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THE WHEAT POLL DO WHEAT PRODUCERS FAVOR MANDATORY LIMITS ON PRODUCTION?

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Wheat producers in the U.S. will soon receive a ballot from USDA asking a question similar to that posed in the title of this article. The poll is being conducted as one of the requirements of the Food Security Act of 1985 (farm bill). The outcome of the poll, however, does not bind the Secretary of Agriculture to establish mandatory controls.

The 1985 farm bill states, "Not later than July 1, 1986, the Secretary of Agriculture shall conduct a poll, by mail ballot, of eligible producers of wheat to determine whether such producers favor the imposition of mandatory limits on the production of wheat that will result in wheat prices that are not lower than 125% of the cost of production (excluding land and residual returns to management) as determined by the Secretary." Only those producers who have grown wheat in at least one crop year from 1981-1985 on a farm with a wheat base of at least 40 acres will be eligible to vote.

Although this poll is non-binding, it should not be taken lightly. Its inclusion in the farm bill reflects a growing demand for mandatory production controls by producers in the wheat industry as well as other producer groups frustrated by surplus production and low farm prices. Producers, therefore, must consider the many consequences before answering this simple question.

This article explores the question of mandatory production controls as well as other supply-management alternatives and their consequences for wheat producers. The purpose of this article is to provide wheat producers with information that should be considered in their decision on how to vote. Of course, the discussion in this article focuses on the implications of supply control and does not suggest how a producer should vote in the poll.

Before Making the Decision

Most producers would like to have answers to a number of questions before voting "yes" or "no" on mandatory production controls. Some questions to consider include:

- What does the Secretary of Agriculture consider to be the cost of wheat production?
- What quantities of wheat would be sold if prices were increased to 125% of this cost of production?
- How much will production need to be cut to maintain the price at 125% of the cost of production?
- What mandatory supply-management options are available?
- What are the consequences of continuing with the current farm program?

These are not easy questions to answer. We consider the following analysis reasonable, given available information.

What is the Cost of Producing Wheat?

There probably are as many answers to this question as there are wheat producers. USDA, however, is required by Congress to estimate the cost of producing wheat, feed grains, cotton, and dairy commodities each year. Based on previous USDA cost of production estimates, we estimate

This Economics Newsletter is a reproduction of a report, written by Texas A&M University agricultural economists. The report reviews the potential impacts of imposing mandatory production controls on wheat producers.

A mail ballot asking producers if they favor mandatory production controls will be sent out around the middle of June. This is not the same as the marketing quota referendum which must be completed by August 1, 1986.

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Mandatory Acreage Controls

Mandatory acreage controls or allotments would allow wheat production on a specific number of acres allotted to each farm based on its share of the national allotment necessary to meet the Administration's supply-management objectives. Acreage allotments were used extensively in the 1950's and 60's and still exist in tobacco.

Experience has shown that when acreage allotments are used, in the absence of marketing quotas, the program is ineffective in limiting production to the desired level. Farmers select their best acreage and farm the allotted acreage more intensively. The result is increased production per acre, requiring further tightening of the allotment in future years.

If the Secretary determined, as in our analysis, that 57% of the wheat base would have to be removed from grain production to meet the needs of the market at a price of \$4.04/bushel, farmers might only be allowed to plant wheat for grain on 43% of their allotted acreage. The question that immediately surfaces is, "What can we do with the idled acreage?" Allowances for use of the idled acreage become extremely important to producers in determining their preference for this type of mandatory program.

The rules for transfer of the allotment are also very important. If the allotment is tied to the land and non-transferable, then the price of land tends to be bid-up. If allotments are transferable, then any profits resulting from the allotment will be quickly capitalized into the allotment's value. Is the landowner better off? The answer depends again on what he can do with his idled acreage. If the idled acres can be profitably farmed, then the producer would gain from the capitalized value of the allotment as well as from the earnings on wheat. If the idled acres cannot be farmed, the capitalized value of the allotment must be offset against the reduced value of land that cannot be farmed and the cost of controlling weeds and erosion on the idled land.

Allotments tied to a specific crop tend to restrict the farmer's ability to adjust crop mixes in response to changes in relative crop prices. If idled acreage is allowed to be planted to alternative crops, furthermore, it could result in surpluses for non-allotment crops, thus tending to force these producers to elect allotments for their crops.

The bottom line is that farmers are not automatically better off from mandatory acreage controls. Whether they are better off depends on the rules of the game and each specific situation. At this point, we do not know the rules under which mandatory controls would operate.

Marketing Quotas

It is not surprising that the 1985 farm bill, under its wheat title, has a marketing quota section immediately following the section requiring the "Wheat Poll." A marketing quota is a mandatory mechanism which determines the quantity of a commodity that can be marketed. The national quota, set by the Secretary of Agriculture, is based on the quantity of wheat necessary to meet the expected market needs, taking into consideration domestic

and export requirements as well as emergency food aid needs and adequate carryover stocks.

After the establishment of the national quota, the Secretary would assign a marketing quota for each farm on which wheat was planted or considered planted for harvest during the 1981-1985 base period. The marketing quota would be equal to the product derived by multiplying the farm's base acreage by its farm program yield and reduced by the appropriate percentage necessary to bring national marketing down to the level of national quota. Penalties would be assessed to producers who marketed wheat beyond their assigned quotas.

The Secretary has the authority to announce a marketing quota for wheat to cover the crop years 1987-1990. To implement a quota under the 1985 farm bill provisions, the Secretary must proclaim the national wheat quota by June 15, 1986. He must also conduct, by mail ballot, a marketing quota referendum by August 1, 1986. This referendum is separate from the non-binding poll conducted in June, which is the topic of this paper. The Secretary may proclaim that marketing quotas are in effect for 1987-1990 if he determines that 60% or more of the eligible producers, voting in the referendum, approved marketing quotas. According to the 1985 farm bill, the national quota could be terminated or adjusted in any marketing year the Secretary determines there exists a national emergency or there has been a material change in the demand for wheat. Our analysis indicates that a reduction in export and feed use demand would be likely.

Previous experience with supply control programs indicates that marketing quotas are the most effective means of controlling production because there is virtually no slippage. Quotas are, however, hard to maintain because of political pressure to increase the national quota once it is established.

As was the case with acreage allotments, the use of idled cropland is a big factor in a producer's decision to favor a marketing quota. Many of the same consequences may apply.

In the case of mandatory acreage controls or marketing quotas, the incidence of government involvement in agriculture is high. In terms of taxpayer dollars, however, mandatory programs are relatively inexpensive supply-management alternatives.

What Are the Consequences Of Continuing the Current Program?

The current program calls for voluntary compliance in announced acreage reduction programs in return for direct government income support (deficiency) payments and access to price support loans. In addition, authorization exists for a 45 million acre conservation reserve.

Voluntary acreage limitations call for different levels of idled acreage each year, depending on the projected carryovers. If carryover stocks are expected to exceed 1 billion bushels (highly likely for the next few years), the annual acreage reduction requirement will be between 20-30% (20-27.5%) in 1987 of base acreage. If stocks are expected to be less than 1 billion bushels, the acreage reduction requirements would be not more than 20%.

the national average cost of producing wheat (excluding land and residual returns to management) to be about \$3.23/bushel. The objective of a mandatory production control program, therefore, would be to raise the price of wheat to about \$4.04/bushel (1.25 times \$3.23/bushel).

How Much Wheat Can Be Sold?

The answer to this question is vital to our analysis since it determines the level of production necessary to sustain a \$4.04/bushel market price. Unfortunately, there is no simple answer. The quantity of wheat sold at \$4.04/bushel will depend on a myriad of factors affecting the domestic and export sectors. Due to the importance of the answer to this question, further examination of these sectors is warranted.

Domestic Use

Domestic wheat utilization can be categorized into three components: food, seed, and feed. As shown in Figure 1, the major domestic use of wheat is in the food sector. Wheat for food use, however, has been virtually non-responsive to price. Food demand, thus, would be expected to decline only moderately to approximately 650 million bushels if price is increased to \$4.04/bushel to the farmer.

Seed use is a function of planted acreage and seeding rate. The planted acreage will vary depending on such factors as grain needs, livestock grazing needs, wheat's use as a cover crop on acres idled under government programs, and wheat's importance in double cropping systems. For the purpose of this analysis, we assume seed usage at 70 million bushels, down 22% from 1985 levels.

Feed use has varied over the last several years (Figure 1) depending on the price relationship between wheat and competing feed grains. If mandatory production controls were implemented for wheat irrespective of the feed grain sector, it is likely that the amount of wheat used as feed would drop significantly. For the purpose of this analysis, we assume annual feed use to decline to 90 million bushels.

Export Use

Since the early 70's when the dollar was allowed to float relative to other currencies, the export sector has traditionally absorbed more wheat than the domestic

market. USDA's estimate of 900 million bushels for the 1985/86 marketing year marks the first time since 1971 that importers will demand less U.S. wheat than the domestic sector. The decline in exports (Figure 1) has occurred because of: a strong U.S. dollar, U.S. price support levels (loan rates) exceeding world market levels, foreign competition, and a heavy debt load in many developing countries.

The export wheat market is highly competitive. An increase in the U.S. wheat price would place the United States soundly in the position of a residual supplier. A conservative response to a U.S. price increase to \$4.04/bushel would result in a drop in exports to 750 million bushels.

This analysis suggests that the total demand for U.S. wheat could fall by 21% from 1985 levels to approximately 1.56 billion bushels if U.S. wheat prices were supported at \$4.04/bushel.

How Much Would Production Need to Be Cut?

In 1985, U.S. wheat producers harvested 2.43 billion bushels from 64.7 million acres. Ignoring, for the moment, record levels of carryover (Figure 1), the United States would have to reduce wheat production by about 36% to meet the 1.56 billion bushel demand estimated in the previous section. Further reduction would be necessary, in the short run, if the wheat already in government storage were allowed to enter the market.

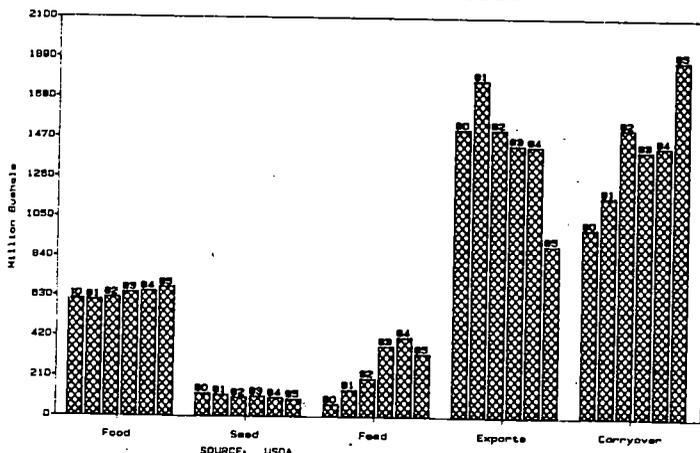
Assuming minimal production control program slippage (slippage is that portion of reduced acreage which does not result in correspondingly lower production, e.g., due to idling the poorest land) resulting in a 39 bushel/acre average yield, the projected demand of 1.56 billion bushels could be produced on 40.0 million harvested acres—only 43% of the wheat base for 1986. In other words, 57% of the wheat base would need to be removed from grain production to support a market clearing price of \$4.04/bushel.

What Mandatory Supply Control Options Are Available?

Mandatory production control programs can take many forms. This discussion, however, will focus on mandatory acreage controls and marketing quotas. The analysis in the previous section applies to either form of production control.

USDA may take the position that even if an overwhelming majority of the farmers vote in favor of mandatory production controls, it has no authority to implement them. The 1985 farm bill contains authority for establishing marketing quotas in wheat. USDA's position could be that from a legal perspective, marketing controls (quotas) are not production controls. However, under conditions of a sufficiently overwhelming favorable vote, the marketing quota authority in the 1985 farm bill might still be utilized. Alternatively, Congress could enact new legislation authorizing acreage allotments or providing legal interpretation of marketing quotas as a tool for controlling production.

Figure 1. Disappearance and Carryover of Wheat, 1980-1985



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The conservation reserve program provides for up to 45 million acres of land being taken out of production for a 10 year period. Available USDA data suggest that about 25% of this land (11.3 million acres) would have wheat base. This is about 22% of the land that would be taken out of grain production under a mandatory control program that was designed to raise the price of wheat to \$4.04/bushel. The main question surrounding the conservation reserve program is whether the money is going to be appropriated to remove 45 million acres from production. With potential Gramm-Rudmann-Hollings budget cut restrictions on funding, this program could suffer.

Continuation of the current farm program would likely result in farm level prices being determined by the loan rate for the next few years. In addition, the presence of large carryover stocks would likely lead to further reductions in the loan rate based on the loan rate formula in the 1985 farm bill. It would be difficult for the market to absorb the expected 1.88 billion bushels of stocks on hand as of June 1, 1986, with the acreage reduction requirements called for in the farm bill. Voluntary acreage reduction programs have never been a very effective tool for controlling production due to slippage.

A policy scenario which could lead to different price results involves the implementation of a wheat marketing loan by the Secretary, which is authorized in the 1985 farm

bill. Initial indications are that in rice, where the marketing loan is currently in effect, exports increase as market prices fall to the world price level. Government payments initially rise sharply, offsetting the fall in market price. Once stocks are drawn down, however, market prices should rise above current levels. Regardless of whether the marketing loan is used, the current program will be relatively costly to the U.S. treasury.

Conclusions

The "Wheat Poll," although non-binding, could have important implications for future wheat programs. The market says we have overproduced. Effectively managed mandatory production controls provide an orderly way to get resources out of agriculture.

The decision to vote in favor or against mandatory production controls is multi-faceted. Producers must consider the short- and long-run consequences of mandatory supply controls versus the current program. The basic choice is between the current voluntary program with relatively high government costs and lower market prices and a mandatory program that costs less but could result in relatively higher prices, lower export and feed demand, and considerably lower production. In any event, as in any political issue, it is important that farmers make their preference known.