Program on Dairy Markets and Policy Information Letter

The Challenge of the Congressional Dairy Baseline

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In Congressional circles and among policy wonks, it is common to talk about "the baseline". A "good" baseline implies you have money to spend that gives you flexibility to be either creative or generous or both. A "bad" baseline infers the opposite. Unfortunately, dairy programs have a bad baseline. This is compounded by the fact that we are in a year when budget pressures are extraordinary.

What is a Baseline

Congress is responsible for passing laws that authorize or require certain programs or actions. It is also responsible for doing so in a way that provides appropriate balance between how much money is available to spend and how much we can expect to spend under the various programs enacted into law. Clearly, what exactly constitutes the "appropriate balance" is subject to debate. That issue notwithstanding, Congress routinely estimates 1) how much money it can expect to be spent under existing laws and 2) how much money is saved or spent if one or more programs are changed. The first is called the Baseline. The second is called the Score.

The analysts responsible for this are in the Congressional Budget Office or CBO. The CBO employees are not subject to change when a new Congress is elected or when there is a change in party control or party leadership. They are expected to be non-partisan and entirely objective in their analyses. When they determine a baseline or a score, those numbers become indisputable. Congress may choose to ignore them, but elected officials can't change them.

A Baseline for the entirety of federal programs is determined three times each year. The March baseline is typically the basis for federal laws that are determined on a fiscal year start and end. The Federal fiscal year begins on 1 October. The March baseline is being used to

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determine how much money can be spent on agricultural and related programs in the current deliberations about a new farm bill.

The leadership of the House and Senate agriculture committees agreed last Fall that they would pass legislation that would save $23 billion over 10-years, relative to the Baseline. There are many programs and provisions in a Farm Bill. A baseline is built up from each part. When Congress says it will save $23 billion, it begs the question just how that savings will be achieved.

Two concepts always come into play when Members of Congress and industry/issue advocates debate new programs – "level playing field" and "our fair share". These concepts are always in full bloom when conditions necessitate a budget cut. Everyone can easily agree that these are two concepts that should be used to guide cuts. Unfortunately, how one defines them seems to curiously depend on what side of any issue one is. It is clear that not everyone uses the same level or has precisely the same idea about what is fair.

Sometimes these concepts are applied in very simple arithmetic terms – if we need to cut back 15%, then let's cut back each item 15%. Sometimes fairness is used to explain why you should be cut back 20% so I only have to cut back 10%.

Without getting into what is fair, let's take a look simply at what is.

<u>Government Program Benefits by Region of the US</u>

USDA has routinely estimated the amount of government program benefits paid and how they are allocated by region. These estimates are based on the Census of Agriculture and on farm management surveys that are conducted annually.[1] The Economic Research Service routinely provides information about government payments annually.[2] In their most recent report, they present the following graphic on government payments by region. The most recent report describes their methodology for generating this information as follows:

> *Direct payments and payments based on market prices represent 'commodity program payments' since they are tied to current or historical acreage of program-eligible crops. For the years 2000-09, commodity program payments represented on average 60 percent of government payments to farmers, conservation payments accounted for 14 percent of all government payments, and other payments represented 26 percent of the total. Direct payments, on average, accounted for half of commodity program payments.*[3]

They further describe the particular regional data in this way:

> *Whether expressed in nominal or constant dollars, government payments in the 2007-09 period represent the lowest total volumes paid to producers since 1997. However during this period, the importance of government payments as a percent of net cash farm income varied by ERS production region. Low levels of crop payments as a function of prices in 2007-09 and low milk program support payments meant that the government payments' shares of net cash farm income were on average less than 20 percent for producers in the Northeast, Corn Belt, Lake States, and the Pacific regions. The government payments'*

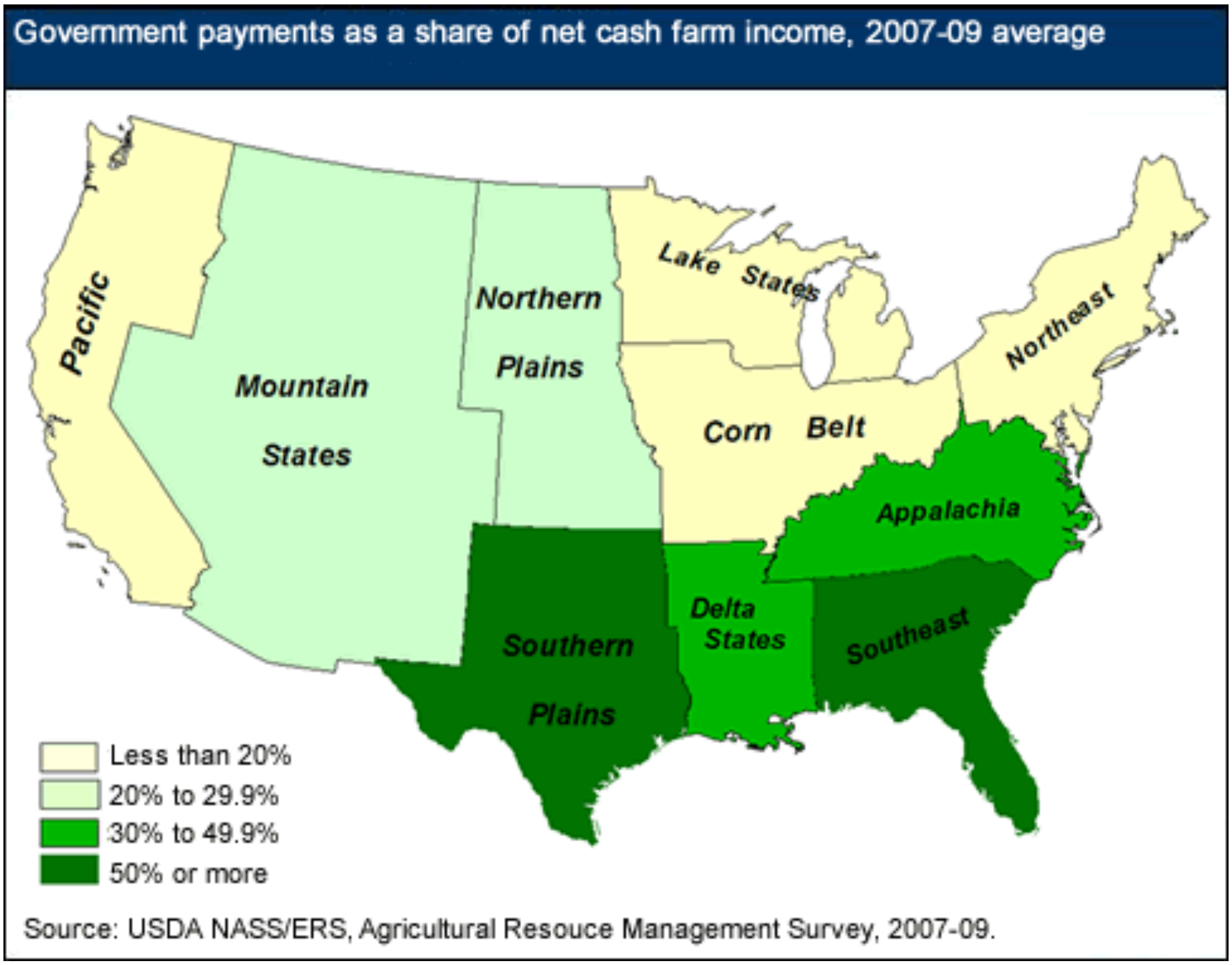
[1] *http://www.ers.usda.gov/Briefing/FarmIncome/*

[2] *http://www.ers.usda.gov/Briefing/FarmIncome/govtpaybyfarmtype.htm*

[3] *Ibid.*

shares of net cash farm income were on average highest in the southeast quadrant of the U.S., where government payments represented on average 50 percent or more of net cash farm income for producers in the Southeast and Southern Plains regions.[4]

The following graphic illustrates the payment pattern, as a share of farm cash receipts, by region of the US. Clearly, the South receives the highest share, followed by the Northern Plains and Mountain States. Agriculture is diverse in all of the US regions but it is true that Southern agriculture tends to have significant incomes from cotton, peanuts, rice, tobacco and several other crops not grown outside the region. The Northern Plains and Mountain States tend to have higher shares of wheat and livestock. The Northeast and Upper Midwest have a relatively higher share of dairy. The Northeast and Pacific states also would tend to have significant specialty crops sectors.

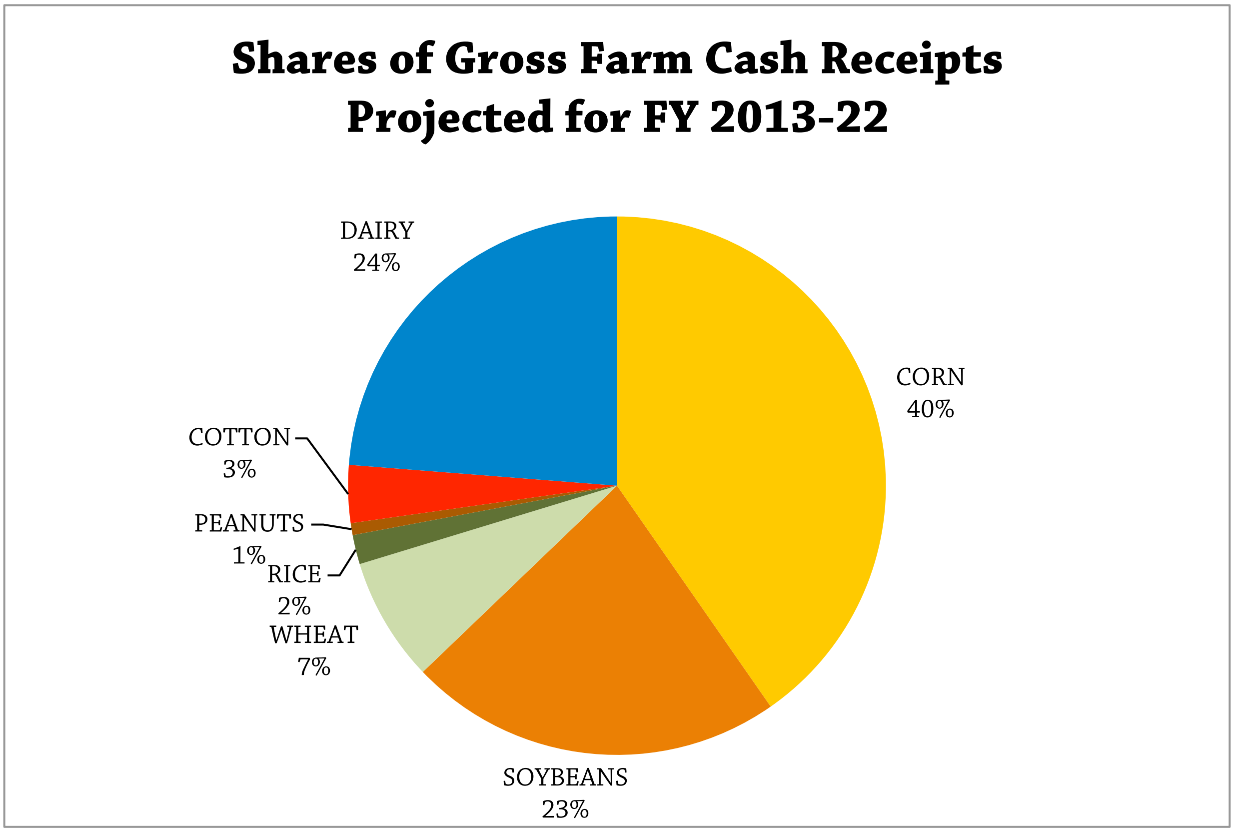


Agricultural programs tend to be defined in terms of commodities, not regions. The South doesn't get more payments per farm cash receipts because there is a special provision for

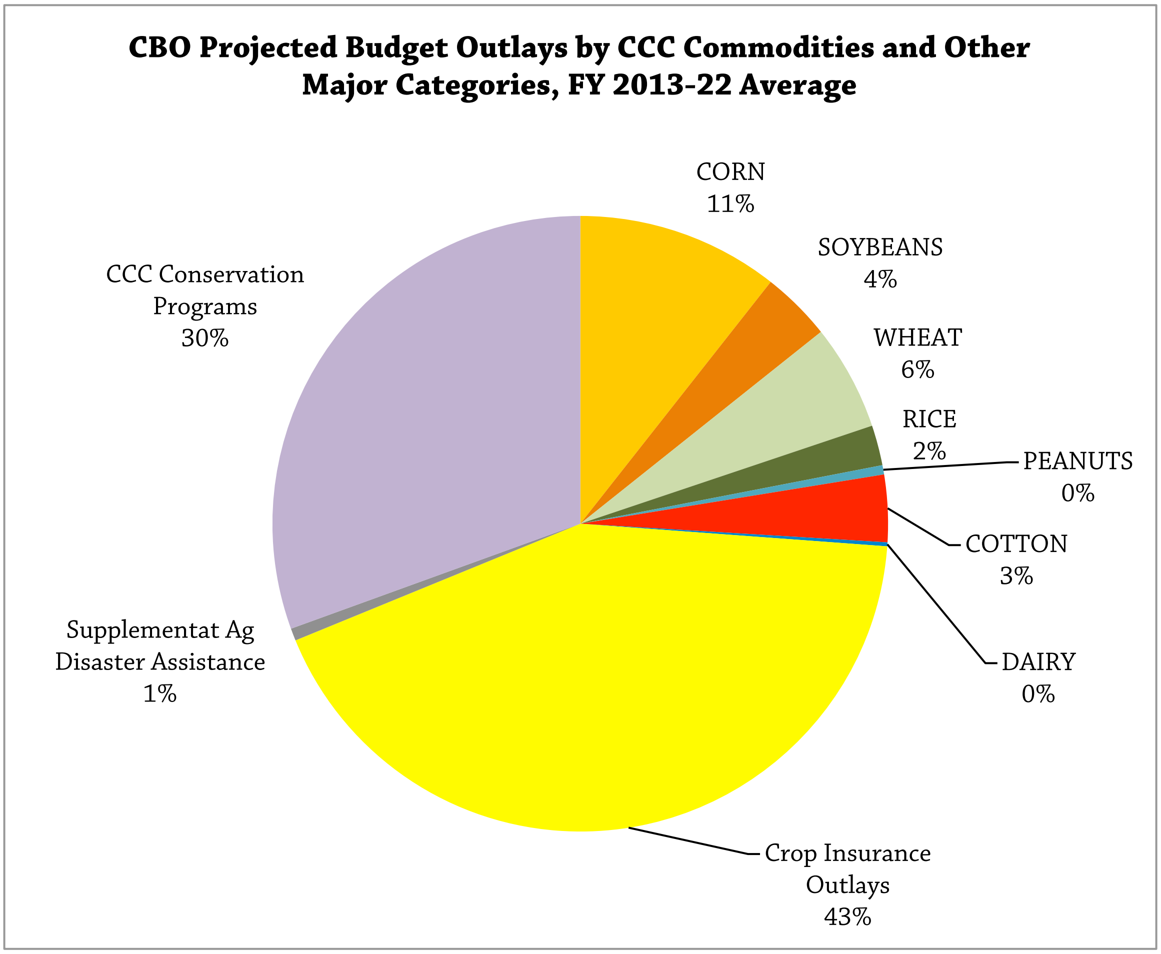
[4] *Ibid.*

Alabama. It gets this on the basis of the agricultural sectors that dominate the region and the nature of the programs for those commodities.

When CBO does a Baseline, it has to build government costs from a basis that begins with estimates of the market activity for each supported product. Thus, it must estimate how much corn will be produced, what is the market price of corn, uses of corn and so on. From the March 2012 baseline data, one can calculate the gross market cash receipts for each commodity (production times market average price). For the FY 2013-22 baseline, the relative share of these farm cash receipts for key commodities is shown below.



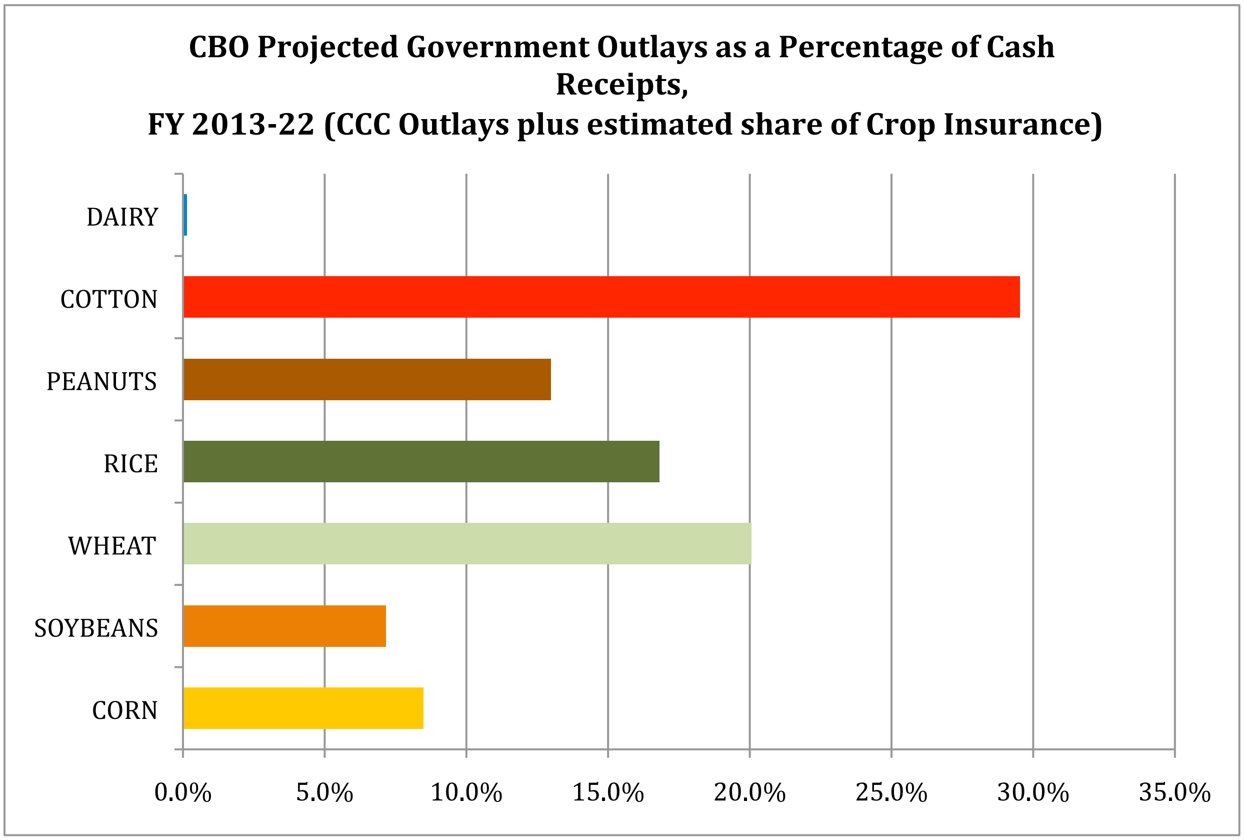
Government outlays are estimated by CBO for major categories of expenditures. They provide a breakdown of outlays by commodity for programs in which payments are tied directly to the commodity. These are referred to as CCC and related expenditures. The obvious examples are Direct or Countercyclical Payments to corn growers, wheat growers etc. MILC payment to dairy farmers would be another example. Crop insurance is not broken out on a commodity basis, nor is conservation or disaster payments. The following graph shows the CBO projected payments under current law for commodity and other programs.



Although CBO does not allocate Crop Insurance Outlays by commodity, USDA reports expenditures on various crop insurance products by commodity. Using the shares from 2011, the last complete year, one can make a gross approximation of the shares of CBO's projected crop insurance expenditures that might accrue to each commodity. If we take this estimate of government outlays and compare them to the CBO implied market farm cash receipts, we get the following graph that shows government outlays as a percentage of market income.

It is rather easy to compare this commodity sector information with the regional graphic shown above. Southern crops tend to enjoy a far greater degree of government support than is true for the more typical wheat areas of the Corn Belt. The Wheat Belt tends to enjoy higher levels of support than the Corn Belt.

Needless to say, dairy stands out, or rather it stands apart by being virtually undetectable on this graph. The projected share of government outlays, relative to the size of the sector is 0.1%. When the old Dairy Price Support Program was the primary form of support for dairy, a fairly similar graph might have been drawn, but the implication that the federal government doesn't have much support for the dairy sector would have been wrong. The nature of the Dairy Price Support Program was one that shifted the cost of the support program to consumers in the form of higher prices.



One obvious absence on this graph, at least for agricultural policy wonks, is Sugar. The Sugar sector enjoys supports in the form of a supply control program. In this case, the supply that is controlled is imports, but the effect is like any other supply control, the price of sugar is higher. There is no government cost, but there is a consumer cost. The old tobacco program was also a supply control program. By restricting acreages that could be harvested, the tobacco program resulted in higher tobacco prices. Tobacco growers, like sugar growers, were not subsidized in the sense of receiving government checks, but tobacco was and sugar is definitely supported.

As Congress continues to look for that fair balance that levels the playing field, participants in the dairy industry could understandably question whether or not they are getting their fair share and just how much of their current, small baseline they should give up for the greater good.