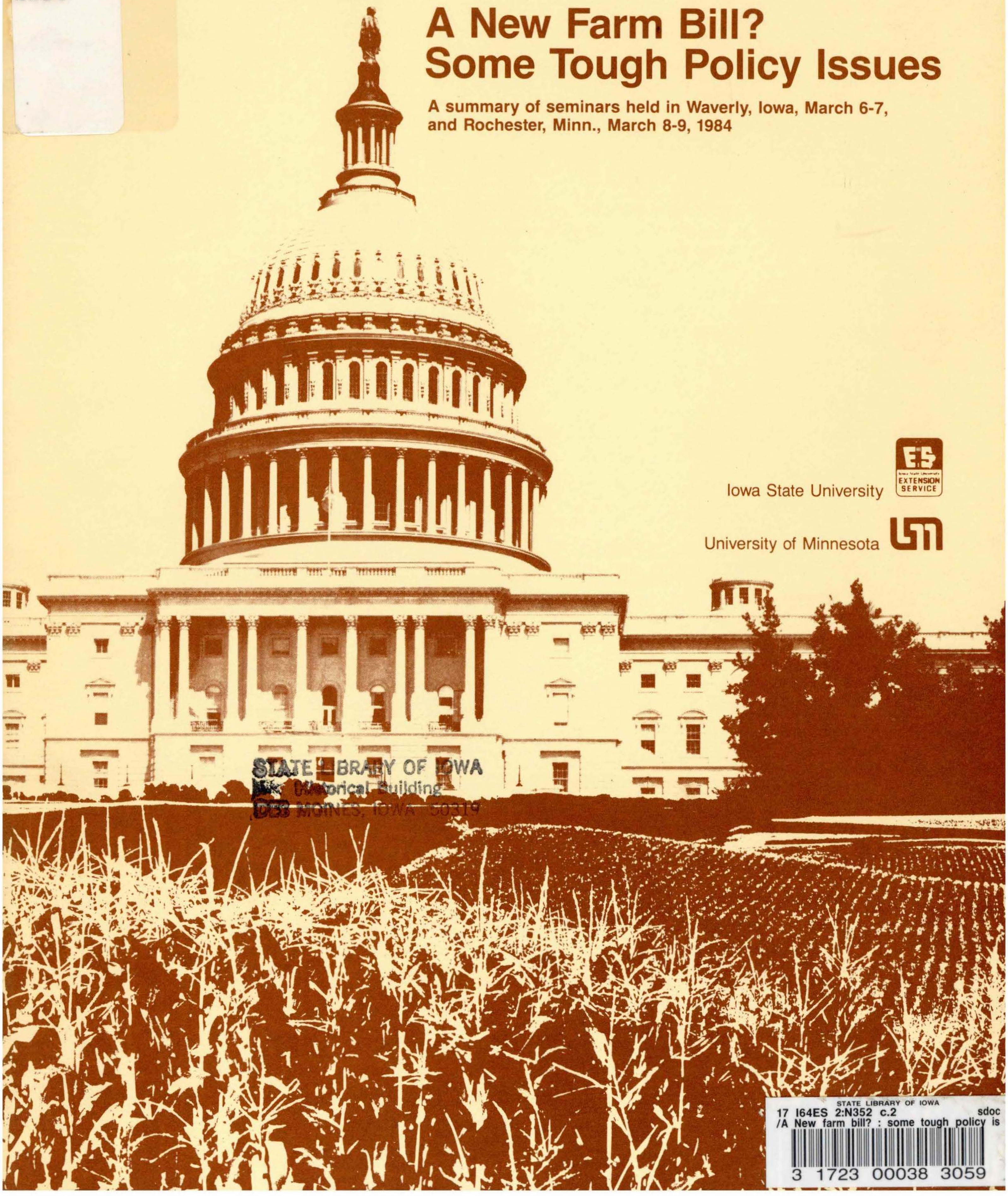
# A New Farm Bill? Some Tough Policy Issues

A summary of seminars held in Waverly, Iowa, March 6-7, and Rochester, Minn., March 8-9, 1984

Iowa State University
University of Minnesota



**Program Chairman:** Luther J. Pickrel, professor at the University of Minnesota

**Program Associate:** Miriam Rykken Schulz, Agricultural Extension Service at the University of Minnesota

**Summary Writer and Editor:** Brian Holding, editor of the North Central Regional Center for Rural Development and the Center for Agricultural and Rural Development, Iowa State University

The seminars were sponsored by the University of Minnesota, through its Agricultural Extension Service and Department of Agricultural and Applied Economics, and Iowa State University, through its Cooperative Extension Service.

General co-sponsors of the seminars were Farm Credit Services, St. Paul, Minn.; Federal Reserve Bank of Minneapolis; First Bank System, Inc.; Minnesota Farm Bureau Federation; Minnesota Farmers Union; and Norwest Corporation.

Local co-sponsors were Byron State Bank; Eastwood State Bank of Eyota and Rochester; Federal Land Bank of Blooming Prairie; Federal Land Bank of Rochester; First Bank of Rochester; First National Bank of St. Charles; First National Bank of Stewartville; Norwest Corporation; People's State Bank of Plainview; Production Credit Association of Blooming Prairie; Production Credit Association of St. Charles; Rochester Chamber of Commerce; Richester Chamber Convention Bureau; Security State Bank of Pine Island; and Tri-State Electric Show of Rochester.

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# A New Farm Bill? Some Tough Policy Issues

A young farmer poses a question at Rochester, Minn.

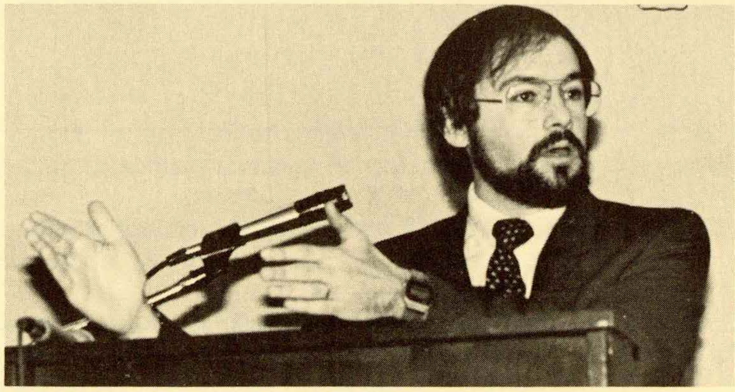
## Introduction

In 1983, the tab for the nation's agricultural programs reached a record $18.8 billion.

Today, as the budget deficit soars—interest rates and the value of the dollar remain high, agricultural exports have fallen, and farmers' debts have risen. Agricultural interests continue to be splintered by commodity, by farm size, and by region.

In this unstable economic environment, Congress will enact legislation during 1985 to replace the expiring Agriculture and Food Act of 1981. The legislation authorizes the federal government's price support programs for crops and milk. It also covers P.L. 480 overseas aid, food stamps, and agricultural research and Extension programs.

To examine these issues and others that Congress will be facing—and to voice their own concerns—over 300 farmers, agribusinessmen, and others interested in agriculture attended policy seminars in Waverly, Iowa, March 6-7, and Rochester, Minn. 8-9. The conferences were sponsored by the Agricultural Extension Service and Department of Agricultural and Applied Economics at the University of Minnesota and the Cooperative Extension Service at Iowa State University.



Robert Lawrence

Robert Hartman

# The General Economy

## Rising Deficit Expected to Influence Economy, Policy Decisions

While the unemployment rate has fallen and inflation appears to have been harnessed, the rising federal deficit has placed the country on "a course that has never been ridden before," according to Robert Hartman, senior analyst for Congressional Budget Office in Washington, D.C.

Robert Z. Lawrence, a senior fellow at the Brookings Institution, agreed maintaining that one major obstacle stands between the United States and sustained growth—the budget deficit.

During the 1960s, the budget deficit was less than 1 percent of the country's gross national product (GNP), Hartman pointed out. In the 38 years since World War II, the total deficit has exceeded 3.0 percent of the GNP only four times, all during years of high unemployment: 1975, 1976, 1982, and 1983. Last year the deficit's share of GNP reached 6.4 percent. Hartman projected record-breaking deficits year after year even in times of relative prosperity. If the economy falters, he warned the deficits will be even larger than the annual projection of $300 billion by 1989.

As the deficit grows, it raises interest rates and consumes a greater share of savings. "Real interest rates right now are on the order of 4 percent. In the past, they were closer to 1 percent," Hartman said. (The real interest rate is the amount by which the actual rate of inflation exceeds the rate of inflation.)

Attracted by the high interest rates and political stability, foreign capital has poured into the United States driving up the value of the U.S. dollar against other currencies, according to Lawrence. "This has priced a lot of American firms out of the world market," Lawrence said. Agricultural products have especially felt this impact, as the American share of the world market has dwindled during the 1980s after the boom times of the 1970s.

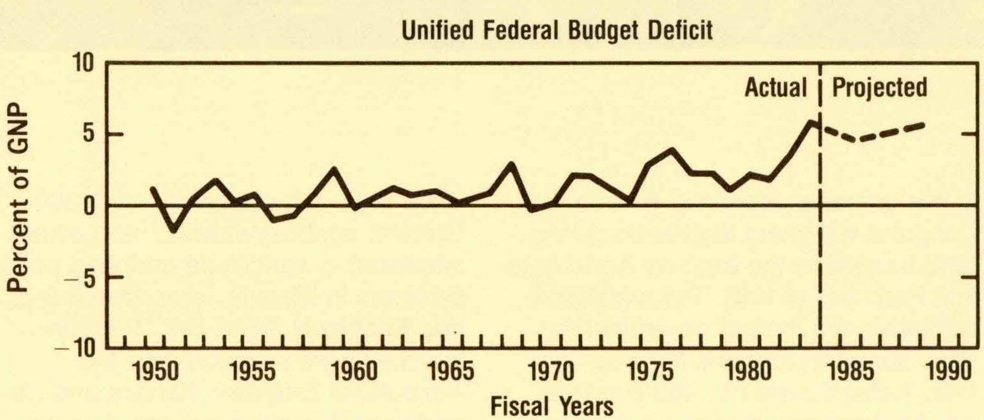
"We are as a nation going to be increasingly indebted to the rest of the world," Lawrence said. He forsees the United States becoming a net debtor nation "owing the rest of the world more than they owe us."

Hartman maintained that the current inflow of foreign capital is unsustainable. Should the inflow slow, he said, the U.S. dollar's value will fall and interest rates will climb.

Both economists offered identical solutions to the budget dilemma: packages of spending cuts and tax increases. Lawrence targeted two areas where spending could be slashed: the interest paid on the deficit (by simply reducing the deficit) and defense.

Immediate cuts would have to be made in defense spending for budget reductions to be effective within the next five to six years, according to Hartman. He pointed out that 33 percent of the 1984 military budget is consumed by procurement expenses for weapons systems with the purchases spread over a period of years. Once a down payment has been made on a system, it becomes increasingly difficult to cut that procurement item, he said.

### Government Borrowing



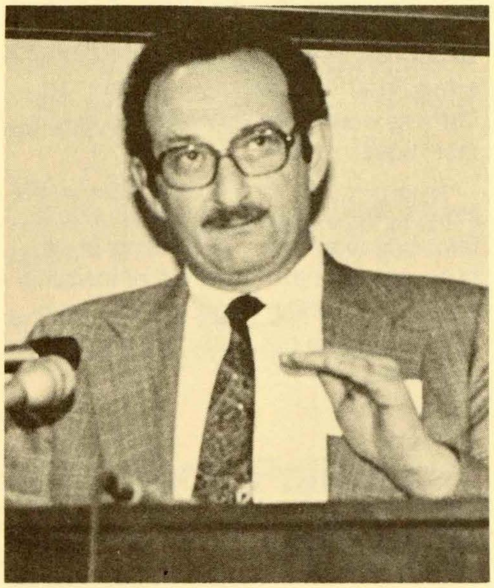

Congressional Budget Office chart shows the path of budget deficit.

Reforms in Medicare and Social Security have made further cuts in those areas difficult, according to Hartman. Legislation passed during 1983 is expected to balance the Social Security fund for the next 20 years, but both economists expect financial troubles as the "baby boom" generation retires unless more changes are made.

Hartman suggested that a value-added or national sales tax may be considered by Congress but did not expect any action until after the November elections. Another tax measure receiving study is an expenditure tax, which would have individuals file taxes on what they spent, not what they earned. Hartman said President Reagan has requested a report on the proposal.

Hartman offered the following steps as possibilities Congress might consider during the coming year:
• A "relatively modest" package of spending cuts.
• An adjustment in the cost-of-living increases to pensioners.
• An adjustment in food stamp benefits.
• A one-year freeze on medical fees covered by Medicare.
• Freezing of nondefense discretionary spending.
• Closing of tax loopholes.

Hartman expected strong support to either modify fully and/or freeze agricultural price supports. Hartman argued that political realities dictate that any solution or partial solution must involve a broad package of changes in spending and taxes. No single maneuver or narrow shift in direction on spending or taxes will be effective or acceptable, he said.



Martin Abel

James Houck

# Critical Policy Issues

## Splintering of Farm Interest Groups Complicates Policy Making

As agriculture becomes more complicated, paradoxes keep popping up before policy makers.

Legislators are discovering that what's good for large farmers may not be good for small farmers; what's good for grain farmers may not be good for livestock farmers; what's good for the domestic market may not be good for the world market; and many other contradictions.

With these various pressures, policy makers face the challenge of writing farm legislation that is not only equitable to competing interests but also effective.

The current approach to farm programs is "not only ineffective and expensive but somehow outmoded," surmised James Houck, a professor in the Department of Agriculture and Applied Economics at the University of Minnesota. Houck believes "something relatively new is needed."

Martin E. Abel, president of Abel, Daft, and Earley of Washington, D.C., agreed with Houck, saying that often government is a major source of instability. "The PIK program was driven by huge surpluses," he said. "The only long-term way to get rid of surpluses is through world economic growth and the recapturing of world markets."

U.S. policies, according to Abel, have moved in oposite directions by keeping U.S. market prices above world equilibrium prices, but then attempting to recapture lost market share by means of a partial export subsidy policy.

Houck added three factors contributing to the push for policy changes:

• With 40 percent of their harvest destined for foreign markets, U.S. farmers are more dependent on world trade. Yet, Abel pointed out that around 40 percent of the capacity of some commodity-exporting facilities is idle. "Policies that don't deal with exports are old-fashioned," Houck said.

• National economic forces, such as the budget deficit and exchange rates, today play a greater role in influencing the agricultural economy.

• The public's perception of agriculture is changing. "The public is less willing to spend money on agriculture," Houck said. More persons are questioning who benefits the most from agricultural programs, he added.

Structural changes in agriculture have weighed on policy makers. Abel pointed out that 12 percent of the nation's farms now produce 70 percent of the agricultural output. The average asset value of these farms, according to Abel, is around $1.6 million—and many of the benefits from farm programs go to these farmers.

While farm interests have splintered into various commodity groups to lobby for their positions, procedural changes in Congress have elevated the power of subcommittees focusing on specific farm products. "In some cases, they have become advocates of special interest groups," Houck maintained. Comparing the situation to the United Nations' Security Council, Houck said the subcommittees have the power to veto specific legislation but are unable to provide broad legislative leadership.

The growing federal deficit could provide the Office of Management and Budget more clout with farm programs than the U.S. Department of Agriculture, according to Abel. "The USDA may have little to say about the 1985 process," he said.

Houck proposed three possible courses for the 1985 programs:

• Tinkering around with the present programs and hoping for crop failures or demand recovery around the world.

• Changing agricultural policies substantially by dropping target prices, controlling acreages, and subsidizing exports.

• Radically changing programs by such moves as dropping all support programs and moving to insuring incomes, altering the loan rates to a pure safety net program, establishing different prices for the domestic and world markets, forming a grain cartel similar to OPEC with other exporters, or tightly controlling production and abandoning exports.

Houck speculated that the "probability is about 60 percent that we'll just tinker around with current programs." He believed that currently there is no agricultural leader with a clear, new policy around whom many interest groups will rally.

Abel offered the alternative of a more actuarial approach to the problems of income instability. He suggested that U.S. policy makers study Canada's Western Grain Stabilization program, which matches farmers' contributions to a fund and then makes payments to farmers when their receipts fall below their costs.

Houck stressed the need for a simple farm policy system, separating price supports from the question of inequitable returns, which might be attacked with payments not associated with production.

# Congressional Concerns About Agriculture

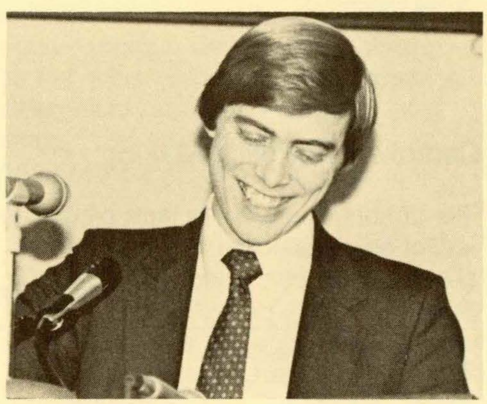
## More Legislators Asking Question: 'What Is It Going To Cost?'

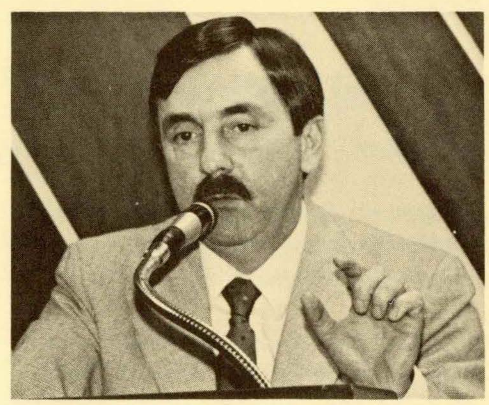
With a record budget deficit looming over their heads, more legislators working on the farm bill are expected to ask, "What is it going to cost?"

After November's elections, the farm bill will receive close scrutiny as one of the first budget-cutting prospects, according to James G. Vertrees, principal analyst for the Congressional Budget Office in Washington, D.C.

Before lawmakers reach that point, many are worried about getting through this year. "We are facing a crisis in agriculture," Rep. Timothy J. Penny, D-Minn., said. "I'm frankly frightened about what's happening in rural America today. I don't know if we can turn it around quick enough."

Penny urged immediate credit help for farmers caught with "high interest rates, low commodity prices, and low land prices." Penny criticized the Farmers'


Rep. Timothy Penny


James Vertress

Home Administration for not offering credit that is currently available.

Penny's overriding concerns were the current interest rates and the threat of the budget deficit increasing those rates. "The farmers get clobbered because interest rates are too high and also because of the value of the dollar," he said. "We've got to cut back on that red ink."

Penny called for a package of budget cuts that would attract the support of both political parties in an effort to whittle the deficit, which is expected to be $200 billion next year and reach $300 billion a year by 1989.

Vertrees, who recently helped prepare a report to Congress on policy options covering price support programs, expected Congressional concerns to revolve around five objectives:

• To raise farm income in periods of overproduction or diminished demand.
• To achieve a reasonable degree of stability in farm prices and income.
• To provide an adequate and stable supply of food and fiber for U.S. consumers at reasonable prices.
• To improve the ability of U.S. agriculture to compete in international markets.
• To keep down taxpayers' costs.

"While agriculture has changed dramatically over the past 50 years, farm programs have not," Vertrees said. Consequently, the programs have become less effective in achieving the major goals of increasing or stabilizing farm prices and incomes.

Meanwhile, the cost of the programs has risen to 1983's record level of $18.8 billion.

With two out of every five acres producing for the export market, legislators are becoming more sensitive to issues abroad, according to Vertrees. He anticipated a greater promotion of exports in the 1985 farm bill.

The changing economic status of farmers has eroded support for expensive farm programs, according to both Vertrees and Penny. Today, about 12 percent of all farms produce most of the nation's food and fiber and earn most of the income from farming; they also receive about 50 percent of the government benefits, according to Vertrees. Less than a third of the farmers receive 80 percent of the government payments.

"There ought to be some type of restriction in size of operation that we assist with the commodity programs," Penny said. "We have to get a lid on providing these benefits because of the enormous costs and the large corporations who benefit."

Penny added that restrictions should be placed on the amount of money a farmer can receive from the Farmers' Home Administration.

Vertrees pointed out a growing awareness among legislators that farm programs can influence exports. "Too high price supports can hurt exports and stimulate production abroad," he said.

Penny urged that the new farm bill incorporate cross-compliance measures linking conservation requirements to program participation.

The growth in the power of subcommittees focusing on various commodities has complicated the writing of a farm bill, according to Vertrees. "Clearly, it makes it more difficult to put legislation together," he said. "The diverse interests make it more difficult to get an omnibus farm bill."

The growing federal deficit will force legislators to make painful decisions concerning the costs of the farm program. "To govern is to choose," said Penny, quoting John F. Kennedy.

"This year we have to choose," he added. "But if we don't choose, we're paving the way for economic disaster."

## U.S. Trade Policies

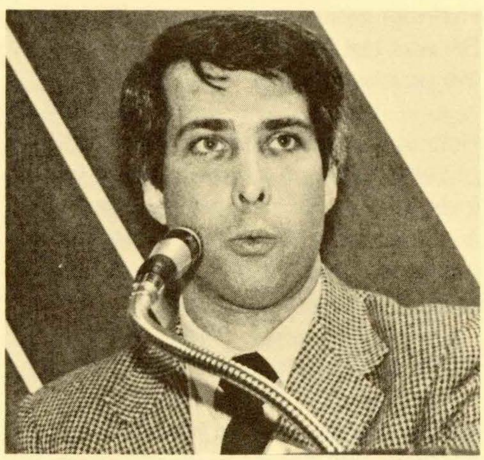
### World Economic Trends, U.S. Farm Programs Help Trim Exports

In 1980-81, American farmers exported $44 billion in agricultural products. In 1983-84, farm exports are projected around $37 billion.

That export decline totals $4,000 from each American farm or $16,000 from each commercial farm, according to John D. Dunmore III, the branch chief for the International Economics Division of the USDA's Economic Research Service.

"Agriculture is dependent on foreign markets," said George Hoffman, associate administrator of the Economic Research Service. "The export market is absolutely crucial for U.S. agriculture."

The rapid growth during the 1970s, according to Dunmore, has left agriculture and agribusiness accounting for 20 percent of the gross national product; 24 million jobs or a quarter of U.S. employment; and 20 percent of the



John Dunmore III

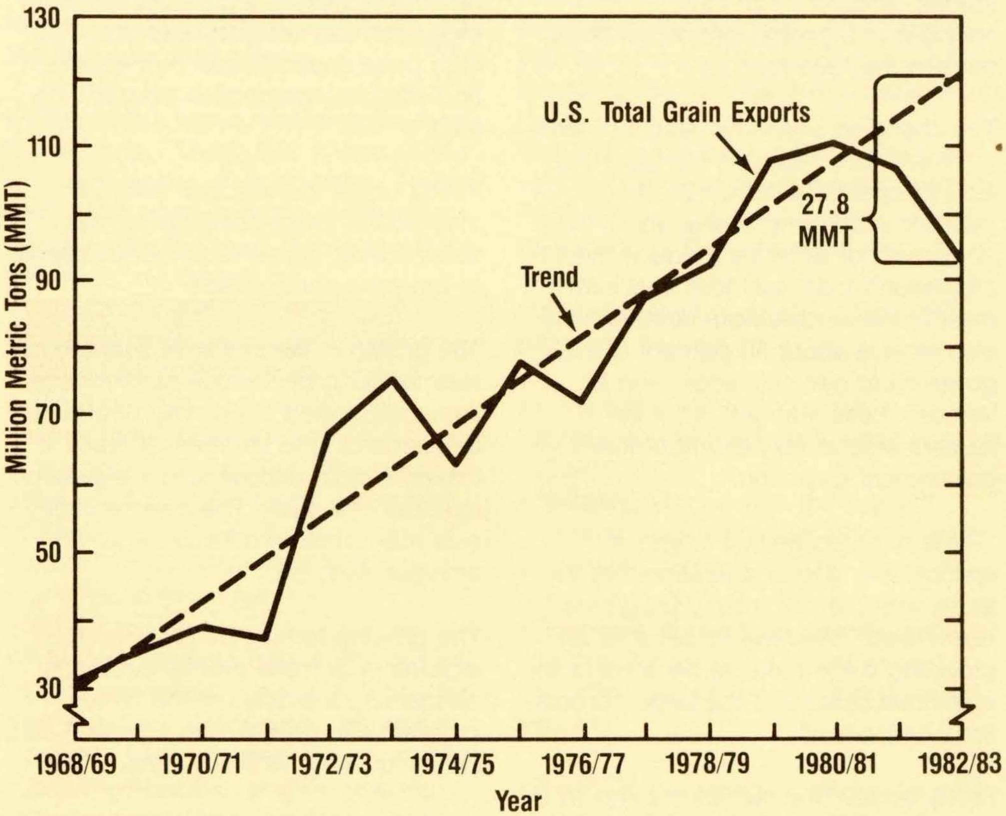
George Hoffman

U.S. foreign exchange. "Agriculture is the only sector that gives us any sort of trade balance," Dunmore said.

Around a quarter of U.S. farm income is attributed to exports, which pass through 15,000 rural elevators and 489 grain terminals and over 4.1 million miles of roads, acording to Dunmore. He pointed out that before the excess capacity occurred at handling facilities an additional $1 billion in exports could generate 35,000 new jobs.

Dunmore placed the blame for the export decline on several factors:

## Decline in 1982/1983 U.S. Grain Exports




Graph, based on U.S. Department of Agriculture figures, illustrates the decline in U.S. grain exports.

• Global demand is weak because developing countries have accumulated too much debt. Pointing out a humorous contradiction in international finance, Dunmore said, "If you as a farmer go in and take out a loan and can't repay it, you're in trouble. If a developing country takes out a loan and can't repay it, the bank's in trouble."

• U.S. price competitiveness has declined as farmers have produced more for stocks rather than a market.

• The strength of the dollar has increased the price of exports.

• Competitors have been subsidizing their exports. The European Community, once a substantial importer, is now an exporter.

• The 1980 grain embargo sent a signal to competitors to increase their production.

Seeing the end of the PIK program, Hoffman is fearful that the projected 36 percent production increase for 1984 will significantly influence the 1985 Farm Bill. "The fear is that we base long-term policies on short-term conditions," he said.

Hoffman maintained that the 1981 Farm Bill was not flexible enough to handle the problems in the early 1980s.

Hoffman emphasized that "commodity prices determine what our trade policies will be. He pointed out that for every acre of wheat idled under the PIK program "our competitors have added more than one acre."

"If the U.S. wants to participate in the world market, it must be among the lowest cost producers," he said. "This conflicts with higher support prices. If U.S. prices are greater, others will sell it for less and U.S. stocks will increase."

Hoffman predicted that, regardless of the farm bill's contents, economic factors, such as interest rates and exchange values, will be more important in determining the health of the agricultural economy.

Michel Petit

### A European's Perspective

"We are on a very serious collision course," said Michel Petit, a professor of agricultural economics from Dijon, France.

Petit defended the European Community's policies of export subsidies saying they do not violate the rules of the Common Agricultural Policy agreed to by the United States and the European Community. He cited the U.S. use of such subsidies in its exporting of flour to Egypt, once a French flour market.

"As we have modernized at a very rapid rate, we have developed overproduction," he said. "We pay export refunds and export subsidies and that causes a problem with you."

"The key criticism is that we do not follow the rule of comparative advantage," he continued. "As we subsidize, we distort the laws of comparative advantage."

Petit maintained that the "institutional rigidity" of the European Common Market has hindered efforts to reform the European Community's agricultural policies and also complicated talks with the United States. "Nobody has the power to cut a deal," he said.

While European farmers, much like American farmers in the past, have enjoyed strong support from countrymen, dwindling financial resources could threaten future subsidy programs, according to Petit.

The Europeans' agricultural policies need to be reformed much like American farm policies, Petit said. French and Italian farmers currently are worried about Spanish and Portuguese farmers joining the European Common Market and bringing with them commodities already over-produced in the community, according to Petit.

Petit anticipated that a ceiling will be placed on subsidies but he is not optimistic that they will be entirely suppressed.

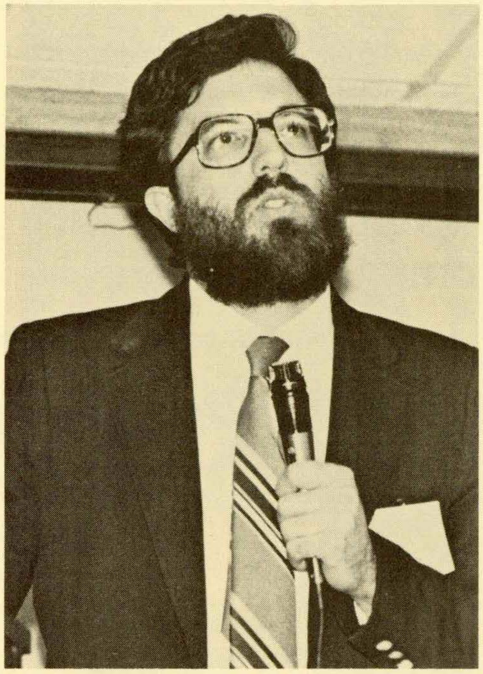
# New Technology: Implications for Policy

## Scientific Breakthroughs Could Complicate Policies in the Future

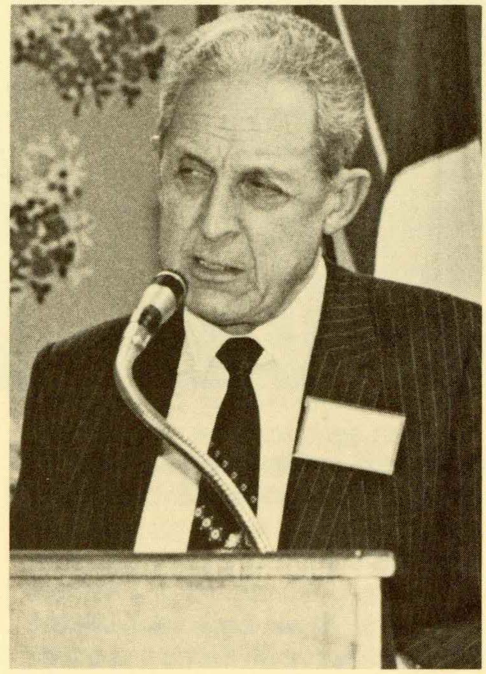
High technology is beginning to change agriculture, according to a plant physiologist from Michigan State University and an economist from Washington, D.C.

"We are now seeing a transformation in the western world agriculture from a resource-based to a science-oriented industry; and from a traditional to a high technology sector," said Sylvan H. Wittwer, director emeritus of the Agricultural Experiment Station at Michigan State University. "U.S. agriculture will probably maintain its technological leadership."

Felix Spinelli, an economist with the Economic Research Service, pointed out that if the technologies are not developed here, they most likely will be developed elsewhere. "Bio-tech firms, for example, exist in Europe," he said. "So if we don't move on increasing our efficiencies, our export share in world markets could be gone—for good."



Felix Spinelli



Sylvan Wittwer

Wittwer cited five advantages that the United States enjoys over the rest of the world:

• A climate-soil-water resource in a vast corn-grain belt adapted for stable high production without equal in any other country.

• A free enterprise system that fosters the profit motive and provides incentives to produce.

• A unique land grant university system and philosophy with a federal-state partnership of more than 100 years' duration with its linkages and coordinations of teaching, research, and extension in each of the 50 states, plus the Tuskegee Institute and the 16 traditionally black 1890 colleges.

• A progressively vibrant privately supported agricultural research and development sector equal to or surpassing in importance the public support of food and agricultural research. This sector also provides a vast infrastructure for food processing, mechanization, chemical supplies, credit, and trade.

• The asset of the English language. English is rapidly becoming the universal communication vehicle for business and science.

"The new agriculture will achieve almost all future increases in production as a result of increases in yield and from growing additional crops during a given year on the same land," Wittwer said. "There are no other viable options. The technologies that will make this possible must be developed today."

Among those technologies are improved pest-resistant and environmentally adapted crops, appropriate mechanization, genetically engineered vaccines, growth hormones, and super plants achieved through cloning, according to Wittwer.

Spinelli pointed out that cell regeneration, which allows a single cell to grow into a whole plant, is currently being used to breed new varieties of asparagus, rapeseed, cabbage, citrus, sunflowers, carrots, cassava, alfalfa, millet, endive, clover, tomatoes, potatoes, and tobacco. Researchers are currently working on regeneration schemes for corn, wheat, and soybeans.

The revolutionary field of gene splicing has enabled researchers to transfer the positive traits of one plant to a completely different plant species, according to Spinelli. "This technology has also been applied to transfers between animal species and last year permitted scientists to transfer traits from an animal species to a plant species," he said.

Genetic breakthroughs have brought U.S. livestock producers to the point where "the future is now for animal agriculture," according to Wittwer. "Semen preservation, pregnancy detection, multiple births, superovulation, and nonsurgical embryo transfer and implantation are now realities," he said.

These developments have already influenced the dairy industry. For example, Cornell University economists estimated that the emergence of bovine growth hormones alone had reduced the market clearing milk price from $10.50 per hundredweight of milk to $8.50 per hundredweight, according to Spinelli.

Wittwer expected computers to play an increasingly greater role in management decisions, improved communications, programming of operations, new sensors, and instrumentation. "We are currently hardware rich and software poor," he said.

As technology enables farmers to produce more placing downward pressure on prices, farm programs will be influenced, according to Spinelli. "Most farm programs were designed when production increases were modest and when U.S. agriculture lived in a vacuum as far as world trade was concerned," he said. "This is not the case today."

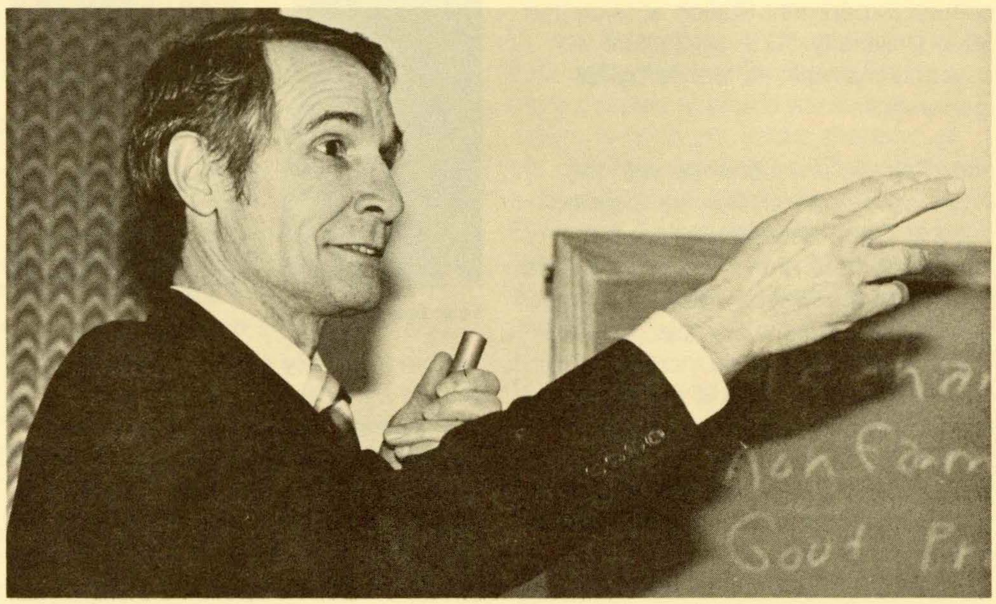
While policy makers may have one eye on the growing federal deficit, Spinelli urged them to protect producers and, yet, also allow real farm prices to be determined by market conditions.

## Changing Structure of Agriculture and Impacts on the Rural Community

### Migration Off Farms Shifts Dependence to Nonfarm Income Opportunities

The dramatic change in the structure of American agriculture has heightened the importance of nonfarm income to farm families and rural communities, according to two Washington, D.C., economists and a Missouri sociologist.

Lyle P. Schertz, an economist with the Economic Research Service, pointed out that around 60 percent of today's farm families derive more income from off-farm sources than from their agricultural effort.



Lyle Schertz

Daryl Hobbs, a rural sociology professor at the University of Missouri, revealed that only 6 percent of rural income in 1980 stemmed from farming. The other major shares of rural income, according to Hobbs, were manufacturing, 19 percent; land income, 15 percent; government employment, 14 percent; and transfer payments, such as Social Security, 11 percent.

"Agriculture was the economic base of the rural community," Hobbs said. "If you change the economic base, then you change the character of the community. This is not to say that agriculture has declined; it is that other industries and economic diversification have occurred."

With the aid of conference participants, Schertz stressed seven forces that have affected the way U.S. farms are organized and managed:

Fred Hines, left, responds to question while Daryl Hobbs listens.

• Inflation increased (1) the wealth of those who own land, (2) the demand for land, and (3) input prices.

• Increases in farm product exports led to (1) a sharp increase in farm earnings in the 1970s, (2) the opportunity to realize politically acceptable prices and farm income with only modest restraints on production, and (3) relatively strong markets for soybeans and corn. This impact led to a greater specialization in corn and soybeans in the Corn Belt.

• The availability of capital-intensive new technologies has enabled some individuals to control larger amounts of production resources. The increased use of such technologies has decreased labor requirements.

• Nonfarm employment opportunities have facilitated the shift of farm people to cities.

• The availability of institutional credit for the purchase of land and capital goods combined with other economic forces gave a competitive edge in buying land to persons with sources of money other than the land being purchased.

• Commodity programs supporting farm product prices have accelerated the shift to larger farms by reducing the risk (1) to people aggressively willing to accumulate land and/or invest in capital goods that facilitate large-scale production, and (2) to lenders willing to extend credit to these kinds of people.

• Tax rules applicable to incomes and estates have increased the attractiveness of owning farm assets and led to (1) larger investments by nonfarm people in farm assets, (2) larger farms owned and/or operated by those farmers who are able to exploit tax opportunities, and (3) more corporate farms.

Hobbs recalled how his hometown of Badger, Iowa, once contained a creamery, hardware store, bank, lumber company, grain cooperative, several grocery stores, a barbershop, and several other retail outlets. While many of those services no longer exist within Badger, the community's population has still risen.

Daryl Hobbs

"Twenty years ago, we were talking about how small towns were going to die, but they didn't die," Hobbs said. Instead, he pointed out that industries have located in rural areas and more residents commute to nearby cities.

Many of these new employment opportunities have been grabbed by small farmers. "Where once small communities existed because of the agricultural economy, today's small farms exist because of the community's economy," Hobbs said, citing the migration of such industries as the textile industry to the rural south, the shoe industry in St. Louis to rural Missouri, and the meat-packing industry from large Midwest cities to smaller towns closer to livestock areas.

"There has been a tremendous diversification of the rural economy across the country," Hobbs said.

This "blurring of the lines between agriculture and nonagriculture" in rural areas complicates the policy-making process, according to Hobbs.

Hobbs contended that no longer can policy makers simply address problems in rural America with agricultural programs. He stressed the need for more rural economic development solutions to keep small communities viable.

### Differences Between Northern Iowa and Southern Minnesota

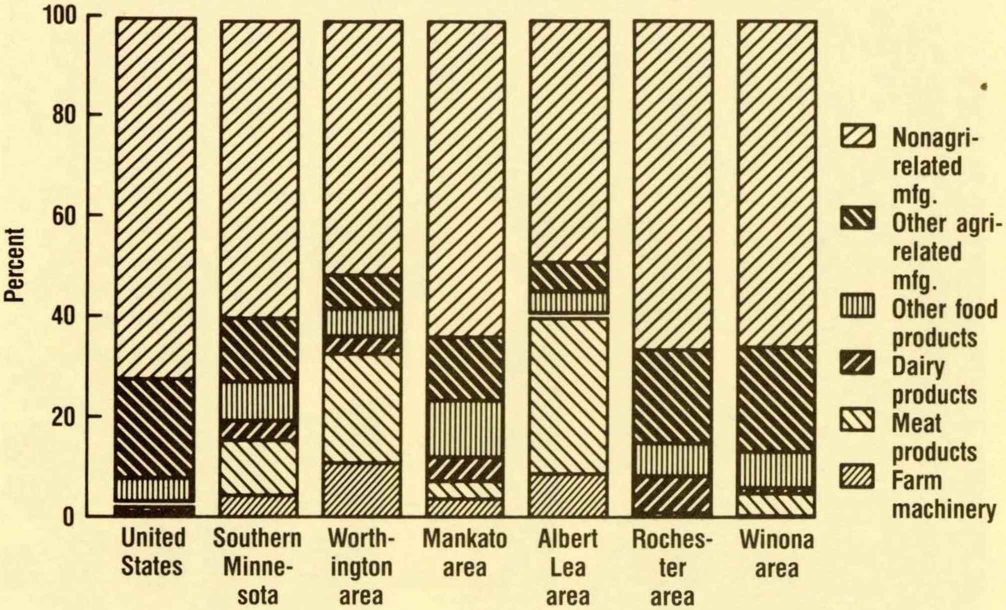
Farm operators in southern Minnesota are more likely to be a full owner of their land, to be older, to have a smaller farm, and to have a lower debt-asset ratio than farmers in northern Iowa, according to Schertz.

Southern Minnesota farmers fall into the following ownership patterns: full owner, 58 percent; part owner, 29 percent; and full tenant, 13 percent. On the average, they are 50 years of age, farm 243 acres yielding $50,000 in annual farm sales, and have a debt to asset ratio of .16.

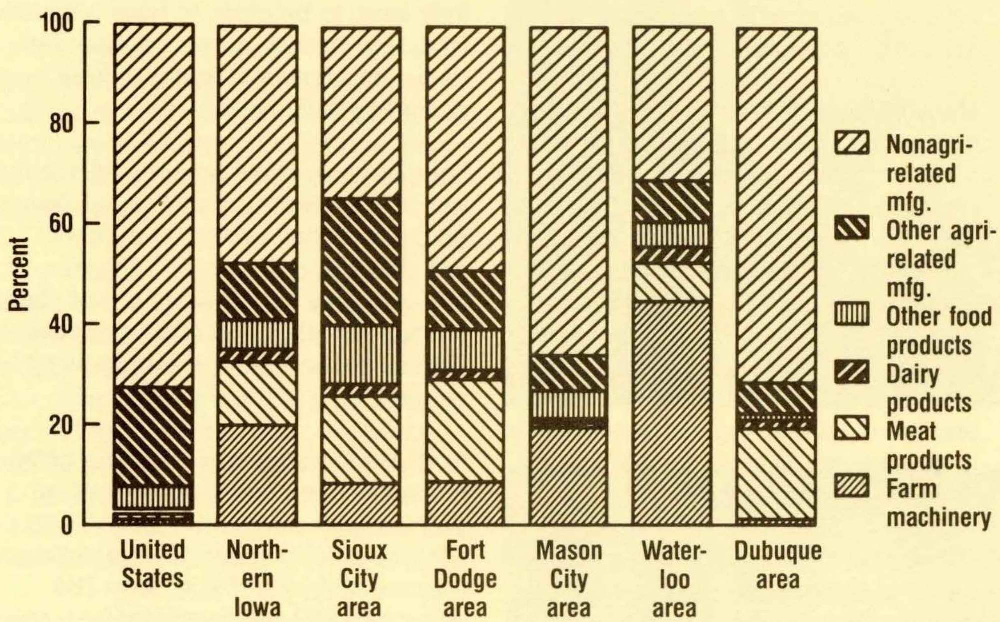
Northern Iowa farmers fall into a different ownership pattern: full owner, 38 percent; part owner, 40 percent; and full tenant, 22 percent. On the average, they are 46 years of age, farm 284 acres with $92,000 in annual farm sales and have a debt to asset ratio of .22.

Fred K. Hines, an economist with the Economic Research Service of the USDA, pointed out that the U.S. population grew 11.3 percent from 1970 to 1980, but northern Iowa's population increased 1.0 percent after falling by 1.3 percent during the 1960s. The Waterloo metropolitan area population climbed 4.6 percent during the 1970s, while the Fort Dodge area population fell by 5 percent.

## Distribution of Manufacturing Employment in Southern Minnesota and the United States, 1979




## Distribution of Manufacturing Employment in Northern Iowa and the United States, 1979




Graphs show the distribution of manufacturing employment in northern Iowa and southern Minnesota.

In southern Minnesota, the population climbed 2.9 percent during the 1970s and 3.1 percent during the 1960s. The Rochester metropolitan area led the way with 9.4 percent in the 1970s and 28 percent during the 1960s. The Worthington metropolitan area population fell 3.2 percent during the 1970s and 5.2 percent during the 1960s.

Hines showed that the two areas had similar educational attainment levels with 13.6 percent of southern Minnesotans having graduated from college and 67.6 percent graduating from high school, while 12.2 percent of the northern Iowans graduated from college and 69.4 percent graduated from high school. Across the country, 16 percent of Americans earn college degrees while 66 percent graduate from high school.

While the national incidence of poverty stood at 12.4 percent in 1979, the northern Iowa rate was 10.3 percent while the southern Minnesota rate was 10.9 percent.

About 40 percent of the two regions' workers are employed in farming or agribusiness, while the national figure is around 20 percent. The two regions nearly match the national averages for employment in manufacturing and nonmanufacturing.

While the national unemployment rate stood at 5.8 percent in 1979 and 9.6 percent in 1983, the jobless rates were 4.6 percent in 1979 and 8.7 percent in 1983 for northern Iowa and 4.0 percent in 1979 and 6.7 percent in 1983 for southern Minnesota.

Hines's statistics showed a dramatic shift in the structure of banking, as the proportion of independent banks in northern Iowa has shrunk from 76.7 percent in 1974 to 37.3 percent in 1983. In southern Minnesota, the proportion of banks has dwindled from 75 percent in 1974 to 41 percent in 1983. Meanwhile, the percent of agricultural loans made by one-bank holding companies has increased from 18.9 percent in 1974 to 51.2 percent in 1983 in northern Iowa. In southern Minnesota, one-bank holding companies have increased their agricultural loans from 15 percent in 1974 to 41 percent in 1983.

James Miller, left, explains dairy program, while Boyd Buxton, center, and Brian Sanders, right, listen.

# Commodity Policy Issues and Outlook Policy for the Dairy Sector

## Paid Diversion Program May Not Solve Dairy Producers' Surplus Problems

Like their grain-growing neighbors, dairy producers plunged into a paid diversion program during 1983, but they still may be faced with surplus problems in the future, according to James J. Miller, an agricultural economist with the Animal Research Division of the Economic Research Service of the USDA.

Miller expected 1984 milk production to decline 3 to 5 percent below 1982 levels. When combined with expanded commercial use, he projected that government purchases would be sliced in half, leaving a huge surplus by any standards except during the last two years.

"It is very clear that the paid diversion program will not make the surplus problem magically disappear. A difficult adjustment remains before production and use are brought into reasonable balance," he said. "The challenge for dairy policy is to steer a course between the twin danger of a failure to deal effectively with the surplus problem and a violent price rise caused by corrective measures that are too harsh or applied for too long."

Dairy producers' problems began in 1979, when cow numbers increased for the first time since World War II, according to Miller. Accompanied by increased output per cow, milk production soared from 121 billion pounds in 1979 to 140 billion pounds in 1983. This increase was aggravated by recessions in 1980 and 1982, which softened demand. Surplus removals jumped from 1 percent of marketings in 1978-79 to 12 percent in 1982-83.

"The moral of this story is not that support prices have been too high since 1979—that is painfully obvious," Miller said. "Neither is it that legal minimums necessarily should be set so low that the worst possible outcome can be handled with no problems. The moral is that legislation should not rigidly require the level of support price expected to be appropriate. Conditions can change with blinding speed. Some escape valve must be provided."

Dairy farming, like other sectors of agriculture has moved toward a more specialized form of commercial farming. Since 1940, the number of farms with milk cows has declined to 300,000 from 4.5 million. Of the current dairy farms, 21,000 of these produce 43 percent of the milk delivered to the federal order system.

The Northwest and Southwest regions of the United States have significantly expanded their milk production, revealing a comparative advantage over dairy producers in the Midwest and Northeast, according to Boyd M. Buxton, an agricultural economist at the University of Minnesota.

Large-scale drylot operations with herds of over 2,000 and as many as 10,000 cows have been established in California, Arizona, and New Mexico posing challenges for producers in Minnesota, Wisconsin, New York, and other northern states, according to Buxton.

Buxton pointed out that these new areas are now supplying not only fluid markets but are also manufacturers of milk products, as plants have been constructed in California and Texas.

Buxton, who recently participated in an economic analysis of dairy production in Minnesota, Arizona, New Mexico, and Washington, found that the rate of return on a dairy investment was significantly higher in the Southwest and West. By reducing per unit production costs associated with buildings, machinery, and land and increasing production per cow, western producers realized returns ranging from a low of 7.3 percent in Washington to as high as 19.9 percent in various scenarios of the Buxton study. Minnesota's returns ranged from 1.5 to 6 percent.

This advantage has helped reduce the number of Minnesota's dairy cows by 18 percent from 1970 to 1980, according to Buxton. "The dairy belt in Minnesota is being tightened as resources move into corn and soybeans," he said.

## A Dairy Perspective from New Zealand

Once known as "Britain's farm," New Zealand is fighting now to keep markets open for its dairy products, according to Brian Sanders, the second secretary with the New Zealand Embassy in Washington, D.C.

While the European Community's agricultural policies have hurt the United States, they slapped New Zealand in the face, according to Sanders. "They caused New Zealand to open its eyes for the first time," he said.

New Zealand shipped 50 percent of its exports to Great Britain prior to 1973 when Britian joined the European Community. Since then the British share has slipped to 12 percent.

With 25 percent of its gross national product devoted to exports, New Zealand has targeted the Middle East, Latin America, and Far East markets to maintain its dairy exports. While New Zealand owns 25 percent of the world dairy market, Sanders pointed out that a 7 to 8 percent increase in Soviet dairy production would account for the entire volume of New Zealand exports. "This illustrates the vulnerability of exporters," he said.

While access to European Community, Japanese, and American markets are limited to New Zealand by quotas and price levels—Sanders could foresee "no windows of opportunity for American dairy exports."

The typical New Zealand dairy farm is operated by husband and wife teams owning about 140 cows, which graze about 75 hectares of grass and clover, according to Sanders. New Zealand dairy producers, like their American counterparts, have also experienced a decline in numbers. In New Zealand, a 35 percent reduction has occurred over the past 16 years.

The average income for a New Zealand dairy producer in 1983 was $12,500, but that amount is expected to fall to $8,500 primarily because of the downturn of dairy prices, according to Sanders. The New Zealand Dairy Board, which governs the country's production, earned a $275 million profit in 1983 but is expected to lose $27 million this year, Sanders said.

New Zealand's dairy sector has been hurt, according to Sanders, by the following factors: the growing debt of developing countries; the expectations of developing countries that the United States will sell products on concessional terms or donate products from surplus supplies; and the domino effect of lower U.S. prices.

"The U.S. has shown considerable sensitivity to New Zealand," Sanders said.

Sander expressed New Zealand's desire that the world trading system remain open to allow the participation of agricultural producers that possess a comparative advantage. He also urged that export subsidies and price supports be more seriously considered before being implemented. "Export subsidies are destabilizing," he said.