The great deficit debate

The deficit and agriculture

by James D. Schaub
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Even as the economic recovery from the recession continues, budget projections point to increasing deficits and an accelerating national debt. This article moves beyond the general concern over the deficit by considering the contribution of agricultural programs to the deficit, and speculating about how the deficit affects agriculture and agricultural policy. But, first, it is important to put the issue in some perspective and to provide some guidance on what the budget actually measures.

Based on estimated receipts of $1.148 trillion and outlays of $1.475 trillion, a deficit of $327.3 billion is now projected for fiscal 1993 (October 1992–September 1993) (OMB). This figure compares to a deficit of $290 billion for fiscal 1992. The last federal budget surplus occurred in fiscal 1969. Although the concept of a deficit may seem simple, outlays greater than receipts, this is not the case for federal accounting. For example, there are the off-budget items—Social Security and Postal Service are "off-budget" operations—as well as other conceptual complications.

Eisner and others, including recent Economic Reports of the President and the President's Budget, have addressed alternative measurements of the deficit and budget. These alternatives include generational accounting, standardizing for full employment, and adjustments to account for the investment component of expenditures on capital items.

These alternative presentations are, in part, responses to some of the issues raised about the effects of deficits and the debt. The basic macroeconomic argument against deficits is that government borrowing to finance deficits leads to higher interest rates, crowds out private investment, and leads to trade deficits. However, more basically, it may be argued that the deficit is a problem because it represents an inappropriate tax on future generations, or simply too much government spending and too little taxation. These later topics are issues in their own right that are present whether the budget is in deficit or surplus. They should be discussed directly rather than indirectly in the context of deficits.

What the deficit means for agricultural costs

The line of reasoning that predicts that deficits cause higher interest rates implies that agriculture will face higher costs because agriculture is a relatively high debt sector. Total interest expense in farm cost accounts is about $14 billion and farm debt is about $140 billion for an average nominal interest rate of 10 percent. It is difficult to determine how big an effect large deficits have on interest rates. If the impact of eliminating the deficit is one percentage point on the average farm interest rate, then the reduction in costs is $1.4 billion out of total farm costs of about $145 billion. There may well be additional impacts on the farm sector through the exchange rate or other mechanisms, but each of these factors seem to be relatively small. Of more importance is the effect of the deficit, or rather attempts to control the deficit, on farm policy, the topic to which we now turn.

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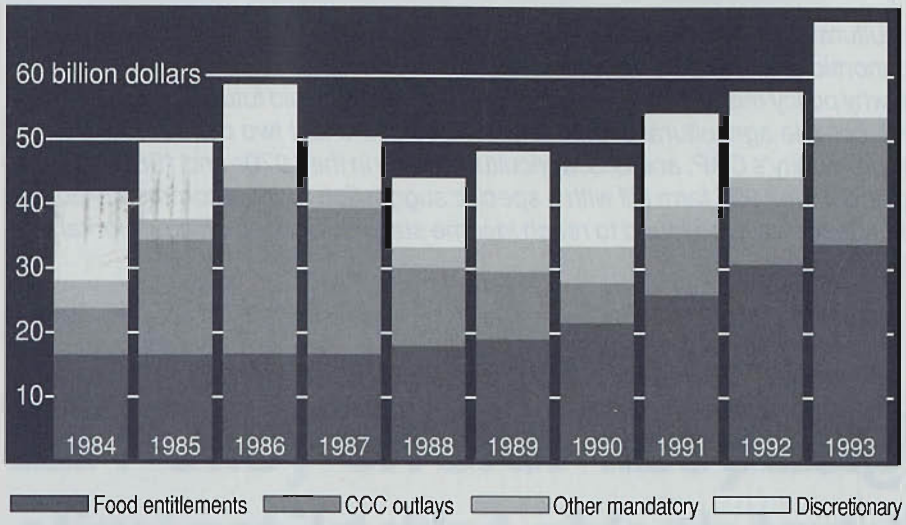

Table 1: USDA budget outlays

Measurement issues and policy

The federal budget is not the same as a household or business budget. The federal budget is a plan for revenues and expenditures. Revenues and expenditures will differ from the plan for a number of reasons. These are often classified as (1) forecast errors, (2) policy changes, (3) technical re-estimates primarily relating to the timing of receipts and outlays, and (4) special events (such as Desert Shield/Storm). In recent years, such factors have changed the deficit by more than $100 billion from year to year.

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Of more direct concern for agriculture is the way budget estimate procedures affect policy. Deficit concerns have led to reforms in accounting for direct and guaranteed loans. Until fiscal 1992, federal credit outlays were measured on a cash basis—that is, outlays for direct loans or outlays to lenders on a defaulted guaranteed loan were recorded in the budget net of collections. Before credit reform, loan guarantees usually appeared to have no budget costs in the year the commitment was made. In the new system, direct loans and guarantees are treated the same: the subsidy cost, meaning the estimated long-term cost to the government calculated on a net present value basis, excluding administrative costs, is treated as an outlay at the time the loans are extended to borrowers. The previous accounting system generally overstated the costs to the government of new direct loans and understated the costs of new loan guarantees. This created a bias in favor of guarantees and against direct loans, because the costs of guarantees were deferred.

How program proposals are scored for budget impacts can affect the deficit, and arcane scoring procedures affect program proposals. Program proposals tend to be assessed only on the impacts within a single budget account, even though there may be significant added costs or offsets that appear in another budget account. For example, proposals to decrease the excise tax on ethanol are scored as a loss in the revenue account. Such proposals are not allowed to score an expenditure decrease in the CCC account when the reduced ethanol tax leads to higher corn prices and reduced CCC costs. But higher outlays for the wheat export subsidies in the Export Enhancement Program (EEP) are offset in the official scoring by lower outlays in the wheat program from higher domestic wheat prices. That means that the EEP has an advantage in the policy process.

Another issue arises because, when outlays are conditional on some uncertain economic projection (such as a commodity price), the projected budget outlays are the calculated cost at the expected price rather than the expected cost based on the price distribution. This situation tends to bias downward projected outlays, because many programs have large costs for low prices but little cost savings for high prices, and because programs are now designed to capitalize on this budgetary convention. This explains in part why the marketing loan program for minor oilseeds, introduced in the 1990 Farm Bill, was initially scored at zero outlays, and why such programs proliferate.

The distinction between mandatory outlays because of entitlement programs and appropriated outlays on discretionary programs must be kept in mind to understand the federal budget. Mandatory programs do not face annual review or decision by either Congress or the president. The commodity price support operations of USDA are mandatory programs.

Discretionary programs require annual appropriation legislation. These include, for example, budgets for research and extension.

Entitlement programs create budget exposure that can only be estimated. For example, commodity price support programs require outlays to any qualified producer and food stamps must be available to qualified persons. Mandatory outlays for fiscal 1992 were $43.97 billion out of total USDA outlays of $57.77 billion.

USDA's two biggest mandatory programs are the Food Stamp Program with outlays of $22.8 billion and the Commodity Credit Corporation (CCC) with outlays of $9.7 billion in fiscal 1992. Another $6.1 billion was spent on mandatory Child Nutrition Programs (table 1).

Record outlays for commodity price support programs were $26 billion in 1986; estimated fiscal 1993 outlays are $17 billion. Thus, completely eliminating CCC outlays would at best reduce the projected

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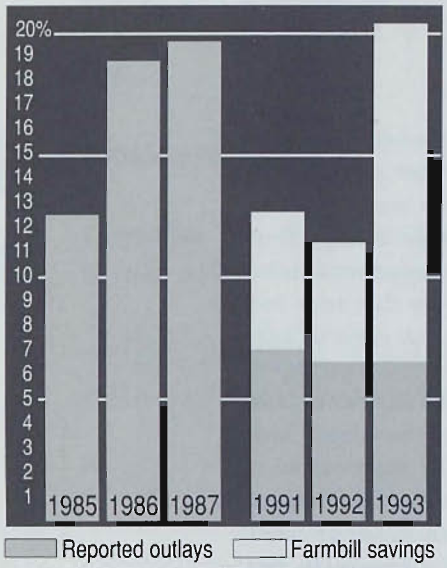

Table 2: CCC net outlays for feed grains, wheat, rice, and cotton

1993 deficit by 5 percent assuming no increase in other federal outlays or decrease in federal receipts as a consequence of the program elimination.

Appropriated outlays in the USDA budget totaled $13.8 billion in fiscal 1992 and included $2.6 billion for Women, Infants and Children's Food Program (WIC) and Commodity Supplement Food Program and $2.4 billion for the Forest Service. Although $13.8 billion is classified as discretionary, this does not mean that the public would consider all these activities unessential. For example, would the public want to trade the $490 million estimated outlays for the Food Safety Inspection Service for a one-tenth percent reduction in the deficit?

Using savings in agriculture to reduce the deficit

Because mandatory programs account for such a large portion of outlays, there is little discretion to make cuts toward reducing the deficit without major legislative changes in entitlements. Entitlement programs, particularly in the health and welfare area (including food stamps) are a large portion of the Government-wide budget.

However, mandatory commodity programs are small relative to the Federal deficit. For example, outlays for the honey program are $17 million, rounding error in most budget presentations. The forecast $17 billion CCC outlays forecast for fiscal 1993 is equivalent to the cost of building roughly 3.5 aircraft carriers.

Although commodity program outlays are too small to make a substantial difference in the deficit, this does not mean that agriculture is irrelevant. The political will to restrain growth in mandatory programs and even to reduce or eliminate some mandatory programs may hinge on building a consensus among "sectors" to accept less from federal outlays. Or, said differently, if agriculture were exempted it would be much more difficult to get other sectors to go along with broad cuts.

Farm interests point out that agriculture has contributed to deficit control via provisions of the 1985 and 1990 legislation. Outlays for commodity programs are lower because of cuts in target prices, freezing program yields, and the triple base program. We estimate that these disciplines lowered the combined outlays for the wheat, feed grains, rice, and cotton programs by $5.6 billion in fiscal 1991 and $4.9 billion in fiscal 1992. A difference of $8.7 billion is estimated for fiscal 1993 (table 2). (It is symptomatic of the role of the deficit in the farm policy debate that some of the major farm policy provisions in 1990 (the triple base and GATT triggers to name two) were contained not in the farm bill but in the Omnibus Budget Reconciliation Act.)

Concern about the deficit can have a myriad of effects on farm policy. When farm policy for 1991–95 was determined in 1990, concerns about budget costs lead to significant cuts in those programs that have direct outlays but only small cuts in programs

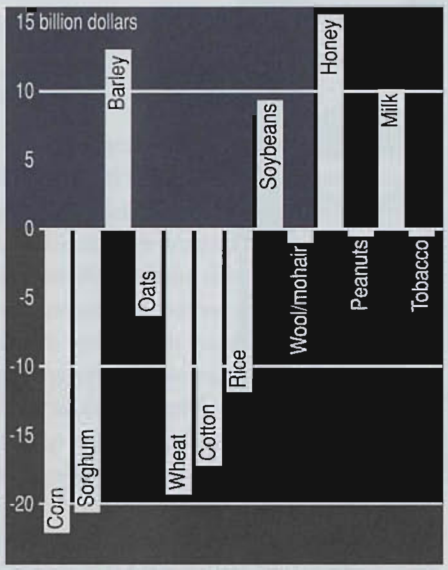

Table 3: Change in direct payments or support per unit of production 1991-93

where support is indirect. The accompanying chart shows that the resulting percent change in payments or support per unit of production varied widely across commodities (table 3). When the economic costs of programs are not transparent, there is no clear budgetary incentive to cut support nor are there clear political incentives to reduce support unless budget saving can be demonstrated.

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In part, because concern was focused on deficits (program costs), commodity programs such as peanuts and sugar were spared significant cuts in 1985 and 1990 Farm Bills. This is in sharp contrast to the cuts made for deficiency program crops. The peanut and sugar programs were spared cuts more because these programs did not involve direct CCC outlays than because they were necessarily the best policies for these commodities. The fact that these programs do not involve direct CCC outlays has lead to proposals to shift more programs to the peanut/sugar paradigm. Such a shift may reduce direct outlays, but may result in greater economic costs for society than deficiency payment programs where costs are transparent. Thus, concerns over deficits may drive agricultural policy toward policies that reduce outlays but increase market distortions and increase social costs.

Deficit pressure does not necessarily lead to more distortionary programs. The triple base provision of the Omnibus Budget Reconciliation Act of 1990 was perhaps the least distorting way to modify the basic commodity programs to save costs. Triple base reduced payment acres but added flexibility thus increasing the role of market signals in planting decisions. The decision to freeze program yields in 1985 similarly had both budget savings and sound economic and environmental effects.

Deficit concerns do not necessarily dictate how commodity programs are operated. For example, a 7.5 percent Acreage Reduction Program (ARP) rather than a 10 percent ARP was selected for the 1993 upland cotton program even though it has about $130 million higher outlays.

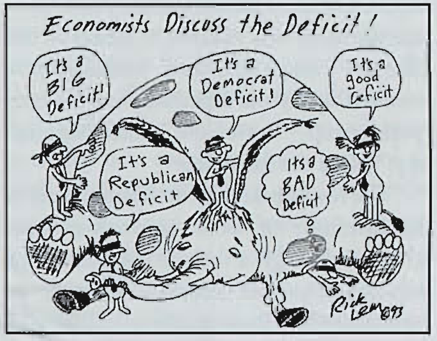
Conclusion

The federal budget deficit has some real consequences for the economy and for agriculture. Perhaps more important is the effect of concern about the deficit on policy debate and policy choices. In some ways discussion of the deficit itself has substituted for or obscured the more basic debate over the appropriate level of government activity and the desirability of specific government programs. It is a major problem indeed when deficit concerns add to, rather than reduce, the detrimental impact of government programs on the functioning of our economy. ■

■ For More Information

Eisner, Robert. "Deficits: Which, How Much, and So What?" *The American Economic Review.* 82(1992):295-298.

Office of Management and Budget. *Budget Baselines, Historical Data, and Alternatives for the Future.* U.S. Government Printing Office, Washington, D.C. January 1993.



Ag policy—looking ahead *continued*