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As We Sow, So Shall We Reap

Last week, the government reported that retail food prices were up by 0.9 percent in April, the highest monthly increase since 1990. Those prices were 5.9 percent higher than twelve months earlier.

Two years ago, corn, the leading feed grain, traded for between around $2.20 and $2.40 a bushel; today, it is over $6. The U.S. Department of Agriculture projects that the U.S. acreage devoted to corn will decline in 2008 by about 8 percent.

High food prices are not just a concern for the American consumer and our government officials trying to cope with potential inflation. In many other countries, large populations have simply been priced out of the market for eating. Rioting in Somalia, starvation in Haiti, skyrocketing prices in Afghanistan, rationing in Pakistan and export controls in many producing countries are some of the stories we read daily about the effects of the price spiral. The rich countries are being asked to contribute billions to relieve the price induced shortages.

The causes are numerous – below average and failed crops in Europe and Australia, developed countries' efforts to reduce production subsidies, economic growth in developing countries, and the competing demand for grain-based biofuel production. The latter cause is especially potent in the U.S. – about 20 percent of the U.S. corn crop went into ethanol production last year, and the figure is expected to rise to 30 percent for the next crop year. We now have 147 ethanol plants making 8.5 billion gallons, and there are plans to increase production by another 5.1 billion gallons.

Whatever the effects of these events on U.S. and foreign consumers, they have been splendid for the American farmer. Net farm income in 2007 was $88.7 billion, up about 50 percent from the prior year and a little more than 50 percent above the 10 year average. USDA estimates that net income will grow by another 4.1 percent in 2008. (Others are doing well, too. The common stock of farm implement manufacturer Deere Co. was at $40 two years ago; it now trades at over $80.)

This then was the setting for the Congress' consideration of the 2008 farm bill: grain prices through the roof, strong demand from new consumers worldwide, a huge new market in biofuels and all-time record farm income.

And what was the response by the Congress? More subsidies to the farmers.

This legislation, which was passed by large, veto-proof majorities in both houses, will deliver –

- $40 billion in subsidies for growers of crops, like corn and wheat, whose prices are at record levels;

- coverage of new crops, like fruits and vegetables, in the subsidy grants;

- $3.4 billion for a new disaster relief fund that will permit many farmers to avoid the weather related risks of planting crops in drought prone areas;

- encouragement for the government to buy excess sugar production for sale to ethanol producers;

- broadened supports for dairy farmers; and,

- billions for farmers who are happy not to farm.

The legislation does take a modest swing at some of the past excesses. It will reduce the tax credit for ethanol production from 51 to 45 cents per gallon. It would also limit payments to farmers earning more than $750,000 in farm income ($1.5 million for couples) and deny any subsidies to individuals making more than $500,000 in non-farm income ($1 million for couples).

Per usual, the bill contains some earmarks, including tax breaks for racehorse owners in Kentucky (Republican leader McConnell's home state) and $170 million in aid to the west coast salmon industry.

President Bush has promised a veto, but, as noted, the support in both houses is great enough to override with ease. One wonders whether any series of events can change our national approach to growing and producing food.

Here is the news on some cost factors for steel production:

- Scrap and Pig Iron. The way that prices have shot up, you would think that scrap and pig iron were things to eat. Number 1 dealer bundles and #1 busheling (Chicago) jumped $110 and $120 per mt respectively last month, to $710 and $720. These prices are *seven times* what they were in 2002 and almost twice the levels of a year ago. The spot price for Brazilian pig iron (cif New Orleans) also skied to $690 per mt, up $100.

- Natural Gas. The Nymex contract price continued to climb, reaching $11.08 per mcf, up $1.17. There has been a relentless upward trend since last September, with prices almost doubling in that period.

- Ocean Freight. Joining the price trends on other items, the Baltic Capesize Index climbed to 10164, up over 3000 since last month.

- Exchange Rates. After reaching record highs, the euro has eased a bit at this writing; it is now at $1.56, down 3 cents from last month. The pound also declined, by 4 cents to $1.95. The Canadian dollar was unchanged at 99 cents.

We appreciate receiving your thoughts and comments; please keep them up. As usual, we are posting this letter on our web site, www.coreysteel.com and on the international site, www.steelonthenet.com.