

PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

Corn yields do not have to drop to 1988 levels to cause greater than 1988 market havoc

Once upon a time, a warm spring and good subsoil moisture made farmers very happy as they planted their corn crop. For the week ending May 6, 2012, 71 percent of the corn acres had been planted, compared to a 5-year average of 47 percent.

In addition, the users of corn were so optimistic that they would have access to a bountiful supply of golden grain that, with a crop progress report like that, the September futures price dropped to a close of \$5.11 per bushel, down from \$6.05 just two months earlier. Even as late as June 15, corn closed at \$5.06.

That once-upon-a-time spring was a couple of short months ago. What a difference a couple of months can make when the weather turns beastly hot in the buckle of the corn belt.

When the July 8th crop report came out, the numbers for two of the three “I’s” that form the buckle of the corn belt were downright ugly. In Indiana, 61 percent of the corn crop was in very poor to poor condition while in neighboring Illinois things were little better with 48 percent of the crop in very poor to poor condition. For the 18 states that are used in the USDA Crop Progress Report, 30 percent of the corn crop was rated as very poor to poor compared to 9 percent of the crop a year earlier.

Many are voicing fears that this year’s short corn crop may equal that of 1988. A yield drop of the magnitude experienced in 1988 seems unlikely since it would mean a national yield in the 105 to 110 bushel per acre range. But—because of major differences between now and 1988—it won’t take that kind of yield drop to cause major havoc in the corn market.

In 1988, the US had total corn commercial and government carryover stocks in the 4 to 5 billion bushel range out of a total annual utilization of 7.3 billion bushels; 1.4 billion bushels were commercial stocks and the rest were stocks held in reserve. This year the total carryover stocks are estimated to be some 900 million bushels compared to a total utilization of 12.7 billion bushels. There are no stocks in reserve.

Livestock producers, many who are just beginning to recover from the 2008 price spike, will again be hit hard as further increases in feed prices push net returns deeply into the red. Because grain prices account for such a small portion of most cereal products, most of the impact on US consumers will be felt in the meat section—lower prices early on as hogs and cattle go to market early and higher prices later, as the result of

reduced supply.

Internationally, the impact is more immediate. Higher US corn prices are quickly transmitted around the world and have a serious impact on consumers in developing countries where corn/grain is a major component of the diets of the poor. We all remember what happened in 2008 and the impact extremely high grain prices had on the number of hungry people in the world.

Ethanol production was expected to account for 5 billion bushels of US corn production. Higher prices will inevitably lead to reduced ethanol production. If the prices go high enough some low-margin ethanol plants will be taken offline.

Just as higher prices are felt by consumers around the world, they are also felt by corn producers around the world. With higher prices, we would see an increased number of acres put into production worldwide, perhaps about the time US yields recover.

We have seen numbers that would suggest that crop revenue insurance payments could go through the roof. At this point, we would hesitate to offer an estimate on our own, but Gary Schnitkey at the University of Illinois (http://www.farmdocdaily.illinois.edu/2012/07/crop_insurance_in_2012.html) estimates that a year like 1988—105 bushels per acre—with a harvest price of \$7.40 could result in a \$318 per acre insurance payment.

As of July 9, 2012, 553,000 Federal Crop Insurance policies had been issued to farmers. At this time in 2009, the number was nearly double at 1.17 million policies. Neither the high crop prices nor the high insurance payments are going to benefit farmers who don’t have crop revenue insurance but experience a serious decline in yield.

At this point in time, we are just holding our breath as we await timely rains, if it is not already too late for that.

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