

Handwritten notes:
I will be in St. Louis
you have
it a

File

LOOKING AHEAD WITH AGRICULTURE

Address
by
Chester C. Davis
President, Federal Reserve Bank of St. Louis

Before the
Agricultural Luncheon
of the
Illinois Bankers Association
Jefferson Hotel, St. Louis, Missouri
Thursday, May 2, 1946

LOOKING AHEAD WITH AGRICULTURE

We are meeting today almost exactly one year from the time that the German armies collapsed and the long-sought victory in Europe was proclaimed. As one looks back over our wartime experiences he cannot help but be impressed by the extent to which our great accomplishments depended upon a singleness of purpose and action by all elements of our population. Now, as we are wrestling with the many problems that have arisen in the struggle to reorient ourselves to peacetime activities, we must not forget that lesson. In peace as in war we must always recognize that mutual interdependence is the great central fact of modern life, and honest cooperation is its best expression.

It is this theme that I wish to stress as I talk with you about the future of agriculture in relation to banking. Some economists argue stoutly that high level employment and prosperity in city occupations must have their roots in high farm income and rural purchasing power. They make a good case. Others contend just as firmly that you cannot have healthy agriculture unless nonfarm consumers are made prosperous by full employment at high wages. I can't quarrel with that view either. The argument between these points of view is like the quarrel of the two knights who approached the Crusader's statue, one from the front, the other from the rear. One claimed that the shield was gold, while the other contended it was silver. They drew their swords to settle the matter, and no telling how it would have ended if they hadn't switched sides in the heat of battle, so that each one saw that the other was right.

It is a good deal like arguing whether your right leg or your left leg is responsible for getting you there when you walk. We need both legs to go anywhere, and we need them healthy. Business management and labor must gear their efforts toward expanding production and maximum employment to

match the full production of American farms. Conversely, industry and labor are largely dependent on a healthy agriculture for the purchasing power required to maintain expanding production and full employment.

Let us take a moment to survey the field. We are in a period when postwar plans are being put into action. It is a time of acute unrest and adjustment, of jockeying for advantage between great economic groups while our industrial plant withdraws from war and goes back to the production of peacetime goods. These days and the days ahead are packed with the most explosive elements with which this country's economy has ever been confronted. To look ahead with agriculture in the light of farm experience between the two world wars is a sobering exercise even for the most optimistic, the most confident.

Farm production has expanded during the war. For the last three years we have been producing annually about a third more food than in the immediate prewar years. The smallest farm labor force in recent history turned out this greatly expanded farm production, and they had less than the normal supply of new machines and replacement parts to work with.

The nation's agriculture has demonstrated its capacity to produce more than we have ever, in peacetime, consumed at home and sold abroad. To be sure, the farmers did it by working long hours and by drawing on stored-up soil fertility and other reserves; they had the help of old people who would normally have retired, and of women and children in the fields.

We had expected the intensity of effort to abate somewhat now that the war has ended. Instead we find ourselves face to face with a world famine emergency that must spur us to farm production efforts in 1946 and 1947 equal to or greater than the phenomenal records of the war years - lest a hard won victory be lost in the shrunken stomachs of a hungry world. Under these

circumstances there can be no letdown in farm production now.

Even after the present acute crisis has passed there will be a tendency to maintain the new high levels of production. This has generally been true in the past, and forces are at work today that will enable one pair of hands on the farm to operate more land, and produce more goods than ever before. We are about to see the greatest advance in the mechanization of agriculture in history, and the rate of technological improvement will continue.

During the war many farmers suffered from a shortage of farm labor, but as more new and improved machinery becomes available relatively fewer workers will be needed in agriculture and a steady expansion in non-agricultural occupations and industries will be necessary to provide job opportunities for those workers who leave the farms. Bear in mind, too, that the population of our cities does not renew itself; it is refreshed and maintained by the higher birth rate out in the country. Such an expanding economy would provide better houses and better living for all. If reasonable balance can be attained, those who remain on the farm -- and I hope they will be the best of each generation -- will constantly increase their efficiency, the output per farm worker will rise, and they should be able to enjoy incomes per farm worker comparable to average incomes in the nonfarm pursuits.

As a member of the financial community, I am interested in the prospect that improvement in the efficiency of farm workers will require the use of much new capital in agriculture. I am not thinking of capital that goes to purchase land in inflated prices, but rather capital that will enable farmers to balance their systems of farming, to conserve the soil and maintain its productivity, and to have adapted new power machinery and equipment to work with. This means capital for soil-saving improvements such as terraces

and waterways, for fences to adjust the layout of the farm to the topography of the land, for new or modernized buildings to bring convenience and comfort into farm living and livestock production, capital for farm ponds and water systems, for electrification, and for many other things that make for better living and more efficient production. Capital for these purposes is productive; it will continue to pay high returns. On the other hand, capital that is spent to bid up prices on farm real estate and other capital goods above the level that can be sustained by normal income is not productive.

A good example of a way increased capital can be used to step up the efficiency of farm production has been developed at St. Joseph, Missouri. As a part of the St. Joseph long term farm program, the Buchanan County extension agent, the agricultural division of the St. Joseph Chamber of Commerce and the St. Joseph banks, all working together, have developed a realistic and interesting plan that is attracting wide attention. This is a plan for advancing credit to dependable and competent farmers for a complete soil conservation program -- to stop erosion, to re-fence fields so they can be farmed on the contour, and to rebuild the productivity of the soil through extensive application of lime and fertilizer. It is an excellent illustration of how the increased use of capital on farms can contribute to greater production, lower costs, and higher incomes on the farm.

Illinois banks have been quick to recognize the merits of soil improvement loans. Many of you have for years advanced credit to farmers for various soil conservation and improvement practices. In recent months a number of announcements have come from Illinois banks outlining a new credit service to farmers for financing a complete soil conservation and improvement program on the individual farm. A definite trend toward a more realistic extension of farm mortgage credit is evident.

More realism must also be injected into loans for the operating capital needs of agriculture. Here I'm thinking of farm machinery, foundation livestock, and household appliances. Farm loans for these purposes can and must be developed on a basis very similar to the term loan which has been developed by city banks and successfully applied in the nonfarm industries. The farmer has too often been in debt to a wide variety of creditors for individual pieces of equipment and appliances, which, in many instances, resulted in payments too heavy to meet since the aggregate of payments were not based on his capacity to pay or timed to his income pattern.

Bankers must sit down with farmer customers and study the over-all needs of the individual farm operation in an attempt to determine the kind and amount of new machinery, foundation livestock, and household appliances that are needed to reach maximum efficiency and maximum net income. Estimates of income and expenses for the individual farm unit can be worked out with reasonable accuracy and a loan set up with the disbursement schedule timed to meet operating capital outlays as they are needed with repayments keyed to earnings. In this way there would be one bank creditor financing the farmer's entire operating capital credit needs with only one planned schedule of payments to meet. Loans developed on this basis can increase the farm loan volume of many banks and remove from the farmer much of the pressure that results from unsound borrowing.

Bank credit programs for saving the soil, for balanced farming, and for operating capital can mean much to Illinois farmers and bankers alike. As they move forward, living standards of farmers will be advanced, and the higher incomes on farms will be reflected in greater business activity and better living in the towns and cities. The farms you will be helping to safeguard will be here to produce wealth for your children, your children's

I do not want to leave the impression that the farm improvements ahead of us can only be paid for by the use of credit. American farmers have come out of the war in the strongest financial position of their history. Although official estimates for the beginning of this year are not yet available, it seems likely that total farm assets rose from \$54 billion on January 1, 1940 to about \$100 billion on January 1, 1946, and farmers' net worth increased from \$44 billion to about \$91 billion. During that period farmers' debts decreased from \$10 billion to \$9 billion. Thus a \$1 billion decrease in debt has been accompanied by an increase of \$46 billion in total assets and \$47 billion in net worth. Much of the dollar gain in agriculture has been due to higher inventory prices for real estate and personal property, but on the other hand a considerable amount has been due to an actual increase in asset volume. For example, cash, deposits and Government securities owned by farmers have increased by over \$15 billion.

Pulling upon these enormous financial reserves is the pent-up demand for many goods that have been scarce during the war. The situation presents a tremendous force for inflation. The most effective brake on price inflation would be an abundant and increasing supply of goods and services people want to buy. But we cannot suddenly increase the number of good farms. For that reason, from the viewpoint of inflation dangers, farm real estate is probably the number one problem in agriculture. To date the overall increase in land prices has not been alarming. In most areas the number of transfers has not been unusually high, and in general the use of credit in connection with farm sales has been reasonable. But many factors are at work which tend to push up the price of land. Lower interest rates, longer term farm mortgages, the desire to hedge against inflation, price support programs, veterans who wish to become farmers, and the enormous volume of money are all forces in a market in which the supply of desirable farms is limited. These inflationary forces

are not peculiar to real estate. They can exert a disastrous influence on the price of such items as farm machinery and household appliances if everyone tries to buy at once, before the manufacturers hit their stride.

Farmers can use their financial power for investment in better living on the farm, for increasing net returns and cutting production costs through better farming practices and the use of new labor-saving farm machinery.

On the other hand, the liquid assets in agriculture can be used to bid up the price of land, and of articles which are still in short supply. If agricultural resources are used in these latter directions, the result will be hardship on farms for at least a generation to come. The decision rests with the farmers, themselves, and the choice they make during the next several months will influence their standard of living and their security for a good many years.

Illinois banks can be instrumental in guiding the liquid assets of Illinois farmers into productive investments. As more goods of all kinds become available there is likely to be a considerable expansion in the total volume of farm credit. Banks, through proper consideration of the individual farmer's overall credit needs, can be very helpful in preventing a recurrence of the many unsound farm credit practices of past years.

I cannot leave the problem of inflation without some reference to the role of monetary policy. It seems to me that the use of general monetary controls is extremely important at this juncture since direct price controls cannot have the same effectiveness as they did under war conditions. At that time we had rationing and other drastic restrictions on production and distribution of many types of goods.

From now on greater reliance must be placed on monetary policy to prevent further expansion in the money supply (deposits and currency) which

toward balancing the budget and the Treasury is using War Loan deposits to retire maturing debt, the underlying conditions which produce further monetization of the debt through cheap and easy access to Federal Reserve funds continue. So long as banks can turn over their low-interest-rate short term securities to the Federal Reserve banks and obtain reserves with which to buy longer-term Government securities away from nonbank holders at high premiums, we can expect a further increase in the supply of money that will add to inflationary pressures. And we must not forget that every dollar of reserve funds which a bank obtains provides the basis for five or six dollars of deposit expansion for the banking system as a whole.

As institutions and other investors sell bank-eligible issues they use the proceeds to bid up prices and reduce yields on longer term Government securities. Some of the funds inevitably spill over into the markets for corporate bonds and stocks, real estate, and other capital assets. The steady reduction which is occurring in long-term interest rates as a result of this process leads people generally to capitalize equities, real estate, and other capital assets on a lower interest basis, thus further contributing to inflation of values. This tends also to induce a higher rate of spending for goods and services, because at a time when capital values are rising people are more willing to spend for consumption a larger proportion of their current incomes.

In my opinion, the monetary policy which was followed during the period of large war financing is no longer appropriate at this stage. It is, of course, important that any change in monetary policy should be carefully coordinated with appropriate fiscal policies. We are still on uncharted ground with respect to the problems that may be involved in managing a debt of \$275 billion. Bankers and other leaders of the financial community must give

advice and counsel to the authorities who are charged with the large responsibility of managing a debt of this size in the period ahead.

Now in conclusion let me return to the note sounded in the beginning -- mutual interdependence and the need for cooperation in all elements of our complex national life. Bankers have enormous responsibilities, and not to their depositors and stockholders alone. The power of influence and example which the individual banker exerts in his community adds up in the aggregate to an enormous force. That force can be used for the national good if it is based on self-restraint and farsightedness in this day of unprecedented money volume, easy profits and inflationary threat. If it moves intelligently, this force can bring about and maintain unity and uniformity in national monetary policy and the agencies that operate in that field. Many prophets tell us that "boom and bust" will be our experience after this war's expansion, as it has been before now. I think that it need not be, and that you men here in this room can help see that it will not be.

ooo000ooo