



INCREASING PRODUCTION COSTS

Background

USDA forecasts that total farm production expenses rose to \$221 billion in 2005, up 5 percent from 2004 and 12.6 percent from 2001. Higher costs from purchased inputs such as fuel, fertilizers, and pesticides explain much of the rise in total farm production expenses. The input prices paid for fuel and fertilizer in 2005 spiked 61.5 percent and have tripled in 3 years. These increases are particularly significant to producers of program crops such as corn and wheat with relatively large energy usages.

Prices paid and received by farmers have generally outpaced general inflation measures in the U.S. economy since enactment of the 2002 farm bill. Annual indexes compiled by the National Agricultural Statistics Service (NASS) show that prices paid by farmers for all items rose 12.9 percent from 2002 to 2005. This was greater than the finished goods producer price index (PPI), which rose 12.1 percent over the same period.

The effect of price increases on profitability varies by enterprise. Productivity increases for some commodities may offset rises in production costs.

Prices Paid and Received by Farmers

Index	2002	2005	Index change
	Index value (1990-92 = 100)		Percent
Prices paid by farmers			
All farms ^{1/}	124	140	12.9
Supplies ^{2/}	132	146	10.6
Fertilizer ^{2/}	109	176	61.5
Farm machinery ^{2/}	149	172	15.4
Fuel ^{2/}	128	256	200.0
Crop farms ^{2/}	128	147	14.8
Livestock farms ^{2/}	122	140	14.8
Prices received by farmers			
All farms ^{1/}	98	116	18.4
Crop farms ^{2/}	101	101	0.0
Livestock farms ^{2/}	95	121	27.4

^{1/} Annual averages. ^{2/} 4th quarter averages.

Source: USDA NASS

General Opinions Expressed

- Many participants expressed concern over rising costs of fuel, fertilizer, and other energy-related inputs. They noted these cost increases were having a negative effect on farm profitability and on the competitiveness of U.S. producers in world markets.
- Some offered suggestions on how higher energy and energy-related input costs could be minimized through various incentives or programs (typically through the tax code) to increase renewable or alternative energy sources, achieve greater energy efficiency in production systems, or bolster domestically produced input use.
- Numerous participants expressed the concern that overall farm production costs were rising faster than the returns to farm production, making it difficult for existing farms to continue their operation.
- Some participants suggested that farm program price support levels and benefits should be adjusted to reflect increasing production costs; others suggested that farm programs should be aimed at reducing or controlling the costs of production.
- Some indicated that the cost of controlling invasive species was burdensome and that more assistance was needed to help mitigate these costs.
- Others noted that growing regulatory costs were making U.S. producers less competitive and that relief from these burdens or monetary compensation was needed.
- Higher input production costs, rising land and machinery costs, and greater regulatory costs were cited as deterring entry into farming.
- Participants pointed out that farm programs, such as the CRP and direct commodity payments, increase production costs through higher land rental or purchase prices.

Detailed Suggestions Expressed

- The U.S. fertilizer industry, which supplied 85 percent of domestic needs through the 1990s, now relies on imports for 45 percent of its supplies. The Department of Energy needs to use authority granted to it in the recently enacted energy bill to develop rules that provide incentives for construction of natural gasification facilities.
- Incentives need to be given to encourage companies to increase domestic production of fertilizer so that U.S. farmers are not forced to pay for the cost of shipping (from exporting countries).
- Given high costs of fuel and fertilizer, profit margins could be increased by a push on bio-products, including biodiesel.
- A fuel tax credit for commodity transportation to the market needs to be developed. The tax break on farm fuels should be extended to the trucks and vehicles used on the farm that go on our roadways.
- Increase the ability of farmers to compete by reducing energy needs and costs through energy efficiency programs and renewable energy systems.
- Look at ways to use solar energy to reduce costs for farmers.

- The new farm bill needs a component to alleviate the loss of profitability that is being caused by high fuel costs. The farm bill should provide a refund on a certain percentage of fuel cost or some type of a discount when fuel prices pass a certain level, which could be based on an inflation index based on global cost of petroleum and steel.
- Provide a (tax) credit to farmers because of high chemical costs.
- Crop prices should be increased as the price of oil increases.
- The cost of nitrogen has doubled each year for the past 2 years and the price of corn is the same as it was during World War II. Subsidies need to take into consideration inflation of production costs and living expenses.
- Establish milk prices such that they will cover the costs of production.
- Create a sliding-scale tax schedule where small and rural farmers pay no tax on income up to a certain threshold, such as \$100,000.
- To assure that farmers (and not landowners) receive the full benefit of commodity payments, direct payments should only be redeemable for agricultural inputs.
- To be competitive, a committee should be in place to monitor our input costs versus those in other countries.
- Establish price support levels that reflect the cost of production plus a fair profit to encourage farmers to stay in business.
- Enacting effective payment limits on commodity programs would hinder the ability of larger farms to drive up land rental and sales values and would hence lower production costs for beginning farmers.
- Increase the Federal share of the crop insurance premium to reduce costs.
- In Alabama, farmers have a growing problem with non-native invasive plants. The cost of spraying to keep these plants under control is nearly prohibitive. More dollars are needed for cost-share programs for invasive plant eradication.
- Provide subsidies to farmers who agree to cut back on fertilizer use. This will cut farmers' costs, improve water quality, and maintain farm income.
- Farm policy should only include regulations that are science-based, affordable, effective, and applicable.
- Review Government regulations and eliminate those that increase costs for farmers.
- The United States should have a committee that continuously monitors our costs versus those of other countries. Then farmers should be compensated accordingly.