Policy Intervention and Unstable Markets

Agricultural Stability and Farm Programs: Concepts, Evidence, and Implications *Edited by Daniel A Sumner Boulder, CO Westview Press, 1988, 177 pages, $23 50*

Reviewed by Margot Anderson

Books like this one on the pervasive instability in agricultural markets and the efficacy of government intervention are always timely, even more so when budgets are under review and agricultural policies are being reconsidered within the GATT This worthwhile collection of six papers, the output of a symposium supported by The Farm Foundation, the North Carolina Agricultural Research Service, and Resources For the Future, addresses sources of instability, their economic effects, and the rationale and effectiveness of agricultural policy

The collection contains general essays on the causes and effects of instability and case studies of specific policies and markets Its likely audience is broad, including graduate students in agricultural policy, practicing economists, and policy analysts Some of the topics addressed in this collection have been previously published in journals or presented at professional meetings. The advantage of the book format is that it provides space for more detailed discussion of each topic The required level of economic rigor needed for a full appreciation of the essays varies from an elementary background in supply and demand analysis to more advanced training in economic theory Each essay is followed by a commentary from a symposium participant

The first essay (Meyers and Oehmke) and the last (Rausser) provide a background for understanding the causes of instability and its potentially adverse effects on economic efficiency Meyers and Oehmke focus their essay on instability and risk as courses of market failure While the existence of market failure can provide the rationale for government intervention, the authors argue that the efficiency gains from policy may be quite small Three types of market failure associated with instability are discussed 1) disequilibrium (due to sticky prices from price rigidities and long-term fixed contracts), 2) incomplete forward markets, and 3) incomplete contingency markets The difficult task of devising and implementing corrective policies rests on an adequate body of empirical estimates of the efficiency losses from these market failures To date, the existing estimates indicate that the efficiency losses are small More important, the authors implicitly stress the need for further empirical analysis on efficiency losses due to market failures

Rausser examines the causes of instability by grouping them into three categories internal, external, and government instability The discussion on internal instability, such as instability caused by environmental shocks, inelastic demand, asset fixity, and incomplete risk markets, covers familiar ground Rausser's coverage of external disturbance arising from macroeconomic and trade factors acknowledges more recent explanations of instability Rausser presents a concise review of both price overshooting and trade effects of volatile macroeconomic policies

Both essays present discussions on instability created by government policies. Rausser has long been associated with examining how intervention policies designed to correct for internal and external instability can themselves be destabilizing This type of nonmarket failure, which is frequently overlooked in agricultural economics literature, occurs because policies may induce outcomes that can be less efficient than in an unregulated and imperfect market The political process that creates agricultural policy can be influenced by nonefficiency goals, such as maximizing agricultural budgets or appeasing powerful special interest groups The resultant effect can induce resource allocations that are no more efficient than nonintervention resource allocation

Fackler's essay compares government policies with market-based institutions designed for stabilization For example, options and futures markets are similar to price supports, but the costs and benefits are significantly different and must by considered by advocates of a more market-oriented agricultural sector. Not discussed in Fackler's essay, but worth attention, are market-oriented stabilization schemes and institutions commonly used in other agricultural subsectors like poultry and fruit and vegetable markets These markets also exhibit instability, although for different reasons, but there is less government intervention

Two case studies are also presented in the collection Martin examines stabilization schemes for the feed grain markets, Sumner examines the tobacco pro-

Margot Anderson is an agricultural economist with the Resources and Technology Division, ERS

gram Both essays discuss the evolution of policies and present estimates of the efficacy of stabilization policies

While collections of papers are not intended to be exhaustive, some additional topics might have been considered An essay or discussion of the connection between instability and uncertainty would have been beneficial These concepts are not synonymous, and as pointed out in Sumner's introductory remarks, the rationale for some types of stabilization policy can be predicated on instability alone But, unanticipated changes in costs and revenues may be more important for other stabilization schemes The book also needed a brief discussion of volatility in other industries How volatile are prices and incomes in other industries? Consideration of policy goals, other than economic efficiency, could have been included, too These goals might include the effects of stabilization policies implemented to achieve equity or smooth adjustment or to correct for instability caused by macroeconomic policies

A small point on measures of instability coefficients of variation, such as those reported by Martin, may be inappropriate measures of instability This would be the case if the variables are not normally distributed which is unlikely given the extremely small sample sizes and existence of outliers particularly during the 1970-79 period Robust estimates of scale and location, however, exist as do hypothesis tests that could compare measures of variability across time for normal data

The papers include (1) "Instability and Risk as Rationales for Farm Programs" by Robert J Meyers and James F Oehmke, (2) "Storage, Stability, and Farm Programs" by Brian D Wright, (3) "An Analysis of Alternative Market and Governmental Risk Transference Mechanism" by Paul Fackler, (4) "Stability and Farm Programs A Case Study of Feed Grain Markets" by Marshall A Martin, (5) "Stability and the Tobacco Program" by Daniel A Sumner, (6) "Stability Issues and Policy Analysis" by Gordon A Rausser