The Economic Recovery Program and the 1981 Farm Bill

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I want to thank you for inviting me to this year's annual meeting of the Western Agricultural Economics Association. As an agricultural economist and a member of the Reagan Administration, this is both a professional challenge as well as an opportunity to discuss with you the economic principles underlying our farm policy proposals.

Once every four years, Congress and the Administration are faced with the task of reviewing, amending, or drafting new farm legislation. Although some people believe that this legislation addresses all dimensions of farm policy, it is not all-encompassing. The farm bill does authorize farm commodity programs, but not all of them. For example, the tobacco program is not a part of the farm bill. This year's farm bill also authorizes agricultural research programs, redirects some of the Federal conservation effort, and reemphasizes agricultural exports.

The process of formulating the 1981 Farm Bill began even before the Reagan Administration took office. The November 4 election was a starting point, expressing the general mood of the Nation for change. From November to January, farm and commodity organizations met to draft their proposals. At the same time, the Reagan agriculture transition team initiated a close examination of current farm policies and programs to determine if they were cost effective, actually helped producers, and were genuinely needed.

By February, the Congress had begun to work on the farm bill. In March, the House and Senate Agriculture Committees held hearings in which members of Congress, farm organizations and other interested groups and individuals expressed their views. On March 31, Secretary Block presented the Administration's bill to the House Committee. By May 19, both Committees had completed the first round of work on the farm bill.

The budget process has played a far greater role in the development of farm legislation this year than at any time in the past. It soon became evident that the farm program authorizations outlined in Congress would exceed the $2.1 billion limit allowed by the first concurrent budget resolution for fiscal year 1982. On examination, it was found that the House was approximately $1.4 billion, and the Senate $100 million over this limit. Therefore, both Agriculture Committees reconvened during the first week of June to make additional program changes to meet a June 12 deadline for budget reconciliation. At this time, much still remained to be done. House and Senate floor debate will not begin until early September. A conference committee will have to be formed once the Senate and House floor action is completed to produce the final version of the farm bill, then both houses will vote on this compromise package. Upon passage, it will be ready for Presidential action.

Timing is a critical factor in the legislative process because without new legislation, or a reenactment of current legislation, programs will revert to basic legislation beginning October 1.

Basic legislation, created thirty years ago, is incompatible with current market conditions. Programs would become less market-oriented, leaving producers with less latitude in their decisionmaking. For example, reversion to basic legislation would reinstitute al-

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lotments for wheat and cotton, and quotas and high levels of price support could again become the norm.

Economic Principles Underlying the Administration's Program Proposals

The President's economic recovery program focuses on tax and spending cuts that are intended to bolster supply, encourage investment and increase productivity. It calls for carefully designed policies at the macro and micro level of the economy.

The election of President Reagan signaled a shift within this Nation toward a more stable monetary system, an environment of freely moving wages and prices, reduced government spending and borrowing, and a reduction in government barriers to risk-taking and enterprise. Economists have advocated many of these policies for agriculture for several years.

We view the present obstacles to a successful economic recovery program as a formidable challenge. Federal spending has nearly doubled since 1976; GNP is actually declining when measured in 1972 dollars; interest rates have risen precipitously; the change in the money supply is needlessly erratic; and the rate of inflation is persistently high. President Reagan has vowed to tackle these high levels of Federal spending, interest rates, and inflation. It falls upon the Government to truly act as a stabilizing force within the economy — a role that has today all but vanished.

We want to curb the growth of federal expenditures, adjust the tax code to stimulate investment, significantly reduce personal tax rates, and offer prudent relief from excessive regulations. These actions will boost growth and slow inflation. This, in turn, will promote an economic climate that will permit the Federal Reserve to provide a stable monetary policy for the nation, enhancing the strength of the private sector.

The Farm Policy Setting

With the 1981 Farm Bill, we can apply the same economic principles to specific programs in agriculture. The benefits of farm programs that reduce unnecessary expenditures of tax dollars and promote the role of market signals could be substantial. We approach farm legislation at a time when a third of our cropland is engaged in export production. Promoting our competitiveness in international trade through market-oriented programs is thus a major goal.

With its $29 billion contribution to export earnings, agriculture is a very positive component of what has been described as a rather lackluster economic period. Business generated by the agriculture sectors contributes about a fifth of U.S. employment. Releasing agriculture from unnecessary market restrictions will therefore contribute to the economy as a whole by improving the trade balance, reducing inflation, as well as providing relief to taxpayers.

The market conditions for our products continue to improve. In the 1970's foreign demand for U.S. agricultural products grew over 8 percent annually, compared to growth rates of 1.5 percent in domestic agricultural demand and 2.8 percent in U.S. farm output. Our current outlook for both population and economic growth suggests that foreign food demand will increase at near record rates of 2.5 to 2.7 percent annually. Foreign demand for U.S. agricultural products increased by more than 8 percent annually during the 1970's. Demand for U.S. products in the eighties is expected to be 25 to 50 percent greater than in the seventies.

Upcoming legislation will increase these opportunities, if we continue to ease restrictions on agriculture. Administrative flexibility in setting loan levels is a critical factor enhancing U.S. agriculture's ability to compete in world markets. Ever present political pressures to fix loan levels at very high rates will return U.S. farmers to what some have characterized as the residual supplier for world markets. Accompanying supply restrictions become especially damaging in the long run when foreign producers rely on our programs as a guarantee for their own expansion in world markets.

U.S. agriculture has matured. The problems we faced in the past of resource misallocation and chronic overproduction have largely disappeared. The tremendous exodus of labor from agriculture has ceased; indeed, hired farm labor is on the rise. Resources employed in agriculture — land, labor and capital — are earning returns comparable to those in the nonfarm sector.

The time is right to introduce new policies that will reflect this changed environment in agriculture. Nevertheless, agriculture will undoubtedly encounter new problems. In 1980, drought and inflated input prices caused many hardships. And while world markets are a great hope for agriculture, world prices can fall just when income is most needed for debt financing. This Administration therefore intends to provide assistance, but in ways that clarify, rather than distort, underlying market signals. This approach would support farm incomes during difficult years, while recognizing that ample rewards for good management are eventually forthcoming through the marketplace.

The Administration's Farm Bill

The Administration began its deliberations on the farm bill with an awareness of agriculture's changed situation. In developing a farm bill that would incorporate the philosophy of the Economic Recovery Program, we used several guidelines: Government spending had to be reduced, especially by eliminating waste, fraud and abuse. In addition, program effectiveness had to be examined. Programs must be flexible to respond to changing market conditions. Also, with government spending being closely scrutinized, we had to make absolutely sure we were getting the most for the taxpayer's dollar. We needed to find the best ways of providing essential economic protection in a cost-effective manner.

We also had to find ways to reduce government's involvement and regulation within the economy. The Department of Agriculture is one of the largest regulators in the Government. Yet, even USDA has played too much of a role in the agricultural economy. Therefore, it was of paramount importance to design a farm bill that would be free from unnecessary and burdensome involvement in the operation of farm businesses and markets.

Third, we wanted to renew efforts to increase soil conservation and basic agricultural research, since the immense success of American agriculture is due to the productivity of our farmers, a fertile land and the progress of agricultural research.

Research must be responsive in this new era of expanding market opportunities and rapidly changing factor prices. Productivity oriented research will take on new relevance. Nitrogen fixing plant technologies, for example, merit considerable emphasis, as do water and nutrient conserving cultivation practices. Efforts to obtain the maximum effectiveness from our conservation programs will likewise need further emphasis in the coming years.

Reactions on Capitol Hill to the Administration's proposals have been mixed. Many understand the need for reduced spending and regulation, but there is also a natural reluctance to move away from traditional farm programs. The House Committee's version of the farm bill is fundamentally a reenactment of the 1977 Act, with relatively minor modifications. While the House did try to reduce budget exposure, it did so only with an accompanying reduction in the Secretary's discretionary authority. The House proposal is not in tune with current economic realities. These times call for flexible farm policies that adapt to the changing needs of the farm sector.

For example, the minimum dairy support level in the House version was lowered from the current 80 percent of parity to 75 percent to reduce budget exposure. But a formula was inserted that would tie the support level to estimated government purchases — the greater the puchases, the lower the supports — in lieu of Secretarial discretion. In the farmer-owned reserve program, both the House and Senate versions returned to the

Secretary the authority to decide whether to waive interest charges, thereby reducing budget exposure. However, the House was very specific about the conditions and price levels under which grain could be released, storage payments stopped, and market rates of interest charged.

The Senate Committee's farm bill takes a middle ground between the Administration and House Committee proposals. Although agreeable with most of the Administration's budget cuts and the need for Secretarial discretion, the Senate Bill would alter, but not remove, the basic aspects of the commodity programs. A comparison of some provisions of the farm bills serves to further highlight these program differences.

Dairy: The Administration's proposal for the dairy program was to set support at 70 to 90 percent of parity, upon the Secretary's discretion, adjusted annually. Authority would be provided to set the support level below 70 percent of parity if the CCC accumulates excessive stocks of milk or milk products.

The Senate Committee called for a program with semi-annual adjustments. The October 1 adjustment would be 75 to 90 percent of parity, set at the Secretary's discretion, unless estimated net costs of the dairy program exceed $500 million, or estimated government purchases exceed 3.52 billion pounds. In this case, the October 1 adjustment could be as low as 70 percent of parity. The April 1 adjustment would be 70 percent or the current actual level, whichever is higher.

As mentioned earlier, the House Committee set the support at 75 to 90 percent of parity, tied to a formula. Because of the budget limitation, the 1982 adjustment would be annual, with later adjustments made semi-annually.

Grains: The Administration proposed sweeping changes for the wheat and feed grain programs. Disaster payment authority would be eliminated since Federal Crop Insurance is now in place. The target price-deficiency payment program of direct payments to farmers would be eliminated because of program inequities, its subsidy nature, and the possibility of budget exposure.

Provisions that place strong restrictions on farmer participation in commodity programs, such as cross-compliance and normal crop acreage requirements, would also be eliminated, since they interfere with farmers' ability to follow market signals. Finally, the Administration proposes that the Secretary be given full discretion to set loans at appropriate levels with respect to not only costs of production, but supply and demand factors and world grain prices.

The Senate Committee proposals come closer to being in line with the Adminstration's views. The disaster payment authority would remain, but it would be used only in those areas with no Federal Crop Insurance coverage, or when the Secretary determines that Federal assistance is inadequate. The set-aside authority would be replaced with a crop-specific acreage limitation program. The Senate Committee agreed that cross-compliance and normal crop acreage requirements should be eliminated.

The Senate Committee chose to retain the target price program. However, instead of mandating annual changes in the target price to reflect changes in the cost of production, target prices would be arbitrarily set at minimum levels, rising 20 cents annually for wheat and 15 cents annually for corn. The Secretary would have discretion to raise these target prices above the minimum levels. In addition, a minimum loan level would be set for wheat and corn with Secretarial discretion for adjustment to a higher level.

The House Committee's version resembles current law. The Committee agreed with the Administration on one point — the disaster payment program is no longer needed and should be available only in 1982 and then, only to producers not covered by crop insurance. The set-aside program, the target price program and the loan level determination as specified within current law would be retained. Since the target prices and loan levels would continue to be adjusted by changes in the cost of production, the committee recommended appointing of a board of producers, to review the Government's cost data.

Soil and Water Conservation

I'd venture to say, having grown up on a farm myself, that farmers are proud to share in the responsibility as stewards of the land they till. This responsibility makes it important to support those programs designed to protect our natural resource base. While we want to continue to encourage increased productivity, and this means bringing additional land into the production process, it also means we'll probably be using land subject to more erosion problems. There has already been some good work done in this area, both at the state and national levels. The Administration pledges to prepare a comprehensive soil and water conservation program for the consideration of the Congress by December 1981. We recognize that if we are to sustain our ability to produce food and fiber for this Nation and our foreign customers, we are charged with the responsibility to reduce any serious erosion of our soil and develop an effective program for the future growth of our agricultural sector.

In Conclusion

Times have changed. We faced a new economic environment, a changed agricultural economy, and a changing role in international trade. And, we have a new set of actors involved in the policy process — in Congress and in the Administration.

At this stage many questions about the next farm bill remain to be answered. But it is important that you know our plan — where we are headed, how we plan to get there, and the progress we are making. To conclude, I would like to address the impact that our plans will have on your own work in the farm economics profession.

The economy is our number one priority — but not all problems can be solved this year. Our goal is to balance the budget by 1984. That means spending must be further reduced as we go along. There will be an increasing need to prioritize research efforts, both the USDA and the Land Grant System.

What are the most essential areas for research to tackle? I'd like to suggest some areas where I foresee the greatest needs:

Certainly, for the West, soil and water conservation, especially water, will be critical. Much more work on water conservation is ahead of us in the next decade or two.

Helping farmers raise productivity is another area essential to the health of our capital-intensive and export-oriented agriculture. Productivity will provide a major focus for agricultural research and extension.

Burdensome regulations are one present barrier to fuller productivity in agriculture. Streamlined, sensible rules are needed.

The farm export market will be an important focus for future research work and practical development efforts. We must ensure our continuing leadership in trade.

We need to work on domestic marketing problems as well. How can we help farmers protect their profitability when they market their output?

People remain our most important rural resource. We need a better grasp on how change affects rural people and local economies.

These, briefly, are areas of critical importance that I foresee. As we work toward a balanced Federal budget, you will be called on to finely tune the priorities of your research agenda.