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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

The Council of Economic Advisers

The second of President Eisenhower's appointments to the Council of Economic Advisers is Neil H. Jacoby, Dean of the College of Business Administration of the University of California at Los Angeles. Thus the first two men appointed to the Council have both been associated with the National Bureau of Economic Research.[1] From Mr. Jacoby's speeches during the last several years, some insight into his economic thinking can be obtained.[2]

Free Enterprise

"The United States today is the leading exponent of a 'free society.' We believe that our political and economic institutions have served to release the latent capacities of every individual. We think that they have provided incentives and opportunities for men to realize their highest potentialities. We are convinced that they have been an indispensable condition of the development of our material wealth and living standards." (1949)

"Experience has shown that over a wide sphere of economic activity, private enterprise can operate with much greater flexibility, efficiency, and responsiveness to the needs of the people than a governmental agency ever can. The 'invisible hand' referred to by Adam Smith two centuries ago is slowly being rediscovered as a source of public welfare. * * * The decentralized planning and decision-making that is characteristic of a competitive private enterprise economy will produce much better decisions than could any government central planning bureau." (1950)

Mr. Jacoby (in the same speech) restricted the Government's role as follows: "Through wise taxing, expenditure, and debt management policy, government can contribute to the maintenance of high employment and economic progress. Government must plan the environment, leaving tens of thousands of individual business managers to plan the operations conducted within that environment."

Inflation

"OPA combats the symptom rather than the cause of price inflation. Direct price control is being used as an excuse for evading the responsibility of following non-inflationary monetary, fiscal, and wage policies. A government which permits politically powerful labor and agricultural groups to raise prices, while holding down the closely-related prices of other economic groups, is not being honest. * * *

"The present situation calls for a strongly deflationary monetary and fiscal policy. The two basic methods of accomplishing these results are to create a substantial surplus in the Federal budget, and to tighten the money markets. * * *

"For further price inflation would guarantee a severe instead of a moderate recession. More serious distortions in the price structure would take more time to eradicate. In no facetious vein I say that moderate recession from present boom conditions would be the best thing that could happen to the United States in 1948." (1947)

Six years later, Mr. Jacoby observed that "During the past year or so there has been an abrupt change in our national monetary and fiscal policies. The long-continued policy of making credit cheap has been replaced by a policy of neutrality. * * *

"Now I believe that the monetary brake should have been applied a long time ago as the most effective curb on price inflation, and that it was necessary for the present Administration to apply it when it did. * * * [However] it may be necessary to relax the monetary brake before long, in order to check the decline in investment spending and in consumer spending consequent upon the higher costs and more stringent terms of consumer credit." (1953)

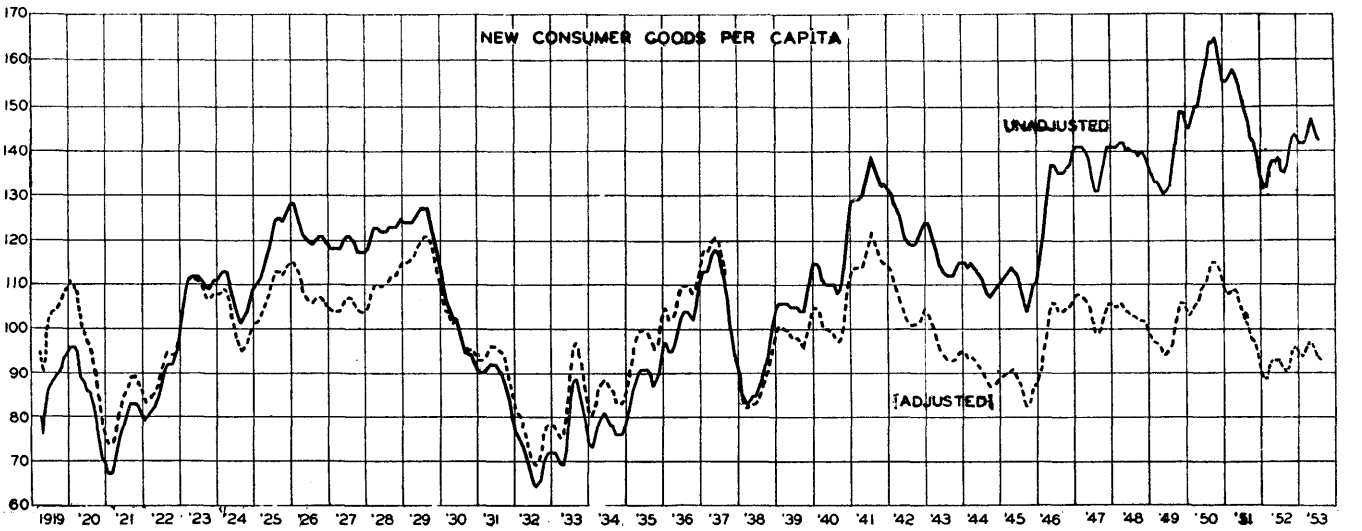
Mr. Jacoby sees danger in a runaway deflation. "Sharp price inflation is a bad thing; but once it has occurred its evils are not cancelled by a rapid fall in prices. Severe price deflation produces unemployment and dislocations which are equally bad for the economy." (1951)

Foreign Aid

Mr. Jacoby believes "The best available evidence in-

[1]Arthur F. Burns, Chairman of the Council, was recently Director of the National Bureau and served on its staff for many years. Mr. Jacoby was a research economist with the Bureau for 5 years and, together with Raymond J. Saulnier, published several books for the Bureau on the subject of business financing and banking.

[2]The speeches include the following and are indicated in the text by showing the appropriate year in parenthesis after the quotation: "Forces Shaping Business Outlook," at the American Finance Conference, Chicago, Illinois, November 19, 1947; "Impact of American Foreign Policy on Business," before the California Bankers Association, Pasadena, California, May 22, 1949; "Economic Tendencies Affecting Trust Investment Policies," before the Western Regional Trust Conference of the American Bankers Association, Los Angeles, California, October 19, 1950; "Some Perspectives of 1952—and Beyond," before the Southern California Mortgage Bankers Association, Los Angeles, California, December 5, 1951; and "Chief Factors in Business Outlook," before the National Association of Purchasing Agents' Thirty-Eighth Annual International Convention, Los Angeles, California, May 26, 1953.



dicates that the Marshall Plan is achieving its objectives. Western Europe is getting on its feet economically. The rising tide of communism has been checked and turned back." (1949) Yet he was aware of the prerequisites necessary for the most effective use of American aid.

"The two factors that would do most to get the economies of Europe off dead center and on the road to recovery are, first, internal stabilization of their finances, and, second, lifting of the 'Iron Curtain' that now cuts across the normal flow of commerce between agrarian Eastern Europe and industrial Western Europe. Neither of these conditions can be satisfied by American exports. If France, Italy and other countries would balance their budgets and stabilize their currencies so that their own people had confidence in them, the need for American dollars would be greatly reduced." (1947)

He is aware of the importance of foreign trade and the need for reducing trade barriers. "Our long run national interest would be promoted by further cuts in trade barriers." (1949)

He does not subscribe, however, to the belief that such trade is indispensable if a depression is to be avoided in the United States. "The notion—nurtured by some British and Continental economists—that large exports are needed to protect the American economy from depression like an international WPA is pure fallacy." (1947)

Price of Gold

"A third course would be to change the dollar price of gold—now $35 per ounce. But no change the United States could make would solve the balance of payments problems of all countries. * * * Clearly this country should not raise the price of gold for this would merely subsidize gold producers, lead to the accumulation of more sterile metal here, and aggravate the difficulties of the principal trading nations. Neither should the United States lower the price of gold, for such action would fail to provide the right amount of readjustment between the dollar and the currency unit of each foreign country that its particular circumstances require." (1949)

Taxes and Investment

"What are the prospects for the continuance of growth of the economy and of individual business firms? The prospects appear to me to be reasonably good, provided that government policies, particularly tax policies, leave adequate incentives and opportunities for business investment, and that sufficient savings will be available to finance such investments." (1950)

"A revision of our Federal tax system should be begun immediately, with the focus of attention on the elimination of features which dampen risk-taking and reduce business investment. I have in mind such features as accelerated depreciation, reduction of the double taxation of dividend income, and a host of other measures." (1953)

Conclusions

We have suggested in prior articles that Mr. Burns apparently shares our belief that the science of economics has not yet advanced to the stage where it can provide grand solutions for all economic problems. Mr. Jacoby too seems aware of the difficulties involved.

"In the kind of world in which we live today, pure economic analysis has limited forecasting value. He who wishes to forecast the future should also be an historian, a political scientist, a military strategist, and a social psychologist. It might even help if he were a psychiatrist! Any economist who is not all these things will approach the task humbly and tentatively, knowing that he may be wrong because his basic premises prove incorrect although his economic logic is impeccable." (1951)

We believe that men such as Mr. Jacoby and Mr. Burns will not advise the President to resort to untested economic panaceas. Therefore, if Mr. Eisenhower follows their advice, he presumably will remain on firmer ground, from an economic standpoint, than did his predecessor under the guidance of Mr. Keyserling.

SUPPLY

Industrial Production

Steel-ingot production, scheduled at 89 percent of capacity for the week ended September 12, 1953, was 1 percent less than that in the preceding week and was 5 percent less than production in the corresponding week last year.

	1929	*1932*	*1937*	*1938*	*1952*	*1953*
Percent of Capacity†	86	16*	72*	40*	101	89*p
Weekly Cap. (Million Tons)	1.38	1.52	1.51	1.54	2.08	2.25
Production (Million Tons)	1.19	.24	1.09	.62	2.10	2.00

Automobile and truck production in the United States and Canada during the week ended September 5, 1953, was estimated at 137,998 vehicles, compared with a revised total of 152,866 vehicles during the previous week.

	1929	1932	1937	1938	1952	1953
Vehicles (000 omitted)†	109*	23	64	22	111*	138p

Electric-power production in the week ended September 5, 1953, increased to 8,694,301,000 kilowatt-hours from 8,539,557,000 kilowatt-hours in the previous week.

	1929	1932	1937	1938	1952	1953
Billion Kilowatt-Hours†	1.68*	1.47	2.38	2.22	7.32*	8.69

Lumber production in the week ended August 29, 1953, increased. *The New York Times* seasonally adjusted index was slightly above that for the preceding week and was 6 points above that for the corresponding week last year.

	1929	1932	1937	1938	1952	1953
The New York Times Index†	130	35	83	100	106	112

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

New Consumer Goods Per Capita

The index of new consumer goods per capita (a 3-month moving average plotted at the last month) unadjusted for long-term trend decreased slightly during July to a level 3 percent below the 1953 high reached during April. The July index was 5 percent above that of a year ago but was 13 percent below the post-World War II peak reached in October 1950. The recent downtrend, which has continued for 3 months, is the third interruption since the upward trend of the index of new consumer goods per capita began in February 1952.

The index adjusted for long-term trend, which decreased 2 percent during June, decreased 1 percent during July. The July figure was 4 percent below the 1953 high reached in April and was 2 percent below that of the corresponding month a year ago. The July index was nearly 7 percent below the long-term trend.

Production of consumer goods was unchanged during July at a level nearly 4 percent below that of March 1953, when the high for the year was reached. July production was 14 percent greater than the production during the corresponding month a year ago but was 12 percent below that of August 1950, when the post-World War II peak was reached. Automobile production, residential construction, and shoe production increased 7, 10, and 11 percent respectively; but these gains were counterbalanced by decreases of 3 and 10 percent in furniture and textile production, respectively. Production of manufactured food and tobacco was unchanged.

Conclusions

In view of the probable curtailment of automobile production during the remainder of 1953 and because there are few signs of a major recovery in production of other consumer goods, we should not be surprised if the high reached in April represented a peak for new consumer goods produced per capita for the next several months at least.

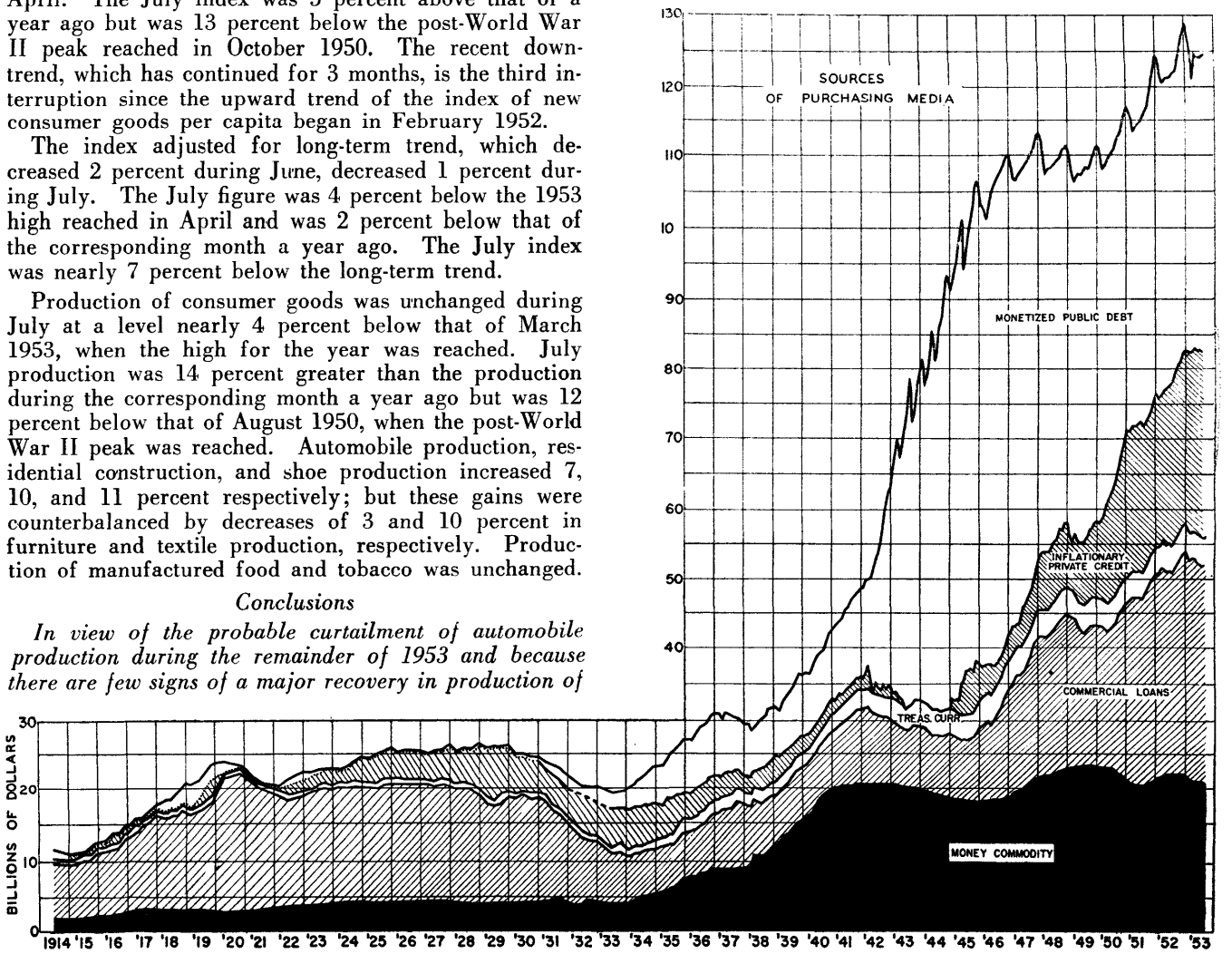
DEMAND

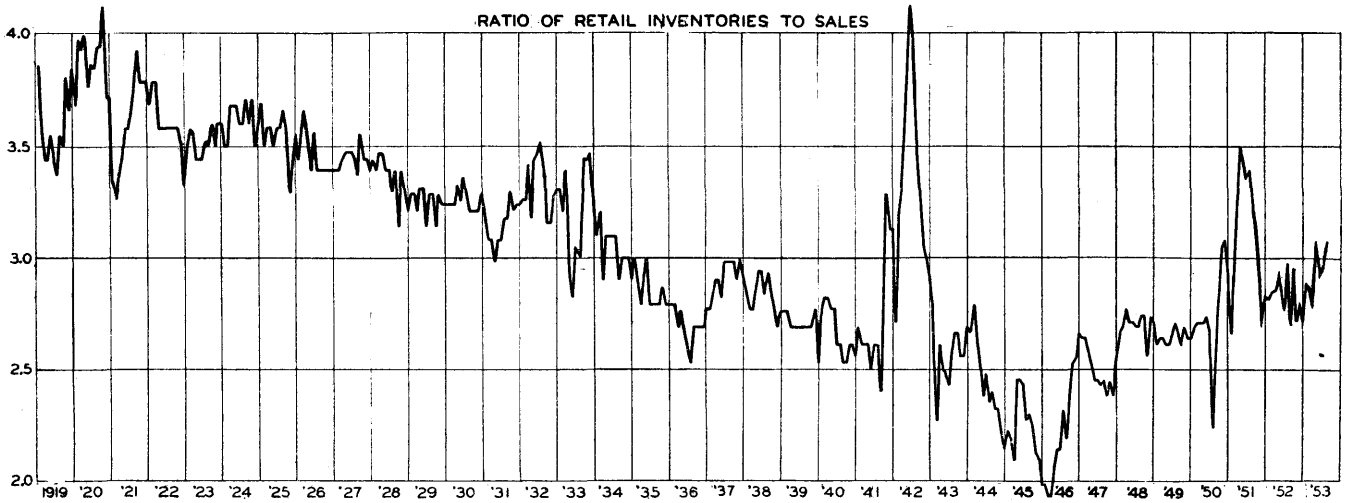
Purchasing Media

Total purchasing media increased slightly during August to $125,535,000,000, about $3,200,000,000 less than the alltime record of $128,700,000,000 reached in December but $3,400,000,000 more than the figure for August 1952. Since May 1953 the purchasing-media total has fluctuated little at about $124,500,000,000.

Purchasing media derived from the first source, the money commodity (monetary gold), decreased $80,000,000 during the first 4 weeks of August. The August decrease was substantially less than the July decrease of $230,000,000. However, data for the week ended September 2 reveal a further decrease of $50,000,000 in the Nation's gold stock. These changes suggest that the outflow of gold that started in late 1952 and was temporarily interrupted in the early spring of 1953 has been resumed.

Commercial, industrial, and agricultural loans, the second source of purchasing media, increased $340,000,000 during August, somewhat less than is seasonally ex-





pected. According to a *Journal of Commerce* report, "semi-official and some private 'projections'" suggest an increase of $3,500,000,000 in commercial, industrial, and agricultural loans during the second half of 1953. Such a gain, 11 percent, would be somewhat more than that seasonally expected. The corresponding increases during 1952, 1951, and 1950 were 10, 9, and 25 percent respectively. We doubt that commericial, industrial, and agricultural loans will increase more than seasonally during the 6-month period ended December 31, 1953.

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 are potentially inflationary, decreased $220,000,000 during August to $68,600,000,000, nearly $2,000,000,000 more than the amount at the end of August 1952 but about $2,000,000,000 less than the amount at the end of December 1952, when a post-Korean peak of inflationary purchasing media was reached. Since April 1953 the amount of inflationary purchasing media has not changed greatly.

The attrition rate in the exchange of the 2-percent bonds maturing on September 15 was relatively low.[3] Consequently, Treasury operations during September probably will be nearly balanced. However, substantial cash deficits are expected in October and November.

No major change in the amount of available purchasing media is expected during September. Thereafter, an increase at least to the December 1952 level is virtually assured as a result of the expected release by the Treasury of purchasing media newly created and accumulated in the general fund and as a result of the seasonal expansion of commercial, industrial, and agricultural loans.

Department-Store Sales

Department-store sales for the week ended September 5, 1953, were unchanged from sales in the preceding week and were unchanged from sales in the corresponding week last year.

[3]Only 3.5 percent of the holders of the $7,986,000,000 of bonds asked for cash. Subscriptions to the new 1-year, 2⅝-percent certificates of indebtedness amounted to $4,717,000,000; subscriptions to the new 3½-year, 2⅞-percent notes, amounted to $2,988,000,000.

PRICES

Commodities at Wholesale

(August 1939=100)	*1952* *Sept. 10*	*1953* *Sept. 3*	*1953* *Sept. 10*
Spot-Market Prices (22 basic raw materials)	290	276	278
Commodity Futures Prices (Dow-Jones Daily Index)	366	330	330

BUSINESS

Ratio of Retail Inventories to Sales

Preliminary estimates indicate that the ratio of retail inventories to sales, which increased 4 percent during July, increased nearly 2 percent more during August to the 1953 high reached in April. The August figure was 14 percent above both that of August 1952 and that of December 1952, when the recent upward trend began.

The seasonally adjusted index of department-store inventories, which increased slightly during July, increased nearly 2 percent during August. The seasonally adjusted index of sales, which decreased 3 percent during July, was unchanged during August. Consequently, the August ratio increased nearly 2 percent. (The ratio is derived by dividing the inventory index by the sales index.) August inventories were 11 percent greater than those of August 1952 and 27 percent larger than inventories at the start of the Korean War.

The dollar value of new orders placed by department stores during July (later data are not available) was 18 percent less than that during June and was 7 percent less than that during July a year ago.

The dollar value of outstanding orders increased 15 percent during July, compared with a seasonally expected increase of 30 percent.

The dollar value of goods received by department stores decreased 2 percent during July, substantially less than the 18-percent decrease seasonally expected.

The ratio of department-store inventories to sales has risen to a level well above that prevailing in 1948 prior to the inventory adjustment that occurred shortly thereafter. We believe that retailers will attempt to alleviate the situation by reducing prices or substantially curtailing new orders in the near future.