ECONOMIC OUTLOOK
Entering the World of the '90s
WORLD TRADE IN THE 1990s
by Vern Sorenson

As we enter the world of the 1990s, we can already see it's a topsy-turvy world in which major new forces are at work. Farmers, in Michigan and elsewhere, are going to have to find their way.

What are some of these forces? Starting with closest to home, we have a new farm bill to be written early this year.

In the next year or two, the rules of trade under GATT may be rewritten. If the U.S. proposals on that score win, we will see major changes in world trade in agricultural goods—a much freer trade. And with that will come a gradual reduction in the $100 billion now paid to farmers, worldwide, by their governments, in the form of subsidies. What will replace that income to farmers?

And then, coming on the scene in 1992, is the United States of Europe, as the European Community agrees to act as a single economic unit. Many changes are in store for agricultural trade.

And what about Eastern Europe? Changes in politics and economy taking place there will mean change again in trade policy. Not only do these affect the U.S., they may affect how Europe finally decides to unify itself.

And then there is plain old competition. How will U.S. fare in a world where ever more players have feed and food to sell?

Let's look at all of these.

EXPORTS. Argentina and Canada are back. That's bad news for U.S. agricultural exports. Early projections point to reduced volumes and lower prices for most exported bulk commodities this year.

Exports are expected to be down to West and East Europe, but up significantly to the USSR and several Asian countries, particularly Japan. Modest increases in sales value also are expected to the Middle East, Africa, Latin America, Canada and Oceana.

U.S. agricultural exports are expected to rise in 1989 by $4.7 billion to $40 billion. But agricultural imports for fiscal 1989 are expected to reach a record $21.5 billion. Still, the overall result will be an increase in the current agricultural trade surplus of $4.2 billion to a net value of $18.5 billion in fiscal 1989.

Preliminary estimates for fiscal 1990 point to a decline in U.S. agricultural exports, reflecting both to reduced volume and lower price for most bulk commodities. This will be caused by a rebound in crops and exports by Canada and Argentina and near-record exports by the European Community.

Is this slowing trend temporary? Or does it indicate a longer-term change? It is hard to say.

The rapid expansion from 1986-1988 was fueled by a number of factors. Primary among these was somewhat improved general economic growth, especially in some lesser developed countries (LDCs), lower U.S. price support loan rates and more competitive pricing and bold new initiative for these negotiations. The U.S. proposed that all subsidies and import barriers that interfere with agricultural trade should be eliminated. This position was supported by other exporters but opposed by importers, especially Japan and the European Community.

The U.S. persisted and negotiations on agriculture blew up at a mid-term review in December 1988 in Montreal, Canada. With a new president of the U.S., talks resumed and agreement was reached to continue negotiating to "ratchet down" the levels of protection for agriculture.

OБSTACLES. Major change will be hard to achieve for several reasons. First, large adjustment costs will fall on some countries, particularly on those with large numbers of small, inefficient farmers.

In addition, countries have different objectives in formulating agriculture and food policy. This is particularly important in countries such as Japan—as well as many LDCs—where food security is a major policy objective.

Most countries, including ours, have political systems that will have difficulty dealing with major change after years of building numerous vested interests in agricultural programs.

But one of the biggest obstacles is that not all of what should be discussed is being discussed. A major cause of distortion in international agricultural markets not being discussed is state trading.

This form of trading predominates in socialist countries, but also exists in non-socialist countries through such things as the Japanese food agency, the European tender system for exports, the U.S. Export Enhancement Program, wheat boards in Canada, Australia and South Africa and some of the cooperatives in Scandinavian Countries.

SOME GAINS. Expect a move toward reduced interference in markets and lower levels of agricultural protection.

Costs to governments have become very high and in some countries, consumer costs are also high. Many countries are less enamoured with farm programs than they used to be.

This, and the idea that improved food and grain distribution would be of benefit to the world as a whole, should
lead to some gains in the current round of trade negotiations. The basic question is: What kinds of agricultural protection will continue and how much government management in the food system will remain?

LDCs represent a second key determinant of long-term improvement in foreign markets for U.S. farm products. Several characteristics of these countries show that, under the right circumstances, they may be important growth markets for U.S. agricultural exports.

Their population is growing rapidly and is expected to represent 57% of world population by the year 2000. This is a change from 51% in 1980 and is a major demographic shift. If this population increase can be augmented with meaningful economic growth, their food needs will increase substantially.

But their economic growth is limited by existing debt burden, now approximately $1.2 trillion. In some countries, debt servicing requires up to 40% of export earnings, creating a major purchasing power gap that hurts economic growth and reduces import potential.

The U.S. and other industrial countries need to view this problem in two policy contexts. One is to remove barriers against their exports, especially processed and semi-processed products.

The second is to provide debt relief for a number of countries with exceptionally high burdens.

**CHANGE IN EUROPE.** Two major uncertainties exist that cloud the potential for growth of U.S. agricultural exports. One is the formation of a more fully unified European Community by 1992; the second is the disintegration of the Communist Bloc in Eastern Europe.

About one-quarter of the 279 changes proposed for the European Community in the Single European Act of 1987 relate to agriculture. Few will directly affect the U.S. except the phyto-sanitary regulations, particularly the import ban on livestock products where growth hormones are used.

Major overall differences may result from changes in the climate for industrial trade and in changes brought about when and if a monetary union, a single European currency and central bank evolve. It is hard to say, at this time, how this will affect agriculture.

What the changes in Eastern Europe will mean for agriculture are completely obscure at this point. Due to mismanaged agricultural economies, the potential for increased food imports exists, at least in the short-run. But in the long-run, improvement in agricultural efficiency could result in a significant increase in agricultural production in the region. While not predictable and completely beyond U.S. influence, how the demand-supply relationship for food and agriculture in Eastern Europe and Russia evolves in the future is of major importance.

It is clear that future U.S. policy must be consistent with continued reliance on international markets. This implies a set of long range objectives that include:

- Maintaining international competitiveness, avoiding policies that obscure our comparative advantage.
- Reducing production costs including continued development of new technology and applied research and education.
- Continued efforts to reduce trade barriers.
- Continued emphasis on promoting global economic development through direct assistance to LDCs.
- Maintaining economic and trade policies that do not penalize LDCs.

These, along with internal objectives related to promoting soil conservation and pollution control, as well as reducing government costs with increased reliance on markets to generate farm income, provide a focus for future U.S. farm policy.

**Shaping the Farm Bill**

A major theme in writing the 1990 Farm Bill will be flexibility to deal with undesirable impacts of existing programs.

High corn program benefits diverted soybean acreage into corn. The resulting shortage contributed to high soybean prices, a diminishing ability of the U.S. to satisfy export demand and expanded soybean production in other countries.

Similarly, land that might otherwise have produced oats was used in the more generous barley program, causing a search by domestic buyers for foreign sources of oats. Environmentalists also argue that program rigidities create barriers to the adoption of more environmentally sound production practices.

Three proposed approaches have emerged to permit farmers more flexibility in making planting decisions.

**THREE OPTIONS.** One approach is to implement a three-tiered base for each crop on each farm. This would include acres planted to program crops eligible for deficiency payments and acres planted to other program and non-program crops with no payment.

A second approach would establish a whole farm acreage base to replace current commodity-specific acreage bases. Program crops would not be allowed on acreage in excess of the farm acreage base (FAB), but there would be no restrictions on the mix of program crops to be planted.

The third is to implement specific flexibility provisions, such as those that were part of the Drought Assistance Act of 1988. Then farmers with a corn base could plant up to 10% of their base to soybeans without losing corn base.

These and possibly other alternatives will be debated. Support for maintaining the present system with no change also exists, based on the argument that flexibility is a back door to decoupling, which is opposed.

Other possible changes in commodity programs that have been proposed include:
- freezing target prices at their current levels.
- making deficiency payments on a historic crop program base used to create the FAB, with an option for farmers to lock in their payments, similar to the way it is used in the 0-92 option.
- developing a multiple one- to five-year Paid Land Diversion Program enrolled on a bid basis and targeted at erodible or otherwise fragile land.
- expanding Conservation Reserve Program eligibility beyond highly erodible acres to include areas of strategic environmental concerns—however that is
defined.

While some of these suggested changes could be significant, it is apparent that all represent marginal adjustments to the 1985 Farm Bill. No proposal for a major restructuring of the 1985 Farm Bill has emerged, nor is one likely to.

A few lonely voices continue to call for high support prices and rigid acreage and production controls as a preferred approach to farm policy. This approach, however, appears to have no political viability.

ENVIRONMENT. Another dimension of debate in the 1990 Farm Bill will center around conservation and environmental protection. A confluence of circumstances and objectives brought commodity price support policy together with soil conservation policy to create a conservation title in the 1985 Farm Bill.

Large commodity surpluses made a long-term program of cropland retirement attractive as a means of helping balance supply and demand. At the same time, there was substantial evidence of serious erosion on large amounts of cropland, much of it brought under cultivation in the 1970s.

The 1985 Program centers around conservation compliance, Sodbuster, Swampbuster and the Conservation Reserve provisions. Incentives to participate in the first three of these is based on retaining eligibility for a range of farm program benefits, particularly those related to commodity policy.

The suggestion has been made that additional programs such as water subsidies be a foregone government benefit if there is non-compliance, or that conservation requirements be incorporated through the Farm Credit System.

Following their success in adding a conservation title to the 1985 Farm Bill, conservation groups will be very active in 1990. A new title dealing with environment and water quality may well emerge.

Concerning the CRP, environmentalists favor a reserve program with objectives beyond reduced soil erosion to include pollution control, flood control and improvement of wildlife habitat. This would require a broadening of land eligibility criteria. Conservationists will push for incentives and controls on practices aimed at both groundwater and surface water quality protection.

Another issue will be water conservation. Irrigated agriculture is a large, consumptive user of water. Another element of conservationists concern is to incorporate incentives in the farm bill to promote sustainable agriculture.

OTHER ISSUES. Several other issues will receive attention. Food quality and nutrition for some segments of the population will be of concern. Food safety, however, will be the big consumer issue following media coverage of the Alar problem with apples, feed additives for livestock and BST for dairy cattle.

Rural development seems to have emerged as a focus of interest in Congress. Only 702 of the U.S.'s 3,069 counties are farm dependent—defined as counties where 20% or more of total labor and proprietary income is from farming. This has led to concern with how the total economy of rural areas can be strengthened, including development of business, industry and infrastructure, as well as institutional and human development.

Farm finance and credit will also likely come in for some attention, particularly as these relate to operations of FmHA. In light of continued losses, Congress may wish to evaluate FmHA lending practices, as well as the extent to which the shift from direct lending to a loan guarantee program should continue.

Finally, some attention will be given to research and education funding at the federal level. Two aspects seem to be of particular concern: research to improve international competitiveness of American agriculture and research related to low input agriculture and its implications for conservation and improvement of the environment.

OUTSIDE INFLUENCES. Two points need to be noted about how farm legislation will develop in the next couple of years. One is that legislation is broadening in its coverage and participants are more diverse. Commodity price supports are no longer the single central issue and the agricultural community is no longer the single dominant political force. Consumer groups and environmentalists will have an increasing and possibly dominant role in developing and implementing farm legislation.

The second point is that the process of developing legislation may be a two-stage affair. In 1990, some "operating" changes likely will be made in some programs.

But, fundamentally changed farm legislation could emerge in 1991, if the Uruguay Round negotiations achieve reductions in trade barriers. This is the hope of the current administration and as is said, "This Farm Bill will be written in Geneva."

—Vern Sorenson

Export Values Rising

Total value of exports rose from $26.3 billion in 1986 to $35.3 billion in fiscal 1988, an increase of 34%. Export volume went up from 109.5 million tons in 1986 to 148.3 million tons in 1988, an increase of 35%.

The most recent USDA forecast for fiscal 1989 is that the value of exports will again increase by $4.7 billion. This is due to grain and oilseed prices being well above a year earlier and a record level of "high-value" exports. Export volume, however, is forecast at 147 million metric tons (MMT), slightly below the 1988 level.

Changes in 1989 differ among commodities. Export value of wheat and flour will increase in excess of $2 billion, whereas export volume will decrease by about 3 MMT.

Both value and volume of coarse grain exports, on the other hand, are expected to increase. Demand for coarse grains has risen throughout 1989, largely due to increased buying by the Soviet Union, Mexico and South Korea.

Oilseed and product exports are estimated at $6.7 billion in 1989, down from $7.8 billion in 1988. Contributing to this reduction are higher U.S. prices and lagging European Community demand for soybean products, weak foreign demand for vegetable oils and record Brazilian soybean production and exports.

Livestock, dairy and poultry exports are expected to reach record levels in fiscal 1989. This upward adjustment is due primarily to strong demand for live animals and red meats. Demand for red meats has been especially strong from Japan, South Korea and Mexico.