By Daryll E. Ray

Tobacco: The darling of supply control and price support programs (until now)

Unless you're in one of the major tobacco producing states, you probably hear a lot more debate about tobacco *consumption* issues and policies than *production* issues and policies. My location in East Tennessee puts me smack dab in the middle of the tobacco belt meaning that lots of interesting questions about tobacco economics and policy land on our doorstep. APAC economist, Dr. Kelly Tiller, fields the majority of these tobacco questions for us, so I thought it would be of broader interest to share some of her insights about tobacco in this column.

The federal tobacco supply control and price support program is one of the longest running and, arguably, most successful crop programs in our history. Today it is in a state of decay, despite its history and success. At best, current issues most likely will result in changes that will, in the future, leave the tobacco program in an unrecognizable state. Or the program could be headed for extinction.

What's happening in tobacco? Why should the other non tobacco producing states care? Who are the winners and losers? What will tobacco production look like in the future? We'll get to all of these questions over the next two columns, but before we do, I'd like to use this column to provide a little background information about tobacco production and the tobacco program.

About 90% of all tobacco produced in the U.S. is grown in six Southeastern states: North Carolina, Kentucky, Tennessee, Virginia, South Carolina, and Georgia. The majority of the tobacco grown is flue-cured tobacco and burley tobacco: two components of the American blend cigarette (along with imported Oriental tobacco). Other minor types of tobacco grown in the U.S. are destined for other tobacco products like snuff, chewing tobacco, and cigars.

Producing tobacco is very labor intensive and difficult to mechanize. Thus, tobacco production looks much the same today as it did 70 or more years ago, right down to hand-hoeing out weeds and hand-picking off bugs in some small plots. Producing an acre of tobacco can require up to 300 hours of hand labor, compared to about 1-2 hours for corn or soybeans. But the hard work pays off for the grower at the end of the season. Tobacco is highly profitable to produce. Also, compared to many other crops or agricultural enterprises, tobacco is easy to grow and market and involves relatively low risk. Tobacco is the nation's sixth largest crop in terms of cash receipts generating about $2 billion, making it the leading cash crop in most of the major tobacco states. Historically, a tobacco grower could expect a return of up to $2,000 per acre for tobacco.

The success and perseverance of tobacco production are due in large part to the federal tobacco program that has been in place since the late 1930s. In fact, it would be difficult to overstate the importance of the federal tobacco program in developing and sustaining the agricultural economy of many communities in the Southeast. Tobacco has single-handedly kept a large number of small family farms afloat for generations.

The program limits annual tobacco production through quotas that determine the amount of tobacco each farmer can sell. A formula incorporating manufacturer's purchase intentions (domestic demand) and the 3-year export average, adjusted by reserve stock levels, determines the annual basic quota. Tobacco quotas have become a transferable asset. Quotas are also a cost of production for the grower who typically owns only a fraction of the quota he grows and leases the remaining quota poundage from quota owners who do not grow a crop. The program also guarantees a minimum price for tobacco. For generations, tobacco has been marketed through the auction warehouse system. In this system, farmers deliver their leaf to a local warehouse where it is graded by USDA graders. Manufacturers and leaf dealers competitively bid on each lot of tobacco. Any lot that does not meet the minimum guaranteed price is placed under CCC loan and held by producer cooperatives for future sale.

The tobacco program has survived while many other ag commodity programs have bitten the dust over the years. The tobacco program has survived in part because it is funded by assessments on the growers and buyers rather than by taxpayer dollars. In addition to keeping tobacco prices high and stable, and supply and demand fairly balanced, the program has also helped preserve a way of life for many farmers in the Southeast by keeping production confined to historical boundaries, limiting expansion, and providing an opportunity for profit on small acreages with relatively low capital investments.

But despite its longstanding success, tobacco production and the tobacco program are under siege. Recent problems – demand cut in half, declining exports, more foreign imports, very high prices, sky-high lease rates, contract marketing, to name a few – are creating a flood that the federal tobacco program, full of cracks and strains itself, can hardly contain. In the next column, we'll explore some of the problems facing tobacco in a little more depth and then examine some of the possible outcomes and their implications.

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