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PolicyPennings by Dr. Daryll E. Ray

Farm commodity policy: Cost is an issue

The three previous columns examined the reasons one might use to justify the elimination of key elements of the U.S. farm program if President Bush's proposal for the developed nations to reduce their farm subsidies by $120 billion a year were to be taken seriously. Given Bush's proposal, U.S. budget pressures, the Brazil WTO cotton case, and the colored box issues of trade negotiations, it is clear that one of the forces that will contribute to the shaping of the 2007 Farm Bill debate is the need to reduce and/or reshape subsidies and the cost of agricultural programs in the U.S.

At this point it would appear that the question is not whether agriculture's budget will be cut, but rather how much? Can we cut as much as $10 billion from the agriculture budget without devastating production agriculture for crops in the U.S.? From our perspective, the answer is yes, but we need to do it properly.

Before looking at how we might do that, let us take a few moments and review our analysis of direct payments, Loan Deficiency Payments/Marketing Loan Gains (LDP/MLGs), and counter-cyclical payments (CCPs). One of the ways to look at the impact of those programs is to "follow the money." Who benefits from the payments that are being made under current legislation?

In the case of direct payments, most of the benefits are ultimately captured by landowners as rents and land prices increase. Bankers also benefit as they encumber the direct payments as a condition for making operating loans to farmers. High land prices make it more difficult for young families to begin farming. This program also costs the taxpayer because direct payments are made whether commodity prices are high or low.

With LDP/ MLGs, farmers are a conduit through which the money flows from the government to livestock integrators, grain and seed processors, and importing countries as these groups are provided with crops at well below the cost of production. Farmers receive little more than they would if they were to receive their income from the marketplace instead of the mailbox. The suppliers of agricultural inputs also benefit because, without setasides, farmers plant crops on their full acreage. The losers include U.S. taxpayers who end up paying the tab and producers in the rest of the world who end up facing the low prices without a government safety net.

Having said that, we want to point out that it is just as much of a problem to think that if we were to eliminate all agricultural programs, crop agriculture would adjust supply and prices would recover. But, total supply adjusts very little and prices will not recover in a timely fashion because (1) low prices do not cause consumers to eat five or six full meals a day, and (2) low prices do not cause farmers to significantly reduce their production. Therefore a farm program that does not take this reality into consideration is likely to be very expensive and/or not achieve income stabilizing goals.

The Agricultural Policy Analysis Center has looked at a series of farm policy alternatives that ranged from doing nothing to reintroducing some previous policy mechanisms to totally new approaches. Several of the analyses indicated that farmers could receive more of their income from the marketplace and less from the government while maintaining annual net farm income in the $46 to $53 billion range while reducing annual government payments to between $5.8 and $8.1 billion – a far cry from the $20 billion currently budgeted.

In future columns we will provide summaries of those analyses. One thing that seems clear from the work done so far: farm policy objectives can be achieved for a lot less cost and with less price distortion than current legislation.

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