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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Looking Farther Ahead

The desirability of considering long-term prospects at a time when the immediate necessity of winning the war is so pressing is frequently questioned. Speeches of Government officials often stress the need for complete concentration of thought and effort on the primary objective. This was the attitude of British leaders after disaster on the Continent brought home the perilous position of the British Isles. However, after another year of war, discussions of longer-term considerations again become prominent features in British periodicals. It was realized that the people's faith in the future was highly important in shaping their attitude toward the war effort.

A general belief that winning the war will be followed by resumption of progress toward better living conditions will contribute profoundly to stimulating the effort expended on the task in hand. A general feeling that civilization has passed its prime and that, no matter what the outcome of the war may be, the advantages of the past will not be regained cannot fail to promote a feeling of apathy similar to that which proved so disastrous to France.

It is therefore reassuring to find a statement of faith in the future progress of the human race expressed by one of the world's outstanding economists, Professor Gustav Cassel of Stockholm. His article in the *Quarterly Review, Skandinaviska Banken* was discussed in "The Weekly Review of Periodicals" compiled by the Board of Governors of the Federal Reserve System (January 6, 1942). Professor Cassel blames the theory that there are insufficient available resources for the world's civilized population for much of the rabid nationalism that has culminated in the present world war. He denies that progress is dependent on land frontiers and argues that extensive progress can be best achieved through the scientific utilization of available resources.

In his refutation he points to the frontiers of scientific development that were opened during the two decades intervening between the world wars. He refers briefly to the many fields of endeavor, the atomic and macro-molecule research in chemistry, the metallurgical discoveries and mechanical improvements, and the progress in many branches of biology and agriculture. Even a superficial list of the principal examples of scientific advance would suffice to establish his point.

Progress has undoubtedly been less satisfactory in the social sciences, but Professor Cassel protests against the charge that scientific progress has been responsible for the growth of undue materialism. He characterizes as sheer thoughtlessness the condemnation of a cultural development that aims to promote the well-being of mankind.

Although Professor Cassel expresses his faith in the future of scientific endeavor, he feels that a threat to such progress is contained in the tendency to condemn the formation of capital through savings. He believes that capital resources are necessary if the desirable scientific research is to be carried on and therefore believes that such trends of thought as are embodied in the oversavings theory must be discouraged.

Scientific Progress and War

Economists have recently been engaged in an inconclusive discussion as to whether technological developments have been stimulated or retarded by wars. The fact that the central years of the Industrial Revolution, which laid the foundation for our present-day mass-production methods and their accompanying technology, coincided with the protracted Napoleonic Wars suggests the possibility of causal relationship. The World War in 1914-1918 was accompanied by considerable scientific progress. Our chemical and airplane industries undoubtedly made great strides during those years, and important contributions were made to medicine and surgery. However, there is no convincing evidence that as great or greater scientific achievements might not have been made in the absence of wars.

In the present type of all-out war in which all processes are devoted to the objective of victory, it is logical to expect that the major part of scientific research will be channeled into fields related to the war. New discoveries and new improvements are to be expected in these fields of concentration.

It can be confidently expected that there will be a great surge of scientific progress after the war. Some war discoveries can be adapted to peace-time requirements; and the fruit of other research that was held in abeyance during the conflict will be practically employed. Only the stupidity of governments in failing to recognize the incentives that provide the driving force in economic progress endangers Professor Cassel's standing as a prophet.

THE FUNDAMENTALS

Industrial Production

The Institute's revised index of industrial production for December 1941 was substantially the same as the preliminary index for that month, and the preliminary index for January 1942 remained at about the same level. The former was 152.9, and the latter, 153.0 per cent of normal.

Until the United States entered the war, by far the greater proportion of goods produced was for civilian consumption in spite of the progressive increase in the production of materials for national defense. The situation in 1942 will of course be different, and the trend of the index will measure primarily the Nation's success in producing war supplies. Most of the basic industries have recently been operating at practical capacity; and, if the index representing aggregate production fails to make further progress during the change-over period, it will not indicate a let down in the war effort, because plants that cannot immediately be adapted to the production of war materials will be operating at reduced rates until new machine tools are available for the mass production of airplanes, guns, and ships.

Because the character of industrial production during the war is no longer comparable to production in peacetime, we have discontinued the bar charts that have been features of the monthly Research Report bulletins.

The steel-ingot production rate advanced a half point to 96½ per cent of theoretical capacity last week. *The Iron Age* summarized the prospects for the industry in coming weeks as follows: "Steel orders booked so far in January are equaling, or in a few cases exceeding, the volume of the corresponding period in December, although orders had been expected to decline somewhat because of the all-out war program. Approximately 1,750,000 tons of steel will be needed for the 522 merchant ships for which contracts totaling \$948,000,000 were announced last week by the United States Maritime Commission."

	1929	1932	1937	1938	1941	1942
Per Cent of Capacity	83.5	26.0	81.0	31.0	99.0	96.5
	(Latest 1942 weekly data; corresponding week earlier years)					

Electric-power production decreased less than seasonally last week. Last week's output of 3,450,468 kilowatt-hours was 14½ per cent greater than production in the corresponding week of 1941.

	1929	1932	1937	1938	1941	1942
Billion Kilowatt-Hours	1.71	1.60	2.26	2.11	3.01	3.45

Cotton-mill activity decreased last week, and the seasonally adjusted index declined from 174.9 to 162.0 per cent of estimated normal. The curtailment in production was attributed to Government regulations. It was reported that the volume of priority-free production was so small that total sales were only moderate.

	1929	1932	1937	1938	1941	1942
New York Times Index	*	91.1	140.9	88.2	147.6	162.0
	*Not available until third week of March.					

Last week lumber production increased contra-seasonally and the adjusted index advanced from 120.9 to 135.7.

	1929	1932	1937	1938	1941	1942
New York Times Index	145.2	89.3	69.9	53.1	143.0	135.7

The Harwood Index of Inflation

The preliminary Index of Inflation in ratio form for January (based on data for January 14) is 107.4, nearly two points higher than the revised Index of 105.7 for December 1941. The chart on page 15 shows the Index of Inflation 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 Index in ratio form has shown an irregular and gradual upward trend since September 1940, and, in January 1942, it reached the highest level recorded since October 1938. The actual total of inflationary purchasing media increased substantially during the first half of January and reached a total of \$8,000,000,000, compared with \$7,200,000,000 during the height of the 1936-1937 inflation.

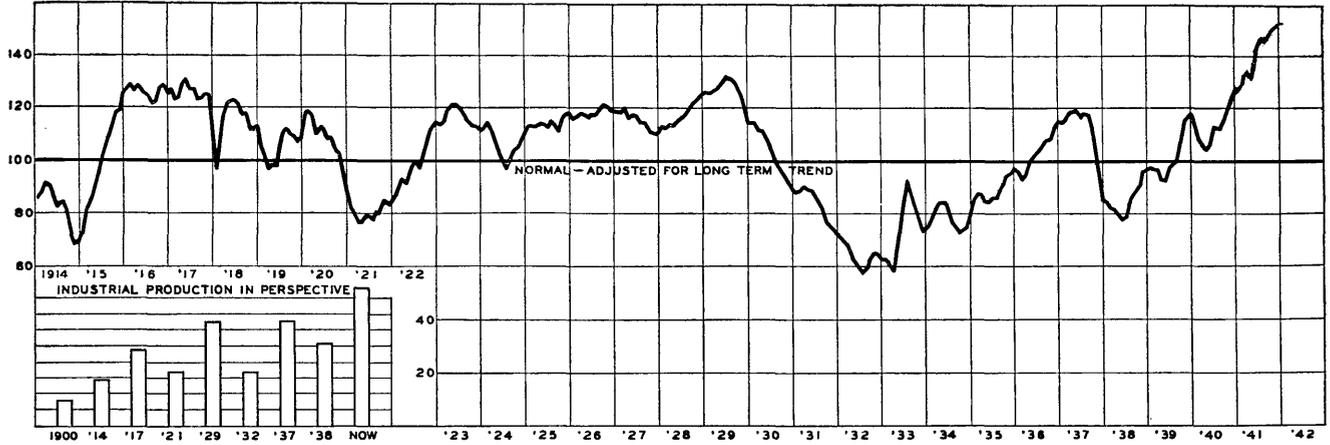
The advance in the Index during the first half of January was caused by several important changes in the money-credit items involved. There was a net increase of about \$300,000,000 in the banks' investment-type assets; a larger increase in security holdings was partially offset by a moderate decrease in loans on securities. A factor as important as the increase in investment-type assets causing the increase in the Index was a decrease of about \$300,000,000 in Government deposits with the Federal Reserve Banks and with other depositories. This occurred as the Government spent a portion of the funds received in the preceding month from the December installment of the income tax and by sales of Savings Bonds. Government deposits are deducted from the inflationary purchasing media, because such deposits represent funds temporarily not available to business; a decrease in the Government's bank balances indicates the distribution of this purchasing media to the public.

Another, although less important, factor in causing the advance in the Index was the decrease of about \$150,000,000 in the banks' savings-type liabilities that comprise the savings available for investment in the investment-type assets. This was caused by a decrease in time deposits, which constitute the major portion of the savings-type liabilities of the banking system.

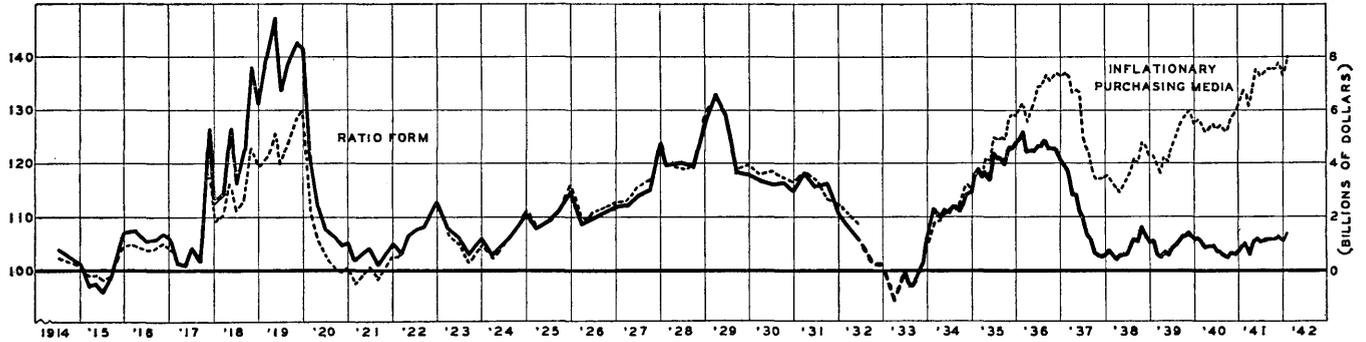
The withdrawal of savings deposits, which has been in process for several weeks, has been attributed to the desire of individuals to use such funds for the purchase of Government Savings Bonds. However, in addition to the large withdrawals of savings from the commercial banking system, more substantial withdrawals are reported from savings banks, and the president of the Savings Banks Association of the State of New York has estimated that these withdrawals about equal the investment in Government Savings Bonds and therefore draws the conclusion: "The people are not saving any substantial portion of their income." In fact, there may have been an over-all withdrawal of savings for the purchase of consumer goods, but this cannot be definitely ascertained because data for the period since we entered the war for all types of savings funds are not yet available.

The withdrawal of savings from banks and other institutions for the purpose of purchasing Government Savings Bonds will of course nullify a primary objective of the campaign for the sale of Treasury savings issues. The investment of savings in Government savings stamps and bonds is effective for limiting the develop-

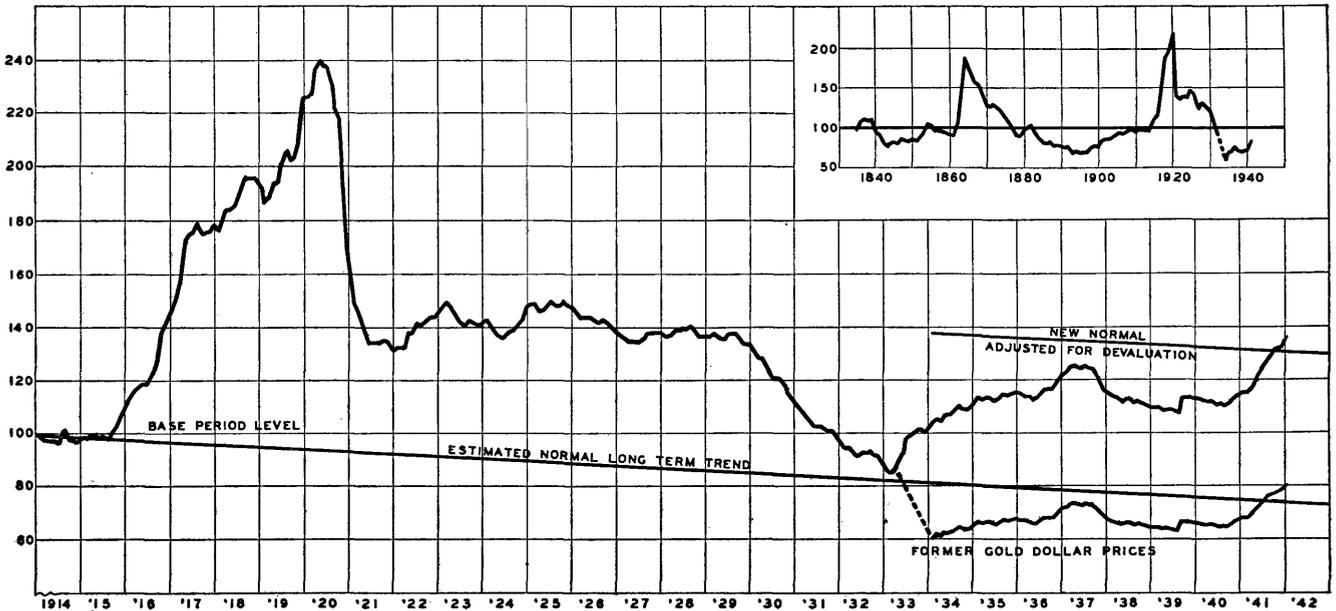
INDUSTRIAL PRODUCTION



HARWOOD INDEX OF INFLATION



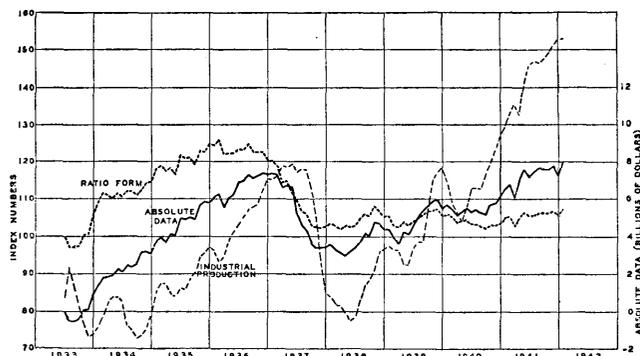
COMMODITY PRICES



ment of inflation only to the extent that the funds are derived from current income that would otherwise be employed for the purchase of goods in the market.

Total available purchasing media increased during the first half of January primarily because the Government's cash disbursements exceeded its cash receipts. Preliminary estimates indicate that substantial sums are still being hoarded each month in the form of currency, so that, for the time being, all the newly created inflationary purchasing media have not appeared as active demand in the market. However, it should be remembered that hoarded currency, which, according to our estimates, now exceeds \$2,500,000,000, constitutes an important inflationary potential that might become active if a flight from dollars into commodities is initiated.

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



The foregoing chart, which presents the industrial production index, together with the absolute data and ratio form of the Index of Inflation, shows that there was a greater increase in the absolute data than in the ratio form of the Index last month. This is attributable to an increase in total purchasing media from sources other than bank credit, which was caused by the Treasury's expenditure of surplus funds accumulated during the preceding month. Both the ratio form of the Index and the absolute data will probably advance substantially between now and March 15, when the next income-tax installment is due. The Treasury's budgetary deficit for the first half of January was \$920,000,000, and a deficit of about \$2,000,000,000 for the month is in prospect. The rate of defense spending is accelerating rapidly, and an even greater deficit for the shorter month of February may be expected.

Other Demand Factors

Reports from merchants throughout the country indicate that demand for some types of consumer goods is more insistent than it has been since the preceding wave of "scare buying" at the end of last summer. The buying is concentrated in the classes of products of which scarcities are rumored or stocks of which are

known to be low on retailers' shelves. The officials of retail-trade associations have warned their members that the present heavy consumer demand may represent business borrowed from later months this year. However, until incomes are curtailed, recurrent buying waves may be expected when fears are aroused concerning the adequacy of consumer supplies. The dollar volume of department-store sales last week was 45 per cent greater than it was in the corresponding period a year ago.

Commodity Prices

The United States Bureau of Labor Statistics' combined index of commodity prices advanced from 133.7 (1913=100) in December 1941 to 136.1 (preliminary) in January 1942. This represented another sizable increment in the advance that has been virtually continuous since the summer of 1940, and the combined index has increased nearly 20 per cent during this period of a year and a half. The chart on page 15 shows that wholesale prices are now substantially higher than normal after allowing for the effects of devaluation. (Normal price relationships and the Institute's method of determining the long-term trend of commodity prices are described in the "Explanation of Basic Charts," which has been sent to all subscribers.)

Changes in the average prices of the three economic classes were irregular last month. The raw-materials average advanced three per cent; the semimanufactures average advanced about 1½ per cent; and there was a fractional decline in the finished-goods average. The fuel-and-light item was the only one among the principal subdivisions of the wholesale commodity price index to record a decline. Fractional advances were the rule among the other subdivisions, but more substantial gains were made by farm products, foods, and chemicals. The accompanying table shows the changes that have occurred in the major classifications of the wholesale commodity price index. The January 1942 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)

	Jan. 1929	Jan. 1932	Jan. 1941	Dec. 1941	Jan. 1942*
Farm Products	148.1	73.8	97.5	131.2	138.2
Foods	154.0	100.8	114.5	141.0	144.1
Hides and Leather	166.5	116.4	150.2	169.0	169.9
Textile Products	161.4	104.0	130.5	159.2	161.3
Fuel and Light	137.4	110.8	117.0	129.4	128.7
Metals and Products	110.2	90.1	107.5	113.9	114.0
Building Materials	168.4	131.9	175.1	189.9	192.1
Chemicals	†	†	96.9	114.0	118.8
House Furnishings	166.8	138.0	157.9	181.5	181.9
Miscellaneous	118.5	94.0	110.7	125.2	125.6
Raw Materials	143.6	84.7	107.0	133.4	137.4
Semimanufactures	126.3	84.2	107.7	120.2	121.9
Finished Goods	136.5	103.9	119.3	136.5	136.0
All Commodities	137.4	96.4	114.6	133.7	136.1

* Preliminary Estimate. † In process of revision.

Statistical Summary; Production, Purchasing Media, and Prices

	1941												1942
	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.*
Index of Industrial Production	129.4	133.0	135.5	132.6	141.5	146.0	146.8	146.5	147.3	148.9	151.3	152.9	153.0
Index of Inflation (ratio form)	105.1	105.2	102.8	105.2	106.6	105.3	105.7	106.1	106.2	106.1	106.4	105.7	107.4
Commodity Price Index	115.8	115.5	116.8	119.2	121.6	124.8	127.2	129.4	130.9	131.4	132.5	133.7	136.1
Commodity Price Index	68.5	68.3	69.1	70.5	72.0	73.8	75.3	76.6	77.4	77.8	78.4	79.1	80.5

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