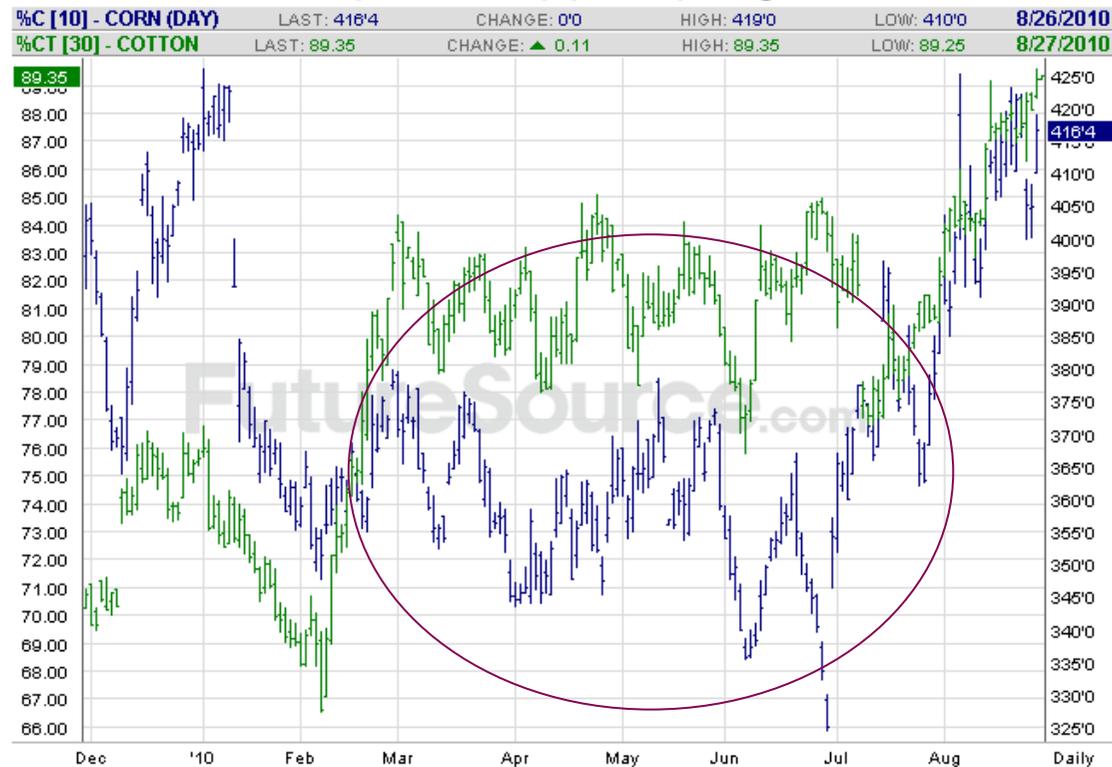
- VERY short stocks going into this harvest
- Production problems in Pakistan (floods)
- Clamoring in India for reserving more of the domestic crop for textile mills (less exports on the world market)

What to expect going forward...

- A global supply response next year (farmers are very good at responding to price signals...how big depends on weather and the price of other crops)
- Mitigating factors
 - RFS—as the RFS goes, so goes the price of ethanol and corn; acreage in the Mid-South and Southeast partially driven by this policy
 - Will sorghum get listed as a “second generation” biofuel? If so, could open the door to acreage diversion from cotton to sorghum
 - Biofuels have important implications for local communities

Farm Bill Prospects

- Tight budgets will mean demand for reductions in spending
- Current Ag Committee Chair Collin Peterson (D-MN) has indicated he strongly prefers eliminating direct payments (and has also said that the only place to get real money is out of the “cotton price support program.”)



Conclusions

- A lot of issues hinge on this mid-term election
 - Budgetary priorities; spending reductions; relative emphasis of programs (environmental vs. business-oriented)
- Resolution of the policy uncertainty may increase business and consumer confidence
- Cotton price rally has legs; but, if we do not see sustained economic growth globally, over-supply next year may be a real damper on prices
- Other policies are important too; RFS, CRP, etc., all have an impact on local market conditions and communities