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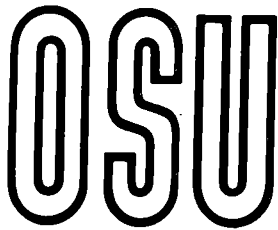

Current Report

Cooperative Extension Service • Division of Agriculture • Oklahoma State University

COTTON PROVISIONS OF THE FOOD SECURITY ACT OF 1985

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The Food Security Act of 1985, better known as the "Farm Bill", was signed into law December 23, 1985. The bill sets forth important new provisions for commodity programs. The purpose of this report is to discuss the cotton provisions and provide some general analysis. An accompanying Current Report #484 provides a budget worksheet to assist producers in the participation decision. Other forthcoming reports will detail other commodity provisions. County ASCS offices will also provide program assistance for sign-up, scheduled to begin March 3, 1986.

Discussion of Provisions

The target price for upland cotton is frozen at the 1985 rate of $.81 per pound in 1986. The Secretary may reduce the price 2-3% each year for 1987-1990. The loan rate will be at least $.55 per pound for 1986.

For 1987-1990, the loan rate will be the smaller of:

1. 85% of the average spot market price for the past five years (excluding the year with the highest average price and the year with the lowest average price);

2. 90% of the Northern European average cash market price for the 15-week period beginning July 1 of the current year.

The producer may take initial 10-month nonrecourse loans and upon his request have the loans extended for 8 months. Deficiency payments will be the lesser of the difference between target price and market price or target price and loan rate, with possible location differences as applicable.

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Special provisions are established in the event the prevailing world market price is below the loan level. The Secretary must select Plan A or Plan B:
-- Plan A - Producers may repay as little as 80% of the loan;
-- Plan B - Producers may repay loans at a level the lesser of the loan level or the prevailing world market price; for 1987-1990 crops, if the world price is less than 80% of the loan level, the Secretary may allow producers to repay loans at a level to minimize potential loan forfeitures, minimize the accumulation of federal cotton stocks and attendant storage costs, and allow competitive domestic and international marketing of U.S. cotton. Plan B has been selected for 1986.

If either plan fails to make cotton competitive in world markets and the world price remains below the loan repayment rate, the Secretary will issue negotiable marketing certificates through the CCC to first handlers of cotton to make cotton more competitive. Their value will be based on the difference between the existing loan repayment rate and the world price. The certificates may be transferrable.

In-kind deficiency payments are limited to 50% of the total payment. Increased payments that result from cuts below the formula loan rate are exempt from the payment limit of $50,000. Advanced deficiency payments must be available for 1986, with up to 50% in-kind, or cash.

An acreage reduction program (ARP) is at the option of the Secretary, but he must use a carryover target of 4 million bales. At state ASCS request, haying and grazing will be permitted on such acreage in 1986, and grazing for 1987-1990. Regardless of ARP, the Secretary may permit land diversion payments on a bid basis. Such reduced acreage may be devoted to the same conservation uses as permissable for wheat and feed grains.

If the monthly average spot market price exceeds 130% of the average price for the past 36 months, the President must establish a special limited global import quota for upland cotton, subject to conditions contained in the bill (mill consumption and prior quota use).

Table 1: Summary of Upland Cotton Provisions

	1986	1987	1988	1989	1990
Target Price ($/lb.)[1]	0.81	0.794	0.77	0.745	0.729
Loan Rate ($/lb.)	0.55[2]	(85% average spot or 90% N.Eur. price; 5% limit, .50 floor)			
Maximum ARP (%)	25	25	25	25	25

[1] Target price for 1987-1990 is estimated; Secretary has discretion to lower 2-3% annually.

[2] Estimate of national average loan rate.

The CCC must sell upland cotton for unrestricted use and export for the same price and that price must be at least 115% of the loan rate adjusted for marketing differentials. If, however, the Secretary permits repayments at levels below the loan rate, the price must be at least 115% of the average loan repayment rate.

Acreage base is determined by the average of planted and considered planted in the last 5 years (excluding zero plantings). Program yield for 1986-87 is the average 1981-85 program yield (excluding the year with the highest average yield and the year with the lowest average yield). The Secretary may phase in use of actual yields for 1988-1990. Cross compliance is at the discretion of the Secretary; he has indicated it is not required for 1986.

Additional upland cotton provisions include:

-- Signup will be held March 3 through April 11.
-- An advance deficiency payment of 7.8 cents per pound (30 percent of the projected total deficiency payment rate of 26 cents per pound) will be paid in cash during signup to producers who request an advance payment;
-- The loan rate cannot be announced until after the adjusted world price is determined and announced. It cannot, however, be less than 55 cents per pound for Strict Low Middling (SLM) 1-1/6 inch cotton at average U.S. location;
-- The loan repayment rate also cannot be determined and announced until the adjusted world price is determined and announced. However, if the adjusted world price is determined to be below the loan rate at the time of announcement of the loan rate, it is the intention of the USDA to implement Plan A under which the loan repayment rate cannot be less than 80 percent of the loan rate.

Additional information may be obtained from your county ASCS office.

Summary of Analysis

Analysis was conducted to compare three alternatives: 1) non-participation; 2) participation in the required ARP, 3) not harvesting 50% of the permitted acreage to cotton (see Table 2, 50/92 option). For the third option (50/92), it is assumed that 37.5% of each acre is devoted to cotton, 25% is devoted to ARP and 37.5% is devoted to a non-program crop. Production costs and returns are weighted to account for harvested, and non-harvested cost associated with the 50% participation option. The 50/92 plan assumes a non-program crop is grown on the 50% not harvested and 92% deficiency payment is received on all permitted acres. Then, costs and returns are calculated for each portion of one acre, as applicable.

The example shown assumes a 400# cotton yield for non-participation, 425# for participation in ARP and 450# for participation on 50/92. The assumption is that the land that is set aside or not harvested is marginal/less productive. This example has

an expected market price of $.45 per lb. for participation. This assumes the market price will be greater than the net loan price.

The individual choice of alternate use of land not planted to cotton in the 50/92 option is a significant decision and may have a major impact on results. In this example, mung beans are the alternative.

Table 2 results show that participation results in higher net returns per base acres ($49-$57 higher). While this example shows the 50/92 plan resulting in the most income, individual situations will vary. Again, Current Report #484 provides more details on a worksheet to determine participation.

Table 2: Expected Cotton Yield, Returns and Costs Per Base Acre[1]

	NON-PARTICIPATION	ARP	50/92
Yield (bushel)			
--Cotton	400	425	450
--Alternate crop[2]	-	-	-
Deficiency Payment (dollars)	-	78	72
Harvest Sales (dollars)			
--Cotton	180	143	76
--Alternate crop[2]	-	-	45
Total Income	180	221	193
COSTS:			
Harvested Acre			
--Cotton	150	113	56
--Alternate crop[2]	-	-	23
Non-harvested Acre (ARP)	-	5	5
Total Costs	150	118	84
Net Return	30	103	109

[1]Costs do not include a land charge or fixed costs.

[2]Depends on alternate crop; this example budgeted for mung beans.

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