PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

The 2012 Farm Bill: Are high prices the future of agricultural production?

As the 2010 crop is being harvested, farmers and their organizations are already beginning to look at the policies that they would like to see in the 2012 Farm Bill. Depending on what happens in the fall elections, hearings on the next farm bill could start up again as early as this coming February.

The issues that will affect this discussion include, the federal deficit, direct payments, crop insurance, and the role of the federal government in the agricultural sector. The discussion is also shaped by the assumptions about the future that people hold. This column will take a look at a common assumption that underlies some of the policy changes being proposed for the 2012 Farm Bill.

Given the concern about deficits in Congress and the current high prices, the money available for the 2012 Farm Bill will probably be more constrained than it has been in the past. Concern about deficits may result in attempts in Congress to reduce the money available for many programs, the farm bill included.

The reason the "high" prices are a factor is because the Congressional Budget Office's projection of the cost of continuing existing farm legislation becomes the starting point or "baseline" for negotiating authorization of expenditures for the new farm bill. So, to the extent that the current high crop prices are projected over the tenure the 2012 farm legislation, the projected baseline expenditures on farm programs will be relatively low compared to, say, projections based on crop prices at levels of a mere five years ago.

The psyche of farmers and their organizations is also affected by "high" crop prices. Consciously or unconsciously farmers and others come to believe that the present is also the future.

This "now is the future" assumption appears to underlie the current push to replace farm programs with a "purely privatized crop-insurance program." What a wonderful world that would be. And it would work too, if prices (revenue actually) averaged at current levels from year-to-year with predictable bell-shaped deviances in individual years.

But, is a simple extension of today's price conditions into the future reasonable? Well, how did today's prices become what they are?

Basically, the crop price increases began in the 2006/2007 crop year in response to projected corn needs for ethanol production in 2007 and beyond. That expectation directly affected corn prices and indirectly affected the prices of soybeans and other crops that would compete for acreage in the following year. After that things got crazy. In 2008 buy-only speculators got involved and wheat crops faltered in some countries among other occurrences.

As has happened during other periods with extreme run-ups in prices, the world quickly geared-up to expand production. Acreages-heretofore unknown to even exist by many-came into production on several continents and agribusiness ramped up the delivery of yield boosting inputs to one and all.

Spring forward to 2010. This avalanche of increased potential worldwide production has not become a reality. Why? Largely, because of the way weather slashed expected feed and food wheat production by 25 to 40 percent in countries of the former Soviet Union. The massive flooding in Pakistan and weather-stunted corn yields in the US have also been factors.

So prices of today are rooted largely-not exclusively of course-in two sets of events: increased demand for staple crops with a speculative bubble (growth in the Chinese export demand for soybeans should also be mentioned) and a drastic 2010 yield decline in several important staple-crop-producing countries.

In the future, is it reasonable to expect a similar demand and supply shifts to occur as needed to ensure $4 per bushel corn prices?

If not, chances are we will experience what we have always experienced after periods of price euphoria-growth in productive capacity and agricultural output that quickly outstrips growth in demand. Yes, this time is said to be different. But then, that is what has always been said during periods like this.

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