Wayne Boutwell on Marketing Loans

An Idea Whose Time Arrived

Now a principal feature of U.S. commodity programs, marketing loans can help U.S. agriculture compete in international markets. It is important to understand how this feature works in conjunction with price supports for it has significant implications for U.S. farm income and government expenditures, as well as the competitiveness of U.S. farm products in international markets.

"In 1985, new farm legislation should be based on policy objectives which reflect the changing global economics of agriculture today . . ."

From the statement by Ben Morgan, Chairman of the Board of the National Council of Farmer Cooperatives, before the U.S. Senate Committee on Agriculture, Nutrition and Forestry, March 7, 1985.

As Congress began to draft the 1985 Farm Bill, the farm economy was steadily deteriorating. In addition, it was increasingly clear that traditional farm programs aimed at reducing production no longer offered a solution to the problems facing agriculture. Changes in global economics and other factors external to agriculture including fiscal and monetary policies—were causing the United States to lose its export markets.

As the U.S. reduced its production other countries simply expanded, capturing a larger and larger share of the world market. This in combination with debt problems of many lower income countries led to continued excess production worldwide and lower prices in the face of stagnating exports.

As worldwide competition began to increase, the U.S. found it difficult to maintain its market share. U.S. price supports (loan rates) for many commodities were set well above market-clearing levels. This, together with the spectacular rise in the value of the dollar, not only made it difficult to compete, but further encouraged even greater foreign production.

With domestic surpluses continuing to mount and little or no improvement in prices, the U.S. faced even more pressure to reduce production at a time when its share of the world market was declining. It was increasingly clear that without a change in direction, this downward spiral in U.S. agriculture would continue.

Clearly, U.S. farm policy was at a crossroad. It was apparent that now was the time to review the objectives of U.S. farm programs and find ways to make U.S. farm products competitive in international markets.

A New Policy Objective

For the past 50 years, U.S. farm programs have had three major policy objectives: (1) provide income support for farmers; (2) maintain adequate supplies of food and fiber at reasonable prices; and (3) ensure the orderly marketing and distribution of agricultural commodities.

All three of these objectives are essential to building broad-based support for any farm program. However, in 1984 it became apparent that an additional objective was necessary if U.S. agriculture was to be prosperous. U.S. agriculture must be able to compete effectively in the international marketplace. Exports had become the lifeblood of U.S. farm prosperity.

The debate then centered on how to compete in export markets without sacrificing long-term objectives of U.S. farm programs including income support for farmers.

In response, a number of farm and commodity groups, including the National Council of Farmer Cooperatives, joined together in support of a new concept called the "marketing loan."

This support prompted a number of Congressmen to introduce bills in both the House and Senate. Among those introducing legislation were Senators Thad Cochran (R-MS) and David Pryor (D-AR), as well as Representatives Arlan Stangeland (R-MN) and Pat Roberts (R-KS).

Thanks to them and other farm state

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How the Marketing Loan Works for Rice

The marketing loan for rice became effective April 15, 1986, as prescribed in the Food Security Act of 1985. For the 1985 crop, the target price remains at $11.90 per cwt and the loan rate at $8.00 per cwt.

Producers who comply with acreage programs may receive a deficiency payment equal to the difference between the target price and the higher of the loan rate or the season average price received by farmers.

With the marketing loan, producers who receive the $8.00 per cwt. loan from the Commodity Credit Corporation (CCC) using their commodity as collateral, may repay the loan at the lower of the loan rate or the prevailing world market price for rice.

This world market price is determined by the Secretary of Agriculture. In early June, that average world price was around $3.40 per cwt. Loan and repayment levels vary with the type of rice produced.

Under the previously announced program, the rice would have been forfeited to the CCC and the cost to the government would equal $8.00 per cwt. plus the interest plus all future storage costs. Under the marketing loan, the government costs are limited to the difference between the loan rate and the repayment level. In early June that would have been $4.60 per cwt. Since the CCC does not receive forfeited grain, there are no future storage costs.

For the 1986 crop, the target price will be $11.90 per cwt with a marketing loan rate of $7.20 per cwt instead of the $8.00 for the 1986 crop. However, the resulting deficiency payments and the loan proceeds will be reduced by 4.3 percent in compliance with Gramm-Rudman-Hollings. Producers will again be able to repay their loans at the lower of the loan rate or the prevailing world price but not lower than 50 percent of the original loan rate, i.e., $3.60 per cwt.

members of Congress, the marketing loan concept was approved by the House and Senate and signed into law as part of the 1985 Farm Bill. For cotton, rice, and honey the program is mandatory while it is discretionary for wheat, feedgrains, and soybeans.

Key Feature

The key feature of the marketing loan is simply this: allow farmers to repay their price-support loans at the lower of the loan level or the world price. In the past farmers repaid price-support loans at the loan level or forfeited the commodity to the Government. Thus, the price support loan became the effective support of market prices. Not the case with the marketing loan.

This simple but fundamental change ensures that U.S. agriculture will be able to compete more effectively in the international marketplace. Price-support levels or loan rates would no longer serve as an umbrella over the world market. At the same time, producer farm income is protected at the established loan rates and target prices.

The marketing loan has other advantages. The need for supply management programs is reduced. In addition, it encourages foreign competitors to share in efforts to adjust production in order to bring about a better balance between supply and demand.

Finally, the marketing loan means smaller government stocks to the extent that increased exports are realized and production adjustment efforts both here and abroad are more effective.

The year-long debate on the marketing loan centered over how low prices would go even though farm income would be protected. This would directly affect the cost of the program.

In the end, Congress produced a compromise that protects the government against unlimited budget exposure by putting limits on how low the repayment can go. Once the limit is hit the repayment level serves as the new price support level and operates the same as the old program.

In Summary

The 1985 Farm Bill found farm programs and policies at a crossroad. Agriculture had changed dramatically since the 1930's and government programs were in need of critical review in recognition of the changing global economy. The development of the marketing loan was in response to that need. How well it succeeds, of course, depends on a number of factors. But to the extent it is fully implemented the opportunity exists for U.S. agriculture to compete effectively in the international marketplace. ■

Marshall A. Martin, Harold D. Guither, and Robert G. F. Spitze on the 1985 Food Security Act

Most Farmers Got Much of What They Wanted

Most farmers got much of what they wanted in the 1985 farm legislation. One major exception was the substantial reduction in the loan rates. The Act did retain most previous farm programs.

Here is how the provisions of the 1985 Food Security Act compare to what, in early 1984, farmers and ranchers in 17 States said they wanted in food and farm policy.

The Act permits a substantial lowering of the loan rates. Comparing 1985 loan rates with those set by the Secretary for 1986, wheat was lowered from \$3.30 to \$2.40 per bushel; corn from \$2.55 to \$1.92 per bushel; rice from \$8.00 to \$7.20 per cwt; and cotton from \$.0573 to \$.044 per pound. Milk remains at \$11.60 per cwt and soybeans at \$5.02 per bushel.

Most farmers in 1984 did not favor the lowering of loan rates to increase exports. Less than 30 percent of the farmers in 16 of 17 States (Washington was the exception with 41 percent) favored such a policy.

The Act bases loan rates on a five-year moving average of market prices (dropping the high and low years).

Forty percent or more of the farmers in each of 17 states favored this approach.

The Act retains all target prices for 1986, and wheat and corn for 1987 at the same levels that prevailed in 1985 with gradual reductions in target prices permitted for 1988, 1989, and 1990. At the

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About the Policy Survey

In anticipation of the 1985 Act, public policy researchers and extension specialists in several states surveyed farmers and ranchers to obtain their views about future U.S. food and farm policy. Mailed in early 1984, the farmer preference survey included questions concerning alternative policies for price and income support, trade, soil conservation, food assistance, and program costs.

More than 8,000 farmers responded to the survey. The 17 States represent 50 percent of all cash receipts from farming in the U.S. and 50 percent of all U.S. farms. These States also represent over one half of the U.S. livestock, food grain, and oilseed production; two-thirds of the feed grain production; and one-third of the cotton production.

The 17 States included in the survey were: Illinois, Indiana, Kansas, Michigan, Minnesota, Nebraska, Ohio, South Dakota, Wisconsin, Idaho, Washington, Alabama, Florida, Oklahoma, South Carolina, Texas, and Maryland.

The specifics of the survey results may be found in *U.S. Farmers' Views on Agricultural and Food Policy: A Seventeen State Composite Report,* authored by Harold D. Guither, Bob F. Jones, Marshall A. Martin, and Robert G. F. Spitze, North Central Regional Research Publication 300 and Extension Publication 227, December 1984.