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Escaping 1980
Episode 5 – The USDA Steps In

<u>Brent Gloy</u>: The government's got a lot of grain. If you don't grow grain on your farm this year, we'll give you some of ours and you can do with it, whatever you want. You just think about idling, 83 million acres of crop land today. That was the policy solution in the 1980s.

<u>David Widmar</u>: A lot of times we hear supply management or acreage reduction programs are bad because they manipulate the market and, I think, we have to step back and say, this wasn't something lost on decision makers. This was the whole point.

<u>Sarah Mock</u>: Within the culture of farming in the U.S. there's a paradox, and it's been there for centuries. American farmers and ranchers are the very picture of rugged individualism in the nation's collective consciousness. They value private property and the near absolute freedom to protect it. Privacy, a strong work ethic, pride and famously, when in need of support, are looking for a hand up and not a handout, but the thing, is American agriculture has needed a lot of hands up over the last 400 years - trillions of dollars' worth to help overcome everything from weather disasters, to bad soil management, to overleveraged investments. The U.S. taxpayer, by way of federal, state, and local governments, has consistently been there to offer those hands up by way of land grants, public investment, and research and infrastructure, tax deductions, special accounting practices, and eventually direct payments to farmers. Ronald Reagan, whose presidency spanned from 1981 to 1989, in a lot of ways embodied this paradox, his famous quote:

<u>Ronald Regan</u>: "The nine most terrifying words in the English language are, 'I'm from the government and I'm here to help."

<u>Sarah Mock</u>: Was belied by the actual actions of his USDA. He not only sent government agents or the government's money to just about every farm in America, he did it to do exactly what he claims here to be terrifying - to help. The federal foreign policy of the 1980s represented some of the biggest direct payments and government intervention ever attempted in the farm economy and yet there was, and remains, enormous animosity from the ag community towards the government and its agents. Reagan, by his own accounting, would have been exactly the kind of interventionists that he despised. This is the paradox, and we continue to exist within it today with the policies embodied in the farm bill.

<u>Brent Gloy</u>: The farm bill's been around for a long time and it's, it traditionally has been [the focus of most of the policy that was directed at the farm sector. Agricultural products have long been viewed as a place where there's some justification for having policy in the sense that some of them are perishable, there's a long production cycle, and then food was viewed as something that was essential for America to have. It's normally written every five years and it came out of the Great Depression when a lot of social programs sprung up and it was designed to try and fix some of the ills at the farm sector, but it covers all kinds of stuff. It's not just corn, and soybeans, and milk, and cotton, and sugar, and all those other things. It covers the environment and forestry, and, of course, the biggest component today's farm bill in terms of expenditures, is on the food side. And I think the farm bill has always been a compromise between rural legislators who have a real strong interest in agricultural issues and urban legislators who may have more interest in the food provision side of the farm bill. So, it was a grand compromise and it's honestly, that has made it possible to keep the farm bill going for as long as it has.

David Widmar: It's a grand experiment, right. There are efforts and tools that are put into place to try to solve a set of challenges that are at the forefront of thinking at that time. Those are the grand themes, but along the way, there are Iterations. And so, you think about crop insurance as a policy that was started, and grew, and changed, and it moved - it's morphed its way into what it is today. But it took several years of experiments and adjusting to see that play in.

Sarah Mock: The farm bill a lot since the 1970s and 80s and had already changed a lot since its original incarnation in 1933. It's meant to change and adapt. It expires every five years to give lawmakers a chance to craft policies according to the circumstance of the day. But the thing about lawmakers is, they're not fortune tellers and rarely are they as focused on the threats of the future as they are of avoiding a repeat of the past, which begs the question - is our modern farm policy prepared to prevent the next farm crisis or the last one?
This is Escaping 1980 - the farm crisis that was, and how to avoid the next one. I'm Sarah Mock. Today we're discussing how the USDA stepped in during the 1980s and what those actions have meant in the years that followed.
Some of the clearest evidence that lawmakers are not fortune tellers is the 1973 farm bill called the Farm and Consumer Protection Act. It provides strong evidence that policy makers were still struggling to understand how the Russian Grain Robbery would play out in the future. It reflected the current administration's perhaps falsely optimistic idea that the good times might just go on forever and the bad could be kept at bay.

David Widmar: The 1973 farm bill was written in the backdrop of Russia just came and bought all of our wheat and books written were saying, "The Great Grain Robbery" that they stole this wheat crop. They surprised us. And prior to this, the farm bill was still working out of these, this parity situation and this New Deal era policy. And so, 19, this 1973 farm bill started to change a lot of the way farm policy was starting to take root and try to adjust and evolve and "Plant fence row to fence row," is one of the slogans that came out of that. And it started this car conversation around how can we, as America, produce the safest, most abundant, and the cheapest food supply in the world? So, it was very starting to get more in this production side.

Sarah Mock: We know, with the benefit of hindsight, that this obsessive focus on production would be the bane of the farm sector, not just through the 80s, but up until today. But policymakers at the time didn't have that knowledge. They only had their own history to look back on. Since the first farm bill Congress and the Department of Ag - the writers and implementers of the farm bill - had explored many different strategies for dealing with the often-problematic swings of agricultural commodity markets. The basic idea behind many federal farm programs, prior to this era, revolved around the government, through the USDA, participating in the free market. It assumed that supplies of grain, and some other farm products, are going to fluctuate dramatically for a number of unpredictable reasons. Here's Brent.

Brent Gloy: We were producing a lot more stuff. In fact, we had government programs in those days that were designed to help smooth out the cycles and what they would do is buy excess commodities and put them in storage so that when prices were low, they put commodities and storage on prices got high they took them out of storage and put them on the market. So, it was designed to kind of buffer some of those cycles.

Sarah Mock: Most of the time surpluses are the problem. Because remember, supply of commodities has been outstripping demand for well over a century. Hence the continuous decline in commodity prices.

Brent Gloy: Occasionally though we get little blips of time where surpluses aren't necessarily a problem as food gets tight. Because agriculture has such a long production cycle, it's difficult to manage all of those things. But generally, what you see is that the few periods of tight supplies lead to a whole bunch of years where we've got excess.

Sarah Mock: The fence row to fence row idea of this time work to fuel that accumulation of excess commodities even more, elevating corn and wheat stocks by the 1980s to almost unimaginable scales.

David Widmar: stocks hit sort of record lows globally in the beginning of the 1970s, by the time we got to the 1985, 1986 global stocks reached a high about 30% and so there's a lot of grain across all crops around the world. We've never been back to those highs at the global level. It's really mind-blowing to see how the stocks played out at the U.S. and the commodity level.

Brent Gloy: What on earth are we going to do? How, how are we going to find demand, find a home for all these commodities? You could have an absolute disaster of a crop and not see any improvement in price - you still have plenty. You could grow half a crop and still have plenty, or two-thirds of the crop. So, they came up with a program to manage that.

Sarah Mock: The drying up of those surpluses during the Grain Robbery years triggered the price climb and expansion, but by the end of the decade, surpluses were back, and the Russian grain embargo made them even bigger. The first line of defense at USDA was re-tendering or reselling that grain around the globe.

David Widmar: One of the first plans that came up when they said the embargo with Russia was to idle acres in 1980, and for a lot of government funding reasons, they said, "No." And so, the USDA worked really hard to find a new home for this grain, sort of, we're going to keep that grain flowing out of the country, we'll solve it that way.

Sarah Mock: The PIK program - short for Payment in Kind - was just the beginning of a massive agricultural policy response meant to help shore up the farm economy in its darkest hour. It was a program that spurred and continues to spur countless pearl-clutching conversations on cable news and in coffee shops about farmers being paid not to farm. And it sought to fundamentally transform the relationship between the federal government and the farm sector. At the heart of the PIK program is the assumption that in the farm economy, there is a chronic state of overproduction. Because of this, it doesn't make sense to try and balance the good years with the bad, because there are just too many good or production years to be offset by the low production, unlucky years. So instead, what if the government simply skip the middleman? The middleman here being the crop itself, and just paid farmers directly to do what the government was doing by buying and storing grain. Taking supply out of the market. Farmers could do that by not planting, or idling acres.

Brent Gloy: We started taking land out of production at that time through set aside, and then the payment in kind, or the PIK program was developed to solve it. And basically, what they did is they said the, "Government's got a lot of grain. If you don't grow grain on your farm this year, we'll give you some ours and you can do with it, whatever you want." And it's called the PIK program. And so, farmers idle acres, something like 30 million acres of corn got idled that year

David Widmar: But 1983, they decided they needed to use this program to get producers to pull back on supply. And the goal of the PIK program in 1983 was to reduce production, reduce ending stocks for commodities, ease the storage problems - the government of course played a big role in the storage - and to ensure adequate supplies of commodities at all times, increase net cash farm income, and, over the long-term, minimize government program outlays. And so, they stepped in and they started to adjust supply. And I think that was something that was different as we rolled into the 1980s.

Sarah Mock: And in 1982, the USDA had the authority to pay farmers to do just that - idling more than 27 million acres. But just a year later, they realized even this dramatic move would fall far too short.

David Widmar: When they got to 1983, they realized it wasn't going to be enough. So, they actually using the CCC funds and the grain reserve programs that they had found a way to put another 49 million acres into idle.

Sarah Mock: In 1983, nearly 80 million acres of crop land were idled. For context, today in the U.S. we plant a little over 90 million acres of corn. Imagine eight out of every nine cornfields in America, standing empty for a year - this was unprecedented. But of course, it also wasn't the end of the story. When it rains, it pours, or in this case, it doesn't rain at all.

David Widmar: And then we turned around, had a drought and we had a pretty tough drought and we, all of a sudden, went from ending stocks that were at about 50% at the end of 1982. We all of a sudden fell below 20% in 1983 and so that program lost some of its appeal. By the time we got to 1984, they actually discontinued the program in 1984. And there's always an element of unknown when you take on such a program. In this case, there was a big drought and that sort of piled on top of the supply management program. And so, that might've have worked a little too effectively, right given the way that yields played out. But at the same time, there were elements that the 1983 efforts for the initial PIK program kind of fell flat or caught a lot of bad press when we turned around and had the drought. That was really hard to sell to the public. With hindsight, it's easy for us to look back and say, "Oh man, it was not a good situation to implement this big reduction in acres in 1983 because there's drought." But when they were making that decision in January 1983, they had 50% ending stocks on the books, right? And they were saying, "We're, what's going to happen if we have just an average year?" And they were really concerned about that. So, they were making decisions in that timeframe with the best information that they had and there's always the role of chance, or the role of luck.

Sarah Mock: To add insult to injury, following the drought and all the negative attention that led to the ending of the PIK program, the latter part of the decade played out like a rerun of the early years with mind-boggling stock levels.

David Widmar: But then by the time we got to 85 and 86, corn stocks actually got above 60%. Now, keep in mind, we were worried at the beginning of this year and 20% is always in the back of our mind as a doomsday scenario here in 2020. So, corn stocks were three times the relative level at 60% of use in 86 and 87. Wheat stocks actually touched right around a 100% - wheat stocks are always high, but wheat stocks actually got to a 100% t at the same timeframe. And these were the two big crops. USDA then again, started using another version of that PIK program they were using in 1983. They, again, in 88 and 89 got more than 70 million acres idled. The 1985 farm bill pulled in the CRP or the conservation reserve program. And so, there's a combination of a lot of levers being pulled, but that CRP was sort of a long-term attempt to idle acres on a more strategic basis and less of an ad hoc annual basis.

Brent Gloy: We come up with the conservation reserve program, which puts, I think somewhere around 35, 36 million acres in pseudo-permanent grasslands, ten-year contracts, I believe, at the time. So, we're into this policy era where we’re like trying to like slow production down a lot because we just got way too much. You just think about idling, 83 million acres of crop land today. That was the policy solution in the 1980s, but it's just, in my mind, almost unbelievable to think about that kind of policy. They knew they had to do something, and they had to take a step that drastic to stabilize things. And I'm not saying it was the wrong policy response. I'm just saying it was massive.

David Widmar: And then to do it in 1983 to come back and do it almost to the same scale in, I think, 85 and 86, and then to roll out long-term. 30-million-acre reserve program - It was a very significant problem, and the response was equally large.

Brent Gloy: Yeah. These severe situations call for substantial solutions. And so, the size of the solutions gives you some idea of how big the magnitude of the problem was. When you combine the amount of direct money that went to the farm sector throughout the 80s, plus the amount of money that was contributed through acreage reduction and other types of programs, it was just absolutely massive.

Sarah Mock: The supply management strategy that the PIK program represents is pretty starkly different from the ones that are common in modern farm bills. And it has its limitations. One of the primary ones being that it takes time to take effect.

David Widmar: We were trying to manage supply and that takes time. We were trying to pay producers to not plant a crop and then that would translate into, hopefully, a better ending stock situation down the road, which would then raise prices. There's a big lag in that side of the policy. By the time we got to the end of the decade, ending stocks start to come back to more normal levels. There's still a very heavy hand from the government in terms of managing supply. Of course, the conservation reserve program crosses 30 million acres by about 1990. There's still another 30 million acres being controlled or pulled out of production through other programs, such as the acreage reduction program. And so, we start to see some stability on the production side, and that starts to provide some stability on the production side and that starts to provide some stability in the price and the income side.

Sarah Mock: Although, the PIK program wouldn't survive the 1980s, the conservation reserve program, its companion in some ways still exist today. And that's not the only legacy program of the era.

David Widmar: There's the LDP payment, right? The loan deficiency payment, which was a big part of foreign policy throughout the 90s.

Brent Gloy: And we haven't even talked about the family farm bankruptcy provision [that] was written into the bankruptcy code - chapter 12. That was a new development that was put in and it had some provisions that made it. If you had the alternative of filing under the family farmer provisions or just the general bankruptcy code, you would most likely choose the family farm section of the code to file under because it had more favorable work-out provisions in it for farmers. And so, chapter 12 was another kind of innovation or policy response that came out of the 80s that's still with us today. And in fact, is brought up frequently about whether it needs to be modified and they did just modify it again and increased the limit.

David Widmar: Again, even the changes that took place in the credit and the financing side of things and how the government tried to make funding available to help those credit markets for ag lending to continue to function in the midst of all the chaos. And so, there were policy efforts during the 80s that extended beyond the farm bill.

Brent Gloy: The way lenders regulate banks, particularly ag banks, changed the way they evaluate credit risk in banks and the farm credit system. The way the farm credit administration supervises the farm credit system changed after the 1980s in a significant way. Conservation reserve is an extremely useful tool to right size the production capacity of the United States. But also, I think, it solved some environmental issues. And it really did take some fragile lands out of production. And so, I think, that was a good example of kind of a win-win solution. Now, although the CRP is not without controversy if you come to a place like where I live, or actually a little bit further west, from where I live, it was a very controversial program because huge amounts of acres were taken out of production and put into conservation reserve. That had a big impact on some of these communities because you're taking the situation where your farmer's buying fertilizer, and seed, and farming the land, and hauling the grain in town, and all of that kind of stuff into a situation where he plants the grass on it and it kind of sits there. And so, some of these rural communities really felt the brunt of that program from an economic perspective. But all of these solutions have trade-offs, right. And as much as we want to avoid trade-offs, we can't.

Sarah Mock: Over the years, since they were first introduced, these programs have certainly had their detractors, but David points out that they were solutions that made sense in their time.

<u>David Widmar</u>: I think it's really challenging for us today because we don't really know what 60% ending stocks on corn look like, and that's what we were facing. And when wheat was at a 100%, so you could not plant a wheat crop and still have enough in inventory to meet all of the projected usage. So that was just a really hard reality. And since then, right, over time, trade has evolved. … Think about the world's trade negotiations that were taking place, we've stepped away from price support and supply management over time for a host of reasons. Part of it was the WTO agreements that we've been negotiating, I don't know, late 90s, early-2000s. So, there's been a big evolution that took place.

<u>Brent Gloy</u>: Systemically large commodity stockpiles is a real challenge to deal with because the answer is pretty clear – you either use more of it or produce less of it. And eventually people produce less of it if you let the market go. Because people will stop producing at some point and it just become so unprofitable that they quit producing and people don't want to see that kind of carnage that would cause. So, we try and smooth it out, but it's really difficult and the 80s helped illustrate that.

<u>Sarah Mock</u>: Before we start working out what conclusions we can draw from the 1980s' farm policies, it's worth remembering that the farm bills of the time, like the farm bills of today, are little more than experiments. Well-informed experiments, but still just experiments. We don't know how these programs are going to work before we do them. We have ideas about economic theory, we have programs in other industries that may be similar, but, in essence, we just really don't know how any of these programs are going to work until after they're implemented. From the very first farm bill with its focus on parity pricing, through grain purchases and the PIK program and into modern crop insurance and conservation reserve programs, the problem with all of these as Brent said, is that all of these solutions have different trade-offs. Every policy has its own intended and unintended consequences and choosing a policy means signing up to deal with both.

<u>David Widmar</u>: We don't have a lot of good tools in our toolkit for policy dealing with excess production and systemically low commodity prices and systemically big ending stocks. We don't have, you know, we have a lot of risk management tools, right. But none of them really fix high ending stocks for multiple years and low commodity prices as a result of this oversupply relative to usage. We don't have a lot of tools and we didn't have any then, we don't really have any now. And so, the lever that they were trying to pull and manage was acres of production. At the same time, the U.S. is making some big adjustments, but at the global level, we talked about the run-up in acres in the 1970s, we hit 1980 and we flat line at about 2.1 billion acres harvested annually. Those acres don't leave production. And so, the U.S. is trying to pull 70, 80 million acres out of production, and we can do that, but the global production picture of 2.1 billion harvested doesn't significantly change for two decades until the next farm economy boom happens. Those acres just don't leave production once they're in production. They find other crops, they move around the 13 primary crops, but they stay in production.

Sarah Mock: In today's podcast, we've thrown a lot of hard to fathom numbers at you, but 2 billion acres of cropland under production worldwide pretty much takes the cake. I could tell you that counting every single acre, the U.S. is only 1.9 billion acres. So even if you put every square inch of U.S. soil under production - from city streets to mountain tops - you'd still be a couple hundred million acre short. But what does all that really mean? We've thrown around the idea of idling acres in many different ways so far, but what did that look like for farmers? In essence, it looked like receiving a check from the local FSA office, compensating you for not farming certain acres. And farmers did it, and they continue to do it. Despite all our ideas about rugged individualism, these farmers did not turn up their noses at the direct payments or the financial rule changes or any of it despite the fact that it represented the dreaded government intervention in the free market and at a massive scale. When we look back at these past policy decisions, many are quick to dismiss them as ill-conceived, because they're supposedly more market distorting than our modern programs. But David warns that evaluating past policy is not quite that simple.

David Widmar: There are three ways that our hindsight or looking back on the reality can be short-sighted. The first one is that we judge the quality of the decision by the outcome. And that's really the drought in 1983. There's a lot of feedback that PIK in 1983 failed because of the drought and that's not a good way to evaluate a decision. The second one is failing to consider all the information known by the decision makers at the time. And I think if you, again, look at that 1983 situation, you really have to look at what ending stocks were looking like when they were making this decision. And the third point is, failing to recognize the overall objective. And if we don't understand what the objectives were in the 1980s, and we apply our objectives from today, we can really miss the point as to what they were trying to solve. And a lot of times we hear supply management or acreage reduction programs or acreage idling programs are bad because they manipulate the market and I think we had to step back and say, “That was the point.” This wasn't something lost on decision makers in the 1980s, this was the whole point. And so, when you take our goal from the conversation in the policy area, especially in 1980, is to step back and say, “Hey, things were really bad. And that led to some really big decisions being made. And they were actually trying to manipulate the market.” And this timeframe, 70 to 80 was full of policy decisions. There was the original policy decision that came out of Henry Kissinger and President [Richard] Nixon and Earl Butz to sell wheat to Russia. Off the bat, that was a policy decision. And then there was the embargo. And then there was the initial efforts to shore up the farm economy after the embargo. There were a whole lot of policy decisions, and that's what we want to capture. We want to capture the magnitude of the problem, and the magnitude of the solutions that were used.

Brent Gloy: I think it's an open question and you would get different answers from different people if you asked them, "Did the programs work?" And I think it's going to come down a little bit on the lines of some people believe more strongly in supporting income and controlling supply and other people think that creates a lot of dead weight losses, so to speak and that the market facilitates those activities that result in some people exiting farming and others staying in. So, I think it's somewhat of a mixed bag, but certainly what we can say is that supply control had a much stronger hand in that environment. That was probably the peak of the people who advocated for that, the peak of their kind of persuasive powers to get a policy like that implemented.

David Widmar: If anything, the ag policy situation in 1980s, when you look back at that, it should leave you more curious. I'm reminded of the quote that I heard recently. It was, "Less certainty and more inquiry." And so, we might say today, supply management is bad because it manipulates the market [but] we really have to use less certainty in that statement and more inquiry. How bad was the situation that led them to use those tools?

Sarah Mock: Since the 1980s, the USDA's strategy of dealing with systemic overproduction of commodities has evolved. What do these programs look like today? We'll get into that right after this break.
Escaping 1980 is brought to you by AEI Premium - that's David and Brent. Here's a message about why you should join today.

David Widmar: What's the state motto of Nebraska – "It's not for everyone." So that's sort of like the Ag Forecast Network. It's not for everyone, but some of the ideas that we keep in our mind is, some mottoes we have is - it's for those who want to cultivate their thinking, who want to develop their thinking, or they want to put their own stake in the ground and be their own guru. You've listened to a whole host of experts now, how do you turn all that information into your own opinion? And then the other one we had talked about for the Forecast Network is you win some, you lose some, but you're always learning. One of the elements of it is, it's very humbling if you put a forecast in and it turns up to be flat out wrong. I have some very low Forecast Network scores - Brent does too - but I have my fair share of low scores. We try to learn from myself, but also from others, where did that go wrong? And that's a really important part.

Brent Gloy: Yeah. And I think that the scoring of the Forecast Network questions is really, really powerful because what it does is it allows you to look back and say, "Hey, did I do better than an average on this question or not?" And as David said, it's very humbling because there are many of them that I don't do as well as I would like. Some I've done pretty well on, but it's fun to do that, and it's a fun way to get better at what you're thinking about and what you're forecasting about. I think that's a powerful tool. And then you combine that with all of the other information that's given to you about how do you get better? And I think it's a pretty neat set of things that we've developed.

Sarah Mock: To learn more about becoming an AEI Premium member today. Visit AEI.ag - AEI Premium. Cultivate your thinking.
Now back to the show - the journey from the knee-jerk policy decisions of the 1980s to today has been a long one.

Brent Gloy: We went from the 80s response of acreage reduction to the 90s where we said, "Well, no, we're just going to set basically price floors, and when prices go below that the farmer can get back up to that price." And they just put, they sell their commodity at whatever price they want and then we'll make up the difference. And that's kind of the policy that we're at. We finally found the policy that created a situation where it got rid of a lot of the excess and that was biofuels and it took a while, but eventually production caught up to it. Now, again, we're in this period of surplus. So, this is what we're dealing with is how do you manage in these periods of surplus and low prices? It's going to be really interesting to see if another shift comes in, where we move back to supply control.

Sarah Mock: The focus on biofuels in the late-2000s and on ethanol in particular was as much a policy of its time as the PIK program was representative of the sensibilities of the 1980s. In the years after the terrorist attack of 9/11 the idea of cutting the U.S.'s dependence on foreign oil was a politically compelling one. So compelling, in fact, that it prompted scientists, policymakers, environmental advocates, and rural America to rally around a 30-year-old technology - corn ethanol - that had long languished in obscurity.

Brent Gloy: The air force was leading this effort and they brought in all kinds of people that I would not normally be invited to work with, like engineers, and military strategists, and all these people. And the whole point was like, "Can we develop a drop in jet fuel?" Because they really wanted a fuel source, they could fill their airplanes up with that was made in the United States. And so, we weren't susceptible to oil problems from other parts of the world. Of course, this is before the shale revolution and all this other stuff, right. We did this whole big feasibility talk about how viable is it to produce this much biofuel? And it was really interesting.

Sarah Mock: But just as a lucky combination of oil scarcity and overlapping political motivations led to the rise of biofuels. In the years since the Renewable Fuel Standard's introduction in 2007 much has changed.

Brent Gloy: Again, that same story plays out. We go from not enough oil to too much and now we have, in agriculture, you can't take corn ethanol out. It's 5 billion bushels worth of demand. If you were to take that away, I don't even know what the farm economy would look like. It'd be terrible. 5 billion bushels on, I mean, it's a third of demand. You couldn't get rid of it if you did. You're just going to have absolute chaos.

<u>David Widmar</u>: Keep in mind demand is, we use demand as a pretty open term, but demand is truly a relationship between quantity and price. And one of the lessons from the 1980s is they were still willing. They were still able to move all that grain after the embargo, right. They were still able to re-tender as they called it, but it was at a different price point and so demand wasn't as strong. And I think one of the lessons here is that in the current days, demand and usage and the price are all important to keep in mind. And when you have less corn and soybeans being used and it's at a lower price, that's a really challenging environment.

<u>Sarah Mock</u>: The problem with the farm economy's dependence on ethanol is there's a good chance the policy won't last forever. The political forces that brought the RFS to life are no longer aligned and further ethanol, and biofuels more broadly, have gained a lot of enemies from the oil industry to some consumer groups, to environmental activists. The threat of electric cars becoming mainstream is no longer a science fiction either. And it is likely that ethanol's days are numbered. And as that time approaches, 5 billion bushels of corn, will need to find a new home. That's a scary proposition because in the time it takes for 5 billion bushels to find a new home, farmers will likely need another hand up from taxpayers, but a lot of public capital has already been used in the farm economy since over the past three years, farmers have received around $60 billion in direct payments, ostensibly to compensate for a years long trade war started by the Trump administration. And for the disruptions associated with the coronavirus pandemic. But as 2020 draws to a close, it seems that those payments have largely left the farm economy in an unusually stable position going into the next crop season. Many farmers are even better than stable marking the last three as some of the best farm income years in memory.

<u>David Widmar</u>: It's a big question though. And Brent, I think you would agree, is we have to take the training wheels off. We have a lot of direct payments in the farm economy today and the big question mark is how do we transition from today, which is close to a stable, we're probably very close to that. Then how do we transition to something that might be more, common for direct payments? Because these have been ad hoc, and we don't have a transition to any of these. And so, the hard part is we don't know what 2021 looks like. And then we don't know what government payments are going to look like in that environment. We're treading water.

<u>Brent Gloy</u>: I think if you take the government payments out of this scenario, we're in a real bad situation at the farm level, it would be very, very ugly.

David Widmar: It's really important also to think about this in the context of 2020. The bigger, the problem, the more outside of the box policy solutions start to become. And frankly, we're here with the COVID response, right? A trillion-dollar stimulus would have seen completely unlikely in December 2019. You to put that at almost a zero-probability event. And now here we are in August 2020 wondering when the next trillion-dollar stimulus is going to be coming.

Brent Gloy: What we've seen is the administration come in and provide substantial direct aid to farmers outside of the farm bill. And that is telling you that the farm bill was not written for the kind of environment we're in. In other words, they've deemed the downturn to be too steep and the farm bill to be insufficient to account for how bad the situation is. Or it just says that Congress is really dysfunctional, and they can't agree and do something. Or it says the administration created a huge mess and they're trying to pay their way out of it. It depends on where you line up politically as to how you interpret those things. And I don't want to get into politics other than to say that right now, we're seeing farm payments of a magnitude that we haven't seen for a while. And I think that speaks to how bad the situation has gotten in the United States, but much of it through because of the trade situation. I think without the trade situation, in the short term, things wouldn't have gotten as bad as they got and that's a debatable point as to whether that short-term pain is ultimately going to be worth whatever gain might come about as a result of the trade war. Everybody's got opinions on that as well. But we know for agriculture, when you start monkeying around with trade and making it hard to trade ag commodities, you're going to end up with huge surpluses in the United States because we just produce way too much stuff to consume it all in the United States.

David Widmar: We're talking about an oversupply situation at the sector level. It's not a commodity level. And so, if during a stable era, let's just say in a random year, in a stable period, we had a bumper crop of corn and there was a lot of corn supplies. What would happen is we move some of those corn acres into soybeans or into wheat, but what happened in the 1980s and what's happened in recent years is that there are ample supplies of everything. And so, we're looking for a least bad option. And so, when you have the 80, 60% ending stocks for corn and a 100% ending stocks for wheat, there really isn't an alternative. And so, producers just keep producing it and in the long run with no intervention and no good luck, you would eventually idle acres. Farms on their own would stop planting. That'd be a very extreme case. And, I think, one of the challenges we have today is that when you have these demand disruptions, like trade to China, and maybe a situation where we're using less ethanol. The challenge is, what do we do next year? And there isn't an alternative to move those acres into.

Sarah Mock: Despite being touted as more market-oriented, the modern farm programs, whether they're in the farm bill or not have their tradeoffs as well.

David Widmar: Every tool has a positive, every tool has a negative. And I think sometimes we look at the supply control in 1980 with our lens today and we say, "Oh, that's too market distorting." Now, today we've been using a lot of ad hoc farm income supporting programs, and typically speaking, those have been politically more palatable. And we've been using a lot of those, but I think what you're starting to see here in 2020 is direct payments are near, at, slightly above all-time highs and so, we see large payments being made. And so, as these farm income support programs that they can have an expensive price tag. And so, I think that's going to be one of the challenges with our current suite of tools that we're using in farm policy. It's interesting that actually some of the legislation working its way through Congress, specifically, the House has included some programs that start to look like a smaller scale version of supply management. The soil health and income protection program, which was included in the House-passed Heroes Act starts to take on some of those flavors. And so, I think bigger challenges take bigger and more creative solutions.

Brent Gloy: What are your options? You can continue to pay farmers a target price, and they'll produce to that target price and they probably produce more than we need, and we'll get rid of it and let the market sell it. That's, we've gotten out of the government owning the reserves, we just set a target price and the farmer gets to sell it. So that's one option. And then if that gets unsustainable from a budget perspective, then I think that's where you get into this question of - Are there other ways to get the same outcome? And that's where things like acreage reductions start to become appealing.

David Widmar: The current era of farm policies also has a problem is that they're non-market distorting which is a huge feature, but at the same time, they're not fixing the fundamental problem of overproduction - too much production relative to usage. Now I think in 2019, we got lucky with the big prevent plant. Soybean stocks were supposed to be over 20% based on the early projections in 2019. So, we had some luck on our side and then this year, 2020, we didn't plant 97 million acres of corn. We had another big year prevent plant, and I think the ending stock situation today, here in 2020, would look a lot different if we would have rolled the dice and had favorable weather - bigger crops, more acreage planted. That would be starting to put the pressure on bigger solutions and bigger tools, maybe more controversial tools, that would start to tackle the ending stock situation. Cause that's fundamentally the problem, right? Farm incomes are low, because of low commodity prices, because of the stock situation. Again, roll the tape back to 1980 and there were very large ending stocks - 50%, and then 60% for corn. And that's something that weather plays a role on them. Luck is a contributing factor to that.

Brent Gloy: Yeah. And I think we have to admit that just given our background, we're a little bit biased toward something like ending stocks being the problem. I think some people would say that's a good thing because it means that there's a lot of ag goods available. I'll never forget in the start of the Renewable Fuel Standard, there was an ag advocacy group that was very wound up about the impact of biofuels on the cost of food and the whole argument was that you're diverting food into fuel and that's going to drive prices up. And this particular group was really into doing a lot of work in developing countries. And they said, this is terrible because these people are, they're going to, you know, have a harder time getting food because more expensive. If you go back just five years before the Renewable Fuel Standard, the same organization was criticizing American foreign policy at the time for subsidizing ag production too much. Remember in the 90s, we had huge government program payments based on target prices that weren't really called target prices at the time - loan deficiency payments and those kinds of things. And as a result, we produced a lot of stuff at very low prices and they were arguing well that disadvantages farmers in developing countries because these farmers overseas can't produce at these very low costs and they don't have a government that bails them out, so they can't make any money, so they can't farm. You're destroying their livelihoods. So, I just find it interesting that the same group has been on both sides of that fence in a matter of 10 years. And I think therein lies some of the challenges when you get to farm policy is, whatever you do is alter the landscape and somebody is always going to be unhappy with how the alteration works its way through the system.

Sarah Mock: This story might sound like one of fickle, anti-farmer, interest groups, but look deeper. In reality, this group is actually holding to the spirit of what Reagan and many farmers claim to believe. These two positions are consistent in being anti-intervention, even though the two types - paying farmers directly versus creating an artificial market work by different mechanisms, they're both intervention It's true Federal support for U.S. farmers in all its different incarnations does disadvantage, farmers in other parts of the world. But it's also worth noting that changes at USDA inspired by the events of the 1980s didn't end at commodity programs.

David Widmar: One of the big ones is the WASDE report - the World Agricultural Supply and Demand Estimates. And the first one of these to come out was November 1973. And again, this was in the context of, we just had a big supply shock in Russia, and they came and bought a bunch of grain. Way more grain than we ever expected they would, and it caught us flatfooted and we didn't want this to happen again. And so, there's a whole bunch of congressional hearings, and thought pieces and opinions, and efforts to make sure we didn't get caught flat footed again. And so, this effort, the WASDE report itself, but also all of the activities that the USDA takes part in to try to assess the state of production and usage of grain and meats as well, all around the world, got started in this, in this timeframe.
Another thing that came out of this is of course, sometimes you see these odd reports coming out of the USDA. Like the Office of the Chief Economist has meteorologists on staff. This also came out of this. Grain Robbery situation as Russia had a significant multi-year drought and being able to understand that and communicate that to the marketplace in a very clear and

regular timeframe was an important objective that came out of that. A second one that we see, is these flash sales and these weekly export sales. These are like Twitter gold, right? Fill in the blank, quantity of metric tons of commodity sold to - and then it's usually China, unknown, or other - and these really get a lot of attention. This system of reporting sales started coming together in response to Russia, making a lot of purchases from different grain buyers without the left hand, knowing what the right hand was doing. And so now if you're making big sales of grain, of U.S. grain to foreign buyers, you need to report that and the USDA aggregates that, and they share that information, so everyone's knows what's going on in this space. So that was another big activity that the USDA undertakes on a regular basis that got started during this timeframe. And I always find it a little bit comical when people get really upset about the WASDE report and errors in the WASDE report and when they move yields. If you ever open the WASDE report, right. It's many pages and most of us only look at a couple of tables, right? U.S. corn production, U.S. soybean production and that's just not even the tip of the iceberg. And then people get really upset when there's quote unquote big changes. When they move corn yields a couple bushels up or a couple bushels lower. And this report was put together to be like a 30,000-foot scanning the, looking for big global problems and global trends. And it was a regularly updated every month. And so, people are like, "Oh, the report came out last month, but it's out of date." But a lot of times we use the WASDE report for a different thing than what it was designed for.

<u>Brent Gloy</u>: One thing we know about crises is that when people don't have good data or good information and they're trying to make decisions, it it's very difficult. And so, if you think about the thing that really made the 80s bad was the financial crisis that went along with the income crisis. The financial crisis was really exacerbated [because] we didn't have the kind of lending data and data on how borrowers were actually performing in real time. It was paper file stuff and banks in the farm credit system were in serious trouble. [They] might have guessed that things were going to be bad, but they didn't have the data to really know just how bad it was actually going to be. And so, I think, that lack of data and being able to work through it, to assess a situation is really hard in a crisis and it tends to make it even worse. So, I think you can look back at it and say, "Yeah, there were people that were talking about how this much leverage in the farm sector was a bad idea." But there were also a lot of people saying, "Absolutely. Why not? Real interest rates are really cheap, go for it." And I think in hindsight, it's easy to see there was a big problem and if you were in the moment, it's a whole different deal. Even going back to putting ourselves in the shoes where we don't have the information. I saw some guy the other day posting pictures of all the commodity prices he'd written down daily for 20 years because the way people charted grain prices in those days was to listen to the radio on the market report. It would tell you what the price of corn was in Chicago or whatever, and they'd write it down and keep track of it. They did that every day for years and years - here's what history looks like. It was a very different environment than we're in today and I think sometimes we underestimate how significant that was. It's hard to go back to a time where you can't just pull up your computer and look at a price chart, or even with the prices of anything it's on your phone right now. Back then you had to wait until the local farm radio station played it on the radio.

Sarah Mock: Today, the USDA is still an information powerhouse and remains the gold standard globally when it comes to world supply and demand estimates. In fact, some countries trust the USDA's predictions of their supply and demand more than they trust even their own state economist's estimates. The USDA has commitment to not being outfoxed after the 1970s has largely worked out, but today China poses a threat that's not dissimilar to the one posed by the USSR in the 70s. China is, in terms of agricultural demand, much more of a black box than most other countries. And at the same time, it dominates world demand for many commodities. When it comes to China, trusted government information is scarce, misinformation is plentiful, and our ability to tell the difference between the two is limited. The resources available to the USDA's economists have also waned since the 1980s as farm crises, haven't revolved around lack of information pressure has grown to limit government spending and so less robust political support has been put towards ensuring that the USDA stays on the cutting edge. Here the antagonism between farmers and the government that they often view as overbearing and limiting of their freedom becomes paradoxical because that same USDA, that farmers despise and often want defunded, which of course is the inevitable end of paying fewer taxes, is their first and most important line of defense against market catastrophe.
Today, where a strong and sophisticated market and information adversary in China crosses with a marginalized USDA information machine there is an unknown amount of risk to global commodity markets and to the stability of the U.S. farm economy. It is possible that in the future, we'll look back on today's rising commodity prices and see the first indicators of a crisis to come.
Throughout the history of farming in the United States corn has been at the center of many, a boom-and-bust cycle. It has had many partners in that, wheat and cotton chief among them. In the most recent cycle, corn found a boom partner in soybeans, a crop with essentially a single global destination – China. Over the last several decades, we've turned over almost as many acres to soybeans as to corn and as prices climb, even in the short term, farmers will have more and more incentive to bring even more acres into production, to take advantage of Chinese demand. USDA policy over the last three years will likely speed that process. That reaction among farmers could be another indicator of whether today's farm economy is headed towards calamity or stability, but that's next time on Escaping 1980.

Brent Gloy: Thanks again for joining. David and I would like to thank the people that made this episode and podcast series possible. First, the subscribers on AEI Premium, second huge thanks to the show series' producer, editor, and co-hosts Sarah Mock. Finally, the rest of the AEI team, this team has been working remote since, before it was popular. Special thanks to Megan H., Jeff and Aerin.
