Bottlenecks and Oil Price Spikes: Impact on U.S. Ethanol and Agriculture

Chad Hart
Center for Agricultural and Rural Development
Iowa State University
chart@iastate.edu
515-294-9911

2007 Iowa Poultry Association Fall Festival
West Des Moines, Iowa
September 13, 2007
Outline

Based on an update of our earlier study “Emerging Biofuels: Outlook of Effects on U.S. Grain, Oilseed, and Livestock Markets”

http://www.card.iastate.edu/publications/synopsis.aspx?id=1050

Updated with available 2006 and 2007 data

The objective is to estimate:
- how large the biofuels sector in the U.S. could become
- the impact of the biofuels sector on crops markets, trade, and on livestock markets
- the response of world agricultural markets
Model Interactions

Trade, Prices, and Physical Flows

- Macroeconomic Variables
- Policy Parameters

International Dairy → International Livestock → International Grains

U.S. Dairy → U.S. Livestock

Ethanol

International Oilseeds → International Sugar → International Rice

U.S. Crops
Current ethanol capacity: 128 plants, 6.78 billion gallons/year

Total capacity under construction and expansion: 6.65 billion gallons/year

77 new ethanol plants and 8 expansion projects underway

2.2 billion bushels of corn were used in producing fuel ethanol in 2006/2007 marketing year.

3.2-3.5 billion bushels of corn are expected to be used in producing fuel ethanol for 2007/2008 marketing year.
Three Cases

- Baseline
  - Current policies, “normal” weather

- Higher oil prices throughout projection period
  - Adding $10/barrel to the crude oil price

- Drought in the 2012 crop year
  - Placing a 1988-style drought in the middle of the projection period
Projected U.S. Ethanol Production

billion gallons

Margins at Various Corn and Gasoline Prices

Wholesale Price of Gasoline

- Corn and Gasoline Prices
  -1.50
  -1.00
  -0.50
  0.00
  0.50
  1.00
  1.50

- Dollars per Bushel
  0.00 1.00 2.00 3.00 4.00 5.00 6.00 7.00

- $ per gallon
  1.00
  1.50
  2.00
  2.50
Projected U.S. Corn Planted Area

million acres

Projected U.S. Corn Production and Prices

- Production (billion bushels)
- Price ($ per bushel)

Key years:
- 2006 to 2016

Legend:
- Orange bars: Production
- Blue line: Price
Projected Utilization of U.S. Corn

million bushels

- Feed
- Fuel
- HFCS
- Seed
- Food, Other
- Exports
Projected U.S. Soybean Meal Production and Prices
Projected U.S. Meat Production

billion pounds


Beef  Pork  Broiler

Projected U.S. Meat Production

billion pounds


Beef  Pork  Broiler
Impact of Higher Crude Oil Price

- Increased crude oil price by $10/barrel over the projection
- Margins on ethanol plants increase
- New incentive to invest in added capacity for ethanol production
- Eventually, a new equilibrium reached where there is no incentive to invest in or exit the ethanol industry
- Will demand for ethanol be enough?
  - E-10 market will saturate around 15 billion gallons
  - Drop in ethanol price will eventually encourage increase in demand for the flex-fuel cars
Projected U.S. Corn Planted Area

- Million acres
- Scenario
- Baseline

- Years: 2006 to 2016
- Values range from 70 to 110 million acres
Projected U.S. Corn Production and Prices
Projected U.S. Distillers Grains Production and Prices
Usage of Distillers Grains by Species

Beef: 66%
Pork: 13%
Poultry: 12%
Dairy: 9%
Projected U.S. Soybean Meal Production and Prices

Production

Price
Impact on Rest of the World

- World grain and oilseed prices increase
- Result in higher feed and food prices
- Higher livestock production cost
- Countries in South America and Asia fill the crop gap
Impact of Short Crop Scenario

- Drought in 2012 similar to 1988
  - Regional yields of corn, soybeans and wheat changed from trend levels
  - Yields were off by 25% for corn, 18% for soybeans, and 11% for wheat in 1988
- Ethanol mandate for 2012 assumed to be 14.7 billion gallons
Historical Corn Production Deviations

-35%
-30%
-25%
-20%
-15%
-10%
-5%
0%
5%
10%
15%
20%
Corn, Soybean and Ethanol Markets

- Corn price increases by 44% above baseline levels
- Soybean price rises by 22%
- Corn exports and stock levels decline by more than 60%
- Corn exports from South America, China, etc. fill part of the gap from decline in U.S. corn exports
- Corn feed use declines by 16% (switch to other feeds)
- Ethanol trade increases moderately
Livestock Market

- Higher feed costs affect the livestock sector but to a lesser extent as shock is perceived as temporary
- Production declines
  - Broiler production declines the most (over 2.5%)
  - Milk production declines the least (0.5%)