1-1-2007

Book Review: *The Nature of the Farm—Contracts, Risk, and Organization in Agriculture* by Allen, Douglas W. and Dean Lueck

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Published in *Agribusiness* 23:2 (2007), pp. 293–294; DOI: 10.1002/agr.20124.

Published online in Wiley InterScience: http://www.interscience.wiley.com

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Allen, Douglas W. and Dean Lueck. (2004). *The Nature of the Farm—Contracts, Risk, and Organization in Agriculture.* Cambridge, MA: The MIT Press, 266 pp., $22.00. ISBN 0262511851.

The conventional wisdom about the future of family farming in North America is that it is a bleak one. Like any other family firms, family farms are not immune to industrialization and eventually all stages of food production will be in the hands of large corporations. The poultry industry has become the poster-industry for the corporate take-over of food production and *the* guide to what is in store for the rest of agriculture. That, among other theories about organizational features of North American agriculture, is closely examined by Allen and Lueck's *Nature of the Farm – Contracts, Risk, and Organization in Agriculture.* As the reader can guess, the leading title of the book is a take on Ronald Coase's classical article, *The Nature of the Firm,* obviating the book's use of the transaction cost approach to explain contracts, risk, and organization in agriculture.

In contrast to the "principal-agent" approach, where risk sharing between risk-averse contracting parties is the motive for contracts, the transaction cost approach Allen and Lueck use bypasses risk preferences by justifiably assuming risk neutrality and focuses instead on the tradeoff between incentives offered by contracts. In doing so, the authors develop models that are more consistent with actual farming practices in North America and with the data than risk-sharing models. Chapter 2 provides a thorough discussion of those farming practices. Chapters 6 and 7 in part II of the book provide the empirical evidence against the risk-sharing explanation of contracts using data on individual contracts.

Less obvious from the title, however, is that the "Nature" Allen and Lueck have in mind is Mother Nature. Through its unpredictable and predictable roles in farm production, Mother Nature "is the fundamental force that shapes the incentives and transaction costs that, in turn, ultimately shape agricultural organization" (p. viii). The unpredictable role provides the uncertainty that allows contracting parties to exploit one another and literally blame it on the weather. For example, farm tenants can exploit landowners by underreporting output, undersupplying effort, and mismanaging the soil. Engaging in and preventing such hidden actions give rise to transaction costs. To mitigate those costs, contracting parties chose from a menu of contracts. In part I of the book, chapter 3 examines various forms of those contracts. Chapters 4 and 5 use a transaction model to empirically examine the determinants of choice between crop share and cash rent contracts, and the determinants of the respective shares of landowners and farmers in the costs of inputs in a crop share contract. What we learn is that a major reason for the simplicity of agricultural contracts is low-cost enforcement because of "the character of the farming economy." In addition, consistent with the transactions costs model, the choice between crop

share and cash contracts and the division of outputs and inputs depend on how close a contract brings the contracting parties to a relationship that mimics vertical integration.

The predictable or systematic role of Mother Nature restricts farm production processes. The biological clocks of crops are preset so there are only so many cycles of crop production, so many stages and tasks between the seed and final output. In such a setting, gains from task specialization are limited because tasks are not as repetitive as they are in factory-style production, timeliness of tasks is critical, and performing those tasks through contracts increases moral hazard costs. Chapters 8 and 9 in part III of the book, respectively, examine how Mother Nature affects farmers' decision to own or contract over the control of assets, and how it shapes the type of agricultural organization.

With respect to asset ownership versus contracting, the analysis makes it clear why, for example, farmers own rather rent expensive combines, which are used only a few weeks a year. With respect to type of organization, the analysis also makes clear why seasonality results in agricultural organization as simple as a family farm or as complex as a factory-style corporate farm. The lower the number of crop cycles, the shorter and less frequent the production stages are, the less tasks are within the stages, and the more critical is the timing between stages, the more prone is the farmer to moral hazard and agricultural production will be in the hands of a family farm. Production of annual grain crops is one example. Therefore, it should be no surprise that 80% of wheat farms are family farms. Wheat production is also less likely to go the route of feedlot cattle, hogs, and poultry factory-style production unless a technology comes along that eliminates seasonal forces in wheat as it did in livestock and allows growing wheat indoors.

Agricultural economists interested in contracts and organization in farming in general, and transactions costs economics, in particular, will find this book a valuable text in their classes and a valuable reference for their research. What is remarkable about the book is that it combines rigor with relevance and confronts theory with data. That is what agricultural economics research is meant to be.

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