

# Agricultural Policy: Objectives for a New Environment

*By Marvin Duncan and Marla Borowski*

After a half century of experience with federal farm legislation, there is increasing evidence that agricultural policies and programs are no longer working well. They also have become unduly costly. Many observers believe U.S. agricultural policy is at a watershed—that the frame of reference in which farmers and agribusinesses operate has changed so dramatically that old prescriptions no longer suffice and new directions are needed.

In 1985, new agricultural legislation will be written and the debate over that legislation has recently begun. There is always considerable confusion and disagreement over what agricultural legislation should contain. Should it be narrowly defined—dealing only with farm problems or more broadly defined—dealing with the problems of the entire food and fiber industry? As yet, the policy objectives of such legislation have not been clearly outlined.

Despite the complexity of the issues

involved, it has never been more important that policy decisions be forward looking and that they be sufficiently broad to encompass food and fiber policy interests, not just narrowly defined farm interests. This article asserts that the changed policymaking environment means traditional objectives must be reexamined and revised before appropriate agricultural programs can be formulated. Without a clear statement of objectives—an understanding of the end product desired—it is unlikely that agricultural legislation will be sufficiently forward looking or comprehensive to meet current and future challenges.

This article reviews the evolution of federal farm legislation and describes changes in agriculture and its linkages to the rest of the economy. It then outlines a number of policy objectives that are important for the environment in which agriculture will operate. Finally, program directions consistent with these policy objectives are suggested.<sup>1</sup>

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<sup>1</sup> Federal dairy and tobacco programs are not included in this discussion. Although these programs are important, a full discussion of them is outside the scope of this article.

## History of farm policies

Agricultural policy objectives have evolved over the past 50 years as conditions in agriculture and the national and international economies have changed. The objectives of higher farm prices, higher farm income, soil conservation, and secure and adequate food supplies have driven U.S. agricultural policy.

The shape of farm policies and programs was determined in the aftermath of World War I and the Depression of the 1930s. After World War I, farmers were faced with falling farm prices, falling land values, a sharp decline in agricultural exports, and an inability to obtain suitable credit. By 1932, farm product prices were less than one-third of their 1919 level, largely the result of export sales that declined to 40 percent of wartime levels. Land values followed farm product prices downward, declining by half. Short-term credit adapted to farm production cycles and fully amortized long-term credit were generally unavailable, exacerbating the sector's cash flow problems.

Although various farm programs were developed and passed by Congress in the 1920s, most were vetoed by Presidents Coolidge and Hoover. A consistent objective of these programs was to raise the prices of farm products above market clearing levels, through a variety of supply-reducing and price-supporting actions. Higher prices for farm products meant increased purchasing power for the farm sector, which accounted for 25 percent of the country's population in 1930. The total rural population, which could also expect to benefit from more money in the hands of farmers, was 44 percent of U.S. population in 1930.

The Agricultural Adjustment Act of 1933 was the nation's first comprehensive farm program and the first major New Deal legislation

directed at agriculture. Its goal was to raise prices by limiting market supplies. Mandatory production controls for basic crops and federal surplus disposal programs were the tools. The Commodity Credit Corporation (CCC)—created that same year by Executive Order—made loans to farmers on their crops. Loan levels were generally set above market rates and loan maturities were set so farmers could hold their crops until prices improved.<sup>2</sup> But the mandatory production controls, an essential part of the program, were declared unconstitutional by the U.S. Supreme Court and discontinued in early 1936.

New legislation passed later in 1936 sought to increase farm income, promote soil conservation and the profitable use of agricultural resources, and ensure adequate supplies for consumers. Payments for soil conservation activities were authorized. Acreage allotments for certain crops were later imposed, along with voluntary acreage set-aside programs to constrain production. These acreage reduction programs were generally not effective. By the end of the decade, the CCC was holding large stocks of major farm commodities.

With the onset of World War II, the thrust of farm programs shifted from restricting supplies to increasing production. CCC loan levels were set high enough to encourage full use of agricultural resources. Food aid to wartime allies markedly increased demand for farm products. When the war ended, legislation extended high CCC loan levels in an effort to avoid repeating the disastrous decline in farm prices and income that followed World War I.

<sup>2</sup> The loan level is the value per unit of product that a farmer receives as a loan from the CCC. For example, if the wheat loan level is \$1.50 a bushel, a farmer can receive a loan of \$900 from the CCC by designating 600 bushels of wheat as loan collateral. At the loan's maturity, a farmer can pay it off along with accrued interest, or under the nonrecourse option, surrender the collateral to the CCC in full settlement of the loan.

Flexibility in setting CCC loan levels was finally authorized following the Korean War, but only after stocks of major crops had grown extremely burdensome.<sup>3</sup>

A series of major policy changes in the 1950s began with the Agricultural Trade and Assistance Act (Public Law 480), enacted to encourage the shipment of surplus commodities in exchange for foreign currency and strategic materials and for purposes of emergency relief. The PL 480 program became a major mechanism for disposing of surpluses and developing markets. It continues so today. To reduce agricultural production, a major multi-year acreage diversion program, the Soil Bank, was enacted. The program, in existence from 1956 to 1975, at its peak removed 58 million acres from production.

Domestic food distribution programs received increased emphasis in the early 1960s. A pilot food stamp program began, the school lunch program was expanded, and international programs were improved.<sup>4</sup> Despite the best efforts of policymakers, agricultural products remained in abundance and farm prices under downward pressure.

A surge in export demand in the early 1970s—fueled by large sales to the USSR—combined with crop shortfalls in major producing countries to cause an abrupt turnaround in the crop supply-demand situation. Surplus stocks were quickly exhausted and crop prices soared. Livestock producers faced much

higher feed costs, and consumers faced sharply higher food prices. But high world crop prices spurred increased production both here and abroad and, by the late 1970s, grain stocks were again becoming burdensome.

A series of measures were enacted in the late 1970s and early 1980s to support farm product prices and income at the higher levels farmers had become accustomed to during the export boom. A target price program was introduced that provided direct subsidies to producers if major crop prices fell below what was deemed a “fair” price. A reserve program insulated large quantities of CCC grain from the market, to be released when market prices rose substantially. This program had perverse impacts—it provided price incentives for farmers to increase production and tended to price their crops out of the market, leaving huge crop surpluses. Government emergency lending programs to farmers added substantially to farm program costs during this period.

As a result of huge crop accumulation and declining export sales, an unprecedented program to reduce the acreage of certain major crops was announced in 1983. The Payment-In-Kind (PIK) program gave CCC crop stocks to farmers as payment for diverting crop land to conserving uses. A total of 77 million acres was idled under PIK and voluntary acreage retirement programs, driving farm program costs to their highest level ever.

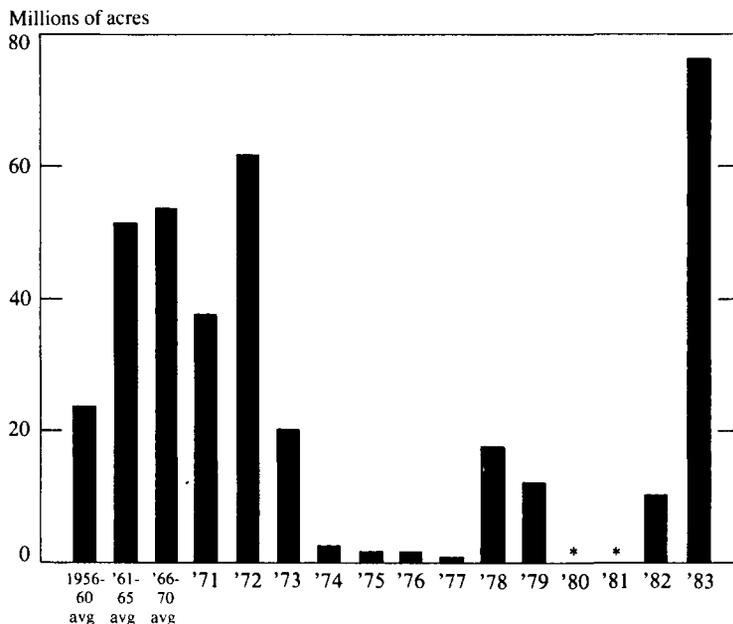
Throughout its history, government policy toward agriculture has been concerned primarily with problems resulting from overproduction. For most of the post-World War II period, government farm programs have idled crop acres to alleviate overproduction (Chart 1). Thus, policy and programs have been directed at limiting what was incorrectly thought to be only temporary excess farm capacity. They also have been directed at lim-

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<sup>3</sup> When flexibility in CCC loan levels was adopted in 1954, U.S. wheat supplies amounted to two years of total domestic and export use. Corn supplies amounted to a year and a half of domestic and export use.

<sup>4</sup> Food distribution programs actually began as part of Roosevelt-era farm legislation. A short-lived food stamp program, the school lunch program, and a milk distribution program were developed. For a fuller discussion, see Murray R. Benedict, *Farm Policies of the United States, 1790-1950*, The Twentieth Century Fund, New York, 1953, ch. 15.

**CHART 1**  
**Acres idled under government programs**



\*No acres were idled under government programs in these years.

Source: Congressional Budget Office.

iting farm income volatility, raising income to levels consistent with the rest of society, and protecting the future productive capacity of U.S. agriculture through soil conservation programs.

Historically, farm policy has been enacted as though the United States was a closed economy. Nevertheless, farmers and the general public were reasonably well served as long as the taxpayer costs of income transfer programs to farmers were not excessive and export markets were relatively unimportant. However, government efforts to insulate farmers from sagging world market demand and falling prices have become extremely expensive in the 1980s.

### **A changing environment**

The number of groups with a special inter-

est in agriculture has proliferated in recent years. New policy participants, such as taxpayer and consumer groups, commodity groups, and agribusinesses, are all becoming more active in the policy process. Moreover, the structure of agriculture has changed, as has its relationship to world markets. Broader economic conditions, as well as conditions within agriculture itself, affect the performance of the sector.

### *Policy participants*

High farm program costs have caused taxpayer groups to question the budget priorities of the U.S. Department of Agriculture (USDA), as well as the efficiency and equity of its farm income support programs. Costs of such programs have soared in recent years, from an average of \$3.5 billion a year in the

1970s to an all-time high of \$20.6 billion in 1983.

Consumer groups have introduced a series of legislative initiatives in recent years, such as food stamps and child nutrition programs, that are concerned primarily with providing adequate food for the disadvantaged. Consumer groups became involved by trying to limit increases in food prices. As they became more knowledgeable, however, they also made their positions known on a broad range of food safety and efficiency issues. Despite farmer concerns about the appropriate role for such groups in developing agricultural policy, taxpayer and consumer groups remain part of the policy process.

Farm commodity groups have changed the way producers interact with policymakers and influence agricultural legislation. In the past, farmers exerted their influence through such general farm organizations as the Grange, the American Farm Bureau Federation, and the National Farmers Union. These organizations, each with a broad based farm constituency but with different approaches to policy, developed comprehensive farm policy and program proposals. There tended to be internal consistency in the proposals. However, the process no longer works that way.

Today, commodity groups as diverse as the American Soybean Association and the Wine Institute develop policy and program proposals of particular benefit to their members. Moreover, as these groups' influence on public policy has increased, the influence of general farm organizations has waned. Agricultural policy and programs that emerge from this process frequently contain internal inconsistencies and contradictions that limit their overall effectiveness and tend to increase their cost. Thus, it is more difficult to produce forward looking legislation. And, in the balancing of conflicts and divergent views, the status

quo tends to predominate.

In the past decade or so, agribusiness has emerged as an even more significant part of the agricultural sector.<sup>5</sup> This is due to the increasing sophistication of technology used in agriculture and the growing specialization in agricultural production and processing. Purchased farm inputs now account for about 55 percent of total inputs into farm production, as compared with only about 44 percent in 1950.<sup>6</sup> As farmers have become more dependent on purchased inputs for agricultural production, a complex input supply system has emerged. On the product side of the farm, processors, transporters, and marketers have grown in number and importance to serve a more geographically dispersed and sophisticated customer base.

Agricultural production accounts directly for 2.4 percent of the nation's nominal GNP and employs 2.7 percent of its labor force. When broadly defined to include agribusiness, however, the agricultural sector is far more important, accounting for 20 percent of the nation's nominal GNP and employing 23 percent of its labor force.<sup>7</sup> Thus, the nation's agribusiness sector is not only important for its ability to support production agriculture, but it also is of major importance in its own right. Agribusiness, dependent on growing farm product markets and a healthy farm economy for its own wellbeing, can be expected to exert an increasing influence in agricultural policy formation.

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<sup>5</sup> Agribusinesses include both firms providing inputs to farmers and firms processing and marketing farm products.

<sup>6</sup> *Crop Price-Support Programs: Policy Options for Contemporary Agriculture*, Congressional Budget Office, February 1984, pp. 11-12.

<sup>7</sup> U.S. Department of Agriculture, *Agricultural Outlook*, January/February 1982, p. 20.

## *Farm structure*

The structure of farming has changed markedly in recent years. It is no longer appropriate to formulate policy and programs to meet the perceived needs of a typical family farm. Farming has become too diverse for that approach to be effective. The idealized family farm, a concept referred to by the press, praised by political leaders, and strongly supported by farmers, rarely exists today due to concentration and specialization in production. Indeed, three different groupings of farms have emerged—each with its own policy needs.

Of the nation's 2.4 million farms, 1.7 million have annual sales of less than \$40,000. These operations are too small to provide an adequate family living. They are usually part-time farmers with income largely from non-farm sources. This group represented 71 percent of all farms in 1982, but produced only 16.6 percent of gross farm returns and overall had losses from farm operations (Table 1). Yet their annual net income per family was only slightly less than \$18,000. Federal farm programs have little effect on these farmers' production decisions and income. Much more important are broader economic policies, infrastructure investment, rural development, and job training.

At the other end of the spectrum are commercial-size farms with annual sales of \$100,000 or more. These 298,000 farms, representing only 12.3 percent of all farms in 1982, produced 64.3 percent of the sector's gross income and earned almost 95 percent of net farm income. Net family income per farm in this group ranged from well above U.S. median family income (\$23,400 in 1982) to nearly \$600,000 for the largest 1 percent of farms. Generally, this group of farms has more than achieved income equity with other Americans, but they have problems with

income instability—a matter of growing concern for agricultural policymakers.

Somewhat fewer than 400,000 farms fell into the \$40,000 to \$99,999 sales class in 1982. These farms accounted for 16.4 percent of all farms and 19.1 percent of the gross income of the sector, but they earned only 9.1 percent of net farm income and had net family income per farm of \$16,200, well below the median family income. In many respects, these farms are in transition. To provide an adequate income, the farms will either grow larger or be operated part time. Those who operate these farms appear to have more income problems than other farmers and share the income instability problem with larger farms.

A single policy prescription will not meet the legitimate needs of all farmers. Indeed, size is not the only differentiating characteristic. Different types of farmers have different policy needs. Livestock producers want ready supplies of feedstuffs at low and stable prices. Crop producers want the opportunity for upward escalation in crop prices. Producers for domestic markets want product prices that reflect U.S. price levels; producers for export markets are more concerned about world market competitiveness. Thus, it will not be easy to develop policy objectives and programs that reflect the differing needs within the farm sector, as well as the legitimate interests of non-farm groups.

## *World marketplace*

Agricultural policy is further complicated by the world market in which U.S. farmers compete. Competition has increased sharply in recent years as a number of countries that previously imported food have become major food exporters. For example, Argentina, Brazil, and the European Economic Community

**TABLE 1**  
**Farm characteristics by sales class**

	Thousands of farms	Gross farm income* (billions of dollars)	Net farm income* (billions of dollars)	Net family income per farm (dollars)	Net worth per farm† (dollars)
Farms with annual sales of:					
\$500,000 and above	25	45.6	14.3	597,900	2,650,300
\$200,000 - 499,999	87	29.5	4.7	67,200	1,274,900
\$100,000 - 199,999	186	30.4	3.7	30,900	821,500
\$100,000 and above	298	105.5	22.7	89,100	1,107,300
\$40,000 - 99,999	393	31.3	2.2	16,200	482,400
\$20,000 - 39,999	273	10.5	0.1	13,400	290,500
\$10,000 - 19,999	281	6.0	-0.2	16,500	176,500
\$5,000 - 9,999	331	4.4	-0.3	18,300	116,800
Less than \$5,000	824	6.3	-0.5	19,500	70,000
Less than \$39,999	1,709	27.2	-0.9	17,800	131,800
All farms	2,400	164.0	23.9	26,400	310,300

\*Before inventory adjustment.  
†As of January 1, 1983.  
Source: U.S. Department of Agriculture, *Economic Indicators of the Farm Sector, 1982*.

all now compete head to head with U.S. farmers in world feed grain, oilseed, and wheat markets and will do so for the foreseeable future.

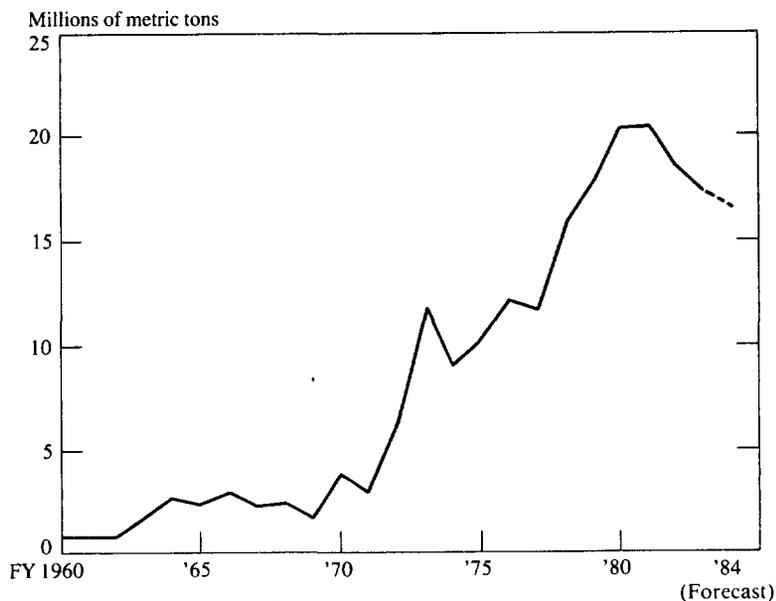
Export markets have become increasingly important to U.S. farmers as output has increased due to productivity gains and additional resources being brought into the sector. Total factor productivity in U.S. farming has grown at an annual rate of 1.75 percent over the post-World War II period.<sup>8</sup> Agricultural economists foresee no slower rates of productivity growth over the rest of this century—and perhaps more rapid rates. Additionally, a great

deal of new capital investment has occurred as farmers added equipment and farming practices embodying new technology. At the same time, the domestic market for farm products has become increasingly mature. Changing lifestyles, an aging population, and slowing population growth rates all point to slower growth in demand for food.

Exported crop production has increased from about 15 percent of harvested acres in 1950 to 32 percent in 1982. Export sales grew rapidly in the 1970s to meet the demands of a growing world market. For a number of major crops, the U.S. share of world trade also has grown. Unfortunately, tonnage of U.S. agricultural exports has been declining since fiscal 1980 (Chart 2), and the U.S. market share for major grain crops has declined from the

<sup>8</sup> V. Eldon Ball, "Measuring Agricultural Productivity, A New Look," Economic Research Service, U.S. Department of Agriculture, May 1984, pp. 15-19.

## CHART 2 U.S. agricultural exports



heights reached in marketing year 1979. Exports, according to the USDA, now appear likely to grow at a rate of about 3 to 3.5 percent a year for the next four years, compared with 8 percent in the 1970s and 2.5 to 3 percent in the 1950s.<sup>9</sup> U.S. market share, while lower than it was during the 1970s, seems likely to remain relatively favorable.

These developments all highlight the increasing importance of exports in policy deliberations. A return to growing U.S. export tonnage is important if the nation's farm sector and its agribusiness sector are to prosper in the years ahead.

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<sup>9</sup> Private discussion with Patrick O'Brien, Economic Research Service, U.S. Department of Agriculture.

### *Broader economic policies*

Agriculture's strengthening linkages to the U.S. economy and to international markets mean broader economic policies are more important to the nation's farmers and agribusinesses than ever before. Monetary and fiscal policies may be more important in determining the U.S. agricultural sector's domestic performance and international competitiveness than narrowly defined farm policies.

Macroeconomic policies determine the frame of reference in which business activity occurs. These policies constrain or promote domestic economic growth, affecting demand at home for agricultural products. These policies also affect price stability and, as a result, the rate of change in agricultural production

and marketing costs. Monetary and fiscal policies interact to determine the cost of carrying debt, to help determine the value of the dollar in foreign exchange markets, and to influence the terms of international trade. The large current federal budget deficits, and concern in financial markets over future financing of deficits, have served to hold up both interest rates and the trade weighted value of the dollar. That, in turn, has added to the cost of carrying the \$215 billion of farm sector debt. The competitiveness of U.S. farm products in international markets has been impaired, as well.

Tax policies are particularly important to agriculture, which is both highly capital-intensive and an industry where investments are locked in place for long periods. Cash accounting, instead of accrual accounting, accelerated depreciation, tax credits, opportunities to convert ordinary income to capital gains for tax purposes, and inheritance tax laws are all immensely important in guiding agricultural investment and management decisions. Relatively favorable tax treatment for profits from agriculture has encouraged capital investment in the sector and added to excess capacity.

Because of the wide-ranging effects macroeconomic policies have on agriculture, it is highly important that these policies be appropriate. It is unlikely that specially targeted farm programs can overcome the adverse effects of unbalanced or unwise macroeconomic policy.

### *Economic conditions in agriculture*

The economic health of the agricultural sector will undoubtedly complicate agricultural policymaking. Since passage of the 1981 agricultural legislation, the sector has been continuously buffeted by both cyclical and secular forces. Agriculture has suffered from the

recent worldwide recession, which has adversely affected demand for farm products. Agriculture has recovered later and more slowly than the U.S. economy as a whole. It also has had to undergo the economic adjustments accompanying the downside of the 1970s export boom. As a result, farm export performance has been disappointing and farm asset values continue under downward pressure.

Secular changes are occurring as well. Continued productivity gains from technological innovation in agriculture mean growing capacity for the industry. Those innovations are fungible and quickly adopted by competitors overseas. U.S. agriculture also has a growing dependence on foreign markets, and is in the midst of adjustment to competition in worldwide food and fiber markets. That process has brought adjustments and uncertainties to the sector.

It now seems likely that new agricultural legislation will be written while the sector is plagued by excess capacity, weak crop prices, disappointing demand for farm exports, farm income pressures, and significant farm financial stress. Such an environment could bias Congress toward short-term, quick-fix farm policy decisions that prop up farm product prices and impede adjustment to market realities. A more forward looking approach to new agricultural legislation is needed—one responsive to changing conditions.<sup>10</sup>

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<sup>10</sup> Some voices, primarily from outside agriculture, assert the sector should stand on its own with no government assistance or intervention, succeeding or failing on its own merits. Those preferring this approach think agriculture is nearly alone in receiving government assistance and that agriculture, having become just like any other business, should be treated as such. However, there are myriad government programs providing assistance and protection to nonfarm sectors.

## Policy objectives

As a first step in developing agricultural legislation, it is useful to identify a few policy objectives as guideposts. To do so is both more difficult and more important than it may seem at first. Setting objectives is difficult, because it requires decisions about the kind of agriculture the country should develop and an understanding of the forces shaping agriculture. Policy had specific objectives when the first federal farm legislation was developed, but some of these objectives have become less relevant in recent years. Thus, new objectives are needed, even as traditional ones continue to be important. Clearly defined objectives are important, because without them programs tend to lose direction and eventually work at cross purposes. Some of agriculture's current problems likely result from programs driving policy, rather than policy defining programs.

### *Objectives of continuing importance*

Some objectives continue to be important to agricultural policymakers. These include an ensured food supply at reasonable cost, continued productive capacity of U.S. agriculture, income equity, and limiting federal budget exposure.

*A safe and adequate supply of food.* Ensuring a safe and adequate supply of reasonably

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Farming has become much more like other American business endeavors. Farmers rely more heavily on purchased inputs and participate in a more complex product marketing system. Nevertheless, farmers remain tied to biological production cycles and the mercy of weather. Capital investment in agriculture may be more fixed than in many other businesses. Finally, with greater dependence by farmers on export markets, government economic and foreign policies are becoming more—not less—important to them. Thus, those calling for no government involvement in agriculture probably are not realistic. The federal government will continue to be involved in agricultural policy and programs in some form.

priced food for U.S. consumers remains an important policy objective. While farmers may question whether reasonable prices are “fair prices,” they nonetheless understand this objective. For more than a century, Congress has funded research—and more recently regulatory programs—to ensure food safety and promote a series of technological breakthroughs that has enhanced agricultural productivity. Partly because of this public investment, U.S. consumers spend less of their income for food (16 percent) than people anywhere else in the world.<sup>11</sup>

The federal government also provides food aid to economically disadvantaged Americans.<sup>12</sup> In fiscal 1985, an estimated 20 million people will receive food stamps. An estimated \$11.6 billion will be spent on this program, along with another \$5.5 billion for child nutrition and other food programs.

*Program costs.* Limiting farm program budget exposure, while not a new objective, has recently become much more important. Budget outlays for agriculture have escalated sharply since 1980 (Chart 3). But because of historically large federal budget deficits, agricultural program budgets now seem likely to be reduced. This is not necessarily bad. Budget constraints force a reevaluation of current and prospective programs. That reevaluation could result in reduced support for annual acreage retirement and income transfer aspects of farm programs and more emphasis on market development and economic adjustment.

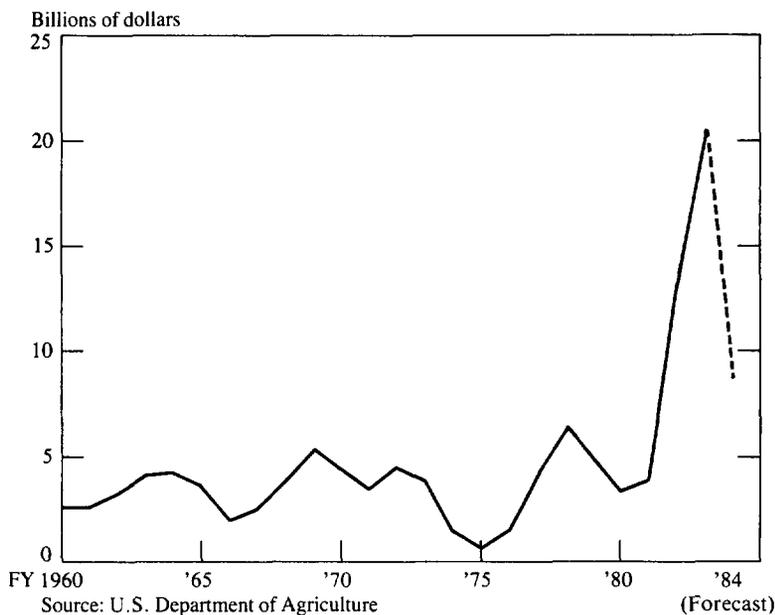
*Productive capacity of agriculture.* Another objective of agricultural policy is to ensure continued productive capacity, an objective

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<sup>11</sup> U.S. Department of Agriculture, *National Food Review*, Winter 1984, p. 32.

<sup>12</sup> *The United States Budget in Brief*, FY 1985, Office of Management and Budget, Washington, February 1, 1984, p. 53.

**CHART 3**  
**Government expenditures**  
**for farm income stabilization**



supported by both farmers and nonfarmers. It implies long-term programs for soil conservation and land reclamation. It also may imply public funding to remove some of the nation's more fragile crop land from production, returning it to a conservation use. While the general public will likely continue supporting conservation practices with cost-share funding, they may increasingly insist that the practices be more permanent, that farmers bear more of the cost, and that there be some recapture of public investment if the conservation practices are discontinued. Farmers and other users might also be asked to share in the cost of reclamation and irrigation projects—perhaps up front.

This objective also implies continued public support for agricultural research. Agriculture has become a major high technology industry

that depends heavily on advances in biochemistry, genetics, plant and animal nutrition, mechanical engineering, processing technologies, and information transfer and processing. To maintain a competitive edge, even more rapid development and adoption of new technologies will be required. Consequently, increased public investment in basic agricultural research and technology transfer to producers and agribusiness is warranted.

*Income equity.* The objective of income equity is valid for the agricultural sector only under a markedly constrained definition. Commercial farmers and most part-time farmers have largely achieved income equity with other Americans. It remains a relevant public policy concern for the rural poor and middle-size farmers that are too big to be part-time operators and too small to be full-time com-

mercial farmers.

Perhaps the best way to address rural poverty and most other problems of part-time farmers is by improving the economic performance of the general economy, and through rural development, infrastructure, and job training programs. However, to further an income equity objective, full-time farms in the middle-size sales class may require continuing income support. Since their numbers are limited, that might be provided at a reasonable cost to government. Moreover, small and middle-size farms are probably the most appropriate recipients of Farmers Home Administration (FmHA) credit programs.

Farmers often object to an income equity criterion, preferring to compare current income with that of a previous year of favorable income. But taxpayers have become increasingly dissatisfied that the bulk of income transfers to agriculture go to only a small proportion of farmers—who typically have family incomes well above the U.S. median family income. Thus, where publicly financed income transfer programs are involved, income equity with other Americans may be a more reasonable—and more attainable—policy objective.

### *Objectives of growing importance*

Other policy objectives are of increasing importance if public policy is to promote a strong and growing agricultural sector. These objectives relate to full use of resources, export market growth, sector adjustments, and income instability.

*Full use of resources.* Promoting reasonably full use of the nation's agricultural capacity is one such objective. The United States has been able to seize market opportunities—domestic and export—because of the growth and vigor of its farms and agribusinesses.

Profitable production levels are necessary to retain those characteristics. Particularly in the case of agribusinesses, a lack of profits could cause capacity to wither, limiting the nation's response to new export market opportunities. Reasonably full use of agricultural resources benefits farmers and agribusinessmen and strengthens the whole U.S. economy.

*Growth in export markets.* The objective of export market growth is closely related to full use of resources. Because the domestic economy is relatively mature, growth in exports appears critical to achieving reasonably full use of the nation's agricultural resources. If agricultural output increases an average of 2 percent or more a year—as many suggest it could—increased export market growth will be needed to avoid growing excess capacity.

Fortunately, export market opportunities will arise as world population and income levels increase. As the economies of developing countries grow, they will likely import more of their total consumption of basic food staples. In the mid-1960s, developing countries imported about 1.5 percent of their consumption of total basic food staples.<sup>13</sup> By the 1970s, the proportion had risen to 5 percent. Extrapolating that trend could mean as much as 8.5 percent of their consumption imported by the year 2000, representing net imports of about 80 million tons of basic food staples. Market opportunities could be particularly bright in the emerging middle-income countries of Southeast Asia and Central and South America.

Expansion of agricultural export markets provides the United States with potential growth in both farm and nonfarm employ-

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<sup>13</sup> Remarks by Dr. John Mellor, director of the International Food Policy Research Institute, Washington, before the spring meeting of the Food and Agriculture Committee of the National Planning Association, April 3, 1984.

ment. For example, USDA estimates that each billion dollars of export sales creates 33,000 U.S. jobs, 54 percent of them off the farm.<sup>14</sup> That same amount of exports adds about \$1.2 billion to total U.S. income. Moreover, export sales are an important source of foreign exchange. Farm exports are expected to total \$38 billion this fiscal year (Chart 4). That will be 18 percent of all U.S. export earnings, a matter of no small consequence in an era of historically high trade deficits. Programs to achieve export growth need to focus on international economic development, market development, value-added exports, trade financing, and—importantly—price competitiveness for U.S. agricultural products.<sup>15</sup>

*Structural adjustment.* A necessary objective for farm policy is to facilitate the adjustment of agriculture to changing technology, economic conditions, and markets. The competitive structure of agriculture, coupled with a steady infusion of new cost-reducing and output-increasing technology, has meant that agriculture is among the U.S. economy's most dynamic sectors. Previous policies have too often impeded sector adjustments. Policies that stand in the way of orderly adjustment have been costly and ineffective for taxpayers—and ultimately for farmers.

Technological innovation and competition in the world market can be expected to change the agricultural sector greatly in the years ahead. Structural changes that led to increased farm size have already made the “family farm” ideal held by most Americans nearly obsolete. Increasing concentration also is

occurring among firms supplying agricultural inputs and marketing farm products.

The day of easy entry and ready success in full-time commercial farming is probably past. Soon it may no longer be realistic to purchase and pay for a farm in a lifetime. Commercial farming has become big business—albeit still firmly in the hands of families, often more than one generation—and is rapidly becoming even bigger. Dealing with such a dynamic industry suggests the need for greater reliance on market forces to allocate resources and reward success in commercial agriculture.

*Instability.* Assistance in managing instability in agriculture is an objective of growing importance. The problem affects all U.S. business, especially firms dependent on export markets. As farmers depend more on purchased inputs and export markets, changes in market supply and demand have greater financial impact and can occur more often. Managing instability is a major problem for commercial farms—and, to less extent, for middle-size farms. Market instability also has a major effect on agribusiness, disrupting expected demand for farm inputs and causing abrupt changes in the volume of products processed, transported, and marketed.

Development of risk management opportunities—such as revenue or production insurance, or the use of commodity futures and options contracts—might offer some long-term solutions to instability. A strategic grain reserve of limited size could also improve stability. Recent history indicates, however, how difficult it is to resist using a grain reserve as an income support device. A well designed and administered multi-year land retirement program that removes land from production in years of excess supply and returns it in periods of supply shortfalls—an elastic crop land base—could also add stability.

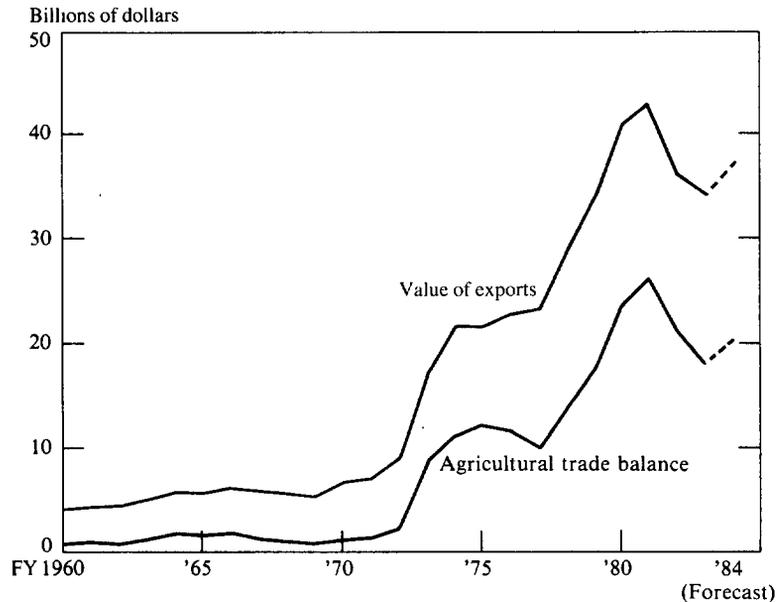
Policy and programs to help manage insta-

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<sup>14</sup> Gerald Schuller, “Impact of U.S. Agricultural Trade,” *National Food Review*, Fall 1983, p. 2

<sup>15</sup> Value added exports of agricultural products are those to which processing has added value beyond that of the raw agricultural product. Examples are flour exports instead of wheat and meat products instead of livestock and feed grain.

**CHART 4**  
**U.S. agricultural trade**



Source: U.S. Department of Agriculture.

bility must distinguish between cyclical instability and secular change. While it may be desirable to help the agricultural sector manage cyclical instability, it would be equally undesirable to prevent secular adjustment. To do so would be inordinately expensive for taxpayers, damage the competitive position of U.S. agriculture, and ultimately result in greater adjustment costs for farmers and agribusinesses. Assisting in an orderly adjustment may be the most that public policy should undertake.

The policy objectives presented here are not an exhaustive set. However, these objectives are important as policymakers deliberate new agricultural legislation. Moreover, these objectives point to a change in direction for legislation. The new legislation must recog-

nize the impact of rapidly evolving technology, the changing structure of farming and agribusiness, increased farm linkages with agribusiness and the rest of the U.S. economy, and the importance of world markets.

Even then, not all policy objectives will be fully achieved. Instead, priorities and weights for the various policy objectives will be determined through the political process. Nonetheless, if legislation aims at achieving the objectives discussed, emphasis will shift from income transfer and price support programs to market development, limited adjustment assistance, and greater market orientation.

**Program directions**

Although it is beyond the scope of this

article to lay out a comprehensive and consistent set of farm programs, the policy objectives discussed imply some broad program directions. It is important that federal agricultural programs not work at cross purposes and that they move to achieve the policy objectives previously discussed. These criteria suggest the following program directions.

#### *For objectives of continuing importance*

Some type of income support for farmers, such as the target price program, appears likely to continue for a long time. However, if funding is to be available for more productive activities, such as market development, income support programs should be carefully targeted to farmers in need of assistance. Moreover, where income support is deemed necessary, direct payments to farmers may be the most cost-effective way to deliver that support. For both equity and efficiency reasons, an upper limit on the amount of government subsidies paid to any one farmer is needed. Currently, that limit is \$55,000 a year.

A strategic reserve of major storable crops is likely to be part of any agricultural legislation. Both export customers and U.S. consumers want assurance of continued supply and some limited protection against food price shocks. A Farmer-Owned Reserve program of limited size and with realistic entry and removal prices would meet those needs.<sup>16</sup>

U.S. farmers increased harvested crop acreage from 290 million acres in the late 1960s to 365 million in 1982. That increase contributes to excess production. Moreover, some of it is

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<sup>16</sup> Under the Farmer-Owned Reserve program, a farmer commits grain under CCC loan for a specific number of years. The grain can be released early if the farmer repays the loan plus a penalty payment or if market prices rise to a specified level, in which case no penalty payment is required.

erosion prone and not well suited to intensive crop production. Thus, it seems appropriate to retire as much as 30 million acres of such crop land to conserving uses for a multi-year period. Such a program also would provide an elastic crop land base that adjusts to market demand and would help avoid abrupt, large, and disruptive one-year acreage adjustment programs. Annual acreage adjustment programs of limited size appear likely to continue. Finally, it is unwise, in a time of excess production capacity, to provide subsidies—perhaps even CCC commodity loans—to producers converting range or forest land to crop land.

Competitive pressures in world agriculture highlight the need for continued technological innovation to lower production costs and increase output. Strong government support of basic agricultural research is needed to help ensure continued success for agriculture.

#### *For objectives of growing importance*

Several major agricultural products have not been competitively priced recently, perhaps as a result of arbitrarily determined CCC commodity loan levels. Yet price competitiveness is increasingly important in international markets. To regain a competitive edge, loan levels for major export crops should be set at or below world market clearing prices and adjusted annually on the basis of a multi-year moving average of such prices. Care must be taken to avoid creating artificial differences in relative crop prices.

Changes in CCC commodity loan programs that would redistribute program benefits have been suggested. One alternative is to make every producer of a CCC commodity eligible for CCC loans, regardless of whether a producer conforms to the current farm program. Such a change would require that CCC loan levels be low enough to avoid borrower

defaults and stocks buildup. It might also require the use of recourse rather than nonrecourse loans. Another suggestion is to vary CCC loan levels to direct greater support to small and middle-size farms. These changes, however, would be controversial.

Given the importance of export markets, a much higher priority should be given to long-term market development programs. More creative financing and marketing arrangements should be developed to assist export customers in purchasing U.S. farm products. Such programs could include intermediate and long-term credit arrangements by the CCC or the Export-Import Bank, along with longer term food aid commitments, programs for infrastructure development in customer countries, and greater use of counter trade. In particular, international economic development programs could be important long-range market development mechanisms in the future, as they were in the past.

The success of agricultural export market development will be affected by a number of factors. The broader economic policies and international relationships of the United States must be conducive to trade growth. Also, the United States needs to be viewed as a reliable supplier. The current spread of trade protectionism needs to be reversed—a need that implies the United States may also have to lower its own import barriers for some products. Successful export market development will entail broad ranging, long-term commitments by both government and private firms.

Farmers likely will continue to call for federal programs to protect them against natural and market instability. Special attention should be given to improving the Federal Crop Insurance Program, implementing commodity options contracts, and developing revenue insurance programs that make use of futures and options markets. Emphasis on private sec-

tor development of such insurance or futures markets programs seems important to their political acceptability and their ultimate success. Public subsidies associated with these programs should be both limited and directed to farmers with the greatest need.

USDA farm credit programs remain popular among farmers. However, a tight rein on credit programs will be necessary. Some of those, such as the Economic Emergency Program, have poor track records. Administration of agricultural lending programs, other than CCC loans, should remain in the FmHA. It seems reasonable to target FmHA lending toward low-income farmers and new entrants into farming. Increased emphasis on loan guarantee arrangements with commercial lenders, rather than direct loans, would likely improve FmHA program performance.

To better achieve the objectives identified, the Secretary of Agriculture should be given more flexibility in administering programs. Although agriculture is a dynamic industry and becoming even more so, in recent years Congress has chosen to write much administrative detail into agricultural legislation, limiting the Secretary's response to changing conditions.

## **Conclusion**

Current federal farm programs were initiated a half century ago out of the problems associated with the aftermath of World War I and the Great Depression. While the programs have changed, they have largely remained rooted in the agriculture of the past. They do not deal effectively with the problems facing today's agriculture and likely will do even less well for tomorrow's agriculture.

Groups with a legitimate interest in agricultural policy are larger in number and have more diverse needs than before. No longer is

Congress dealing only with farm policy. More appropriately, it is food and fiber policy—agricultural policy in the broadest sense. But before Congress can design specific agricultural programs, it must identify the policy objectives these programs aim to achieve.

Policy objectives and programs must reflect agriculture's growing complexity and diversity. More attention should be given policies and programs that further export market growth, efficient and reasonably full use of agricultural resources, adjustment to change, and management of instability.

In the dynamic environment likely to characterize agriculture, increased reliance on market forces is appropriate. Moreover, greater discretionary authority in the administration of federal agricultural programs is preferable to more rigid prescriptions.