Testimony of Tom Lahey

Vice President, Kansas Cotton Association

before the

Committee on Agriculture, Nutrition, and Forestry

U.S. Senate

Manhattan, Kansas

February 23, 2017

Introduction

Chairman Roberts, Ranking Member Stabenow, and Members of the Committee, thank you for the opportunity to provide this testimony regarding the current farm bill and the policy needs of the U.S. cotton industry in the next farm bill.

My name is Tom Lahey, a fourth generation farmer and rancher from Moscow, Kansas. I raise cotton, wheat, corn, and grain sorghum, the majority under pivot irrigation, and have a cow-calf operation. Nearly 20 years ago, I was one of the first two farmers to grow cotton in southwest Kansas. In 2002, we built the first cotton gin in Kansas, Northwest Cotton Growers Inc. (NWCG), in the western part of the state.

I serve as vice president of the Kansas Cotton Association, and I am a producer delegate to the National Cotton Council (NCC). NCC is the central organization of the United States cotton industry. Its members include producers, ginners, merchants, cooperatives, warehouses, textile manufacturers and cottonseed processors and merchandisers.

Current Industry Conditions

As you know, the current economic situation for much of production agriculture is bleak, including for U.S. cotton farmers. The passage of the 2014 Farm Bill coincided with significant changes in the global cotton market. Shortly after the bill was approved, cotton prices began a significant decline, the result of a build-up of global cotton stocks, especially in China, decreased demand, and reduced exports. This led to the lowest U.S. cotton acreage for 2015 in over 30 years. While cotton prices and acreage have increased from the lows experienced in 2015, producers are still struggling with prices at levels not adequate to cover all production costs.

To understand the challenges facing cotton farmers, it is important to review the dynamics at work in global cotton demand. USDA estimates world mill use at 112 million bales for the current 2016 marketing year. However, even with very modest growth, world cotton demand remains almost 13 million bales below the peak demand observed in 2006. Slumping demand is largely the result of the tremendous increase in polyester use. During the 2006-2015 period when cotton mill use fell by 13 million bales, polyester's production capacity, primarily located in China, increased by 145 million bales. Excess production capacity, in many cases fueled by government support, is contributing to polyester prices in Asian markets of approximately 55 cents per pound. While consumers continue to express their preference for cotton products, the tremendous increase in low-priced polyester production has created extraordinary hurdles for increasing cotton demand.

I highlight these issues because of the critical influence of international markets in the financial conditions of U.S. cotton farmers. In recent years, approximately 75% of U.S. cotton production enters export channels. Policies that directly affect international production, consumption and trade have a direct bearing on U.S. market prices.

For 2017, NCC is estimating 11 million acres of cotton plantings, with 45,000 acres in Kansas, a 42% increase from 2016. This increase in Kansas is reflective of several factors, including the availability of seeds with a trait that provides tolerance to 2,4-D herbicide, the yield potential of cotton coupled with minimal water use requirements, and the relative returns compared to other crops.

Cotton Policy and the Farm Bill

While cotton acres across the U.S. are expected to recover, a major concern still exists since cotton is not eligible for the same price and revenue policies as other crops. As you know, these Title I policies in the farm bill are designed to help producers withstand periods of price declines and depressed market conditions. While the ARC/PLC policies have generally performed well for me and other producers in responding to the market downturn we are experiencing in crops like wheat, corn, grain sorghum, and soybeans, I continue to be largely exposed on cotton since it was excluded from these types of programs. Under the current farm bill, cotton has access to the Stacked Income Protection Plan (STAX) crop insurance policy and the marketing loan program with an adjustable loan rate based on prior year market prices. Cotton is the only traditional 'program' crop that does not have any long-term price or revenue protection policy in the 2014 Farm Bill.

Cotton policy in the 2014 Farm Bill was largely dictated by a World Trade Organization (WTO) trade challenge brought by Brazil against components of U.S. farm policy and some cotton policy specifically. This resulted in cotton having to rely largely on STAX as the core safety net for cotton. But just like any revenue based crop insurance policy, STAX is not equipped to address periods of extended low prices, which is exactly what cotton producers experienced beginning the year the farm bill was approved.

For more than a year, the NCC has been working with Congress and the previous Administration to try to get cottonseed designated as a covered commodity and be eligible for the ARC and PLC programs in the farm bill. Cottonseed remains an important co-product of cotton production, along with the cotton fiber. Our industry believes support can be provided for cottonseed without running afoul of the agreement with Brazil that settled the WTO case. We strongly believe we need to get a cottonseed policy in place to help provide support to our producers as a bridge until the new farm bill is enacted, which will hopefully be by the 2019 crop.

NCC is beginning internal discussions on cotton's policy objectives for the new farm bill. We know that a meaningful safety net for cotton must be included in Title I of the farm bill. Better protection in times of depressed markets can take on several forms, and our industry will continue to pursue the best avenue to provide growers adequate protection for the revenue generated by both cotton fiber and cottonseed.

In order for Congress to be able to address the current shortcomings in U.S. cotton policy and to shore up other areas of need in farm policy, we strongly oppose any attempts to reduce the budget for the next farm bill. Further, we urge the Committee to seek any opportunities to increase the Federal investment in farm policies that ensures the U.S. consumer continues to have the safest, most affordable and secure supply of food and fiber in the world. In the January 2017 Congressional Budget Office baseline projection, the cost of the current farm bill is expected to be more than $100 billion less than estimated when the bill was enacted in 2014. Given this significant decline in farm bill spending, coupled with the significant downturn in farm income and generally weak commodity prices, a greater investment in these critical policies for all of rural America should be in order.

In addition to a meaningful safety net, our industry relies heavily on a properly functioning marketing loan program, so maintaining that policy, with minor adjustments, is also a priority.

Maintaining a strong crop insurance program is also critical since in agriculture, one thing is for certain, crop losses will occur in some part of the U.S. each year. Annual losses incurred by farmers clearly demonstrate the need for crop insurance protection and the public-private partnership of program delivery. Farmers, ranchers, their lenders, input suppliers and other stakeholders agree that crop insurance protection should remain a viable, affordable tool for managing risk.

In 2016, 96% of cotton acres were covered by either multi-peril "buy-up" insurance or catastrophic coverage. 88% of these acres were covered by multi-peril insurance. The STAX policy was purchased on over 2.5 million acres covering 26% of total insured acres.

In 2016, crop insurance was purchased on 84% of cotton acres in Kansas and 79% of those acres are covered with multi-peril insurance. Unfortunately, STAX coverage has been used in very limited amounts on Kansas cotton acres. While there are likely several reasons for this low level of participation, it is imperative that cotton producers have access to the same complement of risk management policies and tools as other producers, including commodity policies in Title I, along with crop insurance.

Federal crop insurance provides an effective risk management tool to farmers and ranchers of all sizes when they are facing losses beyond their control, reduces taxpayer risk exposure, makes hedging possible to help mitigate market volatility, and provides lenders with greater certainty that loans made to producers will be repaid. The public-private partnership of program delivery works very well, allowing for timely and outstanding service to producers when they need it the most and providing much-needed jobs across rural America.

While the insurance program is working well and should be defended, there are a few areas that can be improved. NCC is currently working with the Risk Management Agency (RMA) to improve quality loss provisions that have proved inadequate for many producers in the Southeast region who suffered through extensive rains during the 2015 and 2016 harvest seasons. RMA has been a good partner in identifying and pursuing improvements to this feature of the product. Another area that is particularly important here in the Southwest region that was allowed in the 2014 Farm Bill is the ability to insure Enterprise Units by practice. In our view, the RMA has not implemented this provision in the way intended by Congress and should be reconsidered by USDA, and if necessary, further clarified in the next farm bill.

Our industry will work to prevent any further tightening of payment limits and eligibility requirements, as we believe these policies are already too burdensome and restrictive in light of the size and scale of production agriculture necessary to be competitive and viable in a today's global market.

In addition to the above policies discussed for upland cotton, there are important policy considerations for Extra Long Staple (ELS) or Pima cotton as well. The industry is evaluating the potential for an increase in the loan rate for the ELS loan program to better reflect the relative market value of Pima cotton. Since this is a non-recourse loan without marketing loan provisions, there should be little, if any, additional government cost or exposure. Also, the ELS Cotton Competitiveness Program is not currently functioning as intended given the recent shift in the countries that are major producers, importers and exporters of ELS cotton. For the intended objectives of this program to be met, USDA needs to take steps to update the key price data being used.

Conservation programs continue to be extremely popular across the Cotton Belt. Specifically, the Environmental Quality Incentives Program and the Conservation Stewardship Program are both heavily accessed. I commend the Committee for streamlining conservation programs in the 2014 Farm Bill. I believe this will make them easier for NRCS to administer, but more importantly easier for producers like myself to utilize. These programs have become integral parts of many producer's operations and achieve the goal of improving and protecting the environment while also improving our farming operations.

Between 1997 and 2008, the amount of cotton used by U.S. textile mills experienced a precipitous decline, falling from 11.3 million bales down to 3.5 million bales. Since 2008, the U.S. textile industry has stabilized, however there has been a slight decrease in domestic mill use for the current marketing year at 3.3 million bales.

The recent years of stability and expected future growth can be attributed to the continued benefits of the Economic Adjustment Assistance Program (EAAP), first authorized in the 2008 Farm Bill. Recipients must agree to invest the proceeds in equipment and manufacturing plants, including construction of new facilities as well as modernization and expansion of existing facilities. EAAP funds have allowed investments in new equipment and new technology, thus allowing companies to reduce costs, increase efficiency and become more competitive against imported textile products. By allowing U.S. textile mills to make the new investments necessary to remain competitive, the program supports a manufacturing base that is keeping jobs in the United States.

Given the tremendous reliance by our industry on exports of raw cotton fiber and yarn, it is essential that the U.S. agriculture industry have a strong, well-funded public-private partnership to help leverage private resources to expand export markets and grow demand for U.S. agriculture products. A central part of this effort is USDA's Market Access Program (MAP) and Foreign Market Development (FMD) program. Even though the U.S. continues to be heavily outspent by other major agricultural producing and exporting countries, MAP and FMD investments have not increased in more than a decade. For this reason, we believe it is justified for the new farm bill to invest additional funds in these programs.

Conclusion

In closing, for the past three years, U.S. cotton producers have struggled with low cotton prices, high production costs and the resulting financial hardships. While current cotton futures markets have increased from year-ago levels, many producers continue to face economic challenges. The projected increase in cotton acreage is largely the result of weaker prices of competing crops and improved expectations for water in some regions that were experiencing severe drought conditions. As such, it is imperative that the next farm bill bring cotton back into the Title I commodity policy so that cotton is able to access the full complement of risk management tools as other crops.

NCC looks forward to working with the Committee, the other groups and commodities represented here today, and all commodity and farm organizations to develop and pass a new farm bill that effectively addresses the needs of all commodities and producers in all regions of the country.

Thank you for this opportunity to present testimony, and I would be pleased to respond to any questions.