

Policy Pennings by Dr. Daryll E. Ray

# Subsidies and demand

The issue of whether or not the elimination of subsidies among the industrialized nations, particularly the U.S., will result in improved prices for crop farmers around the world is being hotly debated and is deserving of more than one column. In the previous column we talked about the production side of the equation and argued that land has a greater influence on production levels than subsidies.

Because no one farmer can affect price, all farmers have an incentive to plant all of their acres every year, allowing for normal crop rotation requirements. Farmers may change the mix of crops due to relative crop prices and planting conditions, but the incentive is there to plant every possible acre. The net result of all this is total production of crops changes very little, therefore prices change very little.

On the food consumption side of the equation, it is clear that changes in subsidies change nothing. Producer subsidies, almost by definition, do not contract or expand demand (that is, shift the demand curve, as economists say).

If there were to be an indirect effect, it would be because subsidies increased production which lowered price and therefore increased the quantity purchased by consumers (a movement along the demand curve). But that is the point, production is virtually the same with and without subsidies so there is no lower price for consumers to respond to. Any change in mix of crops planted may cause prices for individual crops to rise or decline some but for agriculture as a whole the changes are small and largely offsetting.

Ditto exports. Except for export subsidies (which are inconsequential now), the effect of producer subsidies on exports, compared to no subsidies, is zilch. If price doesn't change perceptibly with the elimination of subsidies, the quantity exported will not change either.

Besides that, both domestic demand and exports respond very little to changes in price anyway. Which means, even if prices were driven down some by subsidies, neither domestic demand nor exports would increase by much.

So just as eliminating subsidies will not materially raise farm prices and incomes here and abroad, neither will eliminating subsidies provide additional business to our export competitors.

It is land in production not subsidies that should receive scrutiny. Those complaining about low crop prices and incomes worldwide are in the right forest but they are barking up the wrong tree.

US farm program changes that eliminated the ability to annually affect the acreage of land used to produce major crops would be the more fruitful "tree" for centering international attention.

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