



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20561

February 7, 1978

TO: Federal Open Market Committee

FROM: Arthur L. Broida *ALB*

Attached for your information is a memorandum by Mr. Peret of the Board's staff dated February 6, 1978, and entitled "Federal Government Commodity Stockpiling Activities."

This memorandum was prepared in response to a question raised at the December 1977 FOMC meeting.

Attachment

FEDERAL RESERVE SYSTEM

Office Correspondence

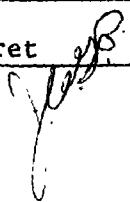
Date February 6, 1978

To Mr. Zeisel

Subject: Federal Government Commodity

From J. Cortland G. Peret

Stockpiling Activities



The Federal Government has four programs which result in the stockpiling of various commodities. Two of the programs, one for crude oil and a second involving other materials strategic to the national security, have as their primary purpose assuring availability of selected commodities during a time of national emergency. Two other programs involve agricultural commodities. One was established primarily for the purpose of providing a minimum price to producers for certain farm products, but this also involves stockpiling of these products--at the present time the period is limited to three months. The other program involving agricultural commodities was designed primarily to encourage the longer-run storage of crops in a grain reserve which can be marketed when certain demand and supply conditions prevail in the market.

These individual programs are described briefly following the table showing the values of the commodities in the stockpiles at the end of 1977.

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VALUE OF COMMODITIES IN U.S. GOVERNMENT STOCKPILES
(Billions of dollars)

	As of December 31, 1977
Strategic Materials	\$8.6
Petroleum Reserves	.1
Agricultural Commodities*	6.5

* Includes both the CCC price-support loan program and the grain reserve program.

The strategic materials program covers 93 commodities and is designed to meet estimated requirements for these materials in time of national emergency. This program is administered by the Federal Preparedness Agency. The quantities of stocks held, or intended to be held, are determined by economic, strategic, and technological factors which may change over time. Stocks of materials held by the Federal Government at the end of 1977 under this program were valued at close to \$8.6 billion; this includes stocks valued at \$4.6 billion being held against specific goals and stocks valued at \$4 billion in excess of current goals. These stocks can be disposed

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of when they are determined to be no longer necessary to national security, providing that their sale does not disrupt commercial markets. At the present time, the strategic materials stockpile has not as yet met the goals set for all materials; reaching the stockpiling objective for all strategic materials would involve an estimated outlay of about \$7 billion in terms of current prices.

The petroleum reserve program, administered by the Department of Energy, is designed to provide a reserve of petroleum products (held mainly in the form of crude oil to be refined later) for national security in the event of a national emergency as well as to provide a supply for civilian non-security use in the event foreign supplies are cut off. This program has as its ultimate goal the stockpiling of about 1 billion barrels of oil by the end of 1985; at current prices this stock would be valued close to \$15 billion. Interim goals of the program are to have in storage 250 million barrels by the end of 1978 and 500 million barrels by the end of 1980. It appears unlikely that the 1978 goal will be met because of the lack of storage facilities; about two-thirds of the total is considered to be a more realistic target. Outlays in calendar year 1977 for this program totaled \$116 million. Outlays are expected to total about \$2.3 billion in fiscal year 1978 and \$3.3 billion in fiscal year 1979.

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The price-support program for agricultural commodities is administered by the Commodity Credit Corporation (CCC) of the Department of Agriculture. Farm products covered by this program are inventoried by producers of the products--these account for the bulk of the stockpiles under this program--and by the CCC. The price supports generally are provided by nonrecourse loans to farmers, using the commodities as collateral for the loan, which enable them to hold off marketings of the product until later in the year when product prices usually are higher than at harvest time. In the case of some farm products, this price support program involves the outright purchases of commodities by CCC from farmers or farm product processors.

The price-support loans may be repaid at or before maturity at the discretion of the farmer-borrower. Repayments of these loans before maturity generally are made only when the market prices of the commodities involved exceeds the support prices. These loans may also be paid off in full by the surrender of the collateral to CCC regardless of the current market prices of the commodities; this method of payment is the usual procedure when the market prices of the commodities are lower than the support prices. Only upon surrender of the commodities in payment of the loan does the Federal Government become the owner of the commodities; it can then hold or dispose of them as desired. It might be noted that even though the Federal Government does not own the commodity until it is surrendered in payment of the loan, the

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the granting of the loan by CCC is treated as a CCC purchase of the commodity in both Federal budget accounting and national income accounting.

The grain reserve program--only recently established--complements the price-support loan program and is designed primarily to provide an inventory of grains which could be marketed at a time of reduced current production or market supplies. It is anticipated that a reserve of 30-35 million metric tons of grains will eventually be accumulated and held (and still owned) by producers. This program also has some price-smoothing effects for those commodities involved. Under the grain reserve program--which requires prior participation in the other price-support programs, price-support loans are extended for longer and specifically-stated periods of time of from three to five years. To induce participation in this longer-term program, payments to farmers are made for grain storage costs and for part of interest charges. To encourage the marketing of grain in the reserves, the storage and interest subsidies are to be cut off when prices rise to about 150 per cent of the support level, and the loans are to be called by CCC when market prices of the commodities increase to 175 per cent of the support price.

As of December 31, 1977 the total value of CCC loans to farmers (under both the regular price-support program and the grain reserve program) and inventories owned by CCC was \$6.5 billion; this amount is

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up from about \$2.5 billion a year earlier. Stocks in the reserve program, which total about 2 million metric tons, are currently only a very small portion of the total grain under loan. During fiscal year 1977 the CCC spent \$3.8 billion on various price-support programs and forecasts \$7.3 billion of price-support payments in fiscal year 1978.