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Statement by

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before the

Senate Committee on Agriculture and Forestry

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I am pleased to meet with this Committee to discuss the impact of grain sales to the Soviet Union on the outlook for food prices.

Your invitation to testify today was no doubt prompted by my comments on this subject in response to questions by Senator Kennedy when I met with the Joint Economic Committee on July 29. At that time, news of the adverse effect of drought on Russian grain harvests, and of large Soviet purchases from the United States and other countries, had already caused sizable increases in our grain prices. Further Soviet purchases were widely anticipated as Russian crops continued to deteriorate. Meanwhile, our own prospective corn yields were being set back by drought in the Midwest.

These developments dashed hopes that there would be significant progress in restoring depleted world inventories of grain during 1975. It now appears that the world still faces an uncomfortably tight balance between demand and supply for wheat and feed grains.

In view of these developments, concern about the effects of rising food prices on the over-all rate of inflation is clearly warranted. To a Federal Reserve official, inflationary developments are troublesome regardless of the sector in which they originate. My comments before the Joint Economic Committee,

however, were not intended to suggest that food prices would rise so drastically that serious consideration should be given to export controls. That was not my judgment then, nor is it now. For the record, I have attached to this statement a complete, unedited transcript of my comments about food prices before the Joint Economic Committee on July 29.

As members of this Committee may know, I am not an expert in agricultural matters. In this area, I must depend on the specialized knowledge and experience of others. But anyone familiar with economic principles should be able to see the general price implications of the developments I have sketched.

It is, first of all, a fact that the Soviet Union is experiencing this year a very disappointing grain harvest, particularly in relation to earlier expectations. Current estimates of the shortfall vary, but it is widely agreed that the deficit is large. It is also a fact that in order to avoid a drastic reduction in its livestock production program, the Soviet Union has entered the world grain market as a buyer of significant quantities. This sudden and large addition to demand for the free world's grain had the predictable effect of raising grain prices substantially.

By the third week of August, cash wheat prices in this country and also the price of corn for delivery in December were about 40 per cent higher than on July 1 -- or immediately before the Russian addition to demand. In recent days these prices have dropped, but they are still about 25 per cent above their early July level.

Given the worldwide market for grain, there is little that we in the United States can do about this increase in grain prices short of imposing export controls. To be effective, such controls could not be restricted to the Soviet Union; they would have to apply to grain shipments to all countries. I have at no time advocated such a step, nor could I do so in circumstances such as those now prevailing. Comprehensive export controls would constitute a sharp departure from our longer-term economic and agricultural policies, and could have unfortunate consequences. Such a step should be contemplated only in the event of a very severe imbalance between demand and supply.

As every student of economics knows, American agriculture is highly productive. Our farmers are capable of producing -- year-in and year-out -- far more wheat, feed grains, and soybeans than we can consume. Foreign markets have been

developed for the excess quantities. These markets must be maintained if American agriculture is to remain relatively free from restrictions on production and continue to make a substantial contribution to our balance of payments. But in developing these markets, we have also assumed responsibilities. Other nations have come to rely on the United States as a source of supply of food and livestock feed. They need assurance that they will have access to our markets on a regular basis. This element of our foreign economic and agricultural policy must not be tampered with lightly.

Let me turn now to the probable impact of Soviet grain purchases on our retail food prices. It is perhaps natural to associate the price of grains with that of bread. This direct effect of increased grain prices should not be large, however, since the cost of grain accounts for only a small fraction of the retail price of cereal and bakery products. In fact, the cost of all farm-produced inputs represents only about one-fifth of the average retail price of these items. The bulk of the impact of higher grain prices on the consumer's food budget may be expected to occur through their indirect effect on the prices of meat and livestock products. In view of higher feed-grain prices, farmers and ranchers will tend to produce and market less meat, poultry,

eggs, and milk in 1976 than they otherwise would have. Prices of these items will therefore be higher than they would have been.

The Department of Agriculture has indicated that the direct and indirect effects of the Russian purchases may cause food prices in 1976 to be about 1-1/2 per cent higher than they otherwise would have been. This estimate is based on Russian purchases already made and announced. Making some allowance for the likelihood of further Soviet purchases, I stated on August 24, in response to a question on Face the Nation, that the impact on retail food prices of sales to the Soviet Union may be on the order of 2 or 2-1/2 per cent in 1976.

The rise in food prices that appears to be attributable to the Soviet Union's harvest deficiency is thus quite sizable. But a much larger factor in the retail food price outlook is the relentless rise of production and marketing costs, both farm and nonfarm. For example, the Department of Agriculture now expects food prices to average 9 per cent higher this year than in 1974, in large part because of increases in wages and other nonfarm costs.

In view of the troubles that inflation has already caused, we cannot look upon price increases of this magnitude complacently. In today's environment, virtually anything that adds to inflation

is deplorable -- whatever its source or size. Nowadays, inflation from almost any source tends to be built into wages and thus to aggravate the wage-price spiral. Although there is little we can do about the rise in food prices in the near term, a major aim of public policy should clearly be to end the relentless upward march of the general price level.

We can look forward with reasonable assurance to stable food prices if and only if the high rates of increase in wages and other costs of food production, processing, and marketing subside. Some relief will be obtained, however, when depleted world grain stocks are restored to levels at which customary variations in annual harvests no longer lead to unduly wide fluctuations in grain prices. Earlier this year it appeared that a significant step toward that goal would be taken in 1975, but it is now evident that we must wait at least another year.

But we need not wait to seek ways of preventing future disruptions by the Soviet Union in our grain markets, and I hope that we will not do so. It seems reasonable to me to expect the Soviet Union to build up a substantial inventory of grains, so that

its purchases in our own and other markets will be less disruptive in the future. This is a matter that officials of our State and Agriculture Departments may well want to explore with their Russian counterparts.

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