PolicyPennings by Dr. Daryll E. Ray

Subsidy elimination: Would it be the panacea seen by some?

If many advocates of trade liberalization had their way, all agricultural subsidies would go the way of the passenger pigeon and dodo bird. They would simply disappear from the face of the earth. The argument is that subsidies distort market signals bringing about excess production of subsidized crops which drives their market prices downward, often below the cost of production. Since the global south cannot afford to pay subsidies, their farmers are forced to compete with below-the-cost-of-production imports coming from the global north.

Hence the argument is that farmers in the global south would benefit from the elimination of farm subsidies that are paid to farmers in the global north, primarily the US and the EU. Without subsidies, it is argued that US and EU farmers would reduce their production of crops which would, in turn, reduce the supply and increase prices for all. In addition this lower production in the US and the EU would expand access for farmers in the global south, allowing them to sell additional products into the lucrative markets of the north.

There is scant evidence that aggregate agriculture responds to price changes with commensurate changes in the amount of land dedicated to crop production. In the period following the adoption of the 1996 Farm Bill, aggregate farm-level prices, adjusted to include all payment types, dropped by as much as 22 percent, while harvested acreage declined by as much as 3.5 percent. It should be noted that the harvested acres in the comparison year, 1996, were higher than in previous years because acreage previously diverted by annual setaside programs was returned to production. Hence the 3.5 percent drop is from an acreage high point.

In those years, as always, farmers shifted land from one crop to another to try to take advantage of any crop that appeared to have the potential of providing a greater financial return. What they did not do was reduce total acreage farmed significantly.

Given this type of behavior on the part of farmers, we should expect that in the absence of subsidies, farmers would shift away from crops with high production costs in favor of crops with lower production costs. Some acreage would move out of cotton and rice production and into corn and soybean production. But farmers would plant all of their cropland all of the time unless prevented from doing so by weather events.

Over time some farmers would run out of resources to tap and would either go bankrupt or quit farming. In the former case, the land would be sold to a new operator who most likely would keep it in production. In the latter case, the farmer would lease it to a neighbor who also would return it to production. Farmers may leave the agricultural production sector, but, with few exceptions, the land remains as active as ever.

Over time, the price of land would drop in an attempt to lower the US cost of production to better match the cost of production in competitor countries like Brazil. Under these constraints some small amount of acreage undoubtedly would be shifted to the production of minor crops or to pasture, but the resulting reduction in production likely would be minimal.

The financial impact of the decapitalization of land in farming areas would be significant especially on local school districts who receive a significant portion of their revenue from property taxes, much of which is based on agricultural land. Other government services from law enforcement to streets and roads would also be negatively affected by a deep and permanent cut in the value of agricultural land.

Farmers who used land as a collateral for their loans (and many do) would find themselves in a financial crisis as the price of land fell. Country banks would have to pull their loans because of insufficient collateral and unless the farmer had another source of cash, the farm would have to be sold to satisfy the loan. As a result land prices would continue to tumble for some time. Under this scenario, banks with considerable ag based loans would face some solvency issues.

With less to spend, farmers would reduce their purchases of capital equipment like trucks, tractors, and combines using them for several years longer than they presently do. Implement dealers and Main Street retailers would be faced with lower farm related sales as well. Undoubtedly churches and civic organizations would also feel the pinch.

Stress levels would be high across rural farming communities. If the experience of the 1980's is at all relevant the number of suicides would increase dramatically as would the number of divorces. The decapitalization of farming communities, brought on by the ending of all subsidies, would also increase the rural to urban migration pattern that has been evident for the past century.

Through all this, the level of production of US aggregate crop agriculture would decline very little. The crop mix would change, but the relatively small increase in crop prices would be a fraction of the per bushel payments farmers currently receive.

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