

Fiscal Year 2006 Budget Reconciliation Proposals: Impact on Southeastern Representative Peanut Farms

National Center for Peanut Competitiveness

Audrey Luke-Morgan

Allen McCorvey

Stanley Fletcher

Situation:

In an effort to help reduce the size of the federal budget deficit, proposals for the fiscal year 2006 budget considered various changes in government farm programs to reduce government outlays. The National Center for Peanut Competitiveness carried out a preliminary study to determine the impact of various potential changes in policy on the Southeastern representative peanut farms using Texas A&M Ag and Food Policy Center's (AFPC) FLIPSIM model.

Response:

Primary methodology used for this study was based on a selected paper prepared for presentation at the American Agricultural Economics Association Annual Meeting in Providence, Rhode Island, entitled "Impacts of Budget Reconciliation on US Crop Producers," by James W. Richardson, Joe L. Outlaw, Marc Raulston, and George M. Knappek, of the Agricultural and Food Policy Center at Texas A&M University.

Scenarios considered for the analysis included changes individually in target prices, payment fractions and loan rates to achieve a \$3 billion budgeted savings to the federal government over the years 2006-2010. The economic viability for each farm was considered for each of the scenarios considering the impact of the changes on the net cash farm income, ending cash reserves and the probability of declining real ending net worth.

A risk ranking procedure, stochastic efficiency with respect to function (SERF), was used to rank the scenarios based on the assumption that decision makers prefer more certainty equivalence of net income (CENI) to less at each risk aversion level.

Results:

A benchmark and three scenarios based on the reductions as forecasted at the \$3 billion level for budget reconciliation were considered. The benchmark considered economic viability based on the AFPC January 2005 baseline. It includes economic factors as projected by FAPRI/AFPC in January 2005 and policy as set forth in the FSRIA of 2002, assuming each farm utilizes either the spouse or three entity rule to maximize payment limits without limits on LDPs/MLGs. It also implements the removal of peanut storage and handling fees paid by CCC after the 2006 marketing year as set forth in FSRIA of 2002. This is considered the benchmark by which cuts in the other scenarios are compared and ranked.

The payment fraction scenario modifies the benchmark by implementing a reduction in the payment fraction from 85% to 80% of base for direct and counter-cyclical payments after 2005. The target price scenario modifies the benchmark by lowering the target price by 1.5% on program crops after 2005. The loan rate scenario modifies the benchmark with a 3.2% reduction

in loan rates on program crops after 2005. Again, all analysis reflects current policy as set forth in the FSRIA of 2002 assuming each farm utilizes either the spouse or three entity rule to maximize payment limits. Analysis also reflects, as established by the representative farm panels, that producers receive 100% of payments from base on the farmland both owned and rented.

For the benchmark and three scenarios considered, the overall financial viability of the 11 southeast peanut representative farms showed 2 good and at least 8 poor. For the benchmark and loan rate scenario, one farm was moderate. However, this farm was poor if the payment fraction scenario or target price scenario was considered.

The probability of negative ending cash reserves showed 3 farms with less than 25% and the remaining 8 farms with greater than 50% probability for the benchmark and loan rate scenario. For the payment fraction and target price scenarios, one farm shifted from less than 25% to the 26-50% range for negative ending cash reserves. The benchmark and all scenarios had two farms with less than 25% probability of decline in real net worth and nine farms with greater than 50% probability.

The SERF (Stochastic Efficiency with Respect to Function) procedure was used as a risk ranking procedure. The three scenarios were ranked considering the net cash farm income under each scenario for each farm based on the assumption that decision makers prefer more net cash farm income to less at each risk aversion level.

Given the assumptions considered in this analysis, nine of the farms indicated the preferred way to achieve budget savings given the options would be to lower loan rates. The remaining two farms indicated reduced payment fraction as the preferred option. The next preferred option would be a reduction in payment fraction (9 farms) with the other two farms ranking lowered target price as second. Lowering the target price was the least favorable option for nine of the farms and lowering the loan rate was the least favorable option for the other two. Again, these preferences were based on the impact on net cash farm income from the alternatives considered.

One key aspect to recall in this analysis is that the farm receives 100% of the payments associated with base on the farm. These results could change as producers have to renegotiate rental agreements with landlords if part, or all, of the payments associated with base are lost by the producer. Also, these results are based on the assumptions set forth in the AFPC January 2005 baseline which was current at the time of analysis.

Acknowledgement:

We wish to gratefully acknowledge the Georgia Peanut Commission for partial funding of the research effort.

[Return to GPC Research Reports on 2005 projects](#)