2008 Feed Market Situation and Outlook
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Summary

Prices for all major U.S. grain and oilseeds will average 50 to 100 percent higher in the 2007/2008 crop year compared to just two years ago. This means that prices for energy and protein feeds, as well as forage crops, will generally be higher than producers have been accustomed to in recent years. Moreover, relative changes in some feed markets means that price relationships between alternative feeds may have changed from historical patterns. Additionally, differing regional impacts have also changed price relationships regionally with significant short run and potential long run regional impacts.

Higher cost for feeds mean that livestock producers must be alert to dynamic feed market conditions and continually evaluate feeding and production alternatives. While all feed prices are expected to be higher, there will be relative feed bargains for producers in various regions and at various times. Producers must evaluate and consider the best use of a wide variety of feed and by-product feed alternatives that will be increasingly available.

U.S. agriculture is operating under a new set of rules. Driven primarily by biofuel demand, competition for agricultural resources is profoundly impacting all agricultural markets, either directly or indirectly. Although it is not yet clear what the permanent impacts will be, agricultural markets will, at a minimum, be in transition for several years.

Corn Markets are the Key

2008 will be a continuation of a massive series of impacts that will reverberate through agricultural markets for several years. 2007 was just the beginning! The sharp rise in corn prices in late 2006 prompted a 20 percent jump in corn plantings in 2007. That acreage increase, combined with good yields, resulted in a record corn crop of about 13.1 billion bushels. Ethanol demand for corn in 2007/2008 crop year, at 3.2 billion bushels, is roughly 50 percent higher than the previous crop year and almost twice the amount of corn used for ethanol just two years ago. This rapidly growing corn demand for industrial use, combined with slight increases in corn used for feed and exports, results in a projected total corn use for the 2007/2008 crop year of 12.69 billion bushels. Because of excellent production in 2007, corn inventories at the end of the crop year (August 31, 2008) are projected at 1.4 billion bushels. For many years, this level of ending stocks would be sufficient to allow corn prices to drop significantly but that is not the case this year. Currently, corn price is over $5.00/bu. in Oklahoma and corn futures for the rest of the crop year suggest that corn prices will be between $5.00 and 6.00/bu. at least until harvest.

There seems to be no relief in sight. New-crop corn futures starting in September are currently approaching $6.00/bu. suggesting Southern Plains corn prices over $5.00/bu. into 2009. The demand driving these price levels appears likely to increase rather than decrease in the coming years. Current ethanol production capacity is about 7.4 billion gallons per year using about 2.64 billion bushels of corn annually. However, if all of the new plants currently under construction are completed in the next 18-24 months, ethanol capacity will expand to roughly 13.4 billion gallons and would use about 4.7 billion bushels of corn per year. A market for this increased ethanol production is ensured by the recently passed Energy Bill that raises renewable fuel standards to 9 billion gallons in 2009 and 15 billion gallons of corn-based ethanol by 2015. The corn market takes no comfort in the 2008 projected ending stocks of 1.4 billion bushels because the current price
levels only hold if the U.S. is able to produce a string of 12-13 billion bushel corn crops in the coming years. In order to do that the corn market must maintain planted acres and have growing conditions that produce record or near-record yields. There are a variety of market and production factors that suggest this will not be an easy feat.

Other Crop Markets will Challenge Corn in 2008

Both current and new-crop corn prices only partly reflect underlying demand and supply conditions; the current ending stock levels suggest that there are adequate corn supplies at this time. The real question is how much corn will be planted and harvested in 2008? Much of the 15 million acre increase in corn acreage in 2007 was facilitated by a nearly 12 million acre decrease in soybeans. Such a decrease in soybean production was possible with minimal market impacts because the current crop year started with record 2006 soybean ending stocks, the result of three large soybean crops in 2004-2006.

2008 soybean ending stocks are projected to be only one-third of 2007 levels. Thus, it is imperative for more acres to return to soybeans in 2008. The market is attempting to ensure that with new-crop soybean futures prices currently trading over $13.00/bu. In other words, corn, soybeans and other crops are in a bidding war for U.S. cropland in 2008. Additionally, there are several production reasons that suggest corn will not be able to maintain 2007 planted acreage. Many of the increased corn acres in 2007 were acres that followed corn in 2006 rather than the more typical 1:1 corn to soybean crop rotation. Planting corn in a 2:1 corn to soybean rotation increases fertilizer needs and increase the odds for disease and pest problems.

Energy versus Protein Feeds

Ethanol production removes the starch from corn and the resulting co-products have considerable feed value, especially for ruminants. The net effect of ethanol production is to reduce the initial volume by two-thirds and return a product that is approximately three times more concentrated with protein. Pound for pound (dry basis), distillers grain has nearly as much energy (from the oil and fiber) as corn and all the protein of the original volume of corn in one-third of the pounds. The result is less total pounds of feed and relatively more protein compared to energy. This does not mean that protein is cheap but it does mean that corn is being driven by the energy value and the result is a relative increase in protein supplies.

Food Gains and Feed Grains

Early in 2007 it appeared that corn prices would likely set a floor for wheat price in the U.S., which happens occasionally when food grain prices drop to feed grain price levels. 2007 was unusual, however, in that it was the sharp rise in feed grain prices up to food grain price levels that appeared to lead to the potential for wheat to be priced and used to a greater degree as a feed grain. However, the poor U.S. wheat crop, combined with strong global demand and tight world stocks, caused wheat prices to rise to record levels for reasons largely unrelated to ethanol production.

Record average wheat prices are expected in 2008 and there appears to be little chance that food grain prices will drop to feed grain price levels in the coming year. Nevertheless, record high wheat prices further enhance, at least indirectly, the bidding war for crop acreage in 2008. Although wheat and corn are grown in different regions and do not, for the most part, compete directly for cropland, they do compete indirectly in the Great Plains where wheat and grain sorghum are alternatives and in the Delta and parts of the Southeast where spring wheat and soybeans compete. Finally, it should be noted that the current high wheat price is largely a function of global supply conditions and will likely decrease with better crops in the U.S. and in other major wheat production countries. In a year or two, we could easily see food grain prices drop again and be influenced directly by the sharply higher feed grain prices, which are not likely to go away for the foreseeable future.
Grain versus Forage

Forage values are generally higher in the U.S. for a variety of reasons related to both demand and supply. Regional droughts have affected forage and cattle production significantly since 2002. The extreme drought conditions in the Southern Plains in 2005 and 2006 resulted in the U.S. having record low hay supplies on May 1, 2006. Hay production recovered somewhat in 2007 and December 1 hay stocks in the U.S. improved compared to the previous year. However, available supplies of hay, especially good quality alfalfa hay, will be tight in 2008. In 2007, the ratio of corn harvested to planted acres was higher than usual, in large part because fewer corn acres were harvested as silage, a situation likely to be repeated in 2008. There is no doubt that some annual pasture and hay acres will be used for other crop production in 2008 and beyond. All of these things indicate that forage supplies will be relatively tight in the coming year.

Implications

Livestock producers must be aware of changing market conditions for both feed and cattle and be prepared to consider a wider range of production alternatives. It is not business as usual for the foreseeable future and while there are significant challenges and potential threats, there are also new opportunities in the current situation. It is imperative to remain vigilant and to be prepared to adjust to a very dynamic feed market environment.
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