Early farm program proposals are found wanting

A year away from the expiration of the 2014 Farm Bill, we don’t see a lot in the way of concrete comprehensive proposals for commodity programs.

We have heard discussions coming out of the northern plains about a 3-4-year land idling program to increase crop prices.

There are hints that serious thought is being given to strengthening the target price, Price Loss Coverage (PLC), program as the Agricultural Risk Coverage program is not performing well in the current sub-$4.00 corn price period.

Despite prices, and thus revenue insurance coverage levels, it would be foolish to underestimate the likely influence of the crop insurance industry in the writing of the 2018 Farm Bill.

Adding to the lack of clarity is the slow confirmation process for the next Secretary of Agriculture and the lack of statements by the administration about its view of the direction it wants to take in the setting of farm policy.

As we think about farm policy, we need to keep in mind the economic characteristics of food and farm policy, especially the response to low prices.

Consumers do not respond to low crop prices in the same way that do for other products. With low crop prices, people do not go from eating 3 meals a day to eating 4 or 5. They may eat a better cut of meat or more highly processed food, but the aggregate amount of food consumed basically remains the same. But let the price of large flat screen televisions drop and watch people move to replace their older and smaller televisions, relegating the old TV to a less used part of the house.

This response to low crop prices on the behalf of consumers is called the low price elasticity of demand.

Similarly, when crop prices are low, crop farmers do not significantly reduce their production of crops. They may switch from one crop to another to minimize their losses but they use all their land all the time. As long as the price or hoped-for price is above the variable cost of production they have every incentive to make up for lower prices with increased production.

This response to low crop prices on behalf of producers is called the low price elasticity of supply.

As a result, in response to low crop prices, neither an increase in the quantity demanded nor a decrease in the quantity supplied is sufficient to result in a timely return to farm profitably. Thus, farmers experience long periods of low prices, punctuated by short periods of high prices.

Any farm program policy will be successful only to the extent that it takes into account the low price elasticity of both supply and demand—other issues like the environmental impacts of crop and livestock production will require other criteria. With that in mind, let us look at the three proposals we described above.

A 3-4 year land idling program does respond to the low price elasticity of supply by paying farmers to idle a portion of their cropland—most likely land with some negative environmental impact. But unless an adequate amount of land is taken out of production over a much longer period of time, the price impact may be short lived.

And, without a crop reserve, consumers are not protected in the event of a repeat of the 2012 drought across the Midwest that resulted in significantly reduced corn production. It takes more than a land idling program to provide price stability for crop producers and consumers.

An enhanced PLC program will provide farmers with more income, but—there is always a but—it is very expensive because the payments are made on nearly every bushel, hundredweight, and bale of production and not on just the relatively small quantity that exceeds demand. Secondly, in historic terms, most target price programs like PLC are not adequate for long periods of low prices.

Crop revenue insurance can adequately handle in-year price variability as long the price is profitable, but get a long period of prices well below the full cost of production and it performs poorly as a mechanism to stabilize farm income. Insurance works best when the covered risk is random in nature. Yield variability is a random risk; the price component of the revenue determination is not.

Where does that leave us? Short of a supply management program, we see no options on the horizon that address the economic characteristics of crop agriculture.

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