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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

Gold Holdings

The decrease in United States gold holdings during recent months has aroused increased interest in this subject.[1] We believe that the following article will help readers to understand what is happening and its significance.

Characteristics of Our Present Monetary System

Our present monetary system may be called a restricted international gold-bullion system. Gold coins are not in circulation in the United States, and United States citizens are unable to demand gold from the United States Treasury in exchange for their holdings of United States paper currency. However, the gold dollar is defined as a specified weight of gold, and the Federal Reserve banks must hold gold certificates in specified ratios as a reserve against their note circulation. Internationally our present monetary system provides dollar convertibility into gold; in other words, foreign governments and foreign central banks can exchange their dollars for gold bullion at will.

Changes in the United States gold stock affect our domestic monetary situation in two major ways: (1) by changing the amount of available purchasing media and (2) by changing the reserves of the commercial banks.[2]

Changes in Domestic Gold Stocks Since 1933

The Nation's stock of monetary gold, which averaged about $4,000,000,000 in the early 1930's, increased rapidly during the later years of that decade and reached nearly $23,000,000,000 in 1942. During World War II the Nation's gold stock decreased nearly $3,000,000,000 but increased again after the end of the war to an alltime high of $24,600,000,000 in August 1949.

After devaluation of the British pound and other continental currencies in September 1949, United States gold holdings decreased, but the rate of decrease was moderate through mid-1950. Following the outbreak of the Korean War, gold flowed out at a faster rate. (Substantial purchases of raw materials by the United States in the British sterling area were primarily responsible for the acceleration.) The Nation's gold stocks decreased nearly $2,800,000,000 through July 1951, the greatest decrease ever recorded in such a short period of time (20 months).

[1]A particularly worthwhile article appeared in the August *Monthly Letter on Economic Conditions* published by The National City Bank of New York.

[2]For a more detailed discussion, see the article, "Purchasing Media," in *Where Are We Going?*

During the third quarter of 1951 the gold holdings of the United States increased again as the balance-of-payments position of the sterling-area countries worsened. However, the third-quarter increase of $1,500,000,000 was less than the preceding decrease, and the record level of August 1949 was not regained.

After a few months of relatively no change, a second postwar outflow of gold began. From the end of 1952 through April 1953 the Nation's gold stock decreased $800,000,000. During the second quarter of 1953 the gold outflow virtually stopped, but it was resumed in July and the early part of August. During the 4-week period ended August 5, 1953, the gold outflow totaled $210,000,000.

Economic Significance of Changes in Gold Holdings

Changes in gold holdings may have great significance. Usually, they reflect changes in the balance of trade between foreign countries and the United States, but at times changes in gold holdings may reflect increased or decreased fear or suspicion on the part of foreign countries. For example, the large inflow of gold described above that ended in 1942 reflected in part the fears of some European nations that gold held in their own vaults might be confiscated by the armed forces of Germany; and suspicion of a nation's solvency or of its intentions to cheat its creditors by devaluation may induce an outward flow of gold from that country. Gold movements attributable to shifts in the balance of trade constitute an important guide to central-bank policy, but gold movements attributable to the other factors mentioned may or may not be of equal importance. Of course, an outflow of gold that reflects suspicion or distrust of a nation's credit and of its intentions with reference to devaluation of the monetary unit should constitute an important warning to the monetary authorities, but the record in recent decades indicates that such warnings are more frequently disregarded than heeded.

Significance of the More Recent Changes in Gold Holdings

The $800,000,000 decrease in United States gold holdings that occurred between October 1952 and the spring of 1953 apparently was attributable largely to improvements in the balance of payments of foreign countries, primarily those of Western Europe. In part, this outflow may also have been attributable to suspicion of the United States' intentions following the widespread discussions of another devaluation of the dollar late last summer. However, authoritative denials that a change in the dollar "price" of gold would be considered presumably soon allayed any distrust that had been aroused.

The improvement in foreign-trade balances was reflected in the fact that the excess of American exports over imports of goods and services declined to a few hundred million dollars per quarter during the second half of 1952 and the first quarter of 1953, compared with an excess of nearly one billion dollars during each of the two preceding quarters. The relatively small foreign-trade deficit was more than counterbalanced by United States private and Government loans and gifts (other than military); consequently, foreign governments were able to accumulate sizeable holdings of American dollars, some of which were converted into gold. During April and May the excess of exports increased and foreign economic aid was insufficient to make up the difference; the further tightening of the money market may have strengthened confidence in the American dollar and thus may have contributed somewhat to the cessation of the gold outflow.

The reasons for the most recent gold exports are not clear as yet. Final data for recent foreign-trade developments are not available. However, one reason may be an expectation on the part of foreign banks that the recent actions of the Federal Reserve Board and the Treasury may precipitate additional inflation that will further decrease the purchasing power of the dollar.

Effects of Changes in Gold Holdings

To the extent that foreign central banks and governments withdraw balances held by United States commercial banks in order to obtain gold, the commercial banks' reserves with the Federal Reserve banks are reduced. Such a development with the present amount of credit outstanding could force some liquidation of loans. Of course, reserves could be increased by selling bonds to the Federal Reserve or by temporarily borrowing from the Federal Reserve. The Federal Reserve Board could also ease the situation by reducing reserve requirements as they did a short time ago, but to continue an easy-money policy in spite of increasing gold exports would be dangerous; the outflow of gold then might swell to enormous proportions.

In any event, the Federal Reserve authorities would be limited somewhat by the fact that 25 percent of their reserves must be gold. In fact, because the reduction in reserve requirements from 40 to 25 percent was a wartime measure intended to meet the exigencies of that situation, we doubt that the Federal Reserve authorities would be willing to see their gold reserve fall below the traditional 40 percent without serious misgivings. In all probability, such disregard of the statutory limitations that prevailed for many years would deepen distrust of the dollar by foreign banks and governments.

How Much Gold Could Foreigners Demand?

The present deposits of foreign governments and foreign individuals held by United States banks may be converted to gold for export or earmarking (setting aside for the account of foreign governments and foreign banks). Foreign short-term holdings of United States Government obligations maturing in not more than 1 year from their date of issue could be readily converted to dollars and thence to gold for export or earmarking. According to Federal Reserve Board statistics, such liabilities totaled $9,100,000,000 at the end of April; $4,700,000,000 consisted of liabilities to foreign central banks and governments, and $4,400,000,000 consisted of liabilities to private businesses and individuals. On the other hand, at the end of April, American businesses and individuals had short-term claims against foreigners totaling $1,000,000,000; consequently, the net short-term liabilities to pay dollars to foreigners at the end of April totaled about $8,000,000,000. In addition to these liabilities, foreign governments have invested substantial amounts in United States Government long-term securities. (The precise amount is not known. Total investments in short- and long-term securities at the end of June were $2,500,000,000; consequently, the figure is not greater than $2,500,000,000.)

Among the $4,400,000,000 short-term liabilities to foreign business and individuals some portion presumably represents working balances related to foreign-trade operations; much of the remainder apparently is the so-called "hot money" that was invested in the United States for security reasons during World War II. (Unfortunately, data as to the distribution of these liabilities between the two types are not available.) If distrust of the American dollar becomes widespread, owners of "hot money" probably would try to exchange their holdings for currencies of other nations, which in turn would probably result in an increased demand for gold by foreign central banks.

Those liabilities to foreigners representing working balances used in foreign-trade operations presumably would be liquidated only in proportion to any decrease in trade between other nations and the United States.

Approximately $4,700,000,000 of total short-term liabilities consists of liabilities owed to official institutions —foreign governments and foreign central banks. Distrust of the American dollar undoubtedly would be reflected in a decrease in these liabilities as they were converted into gold.

Conclusions

The changes in gold holdings may merely reflect only the post-World War II improvement in the economic relations of other nations to the United States. Gold exports may, however, reflect in part an increasing distrust of the American dollar. In any event, gold movements should be observed carefully as one of the important clues to future Federal Reserve policies.

SUPPLY

Industrial Production

Steel-ingot production, scheduled at 96.9 percent of capacity for the week ended August 15, 1953, was 3 percent more than that in the preceding week and was 13 percent more than production in the corresponding week last year.

	1929	*1932*	*1937*	*1938*	*1952*	*1953*
Percent of Capacity†	93	15	84	40	93	97p
Weekly Cap. (Million Tons)	1.38	1.52	1.51	1.54	2.08	2.25
Production (Million Tons)	1.28	.23	1.27	.62	1.93	2.18

Automobile and truck production in the United States and Canada during the week ended August 8, 1953, was estimated at 138,683 vehicles, compared with a revised total of 168,267 vehicles during the previous week.

	1929	*1932*	*1937*	*1938*	*1952*	*1953*
Vehicles (000 omitted)†	114	31	80	15	44	139p

Electric-power production in the week ended August 8, 1953, decreased to 8,463,616,000 kilowatt-hours from 8,511,622,000 kilowatt-hours in the previous week.

	1929	*1932*	*1937*	*1938*	*1952*	*1953*
Billion Kilowatt-Hours†	1.73	1.43	2.34	2.19	7.50	8.46

Lumber production in the week ended August 1, 1953, decreased. *The New York Times* seasonally adjusted index was 4 points below that for the preceding week and was 5 points below that for the corresponding week last year.

	1929	*1932*	*1937*	*1938*	*1952*	*1953*
The New York Times Index†	129	35	87	87	109	104

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

DEMAND

Purchasing Media

Total purchasing media increased $1,500,000,000 during July to $125,100,000,000, about $3,600,000,000 less than the alltime high of $128,700,000,000 reached in December 1952 but $3,200,000,000 more than the figure for July 1952. An increase in the purchasing-media total during July is not unusual; during each of the last 7 years an increase has occurred during July, and the average gain has been $700,000,000.

Purchasing media derived from the first source, the money commodity (monetary gold), decreased $230,-000,000 during July, the largest monthly decrease since last February. (For a more detailed discussion of recent changes in gold holdings, see the lead article in this issue.)

Commercial, industrial, and agricultural loans, the second source of purchasing media, increased slightly during July. The amount outstanding at the end of the month was $30,800,000,000, about $2,200,000,000 more than that at the end of July last year but $1,000,000,000 less than the alltime high of $31,800,000,000 reached in December 1952.

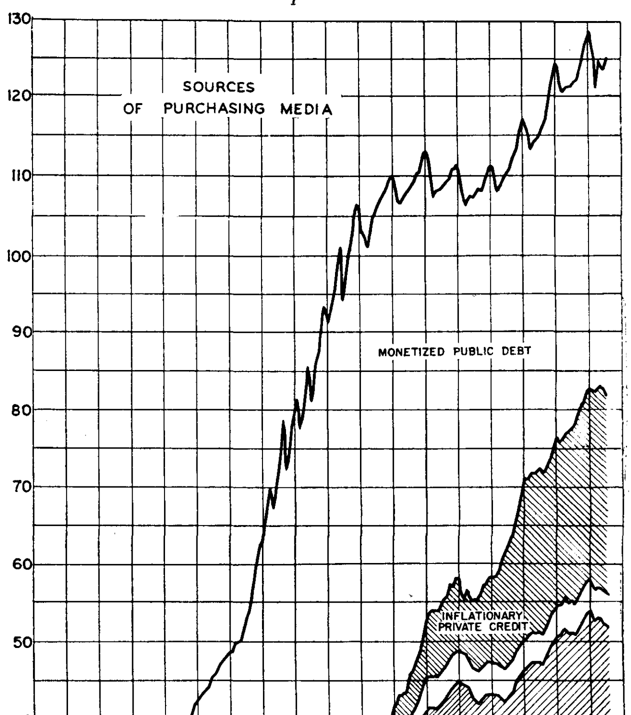
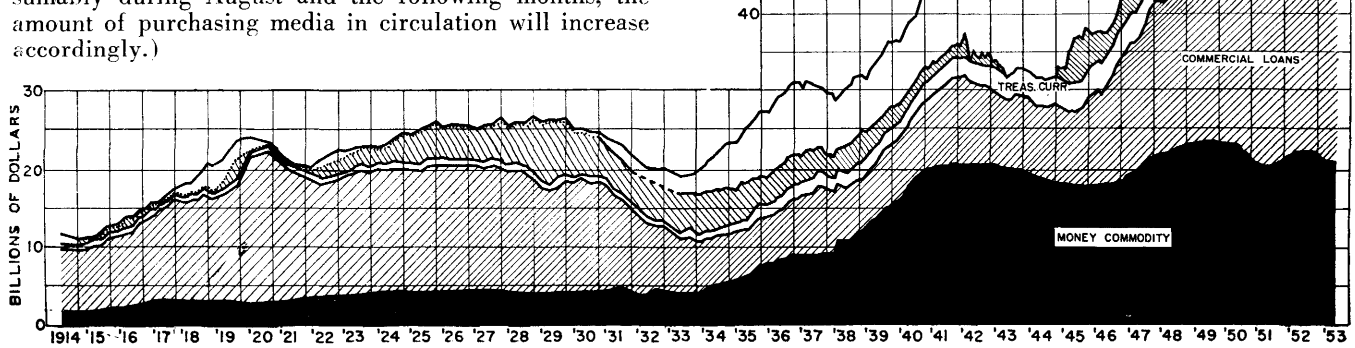
Purchasing media derived from the third source, Treasury currency, have not changed greatly during recent months.

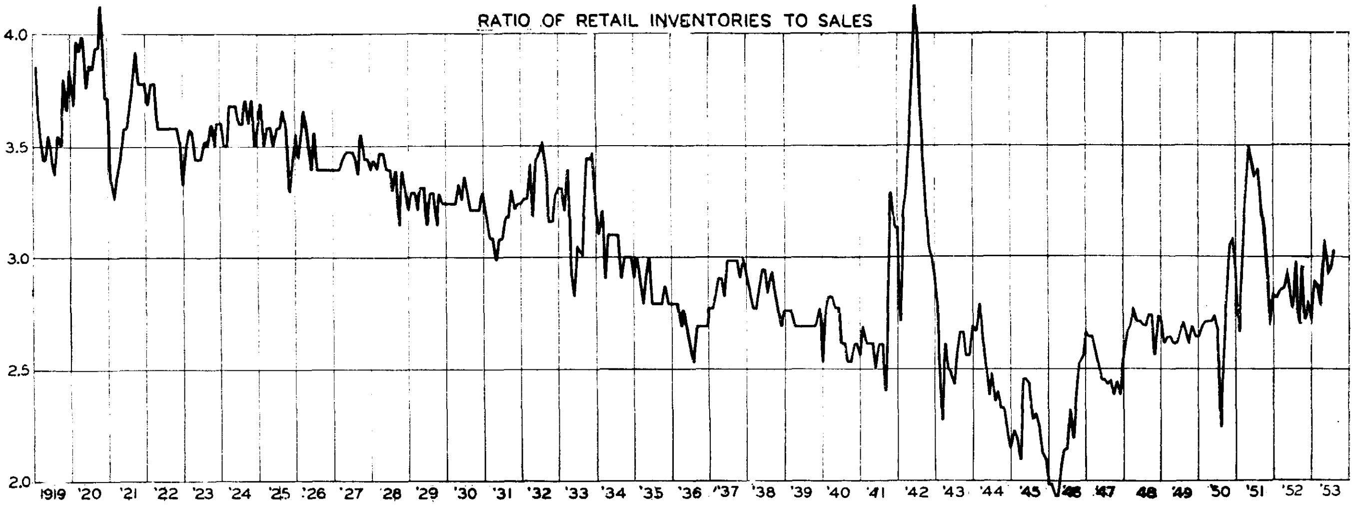
Purchasing media derived from the fourth and fifth sources, both of which potentially are inflationary, increased $1,700,000,000 during July to $69,200,000,000, some $2,000,000,000 more than the amount at the end of July 1952 but $1,500,000,000 less than the amount at the end of December 1952, when the post-Korean peak of inflationary purchasing media was reached.

Investment-type assets of the commercial banks (including the Federal Reserve banks) apparently increased $5,300,000,000 during July: loans on real estate increased $60,000,000; loans on securities increased $160,-000,000; other loans, which include consumer installment credit, increased $50,000,000; corporate securities held by commercial banks increased $190,000,000; Government securities held by the Federal Reserve banks increased $200,000,000; and, according to our preliminary estimates, Government securities held by the commercial banks increased $4,700,000,000. (The substantial increase in the holdings of Government securities by the commercial banks has not resulted as yet in a corresponding increase in the amount of purchasing media in circulation because the proceeds from the sale of new Government issues to commercial banks were credited by the banks to the Treasury's tax and loan accounts and the Treasury has not as yet drawn upon the entire amount of the new balances. As soon as the Treasury disburses the funds accumulated in the tax and loan accounts, presumably during August and the following months, the amount of purchasing media in circulation will increase accordingly.)

Final data for Treasury operations during July reveal that the net cash surplus during the month was $4,070,-000,000. This surplus was possible because the Treasury received $6,500,000,000 of new money through the sale of new issues of tax-anticipation certificates and Treasury bills to commercial banks and to nonbank investors. The net effect of Treasury operations in July, excluding public-debt operations, was a deficit of $2,-600,000,000, about $600,000,000 less than the corresponding deficit during July last year. The relative decrease in Federal spending during July this year was made possible by a decrease in the Post Office deficit and by the temporary withholding of the usual annual Federal contribution of $325,000,000 to the Civil Service Commission. Military expenditures during July were $3,900,000,000, nearly unchanged from the level that has prevailed during the first 6 months of 1953.

Because the Treasury will spend recently accumulated funds during August and October, the amount of purchasing media will tend to increase. Moreover, the seasonal expansion of commercial, industrial, and agricultural loans also will tend to increase purchasing media. However, to the extent that nonbank investors, mainly corporations, acquire tax-anticipation certificates now being held by commercial banks, the increase in purchasing media will be counterbalanced. An increase in purchasing media available by the end of the year to a level approximating, or perhaps exceeding, the record total of December 1952 still seems probable.



Mail-Order and Chain-Store Retail Sales

Sales in the Nation's leading mail-order and chain-store companies during July were 4 percent more than sales in the corresponding month last year. The shoe stores reported the largest percentage increase, followed by the variety stores. The data compiled by *The New York Times* are summarized below.

Percentage Change in Retail Sales for July 1953 vs. July 1952

Mail Order	+ 6
Grocery	+ 6
Variety	+ 7
General Merchandise	+ 7
Automotive-Variety	+ 3
Shoe	+24
Apparel	+ 1
Drug	+ 2
Men's Wear	+ 6

Note: The classes are given in the order of magnitude of dollar sales.

Department-Store Sales

Department-store sales for the week ended August 8, 1953, were 7 percent more than sales in the preceding week and were 2 percent more than sales in the corresponding week last year.

PRICES

Commodities at Wholesale

(August 1939=100)	1952 Aug. 13	1953 Aug. 6	1953 Aug. 12
Spot-Market Prices (22 basic raw materials)	293	269	271
Commodity Futures Prices (Dow-Jones Daily Index)	369	334	328

BUSINESS

Ratio of Retail Inventories to Sales

Preliminary estimates indicate that the ratio of retail inventories to sales, which increased 1 percent during June, increased nearly 3 percent more during July to a level less than 2 percent below the 1953 high reached in April. The July figure is 2 percent above the high reached in July 1952. The July ratio is 12 percent above that of 3 years ago, prior to the beginning of the Korean War.

The seasonally adjusted index of department-store inventories, which was unchanged during June, was unchanged during July also. The seasonally adjusted index of sales decreased nearly 3 percent during July. Consequently, the ratio increased nearly 3 percent during the month. (The ratio is derived by dividing the inventory index by the sales index.) July inventories were 8 percent greater than those of a year ago and 23 percent larger than inventories at the start of the Korean War. The recent level of inventories is the highest since August 1951.

The breakdown of inventories of 325 reporting department stores reveals that main-store inventories were 5 percent larger at the end of April (the latest data available) this year than those at the end of April last year. During the same period piece-goods and household-textiles inventories increased 1 percent; small wares, 5 percent; women's and misses' apparel and accessories, 9 percent; men's and boys' wear, 6 percent; homefurnishings, 1 percent; miscellaneous goods, 4 percent; and basement-store inventories, 7 percent.

The dollar value of new orders placed by department stores during June (later data are not available) was 20 percent more than that during May and was 5 percent more than that during the corresponding month a year earlier. The increase of new orders from May to June was 26 percent in 1952, 29 percent in 1951, 27 percent in 1950, and 21 and 46 percent, respectively, in 1949 and 1948. Thus, the May to June new-order increase is less this year than at any time during the five preceding years.

The dollar value of outstanding orders increased 42 percent from the end of May to the end of June. The increase was somewhat greater than that seasonally expected.

The dollar value of goods received by department stores decreased 19 percent from May to June. The decrease was somewhat greater than usual during the month of June.

Ordering by department-store buyers has not been unusually great during recent months, but because of a downward trend in sales there has been a steady increase in inventories. More cautious ordering and possibly reduced prices in order to stimulate sales appear to be necessary if inventories are not to become burdensome.

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