

POLICY MINUTE

February Prices and Farm Bill Decisions

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On February 11, USDA issued its monthly report of supply and demand estimates for major U.S. agricultural commodities. Just a few days earlier, on February 7, USDA also released its long-term annual projections through 2012. These projections are in a report titled "USDA Agricultural Baseline Projections to 2012" and are available on the website of USDA's Office of the Chief Economist at www.usda.gov/oce.

These reports provide a guideline in setting price

expectations for the coming years. And, as noted in previous issues of the *Policy Minute*, there is an inverse relationship between expected prices and expected counter-cyclical payments under the new farm program. Table 1 provides the USDA price estimates and the corresponding expected counter-cyclical payments.

The combination of the USDA Supply and Demand Estimates and the Agricultural Baseline Projections provide one series of prices that may

Table 1. USDA Price Estimates and Expected Counter-Cyclical Payments, February, 2003.

Price Series and Crop Year	Corn	Sorghum	Barley	Oats	Wheat	Soybeans
USDA Supply & Demand			(\$/bushel)			
2002/2003 Price Forecast ^a	2.35	2.40	2.70	1.75	3.60	5.40
2002/2003 CC Payment ^b	0.00	0.00	0.00	0.00	0.00	0.00
USDA Baseline			(\$/bushel)			
Price Forecast^c						
2002/2003	2.40	2.45	2.60	1.80	3.80	5.40
2003/2004	2.20	2.10	2.35	1.35	3.25	5.15
2004/2005	2.10	2.00	2.30	1.25	2.95	5.00
2005/2006	2.10	1.95	2.30	1.25	2.85	5.05
2006/2007	2.15	2.00	2.30	1.30	2.85	5.10
2007/2008	2.20	2.05	2.35	1.30	2.90	5.20
CC Payment^d						
2002/2003	0.00	0.00	0.00	0.00	0.00	0.00
2003/2004	0.12	0.09	0.00	0.026	0.09	0.21
2004/2005	0.25	0.22	0.00	0.086	0.45	0.36
2005/2006	0.25	0.27	0.00	0.086	0.55	0.31
2006/2007	0.20	0.22	0.00	0.086	0.55	0.26
2007/2008	0.15	0.17	0.00	0.086	0.50	0.16
Average CC Payment^d	0.16	0.16	0.00	0.06	0.36	0.22

^a Based on midpoint of price range of USDA Supply and Demand Estimates, February 11, 2003

^b Counter-cyclical payment rate based on national marketing year average price equal to midpoint price estimate.

^c Based on "USDA Agricultural Baseline Projections to 2012" released on February 7, 2003.

^d Average counter-cyclical payment rates over 2002-2007 crop years, based on national marketing year average price estimates for 2002/2003 through 2007/2008 in the table.

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Table 2. KSU Price Estimates, February 2003^a

Crop Year	Wheat		Corn		Grain Sorghum		Soybeans	
	Price	CC Pay.	Price	CC Pay.	Price	CC Pay.	Price	CC Pay.
	(\$/bushel)							
2002/2003	3.55	0.00	2.31	0.01	2.26	0.00	5.39	0.00
2003/2004	3.26	0.08	2.34	0.00	2.15	0.04	5.08	0.28
2004/2005	3.27	0.13	2.31	0.04	2.14	0.08	5.28	0.08
2005/2006	3.28	0.12	2.30	0.05	2.14	0.08	5.40	0.00
2006/2007	3.29	0.11	2.29	0.06	2.13	0.09	5.47	0.00
2007/2008	3.29	0.11	2.29	0.06	2.13	0.09	5.51	0.00
Average CC Pay ^b		0.09		0.04		0.06		0.06

^a Estimated from KSU price forecast model on February 11, 2003.

^b Average counter-cyclical payment rate over 2002-2007 crop years, based on national marketing year average price estimates for 2002-2007 in the table.

be used to calculate counter-cyclical payments for the life the farm program. Another possible series is based on a price model developed at KSU by Ag Economics Extension Specialist Terry Kastens. Using a futures-adjusted mean-reversion model, commodity prices from February 11, 2003 were used to estimate prices and government payments over the life of the Farm Bill. Those prices and resulting average counter-cyclical payments are shown in Table 2.

Comparing the two price series, there is a substantial difference in the estimated prices and thus the estimated counter-cyclical payments. The USDA projections assume significantly lower prices and thus higher counter-cyclical payments over the life of the current farm program. As to which projection is more accurate, only time will tell. They both represent current information and expectations, but are reliant on different modeling procedures. The USDA projections come from an inter-agency working group in USDA that analyzes the current situation and projected economic trends to arrive at their baseline projections. The KSU projections are based on information currently known and traded by the marketplace, using futures-adjusted prices and historic price relationships to develop long-run price projections.

The different price series will impact the expected counter-cyclical payments. Remember that changing prices can change expected counter-cyclical payments, and changing counter-cyclical payments can change the optimal base and yield

election. So, the decision of which price series to use, or the decision to use yet another series, must be made by the producer with careful consideration. For most, analyzing the decision under various price scenarios will simply prove the stability of their optimal decision, but for some, the specific price scenario used will play a critical role.

If you are considering using either price series with the KSU Farm Bill Spreadsheet, please note that the spreadsheet currently has three price series built in as options. The first is a set of producer-provided price expectations. The second is a series of price projections from FAPRI, and the third is the USDA series from February, 2002. While this new USDA series effectively replaces the old USDA series, we will not be issuing a new version of the spreadsheet just to make this change. Instead, if you are using either the new USDA series or the KSU series, simply enter those numbers in the section for the producer-provided price series. That requires a bit more input on each individual analysis, but it avoids making all of the analyses done previously look incorrect simply because the spreadsheet version number would have changed.

Remember that the deadline for making the base and yield election is coming up on April 1. So, the time to complete this analysis and make a decision is quickly disappearing. Payments due to producers await this decision and sign-up, so there is little reason to wait any longer when completing this analysis and making a decision.