2012 Farm Bill: Will Current Premises Match the Reality of the Future?

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2012 Farm Bill: Issues and Challenges
Organized by U.S Senator Kent Conrad and Won W. Koo, North Dakota State University

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2012 Farm Bill
Economic Expectations

• Extremely low prices won’t happen again
  – Never see sub-$3 corn prices
  – Ethanol and export demand will see to that

• 9.5 billion people in the world by 2050
  – 95 percent of which reside outside the U.S.

• 70% more food will be needed
  – Implicitly assumed that the U.S. will be THE major beneficiary
2012 Farm Bill
Most Popular Policy Direction

• Revenue insurance is the way to go...
  – Insurance engenders positive connotations
  – Private sector is involved (bringing to mind lower costs)
  – Follows the market (and that must be a good thing)
  – Anyway given the a bright prosperous future:
    • Evening out revenue bumps won’t be that big of a deal
Reality Clashes?

- Reality 1: Ethanol demand
  - Represents most of recent increase in grain demand
  - Should not expect that rate of growth during the next five years
Reality Clashes?

• Reality 2: U.S. may benefit little from the 70% increase in food needs by 2050
  – Major growth areas will likely expand their own production (China, India, Africa…)
  • Extreme political pressure to be self-sufficient
  • Farm families make up 60% of population
    – Increasing production promotes economic development
    – Reducing post-harvest loss can quickly increase effective yield
    – 99.5% of farmers are outside the US
    – Pushing farmers off farms only enlarges urban problems
Reality Clashes?

• Reality 2 (cont.): U.S. may benefit little…
  – U.S. export competitors will likely gobble up trade growth for grains and oil seeds
    • For a third of a century, total US crop exports have been flat
    • Trends in U.S. shares of exports have plummeted
**US and World Exports of 5 Grains and Soybeans, 1980-2010**

Five grains: corn, wheat, milled rice, barley and oats.
US Percent of and World Exports of 5 Grains and Soybeans, 1980-2010

US 5 Grains and Soybean Exports as % of World

Percent


Five grains: corn, wheat, milled rice, barley and oats.
So the US Share of World Exports Has Dropped Precipitously

US Soybean Exports as % of World Exports
Reality Clashes?

- Reality 2 (cont.): U.S. may benefit little...
  - U.S. export competitors will likely gobble up trade growth for grains and oil seeds
    - For a third of a century, total US crop exports have been flat
    - Trends in U.S. shares of exports have plummeted
    - Export competitors have more head room than the U.S. to increase agricultural production
      - Open land available in S. America and other countries
      - Yields can be increased by closing technology gaps
Reality Clashes?

• Reality 3: There are no price floors
  – Yes, the price standard for corn increased from $1 per bushel to $2 following the 1970s
    • Commodity Credit Corp supported crop prices and did so at a higher level reflecting inflation
  – Nothing now to stop a catastrophic drop in prices
    • The CCC non-recourse loans cannot do it
    • Loan deficiency and other payments cannot do it
    • Revenue insurance cannot do it
    • Future growth in ethanol and export demand would be helpful but doubtfully a floor
  – Corollary: Land prices could easily be the new “house of cards”
Reality Clashes?

• Reality 4: Possible conclusion from all this…
  – Should not rule out worldwide excess capacity and multiple years of very low prices
    • This happened after the price surge in the 1970s
      – Other countries responded to the high prices and fear of food insecurity by increasing production over time
      – Export demand collapsed
      – The resulting U.S. excess agricultural capacity in the early 1980s turned out to be over 30 million acres
      – And became known as the Conservation Reserve Program
  – Possibility of “too much” production sounds weird, but it sounded weird in the 1970s too
Reality Clashes?

• Reality 5: High-price periods are worst times to do a farm bill...
  – Provisions are put into the farm bill that work during those high-price times
    • Decoupled payments in 1996 FB—prices were high in 1996 when bill was passed
    • High interest in revenue insurance this year—when prices are high “pure profits” could be virtually guaranteed
  – But are completely inadequate/inept when prices go well below the cost of production for multiple years
Reality Clashes?

- Reality 6: Let’s get serious about insurance!
  - It is designed to protect against random incidents
    - A relatively predictable proportion of insurance pools will have their house burn down
  - It is not well-suited for incidents that affect the entire pool of insurance clients
    - All houses do not burn down at once (if that was a possibility—like during wartime—those events would be excluded from coverage)
  - Insurance is primarily for individual incidents not incidents that affect everybody
Reality Clashes?

• Reality 6 (cont.): What about ag then?
  – Makes sense to insure against incidents that affect production of individual farmers or subgroups of farmers
    • Like yield and prevented planting problems
      – especially hail, wind, floods, etc.
      – Rates could/would differ, including by region
  – Not indicated for incidents that affect all farmers (that is, those that are systemic)
    • Like severe price drops, especially for multiple years
    • Ditto price-caused drops in revenue
Reality Clashes?

• Reality 7: Revenue insurance tends to be an upside-down safety net
  – When prices are high, revenue insurance provides protection
    • Depending on circumstances, could guarantee profits well above all production costs
    • Courtesy of U.S. taxpayers
  – When prices remain very “low,” revenue insurance does not provide a meaningful safety net
    • “Guarantees” a proportion of low prices, even when prices are well below production costs

Attractively painted “revenue-insurance bandwagon” seems structurally unsound
Modifications, then?

- The proverbial train (bandwagon) has left the station, what can be done?
  - Keep, but modify
    - Protect taxpayers by limiting revenue insurance to cover no more than a portion of production costs
    - Better protect farmers by requiring that revenue insurance cover at least variable production costs
    - Reduce administrative costs
      - For example, fixed agent fee per policy (or let FSA do it!)
  - Start over—let insurance do what it does best
    - Limit taxpayer subsidized insurance to yield shortfalls or prevented planting (Could provide it free so no need for emergency disaster payments)
    - Use other programs for price protection
Summary

- Conventional wisdom seems to be that we are in a “new price and income era”
- Last time we had similar price situation, worldwide production increases slammed U.S. agriculture
- This time there is no floor on crop prices
- Need a policy for all seasons
- Without modification, current revenue insurance proposals provide a safety net when prices are “high” but not much help when prices are “low”
  - Déjà vu all over again?
  - Possible return to the use of emergency payments like after the 1996 Farm Bill?
Thank You

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