

Policy Pennings by Dr. Daryll E. Ray

## Precarious price conditions could last awhile; fill grain reserve when prices slip

The strong demand for corn by the ethanol industry is behind some of the best corn prices farmers have seen in more than a decade. The corn stock levels in the recently released USDA baseline show corn stocks remaining at historic lows for the full 10-year period. In a recent column we suggested that with stock levels that low we are just one bad crop year away from a full blown crisis and a record-high spike in corn prices. To protect against such a scenario we have suggested the implementation of a FOR-like (Farmer Owned Reserve) storage program that could release grain in case of a spike in demand or a drop in production.

In response to our column we received this response from a reader: “I was hoping you might have some insight on the recent discussion of corn storage. A lot of farmers are planning to switch production to corn in the coming year, increasing the need for on-farm storage. Furthermore, ethanol plants—continuing to be built everywhere—need year-round supplies of corn, also encouraging storage. And finally, some folks have talked about the dwindling end of year corn stocks and needing greater storage to prepare for drought or other agricultural disaster.

“With all this interest in storage, is it really plausible with the price already so high? Withholding any more corn from the market is likely to simply drive prices up, which gives farmers an incentive to sell their corn and buyers an incentive to bid even higher.”

Our reader is correct to assert that as long as prices remain high, filling a corn reserve would just send prices even higher, making it almost impossible to establish a reserve at a reasonable cost. The key condition in the logic is “as long as prices remain high.” If prices were to be lower, say in the \$2.30-\$2.40 range, it would be much easier to fill the reserve at a reasonable cost.

As recently as the 2002 crop year, the year-ending stocks-to-use ratio was 11.4 percent and the price of corn was \$2.32. The following year saw a year-ending stocks-to-use ratio of 9.4 percent and \$2.42 season average corn price.

In the present setting, if the 2007 year-ending corn stocks-to-use ratio were to be in the range of 11.4 percent instead of the projected ratio

of 5.3 percent, it would not be much of a stretch to imagine local elevator corn prices in the \$2.30-\$2.40 range. In corn surplus areas, corn prices could be even lower than that.

The question then becomes, “What would it take to get 11.4 percent stock levels in the 2007 crop year?” The short answer is about 750 million bushels on top of USDA’s projected 660 million bushels—a total year-ending stock level of 1.41 billion bushels.

If corn planted acres were to come in at 90 million acres instead of the projected 86 million acres, and if the crop yield were to remain on trend, the extra 4 million acres would add 612 million bushels to production.

But US farmers are not the only ones to take note of the higher corn prices. We recently read that Brazilian farmers have increased their “second harvest” corn crop planted acres and are expecting to produce an extra 3.5 million tonnes, all of which will go to export markets. That 3.5 million tonnes could displace 140 million bushels of projected US corn exports. Likewise, industry analysts expect that Brazilian farmers will plant additional corn acres in their primary season which will be harvested early next spring, easily bringing in another 200 million bushels.

With increased US production of 612 million bushels and decreased US exports of 340 million bushels, the 2007 year-ending corn stocks could reach or exceed the 1.4 billion bushel level that would result in \$2.30-\$2.40 corn prices.

In answer to our reader, if corn prices were to slip below \$2.50 in the coming year, it would be possible to begin filling a corn reserve without driving corn prices through the roof. Putting grain in the reserve under such conditions would have added benefit of heading-off paying out billions of dollars of government payments.

*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](mailto: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.*

Originally published in *MidAmerica Farmer Grower*, Vol. 24, No. 13, March 30, 2007  
Reproduction Permission Granted with 1) full attribution to Daryll E. Ray and the Agricultural Policy Analysis Center, University of Tennessee, Knoxville, TN; 2) Copy of reproduction sent to Information Specialist, Agricultural Policy Analysis Center, 309 Morgan Hall, Knoxville, TN 37996-4519