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PROCEEDINGS

AGRICULTURE AND INFLATION

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Foreword

For many years the Ontario Agricultural College has organized and presented a program at which topics of current interest and concern to Ontario farmers and others interested in agriculture have been examined. In developing the program for this year's Conference it was readily apparent that the impact which inflation has had and is likely to have on agriculture is a prime concern of farmers. Likewise, consumers are concerned about the extent to which rising food costs are not only contributing to inflation but are also providing the fuel to generate its continuance.

The purpose of this section of the program for the O.A.C. Agricultural Conference '75 was to assess the effect which agriculture has had on inflation, the effect which inflation has had on agriculture, and to suggest alternative courses of action which might be taken to remove the causes of inflation and to minimize its harmful effects.

This Conference, being one of the extension activities carried on by the Ontario Agricultural College, was financed under the research and services contract which the University of Guelph has with the Ontario Ministry of Agriculture and Food.

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AGRICULTURE AND INFLATION: THE ISSUES

T. K. Warley*

Introduction

These are economically troubled times. Having enjoyed an economic boom lasting a generation, the world is now in its worst post-war recession and a paroxysm of virulent inflation. Growth in the developed countries in 1975 will likely be less than 1 per cent for the second year in a row. Inflation will continue at a two-digit rate. Unemployment will reach new post-war record levels. The OECD countries will have an aggregate balance of payments deficit approaching $40 billion. Stock market price indices, which have already fallen by from 25 to 70 per cent from their post-war highs, are unlikely to show much recovery during the year. The possibility that the global economy will degenerate into a slump of alarming proportions is not ruled out by thoughtful observers.

Inflation, which we can define as a persistent increase in prices, is on everyone's worry list. For the OECD countries as a whole it averaged 7.7 per cent in 1973 and 15.5 per cent in 1974 (Table 1). In 1975 prices are projected to increase by a further 11 per cent. For Canada the corresponding rates of increase in the consumer price index are 7.6, 11.6 (October 1973 - October 1974) and 11 per cent in 1975, if we're lucky. Although Canada's price experience is better than that of most other countries, both the record and the prospect are appalling (prices double every seven years with a 10 per cent inflation rate).

Rising prices for food have made a significant contribution to general inflation in all countries. The world commodity spot price index for food stood at 218 in June 1974, with 1970 as 100. Only oil showed a greater rate of increase (index 613). In Canada consumer food prices rose 14.6 per cent in 1973 and by over 15 per cent in 1974 and

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Table 1. "STAGFLATION"

	Inflation		Real Growth		Current Account Balances	
	1974 %	1975 %	1974 %	1975 %	1974 $B	1975 $B
Canada	11.25	11.00	4.50	3.50	-1.50	-3.75
U.S.A.	12.50	10.00	-1.75	-2.00	-3.25	-7.50
Japan	26.75	11.50	-3.25	2.00	-4.75	0.00
Germany	7.25	6.75	1.00	2.50	9.00	6.00
France	15.50	11.50	4.75	3.00	-7.50	-6.25
Britain	17.75	18.00	-0.50	1.75	-9.00	-6.50
Italy	25.25	14.50	4.75	-0.25	-8.25	-5.75
OECD area	15.50	11.00	0.25	0.50	-37.50	-38.50

SOURCE: O.E.C.D.

Table 2. INFLATION IN CANADA 1969 - 1975

	1969	1970	1971	1972	1973	1974*	1975**
				percentage change			
C.P.I.	4.5	3.3	2.9	4.8	7.6	11.6	10-12
Food	4.2	2.3	1.1	7.6	14.6	15.7	14-15

* October 1973 - October 1974

** Estimates

SOURCE: Statistics Canada.

accounted for 51 and 45 per cent respectively of the rise in the consumer price index. Prospects for 1975 are for a further increase of 15 per cent in prices of food to consumers.

Inflation has also hit farm costs. The index of prices of farm inputs rose from 135 (1961 = 100) in 1971 to 166 in 1973. The index will have topped 190 in 1974 and will stand higher again in 1975 (Figure 1).

It is apparent that we are addressing here today a topic of great importance. Farmers as citizens and as businessmen are affected by inflation and have an interest in seeing it brought under control. They worry that rising input prices are eating into profits; that consumer demand is slackening as high consumer prices erode purchasing power; and that their response to demands that they increase supplies might push prices down to red-ink levels. Consumers are deeply alarmed by the large proportion of the erosion of the purchasing power of their incomes which is attributable to rising food prices. They are seeking reassurance that the tide of rising food prices is not unnecessarily swelled by misguided farm policies, and they are demanding that the tide of rising prices and shortages be turned back by an increase in the supply of farm products available in food stores.

My task in opening this conference is to set the stage by briefly reviewing the causes, costs and cures of inflation and to identify some key issues of agricultural and food policy in an inflationary environment. The speakers who follow will treat these issues in greater detail. All the participants in the conference will have an opportunity to express their views.

The Causes

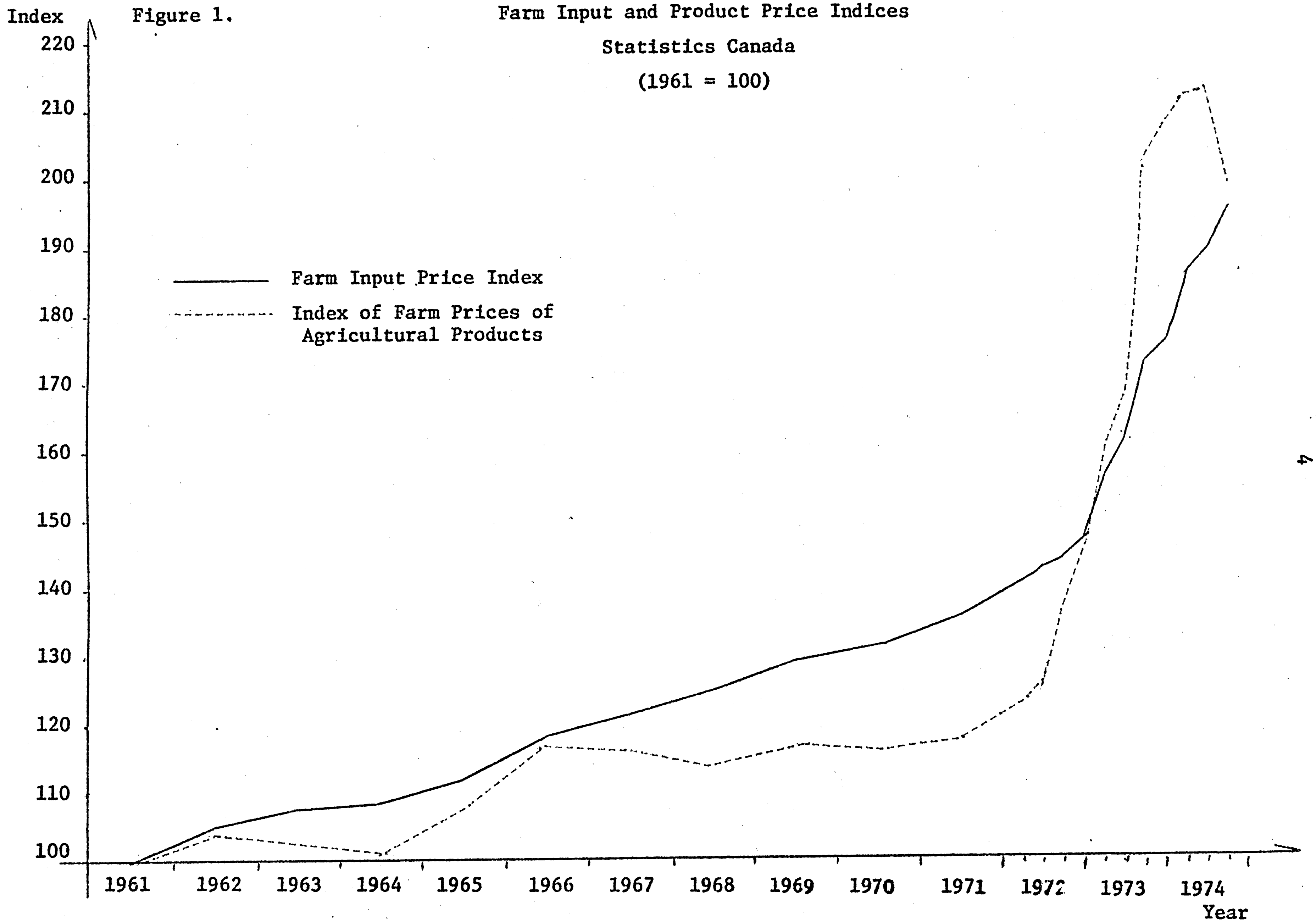
Economists generally agree on the causes of inflation, though they disagree on the relative importance which should be attached to the many elements which contribute to a persistent increase in prices. They tend to make a distinction too between movements in relative prices of particular

Figure 1.

Farm Input and Product Price Indices

Statistics Canada

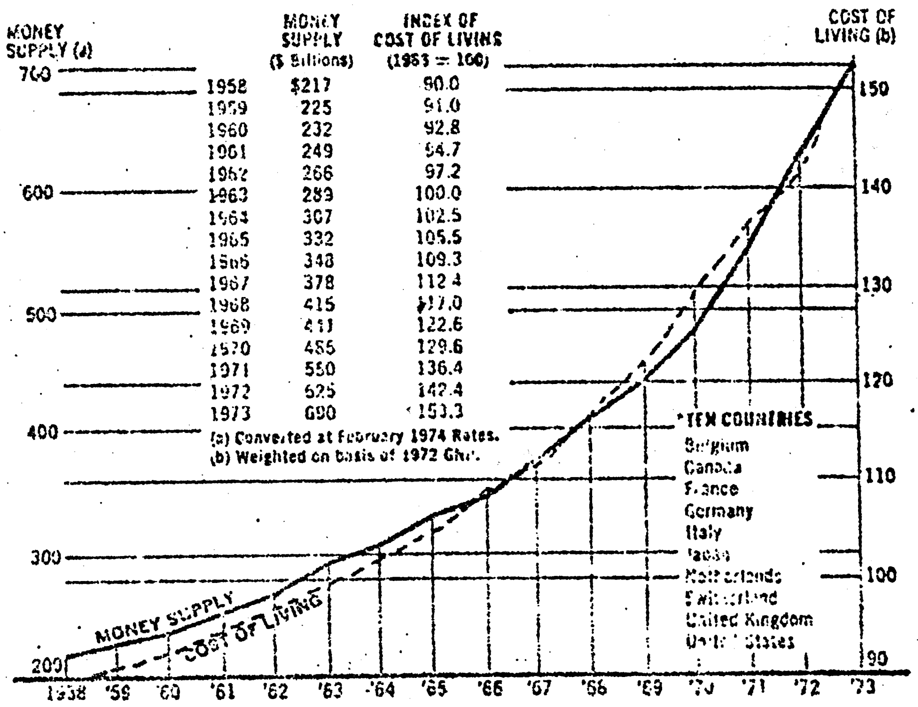
(1961 = 100)



goods and of the general price level, but this may be a distinction without a difference since sudden and large increases in the prices of some goods attributable to changes in supply or demand (e.g., food and oil) have their own inflationary impacts and are in turn affected by general inflationary trends.

There is widespread agreement that the present inflationary spiralling of prices is attributable in large measure to a global expansion in the money supply relative to the growth in world output (Figure 2) (with the U.S. being particularly culpable), and a propensity of governments to finance their ever-expanding spending programs by borrowing and printing rather than taxing. Inappropriate monetary policies and lax fiscal policies result in the growth of aggregate private and public demands on national output being greater than the growth in output itself - too much money chasing too few goods - and inflation is the means by which the face value of each claim on output is debased. Deficit budgeting and excessive rates of increase in the money supply have been widespread in recent years with the consequence that unsustainably high rates of economic activity and overfull employment were coincident in all the major developed countries. Additionally, until quite recently, the defense of inappropriate exchange rates has, on balance, added to inflationary pressures. Once demand-pull inflationary tendencies are afoot, cost-push inflation follows. Groups in society with strong bargaining power (unions, industries, firms) use their strength to "pass-through" the cost increases they experience. They offset erosion of their incomes by wage, price, profit, and rent increases which exceed productivity gains. These primary sources of inflation have been in evidence for some years. More recently the fires of inflation have been fueled by the rapid rise in food and resource prices since 1972 and in energy prices since 1973. Inflation also feeds upon itself. Since expectations of worsening inflation are written into wage settlements, contracts and prices on a precautionary basis, it becomes a self-fulfilling prophecy.

Figure 2. Money Supply: A Prime Culprit



Source: S. Rolfe, "The Great Inflation", Saturday Review, 27 July 1974

This list of the causes of inflation is not exhaustive. Others would include the growth of the private service sector and of the government sector and the difficulty of securing productivity increases in each. Others would not wish to exclude what has been termed "legislated inflation" such as environmentally related cost imposts on producers, "sweetheart regulation" of public utilities and industries, and government imposed inflationary wage settlements (e.g., the grain handlers). Finally, there are those who claim that inflation is deeply rooted in the social fabric of a consumption-orientated society where self indulgence, "a galloping psychology of entitlement", a stress on quantity and immediacy and a "play now - pay later" ethos are matched by a diminution of a sense of social commitment and personal obligation.

We need agree only that inflation has multiple origins, and that the much publicized food and energy shortages are late-coming exacerbants rather than primary causes.

<u>The Costs</u>

Just as the causes of inflation are complex, so the effects of inflation are also pervasive. Traditionally, a good deal of emphasis has been put on its distributional effects. Inflation is a silent, undemocratic and cruel tax which cheats people out of their savings, robs the worker of his wage, and the investor of his return. It falls unequally. "If it scourges the middle classes it whips the poor with scorpions". Low and fixed incomes recipients, small savers, and unorganized groups generally are penalized more heavily than people in unions, industries and government who have significant market power and are not constrained by the discipline of competition. Such groups can not only protect themselves against the ravages of inflation but may even gain in an inflationary environment. Inflation transfers income from savers to debtors, and rewards the hoarding of goods and the mere possession of assets rather than their productive use.

Equally however, inflation is the enemy of growth. It deters saving and investment, distorts price signals, and negates rational and orderly planning. Stern counter-inflationary policies may entail running the economy below its capacity for prolonged periods. Left unchecked inflation will eventually induce economic collapse.

Finally, inflation poses a grave threat to the political fabric of society. An economy with runaway inflation is a society in disorder. Weak groups are alienated, leaders are viewed with cynicism, and authoritarian solutions are favoured over democratic institutions and processes.

The Cures

There is some reason for believing that the worst of the hyper-inflation experienced in the past few years may be over. Most governments have slowed the growth in the money supply from the irresponsibly high rates of 1969-72 and are showing more budgetary discipline. Many commodity prices have dropped substantially from their high water mark; the fear of shortages has receded; and the unloading of accumulated inventories will have some price moderating effects in 1975. Even so, price inflation in Canada will be 11-12 per cent in 1975 and the best that can really be said is that inflation will continue to worsen at a marginally slower rate. Most observers see a continued upward drift in prices (perhaps at a slowing rate) for a number of years, and both the fact and the intolerable rate call for purposive government action.

There is a long list of instrumentalities which governments can use to curb inflation. Traditional theory and most commentators place primary emphasis on the "old-time religion" of reducing the rate of growth of the money supply, curbing consumer credit, and having all levels of government match their lust to spend to their will to tax. A further measure which has recently been strongly debated (and weakly attempted) is the imposition of mandatory controls on prices and incomes as an alternative to deflation. A weaker version entails setting voluntary guidelines and, hopefully, their observance being secured by monitoring, exhortation, and persuasion ("jaw-boning"). Other weapons which governments can use in their fight against inflation include liberalization of trade restrictions to allow cheaper imports to hold domestic prices down; curbs on exports to increase the supply of goods available to domestic consumers; letting the exchange rate rise against other currencies; encouraging savings and investment by taxation changes; taking vigourous action against concentrations of economic power to prevent both gouging and the passing through of cost increases into prices; and the indexation of wages and prices (which doesn't prevent inflation or roll it back but prevents its acceleration by reducing the precautionary element in wage and price increases associated with inflationary expectations). Still other measures include compromises on environmentally-related investment requirements; provisions to cushion the hardships imposed on those thrown out of work or who find their profits reduced by many of the above measures; and the requirement that governments provide an "inflation impact statement" with every piece of legislation or regulation that they introduce.

The battle against inflation is not hampered by a shortage of weapons. The problem lies elsewhere. Chief amongst these is contained in one of the more dismal observations of modern economics that there is a trade-off between the rate of inflation and the rate of unemployment. Even in the best of economic times few governments are eager to deliberately increase the rate of unemployment. And these are the worst of economic times insofar as our present intolerably high rates of inflation are accompanied by recession and distressingly high rates of unemployment. Increasing unemployment and lowering output by applying monetary and fiscal brakes to the economy makes economic and even political sense in periods of economic boom and demand-push inflation - it has little appeal in the midst of "stagflation". Furthermore, there is a real danger that deepened and synchronized recessions in all the major economies could plunge the world into a horrendous slump, just as synchronized booms triggered inflation. Thus, governments and their advisors are presently having some difficulty in making up their minds which of the twin evils of inflation and recession are Public Enemies #1 and #2 respectively. The obvious alternative to intensifying recession in attempting to bring inflation under control would seem to be to impose price and income controls. Alas, international experience with this tool of economic management is none too encouraging. It is politically unpopular. And it is widely, though mistakenly, believed to be worse than the disease insofar as it is alleged to produce more distortions in price signals than does inflation itself. Price controls would be particularly difficult in agriculture by reason of the industry's products being numerous, diverse in quality, seasonal, perishable, geographically dispersed, and interdependent in that the outputs of some farmers are the inputs of others. Thus there are real practical difficulties in bringing to bear the conventional weapons of monetary and fiscal policies and direct controls on the enemy of inflation. Additonally, to change and mix metaphors, the big levers of monetary and fiscal policy are perhaps not well adapted to "fine-tuning" the economy and steering the narrow path between the Scylla of recession and the Charybdis of inflation - they're rather effective in rapidly speeding up the economy, they're not so effective in gently slowing it down. Finally, with inflation a world wide phenomenon, and rapidly transmitted through trade and the monetary system, there are real limits on the ability of national policies to curb inflation.

More generally, the fight against inflation is hampered by special interest and a sclerosis of leadership. We all hate inflation in principle, but some of us gain by it, at least temporarily, and all of us dislike some of the measures which would bring it under control. Equally, since most anti-inflationary measures hurt some vocal groups in society, our political leaders are reluctant to face up to the essentially political problem of determining how the costs of a policy to counter inflation should be borne. The vote is mightier than the resolve. And politicians and public servants characteristically set a poor example for the rest of us when their own interests are involved and have a poor track-record in managing the large slice of the economy which is under government control.

To sum up this section, inflation is endemic; will likely be with us for a considerable period of time; is only partly susceptible to attenuation by national economic action; and there is no costless or painless way to bring it to a halt.

This brings me to the first "issue" that I should like to raise. Prolonged and virulent inflation has a profoundly adverse effect on our society, on our economy, and upon particular industries, including agriculture. Governments need the advice of industry groups on how the campaign against inflation should be conducted. Industry groups have a vital interest in which combination of economic weapons are deployed and how they are used. The issue I want to raise is to ask whether organized agriculture is sufficiently sophisticated and professionally equipped to give counsel to government on the general issue of the control of inflation, to give mature advice on the combination of economic policy instruments which should be employed to combat it, and to analyze the policy requirements which would both minimize the adverse effects on agriculture of the use of particular instruments and permit agriculture to play its full part in eradicating this dangerous economic disease.

Agriculture as Victim

Agriculture as a whole has been shielded from the recent surge in inflation by a more than compensatory surge in commodity prices. Whilst all farm input costs have unquestionably increased (in part due to supply/demand changes, in part due to generally inflationary pressures) the fact is that aggregate farm revenues have increased even faster in a period of acute food shortages and bouyant export demand. Hence, the period of our worst national inflation has coincided with record aggregate gross and net farm incomes and soaring farm asset values. Presumably too, farmers holding mortgages have enjoyed paying off their obligations with depreciated dollars.

It would be fallacious to conclude however that farmers benefit from inflation. In the first place, the unprecedented aggregate prosperity of agriculture is not uniformly spread within the industry. Most crop producers (and especially grain growers) have obviously had a bonanza, whereas some sectors of animal agriculture have found their profit margins squeezed by rising input costs (especially purchased feeds) and sagging farm-level prices attributable to cyclical increases in supplies, to the erosion of consumers' purchasing power and resistance to high prices, and to a rise in marketing margins inflated by cost increases for labour, packaging materials, transport, etc., and by some improvement in processor and distributor's profit margins. Secondly, land prices have risen in part due to people outside agriculture purchasing real estate as a hedge against inflation and this, together with high interest rates, has made it extremely difficult for new entrants to the industry to become established and left those who have entered with an alarming burden of debt to service. Thirdly, inflation has made forward planning and investment decision-making extremely difficult since price signals are hard to interpret in an inflationary environment and cash flow statements are all but meaningless to lenders. Finally, and most important of all, it is possible that agriculture, though temporarily prospering, may be more vulnerable to a precipitous decline in income and a collapse of asset values than at any time in history if market-determined commodity prices fall from their present unnaturally high levels whilst inflation and administered pricing by supply industries continue to sustain and to increase input costs.

I hope, therefore, that we can address a number of the issues which this situation raises. Specifically, we should try to obtain a clearer understanding of which sections of agriculture are gaining and hurting in this inflationary environment, differentiating between those whose gains have been fortuitous (e.g., grain producers), those which have gained because they have been able to index product prices to costs (possibly milk, egg, and poultry producers), those who have experienced a large appreciation of capital assets, and those whose crawl space of profit has been squeezed by sagging prices and inexorably rising costs. Secondly, we should address the question of the vulnerability of incomes and net worths in various sectors of agriculture should the bubble of presently high grain prices burst. Thirdly, we should try to form a view on the likelihood of this latter event occurring and its timing. My own view is that the present level of grain prices is explainable by a combination of unique events which occurred in the 1972-74 period, that prices will not fall back to 1969-71 levels because of rising input prices and the future avoidance of the accumulation of the large price-depressing grain surpluses which overhung markets throughout the 1950's and 1960's, that prices will be sustained in the near term by the need to re-build working and security stocks to more appropriate levels, but that prices are in danger of falling considerably in the medium term (3-5 years) as underlying excess grain production capacity reasserts itself over inadequate effective global demand. Some of you who are more familiar with farm accounting and taxation than I may also wish to address such questions as "inflation accounting" for farm assets and inventories, the adequacy of present investment and depreciation allowances, and the impact of inflation on succession and death duties and the associated problems of farm transfer and farmer entry to and exit from the industry.

Agriculture as Saviour

Agriculture has a long history of moderating inflationary tendencies in our economy. Excess agricultural capacity, rising productivity, the accumulation of surplus stocks of basic foods, an overvalued currency, and possibly inadequate incomes to many farm people and low returns to capital in agriculture, combined for almost two decades to provide an abundance of farm products and hold food price increases well below those for most other items in the Consumer Price Index. As a result, food prices stabilized prices generally. Suddenly, food shortages have ratcheted all prices sharply upwards. Naturally, consumers and governments are anxious to ratchet them down again by encouraging an expansion of supply, and few would disagree that responding to this challenge is one of the most important contributions that agriculture could make to moderating the pace of inflation, thereby meeting one of the preconditions for a renewal of strong economic growth. Furthermore, consumers and food processors and distributors are strong supporters of proposals to create international food reserves so that the assurance of supplies and the stability of prices would be enhanced should the world face periodic crop shortfalls in the future of the magnitude of those experienced in 1972 and again in 1974. Both these matters - going for all-out expansion of food production and creating stabilization reserves - raise important issues for farmers.

In the first place, expanding production can only come about if society makes explicit commitments to ensure that inputs (especially fertilizers, fuel, and pesticides) are in plentiful supply and at reasonable cost; to prevent the unnecessary loss to non-agricultural uses of productive farm land by inadequate planning; to expand expenditures on research and extension to discover and disseminate the improved technologies a falling agricultural labour force will need to apply to a relatively stable land base; and to compromise on environmental standards applied to agricultural production.

More fundamentally, farmers are loath to expand output unless they are given some assurance that product prices will bear a favourable relationship to input costs and will not be depressed to unprofitable levels. At present we are taking hesitant steps in Canada towards a "stabilization policy" for agriculture which puts floors under commodity prices or guarantees minimum incomes or commodity-derived margins, these variables being indexed, to varying degrees, to costs. There are three issues which we might address. First, it is worth asking whether "stop-loss" orientated price, margin or income guarantees (which are unquestionably necessary) are sufficient. It is arguable that farmers should be given specific and unequivocal assurances that increased output will be accompanied by increased profit. Secondly, the indexation of prices, incomes or margins to costs raises such important questions as whose costs and for what part of national output (should the costs of inefficient producers be guaranteed?), which costs (should quota rights, levies and returns to land be included?), and how adequate are present data systems for the task of generating needed cost data? Thirdly, it is arguable that the extension of cost-plus pricing in agriculture will be a giant and irreversible step toward managing the industry as a type of public utility. Is that what farmers and society want?

The question of food reserves is a complex subject and time will not permit our exhausting it. Nonetheless we should at least note that the proposal to establish global grain reserves (which in aggregate might total 50 million tons over and above the working stocks which farmers, traders, and processors would choose to hold) is one which farmers view with some suspicion. Grain growers know from bitter experience that stock levels have a direct effect on prices. Consumer-taxpayers might well be willing to fund the acquisition and holding of stabilization stocks which moderated price increases in short-crop years, and livestock product producers have an interest in more stable feed grain prices. But grain growers are rightly anxious lest such stocks overhang the market and depress prices on a continuing basis.

Agriculture as Culprit

We have seen that rising food prices have contributed close to half the increase in the Consumer Price Index in the past two years. Rising farmgate prices have accounted for much of the rise in retail food prices. The effects of rising food prices on consumer awareness and inflationary expectations are probably even greater than the arithmetic magnitudes involved insofar as they are highly visible and occur in an area where consumers are quite knowledgeable. Consumers meet inflation "eyeball to pocketbook" two or three times a week in the food store, and they know from personal experience that food prices have led the worst inflationary march in their lifetimes.

Most consumers have quickly come to understand that the worldwide food shortages of 1972-74 have been the major contributor to rising prices in the local supermarket. However, they have also found grounds for concern in three aspects of national policies for agriculture and food which they suspect contribute to inflationary food price trends. These are trade policy for farm products, the operations of agricultural marketing boards, and the apparent neglect of consumer interests in agricultural policy formulation.

Consumers have been quick to perceive that elements of our commercial trade policy for farm products result in a higher level of food prices for Canadian consumers, at least in the short term. Specifically, they want to know first the justification for systematically limiting the availability of cheaper supplies of foreign agricultural products in the Canadian market by a variety of tariff and non-tariff measures at a time of rapidly rising food prices. Long-standing targets for their discontent would likely be our import policy for milk products, for some fruits and vegetables, and for wines. Now beef has been added to their list. Secondly, consumers are questioning whether a policy of maximizing exports, and of operating an "open door" export policy, is in the best interest of the Canadian consumer and the Canadian economy. They claim that a policy of restricting exports in periods of shortages would lower consumer prices, strengthen Canada's international competitive position by holding down inflationary price increases, and permit a more expansionist domestic economy. The counter-arguments are, of course, that such export controls invite retaliation; they would destroy Canada's reputation as a reliable international supplier, and stimulate self-sufficiency in importing countries and the search for alternative sources of supply; they would not serve Canada's long-term interests in promoting an open world trading system; and attempting to export inflation is just as dangerous to the world economy as the export of unemployment. Additionally, limiting exports in a hungry world is morally repugnant. Nonetheless, the case for a policy of managing exports is superficially appealing and it needs our attention.

Consumers do not appear to be inherently hostile to the concept of marketing boards. They understand that boards have an important contribution to make in enhancing stability and equity in the production and marketing system for farm products, and in improving the operational and pricing efficiency of food markets. However, consumers argue that some boards have manifestly abused their market power, an action which is particularly intolerable and inflammatory in a period of shortages and rising prices. They suggest that boards should be more closely monitored and regulated and made more accountable; that representation on the boards should be widened to explicitly include representatives of consumer interests; and they demand an end to specific acts of particular boards which are inimical to the long-term interests of consumers. The outrage, indignation and vituperation with which these consumer views have been met to date is unworthy of our industry. A more adequate response to consumers' legitimate concerns is needed.

The debate on marketing boards is but the focal point of a third and wider issue of profound long term significance, namely the extent to which consumer interests are served by contemporary agricultural policies. Consumers are not convinced that the whole process of agricultural policy-making is conducive to an attack on their primary concern, rolling back inflationary trends in the food sector. Rightly or wrongly, consumers seem to have formed the view that agricultural policy is formulated primarily for farmers, behind closed doors, in a cosy conspiracy between representatives of organized agriculture and agribusiness and their patrons, Ministers <u>for</u> Agriculture and the apparatchiks of the Departments of Agriculture who identify the national interest with farmer interest. Consumers too often see themselves as the victims of farm programs, not the beneficiaries. They feel that consumer interests are characteristically downgraded or ignored in the formulation of agricultural policy. They know that they are not being systematically involved in policy decisions which affect their interests, and that they are rarely even consulted. Their experience has been that when organized consumers express what they feel to be their legitimate anxieties they have been at best ignored or patronized, and at worst abused, harrangued, insulted and intimidated. They are demanding that consumers be enlisted, informed, represented, and involved in the whole process of policy formulation, and that Canada develop a "comprehensive food policy" in which agricultural policy would be a part. More recently it has been observed that unless Departments of Agriculture take a less myopic view of their constituency and a less parochial view of their responsibilities, and unless there is a manifest tilt towards urban consumers' interests in the formulation of policy for the agricultural and food system, then at a minimum the influence of the Agricultural Departments will continue to be diluted by assertive departments of consumer affairs and consumer-oriented quasi public bodies, and at a maximum, that Departments of Agriculture will become socially dysfunctional and will cease to be a useful instrument of public policy.

This is a controversial note on which to end this introductory paper. But the maelstrom of inflation necessarily generates and invites radical ideas on social, political, and economic values, policies, and institutional arrangements. These issues, too, we must explore together.

I look forward with real pleasure to subsequent papers which will elaborate on some of these matters, and to the discussion.

INFLATION AND AGRICULTURE - CAUSE AND EFFECT

W. J. Anderson*

Two major questions related to inflation are:

i) how does inflation affect prices and incomes?

ii) where does one find the culprit?

I restrict the scope of this paper to examining how inflation affects agricultural prices and incomes, and to what extent agricultural prices and incomes and agricultural policies have inflationary effects.

Inflation refers to a situation characterized by a rising price level, that is, the average of all prices is increasing. The underlying causes of inflation are complex but in general inflation occurs when the growth in the supply of money and credit available for spending is greater than the growth in output of goods and services available domestically. Inflation induces intense economic activity because people not only earn more but they also spend faster to beat the declining purchasing power of their incomes.

People tend to forget in times of inflation, that deflation, which drives down the average of all prices over a period of time, can also occur. Deflation depressed economic activity and once in motion the depression feeds on itself; as money income declines production slows down and spending falls even more as people wait to purchase in expectation of further declines in prices.

People are ambivalent in their attitude toward inflation. They like the full employment and the increases in wages and net incomes that are associated with inflation but they dislike the price increases of the commodities they buy; they like inflation because it becomes easier to retire old debts but they don't like to pay the higher interest rates when they come to borrow. People are not ambivalent in their attitudes

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toward deflation. Except for those on fixed incomes or receiving contractual payments everyone dislikes deflation because in a period of deflation net incomes and output decline while unemployment increases.

The Great Depression of the 1930's was the last period of deflation; it was instrumental in bringing about a 22 percent reduction in the price level over the period 1929-33, the deflation also induced a great deal of unemployment which increased from 3 to 19 percent of the labor force 1929-33; and resource owners suffered large losses in net income and in capital values of land and other assets. Since the late 1930's the Canadian economy has experienced continual price inflation to some degree. In some periods the rate of inflation has come close to zero but in no period was there price deflation such as was experienced twice in the period between 1900 and 1933.

Quite apart from general inflation or deflation of the price level, prices of individual goods and services are continually changing in relation to each other. These changes are usually regarded as being part of the normal functioning of markets, the result of trading activity as buyers and sellers come to terms and prices are established which reflect the intensity of peoples' wants relative to the available supply of commodities and services. The pricing process in the market performs a key function in the economic system because it serves to translate consumers' wants for goods and services into price signals, which in turn provide decision-makers with the incentives to allocate resources where they can be used most profitably. The incentive derives from the fact that changes in the relative prices of goods and services shift the distribution of income among industries, sectors and individuals in the economy. The result is that some goods become more and others less profitable to produce; this provides the incentives to shift resources, which has the effect of changing the amounts produced of individual goods and services. Providing the incentive to allocate resources may be regarded as the normal function of markets.

The point to note is that the forces behind the relative price changes are fundamentally those of supply and demand for the individual commodity and are quite different than those macro forces such as interest rate, exchange rate and fiscal policies which generate the inflationary or deflationary type of price changes. Nevertheless inflation also induces changes in relative prices and income distribution because even though the forces of price inflation exert pressure on all prices individual prices may change at different rates because of the availability of supplies and because of existing contracts and other institutional reasons. The extreme cases are prices and incomes which are absolutely fixed, the most obvious being incomes derived from investments, for example, annuities.

Although price inflation has been a feature of the Canadian economy since 1933, during the past three years it has become a more prominent public issue because of the accelerated rate of inflation, from an annual rate of 2.5 percent per annum in 1971 to 10 percent in 1974. Moreover, this recent period of rapid inflation has been accompanied by unusually large price changes for certain commodities. In particular prices of the primary commodities, such as grains, oils and metals, have increased very much more than other prices. That is to say the Canadian economy, in the past 3 years, has experienced unusually large price changes emanating from two different sources, one of which is the inflationary type and the other is the force of demand and supply which affects commodity prices unevenly and produces relative price changes.

Tables 1 and 2, illustrate how this combination has affected agricultural prices and incomes. Table 1 demonstrates the effect on all prices of the period of moderate but continuous inflation 1961-71, which advanced the price level by 27 percent. Farm prices taken as a whole increased only 17 percent but as is often the case the average obscures too many differences to be very useful. Within this average farm prices for grain and eggs declined 16 percent, poultry prices gained 3 percent,

Table 1. CHANGES IN PRICE INDEXES, CANADA 1961-74

	(1) 1961 to 71	(2) 1971 to 72	(3) 1972 to 73	(4) 1973 to 74
	Change during the period or from previous year			
	%	%	%	%
General Index	27	3.5	5.6	10
Farm Prices	17	13	39	17
Grains	-16	0	96	38
Cattle & Hogs	28	19	35	0
Dairy	65	4.2	17	33
Poultry	3.3	10	37	11
Eggs	-16	13	54	13
Fruits	25	9	19	6
Vegetables	20	16	12	3
Farm Labour	78	7	13	15
Fertilizer	0	3.4	12	29
Feed	2.3	0	52	32
Petroleum	17	2.3	6.2	7
Farm Inputs	35	5.8	16	14

cattle and hog prices kept up with inflation, fruits and vegetables fell somewhat short, while dairy prices jumped well ahead at 65 percent.

The farm input price index went up faster than the general rate of inflation mainly because the labor index increased by 78 percent; feed and fertilizer prices hardly changed and the price of petroleum went up 17 percent. Within agriculture during the sixties and up to 1972 the combination of inflationary and other forces squeezed the profitability of crop enterprises, especially grain, but enhanced the profitability of livestock enterprises as grain costs declined.

The trend continues into the next year; from 1971 to 1972 all farm prices except grains, which did not increase, advanced faster than the rate of inflation and the price index of farm inputs. After 1972 the situation changed drastically. The price level of every group of farms products advanced faster than the general rate of inflation but grain prices more than doubled. Thus while livestock prices increased more than the rate of inflation the profit in livestock enterprises was wiped out by the exceptionally large increase in grain and other feed prices.

Table 2 shows that during the 1960's and up to 1972, farm net income advanced sufficiently so that real net income in the farm sector remained approximately constant. Real estate value increased by 100 percent so that even allowing for an inflow of new capital invested in buildings and land improvements the increase represents a substantial transfer of real asset value to the farm sector. The price changes in Table 1, however, indicate that a substantial income transfer took place within agriculture from grain to livestock enterprises during the 1960's and up to 1972. Since 1972 agriculture has acquired a major transfer of real income and a further increase of 25 percent in real estate value (Table 2). Within agriculture there has been a major income transfer to grain enterprises from livestock enterprises as well as from overseas sales. Given the location of farm production in Canada this shift of income to grain enterprises also caused a major regional shift of income to the Prairie Region. Net income of farm operators in the Prairie Region doubled from 1972 to 1973 and increased another 50 percent from 1973 to 1974.

The changes in farm prices which have caused these major transfers of income into agriculture and within agriculture, have come about quite independently of the inflationary forces which are at work. However popular opinion, by associating any price change with inflation tends to identify incorrectly the changes in prices of primary products as the cause of inflation. Observing the very large relative price changes as

Table 2. REAL ESTATE VALUES AND NET INCOMES, FARM SECTOR CANADA AND REGIONS, 1960-1974

	Value Real Estate Canada	Net Income					
		Canada	Maritimes	Quebec	Ontario	Prairie	B.C.
	$ billion			$ million			
1960	8.2	1,196	53	150	292	640	60
1961	8.6	922	41	157	309	353	62
1962	9.0	1,526	36	162	348	910	69
1963	9.6	1,521	38	142	314	957	69
1964	10.5	1,292	45	128	301	747	71
1965	11.8	1,567	56	142	340	958	70
1966	13.1	1,949	56	222	468	1,120	84
1967	14.8	1,475	32	188	379	792	83
1968	16.3	1,710	39	198	390	987	96
1969	16.6	1,564	42	213	427	803	79
1970	16.7	1,405	58	233	445	583	86
1971	16.9	1,651	37	200	394	934	86
1972	17.4	1,846	54	262	512	928	90
1973	20.3	3,344	103	356	704	2,046	135
1974		4,556	108	379	810	3,134	125

compared with the rate of inflation suggests that the impact of inflation on agriculture has been rather small, in fact is almost lost in the impact on agriculture of changes in relative prices that have occurred.

The second question referred to at the beginning of the paper was to what extent agricultural income, prices and policies have had inflationary effects. If price changes or policies increase income to agriculture without reducing income somewhere else in the economy the effect will be inflationary. Let us test the agricultural income increases and agricultural policies on this basis.

Subsidies - Farmers receive a number of subsidy payments under various programs; examples are, dairy support, grassland incentive, vendor grants under Small Farm Development. Subsidies shift some of the cost from consumers to the public treasury and add to producers' incomes. To the extent that they add to disposable income without compensatory taxes subsidies are inflationary. Because farm subsidies are small in relation to the Federal budget it seems reasonable to conclude that they are almost pure income transfers within the economy with little inflationary impact.

Income and Payments in International Trade - The increase in the prices of food commodities and farm inputs which are imported have an anti-inflationary effect because purchasing power is drawn out of the country unless the additional expenditures on imports are offset directly by an increase in export sales revenue. In the short-run this offset is not likely to occur and therefore rises in prices of imported food or farm inputs have anti-inflationary effects by reducing income available for purchasing other goods and services. Some groups of course are adversely affected.

An increase occurring in the price of an exported farm commodity will be reflected in a higher domestic price except where special provision is made to keep down prices for domestic usage, e.g., wheat. Such a price increase provides farmers with additional disposable income which is inflationary because the additional income originating from exports is unlikely to be offset in the short-run by exporting the purchasing power to purchase additional imports. For that reason increases in export prices received by farmers over the past 3 years have been inflationary because they have resulted in net additions to domestic disposable income. Conversely a relatively decreasing export price is likely to be anti-inflationary. Throughout the 1960's prices of farm exports were rising more slowly than the general level of prices. This squeezed farm income and therefore had a moderating effect on the general price inflation which was proceeding in that period but the cost was borne by farmers.

The foregoing effects presume a delayed reaction in exchange rate adjustments, and in the flow of capital, and of imports.

Lending - Farm credit is extended to agriculture by various agencies at concessional rates of interest. Lending by Farm Credit Corporation alone increased threefold ($109 to $335 million) from 1971 to 1973 with estimated lending in 1974 amounting to $400 - $430 million. Such a lending policy has an inflationary impact by providing additional purchasing power on favorable terms. The credit policy also facilitates and speeds up the capitalization of high prices into high land values which in turn require larger loans to finance.

Research and Development - The objective of research is to increase the productivity of farm resources and the output per acre and per animal unit. Any resulting expansion of output tends to reduce the price of the product, if it is not an exported commodity, which releases some consumer income for other expenditures. The inflationary effect of this discretionary income is offset by the increased amount of real goods available as a result of the increase in output and the release of resources for other production due to the increase in productivity. On the other hand, if the product is exported the savings in resources as a result of increased productivity benefits producers by increasing net incomes but does not benefit consumers by lowering the price of the product. Research and development occur gradually so that new income from exports tends to generate offsetting expenditures on imports, and resources released provide more goods and services; both effects are anti-inflationary.

Marketing Boards - A major thrust in agricultural policy has been to permit farmers to form marketing boards to enhance their bargain ing power, thereby increasing the prices received for their products. If effective in raising prices marketing boards transfer income to farmers but the purchasing power which is transferred to farmers reduces the purchasing power of consumers or the marketing sector, thereby neutralizing any inflationary impact on price level of the increase in purchasing power in the hands of farmers. To the extent that boards have improved marketing efficiency they have had an anti-inflationary effect.

Stabilization - Stabilization programs have been designed to counter the price cycles in farm produced commodities. These price cycles do not coincide closely with the trends in the general price level. Therefore agricultural commodity price cycles may at times reinforce the trend in the general price level and at times counter it. Stabilization programs, therefore, reduce whatever the reinforcing or countering effect would have been. However as an inflationary force stabilization programs are neutral because the significant impact of price cycles is to cause income to be transferred back and forth between producers and between producers and consumers, which is neutral in either producing or countering inflationary trends in the economy. Stabilization programs merely reduce the amount of these shifts in income.

INFLATION AND FINANCING THE FAMILY FARM

Richard L. Trimble*

The life cycle of a typical family farm can be described in various ways, but for purposes of this discussion I would like to divide the cycle into three major stages. These are:

1. Getting started in farming.
2. Expanding to the position of having established a viable, ongoing commercial operation.
3. Consolidating the operation and planning for retirement and the transferring of the farm to the next generation. This is the final stage in the life cycle of the family farm. At this point the farm is transferred to a beginning farmer and the cycle is started again.

Inflation has an impact on the financing of a farm in all stages of the family farm cycle but its impact and the financial problems it creates for the farmer depend to some extent on the stage he is in the cycle. Now, let us examine the major financial problems inflation can create in each of these stages.

The Beginning Farmer

How does a young man get started in farming? The process used to be described as the "agricultural ladder". The new farmer would begin as a hired worker then proceed to accumulate some operating equipment and other assets. He would then progress to the point of renting some land to farm on his own. Gradually this farmer would proceed to buy some land and become an owner-operator.

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Today, the agricultural ladder has changed to some extent. A new farmer seldom goes through the hired man stage. He may start by renting some land or working out an agreement with his father to share some operating assets. But the new farmer of today still has a strong desire to own the land he works just as his father and his grandfather did. This desire to buy land is where inflation causes financial problems for the beginning farmer.

The Problem of Buying Land

What has happened to the price of land in the past few years? Figure 1 shows the index of per acre land prices for Canada and Ontario over the past five years. The Consumer Price Index (CPI) is included for purposes of comparison. Between 1968 and 1973, the CPI increased some 25 percent. During the same period, the price per acre of land in Canada increased 15 percent. But Ontario land prices increased by almost 70 percent. This rapid increase in the price of Ontario land can be attributed in part to the increase in agricultural product prices but the urban or speculative influence has also had a profound impact.

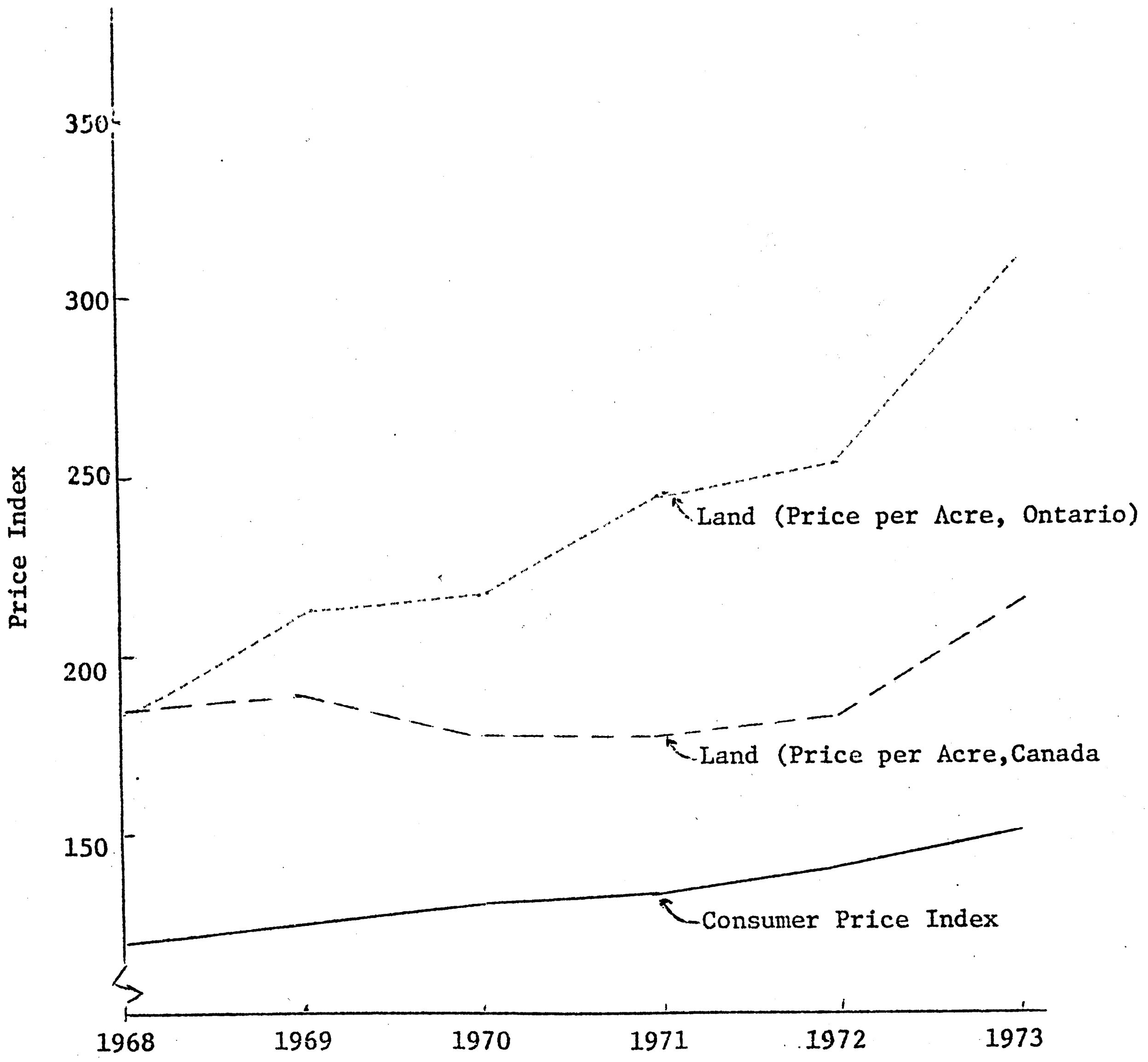
Many people seem to be quite concerned about inflation as measured by the change in the CPI. But, consider the young person that wants to get into farming today. For example, land that was selling for $600 per acre in 1968 would cost over $1,000 today. At this price the young farmer who wanted to own a 200-acre farm today (the average size of an Ontario commercial far was 196 acres in 1971) would require $200,000 just to buy the land.

Financing the Land Purchase

How does the beginning farmer finance such a capital purchase? What does it cost him for interest? As capital requirements in agriculture go up, farmers are relying on debt capital to an ever increasing extent. Therefore to finance the land purchase, the young farmer would likely

Figure 1. Price Indexes

(1961 = 100)



Source: Statistics Canada

attempt to find a source of long-term real estate credit.

The increase in long-term farm credit outstanding over the past few years is shown in Figure 2. The total long-term farm credit outstanding in Canada has gone from .8 billion dollars in 1963 to just over 2.1 billion dollars in 1973. This is an increase of 180 percent.

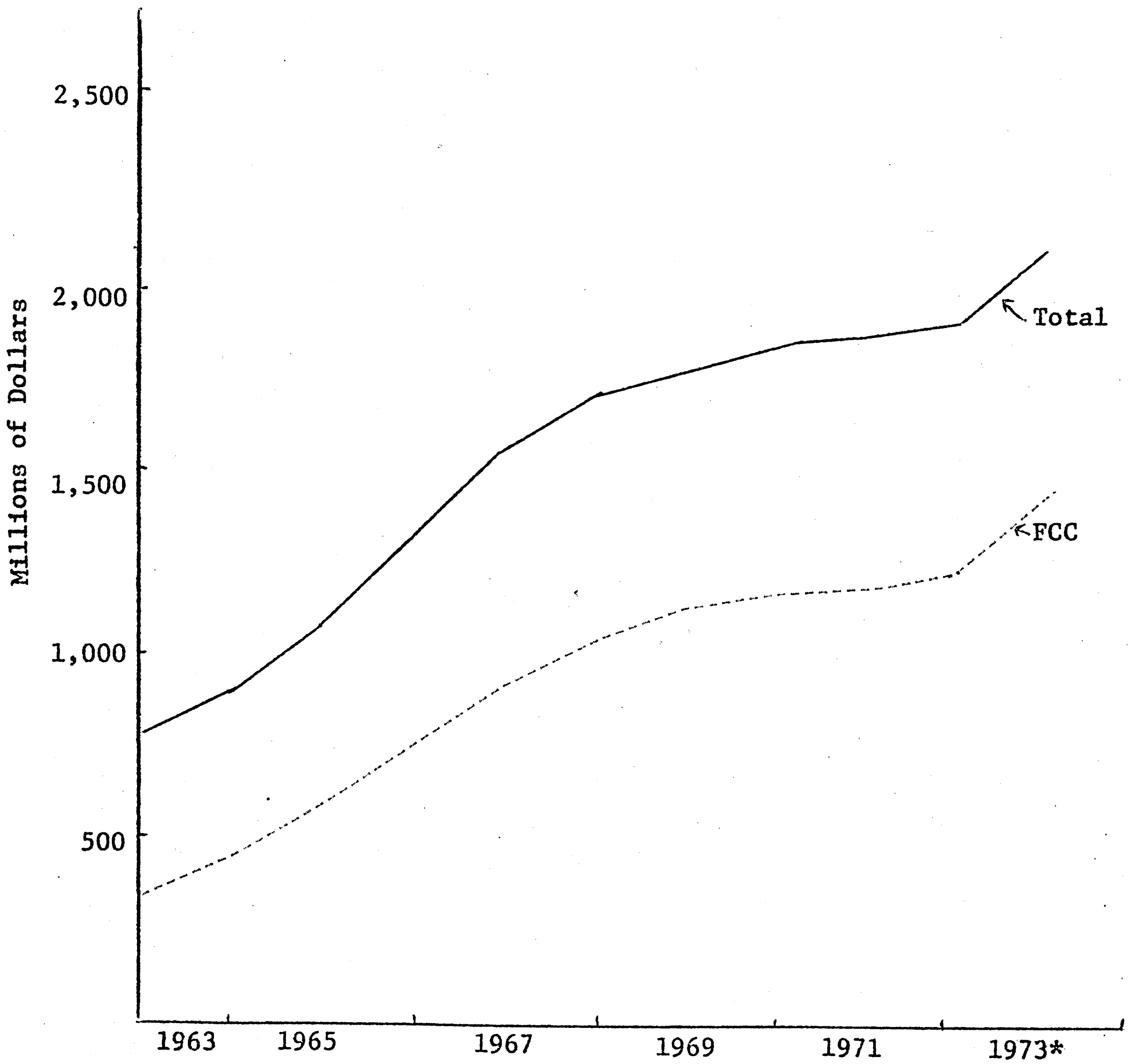
The major supplier of long-term credit is the Farm Credit Corporation (FCC). As indicated in Figure 2, this agency has increased its committment to agriculture from 45 percent of the total long-term farm credit outstanding in 1963 to 65 percent in 1973. Thus, we have seen evidence of an ever-increasing use of long-term credit by farmers.

But, what does this credit cost today? If the young farmer applies to FCC for a real estate loan and succeeds in getting it, he gets a break on the interest cost. The cost of providing credit to the farmer is subsidized by the government so the interest charged by FCC is somewhat less than the going market rate. The historical pattern of interest rates on FCC loans is shown in Figure 3. The interest charged by FCC has ranged between six and nine percent and was 8.25 percent as of September 30, 1974. So it appears that while the farmer just starting out will have to pay considerably more for his land today, he can get his credit at a relatively reasonable cost. But, that is not the whole story.

The next difficulty the young man encounters is the limit of $100,000 on the amount of the loan he can obtain from the FCC. Thus, while our beginning farmer might qualify for credit from FCC at a rather low cost, he can get only one-half of what he needs to buy the land. Even if he had $50,000 in equity, where can he get the remaining $50,000? This might be the most difficult problem facing the beginning farmer, i.e., where to obtain the rest of his long-term credit requirements.

The sources often used in such circumstances are private individuals such as relatives or the seller of the land. There are also other institutional sources which are used to some extent such as the Veterans Land Act,

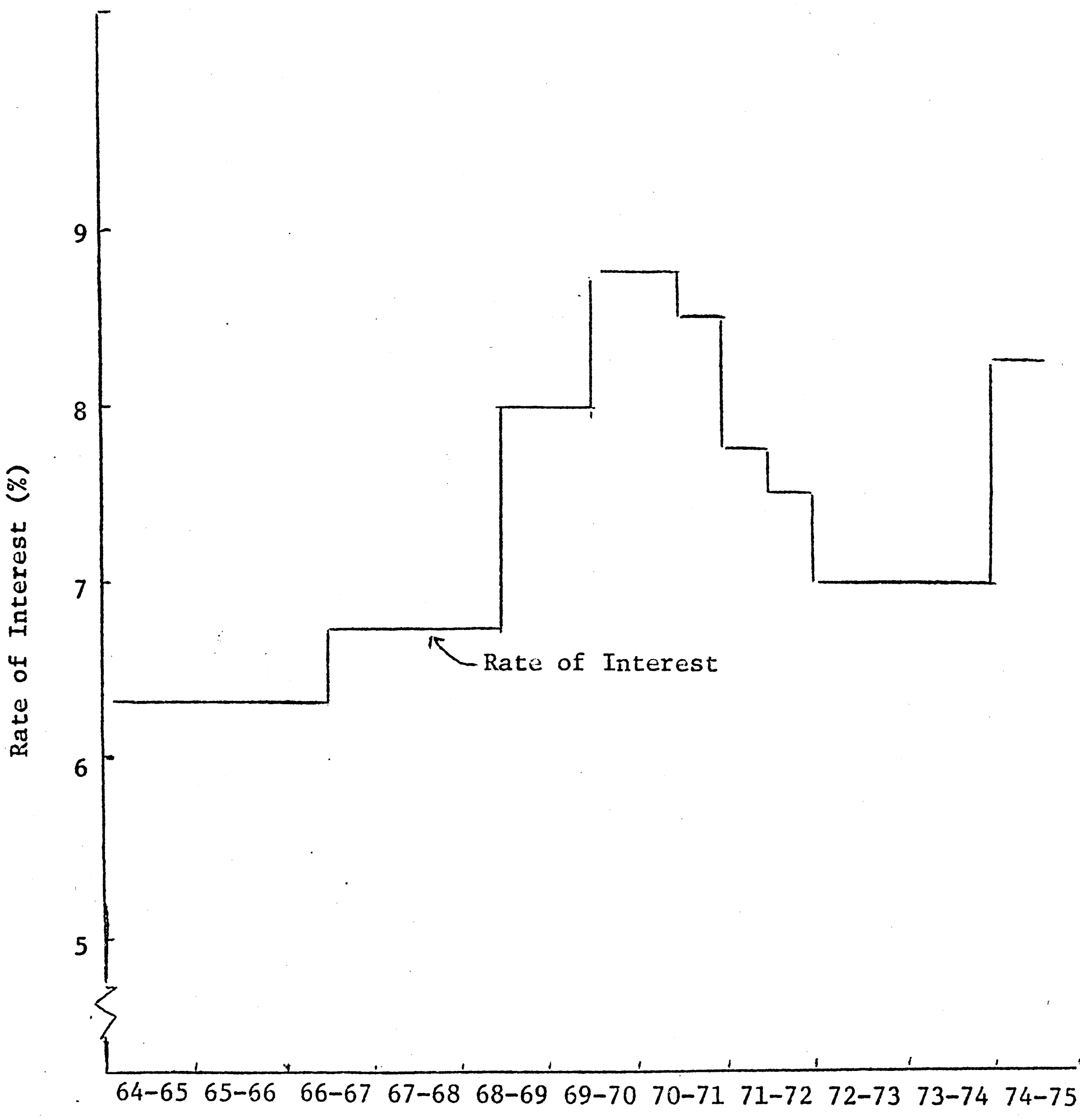
Figure 2. Estimated Long-Term Farm Credit Outstanding Canada 1963 to 1973



* Preliminary Estimate

Source: R. S. Rust, Canadian Farm Economics, various dates and personal consultation.

Figure 3. Farm Credit Corporation Interest Rates 1964 to 1974



Source: Farm Credit Corporation

provincial government agencies, and others. But there are not many choices beyond FCC and that is the unfortunate position in which many young beginning farmers find themselves.

If the young farmer is able to finance the land purchase and enter farming, he can look forward to further problems created by inflation. These are the problems of financing the other operating inputs and meeting the debt repayment requirements that each of these financial committments carry. He has entered the established farmer stage of the life cycle of the family farm.

Inflation and The Established Farmer

As I have defined the family farm life cycle, the next stage involves the farmer who has been in agriculture for a number of years. He has a viable commercial operation and has acquired a sufficient land base. He may still be growing or have growth objectives, but his major concern is the efficiency and profitability of the existing operation. Land acquisition and the financial problems it creates are not a major concern to this farmer. But this is not to say that the price of land is not an important consideration to the established farmer for he must consider the concept of opportunity cost.

The Opportunity Cost of Land

If the price of the land the established farmer owns has increased over time from $600 to $1200 per acre, then his opportunity costs have increased. The farmer could sell his land and invest the proceeds in a savings account earning for example, eight percent (an opportunity he forgoes if he leaves his funds invested in land). Therefore, the return which the land must earn per year for the farmer to keep his capital invested in land has gone from $48.00 to $96.00 per acre; a substantial increase. If one were to budget through the cost of an acre of corn on this basis, one could quickly see how an increase in the opportunity cost of land due to an upward surge in the price of land could affect the analysis.

The major difficulty with this analysis is trying to convince an established farmer that this is in fact the case. The fact that the price of the land he owns has gone up does not really concern the owner in many cases. He sees it as an increase in the value of his assets and is quite pleased about it. The reason he feels as he does is simply because he does not have to lay out the hard cash to pay for the increased value of his assets. Thus, it is not recognized as a problem by the established farmer.

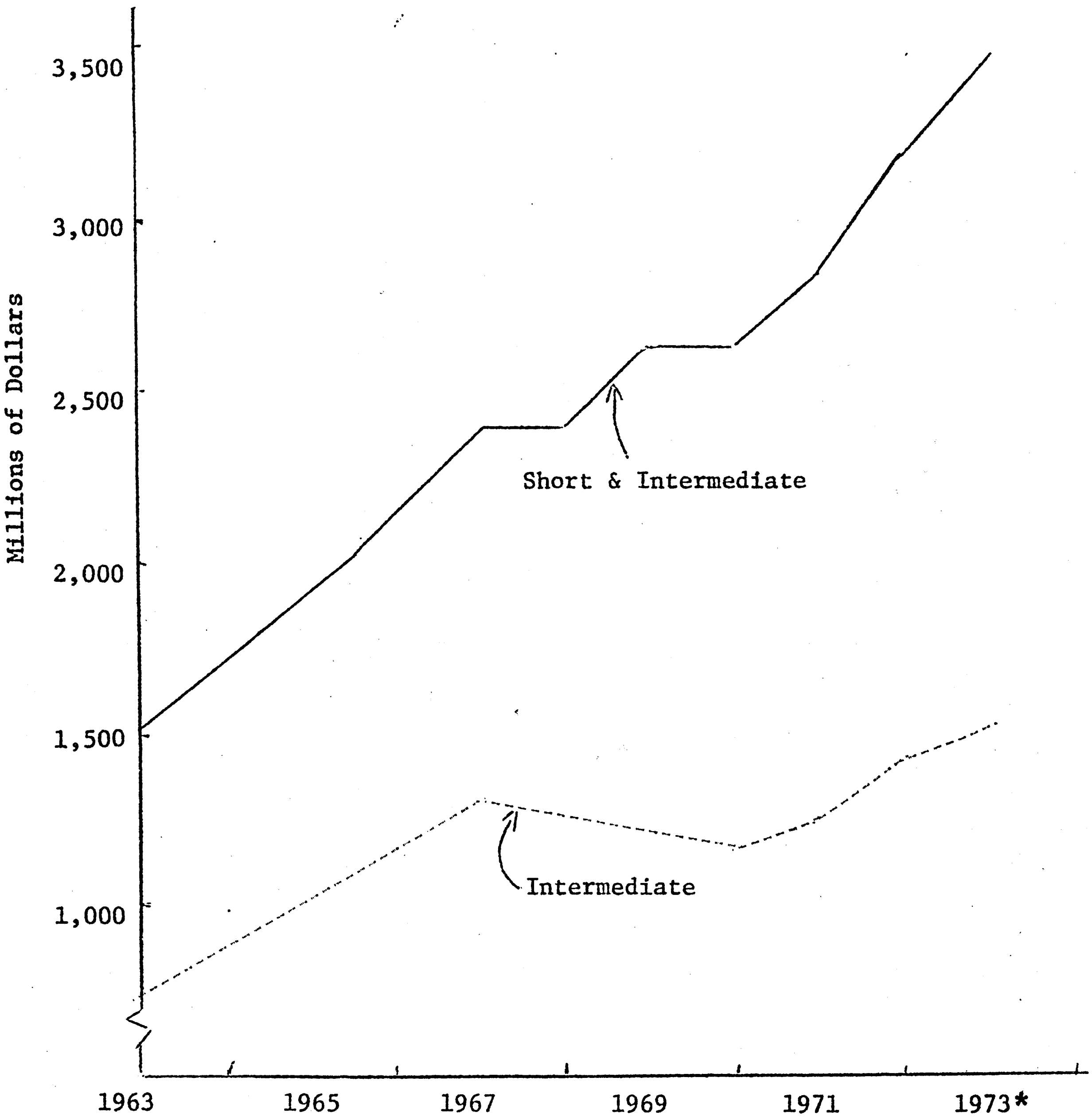
Financing the Purchase of Operating Inputs

What the farmer in this stage of the life cycle of the family farm does see as a real problem is the increase in the price of productive inputs he must buy on a recurring basis. The cost of feed, fertilizer, petroleum, machinery, and equipment and repairs, have increased dramatically. The farmer must pay cash for these higher priced productive inputs. Therefore, he immediately sees this effect of inflation and the problems of trying to finance these higher costs of production. Also, this farmer faces the higher cost of living as does everyone. As a result, he sees ever-increasing drains on his cash flow to meet operating and living expenses with smaller amounts left for savings and reinvestment.

The past year or two have been very good years for farmers. Most farmers, except livestock producers, have had substantial increases in both gross and net incomes in spite of increasing costs of production. But to finance these higher production costs farmers have had to increase their use of short and intermediate-term credit for operating purposes. This is reflected in the increased short and intermediate-term credit outstanding as shown in Figure 4.

The total short and intermediate-term credit (or operating credit for lack of a better term) has gone from 1.5 billion dollars in 1963 to

Figure 4. Estimated Short and Intermediate-Term Farm Credit Outstanding, Canada, 1963 - 1973



* Preliminary Estimate

Source: R.S.Rust, Canadian Farm Economics, various dates and personal consultation.

almost 3.5 billion dollars in 1973; an increase of 130 percent. The increase in short-term credit outstanding, which is used primarily to finance annual operating costs, has been even more dramatic. It has increased 150 percent, going from .7 billion dollars to 1.9 billion dollars.

These statistics indicate the nature of the problem which inflation creates for the established farm operator. To finance the increased costs of production, farmers have increased their use of short and intermediate-term credit. But that is not the end of the difficulties for the established farmer. There are two additional points that must be considered.

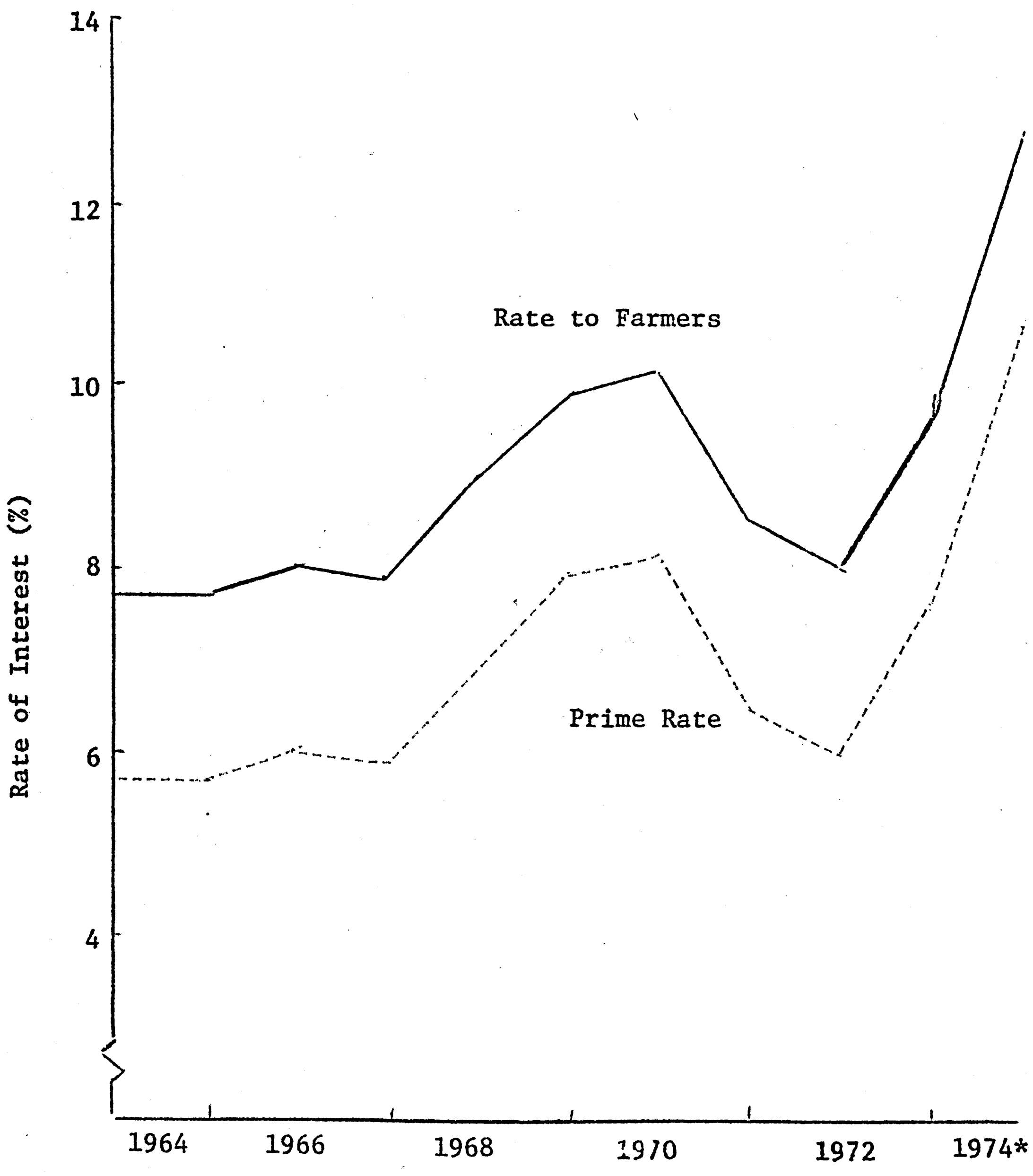
The Cost of Credit

Unlike the case of long-term farm credit, a governmental agency is not the major supplier of short and intermediate-term credit to agriculture. The major source of such credit is the chartered banks, and banks typically do not subsidize credit to farmers except in the case of loans made under the provisions of the Farm Improvement Loans Act. Farmers pay the going market rate for short-term credit.

It is difficult to determine the rate of interest banks charge farmers on short-term credit, but the best estimates put it at 1½ to 2½ percent above a bank's prime rate. Figure 5 indicates how the prime rate has changed over the past 10 years and how this would relate to a rate charged farmers that was two percent above the prime rate. There have been startling increases in these rates in the past year.

Thus, the established farmer is not only borrowing short-term funds at a record pace, but he is also paying dearly for the use of this credit. Increased production costs have resulted in the increased use of credit and government monetary policy to fight inflation has resulted in the higher cost of credit. Hence, there can be little doubt as to the effect inflation has had on the family farm in this stage of the life cycle.

Figure 5. Interest Rate Charged by Chartered Banks, Canada, 1964 to 1974



* First 10 months only

Source: Bank of Canada Review

But, a more critical issue is - What may happen in the future?

Repayment Problems

Farmers have received strong signals to increase production in the form of record high product prices. They have been and continue to buy productive inputs at record high prices to gear up and produce. To finance these increased costs, farmers have increased their use of debt capital a great deal. What happens if product prices take a sharp drop due to good world-wide weather and crop harvests next year? They may face a situation in which product prices, gross farm receipts, and cash inflows are substantially reduced. We could see a resumption of the all too familiar cost-price squeeze situation in which farmers find themselves hard pressed to meet fixed debt repayment committments. Hence, in addition to creating financial problems for the established farmer; inflation has added uncertainty to an already uncertain economic environment created by weather, unstable foreign demand and many other factors.

Thus far, I have painted a very bleak picture concerning the effect which inflation has on financing the family farm. But, there may be one bright spot. This involves the effect which inflation has on the farmer that has achieved his growth objectives and is in the consolidation stage. His goals are somewhat different than farmers in the other stages of the family farm cycle. He is looking to retirement and the relaxation and enjoyment that he has worked so long and hard for. Also, he is likely thinking about transferring his farming operation to his heirs in some form.

Inflation and The Retiring Farmer

Inflation has a major impact on the retiring farmer in two ways. First it has a bearing on the timing of his retirement and how he disposes of his assets. Secondly it has an influence on the adequacy of his income after he retires. Obviously those two considerations are related.

Preparing for Retirement

First, let us look at what might prove to be a bright spot concerning inflation and financing the family farm. How do farmers prepare for retirement? The most common method is savings in the form of reinvestment in the farming operation. Rather than making off-farm investments, farmers simply continue to plow money back into their operation. Recently this has been quite beneficial to retiring farmers. Not only have they continued to accumulate a farm of greater physical size, but of much greater monetary value due to the rate of inflation of land values. Thus, the vexing problems which inflation has created for the young beginning farmers have proven to be a windfall gain for retiring farmers. Thus, inflation may prove beneficial for those farmers looking to sell their operations and retire if they can time their sale to take advantage of inflation.

But, there are difficulties that arise as a result of this seemingly beneficial aspect of inflation for the retiring farmer. These problems involve various taxes levied by both federal and some provincial governments that are of particular importance when the farmer retires. These are the federal tax on capital gains and the provincial gift tax and succession duties.

At retirement, when the farmer wants to take his capital out of the operation or begin transferring some of the assets to his family these taxes become of particular importance. Inflation has increased the value of his farming assets, but government demands its share and these demands are quite progressive in nature.

When the farmer retires he has three options:

1) Sell his assets and keep the proceeds.
2) Give the assets away before death.
3) Keep his assets until he dies and then will them to his heirs.

If he sells his farm assets, the capital gains tax applies. The gift tax applies if he gives them away. If they are transferred to heirs at death, succession duties apply. It seems the only way to avoid giving the government its share is to "take your assets with you".

Tables 1 and 2 set out the basic rates of taxation for the Ontario gift tax and succession duties. These tables show how the government benefits from inflation just as does the retiring farmer. As asset values go up, the rate of taxation also goes up. For example, if a farmer gave away 100 acres of land today valued at $500 per acre, the gift tax would amount to $8,750. If he delayed this gift and the price went up to $1,000 per acre, the gift tax would be $22,500. The government of Ontario is $13,750 richer as a result of nothing but inflation. Therefore, the farmer has realized only $36,250 of the gain from inflation.

The process is similar for succession duties and the federal capital gains tax. As asset values increase, the rates of taxation are fixed and the government's windfall gain from inflation continually increases at an increasing rate. This might explain why governments have so much difficulty fighting inflation. If they stop inflation they also stop the increase in tax revenues due to inflation.

In fairness to those people who write our tax laws, they have recognized this difficulty. The federal government has introduced the idea of indexing the rate of taxation on income based on the rate of inflation. This will help to reduce the capital gains tax since it is based on the income tax rate.

The federal government has also made provisions for the deferral of the capital gains tax on most farm assets transferred to family members through the "rollover" provision. The provincial government has also recognized the effect inflation has on farmers and has made succession duties on some farm assets forgivable over 25 years if the assets stay in the family and agriculture over the period. It has also increased the amount of some exemptions which are available in the case of succession duties.

Table 1. Gift Tax Rates

Amount of Gift	Tax Rate
$ 0 - $ 25,000	15% on first $25,000
$ 25,001 - $ 50,000	$ 3,750 + 20% on next $ 25,000
$ 50,001 - $ 75,000	$ 8,750 + 25% on next $ 25,000
$ 75,001 - $100,000	$15,000 + 30% on next $ 25,000
$100,001 - $125,000	$22,500 + 35% on next $ 25,000
$125,001 - $150,000	$31,250 + 40% on next $ 25,000
$150,001 - $200,000	$41,250 + 45% on next $ 50,000
$200,001 -	$63,750 + 50% on excess over $200,000

Source: Ontario Succession Duty and Gift Tax Legislation

Table 2. Succession Duties*

Size of Estate	Tax Rate	
	Preferred Beneficiaries	Collateral Beneficiaries
$150,000	11%	25%
$200,000	12%	26%
$300,000	13%	27%
$500,000	15%	29%

* Selected Rates only. For complete list, see source.

Source: Ontario Succession Duty and Gift Tax Legislation.

This short discussion of the problems which inflation creates for the farmer who is planning his retirement is far from complete. But, it does show that inflation may not be quite as beneficial for the retiring farmer as some may think. While there are numerous ways of deferring or reducing the taxes paid by the retiring farmer through various means which have not been mentioned here, governments have structured their rules so that they will get their "fair share". This simply means that farmers must manage their assets more carefully and minimize the impact of such taxes. This will help insure a retirement fund that is sufficient to allow a farmer and his family the ability to enjoy their retirement years.

Inflation and The Retirement Years

This brings us to the second major problem which inflation creates for the retiring farmer or any other person who is retiring. What will happen to the cost of living in the future? Will the retiring farmer be able to pay for the higher cost of living? How much of a retirement fund is needed to support the farmer and his family throughout retirement?

The answer to these questions depends on a number of things. What will the rate of inflation be in the future? What level of living does the retiring farmer want to maintain? How long will the farmer and his dependents live? What other sources and amounts of retirement income does the farmer have? Answers to these questions are needed to provide a reliable estimate of the retirement fund needed by the farmer.

Let us look at a very simple example of the effect inflation has on the cost of living. If inflation were to continue at a 10 percent rate for 15 years, the purchasing power of the dollar would fall to 24 cents. This means that it would take about four times as many dollars in 1990 to buy the same items that a dollar will purchase today. Thus, if it costs the farmer $10,000 a year to live today, it would cost $40,000 in 1990. This is not a very pleasant thought but it illustrates the devastating effect which inflation has on people living on fixed incomes.

Therefore, while inflation may prove beneficial to the farmer before he retires, these benefits may be more than wiped out due to the increased cost of living during retirement. One method of combating this problem is not to retire quite as early as one might desire.

The farmer can then obtain the higher income from his operation for these added years. His farm assets may also increase in value even further giving him a good hedge against inflation and a greater retirement fund. Also, he has decreased the number of years which he must live on his fixed retirement income. I am not advocating this method but it is one that many workers, not just farmers, may be adopting.

The result of this method of solving the retirement problem is, that the young farmer cannot enter agriculture as soon. He must wait the additional years by which the older farmer has deferred his retirement. Also, it will cost the younger farmer more to get into farming due to inflation in the value of the retiring farmer's assets.

Thus, we have come full circle in our look at inflation and financing the family farm. We have looked at the full life cycle of the family farm and some of the financial problems inflation can create for farmers in each stage of the life cycle. But, little has been said concerning methods of solving these financial problems. Let us look very briefly at a general method of attacking the financial problems which inflation creates for farmers.

Conclusions

There are no quick or easy solutions. The young farmer wants to know if now is a good time to buy high priced land and get into farming. The established farmer wants to know if he should go ahead and buy more high priced operating inputs and tool up to produce more next year. The older farmer wonders if now is the time to sell out and retire. What all of these farmers have in common is a real concern about what will happen in the future and how it will affect them and their families.

The uncertainty which inflation has created is a common concern.

How can one deal with this uncertain environment? Despite all the uncertainties, careful budgeting and planning is the best method of attacking the situation. Some may think that this is useless advice, when it is so difficult to estimate the prices or costs that should be used in a budget or planning model for next year, let alone anytime thereafter. This suggests one should try more than one estimate and see how the different prices affect the analysis. What minimum output price will generate sufficient cash flows to meet operating expenses, make required debt repayments and leave enough for the family to live on for the year? What is the likelihood that the prices will fall below or costs rise above the estimates used? What do other experts or advisers feel will happen to these prices and costs?

Budgeting and planning to improve decisions is not useless. Given the record high level of product prices, the margin for error in a budgeting analysis is much greater than it used to be because prices can fall much further. Therefore, good management and planning is even more critical today than ever before simply because errors can be so much more costly.

Also, the farm manager of today should look at various methods of removing some of the uncertainties which he faces. Since the major uncertainty involves prices and costs, he would want to consider methods of removing these uncertainties such as hedging, forward contracting and insurance. If the family farm manager combines some of these methods of removing uncertainty with careful planning and budgeting analysis, he should be in a position to protect himself from the problems inflation has created.

INFLATION AND AGRICULTURAL TRADE POLICIES

R. E. Latimer*

The international trading system is today faced with a combination of circumstances that could not have been envisaged even two or three years ago. Rapid increase in prices for many key commodities have brought about distortions and some serious balance of payments strains. These price increases have aggravated inflationary pressures. These increases in price have been due to a combination of factors including reduced crops for many basic agricultural commodities, increasing demand for limited supplies of both agricultural and industrial products, and, in the case of oil and to some extent coffee, producer cartel action. In the past two years the export price for Canadian wheat has increased over 300% to more than $6.00 per bushel. The price of oil on world markets has increased to over $11.00 per barrel, roughly four times greater than it was two years ago and the price of sugar has risen over 600% since the end of 1973.

These developments have put pressure on countries to take trade restrictive measures. However, there has been a determination, through co-operative action, to resist beggar your neighbour policies. In June 1974, the OECD countries adopted a "trade pledge" not to introduce import restrictions to deal with balance of payments problems arising out of the international oil situation. With the passage of the U.S.A. Trade Bill on December 20, 1974, the GATT multilateral trade negotiations can now begin in earnest to examine some of the more fundamental problems affecting the international trading environment.

Before examining some of Canada's trade policy interests in agriculture, it would be useful to review the basis of Canada's agricultural trade relations.

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The Basis of Canada's Agricultural Trade Relations

Canada's agricultural productive capability for many products is well in excess of domestic demand. Therefore, exports are of fundamental importance to the industry. In 1973 exports of agricultural products from Canada exceeded $3 billion, accounting for over 40% of farm cash receipts. Further, as an indication of the agricultural industry's contribution to the total economy, the positive agricultural trade balance in 1973, of approximately $850 million, accounted for more than 60% of Canada's overall trade balance. While the majority of these exports were in the wheat, feedgrains and oilseed sectors (approximately $1.6 billion in 1973), Canada is also an important exporter of a wide range of other farm products.

Canada is also a major importer of a broad range of agricultural commodities which are either not produced in Canada or which, while grown domestically, are imported on a seasonal or year-round basis to supplement domestic production on a regional or national scale. Major Canadian agricultural imports would include certain meats and other animal products, fruits, nuts, vegetables, sugar and other tropical crops. Total agricultural imports in 1973 exceeded $2 billion.

Most of Canada's trade takes place under the contractual provisions of the General Agreement on Tariffs and Trade (GATT) through which rules and procedures governing international trade have been established, and under which tariff and non-tariff barriers to trade are negotiated. The GATT contributes to stability in international trade relations by providing a forum for the discussion and resolution of particular trade problems and has provided in six "rounds" of multilateral negotiations, substantial liberalization of trade. However, in marked contrast to the significant reductions in trade barriers against industrial products in the post-war period, little progress has been made towards dealing with the impediments to trade in agricultural products.

In fact, some GATT articles provide for certain conditional exceptions for agricultural products. The use of import quotas are prohibited under GATT Article XI. Such restrictions are permitted on any agricultural or fisheries product, however, if the restrictions are required for the operation of government measures designed to restrict the production or marketing of the product domestically. Therefore, import action may be taken on an agricultural product if it is to support an effective domestic supply management program. Even under such circumstances, however, imports cannot be prohibited entirely but must be allowed to enter in the same proportion to domestic production as might reasonably be expected to prevail in the absence of restrictions.

The GATT also makes special provision for the use of export subsidies on some agricultural products. Under the provisions of GATT Article XVI, the use of export subsidies are prohibited on manufactured products but may be used on the export of all primary products to the extent that these exports do not result in the exporting country obtaining more than its traditional share of world export trade in the product.

Over the years, most countries have increased their assistance to farmers through some form of price or income support in order to achieve certain domestic, social, economic and political objectives. Such assistance often leads to placing barriers against imports and subsidizing exports of surplus production. The current situation in some of our key markets can be briefly set out as follows:

1. U.S.A.

   Both Canada and the Untied States are each others' largest agricultural trading partners. In 1973, Canada's exports of agricultural products to the U.S. totalled about $550 million, or 17% of our total agricultural exports. In 1970, there were over 170 U.S. agricultural tariff items where Canada was either the principal supplier or had a substantial interest. In the same year, Canada imported $1.2 billion from the U.S., accounting for over half of our total agricultural imports.

In 1955, the GATT granted a waiver to the U.S. to apply import quotas, which would otherwise be unjustifiable under GATT, in order to conform with the provisions of Section 22 of the U.S. Agricultural Adjustment Act. Canada voted against that waiver. Under the waiver, the U.S. has applied quotas on a range of agricultural commodities including wheat, wheat products, butter, cheddar cheese and certain other dairy products and to certain feedgrains.

Recent commodity shortages have resulted in enlargement of these quotas. Further, at least in principle, the U.S. has, in more recent years, been moving away from special measures of protection and relying more on market forces to determine production and distribution patterns. At the same time, there is some evidence that the U.S. may be prepared to take a more pragmatic approach to international commodity arrangements. The U.S. may now be willing to consider the negotiation of international commodity arrangements designed to stabilize international agricultural markets and, at the same time, improve access for agricultural products.

2. <u>The EEC</u>

The EEC, and particularly France, has long claimed that the Common Agricultural Policy (CAP) is the cornerstone of Community integration. The CAP, which was formally instituted in 1961, covers 90% of EEC agricultural production and relies heavily on a system of variable levies to sustain domestic agricultural prices. The EEC has argued that this new form of protection is consistent with GATT. At the same time, the EEC maintains a system of export restitutions designed to allow EEC producers to compete in export markets. The use of export subsidies on agricultural products by the EEC and the U.S. have been particularly damaging to Canadian exports of wheat, flour and barley.

In terms of recent trade policy, the EEC focus continues to be on market stability. The EEC has proposed, as the best way of achieving this, the negotiation of international commodity arrangements for products such as cereals and rice, dairy and sugar. In developing a position for the multilateral trade negotiations, the EEC has stated that to the extent world market stability is achieved through these arrangements, the EEC import regime could be adapted accordingly.

3. Japan

The Japanese agricultural industry is highly protected both by tariffs, quantitative restrictions and the state trading practices of the Japanese Food Agency. Over 50% of Canadian agricultural exports to Japan must overcome tariffs greater than 10%, including tariffs of 355% on unmanufactured tobacco, and over 100% on liquor. In addition, many of the Japanese tariffs on agricultural and food products are not bound under the GATT. This means that Japan may changes its tariff rates on these products in accordance with changes in international markets, and to the detriment of agricultural exporters.

The cumulative effect of these policies of restricted access to key markets and the widespread use of export subsidies were major factors behind the build-up of burdensome stocks in the past. This discouraged the expansion of economic and efficient agricultural production and led to international market instabilities. Although Canada is one of the world's most efficient producers of wheat, during the 1960's Canada was relegated to the role of residual supplier to the EEC. The EEC average support price for wheat remained over 40% higher than the C.I.F. Rotterdam price for prime Canadian wheat from 1967/68 to 1971/72. It was in response to such conditions that the Canadian Government, under Operation LIFT, paid out over $63 million in direct incentives to reduce Canadian wheat acreage by 50 percent.

It was, therefore, in this situation of international market instability and cutbacks in production due, at least in part, to lack of continuing and secure export markets, that Canada and other agricultural exporters faced the dramatic changes of the past two years. Stocks had been cut back, intentionally in many cases; poor crops occurred in many countries; and, at the same time, demand for farm products continued to rise with incomes. This tight market situation was intensified by speculative movements associated with general monetary instability.

Effects of Changes in Agricultural Markets

This sharp rise in world market prices in the past two years, for food and primary commodities, has clearly been a factor behind the recent acceleration of inflation in Canada. Rising world prices mean that Canadians have to pay higher prices for imported commodities and products made from these commodities. They must also pay higher prices to obtain Canadian-produced commodities for which there is strong demand on world markets. However, there is some evidence that the recent slowdown of economic activity in the U.S., Japan, Europe, and Canada is beginning to exert downward pressure on prices.

This combination of circumstances had led to a series of actions by our trading partners quite different from earlier protective measures. For example, some producing countries have sought to exploit their sizeable potential for strategic market power to realize dramatically increased profits in the short term through the use of producer cartels. The undeniable success of the OPEC cartel in increasing the price of oil has encouraged others. Producer cartels have also been established or are being considered for coffee, tea, bananas, and certain non-agricultural commodities.

In some cases, countries have applied export controls or export taxes to certain agricultural commodities in order to ensure adequate supplies to meet domestic demand. This was the case in June and July 1973 when the U.S. applied export controls on soybeans and other protein feeds. The effect of this unilateral action on Canada was such that Canada, in turn, was forced to use limited export controls on domestic supplies of animal protein feed supplements. We are still trying to cope with the disruptive effects of this U.S. action on the North American livestock economy.

While export controls or taxes may have the short-term effect of insulating domestic markets from world price increase, in times of inflation and increasing demand for agricultural products, these controls may also result in a disincentive to investment and production expansion by restricting access to more remunerative world prices. Further, the effect in individual cases will depend on the elasticity of supply and demand with respect to the particular commodity involved.

As a result of these rather dramatic events in world markets, most importing countries have become increasingly interested in the security of supply of agricultural products and in stability in international markets. This has shown up in renewed interest in the negotiation of bilateral long-term contracts for supplies and less preoccupation about access to markets.

It is likely, however, that world agricultural supplies will increase relative to demand over the next few years and that the issue of restricted access to international markets will again come to the fore. Therefore, one of the key roles of international trade policy in contributing to the curbing of inflation is to focus on the more fundamental causes of disequilibrium in the trade of agricultural products and open up markets so that efficient producers are encouraged to not just stay in production but to expand production. A major opportunity to reduce barriers to trade and contribute to a more efficient world agricultural economy lies in the present Tokyo "Round" of trade negotiations under GATT.

The Multilateral Trade Negotiations (MTN)

The Tokyo Declaration (September 14, 1973) formally opened the Tokyo "Round" of trade negotiations. The Declaration identifies a major objective of the negotiations in both the agricultural and industrial sectors as "the expansion and ever-greater liberalization of world trade . . . through the progressive dismantling of obstacles to trade and the improvement of the international framework for the conduct of world trade". With specific reference to agriculture, the Declaration states that the negotiations should include an approach which "while in line with the general objectives of the negotiations, should take account of the special characteristics and problems in this sector". Substantial progress in agriculture will be necessary if the Tokyo Round itself is to be successful.

The Tokyo Round will encompass negotiations on tariffs, import controls and licensing of all kinds, export subsidies, assurance of supply, safeguards, health and sanitary regulations, product standards, customs valuation and the relationship of these issues to international stability in agricultural trade. The negotiations may be carried out both horizontally on the issues referred to above, and vertically on a commodity-by-commodity basis. Specific commodity agreements may be negotiated, as appropriate, in certain commodity sectors.

Any effort in the MTN to improve the conditions of world trade in agriculture should deal specifically with the following interrelated issues.

1. Access

As mentioned earlier, domestic farm policies have been the basis for much of the increased protection against imports and the subsidization of exports. The effect has been to impede structural adjustment to more efficient units in the countries applying such policies and to encourage the expansion of production in more competitive producing areas of the world. A negotiation on these issues in the GATT and a limitation of the trade distorting effect of these policies could lead to more efficient use of agricultural resources to the benefit of both producers and consumers.

A reduction in foreign barriers to trade in agricultural products through the MTN should expand exports of those products and their derivatives (where possible in more processed forms) in which Canada enjoys or could develop, a competitive advantage; such as grains, oilseeds, vegetable oils and meal, forage seeds, selected livestock products, seed and table potatoes, aged cheddar cheese, apples dried peas and beans and some other vegetables, furs, malt, and honey.

An expansion in farm exports could lead to more efficient use of Canadian productive capacity while at the same time expanding farm income. This could permit the shifting of resources and the reduction of protection in certain commodity sectors where imports can be obtained more cheaply.

As part of the negotiations, governments will also review the safeguard measures which permit emergency protective action to be taken in justifiable situations. In addition, Canada would want to ensure that there are adequate arrangements not inconsistent with the general rules pertaining to emergency safeguard action under the GATT, which would allow us to deal with the problems of cross-border trade in certain sensitive agricultural products. The problem here is safeguarding against sudden and disruptive imports from the large U.S. market, particularly where problems of a seasonal nature emerge.

2. <u>Security of Supply</u>
The question of security of supply of key agricultural commodities will, in all likelihood, constitute an important new issue in the GATT negotiations. At this stage, it is difficult to see how this issue might develop and what the trade-offs might be.

3. <u>Stability of International Agricultural Markets</u>
The MTN will provide Canada, as an agricultural exporter and importer, with an opportunity to achieve a degree of stability in agricultural prices. In order to achieve this objective, the negotiations should deal with the effects on agricultural price fluctuations of the encouragement of uneconomic production and the use of import restrictions and export aids.
In this context, it is expected that the negotiations will examine comprehensive international arrangements for certain commodities as a means of market stabilization. Such agreements could incorporate elements guaranteeing, among other things, more reasonable and stable prices to consumers than we have recently experienced but at the same time providing adequate producer returns and a measure of security of supply. However, the actual benefit and practicality for such agreements will have to be examined on a case-by-case basis in the light of the Canadian interest.

Conclusions

1. Against a review of Canada's interests in international trade in agriculture, the international framework involved, and the prospective trade relations developments, it may be possible to draw some conclusions about the implications for the problem of inflation. I would emphasize, however, that the thrust of trade policy is not in itself directed to dealing with problems of inflation. Rather, the issues are problems of access to markets, access to supplies at fair and reasonable prices, problems of trade disruption and problems of instability.

2. As a significant agricultural exporter and importer, Canada has an important stake in ensuring that a greater degree of stability is achieved in international agricultural markets to the benefit of both producers and consumers.

3. A lack of international co-operation and action on the trade disruptive effects of domestic farm policies contributed to a degree of inflation. A collective will to improve international trade relations and policies and deal with the more fundamental causes of disequilibrium in the agricultural sector may not cure inflation, but will go some way towards ensuring that the detrimental effects of inflation are minimized.

4. It would be to the advantage of both the Canadian producer and consumer if we could expand sales opportunities in those sectors where we can efficiently produce and export and sufficiently stabilize international agricultural markets so that small changes in world production or consumption do not have detrimental inflationary or deflationary effects. There is an opportunity to go some way towards meeting these objectives through international negotiations either bilaterally, multilaterally in the GATT or in international commodity arrangements.

INFLATION AND MARKETING BOARDS - CONSUMERS' VIEWS

Mrs. Ruth Jackson*

Marketing boards for agricultural products developed as a result of chaos and abuses in marketing during the Depression. Perhaps too little attention has been given to the good things they have accomplished, (good news doesn't seem nearly as newsworthy as bad news). If we consider where marketing boards fail to solve problems, it gives an opportunity to improve their performance. Our world is changing, as it always has, but sometimes the speed of change today leaves us breathless and bewildered. There is a need to examine and assess how well marketing boards are dealing with problems today - and in particular, if they are or could be contributing to inflation.

Recently, George McLaughlin, chairman of the Ontario Milk Marketing Board used as a definition of inflation a decrease in purchasing power of currency. I can agree with that definition (but certainly not everything in his address), and I would like to add another definition, that inflation is an increase in price levels arising from a mounting effective demand without an increase in commodity supply.

If we consider the powers given to marketing boards, it is quite clear that any board could be a factor contributing to inflation - a truly dangerous situation without proper controls.

From a consumer's point of view, probably the most innocuous thing a board could do is promote its own commodity. As long as producers were able to increase production to meet this stimulated demand, the promotion would not be inflationary - but if production remained the same, the promotional activities would be inflationary.

During the past year we have at times felt some concern about the advertising done by the OMMB - which has had difficulty maintaining total milk production and succeeded in raising it only slightly in 1974.

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* President, Consumers Association of Canada (Ontario).

They have a distinct advantage in controlling the only adequate dietary source of calcium for Ontario residents, which is supplied in milk associated with other good nutrients. If the Ca intake in the Canadian diet were adequate without increasing milk consumption, I would have to object strongly to this advertising. As it is, our Ca intake is not adequate, and no one else appears to be sufficiently successful in meeting our desparate need for nutrition education, and we are grateful for this promotion, even though it is somewhat inflationary. To be acceptable to consumers, marketing boards must behave responsibly.

Supply at a certain price can also remain constant because of interference with free trade through tariffs. Marketing board requests for protective tariffs on agricultural products can, if granted, make sure that the supply does not increase. Marketing boards have been more active than consumers in appearances before Tariff Boards.

By restricting the normal flow of goods, inefficient producers are encouraged to remain and their higher costs of production is often included in the calculations which result in the consumer paying an inflated price. To protect consumers against unfair tariffs, tariffs should not be allowed on goods which are not produced in significant amounts in Canada. Tariffs on produce which is produced in Canada should be limited to adding to the price, the amount by which the product is subsidized or supported in the country of origin.

The mechanism by which a marketing board can cause inflation may however, be much simpler than this. They may intentionally or unintentionally set too high a price. There is more than a little suspicion that the egg marketing board did this last year. Their protestations of merely setting a more stable price to even out the peaks and valleys of past price patterns, is not too believable to most consumers. It seemed that their stabilization price brushed the peaks and ignored the valleys on the graph, as they attempted to recover from losses sustained as they increased production unreasonably in an effort to ensure a high quota when quotas were introduced. This pattern of operation has proven to be disastrous for the small farmer and has added to consumer suspicion and distrust of marketing boards generally. Most consumers don't know that all boards do not operate the same way and that they are not all doing the same thing.

The Forbes Report also suggests that boards controlling milk, broiler chickens, turkeys and processed grapes have set prices too high. No one, including consumers, has been able to develop satisfactory criteria for establishing a "fair" price.

Since less than 20% of farmers receive 58% of total agricultural sales, any increase in price benefits a few and does not greatly affect the 81% of farmers earning relatively little. In this way, raising prices increases the cost of living and probably causes increased prices in many other products. In this way 80% of the farmers and many urban consumers are worse off, with only slightly increased incomes and their expenses greatly increased.

Unpopular as the suggestion is to a tradionally independent and conservative (small c) group of people, some other way of providing a suitable income for legitimate farmers who cannot or should not undertake the expenses of getting into the magic Top 20%, should be found.

We are accustomed to income transfers in the form of taxation, welfare payments, and tariffs, and with proper appeal mechanisms and controls, public approval could be had for adequate incomes for farmers. However, without public participation in decisions, the arbitrary pricing of producer only commodity boards cannot be accepted.

Poor planning on the part of a marketing board can result in a larger supply than the market can use. This adds to consumer costs because resources are diverted to needless production which may then require storage. Marketing is not just selling, but facilitating the movement of a product from production to consumption. Manufacturers have found storage costs have risen so high they cannot afford them. If they are to stay in business, they must achieve a balanced flow of raw materials and sale of final product. Agricultural products suffer from unavoidable storage costs in this country which produces only one crop/year. When we add to ordinary storage costs the costs of refrigeration, humidity control etc. we can see that storage costs for food are very high and we must eliminate as far possible any unnecessary and unplanned storage. Some marketing boards tried to do this where production can be managed or coerced into a fairly uniform flow and they are to be commended for their efforts. Others who might have done it have not always succeeded. Any unnecessary storage, even when the product will not spoil, adds unnecessarily to the cost of production. No one benefits and the consumer must ultimately pay an inflated price. Marketing boards must make the best possible use of information available to them and should negotiate satisfactory ways of disposing of any surplus product.

The ability of marketing boards to capitalize the right to produce through the establishment of saleable quotas, whether on land, the amount of product accepted for sale, or the amount produced, raises the consumer price unnecessarily, and in the long run, results in little advantage for producers. While it is a windfall profit for producers in the plan at the beginning, it forms an artificial barrier to new entrants to the market. You have heard farmers complain that their sons and daughters can't affort to go into farming - they can't finance the capital necessary. Indeed it is large for many types of farming. This is another reason for not adding to it with artificial entry costs as has been done by many boards. Higher prices which must result from a capital value of a quota, is inflationary and should not be allowed. Quotas should revert to the marketing board when they are no longer used, and be fairly distributed.

Many marketing boards have a good deal to do with standards and grades established for their product. Grades are established for various reasons,- to give a fairer payment to producers,- to ensure processors an to stay in business, they must achieve a balanced flow of raw materials and sale of final product. Agricultural products suffer from unavoidable storage costs in this country which produces only one crop/year. When we add to ordinary storage costs the costs of refrigeration, humidity control etc. we can see that storage costs for food are very high and we must eliminate as far possible any unnecessary and unplanned storage. Some marketing boards tried to do this where production can be managed or coerced into a fairly uniform flow and they are to be commended for their efforts. Others who might have done it have not always succeeded. Any unnecessary storage, even when the product will not spoil, adds unnecessarily to the cost of production. No one benefits and the consumer must ultimately pay an inflated price. Marketing boards must make the best possible use of information available to them and should negotiate satisfactory ways of disposing of any surplus product.

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Many marketing boards have a good deal to do with standards and grades established for their product. Grades are established for various reasons,- to give a fairer payment to producers,- to ensure processors an equitable return on the raw product they buy,- and maybe as a last consideration, to aid consumers. Different federal and provincial standards add to the confusion. It is evident that some, if not most, of the grade standards existing today are not useful and are sometimes viewed as unfair to at least one of the three (producer, processor, or consumer). The current steer, heifer, cow controversy is an example of the dissatisfaction that can arise. The farmer and consumer both feel cheated. Savings which could be passed on to the consumer through a rational and equitable grading system are rarely seen. If the grading benefits get dropped along the way, they are a factor in inflation since grading does cost money and no benefit is seen by the consumer. Grades have also been used as trade barriers to restrict the flow of goods.

Outdated grading systems may also prevent the development of consumer-requested products. While this would not be inflationary in the usual sense, it would raise the price of consumer-desired products. Beef and pork grading changes attempted to meet consumers' requests in part. I understand that grading is being reviewed at the present time. I hope the deliberations will be speedy and blessed with great insight and wisdom, because the problems are not always simple, but the grades require a simple and fairly uniform nomenclature if they are to be accepted and used.

Many recent controversies over marketing boards have centred around attempts to limit interprovincial trade. I would like to think that a spirit of cooperation would prevail to allow real economies of geographical location and specialization to be reflected in wider interprovincial trade and lower prices to the consumer. If restrictions prevent this, they are inflationary.

In conclusion, I would like to summarize my recommendations.

1. Marketing boards must act responsibly. If they don't, public pressure will surely remove their powers.

2. Tariffs on agricultural products should not be allowed for goods which are not produced in Canada in significant amounts.

3. Tariffs on products competing with Canadian products should be limited to adding to the price, the amount by which the product is subsidized or supported in the country of origin

4. Arbitrary pricing by producer only commodity boards has not helped those farmers with lower incomes and cannot be accepted by the public. Informed and adequate representation of all interests in a commodity must be established if pricing powers are to be accepted.

5. Unnecessary storage costs must be eliminated.

6. Quotas, where they exist, should not be saleable and not reflected artificially in land or building costs. Unused quotas should revert to boards for redistribution.

7. A review of grading by as many people as are concerned with individual commodities and an overall review to bring as much uniformity as possible to a grading system, so that all in the food chain may profit from useful grading.

8. Provincial barriers to reasonably priced products from other provinces prevent economies of specialization and location. They represent inflationary costs to the consumer and should be phased out.

If the foregoing sounds pretty critical of marketing boards it was meant to be. I was not asked to tell you how marketing boards don't add to inflation, but how they do or may. I'm sure Gordon Hill who is not bashful and who is more knowledgeable than I am will review the producers' side of the story very well.

INFLATION AND MARKETING BOARDS - PRODUCERS' VIEWS

Gordon Hill*

I am pleased and honoured to be asked to represent farmers and offer their viewpoint in this discussion. Some of you know from experience that farmers get as excited as to consumers on the topic of food prices. At least one thing is clearly on the farmer's side in this discussion, and that is the running start we farmers have had at this issue. By late 1972 when the public inquiries and newspaper stories got going, farmers had been riled up about food prices and farm prices for many years. To us it appears that society's increasing neglect of agriculture over the years is finally coming home to roost. There is no smugness in our attitude, but we do feel vindicated that our protests and warnings, ignored for over two decades, have proven accurate and reliable.

The powers that be in our society have been irresponsible in their attitudes toward food prices since the Seond World War. There is nothing wrong with industrialization but the wholesale way we have welcomed it in Ontario -- and are still welcoming it - brings many unnecessary evils that are not part of an industrial society as such.

It is easy to see why this has happened. The promises of industrialization were that machines would reduce drudgery and heavy work, mass production would bring more products into reach for the average consumer, the new biological knowledge would reduce the threats of disease and early death, and, not least, the increase in leisure would allow anyone with the ability to pursue higher education.

These good things have all been realized to some extent. But they have been partly obscured by the more glittering but dubious advantages of over-extended consumer credit, widespread preoccupation with luxuries and frills and the mere symbols of success and a desperate search for

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* President, Ontario Federation of Agriculture.

vibration and excitement to ward off boredom and loneliness. (If you think that extreme, you might take a look at the entertainment page of any city newspaper).

All of these trends are related to the one problem -- we are enticed by the illusion that we are getting something for nothing. The sudden concerns for the environment beginning in the late 1960's are teaching us that we have to live with our waste materials and within our available supply of resources. It was not until 1973 that the new scarcity of resources for food production become part of this new concern. We have as a society been deluded that food can be an ever smaller part of our budget, leaving most of our income for delights and fashions. Of course there are a considerable number of Canadians who share only little in the abundance and for whom food price increases pose a real hardship. However, farmers recognize the strident cries against unfair price increases as the voice of the affluent, articulate, and comfortable majority who see only that their appetites for unnecessary and often frivolous goods may be curtailed.

Consumers have the right to question how food production and marketing works. They have the right to be treated fairly and to pay no more than a fair price for their goods. But they have <u>no</u> right to expect that they not pay actual cost increases as they occur. North Americans and also Europeans have been eating off the backs of farmers who were not fairly compensated and even more off the energy and materials of less developed countries who are finally demanding their due. We have been paying too little for food through the 1960's and we are now seeing the rapid escalation of prices to what would have been a more realistic level all along.

That general perspective is necessary for any accurate discussion of the food price situation. Make no mistake about it: Food prices have gone up faster than other retail prices for over two years now. From 1961 until mid- 1972 food prices were increasing less rapidly than the total range of retail prices. But from November,1972 to November,1974 food went up 37% on the Consumer's Price Index while all other prices increased only 17 percent.

This phenomenon is world-wide in scope and the major causes have often been pointed out. In the short term, the poor grain harvests in Russia and China in 1972 forced both countries into world grain markets to bid for supplies in large quantities. The decline in the Peruvian anchovy catch and, consequently, in fish meal production, and the effects of world currency disruptions were other main factors. In the longer term, strong population growth and rising incomes have continued to exert upward price pressure and this was greatly helped by an economic boom generally in developed countries in 1972 - 1973. At the same time stocks of cereals were declining due to numerous factors in major trading countries. Many people expected food prices to level off in 1974 after a record world grain harvest in 1973. They failed to take into account the unforeseen oil price increases of a year ago and the inflationary effects this would have at all levels of our energy-intensive food production chain, from fertilizer manufacture to transportation and retail costs. Retail food prices have risen again in 1974 by about 15 percent. Most of this of couree is explained by the devaluation of the dollar, consumer prices generally having risen by 11 percent.

How much blame for rising food prices can be laid on higher farm prices?

An Agriculture Canada study estimated that for 1971 the farmer's share of the Canadian retail food dollar was down to 35 percent. The U.S. Department of Agriculture estimated the corresponding American figure at 38 percent.

This would indicate that if farm prices rose by 50 percent, on that count alone retail prices should increase hardly 20 percent. From 1968 the consumer price index for food has increased by 58 percent. The index of farm product prices has approximately doubled. This means that product prices by themselves would account for only about two-thirds of food price increases on the whole over these past six years. In other words, it means that not only have farm prices on average come up to more realistic levels, but marketing costs have also gone significantly higher.

All of this helps directly to answer the question before us today. What causative role have marketing boards played in these food prices increases? The first point must be to destroy the popular notion that all marketing boards have the power to restrict production or to set prices rather directly. In fact the greatest increase in farmers' returns by far has been in grain prices. <u>But Canadian grain prices more than any of our farm products are set by international grain prices</u>. This undoubted truth in itself should turn the accusing finger of the distraught consumer away from marketing boards.

Make no mistake about it, marketing boards are supported by farmers because we see them as mechanisms to improve farm income levels. However, there are many functions of marketing boards and no board is empowered with them all or exercises them all. Setting prices directly is carried on by few boards and even for these the regional, national, and world markets severely restrict the scope of action. More commonly boards negotiate prices with buyers or processors on behalf of farm producers. At any rate, it is common to attribute to boards more power to over-ride basic economic pressures than they exercise.

The various provincial hog boards serve mainly to centralize sales so as to maximize competition among buyers. In Ontario, for example, the Board groups hogs into lots to be sold on a teletype auction where all buyers bid independently. Another major role is promotion of pork and pork products. No marketing boards exist for beef at all.

About half of Canadian fruits and vegetables are marketed under boards or other regulatory agencies. Commonly the boards negotiate the sale of the product but the entire industry is in severe competition with U.S. imports, making supply restriction impractical.

Thus for the large block of wheat and feed grains, beef and pork, and fruits and vegetables, complaints of monopoly power, supply restrictions and price manipulation have no foundation of any sort. Yet these are products frequently indicated in charges of unreasonable food prices.

One of the main objectives of boards is to help stabilize market conditions and farm incomes, both through a production season and from year to year. Farm incomes have historically been unstable and have lagged behind non-farm incomes. A quick glance at Canadian net farm income figures between 1962 and 1973 is revealing. For example in 1971 the net farm income was approximately equal to that received nine years earlier in 1962. The record net farm income year of 1966 was not exceeded again until 1973, a span of seven years. To demonstrate the instability, net farm income decreased by 24 percent between 1962 and 1964, then it increased by 52 percent in the next two years. This was followed by a 24 percent decrease the following year. In the 12 income years between 1962 and 1973, in only five years was the net income equal to, or greater than in 1962. For farms specialized in one or two commodities the fluctuations were much greater still.

Farmers enjoyed a record year in 1973. The average net farm income per Canadian farm was approximately $9,200. This serves as the return for the farmer's management skill and capital investment as well as for his labour. Allowing six percent return to his investment, the reward for his labour and management activity was about $4,978. By comparison, in 1972 the average construction worker earned about $10,000 as a return to his labour. Net farm income in 1974 is expected to decline from 1973, as costs of farmers have risen rapidly.

Canadian farmers have been proud to be part of a revolution in agricultural production that wins the admiration and envy of the world. We have long realized that the considerable expenditures on agricultural research, extension, and production benefits society in geral. Farmers have not received the benefits in the past and do not expect to in the future. The natural tendency of urban folks and their politicians to seek the path of low cost food is known in the farm community as our "cheap food policy". We don't expect that urban people, who even forget that food is a primary good for themselves, will begin to look out for the interests of farmers. That is why farmers have turned more strongly to marketing boards in recent years. They recognize that the operations of the boards can organize farmers into effective action groups for identifying and dealing with their own problems.

At the same time we believe that marketing boards serve the best public interest. Orderly marketing can only aid processors and retailers in cutting buying and overhead costs, which should aid consumers. A farming industry in structural disarray, unable by sound business practices to manage itself, is no answer to efficient food production. A healthy and sound structure of our agriculture is by far the best hope we have of an adequate, secure, and low cost food supply.

Marketing boards will remain a basic part of this picture. They are a fundamental instrument in creating a situation where individual farm families can foresee a profit for committing their capital and labour.

In summary, marketing boards have not been mainly responsible for higher farm prices these past two years. At the same time some marketing boards have had some upward pressure on prices and have rationalized markets for some products. This increase in farmers' incomes has been only just and has helped the one-family farm compete against much larger producers and buyers. Boards have not been inflationary in the sense of disturbing markets and causing general price increases, however. To the contrary, they have contributed to the long-run stability of our farm scene and the food industry.