# Farm program considerations: Part 5

The 2014 Farm Bill that establishes current farm programs will come up for renewal in 2018 which means identifying problems with current farm programs and thinking about those that would be more effective for farmers, consumers, and the federal government before Congress gets serious about writing the legislation. In this series of columns, we have identified the economic reason for farm programs and proposed returning to a supply management program that builds on what we have learned from past programs.

A key element of supply management is to take excess storable commodities off the market by way of a nonrecourse loan program when prices fall below the loan rate and then release these reserve stocks back into the market when prices exceed a release price. A key task is to identify who would hold these reserve stocks.

In the debate over the 1996 Farm Bill, which eliminated the supply management program, and in the agricultural economics literature in subsequent years, it was argued that if there is a need for reserve stocks, commercial concerns would treat that need like any other crop demand and hold those stocks so they could sell them in the future at a higher price.

For the most part, that is not true. What is true is the argument that was made that government stocks substitute for some commercial stocks. Non-farm commercial demanders do hold somewhat lower stocks when they know that they can rely on a government reserve in a pinch.

But these commercial firms do not hold stocks at a level that would stabilize prices at a level at or near the long-run production costs of the most efficient producers.

But more than that, the level of commercial stocks carried over from 2011 did not prevent the price of a bushel of corn from exceeding $7.00 at points during the 2012 corn marketing year when production dropped by 13 percent—yield declined by 16 percent—as the result of widespread drought across the corn belt. Nor did the level of carryover stocks prevent US corn exports from falling by 53 percent during the 2012 crop year, raising questions about the role of the US as a reliable supplier.

While commercial firms will hold somewhat higher stocks in the absence of government stocks, they have no need to carry the stock level necessary to meet a production problem like we saw in 2012. They can protect themselves from higher prices by purchasing a futures contract and saving storage costs for an occasional event. And most of the difference in commercial stock holding is by farmers not non-farm commercial users.

In the absence of government programs, farmers end up holding the excess stocks as we saw in the 1998 through 2001 crop years. Once corn stocks, mostly on-farm, doubled between 1996 and 1998, farm prices fell below $2.00 and remained there even though carryover stocks remained relatively flat for the four-year period.

It took a 6.3 percent yield decline in 2002 to move prices above $2.30, though the price fell back to $2.06 two years later. Farmers were rescued in 2006 only because of the government-instituted ethanol mandate and a yearly increase in the amount of corn needed by ethanol plants. The ethanol mandate was the result of intense lobbying by corn farmers, though other crops benefitted as well.

So now we have determined that in the absence of a fairly large yield decline—and even that does not work if the previous year saw a good increase—or government action, neither non-farm commercial stock holding nor farmer stock holding can maintain a break-even price. In addition, these market participants do not hold stocks sufficient to meet demand when corn production falls more than 8 or 10 percent.

That leaves government as the only stabilizing force in maintaining crop prices that are at or above the cost-of-production for the most efficient producers. Historically the government has achieved this stability either by holding the stocks in a government-bonded warehouse or in a farmer-owned reserve or both. Next week we will talk about the advantages and disadvantages of each along with some additional issues.

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