

AMERICAN INSTITUTE *for* ECONOMIC RESEARCH

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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Progress of Reconversion

During the months ahead, the progress achieved by industry in readapting itself to peacetime conditions will have a vital bearing on the public's way of living both in the immediate and more remote future. If our industrial mechanism functions smoothly to bring goods to the civilian markets in large volume, the effects of inflation will be less severely felt, the public will enjoy greater physical comforts, and the problem of unemployment will be minimized.

On the other hand, if the process of reconversion is seriously retarded the number of unemployed will increase to depression levels with grave consequences to the economy. Popular demand will force the Federal Government to spend heavily for public works and for relief, and the inflationary progression will be continued. The charge will again be made that the private enterprise system has failed, and the Government will impose central management over the economy. The trend of production this fall and winter must therefore be observed with especial interest.

In order to support the increased cost of Government caused by the war, the annual production of goods and services at current price levels must be larger than the volume in the prewar period. If this objective is to be achieved, the whole economic system devoted to serving the civilian population must start functioning again on a large scale. This will involve increased residential housing construction, purchases of new equipment in large volume by the railroads, a resumption of their long-term expansion program by the utilities, the reconditioning and readaptation of industrial facilities, and similar developments in other important fields. There are data available for observing the progress made by such activities that will enable us to appraise the general trend.

At the time of the substantial recession in industrial activity in the winter of 1937-1938, the Institute's Research Division made a special survey of all the reliable data available that provided indicators of economic trends showing the progress of a recovery movement. In view of the existing circumstances, these have been reexamined and additional factors have been considered that are most significant under present circumstances.

Indicators of Future Trends

After making a careful analysis of available data, we have selected eleven continuing series that should reveal the basic trend during the transition. These are enumerated and briefly described in the following paragraphs.

Private engineering construction contracts awarded are certainly one of the most important indicators under present conditions. Included in these data are contracts for such varied structures as the following: factories, warehouses, grain elevators, office buildings, retail business establishments, industrial transportation systems, railroad bridges, and other major construction awards by the railroads, and the construction of new plants and facilities by the public utilities. These data are shown in advance of actual construction and therefore have forecasting value.

The trend of machine-tool orders has for many years been observed for the purpose of forecasting the rate of industrial activity. It is held that in placing orders for large quantities of machine tools, manufacturers do so in the expectation of increasing production of their products. Certainly the series affords a significant indicator of the breadth of recovery movements, and its accuracy as a forecasting device can be more confidently relied on during the early phases of industrial expansion than it can as indicating the termination of upward movements.

The United States Department of Commerce compiles a monthly statistical series showing orders placed for steel boilers. The principal types of stationary and marine boilers are included in the total and the units are square feet of heating surface. The trend of this series is especially interesting because it represents, with virtually no exception, outlays for producers' goods of a more durable type than is presented by the machine-tool orders index.

Fluctuations in the prices of the common stocks of companies manufacturing capital goods (one of the series included) has in the past proven to have value in indicating the basic industrial trend. Although other factors than earnings are instrumental in causing the rise and fall of stock prices, the activity of the industries concerned, which usually is the most important factor in corporate earnings, is normally the major determinant in establishing quotations for corporate securities.

New capital issues of corporate securities, which are

NEW CONSUMER GOODS PER CAPITA



regularly discussed in the Research Report bulletins, afford another significant indicator of the broad economic trend in the United States. In general, new capital issues of corporate securities are purchased with the Nation's savings by individuals, banks, insurance companies, or other institutional investors; and the funds are invested in new plants, equipment, and other capital facilities. Both opportunity for business expansion and confidence on the part of investors are required for an active market in new capital issues.

The trend of employment is especially significant at this time and may have a profound influence on the Nation's future for reasons discussed in a preceding paragraph. Employment reports are therefore included among the indicators of future trends.

Because steel is used in manufacturing such a large percentage of the goods produced in this industrial age, the trend of steel-ingot production is one of the earliest and most reliable clues to future developments. The trend of this statistical series, which is regularly discussed in the bulletins, is included among the eleven indicators chosen as especially significant.

A resumption of industrial and commercial building as well as improvement in the residential construction field will probably be reflected in an increase of lumber production. For this reason, the lumber production index, which has been discussed each week in the bulletins in the section devoted to the fundamentals, is included among the eleven indicators chosen as significant at the present time.

Another significant statistical series is provided by the record for carloadings of heavy products, which includes loadings of coal and coke, ore, and lumber. These are the basic raw materials necessary for the operation of the Nation's heavy industries, and an increase in such shipments indicates a trend towards a higher level of production by these industries.

Electric-power production has been included among the indicators of future trends although the consumption of power coincides with its production and it therefore does not have the forecasting value afforded by other indicators. Electric-power figures are primarily valuable in indicating promptly the breadth of a recovery movement inasmuch as they are a sensitive indicator of miscellaneous manufacturing activities.

Until the industrial trend during the transition period is clearly marked, the Harwood Index of Inflation will be calculated at weekly intervals and reports of the direction in which it is moving will be presented as one of the eleven indicators in the series under discussion. The trend of this index is of course especially important at the present time, because it indicates the

volume of purchasing media available to the public that presumably will appear as potential demand in the Nation's markets.

Summary

The latest available information regarding the 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, all with respect to the immediately preceding period.

	<i>Latest Indication</i>
Private Engineering Contracts	+
Machine-Tool Orders	+
Orders for Steel Boilers	+
Capital Goods' Stock Prices	+
Employment	-
Steel-Ingot Production	-
New Capital Issues of Corporate Securities	+
Carloadings of Heavy Products	-
Lumber Production	-
Electric Power Production	-
Harwood Index of Inflation	+

It is noteworthy that the indicators assumed to have forecasting value with respect to future production are all favorable, but some refer to the pre-V-J day period. The net result at present is not conclusive; an orderly transition appears to be in progress.

BUSINESS

New Consumer Goods Per Capita

The Institute's index of new consumer goods per capita recorded a small advance during August following a similar fractional gain in July. The index is 84.8 per cent of estimated normal, compared with an index of 84.3 in June and 84.6 in July.

The index shown in the chart at the top of this page is a six-month moving average of the volume of durable and nondurable consumer goods produced in the United States per capita. The index is plotted at the end of the six-month period on the assumption that the average length of time for this type of goods to reach consumers after production is three months. The index is adjusted for seasonal influences and for long-term trend and is expressed as a per cent of estimated normal.

The index has been below normal for the past three years. Following a precipitous decline that occurred during the first year of our participation in the conflict, the index became stabilized at a level varying from twelve to fifteen per cent below estimated normal.

During 1942, virtually all stocks of durable goods that were accumulated before our entrance into the war were distributed to the public, and during the past two and one half years civilians have had to depend on the mechanical equipment previously purchased.

The flow of nondurable consumer goods, such as food and clothing, constitute the most stable element in a nation's economy, and even during the war period the decrease in the supply of this class of goods that was available for the civilian population was far less extensive than was the decrease in the supply of consumer durable goods. The end of hostilities will make possible a rise in the index of new consumer goods per capita, but this will be delayed until a more adequate flow of durable goods is obtainable. It therefore does not appear to be probable that the index of new consumer goods per capita will advance to estimated normal until some time in 1946 after large-scale production of such durable goods as passenger automobiles and household electric equipment has been attained over a three or four month period.

Once the process of supplying the civilian population with the durable consumer goods it desires is established it seems probable that there will exist a situation similar to that in 1941 when the index of new consumer goods per capita reached the highest level recorded during a period of three decades.

The timing and magnitude of the upturn in the distribution of goods to consumers will be influenced by policies adopted by the Federal Government. Price controls may be used for political purposes in such a manner as to prevent early readjustments. It is the objective of the Government to maintain wage rates at a high level while limiting price advances that would compensate for higher production costs. If profitable operations can be maintained only by producing poor quality goods, the eagerness of the public to buy new equipment will not be lasting. Eventually, the competitive system will function to bring improved goods at more reasonable prices into the civilian markets. However, the early part of the transition period is likely to be attended by confusion and uncertainty as long as the Government continues to exert authority over production and price relationships.

THE FUNDAMENTALS

Supply

The steel-ingot production rate was estimated to be 74½ per cent of theoretical capacity last week. This represented a gain of 4½ points from the preceding week's rate of 70 per cent of capacity. The industry's present situation was summarized by *The Iron Age* as follows: "The steel industry this week was still attempting to bring a semblance of order out of the temporary chaos in steel mill schedules occasioned by war contract cancellations, many of which have not yet reached the mill level. That it may take some time before steel activity gets back to normal seems to be apparent. This is especially true because of the slowness in war contract cancellations in reaching mill books. Cancellations of steel orders on mill schedules have not been as rapid as anticipated. Consequently, there are still many orders on the books which will eventually be canceled and until such time as this takes place, complete reconversion of the steel industry to peacetime operation will be

hindered. There is some concern that many consuming industries will not be immediately able to take steel in quantities which would warrant a high level of operations at steel mills. While the railroads, warehouses, freight carbuilders, automobile manufacturers and farm equipment producers will be able to take sizable deliveries of steel, many other industries such as appliance manufacturers still have a major reconversion problem which may take weeks to solve."

	1929	1932	1937	1938	1944	1945
Per Cent of Capacity	87.5	12.0	73.0	41.0	96.5	74.5

(Latest 1945 weekly data; corresponding week earlier years)

Electric-power production last week was 6.8 per cent less than was output in the corresponding week of 1944. In the preceding week, a decrease of 10.5 per cent was reported. The decrease in electric-power production in comparison with output a year ago was most pronounced in the central industrial region. The New England and the Pacific coast states also showed substantial declines. The region including the southern states was the only one in which electric-power production was well sustained.

	1929	1932	1937	1938	1944	1945
Billion Kilowatt-Hours	1.68	1.44	2.15	2.05	4.42	4.12

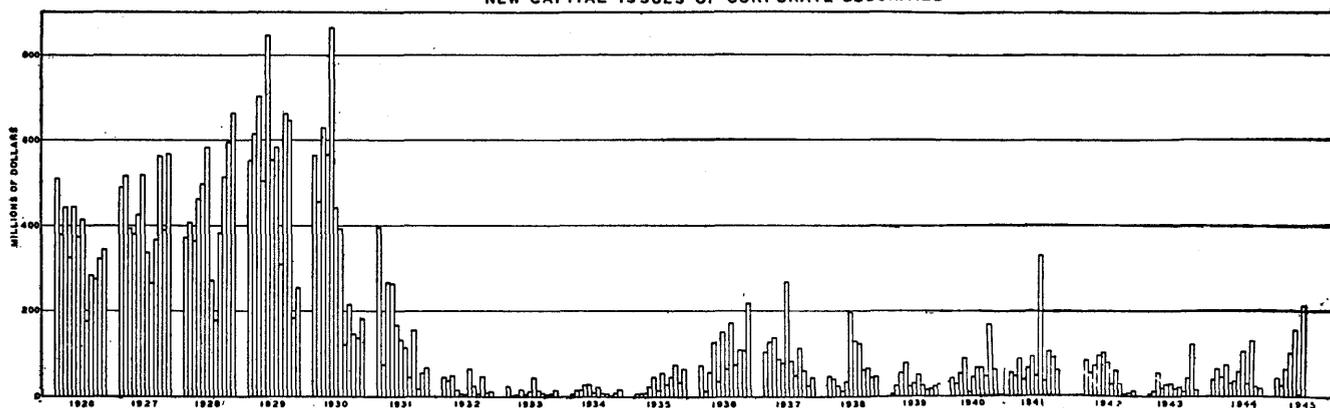
Lumber production decreased more than seasonally last week and the adjusted index declined from 84.5 to 55.2 per cent of the 1935-1939 monthly average. Last week's index was the lowest to be recorded since 1938 and probably marks the low point in the industry's activity for the early postwar period. The lumber industry has virtually no reconversion problem and production can be expanded as soon as more operatives are available to work in the mills and in the woods and as soon as new equipment can be supplied to replace the old machinery that the lumber companies have had to use during the war period.

	1929	1932	1937	1938	1944	1945
New York Times Index	134.8	35.9	83.5	72.0	103.4	54.2

Demand

The Federal Reserve Index of department-store sales last week was six per cent higher than the index reported in the corresponding week of 1944. The Index for the four weeks ended August 25 was seven per cent higher than the average for the corresponding period last year. During the fall and winter months there will be a test of the combined effects on retail sales of conflicting influences affecting the public's desire and ability to buy. An inevitable decrease in aggregate wages and salaries will be partially offset by the payment of unemployment benefits and by the payment of special bonuses to personnel released from the armed services. The volume of checking account deposits and currency now available to the public is greater than it has been during any boom period of the country's history. The extent to which these purchasing media may be lured into the markets will, to a considerable degree, be dependent on the quality and quantity of offerings available. Although the public's discrimination in buying has suffered during the war period, shoppers' attitude towards the market appears to have remained more cautious than it did at the height of the boom during and following the First World War.

NEW CAPITAL ISSUES OF CORPORATE SECURITIES



Prices

Price fluctuations in the staple commodity markets resulted in net gains for the week. The Dow-Jones Index of Commodity Futures closed at 98.68 on August 23 and at 99.60 August 30.

The National Industrial Conference Board reported an advance of more than half a point in the combined cost of living index from the May to the June level. The advance of the combined index was attributable to a substantial increase in food costs during the month. Other items entering into the calculation of the index were substantially unchanged. The combined index and separate items for July 1914, just before the First World War started, for June 1920, the month in which the peak in commodity prices was recorded for the First World War period, for August 1939, the eve of the outbreak of the Second World War, and for May and June 1945 are shown in the following table:

	July 1914	June 1920	Aug. 1939	May 1945	June 1945
All Items Combined	61.3	192.0	84.0	106.2	106.9
Food	66.1	147.2	75.3	112.7	114.8
Housing	57.7	91.2	86.2	91.0	91.0
Clothing	58.8	149.9	81.9	94.9	94.7
Fuel and Light	63.3	98.6	84.0	96.2	96.3
Sundries	59.0	107.3	96.9	115.5	115.5

FINANCE

New Capital Issues

The chart at the top of this page shows the volume of new corporate financing in the United States by months for the years 1926-1944, and for the first seven months of 1945. The data for investment trust issues are excluded to avoid duplication. The chart portrays both the annual and the monthly volume of private capital flowing into industry over a period of two decades. During this time, circumstances governing private investment markets have changed radically.

During the New Era boom shown in the period 1926-1930 new capital issues greatly exceeded the annual savings of the people. This condition was made possible by the inflationary monetization of common stocks through the extension of security loans by the commercial banks. During the depression years that followed that orgy, there was virtually no flow of funds into the private capital markets. Even in the recovery years 1936-1937 the volume of new corporate issues was relatively small.

Compared with the rate of flow of new capital that prevailed before the war, the record after the beginning of our war participation in December 1941 was as

favorable as could be expected. In Great Britain, the new private capital market disappeared after war broke out in 1939 and has since shown only a slight tendency towards revival. Most of the capital borrowed in this country during the war period had as an objective the financing of industrial establishments for the manufacture of war materials. A moderate amount was borrowed by the public utilities to finance increases in electric power capacity. The railroads borrowed only a relatively small amount and virtually all of this represented equipment trust certificates having short-term maturities.

During the war, the United States Treasury entered the market periodically with war loan offerings, thus limiting the opportunity for private corporate financing. In 1929 when the boom in the private capital market was at its height, all new private capital issues aggregated only \$6,400,000,000 (excluding investment trust issues). This sum is less than half of the total raised by the Treasury in one of its war loan campaigns conducted during the past three years. During the first seven months of 1945, new corporate issues aggregating \$598,000,000 par value were 73 per cent greater than the total for the first seven months of 1944. The volume in July this year exceeded that in any month since August 1941.

The total of \$212,000,000 par value of new capital issues in August this year was divided by borrowing corporations as follows: \$193,000,000 by industrial companies; \$17,000,000 by the railroads; and about \$4,000,000 by the public utilities. The relatively heavy volume of new financing undertaken in July was partly attributable to the postponement of borrowing during the preceding month when the United States Treasury was conducting its seventh war loan campaign. New corporate financing in July and in the first seven months of each year during the past twenty years is shown in the accompanying summary.

NEW CORPORATE FINANCING IN THE UNITED STATES

Year	First Seven Months		Year	First Seven Months	
	July	Months		July	Months
1926	415	2,886	1936	63	521
1927	338	3,098	1937	82	911
1928	272	2,957	1938	130	492
1929	583	4,354	1939	50	267
1930	392	3,913	1940	50	320
1931	115	1,422	1941	47	427
1932	63	223	1942	28	511
1933	52	112	1943	19	170
1934	20	119	1944	57	346
1935	55	156	1945	212	598

Source: Commercial and Financial Chronicle.