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Clunkers Theory Rooted in Depression Farm Policy: Caroline Baum

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Commentary by Caroline Baum

Aug. 31 (Bloomberg) -- All the talk about aggressive government intervention saving the U.S. economy from Depression 2.0 made me forget about the remnants of government intervention from Depression 1.0.

It all came rushing back when I read an **article** on how sour-cherry farmers in the U.S. were being told to dump 40 percent of their harvest to prevent prices from falling.

Unbelievable, right? In 2009 the U.S. has vestiges of 1930s farm policy, even though many New Deal initiatives -- destroying food crops when people were starving -- have been exposed as misguided and counterproductive.

People around the world are still starving -- your mother was right when she told you to eat your peas! -- yet farmers are destroying cherries when processors could be buying them on the cheap and canning them for food pantries, homeless shelters and aid to underdeveloped countries. How is this possible?

Policies to manage agricultural production or compensate farmers have been around since the 1850s, according to **Michael Dicks**, professor of agricultural economics at Oklahoma State University, in Stillwater, Oklahoma.

For our purposes, we can start with the Agricultural Adjustment Act (AAA) of 1933, which was designed to raise and stabilize farm prices during the Great Depression. The AAA imposed a tax on food processors and used the revenue to compensate farmers who reduced crop output in line with government specifications. (The act was declared unconstitutional and rewritten, with most of the policies intact.)

Creating Scarcity

With crops already planted for the following year, Secretary of Agriculture Henry Wallace came up with the bright idea of destroying food and livestock, including 10 million acres of cotton and 6 million pigs.

The U.S. no longer manages supply through what Jim Powell, author of "**FDR's Folly**," calls a "scheme of government- enforced scarcity." (If economics is about the allocation of scarce resources, what can you say about policies specifically designed to create scarcity?) Starting in the 1970s, **trade** liberalization opened export markets as an outlet for excess supply.

Today farm policy subsidizes production. The USDA provides direct payments to farmers, counter-cyclical payments (to offset low crop prices), subsidized loans, subsidized crop insurance, **export** subsidies and more.

This support persists even though 1.2 percent of the workforce was employed in agriculture in 2006 compared with 21.5 percent in 1930, according to the U.S. Department of Agriculture. As a share of output, farm production has fallen from 7.7 percent to less than 1.5 percent.

Fruit Loops

Some fruits and vegetables, including sour cherries, are subject to regional **marketing orders**, authorized under the -- what else? -- Agricultural Marketing Agreement Act of 1937. A committee of producers and handlers determining supply and demand for the industry instructed sour-cherry farmers to let 40 percent of the harvest rot.

If this sounds "like Stalin's collective farming, it is," says **Dan Griswold**, director of the Center for Trade Policy Studies at the libertarian Cato Institute in Washington.

What businessman would voluntarily destroy his output? Retailers hold going-out-of-business sales, accepting

whatever price consumers will pay for their merchandise.

Less may be more when it comes to design, but something is better than nothing when it comes to business.

No business dumps its inventory -- unless, of course, it gets taxpayer subsidies.

Supply Management

A policy of managing supply to guarantee a decent livelihood for farmers makes no economic sense. If the goal of society is to improve the standard of living and increase the wealth of the nation, destroying supply or paying for non- production isn't the solution. We obsess over the price of something when we should care about the quantity -- the physical supply -- of goods produced.

"Oversupply and declining demand are just screaming for a price decrease," Griswold says. "What better way to get us re- interested in cherry pie than a steep decline in prices."

At the right price, farmers might find all kinds of new uses for sour cherries, including tasty livestock feed.

What about the argument that farming is different, that farmers have to contend with uncertainty about supply (weather, crop diseases) in addition to uncertainty about demand?

That's why futures markets were created, so that farmers could lay off risk and protect themselves against a sudden collapse in prices. Without government support for sour-cherry farmers, they would ask **CME Group Inc**. to create a futures contract and turn to private insurers to manage their risk.

Freedom to Complain

The 1996 Freedom to Farm Act was an attempt to phase out price supports and give farmers more flexibility. The new freedoms quickly ran up against a collapse in global commodity prices. Farmers asked for relief, and Congress was quick to oblige.

Depression-era farm policy has spawned copy-cat programs. Seventy-five years after the U.S. government started paying farmers to destroy crops, it introduced "cash for clunkers." This "hugely successful" program paid consumers to turn in their gas-guzzlers for scrap and buy more fuel-efficient cars.

If the goal of a nation is to increase productivity, to produce more with less, dumping Chevys or cherries -- targeting "less" as an objective -- isn't the answer.

(**Caroline Baum**, author of "Just What I Said," is a Bloomberg News columnist. The opinions expressed are her own.)

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