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# POLICY ISSUES IN AGRICULTURAL TRADE

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The Nixon round of trade negotiations opened in Tokyo on September 12, 1973 amidst uncertainty and hopeful expectation. World leaders once again began the search for cost-cutting ways to expand the interchange of world goods and increase the gross international product (GIP). The most unusual aspect of this latest round of negotiations was the cloudy atmosphere surrounding agricultural trade. It was not entirely clear from the opening sessions whether negotiations would deal with ways of lowering agricultural import barriers or concentrate on ways of removing food export controls.

The American delegation, led by Treasury Secretary George Shultz, reassured the 600 delegates that despite the recent embargo on soybean exports, the United States does intend to share its grain and oilseed crops with other nations. But Shultz did not stress long-held goals of lower world trade barriers. Instead, he spoke of allocation problems arising from short food supplies. "The current shortages in agricultural supplies and the danger that it will be repeated in the future," Shultz suggested, "give great urgency to the need to find a more rational pattern of production and trade in agricultural commodities." It was an unusual opening statement and reflected the astonishing turnaround of world agricultural trade conditions of the last twelve months.

Negotiating changes in trade policies that have existed for decades is never an easy task. It is especially difficult when the whole structure of income and employment in the countries involved have adjusted to these policies. Sharp and rapid changes in the rules under which international trade and investment are conducted could alter, even interrupt, the flow of goods and capital. Such interruptions (as we have seen in 1973) have international repercussions even when they result from changes in the market place.

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\*The views expressed herein are the author's and may or may not correspond with those of the Council of Economic Advisers.

Even sharper repercussions could occur if economic rules are changed by man-made negotiations. This reality means that trade negotiations will move forward cautiously. Many believe that at least two years will be necessary before new agreements can be reached. In the case of agricultural trade, a two-year lag may be especially appropriate. It could allow adequate time for the new and vastly different structure of farm prices and incomes to stabilize. The present uncertain agricultural outlook makes an unstable foundation on which to negotiate new trade relationships.

#### ISSUES AFFECTING AGRICULTURAL TRADE

In an uncertain world, U.S. agricultural exports have always contained an element of uncertainty. In 1973–74, however, there is an added anxiety; it is the outlook for world food balances. The worldwide balance between future supply, future demand, and future stocks of grain commodities will play a major role in trade. These balances will determine future levels of trade and levels of trade barriers—not to mention levels of grain prices and grower incomes. Nothing removes trade barriers more rapidly than shortages of food. Two recent events prove this point: the reduction to zero of the EEC variable import levy for grains and the relaxation of U.S. import restraints on meat and dairy products.

Chronically food-short nations are particularly affected by the present food outlook. But even some U.S. consumers have faced shortages of certain kinds of food. Low-income families in this country may have actually reduced total food consumption this past year as food prices increased sharply. The causes for the price rises are complex. One big factor was rising incomes in other nations. Consumers from other countries could afford to bid food away from American consumers. Our low-income consumers could not compete; they did not have the purchasing power. Moreover, even high-income consumers were in a weak bargaining position because of price control programs.

Per capita food consumption is declining in spite of the fact that U.S. domestic food distribution programs have expanded. In 1973 the government provided about \$3.9 billion of purchasing power through food stamps and other programs. For the first time in modern times, outlays for domestic food distribution programs will exceed outlays for supply control programs.

There are unanswered questions concerning the future, however. Will American consumers have to continue bidding food supplies away from other nations' consumers? Or will American taxpayers have to return to subsidizing farm exports. As long as

these questions go unanswered, future trade prospects will be uncertain.

While there was widespread belief earlier that the United States had considerable excess capacity to produce crops, the record for 1973 is not very reassuring. We have returned 43 million acres of set-aside land to production—with a consequent increase of 25 million acres of harvested crop acres. Despite this 10 percent increase, total crop production is expected to rise only 6.2 percent in 1973. Total farm production, including livestock products, will likely rise by a smaller amount. Even with the higher level of crop production, a level that may be fairly near total capacity, the carryover of grain stocks by mid-1974 will be lower than this year's (Table 1). This lower expected carryover in the United States plus a similar situation for other major grain exporting nations leads to much wonderment about the future. We may experience continuing increases in demand for farm exports next year if world production does not recover further. On the other hand, we could see a substantial drop if world grain production rises sharply or if livestock production in central planned countries is cut back. Demand will almost certainly drop if the economic boom in rapidly developing nations cools down and their consumers back away from eating more meat and protein products.

TABLE 1. JULY 1 CARRYOVER STOCKS OF GRAIN

	Wheat			Feed Grains <sup>4</sup>		
	1971-72	1972-73 <sup>1</sup>	1973-74 <sup>2</sup>	1971-72	1972-73 <sup>1</sup>	1973-74 <sup>2</sup>
	<i>Million Metric Tons</i>					
United States	23.5	11.5	8	68.1	59.5	56
Major competitors <sup>3</sup>	26.0	17.8	17	14.1	16.3	15
Total	49.5	29.4	25	82.2	75.8	71

<sup>1</sup>Estimated on August 10, 1973. <sup>2</sup>Projected on August 10, 1973. <sup>3</sup>Canada, Australia, and Argentina. <sup>4</sup>Corn, oats, barley, and rye.

The worldwide agricultural production situation in 1973 is, from all reports, near normal with no major unexpected shortfalls as existed in 1972. Despite this fact, so much grain will be consumed that carryover stocks of grains will likely be reduced further by next year. We may well face shortages of fertilizer and fuels in 1974. All of these factors will affect total crop production.

I interpret recent events this way: In 1972 we increased exports by using up grain stocks. In 1973-74 we are maintaining those exports by further reducing U.S. stocks, by reducing ship-

ments to soft currency markets, and by using acreage reserves. With only 20 million acres of reserve capacity left to return to production (and much of that of doubtful productivity), it seems clear that we cannot expect further quantum jumps in farm exports. If so, the prospects for using agricultural exports to balance our trade ledger are much more limited than we realized.

### BALANCING OUR TRADE POLICIES

Consider our experiences of the past year: A 60 percent increase in agricultural exports, a 50 percent increase in farm prices, and a 15 percent increase in retail food prices. These provide some very different problems and hypotheses for analysts to grapple with in the next few years. There is, for example, no clear-cut measure of how much of our large increase in farm exports resulted from the devaluation of the dollar, from the worldwide economic boom, or simply from unfavorable weather in other countries. What is more, no ready solutions are evident for the food policy problems that emerged during the past year. The agricultural export situation demonstrates at least one of these problems. It arises as follows.

For several decades, in the United States, price-supported grain supplies have exceeded effective demand with well-known results: stockpiling, resource restrictions, export subsidies, market development and domestic distribution programs. These policies stabilized: the farm sector (though some would argue it was stabilized in a depressed state), the food sector, and the real value of rural assets, especially those of agriculture. As long as agriculture faced overproduction and depressed prices and incomes, the federal government had a relatively effective set of tools to manage the situation.

But what happened when agriculture was faced with excess demand and rapidly rising prices? We did not have a similar set of policy tools to handle this situation. We of the agricultural establishment had not really evaluated such possibilities. Having faced the opposite conditions for so long, we assumed that any period of excess demand would be temporary with reasonable price increases. As a result, no permanent policies were developed to handle the consequence of quantum jumps in demand and prices. We have an unbalanced set of policies that deal with only one of two problematic situations.

The underlying bias that agriculture always tends toward overproduction shows up in many places including the 1969 Report to the President on Future United States Foreign Trade Policy.

That report recommended that "the United States should attempt to obtain acceptance of the principle that price regulation should be aimed at price stabilization alone, and that import charges, other than moderate tariffs, should be limited in their application." The report went on to outline how import restraints should be modified. It did not mention export controls, export embargoes, wheat marketing board restraints, or the use of export taxes. It did not, in fact, mention any of the many ways in which nations in 1973 limited food exports to encourage internal price stability. The limitations mentioned were those used to restrict the expansion of agricultural imports, not exports. This clearly indicates that continued excess capacity was expected. In 1969, few analysts of trade relationships envisioned any need even to discuss restraints on agricultural exports. Certainly, none foresaw the actual application of export restraints in 1973.

We have all kinds of programs to stabilize agriculture when we have excess supplies: set-aside programs, price-support programs, resale programs, demand creation programs, and import limitation programs. We have almost no policies to handle conditions of excess demand beyond the sales of available grain stocks and the use of set-aside acres. Our policies are one-sided because the historical perspective has convinced us all that a more balanced set of policies is not needed.

Perhaps the prospect for the long term is excess supplies. Nevertheless, agricultural economists should closely scrutinize events of the past year. The nation pays dearly for extreme variations in food prices with their secondary and tertiary impacts on wages and, ultimately, industrial prices. The past year's rises in food costs, lumber costs, and cotton and fiber costs are going to raise all living costs during the next few years and result in continuing inflationary pressures.

Balance is just as essential in food policy as it is in wage policy. It is just as necessary in export policy as it is in industrial price guidelines.

In the trade area, policies have also been oriented toward excess supply conditions. We have a whole set of export subsidy programs. Many kinds of assistance are available to bolster export sales if demand in world markets drops: technical advice on handling sales to foreign buyers, programs to introduce our food products to foreign consumers, low-cost credit programs to encourage sales, and many other types of programs. We also have a carryover of legislative actions that restrict imports of various goods.

But if demand suddenly shifts upward as it did in 1965–66 and in 1972–73, almost no policy responses are available except those with unacceptable foreign policy repercussions. We need to think through and outline a balanced set of trade policies: to handle both familiar conditions of excess supply and newly met conditions of excess demand. Public policy analysts have plenty of hard intellectual work ahead of them in this area.

**LONGER-TERM TRENDS IN AGRICULTURAL TRADE**

For years the major objective of U.S. participation in trade negotiations has been to expand farm exports. In 1972, 1973, and in all likelihood 1974, we have expanded farm trade beyond our most optimistic expectations. Until 1972, the main restraints to expanded farm exports were the import policies of other countries. In 1973, our major restraint turned out to be our shrinking supplies.

Despite the optimism concerning the short-run outcomes, long-range trends in agricultural trade are posing problems, especially in relationships between developed and developing countries. The developed countries have many export options available to balance their trade ledgers. The developing countries have far fewer export alternatives because agriculture and raw materials make up a major share of their gross national products. For these nations to continue developing, they must import industrial goods. For these nations to export, there has to be a demand for the products of a labor-intensive, primary sectoral economy.

The trends in world trade have not favored labor-intensive enterprises of the developing nations in the last twenty years. In a paper nearly two years ago Arthur Mackie used the data in Table 2 to show that the market share of these nations in both total exports and agricultural exports is declining. While the dollar value of developing countries' exports has increased, the real value of their exports has been fairly constant. It is almost certain that the situation has worsened during 1973, especially for food-deficit

TABLE 2. MARKET SHARES OF WORLD EXPORTS

Group of Exporting Countries	Total Exports			Agricultural Exports		
	1955	1960–64	1965–69	1955	1960–64	1965–69
	<i>Percent</i>					
Developed	65	68	70	45	52	55
Developing	25	20	19	45	37	34
Central Plan	10	12	11	10	11	11
Total	100	100	100	100	100	100

SOURCE: Iowa State University Center for Agricultural and Rural Development, *U.S. Trade Policy and Agricultural Exports*, Iowa State University Press, 1973, p. 70.

developing countries. Food imports have expanded to offset shortages due to unfavorable weather and growing populations. The result is very high market prices at the same time that levels of concessional grain exports are being reduced. Where will this leave these countries in another decade if present market conditions for food continue? This issue is receiving too little attention from foreign trade analysts. It seems likely that the result will be either a further drop in consumption levels for the poorest of the poor in these nations, or a growing debt burden for these nations in future years. Neither of these outcomes moves us toward the goal of a reasonably well adjusted and smoothly operating world trade system.

#### **NEW REALITIES IN AGRICULTURAL TRADE**

Events of recent months have brought something new to our attention. In earlier times, discussions on agricultural trade largely ignored the domestic food situation. But as government stocks have disappeared and as exports and prices of grain and oilmeals have soared, it has become much clearer that domestic and export markets are more closely related than we acknowledged. Prospects for meat production, and especially pork production, have gone from moderately good to poor to bleak in a period of only a few months. Expanding exports raised grain prices and despite corresponding rises in pork prices that generally held the hog-corn ratio at levels that used to be conducive to expanded pork production, farmers continued to sell off breeding stock. This action started late in 1972 and continued through mid-1973. With farm income levels up and exceeding all-time records, farmers may not expand total livestock production in the near future.

Given time, grain and livestock prices will assume levels that will lead producers to supply U.S. consumers with growing quantities of pork, milk, and eggs. But it may mean that the structure of agriculture will change. Pork production may become concentrated in specialized producing units as more and more grain producers follow the lead of cash grain farmers in Iowa and Illinois, and move away from livestock production. Labor-intensive enterprises like dairying, and even beef and pork production, may follow vegetable production into Mexico and other lower wage countries.

Whatever the final outcome, it seems clear that the strong export demand of 1972-73, if it continues, is going to reverberate on this nation's agriculture for some time. It will have an impact: first on the value of fixed farm assets, next on the cost of living and hence on wage rates, and ultimately on the prices of services and industrial products.

A different world was spawned forth in the past year. We have experienced fluctuations in farm prices and incomes that few of us ever imagined could occur. We have been faced with shortages, soaring prices, and unimaginable public clamor. Perhaps supplies of grain will expand next year and provide some measure of insurance against world shortfalls. But changed world monetary relationships, coupled with improved consumer purchasing power in many nations, are going to keep our agricultural sector from returning to pre-1972 conditions. Farmers may well experience some very sharp cycles, however, if we continue to have policies that allow prices to soar so far above support levels. Our present policies deal only with the downside of agricultural price trends, and today we are far away from that downside.

The time has arrived for a new assessment of the environment surrounding farm prices, income, employment, and trade. Someone must examine the world implications of energy and resource shortages. These shortages create a tendency toward overheating economies with rising consumer incomes and inflationary pressures on consumer prices. The old price, income, and employment theories assumed tendencies toward underutilization of productive capacity, underemployment of labor and land, and long-term declines in real food and resource prices. The new reality is far different, and policies and programs based on old assumptions are ill suited for handling the new problems. It is, in short, a time of change. It is time to reexamine our traditional assumptions if we are to offer realistic advice and assistance for the future.

The task faced by our representatives to the Nixon round of trade negotiations is large and loosely defined. So is the task facing public policy analysts. Sometimes I think that economic intelligence also takes one step backward for each two steps forward, as Secretary Shultz says of trade negotiations. Your job and mine is to ensure that economic intelligence does not take two steps backward for each step forward.