

AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

1200 Massachusetts Avenue

Cambridge, Massachusetts

WEEKLY
BULLETIN

January 13

1936

RESEARCH REPORTS

Coming Effects of Current Events

Without question, the sweeping Supreme Court decision nullifying the Agricultural Adjustment Act was the past week's most important event. The decision embraces far more than relief from the confusing congeries referred to as the triple A. It offers the people a chance to reject the imposition of a form of centralized control of the nation's economy essentially alien to the American spirit. Only the stunning effect of a devastating depression made the temporary arrogation of such Federal control possible. With the passing of the emergency, more thoughtful consideration may be given to the preservation of individual and states rights guaranteed by the Constitution.

Immediate Effects of the Decision

Temporary fluctuations in the commodity markets following the decision indicated no serious apprehension of a severe collapse in the prices of farm products. The fact that this important decision was in prospect tended to discourage forward buying of commodities affected during the past few weeks. Now that uncertainties regarding the constitutionality of the AAA are banished, consideration must be given to probable steps to be taken by Congress and the Administration to evolve a new farm policy. As we pointed out in our bulletin of November, 1935, the elimination of processing taxes should be favorable to the public, since the processors should be able to pass on to consumers at least a portion of the reduction in cost of finished products. It also seems probable that some means will be found for continued benefits to farmers under existing contracts so that a minimum of dislocation will accompany adjustment to another Federal farm policy. We do not anticipate any sharp contraction of the buying power of the agricultural population. Already Congress has appropriations under consideration for continued farm benefits.

The decision probably comes as a relief to the more intelligent farmers. Crop limitations and the attempt to maintain farm products at a higher price level than that justified by world demand has in large measure destroyed the foreign markets for the products of American agriculture. There is still a chance that these may be regained, at least in part. When a substitute solution for the farm problem is put forward, we hope that more adequate thought will be given to the foreign market for our surplus farm products.

It is within the power of leaders of both major parties to use the apparent conflict of interest between rural and urban populations for political purposes. At the same time, unusual opportunity is offered to real leadership of statesmanlike quality to subordinate political considerations in seeking a more reasonable solution to the farm problem. Within a short time it will become evident which policy is to be pursued.

Principles Involved

We recommend that subscribers read the complete text of the Supreme Court decision nullifying the AAA, if they have not already done so. The Government's case rested largely upon the authority granted to Congress by the "welfare clause" of the Constitution. In the majority decision, the six justices made the vital point that while Congress may tax the people for funds to be used for the general welfare, it has no power to regulate production within the states. Any powers implied to Congress through the "welfare clause" do not permit usurpation of powers reserved to the states. There is no atom of ambiguity in the statement, "The Act invades the reserved rights of the states," nor in the sentence, "The Constitution and the entire plan of our Government negative any such use of the power to tax and to spend as the act undertakes to authorize."

It becomes quite clear that this decision establishes the principles upon which other basic measures of the New Deal are likewise in conflict with constitutional restrictions. Unless and until the Constitution is amended, an end is put to the assumption of positive and detailed control over the people's private affairs by the Federal Government.

In our Research Report bulletin of November, 1935, we reviewed the most important acts which might in whole or in part be declared unconstitutional. It is not necessary to re-enumerate them at this time. We believe that the more serious question which the recent decision raises concerning the status of the Social Security Act is of immense importance. The decision on the AAA not only suggests that the Social Security Act will be found unconstitutional, but indicates the procedure which may follow its probable abrogation. Processing taxes which have already been paid may never be refunded. It may be assumed, however, that excise taxes collected before the Social Security Act is reviewed by the Supreme Court will in large part be retained in such form as to make repayment feasible in the event that the Act is found unconstitutional.

The State of the Union

On the eve of the President's message to Congress, a financial commentator made the following statement in one of the large urban newspapers:

"The Street expects that the President's message will throw light on the Administration's fiscal program, give a survey of the economic conditions of the country, elucidate the Government's ideas on unemployment relief procedure for the coming year and outline a limited legislative program in this vital political year."

It is hardly necessary to point out that this expectation was not fulfilled. A careful survey of the President's speech fails to show that very much light was thrown on any of the matters enumerated in this quotation. Except the President's comments on the foreign situation, the most definite statement made in the message was: "Based on existing laws, it is my belief that no new taxes, over and above the present taxes, are advisable or necessary." The optimistic implication of this statement seems quite likely to be nullified by Congress during its present session.

The Annual Budget

The President's message to Congress leaves no room for doubt that the Federal budget for the fiscal year 1937 anticipates a sizeable Treasury deficit. The President points to an estimated deficit in excess of one billion dollars as an encouraging comparison with the deficit of over three billion dollars for the fiscal year 1936.

If it were not for qualifications which the President deemed necessary to insert, we should agree that this is a favorable trend. The President's budget, however, is a highly tentative one. Huge benefit payments not provided for in the budget are quite likely to be made to farmers during the coming year. In addition, Congress seems very much in the mood to pass legislation authorizing the immediate payment of the Veteran's Bonus. No amount of juggling with the so-called "profit from devaluation," which some Congressmen propose for financing this expenditure, will alter the fact that it represents a disbursement of the people's money.

In both his budget message and his annual message to Congress, the President stated that additional charges upon the Treasury arising from appropriations not provided for in the budget should be accompanied by the imposition of additional taxes. Although Congress is quite likely to sanction large outlays to the veterans and to the farmers, it seems highly improbable that sufficient additional taxes will be imposed to meet these expenditures.

In our opinion, the budgetary deficit for the fiscal year 1937 will not greatly differ from that of the three billion dollars of the 1936 fiscal year. Under additional laws, the budget calls for outlays over one billion dollars in excess of income. The payment of the Veteran's Bonus, together with the payment of farm benefits not included in budgetary estimates, will easily amount to an additional two billion dollars. If the payment to veterans is made before the end of the present fiscal year, this will, of course, have the effect of adding to the 1936 deficit instead of to the deficit for 1937. In any case, there seems to be no escape from the inflationary effects of continued large Treasury deficits.

Supply, Demand, and Prices

Dominant factors indicate that 1936 will witness a continuation of recovery. A more moderate rate of progress may be considered satisfactory during the next few weeks. While no extensive increase in the volume of consumption goods can be expected, we believe that a further development of the heavy industries is assured. Near-term prospects do not call for rapid resumption of manufacturing activity. With the approach of the spring period of normally rising industrial activity, however, demand should warrant better manufacturing volumes.

Supply

Industrial operations during the past week have been at somewhat lower levels than were those during the closing months of 1935. This is indicated by the more moderate gain in electric power output for the initial week of 1936 over the comparative period of 1935. This was chiefly due to diminished operations in the industrial centers of the Atlantic seaboard.

A forecast of higher operations in miscellaneous manufacturing industries during coming weeks is indicated by the sharp rebound in steel ingot production from the period of holiday lull. Production at 51 per cent. of capacity represents a gain of three points for the week, and represents a response to larger orders from the metal trades anticipating the coming manufacturing season. Firming prices for various steel specifications indicate the satisfactory statistical position of the industry.

Demand

Whatever factors there may be which temporarily affect demand, the greatly increased purchasing power of the people, due to the building up of checking accounts through public spending, remains as a constant force encouraging augmented purchases. Unless some unforeseen occurrences cause a diminution in business confidence, we may expect a continuation of sustained demand.

Prices

The first effect on prices of the Supreme Court decision invalidating the AAA has not been great. Spot commodity price indexes are substantially unchanged from levels previous to the decision. The Dow-Jones Index of Commodity Futures has receded only a point.

It is of interest to note that while prices of commodities such as bread flour, which are affected by the abolishment of processing taxes, are being reduced, a number of commodities free from these special taxes continue firm. The announcement of crude oil price advances of ten to fifteen cents a barrel in the Southwest indicates the first move above the one dollar per barrel rate at which this commodity has been stabilized since 1933.

Any effects which abrogation of the AAA will ultimately have upon commodity prices will be subordinated to the effects of the inflationary forces set in motion by the Government in this country and by the long-term upward trend in world commodity prices which has now been established, following the culmination of the period of severe deflation of the early 1930's.

American Institute for Economic Research is a non-political, non-commercial organization engaged in impartial economic research.