PolicyPennings by Dr. Daryll E. Ray

Profitability in crop and livestock sectors

In recent weeks we have seen the impact of corn prices that are nearly double what they were last August. Farmers from South to North in the US are switching some of their crop acres out of other crops and into corn in hopes of cashing in on the results of the projected boom in corn-based ethanol production.

At the same time that crop farmers are looking forward to a year in which they earn their livelihood from the marketplace instead of depending upon government payments, some analysts are concerned about the long-term outlook for the poultry and livestock sector and the negative impact high prices and tight availability of grains and seeds will have on US exports. There is no question that a great many livestock producers are now experiencing reduced incomes and in some cases severe financial hardships because of the suddenness and extent of the recent run-up in corn prices.

As pressing as that short-term concern is, some analysts are focused more on asking if the current high prices will result in reduced meat production and decreased exports. To us the answers to these longer-term questions are yes and yes. But those are different questions than "will the poultry and livestock sector be profitable in the long-run?" or "will crop export revenue decline?"

To start with we need to remember that there is a difference between reduced production of poultry, pork, and beef and reduced profits for these operators. These two concepts are not the same.

In a recent Wilmington Delaware News Journal article by Luladey B Tadesse, Julie De Young, spokesperson for Perdue is quoted as saying, "Like the rest of the industry, we did cut back…about 2 or 3 percent…We produce to customer demand." The industry was facing overproduction before rapid rise in the price of corn, a major portion of the poultry diet. Higher corn prices have forced the timing and extent of the readjustment.

Unlike aggregate crop agriculture, reduction in output readily occurs in animal agriculture, as a result, given a period of transition, they can adjust to $2.00 or $4.00 corn and still be profitable. After a period of adjustment livestock producers will reduce production and the value of their product will rise.

The same News journal article quotes Sam Slabaugh Sr., "In the long term, the higher grain prices might benefit all farmers."

Looking at the export issue we note that if we export 2 billion bushels of $2.00 corn, the value of those sales is $4 billion. At a cost of $2.72 a bushel to produce that corn, US farmers end up losing about $1.4 billion with the US government picking up the much of the export tab.

On the other hand, if supply pressures and $4.00 corn were to reduce US exports to 1.5 billion bushels, the export income would be $6 billion with little cost to the US treasury aside from the direct-decoupled payments. Crop farmers are better off and so is the US treasury.

Higher prices also benefit farmers around the world who see better prices than they have seen in a decade. They can produce without worrying about low-priced US exports driving local prices to levels at or below their cost of production.

While we have, in recent columns, expressed a concern that extremely high prices might trigger an overreaction in the market that would drive corn back to the $2.00 level, we applaud commodity policies that enable US crop farmers to earn their income from the marketplace instead of the US treasury.

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