FEDERAL RESERVE BANK

OF DALLAS

March 30, 1924.

COST AND PRICE

To the Bank Addressed:

Recent reports are to the effect that the Eleventh District's cotton acreage for 1924 will be considerably larger, and the cost of producing the crop will be materially higher, than in 1923. The acreage expansion can of course be attributed in a large measure to the price received by the growers for last year's production. That there is also a definite relation between last season's price level and the current season's production costs is a fact that is perhaps not so generally recognized, but one that deserves the closest attention by all who are genuinely interested in the progress and welfare of our leading industry. The situation, therefore, seems to make this an appropriate time to call the attention of our member banks to some of the fundamental factors that enter into the relation between the cost and price of cotton, using the term "cost" in the broader sense to cover the producer's expenditures during the crop-growing season.

Unlike the merchant or manufacturer, whose operating policies are predicated upon the inflexible rule that costs must always be held down to an irreducible minimum, the farmer usually relies upon the price received for the previous season's crops as the basis for determining the amount of funds he may safely expend during the current growing season. For example, it will be recalled that much of the distress in which our farmers found themselves in the fall of 1914 when the outbreak of the war forced the price of cotton below 7 cents per pound, was largely due to the fact that at the time the crop was planted spot cotton was commanding 12 to 13 cents per pound, and the growers had adjusted their production outlay accordingly. On the other hand in the spring of the following year, 1915, the prevailing price was only 8 cents per pound, and although the 1915 crop was produced on an 8-cent price basis, the market advanced to 11 cents in the fall and yielded the producers an unexpected return.

Then in 1920 the disastrous cotton history of 1914 repeated itself, when a crop planted while the price was around the 40-cent level was sold on the average at the 15-cent level.

These references to the past would, of course, serve no useful purpose now if it were true that production costs were no more subject to the producer's control than is the price he receives for his product. But so long as the farmer is free to decide (1) the amount of acreage he can successfully cultivate; (2) whether his crops will be produced by himself or by hired labor; (3) whether he will raise his own living at home, or obtain it by purchase; and (4) whether he will adopt an economical or extravagant standard of living,—he cannot escape the realization that his crop production costs are not only well within his power to control, but can actually be pre-determined and budgetized.

Since he exercises, therefore, an almost complete control over "costs", but can neither control nor foresee the "price" he will receive, it necessarily follows that the cotton farmer's problems are problems of **cost**, and not of **price**.

In summing up the situation I hope that I may, without presumption, point out to our member banks that a very definite opportunity and obligation confronts them in the form of their privilege to exercise a reasonable degree of bank supervision over the expenditure of funds loaned for agricultural purposes. That such supervision can serve a most helpful and timely purpose in bringing the agricultural industry in this section to a permanently profitable basis has become more clearly apparent than ever before in the light of the conditions under which the farmers are now operating, and which may be summarized as follows:

> **Crop production costs constitute the one definitely determinable and controllable factor of crop profits; are inseparably related to the yield per acre; and in the final analysis depend upon the producer's methods of operation and methods of living, which in turn are largely right or wrong according to the influence exerted upon them by the banker to whom he looks for credit assistance and intelligent counsel.**

In presenting these thoughts to our member banks at this particular time, the beginning of a new crop-growing season, we have in mind the fact that if production costs are held to a minimum from the very beginning of the season such a program would prove far more effective for insuring profitable production than to permit costs to take care of themselves, and then after they were incurred, to seek recourse to some arbitrary price-fixing plan in conflict with economic laws in the hope of recovering both cost and desired profits upon their products.

While cotton is the only commodity referred to in this discussion (on account of its paramount position in our productive industries), the same principles here enunciated would constitute the only satisfactory basis for profitably producing any other commodity.

Yours very truly,

Lynn P. Talley

Federal Reserve Agent.