Booms, Depressions, and the Farmer

if causes are understood, steps can be taken to lessen severity

S. V. Ciriacy-Wantrup

GROSS INCOME per person of farm population is much higher in California than in the rest of the country. Types of products raised and farm organization are very different in the two regions. In spite of these differences, major ups and downs of gross income as a whole and within individual branches occur at the same time and rate in California as in other states.

Gross income depends upon the volume sold and the price per unit. In California, there has been a long-time upward trend in volume, and this corresponds with a long-time upward trend of income. Disregarding this trend and minor year-to-year changes, volume has been fairly stable. Changes of volume do not explain major ups and downs—the booms and depressions—of gross income. These are due to changes of price.

Costs

If farm wages, the prices of things a farmer buys, and fixed charges, like interest and taxes, all changed at the same time and rate as the prices he receives, then price changes would not greatly affect the farmer's position. But changes of farm wages lag behind those of price, and taxes, interest, and the prices of goods the farmer buys are more rigid than prices he receives. These differences make the farmer better off when his prices go up, worse off when they go down.

Demand and Income

Since booms and depressions of gross income and prices are not explained by volume of production, they must be due to changes of demand.

Major changes of demand are due to changes of nonfarm income and of the funds industry and processors spend for agricultural raw materials.

Income Stream

The farmer, then, has a vital interest in what causes changes of nonfarm income and business activity. In the United States, the working force and production per man are increasing. Under these conditions, income per person and prices can be kept stable only if increasing amounts of money are returned to the income stream each turnover period—say every three or four months.

A portion of income is collected as taxes and usually returned to the income stream through government spending.

Most of the rest of the income is returned to the income stream as money spent for food, clothing, and rent.

Another portion is saved. What happens to these savings is the important point. If savings are returned to the income stream as investment, then the income stream will not decrease. But if savings pile up as idle balances in banks or idle money elsewhere, the income stream is decreased.

Investment

"Investment" as used here means the spending of money funds to increase inventories and to produce durable goods, such as factories, irrigation systems, houses, and armaments. Such funds are made up of savings and "new" funds created by the banking system.

We may say then that the real problem of keeping income per person and prices stable is to keep investment in balance with saving. What do we mean by "in balance"? If income per person, prices, and employment are to be kept stable in a growing economy, investment must be larger than saving. How much larger depends on how fast the working force and production per man is increasing. Investment is usually an important factor in increasing production per man.

Changes of investment are the basic cause of income and price changes. This is because they do not depend on income changes as do consumption and savings; because they are violent; because they cause changes of consumption; and because changes of investment in some industries cause further changes of investment in other industries.

The rate of investment is affected by:

1. Conditions within the economic system itself, such as interest rates, wage rates, and prices of industrial raw materials.
2. What we may call outside influences, such as inventions, discoveries, and war.

Public Policies

During the boom of private industry, practical goals—which will not involve uncertain and, therefore, dangerous forecasts of exactly when the downswing will come—are:

1. Postpone public investment. However, consider public health, national security, and technical difficulties of stopping work on such projects as dam construction.
2. Increase public revenues during the boom by keeping taxes, especially pay-as-you-go taxes, as high as can be done without lowering incentives for individual effort.
3. Stop public borrowing, build up liquid reserves, and decrease the public debt, especially short-term obligations held by banks.
4. Cut down credit to purely speculative markets, such as grain exchanges.
5. If necessary, tighten credit conditions in general.

Public measures during prosperity should be precautionary and preparatory. If, in spite of these measures, signs of depression begin to appear, positive action is needed. These steps may be taken:

1. Encourage private investment by specific tax concessions, loan guarantees, and direct subsidies.
2. Increase public works.
3. Lower pay-as-you-go taxes.

What the Farmer Can Do

The individual farmer may take some steps to guard against depressions.

He should keep himself well informed about the national outlook for general business activity.

During prosperity he should try to cut down fixed charges, such as interest.

At the start of the upswing, he can buy land. He should be cautious, however, if he does not have enough cash; it does not pay to exchange rent for even more rigid interest.

He can make investments to cut down cash expenses he has to meet every year; improved buildings may cut upkeep; new equipment may cut hired-labor costs.

He can build up his soils, adopt soil-conservation practices that take cash.

If the farmer takes these steps during prosperity he will be better prepared for a depression than other classes of the population.

S. V. Ciriacy-Wantrup is Professor of Agricultural Economics, Agricultural Economist in the Experiment Station and Agricultural Economist on the Giannini Foundation, Berkeley.

Circular 376, "Booms, Depressions, and the Farmer," a more detailed study of this subject, is to be published in February by the Agricultural Experiment Station. It may be secured without cost by addressing the College of Agriculture, Berkeley 4, California.