Agriculture: Is it Different or Just Better Treated by the Feds?

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What's the Deal with Agriculture?

- **What is the current situation: Problems, problems—domestic & international**
- **Are the most current problems policy based?**
  - Internationally, the "Washington Consensus" policy
  - Domestically, dropped one of two critical policy elements
  - Expectations underlying the change in farm policy direction versus Experience
- **Food and agriculture are different**
- **Farm policy in a changing world**
- **What you need to remember about how agriculture works**

What's the Situation?

- **Crop prices have plummeted in recent years affecting farmers worldwide**
- **US expects to pay $20 billion annually in cash subsidies to farmers; Total for developed countries worldwide is $300 billion**
- **Farmers in other countries accuse US of dumping crops onto the international market at below the cost of production**
- **Developing countries can't provide cash subsidies to offset low crop prices.**
- **800 million people lack access to adequate nutrition**

Questions

- **Were these policy-caused problems?** To a large extent, yes.
- **If so, why didn't the policies work as expected?**
  Markets and policies work differently in agriculture.
- **What needs to be considered when evaluating alternative policies**? Must consider the nature of food and agriculture.

Internationally…

Were promised that the policy trio of:

- De-regulation
- Trade Liberalization
- Privatization

Would provide:

- Reduced malnutrition
- Increased the rate of social gains
- Increased farm prices and incomes

But it Hasn't Worked Out

International policy trio of de-regulation, trade liberalization and privatization…

- Ineffective, contentious and uncooperative
- Decrease in the rate of improvement of social measures
- Collapse in farm incomes
- Increase in concentration and benefits to multinational agribusinesses
- Increase public cost
- Does not allow for distinctive national policies

In the U.S.—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

We Have Dropped the "Managing Plenty" Part

In the past farm policies included:

- Floor price
- Supply management tools
- Price stabilization

Over the years and especially since 1996:

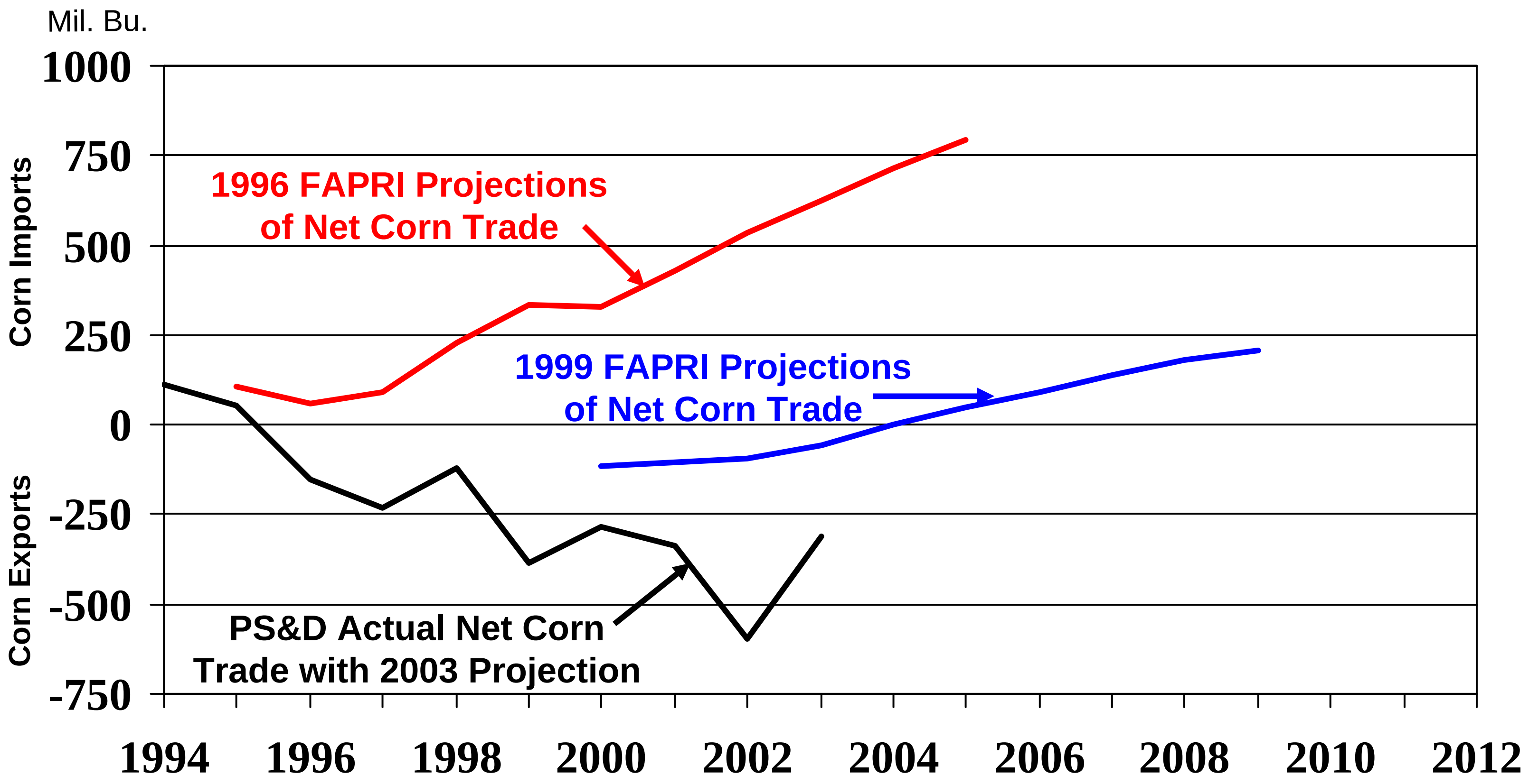
- All three were eliminated because of expectations—expectations that:
- **Exports would drive agricultural growth and prosperity, besides that…**
- *If markets are allowed to be allowed to work agriculture will do just fine*

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



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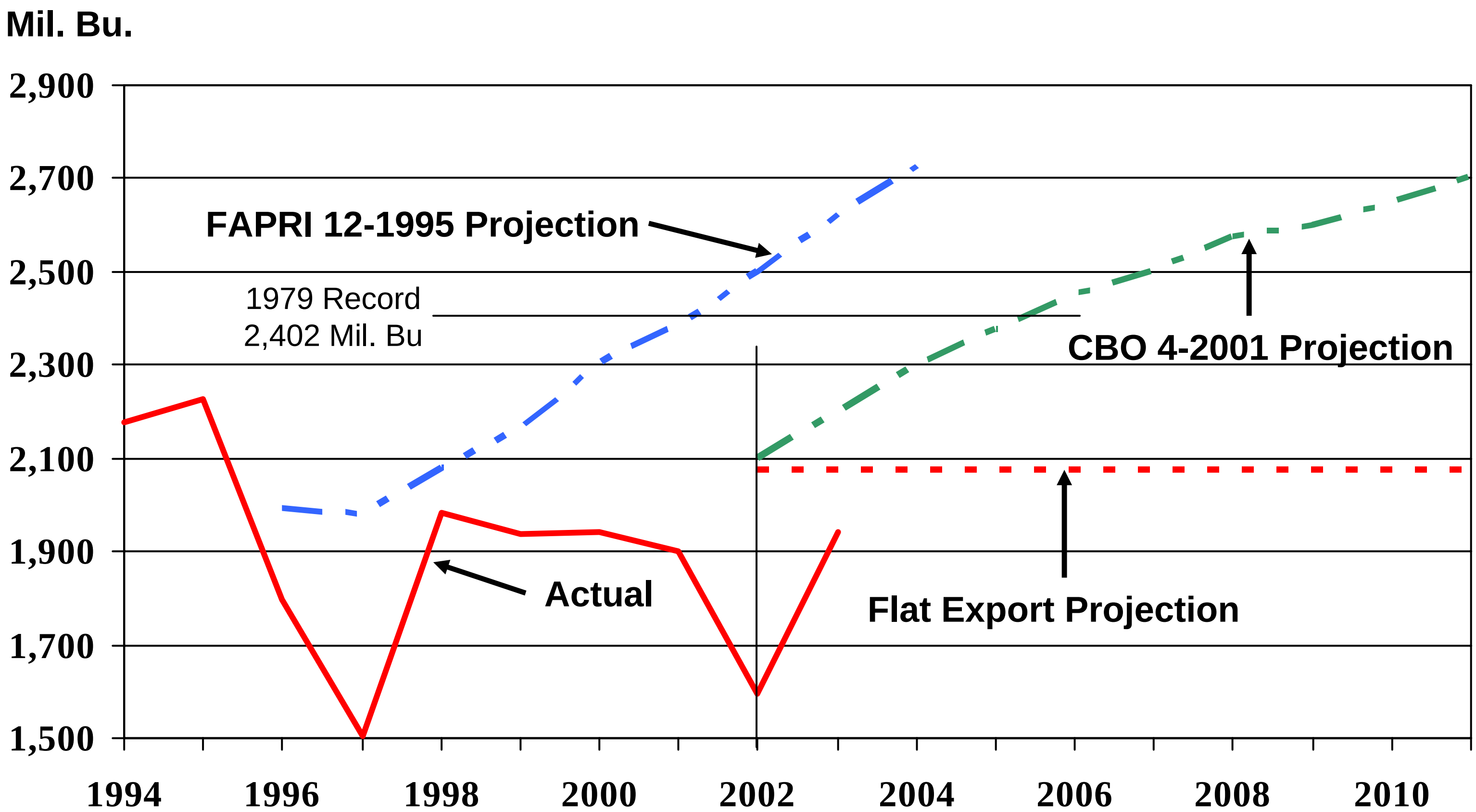
Corn Baseline Projections

U.S. Exports



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Expectations vs. Experience

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

Experience:

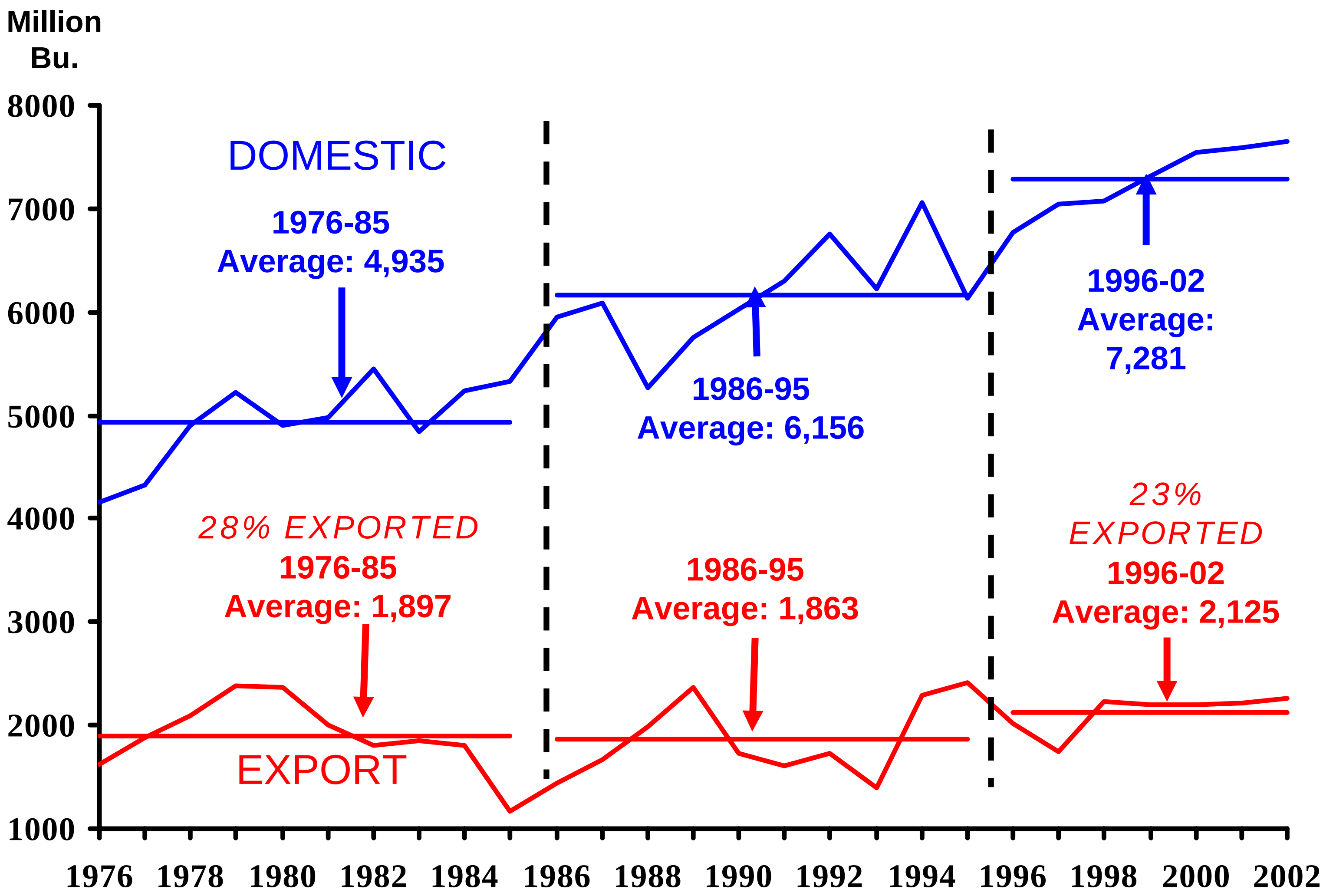
China exported over 500 million bushels of corn in 2002 crop year and over 300 million bushels in 2003 crop year

Expectations vs. Experience

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

U.S. Net Domestic and Net Export Demand

Adjusted for corn fed to import and export beef, pork, and broilers



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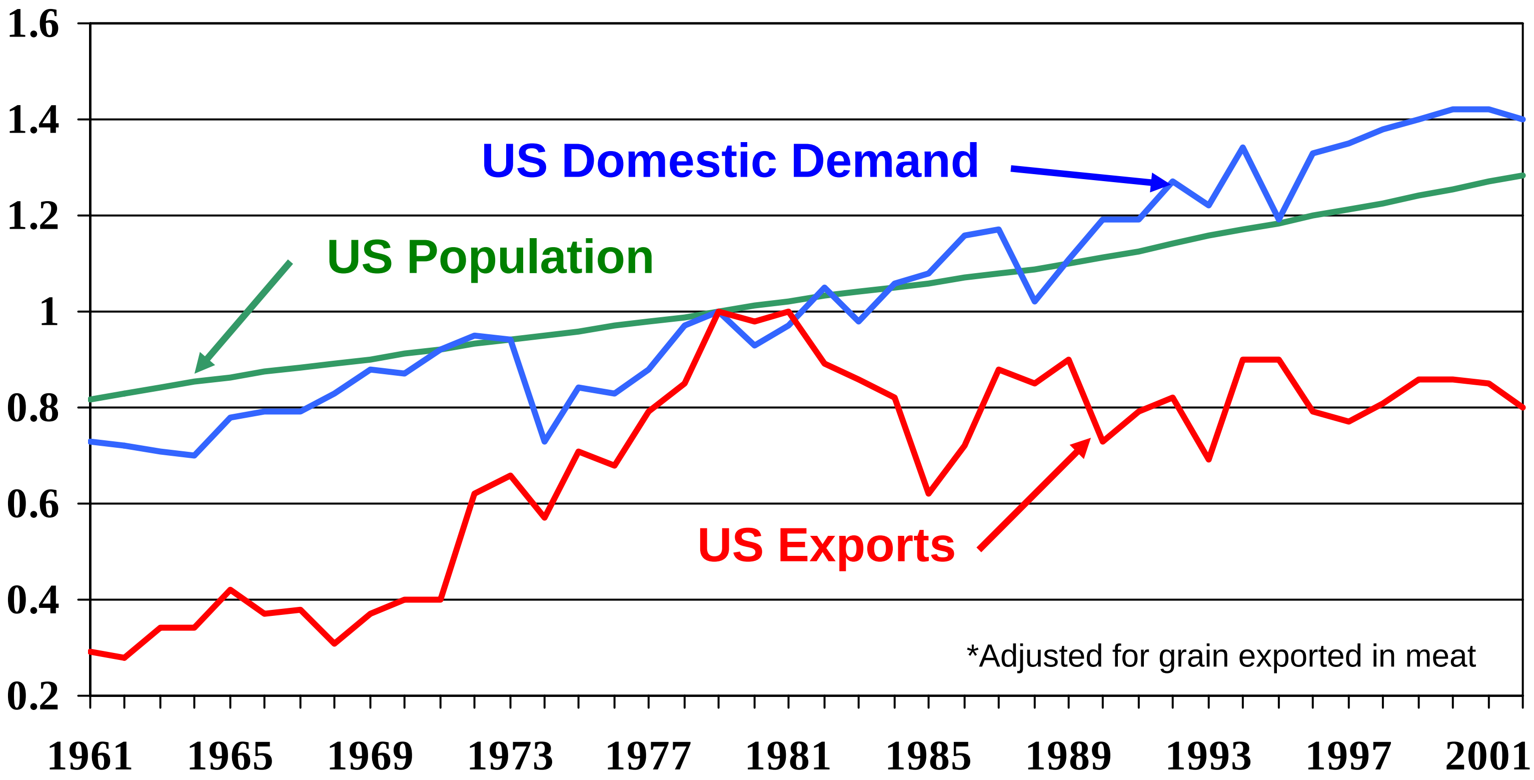
Source: USDA PS&D Database

Exports Did Not Deliver



Index of US Population, US Demand for 8 Crops and US Exports* of 8 Crops 1979=1.00

- **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**

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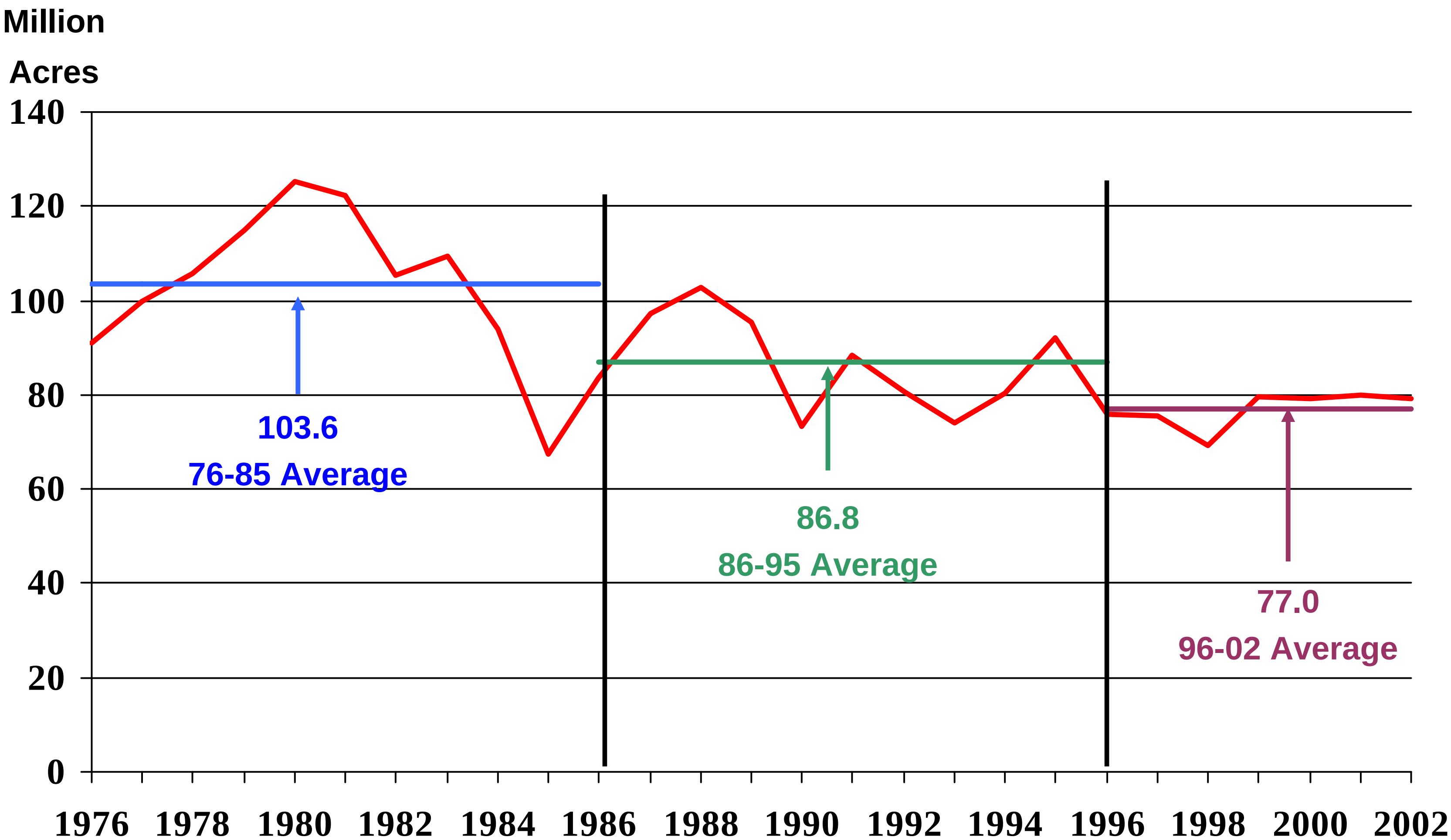
Net Export Acreage for 8 Major Crops



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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 no acreage set-asides and use of direct payments in US, competitors would not be under the US price support umbrella—would reduce production as needed

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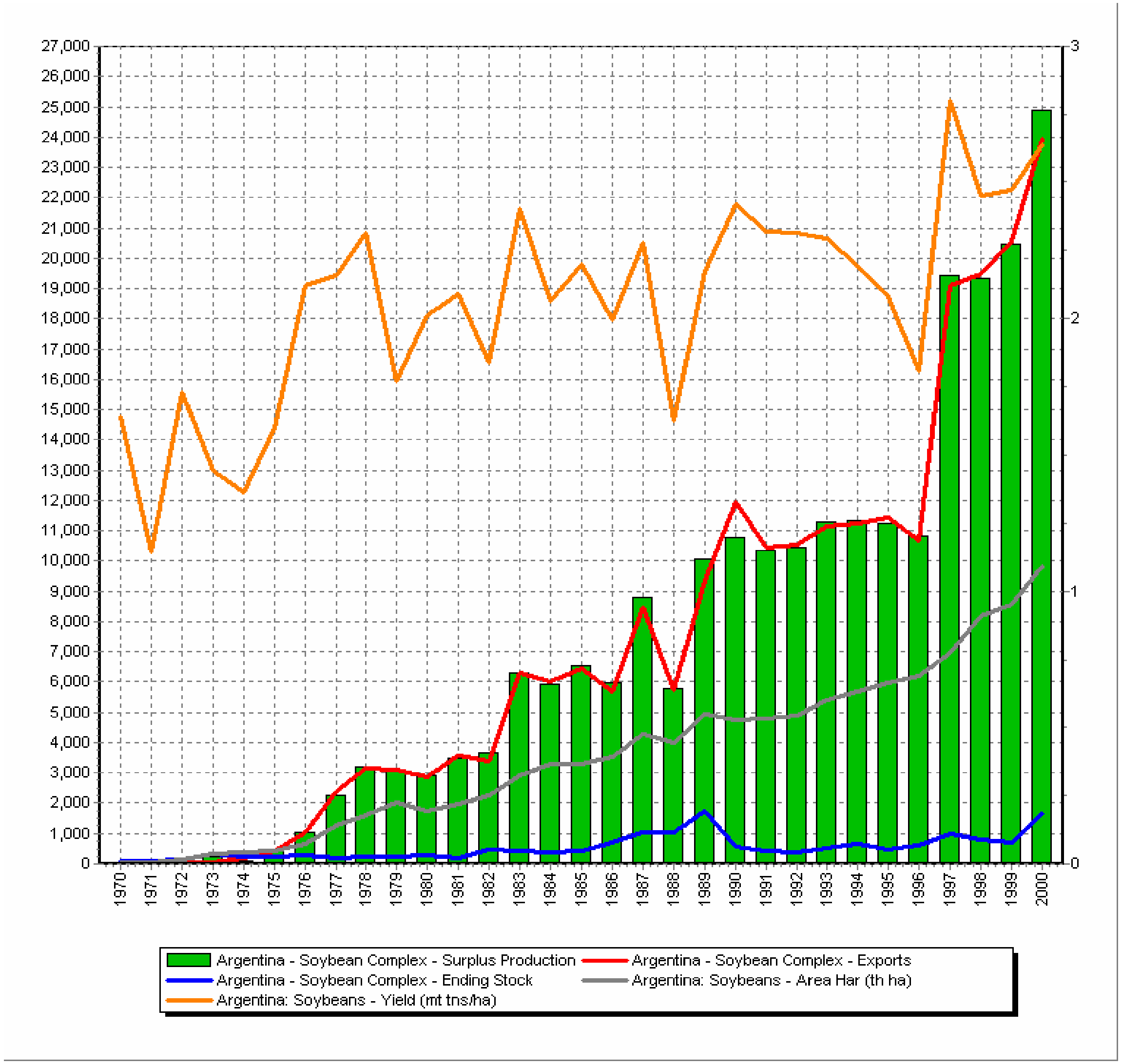
Argentine Soybean Complex Exportable Surplus and Exports



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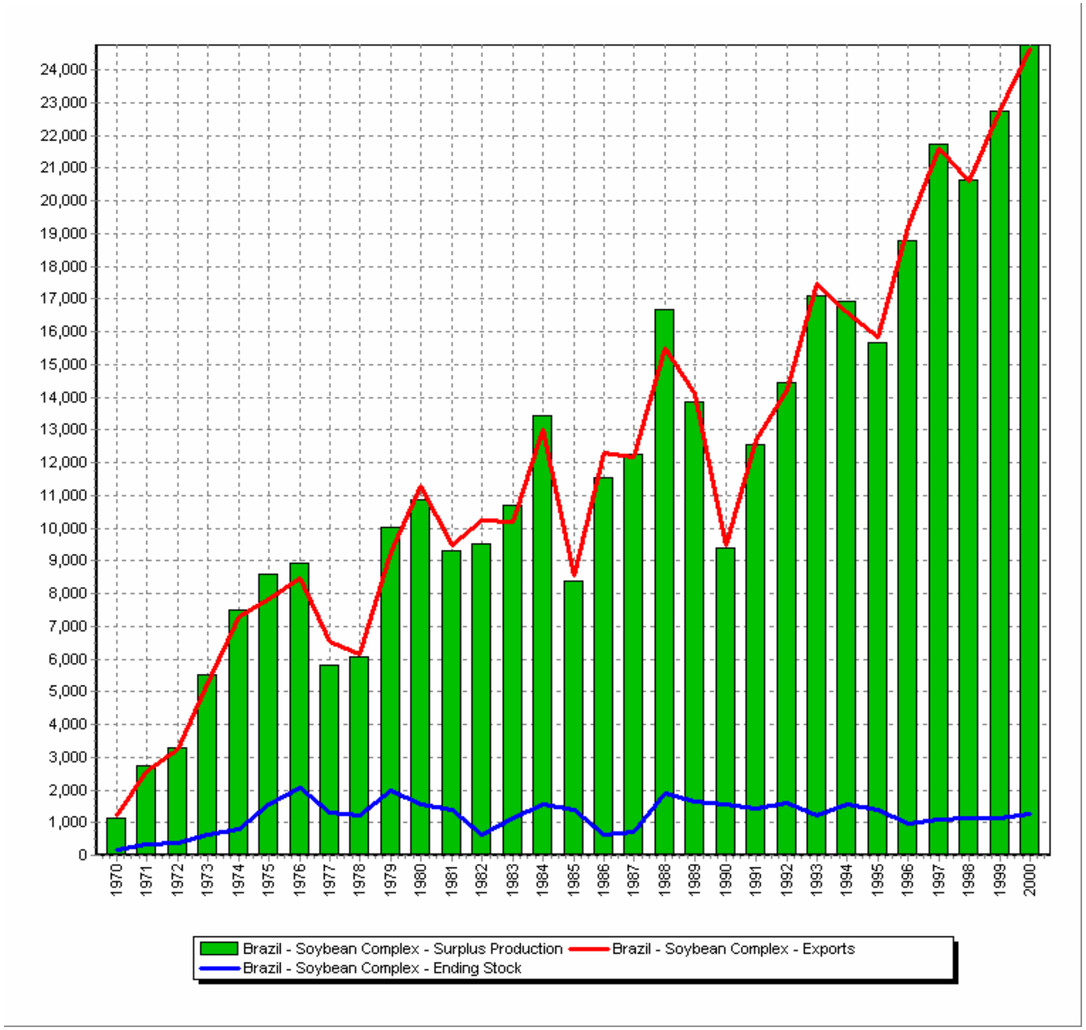
Brazilian Soybean Complex Exportable Surplus and Exports



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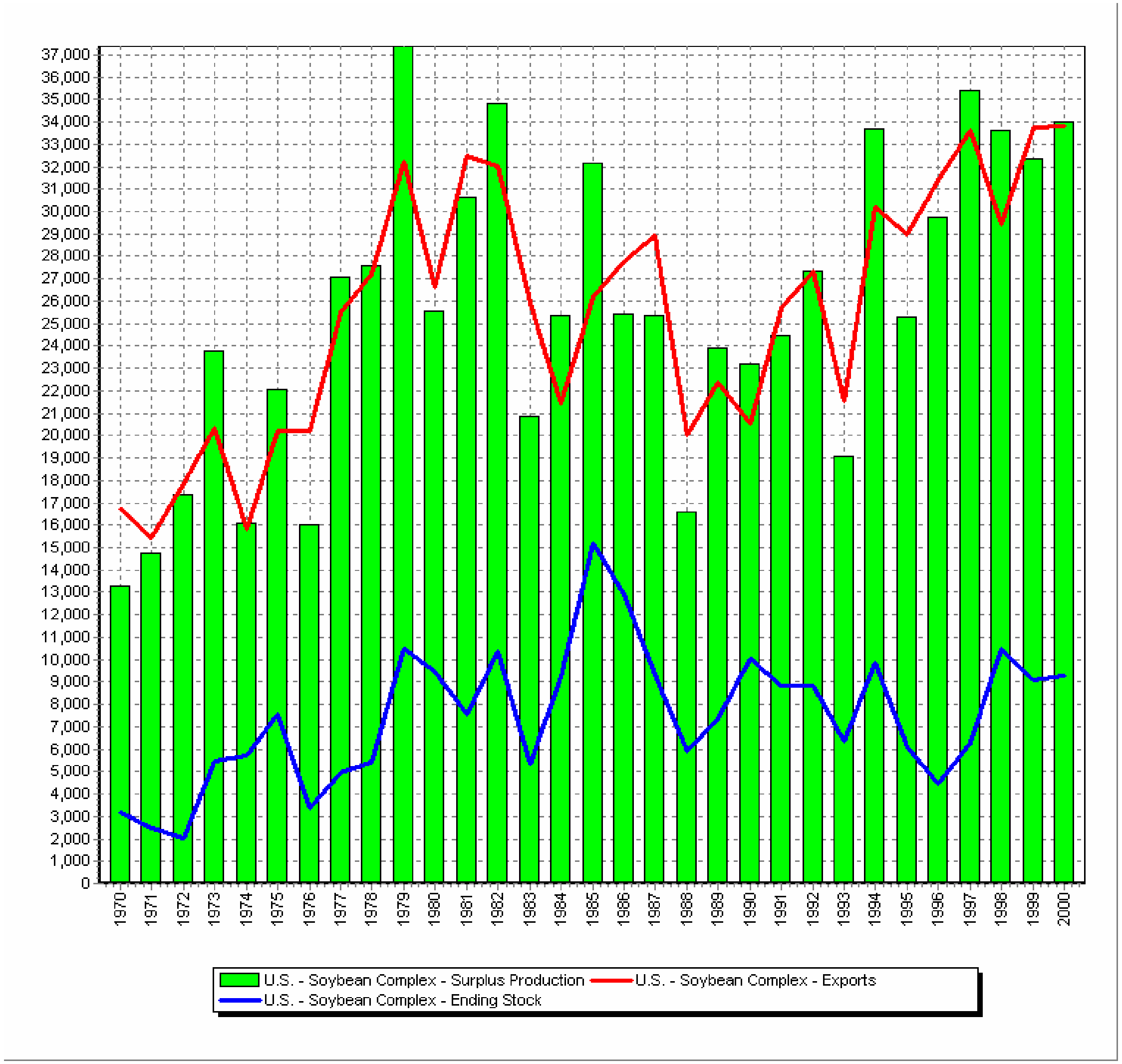
U.S. Soybean Complex Exportable Surplus and Exports



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Expectations vs. Experience

Expectation: With no acreage set-asides and use of direct payments in US, competitors would not be under the US price support umbrella—would reduce production as needed

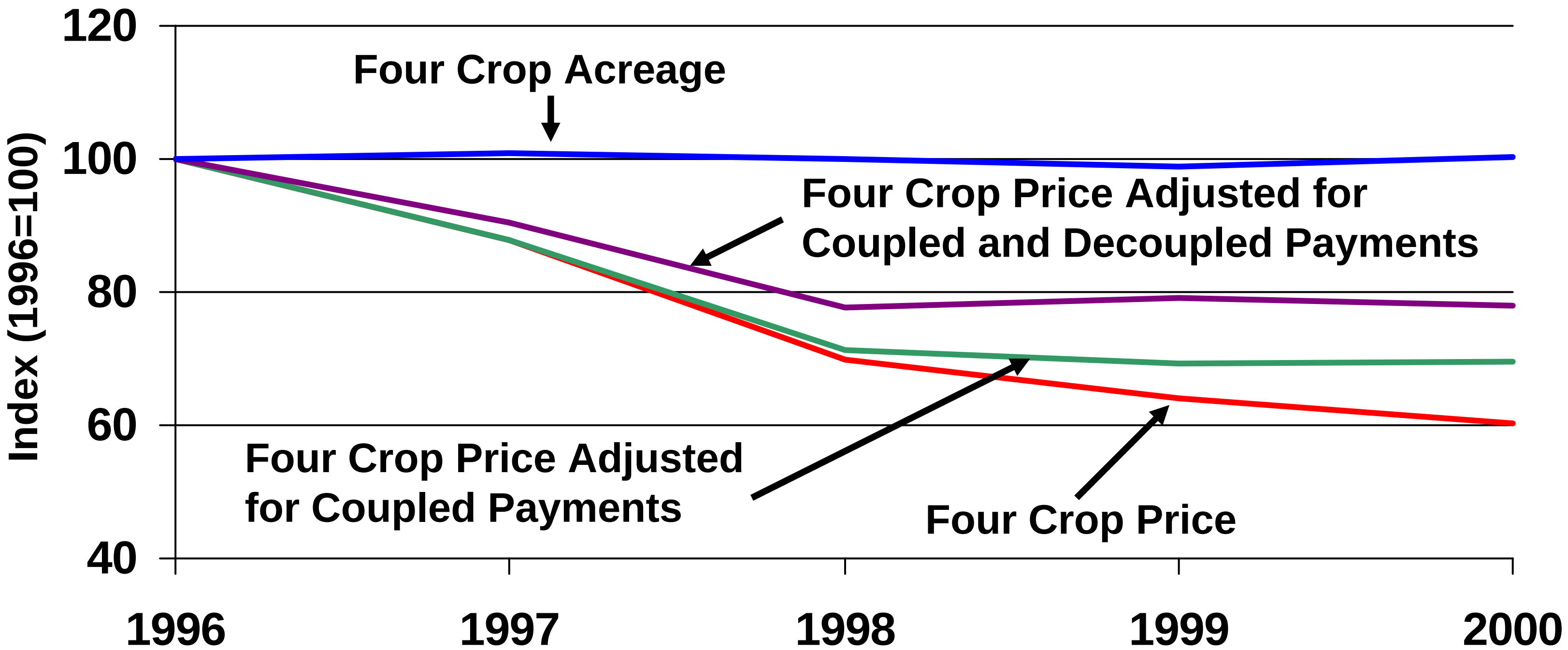
Experience:

- 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 US farmers would plant for the market – reduce production when needed

Acreage Response to Lower Prices?



Since 1996

- **Aggregate US corn, wheat, soybean, and cotton acreage changed little**
- **While "prices" (take your pick) dropped by 40, 30 or 22%**

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Expectations vs. Experience

Expectation: With planting flexibility & decoupled payments US 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

Food and Agriculture ARE Different

- **Why doesn't the invisible hand work?**
- **Food is a necessity for life**
  - Must be consumed on a regular basis
  - Cannot drop out of market until price falls
- **Surplus production is** ALWAYS **preferable to famine**
- **Food is a biological process dependent on uncertain things like rain, sunshine, and wind**

Food and Agriculture ARE Different

- **Taxpayer financed expansion of agricultural output**
  - Free or near free distribution of land
  - Yield increasing technologies
  - Cost decreasing technologies
  - Nationwide system of experiment stations, land grant universities and extension service

Food and Agriculture ARE Different

- Productive capacity of agriculture determined by these public investments
- In other industries, the largest firms often decide how much to increase productive capacity
- Farmers must use latest technology
- Continued expansion of agriculture's productive capacity is a good thing

Food and Agriculture ARE Different

- **Food demand expands little with income**
- **Quantity demanded changes little with price**
- **Aggregate crop output changes little with price**
  - Farmers use all their productive capacity all of the time
  - Farmers cannot influence the price

Food and Agriculture *ARE Different*

- **Other industries would throttle back production and/or decrease productive capacity**
- **Farmers go out of business but the** LAND **stays in production**
- **Chronic price and income problems…**
  - Growth in output exceeds growth in demand
  - Price drops
  - But timely self-correction does not occur

Putting it all Together

- **Technology expands output faster than population and exports expand demand**
- **Market failure: lower prices do not solve the problem**
- **Little self-correction on the demand side**
  - People will pay almost anything when food is short
  - Low prices do not induce people to eat more
- **Little self-correction on the supply side**
  - Farmers tend to produce on all their acreage
  - Few alternate uses for most cropland

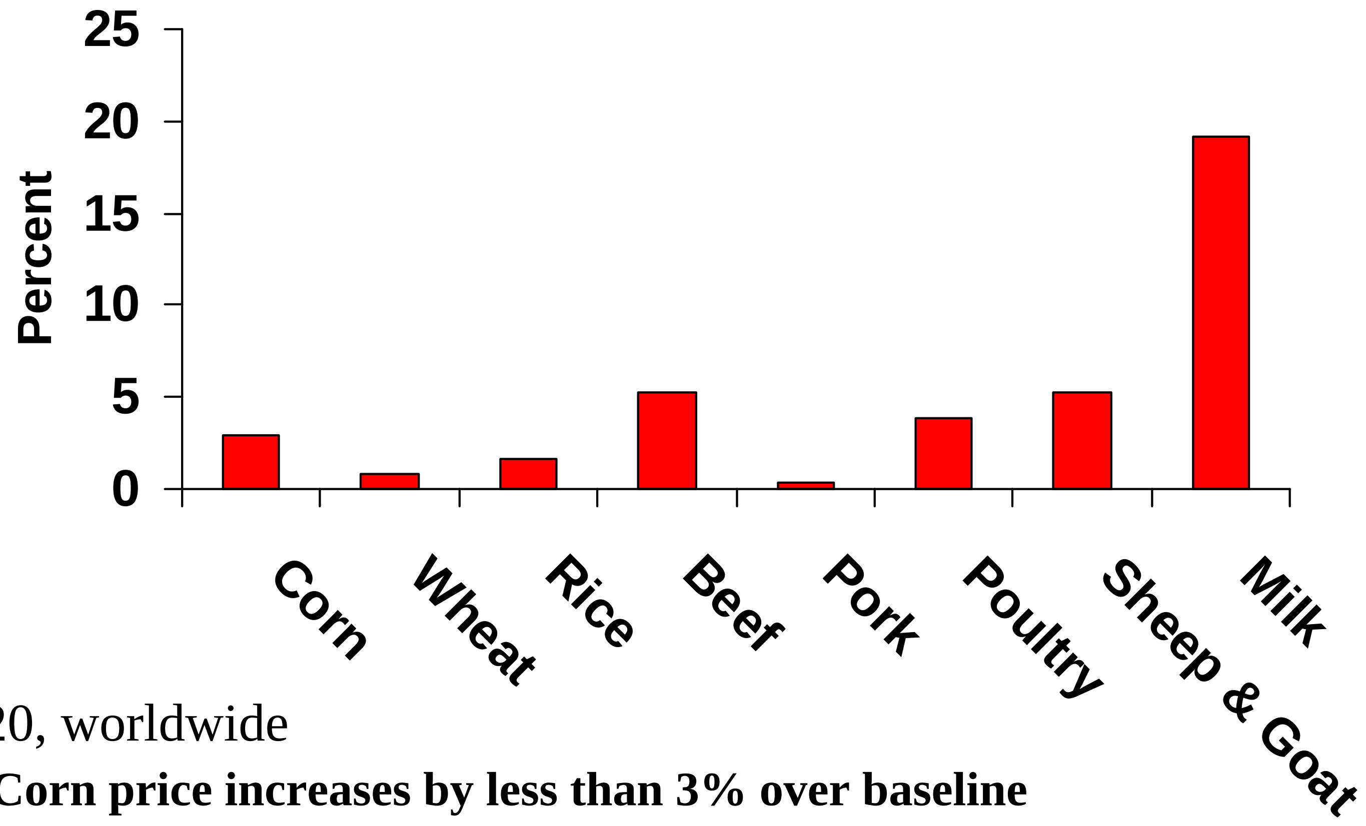
Possible Directions

- **Stay the Course**
- **Intensify the Free Market Prescription**
  - Eliminate trade barriers and government distortions in developed countries only
  - Producers and consumers would be expected to properly adjust to market signals
- **Bring back some traditional farm policy instruments**
- **Move toward dedicated energy crops**
- **Enlist multinational cooperation**

Stay the Course

- **More of the same**
- **Can expect:**
  - Continued low prices: $2 corn; $3 wheat $5 soybeans
  - Continued scheduled large government payments in US and developed world
  - Continued accusations of dumping
  - Continued benefits to livestock, importers and agribusinesses

Intensify Free Markets in Developed Countries



In 2020, worldwide

- **Corn price increases by less than 3% over baseline**
- **Wheat price increases by less than 1% over baseline**
- **Rice price increases by less than 2% over baseline**

IFPRI IMPACT

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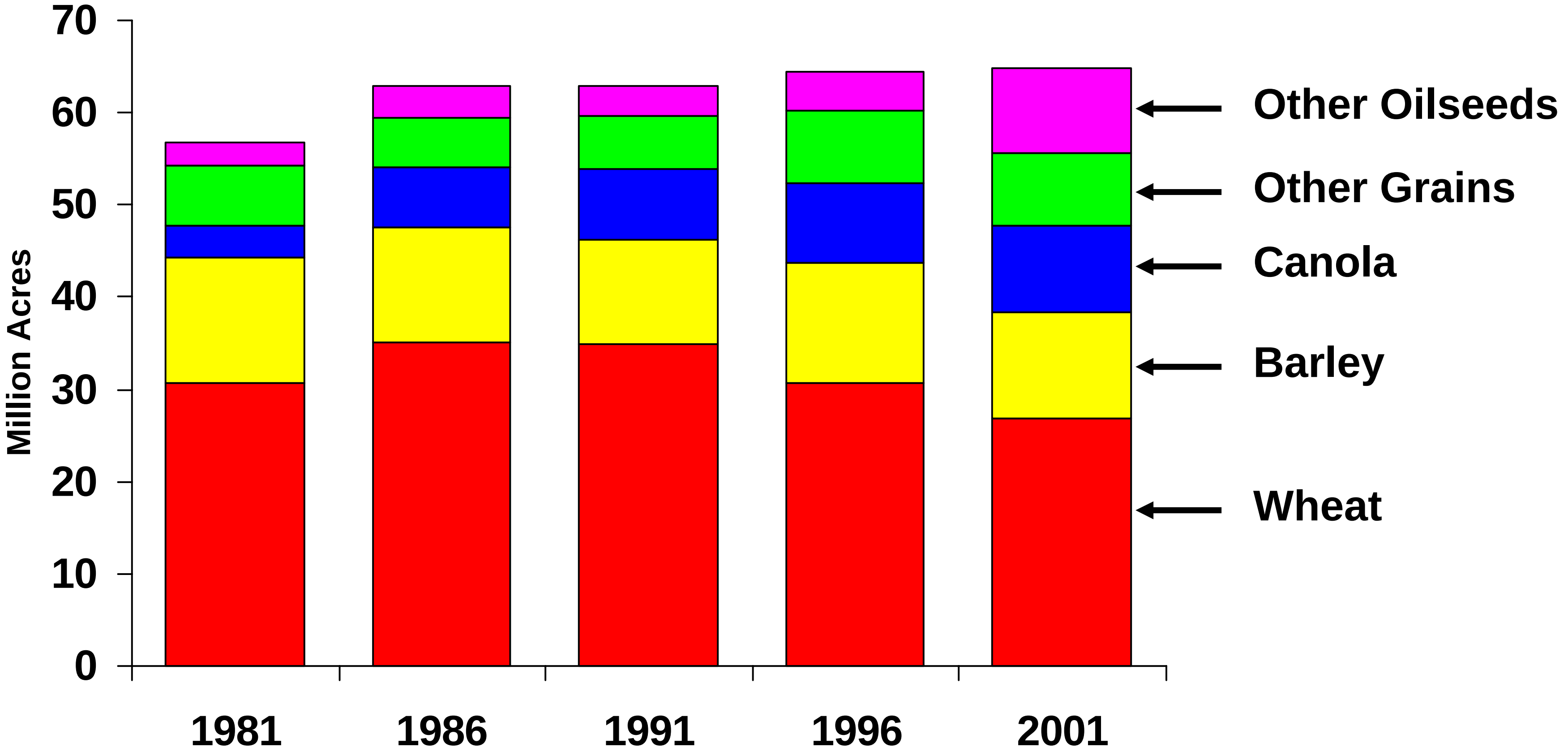
Canada: Farmland Planted



- Canada reduced subsidies in 1990s
- Eliminated grain transportation subsidies in 1995
- Crop mix changed, total acreage remained flat

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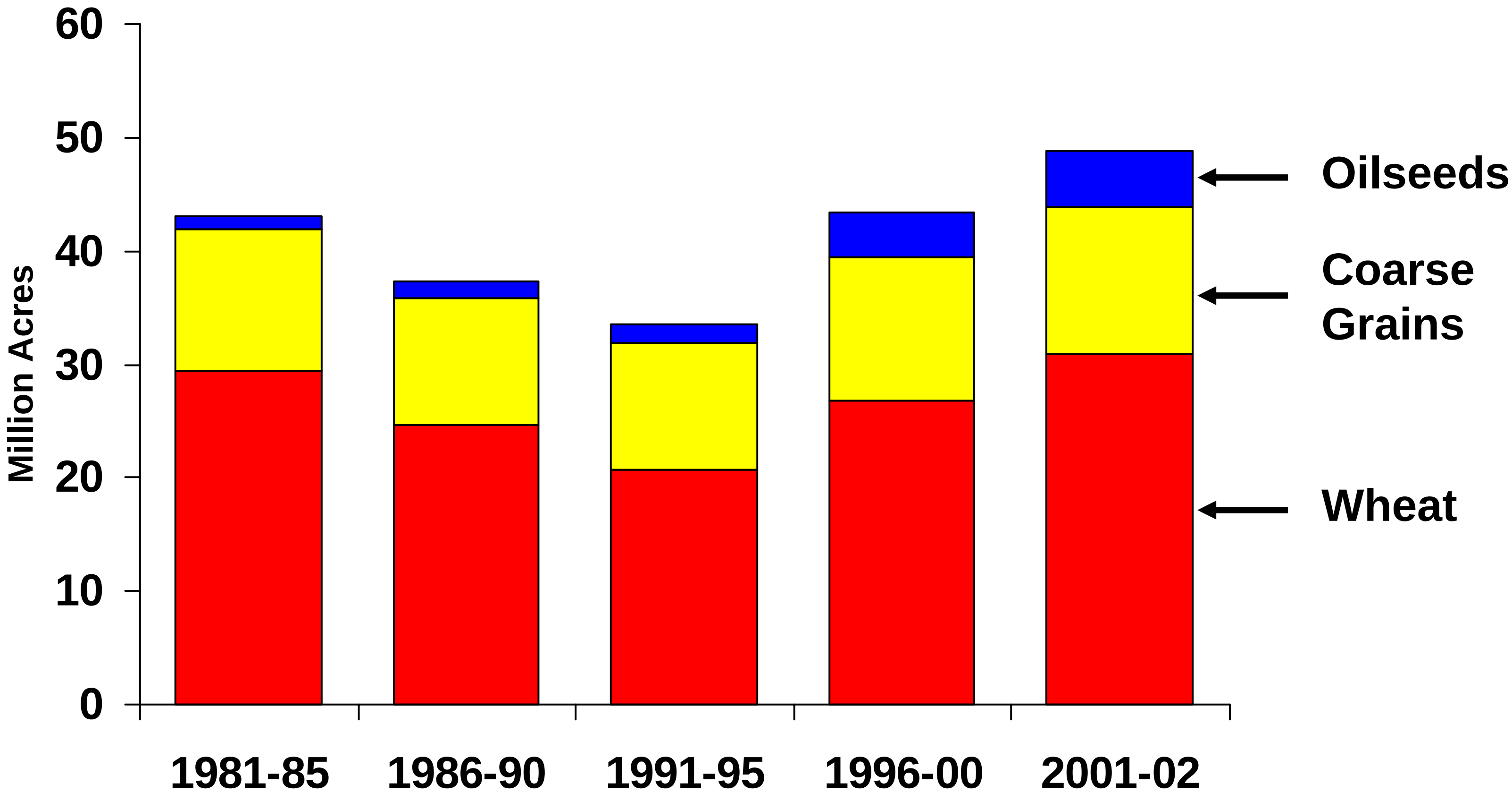
Australia: Farmland Planted



- Australia dramatically reduced wool subsidies in 1991
- Acreage shifted from pasture to crops
- All the while, prices declined

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A More "Managed"

Alternative means of managing crop production could be considered

- **Adding to existing CRP (Conservation Reserve Program) acreage**
- **Creating a shorter-term CRP-like program**
- **Reinstituting:**
  - Annual land withdrawal
  - Inventory/price support programs
- **Energy crops – Could be a win-win-win**

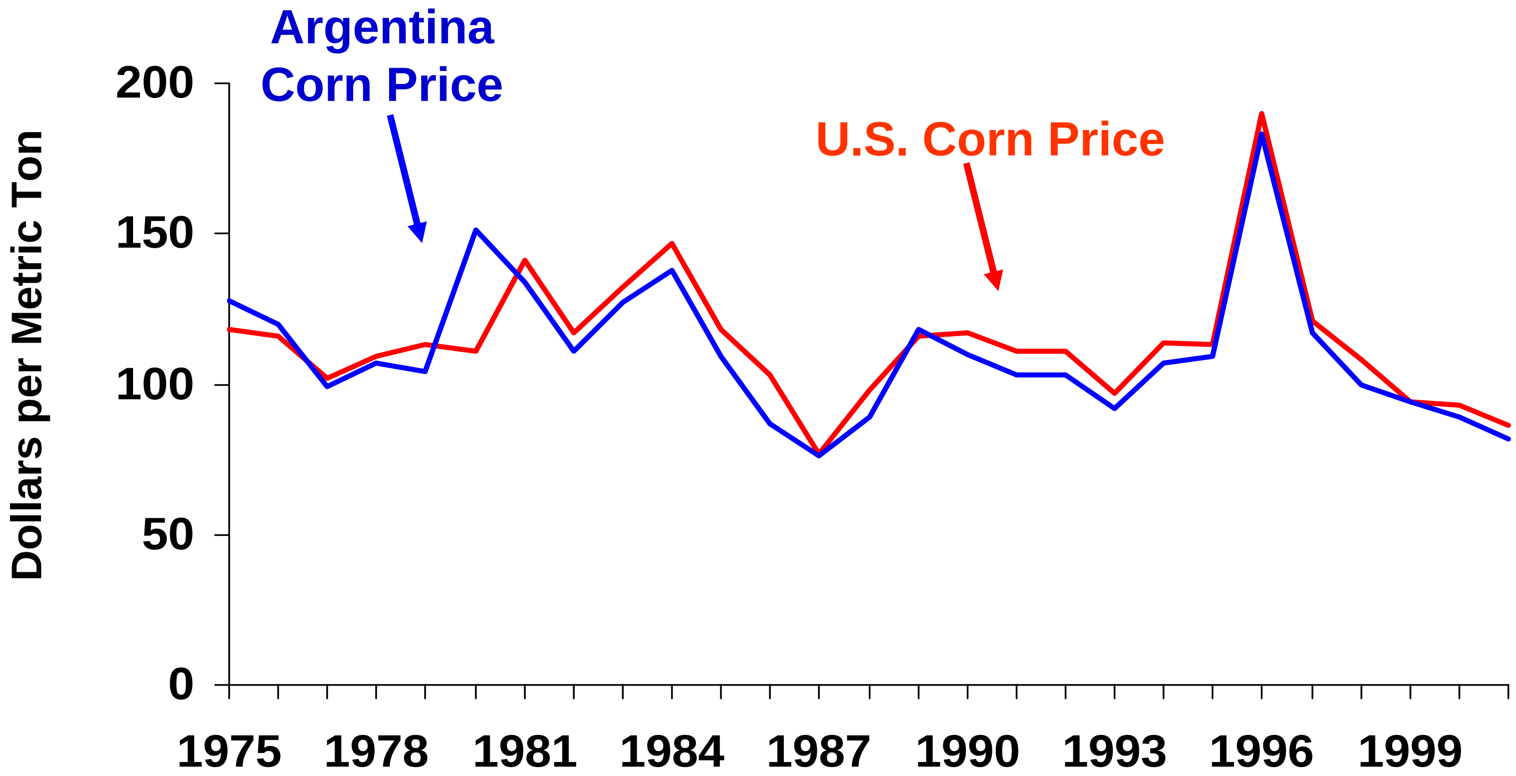
Merge Ag and Energy Policy

- **Biofuels recycle atmospheric, not fossil, carbon**
- **Look at crops not in food equation**
- **Switchgrass**
  - Perennial
  - Reduced inputs
  - Multi-year setaside
  - Burned in boilers for electricity
  - Converted to ethanol
  - Less costly than present ag programs

Multinational Cooperation

- **Excess capacity, not scarcity, is the future of agriculture**
- **Presently the US can still affect prices with supply management**

Corn Price: US and Argentina



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Multinational Cooperation

- Excess capacity, not scarcity, is the future of agriculture
- Presently the US can still affect prices with supply management
- **Sometime in the future this will take multinational cooperation**

Worldwide Excess Capacity Will Be The Long-run Problem

- **Dramatic yield increases in other countries**
  - Cargill, Monsanto, John Deere, etc., etc., etc.
- **Acreage once in production will be brought back in**
  - Russia, Ukraine and others
- **New Acreage**
  - Brazil
  - China

Touchstones

- **Excess capacity is a good thing**
  - We just don’t need to use all of it all the time
- **Managing production is the issue**
- **Total crop demand is not price responsive**
- **Total crop acreage reacts at glacial speed**

Touchstones

- **Most countries view food and agriculture the way we see national defense**
- **Our export competitors are as adamant about keeping their export markets as we are**
- **These “rules of the game” define how agriculture responds**

Thank You

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