

Aggregate Impacts of the 1996 Act Relatively Small

The 1996 Act accelerates market orientation of the previous two major farm acts, which have gradually reduced the Government's influence in the agricultural sector through commodity programs. As producers increasingly respond to signals from the marketplace rather than to commodity programs, agricultural production becomes more efficient. The trend toward fewer but larger farms is expected to continue. The sector will be highly competitive, with successful producers having strong technical and managerial skills. Fixed government payments could make farm income more variable in response to supply and demand shocks, so alternative marketing arrangements, such as marketing contracts and integrated ownership, are likely to be used more to manage risks.

The following discussion presents some of the potential impacts of the 1996 Act on the farm sector. The analysis incorporates impacts on the farm sector from the commodity provisions (Title I), the agricultural trade provisions (Title II), and the conservation provisions (Title III) of the 1996 Act. Impacts are based on a comparison with the February 1996 USDA long-term projections to 2005 (USDA, 1996a) that assume an extension of the 1990 Act and the Budget Reconciliation Acts of 1990 and 1993 (box 6).

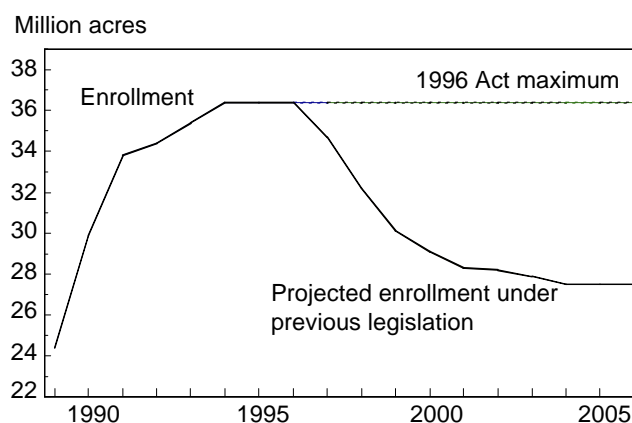
CRP Enrollment Affects Land Available for Crop Production

The amount of cropland enrolled in the CRP plays a significant role in determining the projected impacts of the 1996 Act on U.S. agriculture. Many of the expected changes in planted acreage depend on CRP enrollment, particularly for wheat, feed grains, and soybeans. In 1995, over 245 million acres were planted to contract crops and soybeans. About 4.9 million acres were idled under the ARP and 15 million acres under 0,50/85-92. In comparison, about 36.4 million acres were idled under the CRP. Thus, the CRP represents a significant source of potential harvestable cropland in the United States.

Under the 1996 Act, landowners can remove less environmentally sensitive land from the CRP prior to CRP contract expiration if the contract was entered into prior to 1995 and the contract is at least 5 years old. Additionally, the CRP is extended with Secretarial authority to re-enroll current land at contract expiration and to enroll new land to replace land exiting the program.

Figure 5

Conservation Reserve Program enrollment projected to decline



Previous legislation enrollment from USDA, 1996a.
Compiled by Economic Research Service, USDA.

USDA has authority under the 1996 Act to establish targets for the level of CRP enrollment and the composition of the land enrolled. In addition, farmers will decide whether they want to keep land in the CRP or to farm it and receive production flexibility contract payments on eligible land. Thus, considerable uncertainty exists regarding future CRP enrollment. USDA (1996a) projected CRP enrollment to decline from 1995's enrollment of 36.4 million acres to around 28 million acres by 2002 (fig. 5), based on a continuation of previous law. Depending on program implementation decisions regarding CRP provisions of the 1996 Act, similar levels of total enrollment could occur, but the composition by crop of enrolled area could change depending on the environmental criteria selected for enrolling new acreage and extending previous contracts.

The composition of land enrolled in the CRP is expected to include more environmentally sensitive land under the 1996 Act. Landowners with older CRP contracts and with less environmentally sensitive land have the option of exiting the CRP early. CRP enrollment trends in recent years included more land with higher potential to pollute surface and ground water. Contract extensions and new enrollments under the 1996 Act likely will build on these recent trends. CRP enrollment could increase slightly in regions such as the Corn Belt where water quality is an issue, drawing from land typically planted to corn and soybeans. Conversely, CRP enrollment could decline in regions such as the Northern Plains where soil erosion is the primary environmental issue and

wheat and barley are typically grown. The use of wildlife factors as criteria in selecting land for enrollment in the CRP will limit regional enrollment shifts from the Northern Plains.

U.S. Agriculture More Price-Competitive in Export Markets in the Long Run

Initially, the 1996 Act makes U.S. agriculture less price-competitive in world markets, but price competitiveness increases in the longer run. Cuts in EEP funding under the 1996 Act through FY 1999 will initially reduce wheat, barley, and poultry exports, although impacts are small. Export subsidies add little to total exports when prices are high, so EEP funding cuts with tight grain market conditions have limited wheat and barley export impacts. Corn exports expand to capture a portion of the reduced barley trade. EEP poultry exports represent a very small share of total U.S. poultry exports, so poultry impacts are minimal.

In the longer run, the overall price competitiveness of U.S. agricultural exports increases. Reorienting trade programs toward market development and emerging markets with high potential for U.S. export gains may enhance the effectiveness of those programs. Further, in times of large supplies, U.S. price competitiveness benefits from elimination of authority for ARP's and from suspension of the Farmer Owned Reserve, programs that restricted production, limited marketings, and raised prices under previous legislation.

A notable exception is that U.S. rice will be less competitive in global markets. With lower U.S. rice production under the 1996 Act, rice exports fall because strong domestic rice demand pushes the U.S. rice price premium over world prices higher than projected assuming continuation of previous legislation.

Independent of the 1996 Act, favorable world economic growth and freer trade under the World Trade Organization support gains in trade and U.S. exports (fig. 6). Income growth—particularly in the Pacific Rim, Central and South America, the Middle East, and North Africa—enhances the demand for agricultural goods. Funding for export promotion, credit assistance, and food aid programs is expected to continue to be an important factor maintaining agricultural exports. The 1996 Act also targets trade programs to make them more flexible and to emphasize high-value products, further supporting gains in U.S. exports.

USDA (1996a) projected the value of total U.S. agricultural exports to rise substantially, approaching \$80 billion by 2005. High-value products are projected to gain a larger share of total agricultural exports, rising to about two-thirds of total export value. These trends are expected to continue under the 1996 Act, with lower growth in bulk exports reflecting reduced rice exports.

Aggregate Crop Production Similar Under 1996 Act

The 1996 Act increases farmers' planting flexibility by eliminating ARP's, base acreage planting constraints, and limits on normal and optional flex acreage. Production patterns under the 1996 Act are likely to shift somewhat at the farm level and regionally to reflect differences in comparative advantage for the production of specific crops and to address agronomic, environmental, and conservation needs. These acreage shifts have implications for planting decisions of other farmers as they respond to changes in relative market prices in their cropping choices. The impacts of the 1996 Act will vary across regions reflecting the mix of agricultural products, the degree of diversification, and the availability of production alternatives.

Regional production patterns in the past reflected comparative advantage and led to the regional distribution of historical acreage bases. While comparative advantages may have shifted somewhat, for many areas the changes are relatively minor. Corn Belt States, for example, have an advantage in producing corn and soybeans, so corn and soybean production is likely to remain in this region. Rainfall levels limit production in much of the Northern Plains to crops with low water requirements, such as wheat, barley, and minor oilseeds. Thus, crop production in that region will likely remain in those crops.

The national level of acreage planted to most major field crops will be similar under the 1996 Act to what would have occurred under prior law. Plantings are projected to rise 10 to 15 million acres over the next 10 years, compared with average plantings during the past 5 years under the previous law, in response to growing world demand and less acreage enrolled in the CRP (fig. 7).

Under prior law, the role of government programs had been declining, with the links between government payments and producer planting decisions already small. No government payments were received for the 15-percent normal flexibility acreage. For wheat and feed grains, the 0/85-92 option meant

USDA's February 1996 Long-term Agricultural Projections to 2005

USDA annually prepares 10-year projections of the agricultural sector, representing a Departmental consensus on a long-run scenario for the sector. The latest projections, released in February 1996 (USDA, 1996a), assumed that provisions of the Food, Agriculture, Conservation, and Trade Act of 1990, as amended, remained in effect through 2005.

The long-term projections are a conditional scenario with no shocks and are based on specific assumptions regarding the macroeconomy, the weather, and international developments. The projections cover agricultural commodities, agricultural trade, and aggregate indicators of the sector, such as farm income and food prices. The February 1996 projections are not intended to be a Departmental forecast of what the future will be, but instead a description of what would be expected to happen with an extension of 1990 agricultural law, as amended, and with very specific external circumstances. As such, the February 1996 scenario provides a point of departure for discussing the effects of the 1996 Act.

Key Features of February 1996 Projections

Trends of the last 10 years toward greater market orientation in agriculture continue in the February 1996 long-term projections, gradually reducing the Government's influence in the sector through traditional commodity programs. Global economic growth, combined with liberalized trade under the GATT agreement, supports strong growth in global trade and U.S. agricultural exports. After falling from high levels in the initial years, crop prices rise back toward target prices and deficiency payments are reduced. This agricultural policy and market setting continues a gradual phase-down of the role of Government commodity programs. Thus, the sector responds more to signals from the marketplace and less to Government commodity programs, resulting in agricultural production becoming economically more efficient.

The Conservation Reserve Program (CRP) in the long-term projections is assumed to fall from 1995 levels of about 36.4 million acres to about 27.5 million acres in 2005. The CRP assumptions reflect a combination of assumptions for early termination of contracts expiring in 1996, a new enrollment in 1997 to add approximately 1.6 million acres, and contract extensions and modifications at maturity.

Annual quantity and expenditure levels for the Export Enhancement Program are assumed to be in compliance with GATT reductions, which require that by 2000 subsidized exports be reduced by 21 percent in volume and 36 percent in budget outlays from 1986-1990 levels.

Productive capacity for crops is projected to rise due to increases in resource and input use and in productivity. For most crops, yields are projected to rise at or near their long-term trends. However, the balance between productive capacity and projected demands tightens significantly as the land base is pressured. With only a small reduction in the CRP, increases in land used for crop production draw mainly on lower annual ARP levels, reduced use of the 0/85-92 provisions, and use of other recently unplanted acres. Long-term trends in supply/demand balances imply strengthening nominal prices for crops, with prices for wheat and feed grains rising above their target prices. Real prices for crops are projected to continue their long-term downward trend.

that producers were largely making decisions to plant based on market signals.

At the national level, 15-percent normal planting flexibility was generally sufficient to balance farmers' production choices among competing crops with relative price signals from the marketplace. Some individual producers may have been constrained from expanding production of program crops by their crop acreage bases. And other producers may have been constrained in their planting of alternative crops by the 15-percent limit on planting flexibility without loss of deficiency payments or the 25-percent overall limit on flexibility. However, other producers were

only partially using planting flexibility and could adjust their use of flexibility to respond to any relative price imbalances resulting from planting constraints faced by other producers.

Under the 1996 Act, most planting constraints from agricultural policy are eliminated, so individual producers will be able to more fully make planting choices based on expectations of market returns. Individual producers who may have been constrained in their cropping choices under previous farm law by crop acreage bases may now expand their plantings of program crops. Producers who were constrained in their planting of alternative crops by limits on

planting flexibility may now, with a few exceptions, switch more acreage to other crops. But planting choices of those producers now will have different implications for remaining producers in their use of flexibility to respond to relative price signals, with resulting planting choices bringing land use back toward a similar aggregate cropping mix.

Thus, aggregate planting levels for wheat, feed grains, and soybeans are expected to be similar or slightly lower under the 1996 Act as under previous law. Changes in plantings for these crops are largely related to overall changes in the size and mix of the CRP.

Upland cotton acreage could be slightly higher under the 1996 Act, mostly reflecting expiration of ARP authority, but limited by a number of offsetting factors. Plantings for rice are lower under the 1996 Act because of elimination of the minimum planting requirement and increased planting flexibility.

Prices for most field crops under the 1996 Act will be unchanged from or marginally higher than what would have occurred under previous legislation, with two exceptions. First, wheat and feed grain prices initially may be somewhat reduced as lower EEP funding decreases grain exports. Second, rice prices are expected to be higher under the 1996 Act in response to lower production.

If crop surpluses develop in the future due to excellent growing conditions or to weaker export demand, expected market conditions could be different under the provisions of the 1996 Act than under previous legislation. Previously, when crop surpluses occurred, USDA could use ARP's to reduce crop production and raise prices. While expiration of ARP authority is expected to have relatively little impact assuming normal weather, ARP's might have been implemented in the future in some market situations with continuation of previous legislation.

Wheat, feed grains, and soybeans. Wheat, feed grains, and soybean acreage and production will be greatly influenced by the size and composition of the CRP, which affects the availability of cropland for plantings. If CRP enrollment is targeted toward land with greater potential for environmental damage, such as in the Corn Belt, the amount of land available to produce corn and soybeans could be reduced. As a result, corn and soybean production would be lower and prices higher relative to what they would have been under past legislation.

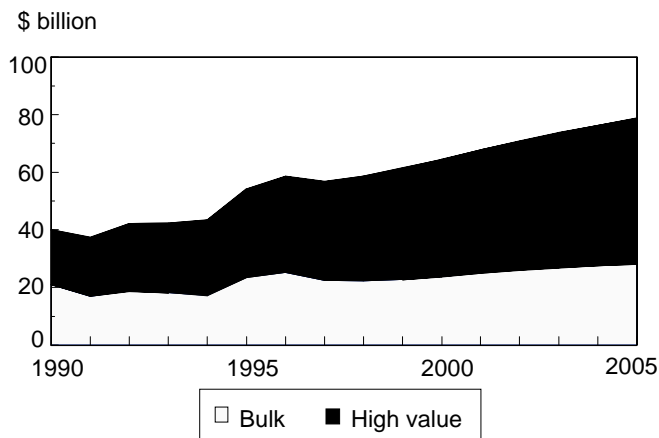
Once CRP policy is determined, plantings will largely reflect domestic and export demand as reflected in prices. Generally, therefore, plantings for these crops are expected to expand over the next 7 years in response to increasing demand, particularly in export markets. This increase in acreage is not much different than had been expected under a continuation of previous farm law since the underlying longrun demand growth is not affected by the 1996 Act.

In the near term, however, the 1996 Act will reduce export demand for U.S. wheat and feed grains through the reduction in EEP funding. Over half of EEP expenditures have supported wheat and wheat flour exports. More than 80 percent of U.S. barley exports, on average, have been exported under EEP since its inception. As a result, reduced EEP funding in 1996-99 lowers wheat and barley exports somewhat and places some downward pressure on wheat and barley prices. For wheat, strong world demand limits the decline in exports. Additionally, with marginally lower prices, exports to nonsubsidized markets increase slightly, partly offsetting the reduction in EEP exports to subsidized markets.

In response to lower prices, wheat and barley acreage under the 1996 Act initially could be lower than under previous legislation. Lower domestic wheat and barley prices also reduce the demand for wheat and barley imports during the first few years. Additionally, with lower wheat and barley prices, feed use of wheat and barley expand to partially offset the loss of EEP-induced exports. Feed use of corn declines, reflecting the relatively lower wheat and barley prices. This lowers corn prices and allows corn exports to expand to regain part of the lost barley exports.

Rice. The provisions of the 1996 Act are expected to reduce the incentives to produce rice. Under the 50/85 provisions of previous legislation, rice producers who planted at least 50 percent of their rice maximum-payment acreage were eligible to receive 85 percent of maximum deficiency payments. Under the 1996 Act, there is no minimum planting requirement. Without the minimum planting requirement and 50/85 deficiency payments, some rice farmers probably will plant less rice. Rice production is expected to decline in regions like southwest Louisiana and Texas where production costs are high and where many producers used the 50/85 provisions.

Figure 6
Growth projected for U.S. agricultural exports



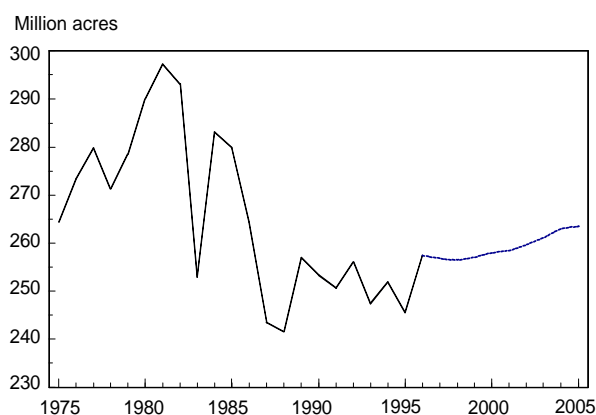
Compiled by Economic Research Service from USDA, 1996a.

Some rice acreage is expected to be idled or to flex to other crops with lower production costs as rice producers seek to diversify. As a result, area planted to rice could decline by about 15 percent. A reduction of this magnitude will raise U.S. rice prices and cause a minor reduction in domestic rice consumption. Higher domestic prices will cause a widening differential between domestic and world rice prices, thereby reducing U.S. competitiveness in export markets and lowering U.S. rice exports. With reduced U.S. exports, world rice prices will rise, lowering the likelihood of Federal program costs associated with rice marketing loans, especially with the loan rate fixed at \$6.50 per hundredweight.

Upland Cotton. Upland cotton acreage could be slightly higher, reflecting a number of offsetting factors. The elimination of ARP's would free additional cotton land for production, as cotton was the only program crop projected by USDA (1996a) to be subject to a positive ARP under continuation of past legislation. Further, cotton is the only crop that had a net gain in acreage under planting flexibility during 1991-95, suggesting favorable market-based producer returns compared with other crops. Offsetting much of this potential for increased cotton plantings, some cotton acreage could move to other crops as some producers diversify to guard against perceived variability in cotton production and market income.

Dairy. The 1996 Act modified the dairy programs by phasing out price supports and consolidating and reforming Federal milk marketing orders. Growth in milk production is expected to slow in response to the lower prices and reduced net returns to dairy farming.

Figure 7
Planted area for 8 major crops to rise from levels in the early 1990's



Compiled by Economic Research Service, USDA.

Consolidating milk marketing orders will expand the size of areas where dairy farmers compete, and thus have regional price impacts by raising prices for some farmers while reducing prices for others. Dairy prices in some locations may be affected by regional impacts of order consolidation more than by the reduction in national price supports. The 1996 Act requirements to use DEIP to the maximum levels permitted under the Uruguay Round Agreement is not expected to cause a significant expansion of dairy product exports, since under a continuation of previous legislation DEIP funding was assumed to be the maximum permitted under the Uruguay Round. Net income in the dairy sector is projected to fall under the 1996 Act relative to projections of net income under past legislation as cash receipts will be lower after 1996 reflecting the phase-out of support. However, elimination of the dairy assessment will partly offset this loss. Dairy producers will benefit from modest increases in forage availability due to planting flexibility; also, feed costs will remain nearly unchanged under the new act.

Beef, Pork, and Poultry. Impacts on the livestock sector, excluding dairy, are expected to be minimal. Feed costs under the 1996 Act are expected to be similar to those under previous legislation, and forage availability may increase modestly due to planting flexibility. Reductions in EEP funding will have a minimal impact on poultry exports. Maximum subsidized poultry volume under the Uruguay Round Agreement represents less than 2 percent of total projected poultry exports.

Sugar. Elimination of authority for sugar marketing allotments may create opportunities for more efficient beet sugar producers to increase production. Small expansion of sugarbeet production in regions such as North Dakota's Red River Valley is likely, raising beet's share of total sugar output. Production in high-cost areas will continue to decline. Production of raw cane sugar is expected to be similar to what would have occurred under previous law. This continues trends that were occurring under past legislation. However, any expansion in beet production will likely be constrained by the possibility that recourse loans will be in effect in years the tariff-rate quota on sugar imports is at or below 1.5 million short tons raw value. Sugar imports are expected to be above 1.5 million short tons in most years. With the continued ability of the Government to affect supply by controlling imports, sugar prices are not expected to change.

Peanuts. Elimination of the minimum poundage quota for marketings eligible for quota support and reduction of the quota support rate will depress peanut prices and lead to a reduction in plantings. Lower production and prices for peanuts under the 1996 Act will reduce the farm value of U.S. peanut production, lowering revenue for peanut producers. Peanut production is centered in the Southeast, with nearly half of U.S. peanut production in Georgia. Quota marketings can be leased or sold. The value of quotas and quota leases is also expected to decline. Consumers will benefit from lower prices for peanuts, increasing domestic food use of peanuts.

Fruits and vegetables. The 1996 Act will have negligible effects on fruits and vegetables because planting limitations on contract acreage are similar to planting flexibility restrictions of previous farm legislation.