The 2018 Farm Program

The announcement by the Trump administration that the United States Department of Agriculture (USDA) budget would be cut by 21 percent came as a surprise given the overwhelming support he received from agricultural counties across the nation. He certainly gave no hint of this level of cuts as he was seeking support in the Iowa Caucuses.

This cut is particularly critical as discussions about the 2018 Farm Bill start heating up. As we have seen in the past, writing a farm bill is particularly difficult when funding is tight. Various interest groups find themselves pitted against each other, delaying the final adoption of the farm bill. One only needs to look at the 2014 Farm Bill to find evidence of this dynamic—the bill was supposed to be adopted in 2012, was extended to cover 2013, and was finally adopted with some major revisions during the lame duck session in early 2014.

An additional factor this year is the low price for all farm commodities and the projection by the USDA that these prices could remain below the cost of production for the next decade. Nothing on the horizon, short of a significant production shortfall somewhere, is likely to change the low-price scenario that the UDSA Baseline Projections laid out and we reviewed in the last three columns.

Revenue insurance is based on the price expected at harvest time and currently the expectation is not good. In addition, farmers need to determine the level of buyup that they want, meaning that only a portion of the production is protected. Most farmers in the corn belt chose the Agricultural Risk Coverage program to protect themselves against a decline in crop revenue only to find that they cannot rely on it as payments are made in one county and not in another even though they all face the same prices. Yield variation from county to county and year to year account for the unpredictable protection from this program.

Thus, many farmers are giving serious thought to working for an enhanced Price Loss Coverage program as part of the 2018 Farm Bill. The problem will be the projected cost of the program over the next decade in the face of the proposed budget cut for the USDA.

Barring a surge in demand or shortfall in production, the only program that will bring prices above the cost of production is a supply management program but modified to allow for planting flexibility. Based on history, setting the loan rate for corn at 95 percent of the full national average cost of production and the loan rate for other crops in their historic price relationship to corn would have a positive impact on the price of all crops. The resulting prices would provide a modest profit for the most efficient farmers and keep the others in business—yield variations could affect who falls into which category in a given year.

The advantage of this type of program is that the market pays for the cost of the crops and the government does not have to provide large but inadequate payments. Despite the large government payments in the 1998-2001 period, most farmers lost money—for many states and thus many farmers direct government payments were over 100 percent of net farm income—and few expect to see payments like those this time around.

If history is any indication, a portion of farmers would take out a 9-month loan on their 2017 crops. At the end of the loan period, it would be a reasonable to expect that farmers would forfeit about a billion bushels of corn to the government (through the Commodity Credit Corporation) reducing the commercial year-end carryout to about a billion bushels. If the release price were set at 175% of the loan rate, the market would have an adequate price range within which to efficiently allocate commodity supplies among competing users.

While the government would incur an initial cost in taking some of the crop off the market, government outlays would be repaid in a year like 2012 when a drought struck a wide swath of the US corn belt. Such an event would increase in the market price above 175 percent of the loan rate and would trigger the sale of the stocks at a profit to the government, covering the initial cost of acquisition, interest on the loans related to the forfeited commodity, as well as other program costs.

If the government stocks became too large, then the USDA would determine the desired reduction in production needed to keep from acquiring additional stocks. Farmers would be invited to bid acreage into a production reduction program. Priority would be given to environmental benefits and it is expected that farmers would offer bids on their least productive, most environmentally challenged acres.

Farmers who are farming the most productive ground and those opposed to nearly any government program would be free to not offer a bid on any of their acres. By using a bid process and the expectation that the largest farmers on the most productive ground would not participate to any significant extent, the program avoids one of the major criticisms made of current programs: most of the payments go to the largest producers, but provide little benefit to the smallest producers.

By affecting price, all farmers, large and small, benefit from the program. By targeting the production reduction program to provide the greatest environmental benefit those funds that are spent provide a public good.

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