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FEDERAL RESERVE BANK OF CHICAGO

AGRICULTURAL LETTER

ISSN 0002 - 1512

September 2, 1983 Number 1611

NAITE MEMORIAL BOOK COLLECTION
DEPT. OF AGRIC. AND APPLIED ECONOMICS

POSSIBLE CHANGES IN THE DAIRY SUPPORT PROGRAM are still veiled in a shroud of uncertainty. The Congress adjourned for a six-week recess in early August without passing the compromise legislation that had been widely expected. That legislation would have lowered the support price of milk from $13.10 to $12.60 per hundredweight, instituted a paid-diversion program for dairy farmers who cut their production by 5 to 30 percent from the levels of fiscal years 1981 and 1982, and retained—on a mandatory basis—the 50 cent per hundredweight deduction from all milk checks to dairy farmers. (A 50 cent deduction has been in effect at the Secretary of Agriculture's discretion since mid-April.) The inaction by Congress prompted the Administration to go ahead with a September 1 implementation of a second 50 cent deduction, to be refunded to dairy farmers who lower their marketings by a specified amount. Whether the highly unpopular second 50 cent deduction will yet be rescinded by Congressional action is subject to considerable debate.

The need to alter the dairy support program has garnered increasing acceptance as the government's cost of maintaining the program has soared. Although unchanged since October 1980, the current $13.10 per hundredweight support price for milk has been sufficient to generate steady increases in milk production. The increases have resulted in a growing gap between milk production and the commercial market demand for fluid milk and manufactured dairy products. To maintain the support price of milk in the wake of the growing imbalance, the government—through the Commodity Credit Corporation (CCC)—must remove the surplus from commercial market channels by purchasing manufactured dairy products from processors. In recent years, CCC purchases have absorbed the equivalent of 10 to 12 percent of all milk marketed by farmers, up from an average of 2.5 percent in the latter half of the 1970s.

The expanded purchases have been costly and have culminated in a huge inventory of CCC-owned stocks of dairy products. After averaging less than $500 million annually in the three fiscal years ending with 1979, net CCC expenditures for the dairy support program have averaged $1.8 billion annually the past three fiscal years and are projected to reach $2.4 billion in the fiscal year that ends this month. The escalating expenditures have boosted the CCC's uncommitted stocks of butter to nearly 5 times the level of three years ago and raised its holdings of butter and nonfat dry milk by multiples of 1.7 and 1.3, respectively, over the same period. In the case of butter and cheese, the ending July CCC inventories were equivalent to roughly half of the poundage of those items sold through commercial channels in all of 1982. CCC stocks of nonfat dry milk were equivalent to nearly 30 months of commercial sales.

Despite a recent dramatic increase in donations from the CCC stockpiles—which has aggravated the imbalance with production by slowing commercial sales—CCC holdings continue to grow. And in addition to the CCC-held stocks, commercially-held stocks remain substantial, although down from typical levels of past years and substantially below the stocks owned by the CCC.

The policy options for correcting the problems of excess production, high government costs, and burdensome government-held stocks are difficult at best, particularly since the problems have grown to such magnitudes. But the options must focus on lowering production incentives and/or raising commercial demand. The compromise legislation has far more industry support than the two 50 cent deduction plans, in part because lowering the support price would lead to lower retail prices and, hence, larger consumer purchases of dairy products. The compromise legislation also offers stronger incentives for cutting production. In addition to effectively cutting farm milk prices by $1—through the 50 cent reduction in the support price and the mandatory 50 cent deduction—the compromise legislation offers a paid diversion option. That option would permit dairy farmers to voluntarily enter contractual agreements for reducing—through the end of 1984—their production

by 5 to 30 percent from their output in fiscal 1982 or, at their option, the average of their output in fiscal 1981 and 1982. For each 100 pounds of eligible reduction, the farmer would receive a payment of $10. The paid diversion option would be attractive to many dairy farmers. However, it would be costly to the Treasury and its lasting impact on production after the end of the program in December 1984 is somewhat suspect.

Whether dairy legislation will yet be enacted in a form similar to the compromise package is uncertain. The fact that the legislation encompasses ties with the Administration's desire for a freeze on grain target prices proved the major stumbling block prior to the Congressional recess. Congress' distaste for a freeze has no doubt been reinforced by the extensive drought damage. And some reports suggest that the Administration's insistence on freezing target prices has waned somewhat. Nevertheless, as things now stand, the second 50 cent deduction will be the major plan attempting to correct the imbalances in the dairy program through September 1984.

The second 50 cent deduction, in conjunction with the 50 cent deduction imposed earlier, will effectively lower milk prices received by dairy farmers by $1 per hundredweight through September 1984. However, farmers who reduce their milk marketings by 8.4 percent from the average of fiscal years 1981 and 1982 will receive a refund of the second 50 cent deduction. Unrefunded deductions will be retained by the CCC to help defray the costs of the dairy support program.

The two 50 cent deductions offer a potential of $1.3 to $1.4 billion—on an annual basis—to offset the CCC's cost for the dairy support program. However, by not lowering the support price, the plan fails to encourage larger consumer purchases. Moreover, analysts are skeptical that the program will be effective in reducing production. Although feed costs will be higher because of the drought, dairy herds still exceed year-ago levels and the level of replacement dairy heifers remains at a record high with respect to the size of the milking herd. Moreover, without legislative changes, dairy farmers would likely position themselves to take advantage of existing statutes that will result in an increase of $1 or more in the support price of milk a year from now. In light of these considerations, USDA forecasts suggest that milk production in fiscal 1984—assuming the two 50 cent deductions remain intact—will virtually equal the record high for the current fiscal year. With production unchecked and no prospects for a significant pickup in commercial use, net CCC removals would remain at a very high level, resulting in a further rise in the already burdensome level of CCC stocks.

Regardless of what provisions ultimately characterize the dairy support program for the next several months, there will be repercussions of consequence. If the provisions are unsuccessful in correcting the imbalance between milk production and commercial use, federal outlays to maintain the support program will remain very large and government-owned stocks of dairy products will continue to mount. If the imbalance is corrected entirely through production cuts, the adjustment will be economically painful to dairy farmers or—if a paid-diversion feature is adopted—add another component to the government's cost of maintaining the dairy support program. Moreover, to the extent that the imbalance is corrected through production cuts, the resulting liquidation of dairy cattle will push some of the burden of the adjustment onto cattlemen in the form of lower cattle prices. To the extent that the imbalance is corrected by lower support prices, the burden of the adjustment on dairy farmers would be partially cushioned and consumers would benefit from lower retail prices on dairy products. But commercial dairy processors would suffer a loss on the value of their inventories, unless reimbursed by the U.S. Treasury. Regardless of the options selected, the short-run consequences will be detrimental to the economic well-being of some interested parties. However, failure to take corrective actions can only aggravate the imbalances and add to the long-run cost to taxpayers of maintaining the program.

Gary L. Benjamin

FARM EQUIPMENT SALES may be on the verge of a turnaround from a long and steep decline. Although trends for individual equipment items were mixed, estimates from the Farm and Industrial Equipment Institute (FIEI) suggest that the decline in farm equipment purchases may have begun leveling off in the first half. Unit sales of tractors and combines were down from year-earlier levels but sales of other equipment were up. More importantly, there has been encouraging news regarding farm prices, income, and 1984 crop plantings that foreshadows increasing sales ahead.

Sales of farm equipment and machinery declined precipitously the past three years. Unit sales of farm tractors, combines, and mower conditioners last year were nearly 50 percent below the strong outturn in 1979. Sales of balers, forage harvesters, and cornheads fell more than 50 percent over the last three years. While

farm equipment sales declined throughout the period, a proportionately large share of the downturn occurred last year as low farm earnings and high interest rates curtailed farmers' capital expenditures.

In the first six months of this year, unit sales of farm tractors with 40 or more horsepower were down 10 percent from the year before. However, sales for the second quarter were up 6 percent, paced by a 19 percent rise in June. Two-wheel drive tractors with over 40 horsepower showed a sales decline of 8 percent through June. Only the largest tractors in this group—those with over 140 horsepower—gained over last year's unit sales. Four-wheel drive tractors, however, continued to lag 1982 sales by 40 percent.

Unit combine sales registered large year-over-year gains in the first quarter. But declines in the second quarter pulled combine sales for the six month period nearly 2 percent below the year-before level. Forage harvesters, grinder-mixers and windrowers were selling 10 percent or more off the pace of the first six months of 1982.

Other types of farm equipment registered their first semi-annual sales increases since 1979. Sales of balers—that produce bales of less than 200 pounds—increased 20 percent from the same period last year. Mower conditioner sales rose 13 percent reflecting farmers' demand for machinery to maintain the cover crops planted on idle land. Cornhead sales through June were running 2 percent ahead of last year, despite a substantial decline in sales for the second quarter.

Farm equipment sales in Seventh District states in the first half were somewhat stronger than for the overall United States. Tractor sales, including units with less than 40 horsepower, were down for the first half of the year, but second quarter sales showed a 2 percent pickup over last year's figures. In contrast to a slight decline nationwide, first-half combine sales in District states were up a third from last year's pace. The increase in combine sales was spread across all states except Michigan which experienced an 8 percent decline from a year ago. Sales of balers in the five state area rose by a fifth from the first six months of 1982. The sales increase was most notable in Michigan where more balers were sold in the second quarter of 1983 than in the entire first half of 1982.

Although less dramatic, sales of mower conditioners and cornheads in District states showed appreciable gains from last year. District sales of mowers and cornheads through June increased 11 and 13 percent, respectively, from the same months a year ago. The increased sales of both items were most pronounced in Indiana where mower sales jumped 47 percent and cornhead sales were almost a third higher than last year for the same period.

Inventories of farm equipment are down considerably from a year ago, reflecting the extensive plant shutdowns that have prevailed for several months. However, inventories of most farm equipment items persist at levels well in excess of the previous twelve months' sales. June inventories of tractors with 40 or more horsepower were down 18 percent from a year earlier. Most of this decline was accounted for by a large reduction in stocks of farm tractors with less than 100 horsepower. Nevertheless, tractor inventories in all categories above 40 horsepower still constituted 92 percent of the sales made during the last twelve months. Similarly, combine inventories were still equivalent to 99 percent of sales for the previous twelve month period despite a 16 percent reduction from last June. Inventories of balers, forage harvesters, mowers and cornheads were down 20 to 32 percent from last year but sales of each during the twelve months ending in June were less than the stocks on hand at mid-year.

The FIEI's figures on farm equipment sales and inventories do not portend a dramatic turnaround for the industry this year. In conjunction with a number of other factors, however, the figures do point to an improving picture for farm equipment sales through the rest of this year and into the next. Following a three-year downturn, the rate of decline in farm equipment sales appears to be leveling off. Moreover, sales in Seventh District states—the major market for much of this equipment—may be foreshadowing increased sales elsewhere. Backing up these sales trends are the recent increase in commodity prices and an improved outlook for farm income in 1983. Current and prospective crop prices have increased sharply in response to the extensive drought damage. The jump in crop prices combined with lower production expenses and the PIK entitlements signal a boost in farm income. Official USDA forecasts suggest that net farm income in 1983 will range from $25 to $29 billion, up from $22 billion last year. Furthermore, it is becoming more apparent that PIK and government programs for limiting 1984 crop acreage will be greatly curtailed. As much of the acreage idled this year under these programs comes back into production it seems likely that farmers will require additional equipment. Barring unfavorable developments in interest rates, prospects for expanded acreage and higher farm earnings could trigger a fairly large recovery in farm equipment sales over the next several months.

Peter J. Heffernan

Selected agricultural economic developments

Subject	Unit	Latest period	Value	Percent change from Prior period	Percent change from Year ago
Index of prices received by farmers	1977=100	August	137	+ 4.6	+ 3
Crops	1977=100	August	136	+ 8.8	+16
Livestock	1977=100	August	139	+ 1.5	- 6
Index of prices paid by farmers	1977=100	August	161	+ 0.6	+ 3
Production items	1977=100	August	154	+ 1.3	+ 3
Producer price index* *(finished goods)*	1967=100	July	286	+ 0.2	+ 1
Foods	1967=100	July	261	- 0.1	0
Processed foods and feeds	1967=100	July	255	+ 0.2	0
Agricultural chemicals	1967=100	July	279	- 1.1	- 4
Agricultural machinery and equipment	1967=100	July	326	+ 0.2	+ 5
Consumer price index** *(all items)*	1967=100	July	299	+ 0.4	+ 2
Food at home	1967=100	July	283	- 0.1	0
Cash prices received by farmers					
Corn	dol. per bu.	August	3.45	+10.2	+50
Soybeans	dol. per bu.	August	8.09	+28.8	+45
Wheat	dol. per bu.	August	3.57	+ 6.9	+ 7
Sorghum	dol. per cwt.	August	5.30	+ 5.4	+34
Oats	dol. per bu.	August	1.56	+ 6.8	+12
Steers and heifers	dol. per cwt.	August	57.50	- 1.9	- 8
Hogs	dol. per cwt.	August	47.00	+ 8.3	-23
Milk, all sold to plants	dol. per cwt.	August	13.30	+ 0.8	0
Broilers	cents per lb.	August	31.8	+ 3.6	+20
Eggs	cents per doz.	August	63.3	+10.1	+24
Income *(seasonally adjusted annual rate)*					
Cash receipts from farm marketings	bil. dol.	2nd Quarter	141	- 0.6	0
Net farm income	bil. dol.	2nd Quarter	26	+ 6.5	+55
Nonagricultural personal income	bil. dol.	July	2,699	+ 0.6	+ 6

*Formerly called wholesale price index.

**For all urban consumers.

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