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FAPRI Examination of Farm Bill Alternatives

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FAPRI EXAMINATION OF FARM BILL ALTERNATIVES

During 1995, the U.S. 104th Congress will evaluate the food and agricultural policy situation and consider alternative legislation. This periodic review and resulting omnibus legislation, commonly called the Farm Bill, provides the opportunity to carefully reexamine agricultural programs and policies. The programs being reviewed, some of which expire in 1995, deal with, among other things, price and income support, trade, conservation, research, domestic food assistance, credit, crop insurance, and rural development. Without a 1995 Farm Bill, permanent statutes incompatible with current national economic objectives, global trading rules, and federal budget or regulatory policies would take effect (Congressional Research Service Farm Bill Report). As of this writing, there is general agreement on only one item of the 1995 Farm Bill discussions—that the final result will differ from its predecessors.

To aid legislative deliberations, the Food and Agricultural Policy Research Institute (FAPRI)* researchers at Iowa State University and the University of Missouri-Columbia have analyzed three program alternatives. The three alternative analyses requested by Congress represent “corner” scenarios because their program emphasis is based on a different set of philosophies regarding current farm problems, the future of production agriculture in the United States, and the evolution of its rural communities.

The scenarios that were evaluated represent three discrete directions for policy change and emphasis in 1995:

1. No Program. This alternative eliminates the existing structure of target prices, deficiency payments, loan rates, export enhancement, and dairy price supports, as well as many specialty programs such as for cottonseed oil and sunflower. It also eliminates Acreage Reduction Programs (ARP) and the 0/50-85-92 programs.

2. Marketing Loan Program. Under this option, target prices, loan rates, ARPs, and 0/50-85-92 would disappear and be replaced by a system of recourse marketing loans, with loan rates set in proportion to each other. Soybeans would be added to the commodity programs. Export enhancement is eliminated, but dairy and other specialty programs are retained.

3. Revenue Assurance. This alternative would do away with target prices, marketing loans, ARPs, and 0/50-85-92. Instead, producers would be ensured of receiving 70 percent of revenue, based on a five-year moving average of county price times a producer's five-year average yield. In addition, transition payments would start at 80 percent of historic deficiency payments in 1996 and decline to zero percent by the

* FAPRI is a dual university institute operated by the Center for Agricultural and Rural Development at Iowa State University and the Center for National Food and Agricultural Policy at the University of Missouri-Columbia.

year 2000. Export enhancement, dairy, and other specialty programs are retained.

In all scenarios, the Conservation Reserve Program is assumed to decline to the 17-million-acre level projected by the Congressional Budget Office, while none of the scenarios incorporates annual ARPs.

Across the scenarios, the safety net configuration, especially income enhancement and risk sharing, shows considerable variation. Other than crop insurance, the safety net is completely gone in the no-program scenario. The marketing loan option provides some reduction of price risk, and enhancement of income, but has basically the same budget outlays as current programs. Revenue assurance offers significant reduction of cash flow risk for producers and provides substantial budgetary savings, but reduces the level of government support for producers by eliminating the direct income transfer aspect of current programs (i.e., deficiency and loan deficiency payments would be eliminated).

Comparison of Results: Key Aggregates

When compared with the 1995 FAPRI baseline, the estimated effects on selected variables, as illustrated in Table 1, show significant early variation across the alternatives. The effects also show that farm income generally tends to converge toward the end of the period. The reader should note that the farm income numbers in the various scenarios do not include any estimated crop insurance or revenue assurance indemnities, nor do they reflect any other risk reduction benefits that

producers would receive. Thus, our results would tend to underestimate the benefits to producers from increased insurance payments and reduction of cash flow risk. A briefing paper to be published after this one explains the process of estimating these non-monetary benefits.

Important average annual estimated impacts for the years 1996 to 2000 and for the final year of the projection period are listed in Table 1.

With the marketing loan program, plantings would increase by about 2 million acres annually; however, crop receipts decline by roughly \$2 billion per year. The decline in crop receipts in the early years is offset by higher government payments; but by the year 2004, government payments also decline slightly. From the point of view of government program efficiency, the analysis indicates that net CCC outlays are virtually unchanged over the full period, while net farm income declines by \$2 billion per year. This implies that, when compared with the baseline continuation of current programs, this alternative is less efficient because it costs the same to operate but results in less income to producers.

For revenue assurance, area planted and crop cash receipts average very close to baseline levels over the full projection period while net CCC outlays decrease by approximately \$4.5 billion annually. The loss of government payments is offset in the early years by the decoupled transition payments provision. Due to increased market orientation, the reduction in government payments does not fully affect

Table 1. Estimated effects on selected variables

Area planted to 8 major crops: corn, sorghum, barley, oats, soybeans, wheat, cotton, rice

| | Crop Years | |
|-------------------|-------------------------|-------------------------|
| | 1996/97-2000/01 | 2003/04 |
| Baseline Value | 254 million acres | 263.3 million acres |
| Marketing Loan | Up 2.92 million acres | Up 1.20 million acres |
| Revenue Assurance | Down 1.38 million acres | Down 0.10 million acres |
| No Program | Down 4.98 million acres | Down 4.80 million acres |

Crop Receipts

| | Calendar Years | |
|-------------------|----------------------|----------------------|
| | 1996-2000 | 2004 |
| Baseline Value | \$ 93.25 billion | \$ 107.2 billion |
| Marketing Loan | Down \$ 1.73 billion | Down \$ 2.85 billion |
| Revenue Assurance | Down \$ 0.57 billion | Down \$ 0.42 billion |
| No Program | Down \$ 1.48 billion | Down \$ 2.20 billion |

Government Payments

| | Calendar Years | |
|-------------------|----------------------|----------------------|
| | 1996-2000 | 2004 |
| Baseline Value | \$ 8.03 billion | \$ 4.86 billion |
| Marketing Loan | Up \$ 1.79 billion | Down \$ 0.17 billion |
| Revenue Assurance | Down \$ 3.58 billion | Down \$ 3.75 billion |
| No Program | Down \$ 6.10 billion | Down \$ 3.75 billion |

Net Farm Income

| | Calendar Years | |
|-------------------|----------------------|----------------------|
| | 1996-2000 | 2004 |
| Baseline Value | \$ 43.48 billion | \$ 52.45 billion |
| Marketing Loan | Down \$ 1.16 billion | Down \$ 2.97 billion |
| Revenue Assurance | Down \$ 2.87 billion | Down \$ 2.55 billion |
| No Program | Down \$ 6.89 billion | Down \$ 4.05 billion |

Estimated Insurance Indemnities (Estimated as 80 percent of total crop insurance indemnities)

| | Fiscal Years | |
|-------------------|-------------------|-------------------|
| | 1996-2000 | 2004 |
| Baseline Value | \$ 1.06 billion | \$ 1.05 billion |
| Marketing Loan | No Change | No Change |
| Revenue Assurance | Up \$.47 billion | Up \$.65 billion |
| No Program | No Change | No Change |

Net CCC Outlays

| | Fiscal Years | |
|-------------------|----------------------|----------------------|
| | 1996-2000 | 2004 |
| Baseline Value | \$ 8.36 billion | \$ 5.62 billion |
| Marketing Loan | Down \$ 0.59 billion | Up \$ 0.10 billion |
| Revenue Assurance | Down \$ 3.83 billion | Down \$ 4.39 billion |
| No Program | Down \$ 7.54 billion | Down \$ 5.43 billion |

net farm income, since income declines by less than \$3 billion on average. In the final year, among the three options, net farm income is highest for revenue assurance. Thus, an efficiency gain is achieved compared with the other alternatives. This efficiency gain is achieved even without including insurance indemnities benefits.

The no program analysis shows steep declines in area planted, cash receipts, government payments, net farm income, and government expenditures. This plan, like revenue assurance, demonstrates efficiency gains from the market orientation as CCC outlays drop more than the declines in net farm income. However, in this scenario the declines in income are severe enough to warrant real concern about disruption in financial sectors, especially since all safety nets are removed.

A few items included in the forthcoming FAPRI report on policy options for the 1995 Farm Bill—but not listed here—should be discussed briefly. Along with the declines in farm income across all scenarios, land values also show decreases when compared with baseline values. In the final year of the projection period, 2004, all three of the scenarios have nominal land values projected above what they were in 1994, though not as high as they would be with continuation of current programs. The baseline projects a 15 percent increase in average nominal land values from 1994 to 2004 compared with 11.6 percent for the marketing loan option, 8.6 percent for the revenue assurance option, and 5.4 percent for the no program option. However, some

regions would see nominal land values decline from current levels, the most severe declines being under a no program option. The implication is that only with the no program option would financial markets be likely to be severely strained. There would be regional variation with elimination of commodity programs, of course. For instance, rice net returns decline significantly compared with a relatively modest impact on corn net returns. Thus, some regions would find credit markets strained more severely than others.

Conclusions

The three policy options discussed here share one policy continuation (CRP is continued) and one major policy shift (ARPs and 0/50-85-92 programs are eliminated). Also, as crop base restrictions are eliminated, with the exception of the marketing loan option, the market drives production decisions and shifts of acreage between crops. For the marketing loan option, production decisions are driven by the loan rates rather than the market prices. Further, in all scenarios government stockholding is reduced and, for the most part, stocks of most commodities remain low in comparison with historical patterns.

Farm income tends to decline in all of the alternatives and the decline in the no program option is severe enough to generate real concerns about disruption of financial/credit sectors. Land values decline relative to baseline projections, but average nominal land values at the end of the period are higher than 1994 in all

scenarios. It is interesting to note that in the year 2004, even without insurance indemnities or non-monetary risk reduction benefits included in the analysis, net farm income is highest for the revenue assurance alternative. And if increased insurance benefits are added, net farm income plus increased insurance benefits under this plan recover to levels close to the baseline and at a much lower cost to the U. S. government.