ESO 149

BOOMING 1973:

GENERAL ECONOMIC AND

AGRICULTURAL OUTLOOK

by
WALLACE BARR

GENERAL ECONOMIC AND AGRICULTURAL OUTLOOK

The gross national product (GNP) or the value of the nation's total output of goods and services grew at an extremely fast pace in the first quarter of 1973. On an annual basis the GNP increased by 14.3 percent to $1.235 trillion in the January-March period. Most observers feel that GNP will be strong throughout 1973 but that this rate of growth cannot be sustained much beyond early 1974. Some feel that we could go from a boom year in 1973 to a bust in 1974. I do not agree to the bust in 1974.

The 14.3 percent gain in the first quarter of 1973 was the sharpest quarterly gain since the 14.7 percent advance registered in early 1951 during the Korean War inflationary period. Much of the gain was due to inflation. Stripping away the effects of inflation the "real" or physical output was up nearly 8 percent. Mr. Stein of the President's Council of Economic Advisors admits "this rate of real output probably cannot go on rising at an annual rate of 8 percent; there isn't enough labor nor capacity to sustain this rate very long."

Today we face two serious problems--an overheated economy and related inflation. Today's inflation reflects both the main types of price pressure--the demand-pull pressure that forces prices higher in response to a spurt in demand (witness food prices) and the cost-push pressure that forces prices higher in response to rapidly rising expenses whether they be wages, fuel or soybean meal. Cost-push inflation can continue even though the economy cools off.

Presented by Wallace Barr, Agricultural Economist, Ohio State University, at the Wisconsin Bankers Association Agricultural Credit Conference, Holiday Inn No. 2, Madison, Wisconsin, May 2, 1973.

The only lasting solutions to the problems appear to lie in the painful and steadfast application of fiscal and monetary restraint. If the restraint is applied wisely a recession may be avoided.

There are bright spots. One is the fact there is no election this year. The Federal Reserve Board has been moving toward a more moderate monetary policy. The federal budget, though still deeply in deficit, is moving in the direction of balance. Higher than expected tax collections help. Both fiscal and monetary restraint are slow in getting results. The effects on various factors vary widely and take from a few months to 18 months to be effective.

Many believe that administration policy makers will have to consider new steps to "cool the economy." Most frequently suggested are taxes that constrain economic activity or rigid wage-price-interest-rent controls. The recent discussion in Congress about price rollbacks and subsequent agreement to extend the current legislation on economic stabilization indicates rollbacks were politically unacceptable.

Major tax policy suggestions and speculation centers around 1) a 10 to 15 percent surcharge on personal and/or corporate income, and 2) lowering or removing the 7 percent investment credit provision. Whether Congress will act quickly enough to dampen demand yet this year is open to serious question. The dilemma does point up the possible need for some fiscal body with authority to adjust tax policies upward or downward quickly within some limits.

Another possibility--though a long shot and not likely to occur until labor contract settlements--is a wage-price freeze announcement similar to the August, 1971 action.

Personal incomes reached a seasonally adjusted annual rate of $1.0 trillion in the first quarter. This record came about through more people working at higher average wage rates. Unemployment is declining but is higher than desired by many. Increasing employment comes from not only the normal entrants into the labor force but also from a reduction in the armed forces now being absorbed into the job market.

In addition to more jobs at higher wages, much higher consumer spending was encouraged by increased social security payments, higher than normal income tax refunds, heavy use of credit and lower savings rates. Consumer spending in the first quarter of 1973 was up 16 percent. Consumer durable goods purchases have been strong as inflation psychology permeated consumer buying. However, family budget commitments means consumer demand may subside somewhat before the end of 1973. This will be partially offset by labor negotiations that call for substantial wage increases.

Business investment increased $6.2 billion in the first quarter as durable production equipment, non-residential and residential construction outlays all increased. These are all expected to continue upward. Further encouragement to business investment will come from the need to replenish inventories.

Federal government expenditures for goods and services will increase slightly. The biggest increase in government expenditures will be at the state and local government level. In recent years a larger portion of the increased government expenditures have been concentrated in transfer payments to individuals; not in goods and services. This seems likely to continue.

In summary, it is expected that GNP in 1973 may average in the $1.27 or $1.28 trillion range. This is a 10 to 12 percent increase over the 1972 level of $1.15 trillion. The mix between real output and price rises is open to question. My assumption is that real output will rise 6 to 8 percent. This means a gradual slowdown in economic activity and more inflation than desirable.

The level of economic activity in 1974 will be influenced by the degree of fiscal and monetary policy actions and the speed with which they are implemented. My best guess is that there will be some action(s) that will slowdown the rate of growth in both real output and inflation in 1974.

AGRICULTURAL OUTLOOK

Prospects for the farm sector in 1973 have taken on a bright glow. Realized net farm income, according to the USDA, may reach a record $21 billion, up from the $19.2 billion in 1972. This $2 billion increase comes on top of a $3 billion increase in 1972.

Expectations are for an expansion in marketings at higher producer prices. The result is for cash receipts in 1973 from farm marketings to increase by $9 billion or be 15 percent above 1972. Increased gross cash receipts from livestock and products (includes milk plus poultry) account for over half of the expected $9 billion increase and will be based on much higher prices and a slight increase in the volume of marketings.

Gross farm receipts from crops in 1973 are expected to increase with substantial improvement in both volume and prices. Some price declines for some crops and livestock products may occur in late 1973 but nothing in our "crystal ball" signals disastrous declines. Government payments to farmers will be reduced by over $1 billion.

The optimism has developed for numerous reasons. Some of the more important factors include:

1. Consumer incomes are rising rapidly resulting in the demand for food being unbelievably strong relative to supplies.
2. Export demand for farm products continues to amaze almost everyone.
3. Dollar devaluation has meant U.S. farm and industrial products are cheaper in many countries.
4. Release of 50 million acres from the set-aside program to expand output of agricultural products, especially feed grains, wheat and soybeans.

Let's examine each of these factors that contribute to an expansion in agricultural receipts in 1973.

Expanding Domestic Demand for Food

The great strength in demand for farm products is basically from more people with more income wanting to upgrade their diets. In the U.S. we add 2½ million more customers each year.

Food prices have increased over 10 percent in the last year largely because there is just too much money chasing too little meat and other foods. Meat, poultry and fish led the way in price increases with a 20 percent increase from March of 1972 to March of 1973. People are asking, "Who did that to us?" and are wondering, "Why?"

The immediate concern of many non-farm people is how to feed ones family without increasing the strain on the family budget. Why are food costs increasing? There are lots of reasons. Some are fairly obvious; others are not.

To begin, we had bad harvest weather last fall and winter. Farmers were unable to get their heavy harvesting equipment into the fields because of the mud. Some grain, especially soybeans, were left in the fields.

Poor weather conditions were not confined to the U.S.A. Reduced harvests occurred in the U.S.S.R., India, Australia and other nations.

The sale of grain to Russia and other countries and resulting higher grain prices has had some effect on the cost of food to date. Increased costs of producing poultry have been reflected in retail prices. Higher feed grain prices encourage cattlemen to sell cattle at lower weights and decrease beef output. Strong beef and pork production encourage herd expansion that reduces slaughter.

The combined effects of corn blight in 1970, increasing feed costs and low hog prices to producers in 1971 encouraged hog producers to reduce output. The result is consumers are paying higher pork prices today.

Poor fishing has meant the cost of fish for human consumption has risen. Poor fishing conditions off the coast of Peru for anchovetas used to make fish meal for livestock feed has put added pressure on the cost of soybean meal.

Ecological concerns are having an effect on food costs, too. Some practices which were acceptable a few years ago are no longer favored and in some cases even forbidden by law. Two examples are the use of DDT as a pesticide and DES (Diethylstilbestrol) as a growth stimulant for cattle. Each tend to raise the cost of production--DES by 5 to 10 percent.

Last but not least, and perhaps the most important reason behind the rising costs of food is simply consumer demand. Many now take for granted luxuries undreamed of twenty or thirty years ago--and this includes food that has increased fantastically in supply and variety.

As our family incomes have risen from about $5,600 in 1950 to over $11,400 in 1972, so have our appetites for meat. For example, consumption of beef was 63 pounds per capita in 1950. In 1972, it was 116 pounds. In addition to our larger appetites per person for more red meat (145 pounds in 1950 to 189 pounds in 1972) we have experienced growth in total population.

Another part of the increased demand for food is related to the government food programs. Food stamps have contributed to better diets for the low income families, but at the same time have contributed about a 3 percent increase in demand. Poor people want more beef, too.

So what can consumers do about higher food prices? Consumers must recognize that they cannot "have their meat and their money, too." If money is very tight for a family, then they must make some choices. Do they wish to spend more for the kinds of food they like and enjoy and do without some other things? Or, are some changes in eating habits in order?

In an outlook sense, food prices increases may ease off a bit later this year. In the longer run food prices will increase with the general price level.

Expanding Foreign Demand

Worldwide, incomes are increasing substantially. On a per person basis, real income growth at an annual rate of 3 percent per year has been realized in recent years. Must of this increase in spendable income is going for food. The result is a booming demand for livestock products, grain and oilseeds. For example,

1) World feed grain trade grew about 5 percent per year in the 1960's. But in the last three years the rate of increase has approached 10 percent;

2) U.S. wheat sales, once concessional, are essentially commercial sales; and

3) World trade in oilseeds has been dynamic--increasing at an annual rate of about 10 percent per year in the last decade. U.S. exports of oilseeds will be over 14 million metric tons this year. And we could sell more soybeans if we had them.

One very important reason for the long-term growth rates in the feed grain and soybean trade is that world cattle, hogs and poultry numbers are increasing. Most spectacular are cattle. The world has added nearly 120 million head of cattle since the mid-1960's. Everybody seems to want more meat, especially beef. The probabilities are great that world livestock numbers will continue to expand and that the U.S. will be a major supplier of feed grains and soybeans.

Some new and short run factors have been added that increased U.S. farm exports in 1972-73 beyond anyone's expectations. The major factors in the expansion include:

1) Poor weather and crop failure in U.S.S.R. leading to the U.S. selling them $1.1 billion worth of farm products. This huge sale involved about 425 million bushels of wheat, 280 million bushels of corn and 40 million bushels of soybeans. The sale reflects three major shortcomings in Soviet agriculture. Their geographic location makes them extremely vulnerable to weather conditions, they have failed to make adequate capital investments in agriculture, and their economic system fails to provide motivation.

The Soviets appear to be changing their priorities. They are committed to supplying their people more protein. They have minimized livestock liquidation by purchasing feed grains and food grains in world markets at a huge expense. Furthermore, last summer they made a long run investment in both feed grain and soybean mills.

Indications are that the U.S.S.R. will be in world markets for substantial amounts of grain in the 1973-74 market year. Their grain supplies and carryover will need replenishing. There is doubt that their grain harvest in 1973 can meet both the livestock needs and build up supplies. We probably won't sell them nearly as much grain next year, as we did in the 1972-73 market year.

2) Drouth in Asia led to the sale of 80 million bushels of wheat to India in the current market year. They apparently need about 200 million bushels, of which much may come from other sources.

3) Drouth in Australia and South Africa where they are now harvesting short crops reduces their export capabilities now and in the year ahead.

4) The continuing failure of the Peruvians to catch anchovetas. Fish meal normally supplies an important part of the world's protein feed. This has contributed to the increased competition and higher prices for soybean protein meal. No one seems to know whether the poor catch was due to overfishing, a shift in ocean currents, or other causes. It appears that some strong competitive pressure on the soybean will continue into the next market year.

For example, I understand the Japanese are contracting for soybeans two to three hears ahead.

In the longer run it does appear that farm products may become a major trade commodity in exchange for U.S. energy and raw material needs. We have a competitive advantage in the production of feed stuffs.

Balance of Trade and Devaluation

Our balance of payments and our balance of trade for farm and industrial products has become serious. We have had continual balance of payments problems but in 1971 this nation had its first trade balance deficit in this century. In 1972 we were in the red by $6.4 billion. The reason is that our competitive position deteriorated as other nations productivity improved. Our balance of trade would be more serious if agriculture were not exporting over $4.0 billion more than we import.

To alleviate our monetary problems including the balance of payments and balance of trade problems we have had two devaluations of the dollar. Oversimplified and overfavorable effects of devaluation have been expounded. They are that 1) devaluation lowers our prices relative to other nations and will increase our exports, and 2) devaluation increases prices of imported goods to U.S. consumers and thus reduces imports. These effects only occur if other nations do not revalue their currency and do not have trade barriers.

A study of the effects of the 1971 devaluation on U.S. farm product exports found some limitation to the benefits from the devaluation. The reasons include the fact that 55 countries buying 1/3 of our farm exports either devalued an equal amount, or devalued more than the U.S. No relative price improvement was possible to expand our exports in these countries.

There were 62 other nations buying 2/3 of the U.S. farm products that permitted the devaluation to occur. But many of them have non-tariff barriers, like the EC variable levy or quotas, etc. that restrict trade regardless of price. The net result was that only 43 percent of U.S. farm exports were free to benefit from the 1971 devaluation. On the import side, for some items prices rose according to the devaluation and for other products, prices rose less than the devaluation. This is because some firms reduced profit margins. Also, some items in the U.S. are not price sensitive. The results on reducing imports are quite mixed.

Agriculture is one of the top U.S. exporters and one of the primary means this nation has to earn foreign exchange to meet not only the payments and trade deficits but to also alleviate the energy and raw material needs of the nation. Devaluation did play a role in expanding the export market and we should continue to reap some rewards from expanded foreign outlets. Major beneficiaries of devaluation have been soybeans, soybean meal and cotton. Feed grains experienced some gain.

The trade situation focuses attention on up-coming trade legislation. Negotiations start this fall to protect the trade rights of U.S. agriculture relative to the enlarged Common Market and is a part of the preparation toward general negotiations toward world-wide trade liberalization.

Expanded Acreage

Farmers know the need and want to produce more farm products to meet the domestic and foreign needs. At the same time they are somewhat cautious in their expansion because they remember well the "feed the world" experience of the mid-1960's.

Farmers indicated March 1 they would plant 72 million or 7 percent more acres to corn and 54 million or 14 percent more acres to soybeans. This increase was made possible by making 37 million acres available from the government set-aside program. With the continued strong prices and anticipated world demand the USDA decided this was an insufficient increase to attain a target output of 6.0 billion bushels of corn and 1.5 billion bushels of soybeans.

As a result additional acreage was released so farmers may plant crops on up to 50 million more acres than the 296 million acres planted to the principal crops in the spring of 1972. This is a percentage increase of 17 percent for the U.S. There will be a wide variety of crops planted on the 50 million acres. Some will be spring wheat. Sign up in the 1973 feed grain program indicates about 28 million acres of cropland will become available for corn, oats, barley, soybeans, hay and other uses. This is an increase of almost 20 percent over the 1972 acreage of feed grains, spring wheat and soybeans. Yields will be lower than average on this increased acreage (about 80 percent) as producers set-aside the poorest acreage on each farm.

Adverse weather reduced fall plowing and is delaying spring land preparation and planting. This means that some of the available acreage will not be planted to feed grains and soybeans. The delays also tend to reduce yields on all acreage.

Considering the domestic and world needs plus the planting and growing prospects it does not seem likely we will "overplant and overdo a good thing" in 1973. Even so, we cannot expect poor weather and poor fishing to continue around the world. Improved prices will elicit a production response not only in the U.S. but around the world. The "overdoing" may occur in 1974. But remember world demand today is based on rapidly rising income and shifts to more meat; not on the need of poor countries without money for food grains.

PRODUCTION EXPENSES

A strong upward surge in farm production expenses is occurring, with an unusually big increase of $6 billion likely. This would mean total farm production expenses of $53 billion or 13 percent above 1972. You will share in this rural business expansion. Let's examine the expense items briefly.

Farm Inputs

The strong feed and soybean prices that are so pleasing to grain producers are an important element in much higher prices of purchased feed. In March feed prices were 38 percent above a year earlier. Feed prices will stay above 1972 until harvest. Also, 4 percent more animal units (mainly hogs, beef and poultry) call for larger quantities of purchased feed. Futures prices indicate a decline in protein meal prices in 1973-74. Cost of replacement livestock will be much higher in 1973 as we experience exceptional strong demand for feeder cattle and pigs. Increased acreages of 15 to 17 percent and higher prices will boost outlays for seed. Whether one regards these developments as a blessing or bane depends upon whether you are buying or selling.

Non-Farm Inputs

Expenses for non-farm inputs will rise. Prices will be up but not comparable to the farm inputs. Big increases in the amount of fertilizer fuel, herbicides, pesticides, etc. will be needed to plant the larger acreage. The "transportation bottleneck" created some doubt if adequate quantities of fertilizers (especially phosphates) with proper formula would be available. Delays in planting and rerouting hopper cars to Florida to pick up fertilizer on their way back to the Midwest has relieved the situation. The energy crisis and possible fuel shortages worry many producers. Some producers may be adversely affected by lack of fuel or fertilizer. However, it appears that those producers with good business relations with responsible fertilizer and fuel suppliers will receive adequate supplies. Farm machinery sales are strong at higher prices, and are expected to continue so into 1974.

Financial Position

The expansion in the agricultural plant of 15 to 17 percent in 1973 and farm prosperity means farmers will want to borrow more money even at higher interest rates. The general financial condition of farmers is noticably better than a year ago. Farmers assets January 1, 1973 climbed to about $370 billion or 9 percent above year ago. Rising farm real estate values provided most of the increase. Farm debt rose 8 percent to $72 billion. Proprietors' equities were nearly $300 billion or up 10 percent.

Increases in 1973 in farm loans will stem mainly from larger investments in land, machinery and equipment and other capital improvements. Some increase in production costs will contribute to larger loan volume. Lenders are confident that ample funds will be available to supply farmer needs. Repayment experience in 1973 should be as good as 1972. About the only borrowers facing difficulties in meeting obligations will be those hit by a disaster or emergency.

SUMMARY

In conclusion we will increase farm output in 1973. This is especially true for feed grains, spring wheat and soybeans. Hog production will be up and a buildup in hog and cattle numbers is in progress. Livestock and milk prices will remain strong throughout the year. Export markets are expected to be strong. This expansion takes nearly equivalent increases in farm supplies and other inputs. This will result in new records in gross farm receipts, expenses and net farm income.