WASHINGTON UPDATE
Remarks of Wayne Bjorlie before the
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Abstract

We are here to look ahead as best we can and refine our expectations as to the likely risks and rewards for planting cotton in 2001. I will try to explore that question from the viewpoint of one who has helped administer the cotton program for some years now. Despite the best intentions of those who conceived the so-called "Freedom to Farm" Act in 1995, and though we might wish otherwise, Government support has assumed a larger role in cotton farming in the last couple of years than it has ever played before. The promise of Government support, I am afraid, is coming to be regarded as one of the indispensable inputs in the spring, along with seed and fuel.

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The other morning I was shaving with my trusty Norelco, when I slipped and fell into the bath tub. Sparks flew, steam rolled, and when I came to some time later, I could see clearly: What Farmers Want :

- Flexibility to plant whatever they want
- Contract payments not linked to anything
- More of those payments on stand-by in case they are needed
- Higher loan rates.

Except for higher loan rates, this has essentially been the program now for three years, and it is not difficult to see why it has become so popular. Or, why it has been so expensive.

Over the last three fiscal years, approximately covering the 1998, 1999, and 2000 marketing years, the Commodity Credit Corporation will have spent a total of almost $72 billion. For just the major field crops, the total over that time comes to about $52 billion. The rest is mostly for assorted conservation and disaster payments and other crops. (Chart 1)

Feed grains are accounting for $22-1/2 billion. Wheat accounts for a little under $11 billion. Soybeans are claiming $7 billion, almost entirely in marketing loan costs. Rice is coming in at over $3-1/2 billion. And, over those three crop years, the cotton program is costing about $7 billion.

We'll look at the cotton program in more detail later, but the point now is that Government supports for farming in general have become very costly since the enactment of the Freedom to Farm law. It is worth remembering that, back in 1995, we still had a budget deficit projected as far into the future as the eye could see, in the words of a former director of the Congressional Budget Office. The Freedom to Farm Act was conceived and initially sold as a budget cutting exercise. It would eliminate target price deficiency payments and eliminate the cost of holding government commodity stocks due to "too-high" loan rates and excessive production.

However, two funny things happened. First, the estimates of the budget deficit began to recede, and deficit reduction began to fade as a national political goal. Second, CCC commodity stocks started to decline in 1996, farm prices started to rise, and CBO recast their budget estimates for the Freedom to Farm Act, transforming the "savings" into a "cost." This happened because, suddenly, the projected target price deficiency payments that were being eliminated were worth next to nothing, and the stocks the government was projected to hold at great cost shrank to almost nothing. The only things that didn't shrink were the flexibility contract payments, because they were written into the Freedom to Farm Act and couldn't respond to market forces. Costs stayed; savings evaporated. Later, new payments were layered on top of the original payments. Marketing loan costs exploded. Voila! Commodity programs spend $52 billion dollars.

I cite these budget figures in order to suggest to you that farm supports in general have grown large enough so they cannot escape notice in Washington among those with other spending priorities.

However, there is some good news. For the 2000 crop, Fiscal Year 2001, it appears that CCC spending will decline rather dramatically compared to what it was for the last fiscal year. This year, the bottom line for CCC is now projected at $20 billion, down $12 billion from last year's record level of $32 billion. For the major field crops this year, costs are projected to decline to just under $12 billion, compared to $26 billion last year. Part of that tremendous drop in program costs is merely appearance --Congress front-loaded the $5 billion of 2000-crop market loss adjustment payments into the previous fiscal year. You got those last September.

Now, let's look at cotton program costs over the last couple of years. Cotton's share of last year's record CCC expenditures was $4 billion, also a record. Because of the low AWP last winter, farmers collected an average of about 20 cents per pound in marketing loan benefits. Those totaled $1.5 billion last fiscal year. The flexibility contract payments and additional market loss payments totaled another $1.8 billion for cotton, including the front-loaded 2000-crop market loss adjustment payments of about $615 million. (Chart 2.)

For the 2000 crop, mostly in Fiscal 2001, as you might expect, expenditures for cotton are down substantially. They are now projected to total about $970 million. The most important component of the big decline is that, so far, no market loss payments have been authorized by Congress to be paid in fiscal year 2001. That, together with the front-loading of the 2000-crop payments, makes projected MLA payments in fiscal year 2001 decline by $1.3 billion. Another important reason for the lower projected program costs for cotton in fiscal year 2001 is that earlier expectations of smaller foreign cotton production this year and tighter world stocks drove the "A" Index higher and increased the AWP to the point where we have actually seen a few weeks with no marketing loan benefits. Thus, projected marketing loan costs decline by $1.2 billion. (Chart 3.)

Returning to the business at hand, here, namely, what you can expect for the 2001 marketing year in the way of government supports, the answer is: less. It is difficult for me to shed any additional light on the expected world situation for the 2001 season since eminent experts already have discussed it. However, to guide us in thinking about what you might expect from the cotton program, let me reiterate what I think they said. World stocks by the end of the 2001 season will be tighter than at the beginning of that year, despite higher production. That probably means that the "A" Index will average higher than it is averaging in this marketing year. If it turns out that way, the AWP also would be higher. If the ICAC expectation of an average "A" Index turns out to be close, about 70 cents for an average, it is not unreasonable to suggest that marketing loan gains will be very minimal or even zero.

Over the last 10 years, the average deviation of the "A" Index during the year from its annual mean has been about plus or minus 4 cents. Thus, if the "A" is going to average 70 cents, it might range during the year between 66 and 74 cents. Not low enough. The AWP would not drop much below 52 cents.

How certain are we that world stocks really will tighten in 2001 and take away most or all the marketing loan gain? First, foreign production. The average "A" Index is up 12 cents from two years ago, and there is no reason to think planted area won't increase as a result. Maybe production rises 2

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million bales, or about 2 percent. The tightening of world stocks, then, would happen on the premise that consumption continues to outstrip production, as it has in each of the last 3 years. World consumption can even decline in 2001, but as long as it is larger than production, stocks will decline, and the likelihood of a significant marketing loan benefit will remain small. (Chart 4.)

The driving force in world consumption over the last 2 years has been the United States economy. Imports of textiles poured in from virtually everywhere at record rates. We know that engine is starting to misfire. Whether the U.S. economy will enter a recession and affect foreign textile manufacturers to the extent that world cotton consumption fails to reach the level of cotton production I would not want to guess. But, that is a variable you should be watching between now and planting time.

So, there are some cautionary notes on the AWP and the marketing loan benefit that just last season averaged 20 cents a pound for farmers but already has dropped to 4 cents this season, for those of you who had cotton to get it.

Your flex payment of about $480 million, or about 6 cents per pound, for the 2001 crop is bankable. Will there be another market loss adjustment payment to supplement it? I suppose one way to get at an answer to that would be to ask, “have we had a market loss?” It is much too early to gauge the political likelihood of another supplemental payment. It will probably still be too early at planting time.

I want to take a minute to talk about a couple of proposals for legislative changes in the cotton program that have surfaced. An increase in the loan rate is seen as a way to prop up prices slightly, but more importantly, to increase the size of any marketing loan benefit that might be obtained for the 2001 or 2002 crops. I estimate that removing the cap from the upland cotton loan rate formula would have resulted in a loan rate for the 2001 crop of 52.25 cents per pound, or some 33 points above the level that was announced. That would solidify the already recognized inclination to plant well over 15 million acres this spring. It would have little effect on the “A” Index but would increase any marketing loan benefit by up to that amount. At best, perhaps, you could expect a marketing loan benefit of somewhere near what you received on the 2000 crop. Under such a legislative change, the loan rate for the 2002 crop already can be pretty well estimated. It would be less than 53 cents.

Making flex payments based on more up-to-date base acreage and payment yields is another idea that has surfaced. If that were done, they would no longer be flex payments since they would hence forth be based on current planted acreage. It would be more difficult to argue that the payments are decoupled from production, with all of the international trade implications that that would entail.

Unless the pot of money available for flex payments were allowed to grow, there would be no net gain for the industry, and regional strife might arise. I estimate that if proven yields and more modern acreage bases were adopted for the flex payments, the payments would increase by about $150 million in each of 2001 and 2002, or about 1.8 cents per pound. Of course, across all commodities that now receive the payments, the cost could rise by $1-1/4 billion or more each year. More important than the monetary cost, however, would be the implicit admission that planting flexibility is no longer in effect.

I have a few minor program matters to report. There will be another round of cottonseed payments this year. Congress authorized $100 million for the payments on the 2000 crop, and it looks as though the payment rate will be about $15 per ton of seed. Payments will again be made to gins. It will facilitate payments if the gin will furnish FSA with an electronic bale list. Gins will be able to fax in their applications for cottonseed payments this year. Ginners will soon receive in the mail a signature verification form which they should fill out and return to FSA. That will make it possible for us to recognize the ginner’s signature on the application when it is faxed.

Gins also may be required to place classing data on the gin tag lists. This is important for bales for which the coarse count adjustment applies when the producer elects to receive a loan deficiency payment rather than a loan.

Regulations for the cotton loan program are being revised so that the process can be streamlined and made less costly to FSA. The most important idea being discussed is that electronic receipts are preferred over the old paper receipts for making loans. In fact, beginning with the 2001 crop, loans backed up by paper receipts are likely to face an additional $20 per bale service fee.

These items will be discussed further at the Cotton Council Annual Meeting, and producers will have other opportunities to comment, as well.