Impressions vs. reality: A look at the first two years of the FAIR Act

It is commonly believed that the 1996 FAIR Act, which was enacted at a time of unusually high prices, worked well for its first two years. What we remember about those years is that prices were good and overall farm income was at a comfortable level. Given the nature of the debate leading up to the adoption of the act, it would be natural to believe the reason prices were good was because of strengthened exports.

Let's see if the data squares with our impressions.

It is ironic that the run-up in crop prices that helped coalesce legislative support for the 1996 FAIR Act peaked about the time the legislation was signed into law. Generally, prices began their drop soon thereafter, and in some cases, the early declines were abrupt and severe. For example, the closing corn futures price for the nearest contract month for the week ending July 12, 1996 was $5.38 per bushel but dropped to $3.58 per bushel for the week ending August 2, 1996, a $1.80 decline in three weeks.

In the case of wheat, the peak came in the month the FAIR Act was signed. The wheat closing futures price for the nearest contract month for the week ending April 26 was $7.16 per bushel. Six weeks later the comparable price had dropped more than $2.00 per bushel to $5.00.

The 1996 peak weekly closing futures price for cotton was 87.25 cents per pound on January 26 and by June 28, it had dropped to 70.65 cents per pound. It should be noted that cotton prices had been over $1.00 per pound during the Spring of 1995.

Corresponding ending weeks and prices for soybeans were July 12, $8.40 per bushel, and July 26, $7.63. Unlike other crops, the soybean price rose above its 1996 peak during portions of calendar year 1997.

Note that, with the exception of soybeans and rice, crop prices for the eight major crops reached their record high levels before the FAIR Act took effect. Although the law was signed April 4 1996, the 1996 crop year—the first crop year governed by the act—did not begin until later in 1996: June for wheat, barley and oats; August for soybeans, rice and cotton; and September for corn and grain sorghum. While prices during the 1996 and 1997 marketing years were well above the target prices of previous legislation, the record nominal crop prices, except for soybeans and rice, actually occurred in the 1995 crop year. Soybeans and rice did not realize their recent price highs until the 1996 crop year.

Corn prices were still relatively high in crop years 1996 and 1997 because stocks brought in from the 1995 crop year were the lowest since 1974 and it took a couple of years for stocks to grow sufficiently to push prices down to the levels of 1998 and 1999. Corn exports were not "high" during the high-price crop years of 1996 and 1997; they declined in both these years. Corn exports dropped 400 million bushels in 1996 and another 300 million bushels in1997. It is inaccurate to claim that corn exports bolstered corn prices in the 1996 and 1997 crop years and then the Asian crisis crashed exports and prices in 1998 and 1999.

Wheat and cotton carryin stocks, exports, and prices followed the same general pattern as corn. Wheat stocks brought into the 1996 crop year were extremely low, the lowest since 1973. They were down due to reduced yields in 1994 and 1995 and relatively strong exports during those years. Again, it was low carryin stocks, not growing exports during the first two crop years of the FAIR Act, that provided support to wheat prices during those years. Compared to crop year 1995, wheat exports were down by 200 million bushels in 1996 and 1997. Wheat prices during the first two crop years of the FAIR Act, the two "high" price years so far under FAIR, occurred with a weak export demand.

In the case of cotton, stocks had become depleted by the beginning the 1996 crop year in part because of the near 50 percent increase in 1994 crop year cotton exports, due almost entirely to increased imports by China. In the 1995 crop year, cotton yield was down by over 20 percent and export demand, although down somewhat, remained high by historical standards.

During this general time period, just as in the case of corn and wheat, the maximum season average price and export level for cotton occurred in years governed by the 1990 Farm Bill, with prices and export levels beginning or continuing their decline in the 1996 crop year, the first crop year covered by the new legislation. An exception to this pattern was 1997 cotton exports which recovered from a 11% drop in 1996 only to plummet to its lowest level since 1985 during the 1998 crop year.

The situation for soybeans was generally similar to the other crops and, yet, quite different in some of the specifics. Low soybean stocks were carried into the 1996 crop year but exports did not decline in 1997 and 1998 as they had for corn and wheat. So rather than beginning the steady decline in season average prices in 1996, soybean prices reached their peak in 1997 and began declining in 1998 while exports remained stable to slightly higher. It was the 300 to 500 million bushel increases in soybean production in the crop years after 1996 that caused inventories to expand and crop year prices to begin their trek to levels not seen in three decades.

This journey through the numbers reveals two things.

First, crop prices were "high" during the first two marketing years of the 1996 Act not because exports were strong those years (soybeans being the exception). It was because—on day one—the granaries were empty. The low stocks carried into the 1996 crop year buoyed prices the first two marketing years. After those two years¾with exports continuing to be mediocre, yields and total crop acreage coming in at supply boosting levels and the granaries no longer echoing¾inventories continued to accumulate and prices sliced through most floors envisioned by farmers and others, e.g., $2.00 corn, $3.00 wheat and $5.00 soybeans.

Second, again except for soybeans and rice, prices were not at record levels during the first two years of FAIR as is sometimes implied. The record prices for six of the eight major crops occurred in the last marketing year of the 1990 Farm Bill, during and shortly after the time the 1996 Farm Bill was being debated and prior to the first marketing year the 1996 FAIR Act was in effect. Prices did not wait until the 1998 marketing year to head south, the price declines were well underway by then. In fact, compared to the 1995 marketing year, most of the drop in prices occurred during the first two years of the FAIR Act. It took until the third marketing year for prices to drop to critical, and politically unacceptable, levels.

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