January 2019

FCC Ag Economics
2019 Outlook

Canada's horticulture sector

FCC Ag Economics helps you make sense of the top economic trends likely to affect horticulture operations in 2019:

- Shifts in North American cranberry supply
- Robust demand for maple products and declining syrup inventory
- Improved 2019 blueberry prices on smaller 2018 North American crop and inventories
- Higher borrowing costs and a weaker loonie

Supply-side factors will drive the profitability stories for cranberries, blueberries and maple syrup, the three Canadian horticulture sectors we focus on in 2019. We expect Canadian cranberry profitability to be near break-even in 2019. Policy changes in the U.S. are expected to help support producer prices and improve the sector's outlook from 2018. However, large inventories, unresolved trade tensions, and changes to payment arrangements will limit those price gains for Canadian producers.

Canadian blueberry profitability is also expected to improve in 2019 as declining inventories lead to improved farm-gate prices. Canadian maple syrup profitability is forecasted to remain strong this year as domestic and foreign demand remain robust.

Cranberries

Cranberry prices have struggled for several years with oversupply, which will continue to define the cranberry market in 2019. U.S. production increased 3% in 2018 while preliminary reports suggest Canadian production grew by more than 50% – and perhaps as much as 70%.

Estimates of a previous USDA marketing order show that approximately 15% of the 2017-18 U.S. cranberry crop was diverted to feed, fertilizer and other low-value markets that year. To address ongoing oversupply concerns, the USDA implemented in October 2018 further production controls to be applied to the 2018-19 crop. The marketing order limits U.S. sales of the current year's crop to 75% of historic sale volumes in an effort to match supply more closely with demand. Although the measures can't address the issue of existing large inventories, they may help in limiting future production adding to the problem of oversupply.

Canadian producers will need to monitor cash flow and working capital requirements after some buyers and producers recently negotiated a new payment structure.

Trade tensions will impact 2019 prices

Production controls combined with a murky trade horizon may create volatility in cranberry markets. U.S. cranberries will face tariffs in 2019 from key markets that will likely curtail competitiveness of their exports. Tariffs include:

- A 25% tariff from the EU on cranberry juice concentrate
- Dual tariffs of 15% and 25% from China on dried cranberry imports
- A 20% tariff from Mexico on sweetened dried cranberries
- 10% tariffs from Canada on cranberry juice and cocktails

With increased domestic availability, the U.S. price could drop. Canadian prices overall are expected to be pressured by the extra supply. However, Canada's preferred access to the EU market, granted through the Comprehensive and Economic Trade Agreement (CETA), may open doors as U.S. exports become relatively more expensive. Access to Japan and other Asian nations will be enhanced by the implementation of the CPTPP.

Strong consumer demand will continue to support industry revenues

Some good news: per capita cranberry consumption in Canada, which has had strong growth since 2007, currently remains in line with the five-year average of 5.67 pounds per person. This trend is expected to continue as consumption is moving towards juices and dried cranberries.

Blueberries

High storage levels, low prices and tight profit margins have most recently characterized the blueberry sector. But Canadian profitability should improve this year. Declining inventories are expected to lead to improved farm-gate prices as global demand continues to grow.

Excellent growing conditions throughout the Pacific Northwest are estimated to have produced a record-setting crop in 2018. British Columbia's production is estimated to have increased 15%. That won't be enough to offset declining North American blueberry inventories. Weather and production issues challenged the North American 2018 growing season.

In eastern Canada, spring frost reduced Quebec production by 4.4% (to an estimated 75 million pounds) and Atlantic Canada by 25% (to 96 million pounds). Some U.S. states also experienced issues. As an example, the crop in Michigan, a top-five U.S. producer, is estimated at 66 million pounds, down 33% from the 10 year average and the smallest since 2005. The year's pressured production helped reduce U.S. cold storage in October to the lowest levels in the last six years.

International demand continues to expand

While Canadian blueberry consumption seems to have matured, holding the five-year average of 2.38 pounds per capita in 2017, U.S. consumption continues to break records. Increasing every year since 2006, it reached an estimated 1.79 pounds per capita in 2017. Opportunities are also ramping up in Asia, where demand continues to grow as a result of trade agreements and active promotion.

Maple Syrup

Canadian maple syrup production in 2018 varied across regions, with enough challenges to shrink the year's total tap. Too much snow and a spring that was too cold then too warm in key producing regions negatively influenced the run. The 3% year-over-year growth in the number of U.S. taps wasn't enough to compensate for a reduced yield-per-tap in 2018. Total U.S. maple syrup production is estimated to have declined 3% for the year.

Quebec harvested 118 million pounds of maple syrup from its estimated 47 million taps, well below the 2017 record of 152 million pounds. Even with that reduction, Quebec's reserves will be more than enough to meet domestic and global demand this year. Producer prices for 2019 are expected to be in line with 2018 levels, supporting continued profitability in the maple syrup sector.

Consumers want more

Demand for maple syrup continues to grow, both domestically and abroad. In 2017, Canadian per capita consumption was estimated at 1.43 pounds, up 8.7% over the five-year average. There are some sweet opportunities ahead for Canada's maple syrup industry: existing free trade agreements with each of our top 10 export destinations gives us a large advantage over U.S. exports, our only real competition in global markets.

Canadian horticulture sectors will all face the same financial conditions in 2019. Here's what to expect.

Higher borrowing costs to pressure net income across all sectors

Enjoying its second-longest economic expansion period ever, the U.S. will break the record if that growth extends into summer. Watch for the Federal Reserve to hike interest rates three times in 2019. At the same time, the Bank of Canada expects inflation to hit its 2.0% mid-point target, with an economy near full potential. Financial markets currently expect no more than two overnight rate increases of 25 basis points this year, with the first rate hike coming in the second half of 2019.

Proper evaluation of financial risks will be especially important on loans due for renewal in 2019, as periods of rising interest rates may require greater shares of revenues to cover interest payments.

Weaker loonie will help offset pressures on net farm income

The loonie declined steadily in 2018. We forecast it to average US$0.75 for 2019 – a good news story for the Canadian horticulture industry. The U.S. market heavily influences Canadian cranberries, blueberries, and maple syrup. A lower Canadian dollar relative to the U.S. dollar will support prices for the Canadian horticulture sector.

On the radar

- The next chapter in U.S.-China trade tensions.
- Expectations of a weaker global economy in 2019, driven in part by uncertainty around China's ability to sustain its debt-fuelled economic expansion without triggering inflation. Chinese debt is a growing financial risk for the health of the world economy.
- Elevated probability of an El Niño event disrupting 2019 production with more rainfall in the southern part of the U.S. and drier conditions in the northern part of the U.S. and Canada. Drier conditions would be expected to prevail as well in Asia and Africa.

Curious about the 2019 outlooks for other Canadian sectors? Here's what is available:

- Agribusiness
- Broilers
- Dairy
- Food processing
- Grains, oilseeds and pulses
- Red meat

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