



Feasibility of Farm Program Buyouts: Is it a Possibility for U.S. Sugar?

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ERS/USDA Farm Policy Research Project

The analysis herein is part of an exploratory two-year ERS/USDA research project titled:

“A New Generation of Farm Policy Tools”

Objectives of the project are to:

- Examine how farm producers utilize various types of support payments that are “decoupled” from current production and/or prices to different degrees
- Provided an exploratory evaluation of a buyout of existing support payments as a long-term policy option

Starting from a trade perspective...

The Road to a WTO Doha Round Agreement has been rocky:

- For developed countries, continued subsidies
- and for developing countries, “offensive” versus “defensive” approaches

have constrained progress in the Doha Round

Evolution of U.S. Farm Policy

- **Policies that have proven feasible have been a slow cash out of past price support and supply control programs**
- **“Decoupling” is a component of the reforms and is accommodated in the WTO Agreements, but “dirty decoupling” is a two-edged sword allowing subsidies to continue**
- **EU has recently followed a similar reform path to some extent and has recently undertaken a substantial sugar program reform**

A Buyout of Farm Support Program

This presentation examines the feasibility of a domestic policy option that would end farm subsidies by buying out farm support programs. The basic argument for a buyout is that it could:

- Provide enhanced transition support to farmers
- Provide long-term savings to taxpayers
- Pave the way for more substantial global agricultural trade liberalization

Alternative Reform Strategies

Compensation	Speed of Implementation	
	Slow	Fast
Yes	Cash out	Buyout
No	Squeeze out	Cutout

Source: Orden, Paarlberg and Roe, 1999

Recent Small-Scale Buyouts

Divergent Policies Among U.S. Peanuts Tobacco and Sugar

- Peanut quota buyout in 2002 farm bill
- Tobacco quota and price support buyout (2004)
- Non-reform of sugar program

Value of the Peanut and Tobacco Buyouts

(per pound of quota, at 5% discount rate)

	Peanuts	Flue-cured	Burley
Ave Quota Rent (95-01)	\$0.037	\$0.47	\$0.41
		\$7.00 Tobacco Buyout	
Buyout Present Value	\$0.550	\$5.67	\$5.67
Infinite Annuity	\$0.026	\$0.27	\$0.27
Years at Average Rent	24	16	21
		\$10.00 Tobacco Buyout	
Buyout Present Value	--	\$8.11	\$8.11
Infinite Annuity	--	\$0.39	\$0.39
Years at Average Rent	--	34	56

Insights from Peanuts, Tobacco and Sugar

- **Narrowly defined benefits are easiest to buy out**
- **Onset of reform aligns with sharp contraction of past benefits**
- **Unique dimensions partly explain the more complete tobacco buyout**
- **Producers must support the reform**
- **Buyout compensation has been quite lucrative**
- **Buyouts may facilitate trade policy reform, but the peanut and tobacco buyouts benefit domestic not foreign producers**

Possible Buyouts of Selected U.S. Farm Payments

	Fixed Direct Payments	Counter-cyclical Payments	
		Maximum	Projected Level
billion dollars (annual payments; present value at 5% discount rate)			
2002 Farm Bill (2002-07)	5.29; 28.20	7.30; 38.79	3.50; 18.30
10-Year Buyout of 25 Years Payments	9.66; 78.11	13.33; 108.06	6.40; 51.87
Infinite Annuity	3.73	5.15	2.47

Possible Buyouts of Selected U.S. Farm Payments (cont.)

	Marketing Loan Benefits
	billion dollars (annual payments; present value at 5% discount rate)
2002 Farm Bill (2002-2007)	2.97; 15.77
10-Year Buyout of 25 Years Payments	5.42; 43.94
Infinite Annuity	2.09

Cost as a Complete Buyout

	Fixed Direct Payments	Counter- cyclical Payments (Projected Level)	Marketing Loan Benefits	Total
	billion dollars			
Annual Cost (10 Years)	9.66	6.40	5.42	21.48
Present Value	78.311	51.87	43.95	174.13
Infinite Annuity	3.73	2.47	2.09	8.29

Alternative Buyout Costs

(10 year buyout of 15 years anticipated payments)

	Fixed Direct Payments	Counter- cyclical Payments (Projected Level)	Marketing Loan Benefits	Total
	billion dollars			
Annual Cost (10 Years)	7.11	4.71	3.99	15.81
Present Value	57.67	38.20	32.36	128.23
Infinite Annuity	2.75	1.82	1.54	6.11

Alternative Buyout Costs

(5 year buyout of 15 years anticipated payments)

	Fixed Direct Payments	Counter- cyclical Payments (Projected Level)	Marketing Loan Benefits	Total
	billion dollars			
Annual Cost (10 Years)	12.69	8.40	7.11	28.20
Present Value	57.67	38.20	32.36	128.23
Infinite Annuity	2.75	1.82	1.54	6.11

Challenges Faced by a Buyout

- **The more complete a buyout is, the more convincing, but also more costly**
- **Asking Congress to increase expenditures in the short run to achieve savings in the longer term**
- **Enforcing the buyout when the long term arrives**

Principles for Sugar Reform

- **Free Up Prices** (let markets balance demand and supply)
- **Avoid Quantitative Interventions** (production or marketing controls, stockholding and disposal)
- **Reduce Incentives for Oversupply** (bring prices more closely into line with world markets)
- **Provide Adjustment Compensation to Farmers in the Short Run** (is a buyout an option?)
- **Create a Sustainable Long-Run Policy** (free trade in our lifetime?)

EU Sugar Reform

- **Pressure for reform within the CAP, from EBA and due to successful challenge to past program in the WTO**
- **Domestic raw sugar prices to decline from €497/MT to €355/MT (from \$0.27 to \$0.19/lb at \$/€= 1.20)**
- **EU25 production expected to decline from 21 MMT to 13MMT (ERS estimate)**
- **A and B quotas combined and total quota will fall, but 1.1 MMT new quota rights can be purchased to facilitate shift of production to efficient areas**
- **Producers to receive “cash out” compensation payments of 65 percent of price decline**

EU Sugar Reform (cont)

- **Buyout (at estimated cost of €5 billion) of some of the processing capacity**
- **Buyout paid for by temporary processor fees**
- **Additional regional assistance for affected areas**
- **Price decline for preferential foreign suppliers, with only a limited national compensation (foreign producers and processors not assured of specific payments)**
- **EU expected to shift from net sugar exporter (0.8 MMT) to net importer (3.5 MMT)**
- **Further proportional quota cuts if necessary**

Possible Buyouts for U.S. Sugar

(10 year buyout of 25 years of anticipated protection)

	Partial (Limited Trade)	Full Trade Opening	
		\$0.06/lb Price Wedge	\$0.09/lb Price Wedge
billion dollars (annual payments; present value at 5% discount rate)			
Protection Lost (2002 Farm Bill)	0.35; 1.89	1.14; 6.05	1.71; 9.08
Annual Payments (10 Years)	0.65; 5.24	2.08; 16.81	3.12; 25.21
Infinite Annuity	0.25	0.80	1.20

Conclusion

This presentation has examined the feasibility of a domestic policy option that would end farm subsidies by buying out farm support programs. The basic argument for a buyout is that it could:

- Provide enhanced transition support to farmers
- Provide long-term savings to taxpayers
- Pave the way for more substantial global agricultural trade liberalization