

THOUGHTS ON THE 2018 TOBACCO SEASON

Look for additional concentration in Kentucky's tobacco industry for 2018. For individual growers, burley contract volume ranged from a small percentage increase to total contract elimination. In aggregate, burley contract volume is likely down around 15% for the upcoming growing season. Burley contract volume fell due to anticipated continual decline in U.S. cigarette production (down 9.1% in 2017 – the largest annual decline since 2009), slumping leaf exports (down 19.2% in 2017), and increased utilization of imported leaf (now likely exceeding 60% of total burley use by U.S. cigarette manufacturers).

USDA's planting intentions, released on March 30, 2018, revealed that U.S. burley growers planned to harvest 72,900 acres in 2018 – 11% lower than the year before. However, the USDA survey was conducted in early March, prior to most company's contract announcements. A 15% drop in "official" U.S. burley acres would generate a crop in the neighborhood of 140 million pounds, which still may be 15 to 20 million pounds more than current market demand. However, the official U.S. burley acres reported by USDA last year seemed on the high side and consequently the expected surplus may not be as large as indicated above. Nevertheless, market conditions are calling for a smaller U.S. burley crop in 2018.

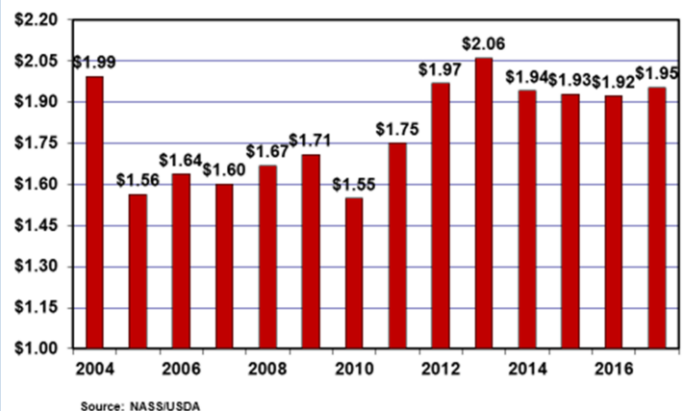
Contract price schedules also varied considerably by company with some companies increasing top grades by two to five cents per pound, while one major buyer kept contract prices constant, with some smaller purchasers actually lowering prices. Based on the weighted contract price schedules below for the largest buyers, a crop graded 30% #1s and 70% #2s across all companies would average \$1.99/lb. in 2018 versus \$1.96/lb. evolving from the 2017 crop price schedules. According to USDA, the 2018 U.S. burley crop averaged \$1.95/lb., 3 cents higher than the 2016 crop, but still below the pre-buyout price of nearly \$2.00/lb. in 2004.

2018 Average Burley Contract Prices by Company and Grade 1/

BUYER	GRADE			
	1	2	3	4
A	\$1.96	\$1.86	\$1.67	\$1.02
B	\$2.13	\$2.04	\$1.94	\$1.24
C	\$2.07	\$2.02	\$1.85	\$1.48
D	\$2.06	\$2.00	\$1.87	\$1.42
2018 WGT AVERAGE	\$2.05	\$1.96	\$1.82	\$1.21
2017 WGT AVERAGE	\$2.02	\$1.94	\$1.80	\$1.20
2016 WGT AVERAGE	\$2.02	\$1.93	\$1.80	\$1.20
2015 WGT AVERAGE	\$2.03	\$1.95	\$1.82	\$1.30

1/ Weighted Average Based on Estimated Percentage Volume Purchased By Buyer and Typical Crop Throw

U.S. Burley Prices



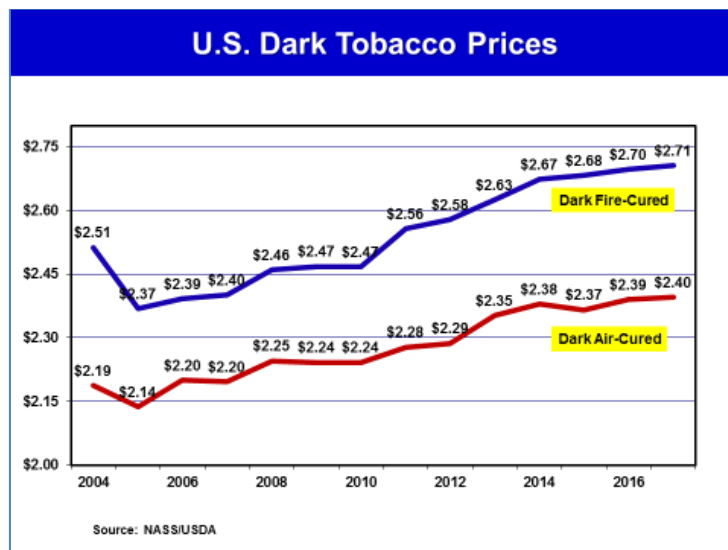
As always, burley returns are extremely variable based on assumed yields and labor expenses. H2A wage rates for Kentucky for 2018 increased to \$11.19/hr. compared to \$10.92/hr. last year. Housing, travel, workers comp, and other fees must be taken into consideration for those employing this legal seasonal workforce to determine the total hired labor wage rate, which is likely approaching \$15.00/hr. Assuming an average burley price of \$1.95/lb., 150 hours of hired labor, coupled with relatively flat non-labor input costs, generates the following net returns for the 2018 crop to compensate for a producer's own labor, management, and land under different wage and yield scenarios (see table below). Given these assumptions, improved yields and labor efficiency will once again be critical to generate a profitable burley crop in 2018.

**2018 Burley Net Returns to Land and Operator Labor and Management
For Various Yields and Total Hired Labor Wage Rates 1/**

Yield	\$10/hr.	\$12.50/hr.	\$15/hr.
1750 lbs./acre	\$0.04	-\$0.18	-\$0.40
2000 lbs./acre	\$0.28	\$0.09	-\$0.10
2250 lbs./acre	\$0.46	\$0.29	\$0.12
2500 lbs./acre	\$0.61	\$0.46	\$0.31
2750 lbs./acre	\$0.66	\$0.52	\$0.38

1/ Based on an average burley market price of \$1.95/lb. and 150 hours of hired labor/acre. The 2018 burley budget can be accessed at <http://www.uky.edu/ag/agecon/pubs/exttobbudget201857.xls>

Dark air cured acres were projected by the USDA planting intentions report to be 13% lower, while dark fire-cured acres were relatively flat, despite one major buyer cutting contract volume in excess of 10%. Overall, dark tobacco production is being constrained by a slowing in the growth in domestic smokeless tobacco consumption, with U.S. consumer sales of snuff relatively flat in 2017. Like burley, look for dark tobacco prices to remain relatively flat for the 2018 crop. Unlike burley, dark tobacco prices are 20 to 30 cents/lb. higher than pre-buyout prices.



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KFBM CROP FARMS SHOW IMPROVEMENT

Preliminary data from crop farms participating in the Kentucky Farm Business Management (KFBM) indicate some financial improvement in 2017 compared to 2016. Highlights include the following.

- Net Farm Income was \$200,356 in 2017 compared to \$68,746 in 2016. Management Returns were positive for the first time since 2013 at \$15,488.
- Average Working Capital totaled \$713,350 in 2017, up more than \$100,000 from previous year. Current ratio was 1.74:1 compared to 1.62 for 2016.
- The average crop farm included \$7.6 million in assets for 2017. Net Worth was \$5.3 million, up about \$200,000 from 2016. Debt-to-Asset Ratio was 31%, up slightly from 30%.

While much of the improvement was due to farm managers reducing cost and restructuring balance sheets, generally increased yields and fairly stable prices helped tremendously this past crop year.

The data come from analysis of farms participating in the Kentucky Farm Business Management program completed by March 1 each year. The Final Analysis will be available by early June. For more information, see the Quick Links at <http://www.uky.edu/Ag/KFBM/>.



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