Chapter 2

Economic Developments in 1959

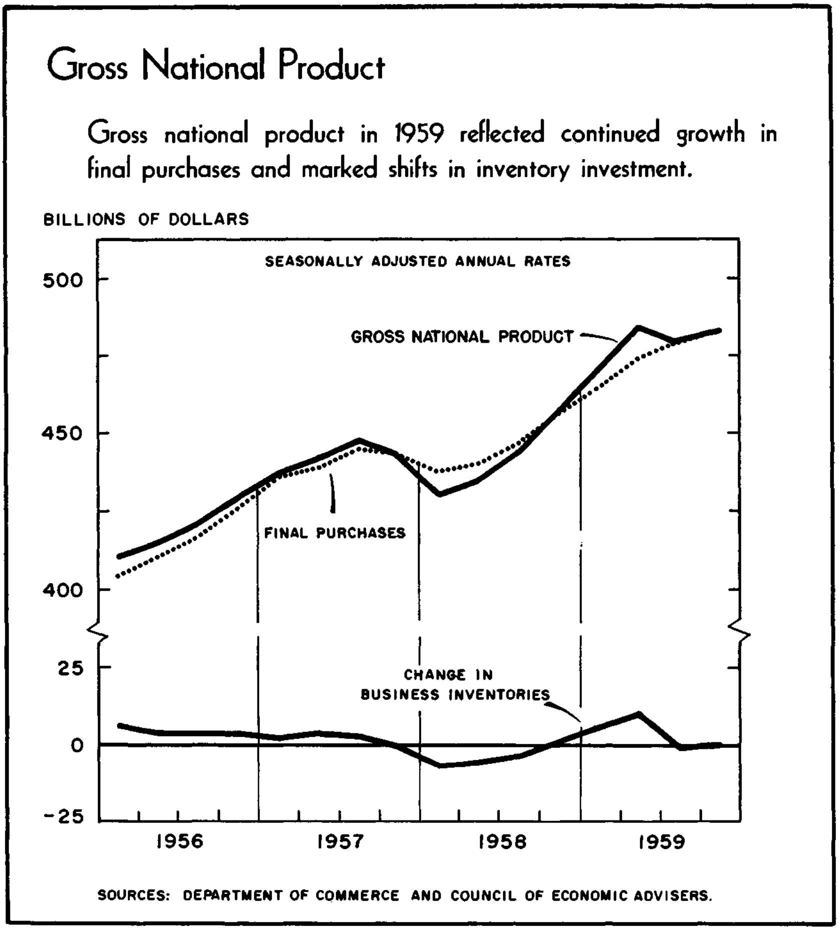
THE ECONOMIC RECOVERY in the United States that started early in 1958 carried production and incomes to new high levels by the first quarter of 1959. The Nation's output, in terms of the physical volume of goods and services, surpassed its previous peak. The flow of income payments also exceeded the previous record, and civilian employment, though still below the high reached in the second quarter of 1957, was 1.2 million greater than in mid-1958, after seasonal adjustments.

These advances were extended into 1959, though economic activity was sharply affected by the 116-day steel strike which began on July 15. Developments in the steel industry had first an expansive, and then an increasingly contractive, effect. Anticipatory purchases of steel and products of steel quickened the advance in the Nation's output in the first half of the year, but led to a drop in gross national product in the third quarter, as about 85 percent of steel capacity was idled and the output of steel-using products had to be sustained in the main out of previously produced steel supplies. Still, by the end of the year, the Nation's aggregate output amounted to $482 billion, on an annual rate basis; employment had risen to 66.2 million (seasonally adjusted), the highest in the Nation's history; and personal income was being received at the rate of $391 billion a year, 5 percent (adjusted for price changes) higher than in the last month of 1958.

Expansion of Output

The rapid rise in general economic activity already in progress as 1959 began raised output to $484.5 billion in the second quarter of the year (Chart 1). This exceptionally rapid expansion reflected not only the abnormal demand for inventories induced by the expectation of a steel strike, but also a substantial, continuing increase in the final demand for goods and services. To a certain extent, these two factors reinforced one another, but increasing outlays by business concerns on plant and equipment, rising expenditures on residential construction, and increased purchases of durable goods by consumers had significant independent effects in stimulating the expansion of production, employment, and income.

CHART 1



The shift between early 1958 and mid-1959 in the inventory policies of business had a marked economic effect. Inventory accumulation began in the latter part of 1958, following a full year of liquidation. It quickened during the first half of 1959, as business firms replenished their stocks of materials and finished goods to meet rising operating needs; and it became especially rapid in the second quarter of the year as businesses sought to assure continuance of their operations in the event of an interruption of steel production. Approximately one-third of the inventory accumulation in the second quarter was attributable to increased holdings of steel mill products. And inventory accumulation alone was equal to one-third of the rise in gross national product from the 1958 recession low to the 1959 high.

The advance in final purchases of goods and services which began in the second quarter of 1958 also reached a peak rate in the second quarter of 1959. Virtually all the main categories of final purchases increased. Improved investment opportunities, supported by higher business earnings and retained income, provided a basis for increased business outlays on plant and equipment. These rose by about 10 percent, from a seasonally adjusted annual rate of $33.4 billion in the fourth quarter of 1958 to $36.6 billion in the second quarter of 1959 (Table D–8). Within nonfarm business investment outlays, expenditures on equipment moved forward somewhat more swiftly, rising approximately 14 percent from the end of 1958 to mid-1959. But nonresidential construction grew at a slower rate, as substantial expenditures for public utility and commercial projects were partially offset by a decline in factory building. Residential construction, on the other hand, rose rapidly in the early months of 1959. The public sector of the economy provided a moderately expansive impetus to aggregate output. State and local purchases of goods and services continued to rise, while those of the Federal Government remained stable. Net exports were the single contractive factor among the major components of national output, declining from $0.2 billion at the close of 1958 to minus $1.8 billion (on a national accounts basis) in the second quarter of 1959.

The underlying strength in these categories of final purchases of goods and services helped bring about a rise in employment and income, and consumers responded by expanding their outlays substantially. A further rise of income incident to the production of goods to meet abnormal inventory needs, particularly in the second quarter, also helped to swell consumer incomes and spending. And consumer confidence, reflected in high personal borrowings, brought particular strength to purchases of durable goods.

Economic developments in the second half of the year were also greatly affected by the inventory factor. In this case, however, it exerted, on balance, a pronounced contractive influence. Largely reflecting reductions of holdings by manufacturers and retail dealers affected by the steel strike, inventories—which had been accumulated at an annual rate of $10.4 billion in the second quarter—were reduced by $1 billion in the third quarter. This reduction was the dominant economic force in that quarter. Although making possible a continued though less pronounced increase in final purchases, the drawing down of inventories incident to the stoppage in steel production resulted in a rather sharp drop—$6 billion—in gross national product. During the fourth quarter of the year, deficiencies and imbalances of steel inventories moderated the growth of final purchases, despite the resumption of steel production in November. As a result, the increase in gross national product (GNP) was limited to $3.4 billion, and most of the recovery in economic activity expected after the strike was postponed beyond the end of the year. Nevertheless, GNP in the fourth quarter was nearly $25 billion (annual rate) above the level in the fourth quarter of 1958.

Divergent movements in the second half of the year in the major components of national output reflected, in part, the impact of steel shortages. Sales of consumer durable goods, which had been rising rapidly, fell as demands could not be fully met. New construction expenditures, which had been very high in early 1959, decreased noticeably, though part of this decline may have reflected the increased competition for funds arising in other sectors of the economy. On the other hand, purchases of consumer nondurable goods and services and of producer durable equipment, and purchases by State and local governments continued to advance in the second half of the year. And net exports of goods and services, which had been a contractive influence before midyear, became moderately expansive.

Employment and Income

The gains in employment and earnings that followed the upturn of the economy in 1958 were extended at a rapid rate into 1959. By January, the average length of the manufacturing workweek had increased to 40.1 hours (seasonally adjusted), from a recession low of 38.7 hours. Total civilian employment had risen by more than 1 million (seasonally adjusted) from its cyclical low, and unemployment had been reduced from the recession high of 7½ percent of the civilian labor force to 6 percent.

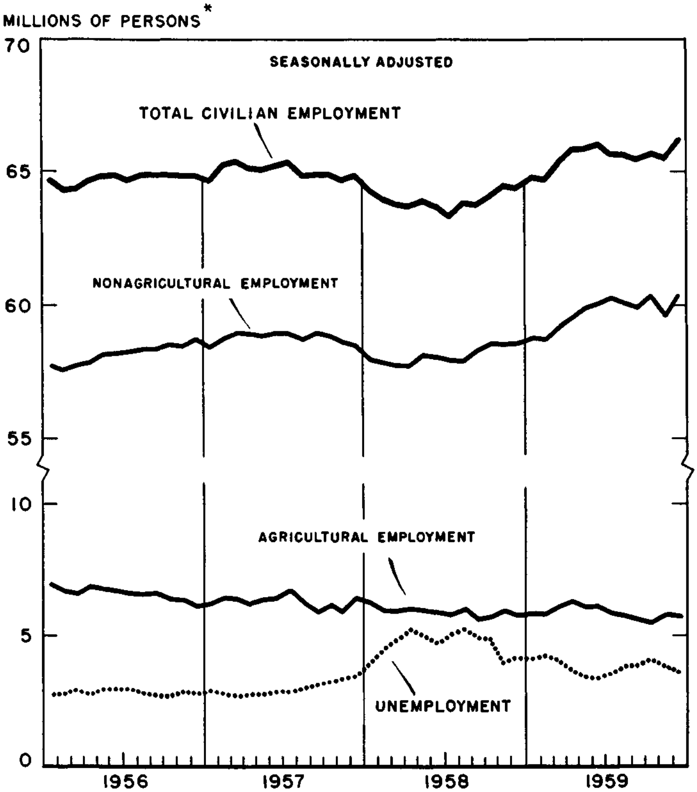
As the year advanced, economic expansion brought about increasingly heavy demands for labor. The average length of the workweek in manufacturing industries advanced to 40.7 hours in April, the highest since April 1956, and the average amount of overtime for production workers increased rapidly, to almost 3 hours a week in June. Longer workweeks and increased overtime were the rule also in most nonmanufacturing industries.

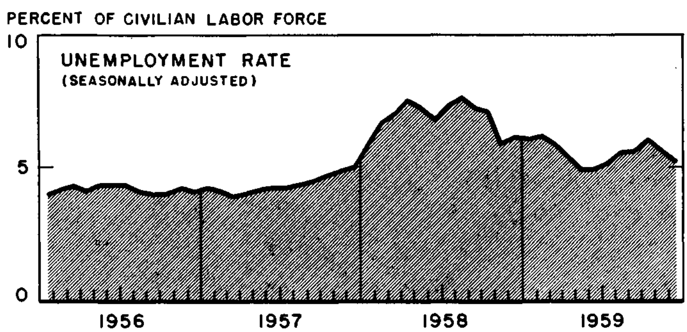
Unemployment changed very little during the early months of 1959, because the expansion in employment was nearly matched by the growth of the labor force. But in the early spring, as production reached record levels, the number of employed persons rose swiftly, exceeding the growth in the labor force, and unemployment declined. Total nonfarm employment expanded by nearly 1.3 million (seasonally adjusted) in the four months from February to June 1959, and unemployment was reduced by 750,000. By midyear, unemployment had fallen to about 5 percent of the labor force; long-term unemployment—the number of individuals seeking work for 15 weeks or more—was 1 million below its recession high of nearly 2 million; unemployment among men 25 years of age and over was sharply below that in 1958; and the unemployment rate for family men in June 1959 was 2.7 percent, likewise far below its recession high. Nevertheless, these unemployment rates were above those prevailing prior to the 1957–58 recession, and unemployment remained comparatively high, especially for persons lacking work experience, for mining employees, and for nonwhite persons. However, total unemployment was being reduced at a rapid rate until the trend was reversed in July by the beginning of the steel strike (Chart 2).

CHART 2

Employment and Unemployment

Employment increased and unemployment fell until July 1959. These trends were interrupted by the steel strike but resumed after its end.





*14 YEARS OF AGE AND OVER.

SOURCE: DEPARTMENT OF LABOR.

After some 500,000 employees in the steel industry went on strike on July 15, nearly 100,000 other persons were soon laid off in related industries, especially in mining and rail transportation. Even though substantial inventories of steel had been accumulated by many firms, stocks were being depleted rapidly by mid-October and serious imbalances were making themselves felt. As a result, layoffs became increasingly heavy. By the time steel production was resumed on November 7, under a Federal court injunction, employment in steel-related industries had declined by more than 500,000, exclusive of the number on strike. In most other industries, employment ceased to advance during this period, and in October the rate of unemployment increased to 6.0 percent of the civilian labor force.

The resumption of steel production brought an increase in employment by the end of the year, and unemployment was again reduced. Although the replenishment of working stocks of steel could not be accomplished immediately, total employment reached 66.2 million (seasonally adjusted) in December, slightly above the record of 66.0 million that had been attained in June. Unemployment in December was 3.6 million (seasonally adjusted), or 5.2 percent of the labor force.

The employment situation in areas of heavy labor surplus was improved significantly by the economic advance of 1959. Although in November 1959 there were 29 major continental labor markets where unemployment exceeded 6 percent of the labor force, the number of such areas was far below the peak of 86 reported in July and September of 1958. And by November 1959, unemployment had fallen below the 3 percent level in 27 major areas. Also, most labor market areas, regardless of their over-all unemployment situation, experienced shortages in 1959 of certain types of workers, notably professional, technical, clerical, and skilled.

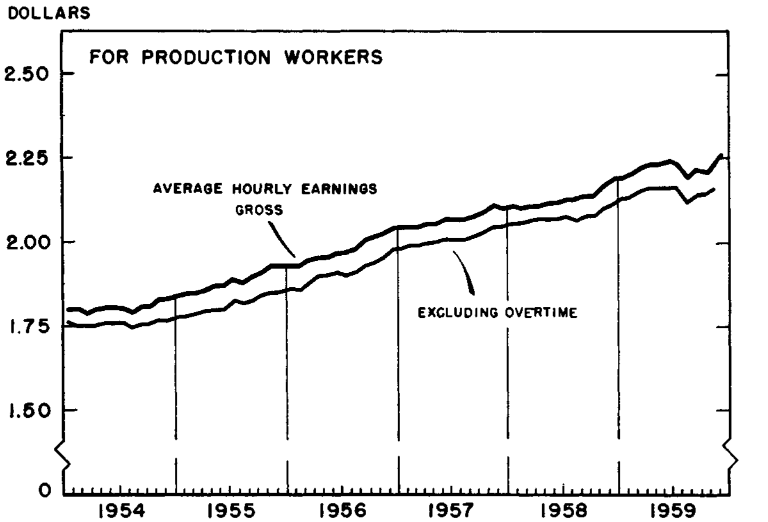
The improving employment situation was reflected in substantial gains in personal income. In the early months of 1959, higher hourly wage rates supplemented the effects of longer workweeks and more extensive overtime employment on average weekly earnings (Chart 3). Wage rates in manufacturing industries advanced in the first six months of the year by about 2 percent, on the average. On an annual rate basis, this gain was about the same as the increases in 1957 and 1958. Average weekly earnings for workers in these industries were 4.5 percent higher in the first six months of 1959 than in the last six months of 1958. In nonmanufacturing industries, also, earnings of workers increased. Despite the fact that the advance of weekly earnings and employment was interrupted by the strike in the second half of the year, wage and salary payments in the fourth quarter exceeded payments a year earlier by $16.4 billion, or 6.7 percent.

Other forms of personal income, not as large in dollar terms as wages and salaries—personal interest, dividends, incomes of nonfarm proprietors (including self-employed professional persons), and transfer payments—also rose above their levels at the end of 1958. Rental income increased slightly, while the income of farm proprietors declined. The aggregate of

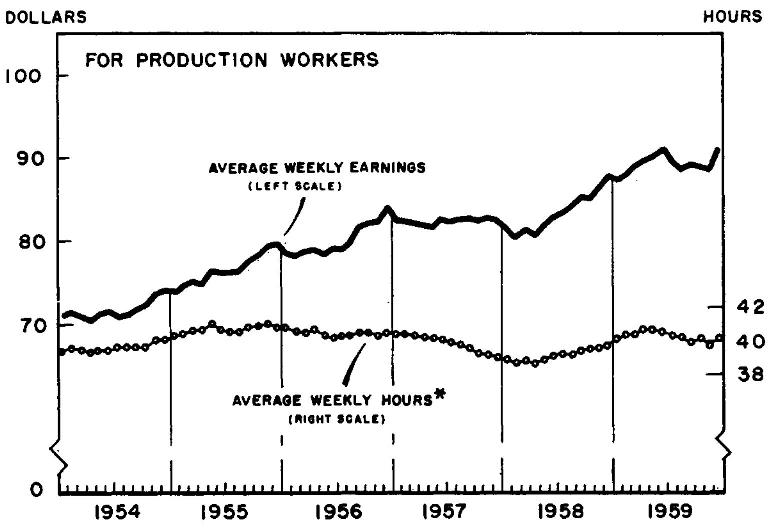
CHART 3

Hours and Earnings in Manufacturing

Hourly earnings were much higher in 1959 than in 1958, as wage rates continued to rise and overtime became more common.



Weekly earnings increased rapidly until the steel strike, reflecting longer workweeks and higher hourly earnings.



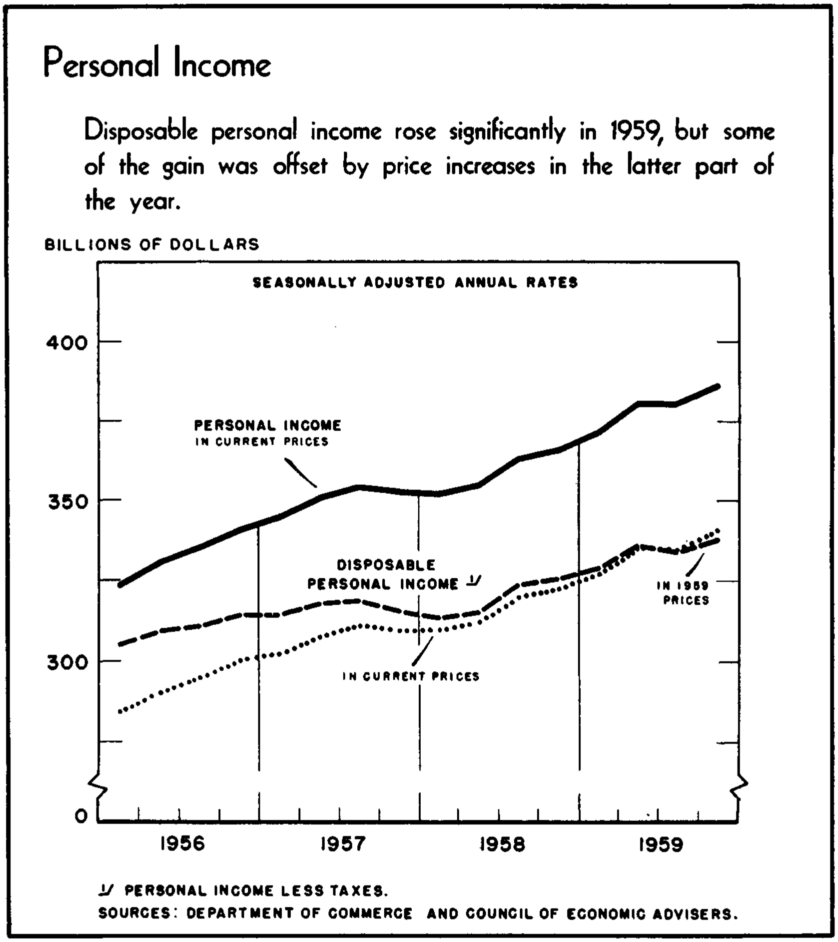
* SEASONALLY ADJUSTED.
SOURCES: DEPARTMENT OF LABOR AND DEPARTMENT OF COMMERCE.

all these income payments—total personal income—rose by $20.3 billion, or 5.5 percent, and the amount of income available for spending and saving after the payment of personal income taxes—disposable personal income—increased at the same rate.

Since prices were relatively stable in much of the first half of the year, the increases in disposable income were reflected almost entirely in increases in real income. In the next six months, however, part of the gain was offset by increases in prices. Over the year as a whole, per capita disposable income, in dollars of constant purchasing power, increased by 2.2 percent (Chart 4).

Personal savings, which had expanded earlier in the recovery period, leveled off in the first half of 1959 as consumer expenditures on goods and services rose by about as much as disposable income. In the final six months, as consumption continued to rise in the face of a much slower

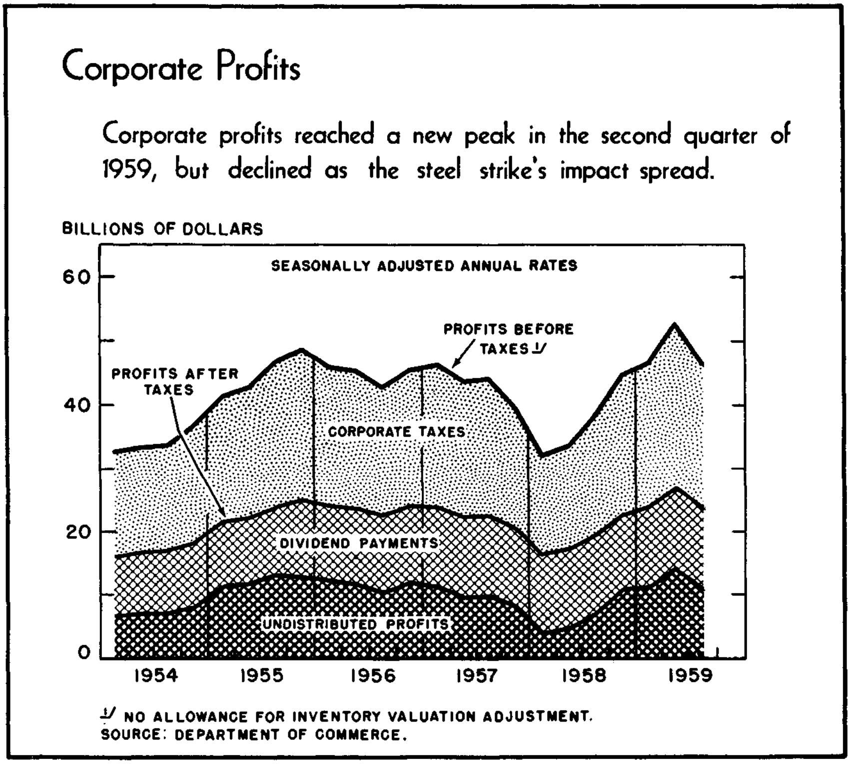
CHART 4



growth in personal incomes, the share of disposable income that was saved fell to about 6.7 percent, the lowest since early 1956. This decline was reflected both in a less rapid addition to most financial assets of individuals and in a more rapid expansion of personal borrowings.

Corporate profits, which are especially sensitive to fluctuations in business activity, expanded in 1959 in response to the increase in production and improvement in profit margins. By the second quarter, earnings (before taxes) reached a record figure of nearly $53 billion—$19 billion more than in the second quarter of 1958, when they had been severely depressed. Subsequently, they declined as the steel strike caused a curtailment of activity, and were about the same as in early 1959 (Chart 5).

CHART 5



Dividends did not match the rapid advance of profits after taxes for the year ended in mid-1959; accordingly, retained earnings recovered sharply. Together with the continued growth in funds generated through depreciation allowances and rapidly rising tax accruals, these retained earnings made it possible for corporations to acquire a substantial volume of United States Government securities in the first half of 1959, while at the same time increasing their outlays for inventory and for plant and equipment.

The impact of rising economic activity was clearly evident in credit and capital markets in 1959. Inventory accumulation in the early part of the year, the resurgence in consumer spending on durable goods, and a high level of construction activity combined to produce a heavy demand for commercial bank credit. Reflecting these demands, bank loans expanded almost $12 billion, about the same as the record increase in 1955. However, Federal Reserve policy made possible only a small expansion in total bank assets, and banks financed about $8 billion of their loan expansion through sales of United States Government securities. The financial markets were under considerable pressure in absorbing these security sales, since they were also financing the Treasury deficit and meeting substantial demands for funds from mortgage borrowers, State and local authorities, and corporations; and interest rates, particularly in the short-term and medium-term range, advanced sharply.

The distribution of the increase in bank credit among the major users largely reflected the character of the year's advance in economic activity (Table 1). The growth in both consumer loans and real estate loans of

TABLE 1.—*Net changes in commercial bank holdings of loans and investments, 1954–59*

[Billions of dollars]

Loans and investments	1954	1955	1956	1957	1958	1959 [1]
Loans (excluding interbank) and investments [2]	10.2	4.6	4.2	4.9	15.1	3.4
Loans (excluding interbank) [2]	2.9	11.6	7.6	3.5	4.3	11.7
Business	−.3	6.4	5.5	1.8	−.1	5.3
Real estate	1.7	2.4	1.7	.6	2.1	2.5
Consumer	(3)	2.3	1.4	1.2	.2	2.5
Security	.9	.6	−.8	−.1	.4	(3)
Agricultural	.2	−.7	−.3	−.1	.9	−.2
All other	.6	.9	.4	.3	1.0	1.4
Investments	7.2	−7.0	−3.5	1.3	10.8	−8.4
U.S. Government securities	5.6	−7.4	−3.0	−.3	8.1	−8.1
Other securities	1.6	.4	−.4	1.7	2.6	−.3

[1] Preliminary estimates by Council of Economic Advisers; excludes Alaska and Hawaii and other bank structure changes.
[2] Total loans are net of, and individual loans are gross of, valuation reserves.
[3] Less than $50 million.

NOTE.—See Table D-41 for data including interbank loans. Detail will not necessarily add to totals because of rounding.

Source: Board of Governors of the Federal Reserve System (except as noted).

commercial banks appear to have exceeded the high rates of 1955. The expansion of business loans up to the middle of the year was comparable to that of 1955, but the liquidation of inventories after midyear reduced this use of bank funds considerably below the amounts extended in 1955. Nevertheless, the business lending activity of banks was markedly greater than in 1958, as most major groups of commercial and industrial businesses employed more bank credit.

Not only was consumer lending by banks at a record rate, but so was the over-all increase in consumer credit outstanding (Chart 6). All major categories of instalment credit other than that extended for the purchase of automobiles rose more than in 1955. Contrary to the developments in that earlier year, however, there appears to have been no appreciable liberalization in 1959 of the maximum terms on which instalment credit was made available to consumers.

Long-term capital markets were subject to divergent influences but, on balance, experienced larger demands. Corporate security offerings for new money were lower than in 1958 by abount $1.5 billion, or 15 percent, as a result of the sharp increase in corporate retentions of income and the greater reliance on bank borrowing. The latter reflected the predominantly short-term nature of business financing requirements in this period and, possibly, the high level of long-term interest rates prevailing. However, the reduction in corporate offerings was more than offset by the flow of credit into home building. The amount of nonfarm residential mortgage credit in use increased by a record $15 billion, compared with an increase of $12 billion in 1958. State and local security issues exceeded those in any previous year, as new authorizations of State and local securities continued to build up a large backlog of issues.

The credit markets were also required to supply funds associated with an increase of $7.9 billion in United States Government debt and to absorb outside of the banking system the $8 billion reduction, referred to above, in bank holdings of United States securities. Most of the new issues of Federal securities were obligations of short- and intermediate-term maturity, because the 4¼ percent interest rate limitation effectively precluded flotations of longer-term United States Government securities after the early part of the year. Hence, the Federal Government was forced to do much of its needed financing in the same maturity range in which commercial banks were reducing their holdings of Government obligations.

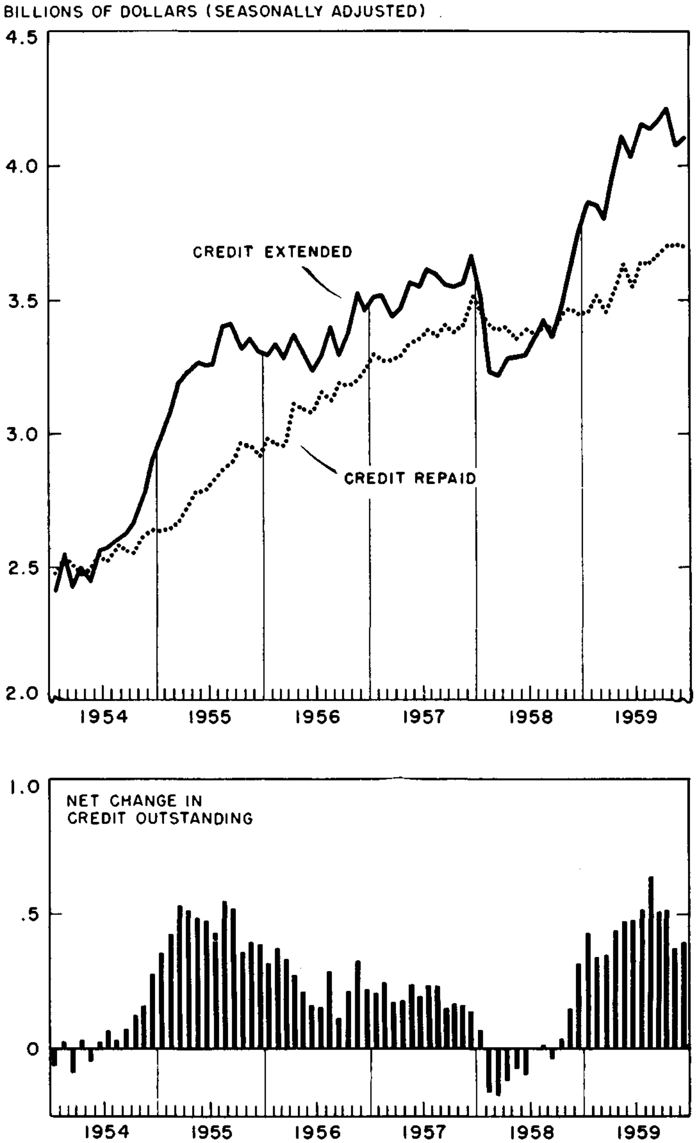
Investment sources outside the commercial banking system absorbed the new offerings of Federal securities, as well as bank sales of short- and intermediate-term Federal obligations, but at a substantial increase in rates. Nonfinancial corporations expanded their holdings by $5 billion (Table D–49), mostly in very short-term securities; foreign and international accounts, savings and loan associations, and individuals likewise added to their portfolios.

These developments in the banking system and in capital markets, jointly with the policies pursued by the monetary authorities, had significant effects on the financial position of the major lending institutions and of nonfinancial businesses and individuals. The liquidity position of commercial banks, as measured by the ratio of their holdings of United States securities to deposits, was at about its postwar low, and the cash and

CHART 6

Consumer Instalment Credit

The amount of consumer instalment credit outstanding rose substantially in 1959, as extensions increased much more rapidly than repayments.



NOTE: SEE APPENDIX TABLES D-44 AND D-45.
SOURCE: BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM.

United States Government security holdings of insurance companies, mutual savings banks, and savings and loan associations declined relative to their respective liabilities.

For the economy as a whole, holdings of liquid assets increased only moderately, though there were significant differences among the components of the total. The money supply expanded by about 0.5 percent. Time deposits of commercial banks advanced by 3½ percent and mutual savings bank deposits by 4 percent, rates of increase that were appreciably lower than in recent years. The volume of outstanding Series E and Series H savings bonds, including accrued interest, leveled off early in the year, and then declined; however, the decline was reversed after a new rate of 3¾ percent was announced for these bonds and the total at the end of the year was almost the same as at the beginning. Total savings bonds, which include other series not currently being sold, decreased by about $3 billion during the year, though this decline partly reflected advance refunding into marketable securities. Savings and loan share accounts rose by 14 percent, about the same as in 1958. The decline in the rate of increase in savings-type liquid assets reflected the failure of personal savings to keep pace with disposable income, as well as a shift of the flow of savings into less liquid assets. On the other hand, the volume of marketable United States Government securities with maturities of less than one year increased by about $7 billion, or 10 percent, contrasted with a small decline in 1958.

The advance in the cost of borrowing in 1959, though less steep than in the second half of 1958, continued through most of the year. The 13-week Treasury bill rate rose from 2.7 percent to more than 4.5 percent. The prime rate of commercial banks was raised in two stages, from 4 percent to 5. The average yield on outstanding long-term taxable Government bonds increased from about 3.8 percent to 4.4, while that on outstanding corporate Aaa bonds rose from 4.1 percent to 4.6. It is estimated that the yield on FHA-insured home mortgages purchased in the secondary market rose from around 5.6 percent to about 6.3.

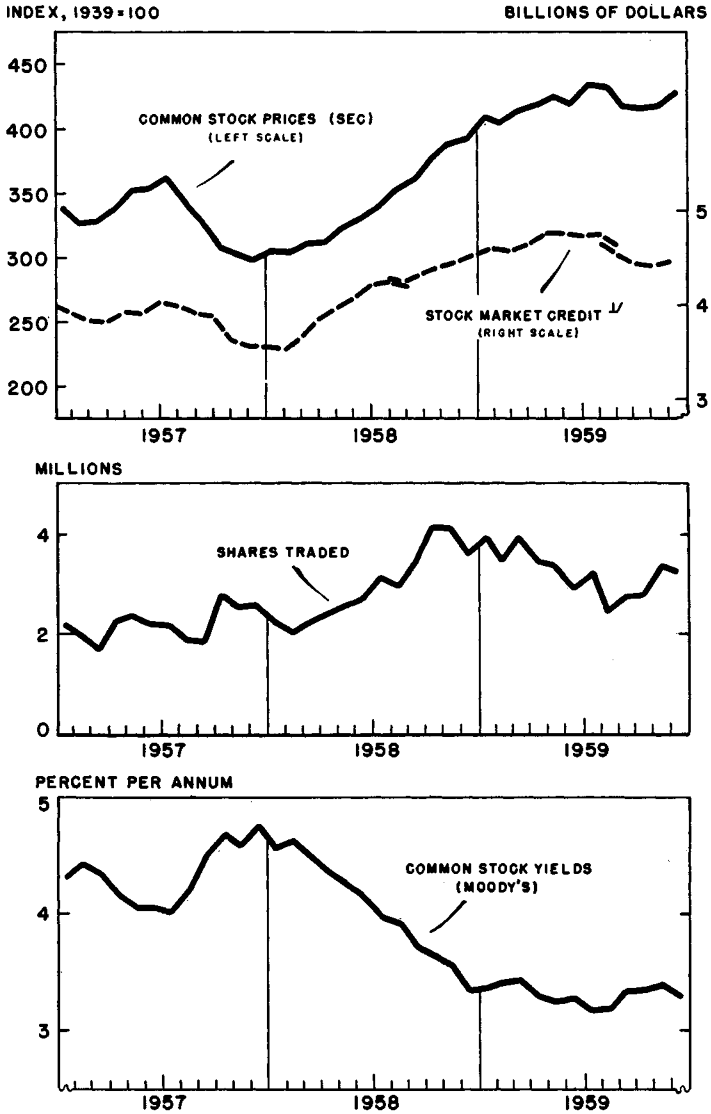
A significant development was the considerably more rapid advance in short- and intermediate-term interest rates than in long-term rates. The change in this relationship was such that short- and intermediate-term borrowing, on which the Federal Government was compelled to rely because of the 4¼ percent limitation on its new issues of longer-term securities, became considerably more expensive than long-term borrowing.

The exuberance that characterized the stock market in 1958 gave way to a more restrained tone in most of 1959. Stock prices advanced about 9 percent, and the amount of credit used in stock market transactions varied little during the year (Chart 7). Since dividends increased at about the same rate as stock prices, the average yield on common stocks remained at

CHART 7

Stock Prices and Yields

Stock prices rose more slowly in 1959 than in 1958. Yields fluctuated within a narrow range.



1/ END OF MONTH. SEE APPENDIX TABLE D-63 FOR EXPLANATION.

SOURCES: SECURITIES AND EXCHANGE COMMISSION, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, NEW YORK STOCK EXCHANGE, AND MOODY'S INVESTORS SERVICE.

about the 3¼ percent level that prevailed in the last few months of 1958. The margin between the yield on outstanding long-term United States Government securities and the yield on common stocks continued to widen as interest rates in general advanced.

PRICES

The stability of the consumer price index that prevailed from the spring of 1958 through the first five months of 1959 was followed by an upward movement in the succeeding months. By November, the index was 1.5 percent higher than at the end of the previous year (Table 2).

TABLE 2.—*Changes in consumer price index in 1959*

Item	Relative importance December 1958 (percent) [1]	Percentage change		
		December 1958 to May 1959	May 1959 to November 1959	December 1958 to November 1959
All items	100.0	0.2	1.3	1.5
Commodities	64.8	−.3	1.1	.8
Food	28.7	−.8	.2	−.7
Food at home	23.9	−1.4	−.1	−1.5
Commodities less food	36.1	.1	1.7	1.8
Nondurable commodities	22.5	.4	2.0	2.4
Apparel	8.7	−.3	2.0	1.7
Footwear	1.5	2.4	4.3	6.7
Durable commodities	13.6	−.2	1.2	1.1
Cars, new	3.1	−3.3	3.9	.5
Cars, used	1.7	3.0	3.3	6.4
Durables less cars	8.8	.2	.0	.2
Appliances [2]	3.1	.0	.4	.4
Services	34.4	1.2	1.7	2.9
Rent	6.2	.4	.9	1.3
All services less rent	28.2	1.3	1.8	3.1

[1] Weights do not add to 100 because the miscellaneous category, not actually priced but imputed, is omitted.
[2] Includes household appliances, radios, and television sets. Comparisons are for December 1958 to June 1959 and June to September 1959.

Source: Department of Labor.

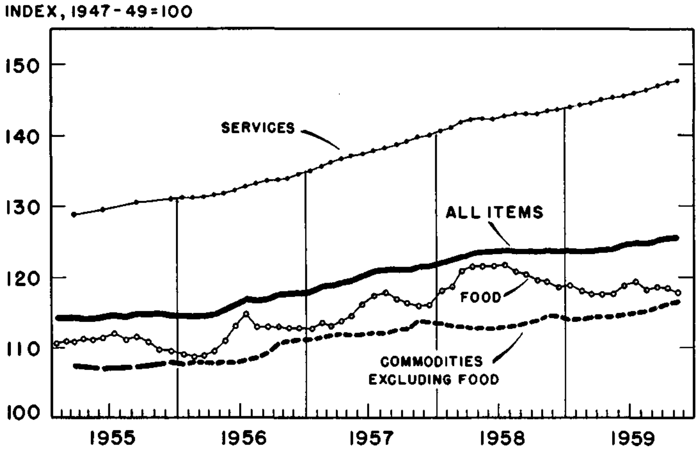
Continuing declines in food prices during the early months of the year offset increases in the prices of consumer services and small advances in the prices of nondurable goods other than food. Prices of consumer durable goods changed little in this period. After late spring, however, food prices fluctuated within a narrow range, primarily in response to seasonal and weather factors, whereas the prices of nondurable commodities (exclusive of food) and of consumer services rose at an increased rate. Accordingly, the over-all index began to rise and continued upward almost without interruption through the end of the year, though at a slower rate than in the corresponding months of 1956 and 1957 (Chart 8).

The index of wholesale prices changed very little in 1959, but divergent trends among its components (Table 3 and Chart 9) are significant for

CHART 8

Consumer Prices

The 1959 rise in the consumer price index was largely due to higher prices of services. Food prices fell but other commodity prices rose moderately.



SOURCE: DEPARTMENT OF LABOR.

the current movement of consumer goods prices and possibly also for future changes in the cost of living. Declines in wholesale prices of a number of farm products and processed foods brought reductions in retail prices of food during the year. Sizable reductions in pork prices reflected a cyclical expansion in hog production; and at the year-end, beef prices, which for most of 1959 had been higher than in 1958, also showed a moderate decline. A sharp increase in supplies exerted downward pressure on poultry and egg prices during the year. At the same time, higher wholesale prices of wool and hides and skins, and a pronounced rise in the prices of intermediate wool and leather products, were major factors in the 2 percent increase in the retail prices of apparel. In the latter part of the year, hide prices declined and a large cotton harvest, in combination with somewhat lower price supports, helped to moderate the rising trend in prices of textiles and apparel.

Prices of crude and semifinished materials and other items important in the manufacture of durable goods rose during 1959, though there was some diversity in their behavior. Prices of steel mill products, which had risen significantly in the second half of 1958, remained substantially unchanged in 1959, as did wholesale prices of consumer finished durable goods. Prices

TABLE 3.—*Changes in wholesale price index in 1959*

Item	Percentage change		
	December 1958 to June 1959	June 1959 to December 1959	December 1958 to December 1959
All commodities	0.4	−0.7	−0.3
Crude materials for further processing [1]	1.1	−4.8	−3.7
Crude foodstuffs and feedstuffs	.3	−7.4	−7.1
Crude nonfood materials, except fuel, for manufacturing	2.9	−1.7	1.2
Crude fuel	−2.6	4.6	1.9
Intermediate materials, supplies, and components [1]	.6	.2	.8
Intermediate materials for food manufacturing	−.9	−2.5	−3.4
Intermediate materials for nondurable manufacturing (excluding food)	2.2	.2	2.4
Intermediate materials for durable manufacturing	1.2	.2	1.4
Components for manufacturing	1.0	.3	1.3
Materials and components for construction	2.4	−.4	2.0
Finished goods	.0	−.3	−.3
Consumer foods	−1.9	−1.9	−3.7
Consumer other nondurable goods	.5	.9	1.4
Consumer durable goods	.5	−.4	.1
Producer finished goods	1.0	.1	1.1
Special group: Steel mill products	−.1	.1	.0

[1] Total for this group includes some items not shown separately.

Source: Department of Labor.

of semifinished aluminum products were stable over most of this period, but price increases were announced at the end of the year. Primary nonferrous metals as a group, and the corresponding semimanufactured products, advanced in price, especially during the final months.

Materials of importance for construction became somewhat more expensive in 1959. By late spring, lumber prices were 12 percent higher than a year earlier, but they receded in the autumn, reflecting a lower rate of home building and seasonal factors in lumber production. Other building materials, particularly those used extensively in nonresidential construction, displayed mixed price trends.

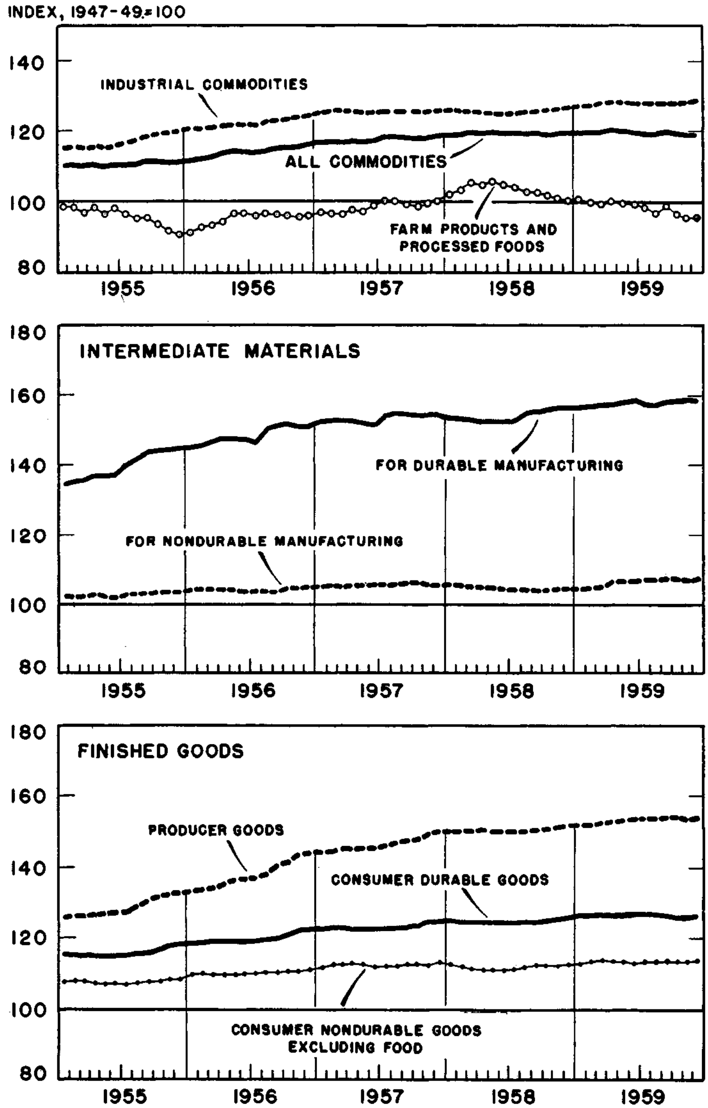
The wholesale price index of producer finished goods, including electrical, metalworking, and general purpose machinery and equipment and related capital goods, advanced in 1959, extending a rise that had begun in Septmber 1958. Including the 1959 increase, the index of these prices has risen almost 25 percent since August 1954. Such a development, unless offset by commensurate increases in operating efficiency, has important consequences for the prices of consumer goods since, in due course, the costs of capital equipment influence retail prices. Foreign trade of the United States could also be affected adversely by these price advances, since machinery accounts for about one-fourth of the country's total exports.

The fact that 1959 and 1955 marked somewhat similar phases in the business cycle suggests a comparison between price developments in these two years. In 1955, the consumer price index remained fairly stable, but substantial cost increases became noticeable as the year progressed. These

CHART 9

Wholesale Prices

The index of wholesale prices was stable in 1959. Declines in farm product prices offset some increases in industrial prices.



SOURCE: DEPARTMENT OF LABOR.

made themselves felt to an extent through price rises at wholesale of such items as building materials, steel, nonferrous metals, and natural rubber, and foreshadowed the consumer price rise that began after the spring of 1956. In 1959, events followed a somewhat different course. Wholesale prices of intermediate materials for durable goods manufacturing advanced, as a group, but at a much slower rate than in 1955, especially after midyear. The corresponding group of materials for nondurable goods manufacturing (food excluded) showed somewhat larger wholesale price increases last year than in 1955; but, significantly, most of the increase in 1955 occurred after June, while in 1959 the index increased scarcely at all over the second half of the year as several important materials declined from earlier levels. On balance, rising costs of materials last year exerted less upward pressure on the prices of finished manufactured goods than they did in 1955, even if the influence of foods is excluded. This is reflected in the fact that the wholesale price index for industrial products rose only about 1 percent in 1959, compared with more than 4 percent in 1955. The contrasting behavior of consumer prices in these two periods is largely explained by the more rapid rise last year in the prices of consumer services and by the fact that prices of consumer durable goods declined in 1955 but were for the most part unchanged in 1959.

Agriculture

Agricultural output in 1959, including a very large harvest of corn and a continued rise in the production of livestock, equaled the high 1958 volume and was 25 percent above the average output of 1947–49. Although per capita food consumption rose to near-record levels, the full volume of this output could not be absorbed by total domestic and export demands at prevailing prices, some of which are supported under provisions of law, and carryover stocks of several price-supported crops continued to increase. An especially large increase in carryover stocks of corn is in prospect from the 1959 harvest. On the other hand, wheat may account for only a small addition to stocks, and an increase in the carryover of cotton may be avoided in the new marketing year.

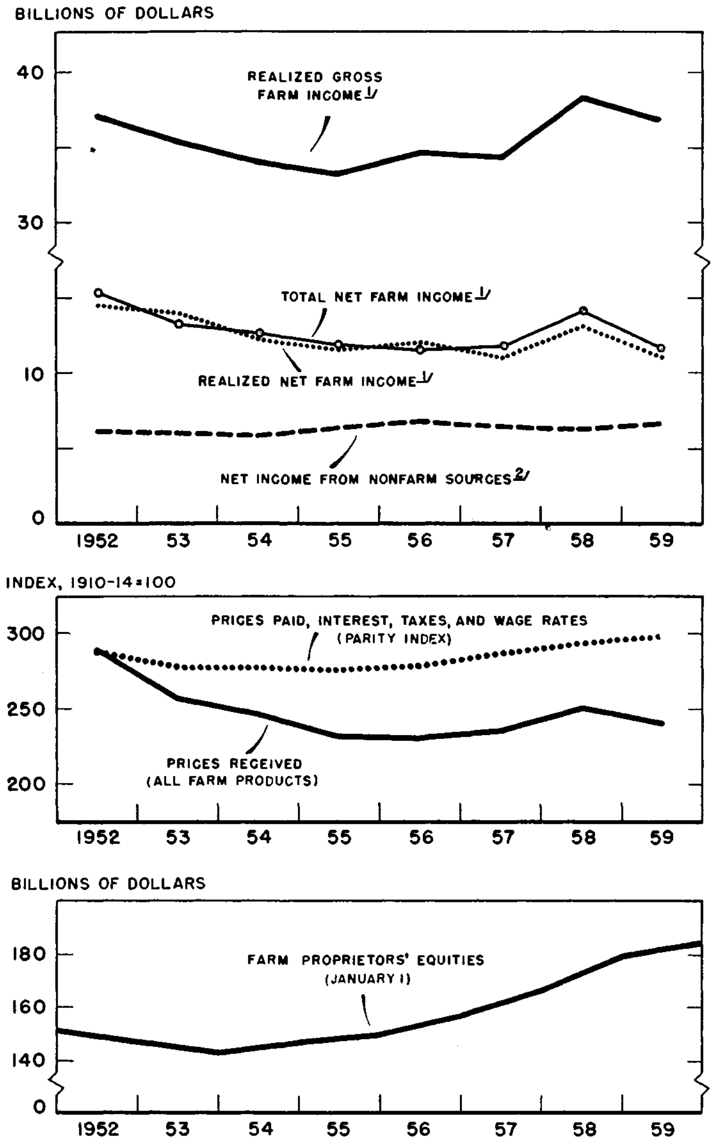
This imbalance between production and commercial demand was also reflected in the lower prices received by farmers in 1959, compared with 1958. Most of the reduction was in prices of livestock and livestock products; crop prices averaged nearly as high as in 1958. Declines in prices of hogs, poultry, and eggs were especially sharp. However, a substantial part of the decrease in livestock prices during 1959 was directly traceable to a cyclical increase in the production of beef cattle and hogs, which had been in short supply in 1958 and for which prices had been unusually high. Among crops, price reductions in 1959 were largely confined to wheat and fruit and oil-bearing crops.

In 1959, the realized net income of farm operators from farming fell back from $13.1 billion in 1958 to the 1957 level of $11.0 billion (Chart 10).

CHART 10

Indicators of Agricultural Conditions

Net farm income declined in 1959 to its 1957 level. Farm proprietors' equities continued to rise.



1/ INCOME OF FARM OPERATORS, INCLUDING GOVERNMENT PAYMENTS.
2/ INCOME OF ALL FARM PEOPLE.
SOURCE: DEPARTMENT OF AGRICULTURE.

The fall was due in part to the decline in farm prices and an accompanying rise in average production costs. Another cause, however, was that income in 1958 had been lifted well above the amounts recorded in the immediately preceding years by certain factors that could not be expected to recur. Among these were the delayed marketings of crops from the previous year's harvest; the record crop of wheat sold at a supported price; payments to farmers for participation in the acreage reserve, which has since been discontinued; and a cyclically strong demand for beef cattle, sheep, and hogs.

The realized net income of farm operators in 1959 was not greatly different, however, than that in the years immediately prior to 1958, especially if allowance is made for the reduction in the number of farms. In fact, realized net income per farm in 1959 was approximately equal to the average for the period since the end of the Korean conflict, exclusive of 1958. Income earned by the farm population from nonfarm sources, on the other hand, continued to increase in 1959, to an estimated $6.7 billion, thus probably amounting to more than half of the net income derived from farming itself.

Farm land values, which had been rising for five years, continued to do so in the first quarter of 1959. The rise was practically halted, however, toward the end of the year. Farmers' indebtedness increased, but by a smaller amount than assets, so that by the end of 1959 farmers' equities were 2 percent larger than at the beginning of the year and 62 percent greater than in 1947–49.

International Economic Developments

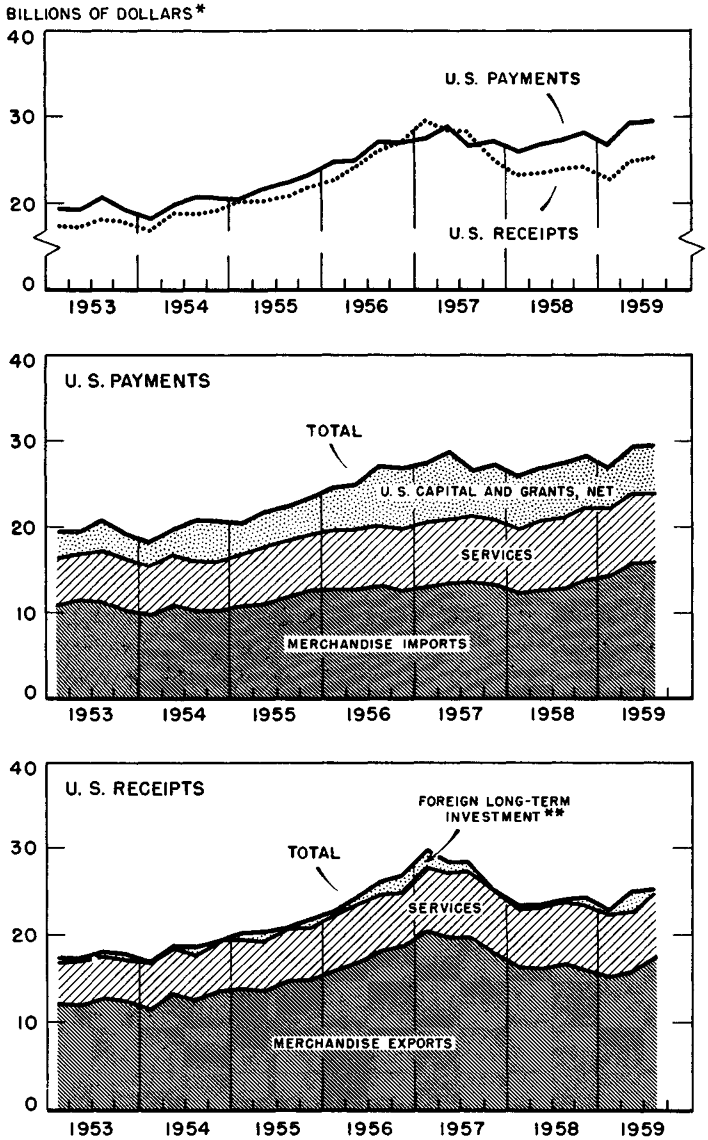
In 1959, as in 1958, United States payments in international transactions exceeded receipts by a wide margin (Chart 11). Exports, seasonally adjusted, fell to a low level in the first quarter of the year, but then began to strengthen and in the third quarter rose vigorously. Though this expansion was interrupted later in the year by the steel shortage, the value of exports in the 11 months through November was about the same as in the corresponding period of 1958. Imports, which were little affected by the 1957–58 recession, staged an exceptionally rapid increase until mid-1959 and, on a seasonally adjusted basis, remained steady thereafter at a level much higher than in previous years.

These developments in trade were superimposed upon a heavy outflow of capital and military expenditures, though both of these flows, especially that of private capital funds, were smaller in 1959 than in 1958. The transfer of gold and liquid dollar assets resulting from the gap between aggregate payments and receipts reached an annual rate of $4.5 billion in the second quarter of 1959. This rate slackened a little in the third quarter, and there was further improvement in later months, reflecting in part a $250 million advance repayment by the United Kingdom to the Export-Import Bank.

CHART 11

U.S. Balance of Payments

The balance of payments deficit remained large in 1959, though exports strengthened after the first quarter.



*SEASONALLY ADJUSTED ANNUAL RATES. ** INCLUDES UNIDENTIFIED RECEIPTS.

SOURCE: DEPARTMENT OF COMMERCE.

Among the underlying factors that have contributed to the change in the trade and payments position of the United States since the early postwar years have been the steady recovery and growth in the productive capacity of other countries, including the re-establishment of old comparative advantages and the introduction of new technologies. On the side of demand, the pressures on domestic resources which persisted in many countries long after the war have generally subsided. In some cases, new international cost and price disparities may now have developed to the advantage of these other countries, and the depressed level of ocean freight rates since 1957 has facilitated the marketing in the United States of certain foreign products. Much of the change in trade may be attributable, however, to intensified production and export efforts by other countries on the basis of previously existing cost differences.

These influences have not operated exclusively in one direction. A detailed examination by the Department of Commerce of recent changes in the shares of the United States in different export markets for manufactured goods reveals a considerable diversity of trends, with many gains as well as losses. Moreover, the serious contractions have been concentrated in a few items. Among these, automobiles and steel stand out, as they do in the rise in imports.

A review of recent developments in the foreign trade of the United States must also take account of the effect of business fluctuations at home and abroad and of the special circumstances affecting trade in particular products that figure prominently in this country's exports or imports. Thus, the decline of exports after mid-1957 was associated with a general weakening of foreign import demands, aggravated by the reversal of special forces which had contributed (notably in the cases of petroleum, coal, cotton, and wheat) to the earlier upswing. Similarly, the strengthening of exports during 1959 reflects the renewal of economic expansion abroad. The progress of expansion in countries that are the principal customers for exports from the United States accordingly deserves attention.

Change in the World Market Situation

Economic conditions in virtually all industrially developed countries improved in 1959. In Canada, as in the United States, production had begun to recover in 1958; after some hesitation in the summer of 1959, it rose again in the autumn. Production in Japan had also rebounded sharply in 1958 and continued an extraordinarily rapid rate of expansion. In Western Europe, the check to production at the end of 1957, though enough to produce marked effects on inventory and import demands in 1958, did not result in any widespread downturn, and a new rise in output got under way early in 1959. The difference of about nine months between North America and Western Europe in the inception of the expansion was of some significance for the development of trade and payments on both sides.

By the second half of 1959, most of the more developed countries were reporting impressive increases in economic activity, compared with a year earlier (Chart 12). This strengthening extended to most industries, although coal mining remained a major exception, with adverse effects on United States coal sales in Europe. In most countries, business fixed investment seems to have played a small role, compared with other demands, in starting the upturn, and the market for capital equipment was generally weak at the beginning of the year. It strengthened, however, in most industrial countries as the expansion gained force, and in some of them, notably Germany and Japan, new orders in the capital goods industries increased markedly in the course of the year.

The renewed expansion in industrial countries abroad was initiated in part by an increase in demand for their exports. It is noteworthy, however, that these increases were, at first, almost exclusively in sales to the United States and Canada, which rose strongly after mid-1958. Elsewhere, these other industrial countries faced much the same market conditions as those confronting the United States. The trade among Western European countries at the beginning of 1959 was scarcely higher than a year earlier, but in March it began to rise significantly. Their exports to the nonindustrial countries in the first quarter were 12 percent below shipments in the first quarter of 1958; and in the second quarter they were still no higher than a year earlier.

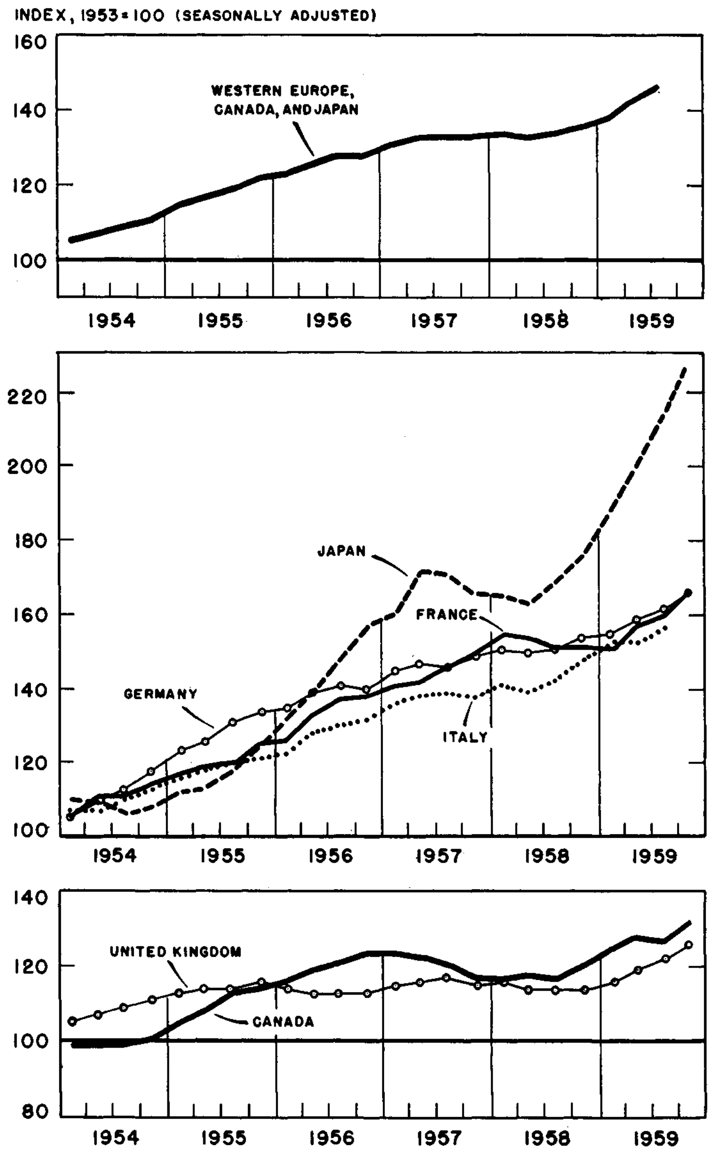
The weakness of demand in the nonindustrial countries at the beginning of 1959 reflected their generally strained foreign exchange position, resulting from the slowness with which their imports had adjusted downward to the progressive fall in their export prices after mid-1957. In some cases, excess capacity contributed to the weakness in these prices. By the first quarter of 1959, the general level of prices in world trade for primary commodities was 5 percent lower than at the beginning of 1958 and 13 percent lower than at the beginning of 1957 (Table D–76). In Latin America—a market that is relatively much more important to the United States than to Europe or Japan—the fall in export prices (exclusive of petroleum) over the two-year period was about 20 percent. The volume of exports from the nonindustrial countries had, however, begun to improve, and in 1959 some of them began to enjoy better export prices and sufficient earnings to permit both some replenishment of their foreign exchange reserves and some increase in their imports. Sterling area countries were helped especially by the improved markets for wool and rubber. Export gains by other primary producers, notably the Latin American countries, were more moderate or were delayed, and some of these countries continued to experience foreign exchange difficulties.

The improvement in the world market situation during 1959 is shown by the summary import figures in Table 4. In the first quarter, imports of industrial countries other than the United States and Canada were little higher, and in some cases lower, than in 1958, and those of the nonindustrial

CHART 12

Foreign Industrial Production

The pace of production abroad, which had slowed after mid-1957, increased rapidly in 1959.



SOURCES: ORGANIZATION FOR EUROPEAN ECONOMIC COOPERATION AND COUNCIL OF ECONOMIC ADVISERS.

TABLE 4.—*World imports, 1958–59* [1]

[Billions of dollars]

Country or area	1958	1959 First quarter	1959 Second quarter	1959 Third quarter [2]
		Seasonally adjusted annual rates		
World imports (c.i.f.) [1]	100.7	98.6	105.5	108.4
United States [3]	14.0	15.2	16.9	17.1
All other countries	86.7	83.4	88.6	91.3
Other industrial countries	51.5	51.6	54.0	55.5
Continental OEEC countries	32.1	31.5	33.3	34.3
United Kingdom	10.6	10.8	10.8	11.2
Canada	5.8	6.1	6.4	6.4
Japan	3.0	3.2	3.5	3.6
Nonindustrial countries	35.2	31.8	34.6	35.8
		Unadjusted annual rates		
Nonindustrial countries	35.2	31.6	34.7	35.0
Sterling area, excluding United Kingdom	14.2	13.1	14.2	14.2
Latin America	8.5	7.0	20.5	20.8
All other	12.5	11.5		

[1] Excludes Soviet Area and Communist China.
[2] The world total and the total for the nonindustrial countries in the third quarter of 1959 are provisional.
[3] Figures for the United States include an adjustment by the International Monetary Fund to a c.i.f. (cost, insurance, freight) basis for purpose of comparability with other countries' data.

Sources: International Monetary Fund, Department of Commerce, and Council of Economic Advisers.

countries were sharply reduced. In the second quarter, imports of the industrial countries and of some of the nonindustrial countries strengthened appreciably, and the improvement continued in the third quarter.

United States Foreign Trade and Payments

In the early months of 1959, United States exports continued to reflect the consequences of the relatively low world demand and certain other unfavorable influences. Coal exports, despite the price advantage favoring the United States, met increasing obstacles because of the oversupply of coal in Europe; cotton shipments were held down in prospect of a change in the United States export price at the start of the new crop season; and exports to many of the primary producing countries, especially in Latin America, remained weak.

In the second quarter, and still more in the third, these influences were offset by the resurgence of economic expansion in the more developed countries. United States exports responded well to the upturn in inventory investment and in expenditures on machinery and equipment in these countries (Table 5). Agricultural exports other than cotton also strengthened in the course of the year, and by the fourth quarter cotton exports were beginning to show the anticipated large increase over the previous year.

TABLE 5.—*United States exports, July to October, 1958 and 1959*

Item	July–October 1958	July–October 1959	Percentage change
	Millions of dollars		
Total exports, excluding "special category" [1]	5,071	5,267	3.9
Cotton, unmanufactured	148	100	−32.4
Coal, petroleum, and related products	358	280	−21.9
Exports, excluding above items, to Latin America	1,268	1,136	−10.4
All other exports	3,297	3,751	13.8
Geographic distribution:			
Canada	1,047	1,143	9.1
Western Europe	1,205	1,404	16.5
Japan	191	238	24.9
Other countries, excluding Latin America	853	965	13.1
Commodity distribution:			
Agricultural products	940	1,077	14.6
Machinery	786	884	12.5
Transportation equipment	332	350	5.5
All other, including reexports	1,240	1,440	16.2

[1] Total and area data include reexports; commodity data exclude reexports.

NOTE.—Detail will not necessarily add to totals because of rounding.

Source: Department of Commerce.

On the other hand, a decrease in exports of machinery and vehicles in November appeared to be attributable to shortages of steel arising from the work stoppage in that industry.

United States merchandise imports rose in little more than a year by about 25 percent from their recession low in the first quarter of 1958. The principal elements in this expansion were the strengthening of demand for industrial materials, as domestic economic activity began to increase; the continued rise in purchases of foreign automobiles and other consumer manufactures; and special demand situations relating to meat, steel, and building materials. With the easing of some of these demands, total imports, seasonally adjusted, did not increase further after midyear.

Changes in service transactions in 1959 were of much less consequence than those in trade. Among United States expenditures abroad, military disbursements were somewhat lower in the first three quarters of the year than in the same period of 1958 and travel outlays somewhat higher. Among receipts, income from direct investments abroad, while lower than in 1958, tended to strengthen in the course of the year.

Influenced by the rise in interest rates in this country, the outflow of capital in the first three quarters of 1959 remained considerably below the high rate of the preceding year, thereby offsetting part of the adverse shift in the goods and services balance. The net outflow of capital was exceptionally low in the first quarter, but rose in the second and remained steady in the third. With imports of goods and services also remaining unchanged and exports rising from the second to the third quarter, the excess of payments on recorded transactions declined. Net transfers of gold and liquid dollar assets to other countries did not diminish correspondingly in the third quarter. This disparity is thought to be due to lags in crediting payments to foreign accounts, with the result of understating the gold and dollar outflow in the second quarter and of overstating it in the third. Incomplete data for the fourth quarter indicate a decline in the rate of gold and dollar transfers, partly attributable to large advance payments of foreign obligations to the United States.

Outlook

Although it is always difficult in a dynamic, free economy such as ours to depict in advance the course likely to be taken by production, employment, and income, present indications warrant the expectation that the expansion now in progress will be extended through 1960. And there are good grounds for belief that, with appropriate public policies and private actions, the expansion can continue well beyond the present year.

Prospective Expansion of Demands

Past developments and present conditions clearly suggest that the demands of business concerns for capital goods and for inventories will be especially important factors in the year ahead. Expenditures on capital goods have been rising for more than a year and should continue upward in 1960. In part, and especially during the early months, the increase will represent a catching-up on projects delayed or postponed because of shortages attributable to the steel strike. Chiefly, however, capital investment should rise in response to favorable underlying factors now discernible and likely to strengthen as the year progresses. Surveys of businessmen's intentions, and the increased volume of contract awards and of new orders for industrial machinery, confirm this outlook. A good demand from the farm economy for machinery and equipment may also be anticipated.

Expenditures for residential construction, a second major category of capital investment, are not likely to be as high as in 1959. However, the extent of the decline should be limited, and activity in this sector of the economy should exceed that of most recent years. Outlays for modernization and alterations should be a steady expansive force in the building industry.

Within the aggregate of government outlays, Federal expenditures for goods and services should change little in the first half of the year; but later, in line with provisions in the fiscal 1961 budget for the development of water resources and other public works, and for space and aviation programs, they should increase moderately. The upward trend of expenditures at the State and local level, which reflects particularly the provision of services needed by the growing urban population, may be expected to continue, though possibly at a slower rate. The construction of schools, public service enterprises, and community facilities in general is expected to advance moderately and to outweigh declines in activity that occur under the Federal-aid highway program as a result of the mandatory reduction in apportionments under the present law.

Changes in investment in business inventories are likely to be less regular during the year than the changes in final demands. Restocking needs are clearly apparent, not only for steel but also for many steel-using intermediate and finished products; and further additions to inventories will be required throughout the economy as production and final sales increase. Inventory expenditures and the other outlays noted above should contribute to a strong expansion in production, employment, and income. The increase in employment should exceed that of the labor force and, correspondingly, unemployment may be expected to fall. Within this context, consumer incomes and expenditures may be expected to increase substantially during the year. Also, consumer confidence is favorable to an increasing volume of purchases of consumer durable goods.

The financing of the investment needs outined here, together with a significant volume of consumer credit, will make strong demands upon the Nation's capital and credit markets. At high levels of income and savings, a greater supply of investment funds may be expected. The sizable Federal budget surplus projected for the fiscal year 1961 would be helpful in relieving pressure on the supply of funds.

Balance of Payments Prospects

A moderate improvement in the United States balance of international payments seems to be ahead in 1960. Imports of capital equipment and consumer manufactures may, on balance, continue their upward trend. And, as industrial production continues to rise, imports of industrial materials may grow, though presumably more slowly than in the recovery phase following the 1957–58 recession. On the other hand, the particular supply and demand situations noted earlier in this chapter, which have been responsible for the rapid rise of certain imports, are shifting; these imports are now expected to increase less rapidly, and some of them may even decline. The growth of total imports, therefore, may well be considerably smaller in 1960 than the rise in the period from early 1958 to mid-1959.

Exports should gain from the strong expansion of production and investment that is proceeding in the industrial countries abroad. This expansion should benefit United States sales indirectly also, as the primary producing countries find their purchasing power raised by their higher exports to the industrial countries. Moreover, certain major exports that declined in 1959, as discussed above, may cease to decline in 1960, or may increase.

On this appraisal, exports in 1960 should rise appreciably more than imports. Also, receipts from services are expected to rise faster than payments for services and military expenditures abroad. Net exports of goods and services, as registered in our national income accounts, should show a positive balance. On the other hand, new United States investment abroad may increase, especially if interest rates in other countries continue to rise. Therefore, the over-all payments deficit may still be relatively large in 1960. To assist in attaining a needed adjustment of the balance of payments consistent with our goal of promoting multilateral world trade, a strengthening of exports continues to be essential. The level of exports will depend on such fundamental conditions as the rate and regularity of expansion of activity abroad, the progress of other countries toward more liberal trade policies, and our own efforts to strengthen the competitive position of United States products in foreign markets.

Conditions for Sound Advance

Our success in realizing the opportunities that 1960 presents, and for extending economic growth at a high and stable rate into the future, will depend upon the actions of business management, labor leaders, and consumers, as well as on the policies of Government, toward maintaining the balance in our economy that is required for sustainable growth. A Federal program for 1960 that is designed to help achieve our national economic objectives is offered in Chapter 4, together with suggestions for appropriate private action.