DEFICIENCY PAYMENTS

More Fair To Some Than To Others?

by Carole Frank Nuckton and B. Delworth Gardner

U.S. price support programs for the major commodities have always been justified at least partially on equity grounds. Subsidized production is supposed to provide a "fair" return on the risky investment that is farming and permits farm families to remain in a sector that without the government programs might have been forced out. Here we analyze whether one important aspect of crop price support programs—the deficiency payment—is "equitable."

Deficiency payments for wheat, the feed grains, cotton, and rice are based on the difference between the target price and the U.S. average market price (whenever the market price is above the loan rate). They are the same for all producers of a commodity who are enrolled in the relevant government program.

By one interpretation the current payment scheme is obviously "equitable," for payments are *equal* for each unit of the commodity marketed, regardless of the market price received for that unit. But is this really "fair" in the sense that net incomes of all producers of the commodity are affected equally by the payment program? Hardly! A farmer in one region of the country who produces a variety of a crop that sells considerably above the U.S. average for all varieties receives the same deficiency payment as one who sells at the average or even below the average market price.

The "equity" of deficiency payments could be questioned on even more basic grounds—like "How come they are made only to growers of certain commodities but not to others?" However, here we confine ourselves to the task of demonstrating the inequity of equal payments within a commodity group. We use wheat as our illustration, but the same conclusions are broadly applicable to rice, cotton, and other supported commodities that differ by region, variety, use, final market, and market price received.

The five major classes of wheat are hard red winter, hard red spring, soft red winter, white, and durum. These wheats differ by production region, yield, protein content, and end use.

Focusing on just two of the five: *Hard red winter* wheat is grown in the central and southern plains and in California. It is high in protein, strong in gluten, and is used primarily for quality yeast breads and hard rolls. *White wheat* is produced in the Pacific Northwest (PNW), with some production in New York and Michigan. It is used for flat breads, cakes, pastries, crackers, and noodles. While hard red winter dominates white in national production (three to five times as many total bushels in a given year), average yields are much higher for white than red wheat (63 bu./acre in 1990-92 compared to 36 1/2 bu.). The two varieties also differ in costs and methods of production.

Despite these differences, in figuring deficiency payments to U.S. wheat growers, the average U.S. market price across all regions/varieties is used. Hence, per bushel deficiency payments for all wheat producers in the country are identical whenever market prices are higher than loan rates. This means that farmers in some regions producing certain varieties receive significantly higher per bushel benefits from the target-price subsidy program than farmers producing other varieties. They get the same deficiency payment as all the others and sell their crop at above average market prices. In fact, conceivably, they might even sell their crop at a price above the target price and still receive a deficiency payment.

Table 1 gives target prices and deficiency payments based on the U.S. average market price for 1986-87 through 1990-91, a period when the market price was always above the loan rate. It also estimates what the deficiency payments would have been had they been based on the market prices of the respective varieties.

Table 1. Deficiency Payments If Based On Varietal Prices

Per 60 Lb. Bu.

	1986-1987	1987-1988	1988-1989	1989-1990	1990-1991
Target price	$4.38	$4.38	$4.23	$4.10	$4.00
U.S. average market price	2.42	2.57	3.72	3.72	2.61
Hard red winter market price	2.39	2.57	3.74	3.70	2.52
Pacific NW ave. market price	2.59	2.74	4.14	3.88	2.75
Deficiency payment if based on average varietal price, hard red winter	1.99	1.81	.49	.40	1.48
Actual deficiency payment made to both	1.96	1.81	.51	.38	1.39
Deficiency payment if based on average varietal price, PNW white	1.80	1.64	.09	.22	1.25

Source: U.S. Department of Agriculture, Economic Research Service, Wheat Situation and Outlook Report, WS-294, August 1991, plus calculations by the authors.

The year 1988-89 is of special interest. PNW producers of white wheat received a price so close to the target price that a deficiency payment based on that difference would have been only 9 cents per bushel, yet they received 51 cents in deficiency payments based on the U.S. average market price. In fact, in all five years, their actual payments were considerably more than they would have been had they been based on varietal market prices.

The production of white wheat that year was approximately 232 million bushels. Assuming that all producers of white wheat received deficiency payments, this means that about $97.3 million were paid out to white wheat producers in excess of what they would have received had a more "equitable" policy been in force. This is not an inconsequential sum.

Unlike so many of the complex, intricate problems with U.S. farm policy, this particular equity problem is relatively easy to fix. When computing deficiency payments, simply use the average varietal market prices, instead of the U.S. average price across all varieties. This policy change would not reduce government payments, except occasionally when farmers sell their crops above the target prices. However, it would provide a fairer distribution of government largesse by not giving more to those who got more for their crops in the first place.

Carole Frank Nuckton is Visiting Associate Professor, Oregon State University, and B. Delworth Gardner is Professor, Brigham Young University.