APAC Agricultural Policy Analysis Center
The University of Tennessee

PolicyPennings by Dr. Daryll E. Ray

Agribusinesses practice inventory management, farmers should not (?)

"Acreage reduction programs unfairly harm small town Main Street business and in particular local suppliers of agricultural inputs like seed, equipment, and farm chemicals." That argument is one of the consistent critiques that have been directed toward farm program policies that either work to prevent the build-up of excess stocks of the major commodities or seek to remove environmentally sensitive land from production.

That argument implies, sometimes subtly and sometimes not, that farmers should produce at full capacity under all economic conditions. Otherwise they will be responsible for the demise of small towns across the land.

Inventory management programs are deemed unacceptable because while they benefit farmers, they reduce the sales of farm inputs, the need for grain haulers, and the use of local elevators. Meanwhile industrial firms like Ford Motor Company and John Deere use inventory management programs all of the time.

On August 19, 2006 a "New York Times" headline read "Ford is slashing production 20% for 4th quarter." The article went on to say, "Together, Ford and General Motors are shedding tens of thousands of jobs, closing more than two dozen plants and cutting billions of dollars of costs. But those measures are effectively cancelled out when automakers cannot sell the vehicles already on the showroom floor."

Those words should sound very familiar to most farmers. In general farmers continue to adopt the latest technologies and seed varieties to achieve the lowest possible cost of production. Precision agriculture, or as some call it "farming by the foot," allows crop producers to apply fertilizer and other nutrients in those areas that will have the greatest production response while lowering their input costs.

But, as with Ford and GM, all of the efforts to become lean on the production side come to naught as long as the supplies on the "showroom floor" exceed those demanded by the customer.

The concern with matching production volume to consumer demand is not limited to Detroit; it is a concern in the Quad Cities as well. John Deere's third quarter earnings report reads, "consistent with ongoing asset-management initiatives, production levels are expected to be down about 5 percent for the year and about 10 percent for the fourth quarter."

As a part of their strategy to reduce inventories, John Deere's "worldwide farm machinery production is expected to be down about 20 percent in the fourth quarter in comparison with the same period last year."

Nowhere do we see that John Deere, Ford and GM, decided that because of a potential negative community impact they were going to keep all of their plants operating at full tilt. While they may be concerned about the financial stability of their input suppliers, that concern is secondary to their concern for their own financial stability.

Obviously, agriculture is different. There is no "John Deere" in total crop production. When crop inventories get large, no farm level CEO can significantly reduce production to restore a balance. What does happen is that farmers tend to produce crops at full-tilt without regard to total crop demand conditions or inventory levels.

They do that because they can't affect industry supply; commodities are not identity preserved; and they do not fill orders like Dell Computers.

But, producing at full-tilt no matter what is a recipe for financial disaster.

Folks who would not operate a business in which products are produced 24/7 irrespective of demand conditions, are often adamantly against inventory management in agriculture.

Arguments that ultimately do not deter John Deere and Ford from production-reducing decisions seem to win out in agriculture.

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