

PolicyPennings by Dr. Daryll E. Ray

## It's futile to push on the corn ethanol barn door—it's a grain reserve that is needed

The impact of the ethanol driven rise in corn prices continues to generate the attention of everyone from members of Congress, to academics, to the end users of these crops, to farmers who are trying to find the mix of crops that will best serve them in the coming year. In the past couple of weeks, two studies that look at the impact of increased demand for ethanol have been released.

The first was produced by the Economic Research Service and the Office of the Chief Economist of the USDA at the request of Senator Saxby Chambliss. The report titled "An Analysis of the Effects of an Expansion in biofuel Demand on U.S. Agriculture" can be found at: [www.usda.gov/oce/newsroom/chamblissethan015-8-07.doc](http://www.usda.gov/oce/newsroom/chamblissethan015-8-07.doc). The report examined two scenarios for increased ethanol demand above the amount included in the February USDA 10-year baseline.

One of the conclusions caught our eye. Not surprisingly, with increased prices, exports of corn and soybeans decline. But, "due to generally higher commodity prices, the value of total U.S. exports increases slightly under both scenarios." What a turn around from attempts over the last 20 years that resulted in lower export revenue as we lowered our price in a futile attempt to increase export quantities.

The study showed a slight decrease in livestock production as producers responded to increased feed costs by reducing animal numbers, resulting in higher farmgate prices. The report notes that "the increase in cash receipts outweighs increases in production expenses in both scenarios." Depending on the scenario, retail meat prices increased 1 to 2 percent above the baseline as the result of lower production levels.

The second study was conducted by the Center for Agricultural and Rural Development (CARD) at Iowa State University. The report titled "Emerging Biofuels: Outlook of Effects on U.S. Grain, Oilseed, and Livestock Markets" can be found at CARD's website: [www.card.iastate.edu](http://www.card.iastate.edu). The CARD study tested higher ethanol production levels than the USDA study and accordingly found larger increases in the retail costs of meats.

The CARD study was funded in part by the National Feed and Grain Association, American Meat Institute, Grocery Manufacturers Association/Food Products Association, National Cattlemen's Beef Association, National Chicken Council, National Pork Producers Council, National Oilseed Processors Association, National Turkey Federation and the North American Millers Association.

In an Agweb.com news story about the release of the report, J. Patrick Boyle, president and chief executive officer of the American Meat Institute (AMI), one of the study sponsors, is quoted as saying: "We recognize the importance of the United States diversifying its energy sources to enhance energy security, but this study clearly shows that we are reaching a tipping point, and that over-reliance on corn-based ethanol to meet stringent government mandates

would further drive up retail food prices, reduce domestic meat and poultry production and erode our vital meat and grain export markets."

The argument of Boyle is that we are spending too many agricultural resources—particularly corn—on energy production. On the other hand, it would appear that the biofuel production train has already left the station with the support of wide sectors of the US public.

Through public policy and private investments, we have already made those decisions. According to the Renewable Fuels Association, 118 bio-refineries are in operation, 79 plants are under construction and 8 existing plants are expanding. Increased ethanol production is going to happen.

And once the livestock industry adjusts production, livestock as well as crop farmers will prosper. It is not that the sharp increase in corn demand for ethanol does not cause challenges for the livestock industry. It does.

The first and very real challenge for livestock producers is to survive the short-run, the time before price-increasing production adjustments can be made but ballooned feed bills must be paid.

A second major challenge for livestock producers is dealing with the effects of a major shortfall in corn production—this year or in immediate years to come. While a higher level of corn prices can be adjusted to by the livestock industry, a significant weather-based plunge in corn yield could cause devastatingly high spikes in corn price.

Ending crop-year corn stock levels are alarmingly low as a percent of corn use and will likely continue that way for several years in the future. When low stock levels are combined with a sudden weather-caused drop in corn yields, a very explosive price mixture results.

Pushing against the barn door of biofuels-driven demand for corn seems futile. For the foreseeable future anyway, livestock and other grain users will no longer pay grain prices that are well below the full cost of production. Instead of lamenting that fact, organizations representing livestock producers could better spend their energy considering policies that will help their members deal with the potentially severe spikes in corn prices that are likely to occur.

Clearly, this country needs a grain reserve. A reserve that would be added to in times of above trend-line yields when prices are lower or more moderate. Then in years of low yields, the reserves could be released to prevent severe price spikes and to provide grain to livestock producers, processors and grain importers.

Not having a reserve potentially invites disaster for domestic grain users and could demolish our credibility as a reliable supplier of grains to the international market.

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