

## PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

### Production destruction leads to both short-term and long-term demand destruction

This week we read an interesting perspective on the drought from someone actively engaged in raising corn. Analyst/corn farmer Jerry Gulke talked about the impact of the drought that has now spread over more than half the country on this year's corn crop. He characterized the situation faced by farmers as production destruction.

No one can disagree with that description. Farmers in some areas of the country appear to have dodged the bullet this time, while many others have seen it firsthand.

A July 29, 2012 article written by Chris Lusvardi of the Herald & Review (Decatur, IL) begins, "[Acting Director of the Illinois Department of Agriculture] Bob Flider stood last week on the edge of a cornfield near Effingham holding an ear of corn with no kernels in his hand. Farmer Doug McCain told Flider that the corn wouldn't even be worth harvesting, as it likely couldn't make it through a combine. The field appeared to have gotten some timely rain, so McCain said the corn there wasn't a total wreck, and Flider wasn't even seeing the worst in the area.

In an opinion piece in the New York Times (July 28, 2012), Frank Brill relates a discussion he recently had with a farmer in Southern Indiana, "He tells me he retired some years ago, but says he's been following what's going on with the heat, the lack of rain. Says the feed corn crops might be growing but they've not pollinated, are not mature, the ears won't reach their peak size."

Given the deterioration in the Crop Progress reports that we have seen in recent weeks, the corn crop that the USDA projected to yield 146 bushels/acre in the July WASDE (World Agricultural Supply and Demand Estimates) report, down 20 bushels/acre from a month earlier, seems destined for another fall come the August report.

Gulke's discussion of production destruction is not what surprised us, nor were we surprised to hear him talk about demand destruction. It was his take on demand destruction that caught us off guard.

Sara Shafer, AgWeb.com Business and Crops Online Editor quotes Gulke as saying "'Not only is there production destruction this year, but also demand destruction. We're going to import a lot more of corn into this country. I think we'll see higher levels of corn coming into this country than in my entire lifetime, which is good because it will offset our US losses.'

"Gulke believes the export market in the U.S. is going to dry up and US end users will start shopping

for corn in Argentina and other countries. 'That's good news for us because these end users are going to keep production viable and aren't going to liquidate herds unless we can help it.'"

Well, good news may not be the unanimous reaction. In the midst of a drought, US corn farmers may not welcome corn coming in from Brazil and Argentina. Smithfield and Pilgrim's Pride may welcome cheaper South American corn, but we do not expect to hear any cheers coming from US corn farmers.

Though they certainly need relief from this drought and will get hit hard by high corn prices, it seems unlikely that US independent cattle producers will substantially benefit from imported corn beyond some reduction in corn prices—they don't have the same economic resources as Smithfield and Pilgrim's Pride.

Gulke's logic is that these corn imports will allow meat producers to maintain their herds until US corn comes back on line in September 2013, at which time Brazil and Argentina will smile and walk away from the US market.

Pilgrim's Pride has told its investors that they are "close to a deal" to import corn from Brazil. The problem is that the 49-day wonders that they produce will be long gone many times over before the 2013 corn crop flows into the bins of US farmers. Besides that for chickens, we are talking about eggs and a 21-day incubation period. Even if production were to fall, it can be ramped back up fairly quickly.

With hogs—115 days gestation for a litter of 10 or more—things are a little more dicey, but by keeping gilts and sending older sows off to slaughter, pork production can be ramped back up fairly quickly.

The problem gets a lot dicier when it comes to cattle—280 days for what is usually one calf. So when a cow goes to slaughter early, it takes some time for cattle to get back to full production. And it is not Smithfield that makes the decision about sending those cows to slaughter. The decision is made by a cow-calf operator who relies mostly on pasturage. Additional cows are going to be sent to slaughter, with or without corn imports.

The extent to which short-term imports of corn into the US helps to maintain current-year livestock production is one thing. But it is the long-term destruction of US corn demand that is most worrisome to us, especially export demand.

The current high prices have one certain result—more corn acres. To the extent that farmers in Brazil,

**Cont. on p. 2**

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**Cont. from p. 1**

Argentina, and everywhere else, see these high prices they are going to increase their production.

In the longer-term, more worldwide production brings lower prices and, from the US perspective, the destruction of export demand that otherwise would have been available to US grain producers.

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