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You have asked me to comment on a number of broad questions regarding the economic outlook and the dangers of inflation. The immediate situation is, of course, a result of war. In wartime people are paid for producing goods and services which are not offered for sale. Therefore, incomes exceed supplies of goods and services available for purchase. Excess buying power can be reduced only by having the Government tax or borrow it to meet war expenditures. It can be prevented from being used by strict rationing and price controls.

We have behind us a period of unheard of economic expansion -- expansion in output, income, Federal budget, the money supply, and many other factors. Serious inflation was arrested during the war by production, price, wage, and rationing controls, as well as by increased taxes and other measures. Although the war is over, many of the expansionary factors are still present and some new ones have been added. At the same time, some controls have been taken off or are falling apart from pressures of special interests. That the situation is explosive can be seen readily if one watches the action of the stock market, tries to purchase a home, or walks through stores selling high-priced products.

In global figures the big job of war financing is behind us. Yet the implications and the aftermath of war finance are still very much with us and will remain with us for a long time to come. During the period from ~~July~~ June 30, 1941, to the end of this calendar year the Federal Government will have spent a total of 345 billion dollars. During the same time we have raised in taxation 145 billion dollars. The remaining 200 billions or nearly 60 per cent of the total was the Federal deficit. In meeting the deficit (and accumulating a 20-

billion balance in the Treasury's general fund for future use), the Federal debt will have been increased from 55 billion to 270 billion dollars.

Of this increase, 110 billion dollars was sold to individuals and corporations, ~~companies~~ (other than commercial banks), either directly to the owners or indirectly to insurance companies or other savings institutions. Of the remaining addition to the debt (which totaled 215 billion dollars), 87 billions was absorbed by the commercial banking system and the residual, or 18 billion dollars, was purchased by various Federal agencies.

The sources of war finance were thus of three major kinds -- taxes, purchases of securities by the public, and purchases by the commercial banking system. The first item - the 145 billions of tax receipts -- is a matter of the past and has little direct bearing upon the present level of purchasing power. The second item -- the 110 billions of securities purchased by individuals and savings institutions, together with 20 billions held prior to the war -- may be considered as being to a large extent firmly invested. However, since the Government securities may be readily converted into cash and since the Government stands ready to maintain a stable security market, these securities are closely equivalent to cash holdings. They present a serious problem with regard to future management of the public debt, particularly in an inflationary period when the holders may wish to sell on balance and thus further increase the funds available for the purchase of scarce supplies. The third item -- the 87 billions of securities sold to the commerical banking system -- has resulted in a corresponding net addition to the country's money supply, since any increase in the bank holdings of securities gives rise to an equal increase in the volume of deposits and currency in circulation.

Considering the private rather than the public side of the Nation's war budget, we find that individuals and corporations during these four and one-half years received a total gross income before taxes of 822 billion dollars. About half of this total was received in payment for goods and services sold to the Government and the bulk of the remainder for goods and services sold to the American consumer. Of the 822 billions of gross income received, only 179 billion dollars was paid out in taxes, of which 145 billions was to the Federal Government; 413 billion dollars was spent on consumption and 30 billions on capital equipment. The remainder, or 200 billion dollars, was saved in the form of monetary claims -- cash, securities, insurance, etc. This total of savings equals the total deficit accrued by the Government.

Of the 200 billion dollars of wartime savings, nearly 120 billions were accumulated by individuals. Most of the remainder went to corporations and unincorporated businesses. This is a wholly unprecedented and staggering amount of savings measured either in dollars or in relation to gross income. Total holdings of liquid assets by individuals, including currency, deposits, and Government securities now amount to 150 billion dollars, as against 50 billions before the war. Holdings by nonfinancial corporations and by unincorporated businesses now exceed 65 billion dollars, four times as much as in 1940.

Thus, the liquidity position of individuals and businesses has been enormously increased because of the heavy reliance on borrowing rather than taxation in the financing of war expenditures, and because the deficit has been financed to such a large extent by borrowing from banks and large corporations rather than from the average citizen -- a process that creates new supplies of money.

It is true, of course, that the entire cost of thw ar could not have been financed from taxation or without expansion in the public debt. The high liquidity ~~position~~ of the economy is ~~was~~, therefore, an inevitable result of war finance. In my opinion, however, taxes should have been raised earlier and further in order that they might have contributed a larger share to financing the war, and more vigorous measures should have been adopted to limit bank purchases of Government securities. Had such policies been followed, the public debt and the interest charges on it would have been smaller and the potentialities for inflation in the present large volume of cash holdings would be much less severe.

The war resulted in a tremendous destruction of capital equipment, deterioration of living standards, and the power to produce throughout Europe and Asia. The United States, in the economic field, has suffered comparatively little. We have gained in realizing what enormous productive capacity this country possesses if its manpower and resources are fully utilized. We have found it possible to produce for war at a scale equal to our prewar civilian output, while at the same time maintaining our over-all consumption standards. This was accomplished even though 10 million of the cream of our labor force were in the armed services.

Nevertheless, ~~C~~consumer demands in the broad fields of housing and durable consumers' goods were largely unsatisfied ~~had to go unmet~~. The cars, houses, household equipment, and even ~~not to mention~~ food, clothing, and various services which the people wished to buy at their high levels of wartime income were not available in adequate quantities. ~~The demand for these items had to be postponed or discarded and~~ As a result large backlogs of consumers' demand have been built up, and an ~~backlogs which are backed by~~ ~~an~~ unheard of volume of liquid asset holdings is available to finance these purchases.

Much the same situation exists in the field of capital expenditures. Business is in need of new plant and equipment; replacements and repairs which were postponed during the war must be made up and inventories need to be replenished ~~built~~. Plant facilities constructed for war production purposes will meet only part of the need; in many cases they will not be useable for peacetime production.

In addition to this backlog of domestic demand, there is an enormous need for American products all over the world. American production must provide some help in the task of rehabilitation if there is to be a functioning world economy. Some part of available American supplies, therefore, must be provided to meet foreign demands, even though this adds to the problems of economic stabilization during the next year or so.

There is no simple key to appraising developments during the twelve months ahead. The economic readjustments and shifts now in progress are vast and defy clear prediction. It is probable that strong inflationary pressures will continue for some time, pressures which might indeed become disastrous if the disintegration of public controls is permitted to continue at its present rate. The prudent course is to err on the side of protecting the line.

We must distinguish clearly between the inflationary emergency confronting us at the moment and the quite different problems with which we are likely to be faced later on. As I have stated repeatedly, the long-run dangers for the American economy lie in the direction of unemployment and insufficient demand for current production. Public policy ultimately will be faced with the problem of preventing contraction and unemployment. It is of crucial importance to recognize, however, that this is not the problem of immediate concern. The urgent need at this time is to prevent inflation, which could only end in a destructive collapse.

The economic outlook for the near-term future has become clearer since V-J Day. Prior to V-J Day there was much uncertainty as to how it would be possible to avoid widespread unemployment in view of a prospective 70-billion-dollar cut in Government purchases and a corresponding reduction of war production, together with the discharge of nearly 10 million people from the armed forces.

In less than four months the task has been half finished. Although war expenditures have been cut from an annual rate of ~~95~~ over 90 billion dollars to ~~about 50~~ less than 50 billions at present and more than 4 million servicemen have been demobilized, unemployment figures are ~~below~~ only 2 million, and the economy's total output is still above 180 billion dollars on an annual basis. The cut of nearly 50 billions in war expenditures has resulted in less unemployment than many expected because the shortening of hours has required more people to produce a given output, some wartime workers have left the labor market, discharged service men have not been in a hurry to look for jobs, and there has been an offsetting rise in production of civilian goods.

No surpluses have yet appeared or are in immediate sight, however. Thus shortages in most fields are still acute. The prospects are that the further 25-billion-dollar cut in Government purchases, which may be expected between now and the end of ~~during~~ 1946, will be largely offset by increased production to meet civilian demand, domestic and foreign. The annual rate of consumers' expenditures, which has been rising sharply since V-J Day, ~~may well~~ is likely increase further when many items in the durable field ~~again~~ re- appear on the market and may well rise to an annual level of 10 billion dollars above the wartime peak~~s~~. Similarly, it is reasonable to expect a~~n~~ further increase of as much as 10 billion dollars a year in private capital expenditures, including construction of plants and commercial buildings, ~~and~~ accumulation of inventories and net exports. The export balance in the course of the next year may well reach an annual rate of 5 billion dollars.

With the release of an additional 6 million or more from the armed forces, substantial unemployment may nevertheless develop. However, this unemployment for the time being will not be a reflection of an inadequate level of total demand, but rather the product of inevitable strains involved in the drastic shifts from war to peace production. A high and stable level of peacetime employment will be reached more promptly and more certainly if we are prepared to tolerate some ~~depressing~~ restrictive influences during these transition months in order to avoid intensifying the pressures toward inflation. There is a serious danger that an excessive scramble may develop for goods which are still scarce in supply. It is important, therefore, that Government policy should assure the consumer and the businessman that prices are not going to rise and that it will not be necessary to beat the market by buying early and accumulating large inventories which will further accentuate supply shortages.

Long ago I sought to emphasize that protective steps were necessary in the field of capital assets -- the most exposed and least protected sector in the line we have been trying to hold against inflation. We have already seen the effects of inflationary and speculative pressures, particularly on real estate values, farm and city. We have seen the reflection of this situation in the stock market. The pressures are inherent in the enormous accumulations of cash or its equivalent at the disposal of the general public. The problem is essentially one of cash, rather than of credit. The most effective single remedy would have been a stiff capital gains tax -- but Congress was not willing to take that step. Much of the inevitable damage has already been done.

Farm land values as of November 1 were approximately 60 per cent above the prewar average for 1935-39. This upward trend has continued since V-J Day and if it follows the pattern following the last war, the situation will be even more acute during 1946. The inflationary situation in the housing market is especially alarming. Prices and costs of buildings have risen sharply, and this trend, which has already gone too far, must be curbed. Fortunately, the President has approved the program recommended to him by Mr. Snyder for ~~putting back~~ reinstating controls over allocation of scarce materials, and for instituting a system of price ceilings on new as well as old houses. That is all to the good. The dangers could be further averted, however, by enacting a high enough capital gains tax which would have general applicability to all capital values and ~~to~~ take the speculative fever out of ~~the~~ farm real estate, ~~market as well as~~ the stock market as well as urban real estate. Stock prices have risen about 20 per cent since last August and are now 40 per cent above 1939 levels, with many stocks at new highs since 1930. Share trading recently has been more active than at any time during the past eight years, notwithstanding the fact that due to the tightening of margin requirements the volume of stock market credit has been declining.

I recognize how strong the pressures from ~~some sections of the public~~ certain groups have been in favor of taking off controls and cutting taxes, even though I believe that the vast majority of the people want their government to stand firm. ~~Even so,~~ Prudent policy demands that these ~~pressures~~ pressure groups be resisted to the utmost in the protection of this Nation. It does not make economic sense to cut taxes deeply while purchasing power is abundant and we are still running a heavy deficit. The Ways and Means Committee, in my judgment, was right in recommending that the excess profits tax be cut to 60 per cent, but no further. Its complete repeal at this time was bound to delay reconversion, to intensify labor problems and to increase the deficit. All the reasons for instituting that tax in the first instance apply with equal or greater force today than ever before. By and large, repeal of this tax gave the biggest tax benefits to those best able to pay taxes -- and it gave it to those whose ~~immediately prospective~~ profits in the transition period will be ~~are~~ as much war profits as if they had been ~~were~~ reaped while the guns were still firing.

I don't like these wartime controls. They should be dropped as soon as it can be done safely, that is, when the transition to a stable postwar economy has been assured and supplies in most lines have become adequate to meet the demand. Increased supplies and production of civilian goods are thus ~~is~~ the ultimate answer to the problem of inflation. Some have ~~It has been~~ argued that ~~adequate supplies will be forthcoming only if~~ all stabilization controls should be ~~are~~ dropped promptly to speed up production. That is a dangerous fallacy. If all controls are discarded prematurely, the result~~s~~ will be a mad competition for scarce materials, the bidding up of prices, the hoarding of goods -- a train of evils that can only end in economic disaster.

In such a competition for scarce materials and supplies, small business would be the greatest victim. Small business organizations which are complaining that price controls should cease at once are doing themselves a great disservice.

In summary, the policies which I think should be pursued at this time are briefly:

1. Assurance to the country that effective price controls will be continued beyond the present cut-off date of June 30, 1946. If the future of price control beyond June 30 is permitted to remain uncertain up to the summer months, it will encourage advance buying and excessive inventory accumulation in anticipation of higher prices. The ill effects will be felt long before controls are actually discarded.

2. Every effort should be made to use, where needed, allocation and inventory controls. The wartime depletion of inventories and the prospective high level of civilian production make it necessary that some inventory re-stocking should occur, but the danger is that this re-stocking will be concentrated in too brief a period and in too few hands, thereby increasing the demand for goods while reducing supplies to the consumer.

3. The basic consideration in the present struggle about increased wages is the need for more production. The rapid decline in working hours which has occurred during the past six months has again been much ahead of the needs of the situation. The vast total of domestic and world demand for the output of the American workers would have required the continuation of a 44- or 48-hour week for some time. Had this approach been taken, it would have been possible to postpone most of the current wage-price debate to a more appropriate time.

After the period of inflationary pressures is over, higher basic wages will be needed to sustain mass purchasing power for the goods that can be produced by American industry. Advances in the productivity of labor should ultimately be passed on to the worker in higher wages and shorter hours, or to the consumer in lower prices. The wartime level of profits, allowing for the repeal of the excess profits tax, is tremendous and cannot be expected to continue. Price reductions or wage increases will in many cases be called for. Above all, it is vitally necessary not to confuse the policy requirements of the present period with those of the long run.

Finally, permit me to say that the coming year affords a better opportunity to balance the Federal budget than this country has seen for the last seventeen years and may see again for a long time. If we do not stop the deficits and the creation of a bigger and bigger money supply now, when can we expect to stop? We owe it to every citizen, to every war veteran, to hold this line against inflation if the victory on the war fronts is not to be lost in the end on the home front.