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Gross: Why There's an Ethanol Backlash

BY **DANIEL GROSS** ON 7/19/07 AT 8:00 PM EDT

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Ethanol, the substitute for gasoline that in the United States is largely derived from corn, is hot. Statistics from the Renewable Fuels Association show that production doubled between 2002 and 2006, from 2.1 billion to 4.9 billion gallons, allowing the United States to surpass Brazil as the Saudi Arabia of ethanol. When the 86 plants under construction today are completed, American production capacity will top 13 billion gallons per year. In his most recent State of the Union address, President Bush called for the United States to produce 35 billion gallons of renewable fuels in 2017.

Any rapidly growing, paradigm-shifting industry is bound to engender both enthusiasm and resistance in roughly equal amounts. And the prospect of using grains, which have generally been cheap in this country, as a replacement for fossil fuels, was bound to excite hope and ruffle feathers. After all, while farmers and ethanol-plant investors will profit, companies and industries that rely on cheap grains, or that produce and distribute fossil fuels, face serious disruption. And so, before it has even emerged as anything more than a marginal contributor to supply—ethanol accounted for about 1.25 percent of gasoline use last year—a full-fledged ethanol backlash is underway. The squawks of protest arise not just from oil companies. They're

coming from economists, environmentalists, poverty fighters, and science nerds. Meet the ethanol-skeptics.

Inflation hawks. Economists and analysts have been quick to note (subscription required) that using corn to make gasoline is contributing to the greatest macroeconomic evil: inflation. Indeed, energy and food now constitute a positive feedback loop. The high and rising energy prices—according to the Bureau of Labor Statistics, energy prices rose in the first half of this year at a 27.8 percent annual rate—contribute to high food prices in two ways. It makes farming, food production, and food distribution more expensive, and it encourages more people to use grains like corn to make ethanol, which also drives up corn prices. (Here's a chart of corn futures and a chart of wheat futures.) As the consumer price index shows, in the first half of 2007, food costs rose at a 6.2 percent annual rate.

Poverty activists. Inflation in food prices can inflict severe damage on the poor, who already spend a larger chunk of their income on food than the well-off. It's possible that America's hunger for gasoline could exacerbate hunger in Africa. Earlier this week, Josette Sheeran, an official of the U.N. World Food Program, told the Financial Times that rising global grain prices, which can be attributed in part to rising ethanol production, may force it to scale back relief efforts in places like Chad, Niger, and Mali. They are confronting a doubling of corn prices in some countries, Shareen said. "In a world where our contributions are holding fairly steady, this [cost increase] means we are able to reach far less people."

Efficiency freaks. For economists, engineers, libertarians, and others who believe that inefficiency and market distortions are the greatest evils, ethanol is a fat target. As Robert Bryce noted in Slate, ethanol receives a generous and increasingly unnecessary federal subsidy. Thus, every gallon of ethanol produced adds to the deficit. And since ethanol doesn't pack as much power per gallon as gasoline distilled from crude oil, you have to burn more ethanol to go the same distance. The Environmental Protection Agency's fuel economy guide concludes that cars built to run on E85 (a gasoline made with 85 percent ethanol) get about 25 percent fewer miles per gallon as the same models that run on plain old gas. Business Week's Ed Wallace has thus dubbed ethanol a net energy waste. The frequent need for ethanol users to stop and refuel wastes time and money, and can be a serious impediment to long-distance car travel. The Department of Energy has a list of some 900 stations that offer E85. And as these guys found out, they are sometimes few and far between.

Environmentalists. Environmentalists are quick to warn about how the use of petroleum and coal for energy is fouling our air and water. The use of ethanol for the same purpose, it seems, could do the same. Earlier this week, the Washington Post described a new report, funded by government and nonprofit enviro groups, that looked at the potential impact of higher corn production in Maryland and Virginia on the Chesapeake Bay. The equation goes something like this: More corn farming requires more fertilizer (bad for the environment), and more tractors (bad for the environment), and produces more chemical runoff into

water sources (bad for the environment). The upshot: If we keep blending ethanol into gasoline, there might not be any crabs in the Chesapeake anymore.

While I'm as susceptible to Malthusian thoughts as the next paranoid guy, I find much of the anti-ethanol case to be unpersuasive. In each instance, the haters would have us look at ethanol, and the ill effects its greater use would assuredly produce, largely in isolation. Might the production of corn ethanol cause pollution? Of course. Is it worse than the sort of pollution created by other types of energy production—i.e., coal and oil? Probably not. Does greater use of corn for ethanol help spur price increases for food? Sure, but so do many other factors, like, say, the transformation of China from a subsistence farming economy into a more modern one. Is ethanol more inefficient, and hence more costly, than gasoline? Yes. But our heavy use of gasoline imposes all sorts of other costs—from pollution to the hundreds of billions of dollars we spend each year in Iraq. Factor those in, and ethanol no longer seems like such an economic loser. Finally, the long-term worries of the ethanol haters are in large measure based on the assumption that ethanol will continue to grow for many years at the same blistering pace it has recently. Such proclamations of boundless growth, which are a recurring feature of bubbles, frequently don't materialize as promised. Remember Dow 36,000?

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