Important farm program issues

In looking toward a farm bill based on a supply management program, today's column examines planting flexibility, the role of crop insurance, World Trade Organization (WTO) compliance, and the problems that accrue with the failure to regularly adjust crop loan rates.

An important change included in the 1996 Farm Bill was the shift from managing acreage crop by crop to allowing for planting flexibility. Previously, as the demand for crops shifted over time—the need for fewer oats and more soybeans—managing US crop acreage crop by crop resulted in farmers making planting decisions that protected base acres rather than responding to the needs of the marketplace.

With planting flexibility, farmers have the ability to adjust their production decisions based on agronomic limitations and market signals rather than program conditions. Planting flexibility continues to be an important part of the APAC/TFU (Agricultural Policy Analysis Center/Texas Farmers Union) supply management program. Farmers are free to grow any combination of major crops.

Over the last two decades, crop insurance has become an increasingly important part of the farm program with crop revenue insurance coming to the fore during the last 10 years. But, in the long term, crop revenue insurance will not work on a regular basis because of the well-documented historical pattern of the production of agricultural crops exceeding the demand for those crops. This imbalance results in prices that fall below the cost of production, even well below the cost of production. Insuring crops at prices that guarantee a loss makes little economic sense.

Revenue insurance only worked well for corn and soybeans when the prices of both crops were above their full cost of production. To maintain the corn price above the full cost of production during the 2007 and 2013 crop years, it took a 500-million-bushels per year increase in corn demand to satisfy the Renewable Fuel Standard (RFS). Once that steady increase in demand ended, the high prices would have not lasted had it not been for a decline in production between the 2010 and 2012 crop years.

The appropriate role for crop insurance is to cover the random risk (yield) not the systemic risk (price) and, even then, many farmers will not purchase it without a government subsidy. The APAC/TFU farm program uses crop insurance to cover yield declines like that seen in 2012. The loan rate determines the price used in any insurance payment calculation.

In the past, Congress responded to wide-spread crop production problems with ad hoc disaster programs. But legislators did not respond to localized reductions in crop yields due to weather or disease. By using yield insurance, the APAC/TFU farm program protects farmers who purchase it against localized crop production problems.

One of the questions raised about the APAC/TFU policy proposal concerns WTO compliance. Will the proposed program put the US out of compliance with its trade obligations? Supply management programs have traditionally been categorized as Blue Box programs and thus trade legal with certain financial limitations.

From the end of WWII until the Uruguay Round of the General Agreement on Trade and Tariffs, agriculture was not subject to the same rules as trade in general products and services. Supply management was seen as way to manage the chronic problem of oversupply in the crop sector while protecting the land and human resources devoted to agricultural production so that future needs can be met. It was also a program, unlike subsidized crop insurance and counter-cyclical payments, that could be implemented by developing countries.

The final topic for this column is an examination of the problems that arose as the result of the decision of Congress to lower the loan rate as a part of the 1985 Farm Bill and not raise it after a slight increase in the 2002 Farm Bill—and even then, it was kept well below the full cost of production. By keeping the loan rate below steadily increasing production costs, Congress had to establish various measures to increase crop prices and revenue: the RFS and the Counter-Cyclical Program, among others.

The result of this decision was a steady increase in the cost of government programs designed to get farm revenue somewhat in line with the steadily increasing cost of producing essential agricultural crops. With these programs, farmers obtained a key component of their net farm income from the government instead of the market.

In attempting to make farmers less dependent on the government, farm programs since the 1996 Farm Bill have done just the opposite. They have made farmers more dependent on income from government programs.

Under the APAC/TFU supply management program, farmers would receive the bulk of their income from the marketplace, with the government protecting farmers against shortfalls in production.

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