

THE MONETARY SITUATION

an address by

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Meeting with all of you here today makes me feel very much at home. As you may know, the Federal Farm Credit System was for me a starting place, and those were truly wonderful years. The friendships made, the knowledge acquired, the problems shared--I'll never forget. Indeed, they became a part of my life, and they remain so. I consider it a very great, personal privilege, therefore, to be here with you at this time.

My purpose, though, is not to reminisce, however tempted I may be. For in this age of unbelievable change, we can ill-afford to spend much time looking back. Indeed, it seems that--individually and collectively--we can just barely meet the problems of the present. And as we struggle with these problems, we are confronted with the still greater challenges of the future.

The managers of our agricultural resources and of the Federal Reserve System share many of these same problems. Both groups have many of the same international economic interests. Both are anxious to preserve the value of our currency. And both equally desire that the limited loan resources available today be used to meet the really constructive credit needs. Let's take a look at just how well these three important efforts are coming along.

First, in the international field, we can take pride that we are much closer to a balance in our international accounts than we were only two or three years ago. This could not have happened without an increase in our nation's exports.

I'd especially like to single out agricultural exports because of their significant contribution to our balance of payments. The United States sells farm products to over 125 foreign countries and territories, and these farm exports make up about one-fourth of all our merchandise exports.

Now, let's get closer to home. In this section of the country, farmers have a particularly large stake in this export market. Over 10 percent of the nation's

agricultural exports come from farms in the six-state region of the Federal Reserve Bank of Atlanta--namely, Alabama, Florida, Georgia, Louisiana, Mississippi, and Tennessee. This represents over 15 percent of the total value of this area's farm products. It also means that about one of every six persons employed in farm production in these six southeastern states is producing commodities for export.

So far as I can tell, however, these facts give only part of the story, because certain exports from farms in this six-state region make a much greater contribution to total U. S. farm exports than is suggested by the figures just cited. To name a few: Of the total value of cotton exported by the United States in 1965, this six-state region's sales accounted for 33 percent; poultry products, 36 percent; cottonseed oil, 33 percent; rice, 26 percent; and fruit and nuts, 22 percent.

Here we can give credit where credit is due. The Gainesville poultry grower, the Mississippi Delta cotton grower, and the Crowley, Louisiana, rice grower, all have strengthened this nation's efforts to reduce its payments deficit.

In fact, the agricultural economy as a whole has done an outstanding job. Let us not, for one solitary moment, underestimate this contribution. The nation's exports of agricultural products are the highest in history. The U. S. Department of Agriculture's estimate of \$6.5 billion or even more for the current 1965-66 fiscal year exceeds export records set in each of the last two years by nearly a half billion dollars.

This growth in farm exports is especially gratifying because other trade results are less encouraging. The 10-percent increase in the agricultural trade balance in the first nine months of this fiscal year, recently reported by the Secretary of Agriculture, was accompanied by a 25-percent decline in the nonagricultural trade balance. Had we not sold more agricultural products abroad, the long-uphill struggle toward equilibrium in our balance of payments certainly would have been far more difficult!

I have discussed this accomplishment in our farm export area at some length because it was significant in helping cut our payments deficit to \$1.3 billion in 1965--a marked improvement over the \$2.8 billion deficit for all of 1964. Every improvement in each sector of our balance of payments, of course, brings us closer to our long-run goal of reaching equilibrium, and I might add here that we did have gains in other sectors.

Now, I would be amiss if I did not mention the Federal Reserve System's voluntary credit restraint program. Aimed at keeping down the overseas lending of commercial banks, this effort has contributed effectively to the reduction in the payments deficit. The success of the program can be laid to the close cooperation received from commercial banks.

Whether the program can be continued indefinitely remains to be seen. But meanwhile, it has worked amazingly well. In the first quarter of 1966, we actually had an inflow of \$255 million in short- and long-term bank funds.

In allowing ourselves some degree of optimism in the battle to reduce the dollar outflow, however, we must not make the mistake of thinking all is well. Rising imports and increased spending abroad in connection with the Viet-Nam build-up are not helping the payments situation. On the contrary! Even making allowance for special factors, we have been barely holding our own. We must do better!

Although I am still hopeful that equilibrium will be achieved eventually, I am just a little discouraged at the moment by another development which does not bode well for our export battle. Here I'm speaking, of course, of nothing other than the small, but steady, increases in our domestic price levels. I do not believe that I need to cite many figures for you to recognize what I'm talking about. It is well known that the consumer price index is now almost 3 percent higher than a year ago and the wholesale price index has advanced by 5 percent in the last 16 months. That adds up to quite a rise in prices when you consider that from 1960 to 1964,

wholesale prices were very stable.

Need I point out that the increase in prices of farm products and processed foods--mainly due to reduced output of certain products--has been a major factor in pushing up the price levels? Surely not! We would be off balance, indeed, if we failed to recognize this element in the price picture during 1965 and early 1966. Yet we would be equally off balance if we believed that we could have enjoyed continued over-all price stability had we only escaped this advance in the cost of food.

The other culprit, rising prices for industrial commodities, has received less publicity. And yet, industrial commodity prices have climbed 3.6 percent since the beginning of 1965. Even more disconcerting is that this trend is becoming more pronounced. Almost one-third of the gain in industrial commodity prices has occurred since the beginning of this year. And much of this acceleration has come from higher prices posted for machinery and equipment.

Price increases in the machinery sector of the economy are particularly troublesome, because we must keep our machinery prices down if we want to sell more machinery abroad. How can we expect to expand our sales abroad or even hold our own unless we can compete effectively in world markets? Our ability to keep industrial prices stable from 1960 to 1964 clearly had helped us expand exports. It would be tragic if a rapid price rise stifled our export growth and set us back in our battle on the international payments front. We cannot afford inflation for balance-of-payments reasons! Neither can we afford inflation for domestic reasons!

You are certainly the last people in the world who need to be told about the dangers of inflation. And you know as well as I do that American agriculture can suffer as much from inflation as any other sector of the economy. When domestic prices increase along a broad front, farmers must pay more for fertilizer, equipment, gasoline, and other supplies. Yet the prices farmers receive for much of their output is determined by other forces, namely the supply and demand for farm products.

If domestic prices paid by farmers rise rapidly while the prices they receive stand still, many farmers will get hurt, some very badly. When farmers get hurt, those who lend to farmers also can suffer economic reverses. Consequently, neither American farmers nor those lending to American farmers can afford to lose the struggle against inflation.

Of course, I realize that prices are almost always on the farmer's mind. And I am not unaware that when we put last year's boost in food prices in proper perspective, we see that developments in farm output and food supplies have been more influential than other underlying inflationary forces in pushing food prices up. In reality, over the long pull, the cost of food has come down. As consumers, we like this record very much.

This accomplishment would not have been achieved without the phenomenal gains in productivity of farming over the years. And productivity, in turn, could not have risen without significant increases in credit which farmers have received and enjoyed.

You helped meet these needs of modern farming last year and the years before. And in so doing, you have furthered not only the progress of the farmer but of your rural community and trade area.

I know these farm credit needs are great. And I recognize that the real credit needs of farmers must be met. But I would also like to point out that superimposed on the credit needs of agriculture today are stepped-up credit demands from almost every sector of the economy.

The Federal Reserve System is keeping a wary eye on this strong expansion of credit. The wisdom of this policy must be obvious: The economy has given signs of overheating, and inflation is a real threat! There is every reason to believe that inflation would not only intensify our balance-of-payments problem but would bring hardship to farmers and others least able to afford it.

In other words, the Federal Reserve System recognizes that if it fails to slow an extraordinary expansion of credit, inflation may get the upper hand. Neither the Federal Reserve nor the country at large can afford this. The decision to moderate the expansion in credit, therefore, was inevitable.

This does not mean that we in the Federal Reserve have any desire to bring our nation's economic activity to a jarring halt. Actually, the policy of restraint has been gradual. The increase in interest rates that you, along with everybody else, have been experiencing in your trips to national credit markets can be laid more to the extraordinary strong demands for credit than on Federal Reserve actions. Admittedly, however, the Federal Reserve is trying to hold in check the expansion in credit even if the result is slightly higher interest rates.

In my view, the System has no other choice. While accepting such action as being necessary, we must, nevertheless, recognize that whenever credit is curtailed, somebody fails to get all the credit he needs. In particular, somebody who may need this credit pretty badly.

Regrettably, monetary policy is not a sufficiently thin-edged blade to assure that all credit-worthy borrowers get their credit needs fulfilled and everybody else gets his credit cut off. Monetary policy just does not work with such fine precision.

Therefore, I submit that the battle to hold prices down cannot be fought with credit restraint alone. In the endeavor, we should likewise restrain increases in wages and other costs; we should keep a close watch on government spending; and we should give serious consideration to higher taxes.

At the outset, I said that we recognize your problems. We do indeed. I am confident that you also recognize our problems with the monetary situation. These problems are not easy to solve. But solve we must and solve we will--with your help and understanding.