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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Summary and Outlook

In spite of the continued strike in the Chrysler plants, industrial production has increased in the past 2 months. Steel production was at record levels in the third week of April, and industry officials expect near-capacity levels of production to be maintained for some time to come. Automobile output increased during March and April in spite of the Chrysler strike. A possible strike in the plants of General Motors at the end of May somewhat obscures the outlook for the automobile industry. Although electric-power production is below the levels reached earlier this year, a relatively high rate of production has been maintained in recent weeks; and output is far above that reported in comparable periods last year. Consumer-goods production increased in March and probably increased further in April. Production of chemicals, paper, household appliances, printing machinery, and television sets has continued at high levels. A somewhat less favorable outlook appears at the retail level of business activity, where inventories appear to have accumulated substantially in February and March.

Pre-Easter sales of department stores were somewhat disappointing to retailers who had hoped for greater-than-seasonal gains, and demand for apparel was especially poor in the weeks immediately following. However, premiums are again being paid for some passenger cars; and the demand for television sets seems to be virtually insatiable. The amount of purchasing media available increased during the first half of April, and probably will increase more in the next several weeks. Therefore, effective demand probably will continue at relatively high levels.

Consumers' prices decreased in February and may have decreased further in March. Wholesale commodity prices, on the other hand, have leveled off in recent weeks.

Construction activity has continued at a high rate for several months and increased to record proportions in March, when residential construction increased substantially. Commercial failures in February were relatively few in number, and the liabilities involved were small. Although the downward trend may have been reversed in March, the relatively few failures are further evidence that the economy is in the recovery phase of a business cycle. Industrial employment was unchanged in February from that reported the previous month. However, employment increased markedly in March; and unemployment decreased from the February peak.

We have repeatedly pointed out that an economy enjoying a boom prosperity supported by inflation is vulnerable and that various combinations of unfavorable developments could induce drastic deflation. Some of the possible deflationary processes are discussed in the following paragraphs.

Because the volume of real-estate and other loans (including consumer credit) now outstanding is large, periodic amortization payments also are substantial. If construction activity and employment decreased, amortization payments might exceed new credit extensions for purchasing real estate and other consumer goods. As a result, inflationary purchasing media would be retired from circulation. Furthermore, substantial sums for investment would thus become available to savings banks, insurance companies, savings-and-loan associations, and other agencies. The investments acquired might well be Government securities purchased from the commercial banking system, with resulting further deflation.

Presumably, in the event of deflation, business activity in general would be curtailed and loans for inventory speculation would contract. Although this development would not necessarily be reflected in our index of inflation (see "The Possibility of Concealed Deflation," *Research Reports,* June 13, 1949), such a development would be deflationary.

We have estimated that, *if* deflation were initiated, the outstanding purchasing media might be reduced by $15,000,000,000 to $18,000,000,000 within a period of 1 or 2 years. Of course, this deflation would be offset to some extent by unemployment-compensation payments of $2,000,000,000 to $3,000,000,000 a year; and a Government spending program probably would be undertaken that ultimately might reverse the deflationary trend. In the meantime, a severe and brief depression could occur if some unfortunate development did initiate a deflation of the magnitude indicated.

However, in the absence of any initiating unfavorable development such as a major disaster or the imminence of war, the present boom may develop further and may continue for several months or a few years. We do not agree with various widely publicized predictions to the effect that a collapse is inevitable within a few months.

Notice to Annual Sustaining Members: The new edition of *How to Invest Wisely* will be mailed to you in the next few days. Several major revisions have been made in this new edition of the booklet, and a section on insurance and investments has been added. If you do not receive your copy within a reasonable time, please notify us.

SUPPLY

Industrial Production

In the first full month of uninterrupted steel and coal production since last summer, the preliminary index of industrial production adjusted for long-term trend increased nearly 4 percent during April to the highest level since March 1949. We expect that final data will reveal a greater increase than that indicated by preliminary estimates.

The April index, which was 6 percent below the postwar highs, was 2 percent above that of April 1949 and 16 percent above the October 1949 low.

Preliminary data reveal the following increases from the March levels of activity: steel, 14 percent; minerals, 3 percent; paper, 2 percent; and automobiles, 1 percent (excluding possible Chrysler production during the last week of April). Lumber production and refined-petroleum output decreased 5 and 4 percent respectively.

Operating at 100 percent of capacity during the week ended April 22, the steel industry made a new all-time production record of 1,906,000 net tons. If this rate of operations is continued through the remainder of April, there is a possibility that more than 8,000,000 tons will be produced in that month. Steel production in a single month has exceeded 8,000,000 tons on only two occasions, in January 1949, when 8,183,495 tons were produced, and in March 1949, when the industry established an all-time peak of 8,387,927 tons. Output probably will remain at record levels for some time in order to make up the losses in production that occurred during the fall steel strike and the more recent coal strikes. According to *The Iron Age* " * * * there are still no signs of a slowing of demand."

Activity in most of the automobile industry also has been at record levels in recent weeks. General Motors, Ford, and Studebaker all have announced that new production peaks were achieved in March. Of course, the Chrysler strike has prevented the industry as a whole from equaling the record production reached in August 1949, when 657,000 cars were manufactured. Production in March was 12 percent below that of the record month. In view of the fact that Chrysler ordinarily produces about 20 percent of the industry's total output, a new peak might have been reached during April had Chrysler resumed full production. Ordinarily, automobile output decreases in May; consequently, even if the Chrysler strike is ended soon, a new peak may not be reached in the near future. Moreover, a General Motors strike at the end of May would curtail output drastically.

Coal production has recovered rapidly since the end of the strike. Output in March was more than 3 times that of February; and a further increase of 4 percent occurred in April, when production was the greatest since April 1949.

According to preliminary data, textile production in March may have reached an all-time high. However, reports in the first few weeks of April suggest that output has since been curtailed slightly. Apparently, some mills that were operating on a schedule of 3 shifts, 6 days a week during March have reduced the working week to 5 days.

Lumber production, which had increased substantially during February and March, seems to have decreased slightly during April. The record levels of construction activity should keep lumber output at high levels. However, a prominent official in the lumber industry has suggested "that a decline in orders from retailers to furniture manufacturers, as well as the building up of lumber inventories by television-receiver manufacturers soon would bring the current sellers market in lumber to an end."

The steel industry already is operating at 100 percent of capacity, textile production is leveling off, and a General Motors strike would further decrease automobile production; therefore, no great increase in industrial production is probable during the next few months. However, if minerals production increases to the postwar peak or resumption of automobile production by Chrysler is accompanied by new output records for the industry, some further rise in our index of industrial production may occur.

Latest Weekly Data

Steel-ingot production, scheduled at 100 percent of capacity for the week ended April 22, 1950, was 2 percent more than that in the preceding week and was 6 percent more than that in the corresponding week last year.

	1929	*1932*	*1937*	*1938*	*1949*	*1950*
Percent of Capacity†	96	23	92	33	98	100p
Weekly Cap. (Million Tons)	1.38	1.52	1.51	1.54	1.84	1.91
Production (Million Tons)	1.32	.35	1.38	.40	1.80	1.91

Automobile and truck production in the week ended April 15, 1950, in the United States and Canada was estimated at 147,657 vehicles, compared with a revised total of 133,172 vehicles for the previous week.

	1929	*1932*	*1937*	*1938*	*1949*	*1950*
Vehicles (000 omitted)†	140	36	125	62	132	148p

Electric-power production in the week ended April 15, 1950, decreased to 5,863,247,000 kilowatt-hours from 5,897,831,000 kilowatt-hours in the previous week.

	1929	*1932*	*1937*	*1938*	*1949*	*1950*
Billion Kilowatt-Hours†	1.71	1.48	2.17	1.96	5.34	5.86

Lumber production in the week ended April 8, 1950, increased less than seasonally. *The New York Times* seasonally adjusted index was 1 point less than that for the previous week but was 9 points more than that for the corresponding week last year.

	1929	*1932*	*1937*	*1938*	*1949*	*1950*
The New York Times Index†	142	41	85	84	91	100

†Latest weekly data; corresponding weeks of earlier years
p=preliminary

DEMAND

The Harwood Index of Inflation

Our preliminary estimate of the Harwood Index of Inflation for April reveals that the inflationary trend that began a year ago, but which was reversed temporarily in the first quarter, has been resumed. Based on preliminary records of Treasury receipts and expenditures, we have estimated that the index rose to 176 from the revised March figure of 172. The April preliminary figure was 6 percent above that for April last year and was only 3 points (2 percent) below the high reached last December.

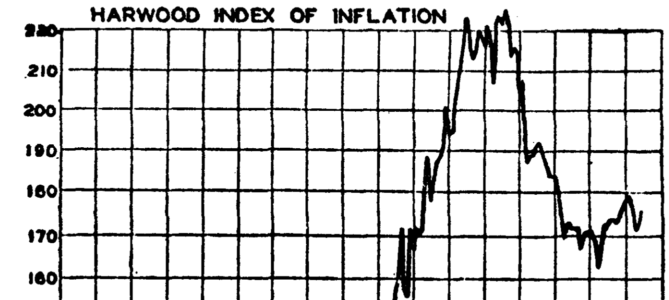
Although the figure for March is not yet final, the revised index at the end of the month was 172, 3 points below the revised February figure, but still within the range of possibilities indicated in the last "Monthly Bulletin." Redemptions of Treasury tax and savings notes during all of March totaled only $315,500,000, which compares with redemptions of $469,200,000 in

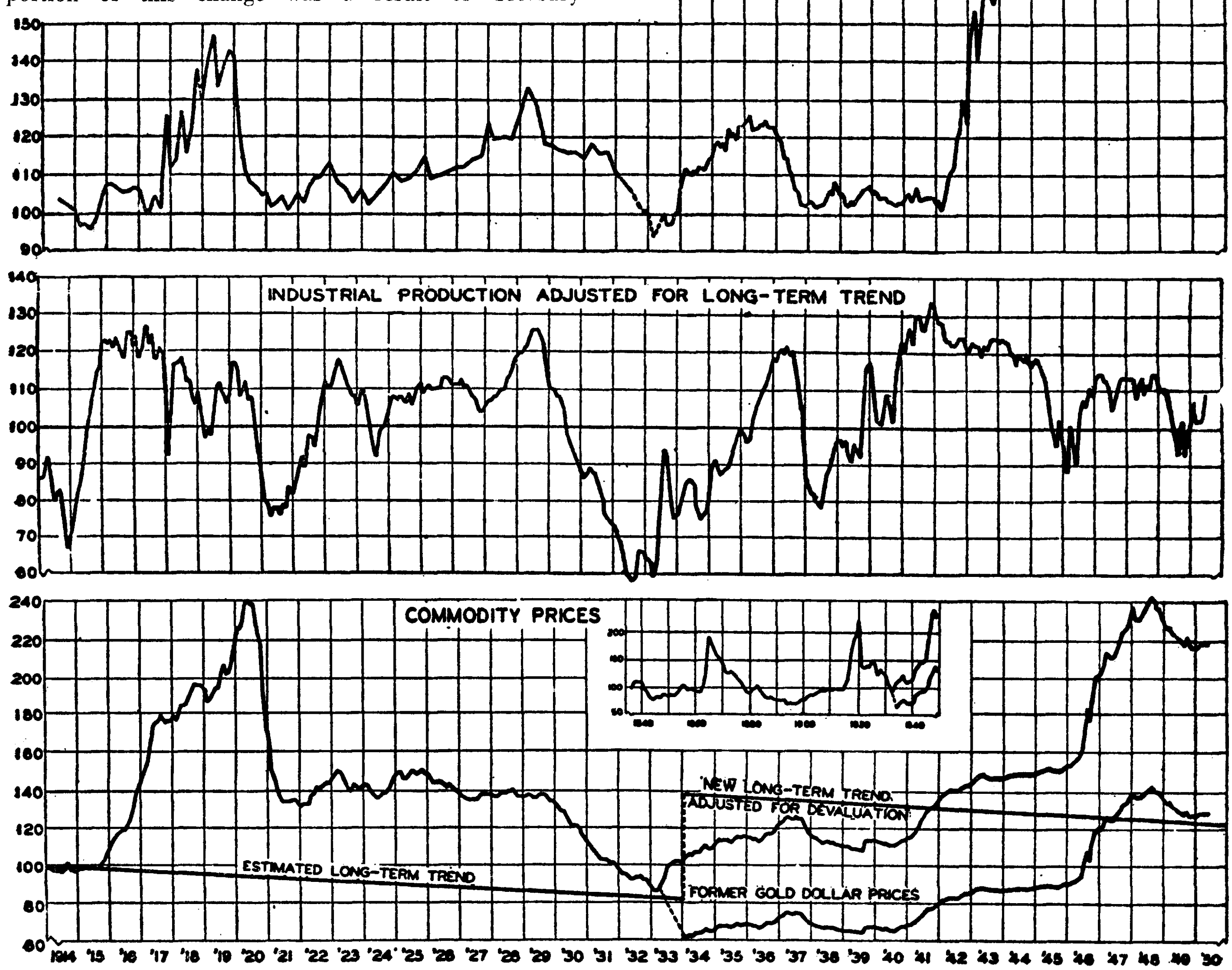
March last year, when the amount outstanding was about one-half that at the end of March this year. Furthermore, sales of tax-savings notes continued large during March and exceeded sales in March last year by $160,-000,000.

After analyzing Treasury cash receipts and expenditures, we have concluded that the cash deficit for April will be at least as large as that reported in April a year ago. By midmonth, receipts were slightly larger than those of the same period last year; but expenditures also were slightly larger. In view of the cash outlay for the veterans' dividends (not reported in the Budget expenditures), cash disbursements probably will be substantially more than those in April last year. Therefore, the cash deficit for the month apparently will be at least as great and perhaps $400,000,000 more than the cash deficit reported in April last year, when our index of inflation rose 4 points.

Although the Federal Reserve banks have purchased small amounts of Government securities in recent weeks, the member banks have continued to dispose of their holdings albeit in somewhat smaller amounts than the sales of earlier weeks. Nevertheless, the net change in the banking system's holdings of securities since the end of March has been a decrease of nearly $115,000,-000. This brings the total decrease since the end of January to approximately $3,115,000,000. A small portion of this change was a result of Treasury cancellation of the public debt. (Of interest in this connection is the fact that retirement of the public debt during the first quarter this year was slightly greater than the retirement reported during the same period last year. Of course, included in this year's figures were the cancellations of notes held in the National Service Life Insurance fund.) However, individuals and corporations have acquired most of the securities sold by the commercial banking system in recent months.

Last year during April the commercial banking system purchased large amounts of Government securities, thereby contributing to the inflationary trend that occurred in that month. However, during the recession then under way, reductions in certain types of bank assets, particularly commercial and agricultural loans, occurred; and the banks replaced some of these assets





with Government securities. On May 5, 1949, the member banks' reserve requirements were lowered, thereby encouraging the banks to expand their security holdings still further.

If the Federal Open-Market Committee's present policy is continued, member banks and other commercial banks presumably will stop selling Governments shortly. Although the commercial banks may not be permitted to buy new issues, they may be eager purchasers of bank-eligible issues that private interests wish to dispose of. If this occurs, additional inflationary purchasing media will augment the inflation attributable to the continued expansion of real-estate and installment loans.

Conclusion

We conclude that an increase in the degree of inflation comparable to that which occurred in the second quarter last year is possible during the present quarter. Presumably, June tax collections will limit the inflationary trend and perhaps reverse it temporarily. Thereafter, the trend of our index of inflation will depend to a large extent on the expenditures approved during the present session of Congress.

Department-Store Sales

Department-store sales for the week ended April 15, 1950, were 21 percent less than sales for the previous week but were 19 percent less than sales in the corresponding week last year.

PRICES

Commodities at Wholesale

At mid-April the index of wholesale commodity prices was unchanged from the March figure. The preliminary April index was 3 percent below that of April 1949 and 10 percent below the all-time high reached in August 1948.

Minor increases in the prices of chemicals and metals and metal products during the first 2 weeks of April were counterbalanced by a decrease in food prices. Prices of farm products, textiles, fuel and light, and building materials were unchanged from those of a month ago.

Changes in the subindexes of the wholesale-commodity-price index during the first 2 weeks of April were slightly greater than those of most of the major components. Prices of meats and livestock decreased; prices of grains increased nearly 3 percent.

The failure of the Congress thus far to appropriate additional funds for the Commodity Credit Corporation has resulted in the abandonment, temporarily at least, of Government price supports for a substantial number of farm commodities. However, few persons, if any, believe that the situation is anything but temporary; consequently, the farmers probably will not hesitate to hold their products if market prices fall below the support prices expected to be available later.

The widespread advertising of Mr. Baxter's new book, *Lower Prices Coming!* invites comment at this time. In 1944 Mr. Baxter's book *No Inflation Coming!* attempted to explain "why common stocks, farms, real estate and commodities will be *cheaper*." In 1946 Mr. Baxter's enlarged postwar edition of *No Inflation Coming!* attempted to explain "why you must have cash in the bank and government bonds to take advantage of coming bargains in business, real estate, commodities, and common stocks." *From 1944 through 1948 the rise in prices of real estate, commodities, and common stocks was one of the greatest in the history of the Nation.* Since 1944 Mr. Baxter has been saying in effect what he is saying now ," * * * the dollar is once again going to be King." If Mr. Baxter continues to adhere to the opinion that prices will be lower, eventually and for a short period at least he probably will be correct. However, we do not agree that "Already developing is a new respect for the American dollar." Present indications, for example, reveal that a substantial degree of inflation probably will continue for some time to come.

We have previously indicated that the long-term (10 to 15 year) trend of prices probably will be downward. However, the additional inflation expected in the next few months, perhaps during all of 1950, may support commodity prices at present levels (that is, at progressively higher levels in relation to *the long-term trend) or may even facilitate a short-lived speculative rise in commodity prices. We see no reason to expect a great decline in commodity prices in the immediate future.*

United States Bureau of Labor Statistics
Wholesale Commodity Price Index
(Monthly Average 1913=100)

	1920 High	*1933 Low*	*1948 High*	*Apr. 1949*	*Mar. 1950*	*Apr. 1950p*
All Commodities	240	86	243	224	218	218
Farm Products	238	57	279	238	221	221
Foods	232	84	296	254	243	242
Textile Products	340	89	263	248	238	238
Fuel and Light	342	99	224	215	212	212
Metals and Products	173	85	191	189	186	187
Building Materials	297	123§	360	346	340	340
Chemicals	238¶	88	173	147	145	147
Hides and Leather	307‡	100	298	264	256*	NA
Housefurnishings	266	127	264	262	258*	NA
Miscellaneous	255	83	177	166	158*	NA
Raw Materials	241	70	268	241	236*	NA
Semimanufactures	338	74§	216	205	193*	NA
Finished Goods	227	95	237	221	215*	NA

p=preliminary; ‡1919; ¶1918; §1932; *February, 1950
NA=not available

Latest Weekly Data

(August 1939=100)	*1949 Apr. 20*	*1950 Apr. 13*	*1950 Apr. 20*
Spot-Market Prices (28 basic raw materials)	244	247	249
Commodity Futures Prices (Dow-Jones Daily Index)	264	286	290

Statistical Summary; Production, Purchasing Media, and Prices

	1949									1950			
	Apr.	*May*	*June*	*July*	*Aug.*	*Sept.*	*Oct.*	*Nov.*	*Dec.*	*Jan.*	*Feb.*	*Mar.*	*Apr.*
Index of Industrial Production	106	100	98	93	101	102†	93†	99†	103*	108*	103*	104*	109*
Index of Inflation (Ratio Form)	166†	173†	172†	174*	174*	173*	175*	177*	179*	178*	175*	172*	176*
Commodity-Price Index	225	223†	222†	220*	219*	220*	218*	217*	216*	216*	218*	218*	218*
Commodity-Price Index (In terms of former gold dollar)	133	132†	131*	130*	130*	130*	129*	128*	128*	128*	129*	129*	129*

*preliminary; †revised