

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date November 19, 1937.

To Chairman Eccles

Subject: Public Utility Capital

On Lauchlin Currie

Backlogs

In view of the amount of misinformation there is about on the size of public utility backlogs, I think you will be interested in the enclosed comments by Mr. Terborgh.

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Date November 19, 1937To Mr. CurrieSubject: Public Utility CapitalFrom Mr. TerborghBacklogs

Recent newspaper stories, some of them purporting to derive authority from studies by "Federal Reserve experts", have described huge "backlogs" of capital expenditure (one figure being 2.6 billion dollars) that would be "released" if public utilities were given certain political assurances. While I have stressed the political hazards facing certain utilities, notably electric power, and while I favor reasonable relief from these hazards, my studies do not support the idea of huge ~~damped~~-up expenditures waiting to be liberated like a flood upon the materialization of this relief.

Electric Power

Except for the current business recession, the seasonal peak load in December of this year would probably strain the productive capacity of existing facilities in some cases, but with output likely to run below the 1936 peak, and with generating capacity slightly larger than a year ago, the situation should be entirely comfortable. In view of the absence of any substantial under-maintenance or under-replacement, this means that the need for enlarged capital expenditure will depend on the expansion of output from the present level. ^{1/} Since we start with a comfortable relation of capacity to output, a substantial backlog exists

1/ So large a proportion of existing plant is of relatively recent origin that replacement construction would still be small, even under favorable conditions. Regardation of replacement attributable to the depression and subsequent events accounts, probably, for a very minor "backlog".

only in the sense that output may expand during the next few years at an extraordinary rate as a result of continued recovery from the depression. This is not the sense in which it is usually understood, namely, as something already in being here and now. In the latter sense it is largely imaginary.

I have estimated that with continued economic recovery the private power industry will need to spend an average of 800,1,000 million dollars a year for five years, inclusive of maintenance (summary of electric power memo, p. 10). In the absence of recovery it will need comparatively little.

To sum up: if by a backlog is meant merely that plant outlays will need to expand above the present level, given a strong business recovery, there can be no doubt of its existence. Outlays might double under such conditions. As something existing irrespective of recovery, the backlog is a myth.

Telephones

The present relation of capacity to utilization is even easier than in the case of electric power. Capacity is well over 1929 while output still falls short of that level. There is little if any under-maintenance or under-replacement as compared with ordinary practice. My observations on the electric power backlog apply to this case, except that a resumption of business recovery would probably entail a relatively smaller increase in capital and maintenance expenditures over this year's level (summary of telephone memo, p. 10).

Transit

The peculiar situation of this industry is set forth in the relevant memorandum. Suffice it to say here that there is no prospect of any very

large expansion of plant expenditures even if recovery and prosperity are ahead.

Conclusion

Recovery and prosperity might raise the annual capital and maintenance expenditures of all utilities (other than steam railroads) 700 or 800 millions above the 1937 level. This potential increase -- which is conditional on recovery and will not occur in its absence -- represents the only "backlog" worth talking about.