

Statement of  
HUGH D. GALUSHA, JR.  
Before the  
National Advisory Commission on Food and Fiber  
Minneapolis, Minnesota  
September 15, 1966

Mr. Chairman and members of the Commission, I am Hugh D. Galusha, Jr., President of the Federal Reserve Bank of Minneapolis, and President of the Upper Midwest Research and Development Council. My statement today is drawn from both backgrounds.

The Council was organized in 1958, and for most of its career was concerned with compilation of data about the major sectors of the Ninth Federal Reserve District economy. Among the four sectors, agriculture received considerable attention. A number of papers specifically dealing with agricultural problems of the district were prepared. These were:

Upper Midwest Agriculture: Structure and Problems, Arvid C. Knudtson and Rex W. Cox (January, 1962); and Statistical Supplement (April, 1962).

Upper Midwest Agriculture: Alternatives for the Future, Elmer W. Learn, Rex W. Cox, and R. J. Herder (December, 1962).

Upper Midwest Commodity Flows, 1958, B. F. Duncombe (October, 1962).

Cattle Feeding in the Northern Great Plains, W. L. Trock (January, 1963).

Adjustment Alternatives in South Central Minnesota Farming, H. R. Jensen and C. O. Nohre; Cost Economies to Size and Resource Use in Red River Valley Farming, Lloyd C. Rixe and Harald R. Jensen (March, 1963).

Optimum Patterns of Production and Distribution of Livestock and Poultry Products, Thor A. Hertsgaard (May, 1964).

The agriculture research findings were summarized in Chapter 4 of the final report, which was entitled, "National Growth and Economic Change in the Upper Midwest."

After the research phase was completed, and a basic body of data accumulated, an action program was launched. This program currently getting under way is headed by special departmental committees of the board of directors; the agriculture section is under the guidance of Dean McNeal, Executive Vice President of Pillsbury, and supported by the agricultural specialist of the staff, Gene Crewdson. In the main, this statement draws upon the above sources. Copies of the agricultural policy statements are attached.

Because of the importance of agriculture to the economy of this Federal Reserve District, the Federal Reserve Bank of Minneapolis has a continuing agricultural research program which is also reflected herein. Perhaps a general disclaimer for both organizations would be appropriate.

Most of the areas of concern with agricultural policy are generally known, and have been dealt with by other witnesses. There are a few which we regard as being either of particular importance, and therefore worthy of reiteration, or of a more specialized nature, and therefore more likely not to have been covered. It seems to me these fall into three categories. The first has to do with the agricultural apartheid in the political and financial communities. The compartmentalization of agriculture as something distinct from American business generally has been an error. Techniques which have developed in banking, credit and business analysis have been sparingly applied to agriculture. An example among these has been application

of computer analysis to financial reporting and cost accounting of agricultural operations. Record keeping as a management tool is a necessity for all American business, large and small, whether agricultural or industrial. There has been limited use of service centers or central computer facilities by agriculture; and yet, where these programs have been undertaken, they have been well received by farmers, regardless of the size of their operations. Such programs have been made available through a few of the universities of the district and the Federal Intermediate Credit Bank of St. Paul; and while it may be early to evaluate them, certainly they will afford the basis for far better farm business analysis than has been possible in the past. The expansion of this type of service is important. Other intermediate credit banks should be encouraged to provide this service where computer facilities on premises are available; commercial service centers are possibilities, as are the facilities of commercial banks and other universities. The development of uniform programs would be a distinct service, so that statistical norms could be developed.

The current period of credit stringency has exposed weaknesses in the commercial banking system and its application to agriculture. Rigid compartmenting of credit according to long, intermediate, and short-term credit does not serve the needs of modern agriculture. The average farming operation often is a hodgepodge of unrelated and uncoordinated public and private financing. The credit needs of a farming operation should be regarded as a total rather than separate elements supplied by unrelated segments of the financial community. As farming operations grow, so do the numbers of decisions facing each farm operator; what is needed is an arrangement permitting the farm operator to delegate to a single source his financial management function.

With the growth in size of agricultural units, the credit needs have increased in almost geometric proportions. Unfortunately, these needs are often greater than can be met by a single local bank. Even more serious in our present banking structure is the violence that is done to an insurance concept of lending with the concentration of major risks in a single geographic and economic area. A device of regional pooling of agricultural credit risks within the conventional banking system is important, and will become a necessity as the years go by. An encouraging note has been the formation of Northwest Agricultural Credit Company by Northwest Bancorporation to serve as a participation medium for Banco affiliates. But continued education of the importance of credit and risk distribution among country banks must be stressed by interested agencies. Key to this process will be the development of agricultural credit staffs in the larger banks, whose services will be available as part of the regular correspondent relationship, so that the total credit needs of the farm customer can be adequately served within the context of the credit needs of the area.

Budget assistance, analysis, marketing advice are just a few of the areas of knowledge in which the modern agricultural credit man must have reasonable proficiency. Many of the patterns of the Farm Credit Administration could be borrowed quite usefully by the commercial banking system in this regard. Agricultural credit conferences, specialized programs within the banking associations, designed to acquaint the country banker with the changing pattern of agricultural credit, are essential parts of this program. Almost by default, the Farm Credit system is continuing to enlarge its participation in agricultural credit at the expense of commercial banking. While competition among the units of agricultural financing is desirable and should be encouraged, there is still room for professional dialog to everyone's advantage.

The future will find the debt on larger farm units being passed from generation to generation as farms continue to increase in size and the requirements for additional capital expand. But this is not new to business generally; what must be established is the methodology for agricultural application. Reliance on borrowed money will continue to grow in importance during this period when agriculture is breaking out in all directions. Yet it is essential that a proper balance of equity capital be preserved, if the farmer is to avoid being caught between debt service pressures on the one hand, and market fluctuations on the other. This requires a further trend toward the corporate farm.

It is peculiar to agricultural financing, and this again is perhaps a byproduct of the small size of many of the units, that the operation is usually associated with a single individual, and expressed in personal terms rather than those of the total operation or a particular enterprise. The ability to repay should be the basis for financing, rather than the personal expression of the operator. This, of course, requires efficiency in production plus higher levels of professional farm management. Growth in size of agricultural units should be encouraged, rather than discouraged. Essential to this process of expansion is a system of financing that will meet not only the capital costs of acquisition, but operating budgets.

Farm expansion is not synonymous with increased acreage, for greater productivity is the objective. More intensive use of existing acreage is often the key to increased yields, frequently requiring an increase in the use of purchased inputs. Important to intensive use is recognition that the farmer is no longer a self-sustaining economic unit, but, like other businesses, is dependent to a great extent on production assists from off-farm sources.

This leads to the second main division of this statement, which relates to federal farm policy, per se. Continued relaxation of controls, the shift from quantity to quality as measures of crop support, a pattern of predictability in administration of reserve stocks, are subjects which have been covered elsewhere. I would like to emphasize, though, that agricultural policy does not stand alone as an isolated phenomenon of our federal government. An example is the stake agriculture has in the establishment of a transportation department on a cabinet level. Freight rates are determinative in many cases of the direction of grain movements. Historically, our entire marketing structure has been directed towards eastern markets. The shift towards west coast sites and markets produces a spectrum of problems and an economic impact that cannot be wished away. This reorientation of our market outlets is of profound importance to the Upper Midwest. The export rate adjustment made a year ago to let the spring wheat producing area from the Red River Valley to the Rocky Mountains compete in Japan with milling wheats produced in Canada and shipped through Vancouver was an imaginative effort to produce an alternative direction. Again, though, it must always be remembered that attempts to reorient production and marketing of agricultural products must be considered within the context of the present structures to minimize the impact of such shifts on domestic markets and the interior processors.

International trade is increasingly important to our grain producers, and a substantial part of this trade will be in the Orient and Latin America. Domestic freight rate structure and the requirement that at least fifty per cent of ocean shipments be in U. S. bottoms require reexamination, if we are to compete with other countries for international grain trade. In a period when balance of payments considerations are of major importance in United States

monetary policy, it is important to reexamine any impediments to the development of this trade.

Foreign exchange is important to this country, not only in terms of our national defense, but as part of our offensive position vis-a-vis the Communist world. Foreign exchange originating from Communist bloc purchases restricts the ability of those countries to compete in the world for goods and services exactly in the degree it strengthens ours upon its receipt by us.

Finally, and equally as important, there is the category of the sociology of agriculture. Emphasis on the small family farm has emotional appeal, but little else. Such emphasis many times tends to perpetuate misery and underemployment. Steps must be taken to encourage the increase in size of agricultural units, with the attendant economies to be derived. If our goal in agriculture is the development of economically viable farm units, then we must accept the fact that the attrition in farm numbers will continue. This must occur, unless we are willing to pay the price in the form of continued subsidization of marginal units.

To offset the impact of the changing economic environment in farming, the establishment of vocational schools should be encouraged to retrain underemployed farmers for industrial employment. The establishment of decentralized industries, and encouragement of local business, are further alternatives that must be utilized to the greatest extent, for such enterprises make it possible to sop up the underemployment on the small farm units, give them a cash income, and still permit them to retain the small, non-commercial farm.

This means that agriculture has a stake in improving the total

environment of the agricultural community, including as it does many small towns which have become marginal as the number of agricultural units have been reduced. Programs of urban renewal and community assistance are at least as important in such a context to the man directly engaged in agriculture as they are to the resident of the small town. Not only is he dependent upon the town for social services, such as primary and secondary schools, medical services, and shopping, but it serves as a cultural focal point. There are practical limits imposed upon commuting for these services.

For those who wish to remain in agriculture, education of a continuing nature is essential. Support on all levels of existing agencies and institutions in this field is of primary importance.

In summary, we urge --

1) An approach to American agriculture as just another sector of American industry -- in short, thinking about it as a business -- which inevitably will lead to application of modern business operating techniques to agriculture, such as specific encouragement to the expansion of computer services and the development of financing patterns which will be full service, one-stop services.

2) Removal of artificial restraints on the ability of American agriculture to compete in world markets. This means continued progress in the removal of controls; stabilized and predictable official attitudes in the administration of reserve stocks, and the confining of the movement of such stocks to normal market channels; administration of domestic freight rates with international as well as national competitive patterns in mind; removal of the restrictions on international shipments.

3) View the transitional problems of agricultural communities as an essential part of the attack on U. S. urban problems.

A D D E N D U M

September 16, 1966

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Because of the breadth of the subject matter, it was not possible to develop fully the several points raised in the formal statement, which was designed primarily to outline our areas of concern. In the oral testimony, the following points were amplified:

Page 3:

In addition to the activities of the Intermediate Credit Bank of Saint Paul, one of the major holding companies has started on an experimental basis computer services to agricultural customers, which deserved further emphasis because the inference was that in the banking field only the Intermediate Credit Bank of Saint Paul was currently involved.

At the bottom of the page, reference was made to delegation to a single source of the "financial management function". I was so obsessed at this point with the importance of developing the single-stop concept for agricultural financing, that I used an unfortunate phrasing. Our concern is with a reference to a single source of the financial management advisory function. Certainly no entrepreneur, including the farm operator, should ever be encouraged to delegate the decision-making responsibility.

Page 4:

Commercial banking could very usefully adapt many of the operating

patterns of the Farm Credit System. The development of a financial structure in the private sector, which could offer the full range of credit needs to agriculture, would be desirable, especially if accompanied with an adequate mechanism for the obtaining of funds through the issuance of money market instruments similar to the FICB. While it is true that the private sector can discount agricultural paper with the FICB, this may turn out to be an illusory escape valve when the purchase of the FICBs by the PCAs has been completed, simply because of the conflict of interest. It might be an idea to think about broadening the ownership base of the FICBs to meet this problem.

Page 5:

The reference to the corporate farm is prompted because in our society this is the most useful form of organization for outside equity financing. I have no idea how equity financing of agriculture will proceed, but attention must be paid to this if the debt structure of commercial agriculture is to be kept within reasonable bounds.

Page 8:

The importance of separating the problems of commercial agriculture from the areas of sociology, such as poverty in agriculture, has a similar parallel in separation of the financing activities of the federal farm program from the international or commodity control goals. Typical of this is the arbitrage that is inherent in the CCC loan, with the farmer able to borrow at an effective rate of 3.6% when the general level of money rates is substantially higher. For example, he can borrow against his crop at 3.6% and buy Treasury bills in excess of 5%, which is certainly an extraordinary arbitrage advantage, and one unintended in the original act.

Assuring the farmer of a supply of credit to keep grain off the markets and in storage on the farm, as stated in the act, is certainly desirable, but this should be separated from the cost of the money. The latter should certainly bear a closer correspondence to market levels.