

The Imperative of Successful Competition

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It is an accepted fact that international markets are necessary to the well-being of U.S. agriculture. The importance of our agricultural base in this country is underlined by the fact that the food and agricultural complex accounts for about one-fifth of our gross national product, with assets exceeding \$1 trillion. It is also the nation's largest employer, providing **23** million jobs, most of them off the farm.

The role of exports in U.S. agriculture — and the nation — is crucial. About one out of every three harvested acres goes to foreign markets around the globe and farmers in recent years have looked to exports for up to one-fourth of their marketing income.

We are fast reaching a point where we need only **50 percent** of our agricultural resources to feed and clothe ourselves. Of necessity, we have increasingly turned to foreign markets as outlets for the remaining production.

Farming has become a business of life as much as a way of life, and today one American farmer produces enough food to feed 77 people. Similar changes in agriculture have been taking place to one extent or another in most of the world. Today, in the developed **countries** — when they have the arable land — farmers can produce much more than they consume.

The implications of increased productivity

Virtually everywhere in the world, farmers have more production potential and more incentive to use it. New developments in production technology, aided by genetic engineering, mean that **record-shattering** increases in production may be the norm rather than the exception.

- Chinese farmers are producing record crops of wheat, coarse grains, rice, oilseeds, and cotton.
- New winter barley varieties have added a million tons a year to British cereal production.
- Encouraged by artificially high wheat prices, the Saudis are literally turning the desert green, setting a world record for generating a wheat surplus.

Potential new uses for agricultural products are being discovered almost daily. What were once weeds are now processed into sophisticated pharmaceuticals. Waste products are now animal feed.

Because farmers can produce in surplus, people have been freed from the quest for food and can devote their energies to other pursuits. This abundance is a blessing, but it is also a problem—to the farmer and to government. We cannot seem to agree on what to do about it, and that has become a global issue.

What happens to farmers in Country A quickly affects Country B and Countries C, D, and E to one degree or another. Domestic farm policy has global implications. Someone said that if a farmer in North Dakota sneezes, a farmer in India catches a cold.

I think most nations share the same goals for farmers—a stable income with a fair return for their labor and investment. We all want for our countries an assured, dependable food supply achieved as efficiently as possible.

Where we differ is on how to reach these goals.

Different approaches to agricultural policy

The European Community (EC) uses the Common Agricultural Policy (CAP), which was put in place some 25 years ago. The CAP provides high domestic price supports that are protected for the most part by variable levies on farm imports. The CAP has been more than successful in meeting its goal of helping the Community achieve food self-sufficiency. Once a net importer, the EC has become a huge net exporter of a number of agricultural items.

In Japan, where agricultural land is limited, the policy is to maximize self-sufficiency by maintaining farm income at levels equal to those of urban workers, and to develop secure offshore sources to meet food requirements that cannot be met with domestic production. The United States has employed an ineffective supply management approach.

Whatever the country—the United States, Japan, Brazil, the European Community, Canada, Australia—each has its own system for providing its people with the most reliable food supply based on a sound farm economy. Given the global nature of agriculture, the international effects of these systems are a matter of growing concern. This was not the case in the 1970s, when world trade was increasing at a 15 percent annual rate. It is now clear that domestic farm programs and international agricultural trade policies require greater coordination if we are to achieve greater worldwide agricultural trade liberalization.

Can the United States compete?

Some argue that U.S. agricultural exports have fallen because the United States has lost its ability to compete and its comparative advantage. If we are to have a coherent discussion of competition and comparative advantage, we must first define our terms. First of all, comparative advantage is not the same as competitiveness. A country can experience a loss in competitiveness, while retaining its comparative advantage. A country can be competitive without having a comparative advantage.

The U.S. comparative advantage

Comparative advantage is a statement about the pattern of trade that would arise between countries in the absence of market distortions. A country with abundant natural resources, a high level of agricultural technology, and skilled agricultural management may have more comparative advantage in its agricultural production than in its production of industrial goods.

Such a country will tend to excel in the production of agricultural commodities, which can then be traded to some other country enjoying a comparative advantage in industry. Consumers in both countries will be better off because resources are used efficiently and the two countries can produce more in total than if each attempted to be self-sufficient.

Compared with other countries, the United States during 1970–81 became relatively more efficient in the production of agricultural goods. We increased our agricultural output per unit of input more than the rest of the world. So, with regard to unit costs, it would appear that the United States gained an advantage over other countries during that period. For example, the average productivity of land in the United States increased 43 percent, compared with 22 percent in the

rest of the world.

Just as significant, the **U.S.** agricultural sector has increased its productivity relative to the rest of the **U.S.** economy. This comparison indicates agriculture should clearly be one of our most dynamic growth sectors.

U.S. competitiveness

Competitiveness in the world marketplace is determined not only by comparative advantage but also by government policies relating to farm programs and trade. An export subsidy or price support policy can turn a country that does not have a comparative advantage over other countries in production into a country that has a competitive advantage in exporting.

Movements in exchange rates can affect foreign purchase prices, thereby changing export levels of a relatively efficient country. Thus, concepts of comparative advantage and competitiveness are not always linked due to market distortions caused by government intervention and the effects of macroeconomic policies.

U.S. farmers have a comparative advantage. **U.S.** farms, compared with other farms in the world, are well equipped, well managed, more efficient in size, and better located on larger expanses of fertile soil with a dependable climate. They also are run by profit-oriented farmers backed by extensive research and agribusiness services.

While the United States still has an underlying comparative advantage, several factors have inhibited our competitive ability in world markets.

The shrinking pie—A decline in agricultural trade

The rapid acceleration in world agricultural trade and **U.S.** exports from the late 1970s until 1980–81 was a phenomenon—an aberration. Those were unusual times triggered by unusual circumstances, the combination of which is not likely to be repeated. It was a boom time and the world was caught up in it. It was caused by:

- A lack of supplies available in other exporting countries and short crops elsewhere.—World food shortages brought on by drought, reduced fish supplies, and other food problems made our bargain prices even more desirable.
- An inflationary mentality that led to a credit binge. Buyers were willing to extend themselves in credit obligations without regard to

the real meaning of the debt service load. They made a bet that continuing inflation would ease their debt servicing burden. And credit was fully available, albeit at high rates of interest.

- A burst in buying power. The OPEC oil boom fueled a lot of buying. Even non-OPEC Third World countries, strengthened by loans from OPEC nations, were shopping in the U.S. market.
- A low U.S. dollar relative to other major currencies because of high U.S. rates of inflation at the time.

The bottom dropped out of this market in the early 1980s. Demand for oil fell. OPEC countries tightened their belts and closed their wallets. Some even borrowed money. The U.S. dollar rose to historic highs as we began to slow our inflation rate and yields and production increased in other countries.

Now the phenomenon is over. The current world picture whereby production is growing faster than consumption and consumption is growing faster than trade is not an aberration. After more than a decade of a boom cycle, agriculture—both here and abroad—has serious economic problems. Total world trade in agricultural products has declined during the past five years. The reasons are well known:

- Reduced world import demand because of rising production in countries that had been traditional 'importers.'
- Diminishing buying power. For example, the OPEC bust greatly reduced the buying power in some Third World countries.
- The debt loads of many developing countries and their reluctance to shoulder more debt servicing burdens.

But U.S. exports have declined faster and further than those of the rest of the world. Since 1980, our annual wheat exports have declined 2 million tons while the rest of the world increased its annual exports by 20 million tons. The United States now accounts for 34 percent of world trade in wheat, down from 43 percent in 1980. Our feed grain exports have dropped 12 million tons while the rest of the world increased its exports 6 million tons. U.S. exports of feed grains have dropped from 59 percent of world trade in those commodities in 1980 to 51 percent. U.S. soybean exports have fallen by 3.5 million tons while the rest of the world increased its shipments by 2.5 million. The U.S. share of world soybean trade has dropped from 78 percent to 66 percent.

The big question is why? Some answers include:

- Unrealistically high production incentives that create overproduction, too much supply relative to demand realities. U.S. farm programs have indeed influenced our price competitiveness in world markets.
- Unfair trade practices by our competitors—and some customers.
- Appreciation of the U.S. dollar against currencies of competitor nations.
- Lack of buying power in much of the world.

Many of the factors behind the slump are interrelated. For example, global demand for agricultural imports in recent years fell because of the global recession and the debt problems of some major importing countries.

A reduction in world import demand alone can change the market shares of various exporters, because exporters do not all react the same way to a change in world market prices. Generally, exporting countries with high and rigid price supports and large domestic use relative to exports will be faced with more rapid changes in exports than countries that have low flexible supports that depend heavily on world markets. This partially explains both the rapid growth in U.S. exports in the 1970s and the drop in recent years.

The effect of a strong dollar

Many people are quick to blame all of our export problems on the strength of the U.S. dollar, but in my view its effects are often considerably exaggerated. It is true that a stronger dollar relative to the currencies of importing nations has increased the price of U.S. commodities in the importer's currency. This was particularly evident in the case of U.S. soybean sales to Europe, where inflation was relatively the same as in the United States and imports of soybeans were not affected by duties. The real cost to importers rose 35 percent because of the dollar.

However, in the case of wheat exports, the appreciation of the dollar has been less important to importers, mostly developing countries, because inflation in those countries has more than offset changes in the exchange rate. Consequently, their real costs have actually fallen by about 17 percent since 1979. In other words, the dollar's impact on U.S. exports varies, depending on circumstances in different markets and regions.

Inflexible U.S. farm programs

The strength of the dollar is not the only problem. Our inflexible domestic farm programs make it impossible for U.S. prices to adjust to world market conditions, and we become less and less competitive.

The U.S. price support programs set a floor under domestic and world market prices for wheat, coarse grains, soybeans, cotton, and rice. Ordinarily, when prices fall to the U.S. loan rate, sufficient quantities are withdrawn from the export market to support world prices at our loan rate. The United States absorbs excess stocks by taking grain under loan.

When stocks become excessive, acreage reduction programs are implemented for U.S. farmers. Thus, the United States reduces world market price risks and bears the burden of stock and production adjustments, all at no cost to **producers** or taxpayers in other countries.

At present, the markets are so weak and surplus stocks outside the United States so large that competitor supplies have driven effective world prices well below U.S. loan rates, making the United States uncompetitive. **In effect**, the U.S. loan program operates as an export tax—and a fairly hefty tax at that. Since 1979, loan prices have increased 26 percent for wheat, **38** percent for corn, and 40 percent for cotton. These support price increases—or export taxes, if you **will**—have prescribed a protective price umbrella under which our competitors have expanded production and market shares. The appreciation in the value of the U.S. dollar has simply enlarged the size of the umbrella. In short, U.S. farm programs and loan rates send far more important signals to competitors and importers than does the value of the dollar.

Our price support system provides competitors with price protection that they can get no other way—and it gives them a clear edge in the international marketplace. To the extent that other countries can produce and sell at less than the U.S. loan rate, they have clear sailing in world markets—and they are taking full advantage of the opportunities we are giving them. Production in other exporting countries, and even in many importing countries, has jumped sharply in response to the world price floors given to them by the United States.

While we have been trying to hold down output with government farm programs, the rest of the world has increased its output. Consider these changes since 1980:

- U.S. wheat production is up 6 million tons, but production in the

rest of the world is up 65 million tons.

- U.S. soybean production is up about 2 million tons, but production in the rest of the world is up 8 million tons.
- U.S. cotton production is up 2 million bales, but production in the rest of the world is up 19 million bales.
- U.S. feed grain production is up **39** million tons (with one-third of it in carryover stocks) but the rest of the world has increased its feed grain output **36** million tons (with carryover stocks 15 percent).

Although utilization has continued to increase, production has increased faster.

The fallacy of our supply management approach is that we have controlled the resources (acres) employed, but we have not controlled marketings. As long as technological improvements in agricultural productivity continue, supply management programs without marketing controls are a farce, and doomed to fail.

The impact of foreign trade policies

The policies of other countries in their conduct of trade also have affected our competitive stance in world markets. Competitors use pricing and export marketing policies that affect their competitive positions relative to the United States.

Among competitors, the policies of the EC have had the most significant impact on reducing U.S. wheat and corn exports and reducing world prices of these commodities. High, protected supports generate surplus that is exported by subsidies, changing the EC from a net importer to a net exporter.

Sugar is a prime example. EC policies that encourage sugar production and export of the surplus by using subsidies have contributed to sugar oversupplies and depressed world prices. This has been particularly damaging to developing countries that depend on sugar exports to earn much of their foreign exchange.

In general, the export subsidy policies of the EC have distorted trade and propelled the EC to the front rank in the export of several major commodities and near the front rank in others. There are other examples, that add to the list of trade distorting policies, including policies promulgated by other countries' marketing monopolies.

Trade practices and market access

The U.S. goal in trade policy is twofold: trade practices that are uni-

form and fair—this is the export subsidy issue—and market access.

Improved access to foreign markets for U.S. agricultural producers and exporters has been one of our basic and long-standing goals. Typically, U.S. agricultural exporters are eager to compete in world markets. They seek only the opportunity to compete on an equal basis with other suppliers. But the problems of market access are many and familiar—the EC's variable import levies and Japan's import quotas are only a few of the multitude of border controls that impair the international movement of agricultural goods.

While important gains have been made in past trade negotiations, tariff and non-tariff barriers remain a major impediment. We have strengthened our efforts to reduce these barriers and can report limited but significant success, particularly in pressing the Japanese to open their market more fully to our farm and forest products.

To regain our competitive position, the United States must restructure its domestic programs. Otherwise, we must be prepared for larger and larger production cutbacks and fewer and fewer exports.

Greater market orientation, including market-oriented loan rates whereby the government provides a safety net, not a market, is critical to strengthening U.S. competitiveness in world markets. In August 1985, the U.S. rice price was 105 percent higher than that of our competitors. Our wheat price was 30 percent higher. Cotton was higher by 19 percent, corn by 17 percent, and soybeans by 7 percent.

The Congress is determining what our legislated agricultural policy will be in the years ahead. We hope for the best.

As we in the United States work toward a long-term solution to make us again more competitive, a rise in protectionist sentiment here at home has forced us to begin an export enhancement program that we would not have freely chosen. We have made up to \$2 billion in surplus commodities available to expand U.S. agricultural exports in selected markets, particularly those characterized by unfair trading practices by other exporting countries. We hope the export enhancement program will encourage meaningful trade talks so that fair trade practices will be the rule and not the exception.

Conclusion

The phenomenon of the rapid growth of export markets in the 1970s created distortion in government policy and private investment. The correction we have witnessed in recent years was unavoidable because of these distortions. But U.S. exports can grow steadily, at a rea-

sonable rate, if we adopt sound farm programs and persevere in our ongoing efforts to negotiate fair **trading** rules among nations.

Global demand for food and fiber will continue to expand. The world's population is expected to grow at the rate of more than 80 million people per year. If comparative advantage is permitted to work, these people will be fed and clothed effectively and **U.S.** farmers that produce efficiently will benefit. On the other hand, if comparative advantage is not permitted to work, distortions in competition will remain a chronic problem and real peace and stability around the world will continue to elude us.