

POLICY FOR COMMERCIAL AGRICULTURE

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I assume that the objective in discussing policy for commercial agriculture is to improve the economic performance of the commercial farm industry. I accept the view that the need for policy and for modifications in policy arises because of differences between actual and desired performance. I also accept the view that policy instruments should be selected on the basis of benefits (contributions to improved performance) in relation to costs (value of alternatives foregone).

The discussion is divided into four main parts: (1) performance goals for the commercial farm industry, (2) a brief evaluation of the industry's recent performance, (3) future adjustment needs, and (4) program direction. The emphasis throughout is on long-range considerations. In the transition from the current situation to the preferred long-run situation, short-run needs must be considered.

Commercial agriculture is roughly defined as that part of agriculture producing output primarily for the market. It includes those farmers whose main source of income is farm production and whose resources are sufficient when efficiently allocated and organized to generate incomes in excess of the socially defined poverty level.

It is probably a rational decision for some people to be part-time farmers. By fitting farming enterprises around a nonfarm job, they can organize a unit that is capable of generating opportunity cost returns for the resources employed. At the same time, they are able to have some of the advantages people associate with country living. Under these conditions, part-time farming can be a stable operation in contrast to a transitional operation on the way to full-time farming or full-time nonfarm employment.

PERFORMANCE GOALS

Nonfarm people are especially interested in the farm industry's performance as a supplier of food and fiber and as a user of purchased farming inputs and consumer products. Farm people are particularly interested in its performance as a generator of income

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and as a user of labor-management skills and investment capital. But there are varied interests, even among farm people. For example, the corn farmer's interest may focus on income from feed production, whereas the feeder's interest may emphasize income from livestock.

All of these interests are interrelated. But they are not always compatible, particularly in the short run. Individual performance goals vary and this variation gives rise to policy disagreements.

Some assumptions have to be made about performance goals for the farm industry. To have political realism, these goals should be reasonably consistent with the broader goals of the American people. Farm people are a minority group, and their political power is waning as a result of reapportionment. Industry goals which complement national goals and result in equality of treatment are likely to have the widest acceptance.

Four broad social goals appear most relevant to the selection of performance goals for commercial agriculture—growth, production efficiency, equity, and stability. The industry goals listed below were selected with these social goals in mind.

1. Growth

- a. A secular rise in the productivity (output per unit of total input) of farm resources consistent with the general scarcity of investment resources and the relative opportunities offered by the farm industry to contribute to national economic growth.

2. Production efficiency

- a. An adequate total quantity of food and fiber for domestic and export needs.
- b. A mix of farm products reasonably well geared to relative demands for different kinds of food and fiber.
- c. An adequate quantity of each product at the lowest cost consistent with available technical know-how and the prices of farm inputs.

3. Equity

- a. Income earning opportunities for labor and capital on commercial farms equal to those offered by other industries, allowing for any differential amenities and the preferences of people for different kinds of work.

- b. Equality of opportunity for commercial farm people to participate in public welfare programs and public services, including education.
- c. Equality of treatment of resource ownership and control arrangements in commercial agriculture.
- d. A degree of income inequality within commercial agriculture consistent with the national concept of distributive justice.

4. Stability

- a. A stability in the year-to-year flow of farm products into the channels of trade and consumption consistent with the efficient production and use of farm products over time.
- b. A degree of farm price and income stability reasonably consistent with the adjustment needs of the industry arising in the process of growth and development.

These performance goals for commercial agriculture provide the basis for our appraisal of recent economic performance and for identifying policy needs and directions. It should be recognized that use of a significantly different set of goals would produce a different appraisal and a different identification of needs and programs.

APPRAISAL OF RECENT PERFORMANCE

How well has the commercial farm industry been meeting these performance goals?

Growth in Resource Productivity

The farm industry's productivity growth since World War II may be categorized as excellent if the farm industry of the United States is compared with that of other countries. The U.S. farm industry has had one of the highest, if not the highest, rates of secular growth in farm output per unit of measured total input in the world.

The high growth rate in the United States results largely from the creation and exploitation of new opportunities for raising productivity of resources on commercial farms. On the one hand, large investments have been made in agricultural research and development, in education, and in facilities for producing the more productive inputs discovered through research and development. On the other hand, conditions have been conducive to the exploitation of these opportunities by commercial farmers. Farmer motivation,

price-cost relationships, and credit facilities, among other things, have been relatively favorable.

If actual productivity increase is compared with potential productivity increase permitted by the rising stock of technological and managerial knowledge, the performance rating is not as high. Exploitation of the opportunities for raising resource productivity has been highly uneven among farms. Moreover, the industry has not been able to fully adapt its resource structure and organization to the impact of improved technology, the changing pattern of input prices, and a relatively slow growth in the demand for farm products. As a consequence, there has been a gap in meeting the minimum cost goal for production efficiency.

Production Efficiency

Until recently the farm industry has been producing more than enough to meet domestic and export demand for food and fiber at prices that would permit comparable returns for labor and capital on well-organized farms. During the 1950's, the excess supply was upwards of 8 percent of total output.

For a time, much of the surplus was simply removed from markets under the government loan and purchase programs. As excessive stocks accumulated, production controls were instituted. Early control programs had little effect on total farm output. Farmers merely shifted resources from controlled crops to uncontrolled crops, and this resulted in increased feed grain production. The failure of these programs to reduce total output prompted programs that limited substitution among crops, that is, programs based on the withdrawal of land from current production. In the 1962-65 period, land withdrawal programs removed upwards of 60 million acres per year. This effort has helped to reduce the imbalance in the level of total output. However, the imbalance in the level of output has been reduced by increasing the imbalance in the level of land utilization.

Since the early 1960's, commercial export demand for U.S. foodstuffs has expanded rapidly. Although cotton exports declined, dollar value of all commercial farm exports more than doubled between 1959 and 1965; exports under U.S. foreign assistance and surplus disposal programs rose about 30 percent.

The combined effects of increased exports and land retirement permitted a large reduction in surplus stocks without an appreciable decline in the level of farm prices. Between 1961 and 1965, wheat

stocks dropped 42 percent, and feed grain, 36 percent. But cotton stocks rose 96 percent. Total value (constant prices) of wheat, feed grain, and cotton stocks declined 17 percent. The ratio of prices received by farmers to prices paid by farmers (1910-14 = 100) stood at 79 in 1961, 77 in 1965, and 80 in 1966.

The mix of products in total farm output has shown some imbalance in recent years. The relative balance position of wheat, a problem in the 1950's, has been greatly improved as a result of production controls and export expansion. Cotton is now the main problem product. Since 1960, cotton exports have declined, and stocks have increased to record levels. Hog production also appears to have been appreciably out of balance, reflecting the contraction phase of the hog cycle. This is now being corrected by an expansion in hog numbers. Imbalances in the product mix are relatively easy to correct, since farmers are quite responsive in the short run to changes in differential returns from production of different products.

The farm industry has scored poorly with respect to the minimum cost goal. With a given set of product prices, there are wide interfarm differences in the long-run earnings of labor and capital that cannot be accounted for by inherent qualitative differences. This imbalance has its origin in the changing pattern of resource productivity and input prices associated with technological advance and economic growth. Some farmers have made adjustments in size and in the mix of land, labor, and capital, enabling production at near minimum costs. The vast majority, however, have lagged. Some have fallen behind badly.

In a recent study, it was estimated that in 1959 if all farms in the North Central states had been as efficiently organized as the most efficient farms, total output would have nearly doubled, and total resource costs would have declined 10 percent. There is a large gap between actual cost and the goal of minimum cost.

In a long-run context, reducing output by land retirement increases the real cost of producing the nation's food and fiber supply. Insofar as land withheld from production in recent years could be substituted for labor and capital, inputs with relatively high opportunity costs, the total cost of producing the control level of farm output could be reduced.

Equity

With respect to equality of income opportunities for labor and capital, the farm industry has compared unfavorably with that of

most other industries. Estimates for 1959 indicate that the typical commercial farm in the North Central states paid a reward (including government payments) for labor and investment capital only about one-third as large as that paid "comparable" resources in the non-farm economy.

The reward to labor has shown the greatest disparity. With advances in farm technology, the minimum cost resource mix has moved in the direction of more capital and less labor, inducing a redundancy of labor. Since farm labor has not declined as much as the decline in demand, labor earnings have been depressed relative to capital earnings.

During much of the period since 1950 rewards on well-organized farms have been fairly well in line with those in nonfarm employment. This probably would not have been true without the support programs. But only a small proportion of all commercial farms have been in the well-organized category.

With respect to equality of opportunity to participate in welfare programs and public service, the evidence is not very clear for some programs and services; it is more adequate for others.

Certainly farmers made real progress toward equality on a major front when they were included for participation in social security.

Farmers may be at some disadvantage in using the federal-state cooperative employment service. Available evidence does clearly suggest that employment aspirations are lower among rural people than among urban people of comparable ability.

The clearest inequality of opportunity for public services is in education. The research evidence on this point all seems to indicate that children from farms and small rural communities are at a decided disadvantage. Schools in rural areas have not been supported as adequately as in urban areas and the poorer the area the less adequate has been the support. In many farm areas, elementary teacher salaries have been low and have not been competitive in the national market for well-trained personnel. Evidence indicates that teacher quality is closely associated with teacher salary levels.

Graduates from small rural high schools have not been as well prepared for college entrance as those from urban and metropolitan schools. A smaller proportion of young farm people go to college, which probably reflects not only poorer preparation but also differences in incomes, occupational preferences, and values attached to higher education. Vocational and technical education beyond

high school has been less available for young people on farms than for young people from urban areas, although this difference now seems to be diminishing.

Since investment in education plays a critical role in economic growth and agricultural adjustment, and in providing equality of income opportunities and distributive justice, the elimination of the educational gap is of paramount importance.

With respect to the income distribution goal, price and income support programs since World War II have provided substantial income benefits for commercial agriculture. These income benefits have been induced partly by maintaining prices persistently above uncontrolled free market levels and partly by direct government payments to producers.

The amount of income benefit received by the individual participating producer has been related directly to the size of his farming operation. Thus, the dollar benefit received by the large producer has been much greater than that received by the small producer. Since large producers tend to have higher incomes than small producers, the effect has been to widen absolute income differences among farm families. Moreover, many of the larger producers receiving program benefits have had higher incomes than people who have contributed to these benefits through higher prices and higher taxes. As a result of the methods used to redistribute income, there has been a strong tendency toward greater inequality rather than less.

Pursuit of economic growth and efficiency may also have unequalizing effects on the distribution of income. For example, it is highly likely that public investment in agricultural research and extension activities has increased income differences within agriculture. Of course, this has not been the objective of these activities but rather a side effect. In the case of the price and income support programs, the main objective has been to redistribute income, but the income distribution effects generated have been inconsistent with available indicators of the national concept of distributive justice.

Stability

The short-run stability of agriculture seems to have been relatively good. The success of general economic stability policy has minimized sharp shifts in domestic demand for farm products. Farm prices have shown only moderate year-to-year fluctuations under the support programs. Storage policy has helped to stabilize the flow of feed grains into animal production.

Until recently stocks were permitted to grow to levels higher than needed for stabilization purposes with attendant heavy carrying charges. And because support programs did not fully recognize the product and resource allocation functions of prices, the cost of additional price stability has been unnecessarily high.

Some parts of the industry still experience self-generating cycles of overproduction and underproduction accompanied by inverse price movements. Past support programs have done little to temper this kind of instability.

ADJUSTMENT NEEDS

The performance gaps relating to production efficiency and equal income earning opportunities reflect a serious lag in the adaptation of the industry's resource structure and organization to the forces associated with economic growth.

An indication of the extent of the adjustment lag is provided by a study of what the commercial farm industry (Census definition) of the North Central states would have looked like in 1959 if it had been meeting the goals of production efficiency and equal income earning opportunities. The number of commercial farms would have dropped from 1,171,000 to 306,000. The input of labor would have declined 66 percent. And total investment in land and operating capital per farm would have increased from \$63,000 to \$212,000. Although some of the estimated change reflected an adjustment to eliminate the overproduction of farm products that existed in 1959, most of it reflected an adjustment to meet the minimum cost goal.

For the next decade or so, adjustment needs are likely to be much the same kind as those of the recent past but perhaps with some decrease in magnitude. The adjustment lag, particularly with respect to the number and organization of individual farms, is so large that even changes in the direction of some of the determinants are unlikely to reverse the pattern.

Export Demand

It now seems likely that commercial export demand for U.S. farm products will continue to grow, although probably at a much slower rate than it did in the 1961-65 period. Most of the increase will be in foodstuffs, especially feed grains and soybeans. U.S. cotton faces increasing competition from synthetics and expanded foreign production, and the longer-run export prospects are not favorable.

Perhaps the biggest uncertainty in the export picture is food aid.

If recent developments are indicative of future trends, greater emphasis in assistance programs on population control and building food production capacity in underdeveloped countries will restrain aid expansion in the form of food. But even if future food aid were to be geared largely to meeting emergency famine conditions abroad, the volume of such aid may be as large as that of recent years and possibly larger.

Domestic Demand

Domestic demand will continue to grow as a result of increases in population and rising per capita income. But a decreasing rate of population growth and a declining income elasticity of demand may hold the increase in domestic demand to less than that suggested by earlier projections.

Resource Productivity and Farm Incomes

Farm resource productivity is likely to grow at least as fast over the next decade as over the past decade, probably faster if the minimum cost gap is reduced. There seems to be no indication that public and private investment in agricultural research and development activities will decline. Investment in general education is increasing rapidly, and any substantial reduction in agricultural education seems improbable. Moreover, there appears to be a large current "technological gap."

The farm industry will still require much resource adjustment to meet the goals of production efficiency and equal income earning opportunities. A large amount of resources, particularly human resources, will likely have to be transferred out of farming over the next two decades. Keeping market supply in line with demand at prices permitting comparable income opportunities for labor and capital on well-organized farms may not be as difficult.

Some indication of the adjustments needed to meet these goals in the North Central states is provided by a recent study projecting the characteristics of an income-efficient commercial farm industry (Census definition) in 1980. Under the income-efficient organization (2 percent factor productivity growth assumption) projected for 1980, total labor input was down 74 percent compared with the commercial farm situation in 1959. Total capital input was 45 percent less, and total land input 3 percent less. The number of commercial farms declined 71 percent. In line with the assumed rise in resource productivity and the clearing of markets at efficiency prices, the ratio of prices received by farmers to prices paid by farmers (1910-14

= 100) was down to 56 compared with an actual ratio of 81 in 1959.

On a per farm basis, the differences were even more extreme. For the income-efficient organization, the input of land and buildings was up 238 percent. Operating capital per farm was 97 percent higher. Total investment (constant prices) in operating capital and land and buildings per farm was projected at \$188,000 compared with \$63,000 in 1959. But labor input per farm was only 9 percent greater. Output per farm was 262 percent higher. Earnings of labor and investment capital were equated with projected opportunity costs and were 475 percent greater than in 1959.

Most of the difference between the projected values and the 1959 actual values reflected an adaptation to the adjustment lag which existed in 1959.

These projections, of course, are subject to substantial errors. Nevertheless, the conclusion still emerges that large adjustments in the structure and organization of North Central agriculture will be needed to meet performance goals by 1980. It is my belief that the needed adjustments are well within the range of feasibility, considering past accomplishments and future potentialities.

FUTURE POLICY DIRECTION

In the foregoing discussion, we have identified major performance gaps in: (1) production efficiency relating particularly to the goals of supply adequacy and minimum cost, (2) income earning opportunities for labor and capital on commercial farms, (3) participation in public services, and (4) distributive justice.

The policy instruments and programs needed to reduce these gaps and improve the over-all performance of agriculture are at hand. Some are already being applied, although in certain instances the level and mix of program activities probably need major modification. Others are available for use if and when they become politically acceptable. Some of the more important program needs can be met by the appropriate application of general programs to the farming sector. This is especially true in the area of human resource policies.

A necessary condition for improving the over-all performance of the farm industry is a high and stable level of nonfarm economic activity. If the adjustment of labor from farm to nonfarm jobs is to proceed smoothly and rapidly, alternative employment opportunities must be available for potential farm entrants and for existing farm

workers who may wish to obtain nonfarm jobs. A high level of non-farm economic activity also is conducive to a strong domestic demand for farm products. Consequently, the farm industry has a large stake in the appropriate application of monetary and fiscal instruments to achieve over-all economic stability.

Commercial agriculture also has an important stake in the nation's foreign trade policy. Much of the expansion in farm exports to Japan has been made possible by the growing volume of U.S. imports of Japanese manufactured goods. Liberalization of trade can provide larger farm markets in Western Europe and some of the underdeveloped countries. On balance, it appears that U.S. agriculture has much more to gain than to lose by a more liberal trade policy.

If the adjustment in manpower on farms is to take place rapidly, monopolistic restrictions on entry into particular fields of employment must be minimized. In some occupations, apprenticeship, recruiting, and licensing requirements are far stricter than can be justified on grounds of public health and safety and limit entry of prospective employees.

The performance goal relating to resource ownership and control arrangements is that these arrangements in the farm industry meet the same criteria for social acceptance as those in other industries. A goal of owner-operated family farms was not specified because such a goal has become increasingly competitive with other goals, and there is little evidence that a majority of people would be willing to pay the necessary price (sacrifice of other goals) to achieve it.

The era of the "agricultural ladder" (farm hand — renter — owner) has ended. Wages paid hired men do not permit saving the needed capital to enter farming with an adequate farm unit. In some Midwest areas, farming entrants are almost all sons of farmers buying into the family business.

Many cost economies of size have emerged, and farms have grown larger. The value of land, improvements, farm machinery, and livestock on a well-organized farm today is upwards of \$200,000. Sole ownership of this bundle of resources may no longer be a relevant farmer goal.

In most types of farming, however, the typical well-organized farm of the foreseeable future is likely to be a unit in which management and most of the labor is provided by the farm family. But because of the high level of investment required, the ownership of land and capital resources is likely to become more diffused among rela-

tives and other people. The corporate form of ownership may well become the principal device for intergeneration transfer of well-organized family farms.

Human Resources

The key to long-run improvement in the industry's economic performance is to be found in the developments which influence human resource investment and utilization.

On the basis of data from the Census Bureau and the Public Health Service, we estimate that about one-half of the 1964 population of commercial farm operators (Census of Agriculture definition) will die or reach retirement age (65) by 1980. This large natural withdrawal of farm operators offers a unique opportunity to adjust the number and organization of farms with a minimum of stress and strain. Projections for the North Central states suggest that the number of farms and the number of farmers in 1980 would be in moderately good balance with performance goal requirements.

There is evidence that the decision to enter farming (or to withdraw from it) is strongly influenced by the following factors: (1) preferences and aspirations regarding income, work, and living conditions, (2) expectations about what farming and alternative occupations have to offer in the way of income, work, and living advantages and disadvantages, and (3) the set of resources (for example, skills, initiative, personality, innate ability, and financial backing) possessed in relation to entrance requirements.

To maximize its contribution toward achieving the performance goals, human resource policy for agriculture probably should emphasize: (1) increased educational investment, (2) more information of the kind needed in making rational occupation and employment choices, and (3) educational and adjustment incentives.

A relative increase in educational investment in farm youth can contribute to national economic growth. At the same time, it can contribute to the performance goals of production efficiency, comparable income earning opportunities, and equal opportunity to participate in public services.

Equalizing the quantity and quality of elementary and secondary education available in rural areas can induce higher student aspirations, improved vocational guidance, and more adequate preparation for post-high school training. Equalizing the opportunities available for vocational and college training can provide the skills needed for

a wider range of nonfarm job opportunities and can decrease the competitive advantage held by nonfarm youth in the urban labor market.

Much of the recent emphasis on federal educational investment seems to be heavily oriented toward the needs of urban and metropolitan centers. It is not clear whether these programs will reduce or increase the disparity in educational opportunities for farm youth. In many areas, increased state aid may offer the best chance of eliminating the disparity.

Because of less exposure to employment alternatives, farm youth need more and higher quality information about occupational alternatives and the requirements and opportunities for gaining entrance. They also need more reliable information on the incomes that can be expected on farms having different size and organizational characteristics. Vocational agriculture teachers' contact with potential entrants should be an excellent opportunity to provide such counseling and to explain the adjustment problem of the farm industry.

The farm industry's performance could be improved by providing young farm operators more opportunity to utilize the federal-state employment service.

Reducing the disparity in educational investment per farm pupil undoubtedly will require a larger allocation of public educational funds to schools serving farm youth. It means continued consolidation of rural schools, widening and deepening of curricula, increased emphasis on vocational and technical subjects, higher salaries to attract more qualified teachers, and school integration. Much of the job will rest with local communities, school boards, and educational administrators.

Much research is needed on: (1) understanding educational motivation and the kinds of incentives that induce educational response among farmers and (2) the dropout problem and how best to cope with it.

Human resource policy for agriculture might include special monetary and nonmonetary incentives to encourage participation in educational and job information programs and to induce greater labor mobility. Such incentives might best be offered in a "lump sum" tied to specific performances (for example, a lump sum to defray costs of moving).

Short-run price and income programs should not operate in a way that creates more favorable long-run income expectations than

those warranted by the long-run supply-demand outlook. For example, if under present circumstances farm prices were permitted to increase appreciably before all retired land were brought back into production, it would likely encourage higher longer-run income expectations and induce an increase in the rate of operator entry. Thus, price and production control programs may affect the rate of effective structural adjustment.

Storage, Production, and Price Support Programs

Storage programs are viewed as a method of encouraging farm price stability and a more efficient use of farm products over time. These programs are not an appropriate tool for persistently raising farm prices above free market levels, since stocks will ultimately increase to an unmanageable and costly level. They are an appropriate tool for tempering the effects of year-to-year weather fluctuations (domestic and foreign), seasonal variations in production, and changes in demand due to domestic emergencies or drought and famine abroad.

Private trade may find it profitable to hold some reserves to sell in years of reduced domestic supply. It is unlikely, however, that the commodity trade would view as profitable private storage to meet crisis shortages in underdeveloped countries that lack resources to purchase imports.

The recent decline in stocks of wheat and feed grains provides a new opportunity to reorient storage policy to meet the requirements of a genuine "ever-normal granary."

To be most consistent with the performance goals, long-range producer price targets for farm products should be just high enough to permit opportunity cost returns to resources on well-organized farms. Prices at such levels would provide persistent incentives to less efficient producers to do a better job of organizing their farms and would not penalize the operators of well-organized units.

Long-range producer price targets also should be sufficiently flexible to take account of underlying changes in the conditions of supply and demand. In other words, they should be adjusted for changes in rates of substitution in production and consumption, reflecting developments affecting tastes, incomes, resource prices, and technology. Since such developments typically are slow moving and persistent, the amount of producer price flexibility needed would not be large.

To assure an efficient allocation of products in trade and con-

sumption, short-run market prices should be more flexible than producer prices. This greater flexibility could be achieved by use of direct payments which provide temporary separation of producer and market prices. Price floors should be set somewhat below producer price targets. Then short-run market prices could fluctuate above and below these price targets and move short-run supplies into the channels of trade and consumption, after allowance for storage needs.

A pricing policy reasonably consistent with these requirements might be approximated by a legal formula based on a moving average of actual market prices or by giving the Secretary of Agriculture discretionary authority to establish price targets and floors according to explicit predetermined criteria.

Production control programs which reduce output by encouraging unemployment or less efficient employment of farming resources (for example, land retirement) are basically inconsistent with the long-range performance goals outlined earlier. Recent developments suggest that demand for soybeans, feed grains, and wheat may be growing rapidly enough relative to resource productivity to absorb some of the land currently under retirement and still maintain producer prices high enough to provide opportunity cost returns on well-organized farms.

If structural adjustment proceeds rapidly enough, voluntary land retirement could become a transitional program. If and when structural adjustment has been achieved, land retirement could be used as a standby program to meet short-run excess supply problems. During the transition, however, the land retirement program would continue to redistribute farm income in a way that favors large prosperous farmers.

If price targets make entry into farming too attractive in the short run to achieve the needed intergeneration adjustment in farm size and output, either the opportunity for relatively painless structural adjustment of the industry would be missed or some additional restraints on entry would be necessary. But restriction of entry is inconsistent with the traditional goal of freedom of individual occupational choice. However, if government is to be partly responsible for the outcome via price and production policies, it would not be inconsistent to restrict entry to support and maintain these policies.

A unique opportunity now exists for greatly improving the economic performance of the commercial farm industry. This opportunity has been created by the high proportion of farm operators who will

die or retire during the next two decades, making it possible to achieve a high rate of adjustment in the number and organization of farms at relatively low cost in terms of personal and social disruptions. Two key variables in achieving the needed structural adjustments are the number of entrants and the number of operators who quit for nonfarm employment. The wisdom of our future human resource, farm price, production control, and storage programs will help to determine the extent to which this opportunity is exploited.