

# AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

W E E K L Y  
B U L L E T I N

March 18  
1940

54 Dunster Street, Harvard Square - Cambridge, Mass.

## R E S E A R C H R E P O R T S

### COMING EFFECTS OF CURRENT EVENTS

#### *Omens from Finland*

Developments in Finland during the past few months, including the peace treaty negotiated last week, will have an important influence on the economic future of the United States. This will not be because Finland may or may not continue payments on her relatively minute debt to the United States; nor is it because we shall apparently make no more loans to that small country. Both the existing debt and the contemplated loans make but an insignificant dollar total in comparison with United States budget figures.

The first important effect on our economic future as the result of developments in Finland will be traceable to the almost complete disillusionment of America's parlor pinks or pseudo-liberals. Too many in this country, who had become enamored with the Russian ideal, had accepted the fallacious notion that the end justifies the means. These misguided liberals have aided the movement toward totalitarianism in this country; some by taking an active part in the New Deal; some by cheering from the sidelines and lending the support of their voices and pens; and some by acquiescence in procedures that could only be justified on the grounds that ultimate attainment of Utopian ends would counterbalance the evils inherent in the choice of means. By far the larger portion of these liberals must now see more clearly that Russia is not the Utopia of their dreams, but is, on the contrary, just another dictatorship functioning in the familiar fashion.

The second important effect of the Russo-Finnish war has been to explode the myth that Russia is one of the world's great military powers, and that the totalitarian bureaucracy and centralized form of government in general necessarily implies great military efficiency, even though it may not be desirable in all other respects. Even unlimited powers in the hands of one man seem to be sufficient to insure efficient functioning of an immense bureaucracy. The so-called man in the street, who is said to do little thinking, must have seen some of the obvious implications of this lesson. If he has, there will be less public tolerance of grandiose experimentation from the banks of the Potomac.

Perhaps the most important effect of the Russo-Finnish affair, especially of its recent conclusion, will be the greatly reduced probability of our early involvement in Europe's wars. As a martyr in the cause of Democracy, Finland was the logical beneficiary of a new crusade to save the world for "Religion and

Democracy." There has been much disturbing evidence that the President was eager to lead such a crusade. The sympathies of the American public were being aroused, and the recent action of Congress in approving a loan to Finland suggested that the emotional response was reaching a fever pitch. Mr. Roosevelt might soon have found a sufficient majority of the public behind him in his efforts to make our weight felt in Europe; and his continued efforts to apply measures "short of war" could easily lead to actual involvement in spite of good intentions.

The most recent developments in Europe have therefore dampened the ardor of American interventionists. What could be sillier than the pleadings of those who would have us save Finland, now that Finland's own neighbors have refused to let their fire departments go to the fire? Although it is certain that we know only a small portion of the truth regarding any negotiations that have occurred between Finland, Sweden, England, and France, it has nevertheless become plainer than ever that Europe's wars must be fought and settled by Europe, rather than by the United States.

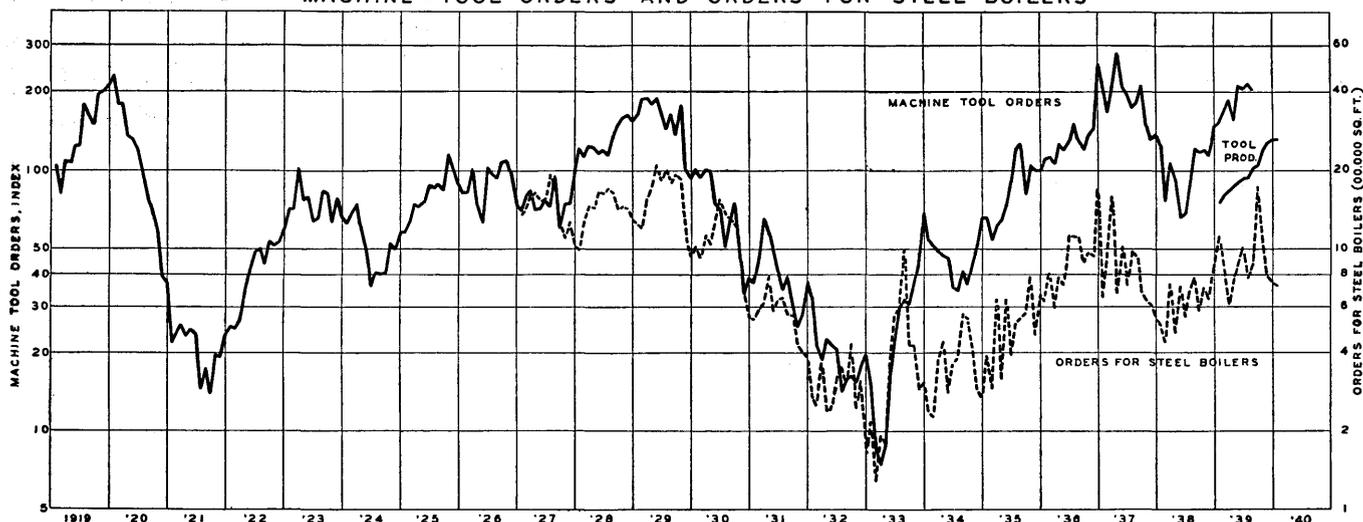
Finally, settlement of the Russo-Finnish war has removed the threat to Germany's source of that essential supply, iron ore. It is also possible that Russia will be able to do somewhat more for Germany, now that war in Finland is no longer draining away manpower and supplies. The possibility of an early collapse of Germany has consequently been lessened; the economic war, at least, will presumably continue, somewhat intensified; and, in the meantime, our domestic economy will be stimulated by demand from South American and other nations that formerly bought in Europe.

#### *Machine Tool Activity and Orders for Steel Boilers*

One of our charts showing indicators of cyclical trends has not been published since July 3, 1939. This chart presented two series, machine-tool orders and orders for steel boilers. Because of the difficulty of obtaining adequate data from an industry receiving a substantial proportion of its orders from foreign sources, the index of machine-tool orders was discontinued at the outbreak of the European war.

The National Machine-Tool Builders Association, which formerly compiled the machine-tool orders index, has recently started a new series, "machine-tool industry operations," which began with data for January 1939. This new series, based on the monthly average

## MACHINE - TOOL ORDERS AND ORDERS FOR STEEL BOILERS



1939=100, has been plotted on the accompanying chart.

During six of the first eight months of 1939, when both series are plotted on the chart, the rate of gain of the orders index exceeded that of the production index. However, after the middle of the year, the orders index tended to remain stable at the high level reached in May while the production index continued to advance. Estimates based on incomplete data indicate that machine-tool orders increased substantially in September from the already high levels of the preceding four months but have since tended to fluctuate within a narrow range somewhat below the September high. The chart shows that the rate of increase in the index of machine-tool industry operations was greatly accelerated during October and November 1939 but thereafter remained about unchanged at a high level.

A comparison of the two machine-tool indexes suggests that the index of machine-tool production is not quite so valuable an indicator of cyclical trends as the machine-tool orders index was, because the former appears to "lag" the orders index by one month. (This conclusion, based on comparison of the two series for only a short period, is of course tentative.) This lag is not particularly important, because, as was pointed out in an earlier discussion, the machine-tool orders index is a more significant indicator of the breadth of recovery movements than it is of other aspects of the business cycle. The influence of the European war as a factor in stimulating activity in the machine-tool industry does not impair the implication that the recovery movement from June 1938 to December 1939 was supported to a considerable extent by rising demand for producers' goods. As an indicator of the cyclical trend during the remainder of 1940, the machine-tool production index is not helpful.

The trend of the index of steel-boiler production has been unfavorable since September. However, the rate of decline since that month has been consistently diminishing, and the decrease in December 1939 was so small as to suggest that the downturn was culminating.

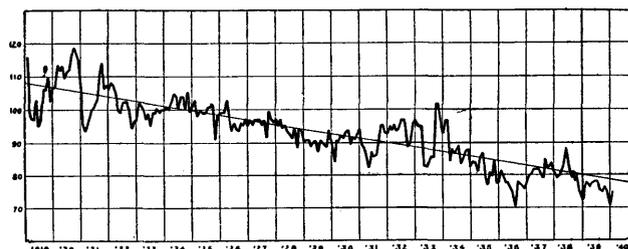
### BUSINESS

#### *Ratio of Retail Inventories to Sales*

The ratio of retail inventories to sales increased substantially in January 1940 from the December 1939

figure. This increase was the result of a substantial decline in sales accompanied by a moderate increase in stocks of merchandise. There was a much greater increase in the ratio of inventories to sales in the New York district than in the ratio for the whole country.

#### RATIO OF RETAIL INVENTORIES TO SALES



Although the ratio in January was lower than the approximate long-term trend indicated by the straight line drawn through the curve on the chart, the index for February will probably more closely approximate the long-term average, because the index of sales in that month was about 2 per cent lower than the index in January. Merchants have recently followed conservative purchasing policies, but an equivalent reduction in inventories is not indicated by available estimates.

#### *Labor Relations under the New Deal*

Data indicating the trend of industrial disputes during 1939 have just become available, and it is now possible to present a statistical picture of labor disturbances

##### WORKERS INVOLVED IN INDUSTRIAL DISPUTES (Thousands of Workers)

	1933	1934	1935	1936	1937	1938	1939
January	9	107	93	59	214	56	72
February	7	161	97	90	239	77	87
March	8	129	99	122	358	106	63
April	14	230	124	95	392	111	420
May	17	234	151	123	441	125	454
June	25	120	130	134	474	96	125
July	49	250	142	125	354	86	207
August	63	163	151	118	239	81	112
September	171	480	514	130	160	133	99
October	94	104	134	149	127	113	136
November	20	95	101	157	119	75	126
December	11	73	62	185	61	62	39
Average	41	179	150	124	265	93	162

during the first seven calendar years of the New Deal. The table on page 48 shows the number of workers involved in industrial disputes in each month during the seven-year period and the monthly average for each of the years shown.

It has been charged by employers and by one of the labor factions that the operation of the National Labor Relations Act has encouraged interruptions of industrial production resulting from labor disputes. The record shown in the foregoing table seems to sustain the charge. The National Labor Relations Act became effective in July 1935, and, although disputes were serious in 1934, disturbances were the most costly in production time lost in 1937, when the monthly average number of workers involved was second highest in the labor history of the country.

During the World War, labor disputes became increasingly serious until the United States entered the war when there was relative improvement, as many of the disputes were settled by the War Labor Board. Immediately after the World War, there was a fresh outbreak of strikes, and, in 1919, the number of workers involved in industrial disputes reached a record monthly average of 347,000. (A discussion of industrial relations in war time with the statistical record is contained in an article on pages 173-174 of the September 18, 1939 bulletin.) An extended period of peace in industrial relations prevailed during the years 1923-1932 inclusive, when the monthly average of workers involved in strikes was only 33,000, and no single labor tie-ups occurred that approached the seriousness of several in the 1916-1920 and in the 1934-1939 periods.

In recent bulletins, we have expressed our opinion that the existing political background favors more amicable industrial relations for the coming year, but there are of course other factors to be considered. If the European war induces a rapid increase in commodity prices and industrial activity, such as that in September 1939, but which is not checked as that movement was, organized labor will naturally endeavor to protect itself by demanding higher wages and will seek to enforce its demands by calling strikes.

## THE FUNDAMENTALS

### Supply

The steel-ingot production rate remained unchanged at 63½ per cent of theoretical capacity last week. The larger volume of export business, together with scattered improvement in the domestic market for steel, was credited with checking the decline, which had persisted through eight consecutive weeks. The *Iron Age* is not definitely convinced that the low point of the current downturn has passed and stated that the present rate "clearly faces further testing as to the ability of mill schedules to hold, and a considerable increase in demand is needed to prevent the production rate from slipping back to the 59 per cent rate which prevailed in early September at the outbreak of the European war."

	1927	1929	1932	1937	1938	1939	1940
Per Cent Capacity	91.5	94.0	25.5	86.0	30.5	56.0	63.5

(Latest 1940 data; corresponding week earlier years)

No change in the rate of miscellaneous manufacturing operations was indicated last week by electric power consumed. The gain in output from that generated in the corresponding week of 1939 remained slightly more than 10 per cent.

	1927	1929	1932	1937	1938	1939	1940
Billion Kilowatt Hours	1.53	1.69	1.54	2.21	2.02	2.24	2.46

Automobile manufacturers expanded production last week in response to an improved volume of orders from dealers in anticipation of increasing public demand. Assembly lines completed production of 103,560 units compared with output of 100,855 during the preceding week.

	1929	1932	1937	1938	1939	1940
Units (000 omitted)	140	31	102	57	84	104

There was a greater-than-seasonal increase in cotton-mill activity last week, and the adjusted index advanced from 131.7 (revised) to 136.6. The price concessions mentioned in last week's bulletin apparently met with immediate response from buyers.

	1929	1932	1937	1938	1939	1940
New York Times Index	*	89.2	139.4	88.7	119.6	136.6

\* Not available until fourth week in March

Lumber production increased last week but not to the extent of the theoretical normal for this season and the adjusted index declined from 82.0 to 80.0.

	1929	1932	1937	1938	1939	1940
New York Times Index	131.9	38.2	80.4	64.6	68.0	80.0

## Demand

It is becoming more certain that the volume of retail sales in March will be very much greater than the totals for January or February. Apparently, the gains are primarily the result of the early Easter. Demand for products of the heavy industries decreased substantially in January and February but has been better maintained during the early part of March, and a turning point may occur within the next few weeks.

## Prices

The sensitive wholesale commodity price indexes were somewhat reactionary during last week. Moody's Spot Commodity Price Index was 159.7 on March 7 and 158.6 on March 14. The Dow-Jones Index of Commodity Futures was 59.99 on March 7 and 58.99 on March 14.

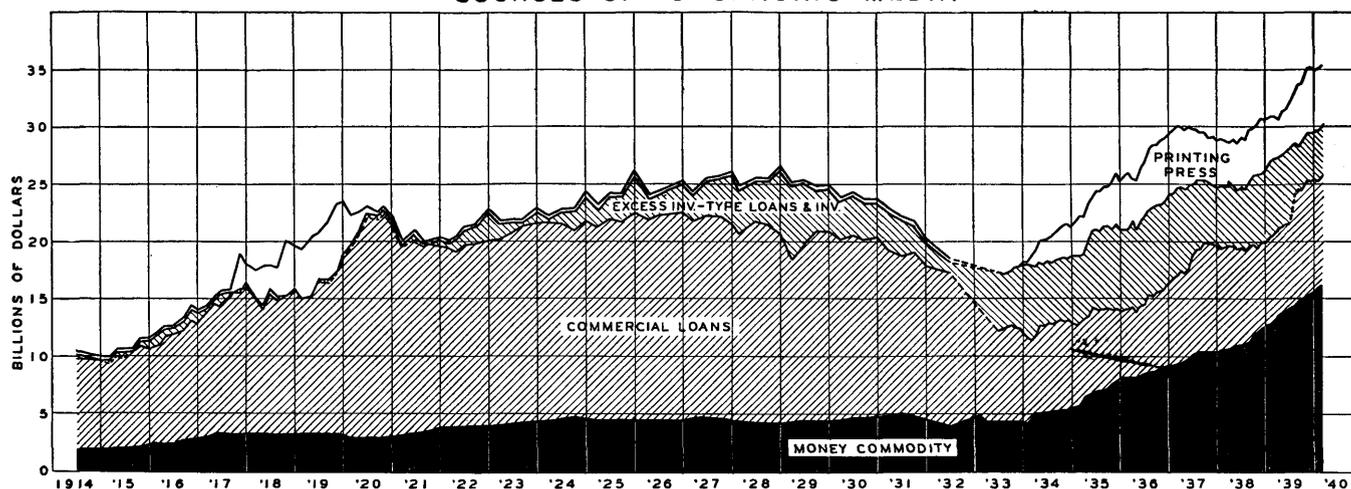
## FINANCE

### Sources of Purchasing Media

The chart showing sources of purchasing media presented in this issue has been revised in accordance with more detailed information now available. The revision covers the period January 1939 to February 1940. It was found unnecessary to make significant changes in the chart with the exception of the section showing purchasing media derived from commercial loans. This will be discussed in a subsequent paragraph. Comparison of the chart on page 50 with that on page 32 of the February 19, 1940 bulletin will show the extent of the changes made.

It will be observed that total purchasing media available to the public during the past six months was somewhat less than was originally estimated. The reason for the change was a revision in the estimate of cash items in process of collection, the value of which is subtracted from total purchasing media. These items, which are referred to as "float," are not available up to date when the monthly calculations are made. Although each item is withdrawn from use only temporarily, there is always a considerable total of checks

## SOURCES OF PURCHASING MEDIA



etc. in the process of collection. Since the creation of the Federal Reserve System, facilities for expediting collections have greatly improved. The total is constantly changing, and, inasmuch as it can be ascertained accurately only on bank-call dates, revisions in the chart are necessary when these data become available. There was an increase of nearly \$400,000,000 in aggregate purchasing media during February, and the total is estimated at \$35,424,000,000, which exceeds the preceding high record made in November 1939 by about \$200,000,000.

There was an increase of \$250,000,000 in purchasing media from the money commodity source during February. This increase was slightly less than the gain from this source during January. The flow of gold to the United States appears to be diminishing moderately. Restrictions now generally prevent the transfer of gold for private accounts. Transfers of gold or release of ear-marked gold from the British Empire may be curtailed if Great Britain is to depend to a greater extent on the disposal of nationalized securities to obtain dollar exchange.

There was a moderate increase in purchasing media derived from commercial loans last month. Beginning in July 1939, the amount of purchasing media derived from commercial loans secured by collateral has been added to that derived from unsecured commercial loans. Changes in the method of reporting data by the Federal Reserve System now make it possible to obtain more accurate figures for commercial loans. During the depression, bankers frequently insisted on security collateral as additional protection for some of their commercial loans. This bank credit was then classified in reports as "loans on securities," although it was created to finance the movement of goods to market. The classification shown in the chart since June 1939 presents a more accurate picture of the situation than that in the period from June 1933-June 1939. However, it is probable that some of the "commercial loans" are not what they appear to be but are actually capital loans to business that the banks prefer to classify as commercial loans.

Commercial banks increased their holdings of Government-guaranteed and "other" securities during February; consequently, there was an increase of approximately \$200,000,000 in purchasing media derived from the third source (an excess of investment-type assets

which represent tangible property with respect to the savings available to the banking system).

The increase in purchasing media from the third source was offset as an inflationary influence by a decrease of \$200,000,000 in purchasing media from the fourth source. The commercial banks disposed of a small amount of their direct Government obligations during February as they did during January. The reduction in Government security holdings during the first two months of 1940 apparently represented distributions to the public and to savings institutions of Government issues purchased in December in connection with the large-scale Treasury operations, which involved heavy refunding and the creation of new Federal debt.

Although Government expenditures during February exceeded those in February 1939 by nearly nine per cent, larger Social Security taxes and other receipts enabled the Treasury to maintain its balances with the commercial banks and with the Federal Reserve banks substantially unchanged. A somewhat more favorable showing, from the Treasury's standpoint, may be expected in March, because the first installment of income taxes, based on incomes for the relatively prosperous year 1939, will then be paid to the Treasury. The net result may be a brief deflationary interlude of a few weeks duration.

## SECURITIES

### *Bonds*

The bond market was steady last week, and the averages remained within a narrow range. The Dow-Jones Average of Forty Bonds was 88.84 on March 7 and 88.90 on March 14.

### *Stocks*

There was no significant change in the character of stock dealings last week. Standard Statistics' average of 420 stocks was 91.8 in January 1939, when the Federal Reserve Board's index of industrial production was 101. The stock price average was at the same level in December, although the Federal Reserve Board's index had advanced to 128. In February the production index had declined to 110 and a further decline is expected in March; yet the stock index is now at the same level as it was in December.

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