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UNITED STATES DEPARTMENT OF AGRICULTURE
Bureau of Agricultural Economics

ADJUSTMENTS FARM FAMILIES ARE MAKING TO THE COST PRICE SQUEEZE.

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The cost-price squeeze is a very real thing to North Carolina farm families. Droughts in 1952 and 1953 along with lower product prices and higher costs have reduced net farm incomes substantially. The income situation in 1953 was further aggravated by modest reductions in allotments of tobacco and peanuts, two of our main sources of farm income.

I believe that every farm family in North Carolina who reads, listens to the radio, goes to farm meetings, goes to a country church, or participates in the philosophic discussions at our numerous country stores heard that the cost-price squeeze was expected to continue in 1953. Furthermore, practically all farmers believed that product prices would be lower and costs higher this year.

There are a few farmers in North Carolina who did not need to adjust in view of the expected situation. There were a few others who decided not to make any adjustment. The vast majority, however, did make some adjustment to meet the expected situation.

The farm families of North Carolina reacted to the intensified cost-price squeeze of 1953 in much the same way they have to previous cost-price squeezes. All families did not adopt the same course of action. Indeed the adjustments by different families were often diametrically opposed. Yet when situations facing each family is understood it seems that the adjustments made by most families were quite logical.

I have classified the adjustments into five categories. The five are:

(1) Increasing output.

(2) Reducing expenditures for capital goods.

(3) Reducing operating costs.

(4) Reducing family living expenditures.

(5) Securing non-farm employment.

Let us now take a closer look at each of these items.

Increasing output

A majority of the farmers made an effort to increase their output in order to maintain the family's net income. Many farmers made changes in production practices on tobacco and peanuts which they believed would result in the same number of pounds as they made the preceding year when allotments of their crops were larger. To a lesser extent, efforts were made to increase the yield of unallotted crops. Farmers tried to increase yield by using more fertilizer, more insecticides, better seed, closer spacing, and better cultural practices.

Efforts to increase output were not limited to increasing yields. Many farmers increased the size of one or more enterprises by using land taken out of tobacco and peanuts, bringing in idle land, and by renting additional land. Those farmers, who increased total acres operated, usually expanded the acreage of one or more crops which they had been producing. Crops which farmers tended to expand were corn, soybeans, oats, wheat, sorghum, sweet potatoes and annual hay crops.

Some farmers believed double cropping was the way to expand output. Hence, there was an increase in the practice of following small grain with milo or soybeans and tobacco and peanuts with small grain.

Dairymen and poultrymen followed about the same pattern as crops farmers. They tried to increase output through expanding numbers and through increasing the output per unit. Most beef and hog producers did not try to increase the output from these enterprises. The expectation of low prices for hogs and beef and a shortage of feed are the reasons most commonly advanced for not expanding these enterprises. Beef cattle and hogs are almost always supplemental enterprises in North Carolina; and the producers of these commodities looked elsewhere to expand output.

Another way to increase output is to add additional enterprises. Few farmers chose this alternative. Where new enterprises were added, they tended to be closely related to enterprises already used. Examples of the type of additions made were adding milo and soybeans on small grain farms. Farmers had a very good reason for not adding new enterprises. Most new enterprises required an outlay of capital, and this is one step many farmers were unwilling to take. (A group of farmers who did not feel this way will be discussed later.)

The fact that farmers tried to increase output in the face of falling prices was not unexpected. They have followed this course before. Also, it is a logical course of action when viewed from the standpoint of the individual farmer, although it does seem inconsistent when viewed in the aggregate. The action is consistent with economic principles for maximizing income on an individual producing unit operating in a competitive situation, if we assume that expected prices will more than cover operating (or variable) costs and that farms were operating with less than the optimum input of productive factors before the cost-price squeeze became effective. The last point should be emphasized. The fact that farmers did believe it to be profitable to increase the input of productive factors in face of the cost-price squeeze is *prima facie* evidence that farmers were previously operating below optimum levels of factor input. If farmers had been operating at the optimum point, it would have been in their interest to reduce the input of factors when a cost-price squeeze is operating.

As a final comment, the course of trying to increase output did not result in higher net incomes in 1953 for most farmers. The reason it did not work, however, was that one of the most severe droughts in our history occurred during the summer of 1953.

Reducing expenditures for capital goods

Many farmers decided to beat the cost-price squeeze by reducing capital outlays. They decided not to trade in the old tractor or buy a second one. They decided not to put up a new barn, granary, or tenant house. Expenditures for drainage, terracing, land clearing, and pasture development were curtailed sharply on many farms. Investments in expensive breeding stock were reduced sharply.

It is not intended to imply that there were no expenditures for capital goods. Some farmers had to buy equipment and invest in buildings. The farmers who did make capital improvements were cost conscious, however. They spent just as little as they could and still get by. This is a quite different situation from that existing two or three years ago when our farmers wanted and got the best - to heck with the cost.

There were some farmers, however, who thought it would be to their advantage actually to increase expenditures for capital goods. A large part of North Carolina and other Southern States have continued to use large quantities of labor. In North Carolina less than half of the farms have tractors and there are very few completely mechanized farms. They have been logical in following farming systems and practices which use a lot of labor. Proof of this statement has been the inability, until quite recently, for either the Experiment Station or farmers to develop alternatives which use substantially less labor and still maintain income.

Labor costs have risen in North Carolina, as in the rest of the nation, much faster than the cost of other productive factors. The expectation that labor costs would continue to rise sharply caused some farmers to mechanize, as one means of beating the cost-price squeeze. This move required a lot of money. Other farmers decided to discontinue producing or to reduce the acres of crops requiring a lot of labor such as cotton and tobacco and to begin producing livestock. This course of action required a large capital outlay.

Thus even in the same community there were farmers following divergent courses of action with regard to capital outlays. The group reducing capital expenditures gave the following reasons for doing so: (1) As there was insufficient income to maintain the standard of living and expand the investment, in farm business, they decided to forego expanding the business. (2) They believed that capital goods would cost much less in the future and hence it was poor business to buy now, particularly if the standard of living had to be reduced to make the investment. (3) They could not afford to invest in capital goods. In some cases this statement was true. In the majority of cases, however, an investment could have been made, particularly by resorting to borrowing. The farmers simply gave this reason as an excuse for either not wanting to squeeze the standard of living or because they were fearful of the future.

The group which made large capital outlays during the year almost invariably gave high labor costs as the reason.

Reducing operating costs

One of the obvious courses of action when faced with a cost-price squeeze is to reduce operating costs. While the farmers tried to follow this course of action, they were remarkably unsuccessful in their efforts. As previously indicated, most farmers wanted to increase output, and particularly through increasing yields. This goal called for increased expenditures for fertilizer, seed, and insecticides. If yields had actually been as high as planned, the cost per unit would have been lower; but total cost for the farm would still have been higher.

On some farms it was possible to reduce labor costs through mechanization, changing enterprise combinations and by using work simplification techniques. On most farms, where labor is performed by the operator's family or tenants, labor is in the nature of a fixed cost in the short run and increases in labor efficiency do not necessarily reduce cash operating costs.

It was possible in some cases to reduce the cost of repairs to machinery. On livestock farms it was possible in many cases to reduce feed costs by producing feed on the farm, substituting cheap feeds such as pasture and silage for grain, and by abolishing wasteful feeding practices.

Our staff saw many farm plans for 1953 and it was indeed rare to find a farmer who believed that he could profitably reduce cash operating costs. Also when the effect of College recommendations for 1953 to individual farms was determined, total cash operating costs were almost always increased, except in those cases where farming systems and practices were radically changed. Bankers in the State tell us that cash operating costs were not reduced in 1953 and farm records bear this out.

Of course there were a few farmers who reduced cash operating expenses by decreasing the amount of fertilizer used and by using home produced seed. Generally speaking, this did not appear to be a wise course of action to follow last spring. With an unforeseen drought coming along, it turned out to be a fairly good course of action. It should be pointed out, however, that most of the farmers who did reduce expenditures for fertilizer, seed, and similar items did so, not because they wanted to, but because they had no alternative. Farmers who started the year in a poor cash position had trouble borrowing enough money to buy the quantity of productive factors they wanted to use. Capital rationing is a very real problem to many of our farmers, although they do not use the ivory tower phraseology.

Reducing family living costs

It is no secret that net farm income for the average Southern farmer is low. It is also axiomatic that when income is already low, a decrease hurts worse than when income is higher. As many North Carolina farm families tend to use all of their net income for family living (i.e. they save practically nothing) a decrease in net income is felt immediately in a lower standard of living. This condition may account for the almost desperate efforts of farm families to maintain income through increasing output.

Many farm families tried to keep lower net farm incomes from reducing the standard of living by producing more food at home and by making more of the families clothing. Undoubtedly many farm families reduced expenditures for insurance which provides security in the future, and contributed less to charity in an effort to maintain their own current living standards.

In spite of all efforts, many families are realizing substantially lower net incomes. Where this has occurred, some families are reducing purchases of durable goods such as new appliances, new automobiles and new furniture. Plans for remodeling and building new homes are being discarded. Other families want the durable goods so badly that they have decided to reduce expenditures for clothing, recreation, and the so-called non essentials such as cigarettes.

For the few families who have been making larger incomes than needed for current living expenses, the only adjustment in family living is a reduction in savings.

We hear that some families have not adjusted family living costs in spite of lower incomes. In a few cases the standard of living is being maintained out of savings. In many more cases, however, the standard of living is being maintained by going into debt. This course must have an end, however.

Securing non-farm employment

A large number of families saw non-farm employment as the solution to their income problem. In many, many cases the operator or a member of the operator's family worked all or part of the year in non-farm employment. The study of Dr. Bishop, of our Experiment Station, and the farm records that we see, indicate that this is a very good way for many families to increase the income available for additional investment in the farm and for improving the standard of living. Most families on small farms that have farm and non-farm income have higher total incomes than either the families securing all of their income from industry or from farming alone.

It is believed that a larger number of people did not choose this alternative because non-farm work was not available in their community. Opportunities for non-farm work are limited in those areas where little or no industrial development has occurred.

Adjustments that will be made next year, assuming the cost-price squeeze continues.

It is my opinion that the same types of adjustments that were made in 1953 will be continued although the proposition of farmers making each adjustment will be different. Many farmers will try to increase output, although an increasing number of farmers will find themselves in the position of not having and not being able to get the operating capital that will be required to increase output. A larger number of farmers will reduce expenditures for capital goods. Farmers would like to reduce operating costs but in most cases will not find it profitable. Standards of living will be lowered. If non-farm employment can be secured, an increasing number of farm families will turn to this alternative.

Adjustments which should be made by the individual farm family

It is necessary when giving opinions as to what should be done to clearly indicate whether you are thinking in terms of society or of the individual farm family. There is frequently a conflict between what is best for the individual and for society, particularly in the short run. For example, from the standpoint of society, it appears foolish to increase output with prices falling. Yet from the individual farmer's point of view it is often the thing to do. I want to emphasize that in my concluding remarks I am thinking in terms of the individual farm family.

I am classifying the adjustments which should be made into three categories. The first category includes all those adjustments which require neither additional operating funds or a larger investment. Examples include using an improved hybrid, fall freshening of milk cows, applying work simplification techniques, substituting silage for grain and changing the spacing on crops. New technology coming out of our Experiment Stations often falls in this category. Some of the adjustments which fall in this category reduce costs; but in our State the majority will increase output. The individual farmer stands to gain by making all of those adjustments which apply to his farm and which do not increase cash costs. Many of the adjustments we are discussing can be made with an additional input of management, which on most farms is a fixed cost.

The second category includes those adjustments which increase cash operating costs. Examples are using more fertilizer, increasing the size of the business by renting more land, feeding at a higher rate, and changing from sharecropper labor to wage hands. Practically all of these adjustments will result in an increased output. If we assume that weather conditions will be normal, it is my opinion that adjustments of this type will result in an increased income. With the Government supporting many prices at a level which protects a farmer with average efficiency from loss and with a short time lag between expenditure and return, the risk of such adjustments not paying off is low for farmers with a reasonable amount of managerial ability.

The third category includes those adjustments which requires a larger investment in the farm business. Examples include mechanization, adding livestock, seeding permanent pastures, fencing, drainage, terracing, land clearing, and purchasing additional land. For the average farmer the decision as to whether such adjustments depends upon the appraisal of future economic conditions. If somewhere near present price relations continue, such adjustments will be profitable on many farms. If another depression is in the offing, they will not be profitable. While I do not expect price relationships to remain as favorable to farmers as they were last year, it is my opinion that conditions will be such the many long run or intermediate investments will be profitable. Those investments which tend to reduce costs have a greater chance of being profitable than other types. Many farmers will undoubtedly find it profitable to add machines and reduce labor costs. Other farmers will find it profitable to add livestock in order to give year round employment to labor and to utilize crops which cannot be marketed to advantage. Although land prices are high and will likely fall, some small farmers will find it desirable to enlarge their farms, if they can buy land conveniently located to their present farm. The economics of scale will more than offset a reasonable drop in farm prices.

After indicating that many adjustments which require capital will be profitable, I will add that I do not believe many farmers will make these adjustments in 1954. The investments will not be made because farmers are applying a much higher rate of discount on future returns from investments than is warranted. The high rate of discount is due to farmers having limited information on the factors which cause prices to change. Also they do not know how to use the economic data secured to make an intelligent appraisal of future prices.

This indicates to me the role that Outlook information can play. It also tells me something about what our objectives should be and the type of information that should be included in Outlook.