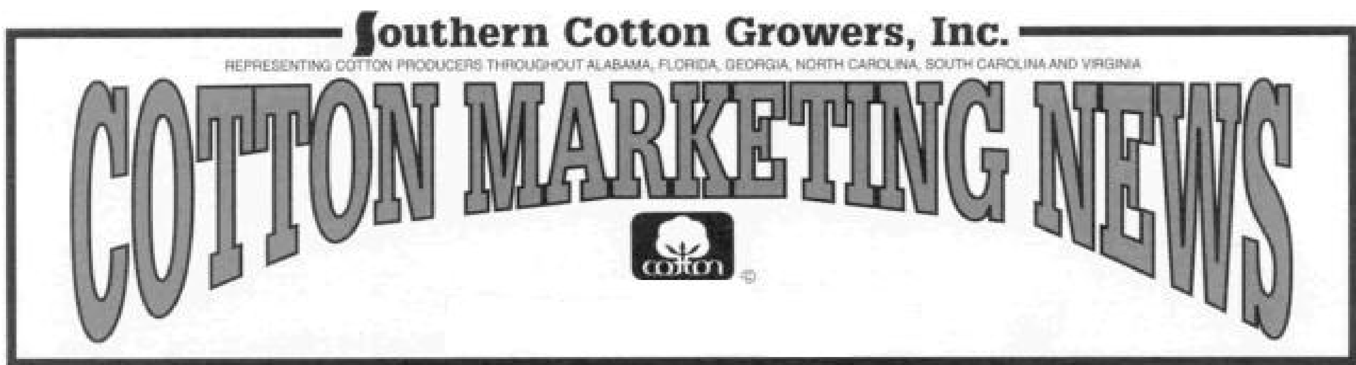

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This newsletter is also available in PDF format on the UGA Cotton web page at:
http://www.griffin.uga.edu/caes/cotton

What Are The Goals Of Farm Bill and Trade Policy?

Debate and discussions regarding the 2008 farm bill have already begun. The current legislation runs through the 2007 crop year. The next farm bill will be shaped by the federal budget situation, WTO and other trade issues, and the opportunities for contributions from agriculture in the country's energy situation and policy. Intertwined among all this is also the continuing debate over farm programs payments—the type of payment(s), structure of payments, and payment limitations.

I find it somewhat surprising and disappointing that in all of this, what seems missing is the importance and impact on the producer. Should not at least some degree of the farm policy debate be concerned with the profitability and sustainability of US agriculture? And in doing so, you have to take a more microscopic view and not look just at what is happening to the total US farm economy. Those who advocate cutting payments and "free trade" need to take a closer look at the complexities of a global agriculture, all the various components of "competitiveness", and be clear and accurate (through good research) that the impacts of such changes will benefit the US farmer and rural communities. What is politically feasible and what is economically feasible may not be the same thing.

I do not know a single farmer that takes great pride in receiving government payments. Wouldn't it be great if market forces set the price at such a level that farmers did not have to worry about LDP's, CCP's, and payment limits. But, in the case of cotton (and perhaps other crops, I do not know) such has not been the case. The decline of the US textile industry and increased reliance on exports has resulted in a lower tier of cotton prices—prices chronically below 60 cents/lb and very often at or below the loan rate of 52 cents.

The marketing loan (POP or LDP) provision allows the US price of cotton to float to levels needed to be competitive in the export market while at the same time providing a safety net for the producer. Such payments, and the US cotton program in general, is challenged by WTO and will possibly be changed in the next farm bill. With cost of production rising and prices under pressure, changes in payments and payment structure would be crucial to net income.

There has been much talk lately of much higher cotton prices to come—perhaps by this fall and certainly longer-term as world cotton demand is expected to continue to grow faster than production capability. China and India are key in this equation. While the *prospect* of higher prices sounds good, the *reality* is that world cotton demand has already increased dramatically over the past decade and yet the US price for cotton still often struggles to stay above the 50's. Talk of 60-cent cotton by this fall is certainly do-able. An outlook for 70 and 80-cent cotton, even years down the road, should be taken with caution.

Supply and demand do not operate independently in a vacuum. For example, the *elasticity* of demand must be considered-- in other words, if cotton prices increase how much will this reduce demand? If demand falls off, this will reduce the upward pressure on price. In other words, it is the role of price to insure that enough stocks remain to carryover to the next season and to attract acres planted to meet demand. Prices for cotton whether it be 60 cents, 70, cents, or 80 cents can only be sustained if foreign and domestic mills continue to purchase cotton at those prices. Eventually, reduced demand and/or increased acreage attracted by higher prices would likely drive prices back down.

So, this gets back to our policy debate. What kind of cotton program, if any, do we need in the US? Clearly, it should be a program that allow the US to be a major (the major) cotton exporter. Without exports, we wouldn't need 7 out of 10 US cotton producers. We need to be able to compete on price and fiber quality with other

exporting countries while at the same time providing a safety net when that price moves low. I think the debate will center on what form payments take and how much. But, anyone advocating drastic cuts or elimination of payments needs a study in cost of production and profitability.

Below is a table taken from UGA Extension Service enterprise budget estimates for BR/Non-irrigated cotton for 2006. I have not made any revisions or updates although prices and costs have changed since these estimates were made. The table and numbers make the point regardless.

BUDGETING THIS WHOLE-FARM COTTON ENTERPRISE			
Acres		**Yields**	
Total Cotton Acres on The Farm:	700.0	2006 Budgeted Yield	700.0
Acres of This Cotton on the Farm:	700.0	Farm Direct Payment Yield:	650.0
Farm Cotton Base Acres:	700.0	Farm Counter-Cyclical Yield:	650.0
DCP PAYMENT ACRES (85% BASE):	595.0		
Prices and Payments		**Costs**	
Expected MYA Price:	55.00	Budgeted Variable Costs Per Acre:	$390.29
2006 Direct Payment (DP):	6.67	Variable Costs Excluding Rent:	390.29
Est. Counter-Cyclical Payment (CCP):	10.73	Land Rent:	0.00

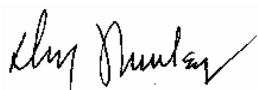
THIS BUDGETED COTTON ENTERPRISE-- TOTAL FARM COSTS AND RETURNS				
Acres:	**700**	**Per Acre**		**Total**
Crop Income (Including LDP/POP/Loan Gain)		$420.00		$294,000
Variable Costs (Excluding Rent)		$390.29		$273,202
NET RETURN BEFORE LAND RENT		**$29.71**		**$20,798**
Land Rent		$0.00		$0
NET RETURN ABOVE VARIABLE COSTS		**$29.71**		**$20,798**
Direct Payment (DP)		$36.85	*	$25,796
Counter-Cyclical Payment (CCP)		$59.28	*	$41,498
NET RETURN AFTER DCP PAYMENTS		**$125.85**		**$88,093**

* DCP Payment per acre planted of this enterprise

At 55-cent cotton, the Net Return Above Variable Costs (excluding land rent, if applicable) is $29.71 per acre including POP/LDP. Without LDP (5 cents/lb), the Net Return would be -$5.29 per acre excluding land rent. Add in $75/acre for rent and the Net Return would be -$45.29 even with POP/LDP. As a matter of fact, for a farmer paying rent the Net Return doesn't become positive until DP and CCP payments are taken into account.

Policy decisions that would greatly alter the marketing loan (eligibility for and amount of LDP), unless these or other policy decisions result in a higher/offsetting increase in the market price or other payments, would have a detrimental impact on the already tight profit margins in cotton production. Further, because DCP payments have undoubtedly resulted in an increase in land rent, lower DP and CCP would reduce the funds available to pay rent which, in return, should result in lower rental rates… but could have no effect on rates (rates remain high) due to increased competition for the land (farmers feeling like they have to farm even still more acres to make up for the drop in payments).

The upcoming new farm bill will be a very important piece of legislation. In terms of cotton, a major goal should be to maintain or improve our export potential while providing a continued safety net for producers. The next farm bill may also be shaped by the 6-year outlook for all commodity prices. Some analysts, for example, believe we are about to see significantly improved prices for corn due to the energy/ethanol situation. I've already mentioned the thought by some that higher cotton prices are also in our future due to world demand. Higher prices and reduced reliance on payments would be good but not a reason to abandon the safety net.



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