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SALES FOR FOREIGN CURRENCIES--THEIR ROLE AND THE PROBLEMS THEY CREATE

by

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For nearly 20 years, sizable portions of U. S. exports of farm products have moved out under some type of special financing. In the Lend-Lease and Marshall Plan periods, the reasons for adopting these procedures were compelling ones and little question was raised as to their appropriateness, provided the United States was willing to foot the bill. The actions taken were generous, statesmanlike, and effective.

The 1950s have seen a revival of this general idea, but under markedly different conditions and in ways that raise more questions as to what our future policy should be. First, there has been a rather subtle change in objectives and, second, there is a marked difference in the prospective duration of the program. Neither the Lend-Lease nor the Marshall Plan operation was undertaken as a means of getting rid of surplus stocks. In fact, we did not have large surplus in either of those periods. Full implementation of the programs involved placing some restraint on U. S. consumption and would have required more sacrifice if we had not had unusually good crops in those years. These shipments did, however, serve to strengthen prices for many of the farm products, and probably postponed to some extent troubles of the kind that have beset agriculture in the 1950s.

In the period since 1953, the purpose of abnormal financing arrangements has been different but with a continuing and perhaps growing undertone of the humanitarian and high policy objectives that characterized the Marshall Plan operations. We are now much concerned about reducing burdensome accumulations of storable commodities. But along with that there is a growing feeling of discomfort about the existence of large unneeded stocks of food and fiber in the United States when so many people in other areas do not have enough of them. Consequently, there has been a gradual but not very clearly defined change in emphasis, away from mere surplus disposal and toward efforts to make effective use of this excess in implementing the emerging policy of aiding other countries to achieve more adequate levels of nutrition.

But the problem is not so simple as these comments imply or as many people assume it to be. In both the Lend-Lease and Marshall Plan operations, there was a clear, well-defined objective and a time limit to the period in which heavy demands would be made on U. S. resources. The war program needs no comment. It was to end when victory was achieved. There is general agreement that it was better to finance our contributions directly and currently, as part of the war cost, than to build up a top-heavy structure of unpayable war debts as we did in World War I. Thereafter, in seeking to restore quickly the productivity and economic health of the West European countries, we were clearly acting in our own political and economic interest as well as that of humanity in general. If the goals could be achieved in the time specified, we could taper off this abnormal type of trade and revert to traditional, or improved, methods of carrying on commerce between nations along lines we had long sought to encourage.

The programs initiated in those years, though vast and expensive, were much more manageable than the one we are now endeavoring to carry out. The West European nations had had well-developed and efficient economic organizations. Their public officials were experienced and competent. Governmental organization was well developed, stable, and relatively efficient. It was a matter of restoring or strengthening something that had already existed, a task which these nations could carry out by themselves if given the wherewithal to do so. Furthermore, the size of the populations we were seeking to aid was not disproportionately out of line with our own.

In the program of recent years, many of the conditions are different from those noted above. The problem in the underdeveloped areas is not that of restoring an efficient economy that has been disrupted by war. Often it means assisting a nation that never has been well-organized, or efficient, to build from the ground up; to break out of age-old ruts; and to try to achieve a position approaching equality in a modern, highly-developed world. In many cases an adequate and experienced civil service is not available, institutional organization is poorly developed, and the government far from stable. The numbers of people needing assistance outnumber our own population many times over.

Under these circumstances, there was some hesitation on the part of Congress to enter upon a new open-end program of aid to the non-European countries along lines similar to those used in Western Europe. Hence, there was reluctance to vote approval for the Aid-to-India Act of 1951 and even to make the grant of wheat to Pakistan in 1953. Here we were embarking on a program of unlimited scope and with no specified termination date. There was some feeling that the needs of the underdeveloped countries as a whole constituted a bottomless pit which even our large surpluses could not fill or even affect in any significant way. Nevertheless, the India and Pakistan Acts were passed and put into effect.

But the surplus problem became increasingly serious as the high and rather speculative demand of the Korean War period slacked off. By January, 1954, CCC holdings and commitments had reached a total of more than $5 billion and there was growing concern not only about excess stocks of wheat and corn but of butter, cheese, dried milk and vegetable oils. In an effort to deal with the situation, the Congress passed the Agricultural Trade Development and Assistance Act of 1954 (P. L. 480), which was in some respects similar to the Foreign Assistance Act of 1948 that implemented the Marshall Plan. Some steps had already been taken along similar lines, under various versions of the Mutual Security Act and others, but our purpose here will best be served by confining attention to operations under

P. L. 480. The Act recognized, as did the Foreign Assistance Act of 1948, that one of the principal stumbling blocks to enlargement of agricultural exports was a shortage of dollar exchange with which to buy them. However, the mechanisms provided in the two Acts were somewhat different. In the European Aid program, the commodities shipped became the property of the receiving country. That is, they were outright gifts so far as the United States was concerned. They were to be sold through normal channels of trade and thus gave rise to sizable balances which were in the currencies of and owned by the countries to which the shipments were made. These were designated as counterpart funds. They were to be used for reconstruction and development, without obligation for repayment to the United States, though there was a provision that the projects on which they were to be spent must have the approval of the United States official in charge for the country concerned before funds could be released from the balances so acquired.

The P. L. 480 plan retained the idea of sales for foreign currencies, where dollar exchange was not available, but provided that the proceeds of these sales should be retained as U. S. owned foreign currency balances in the receiving country. These funds could then be loaned to the recipient country for internal development programs, but they then became internal obligations owed to the United States. In both programs, some portion of these funds was reserved for direct use by the United States. The funds thus acquired may presumably, at some future time, be converted into dollars and repaid to us, if the recipient country agrees to release dollar exchange for that purpose. If large U. S. obligations should be incurred within the countries concerned, such balances could presumably be used in liquidating them.

This does, of course, enable us to retain, in foreign currency, an asset of sorts which is of considerable size. Perhaps more important, it gives us rather complete control over such funds, probably more than if they were counterpart funds owned by the receiving country. But this is not an unmixed advantage. While it is true that withdrawals cannot be made except by agreement between the two countries, the arrangement does impose restraints on the willingness of some countries to make purchases of U. S. farm products on this basis. In these days, when the fear of economic domination is so pronounced in many of the poorer and newer countries, few of them really like having, even internally, large obligations which are owed to the United States.

Furthermore, if negotiations for putting these funds to use on internal development projects are slow or abortive, such a situation can lead to an accumulation of inactive balances that will create problems in the receiving country, possibly even exert some deflationary influence. This means that steps must be taken rather promptly with a view to putting them to effective use. But suitable projects that can be financed solely by local currencies may not be readily available, and the receiving country may not wish to incur long-term obligations for projects it regards as extravagant or of dubious merit.

Probably a more serious danger is that of inflation growing out of loans that may not be realistically geared to the absorptive capacity of the country concerned, or adequately related to the supplies of goods and services available for purchase with the increased incomes that may result from development undertakings, whether financed by funds derived from P. L. 480 sales or by loans derived from outside sources such as the International Bank or the U. S. Development Loan Fund.

Another problem is that a bilateral debtor-creditor relationship does not provide the best climate for other types of intercountry cooperation which are important both to the receiving countries and to the United States. Among the activities to which we are committed are such things as mutual security, technical assistance, increased sales of our products, and the improvement of trade relations. Where a debtor-creditor relationship exists, frictions and bargaining conflicts can arise that may hamper the carrying out of other types of cooperation. This argues strongly for handling loan operations through third parties wherever that is practical, that is, through the international lending agencies.

There are other features of the program that cause difficulties. One is that our surpluses do not, for the most part, consist of the kinds of things most needed by the countries to which we seek to sell them. We have very large stocks of wheat. But so have Canada and, to a lesser extent, Australia and Argentina. Even France is a heavy exporter in some years. Wheat is in strong, if not, in fact excessive, supply almost all through the world. We have very large stocks of corn, but effective use of corn requires a well-developed livestock industry, which most of the needy nations do not have. Furthermore, strong and undiscriminating pressure to sell our wheat on a concession basis inevitably gives rise to grave fears and serious criticism on the part of other wheat exporting countries. Canada's wheat growers are understandably opposed to the existing U. S. program. So are those of Australia. The heavy concession and gift shipments of butter used in liquidating CCC stocks in 1954 and 1955 gave rise to vigorous complaints by Holland, Denmark and other butter exporting countries of Western Europe.

This does not mean, of course, that such criticisms are always justified. But today's international wheat market is a highly competitive one which could degenerate into a scramble for outlets that would be very demoralizing to world markets. It is important that that be avoided and that orderly liquidation and production adjustment be carried out in a spirit of friendly cooperation rather than of cutthroat competition and mutual recrimination. Friction in respect to butter and cheese exports seems to have become a thing of the past as a result of the easing down of support prices from 90 to 75 per cent of parity in early 1954, which apparently has brought production of these commodities into sufficiently good balance with domestic demand that the problem may not arise again.

But the considerations mentioned above make it fairly clear that, in our efforts to dispose of excess stocks, we cannot engage in high-pressure salesmanship in disregard of the effect on competing supplier countries without creating problems we surely would wish to avoid. Even in the receiving countries, unduly aggressive sales effort is bound to lessen the value of our contribution in the eyes of those we seek to aid. Furthermore, the farther we depart from normal trading arrangements, and the longer we continue that practice, the harder it will be to make headway in furthering our more basic policy of promoting freer international trade. So much for the more negative aspects of the program. There are things to be said on the asset side as well, and there are steps we could take which, in my opinion, would make the program both more acceptable and more constructive.

We have, of course, long been committed to an effort to re-establish freer and more normal trading arrangements throughout the world. Our repeated renewals of the Trade Agreements Act of 1934, our leadership in the GATT negotiations of 1947, and in the abortive effort to establish an International Trade Organization, have had far-reaching influence not only within our own borders but in the world at large. The European recovery program was also a long step in the direction of freer trading arrangements. Our tariffs on the whole, and on an ad valorem basis, have been brought down to what is probably the lowest level in effect for any length of time since 1816. There are to be sure some inconsistencies and protectionist features in our existing tariff legislation, for example, those reflected in the Section 22 and Peril Point provisions. Since these are to be discussed by the following speaker, I shall omit further comment on them here.

But in the P. L. 480 program, we have instituted a procedure which is in seeming conflict with our stated policy and one which, if continued indefinitely, would constitute a rather significant modification of it. Some feel that sales for foreign currencies should be abandoned. In the following comments I shall argue, first, that they should not be discontinued in the near-term future and, second, that whether they should be or not, it is probable that this method of financing sales will be continued until the production and stock situation in wheat has been brought into better balance.

It seems to me entirely clear that we could not suddenly put our wheat operations on a normal, hard-currency sale basis, even if we continue to use the enormous capabilities of the Commodity Credit Corporation as a shock absorber. If we did not have similarly burdensome stocks or corn, we could initiate a sizable program for the feeding of subsidized wheat to livestock. We did do that in the war years, and used rather effectively a billion and a quarter bushels of wheat as feed for livestock. But that is not a practical solution now. We did export wheat for foreign currencies in the early postwar years in ways similar to those we are now using. In fact, we exported in that period amounts which, if channeled into our own stocks, would have been seriously burdensome. But that was a time when there was great need and when world supplies of wheat were relatively short. These conditions do not exist now.

For these and other reasons, it seems likely that the foreign currency sales program will be with us for some years to come. Even if we could suddenly cut down production to the equivalent of current needs and normal exports, it still would take several years to liquidate the existing surplus without serious disturbance to the international markets, and Canada's huge surplus would still have to be considered as well as our own.

The people of the United States are, I believe, willing to be very generous in making this huge and costly, but unneeded, stockpile available for the betterment of conditions in needy countries if practical ways of doing so can be found. So far as the U. S. Treasury is concerned, we have already paid the cost of it. Whatever we sacrifice, on past accumulations, is in such amount as we might be able to recover through sale of it in one way or another. It is this that confuses many people. They feel that these excess stocks could somehow be used in such a way as to reduce outlays that we would otherwise have to make in dollars. But that is true only to a limited extent. Even the Mutual Security aid we provide must in large measure be in hard currency, or its equivalent, since the needs cannot be met from resources that exist within the countries whose military strength we wish to build up.

If then we are likely to continue to have a sales-for-foreign-currencies program, how can it be made more effective? First, we should be prepared to make longer term commitments to countries with whom we negotiate agreements. Significant development programs cannot be on a year-to-year basis. They require at least a five-year plan. Some need longer. Unless an underdeveloped country can be assured of outside supplies (which is what we really provide) for more than a year ahead, it cannot afford to modify its production program very much because it may find it necessary a year later to rely on its own resources. Our supply and stock situation, especially in wheat, is such that we could enter into commitments of at least five years' duration without serious concern about our ability to fulfill them. In this way a country in need of outside aid could perhaps ease down temporarily its emphasis on cereal production in order to develop other enterprises, such as livestock and its products, to a point where they could carry part of the load. There is some recognition of this need in the legislation passed in 1959, but the provision for longer term programing still needs to be spelled out more fully and made more flexible. If, as is suggested hereafter, sales pressure is reduced, as a means of achieving more orderly liquidation, this also implies a need for longer term planning.

Secondly, the methods of making plans for use of these surpluses, and initiating agreements, need very careful consideration. To the fullest extent possible, the internal development plans of the various countries should be formulated by them, with abnormal types of supply, such as those we are considering, fitted in only where they will contribute to successful execution of the plan. This precludes a salesmanship approach by the United States itself. Any feeling that the commodities are taken because the United States wants to get rid of them, or that the purchasing countries are being high pressured into accepting them, is bound to lessen their value in the eyes of the countries on the receiving end of the bargain.

The approach suggested above is difficult since many of the most needy nations do not have adequately developed planning organizations or personnel. But, in the main, the assistance needed in the making of plans should be provided by way of the international agencies rather than on a bilateral basis. If we play any large role in the shaping of plans that involve use of surplus U. S. products, there is bound to be some feeling that self-interest is involved, whether that is true or not. While it is desirable that our technicians be used where needed in developing country programs, this should, I believe, be mainly if not wholly as a result of initiative taken by the country itself or, perhaps, more appropriately, under arrangements made by an international agency.

An approach along the lines here suggested seems to me essential as a means of providing the kind of climate needed in furthering our broader international objectives. The more immediate and specific one of disposing of our farm surpluses is of secondary importance and should not be allowed to be the dominant element in our policy. That probably means slower liquidation, but it will put the program in what I believe is its proper setting, namely, that of a genuinely generous effort to aid other countries in the general spirit of the Marshall Plan, rather than that of a self-interest program oriented to our own immediate needs and problems. The United States should stand ready to help implement well-planned programs to the extent that it can, but the initiative should come from the countries desiring aid or from the international agencies. The stress placed on aggressive selling, in P. L. 480 and in the congressional hearings of recent years, constitutes, in my opinion, a disservice to the United States and to the program as a whole. It cheapens our contribution in the eyes of the nations benefited and builds up resistance. If a promotional job is needed, and it probably is, F.A.O. or some similar agency is a more suitable instrumentality than the U. S. Department of Agriculture.

Thirdly, the arrangements for surplus disposal need to be much more carefully coordinated with those of other exporting nations. We cannot go on operating on a unilateral basis without creating more problems than we solve. Continuing efforts to dispose of our wheat surplus without reference to the similar problems of Canada and, to a lesser extent of Australia and Argentina, are bound to cause friction and to decrease rather than contribute to the orderliness and health of the international wheat markets. To handle the matter in that way is clearly inconsistent with our settled longer term policy of encouraging a return to more normal and orderly international trade. In this connection, the procedures used by U. K.-Dominions Wool Disposals Limited, in liquidating excess wool stocks after the close of World War II merits consideration since that operation is one of the few in which problems of this kind have been handled effectively and successfully. The space available here does not permit elaboration on this point. I have discussed it more fully in other connections.[1]

1/ See, for example, The Agricultural Commodity Programs by Murray R. Benedict and Oscar C. Stine, New York, Twentieth Century Fund, 1956, Chapter 8, and Farm Surpluses--U. S. Burden or World Asset? by Murray R. Benedict and Elizageth K. Bauer, Berkeley, Division of Agricultural Sciences, University of California, 1960, Chapter 8.

Fourthly, if these surpluses are to be of maximum usefulness in bettering world conditions rather than a disrupting influence in international trade and an intrusion on the established markets of other countries, particular attention should be given to efforts to aid the poorer and newer nations. It is here that the needs are greatest and the opportunities for actual enlargement of world outlets for the kinds of things we have to spare are most significant. But this kind of market enlargement is very slow and halting. The achievement of normal trading relations may be long delayed and we may need to provide grants of foreign currency funds, as well as abnormal financing of sales and foreign currency loans, if real progress is to be made. But with the rapidly changing situation as to U. S. balance of trade, there is little reason to seek by means of these special types of financing to increase sales in the established markets of the more advanced nations.

These countries are rapidly coming to have holdings of foreign exchange and gold that make abnormal types of sale inappropriate and unnecessary. To use such devices in these circumstances is merely to engage in cutthroat competition with other exporting nations, and to delay progress toward a freer world trading situation, which is our ultimate and broader goal.

A fifth phase of the problem, and one that cannot be adequately discussed here, is that of making better use of the foreign currency balances that do arise as a result of our export operations. For reasons already mentioned, it is desirable to avoid bilateral lending by the United States to the country concerned. That can be avoided in considerable measure by providing, to the fullest extent practical, for administration of these loan funds by international lending agencies such as the International Bank and the International Development Association which is now being organized. This could be done by means of agency contracts under which funds of that kind would be transferred to an appropriate international lending agency for administration, with ownership retained by the United States. There is reason to think the international lending agencies would be receptive to that idea. If that could be done, some of the resistance to the borrowing of such funds would be eliminated and the United States would be freed of the undesirable connotations of being a direct creditor of a country with which it has delicate and fragile relations of many kinds. There would probably be some elimination of duplicating effort and organization, and possibly some improvement in quality of administration. A fund so handled could become a more or less permanent addition to the lending capacity of the administering agency, though with some limitations on the usefulness of the funds loaned because they cannot be used freely for international purchases. Only those projects or parts of projects that can be carried out with resources existing within the borrowing country can be financed in that way. Hard currency loans still would have to come from the International Bank or from countries that are in a stronger financial position.

The modifications of the existing program that have been outlined above do not, of course, lessen the need for constructive readjustments in our own domestic production program. It is illogical to go on producing, on the present scale, commodities which create problems of the kind here discussed. You are so well aware of the difficulties encountered in making readjustments of that kind, and of the time likely to be required in achieving desired results, that I need not elaborate.

For obvious reasons, I have not attempted in these brief comments to deal with these matters quantitatively nor to relate them to formal trade theory. The changing situation as to U. S. balance of trade and such things as the international flow of capital are, of course, elements in the problem, but discussion of them would call for another and different kind of paper. Because of the inherent limitations on the ways in which inconvertible currencies can be used, they do not enter largely into the over-all balance of trade problem. What we are really supplying to the recipient countries is commodities, not money. Unless very carefully handled, such shipments may, of course, reduce hard currency purchases and thus could affect our balance of trade, but presumably that is avoided as much as possible. It cannot be completely eliminated. We do have a program of this kind. It does give rise to foreign currency balances. During such period as it is found necessary or desirable to continue to use abnormal procedures of this kind, we should, to the fullest extent possible, make it work smoothly and make it contribute as fully as possible to our over-all objectives.

DISCUSSION: SALES FOR FOREIGN CURRENCIES--
THEIR ROLE AND THE PROBLEMS THEY CREATE

by

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Professor Benedict has given a thoughtful and constructive paper on the sale of U. S. agricultural surpluses for inconvertible foreign currencies. But I can not accept his major premise that this is a valid method for the United States to subsidize the transfer of its economic resources to low income countries to assist their economic development. There are far better ways to make the transfer: e.g. extremely long term loans in convertible dollars at nominal interest rates, or outright gifts; either bilateral or multilateral, via the United Nations.

If I have a test for my remarks it can be found in the recent article by Harvard Professor Edward Mason in the Atlantic Monthly, entitled "Foreign Money We Can't Spend." Mason points out:

> "Currently we own slightly more than $3 billion in local currencies, mainly Asian, and our holdings are, or will shortly be, increasing at the rate of $2 billion a year. In another four years we shall probably own $10 to $11 billion, and if our aid program continues at the present rate, for another twenty-five years, we may well 'own' all of Asia. Of course, this ownership is as phony as a three-dollar bill, but the potential political repercussions are not at all phony, either in Asia or the United States.[1]

What should we do with these large holdings of inconvertible foreign currency? Professor Mason concludes:

> "All things considered, the best disposition of the vast bulk of local currency accumulations would be for us to grant them back for debt retirement or any other purpose deemed proper by the receiving country. Alternatively, we could burn them, though this would involve the country in the additional expense of printing new currency notes.[2]

What kind of economic reasoning suggests we have a big bonfire of inconvertible foreign currencies?

Consider the basic relations which exist today between consumption, saving, and investment in most of the low income countries. These countries are already attempting to put as much of their resources into investment

1/ Atlantic Monthly. May, 1960, p. 8.
2/ Ibid, p. 84.

as voluntary savings plus taxes will permit. There are inflationary pressures in their market economies. True, these countries may not experience what we call by our standards "full employment." But the apparent existence in countries like India of large-scale disguised unemployment (defined as workers whose marginal product is zero or negative) is not the result of insufficient demand.

It stems chiefly from the disproportions between relative supplies of domestic factor inputs and relative demands for outputs of these factors. Capacity for making substitution among factor inputs may be severely limited by existing technology, traditional ways of doing things, or imperfections of markets. Thus bottlenecks exist and full employment of all resources (as we conceive of this) becomes very difficult, if not impossible. The maximum use of the scarcest factors is encountered long before all of the most abundant factors are used. The bottlenecks are most likely to be in skilled labor, technicians, trained administrators, competent teachers, enterprisers, transport facilities and the like. Given these bottlenecks which seriously limit total output, it may be repeated: the low income countries already attempt to use as much of their resources for investment as voluntary savings plus taxes permit.

Now let us examine what happens when the U. S. ships surplus wheat and cotton (these may stand for all surpluses) for sale against inconvertible local currency. Two hypothetical limiting cases may be specified.

In Case I there is no change in consumption of domestic output but an increase of consumption of imports equal to the shipment of U. S. surpluses. Voluntary saving must fall, as the public buys the imports. The volume of domestic resources for use in consumption, exports, and investment remains unchanged. The release of counterpart funds to offset the fall in monetary savings might be useful if there were no inflationary pressure already. But with this pressure we might just as well burn the money or, better, make an outright gift of the wheat. Anyway, there are no added resources for investment.

In the longer run (and we may well be giving away wheat for many years) improved diets of the working population resulting from eating more wheat and no less of other things may increase labor productivity by reducing absenteeism, illness, and physical exhaustion. But if the rising output goes to consumption no added resources for investment would flow from lending counterpart funds. If some of the increased income is saved the use of counterpart money is pointless because the saving has already occurred.

In Case II consumption of domestic output is replaced by consuming imported U. S. surpluses. Monetary saving is unchanged and resources formerly devoted to consumption are now available to expand exports or investment. To reduce inflationary pressure it might again be advisable to burn the counterpart money or retire government debt.

If the U. S. had a long-term program for providing surplus food and fibre, then the recipient governments would almost certainly budget in their five-year plans for the use (investment or otherwise) of the domestic resources released from consumption goods industries. This they would do whether counterpart money existed or not. If they overshot the mark, counterpart money would not create economic resources to fill the gap. If perchance they undershot and discovered more resources for investment than anticipated they might prefer to borrow from the central bank at 2 per cent than pay 4 per cent to get back their own currency "owned" by the U. S. Incidentally, if consumption of domestic food is reduced this would defeat one of the purposes of our program, i.e. to improve diets.

All this is not to deny that U. S. resources can be a vital ingredient in economic development; nor that we should abdicate all guidance in what resources are provided or how they are used. But it does suggest that the time to exercise the guidance is when the resources are provided (or earlier if possible) and not by carrying on discussions of how to spend or lend foreign currencies which are nothing more than a financial expression of the fact that resources have already come into the country and are being used.

Finally, I have some reservations about using surplus wheat, rice, cotton, and shipping (to mention most of the surpluses) as devices for promoting economic development abroad (with or without counterpart funds):

First, because this escape hatch tends to dull the national will to abolish the foolish policies which continue to create the surpluses.

Second, because it enmeshes us in dumping and other commercial practices we profess to abhor.

Third, because low income countries may well prefer and need from the U. S. a far more varied mix of resources than we define as surpluses. Remember what the main bottlenecks are.

And fourth, because the assured availability of free food from the U. S. may tend to divert domestic investment away from agriculture, which has a comparative advantage, toward types of manufacturing (perhaps steel) which are uneconomic with present factor supplies.

DISCUSSION: AGRICULTURAL SALES FOR FOREIGN CURRENCIES

by

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It is generally agreed that our national agricultural policy has become a conglomerate of splintered fragments, uncoordinated and inconsistent with our most important national and international objectives. Nevertheless it must also be borne in mind that American agriculture has been undergoing revolutionary progress and it is urgent that policies be adapted to stimulate rather than impede the rate of further adjustment. In the past three decades we have witnessed a 40 per cent reduction of the labor force in American agriculture. Real farm income per worker has risen 75 per cent - - a gain which is at least as great as that in non-agricultural employment. The less favored groups in agriculture such as those in Southern areas and non-white persons have improved their income position relative to the rest of agriculture.

I should like to comment on Professor Benedict's paper with respect to the intermediate and long-term aspects of this adjustment problem. His paper may be regarded as a "Preface" to the book written by him and Elizabeth K. Bauer on Farm Surpluses: U.S. Burden or World Asset (Berkeley: University of California Press, 1960). The book contains the most comprehensive and judicious treatment of the subject that I have as yet encountered. Benedict believes that the sale of agricultural surpluses for foreign currencies must be considered in terms of both an intermediate stock-adjustment period and of a longer run production-adjustment period. As regards the intermediate period, it seems clear that many and varied policies will have to be used to reduce our agricultural-surplus stocks. The Congress has gone on record favoring the use of such stocks for economic assistance to newly developing countries. How achieve these mixed objectives without deteriorating the long term economic development of both more, and less, developed economies?

To the challenging recommendations made by Benedict, I submit the following points for consideration. Assuming that foreign aid in the form of agricultural sales for foreign currencies constitutes a net addition to other forms of U.S. foreign aid, most underdeveloped countries would benefit more from greater supplies of protein foods than from cereals. This I believe to be true for at least two reasons: first, because protein foods would serve as a greater stimulus in raising the elasticity of supply of effort with respect to real income; and secondly, because the importation of protein foods into underdeveloped countries would not tend to disrupt their domestic agricultural production. Our surplus stocks and assistance, however, have primarily been in the form of cereals.

These facts notwithstanding, for many years to come, countries like India and Pakistan, as well as other lands in Africa and Latin America, shall not be self-sufficient in cereals. If they succeed in keeping their expanding populations in check, our agricultural sales for foreign currencies could be of substantial importance in enabling them to devote a larger proportion of their resources to industrial investment and education, and hence to the success of their economic development plans.

Underdeveloped countries which are normally self-sufficient in cereals, or are even exporters of them, might still benefit from our agricultural aid. For if we could assure them of such assistance for an interval of five to ten years, they would be better able to adjust their long-term production plans and to establish incentives operating toward more balanced economies, rather than to suffer from the costly over-expansion of agriculture and its consequent relative contraction. Considering the low foreign elasticities of demand for cereals, if at all possible, newly developing countries should be spared from unduly expanding these branches of production as potential suppliers of foreign exchange for the purpose of industrialization.

However, the large and incessant accumulation of foreign currencies by the United States Government clearly is a peril. As of June 30, 1960, our total sales of agricultural commodities for foreign currencies amounted to $6.72 billion (see Table I). I would like to suggest that consideration be given to the funding of such assets into long-term foreign government bonds at nominal rates of interest; say 1.5 per cent. The extant provisions for re-lending foreign currencies by the United States Government, and for guarantees with respect to exchange-rate depreciations should be abolished. The sale of agricultural surpluses for foreign currencies is in itself a highly questionable policy; it should not be burdened by even more questionable by-products.

TABLE I: Sales of Surplus Commodities for Foreign Currencies

Totals as of	Under PL 480 ($ billion)	Sections 550 and 402 ($ billion)
Mar. 31, 1958	2.67	1.45
June 30, 1958	2.83	1.52
Dec. 31, 1958	3.32	1.61
Mar. 31, 1959	3.49	1.64
June 30, 1959	3.68	1.70
Mar. 31, 1960	4.32	1.81
June 30, 1960	4.83	1.88

Source: International Cooperation Administration, Operations Report Washington, D.C. (various issues).

If agricultural sales for foreign currencies are to serve the purpose of reducing surplus stocks during an intermediate period, and of adjusting agricultural production over a longer period, they must be used in conjunction with general measures to encourage differential rates of migration out of American agriculture. The available evidence suggests that substantial differences in earnings still exist as between certain sectors of American agriculture and industry. 1/ Moreover, measures likely to increase differential rates of migration have been virtually ignored in the last three decades of large scale agricultural farm programs. Agricultural sales for foreign currencies would of themselves tend to impede rather than assist long-term agricultural adjustment. I should like to stress that the revolution in American agriculture occurred primarily because of appreciable rates of general economic growth and reduced cyclical instability. Adjustments were able to take place because undue positive or negative impediments were not imposed on the migration of labor from agriculture.

An examination of the evidence now suggests, however, that we have recently suffered not only from an excess of labor in certain branches of American agriculture but from an excess of physical capital investment as well. After the Second World War we witnessed an expansion of investment in American agriculture which has not been warranted by subsequent events. From 1940 to 1950 the increase in the value of farm machinery per person engaged in farming rose more than 200 per cent. If we examine the ratio of physical assets to realized gross farm income, it shows a continued rise until 1952. The ratio declined somewhat thereafter, but was at a maximum for the period in 1959. (See Table II)

The evidence suggests that there have been severe diminishing returns to physical assets in American agriculture at least since 1952. This development appears to have been the result of two sets of interrelated forces: first, high profits in agriculture stemming from high price-supports increased the financial liquidity of farmers; and secondly, this in turn stimulated the expansion of investment in agriculture. The rise in the capital-output ratio has therefore primarily been the result of government policy. As compared with alternative potential returns of real income in other branches of the American economy - - particularly of investment in American agriculture appears to have been a serious misallocation of resources. If agricultural sales for foreign currencies provide further stimulus for such capital investment, and impede the migration of labor from agriculture, they will be a disservice to the potential rate of American and foreign economic development. On the other hand, if they are used to assist in the long term relative contraction of American agriculture, they may aid the economic development of the United States as well as the newly developing countries.

1/ Cf. D. Gale Johnson, "The Dimensions of the Farm Problem", and T.W. Schultz, "Omission of Variables, Weak Aggregates, and Fragmentation in Policy and Adjustment Studies", Problems and Policies of American Agriculture (Ames: Iowa State University Press, 1959) Chapters 4 and 11.

TABLE II: Ratio of Physical Assets: Realized Gross Farm Income in American Agriculture (1910-14 = 100) 2/

			$				$
1950	$\frac{43.90}{12.60}$	=	3.48	1955	$\frac{54.02}{14.35}$	=	3.76
1	$\frac{45.64}{12.35}$	=	3.70	6	$\frac{55.36}{15.04}$	=	3.68
2	$\frac{50.80}{12.85}$	=	3.95	7	$\frac{56.85}{14.64}$	=	3.88
3	$\frac{53.05}{13.84}$	=	3.83	8	$\frac{58.86}{15.28}$	=	3.85
4	$\frac{51.57}{13.78}$	=	3.74	9	$\frac{63.98}{15.63}$	=	4.09

Note: Value of Physical assets were deflated by U.S. Department Agriculture, "Prices Paid by Farmers," for commodities bought for use in production - - 1910-14 = 100. "Realized Gross Farm Income" was deflated by its "Prices Received by Farmers."

2/ Cf. U.S.D.A. Agricultural Statistics 1959 (1960) Washington, D.C., p. 436: Agricultural Prices 1959, Annual Summary (June 1960) p. 7ff; and Agricultural Research Service, The Balance Sheet of Agriculture, Washington, D.C., 1960. For the percentage increase in the value of farm machinery per person engaged in farming, in 1910-1914 prices, United States, by decades, 1880-1950 cf. Alvin S. Tostlebe, Capital in Agriculture: Its Formation and Financing Since 1870 (Princeton: Princeton University Press, 1957), Table 29, p. 119.