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Theme Overview: The 2014 Farm Bill—An Economic Welfare Disaster or Triumph?

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The farm program components of the 2014 Agricultural Act deserve careful, thoughtful, critical assessments with respect to their potential economic benefits and costs, and their overall effects on economic welfare. Too often, perhaps, agricultural economists are accused of focusing only on the effects of farm programs on the farm and closely related sectors. However, any program should be evaluated in terms of its consequences for all of the individuals who are affected by the policies embedded in that program. These impacts are not simply limited to concerns about economic efficiency. As has been the case from the inception of debates over U.S. farm income and price support programs, equity concerns with respect to transfers of income are also important. These are the issues examined by a sequence of six articles in this new *Choices* theme: *The 2014 Farm Bill: An Economic Welfare Disaster or Triumph*?

The articles generally correspond to the major titles in the new farm bill and address price- and income-support programs, subsidized agricultural insurance, conservation programs, international food aid, the effects of domestic- and trade-related agricultural policies on economic efficiency and trade relations, and agricultural research and development policies. (Highlights of the nutrition and other titles were summarized in a related *Choices* theme.) All of the articles, each of which is authored or co-authored by distinguished Fellows of the Agricultural and Applied Economics Association (AAEA), raise substantive concerns about the distributional equity and economic efficiency effects of many of the programs they discuss. In this overview of these analyses, we begin by providing a brief background on the new legislation and evaluating the traditional arguments for farm subsidies that continue to be made by agricultural lobbies and related interest groups. We then provide brief descriptions of the major findings of each of the articles and a short summary of their implications with respect to the economic efficiency and economic welfare effects of the new farm bill programs.

Articles in this Theme:

A Paradox of Plenty: Agricultural Subsidies and the 2014 Farm Bill

After one of the longest Congressional debates ever over agricultural policy, The Agricultural Act of 2014 (P.L. 113-79, HR 113-333) was signed into law by President Obama on February 7, 2014. The omnibus legislation has been hailed by some lawmakers from both parties, especially members of the House and Senate agricultural committees, as a successful example of policy reform and deficit reduction. In his remarks made at the signing of the legislation, President

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Obama paradoxically pointed out that "those at the very top of the economic pyramid are doing better than ever, but the average American's wages, salaries, incomes haven't risen in a very long time…a lot of Americans are working harder and harder just to get by." While the merits of this statement can be debated, it seems rather perverse in light of the fact that some of the wealthiest individuals in the economy are among the major winners of this windfall of subsidies, and the so-called budget deficit reduction aspects of the legislation are for, the most part, achieved through a notional $8.7 billion in cuts to food stamp recipients over a ten year time horizon.

The Congressional Budget Office (CBO) has scored the 10-year cost of the legislation at nearly $1 trillion. However, those cost estimates are based on long-run price projections. If prices fall, as they have recently done, and remain at low levels, the actual cost of the legislation could be far more than what has been projected by CBO. The political dynamics underlying this rare example of bipartisan legislation are showing signs of changing and rhetorical arguments regarding the necessity of subsidies to "save the family farm" are wearing thin. House Republicans attempted bigger farm program spending cuts and proposed separating nutritional assistance from farm subsidies—a change that would make passage of such an immense bundle of subsidies much more difficult.

The conventional wisdom underlying farm subsidies is built on a number of key assertions. Farms are assumed to be at an unfavorable financial position relative to non-farm small businesses. They are asserted to face more financial leverage and a higher probability of bankruptcy than do non-farm businesses. And farm households are often assumed to have less wealth and lower incomes than other households. The standard pro-farm policy rhetoric also typically claims that subsidies are needed to save small family farms. Farm subsidies are also often asserted to be important rural development mechanisms.

The intangible need to use subsidies to "save the family farm" has resonated well with the taxpaying-public and policymakers have appealed to this conventional wisdom to keep farm program subsidies flowing. However, the conventional wisdom is based on a paradigm that is, at best, a relic of history and the assertions that are often put forward to argue for billions of dollars in taxpayer subsidies are false in almost every case.

The fact is that U.S. agriculture is largely comprised of family farms that are made up of households that are far wealthier and that enjoy higher incomes than is the case for the overall non-farm economy. The U.S. Department of Agriculture (USDA) considers 98% of U.S. farms to have "high wealth," which is defined as household wealth greater than the median level for the economy as a whole. Farm households have realized substantially higher median incomes than has the typical U.S. household. In 2012, the USDA estimates that the median farm household realized an income of $68,298, 34% higher than the median total income of $51,017 received by all U.S. households (USDA Economic Research Service, 2014).

Like most small business owners, U.S. farmers depend on borrowed capital. However, the leverage ratio (debts over assets) of farms has fallen to less than 10%, which represents an all-time low. In contrast, the U.S. Department of Commerce (USDC) reported that U.S. households had an average leverage ratio of about 29% in 2010 (USDC, 2012). Between 2010 and 2013, net farm income rose from $78 billion to $130.5 billion. Projections for 2014 indicate a fall in net income to $95.8 billion, a decrease fuelled by lower crop prices, which is still 23% higher than in 2010. The Environmental Working Group (2014) reports that the top 20% of farm payment recipients received 89% of all farm subsidy payments over the period 1995-2012. Over the same period, 25% of all farm program payments went to only 1% of all recipients. Clearly, farm programs work especially well for households at the top of President Obama's economic pyramid.

In addition to the significant cuts to nutritional assistance, the legislation eliminated direct payments, which were made to farms without regard to their current production. Instead, crop insurance subsidies were significantly expanded and farmers are now allowed to choose from a suite of programs that serve to eliminate nearly all of the financial risk from farming. These insurance programs have a rather perverse feature of increasing the revenue guarantee to farmers when times are good. Higher prices yield higher guarantees and a drop in prices such as the one we are currently experiencing may trigger very significant taxpayer outlays.

Despite the rhetoric they use in public, agricultural policymakers and the farm lobbies are clearly well aware of these basic facts. The agricultural lobby is one of the most effective in securing subsidies. Higher cash rents and land values suggest that landowners, many of whom have little direct connection to production agriculture, are significant beneficiaries of subsidy payments. Likewise, the extensive crop insurance industry, which is paid significant subsidies to operate crop insurance programs and afforded risk-sharing terms that one would never find in private insurance lines, also receives a significant share of taxpayer outlays on subsidies. As a concept, insurance sounds like a reasonable approach to providing farmers with a farm safety net. However, with premium subsidies of 65%, the typical farmer receives over $1.90 in payments for each $1 in premiums he or she pays. Add to this the substantial subsidies paid to crop insurance companies to operate the programs and it is easy to see how the CBO baseline score for crop insurance is over $41 billion over the next five years.

The Economic Efficiency and Welfare Effects of the 2014 Farm Bill

The above discussion clearly indicates that the farm program components of the 2014 Farm Bill deserve careful, thoughtful, critical assessments in terms of their potential economic benefits and costs. If the traditional arguments put forward by proponents of income transfers to the farm sector are largely vacuous which, from a factual perspective, certainly appears to be the case, then what economic welfare rationales for those programs do or do not exist? As discussed above, the six articles in this new *Choices* theme, *The 2014 Farm Bill—An Economic Welfare Disaster or Triumph?*, generally correspond to the major titles in the new farm bill. In his article, Professor Bruce Babcock considers the rationale for and the structure of the new subsidy programs introduced in Title I of the farm bill under the guise of farm income safety net programs. He concludes that Becker's hypothesis about the likely structure of programs that benefit the few at the expense of the many applies with respect to the new subsidy programs introduced in the 2014 Agricultural Act. In general, Becker argued, lobbies will seek subsidy programs for the interest groups they represent that tend to minimize adverse economic effects in order to maximize the income transfers while, at the same time, justifying the programs with superficially plausible arguments that often have little basis in fact. He concludes that such seems to be the case for the new quasi-price and -revenue support programs (Price Loss Coverage and Agricultural Risk Coverage) that are tied to a farm's historical production of a crop rather than the farm's current production decisions.

Professor Eric Lichtenberg examines the economic rationales for and the efficiencies of the plenitude of conservation programs authorized under Tittle II of the 2014 Agricultural Act. His careful assessment indicates that, while some of those programs are effective with respect to objectives such as soil conservation and reduced water pollution, many are poorly targeted, tend to be less efficient than they could be, and, in some cases (for example, the Conservation Stewardship Program), appear to provide few or no environmental or other conservation benefits.

Two articles address trade and international aid-related issues. Professors Christopher Barrett and Erin Lentz examine the problems associated with international emergency food aid that derive from cargo preference (requiring that emergency aid be transported on ships flagged in the United States), requiring sourcing of U.S. food aid from the United States instead of locally or regionally relative to the location where the aid is needed, and the monetization of food aid (where some non-government aid agencies sell aid food in markets in or near the country in which they operate and use the funds for other forms of assistance). They conclude that the evidence indicates that the extent to which emergency aid is required to be sourced in the United States rather than locally, monetization of aid is permitted, and cargo preference is required makes the U.S. emergency food aid programs very inefficient, both with respect to the amount of aid that can be provided with the aid budget and the timeliness with which the aid is provided. The cost of these inefficiencies is substantial in human terms: millions of lives that could be saved are not saved. The long-run morbidity consequences of malnutrition for, perhaps especially, children associated with the long delays that result from cargo preference and requiring U.S. sourcing in delivering emergency food aid are also extensive.

Professor Colin Carter investigates the trade policy implications of the 2014 Farm Bill with a particular focus on two aspects of the legislation: the new dairy margin protection program and the deliberate decision of the House and Senate agricultural committees to fail to address the trade relations and World Trade Organization (WTO) violations associated with the livestock-related Country-of-Origin Labeling (COOL) provisions of the 2008 Farm Bill in the new legislation. Both with respect to COOL and the new dairy program, as appears generally to be the case with all of the new subsidy programs, the 2014 Farm Bill appears to pay little attention to current U.S. trade commitments and is likely to adversely affect the ability of the United States to negotiate new trade agreements (such as through the Trans Pacific Partnership initiative) that will create broad-based economic benefits for U.S. consumers, exporters, and the U.S. economy as a whole.

The federal agricultural insurance program has become the elephant in the room with respect to farm subsidy spending, not least because it is politically sellable since it appears to provide subsidies to farmers when they most need them (when yields or incomes are somewhat lower than average). Currently, the program accounts for about 30% of all farm program subsidy spending, an estimated $8 billion a year or more, according to the CBO, and typically exceeds total annual federal spending on all conservation, foreign aid, and public agricultural research and development programs. Professor Brian Wright examines the economic benefits and costs of the federal agricultural insurance program and finds little evidence to suggest that, overall, the program amounts to anything more than an income transfer targeted mainly to wealthier farm operations. At the same time, the program continues to encourage moral hazard behaviors that increase the inherent riskiness of farm operations while transferring most of the financial risks involved in farming to the taxpayers and also having complex spillover effects on the environment.

Finally, professors Philip Pardey, Steven Buccola, and Jason Beddow consider the provisions of the 2014 Agricultural Act with respect to the funding and execution of public research and development programs. They observe that the research title of the 2014 Farm Bill saw a small shift towards redressing a substantial decline in the absolute and relative position of U.S. public agricultural research and development (R&D) evident over the past two decades. The bill included a comparatively modest, but by no means game-changing, increase in nominal funding for agricultural R&D, a continuation of R&D Congressional earmarks, and the establishment of a new Foundation for Food and Agriculture Research (FFAR)—a non-profit corporation seeded with $200 million in one-time startup funds to be matched one-for-one with private funding to conduct research on problems of national and international significance. That, Pardey, Buccola, and Beddow note, is the mildly encouraging good news. The bad news is that the new funding streams are insufficient to redress the chronic market failure and underfunding realities that befall U.S. food and agriculture R&D and are unlikely to reverse the dramatic decline in the United States' share of global public food and agricultural R&D spending, with important adverse consequence for the future productivity of U.S. agriculture. They conclude that failing to sufficiently replenish the stock of public R&D knowledge in the face of ever-evolving pests and diseases, changes in climate, and changes in markets that all act to undermine past R&D-induced productivity gains has profound consequences for the competiveness of U.S. agriculture in the decades ahead.

In summary, from a short-term and longer term economic welfare perspective, the 2014 Agricultural Act generally appears mainly to be focused on transferring income to relatively wealthy farm families as well as some non-farm entities such as the U.S. mercantile marine and private insurance and reinsurance companies. It does so at the expense of consumers and taxpayers, the long-run productivity of the agricultural sector, and efficiently and effectively meeting humanitarian needs through reasonable reforms to international food aid programs. The new farm bill legislation does pay some attention to conservation issues and, relative to recent bills, does not intentionally reduce spending on public research and development programs. However, this *Choices* series of articles, each of which is engaging, provocative, and based on careful scholarship, sends a surprisingly consistent message. Like many of its recent predecessors, and perhaps to an even greater degree, the 2014 Farm Bill does much in the short term to improve farm and landowner incomes and wealth, especially for wealthier households, but does too little to improve agricultural productivity or efficiently address important conservation issues, and is likely to adversely affect the ability of U.S. trade negotiators to obtain new welfare-increasing trade agreements. And the legislation is likely to have such adverse effects for consumers and taxpayers that, in the aggregate, it will almost certainly reduce the economic welfare of the average U.S. citizen.

For More Information

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