

AVOIDING THE FINANCIAL PITFALLS OF THE DEFENSE ERA

Address

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In looking through some files the other day I came across copies of the resolutions adopted by representatives of the farm organizations of the South and the West at the first inter-sectional meeting held to plan joint action to develop a favorable national policy for agriculture. That meeting was held in St. Louis on November 16 and 17, 1926. Two farm leaders of this state, William Hirth of the Missouri Farmers' Association and Zenophon Caverno, then trustee of the American Cotton Cooperative Association, and a veteran Farm Bureau leader, conceived the Convention and had much to do with its success.

We thought the agricultural situation that year was serious. The farm price of cotton had just dropped from a national average of 16.8 cents a pound in September to 11 cents. But no one in that meeting, I dare say no one in the Country, foresaw what was ahead of the farmers and the other economic groups of the land in the dark days that followed 1929. We didn't know that cotton was due to break through a five-cent average farm price in less than 6 years; or that wheat would be hitting a low that was close to thirty cents.

Part of these fluctuations so disastrous for farmers were due to changes in the supply situation of agriculture itself. Part were due to world-wide and national developments with which the farmers were as helpless to cope as the toad under the farmer's harrow. Mainly they grew out of the changed international situation that followed the world war of 25 years ago.

The world, which never stabilized itself after the last war, is again seething in conflict and revolution that covers or directly affects every part of the earth. It has been suggested that I talk here today about avoiding the financial pitfalls of the Defense era. I suspect the word "financial" was put in there because of

my present connection with the Federal Reserve System. Since ours is a money economy, every economic question, therefore, is a financial one, and I shall make no especial effort to confine my remarks to a line that is purely financial.

Nor shall I attempt to limit myself to problems that arise only during the years when our national effort is concentrated on the production of armament, years which constitute the Defense era. The seeds of the aftermath are carried in every present-day problem or trend. It is not possible to consider one event or one era as separate and distinct from those that precede it and those that will follow. An unbroken chain of causes and effects reaches back to the dawn of man's history on earth and stretches endlessly down into the future.

Today every man's business in the United States, we might say with nearly full truth in the whole world, is being influenced and shaped by war. The whole economic scene, in the factory, the store, the bank or on the farm, is being distorted by the convulsions of a world at war. Let us keep that clear in our minds. If we ever get to thinking that the conditions under which business is booming today are permanent realities we are in for a lot of trouble which we can escape or minimize if we will continue to see them for what they are.

The prices, the market and the income of American farmers have all been improved by developments growing out of the war. We may accept this even though we don't like the idea that it had to be the destructive course of war that enlarged domestic consumption and restored the flow of exports. But these temporary gains will melt away and leave heavy losses in their wake unless their causes are clearly seen and comprehended.

Not so long ago, I had serious doubts about how our farmers would fare during these days of international anarchy. In contrast to what happened during

the last war, we lost one outlet after another for our agricultural products as the Nazi war machine rolled over the various countries of Europe. In the early stages even England had to use her available dollar exchange to buy planes and tanks, guns and bombs and powder in this country. But I didn't foresee the scope of our own war expenditures, nor the Lend-Lease bills.

As a result of agricultural loans, of greatly increased domestic purchasing power and of the Lend-Lease program, farm prices and income have moved upward substantially. For the year 1941, it is estimated that farm cash income, including Government payments, will be \$10.7 billions. This compares with \$9.1 billions in 1940, and is the largest since 1929; it has been exceeded in only eight of the past thirty-two years. It was recently estimated by the Department of Agriculture that farm income for 1942 might be in the neighborhood of \$13.0 billions.

Not only has cash farm income increased greatly, but the net cash available to farmers after their farm expenditures has likewise grown. Farming expenses have risen, but not as much as farm income. While no precise figures are available, net income after operating costs will probably reach close to \$4.5 billions this year, which would be the highest return that farmers have enjoyed during the past three decades, with the exception of the period from 1917 to 1920 inclusive. This sum represents the purchasing power that agriculture has to spend on items not directly connected with farm operations; that is, on such goods as clothing, food, automobiles and luxury items. The actual farm market is broader than this because farmers purchase a substantial amount of the products of industry for their farm operations, and because wages which they pay provide purchasing power to agricultural laborers.

The Department of agriculture tells us that we are going to need for export in 1942, three times as much pork and eggs, twice as much dairy products and canned fruits, and half again as much lard and dried fruits as we exported in 1941. These are unexpected demands that came on top of the greatly expanded home market resulting from swiftly rising payrolls and increased national income. But it will pay us to keep in mind that when we compare exports with 1941 we are talking about a pretty low year. Exports of farm products from the United States last winter hit the lowest point in 74 years.

I cannot see anything permanent in this export flow. We have been kidding ourselves about the foreign market ever since the last war. During the 'twenties we kept shipping farm crops in export only because with every cargo that left our shores we, in effect, sent along our own certified checks to pay ourselves. During most of the 'thirties we exported because we were buying up over 80 per cent of the world's monetary stock of gold. Some day we may use our agricultural surpluses to help rehabilitate a war-torn world, but still don't let us delude ourselves - there's only one party who can pay for them, and he lives on this side of the Atlantic.

The exports we had this year and will have in 1942 were important price factors not because of their size but because they came on top of rising consumer demand at home. Now let us see what caused that.

Shortly before Germany struck at the Low Countries in May of 1940 the total of appropriated commitments for new armament in the United States amounted to about two and a half billion dollars. Since then we have been trying to catch up with and actually comprehend a dizzily rising goal in arms production. Counting in the second Lend-Lease bill now pending and England's total orders actually placed here, that two and a half billion of 17 months ago has grown

to 66 billions.

Only a little more than 13 billions of that sum have actually been spent, and yet the effect of it is visible in every state and county and town. The present rate of spending is about 1.4 billions a month, and it is rising rapidly and will continue to grow for a long time.

Last month as the European war entered its third year the level of industrial activity in the United States was 60 per cent over that of 1939 when the war began. National income was at an annual rate of about 90 billion dollars, an increase of 25 per cent in the last two years. Purchases by consumers, shown by volume of retail trade, have reached an all-time peak. Commodity prices have risen sharply since February - the general wholesale index by 14 per cent, farm products by 30 per cent. Factory wage rates and number of employed have been pushing upward. By the middle of 1942 seven million men will be at work here who were idle when the war began.

There are other important and inflationary signs on the horizon. Bank deposits plus money in circulation have risen to nearly 75 billion dollars, almost 20 billions above the total for 1929. Money in circulation has passed 10 billions, double the 1929 mark. Bank loans have gone up three billion dollars in the last year.

Up to now, there has been a general expansion of our national defense program without substantial interference with production for civilian use.

In fact, non-defense production pushed on to new highs in many lines during the present year to date. This was possible because we have been able to draw upon the unemployed and upon unutilized plant capacity. This stage of the defense program has already come to a close in many fields as capacity operations have been reached, skilled labor absorbed, and available materials

contracted for. From now on, and at an accelerated pace, we can increase defense production in many lines only at the expense of civilian production.

The position of agriculture in the post-defense period will depend in part on how successfully we can make the transition back to normal peacetime activities from a condition in which a high percentage of our industry is engaged in armament production. If we cannot find employment for workers in peacetime industry and, thus provide purchasing power for the domestic market, the difficulties of agriculture as well as the rest of the country will be great.

I can see right now that unless I pick out a field with fences around it I won't get through by dark. I have in mind such matters as the course farmers should follow to soften the curse that may follow the changed demand conditions I have described; farm price controls and the principle of agricultural parity; the relationship between food costs and industrial labor wages; and perhaps a final word addressed to you not as farmers but as citizens of the United States and the world.

Farmers can begin now to build up defenses against post-war adjustments if they follow a sane and conservative course.

Increased farm income should be used to pay off debt, rather than as a basis for expansion of debt. Farmers who are out of debt should use profits to build up savings. It would be a fine thing if every farm family that can possibly set the money aside ~~would~~ build up a hoard of Defense Savings Bonds.

Most of us still feel the influence of previous generations which believed the course of land prices must always be upward. We have always been apt to chase land prices through the roof whenever farm earnings rose. I am afraid

the lesson of the last war may be forgotten, when land prices more than doubled to an all-time high, then collapsed to less than half that peak. This was one of the root causes of the farm troubles of the 'twenties.

The educational leaders in the Land Grant Colleges can be a powerful force in helping guide us past this particular pitfall. We aren't in any trouble yet in this state because of land prices; such firming tendencies as have been felt were justified. Lending agencies also have a real responsibility. The Federal Land Banks and the Farm Credit Administration have mapped out and announced a statesmanlike course that should help set the brakes if farm land inflation gets underway. Farmers who have Land Bank mortgages can anticipate future payments now if they are lucky enough to come through the year with a surplus. They can deposit with the Land Bank any amount they are able to spare, and draw a rate of interest on the advance deposit that is equal to the rate charged on the mortgage. This is one way of insuring against future trouble if and when farm prices are less favorable than they promise to be in the years immediately ahead.

Then I would urge farmers to be conservative in demanding political action for ever higher and higher price supports. They should be in court with clean hands when they ask for controls in the other and more dangerous inflationary fields of industrial prices and wages. Right here I want to pay a tribute where I believe one is deserved and overdue. Every thinking person, regardless of his business, recognizes that permanent, stable agricultural prosperity is essential to economic health. The path of the past has had too many peaks and valleys in it. State and national farm leaders have fought hard and well toward the goal of stabilizing the business of farming in relation to other business.



But right now they are up against a situation that calls for a high degree of restraint and even higher courage from farm leadership. I want to congratulate those leaders who are counseling their members to stand fast on the present program of 85 per cent loans on basic commodities, and at the same time are insisting that price ceilings on farm products, if they are set, be at 110 per cent of the parity price.

I believe there is wide misunderstanding of the relationship between farm prices and other prices and wages. I do not think that an agricultural policy intelligently based and carried out on the principle of parity with agricultural costs can produce a serious inflation in this country. We should remember that agricultural prices at pre-war levels were relatively depressed; in fact, had been depressed for more than a decade. In carrying out a policy which aims at parity prices, a certain flexibility must be permitted. If a floor is set under agricultural prices by loans at 85 per cent of parity, and if price ceilings are placed at 110 per cent of parity as has been proposed for basic agricultural products, the average returns to farmers would probably be fair and reasonable in relation to parity. Certainly there are no seeds of dangerous price inflation in such a formula.

Moreover, such approximate parity prices on agricultural products would not in my opinion cause a sufficient rise in cost of living to justify further wage increases. Labor income has already increased as a result of higher wages and full time work so that the average factory worker has more left over after buying his standard food requirements than ever before in our history. I have said many times that neither industrial management nor organized labor should be allowed to take advantage of this national crisis to increase its relative advantage. The conditions that call for price controls call for wage controls,

and both should be applied with judgment, common sense and courage.

Consumer sensitiveness is especially acute on the question of food prices - and consumer memories particularly short. I sometimes felt, when I was on the National Defense Advisory Commission, that there was no room in the consciousness of the consumer section for rents and other non-food elements in the cost of living, they were so preoccupied with quotations on food. Maybe I was a little sensitive on that point myself. It is not only unjust but it is impracticable to attempt to freeze a price relationship which was so far out of line to the disadvantage of the farmer.

That was why I was interested to note an article on Food Prices and Factory Wages written by Dr. Bean for the August issue of *The Agricultural Situation*, published by the Department of Agriculture. I commend it to you. He points out that factory wage earnings per worker were about 5 per cent higher for the first half of 1941 than in 1929 - while food prices averaged about 21 per cent below the 1929 level. With wages up and food costs down, the food purchasing power of factory payrolls per employed worker was about one-third greater the first half of this year than in 1929.

During the first half of this year, also, the average employed factory worker was able to buy 35 per cent more in the form of goods and services other than food, than did the employed worker in 1929.

Looked at from another angle, the factory worker's food costs in 1929 averaged 32 per cent of his wages; in the first 6 months of 1941, only 24 per cent.

Still using 1929 for a base, food prices the first half of this year averaged 79 per cent of their 1929 level. Non-food items averaged 87 per cent.

The article from which I drew these figures was written in July. Since the first half of this year there has been a considerable rise in the retail price of foods. In September the factory worker's food costs were probably about 87 per cent of their 1929 level, or about 10 per cent higher than the average during the first half of this year. Non-foods costs also increased but by a smaller amount. These items in September of this year were about 92 per cent of what they were in 1929. Thus the disparity between food and non-food living costs has been decreased in recent months.

It should also be remembered that the average earnings of wage earners has increased since the first half of this year. At the present time the average worker in industry receives about 75 cents per hour and is probably working about 41 hours a week on the average. On the basis of 50 weeks a year this would give the worker an income of \$1,538 a year. This would be 18 per cent more than the average worker received in 1929 and about 12 per cent more than the earnings rate during the first half of this year.

Thus with the per capita incomes of most wage-earning people substantially higher than in 1929 and with food prices still about 13 per cent below those of 1929 and about  $5\frac{1}{2}$  per cent below non-food items, there would seem to be room for some further, but selective, rise in food prices. The real problem is how to close this disparity without running the danger of an increase beyond the point that would represent price inflation.

It is not easy to know where that line is. On the other hand, it is too easy for a group to go out to "get theirs while the getting is good". The factors which caused the recent sharp advances in agricultural prices will probably continue to provide the basis for adequate farm returns for the

duration of the emergency. However, should the inflationary factors that I mentioned earlier gain further headway, and should the nation fail to adopt a carefully co-ordinated program of control, we might have runaway price advances that would eventually result in great suffering to farmers as well as other important groups of our economy.

The record of what happened at the time of the previous World War boom stands for all to see. Then farmers were able to increase their incomes more rapidly than their expenses and their cost of living. The prosperity which they enjoyed proved to be false, and was quickly dissipated after the break in prices in 1920. The fact that agricultural prices rose more than farm costs presented one real danger. It kept farmers and farm leaders asleep and kept them from fighting their way off from the disaster which general inflation was creating for them .

I hope a repetition of that situation can be avoided. Whether it can or not depends upon the courage and understanding of farmers and responsible farm leaders. For years, agriculture has stood for the principle of parity prices. Already, we hear protests against any price ceilings for farm products. We hear opinions expressed that wheat should go to \$2.00 a bushel, cotton to 35 cents a pound, rice to \$1.50 a bushel and so on. Farmers cannot hope to keep even in that kind of a game. Neither can they afford to be led by a sense of false security into basing their long-time plans for the future on the shifting sands of war demand.

These have all been questions tied in with the actual business of farming. In common with all other elements, the men and women on the farm have a real interest and concern in our general national and international policies. They are as capable of seeing events in proper focus as any group in the land - I think in fact they have a clearer insight than most.

So now in ~~Conclusion~~, I want to leave this specialized field and talk to you as citizens of the United States and the world. This nation has again taken sides in a world-wide war. I can no more answer questions as to how far our participation will go than you can. Forces wholly outside the United States may make or modify the answers anyone can give today.

There are differences as well as many similarities in the world situation today compared with that 24 years ago. For one thing, the nature of war has changed. Modern war is incredible in its speed, range, destructivity, malignancy and totality. It is important to dwell on that last word. We in the United States haven't yet grasped its meaning. Total war as the dictators practice it subordinates every interest and consideration to the one end of complete victory over present and potential enemies of their regime. That is the compact and deadly purpose against which we aligned ourselves when we assumed the role of arsenal for the forces that resist the Axis. Yet even now, 17 months after we started to mobilize our resources for defense, sacrifices are still in the conversational stage. As individuals and as groups we want our privileges and immunities untouched. We have accepted a grim challenge but as a nation we haven't yet geared to meet it.

The years ahead of us will test our individual and national fiber as it has never been tried before. It is a mistake to over-simplify the job. Helping to defeat one dictator, or set of dictators, won't end it. We left unfinished, perhaps even uncharted, the job of domestic recovery and rehabilitation to undertake vast responsibilities in a world-wide war. It would be supreme folly to engage in that war only once again to turn our backs on the peace. If the sacrifices we make are to mean anything they must have a purpose; and that purpose, to have meaning, must seek to avert from the next generation the horror that threatens to engulf this one.

These are real issues; more real, perhaps, than some of your immediate concerns which I have attempted to discuss. The outlook is dark if we cannot hope to meet them better in the future than we have met them in the past. This is a time for understanding, not discouragement; for cooperation, not disunity, and for the kind of optimistic courage that is bred out in the country.