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## CONSEQUENCES OF PUBLIC POLICIES FOR SMALLER FARMS

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### **Smaller Farms and Low Income Farms**

There are many kinds and categories of “smaller farms” in the U.S.A. These include such diverse situations as low resource farmers, urban workers who are rural residents with some agricultural activities, and counter-culture persons seeking a simpler, rural life style. From a policy perspective and for public policy education we need to distinguish among these heterogeneous types and be clear regarding their problems, issues, or objectives.

“Smaller farm” as used in this report is a euphemism for a low resource, low income farmer. We are concerned with farm families whose net income from all farm and nonfarm sources is unacceptably low in the view of our society relative to their consumption needs.

By federal poverty criteria, there were 1.3 million farm persons living in poverty in the U.S.A. in 1977. The farm poor make up only about 5% of all persons in poverty in the country. But 16% of all farm people are classified as poor compared with about 10% of all urban persons. Farm poor are different from their urban counterparts in a number of ways, but of particular importance is their general lack of visibility to public policymakers, program administrators, and educators.

Low-income farm families live in economically disadvantaged circumstances. They are largely nonparticipants in Extension, agency or community activities, and life. There are substantial numbers of such farm families in all states and in rural counties. Farm poverty is not an isolated problem concentrated in a few states or geographic areas of the U.S. but is a universal problem and public policy issue.

### **Farm Income and Farm Policies**

Many factors affect net farm income, including farm product

prices, cost of purchased inputs, weather and other natural phenomena, nonfarm work by the farm family, preference for leisure, and so on. But basic in determining the level of farm income is the quantity and quality of farm resources controlled. Physical resources such as land, buildings, machinery, livestock, and operating inputs directly influence farm production and income. Human resources—the skills of the farm labor force and the operator's management ability — also place upper limits on how much can be produced and how much income can be generated.

### **Commodity Price Programs**

Public policy intervention directed toward increasing agricultural product prices and reducing their variation dates to Colonial days in America. The objective of farm commodity programs usually is to raise and stabilize the income of farmers who produce the commodity, regardless of the size of their farm business. In that regard, commodity programs have been effective, but it is well documented that price programs which base the payments on area of land or quantity of commodity produced benefit the larger farmers most, both in absolute terms and relative to smaller farmers.

If target-efficient public policies were to be developed for increasing the income of low income farmers through higher commodity prices, they would need (a) a system of graduated prices or payments favoring smaller farms, or (b) to be applied to farm commodities produced only on smaller farms, or for which smaller farms had a substantial natural advantage.

In the latter case, family labor-intensive enterprises that do not readily accommodate the substitution of machines or hired labor for family labor would be in order. Dairy farming, tobacco, and certain horticultural food crops may have some of these attributes, but in general, smaller farm businesses are not commodity-specific. Low income farms tend to be smaller scale units with input and product mixes similar to the larger farms in their region. As a consequence, aggregate benefits of federal programs to raise or stabilize commodity prices have accrued primarily to larger farmers.

This is not to say that small farmer well-being is unaffected by the commodity price level. Using an example from the Midwest, an increase in the price of milk by one dollar per hundredweight may increase the net cash operating income of a smaller Wisconsin dairy farmer \$2,500 per year. This may increase the cash residual that is available to him for family living expense, capital replacement, debt retirement, and business expansion from \$4,500 per year to \$7,000 per year, a substantial and important change in absolute income for him. However, his larger neighbor will have gained more than he in absolute income and the income difference between them will have widened. The larger neighbor may have the economic base to outbid the smaller farmer for additional land or other farm resources. But in the short run, the increase in commodity price has helped the smaller farmer.

In a different kind of commodity price program some smaller producers of horticultural food crops have benefited from the organization of cooperatives to pool, grade, and market their commodities. This has resulted in higher product prices and, through group purchases, the co-op has also reduced input costs. Opportunities for such group activities may be limited to small producers of "specialty" crops with currently limited market outlets.

### **Input Costs**

A second factor affecting the level of net farm income is the cost of purchased inputs. The payment of interest for the use of borrowed funds is only one cash operating expense, but for low-equity farmers it may be a substantial cost. It is a policy-relevant input, and most of the legislation proposed in the U.S. Congress and in various states to assist farm entrants and small farmers includes subsidized interest rates.

The recently enacted Agricultural Credit Act of 1978 contains provisions for real estate loans to "qualified small farmers" at 3% interest, increased after three years to 5% and reviewed at two year intervals thereafter to determine ability to pay. Farm operating loans at 5% interest are also permitted by the act, both loan types to be administered through the Farmers Home Administration (FmHA). Compared with commercial market rates of 10% the qualified recipients would enjoy a large input cost saving in reduced interest expense. For maximum loans permitted to small farmers under the act, the first year saving in cash operating cost would be \$19,000 compared with unsubsidized credit.

### **Expanding the Resource Base on Small Farms**

The Agricultural Credit Act of 1978 also increased the upper limits on loans that the Farmers Home Administration may make to \$200,000 on farm real estate and to \$100,000 on farm operating loans. For the eligible small farmer, this provides an opportunity to increase his physical resource base and thus the level of farm production and farm income.

In this way the provisions for smaller farms in the Agricultural Credit Act of 1978 address two of the factors that influence farm income: (a) reducing input costs in the case of interest, and (b) increasing quantity of physical resources controlled. However, the consequences of the act are mixed. Those small farmers that are declared eligible and do receive funding will have a significant advantage in generating farm income.

But, potential problems and adverse consequences from the act involve the issue of horizontal equity; that is, persons who are equally disadvantaged should be treated the same. A loan applicant

will be determined to be either completely eligible for a loan or completely ineligible for a loan. This means that loan evaluators must make decisions of critical importance about applicants near the margin in terms of eligibility. In addition, the level of funding for the act has not been determined. If some eligible small farmers receive loans and others do not because of fund limitations, additional horizontal inequities would be generated.

A second adverse consequence of the act involves the advantage given to eligible small farmers compared with ineligible small farmers. While the eligibility criteria are not yet established, it is likely that net value of assets owned and the established use of conventional credit sources by an applicant will be considered in determining eligibility, as is now the case with FmHA loans.

Thus a farmer through his own efforts may have accumulated enough resources to become a small farmer but be ineligible for assistance under the act because of his asset or credit situation. Assistance through subsidized interest and large loans may permit the very low equity farmer to leap financially far ahead of the ineligible small farmer, who by his own effort and without public assistance had managed to make a start on a smaller farm.

A final consequence is the effect on competition for farm resources. With implementation of the act an additional set of buyers will be active in the farmland market, i.e., small farmers who previously lacked equity and credit. This additional competition will have two effects. First, the market prices of farms and farmland can be expected to increase. Second, some persons who otherwise would have purchased land will be out-bid by the subsidized small farmers.

### **Human Capital**

A final policy-relevant constraint on farm production and net farm income is the quantity and quality of human capital invested in the farm business. The Extension small farms programs now operating in several states are investments in human capital through increasing the technical knowledge and management skills of participant farmers, e.g., programs in Wisconsin, Minnesota, Iowa, Missouri, Texas, etc.

Because of the nature of the need on many smaller farms, such programs must be intensive, on-farm, one-on-one types of problem identification and instruction. Subject matter includes farming technology and financial management and the instructor may assist the family to become involved in community life or explore nonfarm alternatives.

The beneficial consequences of these farm training programs are obvious to participants and instructors. It is clear that income, attitudes, self-perception, and community involvement of many participating families have been enhanced because of their

involvement in small farms programs. However, these are difficult concepts to measure. To separate and measure the impact of being in the educational program from all the other forces that cause change in farm family behavior is a very difficult task.

It is with some subjectivity that improved technical efficiency in farming and higher farm income are cited as consequences of this investment in human capital. While these beneficial changes are expected to continue after the farmer has graduated from the program, their permanence has not yet been measured.

Vocational training, job search, and migration — changing the characteristics of the human resource and finding the best opportunity for its nonfarm employment — is also relevant for small farmers. Some small farmers are recent urban-to-rural migrants and entrants into farming. They have decided that their well-being will be increased by using their human resource in a farm business. But there are other small farmers who could increase their family well-being by shifting their resources out of farming to nonfarm wage employment. For them, public assistance in vocational training and in employment search and placement is needed.

### **Guaranteed Income-Implicit Tax Programs**

Now we turn to public intervention for increasing the income of all low income families, regardless of residence, and consider the consequences and implications for low income farmers. This income support is in the form of a universal, guaranteed income for all Americans. Under this system an eligible family with no income would be guaranteed a certain level of income through a direct transfer from the federal or state government. If the eligible family works and earns income, the transfer is reduced by some amount for every dollar earned, i.e., the “implicit tax.” At some level of earned income the transfer is reduced to zero.

This line of discussion is relevant for Extension public policy education for a number of reasons. First, the direction of change in federal welfare programs has been toward a universal guaranteed income-implicit tax type of system. Republican and Democratic administrations in Washington have both supported this kind of welfare reform, first as the Family Assistance Plan proposed by the Nixon administration, and now as the Program for Better Jobs and Income developed by the Carter administration. We currently have in operation in the U.S.A. a universal public program that is used by the participants as a guaranteed income, i.e., the Food Stamp program. It is, in effect, a guaranteed income (of about \$2,000 for an example family of four) that is reduced by 30 cents for every dollar of earned income.

A second reason for Extension public policy concern about welfare reform is that rural people have historically not shared in public assistance for low income people, in proportion to their need.

Participation rates of those eligible for the Food Stamp Program have been lower in rural areas than in urban areas. Federal programs to create jobs in the public sector to employ low income people have been located primarily in urban areas. Whether by policy design, lack of information by participants, or administrative discretion, rural clientele have not been helped by federal income support programs in proportion to their needs.

A third reason for interest in guaranteed income programs is their impact, through low income farmers, on rural development. Strategies for community and rural development often revolve around the export base of the community, i.e., what goods or services can be produced in the community but sold "outside." In this sense, government programs and transfers to alleviate rural poverty act as an export base industry. Public transfers from more extensive governmental units, including income support payments to individuals, have the same impact on development as an export base industry.

### **Status of Welfare Reform**

The "Program for Better Jobs and Income" (PBJI), the Carter administration welfare reform proposal, was introduced in 1977. This is a universal guaranteed income with a reduction in benefits determined by the amount of nontransfer income. It would replace the present Aid to Families with Dependent Children (AFDC), Supplemental Security Income (SSI), and Food Stamp (FS) programs. Whether welfare reform emerges as a modification of the present system or an extensive reorganization, the movement toward a federal guaranteed income is clear. In either case, how small farmers have fared in the past and how they may fare in the future is a concern.

### **Eligibility and Benefits**

Those eligible under the administration's proposal include resident aliens, students, single persons, married couples, families, and individuals living together in group quarters. Family composition and size will affect the level of benefits received by a particular unit.

One member of all families would be expected to work unless all the adults in the family were either aged, blind, disabled or a single parent with small children. There would be 1.4 million public service job opportunities created for adult workers (with children) who cannot find jobs. One adult from each family would be eligible, and would generally be paid the minimum wage.

Families would also be protected by a guaranteed annual income of \$2,300 (for an example family of four) that would not be reduced for the first \$3,000 of earnings. Beyond that level, the implicit tax would be 50% and the earned income level at which transfers ceased would be \$8,400.

If the proposal is enacted, increased numbers of persons will find participation attractive. First, for any earned income level, the benefits under the new program would be higher than under the AFDC, SSI and FS programs it replaces. Also, the basic income guarantee in the proposal would be in cash, while it currently is tied to the bonus value of food stamps. Removing the need to participate in the Food Stamp program as a condition for receiving benefits would encourage participation.

### **Participation by Small Farmers**

Small farmers generally have little experience with federal welfare programs. Low income farmers (who are not aged or disabled) are currently ineligible for SSI benefits. Very few now qualify for AFDC benefits, and participation of farmers in the FS program is low. Increased numbers of low income farmers, many without experience with any welfare program, would be eligible for benefits under the PBJI. The rules and conditions for receiving benefits may appear complex to them and the procedures for application may seem formidable. As a consequence, an inequity may arise because urban, former recipients of SSI, AFDC or FS will likely participate sooner in the new program (and the percentage of eligibles participating will be higher) than for equally disadvantaged small farmers. Both program outreach and Extension programming could reduce this discrepancy.

### **Reporting Assets—A Problem for Small Farmers**

Net worth is an important aspect of economic well-being. This is recognized in some current welfare programs through an assets test. Under certain conditions the program benefit may be reduced or the family become ineligible for any benefits because of their asset holdings.

The administration's proposal in its current form treats different classes of farm assets in different ways: The value of the dwelling and its contiguous residential lot is excluded from the assets test, as is the value of all household goods and the first \$3,000 of value of one automobile. Value of farm business (net) assets such as land, buildings, machinery, equipment, and livestock has no upper limit currently specified in the bill, but an upper limit will likely be specified by HEW regulation. Farm families with more than that limit would be ineligible for any benefits. If they hold less than that, the limit 10% of farm asset value would be imputed as income.

The key role that assets play in determining eligibility and benefit levels in the PBJI may be troublesome for small farmers. First, if an upper limit is set on farm assets, it may make PBJI more restrictive than the programs it replaces, i.e., FS and SSI. Most farmers lack experience or criteria for developing a realistic estimate of the value of their farm real estate holdings. Estimating the value of the farm house and residential lot apart from the remainder of the farm will

house and residential lot apart from the remainder of the farm will be particularly difficult.

Yet reduced welfare benefits or ineligibility may result from errors in judgment or misinformation in the asset valuation process. County Extension faculty have both the expertise and the geographic position to assist if this condition remains in the final welfare legislation.

### **Visibility of Low Income Farmers**

The farm poor are a small subset of the total population of the poor. For example, less than 2% of the recipients of food stamps are self-employed, including farmers. This is not to suggest that self-employed, should be excluded from guaranteed income programs, but instead to reemphasize their minority status and visibility problems. Farmers' unique characteristics in relation to welfare programs may not be fully accounted for initially in planning welfare reform legislation. It will be appropriate for the Extension service, small farm advocates, and spokesmen for small farmers to monitor the progress of welfare reform to determine if proposals are constructed so that low-income farm families will receive the same level of welfare benefits and achieve equivalent levels of living as their equally disadvantaged urban counterparts. Evaluation will also be needed when the proposal is in operation.

We now turn to the Rural Income Maintenance Experiment for insights into how farm families may respond if the proposal is enacted, i.e., the consequences of a guaranteed income on farm family behavior.

### **The Rural Income Maintenance Experiment**

Several major social experiments have been conducted in the last decade, primarily to determine how much less, if any, the poor would work under a universal guaranteed income program. The Rural Income Maintenance Experiment was one of these. Supported by the Ford Foundation, the Office of Economic Opportunity, and the U.S. Department of Health, Education and Welfare, it was carried out through the Institute for Research on Poverty, University of Wisconsin-Madison.

The rural experiment began in late 1969 and ended with a follow-up survey in early 1973. Its primary purpose was to measure the effect of guaranteed income on the work behavior of rural farm and nonfarm families. The experiment staff was multidisciplinary and involved about 50 professional researchers. Research objectives included measuring the effect on children, changes in consumer expenditures, job search and mobility, farm production and financial management, family nutrition, family consolidation and divorce, psychological well-being, and political involvement.

Two counties in Iowa were selected to reflect a relatively affluent area with a poor white minority and one county in North Carolina

was selected for a site with a high incidence of poverty. A sample of families was drawn from both areas and those eligible were randomly assigned to a control group or to experimental groups. There were 809 families selected, and, of these, 220 had farming as a significant economic activity. The households were interviewed quarterly for three years and received benefit checks (if eligible) every two weeks.

It is important that public policy decisions be made using the best information available about problems, options, and expected outcomes. Usually the "best available" data are not the optimal or ideal data set, but decisions must be made and action initiated. In planning the Rural Income Maintenance Experiment, it was known that the knowledge that would be created also would not be the "ideal" set of information. Technically, the findings from the experiment may only be generalized to the geographic areas from which the samples were drawn. But the results of the experiments are by far the best basis available for predicting how rural families would respond to a universal guaranteed income.

The findings are summarized in a publication, "**Rural Income Maintenance Experiment, Summary Report**" published by HEW in November, 1976. The following synopsis attempts only to reflect the gist of what was discovered.

*Work Behavior.* Both the farm operators and their wives in the experimental plans reported more hours worked on the farm than did their counterparts in the control group, and off-farm wage work, particularly wage work of the wives, declined relative to controls. The extra time reported spent on the farm may not have been used productively, however.

Total farm production, gross farm revenues minus operating costs, and technical farm efficiency decreased for the experimentals. Some of the reported increase in farm hours may reflect reporting as "farm work" all the time spent on the farm. The decrease in non-farm work by spouses, particularly in North Carolina, suggests more time available for the homemaker role by the spouse. Changes in farm, nonfarm and total hours worked were minor.

*Farm Product Sales.* The experiment was found to have partially offsetting effects on levels of crop and livestock sales. In Iowa, farmers increased sales of crops, but that was more than offset by decreased sales of livestock. That is, crops that would otherwise have been fed to livestock were instead sold. In North Carolina, farmers decreased sales of tobacco and other crops. These decreases were not offset by the increased sales of livestock, so net farm product sales also decreased.

Aggregate farm production responses to any politically feasible program would probably not affect total U.S.A. farm production levels or food prices to a measurable degree. First, the smaller farmers in the United States account for a very small percentage of total

farm product sales, and second, the reductions in farm production noted in the experiment tended to be small.

*Farm Financial Management.* Among the various loan sources used by farmers, loan companies usually do not provide on-farm supervision or farm management advice with their loans and are often associated with relatively disadvantageous interest rates and repayment schedules. In Iowa, experimentals reported substantial reductions in the amount borrowed from this source during the experiment. In North Carolina there was a 10% increase in experimentals reporting any farm loans while controls remained unchanged. Analyses established that experimentals increased their farm business loans more than controls. Experimentals increased their use of both Farmers Home Administration and loan companies relative to controls.

*Other Responses.* The earned income plus transfers to families in the experimental plans resulted in higher total family income than for controls. How the experimental families used the extra income may be of interest in considering total farm family response to welfare reform.

Among North Carolina families, a study of nutritional adequacy showed experimental families to be in a superior position to controls in both quarters that nutrition was measured. The absence of an effect in Iowa may have been because of a higher initial level of nutrition.

In North Carolina, the probability that a rural nonfarm experimental family would buy a home was higher for experimentals than controls, with no effect noted for farmers. In both states, home purchase came at an earlier age for experimentals than controls.

Little effect was found in the use of medical care or self-evaluated state of health by experimentals or controls. Farm families in the experimental plans spent more for consumer durables than controls, but were not different in regard to amount of consumer debt or open accounts in stores.

Little difference was noted in job change or job search. However, use of the Public Employment Service had a high payoff for those using it. The infrequency of its use indicated that rural people may have had inadequate access to this service.

Rural nonfarm families in the experimental plans were more likely to move to another location than controls. For them, the transfer payment helped cover the costs of moving and provided a cushion against the resulting short-run unemployment. Persons interested in joining the urban to rural migration would thus have a cushion to help support them in their attempt at self-sufficiency under the Administration welfare reform plan.

## Summary

Commodity price support programs increase the income of small farmers in the short run, widen the income gap between them and larger farmers, and are target-inefficient as a program to assist small farmers.

The small farmer provisions of the Agricultural Credit Act of 1978 would (a) significantly reduce interest costs, and (b) permit substantial farm enlargement for recipients. Adverse consequences involve possible inequities in treatment of eligible and ineligible small farmers and increased competition for farm resources.

Intensive on-farm educational programs for small farmers probably result in lasting improvement in technical efficiency, net farm income, and participation in community life.

Welfare reform in the U.S.A. is moving toward a universal guaranteed income-implicit tax policy and an expanded public service jobs program. Low-income farmers may not fare as well as equally disadvantaged urban persons because of (a) the treatment of assets in calculating benefits, (b) the historic low participation rates by rural people, and (c) the historic disproportionate dispersion of public service jobs to urban areas.

Based on experimental evidence, farm family response to a universal guaranteed income-implicit tax program would include modest reductions in labor intensive farm enterprises, reduction in nonfarm work by spouse and head, improved farm credit position, and increased urban to rural migration by persons seeking self-sufficiency.

