U.S. Farm Policy, A Review

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Neil Conklin
Economic Research Service
U.S. Department of Agriculture
A Review of U.S. Farm Policy

• Farm Bill
  – Provisions
  – Effects
• The Decoupling Debate
• Where do we go from here?
A Difficult Process in 2002

Calendar days from appointment of conference members to a final Bill:

- 1985 farm bill: 12 days
- 1990 farm bill: 33 days
- 1996 farm bill: 11 days
- 2002 farm bill: 69 days
2002 Farm Act: Broad and Complex Legislation

- TITLE I: Commodity Programs
- TITLE II: Conservation
- TITLE III: Trade
- TITLE IV: Nutrition Programs
- TITLE V: Credit
- TITLE VI: Rural Development
- TITLE VII: Agricultural Research, Education, and Extension and Related Matters
- TITLE VIII: Forestry
- TITLE IX: Energy
- TITLE X: Miscellaneous
2002 Farm Act: In Perspective

Sources: Congressional Budget Office, March 2002 Baseline and May 2002 Farm Act Score
Agricultural Spending Levels Close to those of Recent Years

Commodity Credit Corporation (CCC) net outlays

- Additional funds provided by 2002 Farm Act
- CBO March 2002 baseline for 1996 Farm Act
- Actual outlays

Source: CCC Budget and Congressional Budget Office March 2002 forecasts.
2002 Farm Act Doesn’t Change

• U.S. commitment to obligations under the Uruguay Round Agreement on Agriculture

• U.S. commitment to an ambitious trade negotiating result in agriculture
What the 2002 Farm Act does

• Covers a wide range of programs

• Extends and modifies recent legislation
Provisions With Largest Direct Impact on Agricultural Markets

- Commodity programs
- Trade issues
- Conservation programs
Marketing loans: *coupled*

- **Marketing loan program**
  - Paid on current production
  - Depend on market prices
  - Benefit options
    - Forfeit crop to Government
    - Marketing loan gain
    - Loan deficiency payments

- **2002 Farm Act changes**
  - Loan rates increased for most covered crops
  - Crop coverage expanded
Marketing loan rates

- Wheat
- Corn
- Soybeans

Direct payments: *fixed and decoupled*

- Replace former Production Flexibility Contract payments
- Do not depend on current production or market prices
  - Fixed base
  - Fixed payment yield
  - Fixed payment rates
- Coverage extended to more crops
Counter-cyclical payments: mostly decoupled?

- New program
- Affects revenue risk
- May encourage production
- Effects are price dependent
Counter-cyclical payment for Corn

- Payment rate_{corn} =
  - (Target price)_{corn}
  - (Direct decoupled payment rate)_{corn}
  - (higher of commodity price or loan rate)_{corn}

- Counter-cyclical payment_{corn} =
  - 0.85 *(Base acres)_{corn} *
  - (Payment yield)_{corn} *
  - (Payment rate)_{corn}
Maximum Counter-cyclical Payment Rates

<table>
<thead>
<tr>
<th></th>
<th>2002-03</th>
<th>2004-07</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corn</td>
<td>$0.50</td>
<td>$0.70</td>
</tr>
<tr>
<td>Wheat</td>
<td>$0.35</td>
<td>$0.45</td>
</tr>
<tr>
<td>Soybeans</td>
<td>$0.20</td>
<td>$0.30</td>
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</tbody>
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Direct Payment Effects

- Fixed, decoupled payments
  - Wealth effect
  - Increased investment
- Small production impacts
Farms with Base and Yield Designations**

Percent of farms:
- Less than 25
- 25.1-50.0
- 50.1-60.0
- 60.1-70.0
- 70.1-80.0
- 80.1-90.0
- 90.1-95.0
- 95.1-100

* Counties with less than 25 farms are excluded

**As of April 10, 2003
Other Commodity Provisions

- Dairy
- Peanuts
- Sugar
Trade Related Provisions

- Export programs
- WTO “Circuit Breaker”
U.S. AMS Is Under WTO Ceiling

Billion dollars
Conservation Funding Shifts To Working Land

Source: Office of Budget and Policy Analysis, USDA, and Congressional Budget Office
Conservation Security Program: Conservation for everyone?

- Wide ranging objectives; focus on land-based practices, livestock waste management facilities excluded
- Entitlement funding
- Three “tiers” for participation; higher tiers require greater conservation effort and offer larger payments
- No environmental benefit-cost targeting
- Must use practices that meet standard at least cost
- Existing practices can be enrolled
- Cropland eligible only if farmed 4 of 6 years prior to 2002
Conservation Reserve Program Expanded

Market Effects of FSRI

- Acreage and Production
- Prices
- Government Payments
- Farm Income
Planted Area: Eight Major Crops

Direct Government Payments

Billion dollars

Net Farm Income

Debate on Decoupled Subsidies

Lump sum payments argued to be production and trade distorting because:

- may increase on-farm investment
- may increase risk-tolerance of farmers
- may create expectations about eligibility rules for future payments
- may interact with “market failures” and be effectively coupled
- [different preferences of recipients/taxpayers]
Decoupled Payments

• Government program payments to farmers
  – Not linked
  – Production decisions based on market returns

• Examples
  – Production Flexibility Contract Payments
  – Direct Payments
  – Counter-cyclical payments
Coupled vs. Decoupled Programs

- Coupled programs
  - Linked to production
  - Linked to specific crops
  - Increases overall production

- Decoupled programs
  - Not linked
  - Raise total revenue more generally
Impacts of PFC Payments

• No evidence of increased farm investment at the aggregate level
  – Decoupled payments increased land values about 8 percent
  – Investment and Production impacts are under 0.2 percent in the medium run

• Decoupled payments increased well-being of participating farm households
  – Higher income and wealth, higher and more smooth consumption, and more leisure

• Up to 60 percent of program benefits may be passed through to landlords - most of them nonfarming landlords
Who Received PFCs

Commercial farms are fewer but account for over half of PFC payments and two-thirds of production on recipient farms in 2001.
How Farms Allocate Their Assets

Note: Average assets = $768,710
Source: ARMS, 1999
Capitalization is an Issue

Crop prices trended down and flattened over 1996-2001, but the cost of buying cropland went up over the same period.

[Bar chart showing prices received index and indexed value of land per acre for years 1996 to 2001.]
Conclusions

- Production impacts are mostly from:
  - Marketing loan changes
  - Larger Conservation Reserve Program
- Agricultural spending similar to recent years
- Financial and Distributional impacts
Additional Resources

• USDA’s Farm Bill web site
  – http://www.usda.gov/farmbill/

• Economic Research Service (ERS) web site
  – Side-by-side comparison of 1996 and 2002 Farm bills
    http://www.ers.usda.gov/Features/farmbill/
  – Farm bill impacts
    http://www.ers.usda.gov/briefing/FarmPolicy/
Supply curve and price (per-unit revenue) risk under 1996 farm act (without counter-cyclical payments)

Price distribution, 1996 law

Expected market price/per-unit revenue distribution around mean expected price, without counter-cyclical payments
Supply curve and price (per-unit revenue) risk under 1996 farm act (without counter-cyclical payments)

Price distribution, 1996 law

Per-unit revenue distribution, 2002 farm act

Counter-cyclical payments reduce per-unit revenue risk around mean expected price
Direct government payments

* February 2003 forecast
Source: Economic Research Service, USDA.
U.S. WTO domestic support notifications

$ billion

- Green box
- Unused Amber box
- Aggregate Measurement of Support

Fiscal year

Source: WTO Notifications.