AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

If War Is Prolonged

The so-called victory program that has been talked about in Washington during the past few weeks will require the diversion of more than one-half of the Nation's productive capacity to war purposes by the end of next year. If some approach to this program is achieved, its effect will be to reduce domestic consumption down to or below the 1932 level. In 1932 we had productive capacity sufficient to meet the requirements of high living standards, but it was not being used because of economic maladjustments. In 1942 or 1943, the same effect on living standards may result from the use of plants and labor for the production of war materials.

Before Congress grants the authority for the ambitious victory program, its members might give more careful consideration to its objectives than they have when considering earlier requests for blanket defense appropriations that were granted without question. To be sure, legislators have become so accustomed to multiple billion-dollar appropriations that these are no more than symbols having no connection with economic processes of production. Perhaps this is inevitable while extravagance can apparently be indulged in without involving any sacrifices.

Although the Administration has given only a general outline of its victory program, it is no secret that an important share of the enlarged outlays planned is intended for land equipment. For example, a tank-production industry as large or even larger than the Nation's automobile industry is envisaged. When the present experimental and organizing phase of tank production is surmounted and mobile fortresses can be turned out just as automobiles are in normal times, the flow of mechanized equipment will be so great as to raise the question of its disposal.

Even without Senator Pepper's hints of a future expeditionary force, it might be deduced that a production program for land-war equipment in excess of any possible needs for hemisphere defense or lend-lease purposes is intended to implement a second crusade to save democracy. Already priority unemployment and inflationary price increases are more than threats. Before courting more certain economic disaster, Congressmen may ask (1) are the American people ready to make the economic and other sacrifices entailed in a second venture into European warfare; (2) if they are willing or can be "conditioned" into acquiescence, would an expedition be feasible in view of Hitler's difficulties with the English Channel.

No Broad Price Control

The decisive defeat in the House of the Gore plan for over-all control of rents, prices, and wages demonstrates that action sufficient to check the inflation spiral will not be taken by Congress at this time. As we have pointed out in earlier bulletins, control measures that overlook the fundamental causes of inflation can be only partially effective. The restrictions that have delayed the effects of wartime inflation when applied in European countries will hardly be accepted here.

In our opinion, the influence of the labor and farm pressure groups was the dominant factor in defeating the Gore plan, but Mr. Arthur Krock, the *New York Times'* Washington correspondent suggested that another factor played an important part. He charged[1] that Congress is averse to passing legislation that will vest more power over the Nation's economic processes in the hands of New Deal appointees. Experience in recent years has shown that, through partisan administration, quasi judicial Government agencies can extend controls far beyond the scope for which they were ostensibly established.

What Next?

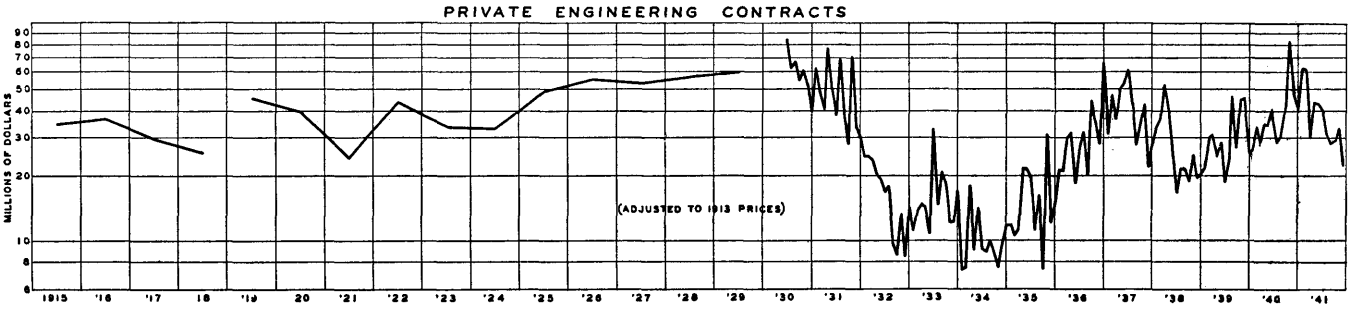
The Continuing Record

The latest available information regarding the more significant indicators of future trends is summarized in the following table. A plus sign indicates an advance in the indicator; a minus sign, a decline; and a zero, an unchanged position.

	Latest Indication
Private Engineering Contracts (November)	−
Machine-Tool Activity (October)	+
Orders for Steel Boilers (September)	+
Capital Goods Stock Prices (Last Week)	−
Durable Goods Employment (October)	+
Steel-Ingot Production (Last Week)	−
Prices of Metals and Metal Products (Last Week)	0
New Capital Issues of Corporate Securities (October)	+
Velocity of Purchasing Media (October preliminary)	+
Carloadings of Heavy Products (Last Week)	+
Lumber Production (Last Week)	−
Harwood Index of Inflation (November preliminary)	−

The number of favorable indicators of cyclical trends increased moderately since the summary was published

[1] *New York Times*, November 27, 1941, page 22.



a month ago. Then there were five pluses, six minuses, and one zero. In this summary, there are six pluses, five minuses, and one zero.

Private Engineering Contracts

The chart at the top of the page shows the dollar total of private engineering construction, adjusted for changes in building costs. The data therefore reflect as closely as practicable the changes in the physical volume of construction activity covered by private engineering contracts. The data are plotted only once annually for the years 1915 through 1929, because monthly figures were not available until June 1930. Prior to that date there are two breaks in the curve, one in 1918, and the other between 1929 and 1930. These were unavoidable, because the data are not continuous for the entire period. Those shown for the years preceding 1930 do not include so large a percentage of all private construction contracts awarded as is included in the data since 1930. However, the earlier figures do give a general picture of trends and totals.

The month-to-month variations in private engineering contracts are so erratic that calculation of a seasonally adjusted index was found to be impracticable. In spite of these irregularities, the longer-term trends of the monthly series are apparent.

During the past decade, two major recovery trends are evident. One extended from the end of 1934 to the middle of 1937; and the other, from the middle of 1938 to the end of 1940. During the past 12 months, the major trend has been downward.

The current decline in private engineering construction coincided with a great expansion in the volume of such projects undertaken by the Federal Government. Much of the engineering construction needed to supply new plants for the production of defense materials has been financed and supervised by the Government, and therefore it is not included in the statistical series shown in the chart. Furthermore, the normal volume of private engineering projects has recently been curtailed by rising building costs and by growing scarcities of essential construction materials. Although the volume of Federal engineering projects will probably continue at a high level for the duration of the war, many private projects must obviously be postponed.

BUSINESS

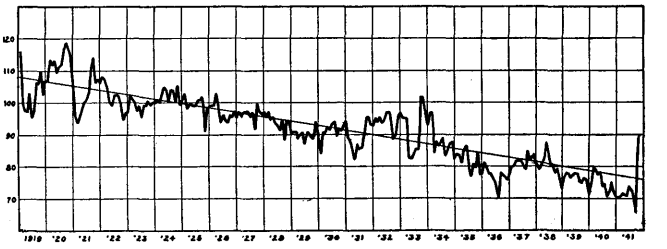
Ratio of Retail Inventories to Sales

The wide fluctuations in the ratio of department-store inventories to sales during the past few months are of course attributable to the abnormal demand-supply situation arising from the war. The value of department-store stocks has been steadily increasing since the beginning of the year and is now about one-third greater than it was in January. In the meantime, the dollar volume of sales has fluctuated widely from month to month. The following summary of the Federal Reserve's seasonally adjusted index of department-store sales (1923–25 = 100) illustrates the movement.

1941	*Index*	*1941*	*Index*
June	104	September	116
July	115	October	104
August	134		

The chart shown below presents the ratios derived by dividing the Federal Reserve indexes of department-store stocks by the indexes of department-store sales.

RATIO OF RETAIL INVENTORIES TO SALES



The position of the ratio in October (the latest month shown on the chart) in relation to the long-term trend line appears to indicate that stocks in the hands of retailers are abnormally large in respect to the volume of sales. However, the holiday-buying season, when the dollar volume of sales is frequently double that in other seasons of the year, is approaching and will afford a test of the situation. If the Christmas trade falls below the optimistic expectations of department-store executives, the retail stores will be left with excessive stocks, and demand for goods at wholesale will be curtailed during the early part of 1942.

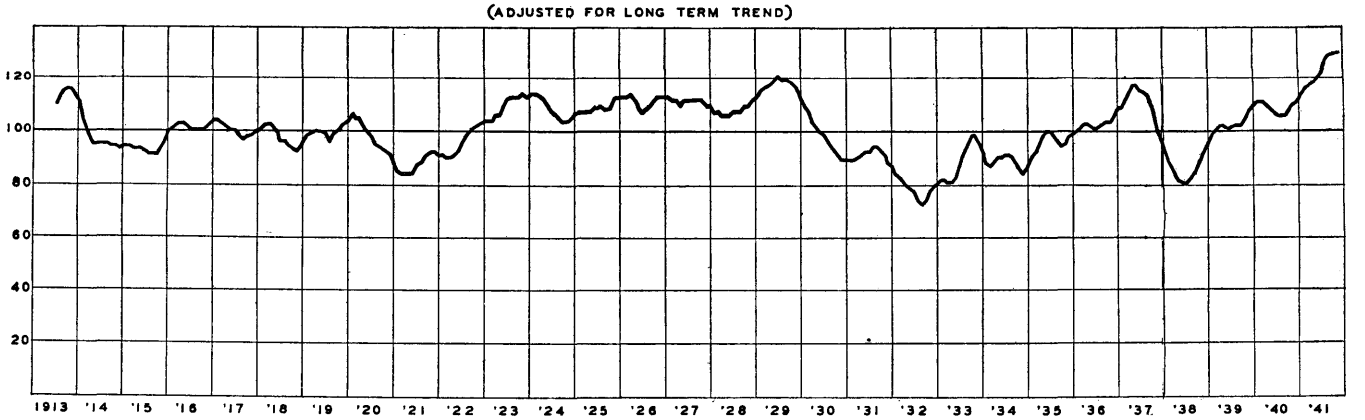
The Trend of Commercial Failures

The liabilities involved in business insolvencies decreased in October 1941 to the lowest level recorded

COMMERCIAL FAILURES, NUMBER AND LIABILITY

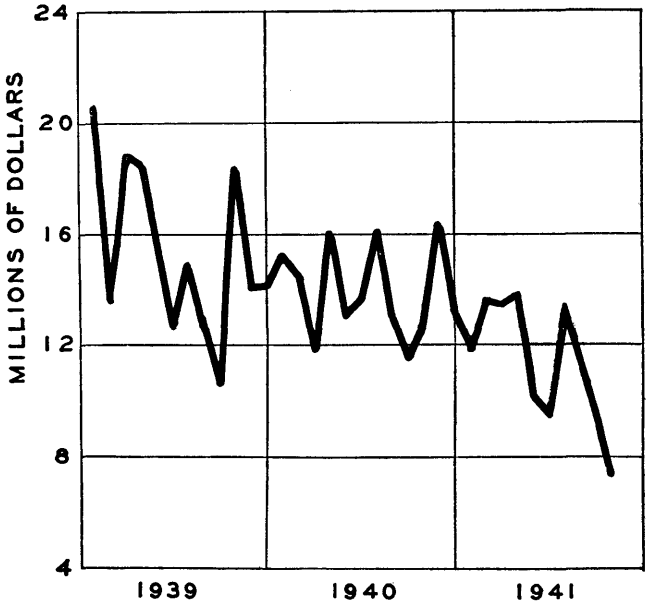
	Number of Failures			*Liabilities of Failures (In Millions of Dollars)*		
	1939	*1940*	*1941*	*1939*	*1940*	*1941*
January	1,567	1,237	1,124	20,790	15,279	11,888
February	1,202	1,042	1,129	13,582	13,472	13,483
March	1,332	1,197	1,211	19,002	11,681	13,444
April	1,331	1,291	1,149	18,579	16,247	13,827
May	1,334	1,238	1,119	15,897	13,068	10,065
June	1,119	1,114	970	12,581	13,734	9,449
July	1,153	1,175	908	14,999	16,213	13,422
August	1,126	1,128	954	12,637	12,997	11,134
September	1,043	976	735	10,545	11,397	9,393
October	1,234	11,11	809	17,464	12,715	7,333
November	1,184	1,024		13,201	16,572	
December	1,153	1,086		13,243	13,309	
Total	14,768	13,619		182,520	166,684	

INDEX OF LIVING STANDARDS
(ADJUSTED FOR LONG TERM TREND)



since the new series was compiled by Dun & Bradstreet beginning January 1939. The number of failures was also moderate compared with those in earlier months shown by the statistical series, with the single exception of September 1941. The number and liabilities of commercial failures during each month of the past two years and during the first ten months of 1941 are shown in the table on page 194.

LIABILITIES OF COMMERCIAL FAILURES



The chart of the liabilities of commercial failures illustrates the steady downward trend followed by the series during the past three years. This trend is unmistakable, in spite of the wide month-to-month fluctuations in the data.

During the first ten months of 1941, total liabilities involved in business insolvencies decreased 17 per cent from the aggregate reported during the corresponding period of 1940; whereas, there was a decrease of only 12 per cent in the number of failures. This comparison, together with the recent increase in the number of insolvencies from the September to the October 1941 level, suggests the possibility that the Nation's transition to a war economy has already caused unfavorable discrimination against the smaller business concerns. The statistical evidence is sufficient only for a tentative conclusion, but, if this trend continues, it should be considered significant.

Index of Living Standards

The method used in calculating the Institute's Index of Living Standards was described in the November 3, 1941 Bulletin (page 178). The chart at the top of this page shows that there was no appreciable change in the Nation's living standards during November. The volume of consumer durable-goods production reached a new high level this summer but has been decreasing this fall. Although the production of nondurable consumer goods failed to increase greatly during the past few months (when allowance is made for seasonal factors), output has been better sustained than might be expected in view of the labor and material shortages that have resulted from the Nation's war effort. The distribution of goods produced this summer has prevented consumers from feeling the effects of the curtailment in durable consumer goods.

The present high level of the Index of Living Standards shows the extent to which the Nation has succeeded in obtaining an apparent advantage from the Government's latest and largest spending spree. The recent leveling off in the trend of the index suggests that this phase of the situation is in the process of changing to a less pleasant one.

THE FUNDAMENTALS

Supply

The steel-ingot production rate declined last week from 97½ to 95½ per cent of theoretical capacity. The curtailment was attributed to the strike in the captive coal mines and to the scarcity of steel scrap. The *Iron Age* stated: "Ending of the coal strike stopped the latest threat to continued production of steel for the defense program and for civilian use. The strike had chalked up another production loss against the defense program, the loss in ingot output in the Pittsburgh area alone being 21,000 tons. Easing of the iron and steel scrap shortage — one of the major industrial headaches of the year — still is far beyond the horizon, and more steel plants have been forced to reduce production because of lack of scrap."

	1929	*1932*	*1937*	*1938*	*1940*	*1941*
Per Cent of Capacity	69.0	16.0	32.0	60.5	97.0	95.5

(Latest 1941 weekly data; corresponding week earlier years)

Electric power generated last week exceeded output in the corresponding week of 1940 by 12.9 per cent. The gain was slightly less than it was in the preceding week.

	1929	*1932*	*1937*	*1938*	*1940*	*1941*
Billion Kilowatt-Hours	1.72	1.48	2.07	2.19	2.84	3.21

The daily average production rate in the automobile industry remained about the same last week as it did in the one preceding, although total output was curtailed by the holiday. Assemblies totaled 76,820 units, compared with production of 92,990 units in the preceding week and 104,444 in the corresponding week of 1940.

	1929	*1932*	*1937*	*1938*	*1940*	*1941*
Units (000 omitted)	28	13	59	84	104	77

Cotton-mill activity decreased contraseasonally last week, and the adjusted index declined from 156.1 (revised) to 153.7. The Government is now purchasing nearly one-third of the industry's finished-goods production and may increase this proportion next year. Although there is a plentiful supply of raw cotton, it is estimated that capacity operations in the cotton-goods industry next year may not suffice to meet household demands after supplying Army requirements.

	1929	*1932*	*1937*	*1938*	*1940*	*1941*
New York Times Index	102.8	105.4	100.1	122.2	131.6	153.7

Lumber production decreased more than seasonally last week and the adjusted index declined from 134.0 to 125.8 per cent of the 1935–1939 monthly average. For the first time this year the index was lower than it was in the corresponding week of 1940.

	1929	*1932*	*1937*	*1938*	*1940*	*1941*
New York Times Index	124.0	33.8	58.7	70.4	129.3	125.8

Demand

Gains in the dollar volume of retail trade from last year's levels were less evenly distributed throughout the country last week than they were earlier in the year. This may be a reflection of the shift in pay-roll distribution occasioned by the concentration of defense production in limited areas. In general, the value of sales exceeds the dollar volume of last year. However, the Fairchild retail price index has advanced about twelve per cent during the past twelve months, and the physical volume of consumer-goods distribution has apparently made only a slight gain. Holiday buying is starting early this year, as it did last. Christmas-club savings are reported to have increased this year but have not kept pace with the increase in prices. Although there is a broader demand for many luxury items, the market for the most expensive goods is already being adversely affected by the certainty of higher surtaxes next year.

Prices

The sensitive wholesale commodity price indexes moved irregularly last week. Moody's Spot Commodity Price Index was 209.4 on November 21 and 208.4 on November 27. The Dow-Jones Index of Commodity Futures closed at 81.08 on November 21 and at 80.79 on November 27.

The National Industrial Conference Board's combined cost-of-living index advanced slightly more than a point during October. There were gains in each of the five separate items, but changes in housing and in fuel and light costs were confined to fractions. During the 12 months ending last October, the combined index advanced 7½ per cent, primarily as a result of a 17 per cent increase in food prices and a seven per cent increase in clothing prices. Rentals increased only two per cent. The composite index and separate items for October 1929, 1932, 1940, and for September and October 1941 are shown in the accompanying summary.

	Oct. 1929	*Oct. 1932*	*Oct. 1940*	*Sept. 1941*	*Oct. 1941*
All Items Combined	101.2	76.0	85.5	90.8	91.9
Food	109.9	67.7	77.4	89.4	90.7
Housing	92.1	69.6	87.4	88.9	89.2
Clothing	99.0	64.4	73.1	76.9	78.3
Fuel and Light	94.0	86.3	85.9	89.4	90.0
Sundries	99.9	92.3	98.1	99.8	101.2

FINANCE

New Capital Issues

There was an encouraging increase in the volume of new corporate financing during October. With the exception of two months in which large issues of American Telephone and Telegraph bonds were sold, the aggregate value of $103,000,000 in new capital issues marketed during the month was the largest for any month in recent years. The total of $873,000,000 for the first ten months of the year was larger than it has been in any corresponding period since 1937.

About three-quarters of the October total was borrowed by industrial corporations, most of the remainder by the railroads, and only $6,000,000 by public utilities. An unusual feature of the October financing was the large proportion (more than one-half) that represented common stocks. This was the first time since 1937 that there has been an appreciable proportion of new financing through this medium.

New corporate financing in October and in the first ten months of each year during the past sixteen years is shown in the accompanying summary.

New Corporate Financing in the United States

Year	*October* (*In Millions of Dollars*)	*First Ten Months*	*Year*	*October* (*In Millions of Dollars*)	*First Ten Months*
1926	276	3,621	1934	....	135
1927	562	4,284	1935	73	304
1928	515	4,035	1936	110	876
1929	646	5,972	1937	67	1,142
1930	148	4,398	1938	64	766
1931	17	1,659	1939	20	329
1932	49	305	1940	48	504
1933	3	138	1941	103	873

Source: *Commercial and Financial Chronicle*

SECURITIES

Bonds

Bond prices remained about unchanged last week. The Dow-Jones Average of 40 Bonds was 90.38 on November 21 and 90.25 on November 27. The United States Treasury last week announced that it intended to market a $1,500,000,000 issue of National Defense Bonds in December. A budgetary deficit that will run well over $1,000,000,000 in November is depleting the Treasury's bank balances.

Stocks

The fact that year-end corporate disbursements announced during November were more generous than they were last year failed to affect the market for common stocks favorably. The market has been handicapped by tax selling, unfavorable foreign news, and such adverse domestic developments as labor demands, higher taxation, and the cyclical business recession that appears to have begun.