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GREAT BARRINGTON MASSACHUSETTS

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RESEARCH REPORTS

COMING EFFECTS OF CURRENT EVENTS

The State of the Union

As we have pointed out before, the Presidents' state of the Union messages have come to have little economic interest, primarily because of the generalities in which they deal. This development results largely from the increased use of other messages and reports, notably the budget message and the economic report. President Eisenhower's seventh message on the state of the Union is no exception to this characterization although the message does reveal the general tenor if not the effectiveness to be expected of his leadership during his last 2 years in office. Moreover, by the attention given to economic considerations and problems among the things discussed in the message, we are reminded of their importance in present-day Government activities.

The focal point of these problems and considerations is the Federal budget, which is a "comprehensive plan of action proposed by the President for meeting our national objectives," and which "affects every phase of life and activity of the Nation."* Whatever political considerations may have been involved in the President's promise of submitting a balanced budget, and whatever political considerations may lead to an unbalanced budget for fiscal 1960, even this recognition of the importance of limiting expenditures to current receipts is heartening.

In recognizing that an unbalanced budget is an invitation to more inflation, the President wisely observed that "We must avoid any contribution to inflationary processes which could disrupt sound growth in our economy." In this and other statements the President seemed more cognizant of the Nation's inflationary problem than he had been in other of his more recent messages. However, positive as that may be, he seized upon symptoms of inflation as causes and proceeded from there to recommend unrealistic and ineffectual attacks upon the problem.

By implication, the President erroneously treated high prices as a condition of inflation and referred to the wage-price spiral as a cause of inflation. Our readers will know that we recognize inflation as a money-credit situation leading to high prices and not as a price condition.† The wage-price spiral is caused by a level of demand that can be maintained despite progressively higher wages and prices only because of an increasing excess of purchasing media.

When, therefore, the President says that "We must encourage the self-discipline, the restraint necessary to curb the wage-price spiral," he is not directing action toward a *cause* but toward an *effect* of inflation. Such a prescription is as ineffective in removing basic causes of the evil as is the application of ice to a patient experiencing a fever caused by a virus. Moreover, because individual realization of available monetary gains is the essence of our free enterprise system, an appeal to suspend or limit individual gains possible from the addition of inflationary purchasing media without artificial restraints upon free enterprise is wholly unrealistic.

Responsibility for further inflation rests squarely with the Congress. The Federal Reserve Board, through appropriate monetary policy, and the Treasury, by means of suitable debt-management policy, could do much to alleviate the consequences of past and current inflationary fiscal policies, but only if the attitude of Congress toward the necessary measures were to become at least permissive. A good approach to the problem of inflation and a first step, at least, toward its solution would be for Congress to balance appropriations with revenues.

Another feature of the President's message having special economic interest was his recognition of the need for revisions in the Nation's uneconomic farm program. In support of his position on the farm program, he pointed out that:

> Outlays of the Department of Agriculture for the current fiscal year for the support of farm prices on a very few farm products will exceed $5,000,000,000. This is a sum equal to approximately two-fifths of the net income of all farm operations in the United States.
>
> By the end of this fiscal year it is estimated that there will be in Government hands surplus farm products worth about $9,000,000,000. And by July 1, 1959, Government expenditures for storage, interest, and handling of its agricultural inventory will reach a rate of $1,000,000,000 a year.

As the President observed, such expenditures might be made temporarily if they lead to a sound solution of the farm problem. However, when this situation fol-

**The Federal Budget in Brief,* Fiscal Year 1957, p. 2.

†The money-credit condition we define as inflation is an excess of purchasing media, as reflected in our index of inflation. For an explanation of what comprises the excess, see our book *Cause and Control of the Business Cycle.*

To Annual Sustaining Members:

Your copy of the 1959 edition of *What Will Social Security Mean to You?* is being mailed to you. If you do not receive your copy promptly, please let us know and a replacement will be sent.

lows a quarter of a century of costly farm-price support and tremendous inventory accumulation there is no valid economic reason for continuing it, particularly in view of the magnitude of the defense and allied expenditures that world conditions seem to demand.

In spite of the loss of one-tenth of our gold reserves last year, a loss accentuated by foreign-aid credit grants, on the one hand, and domestic inflation weakening our competitive position abroad, on the other, and in spite of the tremendous burden of our defense activities, the President seeks to continue subsidizing a large part of the world. This position was made clear through the importance he assigned to continued foreign aid.‡

Although the President's return to a position of emphasis upon a balanced budget is "all to the good" in the fight against more inflation, his continued failure to discuss the problem in terms of its basic causes is disquieting. The conclusion to our discussion of his message of 2 years ago is therefore pertinent. At that time we wrote, "inflation is a threat and will continue to be a threat only so long as those responsible for stopping it can persuade the public that businessmen or labor leaders are responsible. Once there is more widespread understanding of the source of inflation, the threat need continue no longer than will be required to elect more responsible public officials. The fact that such a change today seems far distant accounts for the seriousness of the danger of inflation."

What the Indicators Say

Note: The indicators reported on below are seasonally adjusted.

Among the leading indicators, the liabilities of business failures (inverted) and average hours worked weekly increased in December.

Among the roughly coincident indicators, unemployment (inverted) decreased in December.

The leading indicators, somewhat strengthened by recent data, still forecast continuing recovery.

* * * * *

The *Iron Age* composite price of No. 1 heavy melting steel scrap, not one of the indicators, was $40.50 per ton on January 13, compared with $40.17 on January 6.

‡The economic aspects of foreign aid were the subject of a series of articles in *Research Reports* in early 1948. Our latest article on this subject appeared in *Research Reports* for December 1, 1958.

PRICES

Commodities at Wholesale

	1958	1959	
Index	*Jan. 14*	*Jan. 7*	*Jan. 14*
Spot-market, 22 commodities	260	262	262
Commodity futures	327	308	306

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.

DEMAND

Department-Store Sales

Sales of department stores reporting to the Federal Reserve Board compare with those of corrsponding periods a year earlier as follows:

Period	*Percent Change*
Week ended January 10	+4
Four weeks ended January 10	+8

SUPPLY

New Consumer Goods Per Capita

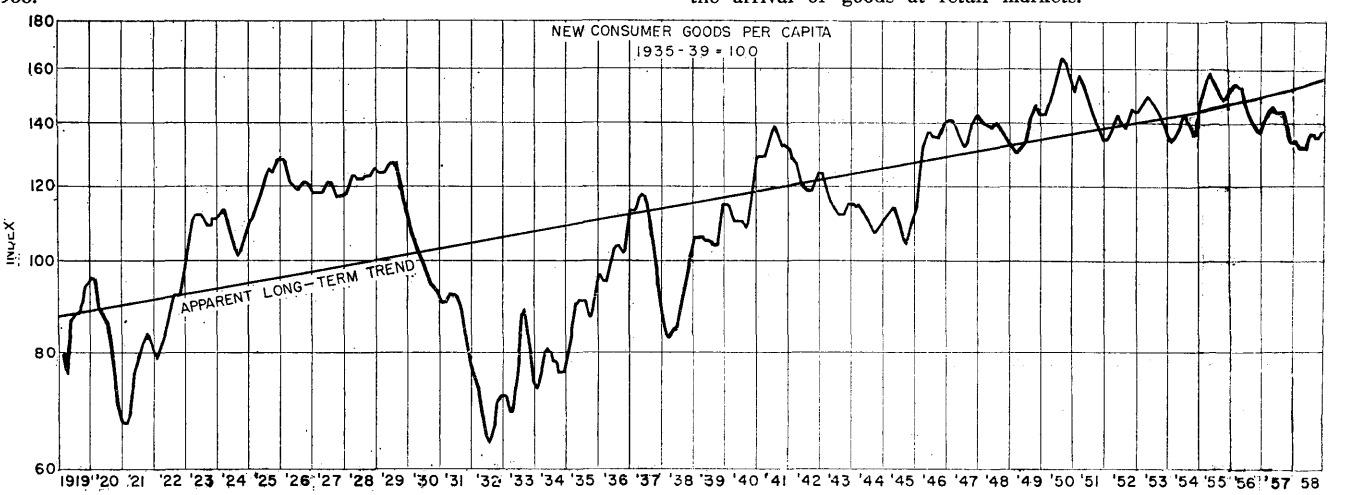
Our index of new consumer goods per capita for November was 1 percent more than that for October, as revised, and was 2 percent more than that for November 1957.§ The November increase was partially attributable to the resumption of full-time automobile production after the early part of the month.

Production of consumer goods in November, unadjusted for population increases, was 2 percent more than that for October, and was 4 percent more than that for November 1957. Textile and furniture production increased by 2 percent and 1 percent respectively, and automobile production increased sharply over that for October, although not to the level of the corresponding month last year. Residential construction was more than that in November 1957, but less than that in October.

Production of automobiles increased further in December, and indications are that production in most other major categories of consumer-durable and nondurable goods increased similarly.

However, any marked and sustained upturn in consumer-goods production will depend on a revival in the demand for consumer-durable goods. Although an early strong upsurge in the demand for such goods is

§The index, which reflects the production of goods accounting for about two-thirds of all consumer purchases, is a 3-month moving average plotted at the third month in recognition of the lag in the arrival of goods at retail markets.



not expected, the outlook seems to be for moderate gains. As indicated in our article on residential construction, home-building activity may not increase more than seasonally this spring. However, as we have noted, if such an increase is realized, it would be made despite the adverse influence of tighter money-credit conditions. For other consumer-durable goods, notably furniture and automobiles, prospects for increased demand seem favorable.

Production of new consumer goods per capita is expected to increase further.

Residential Construction

Our index of residential construction is estimated to have decreased 19 percent during November, after having decreased 1 percent during October. However, the index for November was 30 percent more than that for November 1957.¶

The *Engineering News-Record* index of construction costs decreased slightly in October and again in November. However, the November index was still almost 5 percent more than that for November 1957. In December, the index increased sharply again to an alltime high.

The dollar total of contract awards for residential construction in the 48 States, as reported by the F. W. Dodge Corporation, was 24 percent less for November than that for October but 30 percent more than that for November 1957. Although the November total represented a seasonal decrease somewhat larger than usual, its level was consistent with a continuing favorable rate of residential construction.

Our index of the physical volume of residential construction, derived by dividing the seasonally adjusted dollar value index of contract awards by the index of construction costs, decreased 19 percent during November, after having decreased 1 percent during October. The November index was 24 percent more than that for November 1957.

There were 100,000 new privately owned nonfarm dwelling units started in November, 8 percent fewer than those started in October but 32 percent more than those started in November 1957. New units started in November were at the seasonally adjusted annual rate of 1,330,000, the greatest rate attained since the 1957-58 recession minimum of last February.

The number of new homes financed under Government-sponsored programs totaled 36,800 in November, 72 percent more than the number so financed in November 1957. New homes financed by Veterans' Administration guaranteed loans and those financed by FHA insured loans both likewise increased by 72 percent in November 1957-November 1958 period. New homes financed by conventional loans totaled 63,200, 16 percent more than those similarly financed in November 1957. The 1958 expansion of Government-sponsored private housing, encouraged by enlarged Federal agency mortgage financing appears to be waning in recent months. Partly because of the decreasing attractiveness to lenders of the fixed interest rates attached to VA and FHA mortgages, new homes started in November under these programs decreased 26 percent from the October high of 49,400 units.

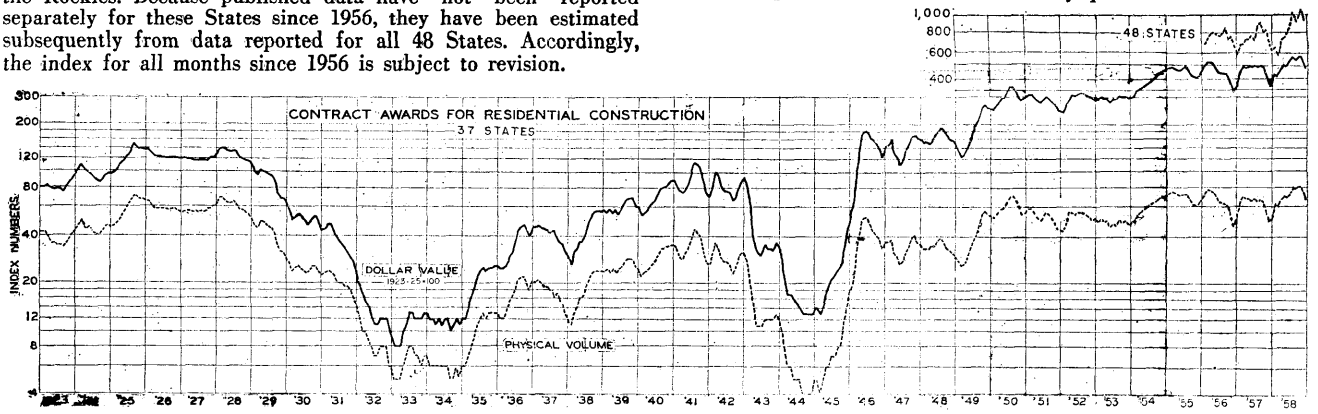
Requests for VA appraisals decreased markedly from the July and August level of 28,500 monthly to 15,300 in November. Similarly, applications for FHA commitments to insure mortgage loans decreased from the September level of 36,800 to 22,300 in November. The combined total of "proposed home construction" under Government-sponsored programs thus has decreased about 40 percent from September to November. To the extent that this decrease reflects lenders' reluctance to finance homes under restricted VA and FHA interest rates, the maintenance of a high level of residential construction in coming months will depend upon a corresponding increase in conventionally financed loans at uncontrolled interest rates. This shift actually began in November, with an apparent transfer of 3,600 new homes from Government-sponsored to conventional mortgage financing. However, in view of the inability of many marginal home buyers to comply with the more severe equity and down-payment requirements attached to conventional loans, longer-term expansion of residential construction will probably require further infusions of Federal credit in the secondary mortgage market as a temporary expedient; or, more soundly but less probable politically, higher interest rate ceilings on VA and FHA loans.

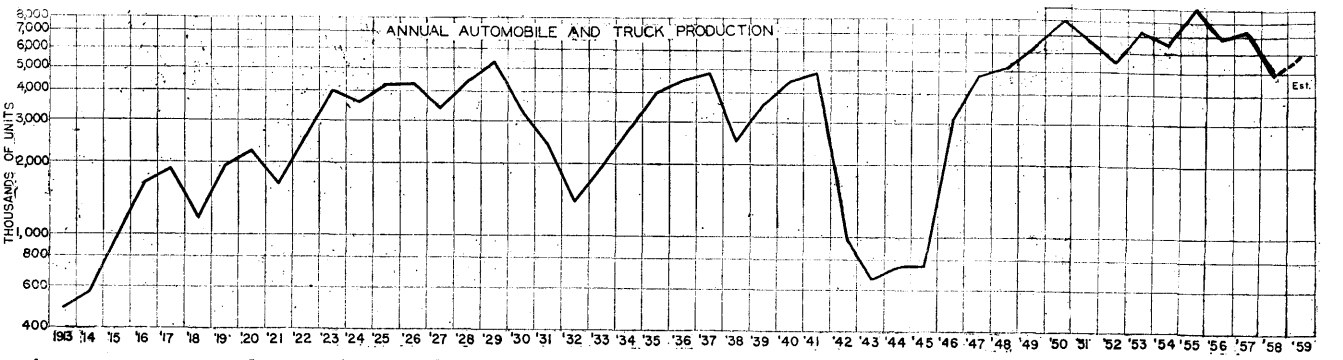
Residential construction may continue at high levels for several months, but is expected to decrease unless bolstered by more Government supports.

Automobile Production

Domestic motor-vehicle production during 1958 totaled 4,895,000 units, a decrease of 30 percent compared with that for the previous year. This total was the least since 1947 when 4,798,000 motor vehicles were produced. Of equal significance is the fact that only 4,244,000 passenger cars were produced in 1958, a decrease of 31 percent from the total produced in 1957 and the smallest number for any year since 1948 when 3,909,000 units were assembled. Production for 1958 reflects the depressed economic conditions during the latter part of 1957 and the early part of 1958. Strikes

¶This index is a centered 3-month moving average of the seasonally adjusted monthly totals of contract awards in the 37 States east of the Rockies. Because published data have not been reported separately for these States since 1956, they have been estimated subsequently from data reported for all 48 States. Accordingly, the index for all months since 1956 is subject to revision.





in the automotive industry during the 1959 model changeover period had little effect on production because of their short duration.

The table below shows the percentage of total domestic motor-vehicle production attributable to each of the Big Three and the 2 independent producers during the past 2 years.

	1957	*1958*
Chrysler	18.7	13.1
Ford	32.0	29.9
General Motors	46.5	51.3
Sub-total	97.2	94.3
American Motors	1.6	4.4
Studebaker-Packard	1.2	1.3
Sub-total	2.8	5.7
Total	100%	100%

Of special interest is the marked increase during 1958 in the proportion of total production represented by American Motors Corporation with its relatively small Rambler car. It now seems probable that the small car (foreign or domestic) can consistently account for at least 5 percent of the total United States auomobile sales and may eventually control as much as 20 percent of the total market. Demand of this magnitude may overcome the reluctance of the Big Three to produce a car that satisfies the wants and needs of a sizeable portion of car buyers.

During 1957, approximately 4,250,000 passenger cars were scrapped. However, because many owners apparently have been willing to drive their old cars for another year or more, we estimate that the number of units scrapped during 1958 was somewhat less than that for 1957. If the average age at which cars are scrapped decreases to that of 1957 or lower, the potential demand for new cars during 1959 or subsequent years presumably will be increased substantially.

Throughout most months during 1958, monthly production of motor vehicles was substantially less than that during the corresponding months in 1957. For example, August 1958 production was 41 percent less than that in August 1957. On the other hand, the number produced during December 1958 was 11 percent greater than that during December 1957, and represented the largest monthly production since January 1957. On January 1, 1959, approximately 450,000 new automobiles were in or en route to dealers' showrooms. This number compares with dealers' inventories totaling 511,000 on January 1, 1958, and a usual inventory of about 500,000 vehicles. Excluding imported cars, new-car sales during 1958 approximated 4,285,000 units, compared with about 5,830,000 units during 1957. However, sales increased significantly during the final month of 1958, and were 3 percent more than sales during December 1957.

Year-end improvement in the industry suggests that domestic production during 1959 may approximate 6,000,000 vehicles.

Industrial Production

Production of steel, automobiles, lumber, and electric power (1) in the 1- and 4-week periods ended on the indicated dates in the current year and (2) in the corresponding periods of earlier years was as follows:

	1929	*1932*	*1954*	*1957*	*1958*	*1959*
Steel						
Ingots—million tons						
Week: January 17	1.15	0.40	1.37	2.47	1.54	2.13*p*
Four weeks: January 17	3.92	1.24	5.22	9.90	6.09	8.32*p*
Automobiles						
Vehicles—thousands*						
Week: January 10	96	31	153	188	146	165*p*
Four weeks: January 10	278	124	471	605	508	578*p*
Lumber						
New York Times Index						
Week: January 3	132	42	123	95	74	96
Four weeks: January 3	138	44	131	107	96	120
Electric Power						
Kilowatt-hours—billions						
Week: January 10	1.73	1.63	8.82	12.33	12.50	13.55
Four weeks: January 10	7.66	7.47	34.07	47.43	48.82	50.82

p Preliminary. * Cars and trucks in U. S. and Canada.

BOOK REVIEW

Elementary Statistical Methods, revised edition, by Helen M. Walker and Joseph Lev, Henry Holt and Company, 383 Madison Avenue, New York 17, New York ($4.75)

This textbook is intended to introduce the college student to statistical methods. Exercises follow the several topics. A list of formulas and glossary of symbols is an important feature of the book. Treatment of statistical frequency distributions in one and two variables, with which most of the book is concerned, makes it appropriate for the student of economics.

PURCHASING MEDIA BY SOURCE AND TYPE
(In millions of dollars as at month ends)

	1957	*1958*	
Source and Type	*Dec.*	*Nov.*	*Dec.*
Gold	22,781	20,609	20,534
Commercial, industrial, and agricultural loans	42,467	43,519	43,932
Total noninflationary	*65,248*	*64,128*	*64,466*
Silver and U. S. debt monetized as Treasury currency by U. S. fiat	3,595	3,781	3,781
U. S. debt monetized as Federal Reserve notes and demand deposits of commercial banks	40,315	45,200	45,838
All other debt monetized as Federal Reserve notes and demand deposits of commercial banks	29,579	27,199	29,616
Total inflationary	*73,489*	*76,180*	*79,235*
Total purchasing media	138,737	140,308	143,701