Research Department
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Watershed

The 1970's mark a watershed in the history of the nation's farm economy, says the Council of Economic Advisers in its recent annual report. The outlines of this major turning point may be hard to discern amid the welter of conflicting headlines, with real income per farm cut almost in half since late 1973, and in contrast, with the price of farm products to the consumer rising almost by half in a slightly longer time-span. Yet behind the headline stories are some crucial new developments—a decline in the farm sector's excess capacity and a significant widening of price fluctuations, all at a time of worsening supply conditions and heavy demand for American products in the world farm economy.

The decline in excess agricultural capacity reflects a slowdown in the growth of farm productivity, as well as a gradual disappearance of traditional surpluses of land and labor. For decades, rising productivity had been the hallmark of American agriculture, despite a relatively stable stock of measurable inputs. But related to this was a sharp change in the proportions in which these physical resources were used. The stock of land remained relatively stable, while the amount of fertilizer applied to that land expanded tremendously; the amount of labor dropped sharply and steadily, while the amount of machinery utilized by the remaining workers rose sharply.

These shifts brought about an 18-percent rise in total factor productivity in the 1940's and a 27-percent increase in the 1950's, but only an 11-percent further rise in the 1960's. Perhaps some deceleration in productivity should have been expected over time. Nonetheless, this deceleration has important implications for the future, since continued increases in productivity had long enabled the U.S. to supply cheap food to both domestic and overseas markets, and at the same time, to provide a constant supply of labor to the nonfarm sector of the U.S. economy.

Less land and labor

The massive migration of farm workers to city jobs may now be coming to an end, partly because of the deceleration in productivity, of course, but also because there simply aren't that many people left on the farm. Farm population has dropped from a peak of 32 million in the 1930's to only 9 million today. The annual rate of decline slowed to 1.2 percent in the first half of the 1970's from 4.6 percent in the 1960's; put differently, average net outmigration of 110,000 annually in the 1970-74 period equalled less than one-fifth of the annual outflow of the preceding decade.

With the farm-labor market approaching equilibrium, the perennial problem of low farm income could decline in importance. Reflecting this factor, the median income of farm families (in real

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terms) jumped 30 percent between 1970 and 1973, compared with a 6-percent rise for nonfarm families. The nonfarm-farm income spread narrowed from $3,700 to $2,100 over this period. The spread has probably widened again in the past year, because of the disproportionately heavy impact of the world recession of the agricultural sector, but over the long run, the disappearance of the labor surplus should ease the downward pressures on farm income.

Similarly, excess farm acreage seems to be a thing of the past. Indeed, many observers wonder what ever happened to the one-sixth of the nation's cropland that reportedly had been kept out of production by government programs. Although 60 million acres were released from acreage controls in the 1972-74 period, only 37 million acres were added to the nation's cultivated area in those years. The answer, according to the Council of Economic Advisers, is that a substantial investment is required to bring new acreage under the plow, and prices simply were not high enough to justify that investment. The uncultivated land generally was marginal acreage, so that its contribution to the expansion of output would be smaller than that of the land now in use.

More foreign demand

A substantial increase in world demand for U.S. products meanwhile occurred, at a time when the supply situation was being affected by the disappearance of excess land and labor. As a result, there was an unprecedented export boom in the early 1970's, measured by a 39-percent boost in export volume between 1969-71 and 1972-74. One factor was the rising European and Japanese demand for feed grains and soybeans, as a result of the upsurge in meat consumption brought about by their increasingly prosperous economies. Another factor was the disastrous slump in world grain production in 1972, which shifted world demand to the shoulders of the largest supplier—the U.S.

The crucial factors, however, were the sharp increase in demand for U.S. goods generated by the worldwide business boom, and the increased competitiveness of U.S. products attributable to the two devaluations of the dollar. Between May 1971 and the end of 1974, the dollar fell 13 percent relative to other currencies, weighted by their trade in U.S. farm commodities.

In the now-vanished days of an overvalued dollar, farm exports remained relatively low, as did also farm prices in domestic markets, despite all the legislative efforts to remedy this situation through farm price supports and export subsidies. In the Council's words, "During this period the United States sacrificed from a trade standpoint part of the comparative advantage that U.S. technological superiority in agriculture would have given it in world markets." The overvalued dollar also contributed to the relatively low returns received by agricultural resources, since it intensified the need for resource adjustment caused by the rapid rise of farm productivity.

Today, in the new post-devaluation world, the owners of agricultural resources should receive a larger share of the benefits arising from technical change in the nation's farm sector. Foreign consumers also should benefit from this shift, but American consumers could be worse off. The U.S. undoubtedly will continue to export a larger proportion of its farm output, while the price of food to U.S. consumers should be heavily influenced by foreign supply-demand conditions.

More instability

Production trends, along with financial trends, underline the increasing interdependence of the world's food markets. Despite rising per capita food production throughout the world economy—at least prior to 1972—the world has come to rely more and more heavily on American supplies. A generation ago, Asia, the Mid-East and North Africa were net exporters of grain, but these and other regions today are all net importers, and as a result, the U.S. now handles over half of the world's grain-export trade.

As a consequence of all the factors mentioned here, the U.S. has entered a period of greater price instability, much different from the long 1950-71 period of relatively stable markets. Without the cushions formerly provided by large reserves of fallow land and large stocks of surplus farm products, there is no way to dampen the year-to-year fluctuations in agricultural prices. The situation has been aggravated by the increasing dependence of U.S. producers on shifting world markets. The European Community and Japan, with their protectionist farm policies, have shifted the burden of adjustment to changing supply-and-demand conditions to the U.S. and other exporters. The U.S.S.R., with its inefficient and unstable farm sector, also has shifted its adjustment problem elsewhere; indeed, the U.S.S.R. has been responsible for about 80 percent of the fluctuations of the world wheat trade since 1960.

We may not again experience the wide swings in farm prices which characterized the period before World War II, largely because of the milder business-cycle conditions of the postwar period. Still, we must expect occasional price fluctuations of the 1972-74 variety. Some observers even believe that the American consumer could experience a ratcheting upward trend in food prices.

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BANKING DATA—TWELFTH FEDERAL RESERVE DISTRICT
(Dollar amounts in millions)

Selected Assets and Liabilities Large Commercial Banks	Amount Outstanding 2/12/75	Change from 2/5/75	Change from year ago Dollar	Change from year ago Percent
Loans (gross, adjusted) and investments*	84,071	− 767	+5,484	+ 6.98
Loans (gross, adjusted)—total	65,803	− 507	+5,926	+ 9.90
Security loans	1,203	− 147	− 8	− 0.66
Commercial and industrial	23,757	− 147	+2,717	+ 12.91
Real estate	19,910	− 34	+1,353	+ 7.29
Consumer instalment	9,873	− 6	+ 726	+ 7.94
U.S. Treasury securities	5,510	− 113	− 526	− 8.71
Other securities	12,758	− 147	+ 84	+ 0.66
Deposits (less cash items)—total*	83,127	+ 66	+7,991	+ 10.64
Demand deposits (adjusted)	22,287	+ 161	+ 460	+ 2.11
U.S. Government deposits	382	− 114	− 400	− 51.15
Time deposits—total*	59,225	+ 428	+7,897	+ 15.39
States and political subdivisions	7,093	+ 81	+ 162	+ 2.34
Savings deposits	18,474	+ 81	+ 768	+ 4.34
Other time deposits‡	30,404	+ 230	+6,387	+ 26.59
Large negotiable CD's	16,892	+ 239	+5,496	+ 48.23

Weekly Averages of Daily Figures	Week ended 2/12/75	Week ended 2/5/75	Comparable year-ago period
Member Bank Reserve Position			
Excess Reserves	37	80r	31
Borrowings	6	2	201
Net free (+) / Net borrowed (−)	+ 31	+ 78r	− 170
Federal Funds—Seven Large Banks			
Interbank Federal fund transactions Net purchases (+) / Net sales (−)	+1,344	+1,525	+ 913
Transactions of U.S. security dealers Net loans (+) / Net borrowings (−)	+1,104	+ 558	+ 182

*Includes items not shown separately. ‡Individuals, partnerships and corporations.

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