Farmers respond to high crop prices but just keep producing when prices drop

If there is a concept that we have talked about more than any other over the last 22 years, it is the idea that crop agriculture—in particular the major crops: corn, soybeans, wheat, rice, other grains and oilseeds, and cotton—experiences long periods of low prices punctuated by short periods of high prices.

We covered this issue not too long ago, but as a part of a summary of our writings over more than 2 decades, we would be remiss if we did not include it in this last series of columns on the principles that have driven our analysis week after week.

Looking at the price of corn and wheat in the 20th and early 21st centuries we see high prices during World War I, World War II, the years immediately following the entry of the Soviet Union into world grain markets in the early 1970s, the implementation of the Renewable Fuels Standard which required the blending of corn-based ethanol into the US gasoline supply, the outbreak of the recent Russo-Ukrainian War, and years with weather-related production problems.

In most other years farmers faced prices that were well below the full cost of production and depended on government programs to keep them afloat.

One might then logically ask why farmers don’t just reduce production and drive prices higher? After all, that is what economic textbooks suggest producers ought to do. And that would work if it were not for the reality that farmers have large fixed-costs—particularly land, equipment, and taxes. Each extra bushel, bale, and hundredweight of production spreads out the fixed costs out over more units or production and reduces total losses.

Unlike the seed companies and the grain merchandisers where at most a half-dozen firms dominate the market and thus influence the prices they charge, farmers world-wide number in the millions and lack even a sliver of pricing power.

In addition, planting a crop is a gamble with mother nature and the only thing worse than having a poor crop on your land is to reduce production and have little to sell in a year when there is a short crop elsewhere and prices have gone through the roof. We have yet to meet a farmer who is willing to take that risk.

While farmers don’t respond as expected to low prices, their response to the periods of higher crop prices are textbook classic. In the face of high prices, they will convert pasture ground and other areas to cropland in a New York minute. And once that land is brought into crop production, it remains in production for an extended period of time. More than that, it usually takes a large program like the Conservation Reserve Program to reduce production enough to have any impact on long-term crop prices.

In addition to these observations, we would argue that from a humanitarian perspective, it is in humanity’s best interest that we maintain the capacity to overproduce and then find ways to ensure farm financial stability. It is better to sustain farm prices while managing the world’s productive capacity than to run short of food and watch people starve.

From where we sit, we think this is particularly true as we face the issue of global warming with severe storms hitting coastal areas and nearly uncontrollable fires burning hundreds of thousands of acres every spring and summer. In addition, we face the probability that as the climate changes we will see crop production shift from one area to another.

As we see it, policy makers today and into the future are going to have to balance the likelihood of long periods of low prices punctuated by short periods of high crop prices on the one hand with global climate change, coastal flooding, and shifting production areas on the other.

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