SELECTIVE

PERCEPTIONS AND THE POLITICS OF AGRICULTURAL POLICY ANALYSIS

by James Duncan Shaffer

Policy analysis and policy debate make a difference in the formulation of public policy. However, policy analysis and debate are often biased or incomplete. People are inconsistent as to the "legal and moral rights" they invoke and apply to different policy issues. We are much like the horse wearing blinders.

For example, many of those who supported the Declaration of Independence, with its ringing endorsement of equality among men, held slaves and perceived no conflict between their beliefs and behavior. The perception of equality and its application in political-economic life was highly selective. Still later, the Civil War was fought over different perceptions of politically or morally acceptable definitions of property rights.

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Entitlements, Contributions, And Equity

Income distribution, the content of demand, and the costs of production are "worked out" through transactions among economic participants based on perceived individual rights. Literally thousands of rules—legal, administrative, customs, conventions, standard procedures—and beliefs define "claims" that people have to the economic benefits that flow from our economy. At the same time these rules and beliefs shape the performance of our economy. Perceptions of legitimate claims are highly selective.

We generally think it proper for both ethical and pragmatic reasons for people to receive economic benefits according to their contribution from individual effort and that of their owned resources such as land and money. We believe that to compensate people according to their contributions encourages people to produce and market the goods and services desired by others in society. But we also believe that the aged, children, and in some cases the disadvantaged have some claims on the economic output of our society independent of their current contribution. The aged have contributed in the past; children are a social investment; and the disadvantaged elicit moral convictions about altruism or charity.

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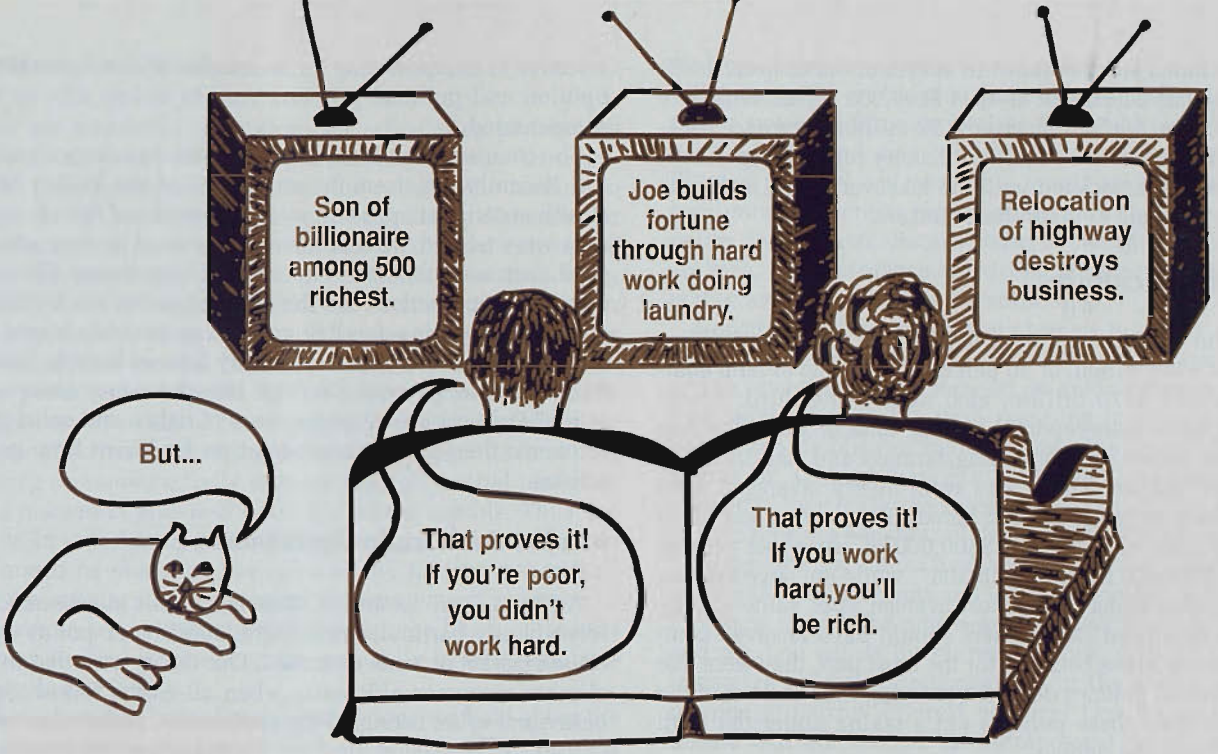
If economic contribution is to be the proper basis of entitlements to goods and services, the policy debate needs to be informed about the difficulty of measuring what people contribute. The difficulty is illustrated by the question, what accounts for changes in productivity? A similar question is, why is the output per worker so many times greater today than 200 years ago? The major source of productivity is not the hard work of individuals, nor the natural resource base, nor even savings for investment, although each influences output. Instead, current productivity of the U.S. economy stems from the inherited knowledge embedded in the political-economic system—the knowledge of how things work and how to make things work and the knowledge embodied in tools, factories, and institutions. Institutions to coordinate economic activity and training are especially influential in increasing productivity. At the same time, knowledge without application contributes nothing to output; human effort is essential as well.

The fundamental question of entitlement to the output attributable to the inherited knowledge of the economic system is not directly confronted in policy debate or analysis. Rather, through the political process, only a highly selected set of rights and issues are considered, while other rights of entitlement remain beyond examination. For example, farm income supports, rules for food stamps, and minimum wages for food system workers are debated without regard to hundreds of other rules critical in determining shares of current output. At the same time situations which raise questions about the current system of entitlements abound. Consider the following:

- Based on a contract previously negotiated with the board of directors, the president of a large food-manufacturing firm was entitled to $2 million severance pay in the face of a highly leveraged buyout of the company. In contrast, a worker who quit a job because of a belief that the chemicals in the workplace make it an unsafe place to work received no unemployment compensation.
- Each year many children starve to death. They lack entitlements to adequate food. In comparison, in 1987, about 14,000 U.S. farmers shared $1.8 billion in exchange for contracts that they would quit producing milk.
- A number of ball players receive salaries of a million dollars or more. These salaries are possible because club owners are entitled to many millions of dollars for the right to televise games. These payments are based, in turn, on the right to advertising fees paid by large food manufacturers who seek to differentiate their products to increase sales to consumers. Finally, the whole package is possible because television stations own rights to exclusive use of designated television frequencies, which were originally given away by the U.S. Government.
- A landowner, fully employed in a lucrative nonfarm job, and having farm assets well in excess of $1 million, may still be entitled to more than $50,000 in farm program payments. At the same time, an unemployed mother who has an automobile valued at $6,000 is not entitled to food stamps. (The law states that a recipient of food stamps can have no more than $1,500 in assets, although there are some exemptions. Specifically, one may have a house and an exemption of $4,500 of value in an automobile.)
- A worker who cleans in an automobile factory can receive more than $30 an hour in wages and benefits while a person doing essentially the same work in a fast food restaurant in the same community receives about $4 an hour.



Wipe Outs And Windfalls

Though we are highly selective in deciding which economic losses should be compensated, rights to windfall benefits, on the other hand, are seldom questioned. In the United States, a huge body of law defines property and codifies the Fifth Amendment to the Constitution. It states that "No person shall...be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use without just compensation." The common law, evolving from many years of court cases, legislation at all levels of government, and convention, defines and elaborates the meanings of "property," "due process of law," "just compensation," what constitutes a "taking" and what is "theft." Selective interpretation of these concepts has important consequences for equity and productivity.

As an illustration, suppose that you were to conduct a careful analysis of the market for a restaurant on one of four corners of a rural intersection. Based on that information, you invest your life savings in the business and install the optimum-sized restaurant for that location. The restaurant is just large enough to produce revenue to meet costs and return a normal profit.

The perceptions we hold about the way the system works and should work are selective.

Now suppose that I see your successful enterprise and decide to build a restaurant of comparable capacity across the street. As a result, you lose business and neither of us can cover our variable costs nor maintain quality to attract return customers. The value of the fixed assets of both businesses drops to salvage value, which is less than our debt, and each of us must file for bankruptcy.

Obviously, I made a mistake and I suffered. Since I could have avoided the mistake, most people would not be concerned that I suffered the consequences of the mistake. But what about you? You performed well, yet you suffered from my mistake. In fact, you suffered more than if I had burned your establishment, in which case you would have received insurance benefits. You may wonder why it is illegal for me to destroy your life savings by one act and not the other. After all, you can buy insurance to protect yourself from fire, but you cannot buy insurance to protect yourself from my mistakes, even though you have more control over the possibility of fire than over the consequences of my business mistakes.

Change the scenario. Suppose that your business thrives, as it should, based on good management and hard work until the government decides to build a new highway some miles from your business. The highway is designed to go through my farm, and I am offered just compensation. Since the farm is mostly corn land, the compensation is based on the expected income from corn production including expected government payments (nearly half of net farm income in 1987). Note that I am entitled to compensation for loss of government payments in this case. And my blessings continue; since the new highway reduces the cost of transportation to the nearby city, my land becomes prime property for development. I become wealthy and send my son to Harvard for an MBA. As a result, he becomes very rich as the manager of a junk bond fund used to finance foreign companies in leveraged buyouts of U.S. food manufacturing and merchandising conglomerates.

The leveraged buyout, now profitable because of a change in tax laws, provides the opportunity for managers of firms with undervalued stock to become rich from golden parachutes and stock options when the poison pills developed by law firms, charging millions of dollars, fail.

In the meantime, you, poor devil, go bankrupt because the new highway, built by the government using gasoline taxes, diverts the traffic from your four corners. You seek just compensation and argue that it is a "taking," but to no avail. Your son cannot go to college and gets a job near the highway working for one of the franchised fast food restaurants taken over in the leveraged buyout. He works for the minimum wage and has joined a radical coalition of poor people who believe the minimum wage should be increased. In defense, the takeover firm hires a retired congressman on an annual retainer of $100,000 a year to make the case against the minimum wage, arguing that the government should not interfere with the market.

This is, of course, a fable. But it does mirror contemporary events. For example, Philip Smith, Pillsbury's departing chief executive officer, will receive benefits of at least $8 million from his five-month tenure with Pillsbury, much of which was spent in a failed effort to avoid a takeover by Grand Metropolitan PLC, a British firm *(Wall Street Journal,* December 21, 1988). At least $2 million of this compensation was part of the severance package,

which also included stock options. In addition, Smith became eligible for retirement benefits of at least $200,000 a year. Only five months earlier, John Stafford received a $2-million severance package when he was replaced by Smith. Pillsbury reported significant additional expenses associated with the takeover battle, including $40 million in fees paid to investment bankers.

The Case Of Agriculture

From 1981 to 1987 the value of farm assets in current dollars declined about $300 billion, or 30 percent. The value of farm equity declined about $270 billion, also nearly one-third. About 250,000 fewer farms were reported in 1987 than in 1981. The loss of asset values varied greatly among farmers and had different effects on their welfare. Those who were highly leveraged were much more likely to be forced into bankruptcy, having lost all of their equity. Farms with sales of $500,000 or more lost average asset value of $760,000 from 1981 to 1987, while the large number of farms with sales under $5,000 lost average asset value of only $3,000. It can be argued that farmers should have received compensation for these losses because, for the most part, they were due to deliberate federal policies designed to wring inflation out of the economy. Why were these policies not a taking under the Fifth Amendment? Does the deliberate deflationary policy provide a justification for the very large losses of the Farmers Home Administration, which attempted to support a few highly leveraged farmers facing bankruptcy? Or do farmers who did not borrow to build unneeded capacity have a case against Farmers Home and the Farm Credit System for reducing the value of *their* assets by contributing to the overcapacity problem?

Satisfactory political-economic performance requires that we adjust the rules to modify the outcome as we go along.

Over the same period, 1981-87, Commodity Credit Corporation net cash outlays totaled about $100 billion. Without these payments, asset values would have dropped much more. If these program payments were to compensate for the lost asset values, then the distribution of payments, most of which went to people with much higher than average levels of wealth and income, would appear equitable; asset values dropped most among farms with the greatest sales, and payments were distributed in about the same proportion as losses. However, if the objective was to achieve equity in farmers' income with other Americans, the distribution of benefits seems to have completely missed the mark. Payments were made to farmers with incomes and wealth much higher than average nonfarm families have.

One might argue that these losses should be compensated by government. But then should there be symmetrical treatment for windfall gains which were due to a large extent to a combination of monetary-fiscal policy, and farm programs? From 1975 to 1981, the value of farm assets more than doubled, increasing about $517 billion in current dollars. Perceptions of equity was again selective with respect to this good fortune. No one suggested that these gains to farm asset owners were undeserved and, therefore, properly belonged to the government that created them.

Recent farm policy discussions raise questions about the nature of entitlements in farm programs when considering the controversial issue of phasing out production-linked payments. Are the payments private property? Up to the point where the Secretary of Agriculture makes a decision on payments due for a particular season, payment programs do not appear to be entitlements that would be recognized in court, except perhaps as they influence land values or are involved in the taking of land. Recognition by Congress is, of course, a very different thing. Congress is very selective in compensating for losses due to its actions. Here, public opinion and political pressure tend to define who or what gets compensated.

The compensation issue is involved in many aspects of food policy. Recently, for example, an official of the British Ministry of Health stated that approximately 40 percent of British poultry and eggs were tainted with salmonella. Sales of poultry plunged, and producers and processors experienced large losses. They claimed a right to compensation, and the official lost her job. Denmark enacted a law requiring poultry growers to provide larger cages for chickens. As a result, Danish poultry farmers became less competitive with other growers. Do these Danish farmers deserve compensation? Political power, perceptions of rights, and court precedents influence the selective compensation for losses from government actions.

Market And Trade Distortions

As far as I can determine, there is no basis in economic theory to identify any particular rule, right, subsidy, or policy as one that causes market or trade distortion. Our theory says that free markets allocate resources efficiently when all actors follow maximizing behavioral rules, taking all the institutions, preferences, wealth distribution, and technology as given. For every different set of rights (including wealth distributions) a different efficient solution exists.

In the pragmatic world of policy, particular regulations, rights, and subsidies, if they do anything, make some people better off and others worse off. Economic analysis can show who is made better off and who is hurt, but it cannot judge if this is good or bad. A policy change may make incomes more or less equal, it may result in more and cheaper butter or more or less trade, but there is no *a priori* basis for judging these outcomes as market distortions. And, in the context of traditional theory, given all of the deviations from the economist's ideal market, one cannot tell if a particular rule that influences market outcome is causing a distortion or a correction.

Trade takes place in response to relative prices. Relative prices are shaped by physical production possibilities and all of the rights that influence costs and demand. If the government prohibited the use of all chemicals that could cause environmental or health problems, costs of food production would increase, relative agricultural prices would change, and exports of farm commodities would fall (unless all countries followed the same rules). In such a case, would eliminating the law be considered a producer subsidy and a trade distortion? If the law were passed and farmers were awarded compensation in the form of price support payments for a taking of property under the Fifth Amendment, would the payments be considered a market and trade distortion? Does Denmark's law specifying cage sizes for chickens create a trade distortion by changing relative prices?

The objective of this discussion is simply to point to the great selectivity inherent in labeling a particular policy as a market or trade distortion and suggesting that the policy should be eliminated in the interest of public welfare. Such labeling clouds the policy debate for it fails to recognize that the market is necessarily an instrument of the regulatory system. Recognizing this fact, on the other hand, permits policymakers to focus attention on the real nature of the policy choices such as the entitlements to the fruits of our inherited knowledge. After all, if all government actions that influence costs and relative prices were eliminated, there would be no trade at all; there would be no rights to trade.

Government And Markets

Markets are wonderful institutions for articulating preferences while coordinating and disciplining economic activity. An essential role of government is to establish the rules of the market, to provide goods and services that cannot be effectively demanded or supplied through markets, and to otherwise modify the outcome of markets to achieve social, political, or economic objectives. In an ideal world, citizens might establish all entitlements and other rules in an economic constitution and let the game be played. In the real world, this has not been the case. Satisfactory political-economic performance requires that we adjust the rules to modify the outcome as we go along. Since properly instituted markets are much more effective mechanisms for articulating preferences and coordinating economic activity than government central planning, the use of markets is preferred when and where feasible. Thus, the first option in redesigning policy to improve unsatisfactory performance should be changing the rules of the market rather than bringing the activity under government management. However, it is equally necessary to understand and accept the limits of markets in achieving desired economic goals, especially in meeting objectives of equity and justice.

The theme here has been that the perceptions we hold about the way the system works and should work are selective. This restricts both the evaluation of performance and the consideration of alternative institutional arrangements. In food policy this theme is particularly relevant to the reevaluation of the farm programs, trade negotiations, wage and salary policies (especially in light of the low incomes of many of the workers in the food system), food safety, regulations and expenditures for environmental protection, market competition and discipline, and food entitlements.

The Future Policy Process

The policy process plays a part in determining the future, but in incremental and evolutionary steps, the future is determined by history. In this process, it is not possible to take everything into account at once. Because we cannot know with certainty, the ultimate nature or impact of many fundamental relationships important to policy questions, we must deal with the uncertainty of consequences of policy action. We must plan on adjusting policy as we learn the consequences of past policy.

Shared myths are the glue that holds the system together. Ideology is a powerful force supporting the established order and shaping the future and may be the ultimate source of political power. Because political and economic power are unequally distributed, concentrated interests exert disproportionate influence in shaping policy in their favor. Because costs of changing the system of rights are high, the persistence of existing policies that regulate the food and agricultural system is not surprising.

Nonetheless, very significant changes in policy and in the system of rights do occur. In food and agricultural policy, much greater attention is now focused on environmental protection and food safety than in the past, resulting in significant changes in rights. The problem of hunger within the United States has been addressed, although imperfectly, through food stamps and welfare programs. Eventually, increased awareness of the maldistribution of farm program benefits will bring changes in those programs, too.

In determining future food and agricultural policy, fundamental questions of entitlements and their relationship to food system performance need to be addressed. But can these issues be debated and acted on within the current political system? Are we destined to realize only marginal changes in the status quo within the bounds of narrow interest politics? One hopes that the policy debate will not become an unimportant sideshow with the real action resulting from the purchase of political influence by political action committees and professional lobbying firms. Analysis and ideas can and should wield power in the policy process.

Data, analysis, experience, and dialogue all work together in changing perceptions of the way the system works and how institutional innovations might alter performance. Understanding the selective nature of the perceptions that shape policy is a first step toward analysis that more effectively relates the characteristics of the system of rights to the performance of the food system.

Author's Note

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