Heritage Foundation blasts farm programs

The Heritage Foundation released a report on September 8, 2016, criticizing all farm subsidies. Needless to say the report, "Addressing Risk in Agriculture" (http://tinyurl.com/gv9vqyp) triggered a storm of reaction, some positive and quite a bit that is critical of the report.

One of the problems with the report is that it is unclear in identifying the unit of analysis, jumping from small producers, who earn most of their income off-farm and have negative on-farm income, to the largest producers, who produce most of the row crop production and thus garner the largest amount of farm subsidies, and then using one to criticize the other. It identifies the percentage of production generated by the largest producers and then criticizes the amount of subsidies they receive without looking at the per unit level of federal support among the different size farm operators, nor does it provide comparable numbers that readers could use to make those calculations.

In comparing the size of government agricultural payment and subsidy costs to various measures of farm income, the report comes to the conclusion that they are very small and by implication inconsequential. In doing so, it fails to recognize that in 1999 government payments were 165 percent of net farm income for Illinois and that includes the positive net farm income for cattle producers. For crop farmers that number would be much larger. In addition to Illinois, there were 7 other states where 1999 government payments exceeded 100 percent of net farm income.

The report uses old critiques that have been lobbed against farm policies like the Direct Payment Program that are no longer in effect. It bemoans the fact that the ARC/PLC programs that are now in effect will cost far more than projected when the current farm bill was debated and adopted without recognizing that the conditions that are driving those higher costs were identified by the two of us and others well in advance of the adoption of that legislation.

The authors of the report fail to recognize that less costly policy options were on the table, but were deliberately ignored by some of those who are now alarmed by the foundation's call to end all farm programs and institute a transitional program to achieve that goal.

For the two of us that approach conjures up Yogi Berra's phrase, its "Déjà vu all over again." We say that because a previous farm bill, the 1996 Farm Bill, replaced historical farm programs with a government payment program in which payments were to transition to zero over time.

But without supply-adjusting farm program components, crop prices plummeted and remained low for years, leaving farmers flailing in a sea of red ink. Congress responded by throwing out an expensive government-payment lifeline. Government outlays exploded. The two subsequent farm bills reversed course and instead of transitioning payments to zero committed taxpayers to provide annual direct payments of about $5 billion to major-crop agriculture in both "good" and "bad" times.

This time around the premise emphasized by the Heritage Foundation is the same as it was in 1996; "the agricultural sector is well equipped to handle risk and does not need special handouts." And while the report discusses risks faced by agriculture, it fails to recognize or even discuss the critical risks, particularly risks for major crops, which account for the largest number of crop acres in the US. For us that is the greatest failure of the report.

It seeks to impose a rigid free-market solution on agriculture, without recognizing that the collective market for major crops does not look like the representations of markets graphed and

discussed in economic textbooks. Farmers could manage risk without any governmental policies if they were facing the textbook markets, but they aren't.

Not to bore our regular readers, but there are still a lot of people who fail to recognize the obvious characteristics of agricultural production, particularly crop production, but also agricultural products like milk as well.

If there were sufficient price response on either the demand side or the supply side, then agriculture would be able to make corrections in a timely fashion, thus eliminating the need for government programs. Let's take a look and see what we find.

We begin by looking at the demand side. If people were to respond to lower prices by increasing their food intake, excess production would be taken off the market and the price would rise to the point where it would equal the cost of the last unit of production needed to match demand.

But it does not work that way. A sharp decrease in price like we have seen recently does not result in increased consumption. People may shift their purchases to go from hamburger to an occasional steak. They may buy more processed food and may eat out more often, but the total number of calories and nutritional profile remains relatively constant. Food is not like Christmas lights on December 26th. A lower price does not clear the food shelves like the whirlwind we see in the Christmas decorations aisle.

Food is like insulin. People will attempt to pay whatever they can to obtain a sufficient supply of food, but once their needs are met they will not increase their aggregate food purchases over the long run.

On the other hand, if farmers were to reduce their production in response to low prices, then prices could self-correct in a timely fashion. But that does not happen, at least quickly. Farmers will change their mix of crops in response to lower prices, but they tend not to reduce their total planted acreage in response to lower prices.

As long as farmers can borrow or use accumulated capital to pay at least variable costs, they continue to produce. Operators who own debt-free land are especially tenacious.

Moreover, farmers who lease land and thus could reduce the land they farm are reluctant to terminate leases in a low price environment because they would lose their access to the land if prices return to profitable levels.

When farmers do terminate leases, that does not mean that the land will be taken out of production. Neighboring farmers will snap up the leases to productive land in a New York minute, and total cropland and production change very little.

These characteristics of crop agriculture can result in long periods of low prices, punctuated by intermittent periods of price spikes.

We believe that to be most effective, farm programs should be framed and administered in light of these characteristics. In our view, the result would be risk management policies that farmers need and are affordable in the long-run.

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