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RESEARCH
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The U.S. Balance of Payments

A persistent adverse balance of payments accounts for the decrease in the Nation's total gold stock from $24.6 billion in 1949 to $15.6 billion currently. Although the adverse balance of payments continued through the first quarter of 1964, there had been a marked diminution in the rate since mid-1963. This was clearly a favorable development; however, its long-term significance can be overrated.

The seasonally adjusted adverse balance of payments decreased to $40 million in the first quarter of 1964, compared with an average of about $135 million in the last two quarters of 1963 and with $2,644 million for the entire year. (These amounts reflect the treatment as liquid liabilities of nonmarketable medium-term Government securities held abroad.) The first-quarter 1964 balance was affected, as it usually is, by temporary or nonrecurring developments, both favorable and unfavorable.

Among the more important temporary favorable developments were:

1. Extraordinarily large agricultural exports including about $100 million of wheat sales to the Soviet bloc.
2. Comparatively small imports during the first 2 months of the quarter.
3. Receipt of about $50 million paid on the account of U.S. logistic support given the United Nations troops during the Korean conflict.
4. Receipt of about $75 million in dividend payments to U.S. parent companies deferred for payment in 1964 in order to take advantage of lower tax rates effective this year.
5. Exceptionally small capital outflows to Canada ($21 million in the first quarter of 1964, compared with average amounts of about $80 million in the first quarters of 1961 through 1963.)

In addition to these influences, there was that of the proposed interest equalization tax on capital outflow through foreign securities issues, the uncertainty of which probably tended to postpone more issues of new foreign securities in U.S. financial markets than would application of the tax.

Partially offsetting the effects of these favorable influences were:

1. An extraordinarily large outflow of short-term funds, including $160 million to Canada, largely in response to higher yields available from Canadian investments. This outflow followed an inflow of $120 million (after seasonal adjustment) from Canada to the United States in the second half of last year.
2. Large increases in the amount of foreign short-term claims reported by U.S. banks.

Net new capital outflows in the first quarter of this year were about $700 million after seasonal adjustment. This was at a record rate (after a special adjustment of the fourth-quarter 1963 figure). The largest part of the $700 million was in loans and acceptance credits, some of which may have been substituted (directly or indirectly) for funds that would have been derived from the sale of long-term securities if the interest equalization tax had not been under consideration.

Walter Lederer, a Department of Commerce economist writing in the *Survey of Current Business* for June 1964, expressed the belief that an increase in merchandise exports for the first quarter may have been the result of a stronger competitive position of U.S. industry than that of recent years, especially in relation to Canada and Western European countries. To the extent that prices and wages have risen in some of these countries, most notably Italy, as a result of inflation, U.S. industry may have gained relatively in its competitive position. However, the information available is too fragmentary to confirm such a conclusion.

First-quarter 1964 improvement in the Nation's international financial position as a result of improvement in its balance-of-payments situation has been widely heralded. However, this position of the Nation improved only to the extent that its holdings of foreign currencies increased. Actually the Nation's gold reserve, including gold on deposit with the International Monetary Fund, decreased $177 million during the first quarter of 1964. This loss, however, was more than offset by an increase in convertible foreign currencies equivalent in value to $228 million, making a net gain of $51 million. Although this gain was relatively small, it compares with a similar one of only $5 million during the preceding quarter and with decreases during most of the quarters since the beginning of 1958.

Recent improvement in the U.S. balance of payments, although small, is helpful even if it was not the result of improvement in the competitiveness of the U.S. economy. However, because the improvement was largely if not wholly the result of fortuitous developments, it would be a mistake to assume that the Nation's international financial problems have been solved. They have not; but the Nation has gained a little more time for solving them.

Foreign Aid

According to the Agency for International Development (AID) of the Department of State, there was on hand on June 30 approximately $7 billion in unexpended appropriations for foreign aid. This compares with estimated expenditures of $3.6 billion for such aid in the fiscal year 1964. Legislation now pending in Congress would appropriate $3.3 billion for the aid program in fiscal 1965. With so much in aid funds already avail-

able, one may wonder why any new appropriation at all is needed.

In a letter dated June 22, Representative Otto E. Passman, Chairman of the Foreign Operations Subcommittee on Appropriations, commented on the confusing situation in AID as follows:

"AID's system of obligating, deobligating and reobligating, and funding projects in excess of the cost to complete, makes it impossible for even the most dedicated member to determine what part of the unliquidated funds are firmly committed. AID's estimates show that there will be unliquidated funds on June 30 of over $7 billion. If history repeats itself, this figure will climb substantially at a later date, and, of the $7 billion plus in the pipeline, as much as $1 billion could revert to the unobligated category. Juggling and overfunding have been so rampant that AID has deobligated funds from 232 projects in the past 60 days.

"It is fantastic but true that our government will be dispensing funds during Fiscal 1965 in 99 nations and 9 territories. Furthermore, this uncontrolled and apparently uncontrollable program now has 71,416 people, including participants, on its payroll. It has reached such proportions that even the confusion is confused."

During the past 19 years well over $100 billion has been disbursed through the foreign aid program. This represents about a third of the Federal debt, which now approximates $311 billion. Moreover, largely because of foreign aid disbursements the total U.S. gold stock has decreased from a record $24.6 billion in 1949 to $15.6 billion, while the net amount of foreign-held, short-term dollar credits, which can be used to claim gold, has increased from about $7.6 billion to nearly $20 billion.

Thus the United States has been letting itself become more and more of a debtor country on short-term account while continuing on a lavish scale its foreign aid program. As this has been going on during the past 19 years, opposition to the program, at least on its present large scale, has developed. In a Congressional Report last year the Minority Views on foreign aid were expressed as follows: "It is obviously impossible for any country, no matter how rich or strong it may be at the start, to continue assistance indefinitely to most of the countries of the world. The growing size of our national debt and our dwindling gold reserves attest to the drain of our reserves resulting from our heavy foreign and domestic commitments."*

*House Report 646, 88th Congress, p. 123.

What the Indicators Say

Among the leading indicators, floor area represented by commercial and industrial building contracts increased in April but is estimated to have decreased in May.

Among the lagging indicators, the index of wage and salary costs per unit of manufacturing output increased slightly in May.

The indicators continue to signal expansion of business activity.

SUPPLY

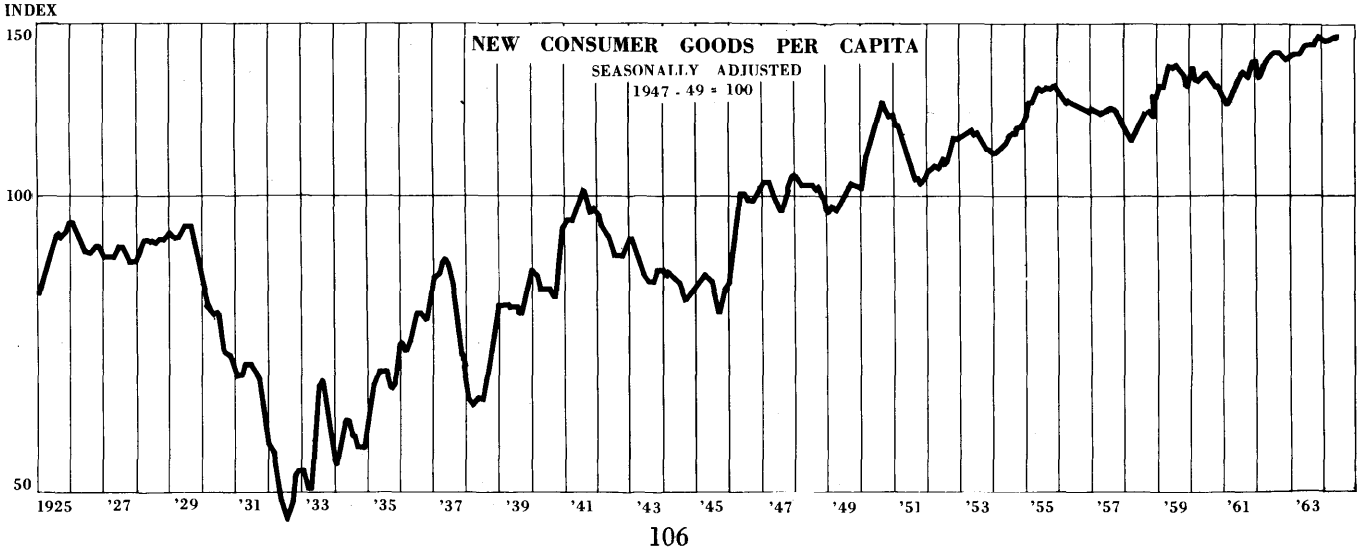
New Consumer Goods Per Capita

Our seasonally adjusted index of new consumer goods produced per capita for May was unchanged from that for April but was about 3 percent more than the index for May 1963. At 145 (1947-49=100), the May index was at the record level reached in November 1963.

The index provides a measure of the portion of the Nation's industrial output that is or soon will be available for final consumption by individuals. Such output includes about one-third of the industrial production reported by the Federal Reserve Board; it also includes residential construction but excludes the production of intermediate materials, capital goods, and defense equipment.

Before adjustment for population changes, seasonally adjusted production of consumer goods for May was slightly more than that in April and 4 percent more than that in May 1963. The small May increase was chiefly attributable to an increase in the output of manufactured consumer goods, which comprise three-quarters of our index of new consumer goods production.

Among the seasonally adjusted components of manufactured consumer goods production, which together increased 1/4 of 1 percent in May, the output of all consumer automotive products increased 1/2 of 1 percent from that in April and was 9 percent greater than that in May 1963. The volume of such output has been large for nearly 9 months, but it is expected to decrease somewhat in July and August; however, because of the difficulties of seasonally adjusting automobile production during the model changeover periods scheduled then, its trend may be obscured temporarily. Production of consumer staples in May, including foods, beverages, tobacco, toiletries, reading materials, and fuels, was 3/4 of 1 percent more than that in April, while the output of home goods and apparel decreased slightly from the



April volume; May production of these two major components of the index was about 4 and 6 percent more, respectively, than such production in May 1963.

The Federal Reserve Board's combined index of consumer durable goods production, comprising automotive and durable home goods, was slightly less for May than that for April but was 5 percent more than the index for May 1963. The May combined index of consumer nondurable goods production, including apparel and staples, was slightly more than that for April and was 4 percent more than the index for May last year.

The new residential construction component of our index decreased slightly from April to May but was 4 percent more than that for May 1963. The number of building permits issued and the value of construction contracts recently awarded now indicate that residential construction (as distinguished from the number of new residences on which work is beginning) soon will decrease.

We expect little change in our index of new consumer goods per capita during the summer months.

Industrial Production

Production of steel, automobiles, electric power, and lumber (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:

Steel	*1929*	*1932*	*1957*	*1961*	*1963*	*1964*
Ingots—million tons						
1 week: June 27	1.31	0.26	2.15	1.98	2.31	2.32
4 weeks: June 27	5.29	1.09	8.78	8.05	9.71	9.53
Automobiles						
Vehicles—thousands*						
1 week: June 27	125	55	160	162	213	229*p*
4 weeks: June 27	503	211	630	601	861	920*p*
Electric Power						
Kilowatt-hours—billions						
1 week: June 27	1.7	1.4	12.1	14.9	17.9	19.8
4 weeks: June 27	6.8	5.7	48.0	59.1	70.5	75.8
Lumber						
New York Times Index						
1 week: June 20	132	39	111	106	91	101
4 weeks: June 20	126	39	107	102	99	110

* Cars and trucks in the United States and Canada.
p Preliminary.

DEMAND

Department-Store Sales

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

Period	*Percent Change*
Week ended June 27	n.a.
Four weeks ended June 27	n.a.

n.a. Not available.

PRICES

Consumer Prices

The Consumer Price Index remained unchanged between mid-April and mid-May at 221.2 on the 1935-39 base (107.8 on the 1957-59 base).† At this level the index was 1.5 percent higher than it was a year earlier.

Among the major components of the index, six increased and two decreased. Prices of personal care increased 0.2 percent; prices of apparel and upkeep, transportation, medical care, reading and recreation, and other goods and services increased 0.1 percent; but prices of food and housing decreased 0.2 percent and 0.1 percent, respectively.

Average weekly earnings after taxes for a factory worker with three dependents increased 75 cents in May to $92.18, a record level, compared with $87.25 a year earlier. The purchasing power of the consumer dollar in May was unchanged at 45.2 percent of what it was in the 1935-39 period.

Sidney A. Jaffe, Deputy Assistant Commissioner of the Bureau of Labor Statistics, has predicted a slight rise in the index for June. In discussing the housing cost index, which decreased 0.1 percent from April to May, Mr. Jaffe noted that residential rents were unchanged for the third month during the last five, and commented that "the upward trend is probably slowing down."

We expect the trend of the Consumer Price Index to continue upward as a result of small increases in some months.

Commodity Prices

Index	*1963 June 29*	*1964 June 22*	*1964 June 29*
Spot-market, 22 commodities	246	254	253
Commodity-futures	311	288	287
Steel-scrap	$25.17	$33.17	$33.83

Note: The indexes are, respectively, those of the U.S. Bureau of Labor Statistics, Dow-Jones, and *Iron Age*. The spot-market and futures indexes are converted so that their August 1939 daily averages equal 100. The steel-scrap index is a composite price for No. 1 heavy melting scrap.

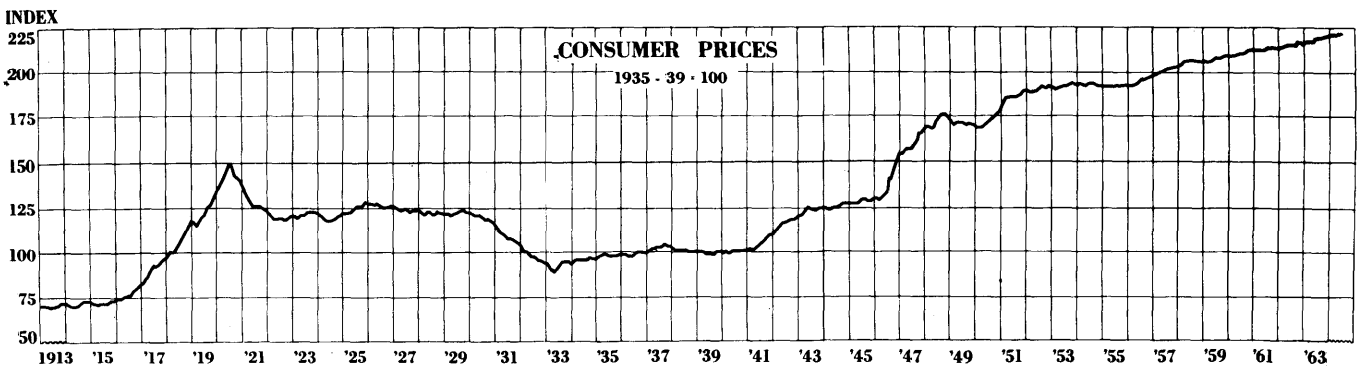
BUSINESS

Business Failures

Liabilities of business failures in May totaled $93,419,000 or 21 percent less than those in May 1963. Our 6-month moving average of seasonally adjusted failure liabilities, centered at the end of February, was $98,820,000 or 22 percent less than the average centered in January and 7 percent less than that centered in February 1963.

The proportion of failure liabilities in the various

†The Consumer Price Index, compiled by the Bureau of Labor Statistics, is a statistical measure of changes in prices of goods and services bought by urban wage earners and clerical workers, including now both families and single persons. The index is often called the "cost-of-living index," but its official name is *Consumer Price Index for Urban Wage Earners and Clerical Workers*. It measures changes in prices that are the most important cause of changes in the cost of living, but it does not indicate how much people actually spend to defray their living expenses.



divisions of industry and trade, expressed as percentages of monthly totals, changed from April to May as follows: mining and manufacturing up from 27 to 40; wholesale trade down from 14 to 8; construction down from 25 to 16; and commercial service up from 9 to 11. The proportion in retail trade was unchanged at 25. Failure liabilities in the first 5 months of 1964 were 6 percent less than those in the corresponding period of 1963. Failure liabilities in May 1964 in the categories listed above changed from their amounts in May 1963 by the following percentages: mining and manufacturing, +13; wholesale trade, −33; retail trade, −41; construction, −26; and commercial service, −29. Liabilities per failure averaged $86,901 in May, compared with $94,306 in April and with $90,770 in May 1963.

The unadjusted number of failures in May was 1,075 or about 10 percent less than that in April and 18 percent less than that in May 1963. In May, the number of failures decreased in all major divisions of trade and industry by 8 to 13 percent of the previous month's numbers, and by 16 to 22 percent of the numbers in May 1963.

The number of failures in the 4 weeks ended June 25 was 1,045 or 12 percent less than the number in the corresponding period last year. Dun's Failure Index, seasonally adjusted and expressed as an annual rate per 10,000 active enterprises, decreased to 49.4 in May, compared with 51.3 in April and 56.4 in May 1963.

The accompanying chart showing our 6-month moving average of seasonally adjusted failure liabilities minimizes the influence of random irregularities and reflects principally the combined cyclical fluctuations and long-term trend of the series. The smoothed average plotted with February as the latest midpoint and incorporating May data decreased sharply from $126 million in January to $99 million in February, compared with $107 million in February 1963. At this level, the average of business-failure liabilities had decreased to a 21-month low.

The weekly average number of business failures with liabilities of $100,000 or more, which account for large irregularities in the series of total failure liabilities, decreased from 46 in April to 39 in May. This indication of improved business conditions in May continued into June.

The failure liabilities series improved sharply in May, thereby providing its first favorable signal as a leading indicator of business-cycle changes in many months.

BUSINESS FAILURES: NUMBER AND LIABILITIES
BY TYPE OF BUSINESS
May 1963 and 1964

	Number			*Liabilities**		
Business	*May 1963*	*May 1964*	*Percent Change*	*May 1963*	*May 1964*	*Percent Change*
Mining & mfg.	241	188	−22	33.5	37.8	13
Wholesale trade	139	115	−17	11.2	7.4	−34
Retail trade	595	501	−16	39.3	23.3	−41
Construction	217	179	−18	19.8	14.7	−26
Com. service	111	92	−17	14.5	10.2	−31
All businesses	1,303	1,075	−18	118.3	93.4	−21

*In millions of dollars.

BOOK REVIEW

The Decay of Money; a Survey of Western Currencies, 1912-1962 by Elgin Groseclose

Institute for Monetary Research, Inc., 1010 Vermont Avenue, NW., Washington 5, D.C. ($1)

This pamphlet gives an excellent simplified account of the degradation during the past five decades of three major European currencies: the British pound, the French franc, and the German mark. The paradox of their deterioration in value, as well as the deterioration of most other European currencies and of the U.S. dollar, is that for about 40 years before World War I "Europe experienced what might be called both literally and figuratively the golden age of money."

Dr. Groseclose says of that golden age: "Beginning in the early 1870s most of Europe had succeeded in settling on a gold parity standard, in which the standard was a gold coin of given weight and fineness, and other forms of money, such as circulating notes or silver or copper coins, were held to parity with gold through guarantee of the state and restraint in the management of the circulating medium. The individual could demand and receive gold for his notes or minor coins and balances owed abroad were settled by the shipment of gold."

All this changed long ago. Now "the hard truth is that modern money is notoriously unstable. * * * A characteristic of all modern money is that it deteriorates."

In three short chapters, which are among the best concise accounts available, the histories of the pound, the franc, and the mark are traced. Another chapter presents a summary account of the depreciation of U.S. currency, concluding with the significant comment that "a variety of stratagems and expedients are being tried out to stem the outflow of gold and shore up public confidence in the dollar, but it is likely that these efforts will be fruitless until the basic cause of the outflow is removed."

The one bright part of this otherwise bleak story of these currency depreciations is the description of the West German currency reform of 1948 and subsequent sound monetary measures in that country, which were "sufficient to give a great burst to trade and production" and bring about "a new boom period" in West Germany that has been one of the most remarkable economic recoveries in history.

We are glad to recommend this worthwhile little booklet to our readers.