



Monthly Review

F E D E R A L R E S E R V E B A N K O F S T . L O U I S

JANUARY 1, 1946

Transition From War to Peace

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For the first time in many years, New Year's Day 1946 finds the world at peace. As we look back over the war years we cannot help but realize that victory was achieved largely because of the unity of purpose and action which all elements of our people brought to their wartime jobs. This same unity of purpose and action will be needed if we are to create an orderly and peaceful world in the future.

Perhaps the most outstanding feature of our wartime experience was the tremendous achievements of scientific research and development. The freeing of atomic energy, for example, points up the fact that our scientific advances justify the belief that almost any physical problem is capable of solution. We are faced with the challenge whether our economic, social, and political institutions and relationships can keep pace so that we can enjoy the fruits promised by our scientific endeavor turned to peacetime pursuits.

It can be done only if the nations of the world have reasonable hope of security and lasting peace. Great progress has already been made toward this goal. The establishment of the United Nations Organization and other international administrative bodies is providing machinery for permanent and continuing cooperation on political, social, and economic problems. The recognition that all nations have a common responsibility in the reconstruction of wartorn lands and the development of backward nations is an important step forward. With the machinery which has been established or

is in process, the nations of the world are in a better position than ever before to consult upon problems as they arise and to reach mutually satisfactory agreements through peaceful means.

Substantial progress has been made in the short period since the end of the war in converting from war to peacetime activity in the United States. Reconversion of industrial plant to civilian production has occurred more rapidly than had been anticipated and although total industrial output has dropped by about 20 per cent from the level just prior to the Japanese surrender, it is still higher than ever before in peacetime.

Barring serious interruptions in production because of widespread work stoppages, 1946 should be a year of extremely high industrial activity. All types of manufactured goods are in strong demand. There is a large deferred demand for the many types of durable consumers goods which have not been produced during the war. The demand for industrial equipment is high, and business firms are restocking inventories of various items which go into civilian goods production. Consumer demand is also strong for many types of nondurable goods the production of which has been curtailed during the war years. Returning veterans are adding to demand for various types of civilian goods, particularly clothing. Purchasing power is plentiful on the basis of high current incomes, mustering-out pay, and accumulated wartime savings. A large demand for American goods from foreign countries may be expected as soon as trade channels are reopened and arrangements are made for financing:

DANGER OF INFLATION

In view of this situation, one of the principal problems that the country must face in 1946 is the danger of inflation, which is more serious today than at any time since the war began. Now that the war is over, the demand by the public for goods has accelerated despite some decline in total income. Increasing pressure is being exerted upon the price control authorities for price relief. There is imminent danger that the public, fearing higher prices, will soon attempt to use the huge supply of purchasing power that it has built up during the war years.

Between 1940 and the present time bank deposits and currency held by individuals and business have more than doubled, and now stand at approximately \$150 billion. In addition individuals and businesses hold some \$100 billion of Government securities. This tremendous volume of liquid assets plus high current income will continue to constitute a highly inflationary force. Should the public enter the market for goods and services with this unprecedented volume of funds our capacity for increased production could not satisfy the demand except at sharply higher prices.

Thus, one of our major tasks in 1946 will be to ward off the danger of inflation. There are three principal lines of attack.

The first is to obtain the largest production possible, since over a period of time the primary safeguard against inflation is a large supply of goods flowing to the market. This will require cooperative action on the part of Government, labor, and management. Some adjustments in prices and wages are necessary, and action must be taken promptly to assure that cost-price relationships do not impede production. Most important, however, is to increase productivity and to avoid restrictive practices on the part of any groups in the hope of gaining special advantage. High production in 1946 will relieve the most serious inflationary pressures; the prospect of an abundance of goods becoming available will restrain anticipatory buying.

Second, although prompt price relief will be necessary on a number of manufactured items and on secondary items where frozen prices restrain production, price ceilings should be maintained as a bulwark against inflation so long as demand is substantially in excess of current production. The need for continuation of general price control has been emphasized by recent experience of sharply rising prices which have occurred in some cases where price ceilings have been prematurely removed. The

continuation of properly administered price ceilings should be no deterrent to production and will give further assurance against the development of widespread speculative buying. While moderate wage increases may be justified on the basis of increased productivity, general wage increases that would materially increase costs and thus require broad upward revision of price ceilings might jeopardize the whole program of inflation control.

Finally, the public must continue the same type of restraint in buying which was evidenced during the war years. Public acceptance of price ceilings and rationing was an important factor in holding down the increased cost of living during the past five years. Patience and willingness of consumers to wait until production catches up somewhat on goods that are scarce will continue to be a major factor in determining whether price advances are kept within reasonable limits in the year ahead.

Although inflation is the most imminent threat to economic stability, we must not neglect the longer run problem of maintaining reasonably full employment of our human and material resources. This problem will be made more difficult as a result of economic disruptions which would occur if we have a postwar inflation followed by collapse and deflation.

POSITION OF AGRICULTURE

One of the areas of the economy that would be most seriously affected in the event of inflation and collapse is agriculture, which in the Eighth District is the most important single activity. Although agricultural income is high and prices of most agricultural commodities have risen since the end of the war, farming is probably more vulnerable to adverse developments than any other major industry.

During the course of the war, agriculture has increased its production by over 30 per cent. Although there is a large demand for farm commodities at present, American agriculture may shortly again be faced with the troublesome problem of persistent surpluses. Even with a high level of domestic purchasing power the demand for agricultural commodities will be reduced as purchases for the armed services and foreign relief are curtailed. Moreover, agricultural production is one of the first activities to recover in countries where it was disrupted by actual warfare. Consequently over a period of time, American agriculture cannot look to foreign outlets for surplus production to the same extent as industry.

In the long run, agriculture will prosper only in an environment of high level employment, unrestricted and abundant production, and high purchasing power. Farmers have always preferred to follow this course in their own operations and have supported restrictive programs only as a matter of self-protection.

The adjustments which face agriculture can best be accomplished against a background of expanding nonagricultural employment at high wages. This is important not only because it will mean higher domestic consumption of farm products, but also because it will encourage shifts from farm areas of surplus workers who would otherwise remain and intensify the problem of over-population and under-employment which has traditionally plagued farming.

Although agricultural prosperity will depend largely upon the major economic forces over which individual farmers have little control, the productivity of the individual farm unit and worker should be greatly increased to provide a higher standard of living for the farmer. During the war substantial progress was made in increasing the productivity of farm workers. The over-all increase in agricultural production of about one-third was accomplished with a farm labor force that declined sharply in numbers and was handicapped by shortages of equipment and fertilizer.

Agriculture has been going through a process of technological revolution which should be greatly accelerated now that peace is here. As a result of the technological developments it is even more important that the farm labor force should not return to its prewar level, for this would mean lower per capita farm income. In fact, over a period of years continued technological development should foster a further reduction in the number of people engaged in agriculture, and their shift to more productive work in nonagricultural trades and services.

Measures designed to encourage veterans and war workers to return to the farm should, therefore, be carefully appraised. Agriculture can absorb some new workers. Many in the wartime farm labor force worked excessively long hours and others in normal times would have retired or devoted more time to schooling. Every effort should be made to see that those returning to the farm are located on adequate-sized units and with sufficient capital and equipment to assure efficient production.

ROLE OF BANKS

The banking system has a great responsibility in helping to bridge the transition from war to peace.

During the war the primary job of the commercial banks was to see that the Government financing program was successful. Although every effort was made to sell as many Government securities as possible to individuals and institutions other than commercial banks, it was still necessary for the banks to buy a large volume of Government debt either directly upon subscription from the Treasury or indirectly through purchases in the market of securities sold by others. This process resulted in a large expansion of bank deposits which are held by the general public.

Now that Government needs for financing are greatly reduced it is desirable that further expansion of deposits be discouraged so long as inflationary pressures exist. The banks of the country should bear this in mind in formulating lending policies. In the period ahead credit may be requested for destructive as well as constructive purposes. Destructive uses of credit are those which will tend to add to the inflationary pressures. Credit extended to finance speculative purchases of real estate, securities, or inventories is of this character. In the public interest and for their own protection banks should discourage applications for credit that are clearly predicated upon a further rise in prices. Credit standards should continue to adhere to normal values for appraising loan applications.

On the other hand banks should encourage credit for constructive purposes that will promote expansion of production and thus lessen the danger of inflation. As has been pointed out earlier, the fundamental safeguard against inflation is to obtain high production as rapidly as possible. Whenever bank loans contribute to this the banks will be performing a useful public service.

The commercial banks of the country are in a favorable position to exert real leadership in the period ahead. The banks have emerged from the war in the strongest financial position of their history. Earnings are high, loans generally are well-margined, and the financial condition of borrowers is generally strong. Through conservative dividend policies the banks have added a large portion of their wartime profits to capital accounts. As a result, the ratio of bank capital to the actual risk assets they hold is now higher than ever before.

There are many factors which indicate that bank deposits and earnings will remain high for several years to come. Since the wartime growth in deposits resulted largely from increased holdings of Government securities, deposits for the banking system as a whole will not be materially reduced unless

debt is retired or shifted to nonbank holders. Even though there is no significant reduction in over-all deposits, shifts in deposits from one region to another are likely to occur. If we can maintain a reasonably high level of economic activity, such shifts as do occur will probably be gradual and of smaller magnitude than many bankers feared earlier. Since the end of the war there has been little evidence of any significant shifts in deposits, and it is unlikely that substantial regional shifts in deposits will take place throughout most of 1946. Since banks generally over the war years have stressed liquidity in their investment policy, whatever deposit shifts do occur can be met without appreciable disturbance to the banking system.

Under these circumstances the banks of the country are able to assume greater responsibilities for leadership. With the tremendous growth in bank holdings of Government securities during the war the character of bank assets has changed completely. Banks must contribute constructive advice to the public authorities charged with the difficult task of managing a \$300 billion debt. Because of high earnings there is little need for banks to compete for speculative loans that will add to inflationary pressures. On the other hand the banks can afford to take somewhat more than normal risks where the proceeds of loans are for productive purposes.

Present conditions also make it possible and de-

sirable for banks to review other management policies. Banks are primarily service institutions. In recent years large sections of the public have not been using banking facilities. In part this may have been due to banks' policies with respect to service charges and interest payments on savings. Some changes in these policies would appear warranted in order to broaden the scope of bank services.

Many banks are giving more attention to the compensation of their employees. In the past bank salaries have tended to be low in relation to those paid by industry and many commercial establishments. Some upward adjustment in salaries of bank employees will be necessary if the better bank personnel is not to shift to other fields. Also many banks are providing more adequate retirement and health benefits for their employees.

In summary, 1946 promises to be a prosperous year for industry, agriculture, trade, and finance in the United States. The aftermath of war brings many difficult domestic and international problems the solutions for which will call for our best thought and effort. Vigorous action will continue to be necessary to avoid the danger of inflation. Government, labor, and management must cooperate in removing barriers to high and sustained production. All nations must resolve to build a firm foundation for international cooperation that will assure an orderly and peaceful world.

Survey of Current Conditions

During November and early December economic activity was maintained at a much higher level than was expected of the transition period. Employment, both industrial and nonindustrial, has increased in recent weeks. Labor disputes, however, have retarded gains in both production and employment.

Consumer incomes are running currently at about the level averaged in 1944. This high current income, backed up by huge wartime savings mostly held in liquid form (cash, bank deposits and Government securities), has led to heavy consumer buying. Retail sales are running at all-time record levels. Civilian goods are beginning to come into the market in greater supply, but demand is increasing faster than supply, and prices continue to press ever harder against ceilings.

EMPLOYMENT

Nonagricultural employment in the United States expanded during the past two months after reach-

ing its post V-J Day low point in September. According to the official statistics, unemployment is currently declining but there is some reason to doubt the validity of the current unemployment estimates in view of the great changes in the labor force at present. As defined, an unemployed person is one who is not working but is actively seeking work. At the present time there are substantial numbers of persons who are not working and are not actively seeking work for a variety of reasons, such as moving from one locality to another, taking vacations between military discharge or war plant work and civilian employment, and the like. In a very real sense these people are in the labor market and are unemployed even though not technically classified as such. Probably over-all unemployment, including such persons, will be on the increase for some months in the future. It should also be noted that workers out on strike are considered as employed in the official statistics.