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Remarks by

Paul A. Volcker

Chairman, Board of Governors of the Federal Reserve System

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Let me say at the outset that I have been following the comments of American Farm Bureau officials on economic policy with special interest over the past year. I regretted missing the Convention in Phoenix a year ago. But I concluded afterwards that I could have done no better than read to you from your own economic policy statement at the time:

"Inflation is our number one economic problem. Inflation is a result of long-term monetary problems related to . . . the nation's supply of money and credit to finance federal deficits.

"Inflation adversely affects agricultural producers in many ways .

"To control inflation will require a sustained long-term monetary policy approach . . . . We support the recent independent policy decisions by the . . Fed to focus its efforts to control inflation on the supply of money and credit. The Fed must adhere to this policy consistently for years to come.

"Congress and the Executive Branch must accept major responsibility with a commitment to fiscal restraint and an end to year-after-year federal deficits."

Well, here we are in New Orleans a year later. Those words still seem to me appropriate. Nevertheless, I suspect not a few of you, looking back at 1980 and ahead to 1981 wonder what, in fact, the Federal Reserve has wrought.

Farmers through the centuries have lived with uncertainty and the unexpected, imposed by natural forces, the market, or governments. The past year was no exception. But on top of all that, you have had to cope with unyielding inflation and recurrent bouts of extraordinarily high interest rates as we have moved to deal with that inflation.

I wish I could offer you assurance that that is all behind us. But you and I are realists. We know that problems that have been years in the making will not disappear easily. We know, or should know, that restraint on money and credit -- while a necessary part of any program to restore price stability -- is not a painless process. We have to anticipate that inflationary practices and attitudes that have become second nature to all of us will not change without painful adjustments in public policies and private behavior. But for all of that, my message is basically a hopeful one -- hopeful because I do believe our nation does have a rare opportunity now to move ahead on several fronts to turn back the inflationary tide. And, as we do so, those needing to borrow in the credit markets will be among the greatest beneficiaries.

Certainly 1980 was even more turbulent for agriculture than most other sectors. Putting aside such "incidentals" as drought and embargos -- matters far removed from the Federal Reserve or economic policy generally -- the price and potential availability of money was perhaps of greater concern to farmers in the early spring planting season than at any time in memory. More recent developments have no doubt raised the spector in your minds again. In between, interest rates did drop sharply, easing the pressures on you, particularly as agricultural prices rose significantly as credit market conditions eased. But through it all, prices of land, equipment, and other inputs have continued to rise about as fast as before, directly reflecting the fact that we have not yet turned the corner on inflation.

Looking at the economy as a whole, business activity turned down sharply, and then snapped back quickly. We talked about balancing the budget last spring -- but now we face a deficit in the $50 to $60 billion area. Spending continues to rise faster than the GNP, and tax rates are effectively rising. Inflationary expectations, as well as inflation itself, remains high. That is not an environment in which stability in financial markets can reasonably be expected, and understandably there was a sense of frustration about our economic course.

The legacy of 1980 will not be quickly forgotten. Nor should it be. Last year's difficulties, in exposing so clearly the deep-seated economic problems that have been building over a long period of time, have served to focus the nation's attention, as perhaps never before, on the need to come to grips in a decisive way with the inflation problem that lies at the heart of so much of our economic malaise. It is the instability and distortions growing out of inflation that undercuts many of our efforts to deal effectively with such problems as declining productivity, energy, low investment and the weakened competitiveness of some industrial sectors.

For a long time, it was fashionable to think we could live with a little inflation -- that it actually added to a sense of well being. Many, including farmers, seemed to have a favorable experience. Inflation was more fun when there were fixed rate mortgage loans at interest rates that did not keep pace with rising land or other prices -- a period, I understand, that agriculturists often refer to as the "golden sixties." During the farm price explosion of 1972-1974 many may have found inflation downright exhilarating. But after OPEC appeared on the scene, and when lenders changed their rules and interest rates caught up with inflation, it began to hurt more and help less.

As long ago as 1969, the Federal Land Banks were one of the first lenders to insist on variable rates on their new mortgage loans. For a long while, insurance companies and others continued to lend at fixed rates, and country banks were relatively liquid and had relatively low costs of funds. All that has changed as lenders and savers have come to anticipate inflation, and to insist on protection. Leveraging inflating land prices for your financing is no longer so opportune as lenders have acted to protect their own real earnings. More broadly, the ability of any large group to gain from inflation is problematical at best.

The message should be clear. Whatever the earlier favorable experiences with inflation or, for that matter, the success that many may have had in adapting personal and business lives to increasing inflation, there is now a widespread public perception of the distortions, inequities and dangers of continually escalating prices -- a recognition that beating back inflation must be our first economic priority. That recognition is an important and critical first step to arriving at the policies to deal with it. But let there be no illusion. Effective actions will require hard and painful choices. They will only be successful with broad public appreciation and understanding of the need. Let us understand there are no quick and easy solutions, in monetary policy or elsewhere.

Monetary policy does have an absolutely essential role to play in the effort to restore price stability, as your own policy statements have explained. History shows no anti-inflationary program can be successful unless the growth of money and credit is restrained to amounts consistent with a return to stable prices. But when the economy is both expanding <u>and</u> inflating, monetary restraint means there is not enough credit to meet everyone's desires. Interest rates are apt to rise, perhaps sharply, as we have seen. Sectors of the economy dependent on credit are squeezed. And, if other policies are aggravating inflation and demand for credit, that squeeze will be painful.

All that is familiar in the light of what has happened in recent months. What that experience illustrates so clearly is the necessity of combining the money and credit restraint required to deal with inflation with appropriate and complementary fiscal and other policies.

Let me be more specific. Growth in the various money and credit measures during 1980 was close to, and in some instances slightly above, the upper end of the ranges we set at the start of the year. Our targets and objectives were generally agreed to be appropriate -- certainly not too low -- if we were to encourage a return to a more stable economic environment. But it is clear that that money and credit expansion fell well short of meeting all of the demands in the economy for financing real growth and investment and the turnover of goods and services at higher prices. As borrowers competed for money as we rebounded from recession, there was not enough to go around, and interest rates got painfully high.

In these circumstances, restrained money and credit growth seem to collide with the needs of an expanding economy. There is an apparent dilemma. On one side, constrained money and credit growth is necessary to control inflation. But that constraint, when inflation adds to demands for credit, places heavy strains on financial markets. The continued growth of business activity may, consequently, be called into question. The more sensitive areas of the economy are saddled with an especially heavy burden.

Farming certainly is in that category. Cyclical interest rate movements are, of course, not a new experience for farmers generally. But I well understand that many of you find the current interest rate experience shocking and alarming. I have been made very aware of both the mounting strains of current interest rate levels and your fears for your future financial condition if the current levels of credit costs are permanent rather than a cyclical or temporary phenomenon. I sympathize with those concerns. But let me say frankly, I see no escape from those problems by easing restraint on money and credit growth -- by pumping up the money supply. Unfortunately, the historical record seems clear that it is inflation and not real growth that would increase as a result. Sooner or later -- and it is all too likely to be sooner -- interest rates would rise again, as inflation became even more embedded in our society.

It is demonstrable, however discouraging, that after long years of inflation financial markets -- indeed, all of us involved in making business or personal spending decisions -- will seek protection against anticipations of inflation. We save less. We buy land or more exotic investments. We demand higher interest rates. Policies or actions that appear to support or acquiesce in the inflationary process rapidly affect expectations about future inflation, and divert savings away from traditional uses. Rather than helping those such as farmers, builders and small businessmen particularly vulnerable to increasing interest rates,more rapid money creation would worsen their position over time.

Under those conditions, the only responsible course is to continue to curb the growth of money and credit in the interest of encouraging the return to price stability. But there are ways to reduce the risks, pains and inequities that result from leaving the fight on inflation to monetary policy. Monetary restraint is essential. What we also need is strong complementary actions in other directions to help change the upward trend of prices and to reduce pressures on financial markets. It is in this area where little has been accomplished, where the need is urgent, and where a great opportunity exists.

The first of those areas, as is widely recognized, is in the fiscal posture of the Federal Government. By any measure, the impact of the Federal Government and its agencies on our credit markets is enormous. In 1980, the Federal Government and sponsored credit agencies accounted for more than 20 percent of the net funds raised by all sectors of our economy, and if funds raised under loan guarantees are added, the total was about 27 percent. The combined deficit of the Federal Government and the Federal Financing Bank is the equivalent of some three-quarters of total personal savings. Can there be any doubt about the pressures these credit needs place on money markets and interest rates in an environment of inflation, expanding private demands and restrained growth of money and credit?

In these circumstances, reduced growth in government spending can have a major pay-off. Other potential borrowers will not be shouldered aside by Federal Government demands. Interest rate pressures should be moderated. Expectations about inflation can begin to be changed.

But you should be under no illusions about the difficulty of the job of restraining and reordering our spending programs. Every change affects someone, and some interest group. Every group, whether agreeing with the general need for restraint or not, will argue that their program is the exception -- that their program deserves priority in spending. And many spending cuts will involve real sacrifice. I suspect those of you in agriculture will be as concerned as others about these decisions. I claim no special wisdom about the problems of your industry, and where there may be opportunities for restructuring and modifying agricultural programs. But I would certainly encourage this organization, and each of you individually, to continue to look carefully and constructively, as you have in the past, for ways of improving the effectiveness of critical farm programs, of reducing their cost and of eliminating those that may be distorting your investment decisions. In that connection, I have noted with interest some of your statements about the dawning realization of many farmers that the solution of agricultural problems does not lie in grand new government programs.

Spending restraint is vitally important for another reason. It is only that restraint that can make the tax reductions we need to reduce costs and improve incentives a prudent policy, consistent with the fight on inflation and the restoration of budgetary balance in a reasonable time frame. Otherwise, the danger is the credit markets could become still more congested, damaging the very prospects for investment and the incentives that tax reduction seeks.

There are a vast array of government programs outside the budgetary area that also need to be controlled. Built up over the years, they are designed for valid purposes -- health, safety, the environment, fair employment practices, and protection for the weakest elements of the economy. But in too many cases, those valid objectives have entailed excessive costs, they have impaired incentives unnecessarily, and even failed in their purposes. No doubt you in agriculture are more familiar than I with the problems, faced as you are with restrictions on the use of chemicals, farm safety and the disposal of animal wastes from feed lots. There is no sweeping generalization about such specific programs that I can validly make. But I do feel that we can, upon close examination, find a better balance between needed protections and our ability to control costs and produce efficiently.

Again, the job will not be easy. Some individuals and groups will fear losing long cherished positions, and resist even small changes out of concern that precedents will be set for further cutbacks. And real compromise of objectives may be necessary.

But in assessing the needs, let me point out the obvious. Relying on monetary and credit restraint alone to fight inflation is not a painless process -- and the strains are spread without much discrimination. Let us not be deluded into thinking there is some combination of policies that, in the short run, can move us to price stability without strain. But let us not also forget the payoff can be huge.

The fiscal and other policies we need are difficult -- and they are dependent on public understanding. It is the individual members of Congress who must change the laws and enact the legislation, and they will need the open and vocal support of our citizens. I hope you will be prepared to back the Congress when they are asked to make the hard decisions.

Our basic objective is to increase productivity, to utilize efficiently more of our human resources, and to resume economic growth. We can't do those things while inflation moves higher. The longer we take to face up to the problem, the greater the difficulty in the end. That seems to me the simple lesson of the 1970's.

That is also why those of us responsible for monetary policy mean to continue to restrain money and credit growth. Without that central policy in place, others will not be successful.

I realize that restraint on money creation, taken alone, poses recurrent risks and pressures on those sectors of the economy dependent on credit. I would urge that those pressures can and should be reduced -- reduced above all by prudent fiscal policy. We can marshal other approaches -- and we should -- in the fight on inflation. And then we will succeed.

That success will not be instantaneous. We have first to turn a powerful, continuing inflationary momentum. But with the objective clear, and policies in place, neither need progress be so delayed as to discourage understanding and support.

Indeed, these are grounds for optimism that the field has been prepared; that the public is ready for new policies and vigorous action. If I may be so trite as to use an agricultural metaphor, the seeds sown now can bear a rich harvest. We will need to carefully nuture the plants of renewed confidence that can soon spring up. We need to persist in our policies in the midst of all those hazards uncertain external events can place in our way. Above all, we must not take the attitude that we can leave it all to somebody else to do the work and take the risks. There is, of course, no group in American life that knows those simple lessons better.

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