

PolicyPennings by Dr. Daryll E. Ray

## GMA rails against ethanol subsidies but benefited from federal farm subsidies for years

The Grocery Manufacturers Association is continuing its full-court press on the ethanol industry while the ethanol industry continues to fight back. In fact in recent days, the skirmishes between the two seem to be intensifying even though GMA's footing, which is tied to the level of farm commodity prices, is crumbling away.

A few months ago GMA could spin a plausible-sounding story. Corn, wheat and other farm-based "ingredient" prices for cereals and baked goods had surged to unprecedented levels by modern-day standards.

GMA provided consumers—who were well aware of food price increases—a pencil with which to connect the proverbial dots.

Never mind that farm ingredients comprise one of smallest categories of cost in the production of cereals and baked goods and never mind the price increase of a more potent determinant of food preparation cost—energy.

But that was several months ago. Things are much different now. Farm commodity and gasoline prices have dropped by 50 to 60 percent. Yes, but there is a new president a comin'.

A group led by the Grocery Manufacturers Association held a press conference on Tuesday, November 18, 2008, at the National Press Club under the banner Food Before Fuel to urge the incoming Obama administration to end ethanol subsidies.

The next day, Secretary of Agriculture Ed Schafer referred to the group in a talk he gave to the Cellulosic Ethanol Summit in Florida before he headed to Sao Paulo, Brazil to attend the International Conference on Biofuels.

In a report on [www.domesticfuels.com](http://www.domesticfuels.com), Cindy Zimmerman writes about the Secretary's speech: "Nobody is talking about us going backward," Schafer said, then quickly corrected himself, saying "almost nobody," noting that the Grocery Manufacturers Association and some others would like to see the industry move backward.

"Speaking to members of the media after his speech, Schafer said the group that held a press conference yesterday calling for an end to ethanol subsidies 'stood up there with no credibility whatsoever,' when they claimed that it will take 18-24 months for the lower commodity prices to bring food prices back down. 'I just think that they are totally off base,' Schafer said. "They are trying to justify the increased cost and increased profits that they're making at the

expense of another industry and that's just not appropriate."

A DTN article by Chris Clayton and Todd Neeley also described the meeting, writing: "Drawing on the market maturity that is expected to come with an industry's age, opponents of federal support for ethanol [the Food Before Fuel Coalition] used a birthday cake—complete with candles highlighting 30 years of the ethanol blenders credit—to paint the industry as a '30-year-old, underemployed child by the name of ethanol.' Said Duane Pardee, president of the National Taxpayers Union.

"He has been living in our basement, eating our food, always begging for money and claiming that all of his peers have a better life than he does and working in a dead-end job for too long. Well, time has come for him to get out of our house."

Schafer's comments about bringing food prices down now that commodity prices have fallen from their summer peak combined with Pardee's accusation that ethanol is "always begging for money and claiming that all of his peers have a better life than he does," as he looked at the 30-year birthday cake, sent us looking for some numbers.

We have often heard farmers complain that any time crop prices rise, food processing firms use higher commodity prices as the rationale for increasing the price of the food products they process and sell, but when commodity prices fall, food prices don't fall as well.

To check on that we looked at corn prices over the last thirty years and compared them to the Consumer Price Index for cereals and cereal products—like those produced by the American Bakers Association, a member of the Food Before Fuel coalition—over that same period.

The numbers are telling. While the season average corn price paid to farmers has risen by 88 percent over the last 30 years—all of that increase in the last two years—the retail price of cereals and cereal products has increased by 268 percent (figure 1).

As recently as the 2005 crop year corn prices (note: wheat prices closely follow corn prices) were 11 percent **below** the 1978 price while the retail price of cereals and cereal products was 206 percent **above** the level thirty years ago.

The farm value share of the retail price of cereals and cereal products dropped from 14 percent in 1979

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# GMA rails against ethanol subsidies

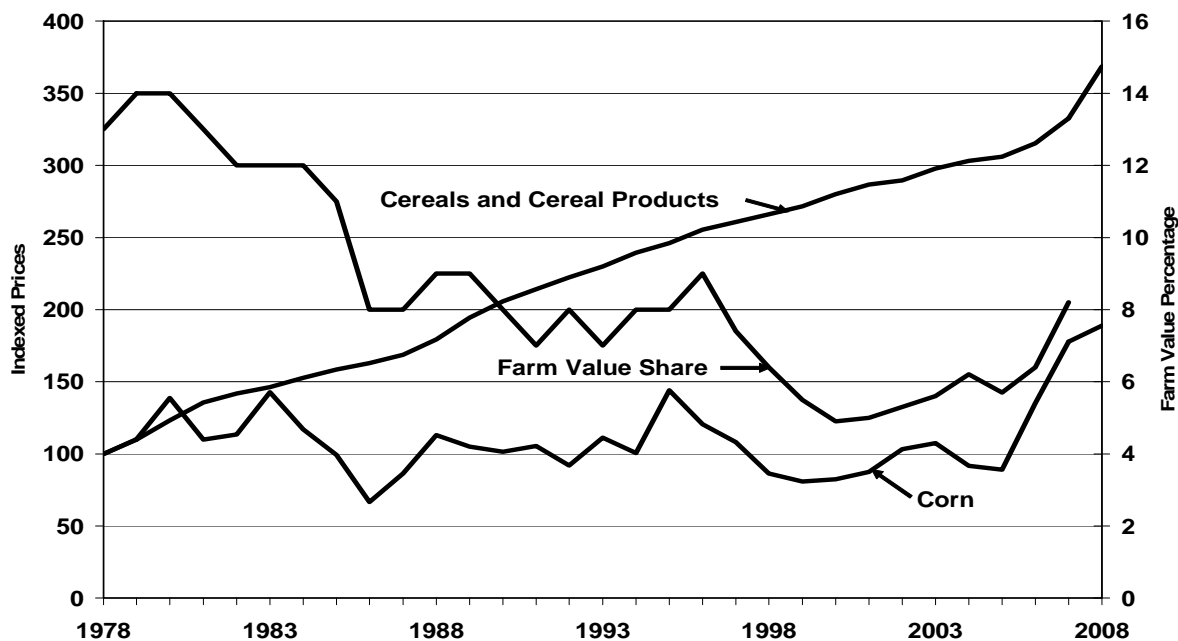


Figure 1. Indexed prices (1978=100) of corn and cereals and cereal products and the farm value share of the retail price of cereals and cereal products, 1978-2008.

Cont. from p. 1

to 6 percent in 2005 before the recent share increase to just over 8 percent projected for the 2008 crop year.

The farm value share fell dramatically from 9 percent in the 1996 crop year to 5 percent in 2002 while the retail price of cereals and cereal products continued to increase, as the processors of these products benefited from the massive farm payments—primarily direct payments, emergency payments, and loan deficiency payments—as farmers sold their commodities at prices below the cost of production.

Our foray into the data suggests a couple of things. First, we suspect that farmers would be thrilled to trade the thirty-year old "ethanol subsidy" for corn price increases that would have maintained the 14 percent farm value share of cereal and baked good prices since 1979.

To accomplish the 14 percent share this year, farm commodity prices would indeed have to be nearly twice their recent levels.

That says nothing about the justification of particular price levels. Its just says that, even with the commodity price rises of late, farm commodity prices would have a long ways to go to catch the price rises that have occurred since 1978 of other components of cereal and baked goods costs.

Secondly, for many years following the passage of the 1996 Farm Act, cereal and baked goods manu-

facturers have bought their farm commodity "ingredients" at well below the cost of production. That is why there is such a large drop in the farm share value between 1996 and 2002.

Yes, food processors are paying market prices now but for years the prices they paid for farm commodities were hugely subsidized by the federal government.

Overall then, the data suggest that food processors should be grateful that farmers have provided their essential ingredients over the years without the historic price increases of their other cost categories.

They should also be thankful for the subsidies that they received (but did not get blamed for) following the 1996 Farm Act which, it would appear from fig. 1, they did not pass along to cereal and baked goods consumers in the form of lower prices.

In fact, especially on subsidy issues, food processors might want to consider the old adage: "People who live in glass houses should not throw stones."

*Daryll E. Ray holds the Blasingame Chair of Excellence in Agricultural Policy, Institute of Agriculture, University of Tennessee, and is the Director of UT's Agricultural Policy Analysis Center (APAC). (865) 974-7407; Fax: (865) 974-7298; dray@utk.edu; <http://www.agpolicy.org>. Daryll Ray's column is written with the research and assistance of Harwood D. Schaffer, Research Associate with APAC.*