

**Statement for the Record from
David Cleavinger, President, National Association of Wheat Growers
and
Ron Suppes, Chairman, U.S. Wheat Associates
to the
House Small Business Committee
Hearing to Examine “Food Prices and Small Businesses”
May 16, 2008**

Madam Chairwoman and Members of the Committee, we appreciate the opportunity to submit these comments on the causes and effects of rising commodity and food prices. We are sensitive to the concerns from bakers and consumers that rising commodity prices have affected the prices they pay for raw goods and food in the grocery store, but we also think it's important to consider the issue from the perspective of the farmer who produces the commodity. This is especially salient for your Committee, since the vast majority of commodity producers are themselves part of small businesses.

What Has Caused Wheat Price Increases?

The historically high wheat prices we have seen recently are the result of a combination of factors including:

- Strong competition for acres among crops in an environment where wheat is losing competitiveness.
- Production problems including poor weather conditions in many wheat growing regions worldwide including the U.S., Australia and parts of Europe.
- Global consumption exceeding production seven of the last eight years.
- Increased world demand for food, especially high quality food including wheat products, from both larger world populations and a rising middle class in developing countries.
- Domestic stocks at 60-year lows and world stocks at 30-year lows.
- A weak dollar promoting increased exports from the U.S., which is the world's largest wheat exporter and sells about half of its wheat crop overseas in a typical year.
- Export restrictions by some countries, which have curtailed the world's access to wheat.

Wheat competitiveness, highlighted in the first bullet point above, has been a particular concern for the wheat industry for a number of years. The decline in wheat acres in the United States is not a recent phenomenon spurred on by biofuels, as many would suggest. On the contrary, wheat acres have been declining steadily for decades; plantings are about 30 percent lower than in the 1980s.

Perhaps the largest single reason for this change is that the availability of technology, including biotechnology, in competing crops like corn and oilseeds has raised the

opportunity cost of growing wheat. From the perspective of a grower, this means that the wheat market has to pay more to encourage plantings. The wheat industry agrees with some in the milling and baking industries who have said that the entire wheat chain is paying a huge cost for our failure to adopt new technology, like biotech traits.

Starting in 2006, NAWG and the North American Millers' Association have led a series of "Wheat Summit" discussions with stakeholders throughout the wheat chain, including producers, millers and bakers, to discuss and find solutions to the competitiveness problem facing domestic wheat production. NAWG and U.S. Wheat Associates are actively working to create a market environment in which biotech traits in wheat are beneficial to producers, users and consumers.

What Impact Does This Have on Consumers and Food-Reliant Small Businesses?

Wheat, like any commodity, makes up a very small portion of a finished food product; the Department of Agriculture says that only 20 percent of food costs are achieved by the farmer, while the other 80 percent go to manufacturing, labor, packaging, transportation and marketing.

A couple of examples illustrate the impact of increased commodity wheat prices on the prices of common wheat-based products:

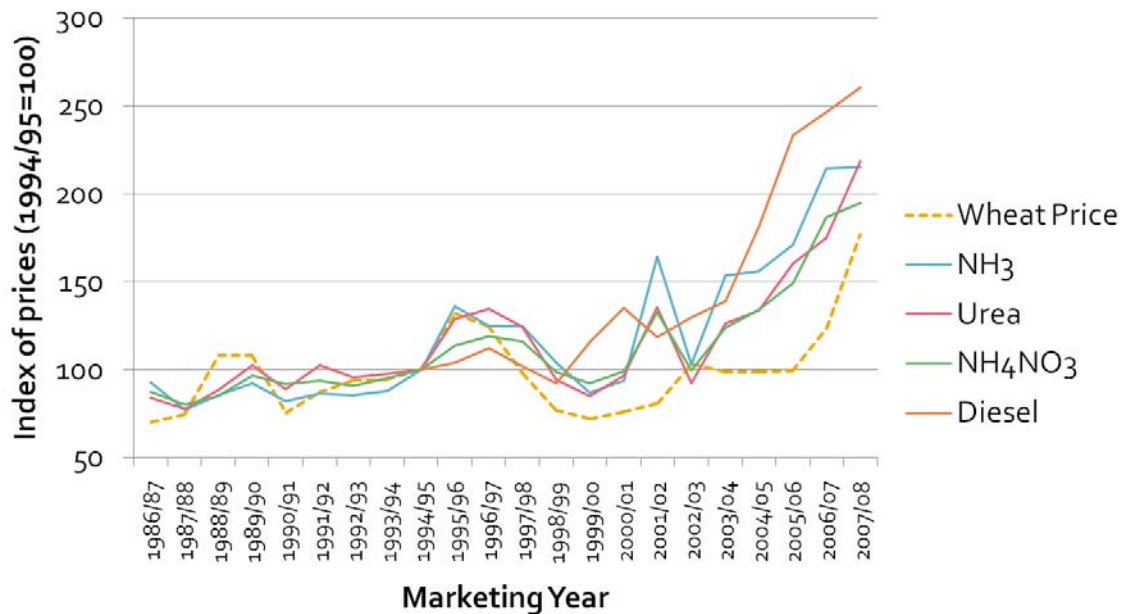
- Wheat consumption in the U.S. is around 200 lb./person/year, which is three and a third bushels. Even at \$12, then, commodity wheat consumption costs each American, on average, less than \$40 per year or about 10.8 cents a day. At \$8 per bushel, which is the approximate range during the time this testimony was being written, commodity wheat consumption would cost each American an average of \$26 per year or 7.2 cents per day.
- On average, a baker can make about 70 one-pound loaves of white bread out of a bushel of wheat. At \$4 per bushel, that makes the commodity wheat portion of a loaf worth about six cents; at \$8 per bushel, about 11 cents; and at \$12 per bushel, about 17 cents.
- In the case of pasta, the numbers are roughly the same. The actual cost of durum in a one-pound package of pasta, even at today's higher prices, is still only 20 to 30 cents of the \$1.50 per package cost paid by the consumer. About a year ago, this was roughly 12 to 15 cents.
- Raising the price of a cookie by 1 cent would cover a \$9 per bushel increase in the price of wheat.

Though the numbers in these examples can vary slightly, they all point to the same reality – increased commodity prices, and specifically increased wheat prices, are not solely responsible for the prices increases we have seen in grocery stores.

What Impact Does This Have on Farmers?

While increased wheat prices are certainly a positive development for wheat farmers in general, the reality on the ground is not rosy for everyone. The vast majority of wheat producers didn't achieve sales at record highs because they had existing contracts that required delivery or had already sold to service debts. Though it's not being reported in the media, wheat futures are down a third from winter highs, with hard red spring wheat, a premium product of the Northern Plains, down by more than half. The decline in prices was not an unexpected market function; short supplies and continued demand typically does and has spurred increased plantings, bringing lower prices on the expectation of bigger crops.

At the same time, the cost of producing wheat continues to rise, with input prices in some cases double what they were just last year (see chart). USDA's Economic Research Service estimates that the total cost of producing an acre of wheat will be around \$230-\$250 in 2008 and 2009 (\$5.75 to \$6.25 per bushel at a 40 bushel yield), versus \$175.63 in 2002 (\$4.39 per bushel at a 40 bushel yield).



In addition to rapidly rising input costs, which necessarily increases risk as growers borrow more to put the crop in the ground, producers are also facing unprecedented market volatility. Trading limits for wheat have been modified a number of times in recent months to allow the wheat market to move as appropriate, but this also allows the wheat market to move within a much wider range than has been historically possible. Higher prices have increased margin calls for those trying to hedge risk in the commodity market, putting stress on local elevators and, thus, farmers, who may no longer have the ability to forward contract with a local facility. Additionally, massive influxes of money from investors who never plan to take possession of any commodity have affected market movements. NAWG detailed these concerns in comments to the Commodity Futures Trading Commission, available at:

What Should We Do?

As calls for action to counteract high commodity prices increase, the wheat industry has consistently emphasized the need to allow the market to work as intended. Previous cycles have proven that global wheat production will assuredly expand in response to higher prices, and evidence of that is already being seen; USDA has forecast U.S. wheat production will be up 16 percent from 2007/2008 and world wheat production will be up 8 percent from 2007/2008 to a record 656 million tons, assuming no serious weather or other production problems.

The fact is U.S. wheat production far exceeds domestic demand. Half of our annual production is purchased by countries that cannot grow enough for their own people, and many wheat producers depend almost entirely on overseas customers. Wheat growers believe we should allow the market to do its job and not attempt to interfere by managing or restricting access to supplies, which could have devastating consequences that ultimately lead to even shorter supplies in the future.

We would like to take this opportunity to address three specific proposals that have emerged in an effort to decrease pressure caused by increased commodity prices.

1) *Restricting exports.* Many in the baking industry have asked the government, specifically the Department of Agriculture, to intervene in the wheat market in a way that would curtail exports. The U.S. wheat industry publicly and wholeheartedly supports fair and open trade of wheat throughout the world and has unequivocally opposed this request for a number of key reasons:

- An ill-timed market disruption, even a temporary one, could dramatically undermine the economic incentive to produce more wheat, exactly the opposite of what the milling and baking industry needs to reduce costs.
- Any export curtailment would also unfairly penalize farmers who can only grow wheat or sell exclusively into export markets at a time when their production costs are rising dramatically.
- Some of the loyal overseas buyers of U.S. wheat – relationships that have taken decades in some cases to cultivate - would begin seeking alternatives to the supplier they have come to rely on, hurting the U.S. wheat producing industry for years to come.

2) *Allowing growers with land in the Conservation Reserve Program to be released from their contracts early without contractual penalties.* The wheat industry also opposes any release of acres from the Conservation Reserve Program without contractual penalties. When CRP contracts are up for renewal, landowners will be able to make a choice between renewing CRP contracts and bringing those acres back into production in a market environment that exists at that time. There is also no guarantee that any acres released from CRP at any time will go into wheat production.

3) *Modify the renewable fuels standard (RFS) approved late last year.* The wheat industry was supportive of the increased renewable fuels standard as it moved through the legislative process last year and remains supportive of this mandate, which will help the continued development of a renewable fuels industry in the United States. While corn ethanol has received a lot of criticism as commodity and food prices have gone up, the commodity corn, like wheat, makes up a very small amount of the cost of any final food product. It is also important to note that field corn, used for ethanol and animal feed, is a different crop than sweet corn, a vegetable used for human consumption. Additionally, the ethanol production process yields byproducts that can be used for animal or human consumption; a 56-pound bushel of corn used in the dry mill ethanol process yields 18 pounds of distillers grains, a good source of energy and protein for livestock and poultry, while a bushel of corn in the wet mill ethanol process creates 13.5 pounds of corn gluten feed and 2.6 pounds of high-protein corn gluten meal in addition to corn oil used in food processing.

It is also important to take into consideration the extent to which soaring energy prices have affected all aspects of food production. Farmers, of course, are facing fertilizer prices that are doubling year-over-year and diesel now more than \$4 per gallon. Increased energy costs have affected the cost of transportation of inputs to the farm and of the commodity away from the farm, of processing, marketing and transportation to the final market. Economic analysis shows that, without ethanol, oil and gasoline prices that affect players throughout the food chain as well as consumers could be as much as 15 percent higher; the Renewable Fuels Association told Congress recently that because ethanol is replacing gasoline in the marketplace, removing 4.5 billion gallons of ethanol would increase gasoline prices in the short term by up to 31 percent.

Though wheat grain is not typically used for ethanol purposes in the U.S., NAWG has been a strong advocate for policies that would spur commercialization of cellulosic ethanol, often referred to as second generation ethanol, which could be made from wheat straw and other agricultural residue. The wheat industry shares the concerns of many others in the renewable fuels community that removing or modifying the RFS at this point would decrease the incentive for the industry as a whole to grow and stall progress toward a full-fledged renewable fuels industry, proving detrimental to our national security and farm economy while not appreciably improving the food price situation.

Conclusion

Wheat growers understand the concerns of millers and bakers facing increased wheat costs and of consumers in the grocery stores facing increased food costs. However, the agricultural market is historically very cyclical and, with increased input costs that are outpacing increases in futures prices, wheat growers also have concerns related to commodity prices. Wheat growers believe that allowing farmers to respond to signals from the marketplace is the correct approach to dealing with rising commodity prices, a position that is supported by the decrease in wheat futures prices by one-third or more in recent months.