

THE PUMP-PRIMING DEFICIT FOR 1933-34

1. The accompanying chart shows the preliminary results of a study of the effects of Federal fiscal policy on the flow of money into the hands of income receivers. What we have called the pump-priming deficit may be briefly defined as the net Government contribution to income-creating expenditure. Certain Government expenditures like the salaries of Government employees obviously create income immediately. Other outlays like loans for construction projects, which are gradually paid over as wages to workmen, do so over a period of time and after passing through intermediate transactions. Outlays of this kind which are fairly certain to become income are referred to as income-increasing outlays. On the other hand, the proceeds of a loan made for the purpose of refinancing a debt to a private creditor may be held idle by the receiver of the funds, may be turned over by him to a second creditor in repayment of another debt, or may be used to purchase some existing asset like a piece of land or a bond. It is not likely to become part of the stream of income again for an indefinite time, and it is not an income-increasing outlay. There is a similar distinction between items of Government revenue. Certain receipts are deductions from the stream of income. The payment of taxes leaves less money in the hands of taxpayers for expenditure on goods and services. On the other hand, the funds obtained by borrowing, under the prevailing conditions in the money market, come out of newly created or idle balances which are not seeking, or which cannot find investment in capital goods industries, which would lead to their conversion into income. When income-increasing outlays exceed income-decreasing receipts, the tendency would be for the national income to increase by the amount of the excess of outlays over the receipts. This excess may be termed the pump-priming deficit and represents the net addition to the national income directly attributable to Government fiscal operations.

The pump-priming deficit is a measure of only the direct and immediate effects of Government spending. Since the average dollar passes into the hands of income receivers several times a year, the dollars introduced into the flow of income by the Government may increase the national flow of income by several times the amount of the original expenditure which put them into the hands of the public. On the other hand, the real or anticipated effects of certain particular kinds of Government expenditure like expenditures in connection with activities directly competitive with private business may decrease private spending by so much that a net decrease in national income will result. These indirect effects, however, cannot be accurately measured and no account is taken of them here.

It is clear from what has been said that in discussions of the effect of Government spending on general business activity it is the pump-priming deficit and not the reported deficit which should be referred to. An unbalanced budget as a deliberate measure of economic policy will fail of its object if the expenditures which keep it unbalanced are not pump-priming in their effects.

Because the pump-priming deficit has never amounted to as much as ten percent of the national income even when running at the high levels of the winter of 1933-34, it is not to be expected that small month-to-month movements will find immediate reflection in corresponding movements in business activity. Throughout the past two years the stimulating effect of Government expenditures have been counteracted in part by continued liquidation and hoarded savings by private individuals and corporations, both forces which tend to decrease the flow of income. The net effect has been rather to prevent incomes from decreasing below their present low level than to bring about an absolute increase. The experience of these years seems to indicate that such an increase in incomes requires a larger pump-priming deficit than the present figure of about \$300,000,000 a month. A strong indication of the stimulating effects on business activity of any pronounced increase in Government expenditures is given by the experience toward the close of 1934 when the rise in the pump-priming deficit from approximately \$100,000,000 to \$400,000,000 a month, associated with the activities of the C. W. A., was followed by a similar rise in industrial production and employment. The absence of other favorable factors in the business situation at the beginning of the upswing in activity strongly suggests that Government expenditures were largely responsible for the movement.

Looked at in relation to the size of the task which it was hoped to accomplish and the strength of the deflationary forces which it was necessary to offset or reverse, the pump-priming deficits of \$1,900,000,000 in the calendar year 1933, and \$3,300,000,000 in the calendar year 1934 seem comparatively small. Although the estimated deficit for the coming fiscal year may appear large absolutely and in relation to the sums involved in the ordinary operations of Government finance, serious doubts may be entertained whether it is sufficiently large to accomplish the desired object of stimulating private expenditures sufficiently to bring about the normal level of production. For this reason it is highly desirable that the expenditure program should as far as possible take the form of grants so as to make full use of the leverage principle, since in this way for every dollar the Federal Government spends at least two additional dollars will be spent. In so far as the leverage principle is utilized, the direct and immediate increase in the national income will be larger than the amount borrowed and spent by the Federal Government.