U.S. Farm Bill Scenarios and Impact on Developing Countries

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U.S. Ag Policies Can Adversely Affect Developing Countries

- By restricting imports of products in which developing countries have a comparative advantage to encourage larger U.S. domestic production, e.g. sugar, ethanol & citrus.
- By inducing larger production of commodities in which developing countries have a comparative advantage, which, when pushed out into world market, depresses world market prices, from which developing country farmers derive their entire incomes, e.g. cotton & rice. (Requires large market share and price distortions.)

U.S. Ag Policies Can Adversely Affect Developing Countries

- In-kind food aid, especially when it depresses market prices in developing country markets, deprives local farmers of sales and reduces their income earning potential, e.g. monetization of food aid.
- By reducing foreign assistance for agricultural and rural development, retard ag development and rural poverty reduction.
  - 70% of poverty is in rural areas; most of the poor are dependant on farming for meager incomes

OECD Policies Depress Commodity Prices Below Long Term Trend

Rice	33 - 50 %
Sugar	20 – 40 %
Dairy Products	20 – 40 %
Cotton	10 – 20 %
Peanuts	10 – 20 %

Source: World Bank. Global Economic Prospects 2003, Chap. 2.

U.S. Role in World Trade (2002-05)

Commodity	% of World Production	% of World Trade	% of Prodn Exported
Cotton	20	40	70
Corn	40	60	18
Soybeans	38	44	35
Wheat	9	25	50
Rice	2	13	52

Source: Congressional Research Service

U.S. Producer Support, 2000-2004

(% of gross revenue provided by all support)

Sugar	53-62
Milk	38-56
Rice	18-52
Sorghum	30-47
Wheat	22-48
Barley	20-42
Corn	13-34
Soybeans	14-28
Wool and lamb	05-26
Pork, beef and broilers	04-05
Overall	15-24

Source: OECD PSE database

The Current Farm Policy Landscape

- Many farm groups happy with 2002 Farm Bill.
- Rapid growth of ethanol industry with resulting increase in crop prices
  - There's more interest today in ethanol than exports.
  - There's little for corn, soybeans, or wheat in extending 2002 Farm Bill.
- Reduction in CBO's budget baseline for ag commodity programs by more than half!
- Even if Doha Round is dead for next several years, threat of more litigation in WTO
- Unprecedented anti-farm program editorial comment in media across the country
- Numerous groups proposing alternatives to present farm programs, including Bush Admin.

Current Farm Supports Are Seen by Many as Inequitable

- 93% of all support goes to 5 commodities.
- Over 60% of US agriculture receives no support, and this part is not perceptibly less profitable than that which does.
- Southern crops (rice, cotton and sugar cane) receive much more support per acre and per farmer than Northern crops (corn, soybeans and wheat).
- 16% of payments go to rural residence farms.

Farm Programs Not Perceived to be Achieving their Stated Objectives

- Low farm family income
  - Most payments go to larger producers whose family incomes & wealth are well above average
  - Low income farmers receive very little from programs
- Variability of farm income
  - Farmers have income averaging, cash accounting & futures markets
- Increase competitiveness
  - Capitalization of payments into land values raises U.S. cost of production and undercuts international competitiveness
  - Public investments in agricultural research & infrastructure declining

Farm Programs Not Perceived to be Achieving their Stated Objectives

- Food security
  - Not a credible problem when U.S. ag grows 1/3 more than we use domestically; food insecurity is due to lack of income, not prod’n.
- Rural development
  - Payments facilitate consolidation; don’t create more jobs

Two Fundamental Philosophical Questions in Writing 2007 Farm Bill

- Of the Federal dollars allocated to agriculture and rural America, how much should go to farmers as individuals & how much should be invested for the greater good of agriculture and rural America?
- Of the fraction that goes to farmers as individuals, how much should be linked to the production of *specific* commodities & how much should be decoupled from what the farmer produces?

Other Issues in 2007 Farm Bill

- Food safety and bioterrorism
- Conservation: Whither the CSP and CRP?
- Rural development: Acknowledgment that ag commodity programs make weak rural development policy.
- Science: Has the pendulum swung too far in depending on the private sector to do the ag research?
- Food aid: When is it an export subsidy?

Other Issues in 2007 Farm Bill

- Concerns re structure of agriculture, e.g. payment limits
- Further increase in biofuels' role in U.S. energy security
- Move farm support from trade-distorting to non-trade-distorting forms:
  - Gross revenue insurance in place of disaster payments, crop insurance, marketing loans, LDPs, and CCPs.
  - Public goods investments, e.g. rural infrastructure, research, etc.
  - Payments to farmers for providing environmental services

Three Trajectories for Commodity Title of 2007 Farm Bill

- Extension of current programs, with some adjustment of loan rates and target prices
- Radical departure from current instruments and objectives, with elimination or “buy-out” of major support provisions
- Change in emphasis and direction of policy, with commodity programs evolving

Extension of Current Provisions

- Favored by major commodity groups (Cotton, Wheat, Rice, Soybeans)
- Supported by mainstream Farm Organizations
- Agreed by Sub Committee last week
- House Ag Committee may include this in the draft bill

Radical Changes in Programs

- Favored by some Think Tanks (CATO, AEI)
- Promoted by some development agencies as way to reduce impacts on developing countries
- Proposed by academics on grounds of efficiency
- Popular with other governments

Change in Emphasis in Policy

- Promoted by Administration (USDA Proposals)
- Developed by Conservation-oriented groups (AFT, Woods Institute)
- Emphasized by policy groups (Chicago Council on Global Affairs)
- Taken up by several Congressmen and Senators (e.g. FARM 21)
- Corn producers also favor some changes in instrumentalities

Other Factors also Link US Farm Policy with Developing Countries

- WTO
  - Possible changes as a result of Doha Round
  - Resolution of trade disputes
- Regional Trade Agreements
  - Farm Policy major impediment to Bilateral and Regional Trade Agreements
- Energy Policy
  - Concern about fossil fuel dependency leading to demand for biofuels
  - Result has been historically high corn prices

Doha Round Agricultural Agreement: What is on the table?

- Eliminate all forms of ag export subsidies
- Reduce trade-distorting domestic subsidies
- Redefine “blue box”
- Reduce tariffs (highest the most: exceptions allowed if increase tariff-rate quota)
- Unlimited access to high-income country markets for least developed countries, but with exemptions.

WTO as a Link to Farm Bill

- Doha Round (if concluded) would lock in lower levels of spending ($17 billion OTDS)
- Developing countries would have some assurance that farm spending on trade distorting support would not go up to the 1986 or 1998 levels (but may not decrease in the short run)

Changes Needed to US Policy under Existing WTO Agreement

- Need to change marketing loan, LDP and CCP provisions for cotton (and for other program crops, e.g. corn & soybeans, or risk losing them in WTO litigation & not getting anything for them)
- The fruit and vegetable production exclusion in qualifying for direct payments needs to be changed to avoid them being counted as amber.
- Any hesitation in conforming could seriously weaken WTO.

New Challenges Likely in WTO

- Canadian case breaks new ground by challenging past notifications
- Other countries could use WTO mechanism to clarify legality of subsidies under SCM
- Litigation could become major way of pressing developed countries to reform
- However, replacement of negotiation by litigation could backfire.

RTAs Could Form Another Link

- US could use RTAs as a way of gaining market access not possible in Doha (but TPA?)
- US could lose out if other countries continue to form RTAs: competitors would gain advantage in emerging markets (the only growth markets)
- Pressures on domestic ag support less direct in the case of RTAs.
- When NAFTA is fully implemented on Jan. 1, 2008, Mexico will get free access to US sugar market. US sugar program will have to change

Cotton as a Political Link

- Agreement to expedite reduction of cotton subsidies in Doha Agreement
- Pressure on subsidies likely to continue even without an agreement
- Impact of US policy on West Africa empirically established
- Response will reflect broader foreign policy imperatives

Energy Policy as a Link

- Ethanol industry growing rapidly with large subsidies, mandated use, tax exemptions, and protection from imports from lower-cost suppliers
- Increased industrial demand for corn has resulted in higher prices; exports will inevitably fall, creating opportunities for other suppliers.
- Higher feed grains prices reducing profitability of U.S. livestock and poultry industries, as well as other countries, especially monogastrics.

Growth in Ethanol Industry

- 2000: 1.6 billion gallons of ethanol produced; used 6% of U.S. corn harvest
- 2006: 5 billion gal.; used 20% of corn harvest
- Now 110 ethanol plants are operating w/total capacity of 5.4 billion gal.; 73 more are under construction plus 8 more expanding
- This will bring capacity to 11.4 billion gal. by 2008-09
  - Energy Bill of 2005 mandated 7.5 billion gal. of biofuels by 2012

Energy Policy

- Could be some time before we have technology for producing ethanol from cellulosic feedstocks.
- Farmers and politicians are more enamored with growth in ethanol and other biofuels than with exports and WTO trade negotiations.

U.S. Ethanol Subsidies May Help Developing Countries

- Ethanol program causes drop in U.S. ag exports, creating export opportunities for developing countries.
- The associated higher world grain and oilseeds prices increase earning potential of developing country farmers, but hurt low income consumers who spend the largest fraction of their incomes on food.
- Higher ag commodity prices should make it easier to bring Doha Round to closure.

Closing Observations

- A lot of new voices will be part of farm bill debate, but the ag organizations will dominate.
- The agriculture committees of Congress are most likely to draft farm bills similar to those in the 2002 Farm Bill, with some tinkering with target price levels and more money in conservation payments.
- The House of Representatives has so few members with rural interests that radical change could occur when the bill comes to the floor of the House for action. This creates the possibility for more fundamental change.

Closing Observations

- However, continuation of current U.S. ag legislation will have less effect during high price period.
- A key impact would be on the perception that the U.S. has abdicated leadership in trade liberalization for agricultural goods.
- Reaction of large emerging countries could be to shelter further their own agricultural sectors and reverse the reform trend of the 1980s and 1990s.