

## MARKETS

# Will Ethanol Finally Bring Gold to Corn Farmers?

By GARY WULF

CENTRAL CITY, Neb.—Depressed corn prices might have U.S. farmers feeling as if they're being left out of the "ethanol gold rush," but agriculture analysts said demand soon might outstrip supply, giving growers an upper hand.

Dozens of multimillion-dollar stills—loftily known as "biorefineries" in ethanol-industry parlance—opened for business during the past year, putting 101 plants in operation nationwide. An additional 37 are under construction, and seven more are in the process of major expansions.

"There is a 'gold rush' occurring now in building ethanol plants," said Purdue University agricultural economist Chris Hurt. "With [Chicago Board of Trade] ethanol futures prices averaging about \$2.20 [a gallon] for the remainder of 2006, net margins above all

costs may be around \$3 per bushel. This means payback could be as short as 15 months, on a preincome tax basis."

The construction boom will dramatically increase domestic production capacity of the alternative fuel, now estimated at 4.8 billion gallons annually. Plants have popped up all over the U.S., largely predicated on record energy prices that have caused ethanol's value to appreciate by 50% in the past 12 months.

The fuel-alcohol industry's consumption of corn is expected to reach 2.15 billion bushels during the next year. That's compared with 1.6 billion this season and 1.32 billion in 2004-05.

Why then, farmers must be asking, is a bushel of corn worth less than it was two years ago, with physical, or cash, prices a dollar a bushel lower than they were in April 2004?

U.S. grain merchandisers were bidding less than \$2.08 for a bushel of corn as of the close of trade Thursday, meaning the cash basis stands near record-low levels, averaging about 38 cents less than spot futures nationwide. Basis is the adjustment applied to futures prices to reflect real-world supply and demand and the availability of local transportation and storage.

"If you simply looked at basis levels and actual cash prices, you would never know we were in a bull market on the futures, or that ethanol even existed," said analyst John Roach.

Dwight Sanders, assistant professor of agricultural economics at Southern Illinois University, said ethanol is to blame for the divergence in prices, pointing out that ethanol plants are drawing corn away from delivery points designated by the CBOT, resulting in greater basis volatility.

Volatility in cash corn prices also may be heightened by the structure of the spot ethanol market itself, which

saw thinly traded spot contracts spike to \$4.23 a gallon, only to plunge 40% during the past five weeks.

The Renewable Fuels Association estimates that only 5% to 15% of all ethanol produced is traded on the open market, with the remainder sold directly by individual plants under long-term contracts of six to 12 months negotiated between ethanol plant and fuel refiners or gasoline blenders.

Feasibility studies conducted by companies considering construction of ethanol plants routinely predict that an average-size facility will improve local cash corn prices in corn-belt states—such as Iowa and Nebraska—by 12 cents to 15 cents a bushel. But a new study conducted by Iowa State University economist David Swenson challenges those figures, placing the net impact at less than half that amount.

"There are claims to economic outcomes associated with ethanol production that seasoned analysts cannot swallow," he said in a report titled, "Input-Outrageous: The Economic Impacts of Modern Biofuels Production."

Mr. Swenson says that claims that a new ethanol plant will produce sharply higher cash prices for local farmers aren't justifiable, and that, in practice, premiums have totaled only about five cents a bushel, at least so far.

"The market is telling us that nobody wants corn," explains Scott Stewart with the Top Farmer market advisory service. "U.S. farmers have managed to produce more corn than what was needed. Thus, a buildup of carry-out has existed in most years, which has kept corn in a prolonged sideways price pattern."

After two consecutive record harvests, U.S. grain bins are expected to contain more than 2.1 billion bushels of leftover corn this fall—the largest surplus in 10 years—even before growers bring in yet-another substantial crop.

It is little wonder that farmers who still have bins full of corn out behind the barn are feeling nauseous, but to Mr. Roach the remedy is simple: "build two more bins and call me in the morning."

"After harvest, I expect the corn market to experience rapid basis improvement and higher futures prices to supply record demand," he said. "We have been saying consistently to store as much corn as you can, because that will be your greatest asset for the next couple of years. We believe that the cash prices we see in the next couple of months may be our lowest for a very long time to come."

U.S. Department of Agriculture economists characterize the cash corn market as on the cusp of a potential sea change, predicting a rise of almost 50 cents a bushel in season-average farm gate prices during the coming crop year, averaging \$2.45 a bushel, the highest return in a decade.

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