DESIGNING AN APPROPRIATE POLICY FRAMEWORK FOR PRODUCTION AGRICULTURE: SEEKING POLICY COMPLEMENTARITIES

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2012 Farm Bill: Issues and Challenges
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DESIGNING AN APPROPRIATE POLICY FRAMEWORK FOR PRODUCTION AGRICULTURE: SEEKING POLICY COMPLEMENTARITIES

- The role and importance of policy complementarities
- A case of policy complementarity in the 2012 farm bill
- The difficult search for complementarities
- Some conclusions
DESIGNING AN APPROPRIATE POLICY FRAMEWORK FOR PRODUCTION AGRICULTURE: ROLE & IMPORTANCE OF COMPLEMENTARITIES

- The “Tinbergen Rule”: In any area of public policy, there must be as many policy tools as policy targets.

- Each policy tool has a comparative advantage/disadvantage at achieving each policy target
  - Advantage/disadvantage:
    - Degree to which the tool increases Objective A
    - Degree to which the tool decreases Objective B
DESIGNING AN APPROPRIATE POLICY FRAMEWORK FOR PRODUCTION AGRICULTURE: ROLE & IMPORTANCE OF COMPLEMENTARITIES

- Examples of Tinbergen’s Rule” and public policy
  - Macroeconomics
  - Pre-1996 farm programs

- The Tinbergen Rule and today’s farm policy

- A case of complementarity for 2012
Two dead birds, one stone... It just doesn't add up...
Some trade objectives of U.S. agricultural policy

Some nutrition objectives of U.S. agricultural policy

Some complementarities of trade and nutrition objectives in U.S. agricultural policy
SEARCHING FOR POLICY COMPLEMENTARITY IN THE 2012 FARM BILL

- Some trade objectives of U.S. agricultural policy
  - Market access as an objective of U.S. agricultural policy
EVOLUTION OF THE FRUIT, VEGETABLE AND WILD RICE PLANTING RESTRICTION

- FAVR originated in Food, Agriculture, Conservation, and Trade Act of 1990 (FACT)
- FACT established “triple-base” flexibility for program base (15% Normal Flex with no payment and 10% Optional Flex with option of no payment)
- Producers permitted to plant on NFA and OFA “any program crop, oilseed, industrial or experimental [or] other crop, except any fruit or vegetable crop (including potatoes and dry edible beans)”
- Secretary may determine crops that could not be planted on Normal Flex or Optional Flex acreage
EVOLUTION OF THE FRUIT, VEGETABLE AND WILD RICE PLANTING RESTRICTION

- FAVR continued in Federal Agriculture Improvement and Reform Act of 1996 (FAIR)

- Program crop producers not permitted to plant fruits or vegetables (other than lentils, mung beans, and dry peas) on base acreage
  - Exceptions for region of double cropping, farm or producer w/ history of producing fruits or vegetables

- Violation of FAVR: loss of direct, countercyclical and market loan payments on all base acres

- FAVR largely unchanged in 2002 and 2008 farm bills. Renamed “Fruit, Vegetable and Wild Rice Planting Restriction” (FAVR)
ISSUES IN THE WTO COTTON DECISION

- Brazil challenge to U.S. cotton program
  - Step 1 & 2: Payments to U.S. cotton mills
  - Marketing loans/LDPs repaid at world price
  - PFC/Countercyclical Payments
  - Operational rules of U.S. programs (FAVR)
2002: THE ROLE OF THE FAVR IN THE WTO COTTON CASE

“The amount of such [direct] payments . . . shall not be related to, or based on, the type or volume of production . . . undertaken by the producer in any year after the base period.”

--WTO Agreement on Agriculture, Annex 2, paragraph 6(b)
2004: THE ROLE OF THE FAVR IN THE WTO COTTON CASE

“The [FAVR] limitations...constrain production choices available to PFC and DP payment recipients and effectively eliminate a significant proportion of them.... [T]he Panel concludes that PFC payments, DP payments, and the legislative and regulatory provisions that provide for the planting flexibility limitations in the DP programme, do not fully conform with paragraph 6(b) of Annex 2 of the Agreement on Agriculture.”

--WTO Panel, United States Subsidies on Upland Cotton

- **2004 – 2008**: U.S. files and loses multiple appeals of WTO Panel decision

- **2008**: U.S. passes farm bill with FAVR unchanged

- **2009**: Brazil requests WTO approval of $829M in retaliatory tariffs on U.S. exports – request granted by WTO

- **March 2010**: Brazil proposes new tariffs on 102 U.S. products

- **March 2010**: Brazil announces new tariffs on 102 U.S. products within 30 days

- **March 2010**: U.S. requests settlement negotiations, Brazil delays tariff implementation

- **April 2010**: U.S./Brazil announce settlement of negotiations, U.S. to pay $147M annually in damages to Brazilian cotton industry
Brazils victory in cotton trade case exposes Americas wasteful subsidies

Thursday, June 3, 2010. A16

AMERICAN taxpayers owe Brazil and its cotton farmers a thank-you. That may sound odd, given that the Obama administration recently agreed to pay the Brazilians $147.3 million a year to settle their international trade case against U.S. cotton subsidies. Indeed, the net effect of the payoff is to enable Washington to continue supporting American cotton farmers to the tune of about $3 billion per year. So what's to be thankful for? Brazil's case laid bare the truth about the U.S. cotton program: Not only is it a wasteful sop to special interests, but it's also an obstacle to free and fair trade that needlessly complicates U.S. relations with the rest of the world. Reform -- or, better, repeal -- is long overdue.

The federal government has spent more than $50 billion propping up cotton growers since 1991, with subsidies averaging more than $3 billion per year over the past decade. Most of this aid supports large, politically connected agribusinesses in the Sun Belt -- although the Arkansas Department of Corrections' operation, manned by convicts, has also received some of the cash. Thanks partly to the subsidies, U.S. producers can outcompete lower-cost producers on the world market; American farms account for about 40 percent of global exports. In 2002, Brazil complained to the World Trade Organization about this, arguing that the U.S. programs violated international free-trade agreements that the United States itself had championed. It took a while, but the WTO has agreed, authorizing Brazil to retaliate bylevying tariffs against other American products. Brazil's threat to use that authority against U.S. goods, from wheat to software, forced the Obama administration to buy a truce last month.

In short, the U.S. cotton industry's dependence on subsidies that violate international trade agreements turned it from a mere waste of taxpayer money into a threat to other American exporters and the jobs they support. As four House members, Democrats Ron Kind (Wis.) and Barney Frank (Mass.) and Republicans Jeff Flake (Ariz.) and Paul D. Ryan (Wis.), put it in a recent letter to the president, the cotton program is "quickly becoming a liability for future trade growth. Instead of effectively reforming our programs, we are electing to pay $147.3 million annually to Brazilian agribusiness so that we can continue to pay around $3 billion a year to large U.S. agribusiness." Of course, the federal government must borrow much of the $147.3 million and the $3 billion. If this sorry episode doesn't shame Washington into ending this fiasco, nothing will.

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The Madness of Cotton

The feds want U.S. taxpayers to subsidize Brazilian farmers.

U.S. cotton farmers took in almost $2.3 billion dollars in government subsidies in 2009, and the top 10% of the recipients got 70% of the cash. Now Uncle Sam is getting ready to ask taxpayers to foot the bill for another $147.3 million a year for a new round of cotton payments, this time to Brazilian growers.

We realize that in today's Washington this is a rounding error. But the reason for the new payments to foreign farmers deserves attention. If it becomes a habit, it is unlikely to end with cotton.

Here's the problem: The World Trade Organization has ruled that subsidies to American cotton growers under the 2008 farm bill are a violation of U.S. trading commitments. The U.S. lost its final appeal in the case in August 2009 and the WTO gave Brazil the right to retaliate.

Brazil responded by drafting a retaliation list threatening tariffs on more than 100 U.S. exports, including autos, pharmaceuticals, medical equipment, electronics, textiles, wheat, fruits, nuts and cotton. The exports are valued at about $1 billion a year, and the tariffs would go as high as 100%. Brazil is also considering sanctions against U.S. intellectual property, including compulsory licensing in pharmaceuticals, music and software.

The Obama Administration appreciates the damage this retaliation would cause, so in April it sent Deputy U.S. Trade Representative Miriam Sapiro to negotiate. She came back with a promise from Brazil to postpone the sanctions for 60 days while it considers a U.S. offer to—get this—let American taxpayers subsidize Brazilian cotton growers.

That's right. Rather than reduce the U.S. subsidies to American cotton farmers that are the cause of the trade fight, the Administration is proposing that U.S. taxpayers also compensate Brazilian cotton farmers for the harm done by the U.S. subsidies. Thus the absurd U.S. cotton program would dip into the Commodity Credit Corporation to pay what is a bribe to Brazil so it won't retaliate.

Talk about taxpayer double jeopardy. As Senator Richard Lugar (R., Ind.) said recently, the commodity credit program was established to assist U.S. agriculture, "not to pay restitution to foreign farmers who won a trade complaint against a U.S. farm subsidy program."

Mr. Lugar wants the subsidies to U.S. farmers cut by the amount that will have to be sent to Brazil. He adds that a better option would be to take on the trade-distortions of the cotton program. "I am prepared to introduce legislation to achieve these immediate reforms," he wrote in an April 30 letter to President Obama.

This is probably tilting at political windmills, since Mr. Obama has shown no appetite for trade promotion, much less confronting a cotton lobby supported by such Democrats as Arkansas Senator Blanche Lincoln. But we're glad to see that at least Mr. Lugar is willing to call out the absurdity of U.S. taxpayers subsidizing foreign farmers to satisfy the greed of a few American cotton growers.
APPLICATION OF BRAZIL COTTON CASE IN THE CANADIAN CORN DUMPING CASE

- Canadian corn growers filed dumping/subsidy complaint against US corn exports in 2005

- Most Canadian corn imports originate in MI, OH, MN, ND, SD

- Occurred during harvest disruption following Katrina, received little attention
OVERVIEW OF CANADIAN DUMPING/COUNTERVAILING DUTY LAW

- Canadian law virtually identical to U.S. law (and WTO requirements). Determination of:
  1. Does dumping or subsidization exist?
  2. Does it cause injury or threat of injury to producers in Canada?

- Definitions:
  Dumping: Good imported into Canada at prices lower than similar goods sold in export country
  Subsidizing: Goods imported into Canada that benefit from foreign government financial assistance.
  Injury: Evidence that imported product displaces Canadian goods or reduces/restrains prices for Canadian goods.
OVERVIEW OF CANADIAN DUMPING/COUNTERVAILING DUTY LAW

- **Determination of existence of subsidy:**
  1. Financial contribution by foreign government
  2. Specific – 1 of 4 definitions:
     - the manner in which discretion is exercised by the granting authority indicates that the subsidy is not generally available.

- **Determination of existence of subsidy:**
  Countervailing tariff applied equal to the size of the subsidy
RESULTS OF CANADIAN DUMPING/SUBSIDY INVESTIGATION

- Canada’s preliminary rulings on issues

Dumping and subsidizing of U.S. corn into Canada was occurring

Threat of injury to Canadian corn growers was posed by U.S. dumping/subsidization

Tariffs imposed pending injury ruling:
- 60 cents/bushel for dumping
- 45 cents/bushel for subsidization
“[A] WTO Panel examined the direct payment program in *Upland Cotton* and found that this program was an actionable subsidy under the Subsidies Agreement.… [T]he Appellate Body stated that *the direct payments did not qualify as “green box” subsidies … because such payments were denied if certain specified crops were produced*. This ban … had the effect of channeling production toward crops that were eligible for payments.… *Fruits, vegetables and wild rice production are generally not eligible for payment benefits under the DCP program*. This restriction… indicate[s] that the program is not "generally available" and that *the program meets the specificity provisions* outlined in [Canadian countervailing duty law].”
RESULTS OF FINAL CANADIAN INJURY INVESTIGATION

- Standards for determination of injury:
  - Volume of imports
  - Price suppression
  - Lost market share

- Results:
  - Injury to Canadian corn industry not due to U.S. subsidies. Conclusions:
    - Due largely to changes in exchange rate.
    - Widening gap of U.S.-Canadian prices.
    - Large share (38%) of Canadian corn used on-farm. If no sale, then no injury possible.
    - No threat of future injury – uncertain after 2007
SEARCHING FOR POLICY COMPLEMENTARITY IN THE 2012 FARM BILL

- Some trade objectives of U.S. agricultural policy

- Some nutrition objectives of U.S. agricultural policy
  - Diet and health as an objective of U.S. agricultural policy
OTHER ISSUES: NUTRITION AND THE FUTURE OF FARM PROGRAMS

USDA's subsidies ignore its own dietary advice

By Andrew Martin
Washington Bureau
Published May 2, 2005

WASHINGTON -- The only reference to corn on the Department of Agriculture’s new food pyramid is an image of a bright-yellow ear among a medley of other vegetables. Soybeans aren’t mentioned at all.

But corn and soybeans receive a good chunk of the $15 billion in subsidies to farmers that the Agriculture Department is doling out this year. And while that might seem logical because the food pyramid advocates a plant-based diet, most of the corn and soybeans grown in the U.S. are used to make things like chicken feed and ethanol.
I'm confused. Does level RED mean severe risk of terrorist attacks, or eat more fruit?
Why Does a Salad Cost More Than a Big Mac?

Federal Subsidies for Food Production, 1995-2005*

- Vegetables, Fruits: 0.37%
- Sugar, Oil, Starch, Alcohol: 10.69%
- Nuts and Legumes: 1.91%
- Grains: 13.23%
- Meat, Dairy: 73.80%

Federal Nutrition Recommendations

- Sugar, Oil, Salt (use sparingly)
- Protein: includes meat, dairy, nuts, and legumes (6 servings)
- Vegetables, Fruits (9 servings)
- Grains (11 servings)
Why Does a Salad Cost More Than a Big Mac?

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- Grains (11 servings)

Corn & Soybeans
March 1, 2008

OP-ED CONTRIBUTOR

My Forbidden Fruits (and Vegetables)

By JACK HEDIN

Rushford, Minn.

IF you’ve stood in line at a farmers’ market recently, you know that the local food movement is thriving, to the point that small farmers are having a tough time keeping up with the demand.

But consumers who would like to be able to buy local fruits and vegetables not just at farmers’ markets, but also in the produce aisle of their supermarket, will be dismayed to learn that the federal government works deliberately and forcefully to prevent the local food movement from expanding. And the barriers that the United States Department of Agriculture has put in place will be extended when the farm bill that House and Senate negotiators are working on now goes into effect.
The Fat of the Land: Do Agricultural Subsidies Foster Poor Health?

Ever since the Great Depression, American farmers have been the beneficiaries of a medley of subsidies and support programs meant to stabilize crop prices, keep farmers farming, and provide U.S. families with an affordable, reliable supply of food. But these programs may have had an unintended side effect. Rather than keep Americans healthy, critics say, these policies have contributed to today's obesity pandemic and other nutrition problems as well.

Writing in the 2004 Annual Review of Nutrition, James Tiltonson, a professor of food policy and international agriculture at the University of Illinois at Urbana-Champaign, argues that the very programs intended to benefit farmers have contributed to the obesity epidemic.
THE ROLE OF THE FAVR IN THE 2012 FARM BILL DEBATE

- Should FAVR be eliminated to protect DCP farm program payments at WTO?
  - FAVR applies to all program crops, not just cotton
  - WTO ruling on cotton was used in 2005/06 Canada dumping case against U.S. corn

- If FAVR eliminated, two key questions:
  - What impact on FAVR crop markets?
  - If market impact significant, what is equitable compensation (if any) for FAVR crop producers?
Michigan: A State at the Intersection of the Debate Over Full Planting Flexibility

By Suzanne Thornsbury, Lourdes Martinez, and David Schweikhardt; Department of Agricultural Economics, Michigan State University

ERS project representative: Barry Krissoff
barryk@ers.usda.gov, 202-694-5250

Abstract

Greater flexibility in U.S. farm programs with elimination of the restriction on the planting of fruit and vegetable (FAVR) crops is likely to be a major issue in congressional 2007 farm policy discussions. Michigan is a state with a wide range of both FAVR and program crops planted under the current policy. To capture the diversity of situations that would apply among crops covered by the current policy, this research has examined a broad set of Michigan FAVR crops (dry beans, pickling cucumbers, processing tomatoes, fresh market tomatoes, squash, and blueberries). We evaluate both those factors that are likely to prevent the entry of Direct and Counter-Cyclical Program (DCP) crop producers into the production of FAVR crops (barriers to entry or disincentives) and those factors that are likely to encourage DCP crop producers to enter the production of FAVR crops (inducements to entry or incentives). The balance will determine the likely outcome from policy changes to enhance flexibility.
40 percent of the total and in Texas they accounted for 20 percent.

Table 3. Average Annual Cash Receipts from DCP and FAVR Crops in Selected States, 2000 - 2004

<table>
<thead>
<tr>
<th>State</th>
<th>DCP Crops</th>
<th>FAVR Crops</th>
<th>Total</th>
<th>FAVR Crop Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illinois</td>
<td>5,832,996</td>
<td>89,723</td>
<td>5,922,719</td>
<td>2 percent</td>
</tr>
<tr>
<td>Indiana</td>
<td>2,938,927</td>
<td>155,217</td>
<td>3,094,144</td>
<td>5 percent</td>
</tr>
<tr>
<td>Texas</td>
<td>2,552,617</td>
<td>626,814</td>
<td>3,179,431</td>
<td>20 percent</td>
</tr>
<tr>
<td>Michigan</td>
<td>859,550</td>
<td>634,851</td>
<td>1,494,401</td>
<td>42 percent</td>
</tr>
<tr>
<td>California</td>
<td>2,411,547</td>
<td>15,953,982</td>
<td>18,365,529</td>
<td>87 percent</td>
</tr>
<tr>
<td>Florida</td>
<td>102,558</td>
<td>3,067,924</td>
<td>3,170,482</td>
<td>97 percent</td>
</tr>
</tbody>
</table>

Source: National Agricultural Statistics Service for each state

**Michigan DCP and FAVR crop allocation**

Clearly, when compared to national totals the share of Michigan DCP crops is relatively low, representing only around two percent of total DCP and CAB crop area (4.8 million acres) in the country (Table 1). Main DCP crops in the state are corn and soybeans which represent around three percent of total U.S. DCP area of these crops (2 million acres). Not all acreage in these crops is enrolled in farm policy programs. Total
<table>
<thead>
<tr>
<th>Crop</th>
<th>Capital Investment</th>
<th>Rotation Restrictions</th>
<th>Market Accessibility</th>
<th>Labor &amp; Mgmt Needs</th>
<th>Financial Incentives</th>
<th>Likelihood of Conversion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dry Beans</td>
<td>Low</td>
<td>Low</td>
<td>Low to Med</td>
<td>Low</td>
<td>Med</td>
<td>High</td>
</tr>
<tr>
<td>Pickling Cucumbers</td>
<td>High</td>
<td>Med to High</td>
<td>High</td>
<td>Med to High</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Processed Tomatoes</td>
<td>Med to High</td>
<td>Med to High</td>
<td>High</td>
<td>Med to High</td>
<td>Low</td>
<td>Low to Med</td>
</tr>
<tr>
<td>Fresh Market Tomatoes</td>
<td>High</td>
<td>Med to High</td>
<td>High</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Squash</td>
<td>Low to Med</td>
<td>Med to High</td>
<td>Med to High</td>
<td>Med</td>
<td>Low</td>
<td>Med to High</td>
</tr>
<tr>
<td>Blueberries</td>
<td>High</td>
<td>High</td>
<td>Med</td>
<td>Low</td>
<td>Low</td>
<td>Low</td>
</tr>
</tbody>
</table>

Source: Authors’ analysis based on interviews

*a Does not include limited volume sales through outlets such as farmers markets or roadside stands*
SUMMARY AND CONCLUSIONS

Due to the recent WTO cotton ruling in the U.S./Brazil case, the FAV planting restriction is likely to be lifted in future U.S. farm policy. The FAV industry fears that the lifting of this restriction will cause declining FAV prices due to increased FAV plantings by DP and CCP program participants. The objective of this study was to estimate potential changes in crop planting preference in the LRGV due to a lifting of the FAV planting restriction.

Based on a mean NI ranking, cabbage becomes preferred over grain sorghum when the planting restriction is lifted and corn base or grain sorghum base acreage is used. Using cotton base acreage, watermelon becomes preferred over cotton, and cabbage becomes preferred over corn.

When risk (variability) is accounted for, the following changes occur in ranking for risk-preferring producers: watermelon becomes preferred over cotton when moving to scenario 2b.
DOMESTIC EQUITY ISSUES IN RESOLVING THE FAVR ISSUE

- If FAVR eliminated:
  - What impact on FAVR crop markets?
    - Most fruit and vegetable crops have substantial barriers to entry
    - Existing DCP payments per acre unlikely to overcome barriers to entry for many FAVR crops.
    - Dry beans most likely to be affected.
  - If impact major, what is equitable compensation (if any) for FAVR crop producers?
<table>
<thead>
<tr>
<th>Crop</th>
<th>(1000 ac.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>All wheat</td>
<td>8,400</td>
</tr>
<tr>
<td>Soybeans</td>
<td>4,070</td>
</tr>
<tr>
<td>Hay</td>
<td>2,550</td>
</tr>
<tr>
<td>Corn</td>
<td>1,880</td>
</tr>
<tr>
<td>Dry beans</td>
<td>770</td>
</tr>
<tr>
<td>Lentils</td>
<td>255</td>
</tr>
<tr>
<td>Potatoes</td>
<td>80</td>
</tr>
</tbody>
</table>
SOME CONCLUSIONS

Complementarities exist in U.S. agricultural policy

Policy complementarities can’t solve all the difficult trade-offs in U.S. agricultural policy
Policy complementarities exist in U.S. agricultural policy.

Policy complementarities can’t solve all the difficult trade-offs in U.S. agricultural policy.

The growing list of policy targets (objectives) in U.S. agricultural policy requires more policy tools and more policy complementarities.
Some policy targets in U.S. agricultural policy

- Stabilize farm income
- Protect environmental resources
- Safe and nutritious diet for consumers
- Control budget cost for taxpayers
- Maintain international competitiveness/market access

Hitting multiple targets requires finding as many complementarities as possible