EDITORIAL

PRODUCTION INCENTIVES

An expansion of agricultural production of the magnitude currently envisaged in Australia is likely to be achieved only if producers are given the necessary incentive to expand their production activities. During World War II and in the early post-war period rural production was frequently restricted, due to the inability of farmers and graziers to obtain adequate supplies of essential productive resources, including labour, machinery, fertilisers, fencing and building materials. No doubt in these years lack of adequate production incentives also tended at times to restrict output, but fundamentally the period from 1940 to early 1952 was characterized by a shortage of the basic physical resources necessary to promote the expansion of agricultural production. More adequate economic incentives would probably in some instances have resulted in an expansion in the output of particular commodities, but frequently, although by no means invariably, such expansion would have been at the expense of other lines of production. During 1952 the situation changed radically. The supply of physical resources increased relative to the demand, and by the end of that year few farm requisites remained in short supply. Inadequate supplies of physical production resources are no longer a serious restricting factor on the level of rural output, although some vital materials, particularly superphosphate, are not yet in full supply.

Following this marked improvement in the supply of physical resources it is apparent that now, more than ever before, plans for agricultural expansion must be focussed directly on the complex problem of production incentives. It is true that not only must continuity in the supply of physical resources be maintained, but the output of many farm requisites must be further increased to meet the needs of an expanding agriculture. It is true, also, that research, both physical and economic, must be intensified, while extension services must be improved and expanded if rural production programmes are to be successful. Nor should the necessity for capital expenditure on irrigation headworks and reticulation, on improved transport and marketing facilities, and on electricity extension schemes be overlooked.

However, while recognizing the necessity for positive action in these various fields, it is quite apparent that the basic problem is that of providing the economic incentives necessary to ensure that producers, by and large, will respond to the demand for greater rural production. Without these incentives, the value of other measures designed to increase rural output will be greatly reduced, and in some cases may be almost entirely nullified. Producers cannot be expected to accept the increased labour effort, risk and responsibility inevitably associated with production expansion unless the economic incentive is adequate. Incentives fall into two broad categories. Direct incentives in the form of price increases, possibly by way of subsidies, can influence the level of output of a particular commodity or commodities, whereas indirect incentives such as taxation concessions are likely to act as incentives to rural production generally.

While it may be clear that production incentives are fundamental to any programme of agricultural expansion, it is by no means always certain how farmers will react to any specific incentives which may be provided, at least in the short term. Both State and Commonwealth Governments have clearly recognized the need for adequate price and other incentives in their current rural production programmes, and the Australian Agricultural Council at its several meetings last year paid particular attention to this problem. Not only has the Agricultural Council recognized the need for incentives, it has also realized that existing knowledge of farmers' short-term reactions to price changes in particular circumstances is inadequate as a basis for future policy decisions.

The problem of price incentives is complicated by the fact that farmers' reactions to price changes may be markedly different for different commodities and under differing circumstances. For instance, an increase in the price paid for a particular commodity may conceivably result in a decline in the production of that commodity in the short period, although over a longer period of time the same price increase may result in an influx of new capital to the industry concerned, and subsequently in a substantial increase in output. That price incentives can, under some circumstances, have the opposite effect in the short term to that desired has been used quite frequently as an argument against using the price mechanism to promote expansion in the output of particular rural products.

Producers' response to price incentives will be affected by three separate sets of factors: the relative and absolute level of price and income levels, physical supply conditions, and the balance of the differing outlooks and attitudes of the farmers concerned. One of the factors which may affect producers' response to price is the level of incomes in the industry concerned. The same relative price alteration will have a different effect on production according to whether the industry is in a phase of prosperity or depression. Furthermore, the production response will be governed not only by the absolute level of price ruling in an industry, but also by the level of price and profits in competing and related industries. The physical supply conditions in an industry are fairly fixed factors limiting the response of producers in that industry to a price rise. Most agricultural industries have only a certain potential to be tapped. Where many existing farms in an industry are being cropped or stocked close to capacity, a very large price rise may be necessary to make expansion into marginal areas profitable. These and many other considerations illustrate the point that the reaction to a price change in, say, the wool industry may vary considerably from the response to the same relative price change in the wheat industry. Furthermore, the response will be much quicker in some lines of production than in others, because of the differing production periods involved. Quite apart from physical supply conditions, much depends on the individual farmers in an industry—their ages, attitudes, ambitions and expectations. The prevalence of the "subsistence" attitude amongst farmers, as against the "businessman's outlook," will greatly affect the overall response of the industry to price or other incentives. Naturally the balance of various types of farmers in different industries will vary considerably.

It is apparent, therefore, that if incentives are to be provided which will have the optimum effect on production, it is essential that they be based on a detailed knowledge and understanding not only of physical supply conditions but of the attitudes, expectations and aspirations of the farmers in the industry concerned. Farm-to-farm surveys, such as that recently conducted jointly by State and Commonwealth authorities in the New South Wales wheat industry, provide the only means whereby this detailed knowledge may be obtained.