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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

The Council of Economic Advisers

The President has recently nominated two new members of the Council of Economic Advisers. The nominees are Dr. Joseph Davis and Dr. Raymond J. Saulnier; they succeed, respectively, Dr. Walter J. Stewart and Dr. Neil H. Jacoby. Although the Council will continue under the chairmanship of Dr. Arthur Burns, the substitution of two new members necessarily reconstitutes the 3-man Council. Accordingly, a question arises whether the newly constituted team will be guided by the same basic philosophies as its predecessor, as these philosophies have been revealed in the reports and recommendations of the Council through its chairman.

The Council chairman, Arthur F. Burns, appears to have earned and to command a position of confidence with the President. Presumably, therefore, the new nominees were acceptable to Dr. Burns. This is not to say that the views of the new members will coincide completely with those of Dr. Burns. Such is neither to be expected nor desired. However, comparing each of the new members with the one he replaces provides some clues as to the continuity to be expected.

Dr. Davis succeeds Dr. Walter W. Stewart, whose appointment was discussed in the bulletin dated December 13, 1953. Both men have experienced the same general historical developments at the same ages in life, factors that probably have influenced their views, both having been born in 1885.

Dr. Davis' specialty has been in the field of agricultural economics and population; that of Dr. Stewart has been in the realm of money and credit. Dr. Davis is a native of Pennsylvania and received his Doctor of Philosophy degree from Harvard in 1913. He has taught at Bowdoin College and at Harvard; he was Director of the Food Research Institute of Stanford University from 1921 to 1951, and Professor of Economic Research at that university from 1938-1951. In addition to his strictly academic duties he has served in various non-academic capacities including that of chief economist to the Federal Farm Board and as a technical assistant to American members of the Dawes Commission.

Dr. Davis' books include "The Farm Export Debenture Plan" (1929), "Three Years of the Agricultural Adjustment Plan" (1937) in collaboration with E. G. Nourse and J. D. Black, "International Commodity Agreements: Hope, Illusion or Menace" (1947) and "The Population Upsurge in the United States" (1949).

Dr. Stewart's age seems to justify the reason that he gave for resigning from the Council ("entirely personal"). With agricultural problems assuming increased importance the President apparently decided to use the vacancy created by Dr. Stewart's resignation as an opportunity to strengthen the agricultural background represented on the Council.

In naming Dr. Saulnier to succeed Dr. Jacoby, whose appointment was discussed in the bulletin dated September 14, 1953, the President again selected a man of an age comparable to that of the retiring member. Thus, Dr. Saulnier, whose age is 46, compared with 45 for Dr. Jacoby, has observed developments during the same span of years as had his predecessor. In this instance, however, the similarity of background of the two men extends further. Both have specialized in banking and finance. Moreover, both were earlier associated as research economists for the National Bureau of Economic Research, where they collaborated in the publication of books on the subject of business finance and banking, one of which was "Term Lending to Business" (1942).

Dr. Saulnier, a native of Massachusetts, received his Doctor of Philosophy from Columbia University, where he had taught since 1934. Since 1946 he had been director of the financial research program of the National Bureau of Economic Research, and since 1950 he had served as an adviser to the Board of Governors of the Federal Reserve System.

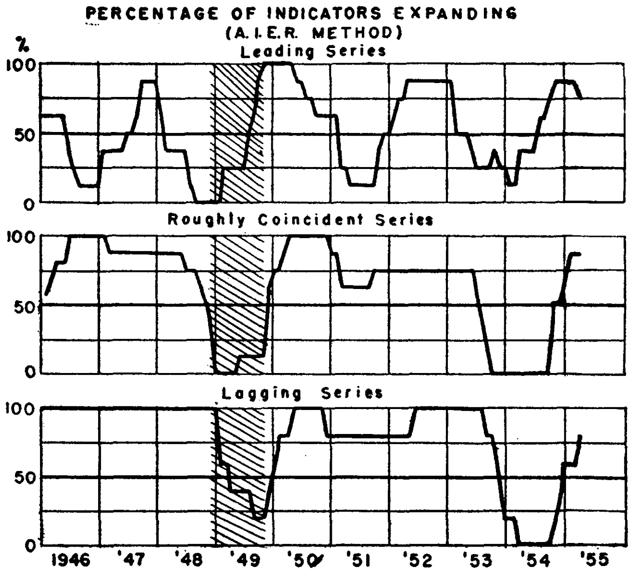
Dr. Jacoby resigned his place on the Council to return to his position as Dean of the School of Business Administration at the University of California. Shortly after returning to California, he expressed clearly his views concerning the inflationary dangers of attempting to achieve the "full employment" objectives of the Employment Act of 1946, which describes the duties and responsibilities of the Council. At the heart of Dr. Jacoby's expressed view is the belief that attainment of full employment via "controlled" but progressive inflation is a snare and a delusion. Although Dr. Jacoby ruled out inflation as a means to full employment, he confidently expressed the belief that "we *can* prevent serious unemployment and maintain a reasonably stable price level in a full economy" without violence to other responsibilities and duties of the Government, one of which is maintenance of a sound monetary unit.

Will Dr. Saulnier share his predecessor's convictions concerning the dangers of inflation to the economy? In attempting to answer this question, the best evidence seems to come from Dr. Saulnier's published work. In his book "Contemporary Monetary Theory" (1938) Dr. Saulnier examined the theories of four recent writers on monetary and business-cycle problems including those of John Maynard Keynes, on whose work is based much of the widely held belief that controlled inflation provides a means to controlling the business cycle.

"As to Keynes's proposition that employment can be increased by raising the prices of wage-goods relatively to money-wages, this depends on there being in actuality the kind of relation between money, interest, the marginal efficiency of capital, and the level of employment which Keynes posits. In the various sections devoted to these special concepts, however, we have found reasons to doubt that increases in the money stock will alone cause an increase in output. We have also seen that the concepts utilized by Keynes are not adequately developed (Chapters III and IV). Keynes's proposition cannot, therefore, be taken as satisfactorily demonstrated."

What positions Dr. Saulnier and Dr. Davis will take as members of the Council concerning inflation and other aspects of the economic problems before the Nations remain to be seen. As of today, we judge that the attitudes and philosophies of the Council will continue basically unchanged.

What the Indicators Say



The percentage of leading indicators expanding during March, as measured by a method developed by the Institute, decreased to 75, that of the roughly coincident indicators was unchanged at 87½, and that of the lagging indicators increased to 80.*

Latest Data

1. The average of the Dow-Jones daily index of the common-stock prices of 30 industrials increased 3½ percent during April.
2. New orders for durable goods increased 10 percent during March.
3. The average of the Bureau of Labor Statistics daily index of wholesale prices of 22 basic commodities increased 1 percent during April.
4. Consumer installment debt increased 3 percent during March.
5. Manufacturers' inventories at the end of March were unchanged from those at the end of February.

*The Institute method was outlined in our bulletin of March 8, 1954.

The *Iron Age* composite price of No. 1 heavy-melting steel scrap for the week ended April 26 was $35.67, compared with $36.00 for the preceding week. The average of these prices for April was $36.50, compared with $37.19 for March.

Conclusions

The patterns of the three curves of expanding indicators suggest that further gains in business activity are probable.

SUPPLY

Industrial Production

Steel-ingot production of 2,328,000 tons during the week ended May 7, as indicated by operations scheduled at 96.5 percent of capacity, compares with 2,307,000 tons during the preceding week and 1,640,000 tons during the corresponding week last year.

The New York Times seasonally adjusted index of lumber production was 115.4 for the week ended April 23, compared with 112.4 a week earlier and 114.5 for the corresponding week last year.

Electric-power production of 9,699,000,000 kilowatt-hours during the week ended April 30 compares with 9,697,000,000 kilowatt-hours for the previous week and 8,390,000,000 kilowatt-hours for the corresponding week last year.

Automobile and truck production in the United States and Canada, estimated at 232,700 vehicles for the week ended April 30, compares with a total of 225,100 for the previous week and 159,200 for the corresponding week last year.

These data compare with those for corresponding weeks of earlier years as follows:

	1929	*1932*	*1948*	*1949*	*1954*	*1955*
Steel						
Operating rate—percent cap.	101	24	91	97	69	96
Ingot prodn.—million tons	1.39	.36	1.64	1.78	1.64	2.33
Lumber						
New York Times Index	135	42	85	92	114	115
Electric Power						
Kilowatt-hours—billions	1.70	1.46	5.04	5.30	8.39	9.70
Automobiles						
Vehicles—thousands	143	37	103	136	159	233*p*

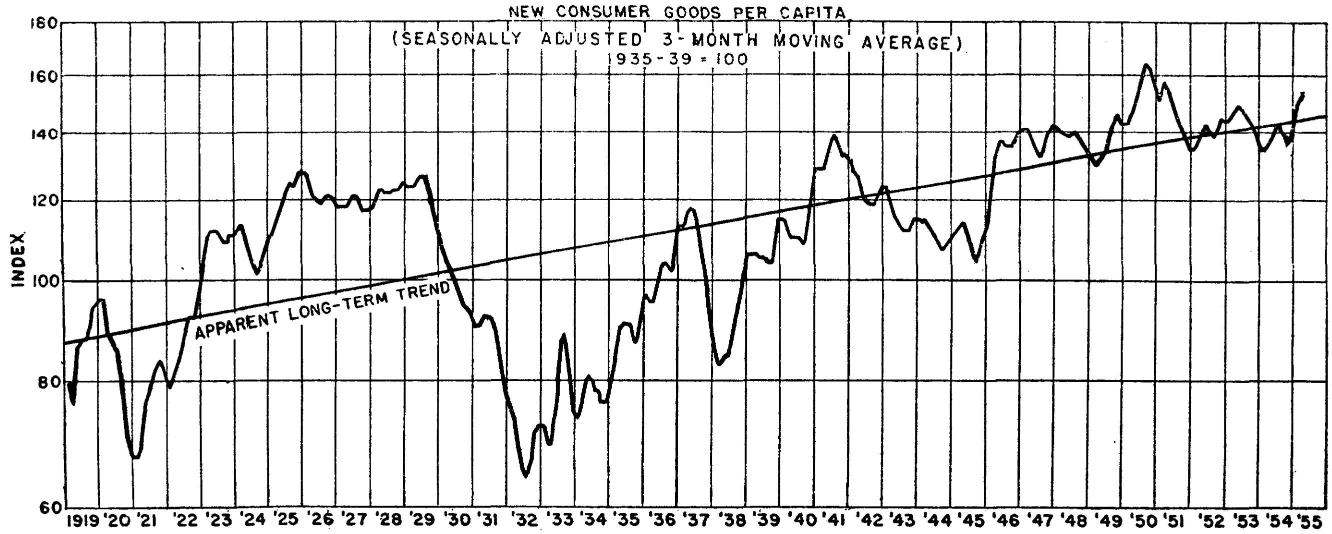
***p* Preliminary**

New Consumer Goods Per Capita

Our index of consumer goods produced per capita increased a little more than 1 percent during March to an amount 12 percent larger than that of March 1954.† The index is now at its highest point since the spring of 1951, when consumers' goods were produced in quantities to replenish shortages caused by scare buying in January 1951.

Production of consumers' goods during March, the third of the 3 months for which the March index reflects production, increased 3 percent, after having gained ½ percent (revised) during February. Furniture production continues to gain relatively little in comparison with that during corresponding periods of 1954. Although the production of food items remains stable, production of nondurable items has increased. Producers are manufacturing 18 percent more consumers' goods than they were last August when the per capita production of consumers' goods approached its lowest rate in 3 years.

†The index reflects production of seven categories of consumer items accounting for more than two-thirds of all consumers' purchases. The index is a 3-month moving average, plotted at the third month.



Each component, except food, in which there was no change, contributed to the increase in the index during the past year. Percentage changes in the components of the index since March 1954 and since March 1953 have been as follows:

	March 1954	*March 1953*
Automobiles	+37	+28
Residential Construction	+25	+40
Furniture	+ 6	− 8
Food	None	None
Textiles and apparel	+ 8	− 3
Shoes	+15	+ 7
Tobacco	+ 4	− 8

Passenger-car production in April totaled 775,000, compared with 794,000 in March and 515,000 in April 1954. As of April 15 the number of new passenger cars in the stockrooms of the nation's 45,000 dealers was 16,400 more than it was a year earlier. *The Wall Street Journal* reports that in the period from March 1 to April 15 sales of new cars to consumers increased 40 percent with an average inventory for that period slightly less than that in 1954.

The number of new private dwelling units started in April is expected to exceed the 116,000 in March and the 106,000 in April 1954.

The expected curtailments of automobile production in the third quarter will tend to decrease the index of new consumer goods. However, the recent record level of personal income appears to be reflected in orders for apparel and other consumer items in amounts sufficient to offset much of the influence of reduced automobile production in the third quarter. Accordingly, we expect the index to level off during the next 4 or 5 months.

Residential Construction

The March index of the dollar total of residential construction, seasonally adjusted, is estimated at 450, compared with 493 (revised) for February and 340 for March 1954. Previous to the present upswing in residential construction, which began early in 1954, the record for the index was 369 reached in July 1950.

The *Engineering News-Record* index of construction costs increased fractionally during March. It is still less than one-half of 1 percent higher than it was January 1, but is 5½ percent above that of March 1954.

The March index of physical volume, which is derived by dividing the index of contract awards by the index of construction costs, is 8 percent smaller than it was in February, but is 27 percent larger than it was in March 1954.

During the first quarter of 1955, 295,000 new nonfarm dwellings were started. This number compares with 236,800 in the first quarter of 1954 and 278,900 in the first quarter of 1950, the previous first-quarter record. If houses are started throughout the year at the seasonally adjusted rate of the first quarter, the total number of houses started in 1955 will exceed 1,400,000.

The increasing importance of Government-underwritten credit in residential construction is indicated in the accompanying table.

Percent of New Houses Financed by F. H. A. and V. A. Underwritten Credit

Period	*Total F. H. A. and V. A.*	*F. H. A.*	*V. A.*
1953	38	24	14
1954	49	23	26
1955, 1st qtr.	50	20	30

On April 1 there were 71,900 requests for V. A. appraisals compared with 34,400 a year ago. There were 35,600 applications for F. H. A. commitments on April 1, compared with 28,100 a year ago. This increase necessarily reflects changes in the backlog of applications and therefore does not accurately measure changes in the rate at which applications are being received. However, the data alone suggest that the present rate of residential building will continue throughout this year.

The trend toward home ownership continues. More than 56 percent of America's families are home owners as compared with 41 percent before World War II. It is estimated that there were 48 percent fewer rental-type dwellings built in 1954 than in 1950. Moreover, in 1954 there were 51 percent more one-family houses built for sale than in 1950.

The question as to whether an overbuilt condition is developing for homes is receiving increased attention. About 22 percent of all single-family homes have been built since World War II, and houses are being built at about double the rate of new household formations. However, many older houses are substandard, and many more are obsolete by modern standards. Increased leisure, the trend to the suburbs, and larger families, are special factors stimulating the demand for houses. Although the number of homes available for rent is greater than it was a year ago, it has not yet reached the 5-percent ratio, which realtors generally regard as a warning signal.

We believe that residential construction will remain at present seasonally adjusted levels for several months at least. However, because of the marked upward trend of residential construction last year, comparisons of the volume of construction this year with corresponding periods of last year are expected to become progressively less favorable.

DEMAND

Department-Store Sales

Sales of the 325 reporting department stores compare with those of corresponding periods a year ago as follows:

Period	*Percent Change*
Week ended April 30	+7
Four weeks ended April 30	+3
Year to date	+6

PRICES

Commodities at Wholesale

	1954	1955	
Index	*May 4*	*Apr. 27*	*May 4*
Spot-market, 22 commodities	283	274	274
Commodity futures	369	324	324

Note: The indexes are respectively those of the United States Bureau of Labor Statistics and Dow Jones. Both indexes are converted so that their August 1939 daily averages equal 100.

FINANCE

Gold Production and Commodity Prices

World production of gold excluding Russian output is estimated to have increased about 8 percent during 1954. Largely responsible for this increase was an 11-percent gain in the amount produced by the Union of South Africa.‡ Other countries reporting increased production in 1954 are the Gold Coast, India, Canada, Venezuela, Japan, and the Philippines. Production of gold in the United States decreased 5 percent last year. Production in all other countries either decreased or has not yet been reported.

‡In 1951 the Union of South Africa produced approximately one-third of all the gold produced in the world.

According to estimates of the United States Bureau of Mines, Russian gold production remained unchanged during 1947, 1948, and 1949, but increased substantially during 1950 and 1951. We have estimated that it remained unchanged during 1952 and 1953, but increased during 1954 by approximately the same percentage as that of the increase in gold production in the rest of the world.

The United States Bureau of Labor Statistics index of wholesale commodity prices increased slightly during 1954, thereby reversing, at least temporarily, the downward trend of that series that was evident during 1952 and 1953.§ Commodity prices in the Union of South Africa increased about 1 percent during 1954; those in Canada, the third major gold-producing country, decreased about 1 percent.

The price of gold in most free markets abroad has continued at, or close to, the statutory definition of the dollar, one thirty-fifth ounce of gold.

The increased world production of gold last year has contributed materially to the improved gold position of many countries. Concerning the gold (and dollar) gains the Federal Reserve Bank of New York writes: "The gold and dollar position of most foreign countries was one of notable strength in 1954. While aggregate foreign holdings increased less than in the previous year, the rise was still substantial, although largely concentrated in Western Europe, the sterling area, and Canada."‖

Although the curve of world gold production in 1955 is not expected to reach the long-term trend line, it is expected to increase at least in parallel with that trend, thereby extending for another year the upward trend which, since 1945, has roughly paralleled at a lower level the long-term trend line. Evidently, commodity prices are still well above a level that would encourage gold production along the indicated long-term trend and thus give some assurance of relative stability for future price trends.

§A reliable index of world commodity prices is not available. Prices plotted on the accompanying chart represent wholesale commodity prices in the United Kingdom prior to 1914 and those in the United States thereafter.

‖"International Gold and Dollar Movements in 1954," *Monthly Review of Credit and Business Conditions*, February 1955.