

*To the Congress of the United States:*

ON January 14, 1948, I transmitted to the Congress my annual Economic Report under the Employment Act of 1946. At the present stage in economic affairs it is again desirable that the Congress and the country be presented with an up-to-date survey of the economic situation, the difficulties it presents, and the solutions called for. This Midyear Economic Report is transmitted to the Congress for that purpose.

## A Time for Action

IN the years since the end of hostilities in World War II, the American economy has offered an impressive display of inherent strength and elasticity. More than 10,000,000 veterans have been smoothly absorbed into the activities of the business world. Month after month, the labor force has been employed at a level which but few were willing to forecast. In spite of high living costs, our people continue to enjoy high standards of living. The income of American consumers, and the resources of American business, furnish the basis for sustained markets. Our financial condition is strong. A national debt of tremendous size has been managed so skillfully that we are prone to treat too lightly the problems which it still offers.

But our present prosperity should not blind us to the growing threats to our well-being. Repeatedly, I have called attention to the developing inflationary conditions which endanger both our domestic strength and our place in world affairs. In addition, recent events have forced us into a preparedness program adding to the strains upon our home economy, and making it even more imperative that we act with courage and dispatch. In my recent message to the Congress upon the opening of the special session, I again advised the Congress of the dangers that we face, and made recommendations to meet them.

I must emphasize that the course of inflation does not run according to any set schedule. Until the very eve of an economic collapse many people are apt to grow more and more confident about the soundness of the economy and the indefinite continuance of the boom. It may not be true that "a boom is always followed by a bust," as many students of business

affairs frequently say. But it would be reckless to assume that the bust will not happen if we neglect action to control the boom.

For 2 years, it has been asserted that if matters were left alone there would be so great an increase in production that it would take care of prices. Increasing the supply of goods is, indeed, to be sought through every practicable means. But, historically, no important inflation has been cured in that manner. Nor has this one, despite the fact that every factor of high profits, heavy market demand, and large funds available for investment has been favorable to the expansion of production.

The policy proclaimed in the Employment Act requires us to devise and adopt positive measures to stop this inflation and secure relative stabilization. It is not too late for preventive measures, and we are not yet forced by the tragic consequences of depression to adopt measures which would interfere with our free economy far more than would any or all of the measures I have proposed. I realize that the anti-inflationary program I have offered will impede some business plans, will curb some profit opportunities, and may limit some wage advances. It is of the very essence of a plan to counteract inflation that this be done. All groups will ultimately benefit when it is done.

## The Economic Situation in Summary

THE recommendations that I have made for dealing with inflation are based upon a candid look at the whole economic situation as it has developed over the past 6 months, and upon a careful analysis of where this situation may lead us if we do not act in time. Below I summarize what seem to me to be the points of greatest significance in this situation and this analysis. A more detailed examination of the facts, and a more extended analysis, is contained in a report on The Economic Situation at Midyear 1948, prepared for me by the Council of Economic Advisers, which I am transmitting to the Congress along with this Midyear Economic Report.

*Employment* in the first half of this year ran continuously above the level of a year ago. Some 850,000 workers were added to the labor force, yet unemployment in June was only 2.2 million—400,000 less than a year earlier. June civilian employment set a new record of 61.3 million.

*Industrial production* reached a new postwar peak in February and, after the work stoppage in coal mining, approached it again in June. Improved

industrial relations and high business confidence reinforced by increased Government commitments for foreign aid and defense give promise of continuing high-level output for the rest of the year.

*Agricultural production* ran below the level of the first half of last year because smaller numbers of livestock and tight feed supplies have reduced the output of most livestock products. At midyear, our second largest wheat crop was being harvested, and generally favorable crop reports were highlighted by an indicated production of over 3.3 billion bushels of corn—a new record. While such a crop could not remedy the meat shortage during the rest of this year, it would provide the basis for more ample supplies of livestock products in 1949 and thereafter.

*Gross national product* reached a new high of 246.5 billion dollars per year during the first half of 1948, reflecting some increase in production but mostly the rise in prices.

*Consumer income* ran at an annual rate of about 208 billion dollars, compared with 195 billion in 1947. Consumer income after taxes increased from a rate of 174 billion dollars to a rate of 186 billion.

*Consumer expenditure*, as a result of some buyer hesitation in the first quarter, increased less than disposable income, leaving a small increase in net consumer saving.

*The distribution of income*, according to the most recent data, has changed but little since 1946. A survey of families, however, showed half the Nation's consumer spending units falling substantially behind in the race of incomes with living costs during 1947. One-fourth of the family units spent more than they earned. Low-income people were spending past savings predominantly for current expenses, higher-income people more often spending theirs for durable goods or converting them into residential or business investments.

*Consumer credit* continued to expand during the first half of 1948.

*Business investment* took a larger share of the national output in the first half of 1948 than during 1947. Equipment outlays have been exceptionally high since the war; plant construction expenditures have increased less strikingly. Present indications are that such outlays will continue high throughout the rest of the year. Nonfarm inventories increased markedly during the first quarter of the year, when sales lagged, but leveled off in the second quarter as sales picked up.

*Profits* exceeded last year's average, reflecting high prices for a high volume of output. First quarter data, however, indicated a drop in profits of small manufacturing firms.

*Residential construction* is expected to increase the total supply of dwelling units by more than a million during 1948. This high output has

been accompanied by an increase in costs that is outrunning consumers' ability to pay for the housing they need.

*Net foreign investment*, at less than half the rate of the last quarter of 1947, in part reflected decreases in exports and increases in imports in our trade with all continents. The foreign aid program will increase our surplus of exports during the rest of the year.

*The Federal cash surplus* during the first half of 1948 amounted to 7.6 billion dollars. Receipts ran 7 percent higher than last year, payments 9 percent lower. The reduction in income taxes and the increase in expenditures for defense and foreign aid will virtually eliminate the surplus for the second half year. The Federal debt was reduced about 5 billion dollars during the first half of the year, bringing it down to 252 billion dollars.

*State and local government expenditures* have overtaken revenues, and deficits are likely to increase.

*Prices* rose after a decline in February. Many farm prices regained or surpassed their earlier levels and industrial prices resumed their climb. By midyear, price increases appeared to be accelerating. The index of consumers' prices has now reached an all-time high.

*Wages* continued the third round of increases that began last fall though interrupted by the break in commodity prices. Most of the third round increases have roughly corresponded to the rise in cost of living since the previous contract.

*Foreign aid and defense expenditures* during the present fiscal year will increase pressure on the domestic economy. New defense expenditures will not be great during the next few months, but will rise thereafter. Both programs have a special impact upon such short-supply items as steel, other metals, and farm machinery, and will draw increasingly upon our already fully employed labor force. More adequate allocation authority is needed if we are to avoid progressively more serious disruptive effects of these programs upon supplies, prices, and the organization of production.

*The reduction in income taxes* will reduce Federal revenues by about 5 billion dollars at the same time that expenditures will be substantially increasing under the new programs. The deflationary influence of recent Government cash surpluses will thus be replaced by the inflationary influence of additional expenditures on the part of consumers whose tax burdens are reduced.

*The general outlook as to inflation* shows conflicting influences. On the one side, the supply situation in a number of industries is improved over a year ago. Bountiful crops are in prospect. Postwar expansion programs are nearing completion in many lines of production, and we should experience a gradual increase in output from an enlarged and modernized

industrial plant. Commendable caution continues to be shown by business in avoiding speculative overexpansion, and many leaders in both industry and labor can be applauded for the conscious restraint they have exhibited in their pricing policies and wage demands.

The immediate situation is dominated, however, by three interacting processes making for continued inflation. First, consumer demand for goods and services, business demand for investment goods, and demands arising from expanding Government defense and foreign aid programs press strongly upon production. Second, we are currently in the midst of a round of substantial wage and price increases in major basic industries. These developments foreshadow continuing and ramifying effects on cost structures and prices in many related lines of production, on the cost of living, and on further wage demands. Third, credit expansion, partly a cause and partly a result of inflation, still persists.

The facts add up to a clear and disconcerting conclusion. In spite of some favorable factors, we are in the very midst of gathering inflationary forces, which day by day are imposing additional hardships upon countless families, and day by day are undermining the foundations of the remarkably high level of postwar prosperity that we have thus far maintained.

The hard facts of today leave no room for complacency. Though most people are optimistic about the immediate business outlook, lasting prosperity is not assured. Even in the midst of the present prosperity, the average American sees that the value of his accumulated savings has declined, and that many of his neighbors living on pensions or fixed salaries are actually worse off than they were a year ago. Looking abroad, we see that, despite great progress, many countries are still far below the living standards needed for sustained production and are dependent on outside help for any hope of further advance. We must be on our guard lest our national prosperity and security be undermined by inflation at home or by misery abroad.

Our American prosperity depends in part on world events, but far more on our own action or inaction right here at home. More than 90 percent of all the goods and services that we produce are for domestic purposes.

But thus far we have shown a blind disregard of the dangers that beset our path. Despite my repeated warnings and recommendations, we have not adopted adequate legislation for controlling inflation. The failure to control inflation effectively in the past makes it increasingly urgent that we adopt and apply vigorous measures to guide us safely from the uneven post-war boom to an era of sustained and stable prosperity.

We are now challenged to carry out the pledge to the American people contained in the Employment Act of 1946 that it shall be the policy of our Government to "utilize all its plans, functions, and resources \* \* \* to

promote maximum employment, production, and purchasing power," in an economy of free competitive enterprise.

It is no less important to take action to forestall a business collapse than it is to use Government measures to overcome a depression once it has arrived. Our success in this effort is essential for the reconstruction of a peaceful world.

# Recommended Program

(Excerpt from the President's Message to the Congress, July 27, 1948)

Positive action by this Government is long overdue. It must be taken now.

I therefore urge the Congress to take strong, positive action to control inflation. I have reexamined the anti-inflation program I proposed to the Congress 8 months ago. In its essentials that program is as sound now as it was then. It has been revised and strengthened in the light of changing circumstances. The program I now propose is as follows:

First, I recommend that an excess-profits tax be reestablished in order to provide a Treasury surplus and provide a brake on inflation.

Second, I recommend that consumer credit controls be restored in order to hold down inflationary credit.

Third, I recommend that the Federal Reserve Board be given greater authority to regulate inflationary bank credit.

Fourth, I recommend that authority be granted to regulate speculation on the commodity exchanges.

Fifth, I recommend that authority be granted for allocation and inventory control of scarce commodities which basically affect essential industrial production or the cost of living.

Sixth, I recommend that rent controls be strengthened, and that adequate appropriations be provided for enforcement, in order to prevent further unwarranted rent increases.

Seventh, I recommend that stand-by authority be granted to ration those few products in short supply which vitally affect the health and welfare of our people. On the basis of present facts, and unless further shortages occur, this authority might not have to be used at all.

Eighth, I recommend that price control be authorized for scarce commodities which basically affect essential industrial production or the cost of living. I have said before, and I repeat, that many profit margins have been adequate to absorb wage increases without the price increases that have followed. Rising wages and rising standards of living, based on increasing productivity and a fair distribution of income, is the American way. Noninflationary wage increases can and should continue to be made

by free collective bargaining. Where the Government imposes a price ceiling, wage adjustments which can be absorbed within the price ceiling should not be interfered with by the Government. The Government should have the authority, however, to limit wage adjustments which would force a break in a price ceiling, except where wage adjustments are essential to remedy hardship, to correct inequities, or to prevent an actual lowering of living standards.

The measures I have recommended make up a balanced program to attack high prices. They are all necessary to check rising prices and safeguard our economy against the danger of depression. If they are made the first order of business by the Congress, as they should be, they can be promptly enacted. Every week of delay will mean additional hardship for the American people.