

Frontiers in Agricultural Policy Research: Discussion

Bob Richardson*

In the distinguished company of Fisher and Edwards, I presume I was asked to discuss the paper from a pragmatic perspective of one relatively more exposed to some types of economic policy makers. My experience in that regard is limited to the Australian Wool Corporation, but when one considers the past enthusiasm of agricultural policy analysts for studying the economics of policies in the wool industry, that experience is perhaps of some relevance.

In the interests of a clean kill, I first want to carefully appraise the target. As I read Brian's paper he is rejecting a suggestion by Bruce Standen (1983) in his 1983 Presidential address that policy analysts are too preoccupied with allocative efficiency, in favour of an hypothesis that we agricultural economists lack relevant data and have an inadequate understanding of human behaviour.

In seeking to elaborate this point Brian reviews the four areas of stabilization policy, the role of expectations, the economics of regulation and competition in agriculture. There seems little in the subsequent sections of the paper to amplify the rejection of Standen's position or to support acceptance of the alternative advanced by Fisher, except to the extent that rational expectations theory is an hypothesis about human behaviour. There are, however, several avenues of further research suggested which are of interest:

(1) *Stabilization Policy*

Brian suggests that analyses should more explicitly incorporate risk, as proposed by Newbery and Stiglitz (1981), that more work should be done on the risk aversion of producers and more flexible functional forms, and that futures markets (and presumably their relationship to private stockholding) affect the viability of price

stabilization schemes. While agreeing that these are important issues I would add the following:

- first, the impact of exchange rate volatility on the value of stabilization measures and how that might vary depending on whether supply or demand volatility is the key source of instability;
- second, questions of the distribution of risk and its redistribution as a consequence of stabilizing intervention. In this regard risk attitudes of buyers and marketing firms are relevant and a paper by Spinks and Monty (1985) is relevant to that issue, as is earlier work by Quiggin (1983) in wool demand;
- third, I consider that the pros and cons of buffer fund schemes as an alternative to buffer stocks is not a dead issue and could be further researched as a policy option.

I may be wrong but I would judge the hidden gains and losses argument about the impact of the reserve price scheme for wool to have reached something of a stalemate following the work of Campbell *et al.* (1980). Avenues for progress may include analysis of the relationship of wool price variance to producer risk attitudes and of supply response to the policy instrument.

(2) *Expectations Formulation*

As you all know Dr. Fisher is something of an enthusiast for the theory of rational expectations and its empirical application to questions of agricultural policy intervention.

*Australian Wool Corporation. Paper presented at the 29th Annual Conference of the Australian Agricultural Economics Society, University of New England, 12-14 February, 1985. Views expressed are not necessarily those of the Australian Wool Corporation.

He has not let this opportunity to push that particular barrow pass in the paper but in his presentation acknowledged the existence of a risk that you would be bored.

I agree with Brian about the importance of assessing the rationality or otherwise of producers expectations. However, I would go a step further in making his point about unanticipated policy changes *causing* economic variables to deviate from their long term trends. I believe that, to the extent that we have any intervention in markets, the policy ground rules must be predictable and announced in advance. In this regard the past practice of using flexible reserves in the wool market, which could be changed at will, probably created as much or more uncertainty as it removed.

Brian suggests the use of combined cross section and time series data to identify the joint relationship of risk attitudes and the form of expectations. I would support this suggested area of research in the belief that more intensive, albeit more costly, survey data may be a more reliable guide to a range of long term parameters relevant to agricultural policy research.

While appreciating the significance of whether expectations formulation is rational or not and the implications for risk distribution, benefits and costs of policy intervention etc., I wonder whether, with the passing of time, the theory of rational expectations will be consigned a similar grandstand seat as other hypotheses about expectations formulation.

(3) Economics of Regulation

The paper contains very little in the way of suggestions for agricultural policy research on the economic consequences of regulation. This is probably attributable to the argument, developed in the paper, that costs sunk in rent-seeking by those trying to get greater regulation are not readily recoverable subsequently through deregulation, unless by "regular reviews". Put another way, it is being

suggested that those seeking regulation generally over-estimate the *net* benefits to them because they ignore or under-estimate the costs of getting the regulations introduced.

I do not share the implicit view that there are not great policy research priorities in the area of regulation, if only to assist rent-seekers in their prior appraisals of expected returns from their endeavours. Aside from economic analyses backing a continued programme of IAC enquiries and reviews, I believe there should be a programme of economic research of an empirical nature on the consequence of additional intervention. As a framework for that it can be argued that the existence of substantive and demonstrable "market failure" is a *necessary* condition for intervention. In the case of intervention by Statutory Marketing Authorities (SMAs), a *sufficient* condition is that they first have to be shown to be the best way to overcome "market failure" in terms of expected net social benefits.

In terms of policy research implications, empirical analysis can and should be undertaken to identify the existence or otherwise of "market failure". Areas in which that analysis may be directed include:

- the level and type of funding of research;
- transfer of technologies developed in research through to commercial adoption;
- efficiency of forward pricing and intra-temporal stockholding mechanisms (in this regard Brian refers to the impact on risk distribution through futures markets, but I would also add forward contracting arrangements which are important in many agricultural commodity markets); and
- the level and type of promotion of products which I believe is becoming a more important and potentially wasteful form of intervention in some commodity markets.

An area in which we presently appear to have little information, and even less analytical results, to guide policy formulation is in marketing and promotional policies. I would argue for more research in this area of

an analytical type using cross sectional data on consumers and surveys of intermediary marketing firms. Eventually we could and perhaps should be devoting similar effort in this area as we presently do, through the BAE, to surveys of producers in the various industries.

To return to one of Brian's general points about the inadequacy of data available to economists to analyse agricultural policy questions, the informational requirements for analyses of these forms of alleged market failure are indeed substantial.

A further comment I would wish to make on Brian's view about the magnitude of benefits from deregulation relates to current government initiatives to deregulate SMA's and make them more accountable to the industries in which they intervene. Acceptance of Brian's argument would, I believe, lead to a conclusion that the present government proposals for deregulation will have their primary impact in changing the ground rules for (and the costs of) rent-seeking activities, rather than producing net benefits to the rural industries in question. For wool, my understanding of history leading to the introduction of the Reserve Price Scheme is that it was not the rent-seekers but the vote-seekers who took the initiative in promoting intervention.

(4) Competitiveness in the Rural Sector

In respect of the data and informational requirements to use the tariff compensation argument and assess competitiveness, I agree with Brian's suggestions for further research on levels of assistance, capital formation and investment in agriculture and soil conservation issues.

Conclusions

I generally agree with Brian's conclusions of

- greater attention to risk attitudes,

- more emphasis on expectations formulation, and

- increased efforts to estimate the magnitude of consequences of policy intervention.

On the question of Fisher vs Standen (i.e., whether it is data problems and failure to understand human behaviour or a preoccupation with questions of efficiency which has limited the contribution of economists to agricultural policy formulation) the issues are complex. In my view the contrasted positions posed by Fisher are really alternate views of the extent to which economists should:

(a) address policy issues in the context of a rigorous efficiency oriented framework of neoclassical economic theory (even accepting the subjective aspects noted by Hardaker (1985)),

OR

(b) seek to understand the preferences of policy decision makers (who are often themselves rent-seekers or re-distributors) and provide them with information with which to rank policy options.

In my view that it is vital we do not resolve this question one way or the other, but that there is healthy debate, from both perspectives, on central questions of agricultural policy. I, like Bruce Standen, see many issues from the latter perspective of perhaps being closer to the policy issues facing an industry and a group of self professed decision makers.

Decision makers often appear to focus their requests for information, by accident or design, in areas where there is little or no data and/or where there are few criteria for discriminating between alternatives.

It reminds me of a story Warren Musgrave plagiarised from somewhere about the drunk econometrician who, well after closing time and having lost his car keys, was found searching for them under a street light, not because that was where he thought they were lost, but because that was where he could see.

References

- CAMPBELL, R., GARDINER, B. and HAZLER, H. (1980), "On the hidden revenue effects of wool price stabilization in Australia: initial results", *Australian Journal of Agricultural Economics* 24(1), 1-15.
- HARDAKER, J.B. (1985), Beliefs and values in agricultural economics research. Presidential address at the 29th Annual Conference of the Australian Agricultural Economics Society, University of New England, February 12-14.
- NEWBERY, D.M.G. and STIGLITZ, J.E. (1981), *The Theory of Commodity Price Stabilization: A Study of the Economics of Risk*, Clarendon Press, Oxford.
- QUIGGIN, J. (1983), "Wool price stabilization and profit risk for wool users", *Australian Journal of Agricultural Economics* 27(2), 31-43.
- SPINKS, M. and MONTY, C. (1985), An economic evaluation of additional measurement in wool processing. Paper presented at the 29th Annual Conference of the Australian Agricultural Economics Society, University of New England, February 12-14.
- STANDEN, B.J. (1983), "Agricultural policy formulation: the differing functions of independent analysts and advisors", *Australian Journal of Agricultural Economics* 27(2), 93-103.