

# AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

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## RESEARCH REPORTS

### COMING EFFECTS OF CURRENT EVENTS

#### *Fluctuating Hopes for Early Victory*

After the capitulation of the Italian Government, it was assumed that the country could be immediately occupied by the Allies and that we could start to move against the homeland of our principal European enemy. Unexpected resistance by German forces in southern Italy soon created a severe psychological reaction to our earlier hopes. The press carried warnings that every foot of the Italian peninsula from Naples up to its northern borders must be won by tough fighting. This second appraisal may prove to be no more accurate than the original was.

Because we suffered a check to our first operations on the Italian mainland, we have overlooked the perilous position that the Germans have accepted in order to hold us away from their borders. Available avenues of supply for the Nazis are so restricted that the pros and cons of an invasion of Switzerland to open up new routes is probably being considered by the German general staff. The German armies occupying Italy also are exposed to an outflanking operation through the Balkans. Defense measures have no doubt been taken to prevent this, but German resources in fighting manpower and in war materials are so widely spread out and have been subjected to such serious impairment that their old effectiveness may be lost.

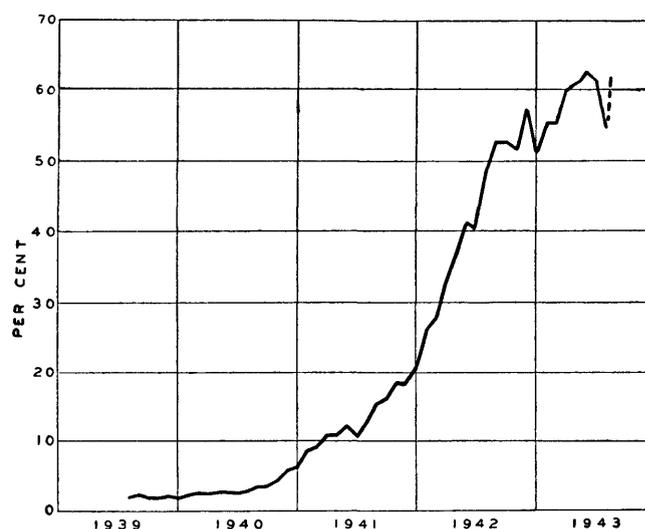
The obvious lesson to be derived from the recent fluctuations in hopes for an early victory is not to assume that the war is virtually over when affairs are going well for us nor to become discouraged over the prospects for a reasonably early victory in the European war theater.

#### *Proportion of the National Economy Devoted to War Activity*

In order to appraise the degree by which the Nation's energies are being devoted to the war effort, we have prepared the accompanying chart of a monthly statistical series showing expenditures for war activity as a per cent of total income payments, which include payments for war activities in their total.

The line indicating the per cent of income devoted to war activities in July is broken, because only preliminary estimates of income payments are available for that month, although expenditures for war activities are known.

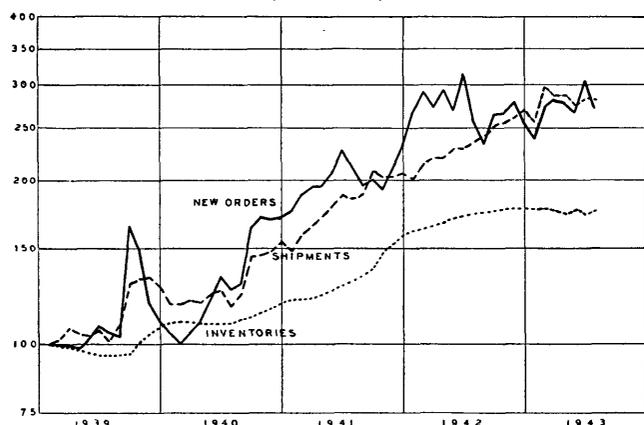
### PER CENT OF TOTAL INCOME FOR WAR ACTIVITIES



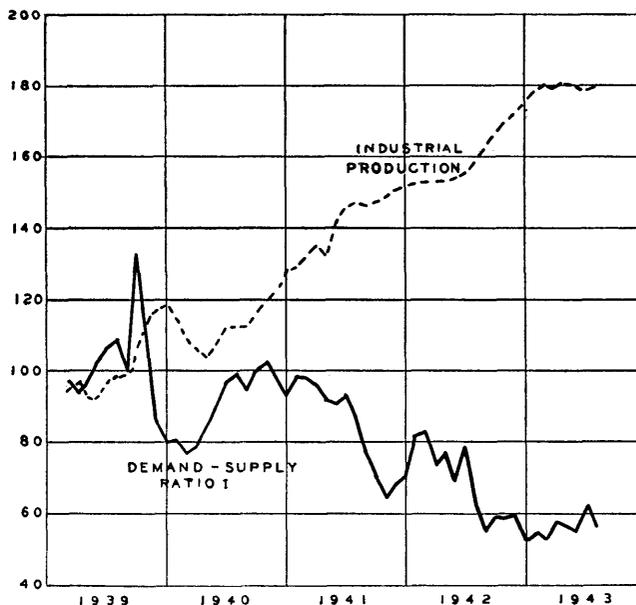
The decline in the chart that was shown in July was only temporary, and the recovery in expenditures for war activities in August raised the total to more than 60 per cent of all income payments for that month. The apparent fact that more than 60 per cent of the Nation's productive effort is being exerted for the prosecution of war does not appear to leave a sufficient amount of the Nation's current resources to supply the civilian population. The primary reason that we have been able to accomplish this diversion of productive effort to the war is that we have been able to expand our whole industrial volume only partly at the expense of the industries serving the civilian population. There have also been other influences that have favored us. The luxury margin in our living standards has been so great that a considerable shrinkage could be effected before the point of hardship is reached. Furthermore, we are less exposed to the devastating effects of air raids and have so far been immune to them. Where these have occurred, they have primarily been directed against war-production centers, but the damage done is ultimately reflected in dwindling consumer supplies.

The following statistical summary shows the expenditures for war activities for the first eight months of 1943, together with the income payments for the corresponding period. The data for the full year 1942

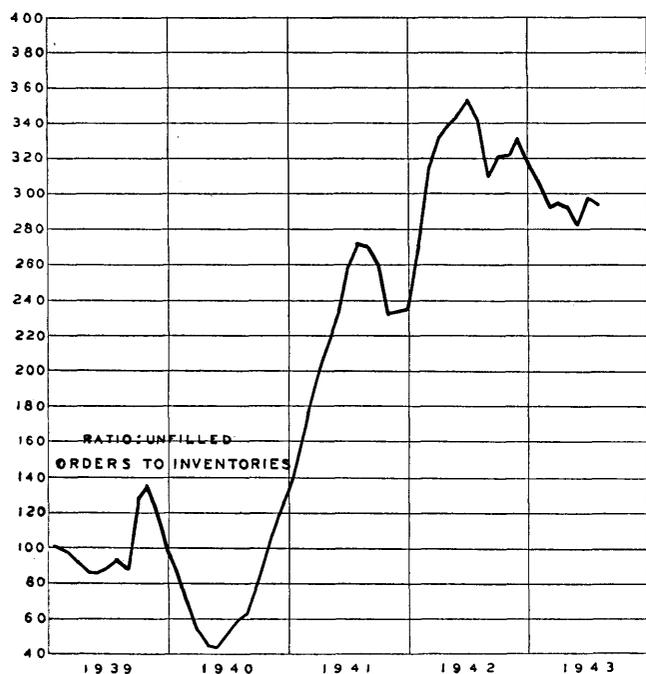
**INDEXES OF MANUFACTURERS' NEW ORDERS,  
SHIPMENTS, AND INVENTORIES  
(1939 = 100)**



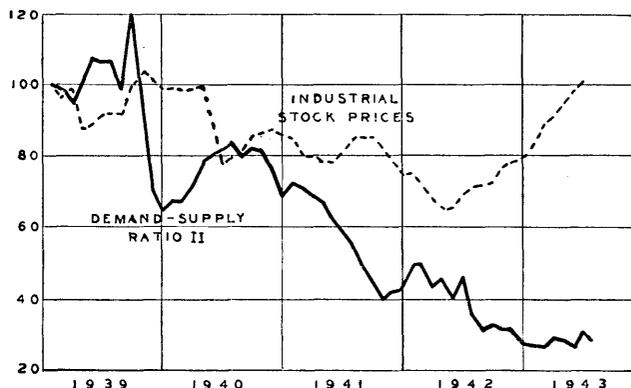
**DEMAND-SUPPLY RATIO I  
VS. INDUSTRIAL PRODUCTION**



**RATIO OF UNFILLED ORDERS TO INVENTORIES**



**DEMAND-SUPPLY RATIO II  
VS. INDUSTRIAL STOCK PRICES**



were published in the August 16, 1943 weekly bulletin, page 130.

	<i>Expenditures for War Activities (In Billions of Dollars)</i>	<i>Income Payments</i>
1943		
January	5,947	10,748
February	5,770	10,443
March	6,744	11,222
April	6,974	11,215
May	7,091	11,138
June	7,469	12,162
July	6,432	11,795
August	7,232	11,600 (est.)

**Demand-Supply Ratios**

The indexes of manufacturers' new orders, shipments, and inventories, compiled by the United States Department of Commerce were published last week for July 1943. The chart in the upper left-hand corner of

this page shows the basic indexes from which our demand-supply relationship charts are derived.

After advancing close to the best level reached during the wartime period in June, the new orders index declined again in July. There was no significant change in either the shipments or the inventories indexes in July compared with the June record.

The ratio of unfilled orders to inventories, shown in the next chart in the same column, was computed by dividing the backlog of orders (obtained by calculating the excess of the new orders index over the shipments index for the period shown in the chart) by the index of inventories. This ratio advanced in June but declined moderately in July, when the shipments index remained about unchanged, and the new orders index declined.

The chart at the top of the next column shows the Institute's Demand-Supply Ratio I (new orders divided by shipments times inventories) with the Institute's index of industrial production, adjusted for long-term trend. Primarily as a consequence of the decline in the new orders index, Demand-Supply Ratio I for July lost the gain that it had made in the preceding month and was again approximately at the May level. Demand-

Supply Ratio I has been relatively stable during the past year. This indicates that American industry is supplying substantially all of the war materials that are demanded by the Government. Comparisons of the ratio with the index of industrial production show that the latter did not become stabilized until several months after the former became relatively steady.

The next chart shown in the same column presents the Institute's Demand-Supply Ratio II with the index of industrial stock prices. This ratio includes industrial production as well as shipments and inventories in the supply factor. Inasmuch as both the production and the inventory factors remained about unchanged during recent weeks, the trend of Demand-Supply Ratio II has closely followed the trend of Ratio I.

## BUSINESS

### *Production and Trade in War Time*

The Federal Reserve Bank of New York recently published its indexes of production and trade for the month of July 1943. These indexes afford a means for tracing the more important changes in the Nation's economy during the war period. The major divisions of the bank's index are production, primary distribution, distribution to consumer, and miscellaneous services. There is a combined index of production and trade.

The components of the production index are based on the usual data for leading industries. Carloadings, waterway traffic, and exports and imports are used to show primary distribution. The index of distribution to consumer is based on reports of retail sales, gasoline consumption, and new passenger-car sales. Miscellaneous services include such records as newspaper advertising, postal receipts, communications, railway and air travel, and hotel-room occupancy. In the combined index, production is given the heaviest weight, and miscellaneous services, the least.

The following table shows the combined index and major divisions of the index for the month of August 1939, just before the war started in Europe, and for July 1943, together with the changes that have occurred expressed in percentages based on the earlier period.

INDEXES OF PRODUCTION AND TRADE			
	August 1939	July 1943	Per Cent Increase
Production	85	134	58
Primary Distribution	80	157	96
Distribution to Consumer	93	84	10*
Miscellaneous Services	82	176	115
Combined Index	86	126	47
* Decrease			

The increase of 58 per cent in production is the net effect of a great expansion in the manufacture of heavy war materials and the curtailment in the manufacture of most types of both durable and nondurable consumer goods. The increase of 96 per cent in primary distribution reflects the movement of the heavy raw materials to points of manufacture and the delivery of the finished products to our own armed forces and to our Allies. The ten per cent decrease in distribution to consumer is a natural wartime development, when the supply of civilian goods is restricted. The increase of 115 per cent in the index of miscellaneous services has

been caused primarily by the expansion in railway and air passenger travel.

## THE FUNDAMENTALS

### *Supply*

The steel-ingot production rate declined from 100½ to 99½ per cent of theoretical capacity last week. The productive capacity of the Nation's steel industry now exceeds 90,000,000 tons per year, and this is being operated at practical capacity. *The Iron Age* commented as follows on the current situation in the industry: "The war's new turn will tighten all domestic supply problems, temporarily at least, and will heighten the critical manpower and coal shortages. The pattern of the military supply program will not be altered at this time and therefore there can be little hope for the additional release of steel and other critical materials to the civilian economy. Italy's capitulation increases the seriousness of the domestic coal crisis, since Italy is dependent on imports of fuel. Already coal is being diverted on a priority basis to metallurgical industrial needs in the United States, and the shortage can be expected to grow more serious. Practical steel executives continue to insist that the immediate picture does not contain the slightest indication of any large scale steel distribution to civilian channels."

	1929	1932	1937	1938	1942	1943
Per cent of Capacity	84.5	15.0	81.0	47.0	99.0	99.5
(Latest 1943 weekly data; corresponding week earlier years)						

Electric-power production last week exceeded that in the corresponding week of 1942 by 18 per cent. The gain was slightly less than that reported in the preceding week. For the second week, the Southern States made a more impressive showing than did the Pacific Coast region, which was the outstanding leader earlier in the year.

	1929	1932	1937	1938	1942	1943
Billion Kilowatt-Hours	1.79	1.49	2.27	2.15	3.58	4.23

There was another substantial decrease in lumber production last week, and the adjusted index declined to the lowest level recorded since last February. The index was 102.0 last week, and 108.5 in the preceding week.

	1929	1932	1937	1938	1942	1943
New York Times Index	120.6	35.5	85.0	77.7	110.2	102.0

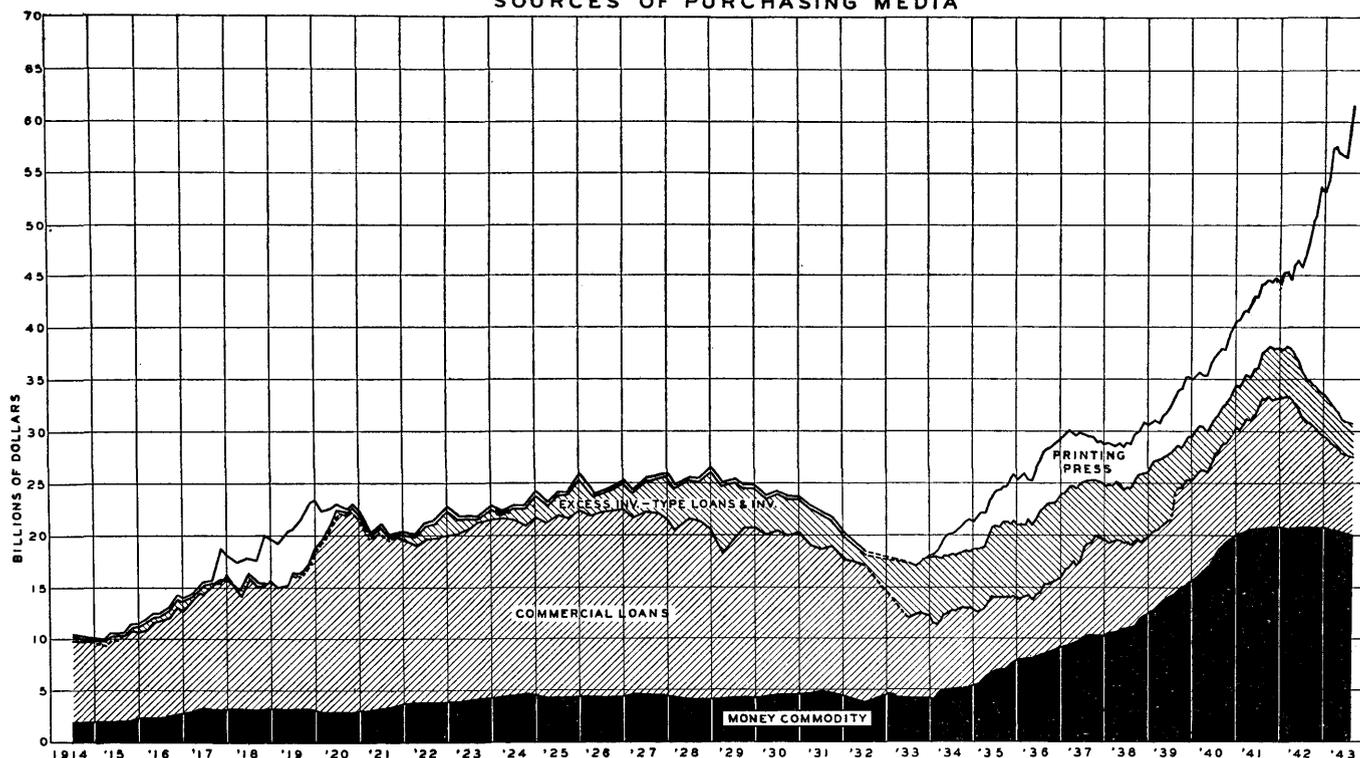
### *Demand*

The dollar volume of department-store sales last week was ten per cent larger than that for the corresponding week of 1942. The combination of the withholding taxes and the pressure on incomes exerted by the Third War Loan drive will no doubt cut into retail sales this fall. Furthermore, consideration by Congress of the possible imposition of still heavier taxes on incomes will tend to encourage a cautious attitude toward spending on the part of the public.

### *Prices*

Neither of the sensitive wholesale commodity price indexes showed decisive trends last week. Moody's Spot Commodity Price Index was 246.6 on September 9 and 247.1 on September 16. The Dow-Jones Index of Commodity Futures closed at 92.28 on September 9 and at 93.41 on September 16.

## SOURCES OF PURCHASING MEDIA



### FINANCE

#### *Sources of Purchasing Media*

The chart showing sources of purchasing media presented in this issue has been revised in accordance with more detailed information now available. The revision covers the period June 1942 to September 1943. The changes that were made will be revealed by comparison between the chart on this page and the chart on page 136 of the August 23, 1943 bulletin. The only significant change was made in the line representing total purchasing media and was caused by revised figures showing greater expansion in purchasing media from the printing press than was indicated by the preliminary data.

Another decrease in purchasing media from the money-commodity source was recorded last month. The total decrease in monetary gold stock during the month was about \$90,000,000. The Nation's monetary gold stock has decreased steadily since we entered the war. The total (excluding the portion represented by the stabilization fund) was \$20,838,000,000 at the end of November 1941, and this was reduced to \$20,300,000,000 at the end of August 1943. The total reduction of about \$500,000,000 in our gold stock has been substantial, but, expressed as a per cent of the dollar value of our monetary gold stock in November 1941, it shows a loss of less than 2½ per cent.

During the period since March 1942, purchasing media derived from commercial loans decreased substantially. The contraction in this type of credit during this period was attributable to policies dictated by the United States Treasury and Federal Reserve authorities. The Government has undertaken much of the financing incident to developing the production of war materials.

There was a small decrease last month in purchasing media derived from the third source (an excess of

investment-type assets representing tangible property with respect to the savings available to the banking system). Purchasing media from this source are usually created as a result of investment by the banks in the obligations of private corporations. The commercial banks have generally restricted their purchases of bonds to United States Treasury issues during the war period.

Inasmuch as there were relatively minor changes in purchasing media from the other sources, it is evident that the large increase in the total last month originated primarily from the printing press. During August, financial requirements of the war made it necessary for the Treasury to draw down its total bank balances from \$8,700,000,000 at the end of July to \$5,700,000,000 at the end of August. The depletion of Treasury cash resources by \$3,000,000,000 indicated the distribution of these purchasing media to the public. This factor was the primary cause of the increase in purchasing media from the fourth source last month.

The volume of purchasing media available to the public during August reached a high level that may not be duplicated again this year. If the Third War Loan campaign is successful, as early reports indicate that it will be, the Government will succeed in withdrawing a substantial volume of purchasing media from the total available to the public. However, when the Treasury disburses the funds received by the sale of securities in its drive, these purchasing media will gradually be returned to the public, and the aggregate may rise to a fresh high level.

*American Institute for Economic Research is a non-political, non-commercial organization engaged in impartial economic research.*