Low-price farm policy has not delivered on its promise of export-led prosperity

In the supply management program that we outlined in last week's column (https://tinyurl.com/yd8eb9rp), the loan rate was set at 95 percent of the full cost of production for corn, with the loan rate for other crops set at the historic price ratio of those crops to corn. It has been argued that setting the loan rate so high has the effect of reducing the competitiveness of US exports in the international markets.

It has been our observation that despite more than 30 years of low-loan-rate/low-price policies, the export of all major US crops, except for soybeans, has languished, with the US share of the export market in significant decline—soybeans included. Simply put, the low-price policies have not delivered on the promise of an export-led era of prosperity for US farmers.

So why is that? Certainly, low prices ought to make the US more competitive! Let's look further.

To understand this conundrum, we need to begin by recognizing that the US is the oligopoly price leader for the major agricultural crops grown in the US and their substitutes. The market itself is oligopolistic because for each crop and its substitutes there is a limited number of countries that, taken together, account for most of the world's exports.

In an oligopolistic market, whether it is countries or companies, market participants sooner or later fall into a follow-the-leader pattern when it comes to price. Those who follow make their sales at prices that are slightly below the price offered by the price leader and clear their markets leaving the remaining sales to the price leader. In this case the oligopoly price leader is also the residual supplier.

If we look at the pattern of crop exports since 1981, it becomes clear that the US is the oligopoly price leader and the residual supplier for the major crops—corn, cotton, rice, soybeans, and wheat—and their substitutes. So why is this?

Since the end of WWII, the US has taken on the role as the world's dominant military, political, and economic power.

One of the results of that in the arena of agricultural economics is that prices for major commodities are established in US venues like the Chicago Mercantile Exchange, the New York Mercantile Exchange, and the Kansas City Board of Trade. But the presence of these exchanges alone would probably not be crucial in the price-setting mechanism if it were not for five other factors.

First, US production of the five major crops was and is sufficient to support the development and maintenance of these exchanges. Second, the unit by which price is measured on these exchanges is the US dollar which is the world's benchmark currency. Third, when it comes to the five major crops, the US consistently produces a surplus of these crops beyond domestic demand—the US is a reliable source of these crops. Fourth, the US has the infrastructure to store these crops for significant periods of time; spoilage is not a significant risk. Fifth, supply and demand estimates for the US are more transparent than similar figures for a major producer/consumer like China.

As a result, changes in US production and year-ending supplies have more impact on the prices set on these markets than changes elsewhere in the world.

We would argue that it is a fool's errand for US policy makers to continue to pursue a low-price-and-exports-will-be-agriculture's-savior policy. When all is said and done, such a policy is not in the interest of US farmers or taxpayers.

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