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Mexico’s New Agricultural Policy Is Mexico’s Old Agricultural Policy (Part II)

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This is the second of three posts where I comment on Mexico’s “new” agricultural policy. For Part I click here.

In the first post I have presented evidence that, in constant prices, the 2019 budget allocations to the “mainline” subsidy programs in agriculture are at historically low levels. [1] In particular, acreage-based payments (irrespective of production levels) are at an all-time low (915 million in 1991 pesos) whereas funding for marketing support is the second lowest in history (682 million in 1991 pesos).

The reason for this is that the AMLO administration has reallocated spending on agricultural subsidies from the “mainline” programs towards three new programs, although not all three of them are actually new: guaranteed prices, “crédito ganadero a la palabra”, and fertilizer subsidies. The guaranteed prices program will cover five products: corn, beans, wheat, rice and fluid milk.

As explained in the first post, the guaranteed prices scheme is not a new program – it was in operation from 1965 through 1998. In its earlier incarnation, it ensured that all domestic production was bought at a government-set price, and whatever demand there was leftover in excess of local production at the government-set price was filled-in by imports subject to import quotas.

That said, the guaranteed prices scheme that has risen from the dead in the AMLO administration is a different animal from the original version, although this is more by accident than by design.

First, because Mexico’s commitments under the WTO would prevent the imposition of import quotas or licenses on products subject to guaranteed prices, the Mexican Government now lacks the ability, under both Mexican and international law,[2] to require private purchasers to buy local production at the guaranteed price as a condition for receiving an import permit. Therefore, the reborn guaranteed price scheme boils down in effect to a program of government purchases (of local production at guaranteed prices) with SEGALMEX playing the role of purchasing agent.

Second, because SEGALMEX lacks downstream processing plants (unlike CONASUPO, its predecessor), it will end up reselling all of what it purchases at guaranteed prices. This role as intermediary will generate freight costs, storage costs and opportunity costs (for holding inventory), not to mention the transaction cost involved in identifying and reaching out to prospective buyers. Importantly, when reselling SEGALMEX will be able to recover less than what it paid to growers since, absent import restrictions, those buying from SEGALMEX will not be willing to pay prices higher than world prices.[3]

SEGALMEX might soon come to the realization that its statutory objective of supporting domestic prices can be achieved more efficiently if it desists from acting as a purchasing agency and switches to providing a direct cash transfer to the local producers of the targeted crops, equivalent to the difference between the guaranteed price and the market price, Unsurprisingly, according to the recently-published *Operating Guidelines for The Guaranteed Prices Program*, in the case of rice and wheat, private buyers will purchase the local crop at market prices, and SEGALMEX will then pay to growers the differential with respect to the guaranteed price. [4] This approach had already been outlined by the head of SEGALMEX in respect of wheat.[5] Interestingly, if this is the form that the reborn guaranteed prices program ultimately takes on, this program will be, in substance, indistinguishable from the marketing support for growers,[6] one of the two "mainline" subsidy programs starved of funds by the AMLO administration.

The specifics of the "crédito ganadero a la palabra" program have not been disclosed yet. If the literal meaning of its name turns out to correspond to its actual operation, the "crédito ganadero a la palabra" program would consist of concessional loans to livestock producers granted without a prior credit check. According to the *Operating Guidelines for Fertilizer Subsidies*, through this program fertilizers (presumably only of Mexican-origin) will be provided free-of-charge to low-income producers of corn, beans and rice, preferably located in the South and South-East of Mexico. [7] Although this program can be expected to be heavily oversubscribed for obvious reasons, the *Guidelines* do not spell out any criteria for objectively selecting the beneficiaries of this program out of the pool of producers that is being targeted.

The 2019 federal budget includes allocations to finance these three programs. In particular, 7.8 billion Mexican pesos (approx. US$ 402 million) have been made available to pay for price support via government purchases or direct cash transfers. Out of this amount, 6 billion Mexican pesos (approx. US$ 310 million) have been earmarked for funding SEGALMEX' price support for corn, beans, wheat and rice whereas 1.8 billion Mexican pesos (approx. US$ 92 million) have been earmarked for funding government purchases of fluid milk. In turn, the amount budgeted for the "crédito ganadero a la palabra" program is 4 billion Mexican pesos (approx. US$ 207 million) whereas the sum set aside for free deliveries of fertilizers is 1 billion Mexican pesos (approx. US$ 52 million). [8]

In 1991 pesos (the unit in which Mexico bound at the WTO its agricultural subsidies that are not output-neutral), the funding for SEGALMEX, government purchases of fluid milk, the "crédito ganadero a la palabra" program, and free deliveries of fertilizers amounts to 610 million, 180 million, 406 million and 102 million, respectively. The four programs add up to 1.3 billion in 1991 pesos. Since Mexico's AMS binding is 25.1 billion in 1991 pesos,[9] the funding for the four programs, combined with the 2019 funding for marketing support (682 million in 1991 pesos),[10] is well below this ceiling.

To understand the potential market effects of government purchases and direct cash transfers, one needs to delve into the details involved.

For starters, all of the announced guaranteed prices are significantly higher than current world prices. Table I compares the guaranteed prices announced on March 1, 2019 for each of the targeted crops against the corresponding world prices in February/March 2019.

Table I: Guaranteed Prices Announced for 2019 vs World Prices

		Panel A		
	GP Pesos/MT	GP US$/MT	WP US$/MT	Difference
White Corn	5,610	290	154	89%
Beans	14,500	750	611	23%
Wheat	5,790	300	218	37%
Rice	6,120	317	187	69%
		Panel B		
	GP Pesos/Liter	GP US$/Liter	+WP US$/Liter	Difference
Fluid Milk	8.2	0.42	0.31	35%

Notes:

GP stands for guaranteed price and WP for world price.

Sources:

Guaranteed prices for 2019: Operating Guidelines for The Guaranteed Prices Program, Official Gazette, March 1, 2019, at para. 2.4. World price for white corn: U.S. price for white corn no. 2 (Kansas City), February 2019, Feed Grains Database, Economic Research Service, USDA. World price for beans: U.S. price for black beans no. 1 (average of North Dakota/Minnesota and Michigan), March 6-12, 2019, Weekly Dry Bean, Pea and Lentil Market News, USDA. World price for wheat: Average of U.S. prices for hard red winter no. 1 and soft red winter no. 2, February 2019, as reported in the World Bank Commodities Price Data. World price for rice: Long-grain, rough basis, February 2019, as reported in the Rice Outlook for February 12, 2019, ERS, USDA. World price for milk: Whole milk powder, March 5, 2019, Global Dairy Trade, converted to a fluid basis.

Thus, the announced guaranteed prices exceed world prices in proportions ranging from almost 25% to nearly 90%. In particular, the announced guaranteed price is 23% higher than the corresponding world price in the case of beans, 35% in the case of fluid milk, 37% in the case of wheat, 69% in the case of rice, and 89% in the case of white corn.

In the next post, I discuss further what might be the market effects of government purchases and direct cash transfers.

[1] As compared with the average annual subsidies in each of the preceding four administrations.

[2] International trade treaties are self-executing under Mexican law. The head of SEGALMEX (the agency in charge of running the guaranteed prices program) has been quoted in the press as saying that private purchasers will not be required to buy local production at guaranteed prices. See, "ANTAD descarta impacto por precios de garantía", *El Economista*, January 27, 2019.

[3] All of the announced guaranteed prices are significantly higher than the corresponding world prices. See below.

[4] *Operating Guidelines for The Guaranteed Prices Program*, Official Gazette, March 1, 2019, at para. 2.6, subparagraph c).

[5] "SEGALMEX, por tiros exactos en precios de garantía", *El Economista*, February 21, 2019.

[6] As noted in the first post, the marketing support program involves payments, per marketed ton, equivalent to the difference between a target price and the market price.

[7] *Operating Guidelines for Fertilizer Subsidies*, Official Gazette, March 1, 2019, at articles 2.I, 7, 8, 12.III, and 15. IX.

[8] Análisis Funcional Programático Económico, Proyecto de Presupuesto de Egresos de la Federación 2019 (available at Hacienda's website), at pages 3,6 and 7. The exchange rate for March 12, 2019 was used for making the relevant currency conversions.

[9] See, *Notification by Mexico*, Committee on Agriculture, WTO document G/AG/N/MEX/41 (September 14, 2018), at page 2.

[10] See Table II in first post.

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