

AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

A More Realistic Approach?

Last year, when the Nation was actively engaged in an ambitious defense effort, we commented from time to time on the President's unwillingness to make the fundamental changes in his policies that were required by the new circumstances. In the April 28, 1941 bulletin under the heading "Defense vs. New Dealism," we said in part:

"Serious misgivings have been voiced in Congress over the appointment of Harry Hopkins, social reformer rather than administrator, to direct the huge lend-lease program. Recent reports of greatly enlarged spending plans invite the suspicion that the New Dealers are more concerned with the opportunity to promote their socialistic theories than they are with either aiding Britain or bolstering our own defense."

The apprehensions of Congressmen appear to have been justified. The President's report on lend-lease aid as of November 30, 1941 showed that, after more than nine months, only \$1,200,000,000 worth of the first lend-lease appropriation of \$7,000,000,000 had been transferred to the beneficiaries in the form of goods and materials.

Again in the July 28, 1941 bulletin under the title "Control," we quoted the statement by the editor of *The Iron Age* that summarized the mounting criticism of the President's failure to appoint a single responsible person to direct the Office of Production Management. Now that the President has made what appears to be a satisfactory appointment to head the direction of the most important part of the Nation's economic war effort, we believe that it is appropriate to repeat the concluding sentences of Mr. Van Deventer's excellent statement:

"Control of power is the cardinal and basic necessity for getting things done. As I said, we take it for granted. Yet underneath it lies not only an adequate organization of the physical means of distributing power but beyond and above that, its control by someone who knows what is going on and what is needed from moment to moment. . . .

"We have the finest equipment and the best resources in the world to make more of anything than any other people, anywhere. But what we lack is an experienced hand in the control room."

Assuming that Mr. Nelson's organizing abilities are employed as successfully in his broader task as they

were in solving the difficult problems of priorities, the statement on "Control" should now be as heartening as it was discouraging six months ago.

The President's extraordinary wartime powers and his great influence over popular sentiment in the country make his trend of thought of primary significance. Before Japan struck, it was apparent that the President was just as adverse to abandoning any of his social objectives to promote a more efficient defense effort as he was reluctant to delegate policy-making powers. The creation of the War Production Board with special powers given to the chairman afforded the first important evidence that the President is now prepared to subordinate the policies that hitherto determined the trend of Government under his administrations and to concentrate on practical measures necessary to win the war.

This evidence was supported by the President's characterization of the Senate's so-called price control bill as a measure for promoting inflation and the implication that he would veto unsatisfactory price-control legislation. This indicated a stiffening attitude toward politically powerful pressure groups. The evidence that he is prepared to take a similar attitude toward organized labor is not yet apparent.

There are other ways in which the President can demonstrate his willingness to make the all-out effort for victory that he is asking of the country as a whole. For example, he would do well to abandon such schemes as the St. Lawrence Waterway project that are of doubtful defense value and that the country can now ill afford.¹

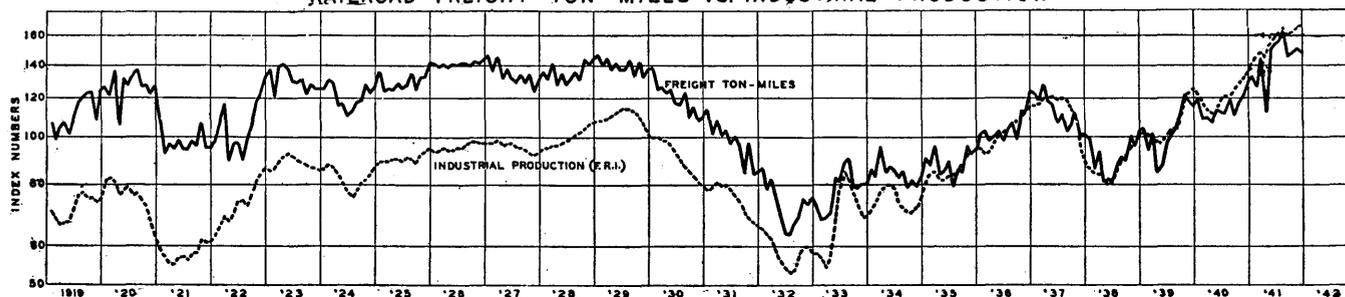
BUSINESS

Telephones in Use

Estimates based on reports of the Bell System indicate that there was an increase of about 1,520,000 telephones in use in the United States during 1941. This was the largest increase ever to be recorded. The total at the close of the year was about 21,200,000, representing a gain of nearly 50 per cent since the depression in the early 1930's. The Institute's index, on the basis of 1935-1939=100, adjusted for population growth, advanced from 116.1 in December 1940 to 124.3 in December 1941.

¹ See, "The St. Lawrence Waterway Project," June 23, 1941 bulletin, page 99.

RAILROAD FREIGHT TON-MILES VS. INDUSTRIAL PRODUCTION



Railroad Freight Ton-Miles vs. Industrial Production

The accompanying chart shows a monthly index taken from the railroad freight ton-mile series compiled by the Bureau of Railway Economics and adjusted for seasonal variations. It is presented, together with the Federal Reserve index of industrial production, and the base period for both indexes is 1935-1939=100. The indexes are charted on a ratio scale in order to facilitate comparisons between the trends of the two curves.

The cyclical changes of the two indexes are parallel for the most part, although the month-to-month fluctuations of the index of freight ton-miles are greater than such changes in the production index. Over the longer term, these two curves maintained about the same relative position on the chart until the end of 1926. The freight ton-miles index failed to gain substantially during the period 1927-1929, declined more during the next three years, and did not recover so rapidly from 1932 to the summer of 1935 as did the Federal Reserve index of industrial production. The relatively unfavorable performance of the railroad freight series during this period can be attributed to increasing truck competition.

Although there are no satisfactory records of the freight tonnage hauled by trucks in competition with the railroads during this period, some conception of the trend can be gained from the production of commercial trucks.

Year (1935-1939 Average=100)	Index of Truck Production	Year (1935-1939 Average=100)	Index of Truck Production
1919	38.6	1930	79.9
1920	45.0	1931	58.3
1921	21.7	1932	32.9
1922	37.8	1933	48.5
1923	57.3	1934	80.5
1924	58.3	1935	97.2
1925	47.2	1936	109.8
1926	72.4	1937	125.1
1927	65.0	1938	68.4
1928	76.1	1939	99.4
1929	108.0	1940	108.8
		1941	149.0 (prelim.)

It will be observed that truck production increased substantially during the period 1923-1929. However, the great increase in truck production during the period 1935-1937 apparently did not materially affect the relationship between freight tonnage carried by the railroads and total industrial production. Although there was a relatively greater increase in the Federal Reserve index during 1940, the ton-miles index advanced substantially during the first eight months of 1941 (the poor showing of the railroads during April 1941 was wholly attributable to the bituminous-coal strike), and the ton-miles index in August was in a relatively

favorable position compared with the industrial production index in spite of the spectacular advance that occurred in the latter.

The relatively less favorable trend of the ton-miles index during the last four months of the year may have been partly attributable to the large production of commercial trucks in 1941, a considerable portion of which was presumably placed in operation (the number of new trucks destined for Army or lend-lease use has not been made public).

It appears to be virtually certain that the railroads will carry a larger proportion of the total freight movement in 1942 than in 1941. Probably the most serious threat to truck transportation is the rubber-tire shortage, but it is also not certain that gasoline will be available in the desired quantities throughout the year, and speed limits imposed on road traffic will provide another differential in favor of the railroads.

The Trend of Commercial Failures

Both the number of insolvencies and the liabilities involved in commercial failures during 1941 were less than they were in the two preceding years. However the record was more favorable during the earlier than in the closing months of the year.

The fact that the liabilities of commercial failures in December 1941 slightly exceeded those in either December 1939 or 1940 suggests that the favorable trend that the series have followed for several years has now come to an end. The war is almost certain to create difficulties for nondefense industries, and commercial casualties are to be expected. The data for the first month of the war do not indicate an alarming increase in failures, but this series may provide a rough measure of the adaptability of American enterprise to war conditions.

The number and liabilities of commercial failures reported by Dun & Bradstreet, Inc. during each month of the past three years are shown in the accompanying table.

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	9,893
October	1,234	1,111	809	17,464	12,715	7,333
November	1,184	1,024	842	13,201	16,572	9,197
December	1,153	1,086	898	13,243	13,309	13,469
Total	14,768	13,619	11,848	182,520	166,684	136,104

THE FUNDAMENTALS

Supply

The steel-ingot production rate declined a half point to 96 per cent of theoretical capacity last week. *The Iron Age* stated: "Repairs, as well as lack of scrap, were a factor in the week's output decline. However, changes in operations due to repairs in the various districts largely counterbalance, while the net loss in the rate last week may be attributed to lack of adequate supplies of raw materials. With steel so urgently needed for the war program, a fractional point loss or gain in ingot output is highly important. Scrap collections slumped in almost all principal consuming centers due to cold weather of the past week. Throughout the country plans are under way to increase metal scrap collections."

	1929	1932	1937	1938	1941	1942
Per Cent of Capacity	82.5	24.5	80.0	30.0	98.0	96.0

(Latest 1942 weekly data; corresponding week earlier years)

Electric-power production increased from 3,288,685,-000 (revised) to 3,480,344,000 kilowatt-hours last week. The increase in power generated last week from that produced in the corresponding week of 1941 was about 16 per cent.

	1929	1932	1937	1938	1941	1942
Billion Kilowatt-Hours	1.74	1.60	2.26	2.12	3.00	3.48

Cotton-mill activity increased substantially last week, and the adjusted index advanced from 166.7 in the preceding week to 174.9 per cent of estimated normal. This industry may be faced with some of the problems that have earlier confronted the metal trades, inasmuch as Government authorities are considering the allocation of textile equipment.

	1929	1932	1937	1938	1941	1942
New York Times Index	*	92.1	145.8	90.6	135.0	174.9

The daily average of lumber production decreased last week and the adjusted index declined from 122.4 to 120.9 per cent.

	1929	1932	1937	1938	1941	1942
New York Times Index	144.3	38.8	68.2	48.9	143.2	120.9

Demand

The Government is attempting to hold spending for consumer goods down to the level of the commodities available at existing prices. Its patriotic appeals intended to encourage investment in Government obligations is only one feature of the general plan for limiting inflation. Thus far, the physical volume of consumer goods being distributed has been adversely affected by price increases, but the dollar volume remains high. The dollar volume of department-store sales last week was 32 per cent greater than that for the corresponding week of 1941.

Prices

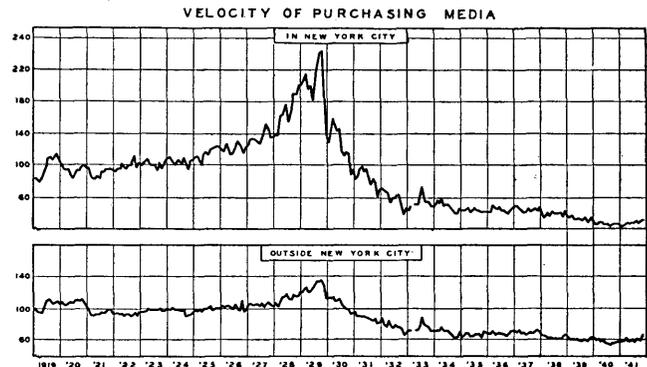
Last week's fluctuations in the sensitive wholesale commodity price indexes resulted in moderate gains. Moody's Spot Commodity Price Index was 221.7 on January 8 and 223.1 on January 15. The Dow-Jones Index of Commodity Futures closed at 85.47 on January 8 and at 86.78 on January 15.

FINANCE

Velocity of Purchasing Media

The accompanying chart shows the velocity of purchasing media for New York City, where there is a con-

centration of speculative transactions, and separately for the remainder of the country. The indexes, based on ratios of bank debits divided by checking-account deposits, are computed by the Federal Reserve Bank of New York. Although the turnover of currency cannot be ascertained, it is estimated that bank checks are used in about ninety per cent of business transactions, measured in terms of dollar value, and only about ten per cent are cash transactions.



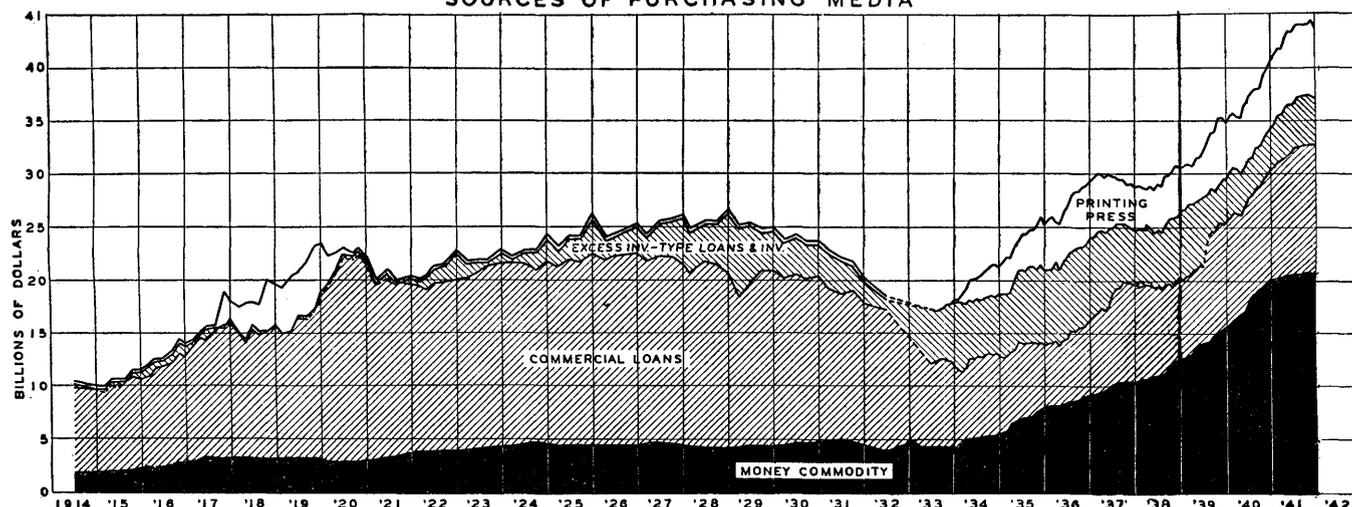
Sharp gains in velocity, such as those that occurred in 1919, 1928 and 1929, and again in 1933, are caused either by greater-than-usual activity in capital goods production or by an abnormal degree of speculative activity, such as that which culminated in 1929 and was concentrated in the stock market. Active speculation in securities has an especially marked effect on the velocity curve for New York City, as the chart indicates. Usually, abnormal speculative activity and great activity in the production of capital goods are concurrent developments. When the public is in a speculative mood, funds are readily available for industrial plant expansion, new office buildings, and apartment house developments.

During the extended period from the middle of 1933 to the middle of 1940, the general trend of the velocity of purchasing media was moderately downward. This was more noticeable in the series for New York City. The dollar volume of checking-account transactions increased steadily throughout this period, although this is not discernible in the indexes of velocity, because checking-account deposits increased even more extensively.

During the late summer of 1940, the downward trend in the velocity of purchasing media appears to have culminated. This was not immediately apparent, because the upward movement was so moderate that it first appeared to be merely one of the fluctuations that have characterized the series throughout their history. However, the duration of the upturn has now been more than a year, and the extent of the recovery of the indexes from their 1940 low points has been 29 per cent for the New York City series and 24 per cent for the series outside New York City.

As the chart of sources of purchasing media on page 12 shows, total purchasing media continued to increase substantially after the velocity indexes turned upward. It is thus evident that there was a still greater increase in the dollar volume of checking-account transactions. The increase in the volume of producers goods output that was stimulated by the vast national defense program was probably the primary factor in determining the change in the trend of the velocity indexes. Another

SOURCES OF PURCHASING MEDIA



factor that may have affected the velocity of purchasing media was the upward trend in commodity prices.

Ordinarily, an upturn in the velocity of purchasing media such as that which has occurred during the past year might reflect greater speculative activity. However, under the present wartime conditions, an increasing velocity of checking-account transactions appears to be a reflection of the activities of the Federal Government in collecting funds by taxation and borrowing and disbursing them for making war materials and new facilities for producing these materials.

Sources of Purchasing Media

During December 1941 purchasing media that were available to the public from all sources decreased approximately \$1,000,000,000. The decrease was caused by the transfer of private checking-account bank balances to Government accounts. As the accompanying chart shows, there has usually been a decrease in available purchasing media during December, but it was more pronounced last month, partly because tax payments were greater and partly because savings are being used more extensively for the purchase of Government securities.

Purchasing media from the money-commodity decreased in December for the second consecutive month. The decrease was not large (only \$45,000,000), and the total monetary gold stock (not held in the Treasury's general fund or in the exchange-stabilization fund) remained only \$60,000,000 less than the \$20,850,000,000 level reached at the end of October 1941. Nevertheless, it is apparent that the prediction made by the Board of Governors of the Federal Reserve System last summer that "stabilization or possibly a net export of monetary gold stock was in prospect" is being realized.

There was a decrease in the purchasing media derived from commercial loans last month. Earlier in the year, the volume of commercial loans and consequently the purchasing media derived therefrom increased substantially. This trend coincided with and was probably primarily attributable to the expansion in inventories of commercial and industrial companies that occurred before our entrance into the war. From now on, Government policies will probably dictate the

extent of private credit granted by the banks, and the future volume of commercial loans may be limited.

There was no appreciable change in purchasing media from the third source (an excess of investment-type assets that represent tangible property with respect to savings available to the banking system).

The net decrease for the month in aggregate purchasing media was primarily caused by a decrease in purchasing media from the fourth source. Although the total par value of Government securities in the commercial banks' portfolios increased during the month, there was a substantial increase in Government deposits with the Federal Reserve Banks. The December installment of the income tax and other tax receipts plus savings invested in new Government securities enabled the Treasury to increase its working balance. Government deposits are deducted from the total purchasing media derived from the printing press, because such deposits represent funds temporarily not available to business.

In spite of an increased rate of disbursements, the Treasury was enabled temporarily to increase its bank balances. Tax receipts for December 1941 of \$1,200,000,000 were 52 per cent more than they were in December 1940. In addition to marketing a \$1,600,000,000 issue of Treasury bonds, a portion of which was sold to individuals and to savings institutions, \$340,000,000 was realized from the sale of tax-anticipation notes, and sales of \$536,000,000 in savings bonds established a new high monthly record in the disposal of these issues.

SECURITIES

Bonds

Another week characterized by strength in the bond market brought the average level up to that existing previous to the 3-point decline in December. The Dow-Jones average of 40 bonds was 89.64 on January 8 and 89.95 on January 15.

Stocks

The stock market followed a generally favorable trend last week with investors showing a preference for railroad issues. Investors apparently believe that the heavy tax burden necessitated by the war will fall less heavily on the railroads than on the other corporations whose issues are listed on the Stock Exchange.