AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Economic Effects of "Free" Aid to Britain

The President's new scheme for aiding Great Britain may have far-reaching consequences. As he has suggested, it may be desirable to remove the dollar sign from the transaction, but this will be helpful only if it enables the American public to judge better what sacrifices and dangers are involved. Most citizens have to work for a living, and to them the dollar sign is no vague symbol of financial power but a definite measure of sweat and toil. However, even the great majority of citizens who have this intimate knowledge of the meaning of a dollar have probably found it difficult to visualize the toil and sweat involved in the astronomical sums squandered by the New Deal.

The first estimates of war orders to be placed in the immediate future by Great Britain are about $3,000,000,000. At this rate, especially if the war continues another two or three years, the more than $10,000,000,000 still owed by the Allies of 1914 will be greatly exceeded in value by our new "loans" of equipment to Great Britain. If we follow the President's suggestion and get rid of the dollar signs, it is possible to present the economic facts involved in a manner more readily understood by the layman.

The per capita annual income of all employees in the United States is approximately $1,300, and about one-fourth of the population is thus gainfully employed. This sum therefore supports four individuals of varying age in the average family represented. Even on a chattel slavery basis, and assuming food and clothing obtained at no greater cost than that supplied to families on relief, at least $700 of the $1,300 would be required to support a single family. Therefore, under such conditions, $600 could be taken from each of the 33,000,000 family groups. The total sum would be $19,800,000,000, nearly twice the minimum probably required to finance Great Britain's part in Europe's war.

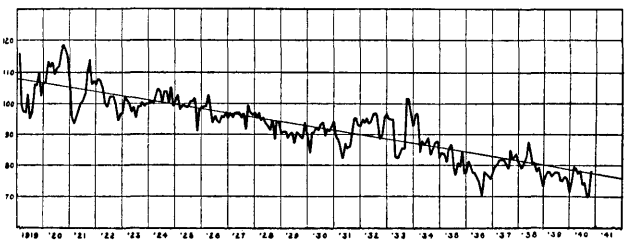
Now that we have the economic facts that the dollar signs represent, the dollar signs can be put aside. The equivalent of chattel slavery for one year, to be endured by about half of the Nation's gainfully employed and their dependents, is the minimum probable price of aid to Britain on the scale apparently contemplated by Mr. Roosevelt. We can believe that a sacrifice of this magnitude would be willingly made by the average worker in order to defend this country directly; perhaps many would even be willing to make the sacrifice for an impoverished Great Britain; but the desirability of making this sacrifice for the largest and wealthiest empire on the face of the globe is not so apparent. The landowners of England also own great estates totaling millions of acres here in the United States, and even greater tracts of land in other parts of the world. Only a small part of the American securities held by English corporations and individuals have been taken by the English Government. Mr. Roosevelt has not yet explained why our gainfully employed should form a great eleemosynary institution for the financial relief of the English landlords and capitalists, when those individuals have the wherewithal to finance their own relief.

BUSINESS

Ratio of Retail Inventories to Sales

The accompanying chart shows the ratios derived by dividing the Federal Reserve index of department-store stocks each month by the Federal Reserve index of department-store sales. The proportion of stocks to turnover has been steadily declining during the period covered by the indexes. Therefore, the current position of the ratio plotted on the chart should be judged in its relation to the approximate long-term trend line that is a feature of the chart.

RATIO OF RETAIL INVENTORIES TO SALES



The chart shows that department-store managers followed a conservative inventory policy during the first ten months of 1940. Stocks have been low in proportion to the volume of sales during most of the period, and the ratio has exceeded the indicated normal only moderately and for brief periods during the year.

Although the Federal Reserve index of department-store stocks is not yet available for November, the index of sales for that month has been published, and the substantial advance recorded makes it probable that the ratio of inventories to sales for the latter month was as

low or lower than any other recorded during the period covered by the chart. The following summary shows the recent trend of the two Federal Reserve indexes from which the ratio is calculated.

INDEXES OF DEPARTMENT-STORE SALES AND STOCKS
(*Adjusted for Seasonal Variations. 1923-25=100*)

1940	*Sales*	*Stocks*
January	92	68
February	89	71
March	89	70
April	89	69
May	87	68
June	91	67
July	91	68
August	99	69
September	99	70
October	91	71
November	101	..

THE FUNDAMENTALS

Supply

The steel-ingot production rate advanced from 96½ to 97 per cent of theoretical capacity last week. The *Iron Age* stated: "Fluctuations are mainly the result of furnaces going in and out before and after repairs. The heavy demand for steel products has not subsided in the major selling areas, though in some sections there has been a moderate let-down which may be only temporary." Although the *Iron Age* a few weeks ago expressed the opinion that the national defense orders would not interfere with supplies of steel for the normal requirements of the country, it now appears possible that deliveries to private domestic consumers may be delayed during 1941 if the national defense program and British requirements absorb a larger proportion of steel tonnage than they have during this quarter.

	1929	*1932*	*1937*	*1938*	*1939*	*1940*
Per Cent of Capacity	63.5	14.5	27.0	53.0	91.5	97.0

(Latest 1940 weekly data; corresponding week earlier years)

Electric-power production last week of 2,862,402 kilowatt hours exceeded output in the corresponding week of 1939 by 9.9 per cent. The gain was approximately the same as that recorded during recent weeks.

	1929	*1932*	*1937*	*1938*	*1939*	*1940*
Billion Kilowatt Hours	1.86	1.55	2.20	2.33	2.60	2.86

The automobile industry increased its total production of cars and trucks from 124,790 in the preceding week to 125,625 units last week. The increase was contrary to the seasonal trend. Inasmuch as the volume of new orders was reported to be decreasing, it is possible that the industry is accumulating stocks of the 1941 models, so that plant capacities may be diverted to national defense production in 1941.

	1929	*1932*	*1937*	*1938*	*1939*	*1940*
Units (000 omitted)	23	31	82	103	118	126

The index of cotton-mill activity declined last week from 161.2 to 155.8 per cent of estimated normal. Although raw-cotton prices continued to fall last week, no price concessions have been made in finished goods. The mills have a large volume of orders on hand, and the Government is issuing invitations to bid on extensive yardages of cotton cloth for military purposes.

	1929	*1932*	*1937*	*1938*	*1939*	*1940*
New York Times Index	101.9	96.1	93.1	125.6	147.3	155.8

Lumber production decreased more than seasonally last week and the adjusted index declined from 99.6 in the preceding week to 94.1.

	1929	*1932*	*1937*	*1938*	*1939*	*1940*
New York Times Index	122.9	34.9	54.4	75.9	92.5	94.1

Demand

The volume of retail sales last week was five per cent greater than it was in the corresponding week of 1939, when holiday sales were making their best postdepression record. This year's offerings of luxury gift items are the most lavish of any since 1929.

Demand for many products of the heavy industries is greater than productive capacity can meet. The decline in the index of machine-tool-industry operations from 138.3 in October to 135.9 in November illustrates the disparity that often exists between blue prints and production. The decline in the index was obviously caused by production difficulties and not to lack of demand.

The metal-trades industries have been abnormally active for more than a year following a period of depression, during which replacements and improvements could not always be afforded. The consequent impairment of manufacturing facilities is now reflected in production delays. Furthermore, the wear and tear on equipment in plants where there are three-shift operations is obviously much more rapid than normal.

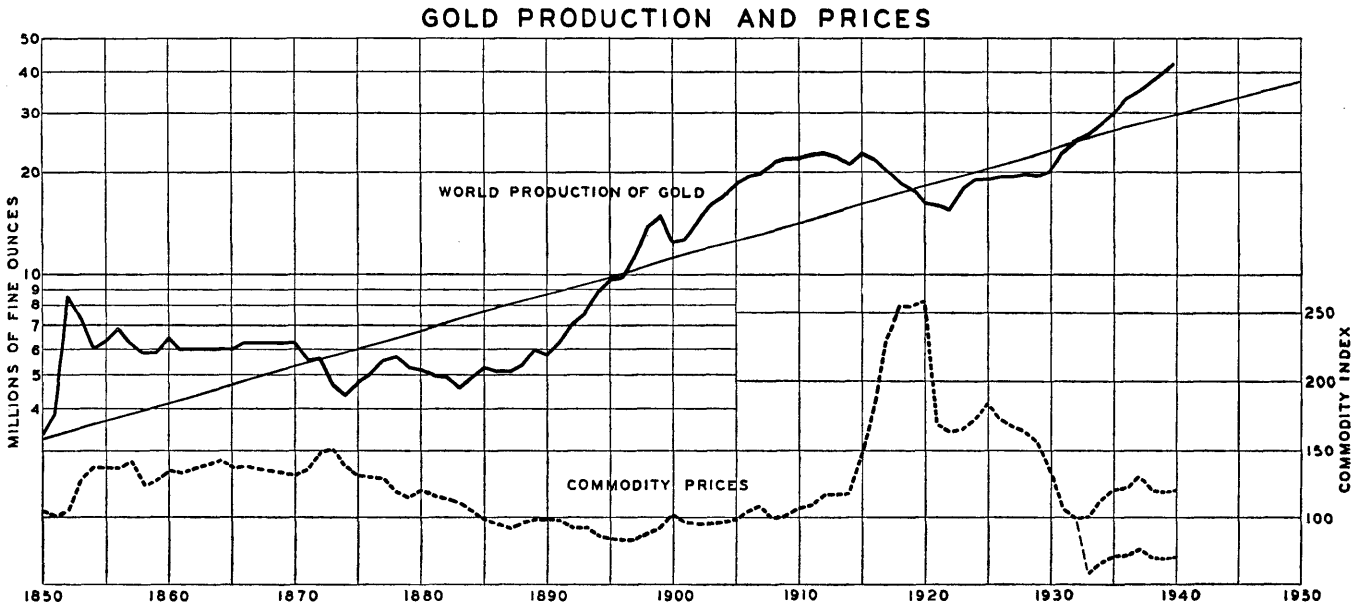
The extraordinary demand probably will be met eventually, and present delays do not surprise experienced manufacturers. The automobile industry is one of the most efficient ever created, but it is not unusual for concerns in this industry to experience costly delays in achieving mass production. More serious delays are much more frequent in work on Government contracts. It is perhaps not generally known to the public that warships have been constructed in private yards according to the Navy Department's specifications and on delivery have been sent to Navy yards for remodeling, a process occupying as long a period as that taken for their original construction. It is no secret that changes in specifications for defense materials recently ordered are responsible for part of the "30 per cent" lag in the defense program. Therefore, it is not surprising that defense orders that often require new machinery and new techniques have not progressed according to schedule.

It is probable that Government officials who are publicly expressing alarm over delays in national defense orders are well aware of the difficulties involved but are endeavoring to spur industry to extraordinary efforts. When the inevitable difficulties incidental to the beginning of the program have been surmounted, American industry will no doubt produce an astonishing volume of war materials.

Prices

There were only moderate changes in the sensitive wholesale commodity price indexes last week. Moody's Spot Commodity Price Index was 168.2 on December 12 and again on December 19. The Dow-Jones Index of Commodity Futures closed at 56.75 on December 12 and at 55.99 on December 19.

After the beginning of the European War, it was found impossible to continue compilation of the combined General Motors-Cornell Index of Wholesale Prices of 40 Basic Commodities. However, separate



indexes for ten countries are now being released weekly. These indexes show that commodity prices have advanced substantially in the nations that either are directly involved in the war or are located within the area where commodity exchanges are hampered by hostilities. Prices in other areas have increased somewhat. The following table presents the most recent indexes, compiled as of December 7, 1940. The base is August 1939 = 100.

Argentina	112	Mexico	111
Australia	126	New Zealand	119
Canada	125	Sweden	143
England	145	Switzerland	164*
Java	119*	United States	119

* Preliminary

FINANCE

Commodity Prices and Gold Production

The Institute's chart, Gold Production and Prices, was previously published in the August 1940 weekly bulletin (page 145). At that time, only preliminary data for the first half of 1940 were available, and a rate of increase in gold production of 8.8 per cent for the year was then indicated. Subsequent data covering production for the first nine months of the year indicate a somewhat smaller rate of gain, although it may exceed the rate of gain for 1939.

The trend of gold production during the past several years is shown in the following summary:

World Gold Production

Year	*Thousands of Fine Ounces*	*Per Cent Gain*
1932	24,098	....
1933	25,414	5.5
1934	27,372	7.7
1935	29,730	8.6
1936	32,100	11.3
1937	35,045	5.9
1938	37,510	7.0
1939	39,604	5.6
1940 (Preliminary)	42,213	6.6

The amount of gold produced each year has an influence on commodity prices, because, as long as gold production continues at a greater-than-normal rate, total purchasing media increase more rapidly than the supply of goods currently being produced. On the other hand, when commodity prices rise to a level higher than normal, costs of producing gold are increased. Production of the metal is consequently discouraged, and annual production decreases. Because the price of gold is fixed in terms of dollars, whereas costs of producing gold usually follow commodity price changes, gold production is stimulated when commodity prices are low and is discouraged when commodity prices are high. A detailed description of the relationship involved, together with a discussion of other aspects of the money commodity, was presented in the February 5, 1940 weekly bulletin (pages 21–23). A similar discussion also is published in the "Explanation of Basic Charts" that has been sent to all subscribers.

An analysis of production by the countries having the most important deposits reveals differences in trends among the individual nations probably attributable to the war. Before the European War, for example in the years 1937 and 1938, there were consistent gains in gold production by all of the major gold-producing nations. Since the war started, the South African gold fields (the largest in the world) have increased production more than in any period during the last decade at least. (Production during the first nine months of 1940 in comparison with that of the corresponding period of 1939 increased 10.1 per cent, but the increase in world production was only 6.6 per cent during this period.) The gains in South Africa reflected a deliberate policy urged on the London mine owners by the British Government to obtain more dollar exchange. On the other hand, there has been some slackening in production in nations where such an incentive has been lacking and there have been increases in commodity prices.

The rate of gain in gold production continues to be greater than the rate indicated by the long-term trend line on the chart, thus showing that commodity prices have not yet risen sufficiently to compensate for the devaluation of the dollar and of other currencies during recent years.

The Harwood Index of Inflation

A moderate inflationary trend during the first half of December was revealed by the Harwood Index of Inflation. The Index advanced from 106.5 to 107.1. During this period, investments held by the banking system increased $220,000,000, and loans on securities increased $90,000,000. Other items were about unchanged, and the increase in all investment-type assets was therefore approximately $310,000,000. The increase in purchasing media created by the banking system was partially offset by an increase of about $50,000,000 in currency hoarded by the public, as revealed by the Institute's estimate. There was no appreciable change in the Government's bank balances, although $100,000,000 was transferred from the Treasury's accounts in the commercial banks to its accounts with the Federal Reserve Banks. This transaction did not affect the money-credit situation.

There was an increase of nearly $300,000,000, or three per cent, in the absolute data for the Index of Inflation. This would have caused a greater advance in the ratio form of the Index had there not been a substantial increase in purchasing media from sources other than bank credit. Purchasing media from the money commodity (gold) increased about $100,000,000. There was an even greater increase in currency in circulation, a seasonal development that has been more pronounced since Christmas-savings clubs have become popular.

During the period from the end of September 1939 to the end of October 1940 (the latest period for which data are available), the Federal Government increased its interest-bearing debt $3,218,000,000. Nearly all of the new obligations were purchased by corporations and individuals who had savings to invest. Of the new debt, $2,340,000,000 was purchased directly by individuals and savings institutions; and $878,000,000 of the new Government securities was purchased by the commercial banks, but most of this also was financed by savings because the commercial banks' savings-type liabilities increased $635,000,000 during this period. Therefore, the increase in inflationary purchasing media would have been almost negligible (compared with the large sums involved) had the Treasury not decreased its bank deposits more than $400,000,000, thereby distributing inflationary credits previously acquired. Apparently, the Treasury can finance a budgetary deficit of $3,000,000,000 from the Nation's savings, but it will surely be forced to resort to inflationary means for meeting the deficit of two or three times this amount that will be incurred next year.

SECURITIES

Bonds

Bond prices advanced during the early part of last week, but most of the gains were surrendered in later dealings. The Dow-Jones Average of Forty Bonds was 90.49 on December 12 and 90.59 on December 19.

Stocks

Stock prices declined steadily but moderately last week. The volume of transactions was somewhat smaller than it was in the preceding week. The action of the market is typical of the year-end tax-selling season.

RECOMMENDED BOOKS

"*Capital Expansion, Employment, and Economic Stability,*" by Harold G. Moulton and Others. The Brookings Institution. ($3.50)

It is unfortunate that Dr. Moulton insists on reviewing some of his earlier statistical studies that have long since been rather thoroughly discredited. Fortunately, however, those data are not the foundation for the present volume. The authors wisely decide that "The conception that the United States has now reached the stage of 'economic maturity' implies — as it did sixty years ago — that little if any further expansion of productive capacity is necessary to provide for the wants of the people. Economic analysis is opposed to such a conclusion. On the contrary, a vast expansion of productive capacity is essential if we are to achieve the standards of living which the American people evidently desire."

The final conclusion emphasizes the importance of the existing taxation system as a barrier to the normal savings-investment procedure. Credit, or rather discredit, is also given to the reckless fiscal policies of the New Deal Administration, which are unquestionably responsible in no small part for the refusal of individual investors to assume business risks by making investments that would readily be made under more encouraging circumstances.

Like most of the Brookings' publications, the body of the book includes much valuable statistical information. The appendices likewise make available in compact form comprehensive data regarding investment outlets, money raised, corporation finance, new security flotations, and so forth.

"*Manufacturers' Product, Package and Price Policies,*" by Albert Wesley Frey. The Ronald Press Company, New York. ($4.50)

This book is "concerned largely with those problems of the manufacturer which revolve about offering to the market the most desirable product and package at the proper price." This activity is commonly called merchandising. It is "the adjustment of merchandise produced or offered for sale to customer demand."

For obvious reasons, the book will be of special interest to those directly concerned with merchandising problems. However, investors may find the volume of value in helping them to appraise merchandise management, so that they may better gauge the competitive ability of companies in which they are interested.

"*Personnel Series,*" American Management Association, New York.

Industrial executives, who have made use of the "Production Series" of booklets listed in our August 12, 1940 Book Review Supplement, may also be interested in recent numbers of the "Personnel Series" listed below: Employee Relations Policies: How to Make Them Specific (50 cents). Labor Economics in a Period of Change (25 cents). Practical Techniques of Industrial Training (50 cents). Values of Psychology in Industrial Management (50 cents). Conciliation and Coöperation in Collective Bargaining (75 cents). New Responsibilities of the Personnel Executive (50 cents).

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