



North American Potato Market News

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EXECUTIVE SUMMARY

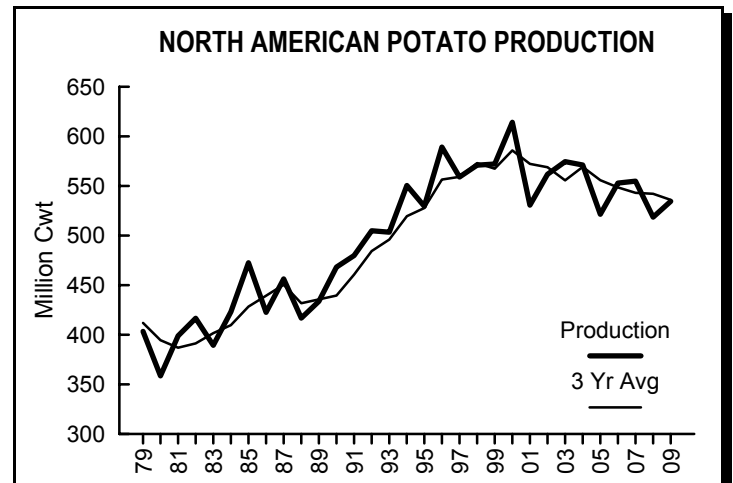
- ☞ **Long term challenges facing the potato industry are becoming more clear, as the decade draws to a close.** Production data suggest that demand for North American potatoes has been declining by at least 1.0% per year since 2000. This year's low open market prices and weak usage suggest that the pace of that decline may be accelerating.
- ☞ **The upward trend in potato yields magnifies the need to limit potato acreage.** Trend yield increases add 1.0% to potato supplies each year, all other things being equal. Such increases point to the need for continual acreage reductions unless demand for potatoes increases by a similar, or greater amount.
- ☞ **North American potato acreage has been trending downward since 1998.** Between then and 2009, the area planted to potatoes has fallen by 20.4%. Current market conditions are signaling that additional acreage cuts are needed.
- ☞ **There is no indication as to when or if the erosion in demand for potatoes can be halted or reversed.** Until that happens, the industry needs to plan for consolidation and supply management. Even if consumption were to stabilize at current levels, yield increases would necessitate a 175,000 acre reduction in planted area by 2020. If demand for potatoes were to decline at a 2.0% annual rate, the needed reduction, by 2020, would be 427,000 acres, or 30% of the 2009 total.
- ☞ **If growers do not take collective action to reduce acreage, market prices will produce the needed cuts.** Both avenues have strong points and weak points. Cooperative efforts to manage supplies can ease the transitional pains by maintaining prices above the cost of production. However, it is difficult to obtain and maintain the solidarity needed to make such efforts succeed. In addition, such collective efforts can reduce incentives to improve productivity. Markets tend to be more efficient supply managers, but the need for continual acreage reductions would keep pressure on prices, and limit returns to growers.
- ☞ **Acreage models point to the potential for a 7.9% reduction in 2010 fall potato acreage.** Growers should not take such a projection to be an invitation to take a contrarian position! Stocks and usage data suggest that such a cut may not be sufficient to balance supplies with demand, at prices that would offer growers a reasonable return. In addition, the model offers only rough guidance as to the number of potatoes that will be planted next year. Growers who choose to ignore the current market signals will be putting their financial future at risk.
- ☞ **Seed potato acreage is down in both Manitoba and Saskatchewan.** The Saskatchewan area is down 25.3%.
- ☞ **Markets have been relatively stable during the holidays.**

PUBLISHING SCHEDULE

North American Potato Market News will not be published on January 6, 2010. We are taking the week off, in order to facilitate attendance at industry meetings in Orlando, Florida. This is one of four scheduled weeks off during the year. The next newsletter will be published on January 13, 2010.

CHALLENGES FOR 2010 AND BEYOND

Balancing potato supplies with demand will continue to challenge the potato industry during the coming decade. A sustainable balance occurs when the market provides growers with a reasonable return on their investment. Directly measuring demand for potatoes is difficult, and the results are imprecise. However, in the long run, supplies must match demand. If supplies fall short of covering demand, prices will rise to levels that will encourage production to expand, to fill the gap. When supplies exceed demand, prices fall to levels that drive production from the market. The chart below is a history of North American potato production since 1979. It provides a good indication of changing demand patterns for North American potatoes, during that time frame.

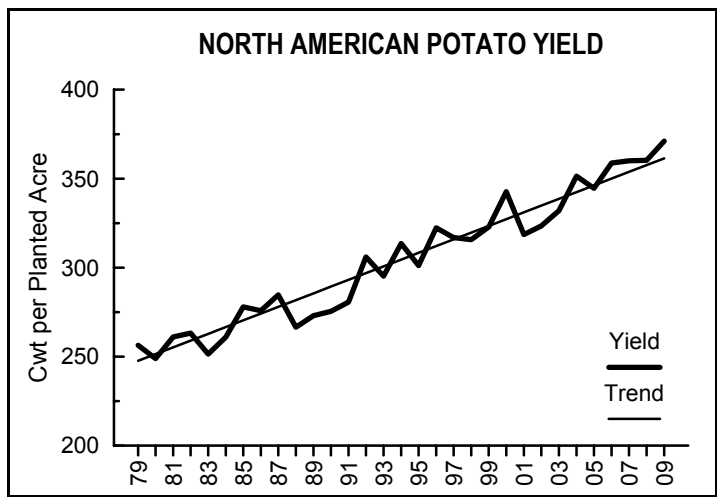


Demand for North American potatoes has been declining for the past nine years. While year-to-year changes in production are volatile, a three-year moving average of production shows discernible trends. Between 1980 and 1990, the three-year average of production grew at a 1.0% annual rate. The growth rate accelerated to 2.9% per year during the 1990s. Since 2000, the trend has reversed. Potato production has been declining at a 1.0% annual rate since it peaked in 2000. Each of the production growth rates can be used as proxies for demand trends during the decade, in which it occurred.

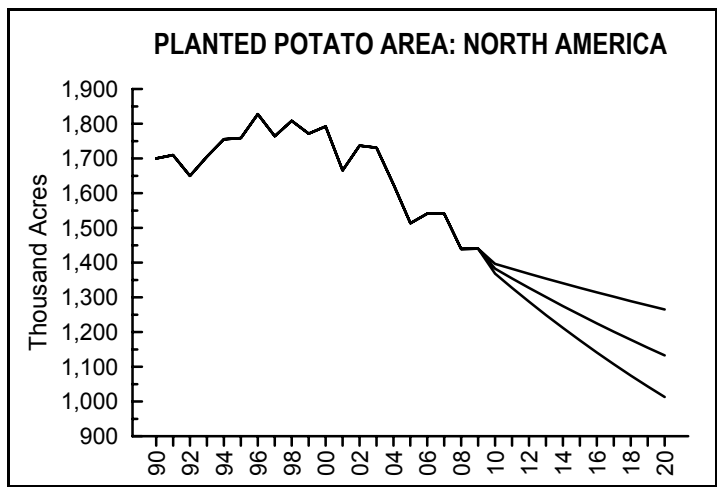
Current market conditions suggest that demand may be declining at an accelerating rate. In 2009, potato production fell 1.48 million cwt short of the three-year average, though it exceeded the 2008 crop by 15.9 million cwt, a 3.1% increase. Contract prices for processing and chip potatoes remain above the cost of production, but open prices for most fresh potatoes have fallen to levels that do not cover production costs. Though this year's production increase was only 3.1%, the industry held 7.0% more potatoes in storage on December 1 (US and Canada combined) than it did a year ago. Early-season disappearance declined by 8.7 million cwt, or 5.5%. If that is a true indication of demand factors, it would suggest that North America has about 39 million cwt more potatoes in storage than the industry needs. Growers are likely to dump some of the extra potatoes. Others will be claimed by shrinkage and waste, but this year's extra potatoes would be enough to extend the

storage season by a month, if nothing were done to mitigate the current supply situation.

The relentless trend in potato yields exacerbates the challenges facing North American growers. Average yields continue to increase by 3.8 cwt per year, a trend which has persisted at least since the end of World War II. Acreage consolidation may be enhancing that trend, as production is concentrated on the best potato ground, and in high yielding areas. Currently, the average yield increase results in slightly more than a one percent increase in potato production each year, all other things being equal.



The clash between upward trending yields and declining demand will force continual adjustments to potato acreage. Assuming that nothing is done to arrest the decline in demand, the potato industry will be forced to continue reducing acreage for the foreseeable future. The extent of the cuts will depend on the rate at which demand declines. In 1998, North American potato acreage reached its highest level in more than 30 years, 1.81 million acres. Since then, it has fallen by 20.4%, to 1.44 million acres. The average decline has been 2.0% per year. The chart below shows projected planting through 2020 under three scenarios. The first scenario assumes that demand stabilizes at the 2009/10 level. Given that assumption, the increase in expected yields would force North American potato area to decline by 175,000 acres from 2009 plantings, by 2020, in order to balance supplies with demand. If demand continues to erode at one percent per year, the needed acreage reduction, by 2020 would be 308,000 acres. Should the rate of decline be two percent, rather than one percent, then the planted area would drop by 427,000 acres. Viewed another way, if the average potato acreage per farming operation were to remain constant



between now and 2020, the number of farms growing potatoes would decline by between 12% and 30%. Such attrition is seldom a painless process. The most likely reason for a farmer to quit growing potatoes is because production costs exceed returns. While that process tends to weed out the least efficient operations, the low prices create a strain for almost all growers. The market pressure will force growers to become more efficient, to survive, but the experience is likely to be less than pleasant.

Voluntary efforts may not be sufficient to keep potato acreage balanced. Unless demand for potatoes turns around, growers only have two options for balancing supplies. They can either act collectively to bring acreage down in an orderly manner, or they can allow market forces to remove excess acreage through attrition. While collective action may be less painful than attrition, it has its drawbacks. It puts the burden for controlling supplies on the shoulders of cooperating growers, while providing non-cooperators with an umbrella under which they can maintain or expand their farming operations. It also creates disputes between cooperating growers on how to equitably share the burden. The *United Potato Growers of America* model for cooperative supply management started with the premise that demand erosion was primarily a fresh potato industry phenomenon. It is now clear that demand for frozen and dehydrated potato products also is eroding. The chip potato demand situation is less clear, but it is doubtful that that sector is growing fast enough to offset trend yield production increases. The complexity of demand conditions, for the various sectors of the potato industry, add to the challenges inherent in balancing supplies with demand through cooperative action. For any such action to succeed, cooperation must be widespread, from all sectors of the potato industry. While it is tempting to believe that each sector could take care of its own issues, spillover effects, both in terms of marketing surplus potatoes from one sector through other market channels, and in terms of growers from one sector shifting production to another, to take advantage of better market conditions, tie all of sectors of the potato industry to a common fate.

Collective action to control supplies creates other challenges not inherent in a free market solution. The economic goal of collective supply actions is to protect a minimum return for growers that would cover production costs plus an additional margin. Defending such a target price requires removing any excess potatoes from the market. Supplies can always fall short of production targets, in which case prices and returns would be likely to exceed the predetermined targets. On the other hand, a successful supply management program would never allow excess potatoes to reach the market. While growers still could work on programs designed to boost demand, the only way that any increase could be fed is if the growers had confidence to produce more potatoes than the current demand environment would support, at the target price. Under those conditions, increased demand might boost prices, but it would be unlikely to result in increased sales volumes, due to supply limitations. Perhaps target production eventually would be increased, but the delayed response times would make it difficult to boost potato consumption. In addition, continually holding grower returns above the cost of production would reduce incentives for innovations designed to lower the cost of production.

FIRST LOOK AT 2010 FALL POTATO ACREAGE

Current market conditions point to a sharp decline in 2010 fall potato acreage. Following this year's collapse in fresh potato prices, potatoes are less competitive with alternative crops than they have been in all but seven years since 1976. We use the ratio of the Idaho Grower Returns Index (IGRI) to the national average price of wheat as an indicator of the relative competitiveness of potatoes. Our studies show that October-December market conditions are a good indicator of changes in fall potato acreage for the com-

ing year. This year marks the eleventh time since 1976 that the October-December IGRI has fallen below the average price for a bushel of wheat. Following 9 of the 10 previous occurrences, fall potato acreage has declined. Our best acreage model, which includes a trend, as well as separate variables for wheat and potato prices, suggests that 2010 fall potato acreage could be down 7.9%.

PRICE RELATIONSHIPS AND US FALL POTATO ACREAGE

(Prices are for the Preceding October-December Period)

Year	IGRI	Wheat	Ratio	Planted	Change
1992	\$3.02	\$3.25	92.9%	1,171.4	-4.2%
1995	\$3.48	\$3.75	92.7%	1,228.1	-1.3%
2005	\$3.14	\$3.43	91.6%	969.7	-6.8%
2010 *	\$4.15	\$4.69	88.5%	??	??
1977	\$2.13	\$2.48	85.8%	1,193.4	0.4%
1986	\$2.73	\$3.19	85.6%	1,083.9	-10.0%
2008	\$6.08	\$7.58	80.1%	931.1	-7.6%
1980	\$2.98	\$3.91	76.3%	1,009.7	-8.3%
1979	\$2.22	\$3.01	73.9%	1,101	-8.4%
1997	\$2.60	\$4.11	63.3%	1,210	-4.7%
2001	\$1.76	\$2.79	63.0%	1,091.3	-10.8%

IGRI is NAPMN's Idaho Grower Returns Index; Wheat price is US average received by growers; planted area is thousands of acres. * Wheat price is preliminary.

Growers should not alter 2010 production plans, based on the acreage model results! While the gut reaction may be that a 7.9% cut should be sufficient to assure good profits for 2010 crops, that may be wrong on at least two counts. First, acreage models only provide general guidance, indicating the direction in which market forces are pointing growers. The margin of error on the best acreage models is quite wide. Several other factors enter into the planting decision, including contract availability and perceived demand conditions, as well as reactions to model projections and planting intentions. For example, our best acreage model projected an 8.2% acreage increase for 2008. The actual increase was limited to 0.6%. The model results received a great deal of publicity, which probably altered planting intentions significantly. In addition, fryers reduced contract volumes significantly from year-earlier levels. Finally, a continual downtrend in potato prices, from January through the planting season, probably discouraged some of the expansion plans. In the end, limiting the acreage increase to 0.6% was not sufficient to stabilize the potato market. One wonders what would have happened had growers planted 8.2% more potatoes in 2009 than they did in 2008.

Would a 7.9% acreage reduction be sufficient to boost 2010 potato prices to profitable levels? Though a significant acreage reduction appears to be in the cards, it may not reduce supplies enough to give market prices a boost. That is the second reason why a contrarian strategy (planting more when models say that the industry will plant less) could be dangerous in 2010. If growers cut 2010 potato acreage by 7.9%, and the 2010 yield fell back to the trend level, 420 cwt per acre, US fall potato production would fall to 357.4 million cwt. That is down 36.6 million cwt from the current estimate of the 2009 crop, a 9.2% decline. If storage potato usage continues to run 5.1% behind the 2008/09 pace for the remainder of the storage season, this year's surplus would be 33.2 million cwt. Not all of that will displace potatoes from the 2010 crop, but the industry is likely to use a portion of the extra potatoes during the July-September quarter. As a conservative estimate, let's assume that half of the extra potatoes will come to market. That is 16.6 million cwt of potatoes that growers would not need to produce next year. Based on current estimates, 2009 fall potato production totaled 394.0 million cwt. If that included a 33.2 million cwt surplus, then the industry could have gotten by with 360.8 million cwt of fall pota-

atoes this year. If we assume no further erosion in demand, for the 2010 crop, then the carryover from the 2009 crop might reduce production needs to 344.2 million cwt. While these calculations are only rough estimates, they illustrate the perils in trying to game the system. If they are accurate, a 7.9% acreage cut could leave the industry with a 3.7% surplus. That does not account for the potential for yields to exceed the trend, nor for any further demand erosion.

SEED AREA DECLINES IN SASKATCHEWAN AND MANITOBA

Saskatchewan growers certified 3,910 acres of seed potatoes in 2009. That is 1,321 acres below the 2008 total, a 25.3% decline. The decline is consistent with December potato stocks data, which show a 26.9% decline in this year's seed potato holdings. The table below outlines variety shifts in the 2009 seed area.

SASKATCHEWAN SEED POTATO AREA

(Acres Accepted for Certification)

	2006	2007	2008	2009	Change
Russet Burbank	1,562	1,374	1,503	1,135	-24.5%
Norland	816	667	673	511	-24.1%
Prospect	39	59	96	285	198.2%
Norkotah	475	163	254	263	3.8%
Shepody	378	358	236	259	9.9%
Baby Boomer	*	*	*	152	- NA -
HO 2000	*	*	*	152	- NA -
Ranger Russet	203	166	200	130	-35.2%
Piccolo	*	*	*	128	- NA -
Umatilla Russet	66	124	22	88	310.7%
Alpha	129	180	148	74	-49.9%
Bintje	45	3	14	57	323.7%
Gemstar Russet	*	*	*	55	- NA -
Other	1,438	1,453	2,087	620	-70.3%
Total	5,150	4,547	5,231	3,910	-25.3%

Sources: PAA and CFIA

* May be included with "other"

Manitoba growers certified 6,524 acres of seed potatoes in 2009. That is 253 fewer acres than they certified in 2008, a 3.7% reduction. On December 1, Manitoba reported that it held 1.28 million cwt of seed potatoes, virtually the same as in 2008. However, 140,000 cwt of the 2008 seed crop had moved by December 1.

MANITOBA SEED POTATO AREA

(Acres Accepted for Certification)

	2006	2007	2008	2009	Change
Russet Burbank	3,392	3,566	3,274	3,027	-7.5%
Umatilla Russet	185	297	452	481	6.4%
Yukon Gold	234	442	432	390	-9.6%
Norkotah	127	96	130	368	184.0%
Norland	327	410	182	262	44.0%
Sangre	276	462	366	244	-33.1%
Innovator	--	--	60	239	300.5%
Shepody	315	581	478	210	-56.1%
Viking	171	161	135	183	35.6%
AC Peregrine Rd	8	49	146	142	-3.1%
Ambra	*	*	*	100	- NA -
Dakota Pearl	85	67	100	78	-21.9%
Adora	98	79	120	62	-48.1%
Ivory Crisp	*	*	*	59	- NA -
Goldrush	94	84	51	59	15.7%
Vivaldi	*	59	18	51	187.1%
Other	815	756	835	568	-32.0%
Total	6,127	7,109	6,777	6,524	-3.7%

Sources: PAA and CFIA

* May be included with "other"

SHIPPING POINT PRICES: DECEMBER 30

	Dec 30	-----Change From-----	
		Dec 22	Last Year
Idaho Russet Burbanks			
Baled 10# Size A	\$7.50		-\$8.00
Baled 10# Film Non-A	\$6.50		-\$7.50
40 Count Cartons	\$11.50		-\$10.50
50 Count Cartons	\$11.50		-\$10.50
60 Count Cartons	\$11.50		-\$10.50
70 Count Cartons	\$11.00		-\$11.00
80 Count Cartons	\$10.50		-\$11.50
90 Count Cartons	\$10.50		-\$9.50
100 Count Cartons	\$10.50		-\$9.50
#2 - 10 oz Minimum	\$10.00		-\$10.00
San Luis Valley			
Russet Baled 10# Film	\$10.00		-\$8.50
Russet 40 Count	\$12.00		-\$8.00
Russet 60 Count	\$12.00		-\$10.00
Russet 70 Count	\$12.00		-\$10.00
Russet 80 Count	\$12.00		-\$10.00
Russet 100 Count	\$12.00		-\$10.00
Russet Dry Bulk	\$5.25		-\$7.25
Columbia Basin			
Norkotah 10# Film	\$7.50		-\$7.50
Norkotah 40 Count	\$12.50		-\$12.50
Norkotah 60 Count	\$12.50		-\$13.50
Norkotah 70 Count	\$12.50		-\$13.50
Norkotah 80 Count	\$12.50		-\$12.50
Norkotah 100 Count	\$12.50		-\$8.50
NW Washington			
Red 50# Size A	\$26.00		-\$10.00
Red 50# Size B	\$40.00		-\$6.00
Red 50# Creamer	\$70.00		-\$4.00
Yellow 50# Size A	\$36.00		-\$12.00
Yellow 50# Size B	\$26.00		-\$6.00
Yellow 50# Creamer	\$70.00		-\$2.00
Wisconsin			
Russet 10# Film Size A	\$10.75	-\$0.25	-\$9.25
Russet 60 Count	\$12.00	-\$0.50	-\$12.50
Russet 70 Count	\$12.00	-\$0.50	-\$12.50
Russet 80 Count	\$12.00	-\$0.50	-\$10.50
Russet 100 Count	\$11.00	-\$1.00	-\$10.50
Red 50# Size A	\$12.50		-\$9.50
Red 50# Size B	\$27.00		-\$8.00
Klamath Basin			
Russet Baled 10# Film	\$8.50		-\$7.00
Russet 70 Count	\$14.00		-\$14.00
Russet 80 Count	\$14.00		-\$14.00
Russet 100 Count	\$13.00		-\$10.00
Red River Valley			
Red Baled 10# Size A	\$15.00		-\$5.50
Red 2000# Size A	\$10.50		-\$6.50
Red 50# Size B	\$27.00		-\$8.00
Red 50# Creamers	\$50.00		-\$3.00
Michigan			
Russet 10# Size A	\$13.50		-\$7.75
R White 10# Size A	\$12.50		-\$8.75
Maine			
Russet 10/5# 2" Min	\$12.50	-\$1.00	-\$8.00
R White 10/5# 2" Min	\$13.50		-\$6.00
Long Island			
R White 10/5# Size A	\$16.50		-\$9.00
R White 50# Size A	\$12.50		-\$9.00
R White 50# Large	\$13.00		- NA -

Source: Federal-State Market News. Midpoint of "mostly" range.
All prices are \$/Cwt basis. NA = Not Available. Blanks signify no change.

RUSSET TABLE POTATO PRICE INDICES: DECEMBER 30

	Dec 30	-----Change From-----	
		Dec 22	Last Year
Fresh Weighted Average			
Idaho Russet Burbank	\$8.60		-\$8.98
Idaho Russet Norkotah	\$8.24		-\$8.82
San Luis Valley	\$10.63		-\$9.03
Columbia Basin	\$10.20		-\$9.94
Klamath Basin	\$11.08		-\$9.85
Wisconsin	\$10.33	-\$0.41	-\$9.28
Grower Returns Index			
Idaho Russet Burbank	\$3.56		-\$5.25
Idaho Russet Norkotah	\$3.12		-\$6.51
San Luis Valley	\$5.31		-\$7.95
Columbia Basin	\$4.43		-\$6.24
Klamath Basin	\$4.50		-\$7.25
Wisconsin	\$5.20	-\$0.32	-\$8.25

Derived from Federal-State Market News price data for packaged potatoes
All prices are \$/Cwt basis. NA = Not Available. Blanks signify no change.

CURRENT MARKET DEVELOPMENTS

Fresh market prices have been relatively stable, over the past two weeks. However, this week Wisconsin packers decided to bring their Russet potato prices into closer alignment with prices from other shipping areas. The price cuts reduced the weighted average of Wisconsin's Russet potato shipping point prices to \$10.33 per cwt, down \$0.41 per cwt from the previous week.

Fresh potato shipments for the Christmas week totaled 1.54 million cwt. That exceeded year-earlier shipments by 19.2%. Some of the increase may be because Christmas occurred on Friday rather than Thursday, extending this year's run time. Nevertheless, this year's increased movement is an indicator that supplies are more plentiful than they were a year ago.

Holiday demand for potato chips has been strong. Dealers are scrambling to find enough potatoes that will fry. Chip plants are trying to work with potatoes that don't meet grade standards, rather than rejecting them, reflecting a tightening of storage supplies.

FRESH SHIPMENTS: WEEK ENDING DECEMBER 26

State	(Thousand Cwt)				
	2006	2007	2008	2009	Change
Idaho	659	313	381	580	52.4%
San Luis Valley	363	241	236	265	12.1%
Wisconsin	206	144	132	177	33.8%
Columbia Basin *	252	211	95	121	27.6%
Maine	103	90	63	62	-1.0%
Red River Valley	120	95	81	60	-26.2%
Michigan	48	31	47	43	-8.9%
Klamath Basin	60	39	41	41	0.7%
Kern County CA	53	38	25	40	62.1%
Other	197	170	190	149	-21.5%
US Total	2,061	1,371	1,290	1,538	19.2%
By Type †					
Russet	1,562	1,028	967	1,227	26.9%
Red	226	158	169	160	-5.8%
Round White	122	90	66	60	-10.2%
Yellow	100	56	60	52	-12.1%
Long White	51	33	27	36	33.5%
Other ‡	0	6	0	3	- NA -

Source: Preliminary Federal-State Market News data * 2006 data include Skagit Valley
† 2006 and 2007 are NAPMN estimates ‡ Includes miscellaneous and unclassified potatoes