

Conclusions

The 2002 Farm Act governs agricultural programs through 2007, covering a wide range of programs for commodities, conservation, trade, rural development, nutrition, credit, forestry, and energy. While this new farm law introduces some new policies to the array of agricultural commodity programs, in many ways, the 2002 Farm Act extends provisions of the 1996 Farm Act and the ad hoc emergency spending bills of 1998-2001.

Commodity policy changes of the 2002 Farm Act include changing marketing assistance loan rates, adding counter-cyclical payments, and replacing production flexibility contract payments with direct payments. Also, the commodity coverage under these programs is expanded in the new legislation.

Analysis of FAPSIM model scenarios under alternative policy assumptions is used to assess impacts of the 2002 Farm Act on markets for most program commodities and livestock. These results are supplemented with USDA interagency commodity committee analyses for selected commodities. The model simulations cover 10 years and reflect USDA long-term projections at the time the new legislation was enacted. These projections include a backdrop of improving domestic and international economic growth, particularly in developing countries, which provides a foundation for gains in global trade and U.S. agricultural exports, resulting in rising market prices in the sector over the next decade.

The primary crop sector impacts of the 2002 Farm Act are through acreage and production changes. Thus, much of the crop sector focus in this report covers the effects of the new legislation on economic incentives underlying planting decisions of farmers and the resulting acreage impacts. Additional market effects for crops reflect changes in equilibrium levels of prices and demand in response to the acreage and production changes.

Analysis of impacts of the 2002 Farm Act on commodity markets indicates that loan rate changes under the marketing assistance loan program have the largest effect on production choices in the initial years of the analysis when prices are low enough that marketing loan benefits exist. Overall plantings of the eight major program crops studied are initially higher under the 2002 Act than plantings under a 1996 Farm Act scenario that assumes market-price-based formula determination of loan rates. However, the largest

increase in plantings of about 2 million acres is relatively small (less than 1 percent) partly due to the inelasticity of acreage response in the sector where plantings change proportionately less than the economic incentives provided by prices and net returns. Some switching in the cropping mix from soybeans to competing crops, particularly corn, also occurs, reflecting relative changes in loan rates.

Increases in total plantings in the initial years of the analysis of the 2002 Farm Act are smaller (less than 1 million acres) compared with an alternative 1996 Farm Act scenario that leaves loan rates at the maximum levels allowed under that legislation. However, compared with this alternative loan rate scenario, the switch away from soybeans under the 2002 Act is larger and extends over more years, reflecting a reduction of the soybean loan rate from its capped level under the 1996 Act.

Other features of the 2002 Farm Act that affect plantings include the expansion of the Conservation Reserve Program and the addition of marketing loans for dry peas and lentils, both of which reduce somewhat the land available for production of the eight major program crops. In the longer run, as projected market prices for most commodities rise above ranges where there are marketing loan benefits, overall plantings of the eight major program crops are lower under the 2002 Farm Act, reflecting larger enrollment in the CRP and increased plantings of dry peas and lentils. Still, these acreage reductions are relatively small, generally ranging from 1.0-1.5 million acres in 2006-11.

Program changes for dry peas, lentils, dairy, and peanuts suggest some increases in production of these agricultural commodities. With small impacts on production and prices of feed grain and protein meal crops, livestock sector impacts are relatively small. Retail food prices are not expected to change appreciably. Farm income under the 2002 Farm Act is higher than under a continuation of the 1996 Farm Act, mostly due to an increase in government payments to the sector under the new law.

Additional market effects may result from counter-cyclical payments, direct payments, and provisions of the 2002 Farm Act that permit the updating of base acreage and payment yields. Even though benefits of these provisions are not linked to current production of farmers, they may, nonetheless, provide indirect incentives that influence production decisions and overall agricultural output.

Counter-cyclical payments may influence production choices because of their link to market prices, which can lower risks to producers by reducing the variability of revenues in some price ranges for program crops. Although expected net returns would likely remain a dominant consideration in cropping choices for most situations, revenue risk reduction provided by counter-cyclical payments could affect production choices for risk-averse producers. For a risk-averse farmer, the production mix chosen, as well as the use of risk management strategies, would be based on the joint

consideration of profit maximization and revenue risk reduction concerns and would reflect the degree of risk aversion of the farmer.

Direct payments are the least coupled of these programs but may influence production through wealth and investment effects. Provisions for updating base acreage and program yields may also have some influence on current production choices if farmers expect future legislation will again allow them to update these items for their farms.