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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Will Inflation Be Controlled?

The announcement made last week by Government defense officials that plans for armament expenditures for the next two years would be revised from \$60,000,000,000 to \$100,000,000,000 will have little immediate inflationary effect, even if appropriations are made to implement this expansion, because the former program contemplated a faster rate of spending than can possibly be achieved for months to come. However, the Government is not only committed to buy as much war materials as the Nation can be spurred on to produce, but the enlarged war-spending program will ultimately necessitate an increase in the proportion of Federal budgetary deficits that cannot be financed through savings. As the Nation's productive facilities are more extensively devoted to the production of war materials, available supplies of consumer goods will become limited. The inflationary purchasing media that are meanwhile being created will appear as demand in a market characterized by shrinking supplies.

Past experience indicates that Government price controls can only postpone but not prevent a substantial rise in commodity prices when there exists an excessive supply of purchasing media available to the public. The bootlegging of commodities at higher-than-legal prices in totalitarian Europe at present is apparently increasing. The volume of trade carried on by the so-called "black markets" has grown in volume there in spite of severe penalties for offenders. Too great reliance therefore should not be placed on the Government's ability to restrain soaring commodity prices in this country.

The hope that inflation will be checked if the war ends before the maximum spending level of the enlarged war program is reached unfortunately may prove illusory. Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System, recently outlined one portion of the Government's post-war plans as follows:

"In the future, the most important safeguard against the danger of a relapse into the intolerable conditions of the early 30's will be a long-run plan for public investment, adapted to differing needs and conditions of our different geographical areas. So far as possible this should take the form of productive public works and expenditures, not only to improve the basic conditions which are responsible for keeping the standards of living in some of our states lower than in others, but

also to raise the standards of living, particularly in the lower income groups wherever they may be."

Judging by this and other statements by responsible Government officials, the Administration's series of emergencies, all requiring enormous Federal spending, will not be concluded with the present one, climactic as this crisis seems to be. A change in the trend from Government spending to retrenchment, the only way by which a disastrous inflationary progression can be averted, appears to be more remote than ever.

THE FUNDAMENTALS

Industrial Production

The leveling off in the trend of industrial activity that was discernible soon after the middle of the year persisted during August and September and developed into a downward movement (after allowance for seasonal factors) during recent weeks. The Institute's revised index of industrial production for September was 146.4, substantially the same as the preliminary index; and the preliminary index for October is 144.0. Durable goods production primarily for defense has increased moderately since June, but the trend of consumer goods production has been downward. Although demand for products classified as minerals is urgent, aggregate production of the mines has failed to increase from the advanced level attained in June. In fact, the seasonally adjusted minerals index was slightly lower in September than it was during the summer months.

The failure of aggregate industrial activity to rise according to seasonal expectations this fall is not surprising. The defense industries are hindered by strikes, material shortages, and the inefficiencies that always develop when rapid expansion in output is attempted. A let-down in the production of most non-durable goods would probably have occurred at this time even if the Government were not deliberately discouraging consumer goods output. Both manufacturers and consumers have been accumulating inventories as a precaution against rising prices. This process sooner or later is limited by financial considerations and storage facilities.

Steel-ingot production in October 1941 was greater than that for October in any of the other years shown in the bar charts on page 174, although it was only slightly more than the total for October 1940, when the industry was operating at practical capacity. The gain in production over output in October 1940 is probably attributable to the increase in plant facilities made during the present year.

IRON AND STEEL PRODUCTION



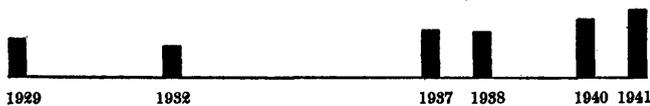
Last week the steel-ingot production rate declined from 97½ (revised) to 96½ per cent of theoretical capacity. The *Iron Age* stated: "This week, as last, strikes figure in ingot production and the Great Lakes Steel Corp. strike at Detroit slashed the operating rate there to 39 per cent from 74 per cent a week ago. Before this strike, the Detroit steel rate was the highest in the Nation at 107.5. In other steel-producing areas, the shortage of scrap was added to strikes as a factor in mill schedules. The steel industry this week continued to book more tonnage than is being produced or shipped, although the influx of new orders is below the record-breaking volume of August."

	1929	1932	1937	1938	1940	1941
Per Cent of Capacity	80.0	20.0	65.0	54.0	95.5	96.5

(Latest 1941 weekly data; corresponding week earlier years)

Production of electric power during October was about 17 per cent greater than output for October 1940. As the bar charts show, production during October 1941 exceeded that for any other corresponding period in preceding years.

ELECTRIC-POWER OUTPUT

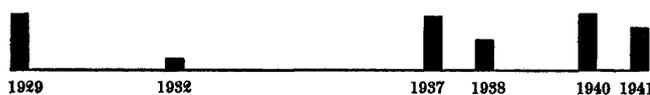


There was a moderate decrease in electric power generated last week, and the gain from output in the corresponding week of 1940, when the industry's production was increasing rapidly, was smaller than was revealed by similar comparisons earlier in the month.

	1929	1932	1937	1938	1940	1941
Billion Kilowatt Hours	1.80	1.53	2.28	2.21	2.84	3.27

Production schedules of the automobile companies for the new-model season have been advanced less rapidly this year than during any other season since 1938. However, a weekly output of 100,000 vehicles may be attained during the late fall.

AUTOMOBILE PRODUCTION

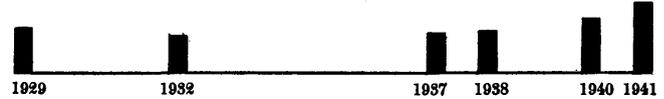


The automobile companies last week produced 85,600 units compared with output of 79,065 in the preceding week. During the corresponding week of 1940, 114,672 cars and trucks were produced.

	1929	1932	1937	1938	1940	1941
Units (000 omitted)	82	13	92	68	115	86

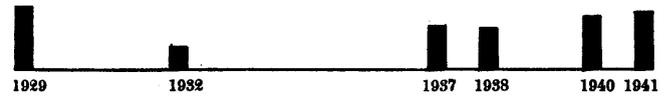
Although cotton-mill activity has decreased somewhat since price ceilings were established by the Government, production during October was at a higher level than was recorded in any previous period shown by the bar charts. The industry enjoys a more stable volume of demand than do the metal trades, but it does not reflect the favorable growth-rate of the electric-power industry.

COTTON-MILL PRODUCTION



Lumber output during October 1941 showed only a moderate improvement over the volume for October in the preceding three years. Unlike the other industries whose activity is represented by the bar charts, the lumber industry has not yet reached the level of activity recorded in 1929.

LUMBER PRODUCTION



Lumber output decreased contraseasonally last week and the adjusted index declined from 125.4 to 122.4

	1929	1932	1937	1938	1940	1941
New York Times Index	124.0	36.8	78.3	75.3	114.7	122.4

The Harwood Index of Inflation

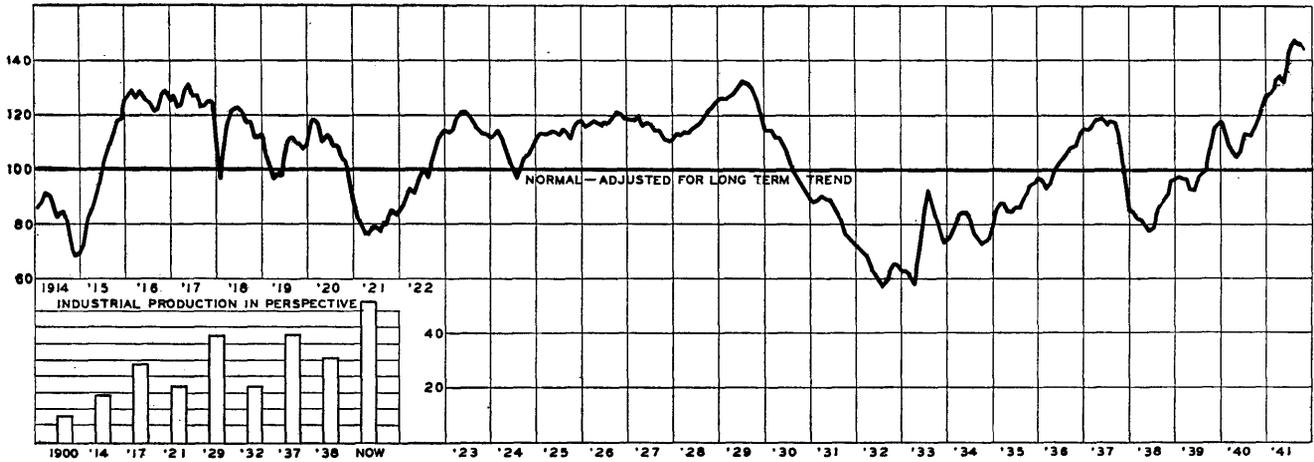
The preliminary Index of Inflation in ratio form for October at 107.3 was about a point higher than the September Index (revised from 106.6 to 106.2). There was no significant change in the volume of bank credit during the first half of October (the preliminary Index was based on reports as of October 15), and the advance in the Index was the result of a substantial reduction in Government deposits with the Federal Reserve Banks and the commercial banks. This indicated the distribution of Government funds to the public.

The chart on page 175 shows the Index in ratio form, which is the ratio of all purchasing media available for use to the portion that is not inflationary. The dotted line on this chart shows the actual totals of inflationary purchasing media. (The scale for the ratio form is at the left side of the chart, and the scale in billions of dollars for the total of inflationary purchasing media is at the right.)

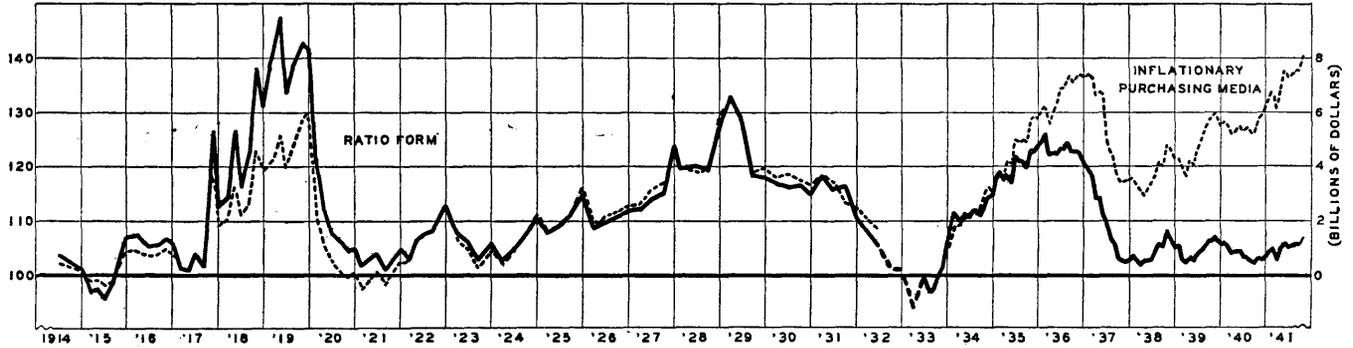
The volume of inflationary purchasing media available to the public at the middle of October was approximately \$8,125,000,000, a gain of \$525,000,000 since the end of September. This was nearly the amount by which Government bank deposits were reduced during the same period. Although the ratio form of the Index shows that inflationary purchasing media are not excessive in relation to all available purchasing media, the actual totals of inflationary purchasing media are at an all-time high, and exceed the peaks reached in preceding inflationary periods such as 1919, 1929, and 1936. It appears probable that the revised Index for October will show a somewhat smaller increase in the degree of inflation than is indicated by the preliminary reports. The settlement day for the Treasury's new \$1,200,000,000 bond issue was subsequent to the date of the bank reports on which the preliminary Index was based. Purchasing media will be withdrawn into Government depositaries to the extent that the new issue was purchased by actual savings.

In order to facilitate study of the fluctuations that have occurred during recent years, the Index has been reproduced on a larger scale in the chart accompanying this discussion. In addition to the Index in ratio form, the absolute data (inflationary purchasing media) for the Index of Inflation and the Institute's industrial production index are shown.

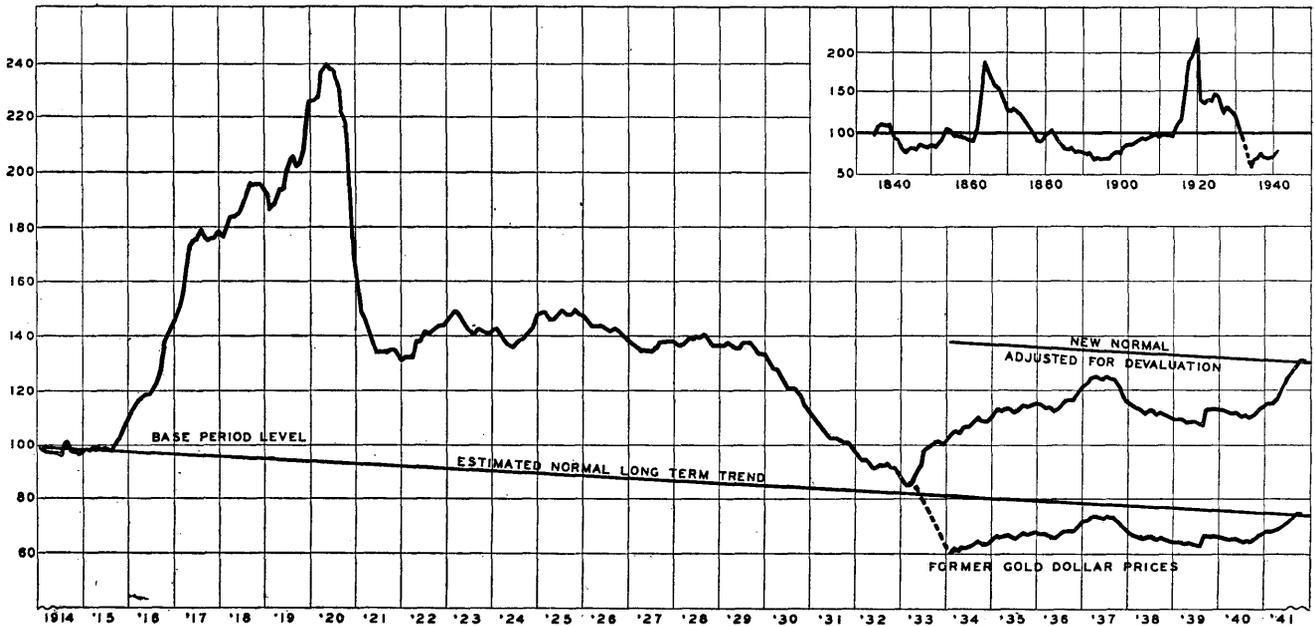
INDUSTRIAL PRODUCTION



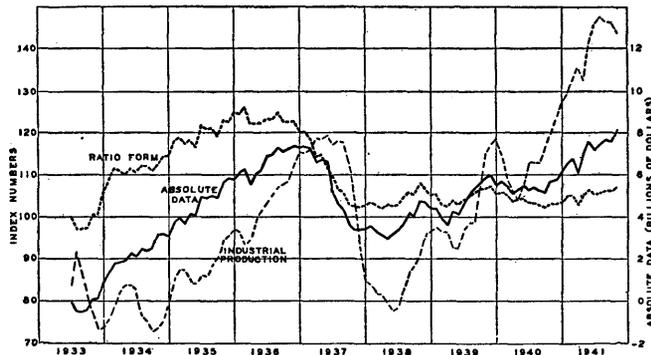
HARWOOD INDEX OF INFLATION



COMMODITY PRICES



HARWOOD INDEX OF INFLATION, RATIO FORM, ABSOLUTE DATA, AND INDUSTRIAL PRODUCTION



The continued upward trend of the two demand curves during the past few months when the rate of industrial activity has been receding suggests that the recession in manufacturing activity will not be extensive. However, during a period when Government actions may exert a dominant influence over economic processes, less reliance can be placed on the usual indicators of future trends than is justified under normal conditions.

Other Demand Factors

Statistics of the volume of retail trade, covering the period since the Government's new excise taxes were imposed October 1, suggest that they have had a moderately adverse effect on store sales. However, this may prove to be only temporary. After the effects of purchases in anticipation of higher prices have worn off, buying may be resumed by beneficiaries of the war boom whose incomes have recently increased substantially beyond the standard to which they were accustomed. The Federal Reserve index of department-store sales was seven per cent higher last week than it was in the corresponding week of 1940, not enough to compensate for the rise in retail prices during the year.

Commodity Prices

For the first time in nearly a year, the United States Bureau of Labor Statistics' combined index of commodity prices failed to advance last month. The preliminary index for October was 130.7, compared with a revised index of 130.9 for September. The sensitive commodity price indexes were reactionary during September and most of October, and this trend was reflected in the more comprehensive commodity price index last month.

Although the average price of raw materials was a point lower in October than it was in September, there were fractional advances in the other two major economic classes, semimanufactures and finished goods. Changes in the commodity classes comprising the principal subdivisions of the wholesale commodity price

index were mixed. Contrary to the usual tendency for prices of farm products and foods to move in the same direction, there was a decline in the index of the former and an advance in the latter index last month. Losses and gains were about equally divided between the remaining commodity classes. The accompanying table shows the changes that have occurred in the major classifications of the wholesale commodity price index. The October 1941 preliminary indexes are compared with the revised indexes of earlier significant periods.

UNITED STATES BUREAU OF LABOR STATISTICS
WHOLESALE COMMODITY PRICE INDEX
(Monthly Average 1913=100)

	Oct. 1929	Oct. 1932	Oct. 1940	Sept. 1941	Oct.* 1941
Farm Products	145.0	65.6	92.9	125.6	124.9
Foods	157.9	94.2	110.7	137.2	139.4
Hides and Leather	162.0	106.9	147.4	163.7	163.6
Textile Products	156.2	96.0	128.4	156.2	157.9
Fuel and Light	135.6	116.0	116.8	130.5	130.7
Metals and Products	109.9	88.4	107.2	108.7	108.7
Building Materials	169.1	124.7	172.5	187.5	186.4
Chemicals	†	†	95.9	109.1	111.0
House Furnishings	168.2	130.9	157.4	173.7	174.6
Miscellaneous	119.2	91.8	110.2	121.6	121.1
Raw Materials	141.1	79.4	103.8	129.4	129.4
Semimanufactures	126.4	81.0	106.0	120.4	120.8
Finished Goods	135.7	100.3	118.3	133.6	134.0
All Commodities	136.2	92.3	112.8	130.9	130.7

* Preliminary estimate. † In process of revision.

Last week the sensitive wholesale commodity prices were stronger. Moody's Spot Commodity Price Index was 203.9 on October 16 and 208.6 on October 23. The Dow-Jones Index of Commodity Futures closed at 76.43 on October 16 and at 80.21 on October 23.

The largest monthly increase in the cost of living since the initial wartime advance in September 1939 was recorded in September 1941. The National Industrial Conference Board's combined index advanced from 89.4 per cent of the 1923 monthly average in August to 90.8 per cent in September. All items participated in the increase, but the largest gains were made by the more sensitive items, food and clothing. The composite index and separate items for September 1929, 1932, 1940 and for August and September 1941 are shown in the accompanying summary.

	Sept. 1929	Sept. 1932	Sept. 1940	Aug. 1941	Sept. 1941
All Items Combined	101.1	76.6	85.7	89.4	90.8
Food	110.3	68.1	78.2	87.3	89.4
Housing	92.3	70.5	87.0	88.6	88.9
Clothing	98.6	64.2	73.1	74.5	76.9
Fuel and Light	93.1	86.0	85.3	88.6	89.4
Sundries	99.1	93.5	98.1	98.8	99.8

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Statistical Summary; Production, Purchasing Media, and Prices

	1940			1941									
	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.*
Index of Industrial Production	120.7	124.3	128.7	129.4	133.0	135.5	132.6	141.5	146.0	147.7	146.5	146.4	144.0
Index of Inflation (ratio form)	103.2	103.0	103.6	105.1	105.2	102.8	105.2	106.6	105.3	105.7	106.1	106.2	107.3
Commodity Price Index	112.8	114.3	114.6	115.8	115.5	116.8	119.2	121.6	124.8	127.2	129.4	130.9	130.7
Commodity Price Index	66.7	67.6	67.8	68.5	68.3	69.1	70.5	72.0	73.8	75.3	76.6	77.4	77.3

(In terms of former gold dollar) * Preliminary Estimate.