

U.S. Agricultural Policy

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*Philip Morris Agricultural Leadership Development Program
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Introduction

- Why does agriculture have chronic price and income problems?
- What are the implications of 2002 Farm Bill on:
 - Crop price possibilities
 - Winners/losers
- **Expectations** underlying the change in farm policy direction **versus Experience**
- What can we **realistically** expect from world trade

Historically—there have been Two Major Components of Farm\Commodity Policy

- **Policy of Plenty:** Ongoing public support to expand agricultural productive capacity through research, extension and other means
- **Policy to Manage Plenty:** Mechanisms to manage productive capacity and to compensate farmers for consumers' accrued benefits of productivity gains

What is the Problem?

- Technology expands output faster than population and exports expand demand
- Market failure: lower prices do not solve the problem
- No self-correction on the demand side
 - People will pay almost anything when food is short
 - Low prices do not induce people to eat more
- No self-correction on the supply side
 - Farmers tend to produce on all their acreage
 - Few alternate uses for most cropland

Traditional Policy Levers

- **Government Stock Management**
 - Loan rate/support price to set a floor price.
 - Limit price increases by Gov't & FOR released stocks
- **Restrict supply**
 - Short-term set-aside
 - Long-term Conservation Reserve Programs
- **Expand demand**
 - Domestic
 - Foreign
- **Government payments**
 - Coupled to production
 - Decoupled

Implications of Current Farm Program

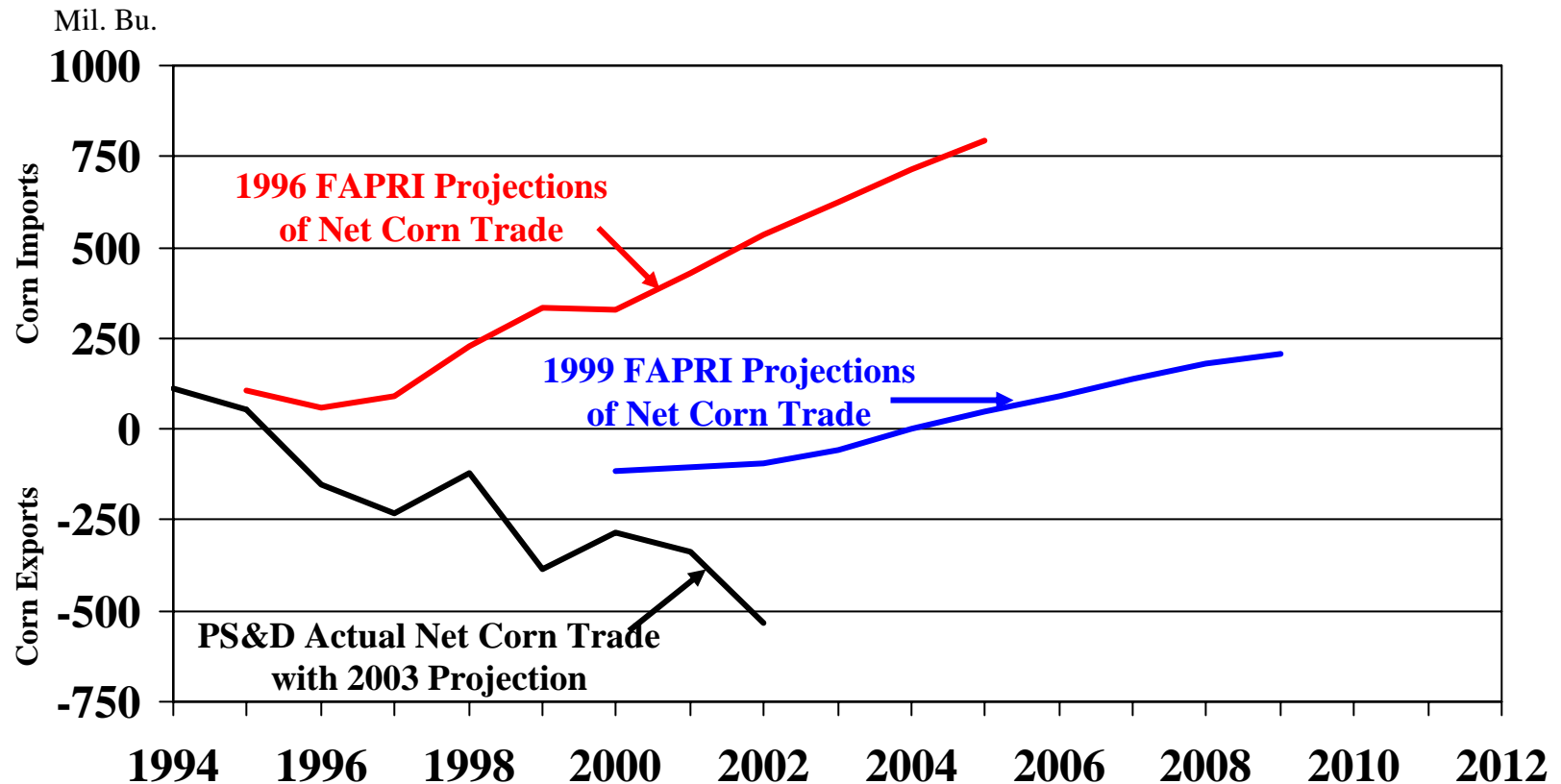
- **No price floor** – Since LDPs effectively replaced non-recourse loans
- **No emergency reserves**—Since no CCC or FOR buffer stock policy
- **No price ceiling**—Since Incomes are supported, not prices
- **Primary beneficiaries:**
 - Livestock producers, importers and other users are subsidized
 - Agribusiness input suppliers and output processors are subsidizedNot crop farmers (land owners?)

Expectations vs. Experience

Expectation: Rapid per capita growth in China/Asia will increase demand and US exports

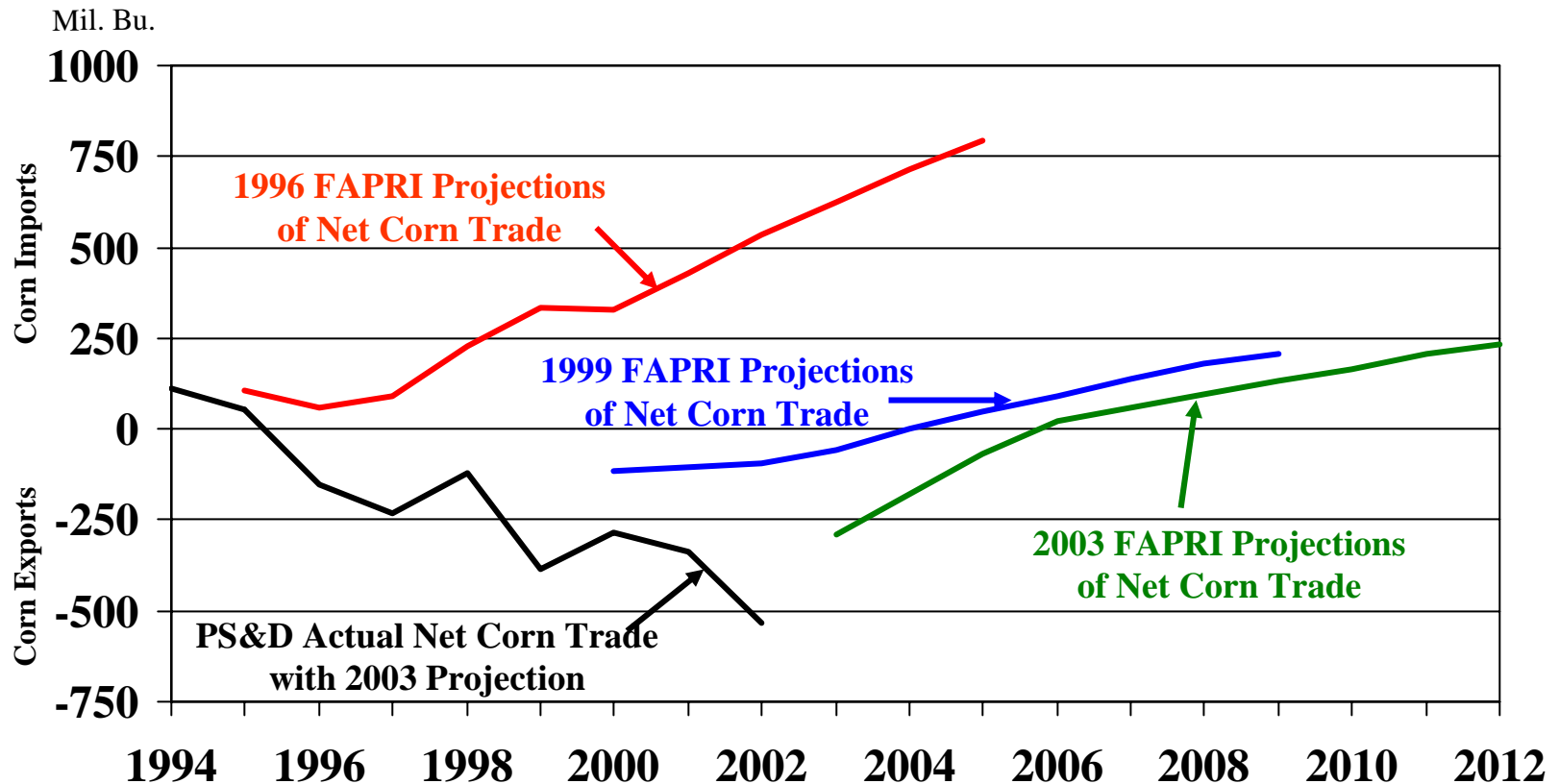
China Net Corn Trade

Comparison between 1996 and 1999 FAPRI projections and PS&D actual



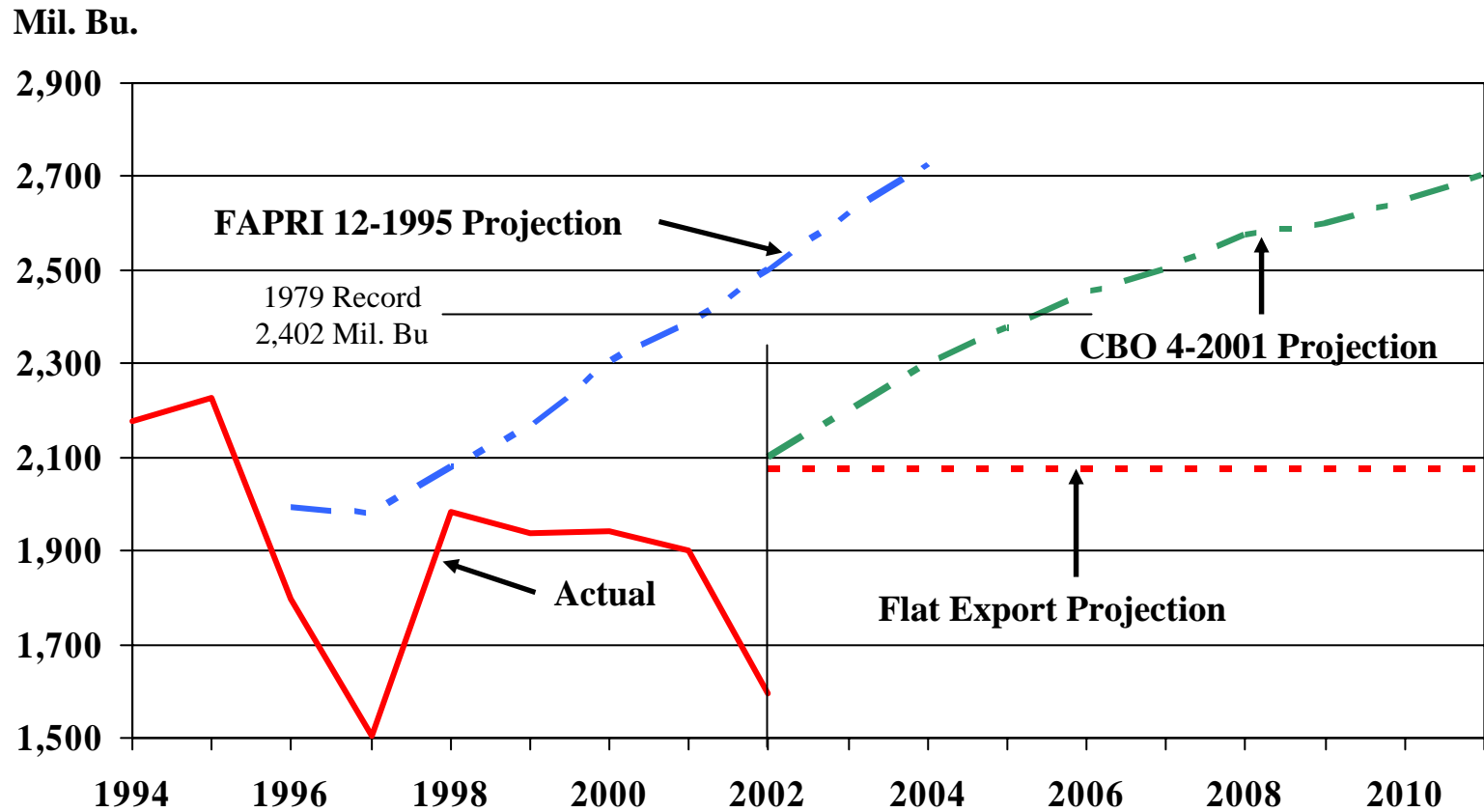
China Net Corn Trade

Comparison between 1996, 1999 and 2003 FAPRI projections and PS&D actual



Corn Baseline Projections

U.S. Exports



Expectations vs. Experience

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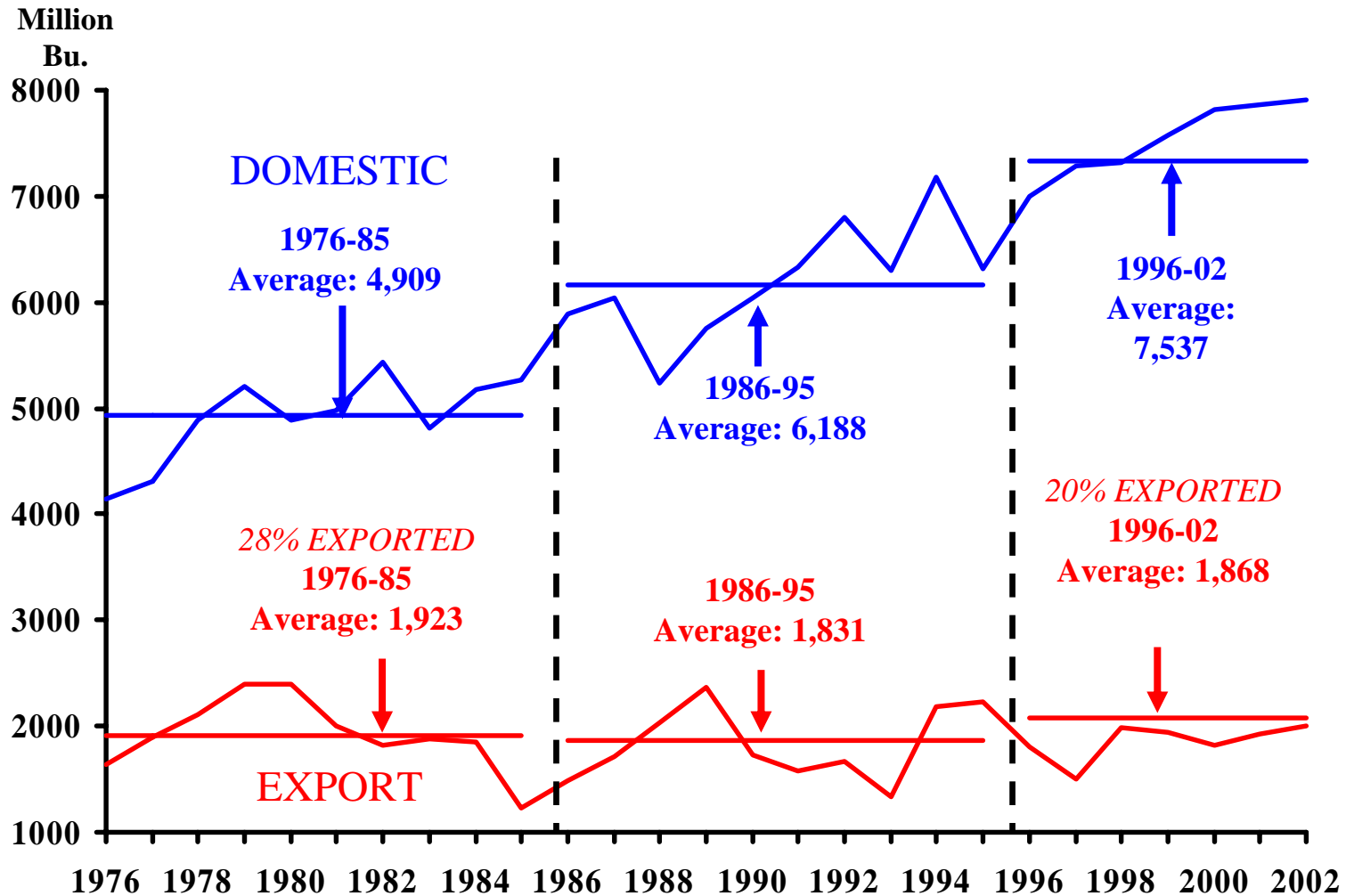
Experience:

China exported 500 million bushels of corn last year

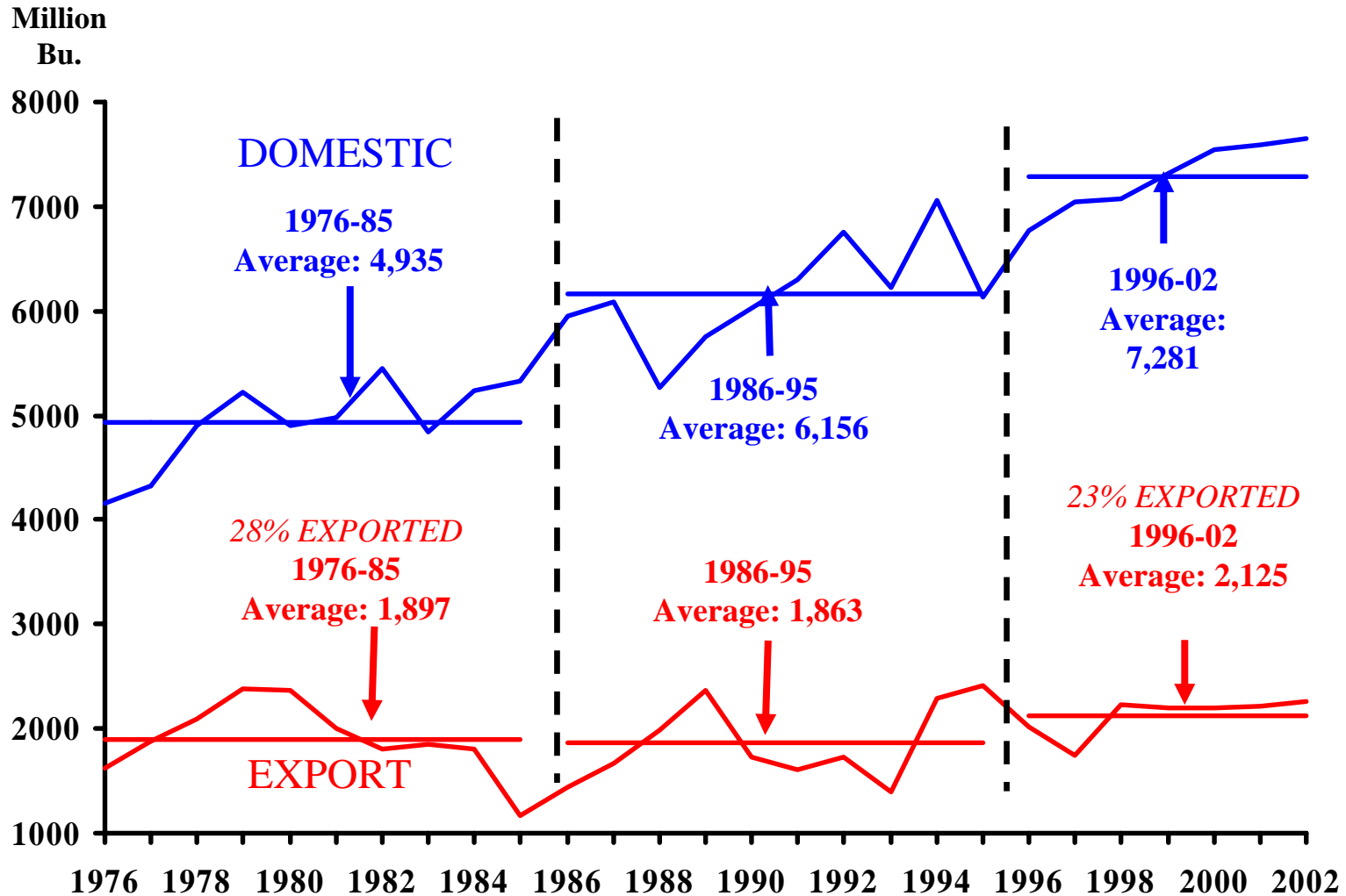
Expectations vs. Experience

Expectation: Export led farm prosperity just around the corner (been saying this for over 25 years)

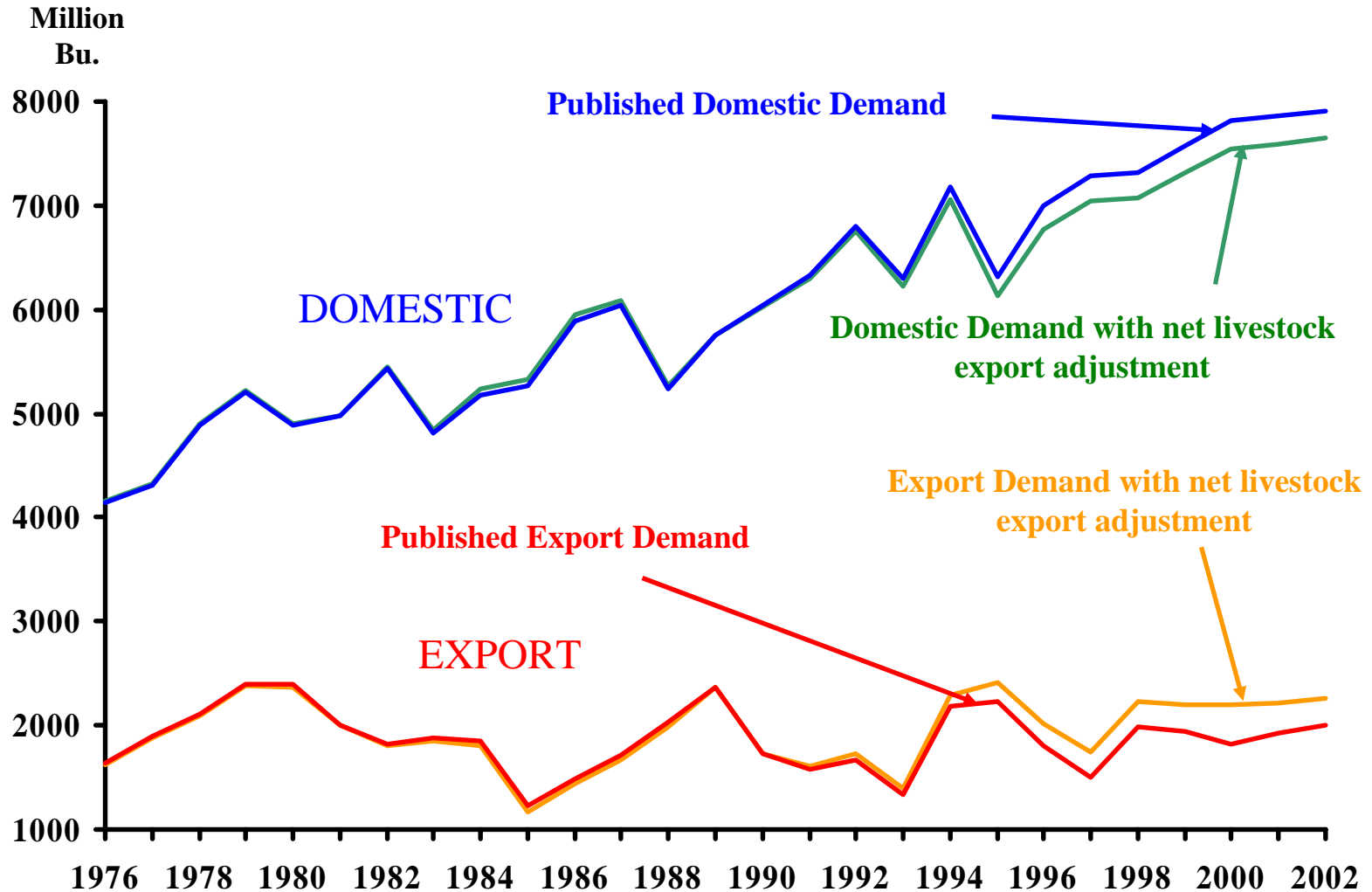
U.S. Domestic and Export Demand



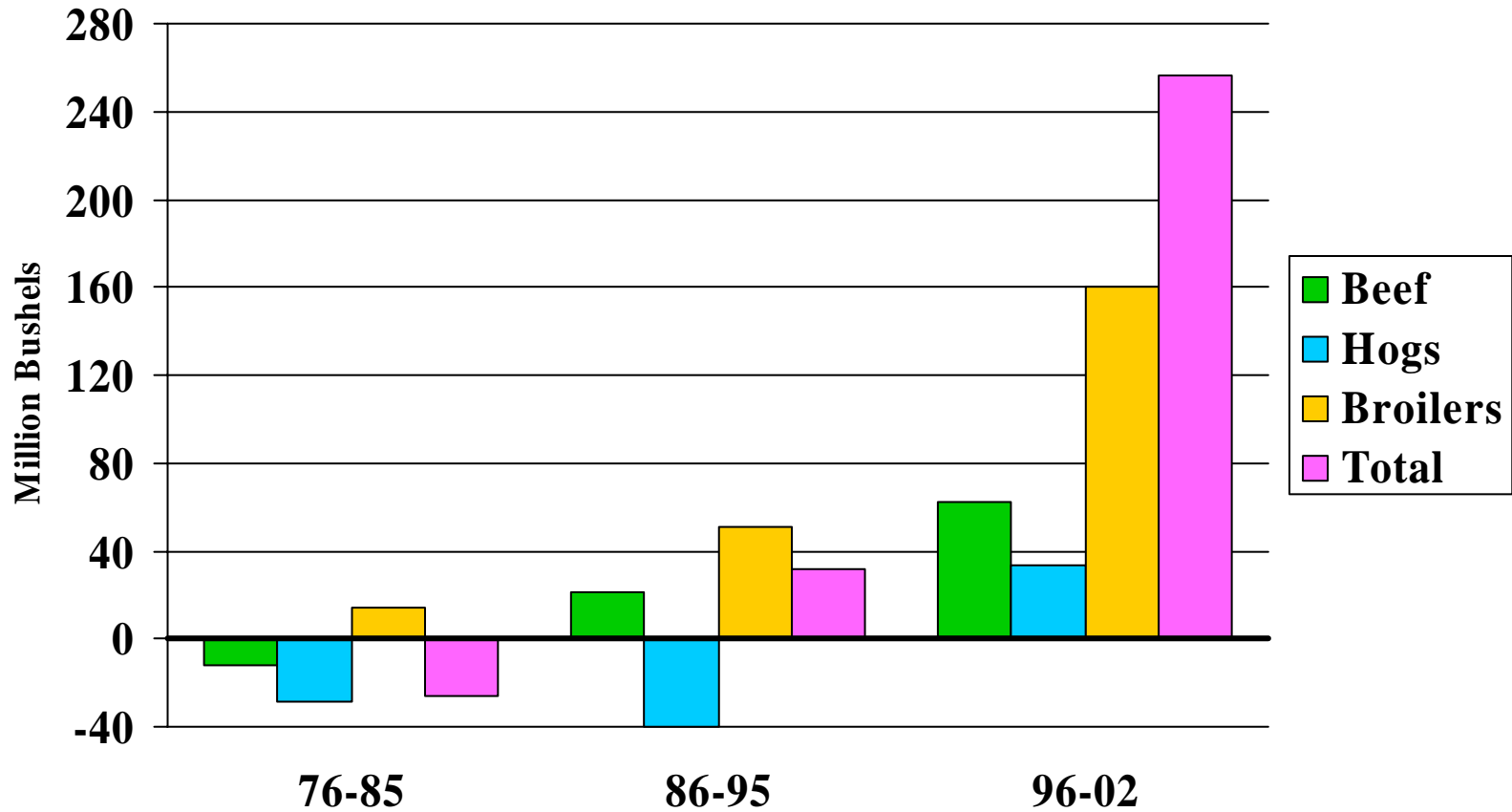
U.S. Net Domestic and Net Export Demand Adjusted for corn fed to import and export beef, pork, and broilers



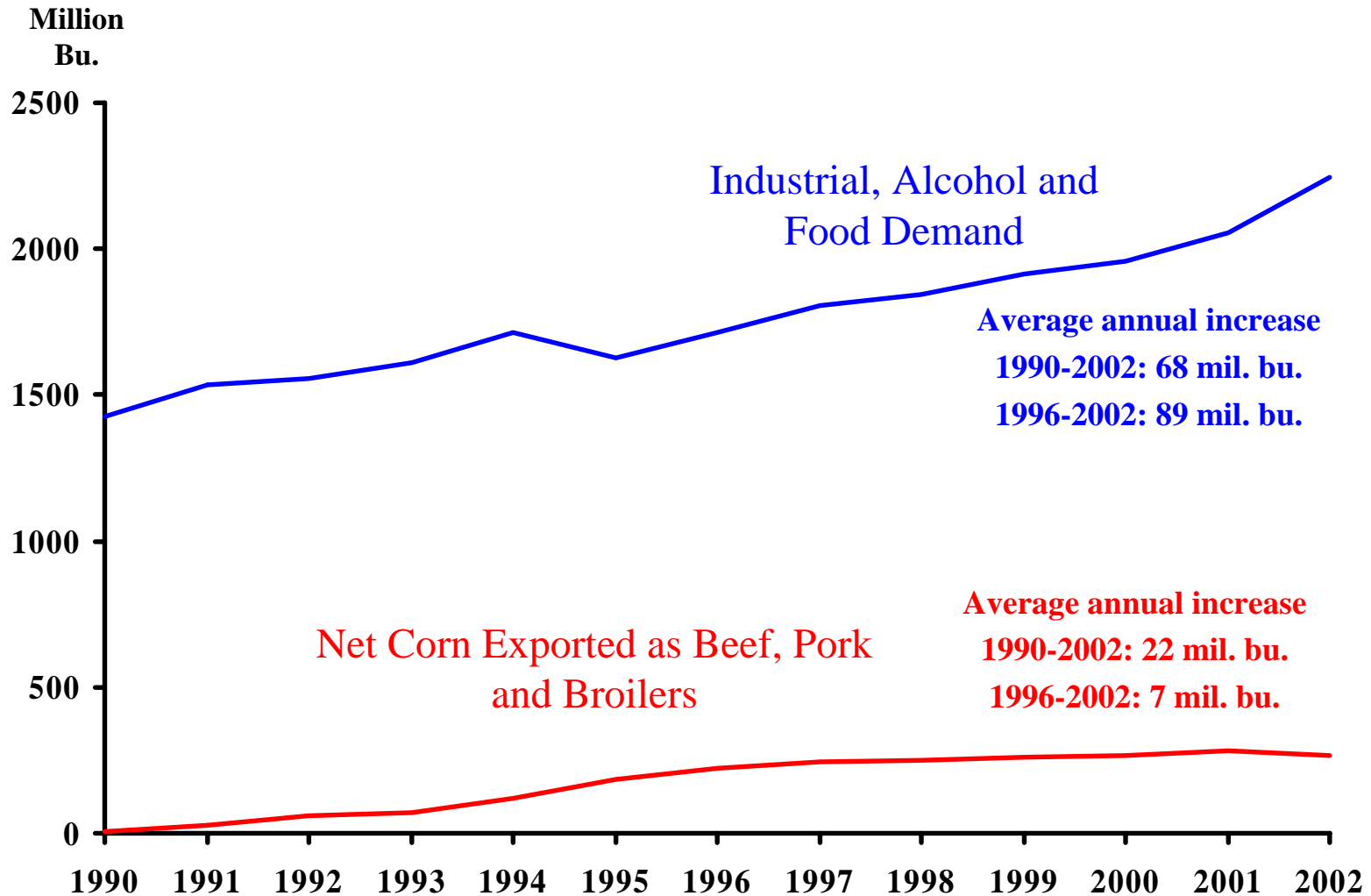
U.S. Net Domestic and Net Export Demand With and without net livestock export adjustment



Net U.S. Corn Exported in Livestock

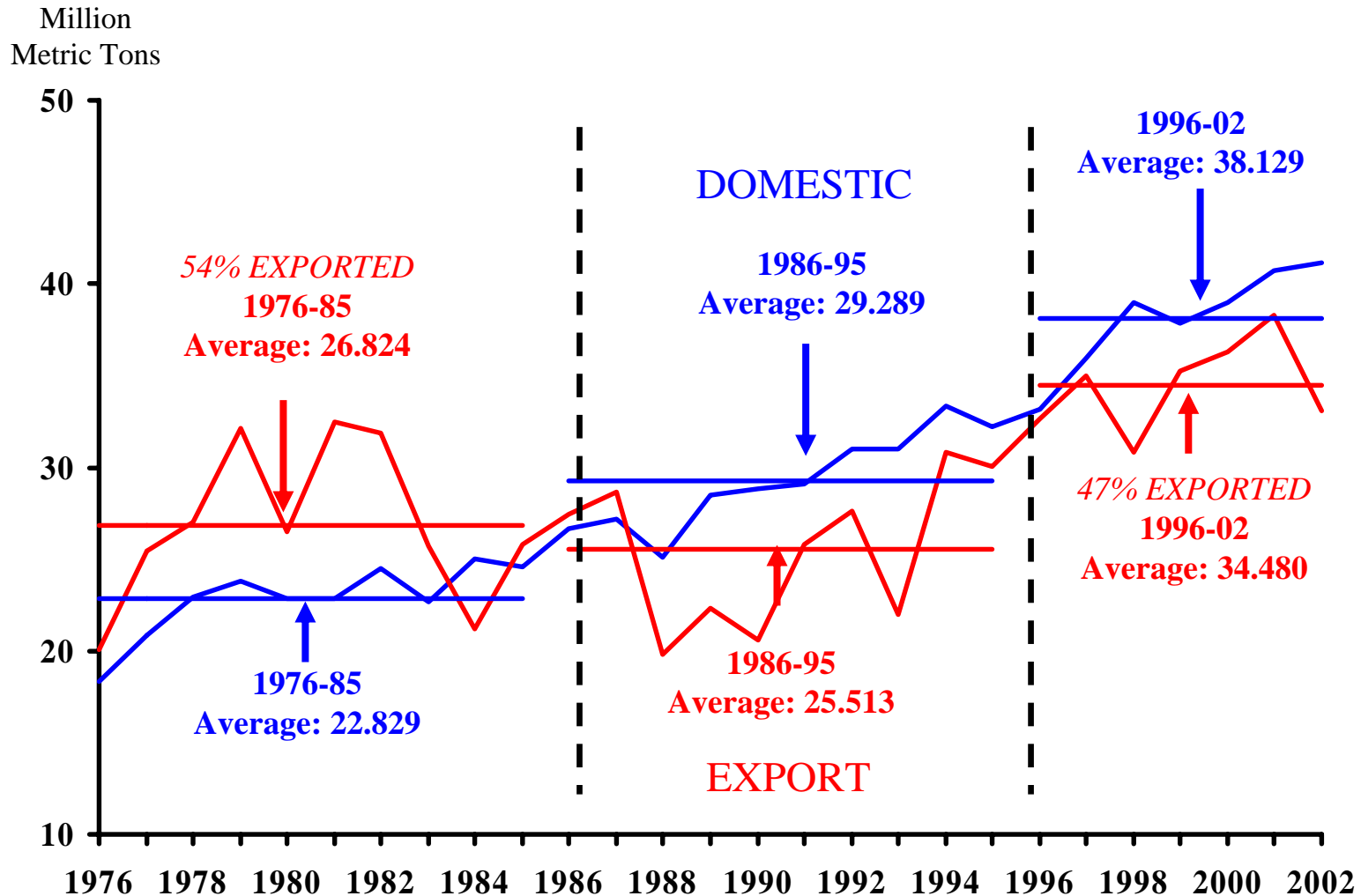


U.S. Net Corn Exported as Meat and Domestic Industrial, Alcohol and Food Demand

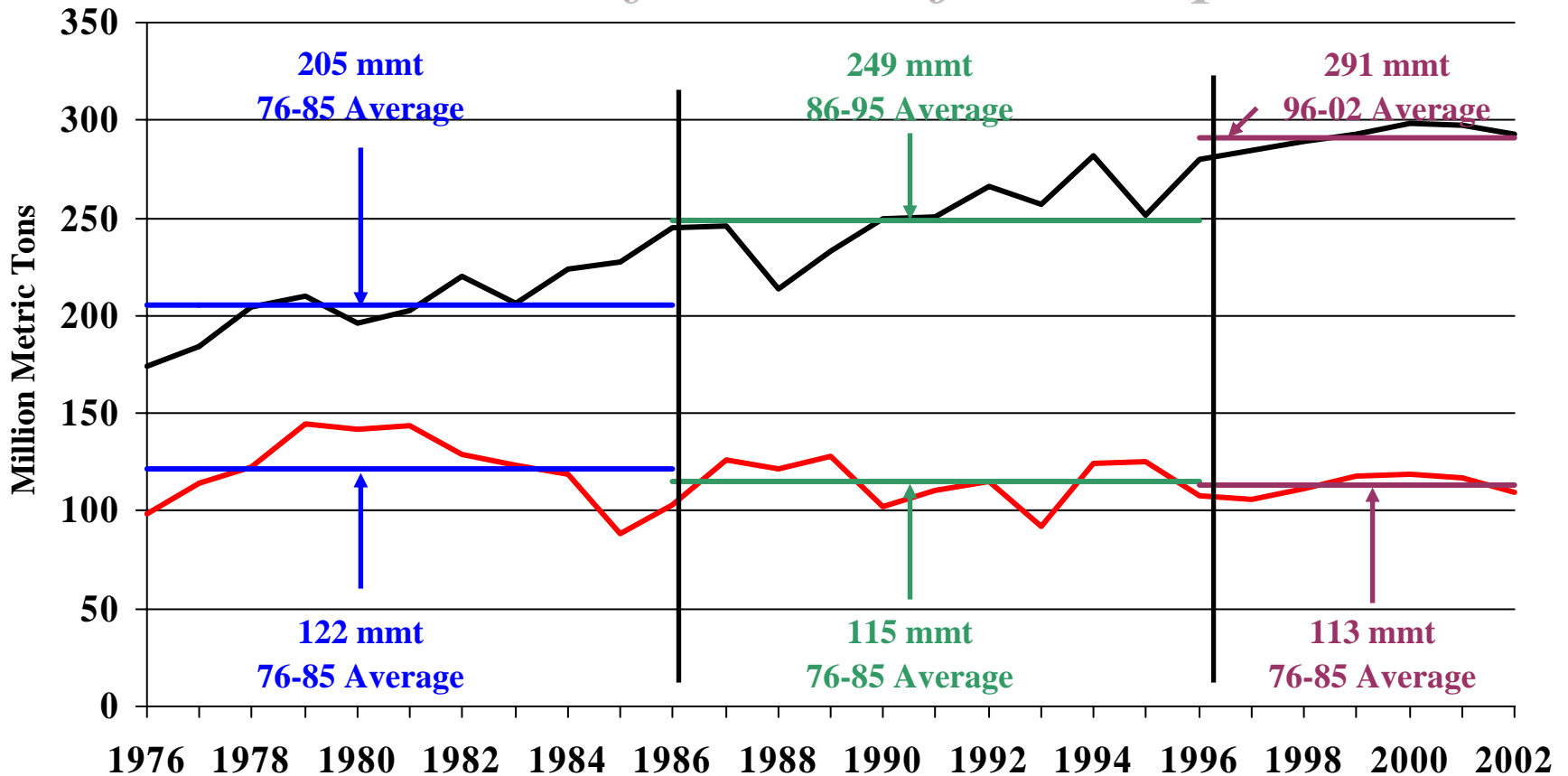


SOYBEAN COMPLEX

U.S. Net Domestic and Net Export Demand Adjusted for soy fed to import and export beef, pork, and broilers

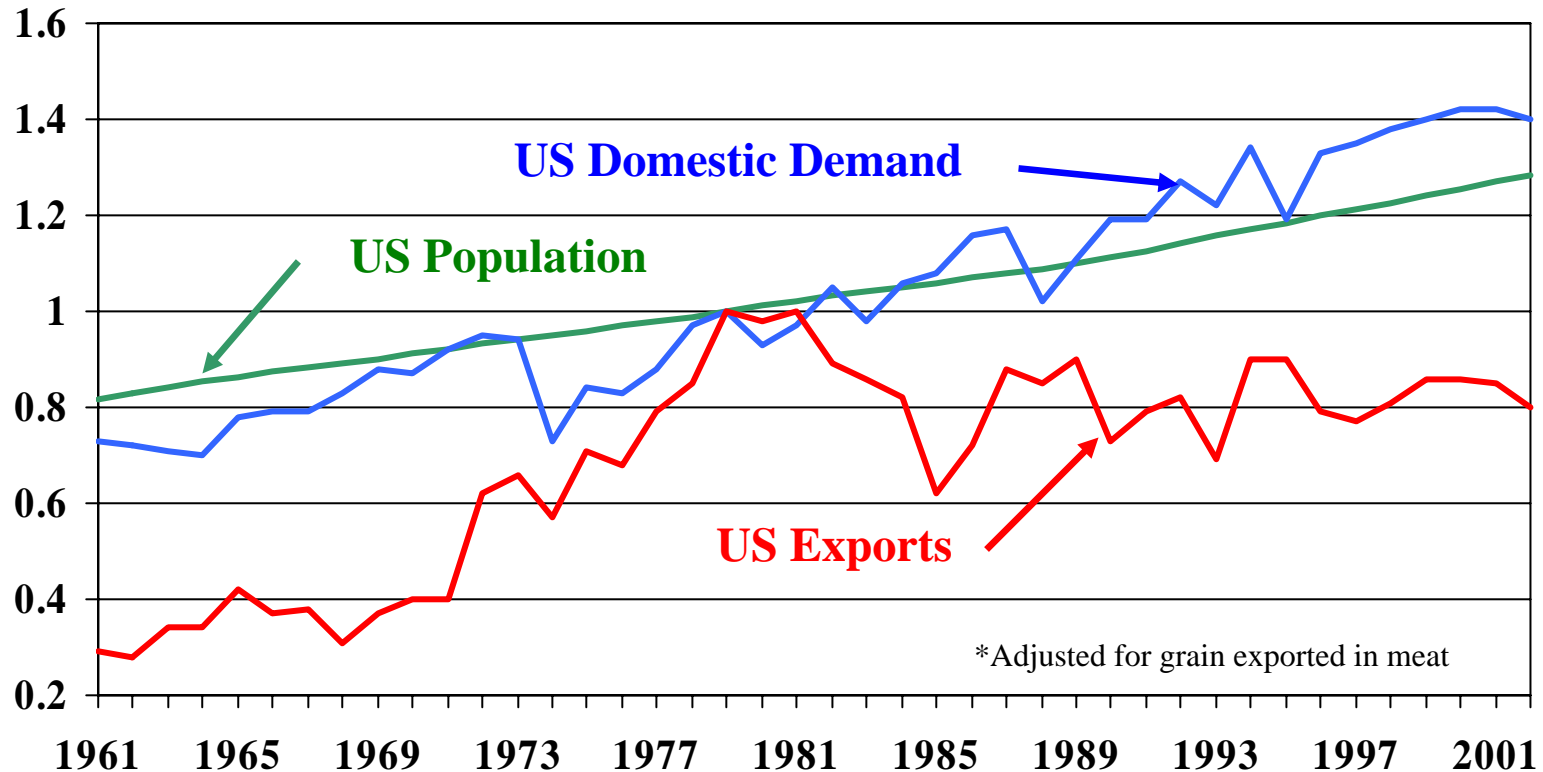


Net Export and Domestic Demand for 8 Major Crops



Guess which is exports and which is domestic demand

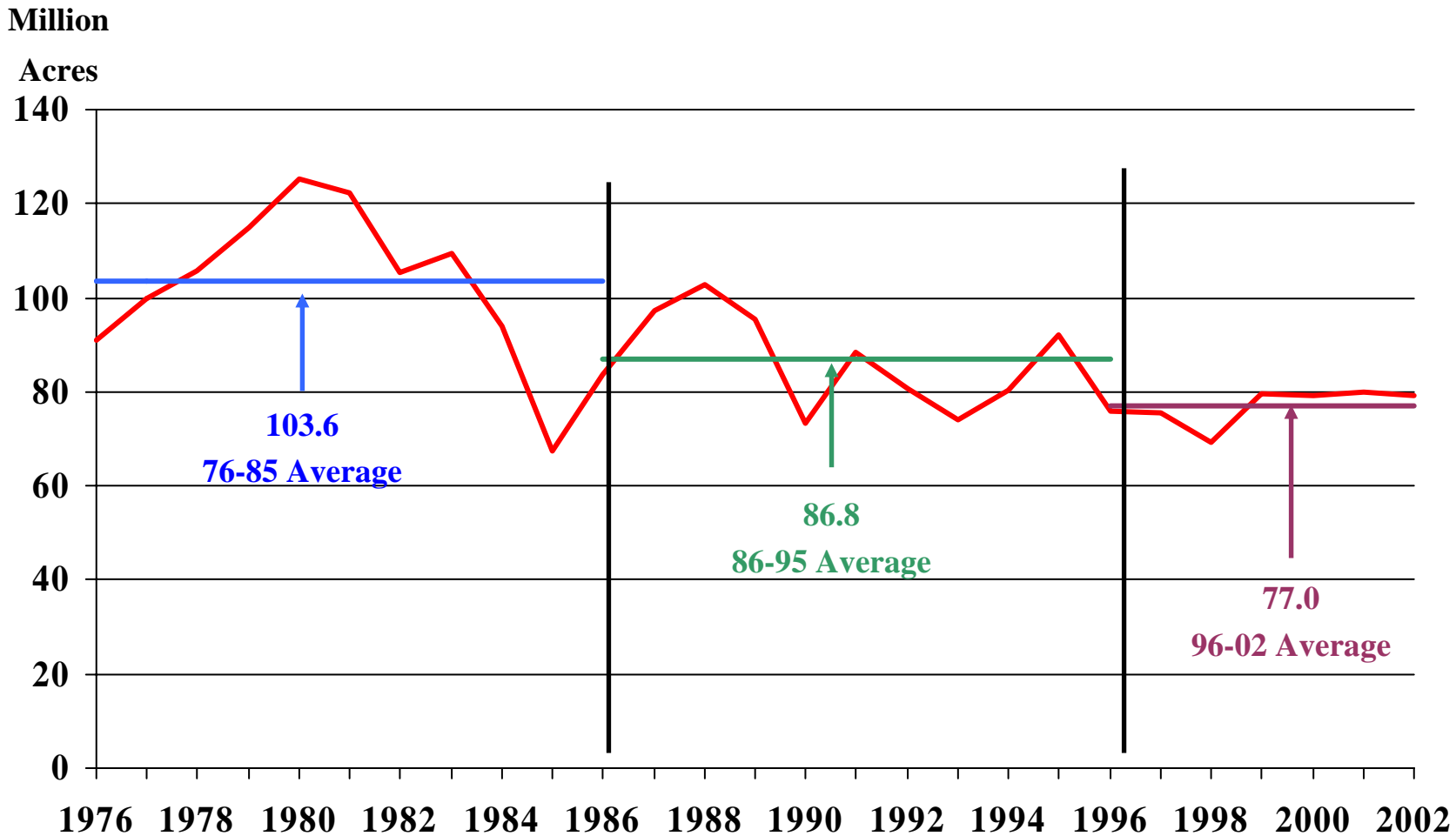
Exports Did Not Deliver



Index of US Population, US Demand* for 8 Crops and US Exports* of 8 Crops 1979=100

- Exports down to flat for last two decades
- Domestic demand increases steadily
- Since 1979, exports have NOT been the driving force in US crop markets

Net Export Acreage for 8 Major Crops



Expectations vs. Experience

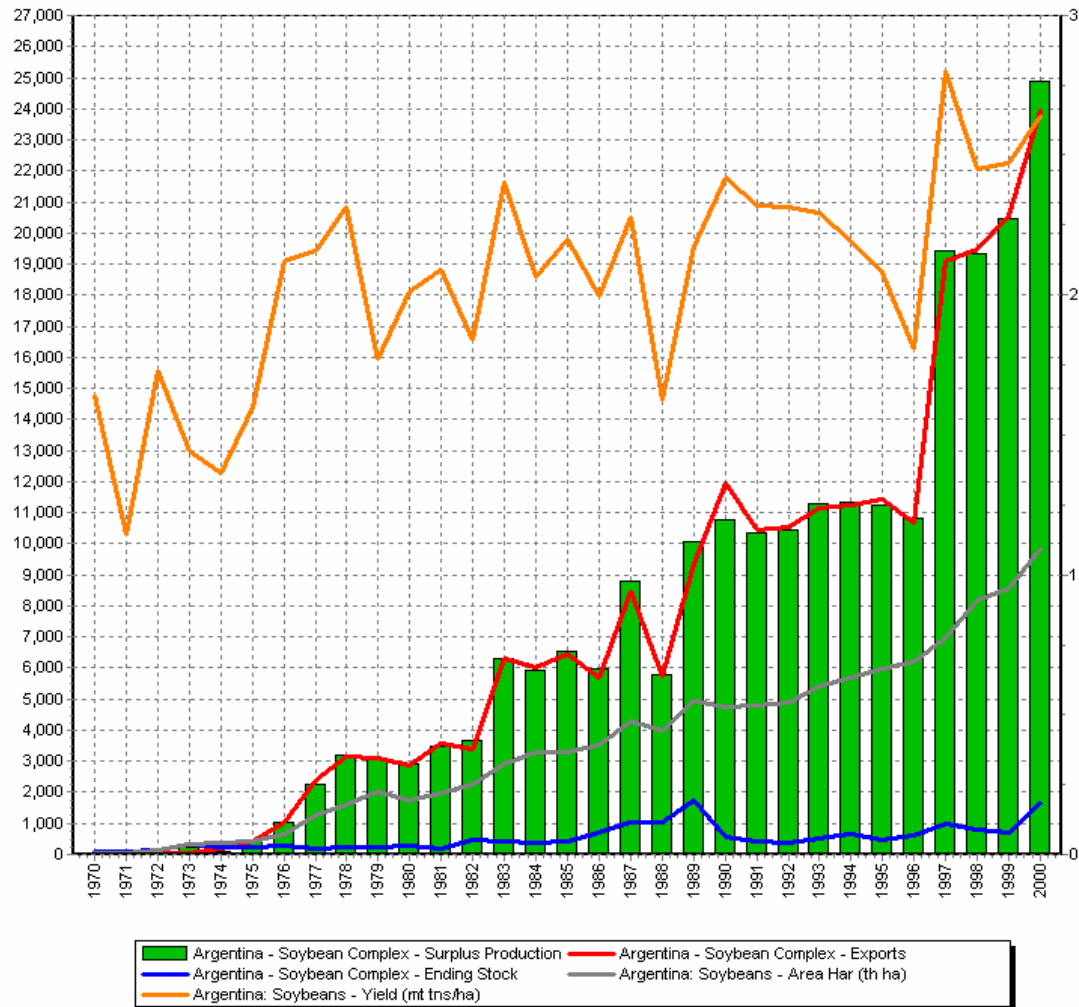
Expectation: Export lead farm prosperity just around the corner (been saying this for over 25 years)

Experience: Crop exports have been flat for years. Exports have not been the driving force of crop utilization

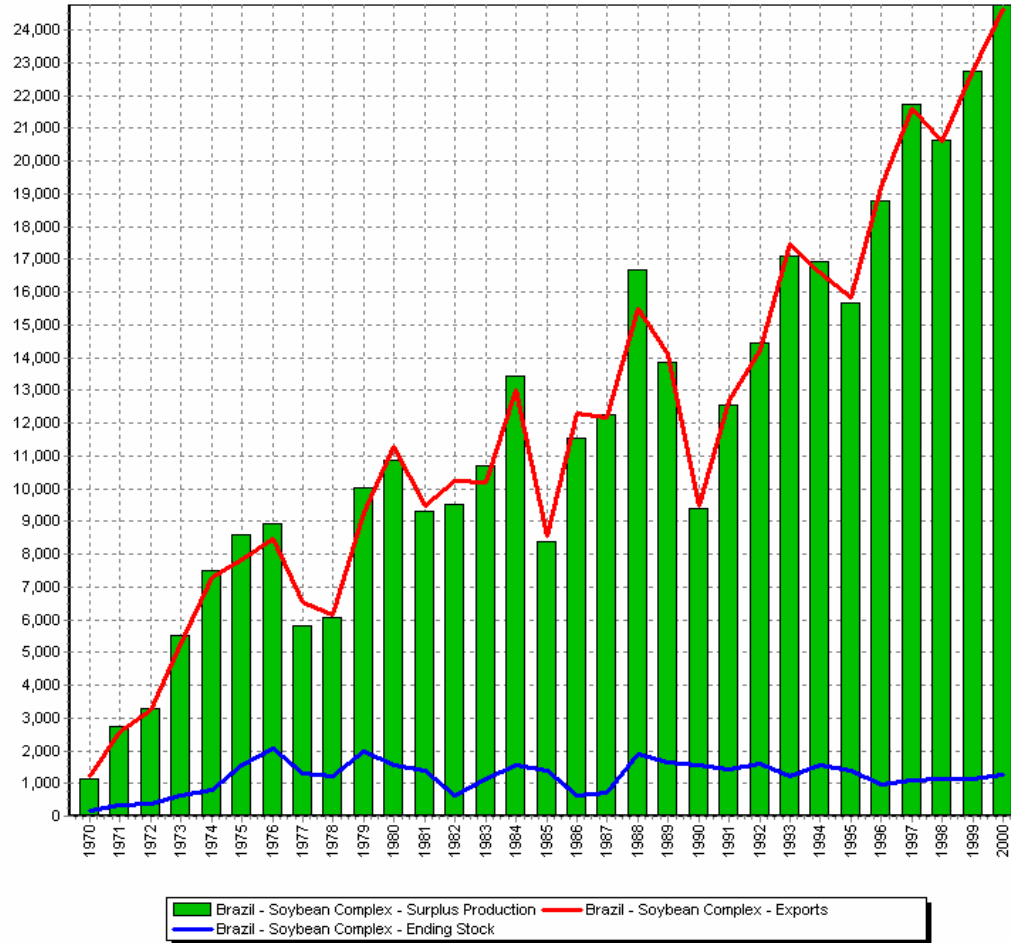
Expectations vs. Experience

Expectation: With marketing loans and no acreage set-asides, competitors would not be under the US price support umbrella—would reduce production as needed

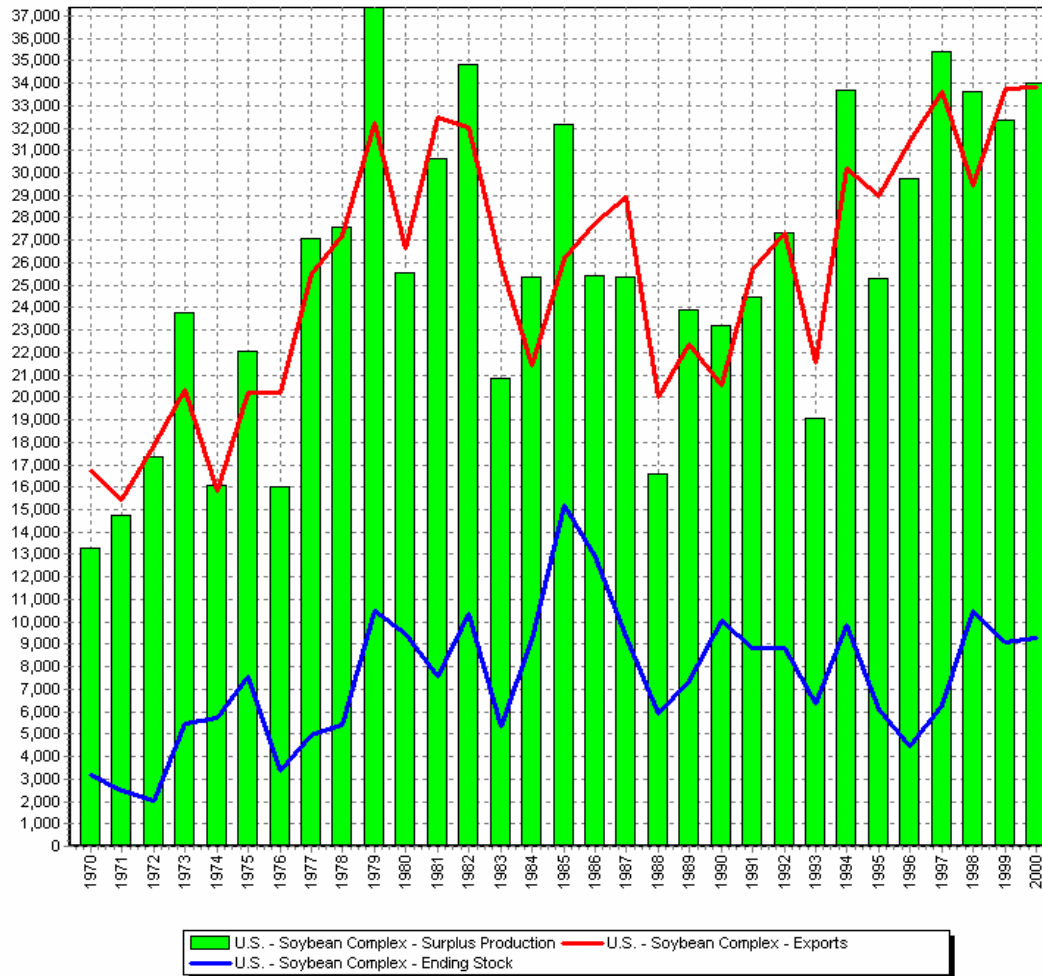
Argentine Soybean Complex Exports and Surplus Production



Brazilian Soybean Complex Exports and Surplus Production



U.S. Soybean Complex Exports and Surplus Production



Expectations vs. Experience

Expectation: With marketing loans and acreage no set-asides, competitors would not be under the US price support umbrella—would reduce production as needed

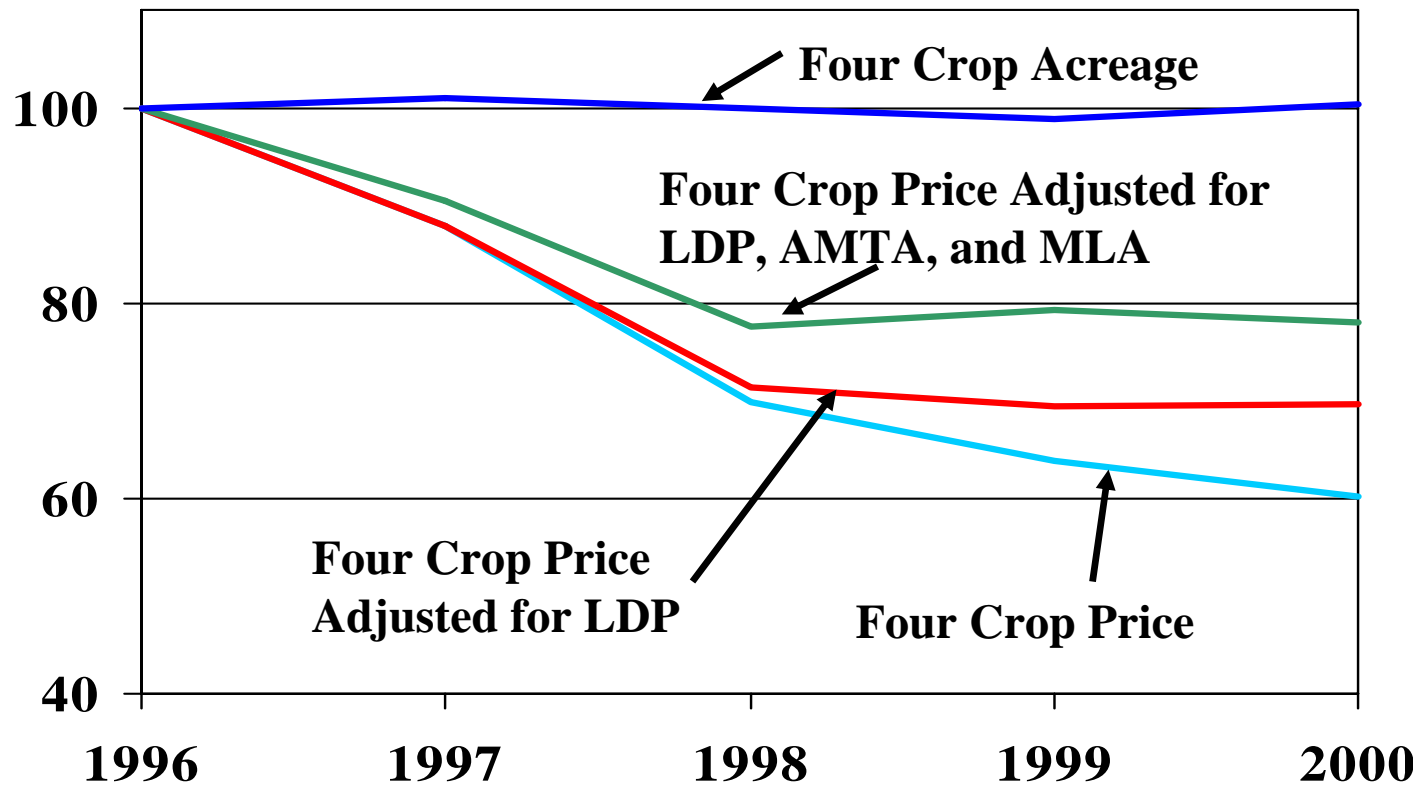
Experience:

- Export competitors export all production above domestic demand
- Eliminating set-asides and lower commodity prices did not cause competitors to reduce acreage

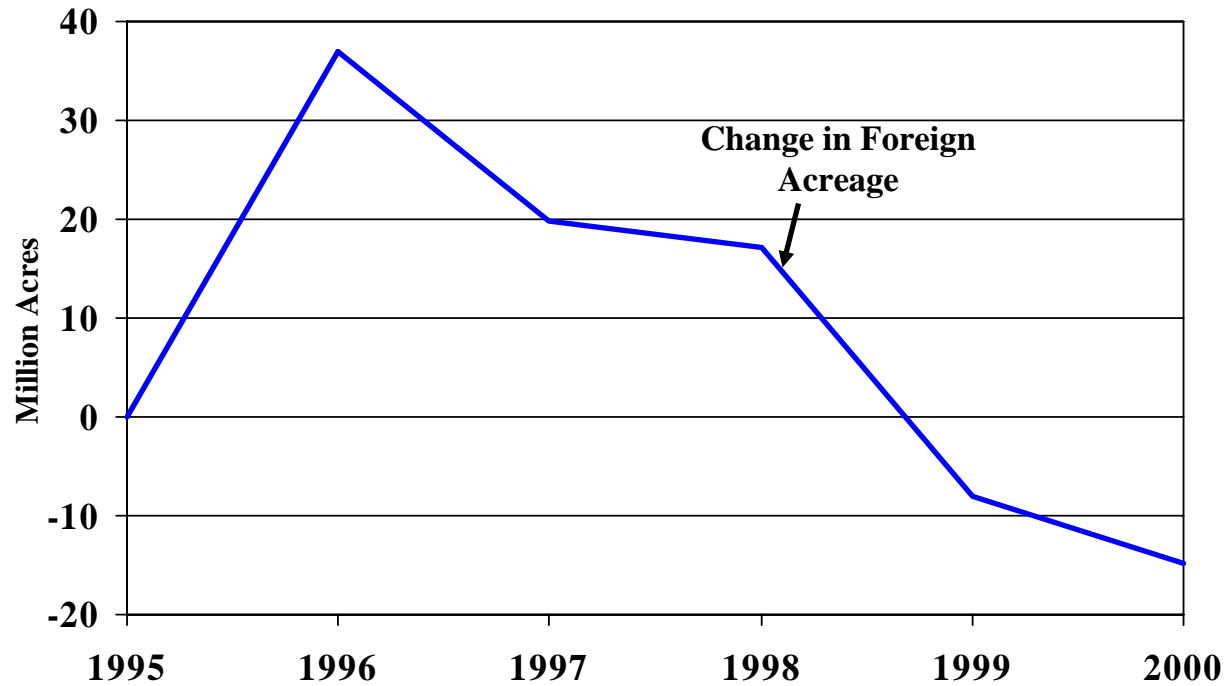
Expectations vs. Experience

Expectation: With planting flexibility & decoupled payments farmers would plant for the market – reduce production when needed

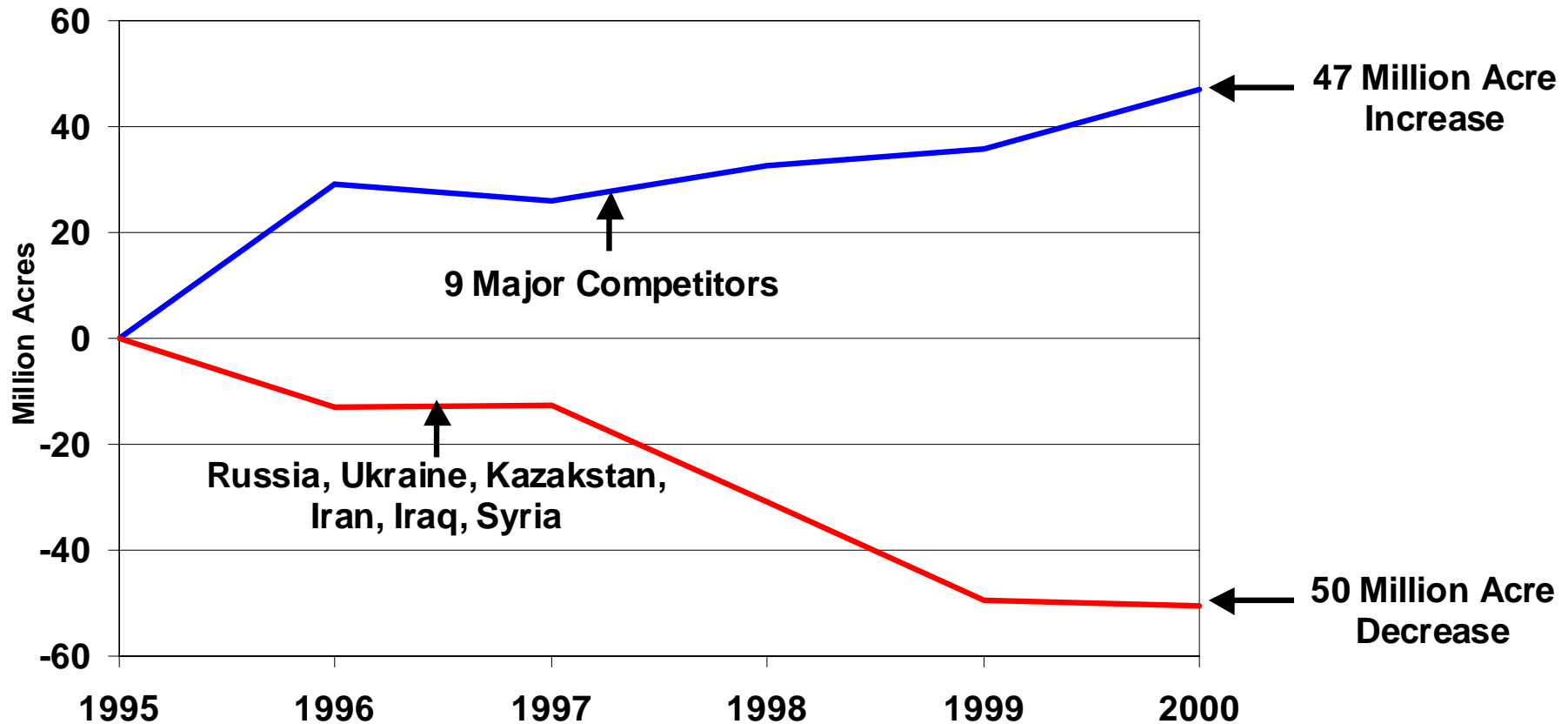
Indexed Four Crop Acreage, Price and Price Adjusted for LDP and Contract Payments



Foreign Crop Acreage



Change in Foreign Crop Acreage



Expectations vs. Experience

Expectation: With planting flexibility & decoupled payments farmers would plant for the market – reduce production when needed

Experience:

- Farmers change the mix of crops but use all their acreage
- Farmers have every incentive to produce full out
- Land remains in production even if the current farmer goes bankrupt

Expectations vs. Experience

Expectation: International trade and market response/privately-held stocks will perform price stabilizing function

Experience:

Export markets respond too little to price to rebalance inventories

Privately-Held Stocks

- Are always “On the Market” so takes less stock to drive down prices
- No incentive to hold sufficient stocks to cover a true “low yield” year

Points to Ponder

- Since 1985 farm policy has been driven by:
 - Exports, exports, exports (Those are OUR exports! And we'll do ANYTHING to get them back and to make them grow.)
 - Agribusinesses' lobbying ability (We MUST lower prices and maximize output. "If we build it, they will come.")
- Exports have not delivered after two decades of promises
- Agribusiness got everything they wanted (except elimination of the CRP)
 - No bottoms or tops on prices (Increases the value of superior information.)
 - Elimination of annual acreage reduction programs (Volume is everything.)
- Farmers relinquished the farm policy agenda to agribusiness and those that believe agriculture will self-correct with unfettered free markets

Recent Policy Choices

- 1996 & 2002 Farm Bills failed to recognize that:
 - Timely self-correction does not take place in agriculture
 - Aggregate demand of major crops responds very little to price
 - Aggregate supply of major crops responds very little to price
 - Crop exports are NOT going to provide the ever-increasing rate of growth agriculture needs to be prosperous on its own
- The policy choice was to:
 - reject these realities
 - allow prices to plummet
 - write very large checks to cover losses; which, in turn, has raised all kinds of distributional issues including the possible payment limitations

Policy Premises

- U.S. and world output will continue to outpace demand
- Aggregate crop agriculture does not self-correct on its own in a timely manner (assuming otherwise is denying the obvious)
 - Total acreage changes too slowly to be of help
 - Consumers will never oscillate between 1 and 5 meals a day depending on prices
- Exports
 - Competitors are as committed to producing for international markets as we are
 - Import customers view food as a national security issue and abhor increased dependence

Policy Implications?

- Farmers have been sold a bill of goods on the elimination of acreage reduction programs
 - Trends in competitors' acreage and production were unaffected by U.S. elimination of set aside
 - Elimination of set-aside was good for agribusiness but not good for farmers' market income
 - EVERY other non-farm industry watches demand when deciding output levels
- Storage programs weren't as expensive as we thought (millions compared to billions)

Challenges of the Day

- U.S. budget deficit
 - Payment limitations
 - Reduce all farm payment outlays
- Free trade challenges
 - Call for end of subsidies
 - Grain and livestock issues

Free Trade Challenges

- Call for end of subsidies
 - WTO, Free Trade Area of Americas, G20, and G90
- Grain trade
 - Imports – Wilmington Bulk
 - China
 - Corn export competitor
 - Soybean self-sufficiency
 - Brazil
 - Low land costs
 - 400 million acres available for crop production

Free Trade Challenges

- Livestock trade
 - Brazil
 - Meats
 - Poultry, Pork, Beef –particularly box beef
 - With frost free areas include winter pasturage in crop rotation regimen
 - Switch exports
 - from high-bulk/low-value seeds
 - to low-bulk/high value meats

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