

U.S. Farm Policy, A Review

**Prepared for PDIC
Montreal, Quebec, Canada
April 23-25, 2003
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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:

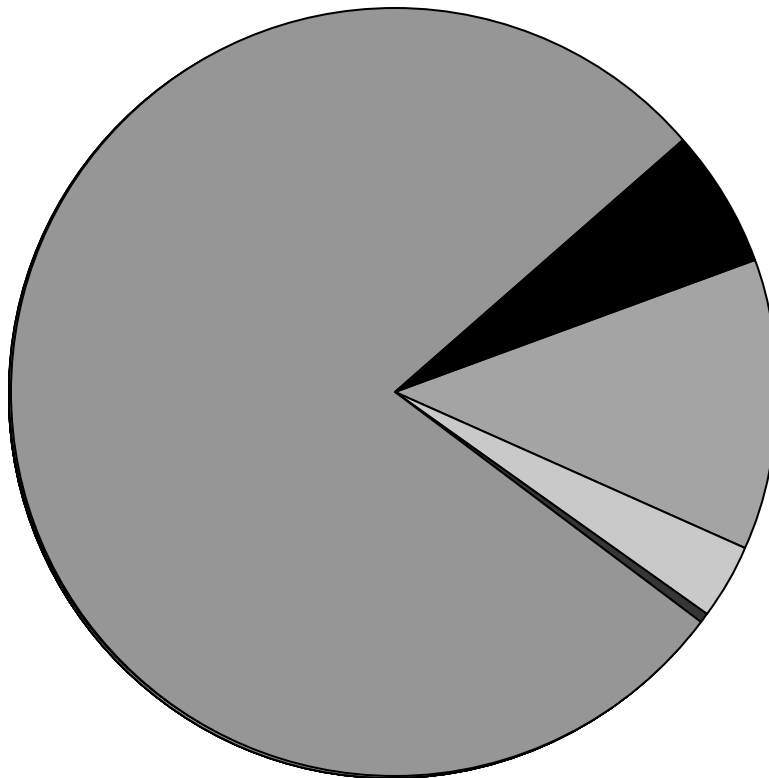
- 1985 farm bill: 12 days
- 1990 farm bill: 33 days
- 1996 farm bill: 11 days
- 2002 farm bill: 69 days

2002 Farm Act: Broad and Complex Legislation

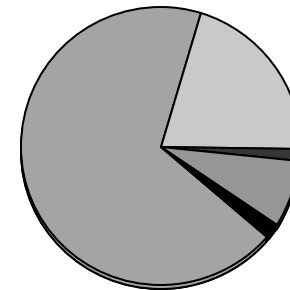
- **TITLE I: Commodity Programs**
- **TITLE II: Conservation**
- **TITLE III: Trade**
- **TITLE IV: Nutrition Programs**
- **TITLE V: Credit**
- **TITLE VI: Rural Development**
- **TITLE VII: Agricultural Research,
Education, and Extension
and Related Matters**
- **TITLE VIII: Forestry**
- **TITLE IX: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

2002 Farm Act: In Perspective

Baseline \$ 699 billion



2002 Farm Act \$ 83 billion



■ Commodity
■ Trade
■ Other

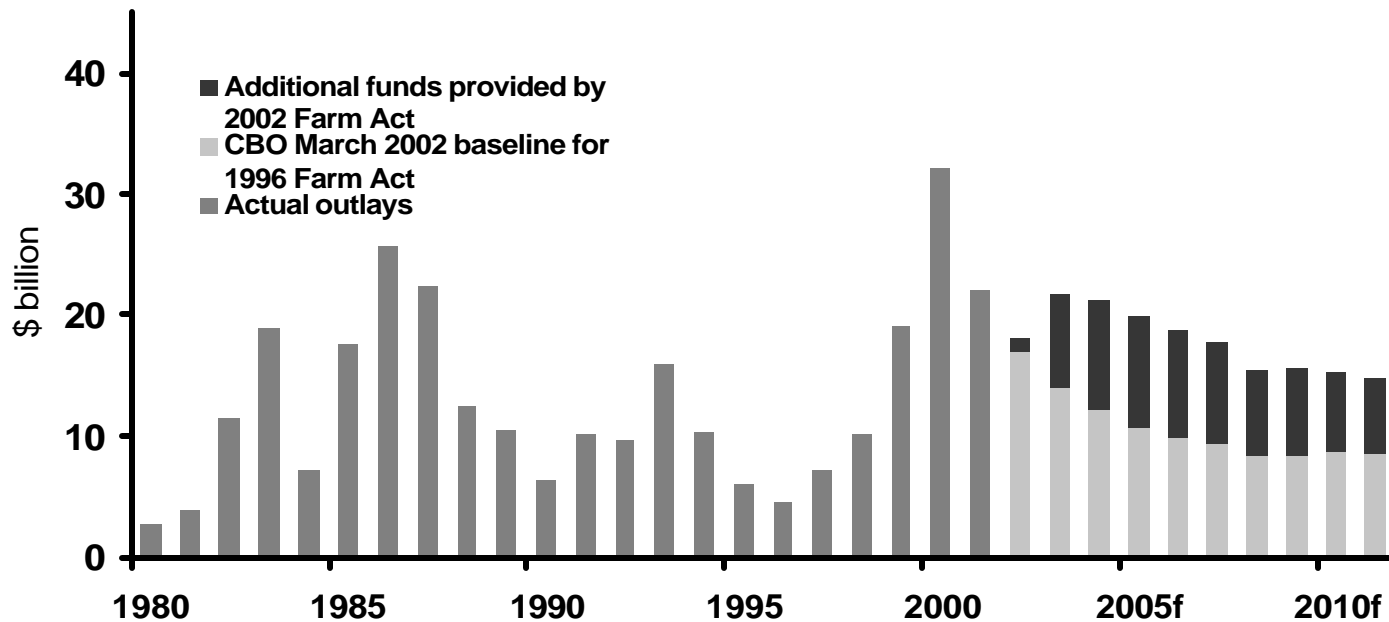
■ Conservation
■ Nutrition

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



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**

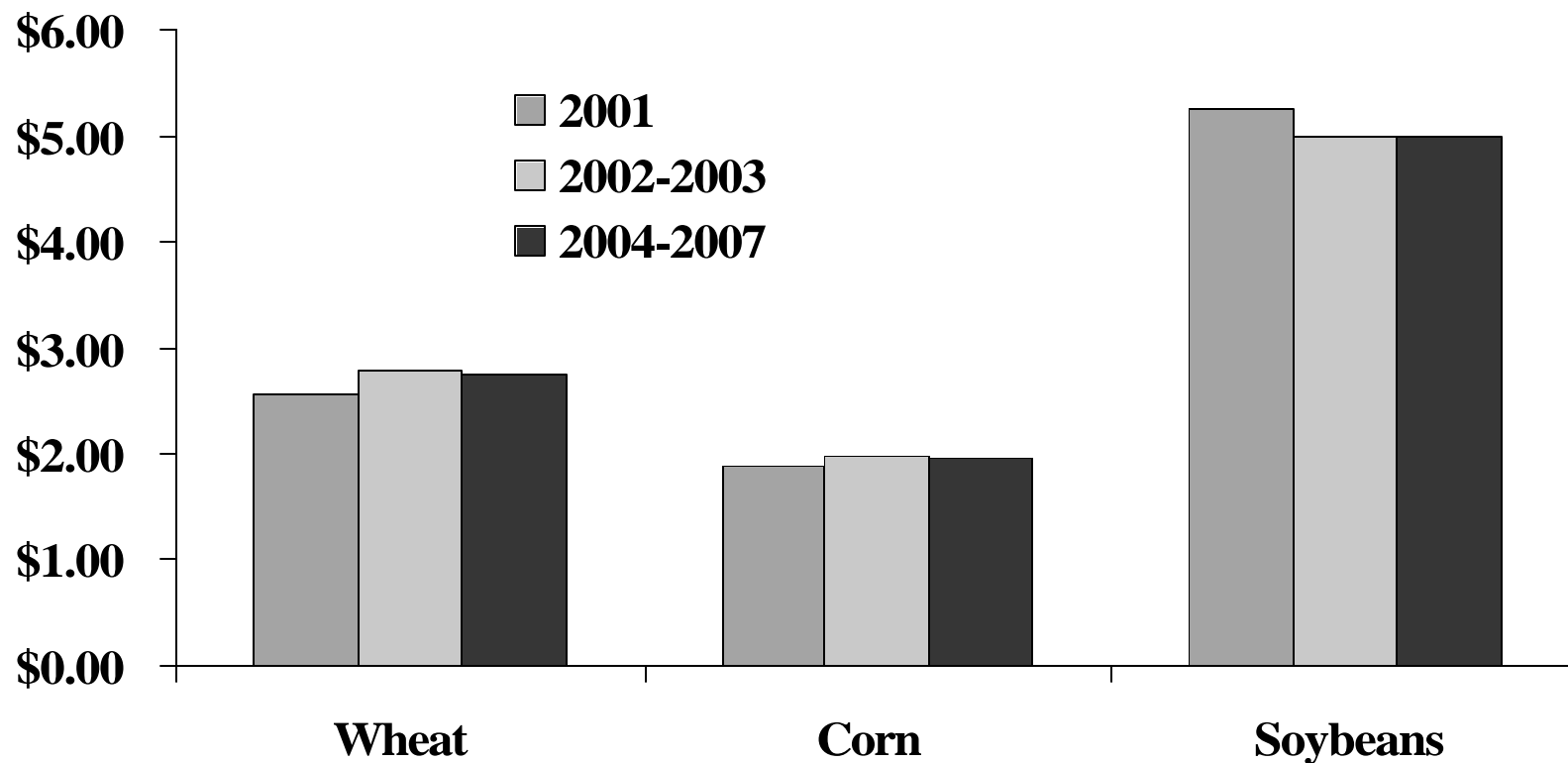
Provisions With Largest Direct Impact on Agricultural Markets

- **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



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?*

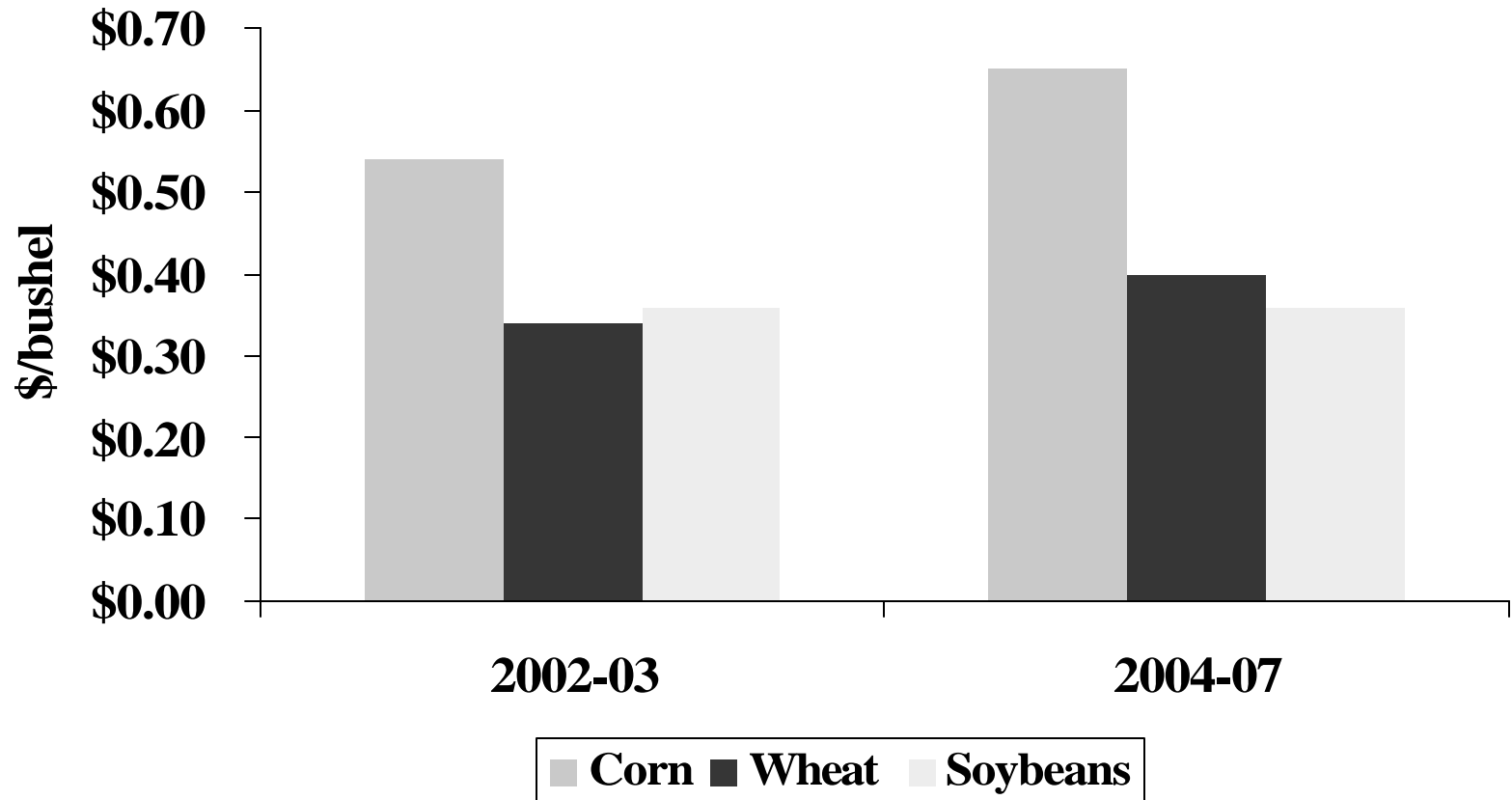
- New program
- Affects revenue risk
- May encourage production
- Effects are price dependent

Counter-cyclical payment for Corn



- $\text{Payment rate}_{\text{corn}} =$
 $(\text{Target price})_{\text{corn}}$
 – $(\text{Direct decoupled payment rate})_{\text{corn}}$
 – $(\text{higher of commodity price or loan rate})_{\text{corn}}$
- $\text{Counter-cyclical payment}_{\text{corn}} =$
 $0.85 * (\text{Base acres})_{\text{corn}}$
 $* (\text{Payment yield})_{\text{corn}}$
 $* (\text{Payment rate})_{\text{corn}}$

Maximum Counter-cyclical Payment Rates



Direct Payment Effects

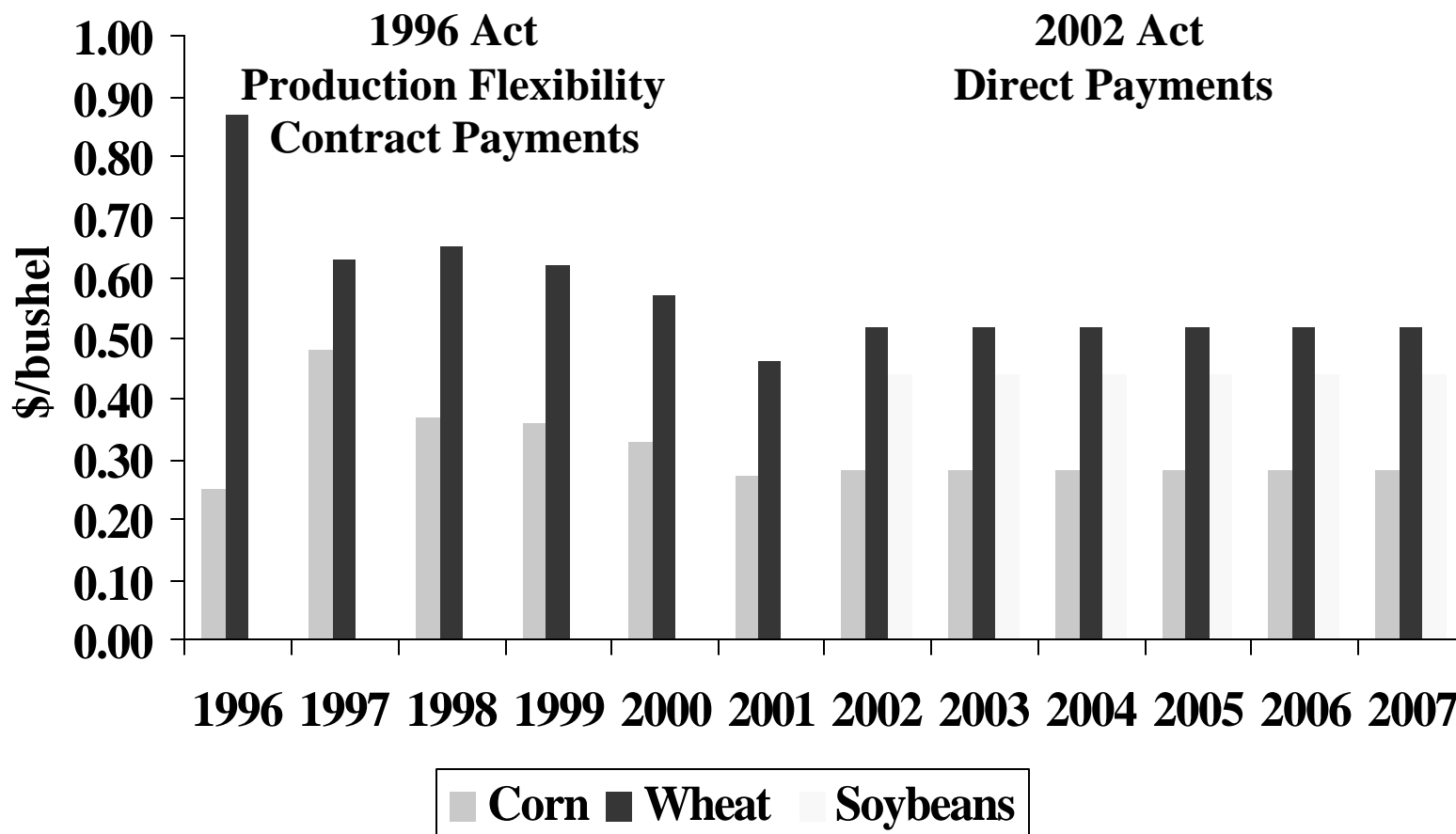
- Fixed, decoupled payments
 - Wealth effect

Increased investment

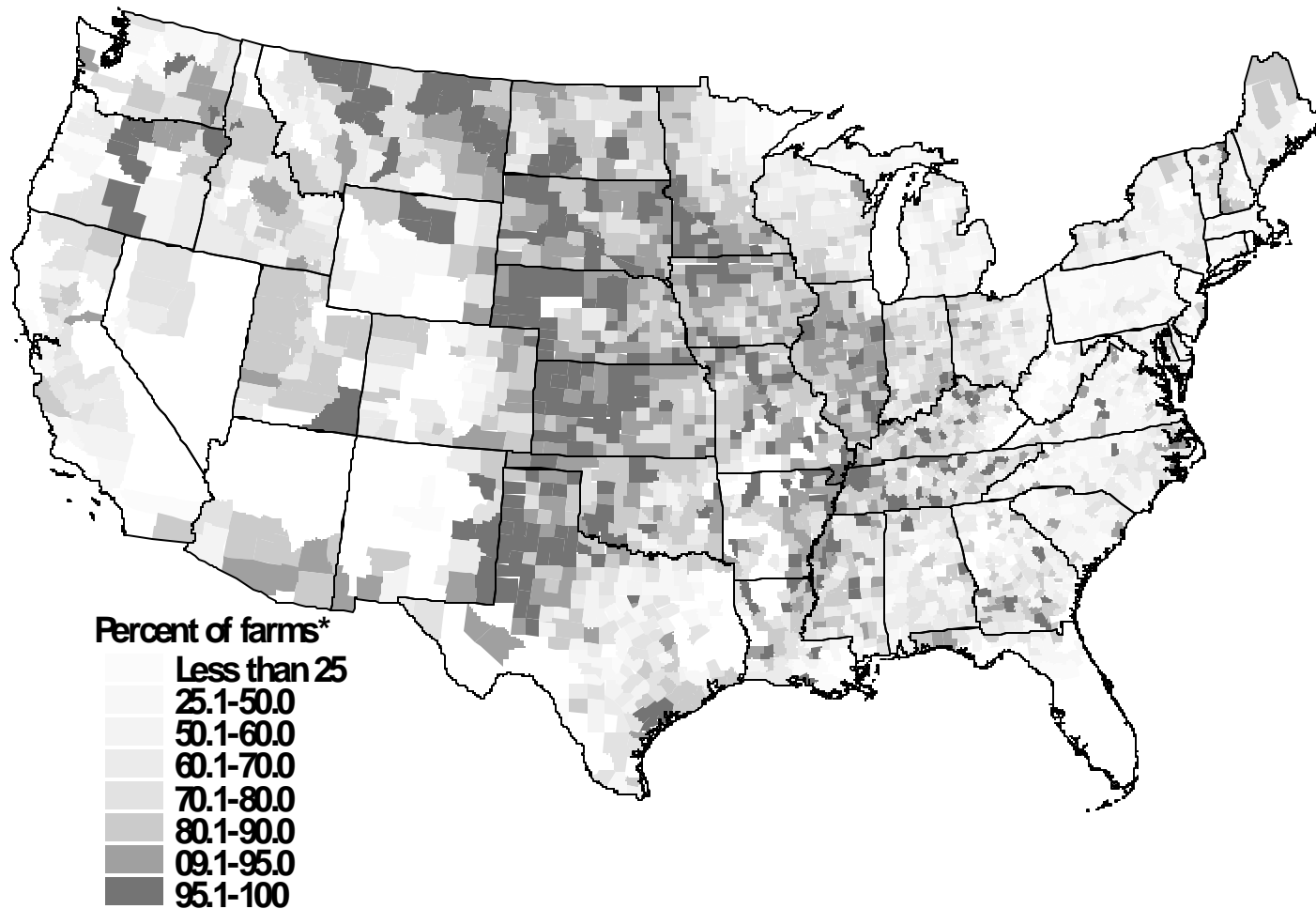
- Small production impacts



Direct Payment Rates



Farms with Base and Yield Designations**



* Counties with less than 25 farms are excluded

**As of April 10, 2003

Other Commodity Provisions



- Dairy
- Peanuts
- Sugar

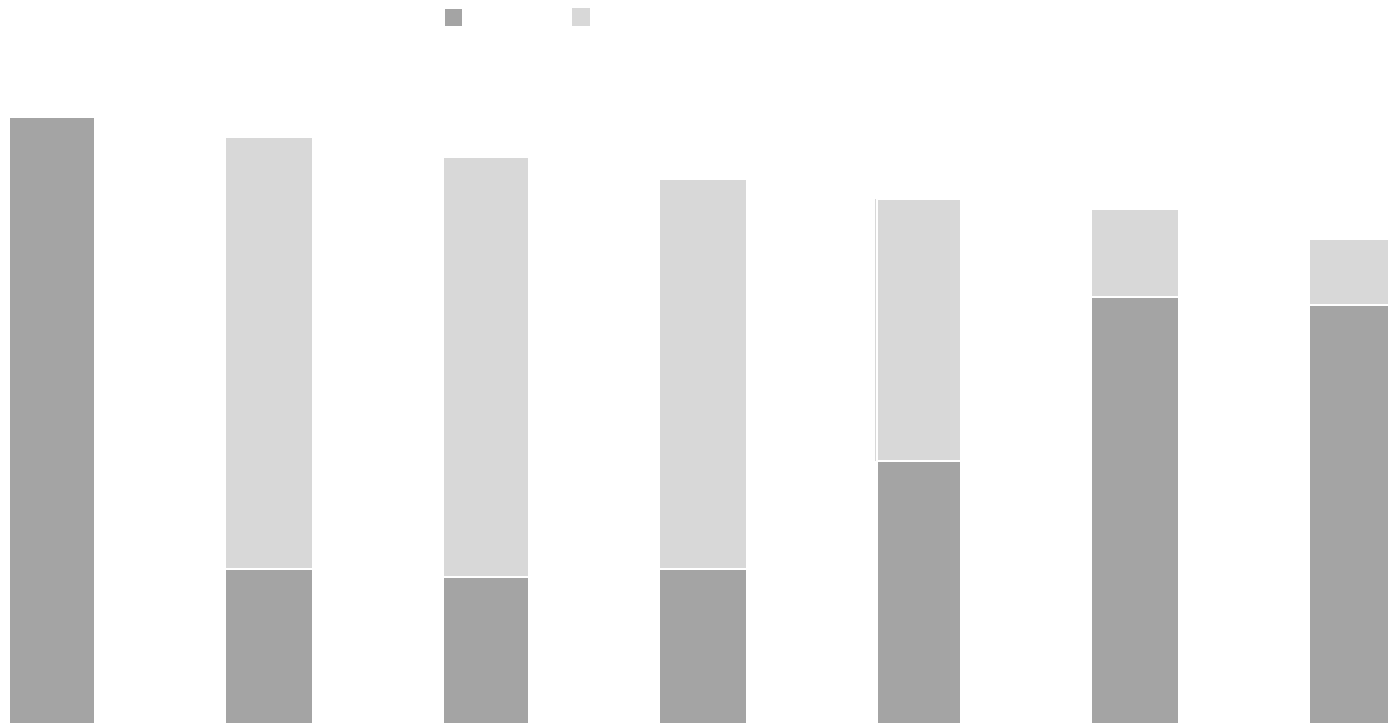
Trade Related Provisions

- **Export programs**
- **WTO “Circuit Breaker”**

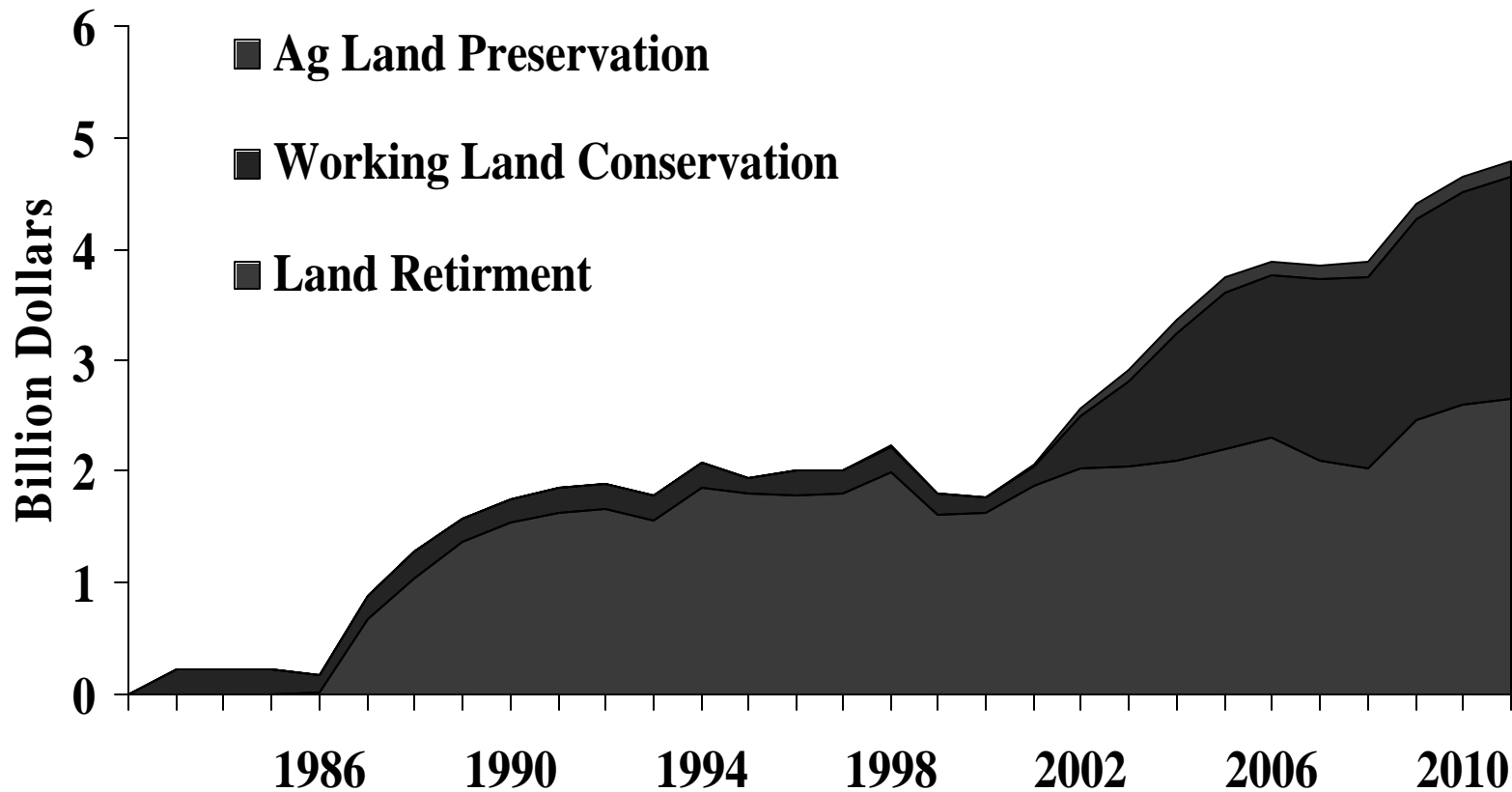


U.S. AMS Is Under WTO Ceiling

Billion dollars



Conservation Funding Shifts To Working Land



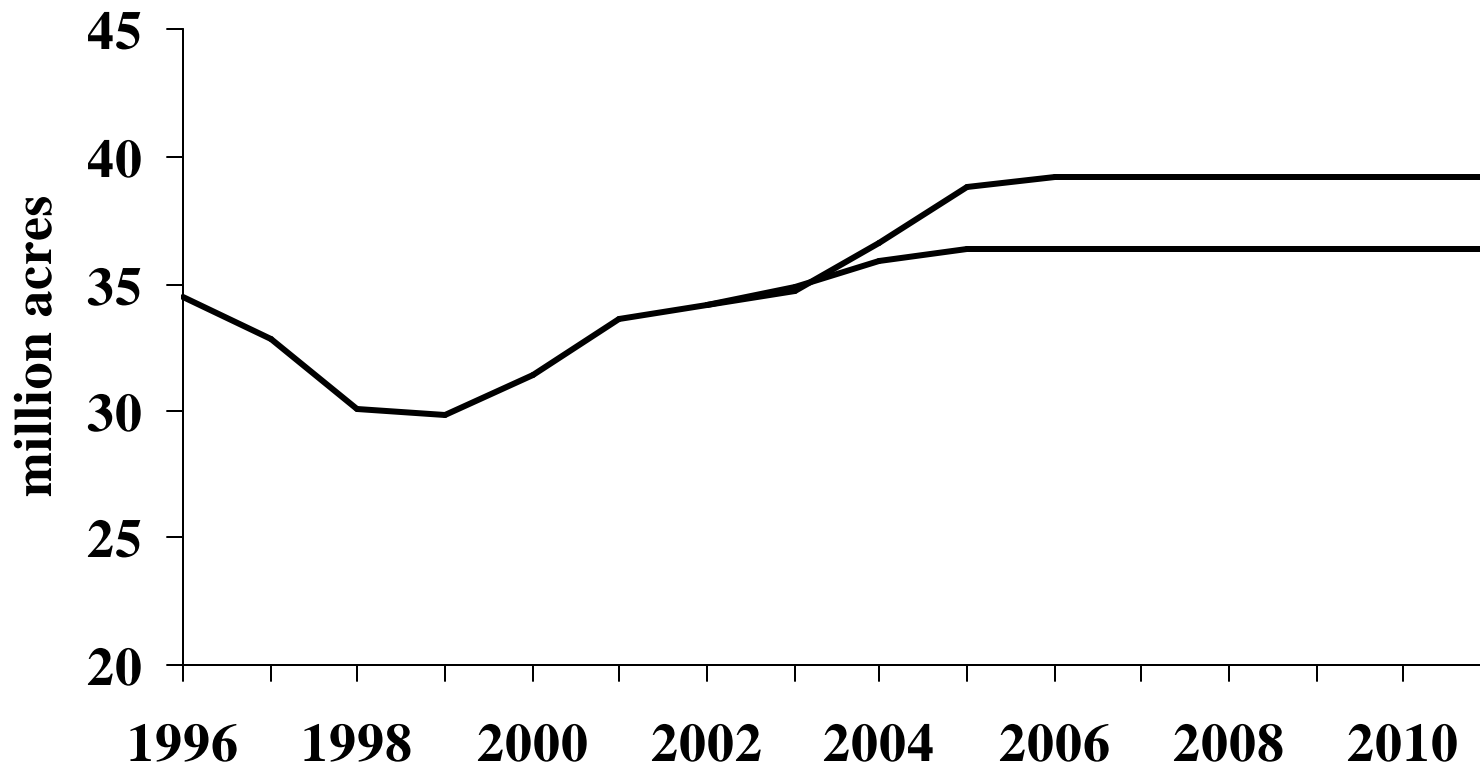
Source: Office of Budget and Policy Analysis, USDA, and Congressional Budget Office



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



Source: The 2002 Farm Act: Provisions and Implications for
Commodity Markets, ERS/USDA, AIB 778 (November 2002).

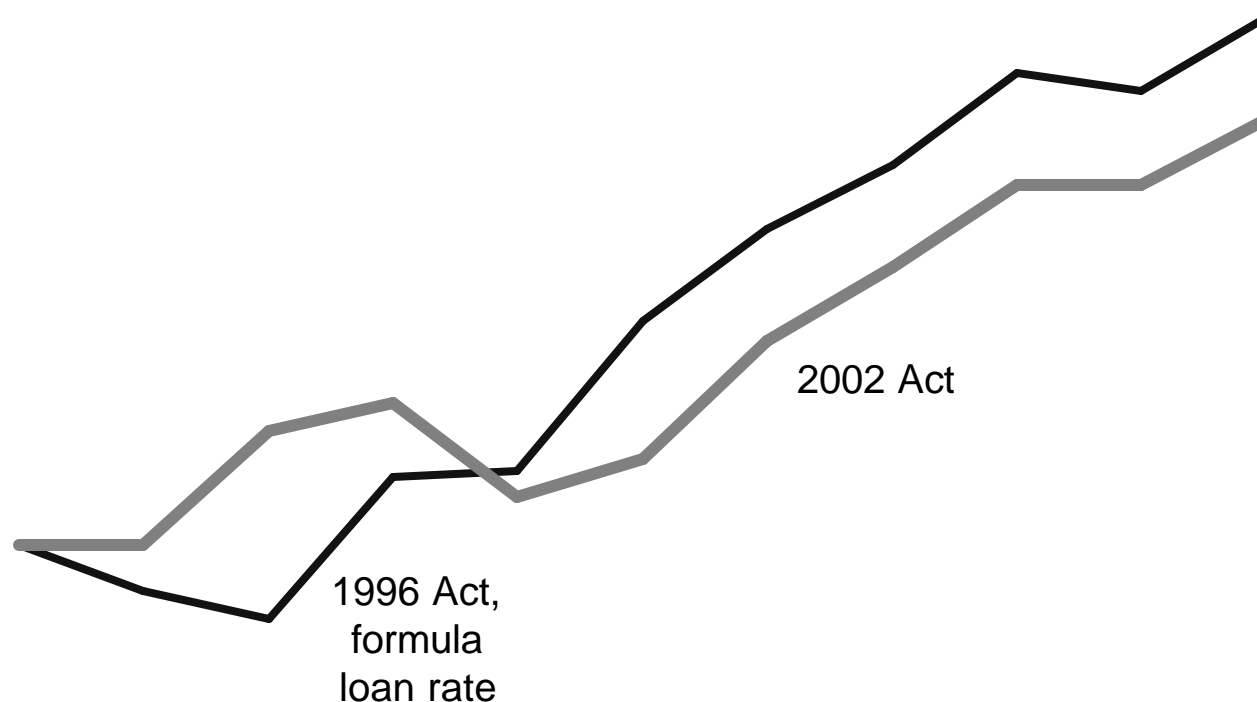


Market Effects of FSRI

- Acreage and Production
- Prices
- Government Payments
- Farm Income

Planted Area: Eight Major Crops

Million acres

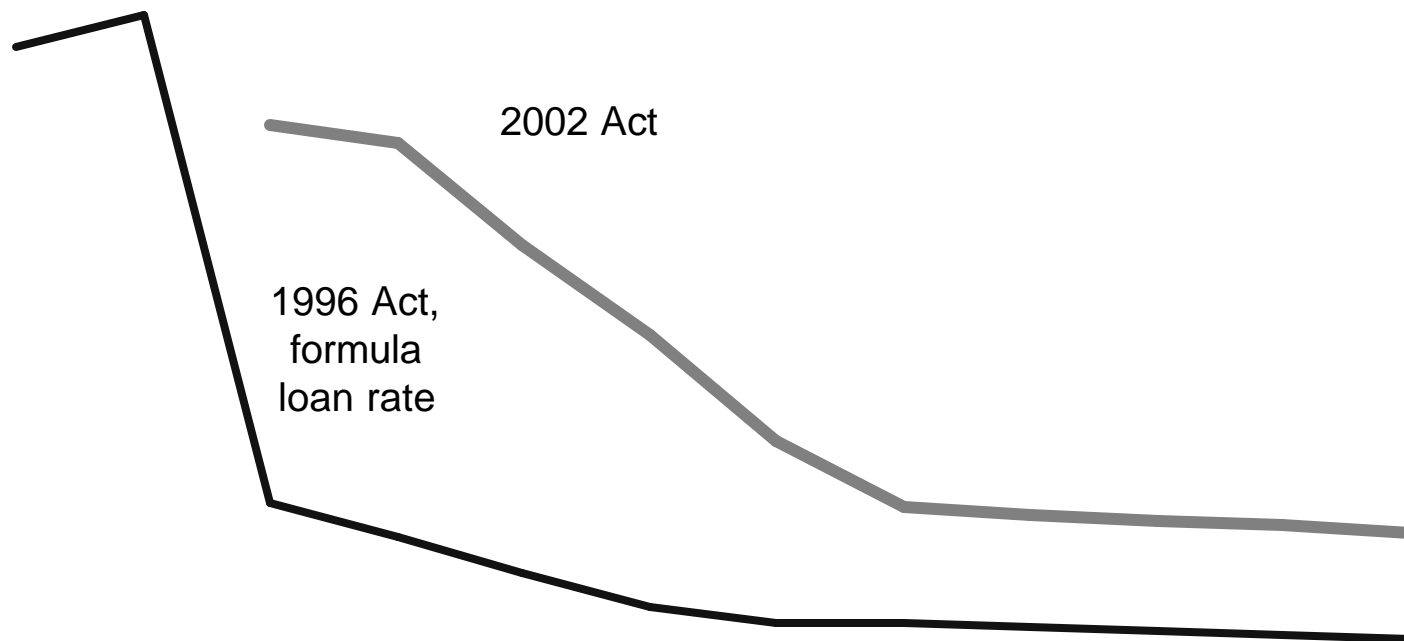


Source: The 2002 Farm Act: Provisions and Implications for
Commodity Markets, ERS/USDA, AIB 778 (November 2002).



Direct Government Payments

Billion dollars

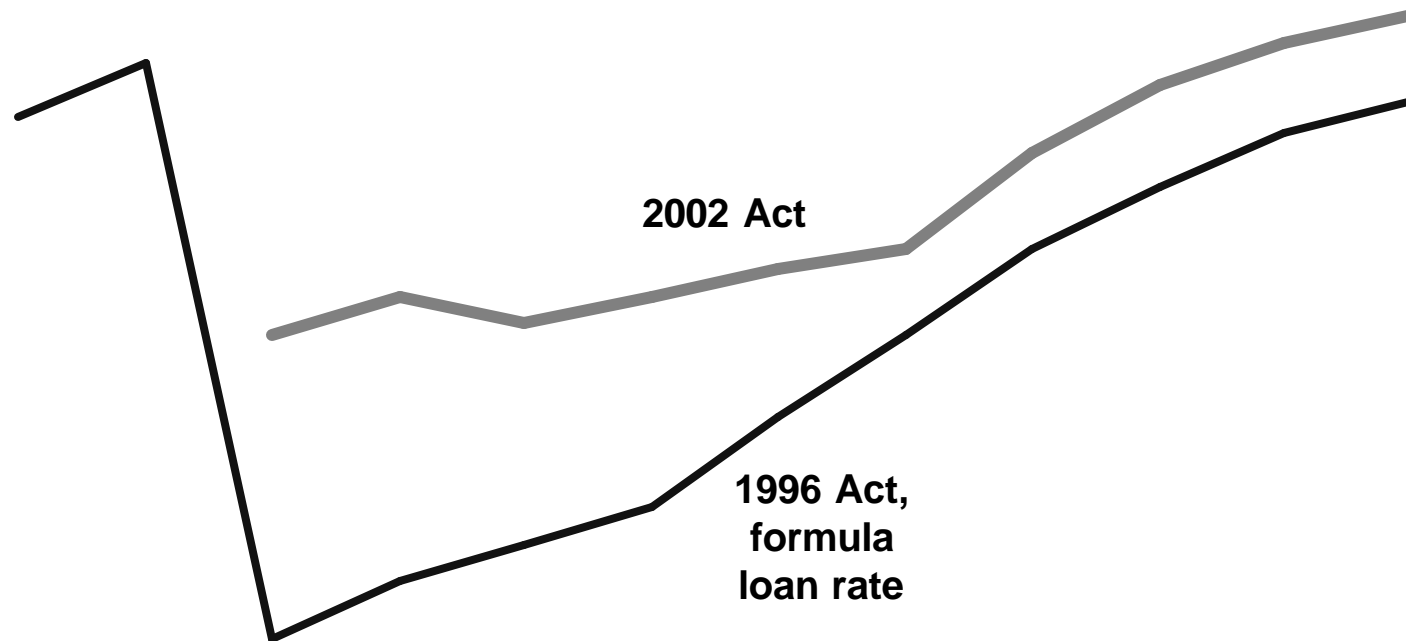


Source: The 2002 Farm Act: Provisions and Implications for
Commodity Markets, ERS/USDA, AIB 778 (November 2002).



Net Farm Income

Billion dollars



Source: The 2002 Farm Act: Provisions and Implications for
Commodity Markets, ERS/USDA, AIB 778 (November 2002).



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

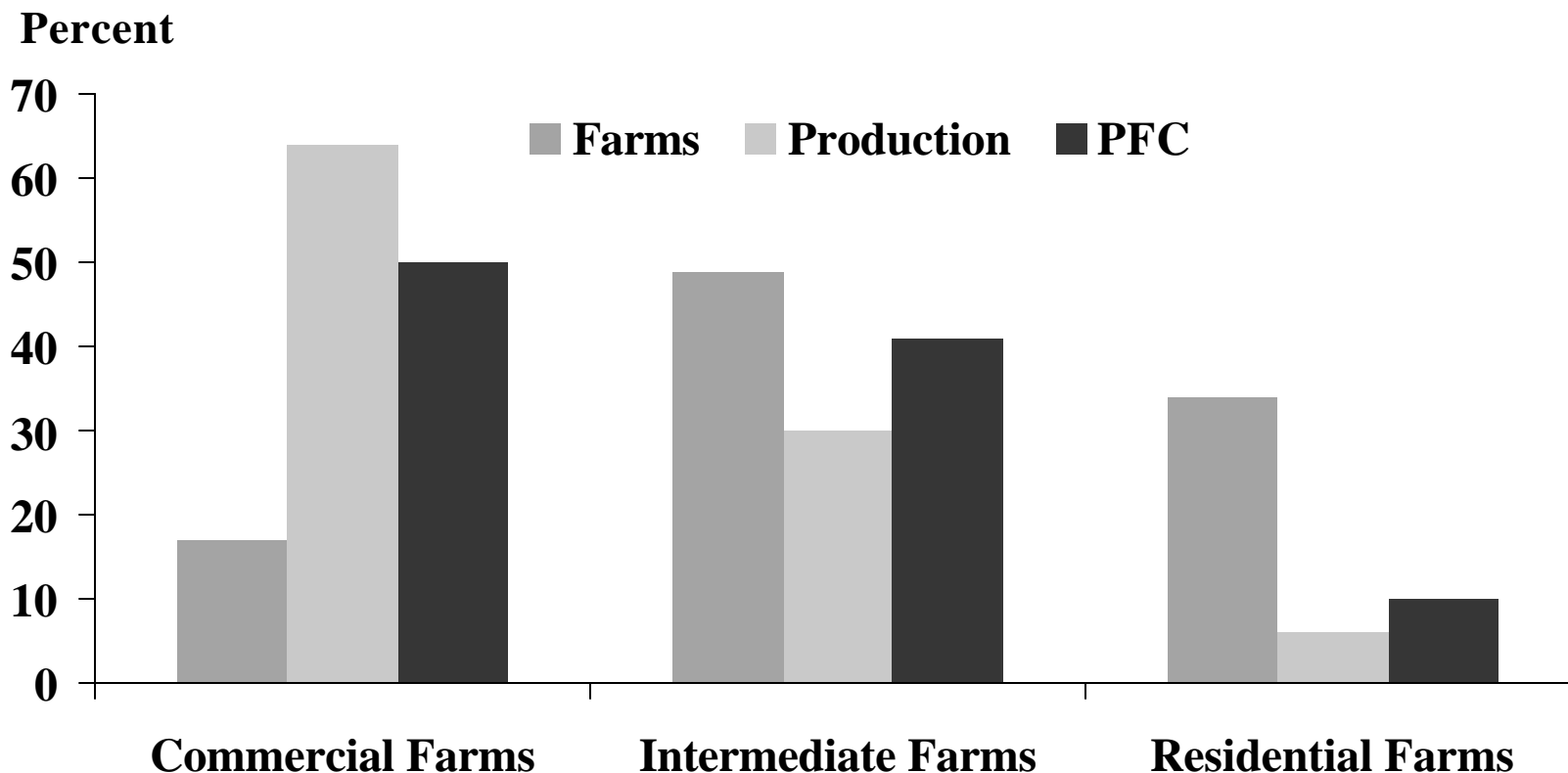


Impacts of PFC Payments

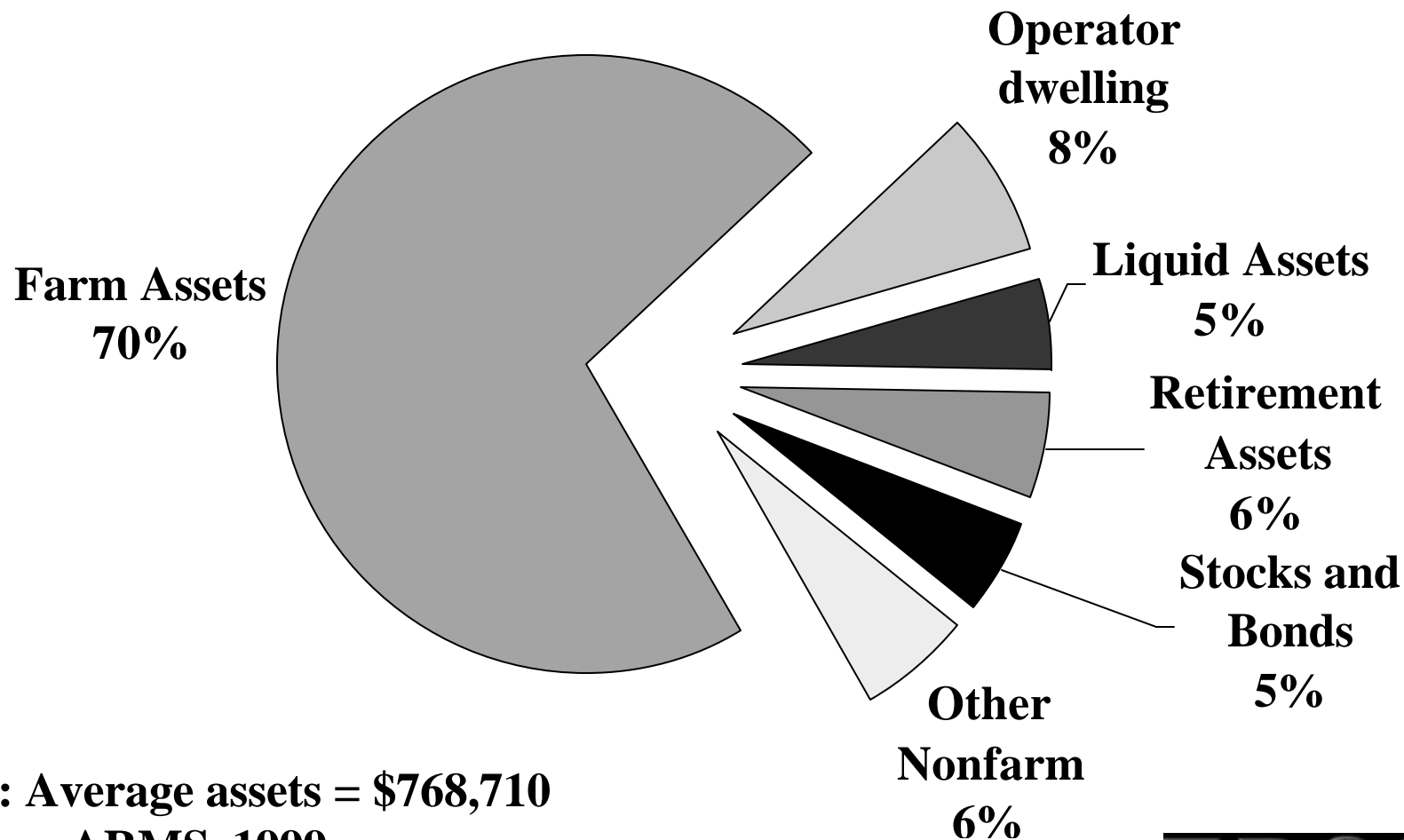
- No evidence of increased farm investment at the aggregate level
 - Decoupled payments increased land values about 8 percent
 - Investment and Production impacts are under 0.2 percent in the medium run
- Decoupled payments increased well-being of participating farm households
 - Higher income and wealth, 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

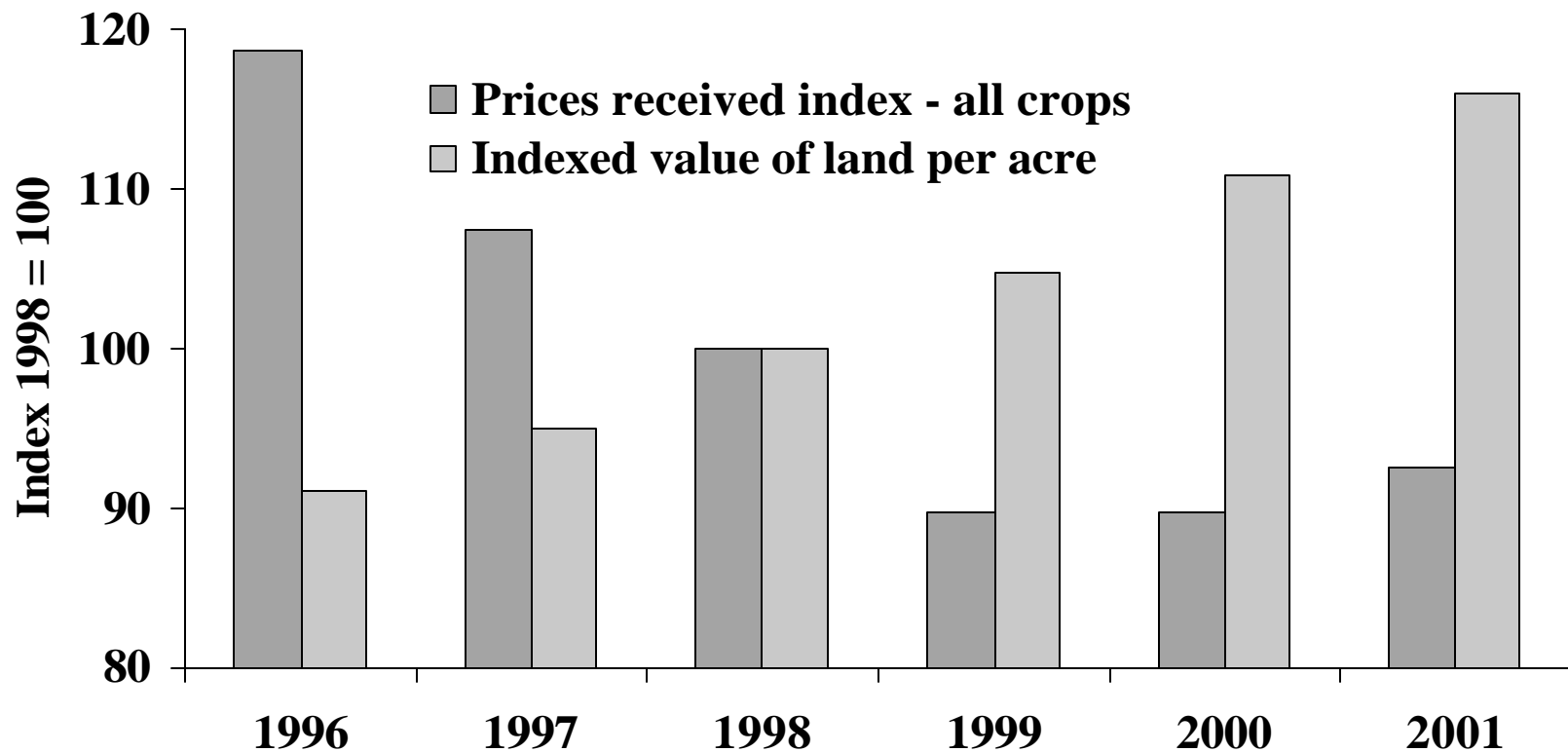


Note: Average assets = \$768,710

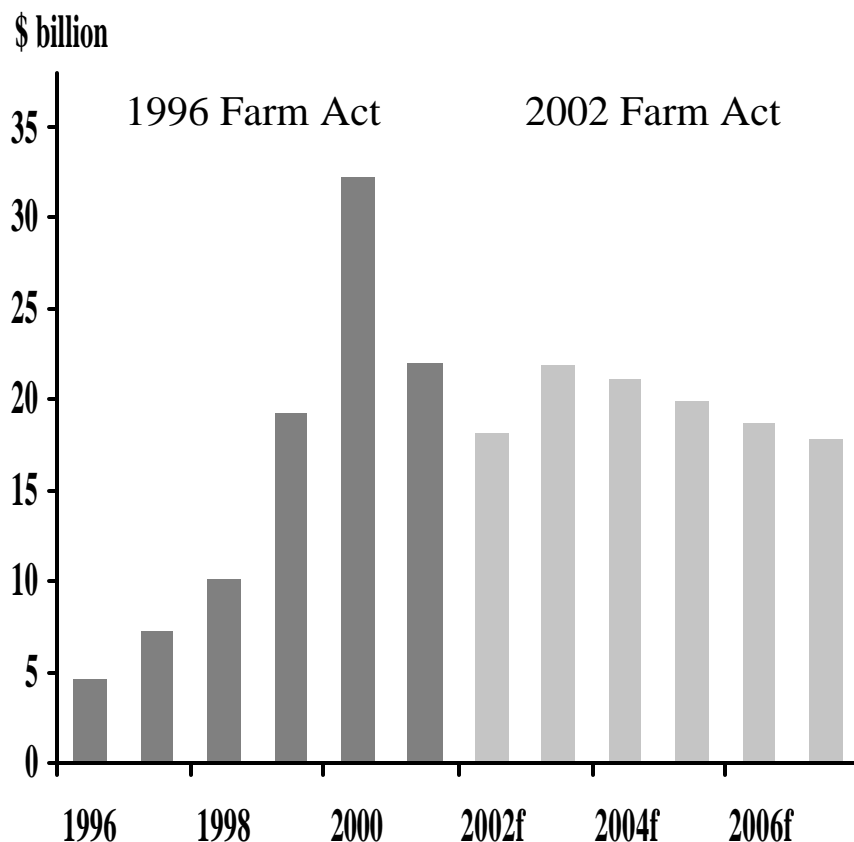
Source: ARMS, 1999

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



Conclusions



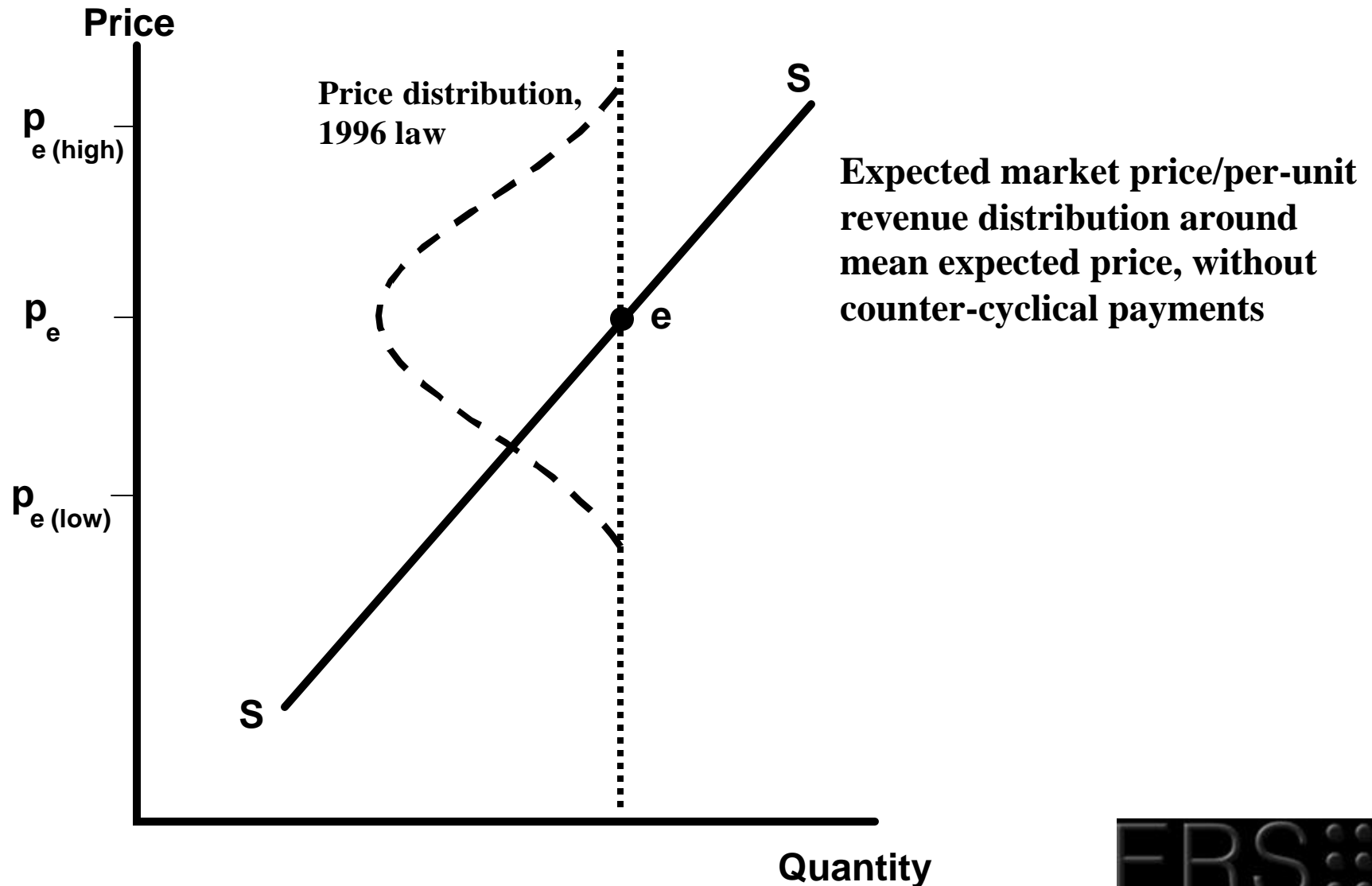
- **Production impacts are mostly from**
 - Marketing loan changes
 - Larger Conservation Reserve Program
- **Agricultural spending similar to recent years**
- **Financial and Distributional impacts**

Additional Resources

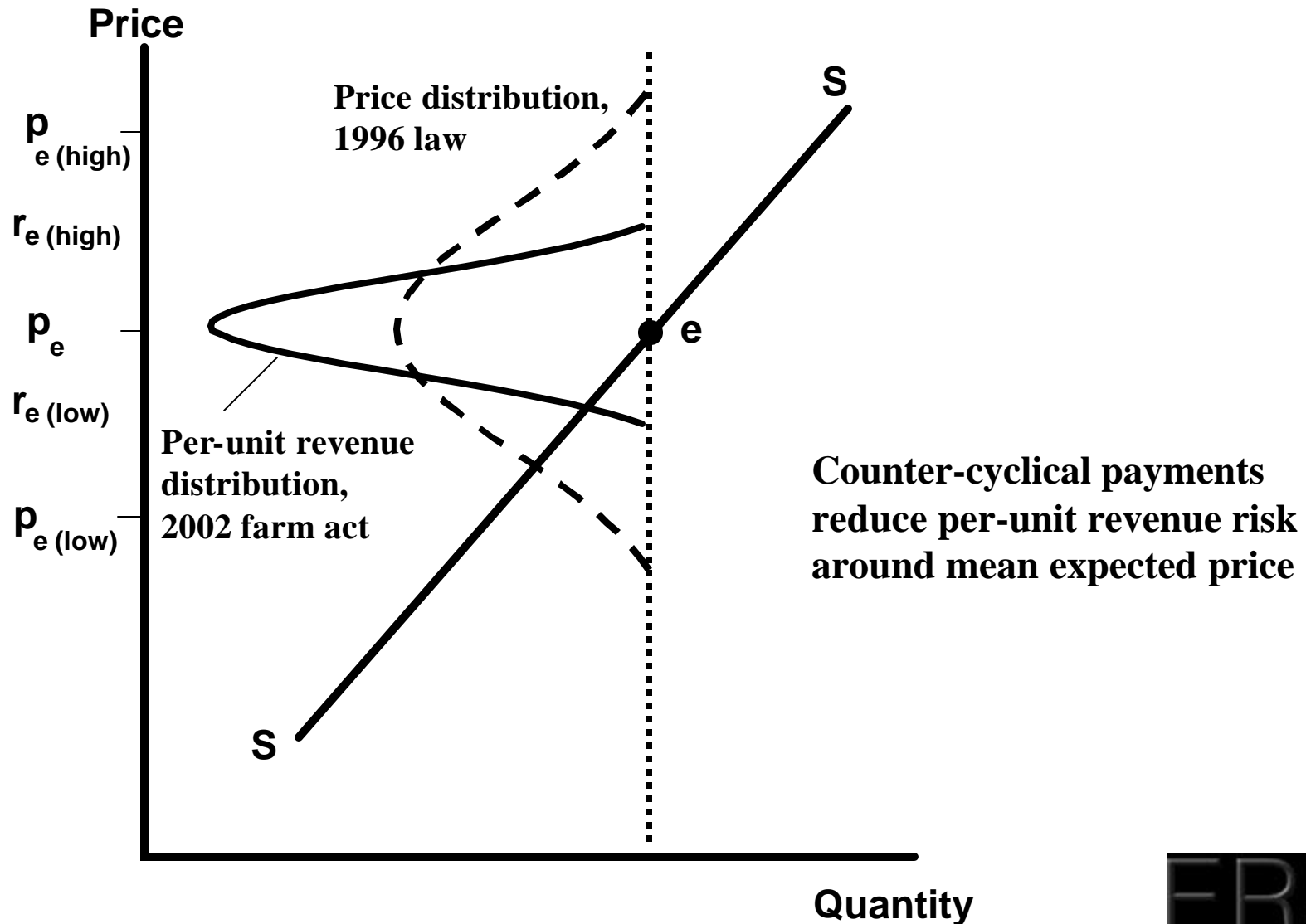
- **USDA's Farm Bill web site**
 - <http://www.usda.gov/farmbill/>
- **Economic Research Service (ERS) web site**
 - <http://www.ers.usda.gov/>
 - **Side-by-side comparison of 1996 and 2002 Farm bills**
<http://www.ers.usda.gov/Features/farmbill/>
 - **Farm bill impacts**
<http://www.ers.usda.gov/publications/aib778/>
<http://www.ers.usda.gov/briefing/FarmPolicy/>



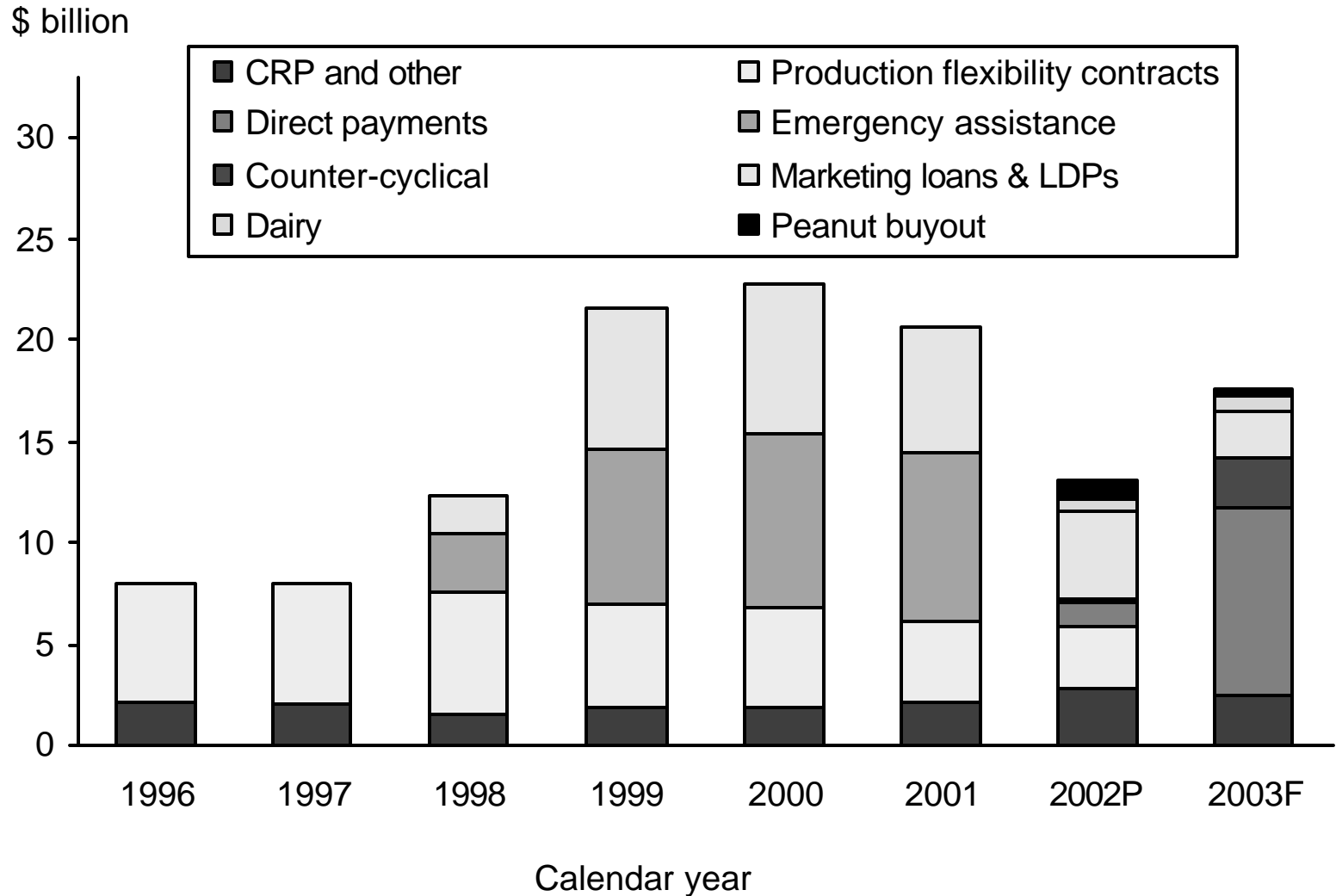
Supply curve and price (per-unit revenue) risk under 1996 farm act (without counter-cyclical payments)



Supply curve and price (per-unit revenue) risk under 1996 farm act (without counter-cyclical payments)



Direct government payments

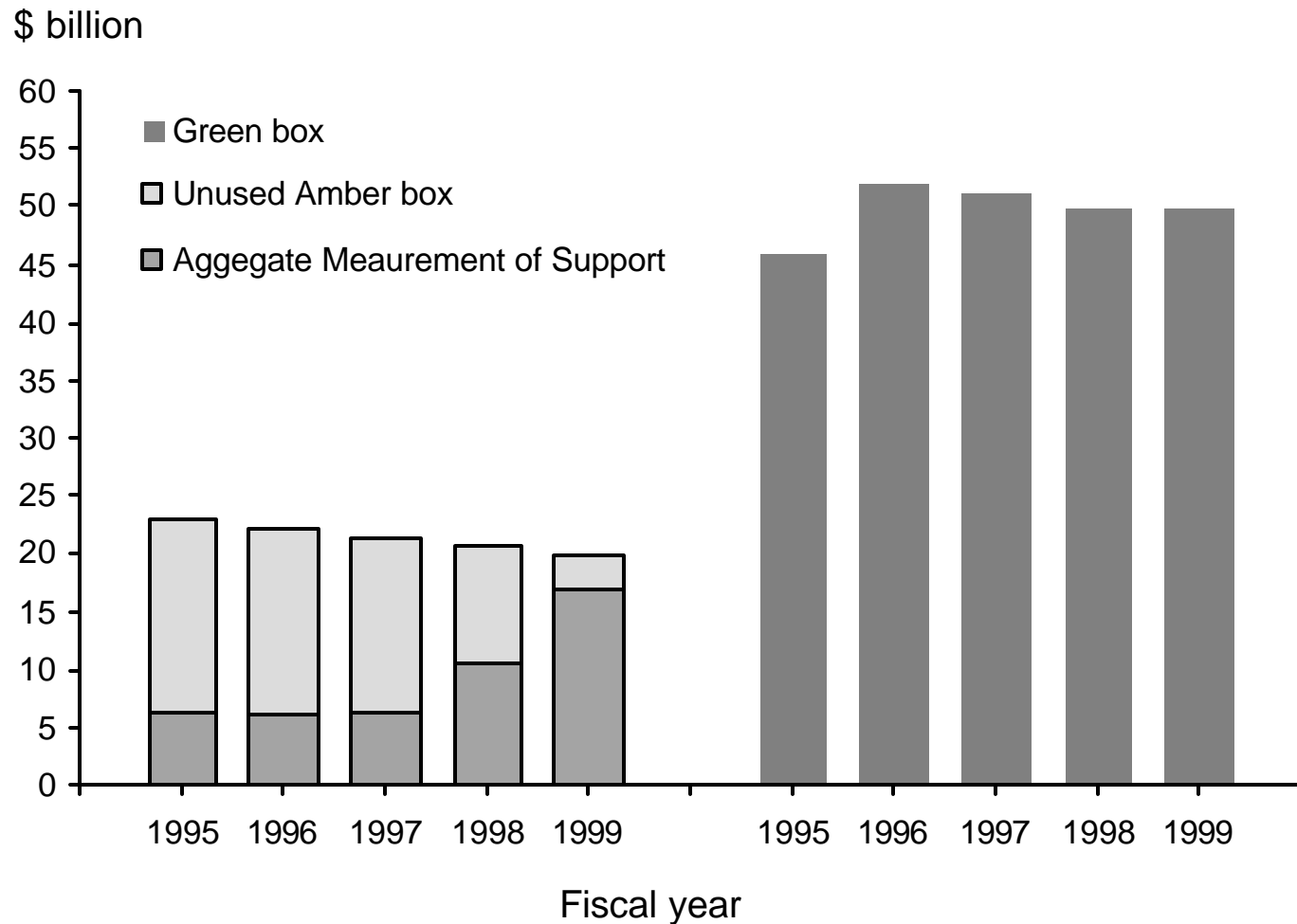


* February 2003 forecast

Source: Economic Research Service, USDA.



U.S. WTO domestic support notifications



Source: WTO Notifications.

