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Staff Paper

Issues and Alternatives in the 1995 Farm Bill
Debate: Wheat and Feed Grains Programs

By

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6 pages

Abstract

Commodity programs will again be at the center of the debate as consideration of the 1995 farm bill begins. A wide range of alternatives will be proposed as 1995 approaches. Each of these proposals would affect Michigan farmers, regardless of whether they participate in existing farm programs. Given the diversity of Michigan agriculture, few states have as much at stake in the upcoming farm bill debate as does Michigan.

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ISSUES AND ALTERNATIVES IN THE 1995 FARM BILL DEBATE: WHEAT AND FEED GRAINS PROGRAMS

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From the Series: Michigan Agriculture in a Global Economy

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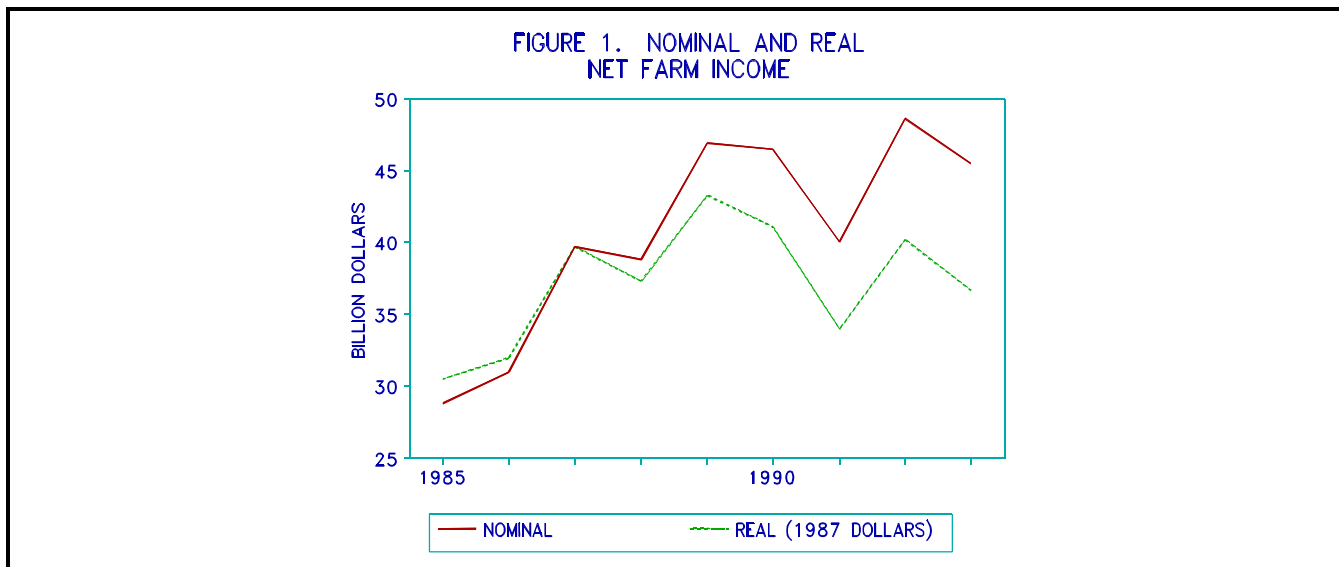
Setting the Stage: How Well Has the 1990 Farm Bill Performed?

The debate over the Food, Agriculture, Conservation and Trade Act of 1990 was dominated by budget concerns. The budget cost of the 1985 farm bill had been greater than expected and, by 1990, Congress' main objective was to reduce the cost of farm programs while providing farmers with greater flexibility to respond to market signals. The major provisions of the 1990 farm bill included:

- Deficiency payments were eliminated on 15 percent of each farmer's base acreage. Farmers were permitted to plant other crops on this portion of their base with no reduction in their program base.
- Target prices were frozen at their 1990 level through 1995.
- Loan rates were to be maintained at 85 percent of the 5-year moving average market price (excluding the high and low years during the period). The Secretary of Agriculture was granted discretion to adjust loan rates based on expected carryover stocks.

The performance of the 1990 farm bill will provide the starting point for the 1995 farm bill debate. The impact of this legislation on farm income, budget cost, exports, and accumulation of government stocks will all be examined as the farm bill debate begins.

Farm Income: Net farm income averaged \$45 billion during 1991 to 1993, compared to an average of \$41 billion between 1986 and 1990 (Figure 1). Adjusted for inflation, real net farm income averaged \$37 billion from 1991 to 1993, compared to an average of \$39 billion from 1986 to 1990 (in constant 1987 dollars). Farm program payments



represent a smaller share of net farm income in recent years, with program payments representing 11 percent of net farm income since 1990, compared to 16 percent during the period from 1986 to 1990.

Budget Cost: While the cost of farm programs (including feed grain, wheat, rice, cotton, and dairy programs) under the 1990 bill is less than in the mid-1980's, the average budget cost since 1991 is slightly greater than the cost of programs during 1988-90. Farm program expenditures for 1988-90 averaged \$10 billion annually, while the cost of farm programs is expected to average \$11 billion for the 1991-95 period (Figure 2). Much of this increase is the result of increased expenditures on export subsidies and disaster assistance programs. Direct payments to farmers averaged \$8.1 billion between 1991 and 1994, while disaster payments averaged \$1.2 billion and export subsidies averaged \$1.6 billion during the same period.

Exports: U.S. corn exports averaged 1.5 billion bushels during the period from 1991 to 1993, compared to 1.8 billion bushels during the period from 1986 to 1990 (Figure 3). Exports have accounted for 19 percent of U.S. corn production since 1991, compared to 24 percent during 1986 to 1990.

U.S. wheat exports averaged 1.3 billion bushels during the period from 1991 to 1993, representing 56 percent of U.S. wheat production. Wheat exports averaged 1.2 billion bushels, or 60 percent of U.S. production, during the period from 1986 to 1990.

Government stocks: Government stocks (purchased through the Commodity Credit Corporation or held through the Farmer-Owned Reserve) have decreased from their high levels of the mid-1980's. The Food Security Act of 1985 reduced loan rates in an effort to reduce government stocks. As the loan rate fell below the market price beginning in 1987, government stocks of both wheat and corn were reduced (Figures 4 and 5). The 1990 farm bill continued this movement by requiring the Secretary of Agriculture to maintain loan rates at 85 percent of the average market price during the previous five years.

A look ahead: Given the continued pressure in Congress to reduce spending on most government programs, budget cost will once again dominate the Congressional debate. At the same time, farmers, environmental organizations,

FIGURE 2. COST OF DEFICIENCY PAYMENT, LOAN RATE AND EXPORT SUBSIDY PROGRAMS

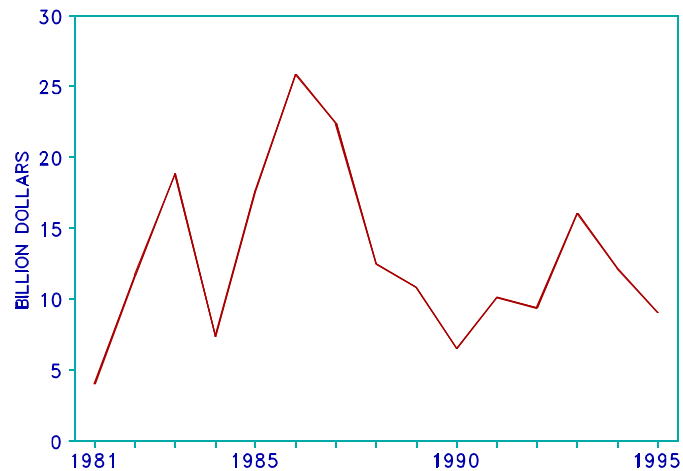
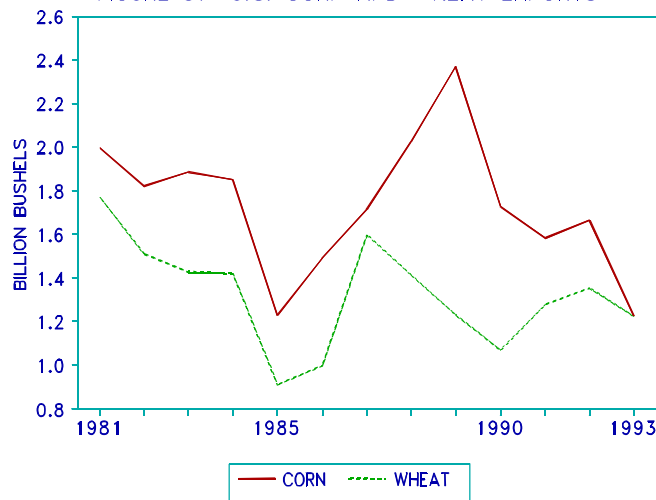


FIGURE 3. U.S. CORN AND WHEAT EXPORTS



and members of Congress are all questioning whether the existing farm program should undergo only minor modification or whether these programs should be restructured to accomplish a broader range of objectives. Three questions will dominate this debate: How can the USDA's limited budget resources be used to protect or stabilize farmers' income? How can farm programs help farmers respond to market signals? And can farm programs help accomplish environmental objectives?

Alternative Programs for Wheat and Feed Grains

Several alternatives to the existing wheat and feed grain programs are likely to be considered before the 1995 farm bill debate is completed. The provisions of the major programs that have already been proposed are shown in Table 1.

Option 1 -- Modify Existing Programs: If the agriculture committees in Congress are forced to reduce farm program spending, the first alternative would be to modify the existing farm programs. The most likely alternative

would be to increase flex acres beyond the current 15 percent of each farmer's base. Analysis by the Congressional Budget Office indicates that increasing flex acres to 25 percent would reduce the annual cost of farm programs by \$900 million. Such a change would result in lower deficiency payments for farmers and would provide greater flexibility in planting decisions.

A second alternative would be to eliminate the Acreage Reduction Program (ARP) setaside requirements contained in the 1990 farm bill. The ARP provisions specify the portion of each farmer's base acreage that must be idled in order to receive deficiency payments. The ARP requirements for all program crops decreased following the introduction of flex acreage in the 1990 bill. Since flex acres receive no deficiency payments, the USDA does not have to use large setasides to reduce budget costs. Consequently, ARP requirements have been reduced in recent years, giving rise to suggestions that the ARP might be eliminated entirely or replaced with a "flexible flex" provision that would allow the USDA to announce an annual flex requirement rather than announcing both flex acres and an ARP requirement. For example, under the "flexible flex" alternative, the USDA might announce that the flex acreage would be 25 percent of each farmer's base rather than requiring a 15 percent flex and a 10 percent ARP setaside. This alternative could allow greater flexibility for farmers and continue to provide USDA with a tool for achieving annual budget savings.

Another alternative that could be considered would be the elimination of crop program bases and the "decoupling" of program payments from the program base. This alternative, considered in both 1985 and 1990, would allow farmers to continue receiving deficiency payments for the existing program crop, but would allow program participants to plant any crop of their choice on their base acres. This approach would give farmers the maximum freedom to modify their production plans, but would probably not result in significant budget savings

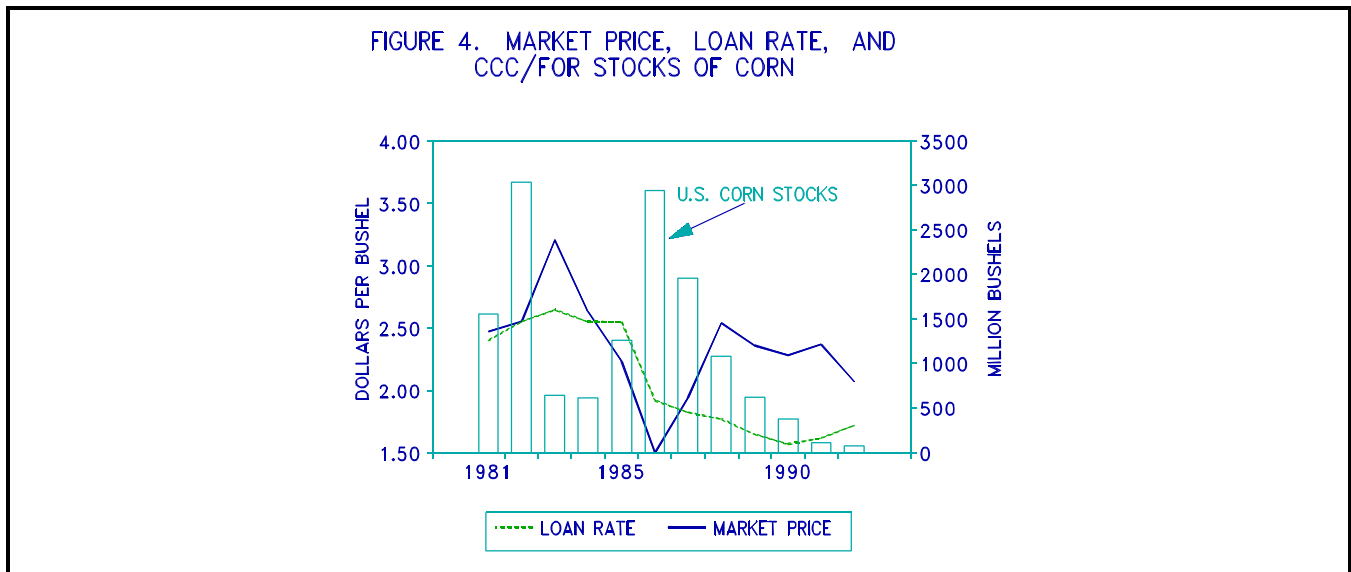
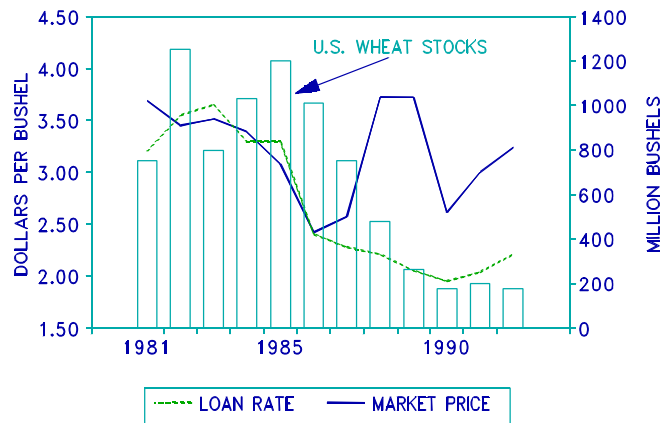


FIGURE 5. MARKET PRICE, LOAN RATE, AND CCC/FOR STOCKS OF WHEAT



unless it was combined with a reduction in the number of acres on which payments were made. Questions about the equity of such a program might arise if farmers with program base receive program payments, while farmers producing the same crop without a program base did not receive payments.

Option 2 -- Revenue Protection Programs: A variety of revenue protection programs will be considered in 1995. While each has its own details, all are designed to provide protection of farmers' revenue rather than protecting farmers from low prices through deficiency payments. Most of these programs would make payments to farmers only if their revenue fell below a designated level.

The first alternative is the **revenue assurance** program proposed by the Iowa Farm Bill Study Team, a coalition of 11 Iowa farm organizations. This program would make payments to farmers only if their revenue fell below 70 percent of their "normal" crop revenue (normal revenue is defined as the producer's average yield for the previous 5 years times the average county price for the previous 5 years). Under this program, normal crop revenue could be calculated to include existing deficiency payments (the "total revenue" approach) or exclude deficiency payments (the "market revenue" approach). Such a program would eliminate deficiency payments, program bases, ARP setasides, flex acres and disaster payments. Farmers would be eligible for revenue assurance payments if their revenue fell below 70 percent of the normal benchmark, regardless of whether the revenue shortfall was due to decreases in price or yield.

A revenue assurance program would shift the focus of commodity programs from price protection through deficiency payments to income protection through revenue assurance payments. Rather than making deficiency payments to all farmers when the market price falls below the target price, the revenue assurance program would make payments only to those whose revenue fell below the benchmark level.

Another form of revenue protection is a **targeted revenue** program. Under this alternative, the existing deficiency payment program would be replaced with a system of payments based on average county revenue. Each county's "target revenue" per acre would be calculated using the average deficiency payment, yield and market price for that county. If the county's average revenue per acre fell below this level in the future, farmers in that county would receive a payment equal to the difference between the target revenue and the actual revenue. Farmers in those counties where the actual revenue exceeded the target revenue would receive no payments. A targeted revenue program based on historic county data would yield the same average payments over time as the existing deficiency payment program, but the distribution of payments among years would vary as the revenue in the county varied.

This alternative would also result in a wider variation in payments across counties. As with the revenue assurance program, this alternative would provide payments regardless of whether the shortfall in revenue was caused by decreases in prices or yields.

Though analysis of these programs is incomplete, some preliminary analysis of the Iowa revenue assurance proposal has been conducted by USDA. Under a scenario that continues the existing target price program, corn producers could expect to receive \$39.19 per acre in deficiency payments and \$5.80 in disaster or crop insurance payments each year. Under a 70 percent market revenue assurance program, farmers could expect to receive an annual average revenue assurance payment of \$4.06 per acre. If the revenue protection was increased to the 80 percent level, a total revenue assurance program would yield annual payments of \$16.36 (the highest payments calculated under revenue assurance scenarios). However, farmers would have some increase in revenue from the cropland that would no longer be idled to comply with the ARP requirement of the deficiency payment program. This comparison was based on the assumption that flex acreage would remain at 15 percent after 1995. If flex acreage is increased, the difference between a deficiency payment program and a revenue assurance program would be reduced.

Option 3 -- Green Payment Programs: A third option would be to replace existing deficiency payments with a system of payments designed to compensate farmers for the use of designated farming practices that prevent environmental damage. Though no specific green payment program has been proposed, the concept of green payments is being discussed and might have three components. First, while such a program could be designed to operate outside the traditional deficiency payment program, budget constraints would probably dictate that a green payment program would have to replace the existing deficiency payment program. Second, a green payment program would have to establish a schedule of practices and payments aimed at addressing specific environmental problems. Third, such a program would have to be tailored to specific local conditions and would probably have to include a wider range of commodities than traditional commodity programs if high priority environmental problems are to be addressed.

While a green payments program might attract broader public support for farm programs, the use of a green payment program might result in a different distribution of payments than the current program. In most versions of this program, green payments would be distributed according to the type and severity of environmental problems rather than being determined by base acreage enrolled in the deficiency payment program. However, green payments could be distributed to all program participants using Best Management Practices regardless of whether environment problems are associated with a specific farm.

A green payment program might result in a shift in payments among regions or, if producers of non-program crops participate in this program, payments might be shifted from existing participants to producers of non-program crops that do not receive payments under the existing program. Because the objective of this program is to accomplish environmental objectives rather than farm income objectives, a green payment program would probably do little to stabilize farm prices or farm revenue. If a program based on environmental objectives is adopted, Michigan farmers who produce non-program crops and do not receive deficiency payments might become eligible for green payments.

Some Common Questions for All Programs

The 1995 farm bill is already shaping up as one of the most important in history. Fundamental questions are being raised about the objectives and structure of farm programs. When such drastic change is proposed, some common questions ought to be asked about each alternative:

- What is the objective of commodity programs -- protection of farm income, maintenance of environmental quality, or both? Which of these objectives will each alternative accomplish?

- How would major changes in programs change the distribution of payments among existing program participants and producers of non-program crops who do not participate in existing programs?
- Should the USDA's limited budget for farm programs be distributed among farmers according to existing crop acreage bases or to protect farm revenue?
- Should only the existing program crops be eligible for programs such as revenue protection or green payments, or should all crops be eligible? What would be the budget cost of an expansion in the number of crops eligible for such payments?
- What is the impact of each alternative on exports, input industries, and rural communities?

Few states will be as affected by this debate as will be Michigan. In addition to the impact on grain farmers, this debate will affect the future of disaster programs, crop insurance and environmental compensation -- all of which affect producers of other commodities.

Table 1. Comparison of Target Price, Revenue Protection, and Green Payment Programs.

	Target Price	Revenue Assurance	Targeted Revenue	Green Payments
Who is eligible	Program crops (corn, wheat, cotton, rice)	Uncertain. Program crops only in Iowa proposal	Uncertain. Could include non-program crops	Uncertain. Could include non-program crops
When are payments made?	When market price is less than target price	When farmer's revenue is less than benchmark level (70 percent in Iowa proposal)	When average county revenue per acre is less than benchmark level	When specified production practices are used or when approved plan is adopted
How are payments calculated?	Payment acres X program yield X deficiency payment	Benchmark revenue level minus actual revenue level	Payment acres X (benchmark revenue per acre minus actual revenue per acre)	Based on percentage of cost of implementing approved plan
Is protection from price risk provided?	Some protection on payment acres	Some protection if revenue is below benchmark	Some protection if revenue is below benchmark	No
Is protection from yield risk provided?	No	Some protection if revenue is below benchmark	Some protection if revenue is below benchmark	No
Is ARP setaside required?	Yes	No in Iowa proposal	Probably no	Probably no
Is Crop Acreage Base used?	Yes	No in Iowa proposal	Probably no	Probably no
Is loan rate program available?	Yes	Yes in Iowa proposal	Uncertain	Uncertain
Is payment limitation required?	Yes	Not included in Iowa proposal	Uncertain	Uncertain
Is Federal Crop Insurance program available?	Yes	No in Iowa proposal	Uncertain	Uncertain
Is disaster program available?	Yes	No in Iowa proposal	Uncertain	Uncertain