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How Important Are Farm Payments to the Rural Economy?

Advocates of farm program payments frequently assert that support for the farm sector is necessary for the survival of rural communities. They might draw on several facts about Federal farm payments to back up their case. For example, most government payments to agriculture go to rural areas, and they have a positive effect on incomes. Government payments smooth fluctuations in farm income caused by swings in commodity prices, and they also inject cash into the rural economy, providing farm businesses and households with income to support other rural businesses.

During the 1990's, about 8 of every 10 dollars in Federal direct farm payments went to farms in nonmetropolitan (nonmetro) counties. (About three-fourths of the more than 3,000 U.S. counties qualify as nonmetro because they have no population center of 50,000 persons or more.) Of the $20.6 billion in Federal direct government payments to farms in 1999, an estimated $16.7 billion went to farms in nonmetro counties.

In 1999, a dramatic fall in crop prices plunged estimated nonmetro gross farm receipts down $17.8 billion from their 1997 level. Farm aid to nonmetro areas increased by an estimated $10.6 billion between 1997 and 1999, offsetting 60 percent of the decline in gross receipts. Without the increase in government payments, the impact of falling commodity prices on farm income in nonmetro areas would have been more severe.

Incomes of other rural businesses would have been affected as well. Purchases of farm inputs and equipment, as well as consumer spending by farm households, would have fallen without the cash-flow provided by government payments, dragging down sales of farm supply businesses, farm equipment dealers and manufacturers, retailers, and other rural businesses that depend on farm spending. Without government payments, some farms may have lacked sufficient cash to make mortgage and other loan payments to financial institutions.

Farm Share of Rural Economy Shrinks…

Farm payments have important impacts on farm income, planting decisions, and the allocation of resources to the farm sector, but they play a minor role in the economies of most rural communities. Over the seven decades since the first price support legislation was passed, most rural communities have reduced their reliance on agriculture as additional nonfarm jobs and businesses supplemented their economies.

While government payments have been important to farms and related rural businesses, the rural nonfarm economy has grown to such an extent that a strong downturn in the farm sector is barely noticeable in the statistics for the rural economy as a whole. What is more, other government programs have grown over the years so that today Federal income security payments and other types of programs play a much larger role in the rural economy than do farm program payments.

Today, net farm income amounts to only 2-3 percent of total nonmetro personal income. In most years of the 1990's, less than 1 percent of total nonmetro personal income came from government payments to nonmetro farmers.

Despite financial troubles in the farm sector during 1998 and 1999, total nonmetro personal income surged ahead by an estimated $103 billion between 1997 and 1999. Most rural communities would have grown strongly even without the cushion provided by increased government farm payments. Sectors that have little to do with agriculture, such as service industries and manufacturing, provided most of the growth in rural income. Some rural industries, notably food processors that buy agricultural commodities, likely benefited from the low commodity prices that buffeted the farm sector.

…But Farming Remains Important in Some Areas

Is this too broad-brush an approach? While most of rural America has experienced substantial nonfarm growth over the past few decades, some areas remain highly dependent on agriculture. However, only a fraction of government farm payments go to those areas where farming is a key source of income and

Nonmetro counties are those that have no population center of 50,000 persons or more. *Farm-dependent counties* are those that receive 20 percent or more of labor and proprietors' income from farming.

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How Government Farm Payments Affect the Local Economy

Farms and farm households affect local economies primarily through business and consumer spending. When farmers purchase seed, livestock, fertilizer, equipment, insurance, and fuel, and when they hire workers, make mortgage payments, spend their profits on household items, or pay local taxes, they inject money into the local economy, supporting local businesses and creating jobs. Government farm program payments may affect local economies indirectly by providing income to farmers that generates spending.

The effect on the rural economy depends on where money is spent. If a check from the government induces a farmer (or landlord) to increase spending locally, it will benefit the local economy. For example, a government farm payment used to purchase seed from a local farm supply store or to pay property taxes provides a boost to the rural economy. But if the payment is spent on a truck made in Detroit and purchased in Chicago, there will be little local impact.

The impact of farm program payments also depends on whether resources are fully employed in the local economy. If there is full employment locally, increased farm spending induced by government aid will simply bid workers and land away from other sectors, resulting in higher farm income at the expense of taxpayers, artificially inflated agricultural land prices, and a misallocation of resources. However, in a region with less than full employment and underemployed resources, agricultural program payments could strengthen the local economy.

Whether government payments induce farmers to increase spending depends on the type of program with which the payment is associated. Disaster payments to compensate for natural disasters or unusually low prices may prop up farmers' cash flow and encourage spending, protecting businesses that rely on farm spending from a disaster-induced slump.

However, payments that require farmers to idle land may have little net effect on the local economy. Farmers will still spend at least part of their government checks at their local grocery store or auto dealer, providing a boon to those businesses. But at the same time, they reduce their production expenditures on the idled land to comply with the program, hurting farm supply businesses. Also, some farm payments are in the form of loans that are paid back to the government. A loan has less local impact than a nonloan payment of equal amount.

jobs, and aggregate statistics may mask serious problems in isolated areas.

USDA's Economic Research Service (ERS) identified 556 nonmetro counties as "farm-dependent," with at least 20 percent of labor and proprietors' income derived from farming during 1987-89. These counties are concentrated primarily in the Great Plains from North Dakota to the Texas and Oklahoma Panhandles, in Iowa, and in parts of the Northwest, South, and Midwest. These are some of the least densely populated places in the U.S., where the dominance of farming often reflects the absence of other major industries. (Due to revisions in farm income accounting by the Bureau of Economic Analysis and the growth in nonfarm income, many of the 556 counties identified as farm-dependent would no longer be included in an updated list.)

Income growth in farm-dependent counties lagged behind that of other nonmetro counties during the 1990's. Inflation-adjusted total personal income in farm-dependent counties grew 13 percent between 1990 and 1998, compared with 21 percent growth in other nonmetro counties. This probably reflects farm-dependent counties' reliance on the relatively slow-growing farm sector.

Income growth also is more volatile from year to year in farming counties than in other nonmetro counties. For example, real total personal income in farm-dependent counties fell 0.6 percent between 1994 and 1995, then rose a dramatic 5.3 percent in 1996 before slowing to a modest 0.9 percent in 1997. In other nonmetro counties, growth was fairly steady at 2-3 percent annually during 1991-98.

Farm-dependent local economies are like an investment portfolio loaded up with shares of a single company whose earnings bounce around from year to year. Farming is one of the more unstable industries, subject to vagaries of weather, disease, and world markets. The experience of the 1990's indicates that volatility of farm income is reflected in variability in total income growth of farm-dependent counties. The 1994-95 decline in real personal income for the 556 farm-dependent counties coincided with a 22-percent fall in farm income. The 5.3-percent income rise during 1995-96 likely reflected a large increase in farm income during 1996, a year of high crop prices. The slowing of farm-dependent county personal income growth during 1996-97 to 0.9 percent corresponded with a 20-percent decline in farm income during that year.

Nonmetro Total Personal Income Grew from 1997 to 1999 Despite Decline in Farm Income

	1997	1999	Change
	$ billion		*Percent*
Gross farm receipts	135.1	121.2	-13.8
Plus Government payments	6.1	16.7	10.6
Plus Farm-related income	8.4	10.1	1.7
Minus Farm expenses	111.8	112.1	0.3
Equals Farm net cash income	37.7	35.9	-1.8
Total nonmetro personal income	1,053.90	1,157.10	9.8

Figures may not add to total due to rounding
Source: Estimates based on data from the U.S. Department of Commerce, Bureau of Economic Analysis.
Economic Research Service, USDA

This apparent link between farm income volatility and variability in total income growth suggests that cash-flow fluctuations for farmers can reverberate more strongly in those counties that rely on the farm sector and that offer fewer alternative income sources. In these local economies, government payments may play a more important role in smoothing out cyclical fluctuations.

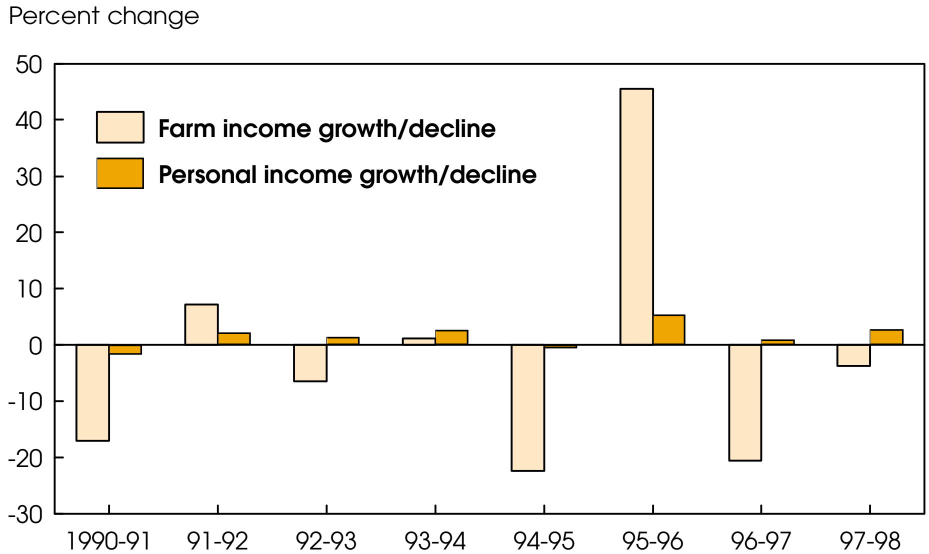
Government payments may also keep some farms in operation that would otherwise not be in business. In most areas where there are promising alternative uses for the land, labor, and capital, farm payments may encourage an inefficient allocation of resources. However, in a farming-dependent region where opportunities for alternative uses of these resources are lacking, a payment that keeps land, labor, and capital in farming may boost the local economy. Removal of farm program payments would lead to faster loss of population, decline in land values, and failure of local businesses that rely on farm spending.

It is very difficult to gauge the actual effect of farm payments on rural economies. However, simulations using economic models have predicted that removing farm payments would reduce output and employment in the rural economy while benefiting the urban areas of the U.S.

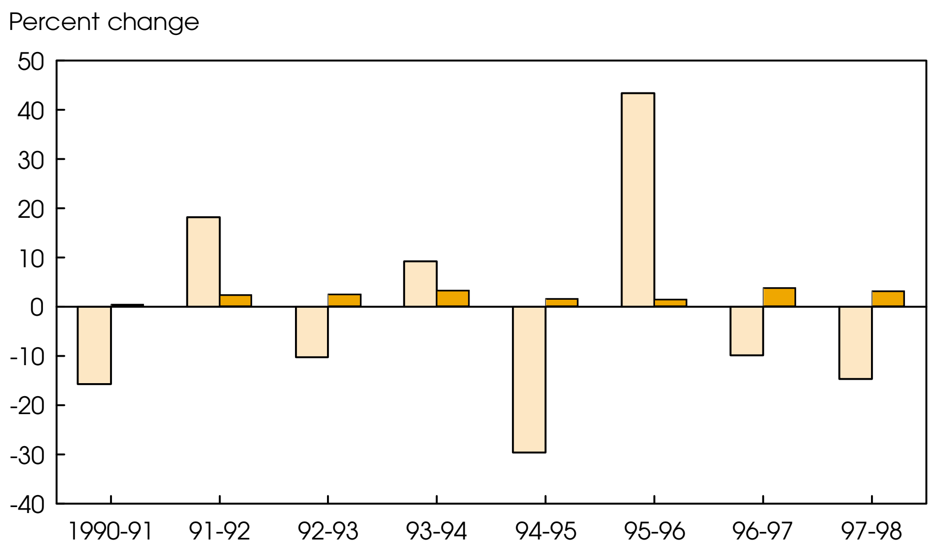
Government programs that provide payments to farmers can benefit some rural areas. But as economic development policy they perform poorly. A large part of government farm payments go to areas where they are barely a blip in the local economy. Farming-dependent counties—where government payments to farmers play a significant role in the local economy—received only 37 percent of farm program payments in 1998, while 19 percent went to metro counties and 44 percent went to non-farm-dependent nonmetro counties.

In metro and non-farm-dependent nonmetro counties, government payments to farms have no noticeable effect on the local economy because they account for such a small share of income. In communities with healthy growth prospects, government payments to farms may slow the growth of other economic sectors by driving up land prices and diverting capital away from other local businesses.

Personal Income Growth Rates in Farm-Dependent Counties Reflect Volatility of Farm Income. . .



. . .But Remain Fairly Steady in Other Nonmetro Counties Despite Swings in Farm Income



Nonmetro counties are those with no population center of 50,000 or more. Farm-dependent counties are those with at least 20 percent of labor and proprietors' income from farming in 1987-89.

Economic Research Service, USDA

Farm Payments a Small Part Of Federal Assistance in Rural Areas

Program payments to farmers are a small fraction of what the Federal government spends in rural areas today, as other Federal government programs that pro-

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Income Security Payments Account for Largest Share of Federal Funds Received by Rural Areas in 1998

	County type		
	Nonmetro		Metro
	All	Farm-dependent	
	$ per person		
All Federal funds, 1998	5,028	5,685	5,514
Direct payments to farms	182	937	11
Other agricultural and natural resources	87	339	14
Community resources[1]	407	484	634
Defense and space	305	142	728
Human resources[2]	117	123	100
National functions[3]	508	344	879
Income security[4]	3,422	3,315	3,147
	Million persons		
Estimated population, 1998	54.5	4.8	215.7

Figures may not add to total due to rounding.
1. Includes business assistance, community and regional development, environmental protection, housing, transportation. 2. Includes education, food and nutrition, health services, social services, employment.
3. Includes criminal justice, law enforcement, energy, higher education, research.
4. Includes medical benefits, public assistance, unemployment compensation, Social Security.
Source: Calculated by ERS using Bureau of the Census Federal funds data.
Economic Research Service, USDA

vide assistance to individuals, businesses, and state and local governments have grown over the years. In 1998, per capita Federal spending in nonmetro counties totaled $4,725, including only $182 for farm payments. In farm-dependent counties, farm payments were much higher—$937 per capita—but still less than one-fifth of $5,369 in per capita Federal spending. Higher levels of government payments in 1999 brought per capita farm payments to an estimated $300 in nonmetro counties and $1,575 in farm-dependent nonmetro counties, still a small share of all Federal spending in those counties.

Most Federal funds received by nonmetro counties are for income security, including Social Security, disability payments, other retirement benefits, medical and hospital benefits, public assistance, and unemployment compensation. Income security payments have a large impact on the rural economy. In 1998, nonmetro income security payments averaged $3,143 per capita—two-thirds of total per capita Federal funds received—and accounted over 12 percent of nonmetro total personal income.

Income security payments support spending by the large share of rural residents that are retired, including the substantial proportion of farmers who receive Social Security and other Federal retirement income. The payments also provide disposable income to disabled and unemployed persons, as well as funds for maintenance of rural medical services.

In nonmetro counties as a group, the 1998 per capita direct payments to farmers ($182) were outweighed by 1) per capita community resource funding ($406 per person), which includes business assistance, community facilities, regional development, environmental protection, housing, Native American programs, and transportation; 2) defense and space programs ($305 per person); and 3) national functions ($508 per person), which include law enforcement, energy, higher education, and research and other programs. The average $1,219 per capita disbursed under these programs affects rural economies by providing infrastructure, stimulating construction projects, and providing salaries for Federal government employees.

In nonmetro counties, per capita funding for farm programs in 1998 exceeded per capita Federal funding for other agricultural and natural resource programs—agricultural research and services, forest and land management, water and recreation services—and for human resources programs—elementary and secondary education, food and nutrition, health services, social services, training and employment. Federal grants also support many of the larger human resources programs, but local area funding amounts are not known because the funds are distributed by state governments.

In 1998, total per capita Federal funding for metro counties ($5,212) outpaced nonmetro counties ($4,725), but funding was higher for farm-dependent counties ($5,369), because of their relatively high per capita agricultural payments. Nonmetro counties received more funding per capita for income security programs—$3,143 versus $2,864 per capita for metro counties—due mainly to retirement benefits received by the somewhat older population in rural areas. Higher per capita agricultural and income security funding in nonmetro counties partly makes up for the smaller nonmetro share of funding for community resource, defense and space programs, and national functions in rural areas.

Changes in farm programs, or even a discontinuation of commodity programs, would not have major impacts on most rural communities. Only a minority of rural counties appear vulnerable to the loss of farm payments, and the number appears to be shrinking; a recent study of data from the mid-1990's indicates that many fewer counties meet the farm-dependent criterion than a decade ago. In most rural communities, farm payments will continue to play a minor role in the economic landscape, a role that is overshadowed by the impact of Federal retirement payments, medical payments, and other nonfarm programs.

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For more information on Federal funds data, see S.D. Calhoun, R.J. Reeder, and F.S. Bagi, "Federal Funds in the Black Belt," *Rural America* Vol. 15, No.1 (January 2000): pp. 20-27; <http://www.ers.usda.gov/epubs/pdf/ruralamerica/ra151/contents.htm>.