PolicyPennings by Dr. Daryll E. Ray

Devolution: A desirable revolution or impossible solution

In our recent column we gave an overview of a USDA report titled, "A Consideration of the Devolution of Federal Agricultural Policy" (http://www.ers.usda.gov/publications/AER836/). In that column we traced the history of the idea of devolution, that is the turning over of federal funds and/or responsibility for what once were federal programs to the states. In this report, the authors examine the concept and make a recommendation on the programs they think are candidates for devolution.

At the end of their analysis, the report's authors identify the $22 billion currently targeted toward farm programs including direct payments, loan deficiency payments, and counter-cyclical payments as the starting point for devolution. Instead of dividing that money up according to the current farm programs which for the most part target storable commodities, the money would be divided up among the states and the states would be free to spend that money on the rural and agricultural sector according to their own priorities. That would mean no more commodity programs, disaster payments, or emergency programs. The responsibility for those issues would rest with the individual states.

The report comes to this conclusion in part based on the goals they identify as underlying current agricultural programs. These goals include "equalizing the distribution of income by measures related to landholdings; stabilizing farm incomes; achieving rural development; saving family farming; . . . [and] increasing price supports, deficiency payments, or other transfers to make current farmers more wealthy. . ." If the goal of U.S. federal farm programs in general and commodity programs in particular are "to make current farmers more wealthy," then we have no problem with the idea of devolution of farm programs. Go for it!!

On the other hand, that is not what we thought farm programs were all about. That is not why they came into being in the 1930s. These programs came into being because of the unique characteristics of crop agriculture; the characteristics that make it different from, say, used car sales. In used car sales, if the dealer wants to move a vehicle off the lot, he reduces the price until it attracts a buyer. The market clears. The car may go to a family that then sends their old car to the junk yard. It may go to someone who gives it to their teenager as a first car. Or, if the car is old enough and the price is low enough it will go directly to the junk yard to be converted into scrap metal. In any case, a low price causes the market to clear.

In crop agriculture, on the other hand, low prices do not clear the marketplace of extra foodstuffs. Just because prices are low, people don't begin to eat four or five meals a day. Overall food demand is relatively inelastic. If the commodity price drops families may purchase more highly processed foods or eat out more often, but the total food intake does not increase significantly, especially in the short to medium run. Food that is produced in excess of a given year's demand is carried over into the following year, depressing that year's market price as well.

On the production side of the equation, in response to low prices, farmers do not significantly reduce the total acreage planted to crops. They may change the mix of crops in an attempt to maximize income and profit, but it is rare that farmers will deliberately let an acre of cropland stand idle. The farmer has no incentive to allow cropland to remain idle. As long as the price the farmer receives covers the variable cost of production, the rational thing to do is put the crop in. Besides that, this might be the year when there is a crop failure somewhere else in the farm belt and the only way to cash in on the high prices is to have a crop in the field.

Back to our used car illustration, we need to remember that every used car was once a new car. And Chrysler does not produce cars to sit around unsold. In a tight market, Chrysler holds back on production, reduces or eliminates over time, idles a plant for a week or two. If it is not going to sell, they don't produce it.

Because there are a limited number of firms in the business of producing cars, any one individual firm has some impact on total production. The same is not true of farmers.

If sales pick up, Chrysler can ramp up production in a matter of days and have the cars on the dealer's lot in a matter of weeks. The same is not true of farmers. The farmer has only one chance to determine the year's production potential – planting time. If she misses that window, it is a whole year until she has another decision opportunity.

In the past, farm programs were established to provide a means of doing what industrial firms do every day of the year: manage production. In the past under production management programs, the Secretary of Agriculture served as the de facto CEO of American agriculture and gauged production to demand, thus stabilizing prices and assuring markets of a steady, reliable supply of food and fiber.

In our view, this is not a function that can be devolved to the states. It will not work well if Iowa establishes programs to manage the supply of foodstuffs, while Illinois decides to encourage all out production. It only makes sense for this function to be carried out at the federal level.

Despite what some people may argue, the goal of US agricultural policy is not to make farmers wealthy. It should be designed to address very specific market failures, in the interest not only of farmers, but consumers as well. In the long run, consumers benefit from a long term, stable supply of food produced at a reasonable price.

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